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1. **Introduction**

1. The Central Bank of Nigeria (CBN), as part of its efforts to enhance the resilience of Deposit Money Banks (DMBs) and the Nigerian Banking System, has developed this Revised Guideline on Regulatory Capital, which sets out the criteria that banks’ capital instruments must meet to be eligible for regulatory purposes as per the Basel III standards.

2. This Guideline also sets out the supervisory requirements for banks operating in Nigeria in relation to: minimum regulatory capital, adjustments to the components of regulatory capital, transitional arrangements, disclosure requirements and the additional capital buffers above the minimum requirements.

3. The aim of this Guideline is to further strengthen the resilience of Nigerian banks by increasing the minimum requirement for high quality capital which can absorb losses on a going concern basis, and by requiring banks to build up additional capital buffers to cushion against future unexpected losses.

2. **Scope of Application and Reporting Requirements**

4. All banks are required by the CBN to maintain the minimum capital and capital buffer requirements as laid out in this Guideline at all times at both stand-alone (solo) and consolidated (group) levels. Please see Appendix 1 for further details.

5. All banks are required to submit electronic copy of their respective returns of capital adequacy position to the CBN using the prescribed reporting templates. The frequency of reporting shall be as follows:

   a) Monthly basis for the capital adequacy position on a stand-alone basis; and

   b) Quarterly basis for the capital adequacy position at the consolidated level (where applicable).

6. Notwithstanding the prescribed frequency of submission of returns of capital adequacy to the CBN specified in Paragraph 5 above, the CBN may at any time require a bank to calculate and report its capital adequacy ratios for any financial period or as at any specified date on a: (i) stand-alone basis, (ii) consolidated basis in respect of the bank and all its subsidiaries; and/or, (ii) consolidated basis in respect of the bank and one or more specified subsidiaries or associates.
2.1 Capital Adequacy at Stand-Alone Level

7. Capital adequacy position of a bank on a stand-alone (solo) level measures its capital strength and risk profile. It takes into consideration a bank’s global operations including its foreign subsidiaries and overseas branch operations, on a stand-alone basis.

8. In the assessment of capital adequacy at the stand-alone level, banks are required to incorporate all regulatory adjustments set out in this Guideline.

9. Investments in the capital instruments of subsidiaries, which are consolidated in the consolidated financial statements of the banking group, should be deducted from the corresponding capital instruments issued.

2.3 Capital Adequacy at Group or Consolidated Level

10. The capital adequacy at the consolidated (“Group”) level measures the capital strength and risk profile of a bank or HoldCo after consolidating the assets and liabilities of its subsidiaries, joint ventures, associates etc. excluding the entities or subsidiaries which are predominantly engaged in non-financial sector activities.

11. Investments in subsidiaries, joint ventures, associates etc shall be subject to the CBN’s Regulation 1, 2 and 3.

12. The adopted consolidation technique should be consistent with the requirements of International Financial Reporting Standard (IFRS) and should take into consideration the necessary adjustments specified in this Guideline.

13. For the purpose of this Guideline, financial sector activities shall mean activities undertaken by institutions in one or more of the following businesses or activities, whether by itself or through any of its subsidiaries: (i) banking, (ii) securities business, (iii) insurance business, (iv) financial leasing, (v) portfolio management, (vi) investment advisory services, (vii) custodial services, (viii) central clearing services, and (ix) activities ancillary to banking.

14. In computing capital adequacy ratio on a consolidated basis, a banking group or HoldCo group shall aggregate its consolidated group’s risk weighted assets for credit risk, market risk, and operational risk. The calculation of the risk weighted assets shall be as per the requirements of the CBN Guidance Notes on Credit, Market and Operational Risk.

1 There are two group structures under the focus of this Guidance Notes i.e. Banking Group and Holding Company Group (HoldCo Group)
15. All regulatory adjustments set out in this Guideline are required to be made to the consolidated CET1 capital of the banking group or HoldCo group.

16. Minority interest (i.e. non-controlling interest) and other capital issued out of consolidated subsidiaries held by third parties will be recognized in the consolidated regulatory capital of the group subject to certain conditions as stipulated in Paragraph 48 to 52 of this Guideline.

17. Where a reporting entity determines that consolidation of a subsidiary is not feasible, the entity shall seek the approval of the CBN to:

   a) In the case of a subsidiary engaged in financial sector activities, deduct such investments from capital; and
   b) In the case of a non-financial subsidiary, apply a risk weight of 1,250%

18. All banking and financial holding companies (HoldCos) groups shall comply with the capital adequacy requirements specified in this Guideline (at the consolidated level).

3. Minimum capital requirements and buffers

3.1 Components of capital

19. Total Regulatory Capital (TRC) is the sum of Common Equity Tier 1 (CET1), Additional Tier 1 Capital (AT1) and Tier 2 Capital (T2), net of regulatory adjustments.

20. Tier 1 capital is the sum of CET1 and AT1 capital, net of the regulatory adjustments applied to those categories.

21. CET1 and AT1 capital are going-concern capital\(^2\) while Tier 2 capital is gone-concern capital\(^3\).

22. A bank shall compute its regulatory capital adequacy ratios (CAR) as follows:

\[
\text{a) } \frac{\text{CET1 Capital}}{\text{Total Risk Weighted Assets (TRWA)}} \times 100
\]

\(^2\) This component is able to absorb losses without constituting an event of default on the holders of the instrument.

