

## **ANNEX 1: REQUIREMENTS FOR INNOVATIVE TIER I CAPITAL INSTRUMENTS**

### Requirements relating to the Reporting Bank issuing Innovative Tier 1 Capital Instruments

1.1 A Reporting Bank intending to issue any innovative Tier 1 capital instrument ("IT1") for the purpose of inclusion as Tier 1 Capital, shall:

- (a) consult the Authority well in advance if the instrument has features that are not explicitly addressed by this Annex; and
- (b) obtain the approval of the Authority for the instrument to qualify as Tier 1 Capital.

1.2 In applying for such approval, a Reporting Bank shall:

- (a) submit an appropriate memorandum of compliance stating how the proposed issuance complies with the requirements set out in paragraph 1.3 and where applicable, paragraph 1.4 and identifying the relevant portions of the agreement governing the issuance of the instrument which address the requirements; and
- (b) confirm to the Authority in writing that it has received written external legal and accounting opinions stating that the requirements in paragraph 1.3 and, where applicable, paragraph 1.4 have been met.

### Minimum Requirements for IT1 Issued Directly by Reporting Bank

1.3 To qualify for inclusion as Tier 1 Capital, an IT1 shall satisfy the following requirements:

- (a) the IT1 is issued and fully paid-up in cash. Only the net proceeds received from the issuance of IT1s shall be included as capital;
- (b) the IT1 does not have a maturity date;
- (c) the IT1, if redeemable, (whether through a call option, repurchase or otherwise), may only be redeemed -
  - (i) in the case where the IT1 is to be redeemed by, or with the proceeds from, the issuance of equal or higher quality capital, with the prior approval of the Authority; and

- (ii) in any other case, at the option of the Reporting Bank with the prior approval of the Authority<sup>1</sup>.

Without prejudice to any other matter that the Authority may consider relevant, the Authority shall, in determining whether to grant its approval, have regard to whether the capital of the Reporting Bank is likely to remain adequate after redemption;

[MAS Notice 637 (Amendment) 2007]  
[MAS Notice 637 (Amendment 2) 2007]

- (d) the agreement governing the issuance of the IT1 does not have any call option within the first five years from the issue date, other than a call option which may be exercised by the Reporting Bank where:
  - (i) the IT1 was issued for the purpose of a merger with or acquisition by, the Reporting Bank and the merger or acquisition is aborted;
  - (ii) there is a change in tax status of the IT1 due to changes in the applicable tax laws of the country or territory in which the IT1 was issued;
  - (iii) in the case of a merger or acquisition, the IT1 is exchanged for shares or any instrument of the surviving or new Reporting Bank (as the case may be) with terms and conditions that qualify the shares or instrument as equal or higher quality capital; or
  - (iv) there is a change in this Notice relating to the recognition of the IT1 as capital for calculating CAR;

[MAS Notice 637 (Amendment) 2007]

- (e) the agreement governing the issuance of the IT1 does not contain any provision that mandates or creates an incentive for the Reporting Bank to repay the outstanding principal of the instrument early<sup>2</sup>, other than a call option which may be exercised by the Reporting Bank no earlier than 10 years after the issuance of the IT1, accompanied by a provision whereby the dividend or coupon

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<sup>1</sup> The Authority is not likely to grant any approval for redemption under paragraph 1.3(c)(ii) within the first 5 years from the issue date except in any one of the situations set out in paragraph 1.3(d).

Approval is likely to be granted after the first 5 years from the issue date:

- (a) where the IT1 is replaced by equal or higher quality capital (including an increase in retained earnings);
- (b) where the Reporting Bank or any of its banking group companies is reducing its operations in Singapore or elsewhere; or
- (c) in any one of the situations set out in paragraph 1.3(d).

