भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA
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RBI/2014-15/201
DBOD.No.BP.BC.38/21.06.201/2014-15 September 1, 2014

The Chairman and Managing Director/
Chief Executive Officer
All Scheduled Commercial Banks
(Excluding Regional Rural Banks and Local Area Banks)

Madam / Sir,

Implementation of Basel III Capital Regulations in India – Amendments

Please refer to the 'Guidelines on Implementation of Basel III Capital Regulations in India' issued vide circular DBOD.No.BP.BC.98/21.06.201/2011-12 dated May 2, 2012. These guidelines along with subsequent amendments have been incorporated in the latest Master Circular DBOD.No.BP.BC.6/21.06.201/2014-15 dated July 1, 2014 on 'Basel III Capital Regulations'. The existing guidelines have been reviewed further with a view to facilitate raising of non-equity regulatory capital instruments by banks under Basel III framework. Accordingly, certain specific eligibility criteria of such instruments have been amended as indicated in the subsequent paragraphs. These are also intended to incentivise investors and to increase the investor base.

2. Non-equity Regulatory Capital Instruments (Additional Tier 1 and Tier 2) - Loss Absorption Mechanism

2.1 One of the criteria for Additional Tier 1 (AT1) capital instruments issued by banks requires that these instruments should have principal loss absorption at an objective pre-specified trigger point through either (i) conversion into common shares or (ii) a write-down mechanism which allocates losses to the instruments. Banks were advised to consider issuing AT1 instruments with either conversion into common shares or a permanent write-down mechanism. The criteria for principal loss absorption of AT1 capital instruments at the objective pre-specified trigger point have been reviewed afresh. Banks may now issue these instruments with the principal loss absorption through either (i) conversion into common

Department of Banking Operations and Development, Central Office, 12th Floor, Central Office Building,
Shahid Bhagat Singh Marg, Mumbai - 400 001
बैंकिंग परिचालन और विकास विभाग, केंद्रीय कार्यालय, 12वीं मंज़िल, भारतीय रिजर्व बैंक, केंद्रीय कार्यालय भवन, शहीद भगत सिंह मार्ग, मुंबई – 400 001
Tel No: 022-2266 1602 Fax No: 022-2270 5691 Email ID: cgmicdbodco@rbi.org.in
हिंदी आसान है, इसका प्रयोग बढ़ाइए

shares or (ii) write-down mechanism (temporary or permanent) which allocates losses to the instruments.

2.2 It is, however, reiterated that the terms and conditions of all non-equity capital instruments (i.e. both Additional Tier 1 and Tier 2) issued by banks must have a provision that requires such instruments, at the option of the Reserve Bank of India, to either be permanently written off or converted into common shares upon the occurrence of the 'Point of Non-Viability (PONV)' trigger event.

2.3 Banks shall ensure that the non-common equity capital instruments issued by them meet all the eligibility criteria such as legal, accounting and operational etc., in order for such instruments to be recognised as regulatory capital instruments. Accordingly, a revised Annex 16: *'Minimum Requirements to Ensure Loss Absorbency of Additional Tier 1 Instruments at Pre-specified Trigger and of All Non-equity Regulatory Capital Instruments at the Point of Non-viability'* of the Master Circular is enclosed.

3. Additional Tier 1 Capital Instruments - Exercise of Call Option

In terms of paragraphs 1.6 (a) of Annex 3 and Annex 4 of the Master Circular, call option on the Perpetual Non-Cumulative Preference Shares (PNCPS) and Perpetual Debt Instruments (PDI) respectively is permissible only after the instrument has run for at least ten years. It has been decided that the call option on Additional Tier 1 instrument (PNCPS and PDI) will be permissible at the initiative of the issuer after the instrument has run for at least five years. All other criteria relating to paragraphs 1.6 - 'Optionality' of these Annexes remain unchanged.