\(^3\) This component can absorb losses only when Tier 1 capital has been eroded and a bank is in liquidation.
b) Tier 1 Capital Ratio  \[= \frac{\text{Tier 1 Capital}}{\text{Total Risk Weighted Assets (TRWA)}} \times 100\]

c) Capital Adequacy Ratio (CAR)  \[= \frac{\text{Total Regulatory Capital (TRC)}}{\text{Total Risk Weighted Assets (TRWA)}} \times 100\]

Where Total Risk Weighted Assets (TRWA) is calculated as the sum of:

a) Credit Risk Weighted Assets (RWAs) as defined in the Guidance Notes on the Calculation of Capital Requirement for Credit Risk;

b) Market RWAs as defined in Guidance Note on the Calculation of Capital Requirement for Market Risk;

c) Operational RWAs as defined in Guidance Notes on the Calculation of Capital Requirement for Operational Risk.

23. The RWAs for market and operational risk shall be determined as **12.5 times** the sum of the estimated Pillar 1 capital charges as per the relevant Guidance Notes.

24. The non-distributable Regulatory Risk Reserve (RRR)\(^4\) should not be recognised as a component of the total qualifying regulatory capital. Any balances in the RRR may however be netted against the TRWA and such balances must be based on the last audited financial statement.

### 3.2 Limits and Minimum Requirements

25. A minimum Pillar 1 regulatory Capital Adequacy Ratio (CAR) of 15% will be applicable to all banks and banking groups with international authorisation and those that have been categorized by the CBN as being Domestic Systemically Important Banks (D-SIBs). A minimum CAR of 10% will be applicable to all other banks.

26. With respect to a holding company group, its minimum capital adequacy ratio shall not be less than the capital ratio requirement of any banking subsidiary within the group. In this regard, the reference subsidiary shall be that with the highest minimum capital requirement.

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\(^4\)This arises where the provision determined under the prudential guidelines is greater than IFRS 9 provisions. The current practice is to transfer the difference from the general reserve to a non-distributable regulatory risk reserve.
27. The CBN may require a bank to maintain a higher minimum level of capital than those stated in Paragraph 25 and Table 1 after taking into consideration the outcome of the supervisory review of its Internal Capital Adequacy Assessment Process (ICAAP) under Pillar 2. The aim will be to ensure that the level of a bank’s minimum capital requirement reflects its risk profile, business strategy and risk management capacity.

Table 1: Minimum Regulatory Capital Requirements

<table>
<thead>
<tr>
<th>Regulatory Capital Ratio</th>
<th>As a percentage of TRWA</th>
<th>National and Regional Banks</th>
<th>International Banks and D-SIBs</th>
</tr>
</thead>
<tbody>
<tr>
<td>CET1 Capital Ratio</td>
<td>7.0%</td>
<td>10.5%</td>
<td></td>
</tr>
<tr>
<td>Tier 1 Capital Ratio</td>
<td>7.5%</td>
<td>11.25%</td>
<td></td>
</tr>
<tr>
<td>Capital Adequacy Ratio</td>
<td>10.0%</td>
<td>15.0%</td>
<td></td>
</tr>
</tbody>
</table>

28. The minimum requirements set out in Table 1 do not take into consideration the additional capital buffers which the CBN may require banks in Nigeria to maintain from time to time depending on, amongst others, the prevailing macroeconomic conditions and the systemic importance of the individual banks.

29. The inclusion of eligible Tier 2 Capital would only be permitted subject to the minimum thresholds set out in Table 1 being met. In the absence of AT1 capital, the minimum Tier 1 capital ratio should be met from CET1 capital.

30. The minimum CAR for the institutions that have been designated as D-SIBs should be further enhanced with the Higher Loss Absorbency (HLA) requirement of 1.0% consisting wholly of CET1 capital.

31. In addition to the minimum CET 1 capital ratios specified in Table 1, banks are also required to maintain minimum capital conservation and countercyclical buffers specified Paragraph 80. This should be in form of CET1 capital.

4. Requirements for Inclusion in Regulatory Capital

4.1 Common Equity Tier 1

32. CET1 capital consists of the sum of the following elements:

a) Common shares issued by the bank that meet the criteria for classification as common shares for regulatory purposes;
b) Stock surplus (share premium) resulting from the issue of instruments included CET1;

c) Retained earnings (only audited components);

d) Small and Medium Enterprises Equity Investment scheme (SMEEIS) reserves and or any other scheme as may be stipulated from time to time by the CBN;

e) Statutory reserve;

f) Common shares issued by consolidated subsidiaries of the bank and held by third parties (i.e. minority interest) that meet the criteria for inclusion in CET1 capital. Please see Paragraph 49 to 53 for the relevant criteria;

g) Other reserves as may be determined by the CBN; and

33. For an instrument to be included as part of CET1 capital, it must meet all of the criteria set out below. The criteria must be met solely with common shares. In the rare cases where banks need to issue non-voting common shares as part of CET1, they must be identical to voting common shares of the issuing bank in all respects except the absence of voting rights:

a) Represents the most subordinated claim in liquidation of the bank;

b) Entitled to a claim on the residual assets that is proportional with its share of issued capital, after all senior claims have been repaid in liquidation\(^5\);

c) Principal is perpetual and never repaid outside of liquidation;

d) The bank does nothing to create an expectation at issuance that the instrument will be bought back, redeemed, or cancelled nor do the statutory or contractual terms provide any feature which might give rise to such an expectation;

e) Distributions are paid out of distributable items (retained earnings included). The level of distributions should not in any way be tied or linked to the amount paid in at issuance and should not be subject to a contractual cap;

f) There are no circumstances under which the distributions are obligatory and therefore non-payment is not a default event\(^6\);

\(^5\) That is, has an unlimited and variable claim, not a fixed or capped claim.

