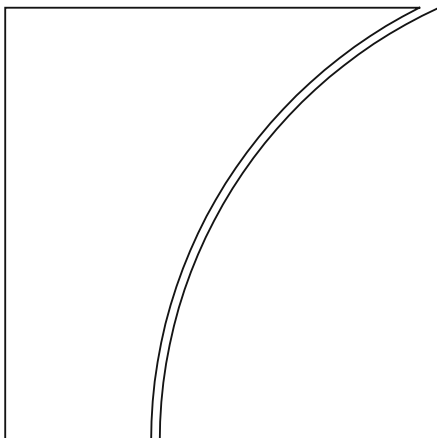


# Basel Committee on Banking Supervision



## Regulatory Consistency Assessment Programme (RCAP)

### Assessment of Basel large exposures regulations – India

July 2019



BANK FOR INTERNATIONAL SETTLEMENTS

**Note that this report refers to the RCAP grades prior to October 2025. The grade 'materially non-compliant (MNC)', ie one notch above the lowest grade, has since been renamed to 'partially non-compliant (PNC)' for greater clarity**

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## Glossary

BIS	Bank for International Settlements
C	Compliant (grade)
G-SIB	Global systemically important bank
HDFC	Housing Development Finance Corporation
ICICI	Industrial Credit and Investment Corporation of India
LC	Largely compliant (grade)
MNC	Materially non-compliant (grade)
MSME	Micro-, small or medium-sized enterprise
NABARD	National Bank for Agriculture and Rural Development
NC	Non-compliant (grade)
RBI	Reserve Bank of India
RCAP	Regulatory Consistency Assessment Programme
RIDF	Rural Infrastructure Development Fund
SA-CCR	Standardised approach for counterparty credit risk
SIG	Supervision and Implementation Group

## Preface

The Basel Committee on Banking Supervision (Basel Committee) places a high priority on the implementation of regulatory standards underpinning the Basel III framework. The prudential benefits from adopting Basel standards can only fully accrue if these are implemented fully, consistently and in a timely manner by all member jurisdictions. The Committee established the Regulatory Consistency Assessment Programme (RCAP) to monitor, assess and evaluate its members' implementation of the Basel framework.

This report presents the findings of an RCAP Assessment Team on the domestic adoption of the Basel large exposures framework in India. The assessment focused on the completeness and consistency of the domestic regulations in force on 7 June 2019, as applied to commercial banks in India, with the Basel large exposures framework. Issues related to prudential outcomes, the resilience of the banking system or the supervisory effectiveness of the Indian authorities were not in the scope of this assessment. The assessment relied on regulations, other information and explanations provided by the Indian authorities, and it ultimately reflects the view of the Basel Committee.

The RCAP Assessment Team was led by Vasily Pozdyshev, Deputy Governor of the Central Bank of the Russian Federation. It comprised four technical experts, from Belgium, Brazil, Denmark and the Basel Committee Secretariat (see Annex 1). The main counterpart for the assessment was the Reserve Bank of India. The work was coordinated by the Basel Committee Secretariat with support from staff from the Central Bank of the Russian Federation.

The assessment began in early 2018 and comprised four phases: (i) self-assessment by the assessed jurisdiction's authorities; (ii) an assessment phase (June to December 2018), including an on-site assessment involving discussions with the Indian authorities, banks and rating agencies; and (iii) a review phase (January and February 2019), including a technical review of the Assessment Team's findings by a separate RCAP Review Team, the Committee's Supervision and Implementation Group, the RCAP Peer Review Board and the Basel Committee; (iv) a desk assessment phase of a draft regulation addressing a material and another potentially material finding (March to May 2019). More information on the RCAP assessment process is available on the Committee's website.<sup>1</sup>

The Assessment Team acknowledges the professional cooperation received from the Reserve Bank of India (RBI) throughout the assessment process. In particular, the team sincerely thanks the staff of the RBI for coordinating the exercise and the series of comprehensive briefings and clarifications received, as well as the representatives of Indian banks and rating agencies that provided information. The Assessment Team is hopeful that the RCAP assessment will contribute to the sound initiatives already undertaken by the Indian authorities and to further strengthening the prudential effectiveness of the large exposures framework in India.

<sup>1</sup> See [www.bis.org/bcbs/implementation.htm](http://www.bis.org/bcbs/implementation.htm).

