

**Draft Reserve Bank of India (All India Financial Institutions (AIFIs)-Prudential
Norms on Capital Adequacy) Directions, 2025**

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**Reserve Bank of India (All India Financial Institutions (AIFIs)-Prudential Norms
on Capital Adequacy) Directions, 2025**

Table of Contents

| | |
|---|-----------|
| Chapter I Preliminary..... | 4 |
| A Short title and commencement..... | 4 |
| B Applicability | 4 |
| C Definitions | 4 |
| Chapter II Board approved policies and scope of application..... | 17 |
| A Instructions regarding Board approved policies and documents to be reviewed by the Board | 17 |
| B Scope of application of capital adequacy framework | 17 |
| Chapter III Regulatory capital | 20 |
| A Composition of regulatory capital | 20 |
| B Common Equity Tier 1 (CET 1) capital..... | 22 |
| C Additional Tier 1 (AT 1) capital | 26 |
| D Tier 2 capital..... | 44 |
| E Minimum requirements to ensure loss absorbency of AT 1 instruments at pre- specified trigger and of all non-equity regulatory capital instruments at the point of non-viability | 56 |

| | | |
|--|---|------------|
| F | Recognition of minority interest (i.e., non-controlling interest) and other capital issued out of consolidated subsidiaries that is held by third parties | 66 |
| G | Regulatory adjustments / deductions | 71 |
| H | Transitional arrangements for an AIFI..... | 88 |
| Chapter IV Risk weighted assets (RWAs)..... | | 89 |
| A | Capital charge for credit risk | 89 |
| B | External credit assessments | 168 |
| C | Credit risk mitigation..... | 177 |
| D | Capital charge for market risk | 199 |
| E | Capital Charge for Operational Risk..... | 235 |
| Chapter V Supervisory review and evaluation process (SREP) and market discipline | | 238 |
| A | Introduction to the SREP and ICAAP | 238 |
| B | ICAAP of an AIFI..... | 245 |
| C | Select operational aspects of the ICAAP | 256 |
| D | Format of an ICAAP document | 286 |
| E | Market discipline | 297 |
| Chapter VI Leverage ratio framework | | 304 |
| A | Minimum requirement and scope of application of the leverage ratio | 304 |
| B | Scope of consolidation | 304 |
| C | Capital measure | 304 |
| D | Exposure measure | 304 |
| E | Disclosure and reporting requirements | 320 |
| F | Disclosure templates..... | 322 |
| Chapter VIII Repeal and Other provisions | | 323 |
| Annex 1 Reporting format for details of investments by FIIs and NRIs in PNCPS qualifying as AT 1 capital..... | | 325 |

| | |
|---|------------|
| Annex 2 Format for reporting of capital issuances | 326 |
| Annex 3 Pillar 3 Disclosure requirements for an AIFI | 327 |

In exercise of the powers conferred by Section 45L of the Reserve Bank of India Act, 1934, the Reserve Bank of India being satisfied that it is necessary and expedient in the public interest and in the interest of financial sector 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 (All India Financial Institutions (AIFIs)-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 All India Financial Institutions (hereinafter collectively referred to as 'AIFIs' and individually as a 'AIFI'), viz., Export-Import Bank of India (EXIM Bank), National Bank for Agriculture and Rural Development (NABARD), National Housing Bank (NHB), Small Industries Development Bank of India (SIDBI), and National Bank for Financing Infrastructure and Development (NaBFID).

C Definitions

4. In this chapter, unless the context states otherwise, the terms herein shall bear the meanings assigned to them below.
 - (1) 'Available for sale (AFS)' means the category of investment portfolio of an AIFI which includes investment that do not fall within the Held to Maturity (HTM) or Held for Trading (HFT) category.
 - (2) 'Basis risk' means the risk that emanates from the changes in interest rate of different assets, liabilities and off-balance sheet items in different magnitudes.
 - (3) 'Capital funds' means the total regulatory capital of an AIFI, fulfilling the criteria defined in the prescribed capital regulations as per Chapter II of these Directions, as per the last audited balance sheet.
 - (4) 'Central counterparty' (CCP) means a system provider, who by way of novation interposes between system participants in the transactions admitted for

settlement, thereby becoming the buyer to every seller and the seller to every buyer, for the purpose of effecting settlement of their transactions.

- (5) 'Clean-up call' means an option that permits the originator to call the underlying exposures or the securitisation exposures when the outstanding value of the underlying exposures falls below a pre-defined threshold, thereby extinguishing the remaining securitisation exposures of all parties.
- (6) 'Clearing member' means 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.

Note - For the purpose of these guidelines, 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.

- (7) 'Client' means 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.
- (8) 'Control' shall have the same meaning as assigned to it under clause (27) of Section 2 of the Companies Act, 2013 as amended from time to time.
- (9) 'Corporate bonds / debentures' for the purpose of these Directions mean debt securities which create or acknowledge indebtedness, including (i) debentures (ii) bonds (iii) commercial papers (iv) certificate of deposits and such other securities of a company, a multilateral financial institution (MFI) or a body corporate constituted by or under a Central Act or a State Act, whether constituting a charge on the assets of the company or body corporate or not, and includes convertible instruments and instruments of a perpetual nature, but does not include debt securities issued by Central Government or a State Government,

or such other persons as may be specified by the Reserve Bank, security receipts and securitised debt instruments.

- (10) 'Counterparty credit risk' (CCR) means the risk that the counterparty to a transaction may 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.

Note - Unlike a firm's exposure to credit risk through a loan, where the exposure to credit risk is unilateral and only the lending AIFI faces the risk of loss, CCR creates a bilateral risk of loss: 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 factors.

- (11) 'Credit enhancement' means a contractual arrangement in which an entity provides some degree of added protection to other parties to a transaction so as to mitigate the credit risk of their acquired exposures.
- (12) 'Credit risk' means the potential that an AIFI's borrower or counterparty may fail to meet its obligations in accordance with agreed terms and also includes the possibility of losses associated with diminution in the credit quality of borrowers or counterparties.
- (13) 'Credit valuation adjustment' means 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 AIFI and the counterparty.
- (14) 'Cross-product netting' means the inclusion of transactions of different product categories within the same netting set.
- (15) 'Current exposure (often also called Replacement Cost) under the Current Exposure Method' means 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.

(16) 'Current or valid credit rating' means a credit rating granted by a credit rating agency in India, registered with the Securities and Exchange Board of India (SEBI) and fulfilling the following conditions:

- (i) The credit rating letter shall not be more than one month old on the date of opening of the issue.
- (ii) The rating rationale shall not be more than one year old on the date of opening of the issue.
- (iii) The credit rating letter and the rating rationale shall preferably be part of the offer document.
- (iv) In the case of secondary market acquisition, the credit rating of the issue shall be in force and confirmed from the monthly bulletin published by the respective rating agency.

(17) 'Default funds' means clearing member's funded or unfunded contributions towards, or underwriting of, a CCP's mutualised loss sharing arrangements.

Note - Default funds are also known as clearing deposits or guarantee fund contributions (or any other names). 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.

(18) 'Deferred tax assets' shall have the same meaning as assigned under the extant accounting standards.

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

(20) 'Duration (Macaulay duration)' measures the price volatility of fixed income securities often used in the comparison of the interest rate risk between securities with different coupons and different maturities.

Note - Duration is calculated the weighted average of the present value of all the cash flows associated with a fixed income security. It is expressed in years. The duration of a fixed income security is always shorter than its term to maturity, except in the case of zero-coupon securities where they are the same.

- (21) 'Early amortisation provision' means a mechanism that, once triggered, accelerates the reduction of the investor's interest in underlying exposures of a securitisation structure and allows investors to be paid out prior to the originally stated maturity of the securitisation notes issued.
- (22) 'Excess spread (or future margin income)' means the difference between the gross finance charge collections and other income received by the special purpose entity (SPE), and securitisation notes interest, servicing fees, charge offs, and other senior SPE expenses.
- (23) 'Exchange' means 'recognised stock exchange' and shall have the same meaning as defined in Section 2 (f) of Securities Contracts (Regulation) Act, 1956.
- (24) 'Exposure amount' of a securitisation exposure means the sum of the on-balance sheet amount of the exposure or carrying value – which takes into account purchase discounts and write-downs / specific provisions an AIFI took on this securitisation exposure – and the off-balance sheet exposure amount, where applicable.
- (25) 'Financial services company' means a company engaged in the 'business of financial services as defined in the [Reserve Bank of India \(All India Financial Institutions – Undertaking of Financial Services\) Directions, 2025](#) as amended from time to time.
- (26) 'First loss facility' means the first level of financial support provided by the originator or a third party to improve the creditworthiness of the securitisation notes issued by the SPE such that the provider of the facility bears the part, or all of the risks associated with the assets held by the SPE.
- (27) 'Forward contract' means an agreement between two parties to buy or sell an agreed amount of a financial instrument or currency at an agreed price, for delivery on an agreed future date.

Note - In contrast to a futures contract, a forward contract is not transferable or exchange tradable, its terms are not standardised and no margin is exchanged. The buyer of the forward contract is said to be long the contract and the seller is said to be short the contract.

- (28) 'General market risk' means risk of losses in on-and off-balance sheet positions arising from movements in market prices.
- (29) 'Government security' shall have the same meaning as assigned to it in Section 2(f) of the Government Securities Act, 2006.
- (30) 'Going-concern capital', from regulatory perspective, is the capital which shall absorb losses without triggering bankruptcy of the AIFI
- (31) 'Gone-concern capital', from regulatory perspective, is the capital which shall absorb losses only in a situation of liquidation of the AIFI
- (32) 'Hedging' means taking action to eliminate or reduce exposure to any type of risk.
- (33) 'Hedging set' means a group of risk positions from the transactions within a single netting set for which only their balance is relevant for determining the exposure amount or Exposure at Default (EAD) under the CCR standardised method.
- (34) 'Held for Trading' means the category of investment portfolio maintained by an AIFI with the intention to trade in securities by taking advantage of short-term price / interest rate movements.
- (35) 'Held to Maturity' means the category of investment portfolio maintained by an AIFI with an intention to hold securities up to maturity.
- (36) 'Horizontal disallowance' means a disallowance of offsets to required capital used for assessing market risk for regulatory capital. In order to calculate the capital required for interest rate risk of a trading book, offsetting of long and short positions is permitted. However, interest rate risk of instruments at different horizontal points of the yield curve are not perfectly correlated. Hence, this method requires that a portion of these offsets be disallowed.
- (37) 'Implicit support' means the protection arising when an AIFI provides support to a securitisation in excess of its predetermined contractual obligation.
- (38) 'Infrastructure projects / infrastructure lending' means any credit facility in whatever form extended by an AIFI to any infrastructure facility that is a project in any of the sectors incorporated in the latest updated Harmonized Master List of Infrastructure Sub-sectors published by the Government of India.

(39) '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. Initial margin shall not include contributions to a CCP for mutualised loss sharing arrangements.

Note - In cases where a CCP uses initial margin to mutualise losses among the clearing members, it shall be treated as a default fund exposure.

(40) 'Interest-only strip (I/O)' means an on-balance sheet asset of the originator that represents a valuation of cash flows related to future margin income;

Provided that, if the interest-only strip is subordinated, it shall serve the purpose of credit enhancement and shall be referred to as credit-enhancing interest-only strip.

(41) 'Interest rate risk' means risk that the financial value of assets or liabilities (or inflows / outflows) may be altered because of fluctuations in interest rates.

(42) 'Investments in entities that are outside of the scope of regulatory consolidation' means 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.

(43) 'Large exposure' means the sum of all exposure value of an AIFI measured in terms of [Reserve Bank of India \(All India Financial Institutions – Concentration Risk Management\) Directions, 2025](#), to a counterparty and / or a group of connected counterparties, if it is equal to or above 10 per cent of an AIFI's eligible capital base.

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

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

(45) 'Listed security' is a security, which is listed on an exchange.

(46) 'Long position' refers to a position where gains arise from a rise in the value of the underlying.

- (47) 'Market risk' means the risk of losses in on-balance sheet and off-balance sheet positions arising from movements in market prices.
- (48) 'Modified duration' or volatility of an interest-bearing security is its Macaulay duration divided by one plus security's yield to maturity (YTM) per period. It represents the percentage change in a securities' price for a 100 basis points change in yield (generally accurate for only small changes in the yield).

$$MD = -\frac{dP}{dY} \cdot \frac{1}{P}$$

where:

MD = Modified duration

P = Gross price (i.e., clean price plus accrued interest).

dP = Corresponding small change in price.

dY = Small change in yield compounded with the frequency of the coupon payment;

- (49) 'Mortgage-backed security' shall have the same meaning as assigned under [Reserve Bank of India \(All India Financial Institutions – Securitisation Transactions\) Directions, 2025](#) as amended from time to time.
- (50) 'Netting set' means 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 which is recognised for regulatory capital purposes shall be interpreted as its own netting set for the purpose of these Directions.
- (51) 'Net interest margin' means the net interest income divided by average interest earning assets.
- (52) 'Net worth' shall have the same meaning as assigned to it under clause (57) of Section 2 of Companies Act, 2013 as amended from time to time.
- (53) 'Non-financial services company' means a company not engaged in any of the activities being conducted by a financial services company.

- (54) '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).
- (55) 'One-sided credit valuation adjustment' is a credit valuation adjustment that reflects the market value of the credit risk of the counterparty to an AIFI but does not reflect the market value of the credit risk of an AIFI to the counterparty.
- (56) 'Open position' means the net difference between the amounts payable and amounts receivable in a particular instrument or commodity. It results from the existence of a net long or net short position in the particular instrument or commodity.
- (57) 'Originator' refers to an AIFI that transfers from its balance sheet a single asset or a pool of assets to an SPE as a part of a securitisation transaction and shall include other entities of the consolidated group to which the AIFI belongs.
- Explanation* - Originator may not be the same lender which had initially sanctioned one or more of the exposures underlying a securitisation transaction since loans purchased from an AIFI/bank shall also be sold to SPEs for the purpose of securitisation.
- (58) 'Operational risk' means the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This definition includes legal risk, but excludes strategic and reputational risk. Legal risk includes, but is not limited to, exposure to fines, penalties, or punitive damages resulting from supervisory actions, as well as private settlements.
- (59) 'Option' means a contract which grants the buyer the right, but not the obligation, to buy (call option) or sell (put option) an asset, commodity, currency or financial instrument at a specified rate (exercise price) on or before an agreed date (expiry or settlement date).
- (60) 'Overcollateralisation' means any form of credit enhancement by virtue of which underlying exposures are posted in value which is higher than the value of the securitisation notes
- (61) 'Outstanding Exposure at Default (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 an AIFI as an incurred write-down (i.e., a CVA loss).

- (62) 'Qualifying central counterparty' (QCCP) means 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.
- (63) 'Quoted security' is a security for which market prices are available at stock exchanges / reporting platforms / trading platforms authorized by the Reserve Bank / Securities and Exchange Board of India (SEBI).
- (64) 'Rated security' means a security which is subjected to a detailed credit rating exercise by a SEBI-registered credit rating agency and shall carry current or valid credit rating.
- (65) 'Repo' and 'reverse repo' shall have the same meaning as defined in Section 45U of the Reserve Bank of India Act, 1934. For the purpose of these Directions, the word 'repo' is used to mean both 'repo' and 'reverse repo' with the appropriate meaning applied contextually.
- (66) 'Securities' shall have the same meaning as defined in Section 2(h) of Securities Contracts (Regulation) Act, 1956.
- (67) 'Securities financing transactions' (SFTs) means 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.
- (68) 'Securitisation' shall have the same meaning as assigned under [Reserve Bank of India \(All India Financial Institutions – Securitisation Transactions\) Directions, 2025](#).

(69) 'Securitisation exposures' shall have the same meaning as assigned under [Reserve Bank of India \(All India Financial Institutions – Securitisation Transactions\) Directions, 2025](#).

(70) 'Securitisation notes' mean securities issued by the special purpose entity as a part of securitisation.

(71) 'Securitized debt instrument' means securities of the nature referred to in Section 2(h)(ie) of the Securities Contracts (Regulation) Act, 1956.

(72) 'Security Receipts' shall have the same meaning as defined in Section 2(1)(zg) of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002.

(73) 'Senior tranche' means a tranche which is effectively backed or secured by a first claim on the entire amount of the assets in the underlying securitised pool.

Provided that, where all tranches above the first-loss piece are rated, the most highly rated position shall be treated as a senior tranche.

Provided further that when there are several tranches that share the same rating, only the most senior tranche in the cash flow waterfall shall be treated as senior (unless the only difference among them is the effective maturity).

Provided further that when the different ratings of several senior tranches only result from a difference in maturity, all of these tranches shall be treated as senior tranches

(74) 'Significant influence' shall have the same meaning as assigned under the extant accounting standards.

(75) 'Special purpose entity (SPE)' means a company, trust or other entity organised for a specific purpose, the activities of which are limited to those appropriate to accomplish the purpose of the SPE, and the structure of which is intended to isolate the SPE from the credit risk of an originator.

Explanation - Any reference to SPE in these directions shall also refer to the trust settled or declared by the SPE as a part of the process of securitisation.

(76) 'Specific market risk' refers to the risk associated with a specific security, issuer or company, as opposed to the risk associated with a market or market sector (general market risk).

(77) 'Subsidiary' shall have the same meaning as assigned under the extant accounting standards.

(78) 'Trade exposures' include the current and potential future exposure of a clearing member or a client to a CCP arising from OTC derivatives, exchange traded derivatives transactions or SFTs, and initial margin.

Note - for the purpose of this definition, the current exposure of a clearing member includes the variation margin due to the clearing member but not yet received.

(79) '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.

(80) 'Tranche maturity' means the tranche's effective maturity in years and is measured as prescribed in paragraphs 99 to 101.

(81) 'Tranche thickness' means the measure calculated as detachment point (D) minus attachment point (A), where D and A are calculated in accordance with paragraphs 94 to 98.

(82) 'Unrated securities' means securities, which do not have a current or valid credit rating by a SEBI-registered credit rating agency.

(83) 'Value at risk' (VAR) means a method for calculating and controlling exposure to market risk. VAR is a single number (amount) which estimates the maximum expected loss of a portfolio over a given time horizon (the holding period) and at a given confidence level.

- (84) '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.
- (85) 'Vertical disallowance' means a reversal of the offsets of a general market risk charge of a long position by a short position in two or more securities in the same time band in the yield curve where the securities have differing credit risks under the method followed for determining regulatory capital necessary to cushion market risk.
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

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

6. An AIFI's Board shall have the following responsibilities:
- (1) The structure, design and contents of an AIFI'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 an AIFI.
 - (2) An AIFI 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.
 - (3) An AIFI shall have a formal disclosure policy approved by the Board of Directors that addresses the AIFI's approach for determining what disclosures it shall make and the internal controls over the disclosure process.
7. The Board shall assess and document, at least once a year, whether the processes relating to the ICAAP implemented by an AIFI 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) An AIFI shall comply with the capital adequacy ratio requirements at two levels on an ongoing basis:
 - (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 an AIFI based on its capital strength and risk profile after consolidating the assets and liabilities of its subsidiaries /

joint ventures / associates except those engaged in insurance and any non-financial activities; and

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

Capital adequacy at solo level

- (2) While assessing the capital adequacy of an AIFI at solo level, all regulatory adjustments indicated in paragraph 24 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 also have to be deducted from the corresponding capital instruments issued by an AIFI.
- (3) 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 (CET 1) capital.

Capital adequacy at group / consolidated level

- (4) For capital adequacy at consolidated level, all banking and other financial subsidiaries except the subsidiaries engaged in insurance or any non-financial activities (both regulated and unregulated) shall be fully consolidated.
- (5) The insurance and non-financial subsidiaries / joint ventures / associates of an AIFI 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. Equity and other regulatory capital investments in the unconsolidated insurance and non-financial entities / subsidiaries of an AIFI (which also include joint ventures / associates of the parent AIFI) shall be treated in terms of paragraph 24 (7) and paragraph 67 respectively.
- (6) All regulatory adjustments indicated in paragraph 24 are required to be made to the consolidated capital of the parent AIFI as indicated therein.
- (7) Minority interest (i.e., non-controlling interest) and other capital issued out of consolidated subsidiaries as per paragraph 23(1) that is held by third parties shall be recognised in the consolidated regulatory capital of the parent AIFI subject to certain conditions as stipulated in paragraph 23.

- (8) An AIFI 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 CET 1 capital.

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. An AIFI shall maintain a minimum Pillar 1 Capital to Risk-weighted Assets Ratio (CRAR) of 9 per cent on an on-going basis. The Reserve Bank shall take into account the relevant risk factors and the internal capital adequacy assessments of each AIFI to ensure that the capital held by them is commensurate with its overall risk profile. This shall include, among others, the effectiveness of an AIFI'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 shall consider prescribing a higher level of minimum capital ratio for each AIFI under the Pillar 2 framework on the basis of its respective risk profiles and its risk management systems. An AIFI shall compute Basel III capital ratios in the following manner:

$$\begin{aligned} \text{CET 1 capital ratio} &= \frac{\text{CET 1 capital}}{\text{Total Risk Weighted Assets (RWAs)}} \\ \text{Tier 1 capital ratio} &= \frac{\text{Eligible Tier 1 capital}}{\text{Total RWAs}} \\ \text{Total Capital (CRAR)} &= \frac{\text{Eligible Total Capital}}{\text{Total RWAs}} \end{aligned}$$

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

A.2 Elements of regulatory capital and the criteria for their inclusion in the definition of regulatory capital

10. Total regulatory capital shall consist of the sum of the following categories:
- (i) Tier 1 Capital (going-concern capital)

- (a) CET 1
- (b) Additional Tier (AT) 1
- (ii) Tier 2 Capital (gone-concern capital)

A.3 Limits and minima

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

- (1) An AIFI shall maintain a minimum total capital (MTC) of 9 per cent of the total RWAs on an ongoing basis i.e., CRAR shall be at least 9 per cent on an ongoing basis. This shall be further divided into different components as described under following paragraphs.
- (2) CET 1 capital shall be at least 5.5 per cent of the total RWAs on an ongoing basis.
- (3) Tier 1 capital shall be at least 7 per cent of the total RWAs on an ongoing basis. Thus, within the minimum Tier 1 capital, AT 1 capital shall be admitted maximum at 1.5 per cent of the total RWAs.
- (4) Total capital (Tier 1 capital + Tier 2 capital) shall be at least 9 per cent of the total RWAs on an ongoing basis. Thus, within the minimum CRAR of 9 per cent, Tier 2 capital shall be admitted maximum up to 2 per cent of the total RWAs.

Explanation - If an AIFI has complied with the minimum CET 1 capital ratio, prescribed in these Directions, then excess CET 1 capital shall be admitted for compliance with the minimum Tier 1 of 7 per cent of the total RWAs. Further, if a bank has complied with the minimum CET 1 and Tier 1 capital ratios, prescribed in these Directions, then the excess CET 1 and / or AT 1 capital shall be admitted for compliance with the minimum CRAR of 9 per cent of the total RWAs.

- (5) The capital requirements for an AIFI are summarised in Table 1 below:

Table 1: Minimum capital requirement applicable to an AIFI

| Sr. No. | Regulatory Capital | As % to RWAs |
|---------|--|--------------|
| (i) | Minimum CET 1 Ratio | 5.5 |
| (ii) | AT 1 Capital | 1.5 |
| (iii) | Minimum Tier 1 Capital Ratio [(i) +(ii)] | 7.0 |
| (iv) | Tier 2 Capital | 2.0 |
| (v) | Minimum Total Capital Ratio (MTC) [(iii)+(iv)] | 9.0 |

B Common Equity Tier 1 (CET 1) capital

12. CET 1 capital shall comprise the following:

- (i) Common shares (paid-up equity capital) issued by an AIFI which 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) Revaluation reserves arising out of change in the carrying amount of an AIFI'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) AIFI is able to sell the property readily at its own shall and there is no legal impediment in selling the property;
 - (b) the revaluation reserves are shown under "Schedule: Reserves & Surplus" in the balance sheet of the AIFI;
 - (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 AIFI have not expressed a qualified opinion on the revaluation of the property;
 - (f) the instructions on valuation of properties and other specific requirements as mentioned in the [Reserve Bank of India \(All India Financial Institutions – Credit Risk Management\) Directions, 2025](#) addressed to a bank are strictly adhered to.

Revaluation reserves which do not qualify as CET 1 capital shall also not qualify as Tier 2 capital. An AIFI may choose to reckon revaluation reserves in CET 1 capital or Tier 2 capital at its discretion, subject to fulfilment of all the conditions specified above.

- (vi) An AIFI 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 CET 1 capital at a discount of 25 per cent subject to meeting the following conditions:
 - (a) the FCTR is shown under “Schedule: Reserves & Surplus” in the balance sheet of the AIFI;
 - (b) the external auditors of the AIFI have not expressed a qualified opinion on the FCTR.
- (vii) Other disclosed free reserves, if any;
- (viii) Balance in profit and loss account at the end of the previous financial year;
- (ix) An AIFI 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 shall 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 / surplus (balance of profits) transferred during last three years

Note - Cumulative net loss up to the quarter end shall be deducted while calculating CET 1 for the relevant quarter.

- (x) While calculating capital adequacy at the consolidated level, common shares issued by consolidated subsidiaries of an AIFI and held by third parties (i.e., minority interest) which meet the criteria for inclusion in CET 1 capital (refer to paragraph 23(2)); and
- (xi) Less: Regulatory adjustments / deductions applied in the calculation of CET 1 capital [i.e., to be deducted from the sum of items (i) to (x)].

Criteria for classification as common shares (paid-up equity capital) for regulatory purposes

13. Common shares to be included in CET 1 capital shall meet the criteria as under.

- (i) All common shares shall ideally be the voting shares. However, in rare cases, where an AIFI needs to issue non-voting common shares as part of CET 1 capital, they shall be identical to voting common shares of the issuing AIFI in all respects except the absence of voting rights. Limit on voting rights shall be applicable based on the provisions of respective statutes governing an individual AIFI.
- (ii) Represents the most subordinated claim in liquidation of an AIFI.
- (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) An AIFI 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 an AIFI 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 is 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 (in cases where capital instruments have a permanent write-down feature, this criterion is still deemed to be met by common shares). Within the highest quality capital, each instrument absorbs losses on a going concern basis proportionately and *pari passu* with all the others.
- (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 an AIFI shall not directly or indirectly have funded the purchase of the instrument. An AIFI shall also not extend loans against its own shares as this shall be construed as indirect funding of its own capital.
- (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 shall 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 AIFI.

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

- (xv) Paid up capital is clearly and separately disclosed in an AIFI's balance sheet.

C Additional Tier 1 (AT 1) capital

14. AT 1 capital of an AIFI shall consist of the sum of the following:

- (i) Perpetual Non-Cumulative Preference Shares (PNCPS), which comply with the regulatory requirements as specified in paragraph 16;
- (ii) Stock surplus (share premium) resulting from the issue of instruments included in AT 1 capital;
- (iii) Debt capital instruments eligible for inclusion in AT 1 capital, which comply with the regulatory requirements as specified in paragraph 17;
- (iv) Any other type of instrument generally notified by the Reserve Bank from time to time for inclusion in AT 1 capital;
- (v) While calculating capital adequacy at the consolidated level, AT 1 instruments issued by consolidated subsidiaries of an AIFI and held by third parties which meet the criteria for inclusion in AT 1 capital (refer to paragraph 15); and
- (vi) Less: Regulatory adjustments / deductions applied in the calculation of AT 1 capital [i.e., to be deducted from the sum of items (i) to (v)].

Criteria for loss absorption of AT 1 instruments

15. Paragraph 22 contains criteria for loss absorption through conversion / write-down / write-off of AT 1 instruments on breach of the pre-specified trigger and of all non-common equity regulatory capital instruments at the point of non-viability. An AIFI's non-common equity capital instruments shall meet these criteria for them to be considered as regulatory capital.

C.1 Criteria for inclusion of PNCPS in AT 1 Capital

16. The PNCPS shall be issued subject to extant legal provisions only in Indian rupees and shall meet the following terms and conditions to qualify for inclusion in AT 1 Capital for capital adequacy purposes:

- (1) Paid up status

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

(2) Amount

The amount of PNCPS to be raised shall be decided by the Board of an AIFI.

(3) Limits

While complying with minimum Tier 1 of 7 per cent of total RWAs, an AIFI shall not admit, PNCPS together with PDI in AT 1 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 an AIFI shall be included in total Tier 1 capital reported. Excess PNCPS and PDI shall 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 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, an AIFI 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 an AIFI shall receive prior approval of the Reserve Bank (Department of Regulation); and
- (iii) An AIFI shall not do anything which creates an expectation that the call shall be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date shall not be co-terminus with the call date. An AIFI may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and

Explanation - If an AIFI was 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 an AIFI will exercise calls on its other capital instruments. Therefore, an AIFI shall not be permitted to call an instrument if an AIFI intends to replace it with an instrument issued at a higher credit spread. This is applicable in cases of all AT 1 and Tier 2 instruments.

- (iv) An AIFI 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 an AIFI. Replacement issues shall be concurrent with but not after the instrument is called; or
 - (b) An AIFI demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Here, minimum refers to CET 1 ratio of 5.5 per cent of RWAs and total capital of 9.0 per cent of RWAs including 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) of paragraph 16(6). The Reserve Bank shall permit an AIFI to exercise the call only if it is convinced that an AIFI 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 an AIFI shall have the option (not obligation) to repurchase the instrument. In such a situation, the AIFI shall 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 AIFI shall 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, an AIFI 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 an AIFI 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 AIFI. 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, shall lie with the investors whereas, in case of the latter, it lies with the AIFI).
- (ii) An AIFI shall 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 AIFI; or
 - (b) An AIFI demonstrates that its capital position is well above the minimum capital requirements after the repurchase / buy-back / redemption.

(8) Dividend discretion

- (i) An AIFI 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 an issuing AIFI 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 an AIFI to make distributions / payments in kind.

- (ii) Cancellation of discretionary payments shall not be an event of default;
- (iii) An AIFI shall have full access to cancelled payments to meet obligations as they fall due;
- (iv) Cancellation of distributions / payments shall not impose restrictions on an AIFI except in relation to distributions to common stakeholders; and
- (v) Dividends shall be paid out of distributable items. As regards 'distributable items', it is clarified that the dividend on PNCPS shall be paid out of current year's profit only.
- (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 an AIFI's credit standing. For this purpose, any reference rate including a broad index which is sensitive to changes to an AIFI's own creditworthiness and / or to changes in the credit worthiness of the wider financial sector shall be treated as a credit sensitive reference rate. An AIFI desirous of offering floating reference rate shall take prior approval of the Reserve Bank (Department of Regulation) as regard permissibility of such reference rates.
- (viii) In general, it may be in order for an AIFI to have dividend stopper arrangement that stop dividend payments on common shares in the event the holders of AT 1 instruments are not paid dividend / coupon. However, dividend stoppers shall not impede the full discretion that the AIFI shall have at all times to cancel distributions / payments on the AT 1 instrument, nor shall they act in a way that shall hinder the re-capitalisation of the AIFI. For example, it shall not be permitted for a stopper on an AT 1 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 AT 1 instrument are resumed;
- (c) impede the normal operation of the AIFI 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 an AIFI 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 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 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 22.

(11) Prohibition on Purchase / Funding of PNCPS

Neither an AIFI nor a related party over which an AIFI exercises control or significant influence (as defined under relevant accounting standards) shall purchase PNCPS, nor shall an AIFI directly or indirectly shall fund the purchase

of the instrument. An AIFI shall also not grant advances against the security of PNCPS issued by them.

(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

All instances of non-payment of dividends shall be notified by the issuing AIFI to the Chief General Managers-in-Charge of Department of Regulation and Department of Supervision 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;
- (ii) Subordinated to the claims of PDIs, all Tier 2 regulatory capital instruments, depositors and general creditors of an AIFI; and
- (iii) is 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 an AIFI creditor.

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

- (i) Investment by Foreign Institutional Investors (FIIs) and Non-Resident Indians (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 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 an AIFI shall be subject to the applicable statutory/ regulatory limits.

- (ii) An AIFI shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities regarding issue of the instruments.

(16) Reporting of Issuances

- (i) An AIFI issuing PNCPS shall submit a report to the Chief General Manager-in-charge, Department of Regulation, Central Office, Reserve Bank, Mumbai, as per format prescribed in Annex 2 giving details of the debt raised as per the format prescribed below duly certified by the compliance officer of the AIFI, soon after the issue is completed.
- (ii) The issue-wise details of amount raised as PNCPS qualifying for AT 1 capital by an AIFI from FIIs / NRIs are required to be reported within 30 days of the issue to the Chief General Manager, Foreign Exchange Department, Reserve Bank, Central Office, Mumbai in the **proforma** given at Annex 1. The details of the secondary market sales / purchases by FIIs and the NRIs in these instruments on the floor of the stock exchange shall be reported by the custodians and designated a bank, respectively, to the Reserve Bank through the soft copy of the LEC Returns, on a daily basis, as prescribed in [Schedule 2](#) and [3](#) of the FEMA Notification No.20 dated May 03, 2000, as amended from time to time.

(17) Investment in AT 1 capital instruments (PNCPS) issued by a bank / another AIFI

- (i) An AIFI's investment in PNCPS issued by a bank and another AIFI 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 AIFI's total regulatory capital.
- (ii) AIFI's investments in PNCPS issued by a bank / another AIFI shall attract risk weight as provided in paragraphs 37 to 40, and paragraphs 181 to 184 of these directions, whichever applicable for capital adequacy purposes.
- (iii) An AIFI's investments in the PNCPS of a bank 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.

(18) Classification in the balance sheet

PNCPS shall be classified as capital and shown under 'Schedule - Capital' of the Balance sheet.