\(^6\) Amongst other things, this requirement prohibits features that require the bank to make payment in kind.

\(\text{g)}\) Distributions are paid only after all legal and contractual obligations have been met and payments on more senior capital instruments have been made;

\(\text{h)}\) It is the issued capital that takes the first and proportionately greatest share of any losses as they occur. Within the highest quality capital, each instrument absorbs losses on a going concern basis proportionately and pari passu with all the others;
i) The paid-in amount is recognised as equity capital (not as liability) for determining balance sheet insolvency;

j) The paid-in amount is classified as equity under IFRS;

k) It is directly issued and paid-in and the bank cannot directly or indirectly have funded the instrument or the purchase of the instrument;

l) The paid-in amount is neither secured nor covered by a guarantee of the issuer or related entity\(^7\) or subject to any other arrangement that legally or economically enhances the seniority of the claim;

m) It is only issued with the approval of the owners of the issuing bank, either given directly by the owners or, where permitted by applicable law, given by the Board of Directors or by other persons duly authorised by the owners;

n) It is clearly and separately disclosed on the bank’s balance sheet published in the bank’s annual report.

34. There is no limit on the inclusion of Tier 1 capital for the purpose of calculating total regulatory capital.

4.2 Additional Tier 1 capital

35. Additional Tier 1 capital (AT1) consists of the sum of the following elements:

   a) Instruments issued by the bank that meet the criteria for inclusion in AT1 capital and not included in CET1;

   b) Stock surplus (share premium) resulting from the issue of instruments included in AT1 capital;

   c) Instruments issued by consolidated subsidiaries of the bank and held by third parties that meet the criteria for inclusion in AT1 capital and are not included in CET1 capital. Please see Paragraph 48 to 52 for the relevant criteria;

36. The following criteria must be met or exceeded for an instrument issued by the bank to be included in AT1 capital.

   a) Issued and paid-in;

   b) 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 bank general creditors;

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\(^7\) A related entity can 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 banking group.
c) May be callable at the initiative of the issuer only after a minimum of five years (see Paragraph 38 below for further details);

d) The instrument cannot have a credit sensitive dividend feature. That is, a dividend or coupon that is reset periodically based in whole or in part on the bank’s credit rating;

e) Neither the bank nor a related party over which the bank exercises control or significant influence can have purchased the instrument, nor can the bank directly or indirectly have funded the purchase of the instrument;

f) The terms and conditions must have a provision that requires, at the option of the CBN, the instrument to either be written off or converted into common equity upon the occurrence of a trigger event (see Paragraphs 42 to 43 for further details);

g) Is perpetual i.e. there is no maturity date and there are no incentives to redeem;

h) Any repayment of principal (e.g. through repurchase or redemption) must be with the prior approval of the CBN and banks should not assume or create market expectations that the CBN will grant the approval;

i) It has dividend or coupon discretion (see Paragraph 39 below for further details);

j) Dividends or coupons must be paid out of same distributable items;

k) The instrument cannot contribute to liabilities exceeding assets for the purpose of insolvency testing;

l) Instruments classified as liabilities for accounting purposes must have principal loss absorption mechanism (see Paragraph 40 for further detail);

m) The aggregate amount to be written down or converted for all instruments classified as liabilities for accounting purposes 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;

n) Neither the bank nor a related party over which the bank exercises control or significant influence can have purchased the instrument, nor can the bank directly or indirectly fund the instrument or the purchase of the instrument;

o) The instrument cannot have any features that hinder recapitalisation, such as provisions that require the issuer to compensate investors if a new instrument is issued at a lower price during a specified time frame;

p) If the instrument is not issued out of an operating entity or the holding company in the consolidated group8, proceeds must be immediately available without

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8 For example, a special purpose vehicle (SPV)
limitation to an operating entity\(^9\) or the holding company in the consolidated group in a form which meets or exceeds all of the other criteria for inclusion in AT1 capital.

q) Subordinated to depositors, general creditors, and subordinated debt of the bank. In the case of an issue by a holding company, the instrument must be subordinated to all general creditors;

37. Stock surplus (share premium) that is not eligible for inclusion in CET1, will only be permitted to be included in AT1 capital if the shares giving rise to the stock surplus are permitted to be included in AT1 capital.

38. Where an instrument is callable at the initiative of the issuer:

a) A bank must receive prior written approval from the CBN before the call option can be exercised; and

b) A bank must not do anything which creates an expectation that the call option will be exercised; and

c) Banks must not exercise a call unless: (i) they replace the called instrument with capital of the same or better quality and the replacement\(^{10}\) of this capital is done at conditions which are sustainable for the income capacity of the bank; or (ii) it is able to demonstrates that its capital position will be well above the CBN’s prescribed minimum capital requirement after the call option is exercised.

39. Regarding the discretions on dividends or coupon:

a) The bank must have full discretion at all times to cancel distributions or payments;

b) Cancellation of discretionary payments must not constitute a default event;

c) Banks must have full access to cancel payments to meet obligations as they fall due;

d) Cancellation of distributions or payments must not impose restrictions on the bank except in relation to distributions to common stockholders.