## Executive summary

In India, the large exposures framework applies to all scheduled commercial banks apart from regional rural banks. The framework was implemented by way of a circular issued in December 2016, modified in June 2019, and became partially effective on 1 April 2019, since the obligation to assess connectedness based on economic interdependence and the inclusion of non-centrally cleared derivatives exposures in the calculation of the large exposure limits enter into force from 1 April 2020 as per the modified circular.

Overall, as of 7 June 2019, the large exposures regulations in India are assessed as Compliant with the Basel large exposures framework. This is highest possible grade. The components were all assessed as Compliant: scope and definition of the framework, minimum requirements and value of exposures.

In some other respects, the Indian regulations are stricter than the Basel large exposures framework. For example, banks' exposures to global systemically important banks are subject to stricter limits, in line with the letter and spirit of the Basel Guidelines, and the scope of application of the Indian standards is wider than just the internationally active banks covered by the Basel framework.

## Response from the Reserve Bank of India

The RBI appreciates the thorough and professional assessment of the implementation of guidelines on the Large Exposures Framework in India by the Assessment Team led by Mr Vasily Pozdyshev, Deputy Governor of the Central Bank of the Russian Federation. The exercise has been of immense help to RBI as we have gained from useful insights provided by the team. The RBI welcomes the opportunity given to respond to the findings on implementation of Large Exposures Framework in India.

The Assessment Team initially identified two findings on i) not incorporating economic interdependence between counterparties for aggregating exposures, and ii) non-mandatory nature of the Look-through Approach (LTA) under RBI guidelines, which the RBI addressed as described below.

Regarding economic interdependence criteria, the Assessment Team was of the view that economic interdependence criteria is a key component of the LEX framework and is required to assess contagion risk among larger counterparties which may also have some likelihood of being connected through economic interdependence. After discussions with the Assessment Team and internal data analysis, RBI decided to incorporate economic interdependence criteria for determining group of connected counterparties in all cases where the sum of all exposures to each such counterparty exceeds 5 per cent of the eligible capital base. In order to provide time to the banks to adjust to the new requirement, the introduction of economic interdependence criteria in definition of connected counterparties will be effective from April 1, 2020.

Regarding LTA, considering low materiality because of low exposure to structures such as mutual funds, our default approach was to aggregate exposures on an 'unknown client' and apply LEX limit on aggregate exposure to such unknown client. At the same time, banks had the option to look-through structures. After discussion with the Assessment Team, in order to safeguard against a scenario where combined exposure to underlying entities through structures and otherwise may become a material source of concentration risk, RBI decided to make the LTA as the default approach for computing exposures to counterparties through structures, thus bringing our guidelines in line with the BCBS LEX framework.

We take this opportunity to thank the Assessment Team for the learnings and fresh perspectives we have gained from our interactions.



# 1 Assessment context

## 1.1 Status of implementation of the large exposures framework

The Reserve Bank of India (RBI) is the monetary and banking authority of India. As the banking authority, it is responsible for supervision and control of the banking sector under the Indian Banking Regulation Act. The RBI implemented the large exposures framework in December 2016 by way of a circular modified in June 2019. Most of the requirements came into effect on 1 April 2019. The requirements apply to all scheduled commercial banks with the exception of regional rural banks.<sup>2</sup> This scope of application is consistent with the RBI's application of other Basel III requirements.

## 1.2 Regulatory system

The Indian Banking Regulation Act empowers the RBI to issue and amend banking regulations, as well as to issue banking licences and carry out supervisory inspections of any banking entity in India. The large exposures framework has been implemented in India by way of a circular, which is considered binding for the purpose of this assessment. More information is provided in Annex 2.

## 1.3 Structure of the banking sector

The Indian banking sector comprises both public sector and private banks, with public sector banks playing a significant role. Scheduled commercial banks dominate the banking system, with the balance comprising small regional rural banks, rural cooperative banks and urban cooperative banks. Although these latter entities hold a relatively small share of banking system assets, they play a key role in providing access to banking services for low- and middle-income households.

The RBI applies Basel III requirements, including the large exposures framework, to all scheduled commercial banks. Of around 100 banks operating in India, around 90 are subject to these requirements. Scheduled commercial banks have a range of business models, including universal banking in some cases.

