



भारतीय रिज़र्व बैंक
RESERVE BANK OF INDIA
www.rbi.org.in

RBI/2010-11/50

DBOD No. BP. BC. 18/ 21.04.141 / 2010-11

July 1, 2010

**All Commercial Banks
(excluding Regional Rural Banks)**

Dear Sir,

**Master Circular – Prudential norms for classification,
valuation and operation of investment portfolio by banks**

Please refer to the [Master Circular No. DBOD. BP. BC.3 / 21.04.141/ 2009-10 dated July 1, 2009](#), containing consolidated instructions/guidelines issued to banks till June 30, 2009, on matters relating to prudential norms for classification, valuation and operation of investment portfolio by banks. The above Master Circular has since been suitably updated by incorporating instructions/guidelines issued between July 1, 2009 and June 30, 2010, and furnished in the Annex. This updated version has also been placed on the RBI web-site (<http://www.rbi.org.in>).

2. An Appendix containing a list of circulars referred for the purpose of the current Master circular is furnished at the end of the Annex.

Yours faithfully,

(B.Mahapatra)
Chief General Manager-in-Charge

Encl: As above

**MASTER CIRCULAR – PRUDENTIAL NORMS FOR CLASSIFICATION,
VALUATION AND OPERATION OF INVESTMENT PORTFOLIO BY BANKS****Table of Contents**

1.	Introduction	4
1.1	Investment Policy	4
	1.1.1 STRIPS	7
	1.1.2 Ready forward contracts in Government Securities	7
	1.1.3 Transactions through SGL account	10
	1.1.4 Use of Bank Receipts (BR)	12
	1.1.5 Retailing of Government Securities	13
	1.1.6 Internal Control System	13
	1.1.7 Engagement of brokers	16
	1.1.8 Audit, review and reporting of investment transactions	18
1.2.	Non-SLR investment	19
1.3	General	26
	1.3.1 Reconciliation of holdings of Govt. securities, etc	26
	1.3.2 Transactions in securities - Custodial functions	27
	1.3.3 Portfolio Management on behalf of clients	27
	1.3.4 Investment Portfolio of bank - Transactions in Government Securities	28
2.	Classification	29
	2.1 Held to Maturity	29
	2.2 Available for Sale & Held for Trading	32
	2.3 Shifting among categories	32
3.	Valuation	34
	3.1 Held to Maturity	34
	3.2 Available for Sale	34
	3.3 Held for Trading	34
	3.4 Investment Fluctuation Reserve	35
	3.5 Market Value	37

		3.6	Unquoted SLR securities	37
			3.6.1 Central Government Security	37
			3.6.2 State Government Security	38
			3.6.3 Other Approved Security	38
		3.7	Unquoted Non-SLR Securities	38
			3.7.1 Debentures/Bonds	38
			3.7.2 Zero Coupon Bonds	39
			3.7.3 Preference Share	39
			3.7.4 Equity Share	40
			3.7.5 Mutual Fund Units	40
			3.7.6 Commercial Paper	40
			3.7.7 Investment in RRBs	41
		3.8	Investment in securities Issued by SC/RC	41
		3.9	Valuation & classification of bank's investment in VCF	42
		3.10	Non Performing investments	43
4.	Uniform Accounting for Repo/Non-Repo Transactions			44
5.	General			47
	5.1	Income Recognition		47
	5.2	Broken period Interest		48
	5.3	Dematerialized Holding		48
Annexes				49
Appendix				87

**MASTER CIRCULAR – PRUDENTIAL NORMS FOR CLASSIFICATION,
VALUATION AND OPERATION OF INVESTMENT PORTFOLIO BY BANKS**

1. Introduction

With the introduction of prudential norms on capital adequacy, income recognition, asset classification and provisioning requirements, the financial position of banks in India has improved in the last few years. Simultaneously, trading in securities market has improved in terms of turnover and the range of maturities dealt with. In view of these developments and taking into consideration the evolving international practices, Reserve Bank of India (RBI) has issued guidelines on classification, valuation and operation of investment portfolio by banks from time to time as detailed below:

1.1 Investment Policy

i) Banks should frame Internal Investment Policy Guidelines and obtain the Board's approval. The investment policy may be suitably framed/amended to include Primary Dealer (PD) activities also. Within the overall framework of the investment policy, the PD business undertaken by the bank will be limited to dealing, underwriting and market-making in Government Securities. Investments in Corporate/ PSUs/ FIs bonds, Commercial Papers, Certificate of Deposits, debt mutual funds and other fixed income securities will not be deemed to be part of PD business. The investment policy guidelines should be implemented to ensure that operations in securities are conducted in accordance with sound and acceptable business practices. While framing the investment policy, the following guidelines are to be kept in view by the banks:

(a) Banks may sell a government security already contracted for purchase, provided:

- (i) The purchase contract is confirmed prior to the sale,
- (ii) The purchase contract is guaranteed by CCIL or the security is contracted for purchase from the Reserve Bank and,
- (iii) The sale transaction will settle either in the same settlement cycle as the preceding purchase contract, or in a subsequent settlement cycle so that the delivery obligation under the sale contract is met by the securities acquired under the purchase contract (e.g. when a security is purchased on T+0 basis, it can be sold on either T+0 or T+1 basis on the day of the purchase; if however it is purchased on T+1 basis, it can be sold on T+1 basis on the day of purchase or on T+0 or T+1 basis on the next day).

For purchase of securities from RBI through Open Market Operations (OMO), no sale transactions should be contracted prior to receiving the confirmation of the deal/advice of allotment from the RBI .

- In addition to the above, the Scheduled Commercial Banks (other than RRBs and LABs) and Primary Dealers have been permitted to short sell Government securities in accordance with the requirements specified in **Annex I - A**.
- Further, the NDS-OM members have been permitted to transact on 'When Issued' basis in Central Government dated securities, subject to the guidelines specified in **Annex I-B**.

(b) Banks successful in the auction of primary issue of government may enter into contracts for sale of the allotted securities in accordance with the terms and conditions as per **Annex I-C**.

(c) The settlement of all outright secondary market transactions in Government Securities will be done on a standardized T+1 basis effective May 24, 2005.

(d) All the transactions put through by a bank, either on outright basis or ready forward basis and whether through the mechanism of Subsidiary General Ledger (SGL) Account or Bank Receipt (BR), should be reflected on the same day in its investment account and, accordingly, for SLR purpose wherever applicable.

(e) The brokerage on the deal payable to the broker, if any, (if the deal was put through with the help of a broker) should be clearly indicated on the notes/ memoranda put up to the top management seeking approval for putting through the transaction and a separate account of brokerage paid, broker-wise, should be maintained.

(f) For issue of BRs, the banks should adopt the format prescribed by the Indian Banks' Association (IBA) and strictly follow the guidelines prescribed by them in this regard. The banks, subject to the above, could issue BRs covering their own sale transactions only and should not issue BRs on behalf of their constituents, including brokers.

(g) The banks should be circumspect while acting as agents of their broker clients for carrying out transactions in securities on behalf of brokers.

(h) Any instance of return of SGL form from the Public Debt Office of the Reserve Bank for want of sufficient balance in the account should be immediately brought to Reserve Bank's notice with the details of the transactions.

(i) Banks desirous of making investment in equity shares/ debentures should observe the following guidelines:

(i) Build up adequate expertise in equity research by establishing a dedicated equity research department, as warranted by their scale of operations;

(ii) Formulate a transparent policy and procedure for investment in shares, etc., with the approval of the Board; and

(iii) The decision in regard to direct investment in shares, convertible bonds and debentures should be taken by the Investment Committee set up by the bank's Board. The Investment Committee should be held accountable for the investments made by the bank.

ii) With the approval of respective Boards, banks should clearly lay down the broad investment objectives to be followed while undertaking transactions in securities on their own investment account and on behalf of clients, clearly define the authority to put through deals, procedure to be followed for obtaining the sanction of the appropriate authority, procedure to be followed while putting through deals, various prudential exposure limits and the reporting system. While laying down such investment policy guidelines, banks should strictly observe Reserve Bank's detailed instructions on the following aspects:

- | | |
|---|-------------------|
| a. STRIPS | (Paragraph 1.1.1) |
| b. Ready Forward (buy back) deals in G-Sec | (Paragraph 1.1.2) |
| c. Transactions through Subsidiary General Ledger A/c | (Paragraph 1.1.3) |
| d. Use of Bank Receipts | (Paragraph 1.1.4) |
| e. Retailing of Government Securities | (Paragraph 1.1.5) |
| f. Internal Control System | (Paragraph 1.1.6) |
| g. Dealings through Brokers | (Paragraph 1.1.7) |
| h. Audit, Review and Reporting | (Paragraph 1.1.8) |

iii) The aforesaid instructions will be applicable mutatis mutandis, to the subsidiaries and mutual funds established by banks, except where they are contrary to or inconsistent with, specific regulations of Securities and Exchange Board of India (SEBI) and RBI governing their operations.