(19) PNCPS to retail investors

An AIFI 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 may 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 an AIFI] 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.2 Criteria for Inclusion of PDI in AT 1 Capital

- 17. The PDI that shall be issued as bonds or debentures by an AIFI shall meet the following terms and conditions to qualify for inclusion in AT 1 Capital for capital adequacy purposes:

Terms of Issue of instruments denominated in Indian rupees

(1) Paid-in status

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

(2) Amount

The amount of PDI to be raised shall be decided by the Board of an AIFI.

(3) Limits

While complying with minimum Tier 1 of 7 per cent of RWAs, an AIFI shall not admit, PDI together with PNCPS in AT 1 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 an AIFI shall be included in total Tier 1 capital reported. Excess PNCPS and PDI shall 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 is no maturity date and there are 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, an AIFI shall 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 an AIFI shall receive prior approval of the Reserve Bank (Department of Regulation);
- (iii) An AIFI shall not do anything which creates an expectation that the call shall be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date shall not be co-terminus with the call date. An AIFI may, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and
- (iv) An AIFI 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 AIFI Replacement issues can be concurrent with but not after the instrument is called; or

- (b) An AIFI demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Minimum refers to CET 1 ratio of 5.5 per cent of RWAs and total capital of 9.0 per cent of RWAs including 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) of paragraph 17(6). The Reserve Bank shall permit an AIFI to exercise the call only if it is convinced that an AIFI 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, then an AIFI shall have the option (not obligation) to repurchase the instrument. In such a situation, the AIFI 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) an AIFI shall 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, an AIFI 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 shall be repaid (e.g., through repurchase or redemption) only with the prior approval of the Reserve Bank and an AIFI 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 AIFI. 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, shall lie with the investors whereas, in case of the latter, it lies with the AIFI).

- (ii) An AIFI 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 AIFI; or
 - (b) An AIFI demonstrates that its capital position is well above the minimum capital requirements after the repurchase / buy-back / redemption.

(8) Coupon discretion

- (i) An AIFI 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 an issuing AIFI 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 an AIFI to make distributions / payments in kind.

- (ii) Cancellation of discretionary payments shall not be an event of default
- (iii) An AIFI shall have full access to cancelled payments to meet obligations as they fall due.
- (iv) Cancellation of distributions / payments shall not impose restrictions on an AIFI 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 shall 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, foreign currency translation reserve, investment reserve and reserves created on amalgamation.
 - (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 the AIFI shall make appropriation from the statutory reserves. In such cases, the AIFI shall report to the Reserve Bank within twenty-one days from the date of such appropriation.
 - (e) However, payment of coupons on PDIs from the reserves is subject to the issuing AIFI meeting minimum regulatory requirements for CET 1, Tier 1 and total capital ratios.
 - (f) To meet the eligibility criteria for perpetual PDIs, an AIFI shall ensure and indicate in its offer documents that it has full discretion at all times to cancel distributions / payments.
- (vi) the interest shall not be cumulative.
- (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 an AIFI's credit standing. For this purpose, any reference rate including a broad index which is sensitive to changes to an AIFI's own creditworthiness and / or to changes in the credit worthiness of the wider financial sector shall be treated as a credit sensitive reference rate. An AIFI desirous of offering floating reference rate may take prior approval of the Reserve Bank (DOR) as regards permissibility of such reference rates.
- (viii) An AIFI may have dividend stopper arrangement that stop dividend payments on common shares in the event the holders of AT 1 instruments are not paid dividend / coupon. However, dividend stoppers shall not

impede the full discretion that an AIFI shall have at all times to cancel distributions / payments on the AT 1 instrument, nor shall they act in a way that shall hinder the re-capitalisation of an AIFI. For example, it shall not be permitted for a stopper on an AT 1 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 AT 1 instrument are resumed;
- (c) impede the normal operation of the AIFI or any restructuring activity (including acquisitions / disposals).

A stopper shall act to prohibit actions that are equivalent to the payment of a dividend, such as an AIFI 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 18(9)). 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 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 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 22.

(11) Prohibition on purchase / funding of instruments

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

(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 coupons

All instances of non-payment of coupon shall be notified by the issuing AIFI to the Chief General Managers-in-Charge of Department of Regulation and Department of Supervision of 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 perpetual non-cumulative preference shares;
- (ii) subordinated to the claims of depositors, general creditors and subordinated debt of an AIFI;
- (iii) is neither secured nor covered by a guarantee of the issuer nor related entity or other arrangement that legally or economically enhances the seniority of the claim vis-à-vis an AIFI creditor.

(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 not exceeding 10 per cent of the issue and investment by each NRI not exceeding 5 per cent of the issue.

- (ii) An AIFI 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

An AIFI 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 applicable FEMA guidelines and requirements mentioned below:

- (i) The instruments shall comply with all terms and conditions as applicable to the instruments issued in Indian rupees.
- (ii) Not more than 49 per cent of the eligible amount shall be issued in foreign currency and / or in rupee denominated bonds overseas (Illustration given in the below table).

‘Eligible amount’ in this context shall mean the higher of:

- (a) 1.5 per cent of RWA or
- (b) Total AT 1 capital

as on March 31 of the previous financial year

- (iii) Instruments issued in foreign currency shall be outside the existing limit for foreign currency borrowings by Authorised Dealers, stipulated in terms of FMRD Master Direction No. 1/2016-17 dated July 5, 2016 on Risk Management and Inter-Bank Dealings as updated from time to time.
- (iv) An AIFI raising PDIs overseas shall obtain and keep on record a legal opinion from an advocate / attorney practising in the relevant legal jurisdiction, that the terms and conditions of issue of the instrument are in conformity with these Directions and shall be enforced in the concerned

legal jurisdiction and the applicable laws there do not stand in the way of enforcement of those conditions.

(17) Reporting of issuances

An AIFI issuing PDIs shall submit a report to the Chief General Manager-in-charge, Department of Regulation, Reserve Bank, Mumbai giving details of the debt raised as per the format prescribed below duly certified by the compliance officer of the AIFI, soon after the issue is completed.

(18) Investment in AT 1 debt capital instruments (PDIs) issued by another AIFI / a bank

- (i) An AIFI's investment in debt instruments issued by a bank and another AIFI 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 for cross holding of total regulatory capital among a bank / an AIFI prescribed under Exposure Norms applicable to an AIFI and also subject to cross holding limits.
- (ii) An AIFI's investments in debt instruments issued by a bank shall attract risk weight for capital adequacy purposes, as prescribed in paragraphs 37 to 40, and paragraphs 181 to 184 of these directions, whichever applicable.

(19) Classification in the balance sheet

The amount raised by way of issue of debt capital instrument may be classified under 'Schedule - Borrowings' in the Balance Sheet.

(20) PDIs to retail investors

An AIFI issuing Perpetual Debt Instruments to retail investors, subject to approval of its Board, shall adhere to the following conditions:

- (i) For floating rate instruments, an AIFI 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 may 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 an AIFI] 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.

(21) Illustration on the 'eligible amount' that can be raised as per paragraph 17(3) above is given below.

Considering that an AIFI has RWAs of ₹1000 crore as on March 31 of previous financial year

| | Scenario | Maximum amount of AT1 bonds that shall be raised overseas (in foreign currency and / or in rupee denominated bonds overseas) |
|---------|--|---|
| Case I | An AIFI had AT1 capital of less than or equal to 1.5% of RWAs as on March 31 of the previous financial year. Illustratively, an AIFI did not have any AT1 capital as on March 31 of the previous financial year. | Equals ₹. 7.35 crore (49% of 1.5% of RWAs). |
| Case II | An AIFI had AT1 capital more than 1.5% of RWAs as on March 31 of previous financial year. Illustratively, an AIFI had AT1 capital of ₹50 crore as on March 31 of the previous financial year. | Equals 49% of ₹50 crore i.e., ₹ 24.5 crore (49% of total AT1 capital as it is more than 1.5% of RWAs). |

Note - The amount of AT1 capital recognised for inclusion in Tier 1 capital shall be subject to the limits mentioned in paragraph 11 and paragraph 17(3).

D Tier 2 capital

18. Tier 2 capital shall consist of the following elements.

(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, investment reserve account, 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.

Provided that, an AIFI may either net off floating provisions from Gross NPAs to arrive at Net NPA or reckon it as part of its Tier 2 capital.

Note - For provision on unhedged foreign currency exposures, an AIFI may refer [Reserve Bank of India \(All India Financial Institutions – Credit Risk Management\) Directions, 2025](#).

(b) 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 an AIFI which comply with the regulatory requirements as specified in paragraph 20;

(iii) Preference Share Capital Instruments [Perpetual Cumulative Preference Shares (PCPS) / Redeemable Non-Cumulative Preference Shares (RNCPS) / Redeemable Cumulative Preference Shares (RCPS)] issued by

an AIFI which comply with the regulatory requirements as specified in paragraph 21;

- (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 an AIFI and held by third parties which meet the criteria for inclusion in Tier 2 capital (refer to paragraphs 23(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)].

Criteria for classification as Tier 2 capital for regulatory purposes

- 19. Paragraph 22 contains criteria for loss absorption through conversion / write-off of all non-common equity regulatory capital instruments at the point of non-viability.

D.1 Criteria for Inclusion of Debt Capital Instruments as Tier 2 Capital

- 20. The Tier 2 debt capital instruments that may be issued as bonds / debentures by an AIFI shall meet the following terms and conditions to qualify for inclusion as Tier 2 capital for capital adequacy purposes (the criteria relating to loss absorbency through conversion / write-down / write-off at the point of non-viability are furnished in paragraph 22):

Terms of issue of instruments denominated in Indian rupees

- (1) Paid-in status

The instruments shall be issued by an AIFI (i.e., not by any 'SPV' etc. set up by an AIFI 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 an AIFI.

(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 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 an AIFI's credit standing. An AIFI desirous of offering floating reference rate shall take prior approval of the Reserve Bank (Department of Regulation) as regards 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 the following conditions:

- (i) To exercise a call option an AIFI shall receive prior approval of the Reserve Bank (Department of Regulation); and
- (ii) An AIFI shall not do anything which creates an expectation that the call shall 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. An AIFI shall, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and
- (iii) An AIFI 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 an AIFI. Replacement issues shall be concurrent with but not after the instrument is called; or
 - (b) it demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Minimum refers to CET 1 ratio of 5.5 per cent of RWAs and total capital ratio of 9.0 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 the calls on account of these events is subject to the requirements set out in points (i) to (iii) of sub-paragraph 20(6). An AIFI shall be permitted to exercise the call only if the Reserve Bank is convinced that an AIFI was not in a position to anticipate these events at the time of issuance of these instruments as explained in case of AT 1 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 an AIFI nor a related party over which an AIFI exercises control or significant influence (as defined under relevant accounting standards) shall purchase the instrument, nor shall an AIFI directly or indirectly fund the purchase of the instrument. An AIFI shall also not grant advances against the security of the debt instruments issued by them.

(9) Reporting of non-payment of coupons

All instances of non-payment of coupon shall be notified by the issuing AIFI to the Chief General Managers-in-Charge of Department of Regulation and Department of Supervision of Reserve Bank, 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 an AIFI; 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 AIFI 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 subject 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) An AIFI shall comply with the terms and conditions, if any, stipulated by the SEBI / other regulatory authorities regarding issue of the instruments.

(12) Issuance of rupee denominated bonds overseas by an AIFI

An AIFI shall be 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 applicable FEMA guidelines.

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

An AIFI 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 24(7)(ii) of this Chapter.
- (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) An AIFI raising Tier 2 bonds overseas shall obtain and keep on record a legal opinion from an advocate / attorney practising in the relevant legal jurisdiction, that the terms and conditions of issue of the instrument are in conformity with these Directions and shall be enforced in the concerned legal jurisdiction and the applicable laws there do not stand in the way of enforcement of those conditions.

(14) Reporting of issuances

An AIFI issuing debt instruments shall submit a report to the Chief General Manager-in-Charge, Department of Regulation, Central Office, Reserve Bank, Mumbai giving details of the debt raised as per the format prescribed in Annex 2

duly certified by the compliance officer of an AIFI, soon after the issue is completed.

(15) Investment in Tier 2 debt capital instruments issued by other AIFIs / banks

- (i) An AIFI's investment in Tier 2 debt instruments issued by a bank and another AIFI 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 for cross holding of total regulatory capital among a bank / an FI prescribed under Exposure Norms applicable to an AIFI and also subject to cross holding limits.
- (ii) An AIFI's investments in Tier 2 instruments issued by a bank / another AIFI shall attract risk weight as per paragraphs 37 to 40, and paragraphs 181 to 184 of these directions, whichever applicable for capital adequacy purposes.

(16) Classification in the balance sheet

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

(17) Debt capital instruments to retail investors

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

- (i) For floating rate instruments, an AIFI 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 may 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 an AIFI] 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

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 shall be obtained.

D.2 Criteria for Inclusion of PCPS / RNCPS / RCPS as part of Tier 2 Capital

21. Terms of Issue of Instruments (the criteria relating to loss absorbency through conversion / write-down / write-off at the point of non-viability are furnished in paragraph 22)

(1) Paid-in status

The instruments shall be issued by an AIFI (i.e., not by any ‘SPV’ etc. set up by an AIFI for this purpose) and fully paid-in.

(2) Amount

The amount to be raised shall be decided by the Board of an AIFI.

(3) Maturity period

These instruments shall 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 Table 3 below for being eligible for inclusion in Tier 2 capital.

Table 3: 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 be either at a fixed rate or at a floating rate referenced to a market determined rupee interest benchmark rate. An AIFI desirous of offering floating reference rate shall take prior approval of the Reserve Bank (Department of Regulation) as regards permissibility of such reference rates.

(6) Optionality

These instruments shall not be issued with a 'put option'. However, an AIFI 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; and
- (ii) To exercise a call option an AIFI shall receive prior approval of the Reserve Bank (Department of Regulation); and
- (iii) An AIFI shall not do anything which creates an expectation that the call shall be exercised. For example, to preclude such expectation of the instrument being called, the dividend / coupon reset date shall not be co-terminus with the call date. An AIFI shall, at its discretion, consider having an appropriate gap between dividend / coupon reset date and call date; and
- (iv) An AIFI 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 an AIFI (replacement issues shall be concurrent with but not after the instrument is called); or
 - (b) An AIFI demonstrates that its capital position is well above the minimum capital requirements after the call option is exercised.

Explanation - Minimum here refers to CET 1 ratio of 5.5 per cent of RWAs and total capital ratio of 9.0 per cent of RWAs including 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) of paragraph 21(6). The Reserve Bank may permit an AIFI to exercise the call only if the Reserve Bank is convinced that an AIFI was not in a position to anticipate these events at the time of issuance of these instruments as explained in case of AT 1 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 an AIFI nor a related party over which an AIFI exercises control or significant influence (as defined under relevant accounting standards) shall purchase these instruments, nor shall an AIFI directly or indirectly fund the purchase of the instrument. An AIFI shall also not grant advances against the security of these instruments issued by them.

(9) Reporting of non-payment of coupon

All instances of non-payment of coupon shall be notified by an issuing AIFI to the Chief General Managers-in-Charge of Department of Regulation and Department of Supervision of the Reserve Bank, 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 an AIFI;
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 AIFI 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 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 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 a public sector bank shall be subject to the statutory / regulatory limit.
- (ii) An AIFI shall comply with the terms and conditions, if any, stipulated by SEBI / other regulatory authorities in regard to issue of the instruments.

(12) Reporting of issuances

An AIFI issuing these instruments shall submit a report to the Chief General Manager-in-Charge, Department of Regulation, Central Office, Reserve Bank, Mumbai giving details of the debt raised as per the format prescribed in Annex 2 duly certified by the compliance officer of an AIFI, soon after the issue is completed.

(13) Investment in these instruments issued by another AIFI / a bank

- (i) An AIFI's investment in these instruments issued by a bank and Another AIFI 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 AIFI's total regulatory capital prescribed under Exposure Norms applicable to an AIFI and also subject to cross holding limits.
- (ii) An AIFI's investments in these instruments issued by a bank and another AIFI shall attract risk weight for capital adequacy purposes as provided vide

paragraphs 37 to 40, and paragraphs 181 to 184 of these directions, whichever applicable.

(14) Classification in the balance sheet

These instruments shall be classified as 'Borrowings' under the Balance Sheet.

(15) PCPS / RNCPS / RCPS to retail investors

An AIFI 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 may 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 an AIFI] 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 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 AT 1 instruments at pre-specified trigger and of all non-equity regulatory capital instruments at the point of non-viability

22. For an instrument issued by an AIFI to be included in AT 1 (i.e., non-common) or in Tier 2 capital, in addition to criteria for individual types of non-equity regulatory capital instruments mentioned in paragraphs 16,17,20 and 21, it shall also meet or exceed minimum requirements set out in the following paragraphs.

Loss absorption of AT 1 Instruments at the pre-specified trigger

(1) Loss absorption features

- (i) AT 1 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, an AIFI shall issue AT1 instruments with either 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 an AIFI (a non-common equity instrument) and creates CET 1. 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 AT 1 instruments (PNCPS and PDI) shall be at least CET 1 capital of 6.125 per cent of RWAs. The write-down of any CET 1 capital shall not be required before a write-down of any AT 1 capital instrument.
- (ii) The conversion / write-down mechanism (temporary or permanent) which allocates losses to the AT1 instruments shall generate CET 1 capital under applicable Indian accounting standards. The instrument shall receive recognition in AT1 capital only up to the extent of minimum level of CET 1 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) An AIFI shall obtain and keep on its records a certificate from the statutory auditors clearly stating that the conversion / write-down mechanism chosen by an AIFI for a particular AT 1 issuance is able to generate CET 1 capital under the prevailing accounting standards. Further, an AIFI shall also obtain and keep on its records an external legal opinion confirming that the conversion or write-down of AT 1 capital instrument at the pre-specified trigger by the issuing AIFI is legally enforceable.

Note - Auditors 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 CET 1 capital).

- (iv) The aggregate amount to be written down / converted for all AT 1 instruments on breaching the trigger level shall be at least the amount needed to immediately return an AIFI's CET 1 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 AT 1 instruments to be converted / written-down subject to the amount of conversion / write-

down not exceeding the amount which shall be required to bring the CET 1 ratio to 5.5 per cent of RWAs.

- (v) The conversion / write-down may be allowed more than once in case an AIFI hits the pre-specified trigger level after the first conversion / write-down which was partial.
- (vi) The conversion / write-down of AT1 instruments is primarily intended to replenish the equity in the event it is depleted by losses. Therefore, an AIFI shall not use conversion / write-down of AT1 instruments to support expansion of balance sheet by incurring further obligations / booking assets. Accordingly, an AIFI whose CET 1 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 shall 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. An AIFI 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 CET 1 below 8 per cent shall not be subtracted. In other words, if CET 1 of an AIFI now is above the trigger level though it shall 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 an AIFI
 - (i) If an AIFI goes into liquidation before the AT 1 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 an AIFI goes into liquidation after the AT 1 instruments have been written down, the holders of these instruments shall have no claim on the proceeds of liquidation.
 - (iii) If an AIFI is amalgamated with any other institution before the AT 1 instruments have been written-down / converted, these instruments shall become part of the corresponding categories of regulatory capital of the new institutions emerging after the merger.
 - (iv) If an AIFI is amalgamated with any other institution after the AT 1 instruments have been written down temporarily, the amalgamated entity shall write-up these instruments as per its discretion.
 - (v) If an AIFI is amalgamated with any other institution after the non-equity regulatory capital instruments have been written-down permanently, these shall not be written-up by the amalgamated entity.
 - (vi) If the relevant authorities decide to reconstitute an AIFI or amalgamate an AIFI with any other institution, such an AIFI 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 paragraphs 22(6) to 22(10)) 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) An AIFI may issue AT1 instruments 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; An AIFI shall use any pricing formula such as weighted average price of shares during a particular period before conversion.
 - (ii) There shall be 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 shall end up holding the number of shares and attached

voting rights exceeding the legally permissible limits. An AIFI 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, an AIFI shall cap the number of shares and / or voting rights in accordance with relevant laws and regulations on Ownership and Governance of an AIFI. An AIFI 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, an AIFI shall immediately inform the Reserve Bank (Department of Regulation) 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 AIFI, the conversion price shall be determined based on the fair value of the AIFI'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 an issuing AIFI 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 shall the trigger event occur, the capital clause of each AIFI shall have to be suitably modified to take care of conversion aspects.

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

An AIFI 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 an AIFI 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

(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 an AIFI 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 'Point of Non-Viability (PONV) Trigger' stipulated below.
- (ii) The PONV Trigger event is the earlier of:
 - (a) a decision that a conversion (full conversion to common shares) or write-off (full and permanently write-off), without which the firm shall 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 shall have become non-viable, as determined by the relevant authority.
- (iii) The Write-off of any CET 1 capital shall not be required before the write-off of any non-equity (AT 1 and Tier 2) regulatory capital instrument.
- (iv) 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 an AIFI (or 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 may 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 AIFI 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 shall the trigger event occur.
- (vi) To ensure that these requirements are met, an AIFI shall obtain and keep on its records an external legal opinion confirming that the conversion or write-off feature of non-equity capital instruments (AT 1 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 an AIFI (or a group entity, where applicable) or write-off upon a trigger event. The Reserve Bank may also require the AIFI to submit additional information to ensure that such instruments are eligible for inclusion into regulatory capital.

(7) A non-viable AIFI

For the purpose of these guidelines, a non-viable AIFI shall be an AIFI 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 an AIFI shall be such that these are likely to result in financial losses and raising the CET 1 capital of an AIFI shall be considered as the most appropriate way to prevent an AIFI 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. In rare situations, an AIFI may also become non-viable due to non-financial problems, such as conduct of affairs of an AIFI 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

An AIFI facing financial difficulties and approaching a PONV shall be deemed to achieve viability if within a reasonable time in the opinion of the Reserve Bank, it

shall 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 an AIFI 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 so as to absorb losses at the PONV
- (i) Instruments may be issued with either of the following features:
 - (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) The provisions regarding treatment of AT 1 instruments in the event of winding-up, amalgamation, acquisition, re-constitution etc. of an AIFI as given in paragraph 22(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.
 - (iv) The provisions regarding fixation of conversion price, capping of number of shares / voting rights applicable to AT 1 instruments in terms of paragraph 22(4) above shall also be applicable for conversion of all non-common equity capital instruments (AT 1 and Tier 2 capital instruments) at the PONV.
 - (v) The provisions regarding order of conversion / write-down of AT 1 instruments as given in paragraph 22(5) above shall also be applicable for conversion / write-off of all non-common equity capital instruments (AT 1 and Tier 2 capital instruments) at the PONV.

(10) Criteria to determine the PONV

- (i) The above framework shall be invoked when an AIFI 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 an AIFI; and
 - (b) if left unattended, the weaknesses shall inflict financial losses on an AIFI and, thus, cause decline in its common equity level.
- (ii) The purpose of write-off and / or conversion of non-equity regulatory capital elements shall be to shore up the capital level of an AIFI. The Reserve Bank shall follow a two-stage approach to determine the non-viability of an AIFI. The **Stage 1** assessment shall consist of purely objective and quantifiable criteria to indicate that there is a *prima facie* case of an AIFI approaching non-viability and, therefore, a closer examination of an AIFI'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 an AIFI 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 an AIFI shall 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 shall 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 an AIFI including overseas subsidiaries, if any, shall be included in the consolidated capital of the 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 an AIFI 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 an AIFI or the subsidiary shall 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 an AIFI or the subsidiary shall 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 shall not matter whether or not it has same characteristics as an AIFI'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 shall be admitted only when it (and consequently the entire capital in that category) has the same characteristics as an AIFI'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 22(10)(v) above.
- (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 AIFI (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

23. Recognition of minority interest and other capital issued out of consolidated subsidiaries that is held by third parties shall be as per the following paragraphs.

(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 that is a bank shall be included in group's CET 1 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 would be excluded from the group's CET 1 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 an AIFI may receive recognition in CET 1 capital only if: (a) the instrument giving rise to the minority interest, if issued by an AIFI, 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 CET 1 capital shall be calculated as follows:

(i) Total minority interest meeting the two criteria above minus the amount of the surplus CET 1 capital of the subsidiary attributable to the minority shareholders.

(ii) Surplus CET 1 capital of the subsidiary is calculated as the CET 1 of the subsidiary minus the lower of: (a) the minimum CET 1 capital requirement of the subsidiary plus the capital conservation buffer (CCB) (i.e., 8.0 per cent of RWAs) and (b) the portion of the consolidated minimum CET 1 capital requirement plus the CCB (i.e., 8.0 per cent of consolidated RWAs) that relates to the subsidiary.

- (iii) The amount of the surplus CET 1 capital that is attributable to the minority shareholders is calculated by multiplying the surplus CET 1 by the percentage of CET 1 that is held by minority shareholders.

Note - For the purposes of treatment of minority interest, AIFIs, NBFCs regulated by the Reserve Bank and Primary Dealers shall also 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 an AIFI to third party investors (including amounts under paragraph 23(2)) may receive recognition in Tier 1 capital only if the instruments shall, if issued by an AIFI, meet all of the criteria for classification as Tier 1 capital. The amount of this capital that shall be recognised in Tier 1 capital shall be calculated as follows:

- (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 is 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 RWAs) and (b) the portion of the consolidated minimum Tier 1 capital requirement plus the CCB (i.e., 9.5 per cent of consolidated RWAs) that relates to the subsidiary.
 - (iii) The amount of the surplus Tier 1 capital that is attributable to the third-party investors is calculated by multiplying the surplus Tier 1 capital by the percentage of Tier 1 capital that is held by third party investors.
 - (iv) The amount of this Tier 1 capital that shall be recognised in AT 1 capital shall exclude amounts recognised in CET 1 capital under paragraph 23(2).
- (4) Treatment of minority interest corresponding to Tier 1 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 an AIFI to third party investors (including amounts under paragraphs 23(2) and 23(3)) shall receive recognition in total capital only

if the instruments, if issued by an AIFI, 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 is calculated as the Total Capital of the subsidiary minus the lower of: (a) the minimum Total Capital requirement of the subsidiary plus the capital conservation buffer (i.e., 11.5 per cent of risk weighted assets) and (b) the portion of the consolidated minimum Total Capital requirement plus the capital conservation buffer (i.e., 11.5 per cent of consolidated risk weighted assets) that relates to the subsidiary.
 - (iii) The amount of the surplus Total Capital that is attributable to the third-party investors is calculated by multiplying the surplus Total Capital by the percentage of Total Capital that is held by third party investors.
 - (iv) The amount of this total capital that shall be recognised in Tier 2 capital shall exclude amounts recognised in CET 1 capital under paragraph 23(2) and amounts recognised in Tier 1 capital under paragraph 23(3).
- (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. This example illustrates the treatment of minority interest and other capital issued out of subsidiaries to third parties, which is set out below.
- (i) A 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 CET 1 of Bank S | 7 | | |
| Investment in the AT 1 of Bank S | 4 | | |
| Investment in the Tier 2 of Bank S | 2 | | |

| Bank P Balance Sheet | | Bank S Balance Sheet | |
|------------------------|-----|------------------------|-----|
| Total | 113 | Total | 150 |
| Liabilities and equity | | Liabilities and equity | |
| Depositors | 70 | Depositors | 127 |
| Tier 2 | 10 | Tier 2 | 8 |
| AT 1 | 7 | AT 1 | 5 |
| Common equity | 26 | Common equity | 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 AT 1 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 |
| AT 1 | 4 | 1 | 5 |
| Tier 1 | 11 | 4 | 15 |
| Tier 2 | 2 | 6 | 8 |
| Total capital | 13 | 10 | 23 |

| Consolidated Balance Sheet | | |
|---|-----|---|
| Assets | | Remarks |
| Loans to customers | 250 | Investments of P in S aggregating ₹13 shall 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 | |
| AT 1 issued by subsidiary to third parties | 1 | (5-4) |
| AT 1 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 plus capital conservation buffer 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 |
| CET 1 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 |

Note – Illustration is based on Basel III minima as indicated in the BCBS document ‘Basel III: A global regulatory capital framework for more resilient banks and banking systems issued in December 2010 (rev June 2011)’. The CET 1 in the example should be read to include common shares plus retained earnings and reserves in Bank S.

- (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 23(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) |
| CET 1 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. AT 1 is calculated as the difference between CET 1 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 |
|----------------|--|---|---|
| CET 1 capital | 26 | 2.10 | 28.10 |
| AT 1 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 |

Note - Illustration is based on Basel III minima as indicated in the BCBS document 'Basel III: A global regulatory framework for more resilient banks and banking systems issued in December 2010 (rev June 2011)' The CET 1 in the example shall be read to include issued common shares plus retained earnings and reserves in Bank S.

G Regulatory adjustments / deductions

24. 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 CET 1 capital including any goodwill included in the valuation of significant investments in the capital of other financial and insurance entities which are outside the scope of regulatory consolidation. In terms of accounting standards 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 shall be attributable to goodwill, this shall be deducted from the CET 1 capital of an AIFI.

(ii) The full amount of the intangible assets shall be deducted net of any associated DTL which shall 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 CET 1 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 CET 1 capital which is attributed to the subsidiaries, in addition to deduction of goodwill and other intangible assets which pertain to the solo AIFI.
- (2) Deferred tax assets (DTAs)
- (i) DTAs associated with accumulated losses and other such assets shall be deducted in full from CET 1 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 CET 1 capital up to 10 per cent of an AIFI's CET1 capital, at the discretion of the AIFI [after the application of all regulatory adjustments mentioned from paragraph 24].
 - (iii) Further, the limited recognition of DTAs as at Paragraph 24(2)(ii) above along with limited recognition of significant investments in the common shares of unconsolidated financial (i.e., financial and insurance) entities in terms of paragraph 24(7)(ii)(c)(iii) taken together shall not exceed 15 per cent of the CET 1 capital, calculated after all regulatory adjustments set out in paragraph 24. However, an AIFI shall ensure that the CET 1 capital arrived at after application of 15 per cent limit shall in no case result in recognising any item more than the 10 per cent limit applicable individually (please refer to illustration at paragraph 24(2)(viii) below).
 - (iv) The amount of DTAs which is to be deducted from CET 1 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 CET 1 capital as at (i) and (ii) above.
- (v) The amount of DTAs which is not deducted from CET 1 capital [in terms of clause (ii) above] shall be risk weighted at 250 per cent as in the case of significant investments in common shares not deducted from an AIFI's CET 1 capital as indicated in paragraph 24(7)(ii)(c)(iii).
- (vi) Where the DTL is in excess of the DTA (excluding DTA associated with accumulated losses), the excess shall neither be adjusted against item (i) nor added to CET 1 capital.
- (vii) Application of these rules at consolidated level shall mean deduction of DTAs from the consolidated common equity, which is attributed to the subsidiaries, in addition to deduction of DTAs which pertain to the solo AIFI.
- (viii) Take an AIFI with ₹85 of common equity (calculated net of all deductions, including after the deduction of the specified items in full). The maximum amount of specified items that can be recognised by this AIFI in its calculation of CET 1 capital is ₹85 x 17.65 per cent = ₹15. Any excess above ₹ 15 shall be deducted from CET 1. If an AIFI 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, CET 1 after inclusion of the specified items, shall amount to ₹ 85 + ₹ 15 = ₹ 100. The percentage of specified items to total CET 1 shall equal 15 per cent.

(3) Cash flow hedge reserve

- (i) The amount of the cash flow hedge reserve which 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 CET 1 capital. This means that positive amounts shall be deducted, and negative amounts shall be added back.
- (ii) Application of these rules at consolidated level shall mean derecognition of cash flow hedge reserve from the consolidated CET 1 capital, which is attributed to the subsidiaries, in addition to derecognition of cash flow hedge reserve pertaining to the solo AIFI.

- (4) Gain-on-sale related to securitisation transactions, unrealised profits arising because of transfer of loans, and Security Receipts (SRs) guaranteed by the Government of India
- (i) An AIFI shall be guided by the paragraphs 80 to 118 of these directions in this regard.
 - (ii) Application of these rules at consolidated level shall mean deduction of gain-on-sale from the consolidated common equity which is recognised by the subsidiaries in their profit and loss account and / or equity, in addition to deduction of any gain-on-sale recognised by an AIFI at the solo level.
 - (iii) An AIFI shall be guided by the [Reserve Bank of India \(All India Financial Institutions – Transfer and Distribution of Credit Risk\) Directions, 2025](#), as amended from time to time, for the prudential treatment of unrealized profits arising because of transfer of loans and SRs guaranteed by Government of India.
- (5) Cumulative gains and losses due to changes in own credit risk on fair valued financial liabilities
- (i) An AIFI shall derecognise in the calculation of CET 1 capital, all unrealised gains and losses which have resulted from changes in the fair value of liabilities that are due to changes in the AIFI's own credit risk. In addition, with regard to derivative liabilities, derecognise all accounting valuation adjustments arising from the AIFI's own credit risk. The offsetting between valuation adjustments arising from the AIFI's own credit risk and those arising from its counterparties' credit risk shall not be allowed.
 - (ii) If an AIFI values its derivatives and Securities Financing Transactions (SFTs) liabilities taking into account its own creditworthiness in the form of Debit Valuation Adjustments (DVAs), then the AIFI shall deduct all DVAs from its CET 1 capital, irrespective of whether the DVAs arise due to changes in its own credit risk or other market factors. Thus, such deduction also includes the deduction of initial DVA at inception of a new trade. In other words, though an AIFI shall have to recognise a loss reflecting the credit risk of the counterparty [i.e., credit valuation adjustments (CVA)], the AIFI shall not recognise the corresponding gain due to its own credit risk in CET 1 capital.

