



CIRCULAR

F. No 172/ IFSCA/Finance Company/Unit Regulations/2021-22/6 May 25, 2021

**To,
All Finance Companies / Finance Units in the International Financial Services
Centre (IFSC)**

**Subject: Framework on computation of Exposure Ceiling for Finance Companies
(FC) / Finance Units (FU)**

The framework on computation of Exposure Ceiling complements the regulatory capital requirements as prescribed by the International Financial Services Centres Authority (herein referred to as 'Authority'). This framework aims at monitoring the exposures that are significant compared to the capital resources of the Finance Companies/Finance Units (FC/FUs) and thus protecting them from concentration risk arising from large exposure to a single counterparty or to a group of connected counterparties.

2. The FC/FUs may draw reference to sub-regulation (4) of regulation 4 on Exposure Ceiling (EC), of the International Financial Services Centres Authority (Finance Company) Regulations, 2021 (herein referred to as 'Regulations') dated March 25, 2021 issued by the Authority.

3. The Authority directs the FC/FU in the International Financial Services Centres (herein referred to as 'IFSCs') to adhere to the following framework for the computation of Exposure Ceiling.

A. Applicability

4. This circular shall be adopted by a FC/FU as the case may be, registered under regulation 3 of the Regulations and intending to undertake activities mentioned in the point 5 and point 6 of the Schedule therein, viz;

- (i) Undertaking one or more core activities with or without non-core activities, and;
- (ii) Undertaking specialized activities with or without core or non-core activities.

5. The guidelines/circular issued on prudential regulations as specified in regulation 4 of the Regulations shall be applicable to specialized and core activities

being undertaken by the FC/FU registered with the Authority unless such specific requirements are prescribed for undertaking any of the non-core activities, as defined in the Regulations, by the Authority from time to time.

B. Exposure Ceiling Framework

6. Exposure Value

A FC/FU in general shall consider both on and off-balance sheet exposures and instruments with counterparty credit risk which are included in the risk based capital framework¹ in order to identify exposures to a counterparty.

7. Eligible capital base

The eligible capital base shall be the effective amount of Tier 1 capital fulfilling the criteria as defined in the circular on 'Computation of Regulatory Capital' dated April 26, 2021.

8. Exposure Ceiling

The Exposure Ceiling shall be the sum of all exposure values of a FC/FU to a single counterparty or to a group of connected counterparties which shall not exceed *twenty-five* percent of its eligible capital base at all times without the approval of the Authority, subject to the provisions of sub-regulation (4) of regulation 4 of the Regulations.

Herein, a group of connected counterparties shall have the same meaning as defined under sub-section E of section II of the Basel document titled 'Supervisory framework for measuring and controlling large exposures' dated April 2014.

Further, the exposure ceiling shall not take into account the fee income or income receivables generated while undertaking any of the non-core activities as specified in the Regulations, unless otherwise prescribed by the Authority in any of the activity specific circular/guidelines/regulations.

9. Large Exposure

The sum of all exposure values of a FC/FU to a counterparty or to a group of connected counterparties must be defined as a large exposure if it is equal to or above *ten* percent of the FC/FUs eligible capital base.

10. Measurement of exposure values

All exposure values must be defined and measured as specified in the Basel document titled 'Supervisory framework for measuring and controlling large exposures' dated April 2014, on *mutatis mutandis* basis. However, sub-section B of section IV of the

¹ As per the circular issued by the Authority on 'Computation of Regulatory Capital' dated April 26, 2021

above mentioned Basel document shall not apply to an FC or FU as the case may be. Computation of exposure values for OTC derivatives and any other instrument with counterparty credit risk and are not securities financing transaction (SFTs), shall be as per the Current Exposure Method (CEM) specified in the Basel document titled 'International Convergence of Capital Measurement and Capital Standards: A Revised Framework – Comprehensive Version (June 2006)'.

11. Breaches in the limits as prescribed in paragraph 8 above, which must remain an exception, shall be communicated immediately to the Authority and must be rectified immediately.

12. A FC/FU shall have an internal Board approved policy to cover general concentration risk and such other specific concentration risks arising from the sectoral concentration of asset exposures, geographical concentration of asset exposures, reliance on concentrated funding sources, and significant net short position in securities.

C. Regulatory reporting

13. The FC/FU shall report to the Board at regular intervals and to the Authority as may be specified by the Authority from time to time, on the following exposure values before and after the application of credit risk mitigation techniques:

- (i) All exposures, measured as specified in this circular, with values equal to or above *ten* percent of the FC/FU's eligible capital base.
- (ii) All other exposures, measured as specified in this circular without the effect of credit risk mitigation (CRM) being taken into account, with values equal to or above *ten* percent of the FC/FUs eligible capital base
- (iii) Twenty largest exposures included in the scope of application, irrespective of the values of these exposures relative to the FC/FUs eligible capital base.

14. All FC/FUs on which this circular is applicable, are directed to ensure compliance with this circular as amended from time to time.

Yours faithfully,

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