40. The principal loss absorption mechanism must operate through either:

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\(^9\) An operating entity is an entity set up to conduct business with clients with the intention of earning a profit in its own right.

\(^{10}\) Replacement issue can be concurrent with but not after the instrument is called.
a) Conversion to common shares at an objective pre-specified trigger point of at least 7.25% CET1 (7.0% + 25% of 1.0%) for banks with National Authorization Licence, 10.75% CET1 (10.5% + 25% of 1.0%) for banks with International Authorization Licence and 11.00% CET1 (10.5% + 25% of 1.0% + 1.0%) for D-SIBs; or

b) A write-down mechanism which allocates losses to the instrument at a pre-specified trigger points specified in (a) above. The write-down will 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 or dividend payments on the instrument.

41. Any compensation paid to instrument holders as a result of a write-off must be paid immediately in the form of common stock of either the issuing bank or the parent company of the consolidated group (including any successor in resolution) and must be paid prior to any public sector injection of capital.

42. The issuing bank must maintain at all times all prior authorization necessary to immediately issue the relevant number of shares specified in the instrument’s terms and conditions should the trigger event occur. The trigger event is the earlier of:

a) a decision that a write-off, without which the firm would become non-viable, is necessary, as determined by the CBN; 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 CBN.

43. Where an issuing bank is part of a wider banking group and the issuing bank wishes the instrument to be included in the consolidated group’s capital in addition to its solo capital, the terms and conditions must specify an additional trigger event. This additional trigger event is the earlier of:

a) a decision that a write-off, without which the firm would become non-viable, is necessary, as determined by the CBN; or

b) the decision to make a public sector injection of capital, or equivalent support, in the jurisdiction of the consolidated supervisor, without which the firm receiving the support would have become non-viable, as determined by the CBN in consultation with the host regulator in the relevant jurisdiction.
4.3 **Tier 2 capital**

44. Tier 2 capital consists of the sum of the following elements:

a) Instruments issued by the bank that meet the criteria for inclusion in Tier 2 capital (and are not included in Tier 1 capital);

b) Stock surplus (share premium) resulting from the issue of instruments included in Tier 2 capital;

c) Instruments issued by consolidated subsidiaries of the bank and held by third parties that meet the criteria for inclusion in Tier 2 capital and are not included in Tier 1 capital. Please see Paragraph 48 to 52 for the relevant criteria;

d) Regulatory adjustments applied in the calculation of Tier 2 capital.

45. In addition to the criteria set out in Paragraph 36 [(a) to (f)], the following criteria must also be met or exceeded for an instrument to be included in Tier 2 capital.

a) Minimum original maturity of at least five years (recognition in regulatory capital in the remaining five years before maturity will be amortised on a straight-line basis by 20% per annum and there should be no step-ups or incentives to redeem by the holder);

b) Subordinated to depositors and general creditors of the bank;

c) The investor must have no rights to accelerate the repayment of future scheduled payments (coupon or principal), except in bankruptcy and liquidation;

d) If the instrument is not issued out of an operating entity or the holding company in the consolidated group e.g. a Special Purpose Entity (SPE), proceeds must be immediately available without limitation to a single operating entity or the holding company in the consolidated group in a form which meets or exceeds all of the other criteria for inclusion in Tier 2 capital.

46. Stock surplus (share premium) that is not eligible for inclusion in Tier 1 will only be permitted to be included in Tier 2 capital if the shares giving rise to the stock surplus are permitted to be included in Tier 2 capital.

47. Other comprehensive income items other than fixed asset revaluation reserves that are created by the adoption of IFRS may be accepted as part of the Tier 2 capital subject to limitations that may be specified by the CBN from time to time.

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11 An operating entity is an entity set up to conduct business with clients with the intention of earning a profit in its own right
4.4 Minority interest and other capital issued out of consolidated subsidiaries

48. Minority interest (non-controlling interest) arising from common share equity capital issued by a fully consolidated subsidiary of a bank or a HoldCo may receive recognition in CET1 capital only if:

a) the instrument giving rise to the minority interest would, if issued by the bank/HoldCo, meet all the criteria for classification as CET1 for regulatory capital purposes as stipulated in this Guideline; and

b) the subsidiary that issued the instrument is itself a bank in the case of a banking group or a non-bank financial entity for a HoldCo group.

49. Minority interest in a subsidiary that is a bank is strictly excluded from the parent bank’s common equity if the parent bank or affiliate has entered into any arrangements to fund directly or indirectly minority investment in the subsidiary whether through an SPE or through another vehicle or arrangement.

50. The amount of minority interest meeting the criteria set out in Paragraph 48 that will be recognized in consolidated CET1 will be calculated as follows:

a) Total minority interest meeting the two criteria set out in Paragraph 48 above minus the amount of the surplus CET1 of the subsidiary attributable to the minority shareholders.

b) Surplus CET1 of the subsidiary is calculated as the CET1 of the subsidiary minus the lower of: (i) the minimum CET1 requirement of the subsidiary plus the capital conservation buffer or (ii) the portion of the consolidated minimum CET1 requirement plus the capital conservation buffer that relates to the subsidiary.

c) The amount of the surplus CET1 that is attributable to the minority shareholders is calculated by multiplying the surplus CET1 by the percentage of CET1 that is held by minority shareholders.