- (iii) Application of these rules at consolidated level shall mean derecognition of unrealised gains and losses which have resulted from changes in the fair value of liabilities that are due to changes in the subsidiaries' credit risk, in the calculation of consolidated CET 1 capital, in addition to derecognition of any such unrealised gains and losses attributed to an AIFI 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 CET 1 capital (i.e., CET 1 capital shall not be increased through 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 CET 1 capital net of any associated DTL which shall be extinguished if the asset becomes impaired or derecognised under the relevant accounting standards.
 - (ii) Application of these rules 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 CET 1 capital, in addition to those pertaining to the solo AIFI.
- (7) Investments in the capital of banking, financial and insurance entities

(These rules shall be applicable to an AIFI's equity investments in banking, financial and insurance entities, even if such investments are exempted from 'capital market exposure' limit)

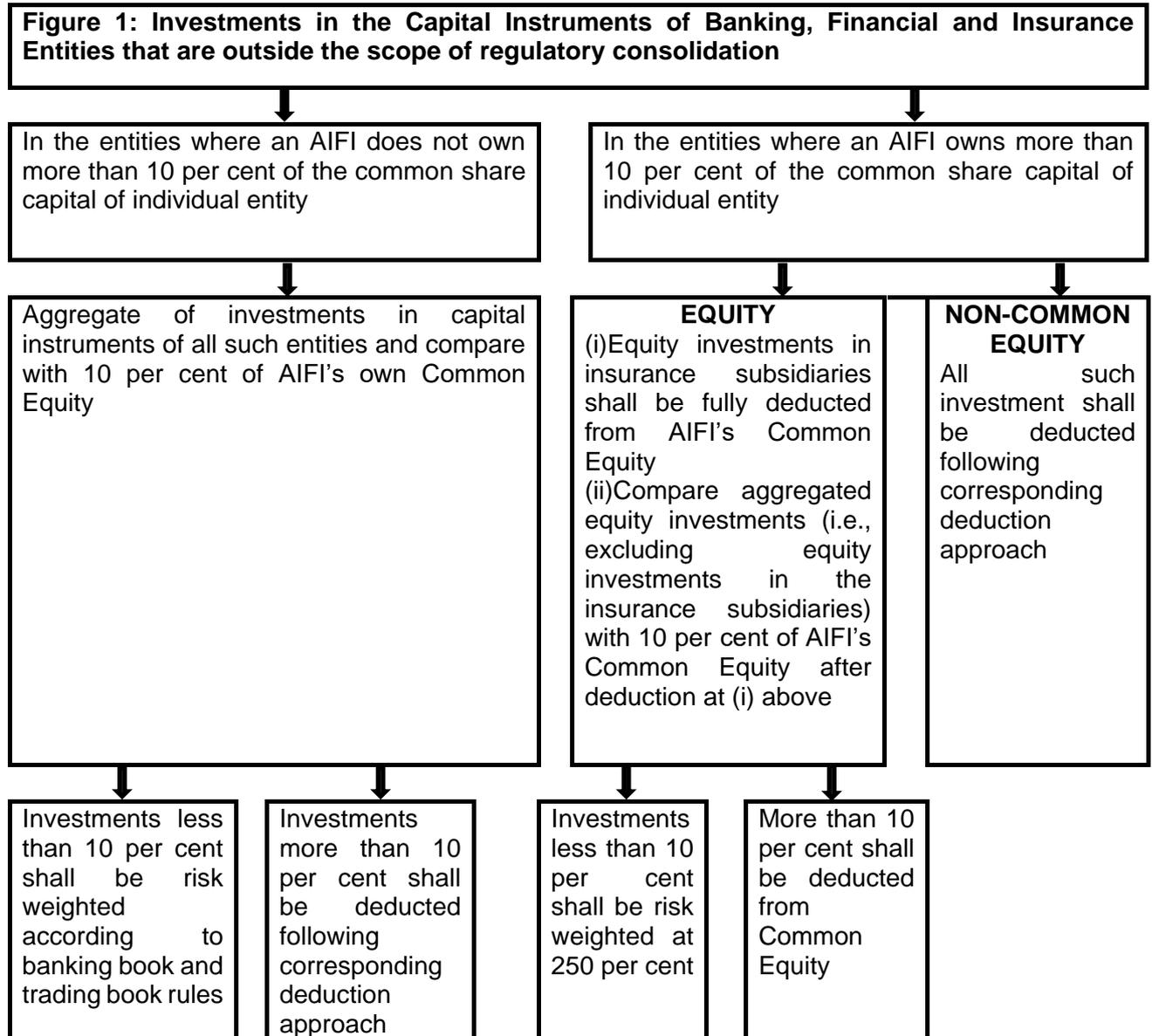
 - (i) Limits on an AIFI's investments in the capital of banking, financial and insurance entities
 - (a) The AIFI's investments in the capital instruments issued by banking, financial and insurance entities shall not exceed 10 per cent of its total regulatory capital (Tier 1 plus Tier 2), but after all deductions mentioned in paragraph 24.
 - (b) The AIFI shall not acquire any fresh stake in a bank's / an AIFI's equity shares, if by such acquisition, the investing AIFI's holding exceeds 5 per cent of the investee bank's / AIFI's equity capital.

- (c) The AIFI's equity investment in a single company / non-financial / commercial entity that is made in conformity with its statutory mandate shall not exceed 49 per cent of the equity of the investee company / entity. An AIFI can hold up to 49 per cent of equity of a company as a pledgee. However, if an AIFI ends up acquiring this in satisfaction of its claims, it shall be brought down below 10 per cent limit within three years.
- (d) Equity investment by the AIFI in a subsidiary company, financial services company, financial institution, stock and other exchanges shall not exceed 10 per cent of the AIFI's paid-up share capital and reserves.
- (e) Equity investment by the AIFI in companies engaged in non-financial services activities (except as permitted in sub-paragraph (c) above) shall be subject to a limit of 10 per cent of the investee company's paid up share capital or 10 per cent of the AIFI's paid up share capital and reserves, whichever is less.
- (f) Equity investments in any non-financial services company held by (a) an AIFI; (b) entities which are AIFI's subsidiaries, associates or joint ventures or entities directly or indirectly controlled by the AIFI; and (c) mutual funds managed by AMCs controlled by an AIFI shall in the aggregate not exceed 20 per cent of the investee company's paid-up share capital.
- (g) An AIFI's equity investments in subsidiaries and other entities that are engaged in financial services activities together with equity investments in entities engaged in non-financial services activities shall not exceed 20 per cent of an AIFI's paid-up share capital and reserves. The cap of 20 per cent shall not apply for investments classified under 'Held for Trading' category and which are not held beyond 90 days.
- (h) An indicative list of institutions which may be deemed to be financial institutions other than a bank and an insurance company for capital adequacy purposes is as under:

- (i) Asset Management Companies of Mutual Funds / Alternative Investment Funds / Private Equity Funds etc;
 - (ii) NBFCs;
 - (iii) HFCs;
 - (iv) Primary Dealers;
 - (v) Merchant Banking Companies;
 - (vi) Entities engaged in activities which are ancillary to the business of banking as defined under the BR Act, 1949; and
 - (vii) Central Counterparties (CCPs)
- (i) Investments made by a banking subsidiary / associate in the equity or non-equity regulatory capital instruments issued by its parent AIFI shall be deducted from such subsidiary's regulatory capital following corresponding deduction approach, in its capital adequacy assessment on a solo basis. The regulatory treatment of investment by the non-banking financial subsidiaries / associates in the parent AIFI's regulatory capital shall, however, be governed by the applicable regulatory capital norms of the respective regulators of such subsidiaries / associates.
- (ii) Treatment of an AIFI's investments in the capital instruments issued by banking, financial and insurance entities within limits

A schematic representation of treatment of an AIFI'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 24(7)(i) shall be subject to the following rules:

Note - For this purpose, investments held in AFS / HFT category shall be reckoned at their market values, whereas those held in HTM category shall be reckoned at values appearing in the balance sheet of the AIFI.



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

Reciprocal cross holdings of capital shall be fully deducted. An AIFI shall apply a 'corresponding deduction approach' to such investments in the capital of another bank, other financial institutions and insurance entities. This means the deduction shall be applied to the same component of capital (CET 1, AT 1 and Tier 2 capital) for which the capital shall qualify if it was issued by the AIFI itself. For this purpose, a holding shall be treated as reciprocal cross holding if the investee

entity has also invested in any class of an AIFI's capital instruments which shall not necessarily be the same as an AIFI's holdings.

(b) Investments in the capital of banking, financial and insurance entities which are outside the scope of regulatory consolidation and where an AIFI does not own 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 and where an AIFI 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, an AIFI shall look through holdings of index securities to determine their underlying holdings of capital.

Explanation - Indirect holdings are exposures or part of exposures that, if a direct holding loses its value, shall result in a loss to a 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 an AIFI has invested does not meet the criteria for CET 1, AT 1, or Tier 2 capital of an AIFI, 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, an AIFI may 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 sub-paragraph (i) above, in aggregate exceed 10 per cent of an AIFI's CET 1 capital (after applying all other regulatory adjustments in full listed prior to this one), then 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 shall qualify if it was issued by the AIFI itself. Accordingly, the amount to be deducted from CET 1 shall be calculated as the total of all holdings which in aggregate exceed 10 per cent of the AIFI's CET1 capital (as per above) multiplied by the CET 1 capital holdings as a percentage of the total capital holdings. This shall result in a CET 1 capital deduction which corresponds to the proportion of total capital holdings held in common equity. Similarly, the amount to be deducted from AT 1 capital shall be calculated as the total of all holdings which in aggregate exceed 10 per cent of the AIFI's CET 1 capital (as per above) multiplied by the AT 1 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 AIFI's CET 1 capital (as per above) multiplied by the Tier 2 capital holdings as a percentage of the total capital holdings. (Please refer to illustration given in paragraph 24(7)(ii)(b)(vi)).
- (iii) If, under the corresponding deduction approach, an AIFI shall make a deduction from a particular tier of capital and it does not have enough of capital under that tier capital to meet that deduction, the shortfall shall be deducted from the next higher

tier of capital (e.g., if an AIFI does not have enough AT 1 capital to satisfy the deduction, the shortfall shall be deducted from CET 1 capital).

- (iv) Investments below the threshold of 10 per cent of an AIFI's CET 1 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 mentioned in this Master Direction. 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 CET 1 capital of the investing AIFI as indicated in paragraphs 37 to 40, paragraphs 181 to 184, and paragraph 191.
- (v) For risk weighting of investments in 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 an AIFI

| | (Amount in ₹ crore) |
|------------------------------|---------------------|
| Paid-up equity capital | 300 |
| Eligible Reserve and Surplus | 100 |
| Total common equity | 400 |
| Eligible AT 1 capital | 15 |
| Total Tier 1 capital | 415 |

| | |
|-------------------------|-----|
| Eligible Tier 2 capital | 135 |
| Total Eligible capital | 550 |

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

| Entity | Total Capital of the Investee entities | | | | Investments of AIFI in these entities | | | |
|--|--|------|--------|---------------|---------------------------------------|------|--------|------------------|
| | CET 1 | AT 1 | Tier 2 | Total capital | CET 1 | AT 1 | 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 AIFI 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 AIFI does not own more than 10 per cent of the Issued common share capital of the entity

| C-1: Bifurcation of Investments of AIFI into Trading and Banking Book | | | | |
|---|-------|------|--------|-------------------|
| | CET 1 | AT 1 | Tier 2 | Total investments |
| 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 | | | | |
| AIFI's aggregate investment in CET 1 of A & B | | | | 26 |
| AIFI's aggregate investment in AT 1 capital of A & B | | | | 10 |
| AIFI's aggregate investment in Tier 2 capital of A & B | | | | 15 |
| Total of AIFI's investment in A and B | | | | 51 |
| AIFI CET 1 | | | | 400 |
| 10% of AIFI's CET 1 | | | | 40 |

| | |
|---|----|
| AIFI's total holdings in capital instruments of A & B more than 10% of An AIFI CET 1 (51-40) | 11 |
| <i>Note</i> - Investments in both A and B shall 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 AIFI'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 CET 1 of an AIFI (26 / 51) *11 | 5.60 | | |
| Amount to be deducted from AT 1 of an AIFI (10 / 51) *11 | 2.16 | | |
| Amount to be deducted from Tier 2 of an AIFI (15 / 51) *11 | 3.24 | | |
| Total Deduction | 11.00 | | |
| CET 1 investments of an AIFI in A & B to be risk weighted | 20.40 (26-5.60) | 8.63 (11 / 26) *20.40 | 11.77 |
| AT 1 capital investments of an AIFI in A & B to be risk weighted | 7.84 (10-2.16) | 4.70 | 3.14 |
| Tier 2 capital investments of an AIFI 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

| | |
|--|-----------|
| AIFI's aggregate investment in CET 1 of C & D | 45 |
| AIFI's aggregate investment in AT 1 capital of C & D | 15 |
| AIFI's aggregate investment in Tier 2 capital of C & D | 5 |
| Total of AIFI's investment in C and D | 65 |
| AIFI's CET 1 | 400 |
| 10% of AIFI's CET 1 | 40 |
| AIFI'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 CET 1 of an AIFI (excess over 10%) | 5 |
| Amount to be deducted from AT 1 of an AIFI (all AT 1 investment to be deducted) | 15 |
| Amount to be deducted from Tier 2 of an AIFI (all Tier 2 investments to be deducted) | 5 |
| Total deduction | 25 |
| CET 1 investments of an AIFI in C & D to be risk weighted (up to 10%) | 40 |

(e) Total Regulatory Capital of an AIFI after Regulatory Adjustments

| | Before deduction | Deductions as per Table C-3 | Deductions as per Table D-1 | After deductions |
|--|------------------|-----------------------------|-----------------------------|------------------|
| CET 1 | 400.00 | 5.61 | 5.00 | 387.24* |
| AT 1 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 AT 1 capital of an AIFI after deduction, which has to be deducted from the next higher category of capital i.e., CET 1. | | | | |

(c) **Significant investments in the capital of banking, financial and insurance entities which are outside the scope of regulatory consolidation**

- (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 an AIFI owns more than 10 per cent of the issued common share capital of the issuing entity or where the entity is an affiliate of an AIFI. In addition:
- (a) Investments include direct, indirect and synthetic holdings of capital instruments. For example, the AIFI shall look through holdings of index securities to determine their 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 an AIFI has invested does not meet the criteria for CET 1, AT 1, or Tier 2 capital of a 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, an AIFI shall 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 an AIFI is defined as a company that controls, or is controlled by, or is under common control with, the AIFI. Control of a company is defined as (a) ownership, control, or holding with power to vote 20 per cent or more of a class of voting securities of the company; or (b) 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, shall result in a loss to a 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 shall qualify if it was issued by an AIFI itself. If an AIFI shall make a deduction from a particular tier of capital and it does not have enough of that tier of capital to satisfy that deduction, the shortfall shall be deducted from the next higher tier of capital (e.g., if an AIFI does not have enough AT 1 capital to satisfy the deduction, the shortfall shall be deducted from CET 1 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 an AIFI's CET 1 capital (after the application of all regulatory adjustments) shall be deducted while calculating CET 1 capital. The amount

that is not deducted (up to 10 per cent if an AIFI's CET 1 capital invested in the equity capital of such entities) in the calculation of CET 1 capital shall be risk weighted at 250 per cent (refer to illustration given in paragraph 24(7)(ii)(b)(vi)). However, in certain cases, such investments in both scheduled and non-scheduled commercial banks shall be fully deducted from CET 1 capital of an investing AIFI as indicated in paragraphs 37 to 40, paragraphs 181 to 184, and paragraph 191.

- (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 24(7)(ii)(b) and 24(7)(ii)(c) above, the following rules may be observed:
- (a) If the amount of investments made by the mutual funds / index funds / alternative investment funds / private equity funds / investment companies in the capital instruments of the financial entities is known; the indirect investment of an AIFI in such entities shall be equal to the AIFI'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 / alternative investment funds / private equity funds / investment companies in the capital instruments of the financial entities is not known but, as per the investment policies / mandate of these entities such investments are permissible; the indirect investment shall be equal to AIFI's investments in these entities multiplied by maximum permissible limit which these entities are authorized to invest in the financial entities' capital instruments.
 - (c) If neither the amount of investments made by the mutual funds / index funds / alternative investment 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 an AIFI in these entities shall be treated as indirect investment in financial entities. An AIFI shall note

that this method does not follow corresponding deduction approach i.e., all deductions shall be made from the Common Equity Tier 1 capital even though, the investments of such entities are in the AT 1 / Tier 2 capital of the investing AIFI.

- (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 paragraph 24(7)(ii) 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.
 - (ii) the consolidated CET 1 capital of the group shall be taken into account.
- (8) When returns of the investors of the capital issues are counter guaranteed by an AIFI, such investments shall not be considered as regulatory capital for the purpose of capital adequacy.
- (9) Equity investment in non-financial subsidiaries
- As indicated in paragraphs 8(2) and 8(5), equity investments in non-financial subsidiaries shall be fully deducted from the consolidated and solo CET1 capital of an AIFI respectively, after making all the regulatory adjustments as indicated in above paragraphs.
- (10) Intra group transactions and exposures
- Intra-group exposures beyond permissible limits subsequent to March 31, 2016, if any, shall be deducted from CET 1 capital of a bank. The same instructions shall apply to an AIFI.
- Note* - Permissible limits are as mentioned in the [Reserve Bank of India \(All India Financial Institutions – Concentration Risk Management\) Directions, 2025](#)
- (11) Investment by an AIFI in the subordinated units of any AIF scheme

Contribution by an AIFI in the form of subordinated units of any AIF scheme shall be deducted proportionately from both Tier 1 and Tier 2 capital (wherever applicable).

Note - An AIFI shall also refer to [Reserve Bank of India \(All India Financial Institutions – Undertaking of Financial Services\) Directions, 2025](#) in this regard.

- (12) In terms of [Reserve Bank of India \(All India Financial Institutions – Credit Facilities\) Directions, 2025](#), if an AIFI is the Default Loss Guarantee (DLG) provider, it shall deduct full amount of the DLG, which is outstanding, from its capital.

H Transitional arrangements for an AIFI

25. Capital instruments already issued by an AIFI which no longer qualify as regulatory capital under Basel III shall be allowed to be counted as Tier 1 or Tier 2 as per the existing rules until their maturity or the first call date, whichever is earlier. All capital instruments issued by an AIFI after these Directions come into effect shall comply with the requirements set out in these Directions.

Chapter IV

Risk weighted assets (RWAs)

A Capital charge for credit risk

A.1 General

26. An AIFI shall follow the standardised approach for computing the capital charge for credit risk. Under this approach, an AIFI shall rely upon the ratings assigned by the external credit rating agencies or specific risk weights prescribed in these directions, as the case may be.

A.2 Claims on domestic sovereigns

27. Both fund-based and non-fund-based claims on the central government shall attract a zero per cent risk weight. Central Government guaranteed claims shall attract a zero per cent risk weight.

28. Direct loan / credit / overdraft exposure, if any, of an AIFI 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. The claims on ECGC shall also attract a risk weight of 20 per cent.

29. The risk weight applicable to claims on central government exposures shall also apply to the claims on the Reserve Bank and DICGC. The Lines of Credit (LOCs) extended by EXIM Bank at the behest of Central Government and secured by guarantee of the Central Government shall attract zero per cent risk weight. The risk weight of zero per cent shall be applicable in respect of exposures guaranteed under any existing or future schemes launched by 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) 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 159 to 168 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, 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 lodgement, and the lodgement shall be permitted within sixty days from the date of default.
- (v) Some illustrative examples of risk weights applicable on credit facilities 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 <u>Counterparty / Regulatory Retail Portfolio (RRP) RW as applicable.</u> <i>Note - The maximum capital charge shall be capped at a notional level arrived by treating</i> |

| Scheme name | Guarantee Cover | Risk Weight |
|---|--|---|
| | | 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 - <u>Counterparty / Regulatory Retail Portfolio (RRP) RW as applicable.</u> |
| 3. Credit Guarantee Fund for Micro Units (CGFMU) | <p><u>Micro Loans</u></p> <p>The first loss to the extent of 3% of amount in default.</p> <p>Out of the balance, guarantee will be to a maximum extent of 75% of the amount in default in the crystallized portfolio</p> | <p>First loss of 3% amount in default – Full capital deduction</p> <p>72.75% of the amount in default - 0% RW, subject to maximum of</p> $((15\% * CP) - C) * \left[\frac{SLA}{CP} \right]$ <p>Where-</p> <ul style="list-style-type: none"> 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 <p>Balance amount in default - <u>Counterparty / RRP RW as applicable.</u></p> <p><i>Note</i> - The maximum capital charge shall be capped at a notional level arrived by treating the entire exposure as unguaranteed.</p> |

| Scheme name | Guarantee Cover | Risk Weight |
|---|---|---|
| 4.CGTMSE guarantee coverage for Micro-Enterprises | <u>up to ₹5 lakh</u> 85% of the amount in default subject to a maximum of ₹4.25 lakh <u>Above ₹5 lakh & up to ₹50 lakh</u> 75% of the amount in default subject to a maximum of ₹37.50 lakh <u>Above ₹50 lakh & up to ₹200 lakh</u> 75% of the amount in default subject to a maximum of ₹150 lakh | Guaranteed amount in default – <u>0% RW*</u> Balance amount in default - <u>Counterparty / RRP RW as applicable.</u> |
| *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) Guarantee coverage, first loss percentage and payout cap ratio may be factored in as given below and as amended from time to time in the respective schemes
- (b) The above regulatory stipulation shall be applicable to a bank to the extent it is recognised as eligible MLIs under the respective schemes.

30. 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 paragraph 56 to 61.

31. 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

32. Subject to paragraph 33 below, claims on foreign sovereigns and their central banks shall attract risk weights as per the rating assigned to them by international rating agencies as follows:

Table4: Claims on Foreign Sovereigns / Central 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 (%) | 0 | 20 | 50 | 100 | 150 | 100 |

* Standard & Poor's

33. Claims on the foreign sovereigns or foreign central banks in their jurisdiction, denominated in domestic currency of that jurisdiction, met out of the resources of the same currency shall attract a risk weight of zero per cent. However, in case a Host Supervisor requires a more conservative treatment to such claims in the books of the foreign branches of an AIFI, they shall adopt the requirements prescribed by the Host Country Supervisors for computing capital adequacy.

Explanation –

- (i) The risk weight assigned to an investment in US Treasury Bills by an AIFI's branch in Paris, irrespective of the currency of funding, shall be determined by the rating assigned to the Treasury Bills, as indicated in Table 4.
- (ii) The risk weight assigned to an investment in US Treasury Bills by an AIFI's branch 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 an AIFI's branch in New York. In case an AIFI's branch 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 4.

A.4 Claims on public sector entities (PSEs)

34. Claims on domestic public sector entities shall be risk weighted in a manner similar to claims on Corporates, as mentioned on paragraphs 42 to 44.
35. Claims on foreign PSEs shall be risk weighted as per the rating assigned by the international rating agencies as under:

Table 5: 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 |
| RW (%) | 20 | 50 | 100 | 150 | 100 |

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

36. Claims on the BIS, the IMF and the following eligible MDBs evaluated by the Basel Committee on Banking Supervision (BCBS) shall be treated similar to claims on scheduled commercial 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 and
- (xi) Council of Europe Development Bank
- (xii) International Finance Facility for Immunization (IFFI)
- (xiii) Asian Infrastructure Investment Bank (AIIB)

A.6 Claims on a bank (Exposure to capital instruments)

37. In case of an AIFI's investment in capital instruments of banks, the following such investments shall not be deducted, but shall attract appropriate risk weights as elaborated in Table 6:

- (i) Investments in capital instruments of a bank where an investing AIFI holds not more than 10 per cent of the issued common shares of an investee bank, 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 an investing AIFI; and
- (b) The equity investment in the investee entities is outside the scope of regulatory consolidation.
- (ii) Equity investments in a bank where the investing AIFI holds more than 10 per cent of the issued common shares of an investee bank, 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 AIFI.
- (b) The equity investment in the investee entities is outside the scope of regulatory consolidation.

Table 6: Claims on a bank 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 Common Equity Tier 1 capital (CET1) including applicable capital conservation buffer (CCB) (%) of the investee bank under Basel III / Total Capital of other banks (where applicable) | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (ii) | All other claims | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (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, whichever is higher | 250 | 20 | 125% or the risk weight as per the rating of the instrument or counterparty, whichever is higher | 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 Common Equity Tier 1 capital (CET1) including applicable capital conservation buffer (CCB) (%) of the investee bank under Basel III / Total Capital of other banks (where applicable) | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (ii) | All other claims | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (ii) | All Other Claims |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| 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 |
| 0 to < 3 | 350 | 450 | 150 | 625 | Full deduction* | 350 |

| | 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 Common Equity Tier 1 capital (CET1) including applicable capital conservation buffer (CCB) (%) of the investee bank under Basel III / Total Capital of other banks (where applicable) | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (ii) | All other claims | Investments referred to in paragraph 37 (i) | Investments referred to in paragraph 37 (ii) | All Other Claims |
| 1 | 2 | 3 | 4 | 5 | 6 | 7 |
| Negative | 625 | Full deduction* | 625 | Full deduction* | Full deduction* | 625 |

* The deduction shall be made from CET 1 Capital.

Note - For claims held in trading book, a bank shall refer the paragraphs 181 and 191 under 'capital charge for market risk'.

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

Table 7: Claims on a Foreign Bank – 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 |

If an AIFI reckons the exposure on the original counterparty, it shall attract the risk weight as per Table 7, if the counterparty is a person resident in India, or 150 per cent if the counterparty is a person resident outside India.

39. 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 a bank complies with the minimum CRAR prescribed by the concerned bank regulator(s).

Explanation - For example, a Euro denominated claim on a European bank in Paris, which is funded from out of the Euro denominated deposits of an AIFI in Paris, shall attract a 20 per cent risk weight irrespective of the rating of the claim,

provided the 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 6.

40. However, in case a Host Country Supervisor requires a more conservative treatment for such claims in the books of the foreign branches of an AIFI, they shall adopt the requirements prescribed by the Host Supervisor for computing capital adequacy.

A.7 Claims on Primary Dealers

41. Claims on Primary Dealers shall be risk weighted in a manner similar to claims on corporates.

A.8 Claims on corporates and NBFCs

42. 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. Exposure to CICs, rated as well as unrated, shall be risk-weighted at 100 per cent. Tables 8.1 and 8.2 indicates the risk weight applicable to claims on corporates and 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 8.1: 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 8.2: Short Term Claims on Corporates and NBFCs (excluding CICs) - Risk Weights

| CARE | CRISIL Ratings Limited | India Ratings and Research Private Limited (India Ratings) | ICRA | Acuite Ratings & Research Ltd. (Acuite) | INFOMERICS | Brickwork India Ratings Private Limited | (%) |
|-------------|-------------------------------|---|-------------|--|-------------------|--|------------|
| | | | | | | | |

| | | | | | | | |
|-------------|---------------|------------|-------------|---------------|-------------------|------------------|-----|
| CARE A1+ | CRISIL A1+ | IND A1+ | ICRA A1+ | Acuité A1+ | INFOMERICS A1+ | Brickwork A1+ | 20 |
| CARE A1 | CRISIL A1 | IND A1 | ICRA A1 | Acuité A1 | INFOMERICS A1 | Brickwork A1 | 30 |
| CARE A2 | CRISIL A2 | IND A2 | ICRA A2 | Acuité A2 | INFOMERICS A2 | Brickwork A2 | 50 |
| CARE A3 | CRISIL A3 | IND A3 | ICRA A3 | Acuité A3 | INFOMERICS A3 | Brickwork A3 | 100 |
| CARE A4 & D | CRISIL A4 & D | IND A4 & D | ICRA A4 & D | Acuité A4 & D | INFOMERICS A4 & D | Brickwork A4 & D | 150 |
| Unrated | Unrated | Unrated | Unrated | Unrated | Unrated | Unrated | 100 |

Note -

- (i) No claim on an unrated corporate may be given a risk weight preferential to that assigned to its sovereign of incorporation.
 - (ii) 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.
 - (iii) 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.
43. 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 shall also consider whether the credit quality of unrated corporate claims held by individual an AIFI shall warrant a higher standard risk weight.
44. The claims on non-resident corporates shall be risk weighted as under as per the ratings assigned by international rating agencies.

Table 9: Claims on Non-Resident Corporates – 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 |
| RW (%) | 20 | 50 | 100 | 150 | 100 |

Note –

- (i) No claim on an unrated corporate may be given a risk weight preferential to that assigned to its sovereign of incorporation.
- (ii) All unrated claims having aggregate exposure from banking system of more than ₹ 200 crore shall attract a risk weight of 150 per cent.
- (iii) Claims 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%.

A.9 Claims included in the regulatory retail portfolios

- 45. Claims (including both fund-based and non-fund based) that meet all the four criteria listed in paragraph 47 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 56 to 61 for non-performing assets.
- 46. 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 48 to 52) or claims secured by commercial real estate (refer paragraphs 53 to 53);
 - (iii) Loans and Advances to AIFI'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;
 - (vi) Alternative Investment Funds.
- 47. The qualifying criteria for the claims to be included in the regulatory retail portfolios 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 shall include but not be restricted to individual and HUF; small business shall 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., installment loans and leases, student and educational loans) and small business facilities and commitments.
- (iii) Granularity Criterion – This criterion implies that no aggregate exposure to one counterpart shall 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 an AIFI's aggregated exposure on both businesses). While an AIFI may appropriately use the group exposure concept for computing aggregate exposures, they shall evolve adequate systems to ensure strict adherence with this criterion. NPAs under retail loans are to 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.

Note –

- (i) 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.
- (ii) The Reserve Bank shall evaluate at periodic intervals the risk weight assigned to the regulatory retail portfolio with reference to the default experience for these exposures. As part of the supervisory review process, the Reserve Bank shall also consider whether the credit quality of regulatory retail claims held by an AIFI shall warrant a standard risk weight higher than 75 per cent.

A.10 Claims secured by residential property

48. Lending to individuals meant for acquiring residential property which are fully secured by mortgages on the residential property that is or shall be occupied by the borrower, or that is rented, shall be risk weighted as indicated as at Tables 10.1, 10.2, 10.3 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 an AIFI in the denominator.

Table 10.1: 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) | NA | 75 |

Table 10.2: 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 | NA | 75 |
| (c) Commercial Real Estate (CRE) | NA | 100 |

49. 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 10.3: 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 |

Notes:

- (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) An AIFI's exposures to third dwelling unit onwards to an individual shall also be treated as CRE exposures for risk weight purpose.
50. 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 an AIFI has extended finance.
51. 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.
52. Investments in Mortgage Backed Securities (MBS) backed by exposures as at paragraph 48 above shall be governed by the guidelines pertaining to

securitisation exposures – [Reserve Bank of India \(All India Financial Institutions – Securitisation Transactions\) Directions, 2025](#) (refer to paragraphs 80 and 118 below).

A.11 Claims classified as commercial real estate exposure

53. CRE exposure is described in the guidelines issued [Reserve Bank of India \(All India Financial Institutions – Credit Facilities\) Directions, 2025](#).
54. CRE (RH) will attract a risk weight of 75 per cent as mentioned in Table 10.1 and 10.2 above. CRE other than CRE (RH) shall attract a risk weight of 100 per cent.
55. Investments in mortgage backed securities (MBS) backed by exposures as at paragraph 52 above shall be governed by the guidelines pertaining to securitisation exposures - [Reserve Bank of India \(All India Financial Institutions – Securitisation Transactions\) Directions, 2025](#) (refer to paragraphs 80 and 118).

A.12 Non-performing assets (NPAs)

56. The unsecured portion of NPA (other than a qualifying residential mortgage loan which is addressed in paragraph 61), 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;
 - (iii) 50 per cent risk weight when specific provisions are at least 50 per cent of the outstanding amount of the NPA
57. 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.
58. For defining the secured portion of the NPA, eligible collateral shall be the same as recognised for credit risk mitigation purposes (paragraph 153). Hence, other forms of collateral like land, buildings, plant, machinery, current assets, etc., shall not be reckoned while computing the secured portion of NPAs for capital adequacy purposes.

59. 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.
60. The above collaterals (paragraph 59) shall be recognised only where an AIFI is having clear title to realise the sale proceeds thereof and shall appropriate the same towards the amounts due to an AIFI. An AIFI's title to the collateral shall be well documented. These forms of collaterals are not recognised anywhere else under the standardised approach.
61. Claims secured by residential property, as defined in paragraph 48, 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

62. Fund based and non-fund-based claims on Alternative Investment Funds, which are considered as high-risk exposures, shall attract a higher risk weight of 150 per cent.

Explanation - SIDBI's investment limit in MSME-dedicated VCFs without the prior approval of the Reserve Bank shall be 20% subject to the proviso that SIDBI shall maintain a capital charge of 175%. For specific risk where SIDBI's CME is between 20% and 30%, the capital charge shall be at 200% and for CME above 30% and up to 40% the capital charge on specific risk shall be 225%.

63. 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.
64. Consumer credit, including personal loans shall attract a risk weight of 100 per cent. 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 152. The 'exposure value after risk mitigation' shall attract the risk weight of 125 per cent.
65. 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 an AIFI's equity investments in a bank / financial institution etc., are covered under paragraphs 37, 181 and 191. These risk weights / capital charge shall also apply to exposures which are exempt from 'capital market exposure' limit.

66. The exposure to capital instruments issued by NBFCs which are not deducted and are required to be risk weighted in terms of paragraph 24(7)(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 24(7)(ii)(c) shall be risk weighted at 250 per cent.
67. All investments made by an AIFI in the paid-up equity of non-financial entities (other than subsidiaries) made under their statutory mandate which exceed 49 per cent (for investments not made under an AIFI's statutory mandate, this limit shall be 10%) of the issued common share capital of the issuing entity or where the entity is an unconsolidated affiliate as defined in paragraph 24(7)(ii)(c)(i) shall receive a risk weight of 1250 per cent. Equity investments equal to or below 49 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.

