

**CHARTERED FINANCE & LEASING LTD.
(CFL)**

(“NBFC/ B-13.02480”)

**INTERNAL CAPITAL ADEQUACY
ASSESSMENT PROCESS (ICAAP)**

SUMMARY OF POLICY

Particular	Details
Policy Name	Internal Capital Adequacy Assessment Process (ICAAP)
Version	V2
Latest Approval/Review Date	07th April,2026
Review Cycle	Annually
Approver	Board of Directors of Chartered Finance & Leasing Ltd

VERSION HISTORY

VERSION NO.	APPROVAL	VERSION DESCRIPTION	REGULATORY REFERENCE	REMARKS
I	11 th July, 2025	2025	RBI Regulation	Policy adopted by the Board
II	07 th April,2026	2026	RBI Regulation	Policy adopted by the Board

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Internal Capital Adequacy Assessment Process (ICAAP)

1. Capital Adequacy framework

The Reserve Bank of India, vide Chapter V (the Reserve Bank of India (Non-Banking Financial Companies – Prudential Norms on Capital Adequacy) Directions, 2025, as amended from time to time, requires the Company to undertake an internal assessment of the need for capital commensurate with the risk profile of its business.

This internal assessment shall be on similar lines as ICAAP prescribed for commercial banks under Pillar 2 under the Reserve Bank of India (Commercial Banks – Prudential Norms on Capital Adequacy) Directions, 2025.

Basel III reforms strengthen the bank-level i.e. micro prudential regulation, with the intention to raise the resilience of individual banking institutions in periods of stress. The new global regulatory and supervisory standards mainly seek to raise the quality and level of capital to ensure banks are better able to absorb losses on both a going concern and a gone concern basis, increase the risk coverage of the capital framework.

2. Scope of application of capital adequacy framework:

The Company is required to calculate capital adequacy ratio, which measures the capital adequacy based on its capital strength and risk profile.

The Company will quarterly evaluate capital adequacy and consider different business case scenarios to see minimum threshold capital requirement maintained even at worst-case scenario.

Profits in the current financial year shall be included in owned fund on a quarterly basis only where the financial statements are subjected to limited review / audit by the statutory auditors, and shall be reduced by the average dividend paid in the last three years in the manner specified ($E_{Pt} = NP_t - 0.25 \cdot D_t$); losses in the current year shall be fully deducted.

Three pillars of capital adequacy

The Capital Adequacy Framework rests on three components or three Pillars. Pillar 1 is the Minimum Capital Ratio while Pillar 2 and Pillar 3 are the Supervisory Review Process (SRP) and Market Discipline, respectively.

- Pillar 1: Minimum Capital Requirements - which prescribes a risk-sensitive calculation of capital requirements that explicitly, includes operational risk in addition to market and credit risk.
- Pillar 2: Supervisory Review Process (SRP) - which envisages the establishment of suitable risk management systems in banks and their review by the supervisory authority.
- Pillar 3: Market Discipline - which seeks to achieve increased transparency through expanded disclosure requirements for banks.
- Note: Unlike commercial banks, RBI has clarified that NBFCs are required to carry out an internal assessment of capital adequacy under Pillar 2 (ICAAP) as a supervisory tool for capital planning and risk management, but a separate Pillar 2 capital charge over and above the minimum capital ratio prescribed under Pillar 1 will not be insisted upon by RBI for NBFCs. Accordingly, the outcome of this ICAAP is used by the Company for internal capital planning, risk management and Board oversight purposes, and does not by itself create an additional regulatory capital requirement.

The main aspects to be addressed under the SRP would include:

- (a) the risks that are not fully captured by the minimum capital ratio prescribed under Pillar 1;
- (b) the risks that are not at all taken into account by the Pillar 1; and
- (c) The factors external to the Company.

The capital adequacy ratio prescribed by the RBI under the Pillar 1 of the Framework is only the regulatory minimum level, addressing only three specified risks (viz., credit, market and operational risks). Additional capital might be necessary for the Company, because of both the possibility of some under-estimation of risks under Pillar 1 and the Company's actual risk exposure vis-à-vis the quality of its risk management architecture.

3. Internal Capital Adequacy Assessment Process (ICAAP)

Pillar 2 requires NBFCs to implement an internal process, called the Internal Capital Adequacy Assessment Process (ICAAP), for assessing their capital adequacy in relation to their risk profiles, as well as a strategy for maintaining their capital levels.

The ICAAP comprises the Company's procedures and measures designed to ensure the following:

- (a) An appropriate identification and measurement of risks;
- (b) An appropriate level of internal capital in relation to the Company's risk profile; and

- (c) Application and further development of suitable risk management systems in the Company.

4. Board of Directors Meeting and Review

The Board of Directors, in their board meetings, will oversee the implementation of the system and review its functioning periodically. The ultimate responsibility for designing and implementation of the ICAAP lies with the Company's board of directors.

5. Scope

Internal Capital Adequacy Assessment Process (ICAAP)

While working on the ICAAP, the Company takes an integrated, firm-wide perspective of its own risk exposure, in order to support its ability to identify and react to emerging and growing risks in a timely and effective manner.

6. Purpose

The purpose of this guidance is to enhance firm-wide oversight, risk management and controls around the Company's business activities.