In evaluating the materiality of its findings, the RCAP Assessment Team focused on 11 of the largest banks in India, which included the six that are internationally active. Together, these banks account for about 64% of the banking sector and all the assets of internationally active banks in India.

## 1.4 Scope of the assessment

The Assessment Team considered the large exposure limits applicable to scheduled commercial banks in India as of 7 June 2019. The assessment had two dimensions:

- a comparison of domestic regulations with the Basel large exposures framework to ascertain that all the required provisions have been adopted (*completeness* of the regulations); and
- whether there are any differences in substance between the domestic regulations and the Basel large exposures framework and, if so, their significance (*consistency* of the regulations).

In its assessment, the RCAP Assessment Team considered all binding documents that effectively implement the Basel large exposures framework in India. Annex 2 lists the Basel standards used as the

<sup>2</sup> A scheduled bank refers to a bank which is listed in the Second Schedule of the Reserve Bank of India Act, 1934. Banks not under this schedule are called non-scheduled banks. Scheduled banks are usually private, foreign and nationalised banks operating in India.

basis for the assessment. The assessment did not evaluate the resilience of the banking system in India or the supervisory effectiveness of the RBI.

As set out in the RCAP methodology, the Assessment Team evaluated the materiality and potential materiality of identified deviations between the Basel large exposures framework and the local regulations. The quantification was limited to a sample of banks. In addition, the Assessment Team reviewed the non-quantifiable aspects of identified deviations and applied expert judgment as to whether the domestic regulations meet the Basel framework in letter and in spirit. The materiality analysis is summarised in Annex 3, which also lists the sample of banks. Unless stated otherwise, all of the data are as of 31 March 2018.

In several areas, the Basel large exposures framework refers to other parts of the Basel risk-based capital framework. These regulations were reviewed by a separate RCAP-Capital assessment, published in 2015.<sup>3</sup> Where the previous RCAP assessment considered the Indian implementation of the rules to be compliant, the RCAP-LEX Assessment Team limited its enquiries to changes in the relevant regulations since 2015.

The Assessment Team noted that, in some areas, the assessed jurisdiction's rules go beyond the minimum Basel standards. Although these elements provide for a more rigorous implementation the Basel framework, they have not been taken into account for the assessment of compliance (listed in Annex 6).

The outcome of the assessment is summarised using a four-grade scale, both at the level of each of the three key components of the Basel large exposures framework and the overall assessment of compliance. The four grades are compliant, largely compliant, materially non-compliant and non-compliant.

## 2 Assessment findings

### 2.1 Assessment grades and summary of findings

Overall, the Assessment Team finds the implementation of the large exposures framework in India to be compliant with the Basel standards. This grade is based on the materiality assessment (summarised in Annex 3).

Assessment grades

Table 1

Component of the Basel large exposures framework	Grade
Overall grade	C
Scope and definitions	C
Minimum requirements and transitional arrangements	C
Value of exposures	C

Assessment scale: C (compliant), LC (largely compliant), MNC (materially non-compliant) and NC (non-compliant).

#### 2.1.1 Scope and definitions

The Assessment Team finds the scope and definitions to be compliant with the Basel standard.

<sup>3</sup> BCBS, *Regulatory Consistency Assessment Programme (RCAP) – Assessment of Basel III risk-based capital regulations – India*, June 2015, [www.bis.org/bcbs/publ/d320.htm](http://www.bis.org/bcbs/publ/d320.htm).

### 2.1.2 Minimum requirements and transitional arrangements

The RBI regulation on the minimum requirements and transitional arrangements is assessed to be compliant with the Basel standard.

### 2.1.3 Value of exposures

The RBI regulation on the value of exposures is assessed to be compliant with the Basel standard. Two findings were identified: (i) counterparty credit risk and the use of the “current exposure method” instead of the standardised approach to counterparty credit risk; and (ii) the identification of additional risks and the lack of commensurate specificity.

The Basel large exposures framework uses the Basel standardised approach to counterparty credit risk (SA-CCR) for calculating the exposure value for instruments that give rise to counterparty credit risk and are not securities financing transactions. Although the RBI has implemented regulations for the SA-CCR, they are not in force. Therefore, the exposure value for instruments that give rise to counterparty credit risk (apart from securities financing transactions) is determined according to the Committee’s previous standards for measuring counterparty credit risk, using the current exposure method. This is a non-material finding.