68. The exposure to capital instruments issued by financial entities (other than a bank and an NBFC) which are not deducted and are required to be risk weighted in terms of paragraph 24(7)(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 a bank and an NBFC) which are not deducted and are required to be risk weighted in terms of paragraph 24(7)(ii)(c) shall be risk weighted at 250 per cent.
69. An AIFI's investments in the non-equity capital eligible instruments of a bank shall be risk weighted as prescribed in paragraph 37.
70. Unhedged foreign currency exposure

Table 11: 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 shall become 75 per cent.) |

* EBID = Profit After Tax + Depreciation + Interest on debt + Lease Rentals, if any

Note - Please refer to [Reserve Bank of India \(All India Financial Institutions – Credit Risk Management\) Directions, 2025](#).

A.14 Other assets

71. Loans and advances to an AIFI'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 An AIFI 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 an AIFI is holding eligible collateral in respect of amounts due from a staff member, the outstanding

amount in respect of that staff member may be adjusted to the extent permissible, as indicated in paragraph 149 to 157.

72. Other loans and advances to AIFI's own staff shall be eligible for inclusion under regulatory retail portfolio and shall therefore attract a 75 per cent risk weight.
73. All other assets shall attract a uniform risk weight of 100 per cent.

A.15 Off-balance sheet items

74. The total risk weighted off-balance sheet credit exposure is 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 is generally calculated by means of a two-step process:
 - (i) the notional amount of the transaction is converted into a credit equivalent amount, by multiplying the amount by the specified credit conversion factor or by applying the current exposure method; and
 - (ii) the resulting credit equivalent amount is multiplied by the risk weight applicable to the counterparty or to the purpose for which an AIFI has extended finance or the type of asset, whichever is higher.
75. Where the off-balance sheet item is secured by eligible collateral or guarantee, the credit risk mitigation guidelines detailed in paragraphs 146 to 173 may be applied.
76. 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 credit conversion factor (CCF) as elaborated in Table 12.
 - (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 shall be drawn during the

remaining period to maturity. Any drawn portion of a commitment forms a part of AIFI's on-balance sheet credit exposure.

Explanation –

- (i) For example, in the case of a cash credit facility for Rs.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% 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 cr is sanctioned for a large project which shall be drawn down in stages over a three-year period. The terms of sanction allow draw down in three stages – ₹ 150 cr in Stage I, ₹ 200 cr in Stage II and ₹ 350 cr in Stage III, where the borrower needs an AIFI's explicit approval for draw down under Stages II and III after completion of certain formalities. If the borrower has drawn already ₹ 50 cr under Stage I, then the undrawn portion shall be computed with reference to Stage I alone i.e., it shall be ₹ 100 cr. If Stage I is scheduled to be completed within one year, the CCF shall be 20 per cent and if it is more than one year then the applicable CCF shall 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.

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) Irrevocable commitments to provide off-balance sheet facilities shall be assigned the lower of the two applicable credit conversion factors. 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 12: CCFs – 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 and confirming financial entity. | 20 |
| 4. | Sale and repurchase agreement and asset sales with recourse, where the credit risk remains with an AIFI. (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 |
| 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 securities or posting of securities as collateral by an AIFI, 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 a 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 |

| Sr. No. | Instruments | CCF (%) |
|---------|-----------------------------------|---------|
| | (ii) Conditional take-out finance | 50 |

*However, this shall be subject to an AIFI 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. An AIFI's compliance to these guidelines shall be assessed under Annual Financial Inspection / Supervisory Review and Evaluation Process under Pillar 2 of the Reserve Bank.

(5) Regarding non-market related off-balance sheet items, the following transactions with non-bank counterparties shall be treated as claims on a bank:

- (i) Guarantees issued by a bank against the counter guarantees of an other bank.
- (ii) Rediscounting of documentary bills discounted by a bank and bills discounted by a bank which have been accepted by another bank shall be treated as a funded claim on a bank.

In all the above cases an AIFI shall be fully satisfied that the risk exposure is in fact on the other bank. If they are satisfied that the exposure is on another bank, they may assign these exposures the risk weight applicable to a bank as detailed in paragraphs 37 to 40.

(6) Issue of Irrevocable Payment Commitment by an AIFI to various Stock Exchanges on behalf of Mutual Funds and FII is a financial guarantee with a Credit Conversion Factor (CCF) of 100 per cent. However, capital shall have to be maintained only on exposure, which is reckoned as CME, i.e., 50 per cent of the amount, 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.

(7) For classification of AIFI's guarantees viz. direct credit substitutes and transaction-related contingent items etc. (Sr. No. 1 and 2 of Table 12 above), the following principles shall be kept in view for the application of CCFs:

- (i) Financial guarantees are direct credit substitutes wherein an AIFI 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 for mobilisation advance, advance money before the commencement of a project and for money to be received in various stages of project implementation;
 - (d) 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;
 - (e) Credit Enhancements;
 - (f) Liquidity facilities for securitisation transactions;
 - (g) Acceptances (including endorsements with the character of acceptance);
 - (h) 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 shall 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;

(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 an AIFI, 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 AIFIs.

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.

77. 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, CVA). Counterparty risk may arise in the context of OTC derivatives, exchange traded derivatives, and Securities Financing Transactions.

The 'capital charge for default risk' shall be calculated using **Current Exposure Method** as explained in paragraph 77(2). The 'capital charge for CVA risk' shall be calculated as explained in paragraph 77(3). The Current Exposure method is applicable only to OTC derivatives and exchange traded derivatives. The counterparty risk on account of Securities Financing Transactions is covered in paragraph 156 of this Master Direction.

Explanation –

Instruments that give risk to counterparty credit 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

(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 paragraphs 149 to 157 and the provisions held by an AIFI for CVA losses.

(ii) The CVA loss shall be calculated as a prudent valuation adjustment as per prudent valuation guidance contained in paragraph 207, without taking into account any offsetting debit valuation adjustments (DVA) which have been deducted from capital (refer paragraph 24). 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 an AIFI's capital, the CVA loss used to determine outstanding EAD shall be net of such DVA. RWAs 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 77(3).

- (iii) While computing the credit exposure an AIFI 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.
- (iv) Current credit exposure is defined as 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 is 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 13: Add-on factors for Market-Related Off-Balance Sheet Items (see paragraph 197 for CDS exposures)

| | PFE Add-on Factors (%) | |
|-----------------------------|-------------------------|----------------------------------|
| | 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 |

Notes:

- (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 is 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, an AIFI 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 Prime Lending Rate (PLR) / Base Rate shall have an effective notional amount of USD 2 million.
- (vi) When effective bilateral netting contracts as specified in paragraph 79 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:

$$A_{Net} = 0.4 \cdot A_{Gross} + 0.6 \cdot NGR \cdot A_{Gross}$$

where:

NGR = level of net replacement cost / level of gross replacement cost for transactions subject to legally enforceable netting agreements

Note - An AIFI 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 12 and the tables in paragraph 197) 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 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 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 79.

(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 79.

(iii) For such exposures as at (ii) above, Replacement Cost shall be Net Replacement Cost and Potential Future Exposure will 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 249, 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 249. The exposure computation under the Large Exposure Framework shall be as per this Master Direction. 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 this Master Direction. 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 79. The Current Exposure Method, as provided in this Master Direction, shall be applicable for measurement of credit exposure of derivatives products for the purpose of [Reserve Bank of India \(All India Financial Institutions – Concentration Risk Management\) Directions, 2025](#).

(3) CVA risk capital charge

- (i) The CVA capital charge shall be calculated in the manner indicated below in paragraph (ii). An AIFI are not required to include in this capital charge (a) transactions with a central counterparty (CCP); and (b) securities financing transactions (SFTs).
- (ii) An AIFI shall use the following formula to calculate a portfolio capital charge for CVA risk for its counterparties:

$$K = 2.33 \cdot \sqrt{h} \cdot \sqrt{\left(\sum_i 0.5 \cdot w_i \cdot (M_i \cdot EAD_i^{total} - M_i^{hedge} B_i) - \sum_{ind} w_{ind} \cdot M_{ind} \cdot B_{ind} \right)^2 + \sum_i 0.75 \cdot w_i^2 \cdot (M_i \cdot EAD_i^{total} - M_i^{hedge} B_i)^2}$$

Where;

- (a) **h** is the one-year risk horizon (in units of a year), $h = 1$.
- (b) **w_i** is the weight applicable to counterparty ‘i’. Counterparty ‘i’ shall be mapped to one of the seven weights w_i based on its external rating as shown in the Table 14.1 below.

Table 14.1: Weights (w_i) based on external credit rating

| Rating | W _i |
|---------------|----------------|
| AAA | 0.7% |
| AA | 0.7% |
| A | 0.8% |
| BBB | 1.0% |
| BB | 2.0% |
| B and unrated | 3.0% |
| CCC | 10.0% |

- (c) **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 Current Exposure Method (CEM) as applicable to the calculation of counterparty risk capital charges for such counterparty by an AIFI. 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 $(1 - \exp(-0.05 * M_i^{\text{hedge}})) / (0.05 * M_i^{\text{hedge}})$.
- (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 $(1 - \exp(-0.05 * M_{\text{ind}})) / (0.05 * M_{\text{ind}})$.
- (f) **w_{ind}** is the weight applicable to index hedges. An AIFI 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 M_i^{hedge}. B_i 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) may 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) In cases where the unrated counterparty is a scheduled commercial bank, an AIFI may use the following Table 14.2 to arrive at the implied ratings of the counterparty-bank and consequently, the W_i .

Table 14.2: Implied ratings and weights (w_i) to be used where the unrated counterparty is a SCB

| Applicable Risk weight of the Counterparty-bank according to Table 6 | Implied ratings | W_i |
|--|-----------------|-------|
| 20 | AAA / AA | 0.7% |
| 50 | A | 0.8% |
| 100 | BBB | 1% |
| 150 | BB | 2% |
| 625 | CCC | 10% |

- (l) An AIFI shall continuously monitor the capital adequacy position of its counterparty bank so that the effect of any change in the implied ratings is adequately reflected in CVA capital charge calculations.

- (iii) An illustration of CVA risk capital charge calculation

(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:

$$K = 2.33 \cdot \sqrt{h} \cdot \sqrt{\left(\sum_i 0.5 \cdot w_i \cdot (M_i \cdot EAD_i^{total} - M_i^{hedge} B_i) - \sum_{ind} w_{ind} \cdot M_{ind} \cdot B_{ind} \right)^2 + \sum_i 0.75 \cdot w_i^2 \cdot (M_i \cdot EAD_i^{total} - M_i^{hedge} B_i)^2}$$

Where,

- (i) B_i is the notional of purchased single name CDS hedges - nil
- (ii) B_{ind} is the full notional of one or more index CDS of purchased protection, used to hedge CVA risk. - nil
- (iii) w_{ind} is the weight applicable to index hedges - nil
- (iv) M_{ihedge} is the maturity of the hedge instrument with notional B_i
- (v) M_i is the effective maturity of the transactions with counterparty 'i'
- (vi) EAD_i total is the exposure at default of counterparty 'i' (summed across its netting sets). For non-IMM banks the exposure should be discounted by applying the factor: $(1 - \exp(-0.05 \cdot M_i)) / (0.05 \cdot M_i)$.
- (vii) $h = 1$ 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: $(1 - \exp(-0.05 \cdot M_A)) / (0.05 \cdot M_A) = 0.95551$

Discounted $EAD_A = 4.5 \cdot 0.95551 = 4.2981$

Discount factor to be applied to counterparty B: $(1 - \exp(-0.05 \cdot M_B)) / (0.05 \cdot M_B) = 0.8846$

Discounted $EAD_B = 52.8 \cdot 0.8846 = 46.7061$

$$K = 2.33 \cdot 1 \cdot \left[\left\{ (0.5 \cdot 0.008 \cdot (1.85 \cdot 4.2981 - 0) + (0.5 \cdot 0.007 \cdot (5.01 \cdot 46.7061 - 0)) - 0) \right\}^2 + (0.75 \cdot 0.0082 \cdot (1.85 \cdot 4.2981 - 0))^2 + (0.75 \cdot 0.0072 \cdot (5.01 \cdot 46.7061 - 0))^2 \right]^{1/2}$$

$$= 2.33 \cdot 1.66 = 3.86$$

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 an AIFI is 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 77(2); and
- (ii) The standardised CVA risk capital charge determined as per paragraph 77(3).

(5) Capital requirement for exposures to Central Counterparties (CCPs)

Scope of Application:

- (i) Exposures to central counterparties arising from OTC derivatives transactions, exchange traded derivatives transactions and securities financing transactions (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.) are not subject to this treatment. The settlement of cash transactions remains subject to the treatment described in paragraph 78.
- (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 are to capitalise that transaction as an OTC derivative.
- (iv) For the purpose of capital adequacy framework, CCPs shall be considered as financial institution. Accordingly, an AIFI's investments in the capital of CCPs shall be guided in terms of paragraph 24.
- (v) Capital requirements shall be dependent on the nature of CCPs viz. Qualifying CCPs (QCCPs) and non-Qualifying CCPs.
 - (a) Regardless of whether a CCP is classified as a QCCP or not, an AIFI retains the responsibility to ensure that it maintains adequate capital

for its exposures. Under Pillar 2, an AIFI shall consider whether it may 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 AIFI's dealings, it is unclear that the CCP meets the definition of a QCCP.

- (b) An AIFI 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. This might be considered appropriate where, for example, an external assessment such as a Financial Sector Assessment Program (FSAP) of International Monetary Fund / World Bank has found material shortcomings in the CCP or the regulation of CCPs, and the CCP and / or the CCP regulator have not since publicly addressed the issues identified.
- (c) Where an AIFI is acting as a clearing member, the AIFI 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) An AIFI 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 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, an AIFI's

exposures with such a central counterparty shall be capitalised according to rules applicable for non-QCCP.

(6) Exposures to Qualifying CCPs (QCCPs)

(i) Trade exposures

Clearing member exposures to QCCPs

- (a) Where an AIFI acts as a clearing member of a QCCP for its own purposes, a risk weight of 2 per cent shall be applied to an AIFI'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 (CEM) for derivatives and rules as applicable for capital adequacy for Repo / Reverse Repo-style transactions.
- (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 79.
- (d) An AIFI shall have to demonstrate that the conditions mentioned in paragraph 79 are fulfilled on a regular basis by obtaining independent and reasoned legal opinion as regards legal certainty of netting of exposures to QCCPs. An AIFI 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.

Client AIFI exposures to clearing member

- (e) Where an AIFI 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 prescribed in clause (i) above provided the 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 AIFI shall obtain an independent, written and reasoned legal opinion that 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 AIFI, clearing member and QCCP;*
 - (b) *the law of the jurisdiction(s) of the foreign countries in which a client AIFI, 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 this condition.*
- (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. In this context, it is clarified that 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 is not sufficient to conclude that they are highly likely to be ported. Other evidence such as the criteria mentioned in this paragraph is necessary to make this claim.

- (f) 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.
- (g) Where a client AIFI does not meet the requirements in the above paragraphs, an AIFI shall be required to capitalise its exposure (including potential CVA risk exposure) to the clearing member as a bilateral trade.
- (h) 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 herein.

Treatment of posted collateral

- (i) In all cases, any assets or collateral posted shall, from the perspective of an AIFI 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. Thus, 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 AIFI posting such assets or collateral shall also recognise credit risk based upon the assets or collateral being exposed to risk of loss based on 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.

- (j) 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 will 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.

- (k) 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 be applied to the collateral if the conditions established in the paragraph on "client AIFI exposures to clearing member" of this paragraph are met (mentioned above). A risk weight of 4 per cent shall be made applicable 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 mentioned in the paragraph on “client AIFI exposures to clearing members” of this paragraph are met.

- (l) If a clearing member collects collateral from a client for client cleared trades and this collateral is passed 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 set forth below, 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 set forth below 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 AIFI is required to capitalise its exposures arising from default fund contributions to a qualifying CCP by applying the following methodology:

- (i) A clearing member AIFI shall apply a risk-weight of 1250 per cent to its default fund exposures to the qualifying CCP, subject to an overall cap on the risk-weighted assets 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 RWAs for both AIFI i's trade and default fund exposures to each QCCP are equal to:

$$\text{Min} \{(2 \text{ per cent} * TE_i + 1250 \text{ per cent} * DF_i); (20 \text{ per cent} * TE_i)\}$$

Where;

TE_i is AIFI i's trade exposure to the QCCP; and

DF_i is AIFI i's pre-funded contribution to the QCCP's default fund.

Note - The 2% risk weight on trade exposures does not apply additionally, as it is included in the equation.

(7) Exposures to non-qualifying CCPs

- (i) An AIFI 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 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) An AIFI shall apply a risk weight of 1250 per cent to its default fund contributions to a non-qualifying CCP.
- (iii) For the purposes of this paragraph, the default fund contributions of such an AIFI 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.

78. Failed transactions

- (1) With regard to unsettled securities and foreign exchange transactions, an AIFI is exposed to counterparty credit risk from trade date, irrespective of the booking or the accounting of the transaction. An AIFI 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) An AIFI 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 an AIFI 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 an AIFI 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. The following capital treatment is applicable to all failed transactions, including transactions through recognised clearing houses and Central Counterparties. Repurchase and reverse-repurchase agreements as well as securities lending and borrowing that have failed to settle are excluded from this capital treatment.
- (4) For DvP Transactions – If the payments have not yet taken place five business days after the settlement date, an AIFI shall calculate a capital charge by multiplying the positive current exposure of the transaction by the appropriate factor as provided Table 15. In order to capture the information, an AIFI shall need information system that can track the number of days after the agreed settlement date and calculate the corresponding capital.

Table 15: Capital charge for delayed settlement of DvP transactions

| Number of working days after the agreed settlement date | Corresponding risk multiplier (in %) |
|--|---|
| From 5 to 15 | 9 |
| From 16 to 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, an AIFI 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. An AIFI 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, an AIFI 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.

79. 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; and
- (d) be, together with the rights arising from the provisions required in (i) to (iii) above, legally enforceable in each relevant jurisdiction upon the occurrence of an event of default and regardless of the counterparty's insolvency or bankruptcy.
- (e) Netting across positions in the banking book 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) An AIFI may net transactions subject to novation under which any obligation between an AIFI 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) An AIFI 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), an AIFI 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 AIFI 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 default, bankruptcy, liquidation or similar circumstances;

- (b) Written and reasoned legal opinions that, in the event of a legal challenge, the relevant courts and administrative authorities would find the AIFI'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 instructions. 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

80. An AIFI 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 an AIFI, the exposure shall be treated as retained exposure and not a fresh exposure. An AIFI shall

deduct from CET 1 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.

81. For calculating exposure amount, an AIFI shall measure the exposure amount of its off-balance exposure as follows:
 - (i) for credit risk mitigants sold or purchased by an AIFI, the treatment set out in paragraphs 146 to 173 shall apply;
 - (ii) for facilities that are not eligible credit risk mitigants, the AIFI 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 AIFI, to the extent not covered by paragraphs 81(i) and 81(ii) above, the measurement approach set out in paragraph 77(2) the [dated November 10, 2016](#) on 'Guidelines for computing exposure for counterparty credit risk arising from derivative transactions' shall apply.
82. For the purpose of calculating capital requirements, an AIFI's exposure A overlaps another exposure B if in all circumstances the AIFI will preclude any loss for the AIFI on exposure B by fulfilling its obligations with respect to exposure A. For example, if an AIFI 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 an AIFI can verify that fulfilling its obligations with respect to exposure A shall preclude a loss from its exposure to B under any circumstance, the AIFI does not need to calculate risk-weighted assets for its exposure B.
83. To arrive at an overlap, an AIFI 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 AIFI 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 AIFI 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 AIFI shall only need to calculate capital requirements on the liquidity facility.

84. Overlap may also be recognised between relevant capital charges for exposures in the trading book and capital charges for exposures in the AIFling book, provided that the AIFI is able to calculate and compare the capital charges for the relevant exposures.
85. Liquidity facilities provided by an AIFI that satisfy the requirements of [Reserve Bank of India \(All India Financial Institutions – Transfer and Distribution of Credit Risk\) Directions, 2025](#) attract risk weights as per the SEC-ERBA approach prescribed in paragraphs 107 to 114.
86. Liquidity facilities provided by an AIFI that do not satisfy the requirements of [Reserve Bank of India \(All India Financial Institutions – Transfer and Distribution of Credit Risk\) Directions, 2025](#) shall maintain capital charge equal to the actual exposure, after applying a CCF of 100 per cent for the undrawn portion.
87. 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 as per [Reserve Bank of India \(All India Financial Institutions – Transfer and Distribution of Credit Risk\) Directions, 2025](#) or where originator is not an AIFI referred to in [Reserve Bank of India \(All India Financial Institutions – Transfer and Distribution of Credit Risk\) Directions, 2025](#), or for which prudential treatment is not advised explicitly in these directions, an AIFI 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

88. 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.

89. 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

90. An AIFI shall apply Securitisation External Ratings Based approach (SEC-ERBA) for calculation of RWA for credit risk of securitisation exposures. For unrated securitisation exposures, an AIFI shall maintain capital charge equal to the actual exposure.
91. 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.
92. 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.
93. When an AIFI 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, an AIFI shall not be permitted to recognise in regulatory capital any gain on sale.

Determination of attachment point (A) and detachment point (D)

94. 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.

95. 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.
96. 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.
97. 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.
98. An AIFI 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

99. For risk-based capital purposes, tranche maturity (M_T) shall be measured at the AIFI'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.

100. When determining the maturity of a securitisation exposure, an AIFI shall take into account the maximum period of time they are exposed to potential losses from the securitised assets. In cases where an AIFI provides a commitment, the AIFI 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 AIFI shall be exposed after a draw has occurred.
101. For credit protection instruments that are only exposed to losses that occur up to the maturity of that instrument, an AIFI shall be allowed to apply the contractual maturity of the instrument and shall not have to look through to the protected position.

Treatment by an AIFI of credit risk mitigation for securitisation exposures

102. AN AIFI 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 153. Eligible Collateral pledged by SPEs shall be recognised;
 - (ii) credit protection provided by the entities listed in paragraph 163 shall be recognised. SPEs shall not be recognised as eligible guarantors; and
 - (iii) where guarantees fulfil the minimum operational conditions as specified in paragraphs 159 to 168 of these Directions, an AIFI shall take account of

such credit protection in calculating capital requirements for securitisation exposures.

103. When an AIFI 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).
104. Provided that the conditions set out in paragraph 102 of this chapter are met, the AIFI buying full (or pro rata) credit protection shall recognise the credit risk mitigation on the securitisation exposure in accordance with the CRM framework.
105. 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 paragraph 4(72).
106. 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 169 to 172 of these [Directions](#) (as amended from time to time). When the exposures being hedged have different maturities, the longest maturity shall be used.

SEC-ERBA

107. 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 108 to 110 as mentioned in this chapter 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 AIFI has with regard to all payments owed to it. For example, if an AIFI 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 124 to 145 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, an AIFI 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 144 shall apply.
- (v) Where CRM is provided to specific underlying exposures or the entire pool by an eligible guarantor as defined in paragraph 163 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 AIFI shall treat the exposure as if it is unrated and then apply the CRM treatment outlined in paragraphs 146 to 173 of these Directions.
- (vii) AN AIFI 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 AIFI. For example, if an AIFI 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 AIFI shall treat the ABS as if it were not rated. The AIFI shall continue to hold capital against the other securitisation exposures it provides (e.g., against the liquidity facility and / or credit enhancement).

108. For exposures with short-term ratings, the following risk weights shall apply:

| Table 16: ERBA risk weights for short-term ratings | | | | |
|---|----------|-----|------|-------------------|
| External credit assessment | A1+ / A1 | A2 | A3 | All other ratings |
| Risk weight | 15% | 50% | 100% | 1250% |

109. 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.

110. 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 111 as mentioned below.

| Table 17: ERBA risk weights for long-term ratings | | | | |
|--|--------------------------------|---------|--------------------------------|---------|
| Rating | Senior tranche | | Non-senior (thin) tranche | |
| | Tranche maturity (<i>MT</i>) | | Tranche maturity (<i>MT</i>) | |
| | 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% |

| Table 17: 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 |
| 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% |
| 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% |

111. The risk weight assigned to a securitisation exposure when applying the SEC-ERBA is calculated as follows:

- (i) To account for tranche maturity, an AIFI shall use linear interpolation between the risk weights for one and five years.
- (ii) To account for tranche thickness, an AIFI shall calculate the risk weight for non-senior tranches as follows:

$$\text{Risk weight} = (\text{risk weight from table after adjusting for maturity}) * (1 - \min(T, 50\%))$$

where T is the tranche thickness.

112. 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.

113. 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.

114. 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

$$M \text{ years} = \text{RW}_{\text{year1}} + (M-1) * \frac{\text{RW}_{\text{year 5}} - \text{RW}_{\text{year 1}}}{(5-1)} \text{ (Column 4 below);}$$

- (viii) Risk Weight (%) = Risk weight as given in table in paragraph 110 (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 17) | 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 17) | 90% * (1- Min(0.5,0.125)) = 78.75% | 250 * 78.75% |

| 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) |
|-----------------------------------|--|--|---|--|--------------------------------------|
| | | | | | =196.875 crores |
| | Detachment Point: $(250+50+200) / 2000 = 0.25$ | | Actual RW adjusting for maturity | | |
| | Tranche thickness (T): $(0.25-0.125) = 0.125$ | | $40\% + (140-40)\% \cdot 2 / 4 = 90\%$ | | |
| Note C: 50 crores | Attachment point: $200 / 2000 = 0.10$ | BB+ | RW for 1 year = 470% RW for 5 year = 580% (from table 17) | $525\% \cdot (1 - \text{Min}(0.5, 0.025)) = 511.875\%$ | $50 \cdot 511.875\% = 255.94$ crores |
| | Detachment Point: $(50+200) / 2000 = 0.125$ | | $470\% + (580-470)\% \cdot 2 / 4 = 525\%$ | | |
| | 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 Chapter III of MD on Credit Risk Distribution fall within the scope of the STC framework)

115. For exposures with short-term ratings, the following risk weights shall apply:

| Table 18: ERBA STC risk weights for short-term ratings | | | | |
|---|----------|-----|-----|-------------------|
| External credit assessment | A1+ / A1 | A2 | A3 | All other ratings |
| Risk weight | 10% | 30% | 60% | 1250% |

116. 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 111 as mentioned above.

| Table 19: ERBA STC risk weights for long-term ratings | | | | |
|--|--------------------------------|---------|--------------------------------|---------|
| Rating | Senior tranche | | Non-senior (thin) tranche | |
| | Tranche maturity (<i>MT</i>) | | Tranche maturity (<i>MT</i>) | |
| | 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% |

117. 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 paragraph X of the MD on Credit risk distribution shall be satisfied for a securitisation to receive the alternative regulatory capital treatment as determined by paragraphs 107 to 114.

118. Capital requirements on securitisation exposures undertaken prior to September 24, 2021 shall be as under.

(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. An AIFI'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) An AIFI 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 an AIFI is required to maintain on its other existing exposures to the securitisation 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, an AIFI shall have the information specified below:

- (a) An AIFI 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) An AIFI 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) An AIFI shall have a thorough understanding of all structural features of a securitisation transaction that shall materially impact the performance of an AIFI'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 an AIFI 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 an AIFI 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 an AIFI'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) An AIFI shall apply external credit assessments from eligible external credit rating agencies consistently across a given type of securitisation exposure. Furthermore, an AIFI 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 144 shall apply.
- (ii) If the CRM provider is not recognised as an eligible guarantor as defined in paragraph 163, 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), an AIFI shall treat the exposure as if it is unrated and then use the CRM treatment outlined in paragraphs 146 to 173 of these Directions.
- (iv) The other aspects of application of external credit assessments shall be as per guidelines given in paragraphs 124 to 145 of these Directions.
- (v) An AIFI 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 an AIFI. For example, if an AIFI 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, an AIFI shall treat the securitised assets / various tranches of the ABS / MBS as if these were not rated. An AIFI 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) An AIFI 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 20.1: 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 an AIFI 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 53, 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 20.2: 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 an AIFI other than originators (%) | 100 | 100 | 100 | 150 | 400 | 1250 |
| Risk weight for originator (%) | 100 | 100 | 100 | 150 | 1250 | |

- (iv) An AIFI is not permitted to invest in unrated securities issued by an SPV as a part of the securitisation transaction. However, securitisation exposures assumed by an AIFI 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 an AIFI 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
 - (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 an AIFI 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 an AIFI.
- (vii) If an originating AIFI 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..177/ / 212 dated May 07, 2012](#) on 'Revision to the Guidelines on Securitisation Transactions', it shall have to maintain capital for the securitised assets / assets sold as if these were not securitised / sold. This capital shall be in addition to the capital which an AIFI is required to maintain on its other existing exposures to the securitisation transaction.

- (viii) A investing AIFI shall assign a risk weight of 1250 per cent to the exposures relating to securitisation / 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 an AIFI. Similarly, the capital adequacy treatment for direct purchase of retail loans, shall be as per the rules applicable to retail portfolios directly originated by an AIFI 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) An AIFI 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 an AIFI 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 an AIFI 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 an AIFI 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 146 to 173 of these Directions. Eligible collateral is limited to that recognised under these guidelines in paragraph 153. 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 169 to 172 of these Directions. When the exposures being hedged have different maturities, the longest maturity shall be used applying the methodology prescribed in paragraphs 171 and 172 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, an AIFI in India, including their 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 AIFIs 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 21.1: 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 AIFIs other than originators (%) | 40 | 60 | 100 | 225 | 650 | 1250 |
| Risk weight for originator (%) | 40 | 60 | 100 | 225 | 1250 | |

Table 21.2: 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 AIFIs other than originators (%) | 200 | 200 | 200 | 400 | 1250 |
| Risk weight for originator (%) | 40 | 60 | 100 | 225 | 1250 |

A.17 Prudential Guidelines on Credit Default Swap (CDS)

119. An AIFI can undertake transactions in CDS in terms of Master Direction – Reserve Bank of India (Credit Derivatives) Directions, 2022. As users, an AIFI 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.

120. Classification of CDS into trading book and banking book positions

A CDS being a financial derivative will be classified in the trading book except when it is contracted and designated as a hedge for a banking book exposure. Thus, the CDS positions held in the trading book would include positions which:

- (a) are meant for hedging the exposures in the trading book;
- (b) are held for short-term resale; and
- (c) are taken by the AIFI with the intention of benefiting in the short-term from the actual and / or expected differences between their buying and selling prices

CDS positions meant for hedging banking book exposures shall be classified in the banking book. However, all CDS positions, either in banking book or trading book, should be marked-to-market.

121. 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 would allow the protection provider unilaterally to cancel the credit cover or that would 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 AIFI (protection buyer) that could 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; and
 - (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);
 - (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 can 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 shall be defined conservatively. The effective maturity of the underlying shall 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.

122. 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, if the following conditions are satisfied:
- (i) Operational requirements mentioned in paragraph 121
 - (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 an AIFI breaches any of these conditions subsequently, the AIFI 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 (1) the reference obligation or deliverable obligation ranks *pari passu* with or is junior to the underlying obligation, and (2) 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 shall 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 Rs.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:

$$100 * \{(4 - 0.25) \div (5 - 0.25)\} = 100*(3.75 \div 4.75) = 78.95$$

- (d) Once the residual maturity of the CDS contract reaches three months, protection ceases to be recognised.

123. Internal hedges and other prudential requirements

- (1) An AIFI can use CDS contracts to hedge against the credit risk in its existing corporate bonds portfolios. An AIFI can hedge a Banking Book credit risk exposure either by an internal hedge (the protection purchased from the trading desk of an AIFI and held in the Trading Book) or an external hedge (protection purchased from an eligible third-party protection provider). When an AIFI 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 AIFI transfers the credit risk from the Trading Book to an eligible third party protection provider through a CDS meeting the requirements of paragraphs 121 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 shall 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 paragraphs 122, 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 \(All India Financial Institutions – Classification, Valuation and Operation of Investment Portfolio\) 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 195(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 122 and trading book as indicated in paragraph 195(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

124. 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 AIFIs possesses rating assigned by an eligible credit rating agency, the risk weight of the claim will be based on this rating. An AIFI shall 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 Ltd. (Acuité)
- (ii) Brickwork Ratings India Private Limited
- (iii) Credit Analysis and Research Limited (CARE);
- (iv) CRISIL Ratings Limited;
- (v) ICRA Limited;
- (vi) India Ratings and Research Private Limited (India Ratings); and
- (vii) INFOMERICS Valuation and Rating Pvt Ltd. (INFOMERICS)

125. An AIFI 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) Fitch;
- (ii) Moody's;
- (iii) Standard & Poor's;
- (iv) Care Global (for non-resident exposures originating in IFSCA)

B.2 Scope of application of external ratings

126. An AIFI shall use the chosen credit rating agency and its ratings consistently for each type of claim, for both risk weighting and risk management purposes. An AIFI shall not 'cherry pick' the assessments provided by different credit rating agencies and arbitrarily change the use of credit rating agency. If an AIFI has

decided to use the ratings of some of the chosen credit rating agencies for a given type of claim, it shall use only the ratings of those credit rating agency, despite the fact that some of these claims may also be rated by other chosen credit rating agency whose ratings the AIFI has decided not to use. An AIFI 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 agencies, whose ratings the AIFI 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.