4. Tier 2 Capital Instruments – Maturity Period

In terms of paragraph 1.3, Annex 5 of the Master Circular, Tier 2 debt instruments should have a minimum maturity of 10 years. Further, in terms of paragraph 1.3, Annex 6 of the Master Circular, Redeemable Non-Cumulative Preference Shares (RNCPS) and Redeemable Cumulative Preference Shares (RCPS) issued as part of Tier 2 capital should have a minimum maturity of ten years. On a review, it has been decided that banks can issue such Tier 2 capital instruments with a minimum original maturity of at least five years. All other criteria relating to maturity period of Tier 2 instruments remain unchanged.

5. Limits on recognition of Non-equity Regulatory Capital Instruments (Additional Tier 1 and Tier 2) for CRAR

5.1 The limits on admissibility of excess Additional Tier 1 capital and Tier 2 capital for the purpose of computing and reporting Tier 1 capital and CRAR as indicated in paragraphs 4.2.2 (vii) & (viii) of the Master Circular stand withdrawn. Accordingly, a bank, having met the minimum capital requirements as indicated in paragraph 4.2.2 (i) to (iv) read with paragraph 4.5 - 'Transitional Arrangements', may admit excess Additional Tier 1 capital and Tier 2 capital, if any, for the purpose of computing and reporting Tier 1 and CRAR. Consequently, Part A of Annex 14 of the Master Circular also stands withdrawn.

5.2 The definition of 'capital funds' as indicated in paragraph 4.2.2 (ix) of the Master Circular is also revised. Accordingly, for the purpose of all prudential exposure limits, capital funds[1] will be defined as the sum of all eligible Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital, net of regulatory adjustments and deductions.

5.3 In view of the above, limits on admissibility of excess Additional Tier 1 capital and Tier 2 capital will not be applicable also for the purpose of Pillar 3 disclosure requirements (Table DF-11 of Annex 18 of the Master Circular).

6. Non-equity Regulatory Capital Instruments (Additional Tier 1 and Tier 2) - Issuance to Retail Investors

6.1 In terms of paragraph 1.17, Annex 5 of the Master Circular, banks are permitted to issue Tier 2 debt capital instruments to retail investors, subject to adherence to certain specific conditions relating to investors' education and awareness as indicated therein. It is advised that banks may also issue other forms of Tier 2 capital instruments as permitted under Annex 6 of the Master Circular to the retail investors (i.e. Perpetual Cumulative Preference Shares / Redeemable Non-Cumulative Preference Shares / Redeemable Cumulative Preference Shares. However, such issuances should be subject to the approval of their Board and subject to meeting the requirements of paragraph 1.17, Annex 5 of the Master Circular.

6.2 Further, as indicated in paragraph 4.2.4.1B(ii) of the Master Circular, banks are prohibited from issuing Additional Tier 1 capital instruments to the retail investors. It is advised that banks may now issue Additional Tier 1 capital instruments to the retail investors, subject to the approval of their Board.

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[1] The definition of capital funds for the purpose of prudential exposures is only an interim measure. The applicability of this definition will be reviewed by the RBI, based on the large exposures framework released by the Basel Committee on Banking Supervision.

However, with a view to enhancing investors' education and awareness of risk characteristic of Additional Tier 1 instruments, banks should also adhere to the investor protection requirements analogous to those contained in paragraph 1.17 - issuance of Tier 2 debt capital instruments to retail investors of the Annex 5 of the Master Circular. In particular, the loss absorbency features of the instrument should be clearly explained and the investor's sign-off for having understood these features and other terms and conditions of the instrument should be obtained.

7. Coupon Discretion on Additional Tier 1 Debt Capital Instruments

7.1 In terms of paragraph 1.8 (e), Annex 4 of the Master Circular, if the payment of coupons on perpetual debt instrument (PDI) is likely to result in losses in the current year, their declaration should be precluded to that extent. Paragraph 1.8 (e) is now modified as under:

"Paragraph 1.8 (e): Coupons must be paid out of distributable items. In this context, coupon may be paid out of current year profits. However, if current year profits are not sufficient i.e. payment of coupon is likely to result in losses during the current year, the balance amount of coupon may be paid out of revenue reserves (i.e. revenue reserves which are not created for specific purposes by a bank) and / or credit balance in profit and loss account, if any.

