**ANNEX - 5**

## Issue of unsecured bonds as subordinated debt by banks for raising Tier-II capital

### 1. *Terms of issue of bond*

To be eligible for inclusion in Tier – II Capital, terms of issue of the bonds as subordinated debt instruments should be in conformity with the following:

**(a) Amount**

The amount of subordinated debt to be raised may be decided by the Board of Directors of the bank.

**(b) Maturity period**

(i) Subordinated debt instruments with an initial maturity period of less than 5 years, or with a remaining maturity of one year should not be included as part of Tier-II Capital. They should be subjected to progressive discount as they approach maturity at the rates shown below:

| Remaining maturity of the instruments | Rate of discount |
|---|---|
| a) Less than One year | 100% |
| b) More than One year and less than Two years | 80% |
| c) More than Two years and less than Three years | 60% |
| d) More than three years and less than Four Years | 40% |
| e) More than Four years and less than Five years | 20% |

(ii) The bonds should have a minimum maturity of 5 years. However if the bonds are issued in the last quarter of the year i.e. from 1st January to 31st March, they should have a minimum tenure of sixty three months.

**(c) Rate of interest**

The coupon rate would be decided by the Board of Directors of banks.

**(d) Options**

Subordinated debt instruments shall not be issued with a 'put option' or ‘step-up option’. However banks may issue the instruments with a call option subject to strict compliance with each of the following conditions:

(i) Call option may be exercised after the instrument has run for at least **five years**; and

(ii) Call option shall be exercised only with the prior approval of RBI (Department of Banking Operations & Development). While considering the proposals received from banks for exercising the call option the RBI would, among other things, take into consideration the bank's CRAR position both at the time of exercise of the call option and after exercise of the call option.

**(e) Other conditions**

(i) The instruments should be fully paid-up, unsecured, subordinated to the claims of other creditors, free of restrictive clauses and should not be redeemable at the initiative of the holder or without the consent of the Reserve Bank of India.

(ii) Necessary permission from Foreign Exchange Department should be obtained for issuing the instruments to NRIs/ FIIs.

(iii) Banks should comply with the terms and conditions, if any, set by SEBI/other regulatory authorities in regard to issue of the instruments.

**2. Inclusion in Tier II capital**

Subordinated debt instruments will be limited to 50 per cent of Tier-I Capital of the bank. These instruments, together with other components of Tier II capital, should not exceed 100% of Tier I capital.

**3. Grant of advances against bonds**

Banks should not grant advances against the security of their own bonds.

**4. Compliance with Reserve requirements**

The total amount of Subordinated Debt raised by the bank has to be reckoned as liability for the calculation of net demand and time liabilities for the purpose of reserve requirements and, as such, will attract CRR/SLR requirements.

**5. Treatment of Investment in subordinated debt**

Investments by banks in subordinated debt of other banks will be assigned 100% risk weight for capital adequacy purpose. Also, the bank's aggregate investment in Tier II bonds issued by other banks and financial institutions shall be within the overall ceiling of 10 percent of the investing bank's total capital. The capital for this purpose will be the same as that reckoned for the purpose of capital adequacy.

**6. Subordinated Debt in foreign currency raised by Indian banks:** Banks may take approval of RBI on a case-by-case basis.

**7. Subordinated debt to retail investors**: Banks issuing subordinated debt to retail investors are advised to adhere to the following conditions:

a) 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 J of [ Name of The Bank J as disclosed in the Draft Shelf Prospectus, Shelf Prospectus and Tranche Document*** ".

b) For floating rate instruments, banks should not use its Fixed Deposit rate as benchmark.

c) All the publicity material, application form and other communication with the investor should clearly state in bold letters (with font size 14) how a subordinated bond is different from fixed deposit particularly that it is not covered by deposit insurance.

**8. Reporting requirements**

The banks should submit a report to Reserve Bank of India giving details of the capital raised, such as, amount raised, maturity of the instrument, rate of interest together with a copy of the offer document soon after the issue is completed.

**9. Classification in the Balance Sheet:** These instruments should be classified under 'Schedule 4 – Borrowings' of the Balance sheet.