127. An AIFI 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 RWAs as required vide Table DF-4 of Annex 3.
128. To be eligible for risk-weighting purposes, the external credit assessment shall take into account and reflect the entire amount of credit risk exposure an AIFI has with regard to all payments owed to it. For example, if an AIFI 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.
129. To be eligible for risk weighting purposes, the rating must 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.
130. 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.
131. For an asset in an AIFI's portfolio that has contractual maturity less than or equal to one-year, short term ratings accorded by the chosen credit rating agencies 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 agencies shall be relevant.

132. 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, an AIFI (if permitted to extend cash credit facility) 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 90 to 98, and paragraphs 100 to 101 below.

B.3 Mapping process

133. 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 134 and 140, which shall be used by an AIFI in assigning risk weights to the various exposures.

B.4 Long term ratings

134. The rating-risk weight mapping furnished in the Table 22 below shall be adopted by an AIFI in India:

Table 22: Risk weight mapping of long-term ratings of the chosen domestic rating agencies

| CARE | CRISIL Ratings Limited | India Ratings and Research Private Limited (India Ratings) | ICRA | ACUITE Ratings & Research Ltd. (Acuité) | Brickwork Ratings India Private Limited | INFOMERIC S | Standardised approach risk weights (in percent) |
|----------|------------------------|--|----------|---|---|-------------|---|
| CARE AAA | CRISIL AAA | IND AAA | ICRA AAA | Acuité AAA | Brickwork AAA | IVR AAA | 20 |
| CARE AA | CRISIL AA | IND AA | ICRA AA | Acuité AA | Brickwork AA | IVR AA | 30 |

| CARE | CRISIL Ratings Limited | India Ratings and Research Private Limited (India Ratings) | ICRA | ACUITE Ratings & Research Ltd. (Acuité) | Brickwork Ratings India Private Limited | INFOMERIC S | Standardised approach risk weights (in percent) |
|----------------------------------|--|--|----------------------------------|--|---|------------------------------|---|
| CARE A | CRISIL A | IND A | ICRA A | Acuité A | Brickwork A | IVR A | 50 |
| CARE BBB | CRISIL BBB | IND BBB | ICRA BBB | Acuité BBB | Brickwork BBB | IVR BBB | 100 |
| 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 | Acuité BB, Acuité B, Acuité C & Acuité D | Brickwork BBB, Brickwork BB, Brickwork B, Brickwork C & Brickwork 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:

- (1) if the aggregate exposure from banking system is more than ₹200 crore
- (2) if the aggregate exposure from banking system is more than ₹100 crore for exposures which were rated earlier and subsequently have become unrated.

135. 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 in the A rating category and assigned 50 per cent risk weight.

136. 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 counterparty, whether short-term or long-term, shall also receive a 150 per cent risk weight, unless an AIFI uses recognised credit risk mitigation techniques for such claims.

B.5 Short term ratings

137. For risk-weighting purposes, short-term ratings are deemed to be issue-specific. They shall only 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 a bank and corporates.

138. 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.
139. 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 counterparty, whether long-term or short-term, shall also receive a 150 per cent risk weight, unless an AIFI uses recognised credit risk mitigation techniques for such claims.
140. In respect of the issue specific short-term ratings the following risk weight mapping shall be adopted by an AIFI:

Table 23: Risk weight mapping of short-term ratings of domestic rating agencies

| CARE | CRISIL Ratings Limited | India Ratings and Research Private Limited (India Ratings) | ICRA | ACUITE Ratings & Research Ltd. (Acuité) | INFOMERICS | Brickwork Ratings India Private Limited | Standardised approach risk weights (in percent) |
|-------------|-------------------------------|---|-------------|--|-------------------|--|--|
| CARE A1+ | CRISIL A1+ | IND A1+ | ICRA A1+ | Acuité A1+ | IVR A1+ | Brickwork A1+ | 20 |
| CARE A1 | CRISIL A1 | IND A1 | ICRA A1 | Acuité A1 | IVR A1 | Brickwork A1 | 30 |
| CARE A2 | CRISIL A2 | IND A2 | ICRA A2 | Acuité A2 | IVR A2 | Brickwork A2 | 50 |
| CARE A3 | CRISIL A3 | IND A3 | ICRA A3 | Acuité A3 | IVR A3 | Brickwork A3 | 100 |
| CARE A4 & D | CRISIL A4 & D | IND A4 & D | ICRA A4 & D | Acuité A4 & D | IVR A4 & D | Brickwork A4 & D | 150 |
| Unrated | Unrated | Unrated | Unrated | Unrated | Unrated | Unrated | 100 |

141. Where '+' or '-' notation is attached to the rating, the corresponding main rating category risk weight shall be used for A2 and below, unless specified otherwise. For example, A2+ or A2- shall be in the A2 rating category and assigned 50 per cent risk weight.

142. 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

143. 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. An AIFI 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

144. An AIFI shall be guided by the following in respect of exposures / obligors having multiple ratings from the chosen credit rating agency chosen by an AIFI 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

145. Where an AIFI 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 an AIFI'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 an AIFI'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 an AIFI'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 94. If not, the rating applicable to the specific debt cannot be used and the unassessed claim shall receive the risk weight for unrated claims.

Note :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 an AIFI 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, an AIFI shall assign 50 per cent risk weight to an unrated short term or long-term claim.

- (ii) It is observed that the Press Releases (PRs) issued by External Credit Assessment Institutions (ECAIs) on rating actions are often devoid of the lenders' details. Absence of such information may result in banks applying the derived risk weights for unrated exposures, without satisfying themselves regarding adherence to prescribed conditions. This may, consequentially, lead to potentially lower provision of capital as well as underpricing of risks. In order to address the above information asymmetry the Reserve Bank had advised the ECAIs vide letter dated June 4, 2021, to disclose the name of the lender and the corresponding credit facilities rated by them in the PRs issued on rating actions, after obtaining requisite consent from the borrowers by August 31, 2021. A loan rating without the above disclosure by the ECAI shall not be eligible for being reckoned for capital computation by an AIFI. An AIFI shall treat such exposures as unrated and assign applicable risk weights in terms of paragraph 36 of this

Chapter. Illustratively, a scenario may be assumed, where a borrower has availed credit facilities from lenders A, B and C and external rating from an ECAI is obtained only in respect of the credit facility extended by Lender A. If the ECAI has disclosed the name of Lender A and the corresponding credit facility rated by it, then Lender A can reckon the said rating for risk weighting purpose. Lenders B and C are permitted to derive risk weights for their respective unrated credit facilities subject to conditions stated in Paragraph 145 of these directions *ibid*, as permitted hitherto. In the event of ECAI not making the above disclosure, none of the Lenders 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 an AIFI intends to extend an issuer or an issue specific rating assigned by a chosen credit rating agency to any other exposure which an AIFI has on the same counterparty and which meets the above criterion, it shall be extended to the entire amount of credit risk exposure an AIFI 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 considered if the credit enhancement is already reflected in the issue specific rating accorded by a chosen credit rating agency relied upon by an AIFI.

- (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.

C Credit risk mitigation

C.1 General principles

146. Credit risk mitigation (CRM) approaches as detailed herein shall be applicable to the banking book exposures of an AIFI. These shall also be applicable for calculation of the counterparty risk charges for OTC derivatives and repo-style transactions booked in the trading book.

147. 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 an AIFI 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 an AIFI's use of CRM techniques and its interaction with an AIFI'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 3 shall also be observed for an AIFI to obtain capital relief in respect of any CRM techniques.

C.2 Legal certainty

148. In order for an AIFI 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. An AIFI 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. An AIFI shall also undertake such further review as necessary to ensure continuing enforceability.

C.3 CRM techniques - collateralised transactions

149. A collateralised transaction is one in which:

- (i) an AIFI have 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 an AIFI has an on- or off-balance sheet credit exposure.
- (ii) an AIFI have a specific lien on the collateral and the requirements of legal certainty are met.

Overall framework and minimum conditions

150. An AIFI 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, an AIFI, which take eligible financial collateral (e.g., cash or securities, more specifically defined below), are 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. Credit risk mitigation 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:

- (i) In addition to the general requirements for legal certainty, the legal mechanism by which collateral is pledged or transferred shall ensure that an AIFI 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). Furthermore, an AIFI shall take all steps necessary

to fulfill those requirements under the law applicable to an AIFI's interest in the collateral for obtaining and maintaining enforceable security interest, e.g., by registering it with a registrar.

- (ii) 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 - shall provide little protection and so shall be ineligible.

- (iii) An AIFI 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 shall be liquidated promptly.
- (iv) Where the collateral is held by a custodian, an AIFI shall take reasonable steps to ensure that the custodian segregates the collateral from its own assets.
- (v) An AIFI shall ensure that sufficient resources are devoted to the orderly operation of margin agreements with OTC derivative and securities-financing counterparties, as measured by the timeliness and accuracy of its outgoing calls and response time to incoming calls. An AIFI shall have collateral management policies in place to control, monitor and report the following to the Board or one of its Committees:
 - (a) the risk to which margin agreements exposes them (such as the volatility and liquidity of the securities exchanged as collateral),
 - (b) the concentration risk to particular types of collateral,
 - (c) the reuse of collateral (both cash and non-cash) including the potential liquidity shortfalls resulting from the reuse of collateral received from counterparties, and
 - (d) the surrender of rights on collateral posted to counterparties.

151. A capital requirement shall be applied to an AIFI 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.

152. The comprehensive approach

- (1) An AIFI shall need to calculate its adjusted exposure to a counterparty for capital adequacy purposes to take account of the effects of that collateral. An AIFI are required to adjust both the amount of the exposure to the counterparty and the value of any collateral received in support of that counterparty to take account of possible future fluctuations in the value of either, occasioned by market movements. These adjustments are referred to as 'haircuts'. The application of haircuts shall produce 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. In other words, 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 an AIFI in the course of its operations, shall not be subject to market volatility, (since the loan disbursement / investment shall be a 'cash' transaction) though the value of eligible financial collateral shall be, the haircut stipulated in Table 24 shall apply in respect of credit transactions only to the eligible collateral but not to the credit exposure of an AIFI. On the other hand, exposures of an AIFI, 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 subject 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 any further adjustment for foreign exchange risk), an AIFI 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 154.

153. 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 AIFI) on deposit with an AIFI which is incurring the counterparty exposure.
- (ii) Gold: Gold shall include both bullion and jewellery. However, the value of the collateralised jewellery shall 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 shall 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 an AIFI shall 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 a bank and a Primary Dealer); 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/ Acuité A3 / IVR A3 for short-term debt instruments.

Explanation - A debenture shall 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 shall 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 an AIFI shall be sufficiently confident about the market liquidity where these are:
- (a) issued by a bank; and
 - (b) listed on a recognised exchange; and
 - (c) classified as senior debt; and
 - (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/ Acuité A3 / IVR A3 by a chosen Credit Rating Agency; and
 - (e) an AIFI 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 / Acuité A3 / Brickwork A3/ IVR A3(as applicable) and;
 - (f) an AIFI shall be sufficiently confident about the market liquidity of the security.
- (viii) Units of Mutual Funds regulated by the securities regulator of the jurisdiction of an AIFI'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) Mutual fund is limited to investing in the instruments listed in this paragraph.

154. Calculation of capital requirement

- (1) For a collateralised transaction, the exposure amount after risk mitigation is 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

He = haircut appropriate to the exposure

C = the current value of the collateral received

Hc = 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 1 | 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 |
| 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 (Govt) 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 (%) | 0 | 0 | 0.08 | 0.08 | 0 |

| Sl. No. | Particulars | Case 1 | Case 2 | Case 3 | Case 4 | Case 5 |
|---------|---|--------|--------|--------|--------|--------|
| (1) | (2) | (3) | (4) | (5) | (6) | (7) |
| | [cf. paragraph 155(5)) of the circular] | | | | | |
| 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 135, 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 24

Case 5: It is assumed that the Mutual Fund meets the criteria specified in paragraph 153 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 24

(4) Illustration on computation of capital charge for Counterparty Credit Risk (CCR) – repo transactions:

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 32 of the Circular) |

Computation of total capital charge comprising the capital charge for Counterparty Credit Risk (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 24 of the Circular | 1050 * 1.014 | 1064.70 |
| 6. | Collateral for the security lent | Cash | 1000 |
| 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 (4.5 * 0.7 % * 1050) {Modified duration * assumed yield change | 33.07 |

| Sr. No. | Items | Particulars | Amount (in ₹) |
|---|-------|---------------------------------|---------------|
| | | (%) * market value of security} | |
| Total capital required (for CCR + credit risk + specific risk + general market risk) | | | 34.23 |

@The supervisory haircut of 2 per cent has been scaled down using the formula indicated in paragraph 155.

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 24 of the Circular | 1000 * 1.00 | 1000 |
| 4. | Collateral for the cash lent | Market value of the security | 1050 |
| 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 155

155. Haircuts

- (1) An AIFI shall use only the haircuts prescribed in this Master Direction 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 24

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 24 represent the ratings assigned by the domestic rating agencies. In the case of exposures toward debt securities issued by foreign Central Governments and foreign corporates, the haircut may be based on ratings of the international rating agencies, as indicated in Table 25
- (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 NCGTC shall also be included under Sovereign.
- (4) An AIFI shall apply a zero haircut for eligible collateral where it is a National Savings Certificate, Kisan Vikas Patras, surrender value of insurance policies and an AIFI' 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 24: Haircuts for Sovereign and other securities which constitute Exposure and Collateral

| SI. 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 | | | |
| | i | AAA to AA A1 | ≤ 1 year | 1 |
| | | | > 1 year and ≤ 5 years | 4 |
| | | > 5 years | 8 | |
| ii | A to BBB A2, A3 and unrated bank securities as specified in paragraph 153(vii) of the circular | ≤ 1 year | 2 | |
| | | > 1 year and ≤ years | 6 | |
| | | > 5 years | 12 | |

| | | | | |
|-----------|---|-----------------------|---|---|
| | iii | Units of Mutual Funds | Highest haircut applicable to any of the above securities, in which the eligible mutual fund {cf. paragraph 153(viii)} shall invest | |
| C | Cash in the same currency | | 0 | |
| D | Gold | | 15 | |
| E | Securitisation Exposures (including those backed by securities issued by foreign sovereigns and foreign corporates) | | | |
| | i | AAA to AA | ≤ 1 year | 2 |
| | | | > 1 year and ≤ 5 years | 8 |
| > 5 years | | | 16 | |
| ii | A to BBB and unrated bank securities as specified in paragraph 153(vii) of the circular | ≤ 1 year | 4 | |
| | | > 1 year and ≤ years | 12 | |
| | | > 5 years | 24 | |

Table 25: Haircut for Exposures and Collaterals which are obligations of foreign sovereigns / foreign corporates

| Issue rating for debt securities as assigned by international rating agencies | Residual Maturity | Sovereigns (%) | 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 an AIFI's exposures are unrated or the AIFI lends non-eligible instruments (i.e., non-investment grade corporate securities), the haircut to be applied on an 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 transactions' (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 below:

Table26: 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 26, as per the formula given in sub-sub-paragraph (10).

- (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 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

H10 = 10-business-day standard supervisory haircut for instrument

NR = actual number of business days between remargining for capital market transactions or revaluation for secured transactions.

TM = minimum holding period for the type of transaction

156. 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 an AIFI 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 24 shall be used as the basis which shall be applied by using the formula in paragraph 155(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 12.
 - (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 AIFI 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 HTM category, and capital for market risk in cases where the securities are held under AFS / HFT categories. 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 an AIFI 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) A lending AIFI 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 154 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 79 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 E_s

E_{fx} = absolute value of the net position in a currency different from the settlement currency

H_{fx} = haircut appropriate for currency mismatch

The intention here is to obtain a net exposure amount after netting of the exposures and collateral and have an add-on amount reflecting possible price changes for the securities involved in the transactions and for foreign exchange

risk if any. 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 154 and 155 equivalently apply for an AIFI using bilateral netting agreements for repo-style transactions.

157. Collateralised OTC derivatives transactions

The calculation of the counterparty credit risk charge for an individual contract shall be as follows:

$$\text{counterparty charge} = [(RC + \text{add-on}) - C_A] \times r \times 9\%$$

where:

RC = the replacement cost,

add-on = the amount for potential future exposure calculated according to paragraph 77(2),

C_A = the volatility adjusted collateral amount under the comprehensive approach prescribed in paragraphs 154 and 155 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 paragraph 79 and paragraph 77(3). The haircut for currency risk (Hfx) 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 CRM techniques - On-balance sheet netting

158. On-balance sheet netting is confined to loans / advances and deposits, where an AIFI have legally enforceable netting arrangements, involving specific lien with proof of documentation. The AIFI shall calculate capital requirements on the basis of net credit exposures subject to the following conditions. Where an AIFI,

- (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 154. 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 paragraphs 154 and paragraphs 169 to 172 shall also apply.

C.5 CRM techniques - Guarantees

159. Where guarantees are direct, explicit, irrevocable, and unconditional an AIFI shall take account of such credit protection in calculating capital requirements.
160. 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.
161. Operational requirements for guarantees eligible for being treated as a CRM mentioned 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 shall allow the protection provider unilaterally to cancel the cover or that shall 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 an AIFI 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 considering 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.

162. In addition to the legal certainty requirements in paragraph 148, in order for a guarantee to be recognised, the following conditions shall be satisfied:

- (i) On the qualifying default / non-payment of the counterparty, an AIFI is able in a timely manner to pursue the guarantor for any monies outstanding under the documentation governing the transaction. The guarantor may make one lump sum payment of all monies under such documentation to an AIFI, or the guarantor may assume the future payment obligations of the counterparty covered by the guarantee. An AIFI 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 165.

163. 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 36, 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, SPEs shall not be recognised as eligible guarantors.

164. 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.
- (2) Provided that 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.
- (3) 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.

165. 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., an AIFI 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.

166. Currency mismatches

Where the credit protection is denominated in a currency different from that in which the exposure is denominated – i.e., 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.,

$$G_A = G \times (1 - H_{FX})$$

Where;

G = nominal amount of the credit protection

H_{FX} = haircut appropriate for currency mismatch between the credit protection and underlying obligation.

An AIFI using the supervisory haircuts shall apply a haircut of eight per cent for currency mismatch.

167. Sovereign guarantees and counter-guarantees

A claim may be covered by a guarantee that is indirectly counter guaranteed by a sovereign. Such a claim may 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 shall 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.

168. ECGC guaranteed exposures

Risk weight (as given in paragraph 28) applicable to the claims on ECGC shall be capped to the maximum liability amount specified in the whole turnover policy of the ECGC. An AIFI 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, an AIFI may apply the risk weight applicable to claims on ECGC. For the remaining portion of individual export credit, an AIFI may apply the risk weight as per the rating of the counter-party. The Risk Weighted Assets computation shall be mathematically represented as under:

| | |
|---|------------|
| <i>Size of individual export credit exposure i</i> | A_i |
| <i>Size of individual covered export credit exposure i</i> | B_i |
| <i>Sum of individual covered export credit exposures</i> | $\sum B_i$ |
| <i>Where:</i> | |
| <i>i = 1 to n, if total number of exposures is n</i> | |
| <i>Maximum Liability Amount</i> | ML |
| <i>Risk Weight of counter party for exposure i</i> | RW_i |
| <i>RWA for ECGC Guaranteed Export Credit:</i> | |
| $\sum \left[\left(\frac{B_i}{\sum B_i} * ML * 20\% \right) + A_i - \left(\frac{B_i}{\sum B_i} * ML \right) * RW_i \right]$ | |

C.6 Maturity mismatch

169. 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 170 to 172. In case of loans collateralised by an AIFI’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 shall

not be attracted provided an explicit consent of the depositor 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.

170. Definition of maturity

The maturity of the underlying exposure and the maturity of the collateral shall both be defined conservatively. The effective maturity of the underlying shall be gauged as the longest possible remaining time before the counterparty is scheduled to fulfil its obligation, considering any applicable grace period. For the collateral, embedded options which may reduce the term of the collateral shall be considered so that the shortest possible effective maturity is used. The maturity relevant here is the residual maturity.

171. Risk weights for maturity mismatches

As outlined in paragraph 169, collaterals with maturity mismatches are 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.

172. When there is a maturity mismatch with recognised credit risk mitigants (collateral, on-balance sheet netting and guarantees) 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 (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 CRM techniques

173. In the case where an AIFI has multiple CRM techniques covering a single exposure (e.g., an AIFI has both collateral and guarantee partially covering an exposure), an AIFI 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

174. Market risk positions subject to capital charge requirement shall include:

- (i) Positions pertaining to interest rate related instruments and equities in the trading book; and
- (ii) Foreign exchange positions (including open position in gold and other precious metals) throughout an AIFI (both banking and trading books).

175. Trading book for the purpose of capital adequacy shall include:

- (i) Securities included under the Held for Trading (HFT) category
- (ii) Securities included under the Available for Sale (AFS) category
- (iii) Open gold position limits
- (iv) Open foreign exchange position limits
- (v) Trading positions in derivatives, and
- (vi) Derivatives entered into for hedging trading book exposures.

176. An AIFI shall manage the market risks in its book on an ongoing basis and ensure that the capital requirements for market risks are being maintained on a continuous basis, i.e., at the close of each business day. The AIFI shall also maintain strict risk management systems to monitor and control intra-day exposures to market risks.

177. Capital for market risk shall not be computed 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.

D.2 Interest rate risk

178. The capital charge for interest rate related instruments shall apply to current market value of these items in an AIFI's trading book. Since it is necessary to maintain capital for market risks on an ongoing basis, the trading position shall be marked to market on a daily basis. The current market value shall be determined as per extant [Reserve Bank of India \(All India Financial Institutions – Classification, Valuation and Operation of Investment Portfolio\) Directions, 2025](#).

179. 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.

180. For the debt securities held under AFS category, in view of the possible longer holding period and attendant higher specific risk, an AIFI shall hold total capital charge for market risk equal to greater of (i) and (ii) below:

- (i) Specific risk capital charge computed (according to Tables 27.1, 28.1, 29.1, 30.1, 3.1, as applicable) notionally for the AFS securities treating them as held under HFT category plus the General Market Risk Capital Charge.
- (ii) Alternate total capital charge for the AFS category computed notionally treating them as held in the banking book

Specific risk

181. 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 | Tables 27.1 and 27.2 |
| b. | Banks' Bonds | Tables 28.1 and 28.2 |
| c. | Corporate Bonds (other than Bank Bonds) | Tables 29.1 and 29.2 |
| d. | Non-common Equity Capital Instruments issued by Financial Entities other than Banks | Tables 30.1 and 30.2 |
| e. | Securitisation Exposure | Paragraph 183 |
| 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) | Tables 27.1 and 27.2 Tables 28.1 and 28.2 Tables 29.1 and 29.2 |
| g. | Equity Investments in Banks | Table 34 |
| h. | Equity Investments in Financial Entities (other than Banks) | Table 35 |
| i. | Equity Investments in Non-financial (commercial) Entities | Table 36 |

Table 27.1: Specific Risk Capital Charge for securities issued by Indian and foreign sovereigns – Held by an AIFI under the HFT Category

| Sr. No. | Nature of Investment | Residual Maturity | Specific risk capital (as % of exposure) |
|-----------|--|--|--|
| A. | Indian Central Government and State Governments | | |
| 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 | 6 months or less | 0.28 |
| | | More than 6 months and up to and including 24 months | 1.13 |

| Sr. No. | Nature of Investment | Residual Maturity | Specific risk capital (as % of exposure) |
|-----------|---|--|--|
| | principal are guaranteed by State Government. | 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 27.2: Alternative Total Capital Charge for securities issued by Indian and foreign sovereigns - Held by an AIFI under the AFS Category

| Sr. No. | Nature of Investment | Residual Maturity | Specific risk capital (as % of exposure) |
|-----------|--|-------------------|--|
| A. | Indian Central Government and State Governments | | |
| 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 | All | 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. | All | 1.80 |
| B. | Foreign Central Governments | | |
| 1. | AAA to AA | All | 0.00 |
| 2. | A | All | 1.80 |
| 3. | BBB | All | 4.50 |
| 4. | BB to B | All | 9.00 |
| 5. | Below B | All | 13.50 |
| | Unrated | All | 9.00 |

**Table 28.1: Specific risk capital charge for bonds issued by a bank
– Held by an AIFI under the HFT category**

| | Residual maturity | Specific risk capital charge (%) | | | |
|--|----------------------------|---|------------------|--|------------------|
| | | 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 Common Equity Tier 1 capital (CET1) including applicable capital conservation buffer (CCB) (%) of the investee bank under Basel III / Total Capital of other banks (where applicable) | | Investments in capital instruments (other than equity [#]) referred to in paragraph 37(i) | All other claims | Investments in capital instruments (other than equity [#]) referred to in paragraph 37(i) | All other Claims |
| 1 | 2 | 3 | 4 | 5 | 6 |
| For banks which are under Basel III Capital Regulations | | | | | |
| 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 |
| For banks which are not under Basel III Capital Regulations | | | | | |
| 9 and above | ≤6 months | 1.75 | 0.28 | 1.75 | 1.75 |
| | > 6 months and | 7.06 | 1.13 | 7.06 | 7.06 |

| | Residual maturity | Specific risk capital charge (%) | | | |
|----------|-------------------|---|-------|--|-------|
| | | 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) | |
| | | ≤ 24 months | | | |
| | >24 months | 11.25 | 1.8 | 11.25 | 11.25 |
| 6 to < 9 | All Maturities | 13.5 | 4.5 | 22.5 | 13.5 |
| 3 to < 6 | All Maturities | 22.5 | 9 | 31.5 | 22.5 |
| 0 to < 3 | All Maturities | 31.5 | 13.5 | 56.25 | 31.5 |
| Negative | All Maturities | 56.25 | 56.25 | Full deduction* | 56.25 |

* The deduction shall be made from Common Equity Tier 1 Capital.

refer to paragraph 191 for specific risk capital charge on equity instruments.

**Table 28.2 Alternative Total Capital Charge for bonds issued by a bank
– Held by an AIFI under AFS category (subject to the conditions stipulated in paragraph 136)**

| | Specific risk capital charge (%) | | | |
|---|---|------------------------|--|----------------------------|
| | 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) | |
| | Investments in capital instruments (other than equity#) referred to in paragraph 37(i) | All other claims | Investments in capital instruments (other than equity#) referred to in paragraph 37(i) | All other claim s |
| 1 | 2 | 3 | 4 | 5 |
| For banks which are under Basel III Capital Regulations | | | | |
| Applicable Minimum CET1 + Applicable CCB and above | 11.25 | 1.8 | 11.25 | 11.25 |
| Applicable Minimum CET1 + (CCB = 75% and <100% of applicable CCB) | 13.5 | 4.5 | 22.5 | 13.5 |
| Applicable Minimum CET1 + (CCB = 50% and <75% of applicable CCB) | 22.5 | 9 | 31.5 | 22.5 |
| Applicable Minimum CET1 + (CCB = 0% and <50% of applicable CCB) | 31.5 | 13.5 | 56.25 | 31.5 |
| Minimum CET1 less than applicable minimum | 56.25 | 56.25 | Full deduction* | 56.25 |

| For banks which are not under Basel III Capital Regulations | | | | |
|--|-------|-------|-----------------|-------|
| 9 and above | 11.25 | 1.8 | 11.25 | 11.25 |
| 6 to < 9 | 13.5 | 4.5 | 22.5 | 13.5 |
| 3 to < 6 | 22.5 | 9 | 31.5 | 22.5 |
| 0 to < 3 | 31.5 | 13.5 | 56.25 | 31.5 |
| Negative | 56.25 | 56.25 | Full deduction* | 56.25 |

* deduction shall be made from Common Equity Tier 1 capital

refer to paragraph 191 for specific risk capital charge on equity instruments

Table 29.1 Specific Risk Capital Charge for Corporate Bonds (Other than bank bonds) – Held by an AIFI under HFT Category

| * Rating by the ECAI | Residual maturity | Specific Risk Capital Charge (in %) |
|------------------------|---|-------------------------------------|
| 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 Standard and Poor. The modifiers '+' or '-' have been subsumed with the main rating category.

Table 29.2 Alternative Total Capital Charge for Corporate Bonds (Other than bank bonds) – Held by an AIFI under AFS Category

| * Rating by the ECAI | Total Capital Charge (in per cent) |
|----------------------|------------------------------------|
| AAA | 1.8 |
| AA | 2.7 |
| A | 4.5 |
| BBB | 9.0 |
| BB and below | 13.5 |
| Unrated | 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 with the main rating category.

Table 30.1: Specific risk capital charge for non-common equity capital instruments issued by financial entities other than a bank – Held by an AIFI under the HFT category

| | Residual maturity | Specific risk capital charge (%) |
|----------------------|----------------------------|--|
| | | Investments in non-common equity capital instruments of financial entities other than banks* |
| 1 | 2 | 3 |
| Specific risk charge | ≤6 months | 1.75 |
| | > 6 months and ≤ 24 months | 7.06 |
| | >24 months | 11.25 |

*Investments falling under paragraph 37 (ii) shall be deducted following corresponding deduction approach

Table30.2: Alternative Total Capital Charge for non-common equity capital instruments issued by financial entities other than a bank - Held by an AIFI under the AFS category

| | Specific risk capital charge (%) |
|----------------------|---|
| | Investments in non- common equity capital instruments of financial entities other than banks referred to in paragraph 37(i) |
| 1 | 2 |
| Specific risk charge | 11.25 |

182. In case of debt mutual fund / ETF which contains a mix of the above debt instruments, the specific risk capital charge shall be computed based on the lowest rated debt instrument / instrument attracting the highest specific risk capital charge in the fund. Debt mutual fund / ETF for which constituent debt details are not available, at least as of each month-end, shall continue to be treated on par with equity for computation of capital charge for market risk as prescribed in paragraphs 188 to 191.

183. 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 HFT and AFS categories shall be calculated according to the revised method as set out in paragraphs 80 to 117 of these Directions. Accordingly, an AIFI 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 securitisation transactions undertaken prior to September 24, 2021, the specific risk capital requirement for securitisation exposures shall be as per the Table below.

Table 31.1: Specific Risk Capital Charge for transactions in Securitisation Exposures prior to September 24, 2021 – Held by an AIFI under HFT and AFS Category

| Rating by the ECAI* | Specific Risk Capital Charge | |
|------------------------|---|---|
| | Securitisation Exposures (in %) | Securitisation Exposures (SDIs) relating to Commercial Real Estate Exposures (in %) |
| 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.

184. An AIFI shall, in addition to computing the CCR charge for OTC derivatives, as part of capital for credit risk as per the Standardised Approach covered in paragraphs 74 to 79, also compute the specific risk charge for OTC derivatives in the trading book as required in terms of paragraphs 199 to 205.

General market risk

185. The capital requirements 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.

186. 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 AIFI 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 32 with no further offsets.
187. An AIFI 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 32);
 - (iii) slot the resulting capital charge measures into a maturity ladder with the fifteen-time bands as set out in Table 32;
 - (iv) subject long and short positions (short position is not allowed in India except in derivatives and Central Government Securities) in each time band to a 5 per cent vertical disallowance; and
 - (v) carry forward the net positions in each time-band for horizontal offsetting subject to the disallowances set out in Table 33.

Table 32 - Duration Method – Time Bands and Assumed changes in Yield

| Time Bands | Assumed Change in Yield | Time Bands | Assumed Change in Yield |
|------------------|-------------------------|-------------------|-------------------------|
| 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 10.6 years | 0.60 |
| 1.0 to 1.9 years | 0.90 | 10.6 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 33 - Horizontal Disallowances

| Zones | Time band | Within the zones | Between adjacent zones | Between zones 1 and 3 |
|---------------|-------------------|------------------|------------------------|-----------------------|
| Zone 1 | 1 month or less | 40% | } | } |
| | 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 10.6 years | | | |
| | 10.6 to 12 years | | | |
| | 12 to 20 years | | | |
| | over 20 years | | | |

Note: The measurement system should include all interest rate derivatives and off balance-sheet instruments in the trading book which react to changes in interest rates, (e.g., forward rate agreements (FRAs), other forward contracts, bond futures, interest rate and cross-currency swaps and forward foreign exchange positions). Options can be treated in a variety of ways as described in paras 202 to 205.

D.3 Equity risk

188. The capital charge for equities shall apply on their current market value in an AIFI'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 mutual funds (other than debt mutual funds / ETFs mentioned in paragraph 182), and commitments to buy or sell equity.

Specific and general market risk

189. Capital charge for specific risk (akin to credit 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 an AIFI'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 an AIFI). 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.

190. Specific Risk Capital Charge for investment in Security Receipts shall be 13.5 per cent (equivalent to 150 per cent risk weight). Since the Security Receipts are by and large illiquid and not traded in the secondary market, there shall be no General Market Risk Capital Charge on them.

191. The specific risk charge for an AIFI's investments in the equity of other banks / other financial entities / non-financial entities shall be as under:

Table 34: Specific risk charge for an AIFI's investments in the equity of a bank held in HFT and AFS portfolios

| Level of Common Equity Tier 1 capital (CET1) including applicable capital conservation buffer (CCB) (%) of the investee bank under Basel III / Total Capital for other banks (where applicable) | All Scheduled Banks (Commercial Banks, Regional Rural Banks, Local Area Banks and Co-operative Banks) | | All Non-scheduled Banks (Commercial Banks, Local Area Banks and Co-operative Banks) (in %) | |
|---|--|------------------|---|------------------|
| | Equity investments in banks referred to in: | | Equity investments in banks referred to in: | |
| | paragraph 37(i) | paragraph 37(ii) | paragraph 37(i) | paragraph 37(ii) |
| For banks which are under Basel III Capital Regulations | | | | |
| 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 |
| 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* |
| For banks which are not under Basel III Capital Regulations | | | | |
| 9 and above | 11.25 | 22.5 | 11.25 | 27 |
| 6 to < 9 | 13.5 | 27 | 22.5 | 31.5 |
| 3 to < 6 | 22.5 | 31.5 | 31.5 | 40.5 |
| 0 to < 3 | 31.5 | 40.5 | 56.25 | Full deduction* |
| Negative | 50 | Full deduction* | Full deduction* | Full deduction* |

*Full deduction shall be made from Common Equity Tier 1 capital

Table 35: Specific risk charge for an AIFI's investments in the equity of financial entities other than a bank

| | Equity investments in financial entities other than a bank referred to in: | |
|--------------------------|--|------------------|
| | paragraph 37(i) | paragraph 37(ii) |
| Specific risk charge (%) | 11.25 | 22.5 |

Table 36: Specific risk charge for an AIFI's investments in the equity of non-financial (commercial) entities

| | Equity investments in non-financial entities |
|--|--|
| | |

| | | |
|--------------------------|--|---|
| | where an AIFI 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 an AIFI (these exposures shall not attract general market risk charge) |
| Specific risk charge (%) | 11.25 | 100 |

D.4 Foreign exchange risk

192. An AIFI'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 AIFI);
- (v) Depending on particular accounting conventions in different countries, any other item representing a profit or loss in foreign currencies;
- (vi) The net delta-based equivalent of the total book of foreign currency options.