[MAS Notice 637 (Amendment) 2007]  
[MAS Notice 637 (Amendment 2) 2007]

<sup>2</sup> Examples are a cross-default or negative pledge clause or a restrictive covenant for an IT1 issued as debt.

rate payable under the IT1 increases by no more than 100 basis points over the initial rate, less the swap spread between the initial index basis and the stepped-up index basis if the Reporting Bank chooses not to exercise its option, such increase in dividend or coupon rate being the only one during the validity period of the IT1;

[MAS Notice 637 (Amendment) 2007]

- (f) subject to sub-paragraph (h), any dividend or coupon to be paid under the IT1 is only paid to the extent that the Reporting Bank has profits distributable under written law, determined as at the last public disclosure of its financial statements;

[MAS Notice 637 (Amendment 2) 2007]

- (g) the Reporting Bank has full discretion over the amount and timing of dividends or coupons under the IT1 where the Reporting Bank –
  - (i) has not paid or declared a dividend on its ordinary shares in the preceding financial year; or
  - (ii) determines that no dividend is to be paid on such shares in the current financial year;
- (h) the dividends or coupons on the IT1 are non-cumulative or where the dividends or coupons are cumulative and deferred, such dividends or coupons shall only be settled by, or with the proceeds from, the issuance of equal or higher quality capital;

[MAS Notice 637 (Amendment 2) 2007]

- (i) [Deleted by MAS Notice 637 (Amendment 2) 2007]
- (j) the dividend or coupon rate, or the formulae for calculating dividend or coupon payments, is fixed at the time of issuance of the IT1 and is not linked to the credit standing of the Reporting Bank<sup>3</sup>;

[MAS Notice 637 (Amendment) 2007]

- (k) the IT1 is available to absorb the losses of the Reporting Bank without it being obliged to cease carrying on business. In this regard, for an IT1 classified legally as debt, this condition may be achieved if the agreement governing the issuance of the IT1 specifically provides for the principal and coupon payments to absorb losses where the Reporting Bank would otherwise be insolvent, or for the holders of the IT1 to be treated as if they were holders of a specified class of share capital in any proceedings commenced for the winding up of the Reporting Bank;
- (l) the holder of the IT1 has a priority of claim, in respect of the principal and dividend or coupon payments of the IT1 in the event

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<sup>3</sup> For the avoidance of doubt, this does not preclude linking dividends or coupons to movements in general market indices.

[MAS Notice 637 (Amendment) 2007]

of a winding up of the Reporting Bank, which is lower than that of depositors, other creditors of the bank, and holders of Tier 2 capital instruments, except where such persons rank equally with, or behind the holders of the IT1;

[MAS Notice 637 (Amendment) 2007]

- (m) the IT1 is not secured or covered under any arrangement that legally or economically enhances the priority of the claim of any holder of the IT1 as against the persons set out in paragraph 1.3(l) above;
- (n) for any IT1 issued as debt by the Reporting Bank, the holder of the IT1 waives his right to set off any amounts he owes the Reporting Bank against any subordinated amount owed to him due to the IT1 and commits to return any set-off amounts or benefits received to the liquidator;

[MAS Notice 637 (Amendment) 2007]

- (o) the subordination provisions of the IT1 are governed by the laws of Singapore. Where the IT1 is to be subject to the laws of a jurisdiction other than Singapore, the Reporting Bank shall satisfy itself and the Authority that all the relevant conditions specified within this Annex are met under the laws of that jurisdiction;
- (p) the main features of the IT1, in particular paragraphs 1.3(f) to (n), are disclosed clearly and accurately;

[MAS Notice 637 (Amendment) 2007]

- (q) the agreement governing the issuance of the IT1 cannot be changed without prior approval of the Authority as the proposed changes may impact its eligibility as Tier 1 Capital.

Additional Requirements For Issuance Via A Special Purpose Vehicle ("SPV")

1.4 A Reporting Bank may include any preference share issued by a SPV which satisfies the requirements in paragraph 1.3 as Tier 1 Capital of the Reporting Bank at the Solo level if the following additional requirements are met:

- (a) the SPV is wholly-owned and managed by the Reporting Bank and under the sole control of the bank;
- (b) the SPV is established for the sole purpose of issuing the preference shares, the entire proceeds of which are lent to the Reporting Bank, without restrictions via an inter-company instrument (hereinafter referred to as "Interco");
- (c) the SPV does not carry on any other business or activity except those mentioned in paragraph 1.4(b) and appropriate arrangements are in place to prevent the SPV from becoming insolvent;
- (d) where dividends from the preference shares are waived by the SPV, the proceeds arising from coupons under the Interco that would

otherwise accumulate in the SPV shall be made available, without restrictions, to the Reporting Bank;

