Guideline for base capital of banks and credit institutions

In order to achieve the supervisory goals in all cases which are subject to prudential regulations, the concept of capital is defined as below.

Article 1: Base capital

Base capital of banks and credit institutions includes the aggregation of core capital (as defined in article 2) and supplementary capital (as defined in article 3) after the required deductions (as described in article 4).

Article 2: Tier one (core) capital

2-1 Components of the core capital include;

- Paid-in capital
- Legal reserve
- Other reserves (except reserves/ provisions due to reevaluation of fixed assets and equities belonging to banks and credit institutions)
- Share premium
- Retained profit (in case there is accumulated loss, that amount will be deducted from the core capital)

Article 3: Tier two capital (supplementary capital)

The following items shall be included in tier two capital;

3-1 General provision of_doubtful debts

For the purpose of this guideline, the maximum acceptable general provisions for doubtful debts equal 1/25% of the risk weighted assets (In accordance with the terms specified in capital adequacy guideline).

3-2 Reserves/ provisions due to reevaluation of fixed assets

Such reserves/ provisions result from the reevaluation of the fixed assets of the bank or credit institution. Having gone through legal procedures, they shall be either recognized in the books of the bank or credit institution as the reserves/ provisions of reevaluation, or directly added to the paid-in capital.

3-3 Reserves due to reevaluation of shares

These reserves result from the difference between the cost price and the reevaluation price of the shares belonging to banks and credit institutions. They can be applied in tier two capital only when legal procedures are followed, the required licenses are obtained, and at least 55% of the difference is deducted. This 55% deduction is because of the volatility of share prices and the probability of reduction of the reevaluation price.

Article 4: Deductions of the aggregate of tier one and tier two capitals

In cases where banks and credit institutions are the shareholders of other banks and credit institutions, it is required that the following items be deducted from the aggregate of tier one and tier two capitals.

4-1 Investments in other banks and credit institutions of which the accounts are not consolidated with those of the bank or parent credit institution. This term is applicable in cases where provision of consolidated financial statements is required based on accounting standards.

4-2 Investments in other banks and credit institutions (upon the approval of the Central Bank of Iran)

Article 5: Ceiling for tier two capital

Total tier two capital may equal tier one capital and the excess amount cannot be included in base capital.

This guideline includes 5 articles and 6 sub-articles and was approved in the 1013^th^ meeting of Money and Credit Council in January 2004.