1.1.1 STRIPS

STRIPS stands for Separate Trading of Registered Interest and Principal Securities. Stripping is a process of converting periodic coupon payments of an existing Government security into tradable zero-coupon securities, which will usually trade in the market at a discount and are redeemed at face value. For instance, stripping a five-year Govt security would yield 10 coupon securities (representing the coupons), maturing on the respective coupon dates and one principal security representing the principal amount, maturing on the redemption date of the five-year security. Reconstitution is the reverse process of stripping, where, the Coupon STRIPS and Principal STRIPS are reassembled into the original Government security. Detailed guidelines outlining the process of stripping/reconstitution and other operational procedures regarding transactions in STRIPS are given in **Annex I-D**.

1.1.2 Ready Forward Contracts in Government Securities.

The terms and conditions subject to which ready forward contracts (including reverse ready forward contracts) may be entered into are as under:

(a) Ready forward contracts may be undertaken only in (i) Dated Securities and Treasury Bills issued by Government of India and (ii) Dated Securities issued by State Governments.

(b) Ready forward contracts in the above-mentioned securities may be entered into by:

- i) persons or entities maintaining a Subsidiary General Ledger (SGL) account with RBI, Mumbai and
- ii) the following categories of entities who do not maintain SGL accounts with the RBI but maintain gilt accounts (i.e gilt account holders) with a bank or any other entity (i.e. the custodian) permitted by the RBI to maintain Constituent Subsidiary General Ledger (CSGL) account with its Public Debt Office, Mumbai:

(a) Any scheduled bank,

(b) Any primary dealer authorised by the RBI,

(c) Any non-banking financial company registered with the RBI, other than Government companies as defined in Section 617 of the Companies Act, 1956,

(d) Any mutual fund registered with the SEBI,

(e) Any housing finance company registered with the National Housing Bank,

(f) Any insurance company registered with the Insurance Regulatory and Development Authority,

(g) Any non-scheduled Urban Co-operative bank,

(h) Any listed company, having a gilt account with a scheduled commercial bank, subject to the following conditions:

(1) The minimum period for Reverse Repo (lending of funds) by listed companies is seven days. However, listed companies can borrow funds through repo for shorter periods including overnight;

(2) Where the listed company is a 'buyer' of securities in the first leg of the repo contract (i.e. lender of funds), the custodian through which the repo transaction is settled should block these securities in the gilt account and ensure that these securities are not further sold or re-repoed during the repo period but are held for delivery under the second leg; and

(3) The counterparty to the listed companies for repo / reverse repo transactions should be either a bank or a Primary Dealer maintaining SGL Account with the RBI.

(i) Any unlisted company which has been issued special securities by the Government of India and having gilt account with a scheduled commercial bank; subject to the following conditions in addition to the conditions stipulated for listed company:

(1) The eligible unlisted companies can enter into ready forward transactions as the borrower of funds in the first leg of the repo contract only against the collateral of the special securities issued to them by the Government of India; and

(2) The counterparty to the eligible unlisted companies for repo transactions should be either a bank or a Primary Dealer maintaining SGL account with the Reserve Bank.

(c) All persons or entities specified at (ii) above can enter into ready forward transactions among themselves subject to the following restrictions:

i) An SGL account holder may not enter into a ready forward contract with its own constituent. That is, ready forward contracts should not be undertaken between a custodian and its gilt account holder,

ii) Any two gilt account holders maintaining their gilt accounts with the same custodian (i.e., the CSGL account holder) may not enter into ready forward contracts with each other, and

iii) Cooperative banks may not enter into ready forward contracts with the non-banking financial companies. This restriction would not apply to repo transactions between Urban Co-operative banks and authorised Primary Dealers in Government Securities.

(d) All ready forward contracts shall be reported on the Negotiated Dealing System (NDS). In respect of ready forward contracts involving gilt account holders, the custodian (i.e., the CSGL account holder) with whom the gilt accounts are maintained will be responsible for reporting the deals on the NDS on behalf of the constituents (i.e. the gilt account holders).

(e) All ready forward contracts shall be settled through the SGL Account / CSGL Account maintained with the RBI, Mumbai, with the Clearing Corporation of India Ltd. (CCIL) acting as the central counter party for all such ready forward transactions.

(f) The custodians should put in place an effective system of internal control and concurrent audit to ensure that:

i) ready forward transactions are undertaken only against the clear balance of securities in the gilt account,

ii) all such transactions are promptly reported on the NDS, and

iii) other terms and conditions referred to above have been complied with.

(g) The RBI regulated entities can undertake ready forward transactions only in securities held in excess of the prescribed Statutory Liquidity Ratio (SLR) requirements.

(h) No sale transaction shall be put through, in the first leg of a ready forward transaction by CSGL constituent entities without actually holding the securities in the portfolio.

- (i) Securities purchased under the ready forward contracts shall not be sold during the period of the contract except by entities permitted to undertake short selling,
- (j) Double ready forward deals in any security are strictly prohibited.
- (k) The guidelines for uniform accounting for Repo / Reverse Repo transactions are furnished in paragraph 4.

1.1.3 Transactions through SGL account

The following instructions should be followed by banks for purchase / sale of securities through SGL A/c, under the Delivery Versus Payment System wherein the transfer of securities takes place simultaneously with the transfer of funds. It is, therefore, necessary for both the selling bank and the buying bank to maintain current account with the RBI. As no 'Overdraft facility' in the current account would be extended, adequate balance in current account should be maintained by banks for effecting any purchase transaction.

- i) All transactions in Govt. securities for which SGL facility is available should be put through SGL A/cs only.
- ii) Under no circumstances, a SGL transfer form issued by a bank in favour of another bank should bounce for want of sufficient balance of securities in the SGL A/c of seller or for want of sufficient balance of funds in the current a/c of the buyer.
- iii) The SGL transfer form received by purchasing banks should be deposited in their SGL A/cs. immediately i.e. the date of lodgement of the SGL Form with RBI shall be within one working day after the date of signing of the Transfer Form. While in cases of OTC trades, the settlement has to be only on 'spot' delivery basis as per Section 2(i) of the Securities Contracts (Regulations) Act, 1956, in cases of deals on the recognised Stock Exchanges; settlement should be within the delivery period as per their rules, bye laws and regulations. In all cases, participants must indicate the deal/trade/contract date in Part C of the SGL Form under 'Sale date'. Where this is not completed the SGL Form will not be accepted by the RBI.
- iv) No sale should be effected by way of return of SGL form held by the bank.

v) SGL transfer forms should be signed by two authorised officials of the bank whose signatures should be recorded with the respective PDOs of the RBI and other banks.

vi) The SGL transfer forms should be in the standard format prescribed by the RBI and printed on semi-security paper of uniform size. They should be serially numbered and there should be a control system in place to account for each SGL form.

vii) If a SGL transfer form bounces for want of sufficient balance in the SGL A/c, the (selling) bank which has issued the form will be liable to the following penal action against it :

a) The amount of the SGL form (cost of purchase paid by the purchaser of the security) would be debited immediately to the current account of the selling bank with the RBI.

b) In the event of an overdraft arising in the current account following such a debit, penal interest would be charged by the RBI, on the amount of the overdraft, at a rate of 3 percentage points above the SBI Discount and Finance House of India's (SBIDFHI) call money lending rate on the day in question. However, if the SBIDFHI's closing call money rate is lower than the prime lending rate of banks, as stipulated in the RBI's interest rate directive in force, the applicable penal rate to be charged will be 3 percentage points, above the prime lending rate of the bank concerned, and

c) If the bouncing of the SGL form occurs thrice, the bank will be debarred from trading with the use of the SGL facility for a period of 6 months from the occurrence of the third bouncing. If, after restoration of the facility, any SGL form of the concerned bank bounces again, the bank will be permanently debarred from the use of the SGL facility in all the PDOs of the RBI.

d) The bouncing on account of insufficient balance in the current account of the buying bank would be reckoned (against the buying bank concerned) for the purpose of debarment from the use of SGL facility on par with the bouncing on account of insufficient balance in SGL a/c. of the selling bank (against selling bank). Instances of bouncing in both the accounts (i.e SGL a/c and current a/c) will be reckoned together against the SGL account holder

concerned for the purpose of debarment (i.e three in a half-year for temporary suspension and any bouncing after restoration of SGL facility, for permanent debarment.)