- (e) the agreement governing the issuance of the Interco offers a level of loss absorbency that is identical to any Upper Tier 2 capital instrument issued by the Reporting Bank, except that the Interco shall be dated with a minimum 50-year maturity. At the maturity of the Interco, the SPV shall invest the proceeds from the Reporting Bank in a similar inter-company instrument if the proceeds are not otherwise applied to pay the holders of the preference shares;
- (f) the Interco is available to absorb the Reporting Bank's losses without the Reporting bank being obliged to cease carrying on business. In this regard, it may be achieved if the agreement governing the issuance of the Interco specifically provides that the principal and coupon payments under the Interco are available to absorb losses where the Reporting Bank would otherwise become insolvent, or for the SPV to be treated as if it was the holder of a specified class of share capital in any proceedings commenced for the winding up of the Reporting Bank;
- (g) the SPV's priority of claim in respect of the principal and coupon payments of the Interco in the event of winding up of the Reporting Bank, which is lower than that of depositors and other creditors of the bank except where such persons expressed to rank equally with, or behind the SPV.
- (h) the subordination provisions of the Interco are governed by the laws of Singapore. Where the Interco is governed by the laws of a jurisdiction other than Singapore, the Reporting Bank shall satisfy itself and the Authority that all the relevant conditions specified within this Annex are met under the laws of that jurisdiction;
- (i) the agreement governing the issuance of the Interco does not contain any provision that would require early repayment of the Interco (e.g. a cross-default or negative pledge clause and any restrictive covenant);
- (j) a mandatory exchange of the preference shares issued by the SPV for shares qualifying as a Tier 1 Capital instrument issued by the Reporting Bank shall take place well before a serious deterioration in the financial position of the Reporting Bank. At the minimum, this mandatory exchange shall be triggered and shall take effect immediately<sup>4</sup> upon the occurrence of any of the following events<sup>5</sup>:
  - (i) the Reporting Bank breaches the published minimum Tier 1 CAR or Total CAR requirements imposed by the Authority;

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<sup>4</sup> The Authority considers it unacceptable for substitution to be contingent on any event, and for the issuance of shares by the Reporting Banks qualifying as Tier 1 Capital to be subject to any delays, such as receipt of approval from investors.

<sup>5</sup> All instrument issued via an SPV approved by the Authority on or before 31 December 2004 or any such proposed instruments for which an application for approval from the Authority has been made for on or before 31 December 2004 need not comply with requirements set out in paragraph 1.4(j) where it has met the requirements set out in paragraph 1.4(j) of MAS Notice 637 on or before 31 December 2004.

- (ii) the Authority exercises its powers under section 49(2)(c) of the Banking Act, or any successor provision, to assume control of and carry on the business of the Reporting Bank or direct some other person to assume control of and carry on the business of the bank;
- (ia) the Authority exercises its powers under section 49(2) of the Banking Act, or any successor provisions to direct the Reporting Bank to effect an exchange;
- (iii) any proceedings are commenced for the winding up of the Reporting Bank, whether in Singapore or elsewhere;
- (iv) the SPV ceases to be wholly owned, managed and under the sole control of the Reporting Bank. For the purposes of this requirement, an SPV is considered to be wholly owned, managed and under the sole control of a Reporting Bank when:
  - (A) The Reporting Bank owns and controls the voting power attached to all the ordinary shares of the SPV;
  - (B) All the executive officers of the SPV are either employees of the Reporting Bank or appointees of the Reporting Bank. Where an appointee is a non-employee, the appointee shall be appointed pursuant to a management contract which requires the appointee to act in accordance with any instruction of the Reporting Bank;
  - (C) The majority of the Board of Directors of the SPV are employees of the Reporting Bank or are appointees of the Reporting Bank. In the case where appointees are non-employees, these persons are appointed pursuant to a management contract which requires them to act in accordance with any instruction of the Reporting Bank; and
  - (D) No person other than the Reporting Bank has the capacity to determine the outcome of decisions on the financial and operating policies of the SPV.

The rate of exchange in terms of the ratio of shares of the Reporting Bank to preference shares issued by the SPV shall be fixed at the time of issuance of the preference shares of the SPV. The Reporting Bank shall maintain a sufficient margin of authorised share capital that is not issued to enable exchange to take place at any time;

[MAS Notice 637 (Amendment) 2004]

- (k) the agreement governing the issuance of the Interco and the preference shares issued by the SPV cannot be changed without the prior approval of the Authority as the proposed changes may impact the instrument's eligibility as Tier 1 Capital.