Foreign exchange open positions and gold open positions are at present risk-weighted at 100 per cent. 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) in the trading book

193. General market risk

A credit default swap 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, 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.

194. 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 Tables below.

| Table 37 Specific risk capital charges for bought and sold CDS positions in the trading book: 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 / ECAs or foreign rating agencies. In the case of foreign ECAs, the rating symbols used here correspond to Standard and Poor. The modifiers '+' or '-' have been subsumed within the main category.

| Table 38: Specific risk capital charges for bought and sold CDS positions in the trading book: 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 Commercial Real Estate Companies beyond 90 days shall be taken at 9.0 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.

195. Specific risk capital charges for positions hedged by CDS

- (1) An AIFI 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) An AIFI 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) An AIFI 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 195(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 122(3).
 - (ii) The position is captured in paragraph 195(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 clauses (a) and (b) 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.

196. Specific risk charge in CDS positions which are not meant for hedging

In cases not captured in paragraphs 195, a specific risk capital charge shall be assessed against both sides of the positions.

197. 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 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 shall 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. An AIFI 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 39: Add-on Factors for Protection Sellers | |
|--|----------------------|
| (As % of Notional Principal of CDS) | |
| Type of Reference Obligation | Add-on Factor |
| 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 40: Add-on factors for protection buyers | |
|---|----------------------|
| (As % of notional principal of CDS) | |
| Type of reference obligation | Add-on factor |
| 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:

$$\text{Counterparty risk capital charge} = [(\text{RC} + \text{add-on}) - \text{CA}] \times r \times 9 \text{ per cent}$$

Where;

RC = the replacement cost,

add-on = the amount for potential future exposure calculated according to paragraph 77(2).

CA = the volatility adjusted amount of eligible collateral under the Comprehensive Approach prescribed in paragraphs 149 to 157 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.

198. 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

199. 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), bond futures, 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 41.

200. Calculation of positions

(1) The derivatives shall be converted into positions in the relevant underlying and subject to specific and general market risk charges. 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, an AIFI shall use the effective notional amount.

(2) Futures and forward contracts, including forward rate agreements (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 fulfill the contract, the AIFI has 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 an AIFI 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.

201. Calculation of capital charges for derivatives under the standardised methodology

(1) Allowable offsetting of matched positions

- (i) The following may be excluded 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 is only 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) In addition, opposite positions in the same category of instruments can 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;
 - (iii) over one year hence: within thirty days.
- (v) An AIFI 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 32.

(2) Specific risk

Interest rate and currency swaps, FRAs, forward foreign exchange contracts and interest rate futures shall not be subject 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 41- Summary of Treatment of Interest Rate Derivatives

| Instrument | Specific risk charge | General Market risk charge |
|---|-----------------------------|---|
| Exchange-traded Future - Government debt security - Corporate debt security - Index on interest rates | No Yes No | Yes, as two positions Yes, as two positions Yes, as two positions |
| OTC Forward - Government debt security - Corporate debt security - Index on interest rates | No Yes No | Yes, as two positions Yes, as two positions 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 - Corporate debt security - Index on interest rates - FRAs, Swaps | No Yes No No | |

Options

202. Alternative approaches for measuring price risk for options are permissible as under:

- (i) an AIFI which solely use purchased options shall be free to use the simplified approach described in paragraph 204;

Explanation - Unless all its written option positions are hedged by perfectly matched long positions in exactly the same options, in which case no capital charge for market risk is required

- (ii) an AIFI which also write options shall be expected to use one of the intermediate approaches as set out in paragraph 205.

203. In the simplified approach, the positions for the options and the associated underlying, cash or forward, are not subject to the Standardised Methodology but rather are '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 178 to 192. 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 paragraphs 178 to 192 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 underlyings. 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 178 to 191 of this Master Direction .

204. Simplified approach

An AIFI which handle a limited range of purchased options only shall be free to use the simplified approach set out in Table 42, 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 ~~18~~ 20.25 per cent (i.e., ~~9 per cent~~ 11.25 per cent for specific risk plus 9 per cent for general market risk) = ₹180 202.50, less the amount the option is in the money (₹11 – ₹10) x 100 = ₹100, i.e., the capital charge shall be ₹80 102.50. A similar methodology applies for options whose underlying is a foreign currency or an interest rate related instrument.

Table 42- Simplified approach: 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 multiplied by the sum of specific and general market risk charges for the underlying less the amount the option is in the money (if any) bounded at zero |
| Long call | The capital charge shall be the lesser of: |

| | |
|--------------------|---|
| Or Long put | (i) the market value of the underlying security multiplied by the sum of specific and general market risk charges for the underlying (ii) the market value of the option |
|--------------------|---|

Note -

- (1) 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 would 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.
- (2) Some options (e.g., where the underlying is an interest rate or a currency) bear no specific risk, but specific risk will 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.
- (3) For options with a residual maturity of more than six months, the strike price shall be compared with the forward, not current, price. An AIFI unable to do this shall take the in-the-money amount to be zero.
- (4) Where the position does not fall within the trading book (i.e., options on certain foreign exchange or commodities positions not belonging to the trading book), it shall be acceptable to use the book value instead.

205. Intermediate approaches

- (1) Delta-plus method
 - (i) An AIFI which writes options shall be allowed to include delta-weighted options positions within the Standardised Methodology set out in paragraphs 178 to 192. 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, an AIFI 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 to calculate the total capital charge. These sensitivities shall be calculated according to an approved exchange model or to the AIFI's proprietary options pricing model subject to oversight by the Reserve Bank. The Reserve Bank may require an AIFI 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 model's 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 32, 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 bought call option on a June three-month interest-rate future shall in April be considered, based on 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 be similarly 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 a six-month reference rate 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 an underlying FRA takes effect and a positive sign at the time an underlying FRA matures (the rules applying to closely matched positions set out in paragraph 201(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 188 to 191. 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 192. 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 risk and for vega risk. An AIFI 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:

$$\text{Gamma impact} = \frac{1}{2} \times \text{Gamma} \times \text{VU}^2$$

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, the Reserve Bank may require a specific AIFI 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 32; (positions have to be slotted into separate maturity ladders by currency)
 - (ii) for equities and stock indices, each national market;
 - (iii) for foreign currencies and gold, each currency pair and gold;
- (d) Each option on the same underlying shall 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, an AIFI 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 AIFIs shall also have the right to base the market risk capital charge for options portfolios and associated hedging positions 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 the purpose of calculating the capital charge, an AIFI 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 205(1)(v). As an alternative, an AIFI which is a 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 defined in Table 32 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 32. An AIFI using the alternative method for interest rate options set out in paragraph 205(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 shall 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 an AIFI undertaking significant options business at the very least to monitor such risks closely. Additionally, an AIFI 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

206. For computing the total capital charge and Risk Weighted Assets for market risks, the calculations shall be plotted in the following table:

Table 43: 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 |
| IV. Total capital charge and RWA for market risks (I+II+III) | | |

D.8 Treatment for Illiquid Positions

207. Requirements related to Prudent Valuation

An AIFI shall have a framework for prudent valuation practices (for positions that are accounted for at fair value) which shall contain the following:

(1) Systems and Controls

An AIFI 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 the organisation (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 AIFI'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) An AIFI shall mark-to-market to the extent possible. The more prudent side of bid / offer shall be used unless the institution is a significant market maker in a particular position type and it can close out at mid-market.
- (b) The AIFI 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, an AIFI shall follow the [Reserve Bank of India \(All India Financial Institutions – Classification, Valuation and Operation of Investment Portfolio\) Directions, 2025](#). For investment and derivative positions other than those covered in the Master Direction *ibid*, the valuation model used by an AIFI shall be demonstrated to be prudent. When marking to valuation model other than that prescribed in 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 AIFI 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 function should 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) 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.

Explanation – 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.

(iv) Valuation adjustments

(a) As part of its procedures for marking to market, an AIFI shall establish and maintain procedures for considering valuation adjustments. Reserve Bank particularly expects an AIFI using third-party valuations to consider whether valuation adjustments are necessary. Such considerations are also necessary when marking to model.

(b) At a minimum, an AIFI 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 @ 0.4% 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 77(2).

(ii) close-out costs, which factors 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 relates to the costs that will be incurred to administer the portfolio and,

(vi) where appropriate, model risk.

- (c) An AIFI shall follow any recognised method / model to compute the above adjustments except provisions against incurred CVA losses. However, the AIFI shall use the following formula to calculate incurred CVA loss on derivatives transactions:

$$\text{ICVAL}_t = \text{Max} [0, \{(EE_t * RP_t) - (EE_0 * RP_0)\}]$$

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

EE₀ = 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.

RP₀ = 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 an AIFI to change valuation procedures for financial reporting purposes.

- (3) Adjustment to the current valuation of less liquid positions for regulatory capital purposes

- (i) An AIFI 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, an AIFI 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, the AIFI shall consider all relevant factors when determining the appropriateness of the adjustment for less liquid positions. These factors may 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/FBIL 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, an AIFI 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 207(3)(ii) shall not be debited to profit and loss account but shall be deducted from CET 1 capital while computing CRAR of the AIFI. The adjustment may exceed those valuation adjustments made under financial reporting / accounting standards and paragraph 207(2)(iv).
- (v) In calculating the eligible capital for market risk, an AIFI 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

208. An AIFI shall adopt the Basic Indicator Approach (BIA) for calculating the Operational Risk capital charge. The Reserve Bank shall review the capital requirement arrived at by the Basic Indicator Approach for general credibility and in the event that credibility is lacking, appropriate supervisory action under Pillar 2 shall be considered.

E.2 The Basic Indicator Approach

209. An AIFI 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 an AIFI's Pillar 1 capital charge, the Reserve Bank shall consider appropriate supervisory action under Pillar 2. The charge may be expressed as follows:

$$KBIA = [\sum (GI_{1...n} \times \alpha)] / n$$

Where:

KBIA = 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.

210. 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), fees received by an AIFI 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 ‘held to maturity’ category;
- (vi) exclude income from legal settlements in favour of an AIFI;
- (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 insurance claims in favour of an AIFI.

211. An AIFI 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 209.
- (ii) Gross income = Net profit (+) Provisions & contingencies (+) operating expenses (Schedule 16) (-) items (iii) to (viii) of paragraph 210.
- (iii) Alpha (α) = 15 per cent

212. 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, an AIFI using this approach is encouraged to comply with 'Guidance Note on Operational Risk Management and Operational Resilience' issued by the Reserve Bank of India on April 30, 2024, and other risk management guidelines prescribed for AIFIs.

213. 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 the SREP and ICAAP

214. The objective of the SREP is to ensure that AIFIs have adequate capital to support all the risks in their business as also to encourage them to develop and use better risk management techniques for monitoring and managing their risks. This in turn would require a well-defined internal assessment process within AIFIs through which they assure the RBI that adequate capital is indeed held towards the various risks to which they are exposed. The process of assurance could also involve an active dialogue between the AIFI and the RBI so that, when warranted, appropriate intervention could be made to either reduce the risk exposure of the AIFI or augment / restore its capital. Thus, Internal Capital Adequacy Assessment Process (ICAAP) is an important component of the SREP.
215. The main aspects to be addressed under the SREP, and therefore, under the ICAAP, shall include:
- (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 an AIFI.
216. 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 AIFIs, on account of both –the possibility of some under-estimation of risks under the Pillar 1 and the actual risk exposure of an AIFI vis-à-vis the quality of its risk management architecture. Illustratively, some of the risks that the AIFIs 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;
- (xv) Collateral risk

217. The quantification of currency induced credit risk shall form a part of an AIFI's ICAAP and an AIFI is expected to address this risk in a comprehensive manner. The ICAAP should measure the extent of currency induced credit risk the AIFI is exposed to and also concentration of such exposures.

Note: An AIFI shall refer to [Reserve Bank of India \(All India Financial Institutions – Credit Risk Management\) Directions, 2025](#) which cover provision on unhedged foreign currency exposures.

218. Under ICAAP, an AIFI 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.

219. The ICAAP document shall, *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 231 for guidance of an AIFI though the ICAAP documents of an AIFI could vary in length and format, in tune with its size, level of complexity, risk profile and scope of operations.

220. The Basel Committee also lays down the following four key principles in regard to the SREP envisaged under Pillar 2:

- (i) Principle 1: AIFIs should have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels.
- (ii) Principle 2: Supervisors should review and evaluate AIFIs' internal capital adequacy assessments and strategies, as well as their ability to monitor and ensure their 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 AIFIs to operate above the minimum regulatory capital ratios and should have the ability to require AIFIs 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 AIFI and should require rapid remedial action if capital is not maintained or restored.

Note:

(1) Principles 1 and 3 relate to the supervisory expectations from an AIFI while the principles 2 and 4 deal with the role of the supervisors under Pillar 2. Pillar 2 (Supervisory Review Process - SRP) requires an AIFI to implement an internal process, called the Internal Capital Adequacy Assessment Process (ICAAP), for assessing their 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 an AIFI to an evaluation process, hereafter called Supervisory Review and Evaluation Process (SREP), and to initiate such supervisory measures on that basis, as might be considered necessary. An analysis of the foregoing principles indicates that the following broad responsibilities have been cast on banks and the supervisors.

(2) AIFIs' responsibilities

- (i) An AIFI should have in place a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels (Principle 1)
- (ii) An AIFI should operate above the minimum regulatory capital ratios (Principle 3)

(3) Supervisors' responsibilities

- (i) Supervisors should review and evaluate an AIFI's ICAAP. (Principle 2)
- (ii) Supervisors should take appropriate action if they are not satisfied with the results of this process. (Principle 2)
- (iii) Supervisors should review and evaluate an AIFI's compliance with the regulatory capital ratios. (Principle 2)
- (iv) Supervisors should have the ability to require an AIFI to hold capital in excess of the minimum. (Principle 3)
- (v) Supervisors should seek to intervene at an early stage to prevent capital from falling below the minimum levels. (Principle 4)
- (vi) 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 an AIFI'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 AIFI's risk profile; and
 - (c) Application and further development of suitable risk management systems in an AIFI.
- (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 an AIFI's ICAAP, conducting an independent assessment of an AIFI's risk profile, and if necessary, taking appropriate prudential measures and other supervisory actions.

These directions seek to provide broad guidance to an AIFI 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 an AIFI in regard to implementation of the ICAAP.

221. Conduct of SREP by the Reserve Bank

- (1) Regulatory capital ratios permit some comparative analysis of capital adequacy across regulated financial 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 an AIFI, conducting analyses that go beyond minimum regulatory capital requirements.
- (2) The Reserve Bank generally expects an AIFI 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 an AIFI through a comprehensive evaluation that takes into account all relevant available information.
- (3) In determining the extent to which an AIFI should hold capital in excess of the regulatory minimum, the Reserve Bank would take into account the combined implications of the AIFI's compliance with regulatory minimum capital requirements, the quality and results of the AIFI's ICAAP, and supervisory assessment of the AIFI's risk management processes, control systems and other relevant information relating to the AIFI's risk profile and capital position.
- (4) The SREP of an AIFI would, thus, be conducted as part of the Reserve Bank's inspection of an AIFI and in the light of the data in the off-site returns received from the AIFI in the Reserve Bank, in conjunction with the ICAAP document, which is required to be submitted every year by an AIFI to the Reserve Bank as per paragraph 222(9)(iii). Through the SREP, the Reserve Bank would evaluate the adequacy and efficacy of the ICAAP of an AIFI and the capital requirements derived by them therefrom.
- (5) 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 an AIFI (as the risks covered under the two processes are different),

an AIFI would be expected to demonstrate to the Reserve Bank that the ICAAP adopted by them 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 an AIFI.

- (6) If considered necessary, the SREP could also involve a dialogue between an AIFI's top management and the Reserve Bank from time to time.
- (7) 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 an AIFI; the nature and extent of such a review would be determined by the Reserve Bank.
- (8) Pillar 1 capital requirements will include a buffer for uncertainties surrounding the Pillar 1 regime that affect the financial entities as a whole. AIFI-specific uncertainties will be treated under Pillar 2. Buffers under Pillar 1 will be set to provide reasonable assurance that an AIFI 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 AIFI to operate with a buffer, over and above the Pillar 1 standard. An AIFI should maintain this buffer for a combination of the following:
 - (i) Pillar 1 minimums are anticipated to be set to achieve a level of AIFI creditworthiness in markets that is below the level of creditworthiness sought by many AIFIs for their own reasons. For example, most international financial institutions appear to prefer to be highly rated by internationally recognised rating agencies. Thus, an AIFI 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 an AIFI to raise additional capital, especially if this needs to be done quickly or at a time when market conditions are unfavourable.
 - (iv) For an AIFI to fall below minimum regulatory capital requirements is a serious matter. It may place an AIFI in breach of the provisions of the Reserve Bank regulations and / or attract corrective action on the part of Reserve Bank
 - (v) There may be risks, either specific to AIFIs or more generally to an economy at large, that are not taken into account in Pillar 1. If an AIFI 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 RWAs, which should be added to the total RWAs of the AIFI. No additional Pillar 2 buffer need be maintained for such identified risks.
- (9) As a part of SREP under Pillar 2, Reserve Bank may review the risk management measures taken by an AIFI and its adequacy to manage currency induced credit risk, especially if exposure to such risks is assessed to be on higher side. An AIFI may also refer to [Reserve Bank of India \(All India Financial Institutions – Credit Risk Management\) Directions, 2025](#), which cover provision on unhedged foreign currency exposures.
- (10) Under the SREP, the Reserve Bank would make an assessment as to whether an AIFI maintains adequate capital cushion to take care of the above situations. Such a cushion would generally be reflected in more than minimum capital ratio maintained by the AIFI.
- (11) Under the SREP, the Reserve Bank would also seek to determine whether an AIFI'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 an AIFI, 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 an AIFI-specific additional capital requirement over and above what has been determined under Pillar 1.

- (12) 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 an AIFI with the eligibility criteria for adopting the advanced approaches.

B ICAAP of an AIFI

222. Structural Aspects of ICAAP

- (1) Every AIFI shall have an ICAAP
- (2) The ICAAP shall be prepared, on a solo basis, at every tier for each entity within the group, as also at the level of the consolidated AIFI (i.e., a group of entities where an AIFI is the controlling entity).
- (3) General firm-wide risk management principles
 - (i) Senior management should understand the importance of taking an integrated, firm-wide perspective of an AIFI'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 AIFI's capital markets activities, including securitization, 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 firm-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 lie with an AIFI's Board.
 - (ii) An AIFI'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) Board and senior management shall define the institution's risk appetite and ensure that an AIFI's risk management framework includes detailed policies that set specific firm-wide prudential limits on an AIFI's activities, which are consistent with its risk-taking appetite and capacity.
 - (iv) To determine the overall risk appetite, the Board and senior management shall first have an understanding of risk exposures on an institution-wide basis. To achieve this understanding, the appropriate members of senior management shall bring together the perspectives of the key business and control functions.
 - (v) To develop an integrated institution-wide perspective on risk, senior management should overcome organisational silos between business lines and share information on market developments, risks and risk mitigation techniques. 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.
 - (vi) 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 an AIFI 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 an AIFI's activities evolve.

- (vii) 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.
 - (viii) 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, an AIFI 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 an AIFI:
 - (a) establishes a risk framework in order to assess and appropriately manage the various risk exposures of an AIFI;
 - (b) develops a system to monitor an AIFI's risk exposures and to relate them to the AIFI's capital and reserve funds;
 - (c) establishes a method to monitor an AIFI's compliance with internal policies, particularly in regard to risk management; and
 - (d) effectively communicates all relevant policies and procedures throughout an AIFI.
- (5) Policies, procedures, limits and controls
- (i) The structure, design and contents of an AIFI'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 an AIFI.

- (ii) Institution-wide risk management programmes should include detailed policies that set specific institution-wide prudential limits on the principal risks relevant to an AIFI's activities.
 - (iii) An AIFI'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 an AIFI may be exposed. These limits should consider an AIFI's role in the financial system and be defined in relation to the AIFI's capital, total assets, earnings or, where adequate measures exist, its overall risk level.
 - (iv) An AIFI's policies, procedures and limits should:
 - (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 institution-wide levels;
 - (b) Ensure that the economic substance of an AIFI's risk exposures, including reputational risk and valuation uncertainty, are fully recognised and incorporated into its risk management processes;
 - (c) Be consistent with an AIFI's stated goals and objectives, as well as its overall financial strength;
 - (d) Clearly delineate accountability and lines of authority across the AIFI'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 an AIFI 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) An AIFI'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) An AIFI'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 an AIFI's aggregate risk profile, as well as the main assumptions used for risk aggregation.
- (7) MIS should be
- (i) adaptable and responsive to changes in an AIFI's underlying risk assumptions and should incorporate multiple perspectives of risk exposure to account for uncertainties in risk measurement.
 - (ii) sufficiently flexible so that the institution can generate forward-looking AIFI-wide scenario analyses that capture management's interpretation of evolving market conditions and stressed conditions.
 - (iii) 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.

- (iv) Third-party inputs or other tools used within MIS (e.g., credit ratings, risk measures, models) should be subject to initial and ongoing validation.
- (8) 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.
- (9) 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 an AIFI 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 an AIFI's changing risk profile on the AIFI'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 an AIFI 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 232, shall be furnished to the Reserve Bank (i.e., to the CGM-in-Charge, Department of Supervision, Central Office, Reserve Bank of India, with a copy addressed to Senior Supervisory Manager of the AIFI). The document shall reach the Reserve Bank latest by end of the first quarter (i.e., April-June) of the relevant financial year.

223. 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 an AIFI successfully achieve the objectives envisaged by the board.

- (2) The senior management should also receive and review the reports regularly to evaluate the sensitivity of the key assumptions and to assess the validity of an AIFI'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 an AIFI. 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 the AIFI management to assess, on an ongoing basis, the risks that are inherent in their activities and material to the institution.

224. The Principle of Proportionality

- (1) The implementation of ICAAP shall be guided by the principle of proportionality.
- (2) Though an AIFI 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 an AIFI's business operations.
- (3) Given below is a broad approach which could be considered by an AIFI with varying levels of complexity in its operations, in formulating its ICAAP.
 - (i) In relation to an AIFI that defines its activities and risk management practices as simple, in carrying out its ICAAP, the AIFI can:
 - (a) identify and consider its 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 the AIFI is exposed;
 - (c) consider how the AIFI shall act, and the amount of capital that shall be absorbed in the event that each of the risks identified were to materialise;

- (d) consider how the AIFI's capital requirement might alter under the scenarios in (iii) 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 the AIFI should hold, ensuring that its senior management is involved in arriving at that view.
- (ii) In relation to an AIFI that defines its activities and risk management practices as moderately complex, in carrying out its ICAAP, the AIFI 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 the AIFI's capital requirement adequately captures the risks identified in (i) and (ii) 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 AIFI and its customers, in addition to any other risk mitigation action the AIFI plans to take;
 - (e) consider the risk that the AIFI'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 AIFI's business activities forward in detail for one year and in less detail for the next 3 to 5 years, and estimate how the AIFI'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 AIFI's capital and capital requirement would alter and what

the AIFI's reaction to a range of adverse economic scenarios might be;

- (h) document the results obtained from the analyses in (ii), (iv), (vi), and (vii) above in a detailed report for the AIFI'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 (ii), (iv), (vi) and (vii) (i.e., systems for back testing) vis-à-vis the performance / actuals.
- (iii) In relation to an AIFI that defines its activities and risk management practices as complex, in carrying out its ICAAP, the AIFI could follow a proportional approach to its's ICAAP which shall cover the issues identified at (a) to (d) in paragraph 224(3)(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 an AIFI considers appropriate to hold for its business needs. An AIFI may also link such models to generate information on the economic capital considered desirable for it. A model which an AIFI 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 an AIFI's stakeholders for a desired level of risk. For example, an AIFI is likely to use value-at-risk (VaR) models for market risk and advanced modelling approaches for credit risk. An AIFI might also use economic scenario generators to model stochastically its business forecasts and risks. However, the AIFI shall take prior approval of the Reserve Bank for migrating to the advanced approaches. Such an AIFI 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.

225. 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 an AIFI's activities so that it accurately reflects the major sources of risk that an AIFI is exposed to.
- (2) An AIFI shall ensure appropriate and effective internal control structures, particularly in regard to the risk management processes, in order to monitor the AIFI's continued compliance with internal policies and procedures. As a minimum, an AIFI 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 an AIFI's capital assessment process based on the nature, scope, scale and complexity of an AIFI's activities;
 - (iii) the timely identification of any concentration risk;
 - (iv) the accuracy and completeness of any data inputs into an AIFI's capital assessment process;
 - (v) the reasonableness and validity of any assumptions and scenarios used in the capital assessment process; and
 - (vi) that the AIFI conducts appropriate stress testing;

226. 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. At a minimum, the management of an AIFI shall develop and maintain an appropriate strategy that should ensure that the AIFI maintains adequate capital commensurate with the nature, scope, scale, complexity and risks inherent in the AIFI's on-balance-sheet and off-balance-sheet activities and should demonstrate as to how the strategy dovetails with the macro-economic factors.
- (2) An AIFI 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.

227. ICAAP to be a risk-based process

- (1) An AIFI 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 AIFI. 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) An AIFI'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.

228. ICAAP to include stress tests and scenario analyses

- (1) As part of the ICAAP, an AIFI shall, conduct relevant stress tests periodically, particularly in respect of its material risk exposures, in order to evaluate the potential vulnerability to some unlikely but plausible events or movements in the market conditions that could have an adverse impact on the AIFI.
- (2) The use of stress testing framework can provide an AIFI's management a better understanding of the AIFI's likely exposure in extreme circumstances. In this context, the attention is also invited to the risk management guidelines applicable to AIFIs. An AIFI 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 AIFIs.

229. Use of Capital Models for ICAAP

While there is no single prescribed approach as to how an AIFI should develop its capital model, an AIFI 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 an AIFI's business strategy;
- (vi) The adequacy of the requisite skills and resources within an AIFI to operate, maintain and develop the model.

C Select operational aspects of the ICAAP

The following paragraph outlines in greater detail the scope of the risk universe expected to be normally captured by an AIFI in its ICAAP.

230. 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 AIFIs.
- (2) Some of the risks to which an AIFI is exposed include credit risk, market risk, operational risk, interest rate risk in the banking book, credit concentration risk and liquidity risk (as briefly outlined below). The Reserve Bank has issued guidelines to AIFIs on various risk management areas from time to time. An AIFI'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 an AIFI and, in such cases, should be given same consideration as the more formally defined risk types. For example, an AIFI 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 should be supported by adequate capital. Additionally, an AIFI 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 an AIFI 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 an AIFI.

231. Scope of risk universe to be captured in ICAAP

(1) Credit risk

- (i) An AIFI 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. 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) An AIFI 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 an AIFI's capital adequacy.
- (iii) An AIFI should assess exposures, regardless of whether they are rated or unrated. In case they are unrated, it would be in order for AIFIs to derive notional external ratings of the unrated exposure by mapping its internal credit risk ratings / grades of the exposure used for pricing purposes with the external ratings scale. Thereafter, it should determine whether the risk weights applied to such exposures, under the standardised approach, are appropriate for their inherent risk. In those instances where an AIFI 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, an AIFI should consider the higher degree of credit risk in the evaluation of its overall capital adequacy.
- (iv) For a more sophisticated AIFI, 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) An AIFI 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 an AIFI's holdings of exposures that give rise to CCR.
- (ii) A sound counterparty credit risk management framework shall include the identification, measurement, management, approval and internal reporting of CCR.
- (iii) An AIFI'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. An AIFI shall 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 should regard this as an essential aspect of the business to which significant resources need to be devoted. The daily reports prepared on an institution'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 an AIFI's overall CCR exposure.
- (v) An AIFI's CCR management system shall be used in conjunction with internal credit and trading limits.
- (vi) The measurement of CCR should include monitoring daily and intra-day usage of credit lines. An AIFI 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) An AIFI shall be able to measure and monitor peak exposure or potential future exposure (PFE), at both the portfolio and counterparty levels through a limit monitoring system. An AIFI shall take account of large or

concentrated positions, including concentrations by groups of related counterparties, by industry, by market, customer investment strategies, etc.

- (viii) The AIFI 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 shall explicitly consider appropriate risk management strategies (e.g., by hedging against that outcome, or reducing the size of the institution's exposures).
- (ix) An AIFI 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 shall 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) An AIFI shall conduct an independent review of the CCR management system regularly through its own internal auditing process. This review should 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; the verification of the consistency, timeliness and reliability of data sources used to run internal models, including the independence of such data sources;
 - (k) the accuracy and appropriateness of volatility and correlation assumptions;
 - (l) the accuracy of valuation and risk transformation calculations; and
 - (m) the verification of the model's accuracy through frequent back-testing.
- (xii) An AIFI shall 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 77(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 an AIFI's relevant transactions (as could be the case with structured, more complex OTC derivatives), the Reserve Bank may require an AIFI 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) An AIFI shall 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 shall also be tailored to capture key portfolio vulnerabilities to the relevant market developments.

(4) Operational risk

An AIFI shall 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 AIFI. This assessment shall 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) An AIFI shall 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 AIFI shall 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 shall 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 231(5)(iv). The AIFI 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) An Illustrative Approach for Measurement of Interest Rate Risk in the Banking Book (IRRBB) under Pillar 2

- (a) An AIFI shall measure the IRRBB and hold capital commensurate with it. If supervisors determine that an AIFI is not holding capital commensurate with the level of interest rate risk, they shall require an AIFI 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) The main components as per the approach prescribed in the BCBS Paper on “Principles for the Management and Supervision of Interest Rate Risk”, are as under:
 - (i) The assessment should 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 should be calculated by applying a notional interest rate shock of 200 basis points.
 - (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
 - (b) Economic perspective: Gap analysis combined with duration gap analysis, simulation techniques and Internal Models based on VaR
- (c) 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. An AIFI may use the Gap Reports to assess the impact of adverse movements in the interest rate on income through gap method. However, an AIFI may use the simulations

also. An AIFI 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) As per the method indicated in the BCBS Paper on “Principles for the Management and Supervision of Interest Rate Risk”, the following steps are involved in the 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.
 - (f) For details an AIFI may refer to the Annex 3 and 4 of captioned paper issued by the BCBS (Principles for the Management and Supervision of Interest Rate Risk (July 2004)).
- (iii) Other techniques for Interest rate risk measurement: An AIFI 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 1 and 2 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 AIFI's exposures to interest rate risk.

- (d) Suggested approach for measuring the impact of IRRBB on capital
 - (i) If the supervisor feels that an AIFI is not holding capital commensurate with the level of IRRBB, it may either require the AIFI to reduce the risk or allocate additional capital or a combination of the two.
 - (ii) An AIFI 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. An AIFI may 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 obtaining in an AIFI. While an AIFI may on its own decide to hold additional capital towards IRRBB keeping in view the Interest Rate Risk (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 AIFI.
- (e) Limit setting: An AIFI shall be well advised to consider setting the internal limits for controlling its IRRBB. The following are some of the indicative ways for setting the limits:
 - (i) Internal limits shall 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) because of 200 or 300 basis point interest-rate shock.

- (ii) The limits shall also be placed in terms of PV01 value (present value of a basis point) of the net position of an AIFI as a percentage of net worth / capital of an AIFI.