This system developed considering the following key features:

- (a) Active board and senior management oversight;
- (b) Appropriate policies, procedures and limits;
- (c) Comprehensive and timely identification, measurement, mitigation, controlling, monitoring and reporting of risks;
- (d) Appropriate management information systems (MIS) at the business and firm-wide level;
- (e) Comprehensive internal controls.

7. Methodology

The board and senior management must first have an understanding of risk exposures on a firm-wide basis. To achieve this understanding, the appropriate members of senior management must bring together the perspectives of the key business and control functions. There is Risk Management committee, which meets at regular intervals to assess the risks related to business.

The Board should ensure that the senior management of the Company:

- (a) Establishes a risk framework in order to assess and appropriately manage the various risk exposures of the Company.

- (b) Develops a system to monitor the Company's risk exposures and to relate them to the Company's capital and reserve funds.
- (c) Establishes a method to monitor the Company's compliance with internal policies, particularly about risk management.
- (d) Effectively communicates all relevant policies and procedures throughout the Company.

The internal capital assessment shall factor in credit risk, market risk, operational risk and all other residual risks as per the methodology specified below, which shall be proportionate to the scale and complexity of operations of the Company. The Company shall maintain capital, on an ongoing basis, at or above its internal capital target, being a CRAR of not less than 18% and a Tier 1 capital ratio of not less than 13%, with any decline in CRAR below 20% to be reported to the Board as an early-warning trigger, which shall in no case be lower than the minimum capital requirements prescribed under the RBI Directions on Capital Adequacy. The methodology for each material risk shall be as under:

(a) Credit risk: the capital requirement shall be computed on the risk-weighted assets arrived at by applying the standardised risk weights and credit conversion factors prescribed under the RBI Directions on Capital Adequacy, supplemented by an assessment of the credit quality of the portfolio, including trends in stressed and non-performing assets and the value and enforceability of collateral;

(b) Market risk: the risk on the investment portfolio (including equity shares, units of mutual funds and debt securities) shall be assessed on the basis of the mark-to-market impact of adverse movements in prices, interest rates and yields, and capital shall be allocated for the loss so estimated;

(c) Operational risk: the risk shall be assessed on the basis of the operational loss events and near misses recorded by the Company, internal audit findings and the risk and control self-assessment, and capital shall be allocated using a gross income based approach on the lines of the Basic Indicator Approach applicable to commercial banks;

(d) Concentration risk: the risk arising from single borrower, group borrower, sectoral and top-borrower exposures shall be assessed against Tier 1 capital and the internal exposure limits approved by the Board, and additional capital shall be allocated where the concentration is material;

(e) Liquidity risk: the risk shall be assessed through the structural and dynamic liquidity statements and the liquidity stress tests conducted under the Company's liquidity risk management framework, and the impact on

capital of meeting a liquidity shortfall (including the cost of raising funds at distressed rates or the loss on liquidating assets) shall be estimated;

(f) Interest rate risk in the banking book: the risk shall be assessed through the interest rate sensitivity (gap) statement, measuring the impact of adverse movements in interest rates on the earnings and on the economic value of equity of the Company;

(g) Other residual risks: strategic, reputational, compliance, legal and model risks shall be assessed qualitatively, and a capital buffer shall be allocated where any such risk is assessed as material;

(h) Stress testing: the capital adequacy of the Company shall be tested under the stress scenarios set out below, and the results, together with the remedial actions proposed, shall be placed before the Risk Management Committee and the Board, to determine whether the Company's capital remains above the regulatory minimum and the internal capital target under stress; and

(i) Capital planning: the ICAAP shall include a capital plan, prepared along with the business plan and reviewed by the Board, which projects the capital requirement against the planned growth and risk profile of the Company, identifies the sources from which capital will be raised (internal accruals, fresh equity or Tier 2 capital) and sets out the actions to be taken if capital approaches the internal capital target.

8. Stress Testing Scenario Assumptions

ICAAP to Include Stress Tests and Scenario Analyses

- (a) As part of the ICAAP, the management of the Company shall, as a minimum, conduct relevant stress tests periodically, particularly in respect of the Company's material risk exposures, in order to evaluate the potential vulnerability of the Company to some unlikely but reasonable events or movements in the market conditions that could have an adverse impact on the Company.
- (b) The first objective of an ICAAP is to identify all material risks. Risks that can be measured and quantified should be treated rigorously as data and methods allow. The appropriate means and methods to measure and quantify those material risks are likely to vary across NBFCs.
- (c) Some of the risks to which NBFCs are exposed include credit risk, market risk, operational risk, interest rate risk, credit concentration risk and liquidity risk.

- (d) Additionally, where the Company employs risk mitigation techniques, it should understand the risk being mitigated and the potential effects of that mitigation, reckoning its enforceability and effectiveness, on its risk profile.

The Company has considered the following scenario for calculating CRAR under various stress conditions.

- (a) Increase in NPA. Deterioration in the credit quality due to economic downturn
- (b) Concentration Risk. Deterioration in the credit quality of top borrowers due to economic downturn/other factors.
- (c) Spiral effect of inflation on macroeconomic factors such as increase in repo rate, reduction of liquidity in market, etc.
- (d) Negative impact of stock market due to adverse news, policies, geopolitical risks, climate risks, etc., on investment portfolio of the company.
- (e) Increase in margin requirement due to volatility in market movements.