51. Tier 1 capital instruments issued by a fully consolidated subsidiary of the bank, whether wholly or partly owned, to third party investors (including amounts under Paragraph 50 above) may receive recognition in Tier 1 capital only if the instruments would, if issued by the bank, meet all of the specified criteria for classification as Tier 1 capital. The amount of this capital that will be recognised in Tier 1 will be calculated as follows:

a) Total Tier 1 capital of the subsidiary issued to third parties minus the amount of the surplus Tier 1 of the subsidiary attributable to the third-party investors.
b) Surplus Tier 1 of the subsidiary is calculated as the Tier 1 of the subsidiary minus the lower of: (i) the minimum Tier 1 requirement of the subsidiary plus the capital conservation buffer or (ii) the portion of the consolidated minimum Tier 1 requirement plus the capital conservation buffer that relates to the subsidiary.

c) The amount of the surplus Tier 1 that is attributable to the third-party investors is calculated by multiplying the surplus Tier 1 by the percentage of Tier 1 that is held by third party investors.

d) The amount of this Tier 1 capital that will be recognised in AT1 will exclude amounts recognised in CET1 under Paragraph 50 above

52. Total capital instruments (i.e. Tier 1 and Tier 2 capital instruments) issued by a fully consolidated subsidiary of the bank, whether wholly or partly owned, to third party investors (including amounts under Paragraph 50 to Paragraph 51 above) may receive recognition in Total Capital only if the instruments would, if issued by the bank, meet all of the criteria for classification as Tier 1 or Tier 2 capital. The amount of this capital that will be recognised in consolidated Total Capital will be calculated as follows:

a) 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.

b) Surplus Total Capital of the subsidiary is calculated as the Total Capital of the subsidiary minus the lower of: (i) the minimum Total Capital requirement of the subsidiary plus the capital conservation buffer and (ii) the portion of the consolidated minimum Total Capital requirement plus the capital conservation buffer that relates to the subsidiary.

c) 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.

d) The amount of Total Capital that will be recognised in Tier 2 will exclude amounts recognised in CET1 under Paragraph 50 above and amounts recognised in Additional Tier 1 under Paragraph 51 above.

4.5 Regulatory Adjustments

53. This section sets out deductions to be applied to regulatory capital. In most cases, these adjustments are applied in the calculation of CET1 capital.

54. All items that are deducted from capital should be excluded from total assets in calculating the CAR.
55. If a bank is required to make a deduction from Tier 2 capital and it does not have sufficient capital to make that deduction, the shortfall will be deducted from Tier 1 capital.

56. In case of any shortfall in the regulatory capital requirements in any subsidiary entity, the shortfall should be fully deducted from the Common Equity Tier 1 (CET1) capital.

4.5.1 Goodwill and other intangibles

57. Goodwill and all other intangibles must be deducted in the calculation of CET1. This includes any goodwill included in the valuation of significant investments in the capital of other financial entities that are outside the scope of regulatory consolidation.

58. The full amount is to be deducted net of any associated Deferred Tax Liability (DTL) which would be extinguished if the intangible assets become impaired or derecognised under the IFRS.

4.5.2 Deferred Tax Assets (DTA)

59. Deferred Tax Assets (DTAs) are to be deducted in the calculation of CET1.

4.5.3 Cash Flow Hedge Reserve

60. The amount of the cash flow hedge reserve that relates to the hedging of items that are not fair valued on the balance sheet should be derecognised in the calculation of CET1. This means that positive amounts should be deducted, and negative amounts should be added back.

4.5.4 Gain on Sale Related to Securitisation Transactions

61. Banks must deduct from CET1 any increase in equity capital resulting from a securitisation transaction, such as that associated with expected future margin income resulting in a gain on sale that is recognised in regulatory capital.

4.5.5 Defined Benefit Pension Fund Assets and Liabilities

62. Defined Benefit (DB) pension fund liabilities, as included on the balance sheet, must be fully recognised in the calculation of CET1. That is, CET1 cannot be increased through derecognising these liabilities.
63. For each DB pension fund that is an asset on the balance sheet, the net asset on
the balance sheet in respect of the plan or fund should be deducted in the
calculation of CET1 net of any associated deferred tax liability which would be
extinguished if the asset should become impaired or derecognised under IFRS.

4.5.6 Investment in Own Shares (Treasury shares) and Own other Capital

64. All of a bank’s investments in its own common shares, whether held directly or
indirectly, should be deducted in the calculation of CET1. In addition, any own stock
which the bank could be contractually obliged to purchase should be deducted in
the calculation of CET1.\(^{12}\)

65. Banks must also deduct investments in their own AT1 in the calculation of their
AT1 capital and must deduct investments in their own Tier 2 in the calculation of
their Tier 2 capital.

4.5.7 Reciprocal cross holdings in the common shares of banking, financial and
insurance entities

66. Reciprocal cross-holdings of capital (e.g. Bank A holds capital of Bank B and Bank
B in return holds capital of Bank A) should be deducted in full.

67. Banks must apply a “corresponding deduction approach” to such investments in
the capital of other banks and financial entities. This means the deduction should
be applied to the same component of capital for which the capital would qualify if it
was issued by the bank itself.