1.1.4 Use of Bank Receipt (BR)

The banks should follow the following instructions for issue of BRs:

- a)** No BR should be issued under any circumstances in respect of transactions in Govt. securities for which SGL facility is available.
- b)** Even in the case of other securities, BR may be issued for ready transactions only, under the following circumstances:
 - (i)** The scrips are yet to be issued by the issuer and the bank is holding the allotment advice.
 - (ii)** The security is physically held at a different centre and the bank is in a position to physically transfer the security and give delivery thereof within a short period.
 - (iii)** The security has been lodged for transfer / interest payment and the bank is holding necessary records of such lodgements and will be in a position to give physical delivery of the security within a short period.
- c)** No BR should be issued on the basis of a BR (of another bank) held by the bank and no transaction should take place on the basis of a mere exchange of BRs held by the bank.
- d)** BRs could be issued covering transactions relating to banks' own Investments Accounts only, and no BR should be issued by banks covering transactions relating to either the Accounts of Portfolio Management Scheme (PMS) Clients or Other Constituents' Accounts, including brokers.
- e)** No BR should remain outstanding for more than 15 days.
- f)** A BR should be redeemed only by actual delivery of scrips and not by cancellation of the transaction/set off against another transaction. If a BR is not redeemed by delivery of scrips within the validity period of 15 days, the BR should be deemed as dishonoured and the bank which has issued the BR should refer the case to

the RBI, explaining the reasons for which the scrips could not be delivered within the stipulated period and the proposed manner of settlement of the transaction.

g) BRs should be issued on semi-security paper, in the standard format (prescribed by IBA), serially numbered and signed by two authorised officials of the bank, whose signatures are recorded with other banks. As in the case of SGL forms, there should be a control system in place to account for each BR form.

h) Separate registers of BRs issued and BRs received should be maintained and arrangements should be put in place to ensure that these are systematically followed up and liquidated within the stipulated time limit.

i) The banks should also have a proper system for the custody of unused B.R. Forms and their utilisation. The existence and operations of these controls at the concerned offices/ departments of the bank should be reviewed, among others, by the statutory auditors and a certificate to this effect may be forwarded every year to the Regional Office of Department of Banking Supervision (DBS), RBI, under whose jurisdiction the Head Office of the bank is located.

j) Any violation of the instructions relating to BRs would invite penal action, which could include raising of reserve requirements, withdrawals of refinance facility from the RBI and denial of access to money markets. The RBI may also levy such other penalty as it may deem fit in accordance with the provisions of the Banking Regulation Act, 1949.

1.1.5 Retailing of Government Securities

The banks may undertake retailing of Government securities with non-bank clients subject to the following conditions:

- i)** Such retailing should be on outright basis and there is no restriction on the period between sale and purchase.
- ii)** The retailing of Government securities should be on the basis of ongoing market rates/ yield curve emerging out of secondary market transactions.

1.1.6 Internal Control System

The banks should observe the following guidelines for internal control system in respect of investment transactions:

(a) There should be a clear functional separation of (i) trading, (ii) settlement, monitoring and control and (iii) accounting. Similarly, there should be a functional separation of trading and back office functions relating to banks' own Investment Accounts, Portfolio Management Scheme (PMS) Clients' Accounts and other Constituents (including brokers') accounts. The Portfolio Management service may be provided to clients, subject to strictly following the guidelines in regard thereto (covered in paragraph 1.3.3). Further, PMS Clients Accounts should be subjected to a separate audit by external auditors.

(b) For every transaction entered into, the trading desk should prepare a deal slip which should contain data relating to nature of the deal, name of the counter-party, whether it is a direct deal or through a broker, and if through a broker, name of the broker, details of security, amount, price, contract date and time. The deal slips should be serially numbered and controlled separately to ensure that each deal slip has been properly accounted for. Once the deal is concluded, the dealer should immediately pass on the deal slip to the back office for recording and processing. For each deal there must be a system of issue of confirmation to the counterparty. The timely receipt of requisite written confirmation from the counterparty, which must include all essential details of the contract, should be monitored by the back office.

(c) With respect to transactions matched on the NDS-OM module, since CCIL is the central counterparty to all deals, exposure of any counterparty for a trade is only to CCIL and not to the entity with whom a deal matches. Besides, details of all deals on NDS-OM are available to the counterparties as and when required by way of reports on NDS-OM itself. In view of the above, the need for counterparty confirmation of deals matched on NDS-OM does not arise. The deals in Government security transactions in OTC market that are mandated to be settled through CCIL by reporting on the NDS, are not required to be confirmed physically as OTC deals depend on electronic confirmation by the back offices of both the counterparties on NDS system like the NDS-OM deals.

However, all government securities transactions, other than those mentioned above, will continue to be physically confirmed by the back offices of the counterparties, as hitherto

(d) Once a deal has been concluded, there should not be any substitution of the counter party bank by another bank by the broker, through whom the deal has been entered into; likewise, the security sold/purchased in the deal should not be substituted by another security.

(e) On the basis of vouchers passed by the back office (which should be done after verification of actual contract notes received from the broker/ counterparty and confirmation of the deal by the counterparty), the Accounts Section should independently write the books of account.

(f) In the case of transaction relating to PMS Clients' Accounts (including brokers), all the relative records should give a clear indication that the transaction belongs to PMS Clients/ other constituents and does not belong to bank's own Investment Account and the bank is acting only in its fiduciary/ agency capacity.

(g) (i) Records of SGL transfer forms issued/ received, should be maintained.

(ii) Balances as per bank's books should be reconciled at quarterly intervals with the balances in the books of PDOs. If the number of transactions so warrant, the reconciliation should be undertaken more frequently, say on a monthly basis. This reconciliation should be periodically checked by the internal audit department.

(iii) Any bouncing of SGL transfer forms issued by selling banks in favour of the buying bank, should immediately be brought to the notice of the Regional Office of Department of Banking Supervision of RBI by the buying bank.

(iv) A record of BRs issued/ received should be maintained.

(v) A system for verification of the authenticity of the BRs and SGL transfer forms received from the other banks and confirmation of authorised signatories should be put in place.

(h) Banks should put in place a reporting system to report to the top management, on a weekly basis, the details of transactions in securities, details of bouncing of SGL transfer forms issued by other banks and BRs outstanding for more than one month and a review of investment transactions undertaken during the period.

(i) Banks should not draw cheques on their account with the RBI for third party transactions, including inter-bank transactions. For such transactions, bankers' cheques/ pay orders should be issued.

(j) In case of investment in shares, the surveillance and monitoring of investment should be done by the Audit Committee of the Board, which shall review in each of its meetings, the total exposure of the bank to capital market both fund based and non-fund based, in different forms as stated above and ensure that the guidelines issued by RBI are complied with and adequate risk management and internal control systems are in place;

(k) The Audit Committee should keep the Board informed about the overall exposure to capital market, the compliance with the RBI and Board guidelines, adequacy of risk management and internal control systems;

(l) In order to avoid any possible conflict of interest, it should be ensured that the stockbrokers as directors on the Boards of banks or in any other capacity, do not involve themselves in any manner with the Investment Committee or in the decisions in regard to making investments in shares, etc., or advances against shares.

(m) The internal audit department should audit the transactions in securities on an ongoing basis, monitor the compliance with the laid down management policies and prescribed procedures and report the deficiencies directly to the management of the bank.

(n) The banks' managements should ensure that there are adequate internal control and audit procedures for ensuring proper compliance of the instructions in regard to the conduct of the investment portfolio. The banks should institute a regular system of monitoring compliance with the prudential and other guidelines issued by the RBI. The banks should get compliance in key areas certified by their statutory auditors and furnish such audit certificate to the Regional Office of DBS, RBI under whose jurisdiction the HO of the bank falls.

1.1.7 Engagement of brokers

i) For engagement of brokers to deal in investment transactions, the banks should observe the following guidelines:

- (a)** Transactions between one bank and another bank should not be put through the brokers' accounts. The brokerage on the deal payable to the broker, if any (if the deal was put through with the help of a broker), should be clearly indicated on the notes/memorandum put up to the top management seeking approval for putting through the transaction and separate account of brokerage paid, broker-wise, should be maintained.
- (b)** If a deal is put through with the help of a broker, the role of the broker should be restricted to that of bringing the two parties to the deal together.
- (c)** While negotiating the deal, the broker is not obliged to disclose the identity of the counterparty to the deal. On conclusion of the deal, he should disclose the counterparty and his contract note should clearly indicate the name of the counterparty. It should also be ensured by the bank that the broker note contains the exact time of the deal. Their back offices may ensure that the deal time on the broker note and the deal ticket is the same. The bank should also ensure that their concurrent auditors audit this aspect.
- (d)** On the basis of the contract note disclosing the name of the counterparty, settlement of deals between banks, viz. both fund settlement and delivery of security should be directly between the banks and the broker should have no role to play in the process.
- (e)** With the approval of their top managements, banks should prepare a panel of approved brokers which should be reviewed annually or more often if so warranted. Clear-cut criteria should be laid down for empanelment of brokers, including verification of their creditworthiness, market reputation, etc. A record of broker-wise details of deals put through and brokerage paid, should be maintained.
- (f)** A disproportionate part of the business should not be transacted through only one or a few brokers. Banks should fix aggregate contract limits for each of the approved brokers. A limit of 5% of total transactions (both purchase and sales) entered into by a bank during a year should be treated as the aggregate upper contract limit for each of the approved brokers. This limit should cover both the business initiated by a bank and the business offered/ brought to the bank by a broker. Banks should ensure that the transactions entered into through individual brokers during a year normally do not exceed

this limit. However, if for any reason it becomes necessary to exceed the aggregate limit for any broker, the specific reasons therefor should be recorded, in writing, by the authority empowered to put through the deals. Further, the board should be informed of this, post facto. However, the norm of 5% would not be applicable to banks' dealings through Primary Dealers.

