

AT1 investors point to YES Bank governance issues

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Synopsis

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Mumbai: The battle between angry bondholders of [Yes Bank](#) and the Reserve Bank of India (RBI) is heading towards a flashpoint amid affidavits filed by some of the [investors](#) on Monday, pointing out that the decision to write down the contentious [bonds](#) was flawed as the private sector [lender](#) had serious governance lapses.

Yes Bank had window-dressed its financials to lure investors to buy the bonds in 2016 and 2017 - a violation that RBI did not factor in while backing the complete write down of additional tier-1 (AT1) bonds in its special leave petition before the apex court.

AT1 bonds are quasi-equity instruments with features to absorb losses when a bank runs into trouble. **In such a situation, the RBI master circular of 2015 (that outlines the internationally accepted Basel III capital rules) allows write down or conversion of these high-return, high-risk bonds into equity to save the bank and keep it afloat as a going concern.**

According to RBI, the write down has to happen before the infusion of fresh capital in a stressed bank to avoid a dilution of capital that new investors bring in. So, a write down of AT1 bonds is necessary to attract investors and save crisis-ridden banks.

However, an often overlooked footnote in the RBI master circular says: "In rare situations, a bank may also become non-viable due to non-financial problems, such as conduct of affairs of the bank in a manner which is detrimental to the interest of depositors, serious corporate governance issues, etc. In such situations raising capital is not considered a part of the solution and therefore, may not attract provisions of this framework." In other words, even if a write down is possible if a bank suffers genuine business losses, the action may be difficult to defend if a bank had masked its losses and misled investors - allegations that [Yes Bank](#) faced, leading to the ouster of its CEO and reconstitution of board of directors.

Two Yes AT1 bondholders ET spoke to said that this provision in the circular strengthens their argument that the write down was against the law and regulations.

Indeed, an affidavit by an institutional investor has highlighted that "the non-performing assets disclosed to the investors as at March 31, 2016 and March 31, 2017 by Yes Bank were ₹7,49 crore and ₹20,18.6 crore respectively whereas such non-performing assets have now been assessed by RBI to be ₹49,25.7 crore and ₹83,73.8 crore respectively."

Yes bank had released the information memorandum for the two tranches of AT1 bonds (aggregating ₹8,415 crore) in December 2016 and October 2017. Thus, the bank, according to bondholders, had not revealed the extent of its sticky assets even when it was readying to approach investors.

Other instances of misleading information being published in the public domain by Yes Bank are: its January 2018 press release for Quarter of financial year (FY) 2017-2018 said, "Asset quality continues to demonstrate resilience"; April 26, 2018 release for FY 2017-18 said, "Improving Asset Quality Outlook"; for 1st Quarter of Financial Year 2018-2019, it was "Healthy Asset Quality Delivery. Similar references to communiqués from the bank were also made for some of the quarters of 2018-19 and 2019-20.

Another argument raised in the counter-affidavit is that the decision to write down the bond could only have been taken between March 5, 2020 (when the RBI invoked the banking Regulation Act to supersede the bank board) and March 13, 2020 when the scheme to reconstruct was notified. However, the bonds were written down on March 14 prior to the injection of funds by SBI which also happened on March 14 – a decision which RBI has supported in its petition before the apex court.

"It is apparent from the public domain that RBI had become aware of misreporting of the financial statements of Yes Bank. Pursuant to which the term of the MD and CEO of Yes Bank was not allowed to be extended in January 2019," said a bond investor.

According to a senior banker, while the master circular allows write down, it's "not a black and white issue". "The situation may differ from bank to bank. Also, whether a bank is being reconstituted or getting wound up --- in the second situation, equity holders are at the bottom and would have to take a bigger hit than bond holders. In the Yes reconstruction, bondholders think they got a raw deal," said the person