4.5.8 Investments in the capital of banking and financial entities outside the
scope of regulatory consolidation where the bank does not own more than
10% of the issued common shares of the entity

68. A bank's aggregate investment in all types of eligible capital instruments, issued
by banks and financial institutions (except its financial subsidiaries) should not
exceed 10% of the investing bank’s capital funds (Tier 1 plus Tier 2 before
regulatory adjustments). Any investment in excess of this limit shall be assigned a
risk weight of 1250%.

69. A bank's investment in the following instruments issued by financial institutions will
be included in the prudential limit of 10%, referred to in Paragraph 68 above:

   a) Equity shares;

\(^{12}\) The treatment described will apply irrespective of the location of the exposure in the banking book or
the trading book.
b) Hybrid debt capital instruments

c) Subordinated debt instruments; and

d) Any other instrument approved by the CBN having the nature of capital.

70. Financial institutions whose instruments shall qualify for capital purposes shall be as defined in the Regulation on the Scope of Banking Activities and Ancillary Matters No. 3 and any other extant regulations issued by the CBN.

71. Investment in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation and where the bank does not own more than 10% of the issued common share capital of the entity should be deducted from capital. For the purpose of this regulatory adjustment:

a) Investments include direct, indirect and synthetic holdings of capital instruments or other liabilities;

b) Holdings in both the banking book and trading book are to be included;

c) For capital instruments, it is the net long position that is to be included (i.e. the gross long position net of short positions in the same underlying exposure where the maturity of the short position either matches the maturity of the long position or has a residual maturity of at least one year);

d) If the capital instrument of the entity in which the bank has invested does not meet the criteria for CET1, AT1, or Tier 2 capital of the bank, the capital is to be considered common shares for the purposes of this regulatory adjustment;

e) Banks may with prior written approval from the CBN exclude temporarily certain investments where these have been made in the context of resolving a distressed institution.

72. If a bank is required to 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 will be deducted from the next higher tier of capital.

73. Amounts that are not deducted will continue to be risk weighted as per the relevant Pillar 1 RWA rules.

4.5.9 Shortfall in impairment

74. Any shortfall in specific and collective impairment is to be deducted from CET1 capital.

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13 Indirect holdings are exposures or parts of exposures that, if a direct holding loses its value, will result in a loss to the bank substantially equivalent to the loss in value of the direct holding.
4.5.10 Significant Investment in the Capital of Banking, Financial and Insurance Entities that are Outside the Scope of Regulatory Consolidation

75. The regulatory adjustment described in this section applies to investments in the capital of banking, financial and insurance entities that are outside the scope of regulatory consolidation where the bank owns more than 10% of the issued common share capital of the issuing entity or where the entity is an affiliate of the bank. In addition:
   a) Investments include direct, indirect, and synthetic holdings of capital instruments;
   b) Holdings in both the banking book and trading book are to be included;
   c) If the capital instrument of the entity in which the bank has invested does not meet the criteria for CET1, AT1, or Tier 2 capital of the bank, the capital is to be considered common shares for the purposes of this regulatory adjustment.

76. All investments in capital instruments included above that are not common shares must be fully deducted following a corresponding deduction approach. This means the deduction should be applied to the same tier of capital for which the capital would qualify if it was issued by the bank itself.

5. Transitional Arrangements for ECL Accounting

77. The transitional arrangement for Expected Credit Loss (ECL) accounting under IFRS 9 should take into consideration the CBN prescribed transitional approach. The transitional period commenced from 1 January 2018 which is the date upon which banks in Nigeria were required to fully adopt IFRS 9.

78. During the transitional period, the transitional adjustment amount should be partially included in CET1. The transitional adjustment amount included in CET1 capital each year during the transition period must be taken through to other measures of capital as appropriate, and to the calculation of the leverage ratio and of large exposure limits.

6. Buffers Above the Regulatory Minimum

80. All banks shall be required to hold and maintain capital buffers above the regulatory minimum, as specified by the CBN from time to time. The capital buffers should be in the form of CET1 and should be above the minimum CET1, Tier 1 and Total Capital Adequacy levels as defined in this Guideline. The capital buffers shall comprise the sum of the following:

14 Transitional Arrangements Treatment of IFRS 9 Expected Credit Loss for Regulatory Purposes by Banks in Nigeria, October 18, 2018, BSD/DIR/GEN/LAB/11/027
a) a Capital Conservation Buffer (CCB1) of 1.0% of TRWA; and

b) a Countercyclical Capital Buffer (CCB2), which will be determined by the CBN from time to time taking into consideration the prevailing macroeconomic conditions and developments within the financial sector amongst other factors.

6.1 Capital Conservation Buffer

81. The capital conservation buffer (CCB1) is designed to ensure that banks build up capital buffers during business as usual time which can be used to absorb losses during periods of crisis.

82. All Nigerian banks are therefore required to maintain a CCB1 of 1.0% of TRWA in the form of CET1 during business as usual periods to withstand future periods of stress.

83. Where buffers have been drawn down, banks are required to restrict discretionary capital distributions, including dividend payments, share buybacks, and employee bonuses\textsuperscript{15}. Discretionary distributions, for the purposes of this Guideline, shall also include payments in respect of intra-group transfer pricing and technical service fees to foreign group members and/or parents.

84. Employees in Paragraph 86 refers to:

(i) individuals whose professional activities have a material impact on the bank’s risk profile, which include senior management, material risk-takers and staff performing important risk management and control functions; and

(ii) groups of employees who may together take material risks, even if no individual employee is likely to expose the bank to material risk (e.g. loan officers who, as a group, originate loans that account for a material amount of the organisation’s credit risk).