(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 an AIFI's capital, total assets, or overall risk level) to threaten an AIFI's health or ability to maintain its core operations. Concentration risk resulting from concentrated portfolios could be significant for most of the AIFIs.
- (ii) The following qualitative criteria could be adopted by an AIFI to demonstrate that the credit concentration risk is being adequately addressed:
 - (a) While assessing the exposure to concentration risk, an AIFI should keep in view that the calculations of Basel capital adequacy framework are based on the assumption that an AIFI is well diversified.
 - (b) Typically, an AIFI would be a sector-specific institution and have a relatively limited scope for diversifying its assets portfolio. As a result, as compared to banks, these institutions have higher credit concentration risk. The ICAAPs prepared by these institutions shall address this risk. Limiting single name concentration by choosing to adopt lower large exposure limits could be one way to reduce overall credit concentration risk. In addition, an AIFI shall consider diversifying its credit portfolios, inter-alia, along the following dimensions:
 - (i) Geographical spread within the country
 - (ii) Domestic / International / across countries (e.g., in case of EXIM Bank)
 - (iii) Industry segment
 - (iv) Direct Lending / Refinance

- (v) Production Credit / Marketing Credit / Investment Credit (e.g., in case of NABARD)
 - (vi) Microfinance / SMEs / Mid-corporate / Large Corporates
 - (vii) Public Sector / Private Sector Borrowers
 - (viii) Financial sector entities- Public Sector Banks / Private Sector Banks / RRBs / Cooperative Banks, etc.
 - (ix) Residential / Commercial Real Estate (e.g., in case of NHB)
- (c) The sectoral concentration risk and the risk arising from the dimensions mentioned at Paragraph 231(6)(ii)(b) of credit concentration of an AIFI shall be specifically evaluated under SREP and the AIFI may be required to hold additional capital to mitigate the risk.
- (d) While the AIFI's single borrower exposures, the group borrower exposures and capital market exposures are regulated by the exposure norms prescribed by the Reserve Bank as per Master Direction on AIFIs there could be concentrations in these portfolios as well. In assessing the degree of credit concentration, therefore, an AIFI shall consider not only the foregoing exposures but also consider the degree of credit concentration in a particular economic sector or geographical area. An AIFI with operational concentration in a few geographical regions, by virtue of the pattern of its branch network, shall also consider the impact of adverse economic developments in that region, and their impact on the asset quality.
- (e) The performance of specialised portfolios may, in some instances, also depend on key individuals / employees of the AIFI. 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 institutions. In developing its stress tests and scenario analyses, an AIFI should, 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) The following quantitative criteria shall be adopted by an AIFI 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).
 - (b) There could be several approaches to the measurement of credit concentration an AIFI's portfolio. For instance, Herfindahl-Hirshman Index (HHI) could be one of possible methods for measuring concentration risk. However, an AIFI 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 an AIFI. These concentrations should be integrated when assessing an AIFI's overall risk exposure.
- (vi) An AIFI 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, an AIFI should be able to identify and aggregate similar risk exposures across the institution, including across legal entities, asset types (e.g., loans, derivatives and structured products), risk areas (e.g., the trading book) and geographic regions.
- (viii) In addition to the situations described in paragraph 231(6)(ii)(c) 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
 - (i) exposures to counterparties (e.g., hedge funds and hedge counterparties) through the execution or processing of transactions (either product or service);
 - (ii) funding sources;
 - (iii) assets that are held in banking book or trading book, such as loans, derivatives and structured products; and
 - (iv) off-balance sheet exposures, including guarantees, liquidity lines and other commitments.
- (ix) Risk concentrations can also arise through a combination of exposures across these broad categories.
- (x) An AIFI should have an understanding of its institution-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 Structured Investment Vehicles (SIVs); contractual and non-contractual exposures; trading activities; and underwriting pipelines.
- (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) An AIFI 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 AIFI should be aware of possible concentrations that might arise as a result of employing risk mitigation techniques.

- (xiii) An AIFI should employ a number of techniques, as appropriate, to measure risk concentrations. These techniques include shocks to various risk factors; use of business level and institution-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) An AIFI should establish internal position limits for concentrations to which it may be exposed. When conducting periodic stress tests, an AIFI 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 an AIFI's ICAAP and the supervisory review process should not be a mechanical process, but one in which each the AIFI determines, depending on its business model, its own specific vulnerabilities. An appropriate level of capital for risk concentrations should be incorporated in an AIFI's ICAAP, as well as in Pillar 2 assessments. An AIFI should discuss such issues with its supervisor.
- (xvii) An AIFI 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) An AIFI 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) An AIFI 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 an AIFI's liquidity profile.
- (iv) An AIFI 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 AIFI and reflected in the strategy and policies that senior management set to manage liquidity risk.
- (v) An AIFI 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.
- (vi) An AIFI 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.
- (vii) An AIFI 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.

- (viii) An AIFI's management of intraday liquidity risks should be considered as a crucial part of liquidity risk management.
 - (ix) An AIFI should also actively manage its collateral positions and have the ability to calculate all of its collateral positions.
 - (x) An AIFI 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 an AIFI'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 an AIFI'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.
 - (xi) It is important that an AIFI 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) An AIFI'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 an AIFI'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 an AIFI's MIS to help ensure that senior management understands the implications of such exposures for liquidity, earnings, risk concentration and capital. More specifically, an AIFI 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) Implicit support
- (i) Provision of implicit support to a transaction, whether contractual (i.e., credit enhancements provided at the inception of a securitised transaction) or non-contractual (implicit support) can take numerous forms. 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. Implicit support may 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. Since the risk arising from the potential provision of implicit support is not captured ex ante under Pillar 1, it must be considered as part of the Pillar 2 process.
 - (ii) For traditional securitisation structures, the provision of implicit support undermines the clean break criteria, which when satisfied would allow an AIFI to exclude the securitised assets from regulatory capital calculations. By providing implicit support, an AIFI signals to the market that the risk is still with the AIFI and has not in effect been transferred and hence its capital calculation therefore understates the true risk. Accordingly, supervisors are

expected to take appropriate action when a financial entity provides implicit support.

- (iii) When an AIFI 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.
- (iv) 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).
- (v) If an AIFI is found to have provided implicit support on more than one occasion, it 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 AIFI 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 AIFI may be required to hold capital against all securitised assets as though the AIFI 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 AIFI may be required to treat all securitised assets as if they remained on the balance sheet; and
 - (d) The AIFI may be required by the Reserve Bank to hold regulatory capital in excess of the minimum risk-based capital ratios.
- (vi) During the SREP, Reserve Bank will determine implicit support and may take appropriate supervisory action to mitigate the effects. Pending any investigation, the AIFI may be prohibited from any capital relief for planned securitisation transactions (moratorium). The action of Reserve Bank will be aimed at changing the AIFI's behaviour with regard to the provision of implicit support, and to correct market perception as to the willingness of the AIFI 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 an AIFI'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). Furthermore, it exists throughout the organisation and exposure to reputational risk is essentially a function of the adequacy of the AIFI's internal risk management processes, as well as the manner and efficiency with which management responds to external influences on AIFI-related transactions.
- (ii) Generally, an AIFI does not engage in the structuring and sale of highly innovative financial products that may raise reputational risk concerns due to possible mis-selling to clients. However, an AIFI that has subsidiaries, may be called upon to provide unexpected capital or liquidity support to them in case the latter face financial / liquidity stress. All the AIFIs are statutory organisations owned by government and public sector entities (except in SIDBI where IDBI Bank is also a shareholder). Owing to such ownership structure, the AIFIs' activities could potentially have implications for the reputation of the Government. The AIFIs need to take into account these factors while conducting its affairs.
- (iii) 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 an AIFI's earnings, liquidity and capital position. An AIFI should identify potential sources of reputational risk to which it is exposed. These include the AIFI'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 AIFI's risk management processes and appropriately addressed in its ICAAP and liquidity contingency plans.
- (iv) An AIFI 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.

- (v) Reputational risk also may affect an AIFI's liabilities, since market confidence and an AIFI's ability to fund its business are closely related to its reputation. For instance, to avoid damaging its reputation, an AIFI 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, an AIFI's capital position is likely to suffer.
- (vi) An AIFI's management should have appropriate policies in place to identify sources of reputational risk when entering new markets, products or lines of activities.
- (vii) An AIFI'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 an AIFI 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) An AIFI 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 an AIFI's credit, market and liquidity risk profile. 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 an AIFI could be exposed.
- (x) An AIFI 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. In contrast to contractual credit exposures, such as guarantees, implicit support is a more subtle form of exposure. Implicit support arises when an AIFI 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 an AIFI to the risk of loss, such as loss arising from deterioration in the credit quality of the securitisation's underlying assets.

- (xi) By providing implicit support, an AIFI 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. The processes for approving new products or strategic initiatives should consider the potential provision of implicit support and should be incorporated in an AIFI's ICAAP.

(11) Risk evaluation and management

- (i) An AIFI should conduct analyses of the underlying risks when investing in the structured products (permitted by Reserve Bank) and should not solely rely on the external credit ratings assigned to securitisation exposures by the credit rating agencies. An AIFI 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) An AIFI 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, an AIFI 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, an AIFI should review the maturity of the exposures underlying structured credit transactions relative to the issued liabilities in order to assess potential maturity mismatches.

- (iv) An AIFI should track credit risk in securitisation exposures at the transaction level and across securitisations exposures within each business line and across business lines. An AIFI should produce reliable measures of aggregate risk.
- (v) An AIFI also should track all meaningful concentrations in securitisation exposures, such as name, product or sector concentrations, and feed this information to institution-wide risk aggregation systems that track, for example, credit exposure to a particular obligor.
- (vi) An AIFI's own assessment of risk needs to be based on a comprehensive understanding of the structure of the securitisation transaction. An AIFI 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 an AIFI's liquidity and capital position should also be considered.
- (vii) An AIFI 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.
- (viii) An AIFI 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 AIFI would address valuation challenges for potentially illiquid positions held for sale or for trading.
- (ix) The risk measures, stress testing results and contingency plans should be incorporated into the AIFI'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.

- (x) An AIFI 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 AIFI does not understate the true risk in its assessment of capital. In particular, an AIFI 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

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. Considering the above, the following guidelines shall be followed for valuation practices in an AIFI:

- (i) The valuation governance structures and related processes should be embedded in the overall governance structure of the AIFI, 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.
- (ii) An AIFI 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.

- (iii) An AIFI's control processes for measuring and reporting valuations should be consistently applied across the institution 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.
- (iv) To establish and verify valuations for instruments and transactions in which it engages, an AIFI 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.
- (v) For exposures representing material risk, an AIFI 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. An AIFI shall test and review the performance of its models under stress conditions so that it understands the limitations of the models under stress conditions.
- (vi) The relevance and reliability of valuations is directly related to the quality and reliability of the inputs. An AIFI 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, an AIFI 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, an AIFI 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.
- (vii) An AIFI'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 AIFI 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. An AIFI 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 an AIFIs' risk tolerance,
 - (f) addressing existing or potential, institution-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 an AIFI. Board and senior management should be involved in setting stress testing objectives, defining scenarios, discussing the results of stress tests, assessing potential actions and decision making to ensure appropriate use of stress testing in AIFI's risk governance and capital planning. 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) An AIFI'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 AIFI.
- (iv) An AIFI, under its ICAAPs 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 an AIFI'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 AIFI's internal definition of capital resources. In addition, the possibility that a crisis impairs the ability of even a very healthy AIFI to raise funds at reasonable cost should be considered.

- (v) An AIFI should develop methodologies to measure the effect of reputational risk in terms of other risk types, namely credit, liquidity, market and other risks that they 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 an AIFI's credit, market and liquidity risk profiles.
- (vi) An AIFI 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, an AIFI 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.

(14) Compensation practices

- (i) Risk management shall be embedded in the culture of an AIFI. 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 should 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 the institution and should consider risk-adjusted performance measures.
- (iii) An AIFI should provide adequate disclosure regarding its compensation policies to stakeholders.

- (iv) An AIFI's board of directors and senior management have the responsibility to mitigate the risks arising from remuneration policies in order to ensure effective institution-wide risk management.
- (v) An AIFI'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 should have independence and expertise in risk management and compensation. In addition, the Board of Directors should 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 should 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 institution. 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 the institution. Employees' incentive payments should be linked to the contribution of the individual and business to the institution'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 institution 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. The firm should be able to explain the rationale for its mix.
- (xi) The Reserve Bank would review compensation practices in a rigorous and sustained manner and deficiencies, if any, shall be addressed promptly with the appropriate supervisory action.
- (xii) The risk factors discussed above shall not be considered an exhaustive list of those affecting any given AIFI. All relevant factors that present a material source of risk to capital should be incorporated in a well-developed ICAAP. Furthermore, an AIFI 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 an AIFI's measurement framework. In some cases, quantitative tools can include the use of large historical databases; when data are scarcer, an AIFI may choose to rely more heavily on the use of stress testing and scenario analyses. An AIFI 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. An AIFI should be cognisant that qualitative approaches have their own inherent biases and assumptions that affect risk assessment; and accordingly, an AIFI 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 AIFI. An AIFI choosing to conduct risk aggregation among various risk types or business lines should understand the challenges in such aggregation.
- (ii) When aggregating risks, an AIFI 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. An AIFI should have systems capable of aggregating risks based on the AIFI's selected framework. For example, an AIFI 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.
- (iv) An AIFI may undertake new activities including the ones which are only indirectly related to their statutory mandates. Normally an AIFI would not have prior experience in these areas. An AIFI should take due care to identify and manage the strategic risks arising from taking new initiatives, e.g., expanding the scope of its refinance activities to a new set of

institutions and designing new refinance products, new investment / financial products, entering into partnership with banks to introduce new products, etc.

D Format of an ICAAP document

232. An illustrative outline of the format of the ICAAP document, to be submitted to the Reserve Bank, by an AIFI, 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 an AIFI's entire spectrum of risks, how an AIFI intends to mitigate those risks and how much current and future capital is necessary for an AIFI, reckoning other mitigating factors. The purpose of the ICAAP document is to apprise the Board of an AIFI on these aspects as also to explain to the Reserve Bank an AIFI's internal capital adequacy assessment process and an AIFI's approach to capital management. The ICAAP could also be based on the existing internal documentation of an AIFI.

(ii) The ICAAP document submitted to the Reserve Bank shall be formally approved by an AIFI's Board. It is expected that the document would be prepared in a format that would be easily understood at the senior levels of management and would contain all the relevant information necessary for an AIFI and the Reserve Bank to make an informed judgment as to the appropriate capital level of an AIFI 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) could 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
 - (viii) Use of ICAAP within an AIFI
- (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 would typically include:
 - (a) the purpose of the report and the regulated entities within a group that are covered by the ICAAP;
 - (b) the main findings of the ICAAP analysis:
 - (i) how much and what composition of internal capital an AIFI considers it should hold as compared with the minimum CRAR requirement (CRAR) under 'Pillar 1' calculation, and
 - (ii) the adequacy of an AIFI's risk management processes;
 - (c) a summary of the financial position of an AIFI, including the strategic position of an AIFI, its balance sheet strength, and future profitability;
 - (d) brief descriptions of the capital raising and dividend distribution plan including how an AIFI intends to manage its capital in the days ahead and for what purposes;
 - (e) commentary on the most material risks to which an AIFI 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 would cover the relevant organisational and historical financial data for an AIFI. 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 an AIFI, total assets, and any conclusions that can be drawn from trends in the data which may have implications for an AIFI's future.
- (iii) Summary of current and projected financial and capital positions
 - (a) This section would explain the present financial position of an AIFI 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 shall 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 an AIFI's risk appetite, in quantitative terms, as approved by an AIFI'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 AIFI's view of the amount of capital required to meet minimum **regulatory needs** or whether represents the amount of capital that the AIFI believes it would 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 the AIFI 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 an AIFI. 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 would materially impact the ICAAP calculations together with their effects

(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 an AIFI 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 securitisation

(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
- (b) 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;
 - (c) where some of these risks have been highlighted in the report of the Reserve Bank's on-site inspection of an AIFI, an explanation of how the AIFI has mitigated these risks;
 - (d) where relevant, a comparison of the Reserve Bank-assessed CRAR during on-site inspection with the results of the CRAR calculations of an AIFI under the ICAAP;
 - (e) a clear articulation of an AIFI's risk appetite, in quantitative terms, by risk category and the extent of its consistency (its 'fit') with the overall assessment of AIFI's various risks; and
 - (f) where relevant, an explanation of any other methods, apart from capital, used by an AIFI to mitigate the risks.
- (iii) Methodology and Assumptions
 - (a) An AIFI shall provide a description of how assessments for each of the major risks have been approached and the main assumptions made.
 - (b) For instance, an AIFI 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, An AIFI could 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 would 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 an AIFI 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 an AIFI'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 an AIFI 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 an AIFI with conglomerate structure, details of any restrictions on the management's ability to transfer capital into or out of the business(es) arising from, for example, by contractual, commercial, regulatory or statutory constraints that apply, should 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 subsidiaries of an AIFI, 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 an AIFI: This section shall describe the risk management infrastructure within an AIFI 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) MIS at the institution wide level
 - (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, an

AIFI 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 an AIFI.
 - (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 affect an AIFI. The Reserve Bank shall assess the effectiveness of an AIFI's stress testing programme in identifying relevant vulnerabilities.
 - (f) **Sound compensation practices:** This section shall describe the compensation practices followed by an AIFI 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 an AIFI 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 an AIFI would manage its business and capital 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 would include:
 - (i) how an economic downturn would affect:
 - (a) an AIFI's capital funds and future earnings; and
 - (b) an AIFI's CRAR considering 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 an AIFI'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 an AIFI's credit risk counterparties (including migration in their ratings during a recession) and an AIFI's capital and its credit risk capital requirement;
 - (iv) an assessment by an AIFI 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;
 - (v) This section shall also explain which key macroeconomic factors are being stressed, and how those have been identified as

drivers of an AIFI's earnings. an AIFI 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.
- (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 would, 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 shall 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;

- (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 an AIFI 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 an AIFI'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 the AIFI as a whole or for certain debt instruments the AIFI 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
 - (a) 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 copy of any relevant report placed before the senior management or the Board of an AIFI in this regard, along with their response, shall 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, shall 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 an AIFI
 - (a) This section shall contain information to demonstrate the extent to which the concept of capital management is embedded within an AIFI, including the extent and use of capital modelling or scenario analyses and stress testing within the AIFI's capital management policy. For instance, use of ICAAP in setting pricing and charges and the level and nature of future business, shall be an indicator in this regard.
 - (b) This section shall also include a statement of an AIFI's actual operating philosophy on capital management and how this fit in to the ICAAP Document submitted. For instance, differences in risk appetite used in preparing the ICAAP Document vis-à-vis that used for business decisions might be discussed.
 - (c) Lastly, an AIFI 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 AIFI believes shall be helpful to the Reserve Bank in reviewing the ICAAP Document.

E Market discipline

233. 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 an AIFI.
234. An AIFI's disclosures shall be consistent with how senior management and the Board of Directors assess and manage the risks of the AIFI.

235. Non-compliance with the prescribed disclosure requirements shall 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).

236. Interaction with accounting disclosures

The disclosure framework under this paragraph 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.

237. Validation

- (1) The disclosures shall be subjected to adequate validation. For example, since information in the annual financial statements shall 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 paragraph 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 necessarily audited by an external auditor, unless specified.

238. Materiality

- (1) Apart from mandatory disclosures, an AIFI 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. An AIFI shall apply the user test to these specific disclosures and where considered necessary make disclosures below the specified thresholds also.

239. General disclosure principle

- (1) An AIFI shall have a formal disclosure policy approved by the Board of Directors that addresses the AIFI's approach for determining what disclosures it shall make and the internal controls over the disclosure process.
- (2) An AIFI shall implement a process for assessing the appropriateness of its disclosures, including validation and frequency.

240. Scope and frequency of disclosures

- (1) Pillar 3 shall apply at the top consolidated level of the group to which the Capital Adequacy Framework applies.
- (2) An AIFI 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 3 shall be made at least on a quarterly basis by an AIFI:
 - (i) Table DF-2: Capital adequacy;
 - (ii) Table DF-3: Credit risk: General disclosures for all AIFIs; and
 - (iii) Table DF-4: Credit risk: Disclosures for portfolios subject to the standardised approach.
- (3) All disclosures shall either be included in an AIFI's published financial results / statements or, at a minimum, shall be disclosed on the AIFI's website.
- (4) An AIFI shall make Pillar 3 disclosures either concurrently with publication of financial results / statements or provide in these financial results / statements, a direct link to where the Pillar 3 disclosures can be found on the AIFI's website. However, an AIFI shall ensure that in the case of main features template [as

indicated in paragraph 242(2)(iii)] and provision of the full terms and conditions of capital instruments (as indicated in paragraph 242(2)(iv)], the AIFI 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.

241. Regulatory disclosure section

- (1) An AIFI shall make disclosures in the format as specified in Annex 3 of these directions.
- (2) An AIFI shall maintain a 'Regulatory Disclosures Section' on its websites, 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 an AIFI'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 an AIFI on its websites.

242. 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 an AIFI 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 an AIFI 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 an AIFI 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, an AIFI is responsible for conveying its actual risk profile to market participants. The information an AIFI disclose shall be adequate to fulfil this objective. In addition to the specific disclosure requirements as set out in these , an AIFI 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 an AIFI shall use is set out in Table DF-11 of Annex 3 along with explanations.
 - (b) An AIFI shall not add or delete any rows / columns from the common reporting template. The template shall retain the same 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) An AIFI shall disclose a full reconciliation of all regulatory capital elements back to the balance sheet in the audited (or unaudited) financial statements.

- (b) An AIFI 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 3(Table DF-11). The three steps are mentioned below and also illustrated in Table DF-12 of Annex 3
 - (i) Step 1: An AIFI shall disclose the reported balance sheet (Table DF-12 of Annex 3) under the regulatory scope of consolidation as explained in paragraph 7 of this chapter.
 - (ii) Step 2: An AIFI shall expand the lines of the balance sheet under regulatory scope of consolidation (Table DF-12 of Annex 3 to display all components which are used in the composition of capital disclosure template (Table DF-11 of Annex 3)
 - (iii) Step 3: finally, an AIFI 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 3 whichever, applicable.
- (iii) Main features template
 - (a) An AIFI shall disclose a description of the main features of capital instruments issued by them. The template in Table DF-13 of Annex 3 represents the minimum level of summary disclosure which the AIFI 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 3 along with a description of each of the items to be reported. An AIFI 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 group.
 - (c) An AIFI shall keep the completed main features report up-to-date. An AIFI shall ensure that the report is updated and made publicly available, whenever it 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, an AIFI is required to make the following disclosure in respect of the composition of capital:

- (a) Full terms and conditions: An AIFI 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 3
- (b) An AIFI shall keep the terms and conditions of all capital instruments up-to-date (**Table DF-14 of Annex 3**). Whenever there is a change in the terms and conditions of a capital instrument, an AIFI shall update them promptly and make publicly available such updated disclosure.

243. Format of disclosure template

All Pillar 3 disclosure templates as set out in these guidelines are furnished in tabular form in Annex 3. Additional relevant definitions and explanations are also provided for the Pillar 3 disclosures.

Chapter VI

Leverage ratio framework

A Minimum requirement and scope of application of the leverage ratio

244. An AIFI shall maintain minimum leverage ratio of 4 per cent. Both the capital measure and the exposure measure along with leverage ratio shall be disclosed on a quarterly basis. However, an AIFI shall meet the minimum Leverage Ratio requirement at all times (on an ongoing basis).

B Scope of consolidation

245. The scope of consolidation for leverage ratio shall be as under.

- (1) The Basel III leverage ratio framework follows the same scope of regulatory consolidation as is used for the risk-based capital framework under paragraph 8.
- (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 CET 1 capital or deduction from AT 1 capital following corresponding deduction approach) as set out in paragraph 24 shall be excluded from the leverage ratio exposure measure.

C Capital measure

246. The capital measure for the leverage ratio is the Tier 1 capital of the risk-based capital framework (as defined in paragraphs 9 to 25), taking into account various regulatory adjustments / deductions and the transitional arrangements. In other words, the capital measure used for the leverage ratio at any particular point in time shall be the Tier 1 capital measure applying at that time under the risk-based framework.

D Exposure measure

247. General measurement principles

- (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 for AFS and HFT positions);
 - (ii) netting of loans and deposits is not allowed.
- (2) Unless specified differently below, an AIFI shall not take account of physical or financial collateral, guarantees or other credit risk mitigation techniques to reduce the exposure measure.
- (3) An AIFI'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 248 to 251 below.

248. On-balance sheet exposures

- (1) An AIFI 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 249 and 250 below.

Note: Where an AIFI according to its operative accounting framework recognises fiduciary assets on the balance sheet, these assets shall 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, an AIFI shall also disclose the extent of such de-recognised fiduciary items.

- (2) To ensure consistency, balance sheet assets deducted from Tier 1 capital as set out in paragraph 24 may be deducted from the exposure measure. Accordingly,

where a banking, financial or insurance entity is not included in the regulatory scope of consolidation (as set out in paragraph 245), the amount of any investment in the capital of that entity that is totally or partially deducted from CET 1 capital or from AT 1 capital of an AIFI [in terms of paragraphs 197 and 24(7)(ii)(c)] may 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 an AIFI's own credit risk as described in paragraph 24(5) shall not be deducted from the exposure measure.

249. Derivative exposures

- (1) An AIFI 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 249(2) below. If the derivative exposure is covered by an eligible bilateral netting contract as specified in the paragraph 79(2), an alternative treatment as indicated in paragraph 249(3) below may be applied. Written credit derivatives shall be subjected to an additional treatment, as set out in paragraph 249(6) below.

Note: (1) To calculate derivative exposure, an AIFI shall use current exposure method.

(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, an AIFI shall use the sum of positive fair values of these derivatives as the RC.

(3) With reference to derivative exposure covered by an eligible bilateral netting contract, 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 an AIFI has a cross-product netting agreement in place that meets the eligibility criteria of paragraph 79(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 79(2), the amount to be included in the exposure measure shall be determined as follows:

$$\text{Exposure measure} = \text{RC} + \text{Add-on}$$

where;

RC = the replacement cost of the contract (obtained by marking to market), where the contract has a positive value.

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 13 of paragraph 77(2) and Tables 39 and 40 of paragraph 197

- (3) Bilateral netting

When an eligible bilateral netting contract is in place as specified in paragraph 79(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 249(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 replacement cost to gross current replacement cost (NGR). This is expressed through the following formula:

$$A_{\text{Net}} = 0.4 \cdot A_{\text{Gross}} + 0.6 \cdot \text{NGR} \cdot A_{\text{Gross}}$$

where:

NGR = level of net replacement cost / level of gross replacement cost for transactions subject to legally enforceable netting agreements. An AIFI 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

13 of paragraph 77(2) and Tables 39 and 40 of paragraph 197) 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 an AIFI's operative accounting or risk-based framework. Therefore, when calculating the exposure amount by applying paragraphs 249(1) to 249(3) above, an AIFI shall not reduce the exposure amount by any collateral received from the counterparty.
- (ii) With regard to collateral provided, an AIFI 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 shall 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 shall 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 shall be 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 shall be 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 shall 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 shall meet this criterion, provided that the variation margin exchanged is the full amount that shall be necessary to fully extinguish the mark-to-market exposure of the derivative subject to applicable threshold and minimum transfer amounts.

- (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 -

- (a) A Master MNA may be deemed to be a single MNA for this purpose.
 - (b) 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.
 - (c) A MNA shall be deemed to be legally enforceable and effective if it satisfies the conditions as specified in Paragraph 79.
- (ii) If the conditions in paragraph 249(5) 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 AIFI may reduce the replacement cost (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 an AIFI's operative accounting standard.
 - (b) In the case of cash variation margin provided to a counterparty, the posting AIFI may deduct the resulting receivable from its leverage ratio exposure measure, where the cash variation margin has been recognised as an asset under an AIFI'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 249(3)).

(6) 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 may 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 may 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; and

Note: For tranching products if applicable, the purchased protection shall be on a reference obligation with the same level of seniority.
 - (b) the remaining maturity of the credit protection purchased is equal to or greater than the remaining maturity of the written credit derivative.

Explanation -

- (i) 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.
- (ii) 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 shall not 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 shall not be reduced at all.

- (iii) Two reference names are 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 shall result in a credit event on the subordinated reference asset.
 - (iv) The effective notional amount of a written credit derivative may be reduced by any negative change in fair value reflected in an AIFI'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. An AIFI may therefore choose to deduct the individual PFE add-on amount relating to a written credit derivative (which is not offset according to paragraph 249(6)(ii) and whose effective notional amount is included in the exposure measure) from its gross add-on in paragraphs 249(1) to 249(3). Accordingly, where effective bilateral netting contracts are in place, and when calculating $A_{\text{Net}} = 0.4 \cdot A_{\text{Gross}} + 0.6 \cdot \text{NGR} \cdot A_{\text{Gross}}$ as per

paragraphs 249(1) to 249(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 in order to avoid the double counting described in this paragraph.

250. 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.

(2) General treatment (AIFI 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 an AIFI has recognised the securities as an asset on its balance sheet. This may apply, for example, under accounting standard 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 shall 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 shall 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) shall 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 77.

(3) Sale accounting transactions

Leverage may remain with a 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 an AIFI's operative accounting framework, the AIFI 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., an AIFI shall include the sum of amounts in paragraphs 250(2)(i) and 250(2)(ii) for such an SFT) for the purposes of determining its exposure measure.

(4) AIFI acting as an agent

- (i) An AIFI 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 AIFI 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 AIFI is one of the principals in the transaction). Where the AIFI does not own / control the underlying cash or security resource, that resource shall not be leveraged by the AIFI.
- (ii) Where an AIFI 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, then the AIFI shall calculate its exposure measure by applying only clause (ii) of paragraph 250(2). Where, in addition to the conditions in paragraph 250(4), an AIFI acting as an agent in an SFT does not provide an indemnity or guarantee to any of the involved parties, the AIFI is not exposed to the SFT and therefore shall not recognise those SFTs in its exposure measure.
- (iii) An AIFI 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 250(4)(ii) above only if the AIFI'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 an AIFI 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 an AIFI is economically exposed to the underlying security or cash in the transaction is, the AIFI 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.

Calculation of SFT exposure for the purpose of leverage ratio

Illustrative balance sheets of an AIFI

| AIFI A | | | | AIFI 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 AIFI A with Bank / AIFI B | AIFI A lends cash of 100 to Bank / AIFI 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 | 100 | Total | 204 |

| | | | | | | | | | |
|--|--|------------|----------------|------------|--|--------------|------------|----------------|------------|
| Repo of Bank A with Bank / AIFI B | Bank A borrows cash of 50 from Bank / AIFI 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 | AIFI A | | | Bank / AIFI 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)

251. 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 70). For the purpose of determining 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.
 - (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 an AIFI 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 issuing and confirming AIFI.

- (vii) Where there is an undertaking to provide a commitment on an OBS item, An AIFI 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.

These above prescribed CCFs of the standardised approach for credit risk under paragraph 76 (including Table 12), 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 an AIFI without prior notice, or that effectively provide for automatic cancellable 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 251(2), the applicable CCF for that item shall be as indicated in the paragraph 76 above.

E Disclosure and reporting requirements

252. An AIFI shall follow following norms for disclosure and reporting of leverage ratio.

- (1) An AIFI shall publicly disclose its Basel III leverage ratio on both on a standalone and consolidated basis and on a quarterly basis.
- (2) To enable market participants to reconcile leverage ratio disclosures with an AIFI's published financial statements from period to period, and to compare the capital adequacy of the AIFI, the AIFI 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, an AIFI 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 an AIFI' 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 an AIFI' 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) An AIFI shall also report its leverage ratio to the Reserve Bank (Department of Supervision) along with detailed calculations of capital and exposure measures on a quarterly basis.
- (6) Frequency and location of disclosure
- (i) With the exception of the mandatory quarterly frequency requirement in paragraph 252(6)(ii) below, detailed disclosures required according to paragraph 253 shall be made by an AIFI, 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 240.
 - (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, an AIFI, 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 246);
 - (b) Exposure measure (as per paragraphs 247 to 251); and
 - (c) Leverage ratio (as per paragraph 1(44)).
 - (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 paragraph 241(3) and 242. However, specific to

leverage ratio disclosures, an AIFI 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

253. The summary comparison table (Table: DF-16), common disclosure template (Table: DF-17) and explanatory table, qualitative reconciliation and other requirements are set out in the Annex 3: Pillar 3 disclosure requirements.

Chapter VIII

Repeal and Other provisions

Repeal and Saving

254. With the issue of these Directions, the existing Directions, instructions, and guidelines relating to Prudential Norms on Capital Adequacy as applicable to All India Financial Institutions stand repealed, as communicated vide notification dated XX, 2025. The Directions, instructions and guidelines repealed prior to the issuance of these Directions shall continue to remain repealed.
255. 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.

Application of other laws not barred

256. 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

257. 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.

Annex 1

Reporting format for details of investments by FIIs and NRIs in PNCPS qualifying as AT 1 capital

- (i) Name of the AIFI:
(ii) Total issue size / amount raised (in ₹):
(iii) Date of issue:

| | FIIs | | | NRIs | |
|----------------|---------------|---|----------------|---------------|---|
| Number of FIIs | Amount raised | | Number of NRIs | Amount raised | |
| | (in ₹) | As a percentage of the total issue size | | (in ₹) | 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 AIFI

Annex 2
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) An AIFI may also email a soft copy of such details in excel format to tocapdor@rbi.org.in.
- (ii) The reporting shall be duly certified by the compliance officer of the AIFI.
- (iii) The compliance of the capital issuances with the applicable norms shall continue to be examined in course of the supervisory evaluation.