The RBI’s large exposures framework also makes no provision for the identification of additional risks, nor does it specify how banks should group these exposures. For example, in cases where the funds that the bank invests in are all managed by the same manager, the manager should then be regarded as a distinct counterparty and all the bank’s investments in the managed funds should be aggregated and subject to the large exposure limit. In the light of the data provided by the RBI, this issue is assessed as not material.

## 2.2 Detailed assessment findings

### 2.2.1 Scope and definitions

The component is assessed to be compliant with the Basel framework. No findings were identified.

### 2.2.2 Minimum requirements and transitional arrangements

The component is assessed to be compliant with the Basel framework. No findings were identified.

### 2.2.3 Value of exposures

The component is assessed to be compliant with the Basel framework. Two non-material findings were identified.

Section grade	Compliant
Basel paragraph number	33: counterparty credit risk
Reference in the domestic regulation	Paragraph 7.3 of the RBI Guidelines on the large exposures framework
Finding	<p>The Basel large exposures framework uses the Basel standardised approach to counterparty credit risk (SA-CCR) for calculating the exposure value for instruments that give rise to counterparty credit risk and are not securities financing transactions.</p> <p>The RBI implemented regulations for the SA-CCR but they are not in force. Therefore, the exposure value for instruments that give rise to counterparty credit risk (apart from securities financing transactions) is determined according to the Committee’s previous standards for measuring counterparty credit risk, ie the current exposure method.</p>

	Based on the data furnished by the RBI, five out of the 11 sample banks have no derivative exposures to any of their top 20 counterparties. For the remaining six banks, exposures at default for their derivative exposures to their top 20 counterparties, individually do not make up more than 1% of Tier 1 capital.
Materiality	Not material
Basel paragraph number	80–83: identification of additional risks
Reference in the domestic regulation	Paragraphs 9.1 and 9.2 of the RBI Guidelines on the large exposures framework
Finding	<p>The Basel large exposures framework requires banks to identify third parties that may constitute an additional risk factor inherent in the structure itself rather than in underlying assets. The standard details how banks must 1) connect their investments in structures with a common risk factor to form a group of connected counterparties, and 2) how banks may aggregate their investments in a set of structures associated with a third party that constitutes a common risk factor to other exposures (such as loans) that it has to that third party.</p> <p>The RBI's implementation of the large exposures framework requires banks to identify such third parties (eg originator, fund manager, liquidity provider and credit protection provider). In addition, in cases where there are multiple third parties considered to be potential drivers of additional risk, the bank must assign the exposures resulting from the investment in the structures to each of the third parties. However, the RBI's large exposures framework does not specify the identification of additional risks, nor provide instructions for banks to group these exposures. For instance, in cases where the funds that the bank invests in are all managed by the same manager, the manager should then be regarded as a distinct counterparty and all the bank's investments in the managed funds aggregated and subject to the large exposure limit. The RBI stated that it will manage this risk on a case-by-case basis under its Pillar 2 framework. If required, the RBI will specify a specific course of action, which may include either a reduction in exposures or the raising of additional capital.</p> <p>Based on the data provided by the RBI on the sample banks' exposures to collective investment undertakings, securitisation and other structures, these exposures are less than 10% of Tier 1 capital for nine of the 11 sample banks and comprise mainly mutual funds, venture capital funds and securitisations. It is noted that there are more than 40 asset management companies and 50 originators of underlying assets for securitisations, meaning that the probability that the funds are managed by the same fund manager/securitisation pools underwritten by the same originator is reduced.</p>
Materiality	Not material

## 2.3 Observations on the implementation of the large exposures framework in India

The following observations highlight certain special features of the regulatory implementation of the Basel large exposures framework in India. These are presented to provide additional context and information. Observations are considered compliant with the Basel standards and do not have a bearing on the assessment outcome.