85. Banks have the option of raising new capital from the capital market as an alternative to conserving internally generated capital. The approach to be taken by banks shall be subject to prior approval from the CBN.

6.2 Countercyclical Buffer

86. In addition to CCB1, all banks in Nigeria will be required to maintain a Countercyclical Capital Buffer (CCB2)\textsuperscript{16} where the CBN determines that there is a build-up of credit risk which could lead to system-wide stress. The CCB2 shall

\textsuperscript{15} The objective of countercyclical capital buffer is to support the broader macro-prudential goal and financial system stability
range from 0% to 2.5% of TRWA and shall be determined by the CBN from time to time taking into consideration, amongst others, the prevailing economic and industry circumstances.

87. The CCB2 is to be met with CET1 capital and thus the restrictions on discretionary capital distribution would also take into consideration banks’ levels of CCB2.

88. The CBN shall apply its macro prudential tools and supervisory judgement in determining the level of CCB2 to be maintained by Nigerian banks. The supervisory judgement shall be informed by, amongst others, the assessment of developments in the macroeconomic and financial conditions including the underlying drivers.

89. The CBN shall announce the required CCB2 twelve (12) months in advance, during which time banks will be expected to take measures aimed at building up their capital buffers to the required level. Where there is an imminent crisis, the CBN may require banks to build up a CCB2 at a much shorter notice.

90. Banks shall be required to maintain, if necessary, CCB2 for a minimum period to be determined by the CBN after the expectation for system wide risk has been alleviated.

91. **The CCB2 buffer for banks with international authorization will be a weighted average of the buffers deployed across all the jurisdictions to which it has credit exposures.**

92. Where in place, banks must calculate and publicly disclose their CCB2 requirements with at least the same frequency as their minimum capital requirements. The buffer should be based on the most current jurisdictional countercyclical buffers.

93. Banks must also disclose the geographic breakdown of their exposures used in the calculation of the buffer requirement.

### 6.3 Higher Loss Absorbency for D-SIBs

94. The CBN’s Framework for The Regulation and Supervision of Domestic Systemically Important Banks (SIBs) in Nigeria issued on September 5, 2014, requires D-SIBs in Nigeria to set aside Higher Loss Absorbency (HLA) or additional capital surcharge of 1.0% to their respective minimum required CAR. The HLA should be fully met with CET1 capital.
The aim of HLA requirement is to reduce the probability of failure of D-SIBs given the relatively higher impact that their failure is expected to have on the domestic financial system and real economy.

6.4 Minimum Capital Adequacy and Buffer Levels

The following table sets out the minimum levels of capital adequacy and capital buffers that are applicable to banks depending on the nature of their authorization and their systemic importance to the Nigerian economy.

Table 2: Minimum Capital Requirements and Buffer Levels

<table>
<thead>
<tr>
<th>Capital Elements as % of TRWA</th>
<th>National Banks</th>
<th>International Banks</th>
<th>D-SIBs</th>
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</thead>
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<td>11.25</td>
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<td>15.0</td>
</tr>
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<td>1.0</td>
<td>1.0</td>
</tr>
<tr>
<td>CCB2</td>
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<tr>
<td>HLA</td>
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<td>Not Applicable</td>
<td>1.0</td>
</tr>
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7. Determination of Maximum Distribution Payment in Nigeria

7.1 Scope of Distribution

Distribution payment for the purpose of this Guideline shall refer to:

a) payment of dividends/coupon in respect of CET1 and AT1 capital;
b) payment for purchase of the bank’s own shares, subject to the existing regulation;
c) discretionary bonus payment to the directors and employees of the bank as defined in Paragraph 87;
d) technical service fees, management fees or other agreed or discretionary payments to a group entity or group member/parent; and
e) any other payment that is in substance a distribution of the bank’s CET1 capital

7.2 Conditions for Payment of Bonuses

Bonus payment to directors and employees shall only be made in respect of a financial year if the following conditions are jointly met. Specifically, no bonus shall be paid where:
(i) National bank - Composite Risk Rating (CRR) is Above Average or High, CET 1 is less than 8% (CET 1 of 7% + CCB1%) and has not satisfied the minimum leverage ratio requirement of 4%;

(ii) International authorization - Composite Risk Rating (CRR) is Above Average or High, CET 1 is less than 11.5% (CET 1 of 10.5% + CCB1%) and has not satisfied the minimum leverage ratio requirement of 4%; and

(iii) D-SIBs - Composite Risk Rating (CRR) is Above Average or High, CET 1 is less than 12.5% (CET 1 of 10.5% + CCB1% + HLA1%) and has not satisfied the minimum leverage ratio requirement of 5%.

99. For failure to meet their leverage ratio buffer requirement. The Table below sets out the criteria that has to be met by each class of banks before bonus payments can be made to directors and employees.

Table 3: Criteria for payment of bonus to directors and employees

<table>
<thead>
<tr>
<th>Criteria</th>
<th>Banks with National Authorization</th>
<th>Bank with International Authorization</th>
<th>D-SIBs</th>
</tr>
</thead>
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<td>Greater than 11.5% of TRWA</td>
<td>Greater than 12.5% of TRWA</td>
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<tr>
<td>Composite Risk Rating (CRR)</td>
<td>Low or Moderate</td>
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100. Any bonuses not paid as a result of failure to meet the criteria set out in Table 3 above shall be forfeited and shall not be paid in the subsequent years.