(g) The concurrent auditors who audit the treasury operations should scrutinise the business done through brokers also and include it in their monthly report to the Chief Executive Officer of the bank. Besides, the business put through any individual broker or brokers in excess of the limit, with the reasons therefore, should be covered in the half-yearly review to the Board of Directors/ Local Advisory Board. These instructions also apply to subsidiaries and mutual funds of the banks.

[Certain clarifications on the instructions are furnished in the **Annex II.**]

ii) Inter-bank securities transactions should be undertaken directly between banks and no bank should engage the services of any broker in such transactions.

Exceptions:

Note (i) Banks may undertake securities transactions among themselves or with non-bank clients through members of the National Stock Exchange (NSE), OTC Exchange of India (OTCEI) and the Stock Exchange, Mumbai (BSE). If such transactions are not undertaken on the NSE, OTCEI or BSE, the same should be undertaken by banks directly, without engaging brokers.

Note (ii) Although the Securities Contracts (Regulation) Act, 1956 defines the term 'securities' to mean corporate shares, debentures, Govt. securities and rights or interest in securities, the term 'securities' would exclude corporate shares. The Provident / Pension Funds and Trusts registered under the Indian Trusts Act, 1882, will be outside the purview of the expression 'non-bank clients' for the purpose of note (i) above.

1.1.8 Audit, review and reporting of investment transactions

The banks should follow the following instructions in regard to audit, review and reporting of investment transactions :

a) Banks should undertake a half-yearly review (as of 30 September and 31 March) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate amendments made to the Investment Policy and

certify adherence to laid down internal investment policy and procedures and RBI guidelines, and put up the same before their respective Boards within a month, i.e by end-April and end-October.

b) A copy of the review report put up to the Bank's Board, should be forwarded to the RBI (concerned Regional Office of DBS, RBI) by 15 May and 15 November respectively.

c) In view of the possibility of abuse, treasury transactions should be separately subjected to concurrent audit by internal auditors and the results of their audit should be placed before the CMD of the bank once every month. Banks need not forward copies of the above mentioned concurrent audit reports to RBI of India. However, the major irregularities observed in these reports and the position of compliance thereto may be incorporated in the half yearly review of the investment portfolio.

1.2 Non- SLR investments

1.2.1

(i) Appraisal

Banks have made significant investment in privately placed unrated bonds and, in certain cases, in bonds issued by corporates who are not their borrowers. While assessing such investment proposals on private placement basis, in the absence of standardised and mandated disclosures, including credit rating, banks may not be in a position to conduct proper due diligence to take an investment decision. Thus, there could be deficiencies in the appraisal of privately placed issues.

(ii) Disclosure requirements in offer documents

The risk arising from inadequate disclosure in offer documents should be recognised and banks should prescribe minimum disclosure standards as a policy with Board approval. In this connection, RBI had constituted a Technical Group comprising officials drawn from treasury departments of a few banks and experts on corporate finance to study, *inter alia*, the methods of acquiring, by banks, of non-SLR investments in general and private placement route, in particular, and to suggest measures for regulating these investments. The Group had designed a format containing the minimum disclosure requirements as well as certain conditionalities regarding documentation and creation of charge for private placement issues, which may serve as a 'best practice model' for the banks. The details of the Group's recommendations are given

in the Annex III and banks should have a suitable format of disclosure requirements on the lines of the recommendations of the Technical Group with the approval of their Board.

(iii) Internal assessment

With a view to ensuring that the investments by banks in issues through private placement, both of the borrower customers and non-borrower customers, do not give rise to systemic concerns, it is necessary that banks should ensure that their investment policies duly approved by the Board of Directors are formulated after taking into account the following aspects:

(a) The Boards of banks should lay down policy and prudential limits on investments in bonds and debentures including cap and on private placement basis, sub limits for PSU bonds, corporate bonds, guaranteed bonds, issuer ceiling, etc.

(b) Investment proposals should be subjected to the same degree of credit risk analysis as any loan proposal. Banks should make their own internal credit analysis and rating even in respect of rated issues and should not entirely rely on the ratings of external agencies. The appraisal should be more stringent in respect of investments in instruments issued by non-borrower customers.

(c) Strengthen their internal rating systems which should also include building up of a system of regular (quarterly or half-yearly) tracking of the financial position of the issuer with a view to ensuring continuous monitoring of the rating migration of the issuers/issues.

(d) As a matter of prudence, banks should stipulate entry-level minimum ratings/ quality standards and industry-wise, maturity-wise, duration-wise, issuer-wise etc. limits to mitigate the adverse impacts of concentration and the risk of illiquidity.

(e) The banks should put in place proper risk management systems for capturing and analysing the risk in respect of these investments and taking remedial measures in time.

(iv) Some banks / FIs have not exercised due precaution by reference to the list of defaulters circulated / published by RBI while investing in bonds, debentures, etc., of companies. Banks may, therefore, exercise due caution, while taking any investment decision to subscribe to bonds, debentures, shares etc., and refer to the 'Defaulters List' to ensure that investments are

not made in companies / entities who are defaulters to banks / FIs. Some of the companies may be undergoing adverse financial position, turning their accounts to sub-standard category due to recession in their industry segment, like textiles. Despite restructuring facility provided under RBI guidelines, the banks have been reported to be reluctant to extend further finance, though considered warranted on merits of the case. Banks may not refuse proposals for such investments in companies whose director's name(s) find place in the 'Defaulter Companies List' circulated by RBI, at periodical intervals and particularly in respect of those loan accounts, which have been restructured under extant RBI guidelines, provided the proposal is viable and satisfies all parameters for such credit extension.

Prudential guidelines on investment in Non-SLR securities

1.2.2 Coverage

These guidelines cover banks' investments in non-SLR securities issued by corporates, banks, FIs and State and Central Government sponsored institutions, SPVs etc, including, capital gains bonds, bonds eligible for priority sector status. The guidelines will apply to investments both in the primary market as well as the secondary market.

1.2.3 The guidelines on listing and rating pertaining to non-SLR securities vide paragraphs 1.2.7 to 1.2.16 are not applicable to banks' investments in:

- (a) Securities directly issued by the Central and State Governments, which are not reckoned for SLR purposes.
- (b) Equity shares
- (c) Units of equity oriented mutual fund schemes, viz. those schemes where any part of the corpus can be invested in equity
- (d) Equity/debt instruments/Units issued by Venture capital funds
- (e) Commercial Paper
- (f) Certificates of Deposit

1.2.4 Definitions of a few terms used in these guidelines have been furnished in **Annex IV** with a view to ensure uniformity in approach while implementing the guidelines.

Regulatory requirements

1.2.5 Banks should not invest in Non-SLR securities of original maturity of less than one-year, other than Commercial Paper and Certificates of Deposits, which are covered under RBI guidelines.

1.2.6 Banks should undertake usual due diligence in respect of investments in non-SLR securities. Present RBI regulations preclude banks from extending credit facilities for certain purposes. Banks should ensure that such activities are not financed by way of funds raised through the non-SLR securities.

Listing and rating requirements

1.2.7 Banks must not invest in unrated non-SLR securities. However, the banks may invest in unrated bonds of companies engaged in infrastructure activities, within the ceiling of 10 per cent for unlisted non-SLR securities as prescribed vide paragraph 1.2.10 below.

1.2.8 The Securities Exchange Board of India (SEBI) vide their circular dated September 30, 2003(amended vide circular dated May 11, 2009) have stipulated requirements that listed companies are required to comply with, for making issue of debt securities on a private placement basis and listed on a stock exchange. According to this circular, any listed company, making issue of debt securities on a private placement basis and listed on a stock exchange, has to make full disclosures (initial and continuing) in the manner prescribed in Schedule II of the Companies Act 1956, SEBI (Disclosure and Investor Protection) Guidelines, 2000 and the Listing Agreement with the exchanges. Furthermore, the debt securities shall carry a credit rating of not less than investment grade from a Credit Rating Agency registered with the SEBI.

1.2.9 Accordingly, while making fresh investments in non-SLR debt securities, banks should ensure that such investment are made only in listed debt securities of companies which comply with the requirements of the SEBI circular dated September 30, 2003(amended vide circular dated May 11, 2009), except to the extent indicated in paragraph 1.2.10 and 1.2.11 below.