### 2.3.1 Scope and definitions

Basel paragraph number	13, 61-62: exemption of state governments
Reference in the domestic regulation	3.1(a) of the RBI Guidelines on large exposures framework and 3.2
Observation	<p>The Basel large exposures framework exempts exposures to sovereigns and their central banks. This exemption also applies to public sector entities treated as sovereigns according to the risk-based capital framework.</p> <p>Under the RBI large exposures framework, the scope of the sovereign exemption includes exposures to the Government of India and state governments which are</p>

	<p>eligible for 0% risk weight under the RBI capital framework as well as exposures to RBI. This scope of exemption is used to apply the Basel paragraph 62 on entities connected with sovereigns.</p> <p>According to data provided by the RBI, three of the 11 sample banks have exposures to state governments below the 25% limit. Five banks have exposures to state governments in excess of 100% of Tier 1 capital and three between 50% and 100% of Tier 1 capital.</p> <p>Under the Indian prudential framework, state government exposures receive a 0% risk-weight under the capital adequacy rules, although guaranteed claims attract a 20% risk weight. The state governments have revenue-raising power and the RBI acts as a debt manager on their behalf, reducing the risk of default. The RBI also provides a short-term liquidity line to state governments.</p> <p>According to information provided by the RBI and the Assessment Team's discussions with banks, no state government has ever defaulted nor had its debt restructured.</p> <p>The RCAP-Capital assessment considered the 0% risk weight to be consistent with the Basel risk-based capital requirements, which allows claims on certain domestic public sector entities to be treated as claims on sovereigns.</p>
Basel paragraph number	13, 61: exemption of food credit borrowers
Reference in the domestic regulation	3.1(g) of the RBI Guidelines on large exposures framework
Observation	<p>The Basel large exposures framework exempts exposures to sovereigns and their central banks. This exemption also applies to public sector entities treated as sovereigns according to the risk-based capital framework.</p> <p>Under the Indian large exposure regulations, exposures to food credit borrowers are also exempted from requirements. "Food credit borrowers" are members of a government scheme to support minimum prices for farmers and to make food affordable for the poor. These entities are authorised by the RBI to borrow up to a certain limit. Food credit borrowers comprise state governments and the Food Corporation of India. Exposures to the latter are guaranteed by the Government of India.</p> <p>Based on data provided by the RBI, the sampled banks' exposures to food credit borrowers are not above the 25% Tier 1 limit. It should, however, be noted that exposures to this specific counterparty are above 10% of Tier 1 capital for three of the 11 sample banks.</p>
Basel paragraph number	13, 61: exemption of the Rural Infrastructure Development Fund
Reference in the domestic regulation	3.1(i) of the RBI Guidelines on large exposures framework
Observation	<p>The Basel large exposures framework exempts exposures to sovereigns and their central banks. This exemption also applies to public sector entities treated as sovereigns according to the risk-based capital framework.</p> <p>The Indian regulations exclude exposures to the Rural Infrastructure Development Fund (RIDF), which are all placed with the National Bank for Agriculture and Rural Development (NABARD).<sup>4</sup> The RIDF administers lending to rural communities linked to agriculture, social services and rural connectivity. The NABARD is owned by the Government of India and is in charge of administering the funds of the RIDF. The RIDF is formed by deposits from banks that do not meet the priority sector lending target of 40% on total outstanding loans.</p> <p>One of the sample banks has an exposure of 44% of its Tier 1 capital. Another seven banks have exposures greater than 10% of their Tier 1 capital.</p>
Basel paragraph number	26–28: economic interdependence
Reference in the domestic regulation	Paragraphs 6.2, 6.3, 6.7, 6.8, 6.9 and 6.10 and Appendices 2 and 3 of the RBI Guidelines on the large exposures framework

<sup>4</sup> NABARD fully controls the RIDF's lending; there are no exposures that are not placed with NABARD. See *NABARD Annual Report 2017–18*, Section 6.2, p 100.

Observation	<p>The 25% large exposure limit is applicable to a single counterparty or to a group of connected counterparties, which makes the definition of connected counterparties a crucial element of the framework. The Basel large exposure standard defines two criteria in order to identify connected counterparties: control relationship and economic interdependence.</p> <p>The RBI rule specifies that banks are required to assess connectedness based on economic interdependence from 1 April 2020, one year after the large exposures requirement enters into force.</p>
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### 2.3.2 Minimum requirements and transitional arrangements