7.3 Conditions for Payment of Discretionary Obligations

101. A bank should be mindful of its capital adequacy and liquidity positions, amongst others, in its decision to fulfil its discretionary obligations18 to a group entity, parent or member of its group.

102. Where payments in respect of technical service fees, management fees or other agreed or discretionary payments to a group entity or group member/parent have been made, details of such payments shall be provided to the CBN not later than three (3) months after payment.

7.4 Conditions for Payment of dividends in respect of CET1

103. Payments of dividends shall be subject to the provisions of the Banks and Other Financial Institutions Act (BOFIA).

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17 This consists of the sum of the minimum CET 1 (as per Table 1), CCB 1 and HLA (where applicable).
18 e.g., discretionary technical service fees, management fees or other discretionary payments.
104. The maximum allowable dividend shall be determined taking into consideration the bank’s: (i) level of CET 1 capital, (ii) the level of non-performing loans (NPLs), and (iii) Composite Risk Rating (CRR) at the point in time. The bank’s maximum dividend for a given financial year shall therefore be restricted to the applicable pay-out ratio contained in Appendix 2.

8. Disclosure requirements

105. To help improve transparency of regulatory capital and enhance market discipline, banks are required to publicly disclose the following as part of their Pillar 3 disclosures:

a) A full reconciliation of all regulatory capital elements back to the balance sheet in the audited financial statements;

b) A description of all limits and minima, identifying the positive and negative elements of capital to which the limits and minima apply;

c) A description of the main features of capital instruments issued;

d) Full terms and conditions of all instruments included in regulatory capital;

e) Where applicable, counter cyclical buffer requirements;

f) Where applicable, geographic breakdown of exposures used in the calculation of the counter cyclical buffer requirement.
9. Appendix 1: Requirement at Solo and Consolidated Level

Below is an illustration of compliance requirement at solo and consolidated level.


Requirements:

a) **Financial Holco**: Consolidated (Group) CAR computation required

b) **Banking Subsidiary 1**: Both solo (stand-alone) and consolidated (group) CAR computation required

c) **Banking Subsidiary 2**: Both solo and consolidated CAR computation required

d) **Non-Bank Subsidiary 3**: No CAR computation required by CBN

e) **Subs A, B, C and D**: No CAR computation required by CBN

**Note**: The Financial Holco, Banking Subsidiary 1 and Banking Subsidiary 2 are Nigerian entities.
10. Appendix 2: Maximum Dividend Pay-out Ratio

1. Dividends for the purposes of this Guideline shall be the summation of dividends in respect of CET1 and AT1 capital.

2. Regardless of the type of authorization and the level of CET1 ratio, no dividend shall be paid where:

   a) The non-performing loans (NPL) ratio is greater than 10%, or,
   b) The Composite Risk Rating (CRR) is High, or
   c) The leverage ratio is below the minimum threshold

3. In all the other cases (scenarios), the maximum dividend pay-out ratio shall be as follows:

   Determination of Maximum Payout Ratio Using CET1, CCB1, CCB2 and HLA

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<tr>
<th>National Banks</th>
<th>CET1 Scenario 1</th>
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<tr>
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<td>NPL &gt; 8% &amp; NPL≤ 10%</td>
<td>NPL &gt; 8% &amp; NPL≤ 10%</td>
<td>NPL &gt; 8% &amp; NPL≤ 10%</td>
</tr>
<tr>
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DSIBs CET1 Scenario 3

<table>
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<tr>
<th>CRR</th>
<th>High NPL &gt; 5% &amp; NPL≤ 8%</th>
<th>Above Average NPL &gt; 5% &amp; NPL≤ 8%</th>
<th>Moderate NPL &gt; 5% &amp; NPL≤ 8%</th>
<th>Low NPL &gt; 5% &amp; NPL≤ 8%</th>
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</thead>
<tbody>
<tr>
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**Maximum Pay-Out Ratio**

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<tr>
<th>CRR</th>
<th>High NPL &lt; 5%</th>
<th>Above Average NPL &lt; 5%</th>
<th>Moderate NPL &lt; 5%</th>
<th>Low NPL &lt; 5%</th>
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<tbody>
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<tr>
<td>&gt; 12.5</td>
<td>0%</td>
<td>25%</td>
<td>75%</td>
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</tbody>
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**NB:** CET1 is computed as the summation of actual level of CET1 plus CCB1 of 1% and HLA of 1%.
HLA only applies to DSIBs

**Computation of Maximum Distributable Profit**

<table>
<thead>
<tr>
<th>Computation</th>
<th>Value</th>
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<tbody>
<tr>
<td>Current Year Profit (after tax)</td>
<td>a XXX</td>
</tr>
<tr>
<td>Less: Statutory Reserves Adjustment</td>
<td>b (xxx)</td>
</tr>
<tr>
<td>Less: Regulatory Risk Reserve adjustment**</td>
<td>c (xxx)</td>
</tr>
<tr>
<td>Adjusted Profit</td>
<td>d=(a-b-c,0) xxx</td>
</tr>
<tr>
<td>Maximum Dividend Pay-Out Ratio (from the Table above)</td>
<td>e xx%</td>
</tr>
<tr>
<td>Maximum Distributable Profit</td>
<td>f= (d) x (e) xxx</td>
</tr>
</tbody>
</table>

**This precludes transfers or writebacks from Regulatory Risk Reserve**