Fixing of prudential limits

1.2.10 Bank's investment in unlisted non-SLR securities should not exceed 10 per cent of its total investment in non-SLR securities as on March 31, of the previous year, and such investment should comply with the disclosure requirements as prescribed by the SEBI for listed companies. Further, as there is a time lag between issuance and listing of securities, investment in non-SLR debt securities (both primary and secondary market) by banks where the security is proposed to be listed on the Exchange(s) may be considered as investment in listed security at the time of making investment. However, if such security is not listed within the period specified, the same will be reckoned for the 10 per cent limit specified for unlisted non-SLR securities. In case such investments included under unlisted non-SLR securities lead to a breach of the 10 per cent limit, the bank would not be allowed to make further investment in non-SLR securities (both primary and secondary market) as also in unrated bonds issued by companies engaged in infrastructure activities till such time bank's investment in unlisted non-SLR securities comes within the limit of 10 per cent.

1.2.11 Bank's investment in unlisted non-SLR securities may exceed the limit of 10 per cent, by an additional 10 per cent, provided the investment is on account of investment in Securitisation papers issued for infrastructure projects, and bonds/debentures issued by Securitisation Companies (SCs) and Reconstruction Companies (RCs) set up under the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFEASI Act) and registered with RBI. In other words, investments exclusively in securities specified in this paragraph could be up to the maximum permitted limit of 20 per cent of non-SLR investment.

1.2.12 Investment in the following will not be reckoned as 'unlisted non-SLR securities' for computing compliance with the prudential limits prescribed in the above guidelines:

- (i)** Security Receipts issued by SCs / RCs registered with RBI.
- (ii)** Investment in Asset Backed Securities (ABS) and Mortgage Backed Securities (MBS), which are rated at or above the minimum investment grade. However, there will be close monitoring of exposures to ABS on a bank specific basis based on monthly reports to be submitted to RBI as per proforma being separately advised by the Department of Banking Supervision.

(iii) Investments in unlisted convertible debentures. However, investments in these instruments would be treated as “Capital Market Exposure”.

1.2.13 The investments in RIDF / SIDBI/RHDF Deposits may not be reckoned as part of the numerator as well as denominator for computing compliance with the prudential limit of 10 per cent of its total non-SLR securities as on March 31, of the previous year.

1.2.14 With effect from January 1, 2005, only investment in units of such mutual fund schemes, which have an exposure to unlisted securities of less than 10 per cent of the corpus of the fund, will be treated on par with listed securities for the purpose of compliance with the prudential limits prescribed in the above guidelines. While computing the exposure to the unlisted securities for compliance with the norm of less than 10 percent of the corpus of the mutual fund scheme, Treasury Bills, Collateralised Borrowing and Lending Obligations (CBLO), Repo/Reverse Repo and Bank Fixed Deposits may not be included in the numerator.

1.2.15 For the purpose of the prudential limits prescribed in the guidelines, the denominator viz., 'non-SLR investments', would include investment under the following four categories in Schedule 8 to the balance sheet viz., 'shares', 'bonds & debentures', 'subsidiaries/joint ventures' and 'others'.

1.2.16 Banks whose investment in unlisted non-SLR securities are within the prudential limit of 10 per cent of its total non-SLR securities as on March 31, of the previous year may make fresh investment in such securities and up to the prudential limits.

Role of Boards

1.2.17 Banks should ensure that their investment policies duly approved by the Board of Directors are formulated after taking into account all the relevant issues specified in these guidelines on investment in non-SLR securities. Banks should put in place proper risk management systems for capturing and analysing the risk in respect of non-SLR investment and taking remedial measures in time. Banks should also put in place appropriate systems to ensure that investment in privately placed instruments is made in accordance with the systems and procedures prescribed under respective bank's investment policy.

1.2.18 Boards of banks should review the following aspects of non-SLR investment at least at quarterly intervals:

- a) Total business (investment and divestment) during the reporting period.
- b) Compliance with the prudential limits prescribed by the Board for non-SLR investment.
- c) Compliance with the prudential guidelines issued by RBI on non-SLR securities.
- d) Rating migration of the issuers/ issues held in the bank's books and consequent diminution in the portfolio quality.
- e) Extent of non-performing investments in the non-SLR category.

Disclosures

1.2.19 In order to help in the creation of a central database on private placement of debt, a copy of all offer documents should be filed with the Credit Information Bureau (India) Ltd. (CIBIL) by the investing banks. Further, any default relating to interest/ instalment in respect of any privately placed debt should also be reported to CIBIL by the investing banks along with a copy of the offer document.

1.2.20 Banks should disclose the details of the issuer composition of non-SLR investments and the non-performing non-SLR investments in the 'Notes on Accounts' of the balance sheet, as indicated in **Annex V**.

1.2.21 Trading and Settlement in Corporate Debt Securities

As per the SEBI guidelines, all trades with the exception of the spot transactions, in a listed debt security, shall be executed only on the trading platform of a stock exchange. In addition to complying with the SEBI guidelines, banks should ensure that all spot transactions in listed and unlisted debt securities are reported on the NDS and settled through the CCIL from a date to be notified by RBI.

All OTC trades in corporate bonds shall necessarily be cleared and settled through the NSCCL or ICCL as per the norms specified by the NSCCL and the ICCL from time to time, with effect from December 01, 2009.

1.2.22 Repo in Corporate Debt Securities

Eligible entities as per detailed guidelines given in Annex I-E can undertake repo in corporate debt securities which are rated 'AA' or above by the rating agencies, that are held in the security account of the repo seller, in demat form. However, Commercial Papers (CPs), Certificates of Deposit (CDs) and other instruments including Non-Convertible Debentures (NCDs) of less than one year of original maturity, shall not be eligible securities for undertaking repo in corporate debt securities.

1.2.23 Limits on Banks' Exposure to Capital Markets

A. Solo Basis

The aggregate exposure of a bank to the capital markets in all forms (both fund based and non-fund based) should not exceed 40 per cent of its net worth as on March 31 of the previous year. Within this overall ceiling, the bank's direct investment in shares, convertible bonds / debentures, units of equity-oriented mutual funds and all exposures to Venture Capital Funds (VCFs) [both registered and unregistered] should not exceed 20 per cent of its net worth.

B Consolidated Basis

The aggregate exposure of a consolidated bank to capital markets (both fund based and non-fund based) should not exceed 40 per cent of its consolidated net worth as on March 31 of the previous year. Within this overall ceiling, the aggregate direct exposure by way of the consolidated bank's investment in shares, convertible bonds / debentures, units of equity-oriented mutual funds and all exposures to Venture Capital Funds (VCFs) [both registered and unregistered] should not exceed 20 per cent of its consolidated net worth.

The above-mentioned ceilings are the maximum permissible and a bank's Board of Directors is free to adopt a lower ceiling for the bank, keeping in view its overall risk profile and corporate strategy. Banks are required to adhere to the ceilings on an ongoing basis.

1.3 General

1.3.1 Reconciliation of holdings of Govt. securities – Audit Certificate

Banks should furnish a 'Statement of the Reconciliation of Bank's Investments (held in own Investment account, as also under PMS)', as at the end of every accounting year duly certified by the bank's auditors. The statement should reach the Regional Office of the DBS, RBI, under

whose jurisdiction the bank's head office is located within one month from the close of the accounting year. Banks in the letters of appointment, issued to their external auditors, may suitably include the aforementioned requirement of reconciliation. The format for the statement and the instructions for compiling thereto are given in **Annex VI**.

1.3.2 Transactions in securities - Custodial functions

While exercising the custodial functions on behalf of their merchant banking subsidiaries, these functions should be subject to the same procedures and safeguards as would be applicable to other constituents. Accordingly, full particulars should be available with the subsidiaries of banks of the manner in which the transactions have been executed. Banks should also issue suitable instructions in this regard to the department/office undertaking the custodial functions on behalf of their subsidiaries.

1.3.3 Portfolio Management on behalf of clients

i) The general powers vested in banks to operate PMS and similar schemes have been withdrawn. No bank should, therefore, restart or introduce any new PMS or similar scheme in future without obtaining specific prior approval of the RBI. However, bank-sponsored NBFCs are allowed to offer discretionary PMS to their clients, on a case-to-case basis. Applications in this regard should be submitted to the Department of Banking Operations and Development (DBOD), RBI, World Trade Centre, Mumbai – 400 005.

ii) The following conditions are to be strictly observed by the banks operating PMS or similar scheme with the specific prior approval of RBI:

(a) PMS should be entirely at the customer's risk, without guaranteeing, either directly or indirectly, a pre-determined return.

(b) Funds should not be accepted for portfolio management for a period less than one year.

(c) Portfolio funds should not be deployed for lending in call/notice money; inter-bank term deposits and bills rediscounting markets and lending to/placement with corporate bodies.

(d) Banks should maintain client wise account/record of funds accepted for management and investments made there against and the portfolio clients should be entitled to get a statement of account.

(e) Bank's own investments and investments belonging to PMS clients should be kept distinct from each other, and any transactions between the bank's investment account and client's portfolio account should be strictly at market rates.