Basel paragraph number	16: the large exposure limit
Reference in the domestic regulation	Paragraph 5.1 of the RBI Guidelines on large exposures framework
Observation	<p>The Basel large exposures framework limits the sum of all exposures of a bank to a single counterparty to 25% of Tier 1 capital.</p> <p>The Indian regulations establish the large exposure limit at 20% adding that, in exceptional cases, banks' boards may allow an additional 5% exposure of the bank's available eligible capital base. Banks must establish a board-approved policy in this regard.</p> <p>There is no regulatory guidance on the exceptional cases in which the limit can be raised to 25%, as such, this is subject to the full discretion of bank boards. The RBI explained to the Assessment Team that exceptional cases may include, among other things, adverse market movements, foreign exchange movements, or mergers of borrowers.</p>
Basel paragraph number	93: implementation date
Reference in the domestic regulation	Paragraph 11 of the RBI Guidelines on large exposures framework
Observation	<p>The Basel large exposures framework expects implementation in full by 1 January 2019. The Indian implementation will be delayed by three months to 1 April 2019 and the obligation to assess connectedness based on economic interdependence enters into force from 1 April 2020. Also, the calculation of value of exposures will include the exposure value related to non-centrally cleared derivatives from 1 April 2020.</p>

### 2.3.3 Value of exposures

Basel paragraph number	<p>33: exposure of banking book and trading book OTC derivatives</p> <p>47: calculation of exposure value for trading book positions</p>
Reference in the domestic regulation	Paragraph 11 of the RBI Guidelines on large exposures framework
Observation	<p>The RBI issued a new circular on the large exposures framework, in which it communicates that non-centrally cleared derivatives exposures will be outside the purview of exposure limits until 1 April, 2020. During the one-year period in which it will not be considered, banks are required to compute these exposures separately and report to the Department of Banking Regulation on a quarterly basis.</p> <p>The reason for that provision is the current absence of a regulatory basis that enable netting in India, which results in derivative transactions being measured on gross basis and, consequently, in a very punitive measurement of a bank's exposure to a counterparty. The RBI expects that the legal aspects related to netting will be solved within one year and sees this provision as a transition measure.</p> <p>Therefore, during the first year of application of the LEX framework in India, the calculation of value of exposures will not include the exposure value related to non-centrally cleared derivatives.</p>

## Annexes

### Annex 1: RCAP Assessment Team and Review Team

#### Assessment Team Leader

Mr Vasily Pozdyshev	Central Bank of the Russian Federation
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#### Assessment Team members

Ms Ana Paula Castro Carvalho	Central Bank of Brazil
Mr Ethan Goh (until 31 Dec 2018)	Basel Committee Secretariat
Mr Joachim Keller	National Bank of Belgium
Ms Anja Krarup Kuhlman (until 28 Jan 2019)	Financial Supervisory Authority, Denmark

#### Supporting members

Ms Elena Dzigoeva	Central Bank of the Russian Federation
Ms Louise Eggett (until 31 Dec 2018)	Basel Committee Secretariat
Mr Mark Pocock (from 31 Dec 2018)	Basel Committee Secretariat
Mr Olivier Prato	Basel Committee Secretariat

#### Review Team members

Mr Neil Esho	Basel Committee Secretariat
Ms Dana Green	Federal Reserve Bank of New York
Mr Faizel Jeena	South African Reserve Bank
Mr Qi Xiang	China Banking and Insurance Regulatory Commission

## Annex 2: List of Basel standards and implementing regulations issued by the Indian authorities

The following Basel standards were used as the basis of this RCAP assessment:

- *Supervisory framework for measuring and controlling large exposures*, September 2016
- *Frequently asked questions on the supervisory framework for measuring and controlling large exposures*, September 2016

Table A.1 lists the regulations issued by RBI to implement the large exposures framework in India. Previous RCAP assessments of India's implementation of the Basel standards considered the binding nature of regulatory documents in India.<sup>5</sup> This RCAP Assessment Team did not repeat this review, but instead relied on the findings of the previous assessments. Those assessments concluded that the types of instrument described in Table A.1 could be considered as binding on banks and supervisors for the purposes of an RCAP assessment.

Overview of relevant regulations on large exposures

Table A.1

Domestic regulations	Type, version and date
Reserve Bank of India Act and the Banking Regulation Act	Statutes, issued in 1934 and 1949 respectively, which empower the RBI to issue directions or guidelines to banks
Circular on large exposures framework	Circular issued on 1 December 2016, superseded by Circular issued on 3 June, 2019. <sup>6</sup>

Source: RBI.

<sup>5</sup> See Annex 7 of the RCAP assessment of the Basel III risk-based capital regulations in India, published in June 2015 and available at [www.bis.org/bcbs/publ/d320.htm](http://www.bis.org/bcbs/publ/d320.htm).