However, payment of coupons on PDIs from the revenue reserves is subject to the issuing bank meeting minimum regulatory requirements for CET1, Tier 1 and Total Capital ratios at all times and subject to the requirements of capital buffer frameworks (i.e. capital conservation buffer, countercyclical capital buffer and Domestic Systemically Important Banks)."

7.2 As indicated in paragraph 1.8 (a), Annex 4 of the Master Circular, banks must, however, ensure and indicate in the offer document that they have full discretion at all times to cancel distributions / payments in order to meet the eligibility criteria for perpetual debt instruments.

8. These guidelines become applicable with immediate effect. These instructions will be incorporated in the subsequent Master Circular on Basel III Capital Regulations.

Yours faithfully,

(Sudarshan Sen)
Chief General Manager-in-Charge
Encls.: a/a

Implementation of Basel III Capital Regulations in India – Amendments

(Ref. Circular DBOD.No.BP.BC.38/21.06.201/2014-15 dated September 1, 2014)

Annex 16

Minimum Requirements to Ensure Loss Absorbency of Additional Tier 1 Instruments at Pre-specified Trigger and of All Non-equity Regulatory Capital Instruments at the Point of Non-viability

1. INTRODUCTION

1.1 As indicated in paragraph 4.2.4 of Basel III Capital Regulations, under Basel III non-common equity elements to be included in Tier 1 capital should absorb losses while the bank remains a going concern. Towards this end, one of the important criteria for Additional Tier 1 instruments is that these instruments should have principal loss absorption through either (i) conversion into common shares or (ii) a write-down mechanism, which allocates losses to the instrument at an objective pre-specified trigger point.

1.2 During the financial crisis a number of distressed banks were rescued by the public sector injecting funds in the form of common equity and other forms of Tier 1 capital. While this had the effect of supporting depositors it also meant that Tier 2 capital instruments (mainly subordinated debt), and in some cases Tier 1 instruments, did not absorb losses incurred by certain large internationally-active banks that would have failed had the public sector not provided support. Therefore, Basel III requires that the terms and conditions of all non-common Tier 1 and Tier 2 capital instruments issued by a bank must have a provision that requires such instruments, at the option of the relevant authority, to either be written off or converted into common equity upon the occurrence of the trigger event.

1.3 Therefore, in order for an instrument issued by a bank to be included in Additional (i.e. non-common) Tier 1 or in Tier 2 capital, in addition to criteria for individual types of non-equity regulatory capital instruments mentioned in **Annex 3, 4, 5 and 6,** it must also meet or exceed minimum requirements set out in the following paragraphs.

2. LOSS ABSORPTION OF ADDITIONAL TIER 1 (AT1) INSTRUMENTS AT THE PRE-SPECIFIED TRIGGER

I. Loss Absorption Features

2.1 One of the criteria for AT1 capital instruments[2] requires that these instruments should have principal loss absorption at an objective pre-specified trigger point through either:

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[2] Please refer to the Appendices 4 & 5 of the circular DBOD.No.BP.BC.98 /21.06.201/2011-12

(i) conversion to common shares, or

(ii) a write-down mechanism which allocates losses to the instrument.

The write-down will have the following effects:

(a) reduce the claim of the instrument in liquidation;
(b) reduce the amount re-paid when a call is exercised; and
(c) partially or fully reduce coupon/dividend payments on the instrument.

2.2 Accordingly, banks may issue AT1 instruments with either conversion[3] or write-down (temporary or permanent)[4] mechanism.

II. Level of Pre-specified Trigger and Amount of Equity to be Created by Conversion / Write-down

2.3 The pre-specified trigger for loss absorption through conversion / write-down of Additional Tier 1 instruments (PNCPS and PDI) must be at least Common Equity Tier 1 capital of 6.125% of RWAs[5]. The Write-down of any Common Equity Tier 1 capital shall not be required before a write-down of any Additional Tier 1 capital instrument.