(f) There should be a clear functional separation of trading and back office functions relating to banks' own investment accounts and PMS clients' accounts.

iii) PMS clients' accounts should be subjected by banks to a separate audit by external auditors as covered in paragraph 1.1.5 (a).

iv) Banks should note that violation of RBI instructions will be viewed seriously and will invite deterrent action against the banks, which will include raising of reserve requirements, withdrawal of facility of refinance from the RBI and denial of access to money markets, apart from prohibition from undertaking PMS activity.

v) Further, the aforesaid instructions will apply, *mutatis mutandis*, to the subsidiaries of banks except where they are contrary to specific regulations of the RBI or SEBI, governing their operations.

vi) Banks / merchant banking subsidiaries of banks operating PMS or similar scheme with the specific prior approval of the RBI are also required to comply with the guidelines contained in the SEBI (Portfolio Managers) Rules and Regulations, 1993 and those issued from time to time.

1.3.4 Investment Portfolio of bank - transactions in Government Securities

In the light of fraudulent transactions in the guise of Government securities, transactions in physical format by a few co-operative banks with the help of some broker entities, it has been decided to accelerate the measures for further reducing the scope of trading in physical forms. These measures are as under:

(i) For banks, which do not have SGL account with RBI, only one gilt account can be opened.

(ii) In case the gilt accounts are opened with a scheduled commercial bank, the account holder has to open a designated funds account (for all gilt account related transactions) with the same bank.

(iii) The entities maintaining the gilt / designated funds accounts will be required to ensure availability of clear funds in the designated funds accounts for purchases and of sufficient securities in the gilt account for sales before putting through the transactions.

(iv) No transactions by the bank should be undertaken in physical form with any broker.

(v) Banks should ensure that brokers approved for transacting in Government securities are registered with the debt market segment of NSE/BSE/OTCEI.

2. Classification

i) The entire investment portfolio of the banks (including SLR securities and non-SLR securities) should be classified under three categories

viz. 'Held to Maturity',
'Available for Sale' and
'Held for Trading'.

- However, in the balance sheet, the investments will continue to be disclosed as per the existing six classifications:

viz. a) Government securities,
b) Other approved securities,
c) Shares,
d) Debentures & Bonds,
e) Subsidiaries/ joint ventures and
f) Others (CP, Mutual Fund Units, etc.).

ii) Banks should decide the category of the investment at the time of acquisition and the decision should be recorded on the investment proposals.

2.1 Held to Maturity

- i) The securities acquired by the banks with the intention to hold them up to maturity will be classified under 'Held to Maturity (HTM)'.
- ii) Banks are allowed to include investments included under HTM category upto 25 per cent of their total investments.

The following investments are required to be classified under HTM but are not accounted for the purpose of ceiling of 25 per cent specified for this category:

- (a) Re-capitalisation bonds received from the Government of India towards their re-capitalisation requirement and held in their investment portfolio. This will not include re-capitalisation bonds of other banks acquired for investment purposes.
 - (b) Investment in subsidiaries and joint ventures (A Joint Venture would be one in which the bank, along with its subsidiaries, holds more than 25 percent of the equity).
 - (c) Investment in the long-term bonds (with a minimum residual maturity of seven years) issued by companies engaged in infrastructure activities
- iii) Banks are, however, allowed since September 2, 2004 to exceed the limit of 25 percent of total investment under HTM category provided:
 - (a) the excess comprises only of SLR securities, **and**
 - (b) the total SLR securities held in the HTM is not more than 25 percent of their DTL as on the last Friday of the second preceding fortnight.
- iv) The non-SLR securities, held as part of HTM as on September 2, 2004 may remain in that category. No fresh non-SLR securities, are permitted to be included in HTM, except the following:
 - (a) Fresh re-capitalisation bonds received from the Government of India, towards their re-capitalisation requirement and held in their investment portfolio. This will not include re-capitalisation bonds of other banks acquired for investment purposes.
 - (b) Fresh investment in the equity of subsidiaries and joint ventures.
 - (c) RIDF / SIDBI/RHDF deposits.
 - (d) Investment in long-term bonds (with a minimum residual maturity of seven years) issued by companies engaged in infrastructure activities.
- v) To sum up, banks may hold the following securities under HTM:
 - (a) SLR Securities upto 25 percent of their DTL as on the last Friday of the second preceding fortnight.

(b) Non-SLR securities included under HTM as on September 2, 2004.

(c) Fresh re-capitalisation bonds received from the Government of India towards their re-capitalisation requirement and held in Investment portfolio.

(d) Fresh investment in the equity of subsidiaries and joint ventures

(e) RIDF/SIDBI/RHDF deposits.

(f) Investment in long-term bonds (with a minimum residual maturity of seven years) issued by companies engaged in infrastructure activities

(vi) Profit on sale of investments in this category should be first taken to the Profit & Loss Account, and thereafter be appropriated to the 'Capital Reserve Account'. It is clarified that the amount so appropriated would be net of taxes and amount required to be transferred to Statutory Reserves. Loss on sale will be recognised in the Profit & Loss Account. As regards, the 'Special Reserves' created by banks under Section 36(1) (viii) of Income Tax Act, 1961, only the net amount of such Reserves (net of tax payable) should be taken into account for the purpose of Tier-I capital.

(vii) The debentures/ bonds must be treated in the nature of an advance when:

- The debenture/bond is issued as part of the proposal for project finance and the tenure of the debenture is for a period of three years and above

Or

The debenture/bond is issued as part of the proposal for working capital finance and the tenure of the debenture/ bond is less than a period of one year

And

- the bank has a significant stake i.e.10% or more in the issue

And

- the issue is part of a private placement, i.e. the borrower has approached the bank/FI and not part of a public issue where the bank/FI has subscribed in response to an invitation.

Since, no fresh non-SLR securities are permitted to be included in the HTM, these investments should not be held under HTM category and they should be subjected to mark- to-market

discipline. They would be subjected to prudential norms for identification of non-performing investment and provisioning as applicable to investments.

2.2 Available for Sale & Held for Trading

- i) The securities acquired by the banks with the intention to trade by taking advantage of the short-term price/interest rate movements will be classified under 'Held for Trading (HFT)'.
- ii) The securities which do not fall within the above two categories will be classified under 'Available for Sale (AFS)'.
- iii) The banks will have the freedom to decide on the extent of holdings under HFT and AFS. This will be decided by them after considering various aspects such as basis of intent, trading strategies, risk management capabilities, tax planning, manpower skills, capital position.
- iv) The investments classified under HFT would be those from which the bank expects to make a gain by the movement in the interest rates/market rates. These securities are to be sold within 90 days.
- v) Profit or loss on sale of investments in both the categories will be taken to the Profit & Loss Account.

2.3 Shifting among categories

- i) Banks may shift investments to/from HTM with the approval of the Board of Directors once a year. Such shifting will normally be allowed at the beginning of the accounting year. No further shifting to/from HTM will be allowed during the remaining part of that accounting year.
- ii) Banks may shift investments from AFS to HFT with the approval of their Board of Directors/ ALCO/ Investment Committee. In case of exigencies, such shifting may be done with the approval of the Chief Executive of the bank/Head of the ALCO, but should be ratified by the Board of Directors/ ALCO.

iii) Shifting of investments from HFT to AFS is generally not allowed. However, it will be permitted only under exceptional circumstances like not being able to sell the security within 90 days due to tight liquidity conditions, or extreme volatility, or market becoming unidirectional. Such transfer is permitted only with the approval of the Board of Directors/ ALCO/ Investment Committee.

iv) Transfer of scrips from AFS / HFT category to HTM category should be made at the lower of book value or market value. In other words, in cases where the market value is higher than the book value at the time of transfer, the appreciation should be ignored and the security should be transferred at the book value. In cases where the market value is less than the book value, the provision against depreciation held against this security (including the additional provision, if any, required based on valuation done on the date of transfer) should be adjusted to reduce the book value to the market value and the security should be transferred at the market value.

In the case of transfer of securities from HTM to AFS / HFT category,

(a) If the security was originally placed under the HTM category at a discount, it may be transferred to AFS / HFT category at the acquisition price / book value. (It may be noted that as per existing instructions banks are not allowed to accrue the discount on the securities held under HTM category and, therefore, such securities would continue to be held at the acquisition cost till maturity). After transfer, these securities should be immediately re-valued and resultant depreciation, if any, may be provided.

(b) If the security was originally placed in the HTM category at a premium, it may be transferred to the AFS / HFT category at the amortised cost. After transfer, these securities should be immediately re-valued and resultant depreciation, if any, may be provided.

In the case of transfer of securities from AFS to HFT category or vice-versa, the securities need not be re-valued on the date of transfer and the provisions for the accumulated depreciation, if any, held may be transferred to the provisions for depreciation against the HFT securities and vice-versa.