<sup>6</sup> See <https://rbidocs.rbi.org.in/rdocs/notification/PDFs/NOTI196099C6B756EDB4C2AAEEC2EE45BCCA122.PDF>.



## Annex 3: Materiality assessment

The outcome of the RCAP assessment is based on the materiality of the findings described in Section 2.2 and summarised in Table A.2. Assessment Teams evaluate the materiality of findings quantitatively where possible, or using expert judgment when the impact cannot be quantified.

The materiality assessment for quantifiable gaps is based on the cumulative impact of the identified deviations on the reported large exposures of banks in the RCAP sample. These banks are listed in Table A.3.

Number of deviations by component			Table A.2
Component	Not material	Potentially material	Material
Scope and definitions	0	0	0
Minimum requirements and transitional arrangements	0	0	0
Value of exposures	2	0	0

RCAP sample banks		Table A.3
Banking group	Share of banks' assets in the total assets of the Indian banking system (%, as of 31 March 2018)	
Bank of Baroda	4.68	
Bank of India	3.98	
Canara Bank	4.02	
Corporation Bank	1.41	
Indian Overseas Bank	1.51	
Punjab National Bank	5.13	
Union Bank of India	3.18	
State Bank of India	22.10	
Axis Bank Limited	4.81	
HDFC Bank Ltd	7.17	
ICICI Bank Limited	6.20	
Total	64.37	

Source: RBI. For this purpose, banking assets are based on the measure of total exposures used in the leverage ratio, which includes both on- and off-balance sheet exposures.

## Annex 4: Rectifications made by the RBI

List of rectifications by the RBI

Table A.4

Basel paragraph	Reference in Indian regulations	Description of the rectification
20-21	6.2 and 6.3	Economic interdependence criteria has been introduced, in addition to control criteria, to identify group of connected counterparties.
26-28	6.7-6.11 and Appendices 2 and 3	Detailed guidelines regarding economic interdependence and relationship between control and economic interdependence criteria have been issued.
33	Preamble and 7.3	As a transition measure, exposure value related to non-centrally cleared derivatives has been excluded for a period of one year until 31 March 2020 in the calculation of value of exposures.
62	3.2	Provision regarding exemption of entities connected with sovereigns has been added.
72-77	8.3-8.8 and Appendix 4	Look through approach has been made the default approach. In earlier guidelines, banks had option to look through or use alternative approach.

Source: RBI.

## Annex 5: Areas for further guidance from the Basel Committee

The Assessment Team identify the following issue for further guidance from the Basel Committee.

### Adjustments for less liquid positions

According to the Basel large exposures framework, the exposure value of straight debt instruments and equities in the trading book must be defined as the market value of the exposure. At the same time, under Basel II and Basel II.5, trading book positions are included in the capital charge calculation after adjustments for less liquid positions with the corresponding adjustments to regulatory capital. It is not clear in the Basel standards whether the market value is to be considered before or after any adjustments for less liquid positions.

## Annex 6: Areas where the Indian rules are stricter than the Basel standards

In some areas, the Indian authorities have adopted a stricter approach than the minimum standards prescribed by the Basel Committee. The stricter rules have not been taken into account as mitigants for the overall or component-level assessment of compliance.

- The Basel standard only applies to internationally active banks. However, the RBI applies the large exposures requirements to all banks apart from regional rural banks. These latter banks account for less than 3% of total loans outstanding for all commercial banks.
- Under the Basel framework, exposures that must be deducted from capital are not added to other exposures for that counterparty for the purpose of the large exposure limit. The RBI has not implemented this requirement, which increases the exposure size relative to the Basel standard, and so results in a stricter treatment, *ceteris paribus*.
- The Basel framework establishes tighter large exposure limits between global systemically important banks (G-SIBs) of 15% rather than 25% of Tier 1 capital. There are currently no G-SIB banks in India; however, in line with the letter and spirit of the Basel Guidelines, the Indian authorities impose large exposure limits of 15% between G-SIBs and, in line with the letter and spirit of paragraph 91 of the Basel LEX standard, large exposure limits of 20% between non-G-SIBs and G-SIBs.
- Covered bonds, under the Basel large exposures framework, may be assigned an exposure value of less than 100% of the nominal value where certain conditions are met. The Indian regulations do not permit the exposure value to be reduced in this way. However, the RBI notes that Indian banks do not currently invest in covered bonds.