ANNEX 5

Terms and conditions for issue of unsecured bonds as Subordinated Debt by banks to raise Tier II capital

I. Rupee Subordinated Debt

Foreign banks operating in India are not permitted to raise Rupee Tier II subordinated debt in India.

1. Terms of Issue of Bond by Indian banks

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:

i) Amount

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

ii) Maturity period

a. 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. Further, they should be subjected to progressive discount as they approach maturity at the rates shown below:

Remaining Maturity of Instruments	**Rate of Discount (%)**
Less than one year	100
More than One year and less than Two years	80
More than Two years and less than Three years	60
More than Three years and less than Four years	40
More than Four years and less than Five years	20

b. 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.

iii) Rate of interest

Banks may issue Subordinated Tier II bonds at coupon rates decided by their Boards. The instruments should be 'vanilla' with no special features like options, etc.

iv) Other conditions

- 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.
- Necessary permission from Foreign Exchange Department should be obtained for issuing the instruments to NRIs/OCBs/FIIs.
- Banks should comply with the terms and conditions, if any, set by SEBI/other regulatory authorities in regard to issue of the instruments.

v) Banks should indicate the amount of subordinated debt raised as Tier II capital by way of explanatory notes/ remarks in the Balance Sheet as well as in Schedule 5 to the Balance Sheet under ‘Other Liabilities & Provisions'.

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. 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.