3. Valuation

3.1 Held to Maturity

i) Investments classified under HTM need not be marked to market and will be carried at acquisition cost, unless it is more than the face value, in which case the premium should be amortised over the period remaining to maturity. The banks should reflect the amortised amount in 'Schedule 13 – Interest Earned : Item II – Income on Investments', as a deduction. However, the deduction need not be disclosed separately. The book value of the security should continue to be reduced to the extent of the amount amortised during the relevant accounting period.

ii) Banks should recognise any diminution, other than temporary, in the value of their investments in subsidiaries/ joint ventures, which are included under HTM and provide therefore. Such diminution should be determined and provided for each investment individually.

3.2 Available for Sale

The individual scrips in the Available for Sale category will be marked to market at quarterly or at more frequent intervals. Domestic Securities under this category shall be valued scrip-wise and depreciation/ appreciation shall be aggregated for each classification referred to in item 2(i) above and foreign investments under this category shall be valued scrip-wise and depreciation/ appreciation shall be aggregated for five classifications (viz. Government securities (including local authorities), Shares, Debentures & Bonds, Subsidiaries and/or joint ventures abroad and Other investments (to be specified)). Further, the investment in a particular classification, both in domestic and foreign securities, may be aggregated for the purpose of arriving at net depreciation/appreciation of investments under that category. Net depreciation, if any, shall be provided for. Net appreciation, if any, should be ignored. Net depreciation required to be provided for in any one classification should not be reduced on account of net appreciation in any other classification. The banks may continue to report the foreign securities under three categories (Government securities (including local authorities), Subsidiaries and/or joint ventures abroad and other investments (to be specified)) in the balance sheet. The book value of the individual securities would not undergo any change after the marking of market.

3.3 Held for Trading

The individual scrips in the Held for Trading category will be marked to market at monthly or at more frequent intervals and provided for as in the case of those in the Available for Sale category. Consequently, the book value of the individual securities in this category would also not undergo any change after marking to market.

3.4 Investment Fluctuation Reserve

(i) With a view to building up of adequate reserves to guard against any possible reversal of interest rate environment in future due to unexpected developments, banks were advised to build up Investment Fluctuation Reserve (IFR) of a minimum 5 per cent of the investment portfolio within a period of 5 years.

(ii) To ensure smooth transition to Basel II norms, banks were advised in June 24, 2004 to maintain capital charge for market risk in a phased manner over a two year period, as under:

(a) In respect of securities included in the HFT category, open gold position limit, open foreign exchange position limit, trading positions in derivatives and derivatives entered into for hedging trading book exposures by March 31, 2005, and

(b) In respect of securities included in the AFS category by March 31, 2006.

(iii) With a view to encourage banks for early compliance with the guidelines for maintenance of capital charge for market risks, it was advised in April 2005 that banks which have maintained capital of at least 9 per cent of the risk weighted assets for both credit risk and market risks for both HFT (items as indicated at (a) above) and AFS category may treat the balance in excess of 5 per cent of securities included under HFT and AFS categories, in the IFR, as Tier I capital. Banks satisfying the above were allowed to transfer the amount in excess of the said 5 per cent in the IFR to Statutory Reserve.

(iv) Banks were advised in October 2005 that, if they have maintained capital of at least 9 per cent of the risk weighted assets for both credit risk and market risks for both

HFT (items as indicated at (a) above) and AFS category as on March 31, 2006, they would be permitted to treat the entire balance in the IFR as Tier I capital. For this purpose, banks may transfer the balance in the Investment Fluctuation Reserve 'below the line' in the Profit and Loss Appropriation Account to Statutory Reserve, General Reserve or balance of Profit & Loss Account.

Investment Reserve Account (IRA)

(v) In the event, provisions created on account of depreciation in the 'AFS' or 'HFT' categories are found to be in excess of the required amount in any year, the excess should be credited to the Profit & Loss account and an equivalent amount (net of taxes, if any and net of transfer to Statutory Reserves as applicable to such excess provision) should be appropriated to an IRA Account in Schedule 2 – "Reserves & Surplus" under the head "Revenue and other Reserves", and would be eligible for inclusion under Tier-II within the overall ceiling of 1.25 per cent of total Risk Weighted Assets prescribed for General Provisions/ Loss Reserves.

(vi) Banks may utilise IRA as follows:

The provisions required to be created on account of depreciation in the AFS and HFT categories should be debited to the P&L Account and an equivalent amount (net of tax benefit, if any, and net of consequent reduction in the transfer to Statutory Reserve), may be transferred from the IRA to the P&L Account.

Illustratively, banks may draw down from the IRA to the extent of provision made during the year towards depreciation in investment in AFS and HFT categories (net of taxes, if any, and net of transfer to Statutory Reserves as applicable to such excess provision). In other words, a bank which pays a tax of 30% and should appropriate 25% of the net profits to Statutory Reserves, can draw down Rs.52.50 from the IRA, if the provision made for depreciation in investments included in the AFS and HFT categories is Rs.100.

(vii) The amounts debited to the P&L Account for provision should be debited under the head 'Expenditure - Provisions & Contingencies'. The amount transferred from the IRA to the P&L Account, should be shown as 'below the line' item in the Profit and Loss Appropriation Account, after determining the profit for the year. Provision towards any erosion in the value of an asset is an item of charge on the profit and loss account, and hence should appear in that account before arriving at the profit for the accounting

period. Adoption of the following would not only be adoption of a wrong accounting principle but would, also result in a wrong statement of the profit for the accounting period:

(a) the provision is allowed to be adjusted directly against an item of Reserve without being shown in the profit and loss account, **OR**

(b) a bank is allowed to draw down from the IRA before arriving at the profit for the accounting period (i.e., above the line), **OR**

(c) a bank is allowed to make provisions for depreciation on investment as a below the line item, after arriving at the profit for the period,

Hence none of the above options are permissible.

(viii) In terms of our guidelines on payment of dividend by banks, dividends should be payable only out of current year's profit. The amount drawn down from the IRA will, therefore, not be available to a bank for payment of dividend among the shareholders. However, the balance in the IRA transferred 'below the line' in the Profit and Loss Appropriation Account to Statutory Reserve, General Reserve or balance of Profit & Loss Account would be eligible to be reckoned as Tier I capital.

3.5 Market value

The 'market value' for the purpose of periodical valuation of investments included in the AFS and HFT would be the market price of the scrip as available from the trades/ quotes on the stock exchanges, SGL account transactions, price list of RBI, prices declared by Primary Dealers Association of India (PDAI) jointly with the Fixed Income Money Market and Derivatives Association of India (FIMMDA) periodically. In respect of unquoted securities, the procedure as detailed below should be adopted.

3.6 Unquoted SLR securities

3.6.1 Central Government Securities

i) Banks should value the unquoted Central Government securities on the basis of the prices/ YTM rates put out by the PDAI/ FIMMDA at periodical intervals.

ii) The 6.00 per cent Capital Indexed Bonds may be valued at "cost", as defined in circular DBOD.No.BC.8/12.02.001/ 97-98 dated January 22, 1998 and BC.18/12.02.001/ 2000-2001 dated August 16, 2000.

iii) Treasury Bills should be valued at carrying cost.

3.6.2 State Government Securities

State Government securities will be valued applying the YTM method by marking it up by 25 basis points above the yields of the Central Government Securities of equivalent maturity put out by PDAI/ FIMMDA periodically.

3.6.3 Other 'approved' Securities

Other approved securities will be valued applying the YTM method by marking it up by 25 basis points above the yields of the Central Government Securities of equivalent maturity put out by PDAI/ FIMMDA periodically.

3.7 Unquoted Non-SLR securities

3.7.1 Debentures/ Bonds

All debentures/ bonds should be valued on the YTM basis. Such debentures/ bonds may be of different companies having different ratings. These will be valued with appropriate mark-up over the YTM rates for Central Government securities as put out by PDAI/ FIMMDA periodically. The mark-up will be graded according to the ratings assigned to the debentures/ bonds by the rating agencies subject to the following: -

(a) The rate used for the YTM for rated debentures/ bonds should be at least 50 basis points above the rate applicable to a Government of India loan of equivalent maturity.

NOTE:

The special securities, which are directly issued by Government of India to the beneficiary entities, which do not carry SLR status, may be valued at a spread of 25 basis points above the corresponding yield on Government of India securities, with effect from the financial year 2008 - 09. At present, such special securities comprise: Oil Bonds, Fertiliser Bonds, bonds issued to the State Bank of India (during the recent rights issue), Unit Trust of India, Industrial Finance Corporation of India Ltd., Food Corporation of India, Industrial Investment Bank of India Ltd., the erstwhile Industrial Development Bank of India and the erstwhile Shipping Development Finance Corporation.

(b) The rate used for the YTM for unrated debentures/ bonds should not be less than the rate applicable to rated debentures/ bonds of equivalent maturity. The mark-up for the unrated debentures/ bonds should appropriately reflect the credit risk borne by the bank.

(c) Where the debenture/ bonds is quoted and there have been transactions within 15 days prior to the valuation date, the value adopted should not be higher than the rate at which the transaction is recorded on the stock exchange.