2.4 The conversion / write-down mechanism (temporary or permanent) which allocates losses to the Additional Tier 1 instruments (AT1) instruments must generate Common Equity Tier 1 (CET1) under applicable Indian Accounting Standards. The instrument will receive recognition in AT1 capital only upto the extent of minimum level of CET1 generated (i.e. net of contingent liability recognised under the Indian Accounting Standards, potential tax liabilities, etc., if any) by a full write-down / conversion of the instrument.

2.5 Banks must obtain a certificate from the statutory auditors clearly stating that the conversion / write-down mechanism chosen by the bank for a particular AT1 issuance is

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dated May 2, 2012 on ‘Guidelines on Implementation of Basel III Capital Regulations in India’.

[3] Conversion means conversion to common shares.

[4] When a paid-up instrument is fully and permanently written-down, it ceases to exist resulting in extinguishment of a liability of a bank (a non-common equity instrument) and creates CET1. 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.

[5] All AT1 instruments issued before March 31, 2019 i.e. before the full implementation of Basel III will have two pre-specified triggers. A lower pre-specified trigger at CET1 of 5.5% of RWAs will apply and remain effective before March 31, 2019; from this date the trigger will be raised at CET1 of 6.125% of RWAs for all such instruments. AT1 instruments issued on or after March 31, 2019 will have pre-specified trigger at CET1 of 6.125% of RWAs only.

able to generate CET1 under the prevailing accounting standards[6]. Further, banks must also obtain an external legal opinion confirming that the conversion or write-down of Additional Tier 1 capital instrument at the pre-specified trigger by the issuing bank is legally enforceable. Both reports should be furnished along with reporting of relevant details issuances to the Reserve Bank of India (DBOD).

2.6 The aggregate amount to be written-down / converted for all AT1 instruments on breaching the trigger level must be at least the amount needed to immediately return the bank's CET1 ratio to the trigger level or, if this is not possible, the full principal value of the instruments. Further, the issuer should have full discretion to determine the amount of AT1 instruments to be converted / written-down subject to the amount of conversion/write-down not exceeding the amount which would be required to bring the CET1 ratio to 8% of RWAs (minimum CET1 of 5.5% + capital conservation buffer of 2.5%).

2.7 When a bank breaches the pre-specified trigger of loss absorbency of AT1 and the equity is replenished either through conversion or write-down, such replenished amount of equity will be excluded from the total equity of the bank for the purpose of determining the proportion of earnings to be paid out as dividend in terms of rules laid down for maintaining capital conservation buffer. However, once the bank has attained total Common Equity ratio of 8% without counting the replenished equity capital, that point onwards, the bank may include the replenished equity capital for all purposes[7].

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

2.9 The conversion / write-down of AT1 instruments are primarily intended to replenish the equity in the event it is depleted by losses. Therefore, banks should not use conversion / write-down of AT1 instruments to support expansion of balance sheet by incurring further obligations / booking assets. Accordingly, a bank whose Common Equity ratio slips below 8% due to losses and is still above 6.125% i.e. trigger point, should seek to expand its balance sheet further only by raising fresh equity from its existing shareholders or market and the internal accruals. However, fresh exposures can be taken to the extent of amortization of the existing ones. If any expansion in exposures, such as due to draw down of sanctioned borrowing limits, is inevitable, this should be compensated within the shortest possible time by reducing other exposures[8].

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[6] Auditors certificate would be required not only at the time of issuance of the instruments, but also whenever there is a change in accounting norms / standards which may affect the ability of the loss absorbency mechanism of the instrument to create CET1)

[7] If the total CET1 ratio of the bank falls again below the 8%, it would include the replenished capital for the purpose of applying the capital conservation buffer framework.

[8] For the purpose of determination of breach of trigger, the fresh equity, if any, raised after slippage of CET1 below 8% will not be subtracted. In other words, if CET1 of the bank now is above the trigger level though it would have been below the trigger had it not raised the fresh

The bank should maintain proper records to facilitate verification of these transactions by its internal auditors, statutory auditors and Inspecting Officers of RBI.