Annex 3
Pillar 3 Disclosure requirements for an AIFI

1. Scope of application and capital adequacy

Table DF-1: Scope of application

Name of the head of the 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 AIFI's holding in the total equity | Regulatory treatment of AIFI'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 deficiencies³ 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 AIFI's holding in the total equity | Capital deficiencies |
|---|----------------------------------|--|---|----------------------|
| | | | | |
| | | | | |

(c) The aggregate amounts (e.g., current book value) of an AIFI'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 AIFI'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 group

Table DF-2: Capital adequacy

| |
|--|
| Qualitative disclosures |
| (a) A summary discussion of an AIFI'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 |

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.

| |
|---|
| (c) Capital requirements for market risk: Standardised duration approach; <ul style="list-style-type: none"> (i) Interest rate risk (ii) Foreign exchange risk (including gold) (iii) Equity risk |
| (d) Capital requirements for operational risk: Basic Indicator Approach |
| (e) CET 1, Tier 1, and Total Capital ratios: <ul style="list-style-type: none"> (i) For the top consolidated group; and (ii) For significant subsidiaries (stand alone or sub-consolidated depending on how the Framework is applied) |

2. Risk exposure and assessment

The risks to which an AIFI is exposed and the techniques that an AIFI 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 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 an AIFI 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), an AIFI 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;
- (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 shall 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 AIFIs

| |
|--|
| <p>Qualitative Disclosures</p> <p>(a) The general qualitative disclosure requirement with respect to credit risk, including:</p> <ul style="list-style-type: none"> (i) Definitions of past due and impaired (for accounting purposes); (ii) Discussion of the AIFI's credit risk management policy; |
| <p>Quantitative Disclosures</p> <p>(b) Total gross credit risk exposures⁴, Fund based and Non-fund based separately.</p> <p>(c) Geographic distribution of exposures⁵, Fund based and Non-fund based separately</p> <ul style="list-style-type: none"> (i) Overseas (ii) Domestic <p>(d) Industry⁶ type distribution of exposures, fund based and non-fund based separately</p> <p>(e) Residual contractual maturity breakdown of assets,⁷</p> <p>(f) Amount of NPAs (Gross)</p> <ul style="list-style-type: none"> (i) Substandard (ii) Doubtful 1 (iii) Doubtful 2 (iv) Doubtful 3 (v) Loss <p>(g) Net NPAs</p> <p>(h) NPA Ratios</p> <ul style="list-style-type: none"> (i) Gross NPAs to gross advances (ii) Net NPAs to net advances <p>(i) Movement of NPAs (Gross)</p> <ul style="list-style-type: none"> (i) Opening balance (ii) Additions (iii) Reductions (iv) Closing balance <p>(j) Movement of provisions (Separate disclosure shall be made for specific provisions and general provisions held by an AIFI with a description of each type of provisions held)</p> <ul style="list-style-type: none"> (i) Opening balance (ii) Provisions made during the period (iii) Write-off (iv) Write-back of excess provisions |

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 of banks. If the exposure to any particular industry is more than 5 per cent of the gross credit exposure as computed under (b) above it shall be disclosed separately.

⁷ An AIFI shall use the same maturity bands as used for reporting positions in the ALM returns.

| |
|---|
| <p>(v) Any other adjustments, including transfers between provisions</p> <p>(vi) Closing balance</p> <p>In addition, write-offs and recoveries that have been booked directly to the income statement shall be disclosed separately.</p> <p>(k) Amount of Non-Performing Investments</p> <p>(l) Amount of provisions held for non-performing investments</p> <p>(m) Movement of provisions for depreciation on investments</p> <p>(i) Opening balance</p> <p>(ii) Provisions made during the period</p> <p>(iii) Write-off</p> <p>(iv) Write-back of excess provisions</p> <p>(v) Closing balance</p> <p>(n) By major industry or counterparty type:</p> <p>(i) Amount of NPAs and if available, past due loans, provided separately;</p> <p>(ii) Specific and general provisions; and</p> <p>(iii) Specific provisions and write-offs during the current period.</p> <p>In addition, an AIFI is encouraged also to provide an analysis of the ageing of past-due loans.</p> <p>(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 shall be disclosed separately.</p> |
|---|

Table DF-4 - Credit risk: Disclosures for portfolios subject to the standardised approach

| |
|--|
| <p>Qualitative disclosures</p> <p>(a) For portfolios under the standardised approach:</p> <p>(i) Names of credit rating agencies used, plus reasons for any changes;</p> <p>(ii) Types of exposure for which each agency is used; and</p> <p>(iii) A description of the process used to transfer public issue ratings onto comparable assets in the banking book;</p> |
| <p>Quantitative disclosures</p> <p>(b) For exposure⁸ amounts after risk mitigation subject to the standardised approach, amount of an AIFI's outstanding (rated and unrated) in the following three major risk buckets as well as those that are deducted.</p> <p>(i) Below 100 per cent risk weight</p> <p>(ii) 100 per cent risk weight</p> <p>(iii) More than 100 per cent risk weight</p> <p>(iv) Deducted</p> |

Table DF-5: Credit risk mitigation: Disclosures for standardised approaches⁹

⁸ As defined for disclosures in Table DF-3.

⁹ At a minimum, An AIFI 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, An AIFI are encouraged to give further information about mitigants that have not been recognised for that purpose.

| |
|--|
| <p>Qualitative Disclosures</p> <p>(a) The general qualitative disclosure requirement with respect to credit risk mitigation including:</p> <ul style="list-style-type: none"> (i) Policies and processes for, and an indication of the extent to which an AIFI makes use of, on- and off-balance sheet netting; (ii) policies and processes for collateral valuation and management; (iii) a description of the main types of collateral taken by an AIFI; (iv) the main types of guarantor counterparty and their credit worthiness; and (v) information about (market or credit) risk concentrations within the mitigation taken |
| <p>Quantitative Disclosures</p> <p>(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.</p> <p>(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)</p> |

Table DF-6: Securitisation exposures: Disclosure for standardised approach

| | |
|--------------------------------|---|
| Qualitative Disclosures | |
| (a) | <p>The general qualitative disclosure requirement with respect to securitisation including a discussion of:</p> <ul style="list-style-type: none"> (i) an AIFI's objectives in relation to securitisation activity, including the extent to which these activities transfer credit risk of the underlying securitised exposures away from an AIFI to other entities. (ii) the nature of other risks (e.g., liquidity risk) inherent in securitised assets; (iii) the various roles played by an AIFI 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 an AIFI'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 an AIFI's policy governing the use of credit risk mitigation to mitigate the risks retained through securitisation exposures; <p>[@] An AIFI 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.</p> <p>[#] An AIFI may provide credit protection to a securitisation transaction through guarantees, credit derivatives or any other similar product, if permitted as per regulatory rules.</p> |
| (b) | <p>Summary of an AIFI's accounting policies for securitisation activities, including:</p> <ul style="list-style-type: none"> (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 shall require an AIFI to provide financial support for securitised assets. |

| | |
|---|---|
| (c) | In the banking book, the names of ECAs 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 AIFI. |
| (e) | For exposures securitised losses recognised by the AIFI during the current period broken by the exposure type (e.g., housing 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 an AIFI for which an AIFI 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

| | |
|--------------------------------|---|
| Qualitative disclosures | |
| (a) | The general qualitative disclosure requirement for market risk including the portfolios covered by the standardised approach. |

Quantitative disclosures

- (b) The capital requirements for:
- (i) interest rate risk;
 - (ii) equity position risk; and
 - (iii) 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 per cent 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: <ul style="list-style-type: none"> (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; (iv) Discussion of the impact of the amount of collateral an AIFI shall 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 . |

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.

| | | |
|--|-----|---|
| | (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 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 an AIFI.
- (ii) The reconciliation requirement in terms of paragraph 242(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 shall 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.
 - (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 sections of the text of this Chapter.

Table DF-11: Composition of Capital (Template to be used by an AIFI)

(₹ in crore)

| Basel III common disclosure template to be used by an AIFI | | | |
|--|--|--|--------|
| 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) | | |
| 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 an AIFI.

| | | | |
|---|--|--|--|
| 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 | | |
| 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 an AIFI 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) ¹⁴ | | |
| 20) | Mortgage servicing rights ¹⁵ (amount above 10% threshold) | | |
| 21) | Deferred tax assets arising from temporary differences (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 | | |
| 25) | of which: deferred tax assets arising from temporary differences | | |
| 26) | National specific regulatory adjustments ¹⁶ (26a+26b+26c+26d) | | |
| 26)(a) | of which: Investments in the equity capital of unconsolidated insurance subsidiaries | | |
| 26)(b) | of which: Investments in the equity capital of unconsolidated non-financial subsidiaries ¹⁷ | | |

¹⁴ Only significant investments other than in the insurance and non-financial subsidiaries shall 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 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.

¹⁵ Not applicable in Indian context.

¹⁶ Adjustments which are not specific to the Basel III regulatory adjustments (as prescribed by the Basel Committee) shall 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 shall be explained in the Notes of this disclosure template.

¹⁷ 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.

| | | | |
|---|---|--|--|
| 26)(c) | of which: Shortfall in the equity capital of majority owned financial entities which have not been consolidated with an AIFI ¹⁸ | | |
| 26)(d) | of which: Unamortised pension funds expenditures | | |
| 27) | Regulatory adjustments applied to Common Equity Tier 1 due to insufficient AT 1 and Tier 2 to cover deductions | | |
| 28) | Total regulatory adjustments to Common equity Tier 1 | | |
| 29) | Common Equity Tier 1 capital (CET1) | | |
| AT 1 capital: instruments | | | |
| 30) | Directly issued qualifying AT 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 AT 1 | | |
| 34) | AT 1 instrument (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) | AT 1 capital before regulatory adjustments | | |
| AT 1 capital: regulatory adjustments | | | |
| 37) | Investments in own AT 1 instruments | | |
| 38) | Reciprocal cross-holdings in AT 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 an AIFI 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) ¹⁹ | | |
| 41) | National specific regulatory adjustments (41a+41b) | | |
| 41) (a) | of which: Investments in the AT 1 capital of unconsolidated insurance subsidiaries | | |
| 41) (b) | of which: Shortfall in the AT 1 capital of majority owned financial entities which have not been consolidated with an AIFI | | |
| 42) | Regulatory adjustments applied to AT 1 due to insufficient Tier 2 to cover deductions | | |
| 43) | Total regulatory adjustments to AT 1 capital | | |
| 44) | AT 1 capital (AT 1) | | |
| 45) | Tier 1 capital (T1 = CET 1 + AT 1) (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 CET 1 and AT 1 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 ²⁰ | | |

¹⁸Please refer to [paragraph 8\(8\) of this Chapter](#). 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.

¹⁹ Please refer to [Footnote 17 above](#).

²⁰ Eligible Provisions and revaluation Reserves in terms [of paragraph 18\(1\)\(a\)](#), both to be reported and break-up of these two items to be furnished in Notes.

| | | | |
|---|---|--|--|
| 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 an AIFI does not own more than 10% of the issued common share capital of the entity (amount above the 10% threshold) | | |
| 55) | Significant investments ²¹ in the capital banking, financial and insurance entities that are outside the scope of regulatory consolidation (net of eligible short positions) | | |
| 56) | National specific regulatory adjustments (56a+56b) | | |
| 56)(a) | of which: Investments in the Tier 2 capital of unconsolidated insurance subsidiaries | | |
| 56)(b) | of which: Shortfall in the Tier 2 capital of majority owned financial entities which have not been consolidated with the AIFI | | |
| 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) | | |
| 60)(a) | of which: total credit risk weighted assets | | |
| 60)(b) | of which: total market risk weighted assets | | |
| 60)(c) | 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) | NA | | |
| 65) | NA | | |
| 66) | NA | | |
| 67) | NA | | |
| 68) | NA | | |
| 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 | | |
| Capital instruments subject to phase-out arrangements | | | |

²¹ Please refer to [Footnote 17 above](#).

| | | | |
|-----|--|--|--|
| 80) | Current cap on CET 1 instruments subject to phase out arrangements | | |
| 81) | Amount excluded from CET 1 due to cap (excess over cap after redemptions and maturities) | | |
| 82) | Current cap on AT 1 instruments subject to phase out arrangements | | |
| 83) | Amount excluded from AT 1 due to cap (excess over cap after redemptions and maturities) | | |
| 84) | Current cap on T2 instruments subject to phase out arrangements | | |
| 85) | Amount excluded from T2 due to cap (excess over cap after redemptions and maturities) | | |

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 an AIFI | |
| | 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 AIFI of the reporting group which meet all of the CET 1 entry criteria set out in paragraph 12 (read with paragraph 13) .This shall be equal to the sum of common shares (and related surplus only) which shall meet the common shares criteria. Other paid-up capital elements shall be excluded. All minority interest shall 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. |
| 4) | An AIFI 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 CET 1 shall be reported here, as determined by the application of paragraph 23(2)(Also see paragraph 23(5) for an illustration). |
| 6) | Sum of rows 1 to 5. |
| 7) | Valuation adjustments according to the requirements of paragraph 207 |
| 8) | Goodwill net of related tax liability, as set out in paragraph 24(1) |
| 9) | Intangibles (net of related tax liability), as set out in paragraph 24(1) |

| | |
|-----|---|
| 10) | Deferred tax assets (net of related tax liability), as set out in paragraph 24(2) |
| 11) | The element of the cash-flow hedge reserve described in paragraph 24(3) |
| 12) | Not relevant |
| 13) | Securitisation gain on sale as described in paragraph 24(4) |
| 14) | Gains and losses due to changes in own credit risk on fair valued liabilities as described in paragraph 24(5) |
| 15) | Defined benefit pension fund net assets, the amount to be deducted, as set out in paragraphs 24(6) |
| 16) | Not relevant |
| 17) | Reciprocal cross-holdings in common equity as set out in paragraph 24(7)(ii)(a) |
| 18) | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation where an AIFI 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 24(7)(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 CET 1 in accordance with paragraph 24(7)(ii)(c) |
| 20) | Not relevant |
| 21) | DTAs arising due to timing differences as per paragraph 24(2) |
| 22) | 15% threshold as per paragraph 24(2)(iii) |
| 23) | Significant investments in the capital of financial entities as per paragraph 24(7)(ii)(c) |
| 24) | Not relevant Row 23 |
| 25) | DTAs arising due to timing differences as per paragraph 24(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]. |
| 27) | Regulatory adjustments applied to Common Equity Tier 1 due to insufficient AT 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 (CET 1), to be calculated as row 6 minus row 28. |
| 30) | Instruments that meet all of the AT1 entry criteria set out in paragraph 9. All instruments issued of subsidiaries of the consolidated group shall 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 in accordance with the requirements of section 7.5 of this Chapter |
| 34) | AT 1 instrument (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 23(4) (please see paragraph 23(5) for illustration). |
| 35) | The amount reported in row 34 that relates to instruments subject to phase out from AT1 in accordance with the requirements of section 7.5 of this Chapter |
| 36) | The sum of rows 30, 33 and 34. |
| 37) | Not relevant |
| 38) | Reciprocal cross-holdings in AT 1 instruments, amount to be deducted from AT1 in accordance with paragraph 24(7)(ii)(a) |
| 39) | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation where an AIFI 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 24(7)(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 24(7)(ii)(c) |
| 41) | Any national specific regulatory adjustments that are required by national authorities to be applied to AT 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 AT 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) | AT 1 capital, to be calculated as row 36 minus row 43. |
| 45) | Tier 1 capital, to be calculated as row 29 plus row 44. |
| 46) | Instruments that meet all of the Tier 2 entry criteria set out in paragraph 18 . All instruments issued of subsidiaries of the consolidated group shall be excluded from this row. Provisions and Revaluation Reserves shall not be included in Tier 2 in this row. |
| 47) | Directly issued capital instruments subject to phase out from Tier 2 in accordance with the requirements of section 7.5 of this Chapter |
| 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 24(4) |
| 49) | The amount reported in row 48 that relates to instruments subject to phase out from Tier 2 in accordance with the requirements of section 7.5 of this Chapter |
| 50) | Provisions and Revaluation Reserves included in Tier 2 calculated in accordance with paragraph 18(1)(a) |
| 51) | The sum of rows 46 to 48 and row 50. |
| 52) | Not relevant |
| 53) | Reciprocal cross-holdings in Tier 2 instruments, amount to be deducted from Tier 2 in accordance with paragraph 24(7)(ii)(a) |
| 54) | Investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation where an AIFI 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 24(7)(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 24(7)(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) | Not relevant |
| 65) | Not relevant |
| 66) | Not relevant |
| 67) | Not relevant |
| 68) | Not relevant |
| 69) | National Common Equity Tier 1 minimum ratio (if different from Basel III minimum). 5.5% shall be reported. |
| 70) | National Tier 1 minimum ratio (if different from Basel III minimum). 7% shall be reported. |
| 71) | National total capital minimum ratio (if different from Basel III minimum). 9% shall 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 paragraph 18(1)(a), prior to the application of the cap. |
| 77) | Cap on inclusion of provisions in Tier 2 under standardised approach calculated in accordance paragraph 18(1)(a) |
| 78) | Provisions eligible for inclusion in Tier 2 in respect of exposures subject to internal ratings-based approach calculated in accordance paragraph 18(1)(a) |
| 79) | Cap for inclusion of provisions in Tier 2 under internal ratings-based approach calculated in accordance paragraph 18(1)(a) |
| 80) | Current cap on CET1 instruments subject to phase out arrangements see section 7.5 of this chapter |
| 81) | Amount excluded from CET1 due to cap (excess over cap after redemptions and maturities), see section 7.5 of this Chapter |
| 82) | Current cap on AT1 instruments subject to phase out arrangements see section 7.5 of this Chapter |
| 83) | Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities) see section 7.5 of this Chapter |
| 84) | Current cap on T2 instruments subject to phase out arrangements see section 7.5 of this Chapter |
| 85) | Amount excluded from T2 due to cap (excess over cap after redemptions and maturities) see section 7.5 of this Chapter |

(2) Three step approach to reconciliation requirements

(i) Step 1: Disclose the reported balance sheet under the regulatory scope of consolidation

- (a) 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 an AIFI specifically, the AIFI'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.

- (b) An AIFI 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. This is intended to enable market participants and supervisors to investigate the risks posed by unconsolidated entities (e.g., unconsolidated subsidiaries). Similarly, an AIFI 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, an AIFI is required to list these legal entities and explain the differences in the consolidation methods.
- (c) 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 group would state that there is no difference between the regulatory consolidation and the accounting consolidation and move to Step 2.
- (d) In addition to the above requirements, an AIFI 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 principal 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 3**.
- (e) Further, under Step 1, an AIFI is required to take its balance sheet in its financial statements (numbers reported the middle column 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, an AIFI are 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. An AIFI 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 a bank | | |
| | of which: Customer deposits | | |
| | of which: Other deposits (pl. specify) | | |
| iii | Borrowings | | |
| | of which: From the Reserve Bank of India | | |
| | of which: From banks | | |
| | of which: From other institutions & agencies | | |
| | of which: Others (pl. specify) | | |
| | of which: Capital instruments | | |
| iv | Other liabilities & provisions | | |
| | Total | | |
| B | Assets | | |
| i | Cash and balances with the Reserve Bank of India | | |
| | Balance with a bank 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 | | |

| | | Balance sheet as in financial statements | Balance sheet under regulatory scope of consolidation |
|-----|---|--|---|
| | | As on reporting date | As on reporting date |
| | of which: Subsidiaries / Joint Ventures / Associates | | |
| | of which: Others (Commercial Papers, Mutual Funds etc.) | | |
| iii | Loans and advances | | |
| | of which: Loans and advances to a bank | | |
| | 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: Expand the lines of the regulatory balance sheet to display all of the components used in the definition of capital disclosure template (i.e., Table DF-11 of Annex 3)

- (a) An AIFI shall 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 3**) are displayed separately. 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 AIFI, the more items would need to be disclosed. Each element must be given a reference number / letter that can be used in Step 3.
- (b) 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 Common Equity Tier 1 (CET1) capital and other elements may only meet the requirements for Additional Tier 1 (AT1) or Tier 2 (T2) capital or may not meet the requirements for inclusion in regulatory capital at all. Therefore, if an AIFI 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 capital' line of the balance sheet in the following way:

| | | |
|-----------------------------------|--|-----|
| Paid-up capital | | Ref |
| of which amount eligible for CET1 | | e |
| of which amount eligible for AT1 | | f |

- (c) 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, the AIFI 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 |

- (d) In addition, as illustrated above, each element of the expanded balance sheet must be given a reference number / letter for use in Step 3.
- (e) An AIFI 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 AIFI met the requirements to be included in CET1, the AIFI would not need to expand this line.

(₹ 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 a bank | | |
| | of which: Customer deposits | | |
| | of which: Other deposits (pl. specify) | | |
| iii | Borrowings | | |
| | of which: From the Reserve Bank of India | | |
| | of which: From a bank | | |
| | 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 the Reserve Bank of India | | |
| | Balance with a bank 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 a bank | | |
| | 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: Map each of the components that are disclosed in Step 2 to the composition of capital disclosure templates

- (a) When reporting the disclosure template (i.e., Table DF-11 of Annex 16), an AIFI is required to use the reference numbers / letters from Step 2 to show the source of every input. Under Step 3 an AIFI 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, an AIFI shall be required to 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 | Source based on reference numbers / letters of the balance sheet under the |

| | | reported by AIFI | 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 shall be reflected in Table DF-11.

(3) Main features template

- (i) Template which an AIFI shall use to ensure that the key features of regulatory capital instruments are disclosed is set out below. An AIFI shall be required to complete all of the shaded cells for each outstanding regulatory capital instrument (an AIFI 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 | |
| | <i>Regulatory treatment</i> | |
| 4 | Basel III rules | |
| 5 | Eligible at solo / group / group & solo | |
| 6 | Instrument type | |
| 7 | Amount recognised in regulatory capital (₹ in crore, as of most recent reporting date) | |
| 8 | Par value of instrument | |
| 9 | Accounting classification | |
| 10 | Original date of issuance | |
| 11 | Perpetual or dated | |

| Disclosure template for main features of regulatory capital instruments | | |
|---|---|--|
| 12 | Original maturity date | |
| 13 | Issuer call subject to prior supervisory approval | |
| 14 | Optional call date, contingent call dates and redemption amount | |
| 15 | Subsequent call dates, if applicable | |
| 16 | <i>Coupons / dividends</i> | |
| | Fixed or floating dividend / coupon | |
| 17 | Coupon rate and any related index | |
| 18 | Existence of a dividend stopper | |
| 19 | Fully discretionary, partially discretionary or mandatory | |
| 20 | Existence of step up or other incentive to redeem | |
| 21 | Noncumulative or cumulative | |
| 22 | Convertible or non-convertible | |
| 23 | If convertible, conversion trigger(s) | |
| 24 | If convertible, fully or partially | |
| 25 | If convertible, conversion rate | |
| 26 | If convertible, mandatory or optional conversion | |
| 27 | If convertible, specify instrument type convertible into | |
| 28 | If convertible, specify issuer of instrument it converts into | |
| 29 | Write-down feature | |
| 30 | If write-down, write-down trigger(s) | |
| 31 | If write-down, full or partial | |
| 32 | If write-down, permanent or temporary | |
| 33 | If temporary write-down, description of write-up mechanism | |
| 34 | Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument) | |
| 35 | Non-compliant transitioned features | |
| 36 | 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 an AIFI 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 regulatory capital treatment under Basel III rules Select from menu: [Common Equity Tier 1] [AT 1] [Tier 2] |
| 5 | Specifies the level(s) within the group at which the instrument is included in capital. Select from menu: [Solo] [Group] [Solo and Group] |
| 6 | 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] |
| 7 | Specifies amount recognised in regulatory capital. Free text |
| 8 | Par value of instrument Free text |
| 9 | Specifies accounting classification. Helps to assess loss absorbency. Select from menu: [Shareholders' equity] [Liability] [Non-controlling interest in consolidated subsidiary] |
| 10 | Specifies date of issuance. Free text |
| 11 | Specifies whether dated or perpetual. Select from menu: [Perpetual] [Dated] |
| 12 | For dated instrument, specifies original maturity date (day, month and year). For perpetual instrument put "no maturity". Free text |
| 13 | Specifies whether there is an issuer call option. Helps to assess permanence. Select from menu: [Yes] [No] |
| 14 | 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 |
| 15 | Specifies the existence and frequency of subsequent call dates, if applicable. Helps to assess permanence. Free text |
| 16 | Specifies whether the coupon / dividend is fixed over the life of the instrument, floating over the life of the instrument, currently fixed but shall move to a floating rate in the future, currently floating but shall move to a fixed rate in the future. Select from menu: [Fixed], [Floating] [Fixed to floating], [Floating to fixed] |
| 17 | Specifies the coupon rate of the instrument and any related index that the coupon / dividend rate references. Free text |
| 18 | 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] |
| 19 | Specifies whether the issuer has full discretion, partial discretion or no discretion over whether a coupon / dividend is paid. If an AIFI has full discretion to cancel coupon / dividend payments under all circumstances it shall select "fully discretionary" (including when there is a dividend stopper that does not have the effect of preventing an AIFI from cancelling payments on the instrument). If there are conditions that shall be met before payment shall be cancelled (e.g., capital below a certain threshold), an AIFI shall select "partially discretionary". If an AIFI is unable to cancel the payment outside of insolvency an AIFI shall select "mandatory". Select from menu: [Fully discretionary] [Partially discretionary] [Mandatory] |
| 20 | Specifies whether there is a step-up or other incentive to redeem. Select from menu: [Yes] [No] |
| 21 | Specifies whether dividends / coupons are cumulative or noncumulative. Select from menu: [Noncumulative] [Cumulative] |
| 22 | Specifies whether instrument is convertible or not. Helps to assess loss absorbency. |

| | |
|----|---|
| | Select from menu: [Convertible] [Nonconvertible] |
| 23 | Specifies the conditions under which the instrument shall convert, including point of non-viability. Where one or more authorities have the ability to trigger conversion, the authorities shall be listed. For each of the authorities it shall 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 |
| 24 | Specifies whether the instrument shall always convert fully, may convert fully or partially, or shall always convert partially Select from menu: [Always Fully] [Fully or Partially] [Always partially] |
| 25 | Specifies rate of conversion into the more loss absorbent instrument. Helps to assess the degree of loss absorbency. Free text |
| 26 | For convertible instruments, specifies whether conversion is mandatory or optional. Helps to assess loss absorbency. Select from menu: [Mandatory] [Optional] [NA] |
| 27 | For convertible instruments, specifies instrument type convertible into. Helps to assess loss absorbency. Select from menu: [Common Equity Tier 1] [AT 1] [Tier 2] [Other] |
| 28 | If convertible, specify issuer of instrument into which it converts. Free text |
| 29 | Specifies whether there is a write down feature. Helps to assess loss absorbency. Select from menu: [Yes] [No] |
| 30 | 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 shall be listed. For each of the authorities it shall 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 |
| 31 | Specifies whether the instrument shall always be written down fully, may be written down partially, or shall 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] |
| 32 | For write down instrument, specifies whether write down is permanent or temporary. Helps to assess loss absorbency. Select from menu: [Permanent] [Temporary] [NA] |
| 33 | For instrument that has a temporary write-down, description of write-up mechanism. Free text |
| 34 | Specifies instrument to which it is most immediately subordinate. Helps to assess loss absorbency on gone-concern basis. Where applicable, an AIFI shall specify the column numbers of the instruments in the completed main features template to which the instrument is most immediately subordinate. Free text |
| 35 | Specifies whether there are non-compliant features. Select from menu: [Yes] [No] |
| 36 | If there are non-compliant features, an AIFI to specify which ones. Helps to assess instrument loss absorbency. Free text |

(4) Full terms and conditions of regulatory capital instruments

Under this template, an AIFI are 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 (All India Financial Institutions – Governance) Directions, 2025 . A private sector AIFI, if any, shall be required to make disclosure on remuneration on an annual basis at the minimum, in its Annual Financial Statements as per the template given below:

Table DF-15: Disclosure Requirements for Remuneration

| Remuneration | | |
|-------------------------|-----|--|
| Qualitative disclosures | (a) | Information relating to the bodies that oversee remuneration. Disclosure shall include: <ul style="list-style-type: none"> • 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 an AIFI'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 shall include: <ul style="list-style-type: none"> • An overview of the key features and objectives of remuneration policy. • Whether the remuneration committee reviewed the firm's remuneration policy during the past year, and if so, an overview of any changes that were made. |

| | | |
|--|-----|--|
| | | <ul style="list-style-type: none"> • A discussion of how an AIFI ensures that risk and compliance employees are remunerated independently of the businesses they oversee. |
| | (c) | <p>Description of the ways in which current and future risks are taken into account in the remuneration processes. Disclosure shall include :</p> <ul style="list-style-type: none"> • An overview of the key risks that an AIFI 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 shall 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) | <p>Description of the ways in which an AIFI seeks to link performance during a performance measurement period with levels of remuneration.</p> <p>Disclosure shall include:</p> <ul style="list-style-type: none"> • An overview of main performance metrics for AIFI, top level business lines and individuals. • A discussion of how amounts of individual remuneration are linked to an AIFI-wide and individual performance. • A discussion of the measures an AIFI shall in general implement to adjust remuneration in the event that performance metrics are weak. This shall include an AIFI's criteria for determining 'weak' performance metrics. |
| | (e) | <p>Description of the ways in which an AIFI seeks to adjust remuneration to take account of the longer-term performance. Disclosure shall include:</p> <ul style="list-style-type: none"> • A discussion of an AIFI'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 an AIFI's policy and criteria for adjusting deferred remuneration before vesting and (if permitted by national law) after |

| | | | |
|---|-----|--|---|
| | (f) | | <p>Description of the different forms of variable remuneration that an AIFI utilizes and the rationale for using these different forms.</p> <p>Disclosure shall include:</p> <ul style="list-style-type: none"> • 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 shall only cover Whole Time Directors / Chief Executive Officer / Other Risk Takers) | (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. |
| | | * | 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) | * | <p>Breakdown of amount of remuneration awards for the financial year to show</p> <ul style="list-style-type: none"> • 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. |
| (l) | | Number of Material Risk Takers identified | |
| (m) | * | Number of cases where malus has been exercised | |
| | * | Number of cases where clawback has been exercised | |
| | * | Number of cases where malus and clawback have been exercised | |
| General Quantitative Disclosures | (n) | | The mean pay for an AIFI as a whole (excluding sub-staff) and the deviation of the pay of each of its Whole Time Directors (WTDs) from the mean pay. |

Table DF-16: Equities – Disclosure for Banking Book Positions

| Qualitative Disclosures | |
|---------------------------------|---|
| 1 | The general qualitative disclosure requirement (Para 2. (1) of this annex) with respect to equity risk, including: <ul style="list-style-type: none"> • 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 shall be classified as: <ul style="list-style-type: none"> • 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) ²² |
| 5 | Total latent revaluation gains (losses) ²³ |
| 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 an AIFI'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 245 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 standard, and are consistent yet proportionate, varying with the

²² Unrealised gains (losses) recognised in the balance sheet but not through the profit and loss account.

²³ Unrealised gains (losses) not recognised either in the balance sheet or through the profit and loss account.

complexity of the balance sheet of the reporting AIFI. Specifically, a common template is set out. However, with respect to reconciliation, an AIFI are to qualitatively reconcile any material difference between total balance sheet assets in its reported financial statements and on-balance sheet exposures as prescribed in the leverage ratio.

(3) Summary comparison table

Applying values at the end of period (e.g., quarter-end), an AIFI 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:

- (a) line 1 shall show an AIFI's total consolidated assets as per published financial statements;
- (b) line 2 shall 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 245 and 248(2);
- (c) line 3 shall show adjustments related to any fiduciary assets recognised on the balance sheet pursuant to an AIFI's operative accounting framework but excluded from the leverage ratio exposure measure, as described in paragraph 249(6)(iii)
- (d) lines 4 and 5 shall show adjustments related to derivative financial instruments and securities financing transactions (i.e., repos and other similar secured lending), respectively;
- (e) line 6 shall show the credit equivalent amount of OBS items, as determined under paragraph 251(2);
- (f) line 7 shall show any other adjustments; and
- (g) line 8 shall show the leverage ratio exposure, which shall be the sum of the previous items. This shall 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) An AIFI 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. An AIFI 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(43) is to be reported in line 22.
- (iii) Reconciliation with public financial statements: An AIFI are 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: An AIFI is required to 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 | |

| | Item | Leverage ratio framework (₹ In crore) |
|--|---|--|
| 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 244 to 253.

| Explanation of each row of the common disclosure template | |
|--|---|
| Row number | Explanation |
| 1 | On-balance sheet assets according to paragraph 248 |
| 2 | Deductions from Basel III Tier 1 capital determined by paragraphs 245(2) and 248(2) and excluded from the leverage ratio exposure measure, reported as negative amounts. |
| 3 | Sum of lines 1 and 2. |
| 4 | Replacement cost (RC) associated with <i>all</i> derivatives transactions, net of cash variation margin received and with, where applicable, bilateral netting according to paragraphs 249(1) to 249(3) and 249(5)(ii). |
| 5 | Add-on amount for all derivative exposures according to paragraphs 249(1) to 249(3) |
| 6 | Grossed-up amount for collateral provided according to paragraph 249(4)(ii). |
| 7 | Deductions of receivables assets from cash variation margin provided in derivatives transactions according to paragraph 249(5)(ii)., reported as negative amounts. |

| Explanation of each row of the common disclosure template | |
|---|---|
| Row number | Explanation |
| 8 | Exempted trade exposures associated with the CCP leg of derivatives transactions resulting from client-cleared transactions according to paragraph 249(6), 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 249(6)(ii) |
| 10 | Adjusted effective notional offsets of written credit derivatives according to paragraph 249(6)(ii) and deducted add-on amounts relating to written credit derivatives according to paragraph 249(6)(iii), 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, removing certain securities received as determined by paragraph 211(2)(i)(b) and adjusting for any sales accounting transactions as determined by paragraph 211(3). |
| 13 | Cash payables and cash receivables of gross SFT assets netted according to paragraph 211(2)(i)(b) and reported as negative amounts. |
| 14 | Measure of counterparty credit risk for SFTs as determined by paragraph 250(2)(iii) |
| 15 | Agent transaction exposure amount determined according to paragraphs 250(4)(i)-250(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 212(2) |
| 18 | Reduction in gross amount of off-balance sheet exposures due to the application of credit conversion factors in paragraph 212(2) |
| 19 | Sum of lines 17 and 18. |
| 20 | Tier 1 capital as determined by paragraph 207 |
| 21 | Sum of lines 3, 11, 16 and 19. |
| 22 | Basel III leverage ratio according to paragraph 4(43) |

- (vi) To ensure that the summary comparison table, common disclosure template and explanatory table remain comparable across jurisdictions, there shall be no adjustments made by an AIFI to disclose its leverage ratio. An AIFI is not permitted to add, delete, or change the definitions of any rows from the summary comparison table and common disclosure template implemented in its jurisdiction. This shall prevent a divergence of tables and templates that shall undermine the objectives of consistency and comparability.