Capital adequacy guideline

Article 1: Definition of capital adequacy ratio

Capital adequacy ratio is the result of dividing base capital (as defined in base capital guideline) by total risk weighted assets (as defined in article 5 of this guideline).

Article 2: Classification of risks based on various countries

According to this guideline, various countries of the world are categorized in two groups based on their sovereign risk;

- Group A: including OECD countries, countries which have received loans from IMF under the contract made according to its general arrangements, and countries which have not extended their foreign exchange debts in the last five years.
- Group B: other than group A countries

Banks and credit institutions categorized in group A include those registered in the countries of group A as well as their branches whereas those registered in countries of group B together with their branches are categorized as group B banks and credit institutions.

Article 3: Minimum capital adequacy ratio

The minimum capital adequacy ratio for all banks and credit institutions (both state owned and non-governmental) is set at 8%. In cases required by international standards or the necessity to maintain banking health, the central bank of Iran can set higher ratios for some banks and credit institutions.

Article 4: Claims

In this guideline, claims include net granted facilities (after deduction of future profits, Mozarabah receivables, joint account for Musharaka); Bank deposit in other banks and credit institutions; inter-bank facilities; facilities in foreign currencies; facilities through foreign currency reserve account; long and short term financing using foreign resources (Usance, finance, refinance,etc.); and the similar cases.

Article 5: Risk weights

All assets belonging to banks and credit institutions including on balance sheet and off balance sheet items should be weighted in accordance with the related risk and as defined in this guideline.

As proportionate to their credit risk, risk weights for various types of assets are set as 0, 20, 50, and 100 percent; therefore, various assets of banks and credit institutions are weighted as described below;

5-1 On balance sheet items

5-1-1 assets with 0% risk weight

- Cash (account of the fund, notes, foreign currencies, gold and silver)
- Claims on the central bank of Iran (including legal reserve, current account with CBI, and the like)
- Facilities granted to the government of I.R. Iran as well as facilities guaranteed by the government
- Claims on central banks of countries categorized as group A as well as claims explicitly guaranteed by such central banks or states
- Claims on the central governments and central banks of countries in Group B in the national currency of the borrower
- Claims on borrowers located in countries belonging to Group B which are explicitly guaranteed by the central government or the central bank of the related country and are paid in the national currency of the related country
- Claims secured by securities issued by the government or central bank of Iran or central governments and central banks of the countries belonging to group A
- Securities issued by the government or the central bank of the Islamic republic of Iran
- Securities issued by the central government or the central bank of other countries

5-1-2 Assets with 20% risk weight

- Outstanding funds
- Claims on domestic banks and credit institutions (governmental or non-governmental) as well as claims guaranteed by such banks and credit institutions
- Claims on banks and credit institutions located in countries belonging to group A as well as claims guaranteed by them
- Claims on banks and credit institutions located in countries belonging to group B as well as claims guaranteed by them provided that there is maximum one year left to their maturity

- Claims on multilateral development banks (as specified in the annex) as well as claims guaranteed by them
- Claims secured by securities issued by multilateral development banks
- Interbank accounts
- Net domestic accounts

5-1-3 Assets with 50% risk weight

- Facilities secured totally by a residential unit

5-1-4 Assets with 100% risk weight

- Claims on public sector entities (municipalities, Social Service Organisation, etc.)
- Claims against non-governmental sector (except those explicitly guaranteed by the government)
- Claims on governmental enterprises and institutions
- Overdue and non-performing loan including governmental, non-governmental and previous loans
- Investments and Musharaka (including direct investments, Musharaka both governmental and non-governmental, equity investment and foreign partnerships) after deduction of the shares of subsidiary banks and credit institutions or (if necessary) other banks and credit institutions
- Goods of Salam, general warehouse, lien collaterals, goods purchased for sales by installments or leasing and the like
- Debtors for paid LCs or LGs
- Claims on central governments or central banks of group B countries in cases where the payment has been made in a currency other than their national currency
- Claims against banks and credit institutions of group B countries when there is one year or more time to their maturity
- Fixed assets
- Temporary debtors
- Other assets which cannot be classified in 1-1-5 to 3-1-5 categories

5-2 Off balance sheet items

Off balance sheet items are not only subject to risk weights in various asset categories (sub-articles related to 1-5), but also subject to conversion factor (as defined in sub-articles of 2-5). Using conversion factor, the off balance sheet items can be given the same critical level as the on balance sheet items while making calculations.

For each off balance sheet items the conversion factor can be applied as described here;

5-2-1 Obligations subject to zero percent conversion factor

- Obligations which are cancellable without condition by the bank and their maturity is less than one year
- Contra accounts and off balance sheet items which are being recognize only for statistical application

5-2-2 Conversion factor of 20%

- Approved or issued letter of credit for which the goods serve as collateral of credit, after the deduction of advance payments
- Letters of guarantee made in Rial or foreign currencies whose maturity date is less than one year, after the deduction of the cash deposit paid by the customer

5-2-3 Conversion factor of 50%

- Approved or issued documentary credits for which the goods do not serve as collateral, after the deduction of advance payments
- Letters of guarantee made in Rial or foreign currencies whose maturity date is one year or more, after the deduction of the cash deposit paid by the customer
- Obligations related to contracts and agreements
- Guarantees of participation bonds issued by companies and other legal entities

5-2-4 Conversion factor of 100%

- Endorsement of documents and bills
- Other obligations

Article 6: Calculation of capital adequacy ratio

Sum of the on and off balance sheet items which are risk weighted is the denominator while the numerator is the based capital as defined in the guideline for base capital. Therefore;

$$\text{Capital adequacy ratio} = \frac{\text{base capital}}{\text{on balance sheet items (risk weight)} + \text{off balance sheet items (conversion factor)(risk weight)}}$$

Article 7: Transmission period for state owned banks

Those sate owned banks whose capital adequacy ratio is less than 8% at the time this guideline is approved are required to present to the central bank a comprehensive and scheduled plan and, accordingly, adjust their status in accordance with article 3 of this guideline no longer than 22 march 2015.

Article 8: future modifications

If necessary, the central bank of Iran may add other items to those included in article 5 of this guideline.

Article 9: Transfer of information

Banks and credit institutions are required to calculate their capital adequacy ratio as specified by the central bank and report it to the central bank every 6 months.

The capital adequacy guideline was ratified by the Money and Credit Council in its 1014th meeting in 2014. This guideline includes 9 articles and 8 sub-articles.

Appendix

List of multi-lateral development banks mentioned in sub-article 2-1-5 of article 5 of the guideline for capital adequacy

- International bank for reconstruction and development (IBRD) and its subsidiaries
- Asian Development Bank
- African Development Bank
- European Investment Bank
- European Bank for Reconstruction and Development
- Islamic Development Bank
- OPEC Fund for International Development
- Arab Fund for Economic and Social Development
- Arab Monetary Fund
- Arab Bank for Economic Development in Africa
- Western Hemisphere Development Bank (Caribbean
- Nordic Investment Bank