III. Treatment of AT1 Instruments in the event of Winding-Up, Amalgamation, Acquisition, Re-Constitution etc. of the Bank

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

2.11 If a bank goes into liquidation after the AT1 instruments have been written-down, the holders of these instruments will have no claim on the proceeds of liquidation.

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

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

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

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

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

2.15 If the relevant authorities decide to reconstitute a bank or amalgamate a bank with any other bank under the Section 45 of BR Act, 1949, such a bank will be deemed as non-viable or approaching non-viability and both the pre-specified trigger and the trigger at the point of non-viability[9] for conversion / write-down of AT1 instruments will be activated. Accordingly, the AT1 instruments will be fully converted / written-down permanently before amalgamation / reconstitution in accordance with these rules.

IV. Fixation of Conversion Price, Capping of Number of Shares / Voting Rights

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equity which it did, the trigger will not be treated as breached.

[9] As described in subsequent paragraph 3 of this Annex.

2.16 Banks 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[10].

2.17 There will 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 will end up holding the number of shares and attached voting rights exceeding the legally permissible limits. Banks should 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. In order to achieve this, banks should cap the number of shares and / or voting rights in accordance with relevant laws and regulations on Ownership and Governance of banks. Banks should adequately incorporate these features in the terms and conditions of the instruments in the offer document. In exceptional circumstances, if the breach is inevitable, the bank should immediately inform the Reserve Bank of India (DBOD) about it. The investors will be required to bring the shareholdings below the statutory / regulatory ceilings within the specific time frame as determined by the Reserve Bank of India.

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

2.19 In order to ensure the criteria that the issuing bank must maintain at all times all prior authorisation necessary to immediately issue the relevant number of shares specified in the instrument's terms and conditions should the trigger event occur, the capital clause of each bank will have to be suitably modified to take care of conversion aspects.

V. Order of Conversion / Write-down of Various Types of AT1 Instruments

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

3. Minimum Requirements to Ensure Loss Absorbency of Non-equity Regulatory Capital Instruments at the Point of Non-Viability

I. Mode of Loss Absorption and Trigger Event

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

3.1 The terms and conditions of all non-common equity Tier 1 and Tier 2 capital instruments issued by banks in India must have a provision that requires such instruments, at the option of the Reserve Bank of India, 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:

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

a. a decision that a conversion[11] or write-off[12], without which the firm would become non-viable, is necessary, as determined by the Reserve Bank of India; and

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

The Write-off of any Common Equity Tier 1 capital shall not be required before the write-off of any Non-equity (Additional Tier 1 and Tier 2) regulatory capital instrument.

(ii) Such a decision would invariably imply that the write-off or issuance of any new shares as a result of conversion consequent upon the trigger event must 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 must not provide for any residual claims on the issuer which are senior to ordinary shares of the bank (or banking group entity where applicable), following a trigger event and when conversion or write-off is undertaken.

(iii) Any compensation paid to the instrument holders as a result of the write-off[13] must be paid immediately in the form of common shares.

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

(v) In order to ensure that these requirements are met, banks should furnish to RBI (Department of Banking Operations and Development) an external legal opinion confirming that the conversion or write-off feature of non-equity capital instruments (Additional Tier 1 or Tier 2) by the RBI at the point of non-viability is legally

[11] Conversion means full conversion to common shares
[12] Write-off means fully and permanently write-off
[13] 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.

enforceable[14]. Further, the legal opinion should also confirm that there are no legal impediments to the conversion of the instrument into ordinary shares of the bank (or a banking group entity, where applicable) or write-off upon a trigger event. The RBI may also require the bank to submit additional information in order to ensure that such instruments are eligible for inclusion into regulatory capital.

II. A Non-viable Bank

3.2 For the purpose of these guidelines, a non-viable bank will be:

A bank which, owing to its financial and other difficulties, may no longer remain a going concern on its own in the opinion of the Reserve Bank unless appropriate measures are taken to revive its operations and thus, enable it to continue as a going concern. The difficulties faced by a bank should be such that these are likely to result in financial losses and raising the Common Equity Tier 1 capital of the bank should be considered as the most appropriate way to prevent the bank from turning non-viable. Such measures would 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[15].

III. Restoring Viability

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

a. Restore depositors'/investors' confidence;

b. Improve rating /creditworthiness of the bank and thereby improve its borrowing capacity and liquidity and reduce cost of funds; and

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

IV. Other Requirements to be met by the Non-common Equity

[14] This may be submitted by banks while reporting of relevant details of issuances of capital instruments to RBI.

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

Capital Instruments so as to Absorb Losses at the PONV

3.4 Instruments may be issued with either of the following feature:

a. conversion; or
b. permanent write-off

3.5 The amount of non-equity capital to be converted / written-off will be determined by RBI.

3.6 When a bank breaches the PONV trigger and the equity is replenished either through conversion or write-off, such replenished amount of equity will be excluded from the total equity of the bank for the purpose of determining the proportion of earnings to be paid out as dividend in terms of rules laid down for maintaining capital conservation buffer. However, once the bank has attained total Common Equity ratio of 8% without counting the replenished equity capital, that point onwards, the bank may include the replenished equity capital for all purposes[16].

3.7 The provisions regarding treatment of AT1 instruments in the event of winding-up, amalgamation, acquisition, re-constitution etc. of the bank as given in paragraphs 2.10 to 2.15 will 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.

3.8 The provisions regarding fixation of conversion price, capping of number of shares/voting rights applicable to AT1 instruments in terms of paragraphs 2.16 to 2.19 above will also be applicable for conversion of all non-common equity capital instruments (AT1 and Tier 2 capital instruments) at the PONV.

3.9 The provisions regarding order of conversion/write-down of AT1 instruments as given in paragraph 2.20 above will also be applicable for conversion/ write-off of all non-common equity capital instruments (AT1 and Tier 2 capital instruments) at the PONV.

V. Criteria to Determine the PONV

3.10 The above framework will be invoked when a bank is adjudged by Reserve Bank of India to be approaching the point of non-viability, or has already reached the point of non-viability, but in the views of RBI:

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[16] If the total CET1 ratio of the bank falls again below the total Common Equity ratio of 8%, it would include the replenished capital for the purpose of applying the capital conservation buffer framework.

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

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

3.11 The purpose of write-off and / or conversion of non-equity regulatory capital elements will be to shore up the capital level of the bank. RBI would follow a two-stage approach to determine the non-viability of a bank. The **Stage 1** assessment would consist of purely objective and quantifiable criteria to indicate that there is a *prima facie* case of a bank approaching non-viability and, therefore, a closer examination of the bank's financial situation is warranted. The **Stage 2** assessment would consist of supplementary subjective criteria which, in conjunction with the Stage 1 information, would help in determining whether the bank is about to become non-viable. These criteria would be evaluated together and not in isolation.

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

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

3.14 As the capital adequacy is applicable both at solo and consolidated levels, the **minority interests** in respect of capital instruments issued by subsidiaries of banks including overseas subsidiaries can be included in the consolidated capital of the banking group only if these instruments have pre-specified triggers (in case of AT1 capital instruments) / loss absorbency at the PONV[17] (for all non-common equity capital instruments). In addition, where a bank wishes the instrument issued by its subsidiary to be included in the consolidated group's capital in addition to its solo capital, the terms and conditions of that instrument must specify an additional trigger event.

This additional trigger event is the earlier of:

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

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

(2) the decision to make a public sector injection of capital, or equivalent support, without which the bank or the subsidiary would have become non-viable, as determined by the Reserve Bank of India. Such a decision would invariably imply that the write-off or issuance of any new shares as a result of conversion consequent upon the trigger event must occur prior to any public sector injection of capital so that the capital provided by the public sector is not diluted.

3.15 In such cases, the subsidiary should 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 3.14 above.

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