3.7.2 Zero coupon bonds (ZCBs)

ZCBs should be shown in the books at carrying cost, i.e., acquisition cost plus discount accrued at the rate prevailing at the time of acquisition, which may be marked to market with reference to the market value. In the absence of market value, the ZCBs may be marked to market with reference to the present value of the ZCB. The present value of the ZCBs may be calculated by discounting the face value using the 'Zero Coupon Yield Curve', with appropriate mark up as per the zero coupon spreads put out by FIMMDA periodically. In case the bank is still carrying the ZCBs at acquisition cost, the discount accrued on the instrument should be notionally added to the book value of the scrip, before marking it to market.

3.7.3 Preference Shares

The valuation of preference shares should be on YTM basis. The preference shares will be issued by companies with different ratings. These will be valued with appropriate mark-up over the YTM rates for Central Government securities put out by the PDAI/FIMMDA periodically. The mark-up will be graded according to the ratings assigned to the preference shares by the rating agencies subject to the following:

- a) The YTM rate should not be lower than the coupon rate/ YTM for a GOI loan of equivalent maturity.
- b) The rate used for the YTM for unrated preference shares should not be less than the rate applicable to rated preference shares of equivalent maturity. The mark-up for the unrated preference shares should appropriately reflect the credit risk borne by the bank.
- c) Investments in preference shares as part of the project finance may be valued at par for a period of two years after commencement of production or five years after subscription whichever is earlier.
- d) Where investment in preference shares is as part of rehabilitation, the YTM rate should not be lower than 1.5% above the coupon rate/ YTM for GOI loan of equivalent maturity.

- e) Where preference dividends are in arrears, no credit should be taken for accrued dividends and the value determined on YTM should be discounted by at least 15% if arrears are for one year, and more if arrears are for more than one year. The depreciation/provision requirement arrived at in the above manner in respect of non-performing shares where dividends are in arrears shall not be allowed to be set-off against appreciation on other performing preference shares.
- f) The preference share should not be valued above its redemption value.
- g) When a preference share has been traded on stock exchange within 15 days prior to the valuation date, the value should not be higher than the price at which the share was traded.

3.7.4 Equity Shares

The equity shares in the bank's portfolio should be marked to market preferably on a daily basis, but at least on a weekly basis. Equity shares for which current quotations are not available or where the shares are not quoted on the stock exchanges, should be valued at break-up value (without considering 'revaluation reserves', if any) which is to be ascertained from the company's latest balance sheet (which should not be more than one year prior to the date of valuation). In case the latest balance sheet is not available the shares are to be valued at Re.1 per company.

3.7.5 Mutual Funds Units (MF Units)

Investment in quoted MF Units should be valued as per Stock Exchange quotations. Investment in un-quoted MF Units is to be valued on the basis of the latest re-purchase price declared by the MF in respect of each particular Scheme. In case of funds with a lock-in period, where repurchase price/ market quote is not available, Units could be valued at Net Asset Value (NAV). If NAV is not available, then these could be valued at cost, till the end of the lock-in period. Wherever the re-purchase price is not available, the Units could be valued at the NAV of the respective scheme.

3.7.6 Commercial Paper

Commercial paper should be valued at the carrying cost.

3.7.7 Investments in Regional Rural Banks (RRBs)

Investment in RRBs is to be valued at carrying cost (i.e. book value) on a consistent basis.

3.8. Investment in securities issued by SC/RC

When banks / FIs invest in the SRs / Pass-Through Certificates (PTCs) issued by SCs / RCs, in respect of the financial assets sold by them to the SCs / RCs, the sale shall be recognised in books of the banks / FIs at the lower of:

- the redemption value of the SRs /PTCs, and
- the net book value (NBV) (i.e. Book value less provisions held), of the financial asset.

The above investment should be carried in the books of the bank / FI at the price as determined above until its sale or realisation, and on such sale or realisation, the loss or gain must be dealt with as under:

(i) if the sale to SC /RC is at a price below the NBV, the shortfall should be debited to the profit and loss account of that year.

(ii) If the sale is for a value higher than the NBV, the excess provision will not be reversed but will be utilised to meet the shortfall / loss on account of sale of other financial assets to SC / RC. All instruments received by banks / FIs from SC / RC as sale consideration for financial assets sold to them and also other instruments issued by SC / RC in which banks / FIs invest will be in the nature of non-SLR securities. Accordingly, the valuation, classification and other norms applicable to investment in non-SLR instruments prescribed by RBI from time to time would be applicable to bank's / FI's investment in debentures / bonds / security receipts / PTCs issued by SC / RC. However, if any of the above instruments issued by SC / RC is limited to the actual realisation of the financial assets assigned to the instruments in the concerned scheme the bank / FI shall reckon the Net Asset Value (NAV), obtained from SC / RC from time to time, for valuation of such investments.

3.9. Valuation and classification of banks' investment in VCFs

3.9.1 The quoted equity shares / bonds/ units of VCFs in the bank's portfolio should be held under AFS and marked to market preferably on a daily basis, but at least on a weekly basis, in line with valuation norms for other equity shares as per existing instructions.

3.9.2 Banks' investments in unquoted shares/bonds/units of VCFs made after August 23, 2006 (i.e issuance of guidelines on valuation, classification of investments in VCFs) will be classified under HTM for initial period of three years and will be valued at cost during this period. For the investments made before issuance of these guidelines, the classification would be done as per the existing norms.

3.9.3 For this purpose, the period of three years will be reckoned separately for each disbursement made by the bank to VCF as and when the committed capital is called up. However, to ensure conformity with the existing norms for transferring securities from HTM, transfer of all securities which have completed three years as mentioned above will be effected at the beginning of the next accounting year in one lot to coincide with the annual transfer of investments from HTM category.

3.9.4 After three years, the unquoted units/shares/bonds should be transferred to AFS category and valued as under:

i) Units: In the case of investments in the form of units, the valuation will be done at the NAV shown by the VCF in its financial statements. Depreciation, if any, on the units based on NAV has to be provided at the time of shifting the investments to AFS category from HTM category as also on subsequent valuations which should be done at quarterly or more frequent intervals based on the financial statements received from the VCF. At least once in a year, the units should be valued based on the audited results. However, if the audited balance sheet/ financial statements showing NAV figures are not available continuously for more than 18 months as on the date of valuation, the investments are to be valued at Rupee 1.00 per VCF.

ii) Equity: In the case of investments in the form of shares, the valuation can be done at the required frequency based on the break-up value (without considering 'revaluation reserves', if any) which is to be ascertained from the company's (VCF's) latest balance sheet (which should not be more than 18 months prior to the date of valuation).

Depreciation, if any on the shares has to be provided at the time of shifting the investments to AFS category as also on subsequent valuations which should be done at quarterly or more frequent intervals. If the latest balance sheet available is more than 18 months old, the shares are to be valued at Rupee.1.00 per company.

(iii) Bonds: The investment in the bonds of VCFs, if any, should be valued as per prudential norms for classification, valuation and operation of investment portfolio by banks issued by RBI from time to time.

3.9.5 Valuation norms on conversion of outstanding

(a) Equity, debentures and other financial instruments acquired by way of conversion of outstanding principal and / or interest should be classified in the AFS category, and valued in accordance with the extant instructions on valuation of banks' investment portfolio, except to the extent that (a) equity may be valued as per market value, if quoted, (b) in cases, where equity is not quoted, valuation may be at breakup value in respect of standard assets and in respect of substandard / doubtful assets, equity may be initially valued at Re1 and at breakup value after restoration / up gradation to standard category.

3.10 Non-Performing Investments (NPI)

3.10.1 In respect of securities included in any of the three categories where interest/ principal is in arrears, the banks should not reckon income on the securities and should also make appropriate provisions for the depreciation in the value of the investment. The banks should not set-off the depreciation requirement in respect of these non-performing securities against the appreciation in respect of other performing securities.

3.10.2 An NPI, similar to a non performing advance (NPA), is one where:

- (i)** Interest/ installment (including maturity proceeds) is due and remains unpaid for more than 90 days.
- (ii)** The above would apply mutatis-mutandis to preference shares where the fixed dividend is not paid.
- (iii)** In the case of equity shares, in the event the investment in the shares of any company is valued at Re.1 per company on account of the non availability of the latest balance sheet in accordance with the instructions contained in paragraph 28 of the Annex to the circular DBOD.BP.BC.32/ 21.04.048/ 2000-01 dated October 16, 2000, those equity shares would also be reckoned as NPI.

- (iv) If any credit facility availed by the issuer is NPA in the books of the bank, investment in any of the securities, including preference shares issued by the same issuer would also be treated as NPI and vice versa. However, if only the preference shares are classified as NPI, the investment in any of the other performing securities issued by the same issuer may not be classified as NPI and any performing credit facilities granted to that borrower need not be treated as NPA.
- (v) The investments in debentures / bonds, which are deemed to be in the nature of advance would also be subjected to NPI norms as applicable to investments.
- (vi) In case of conversion of principal and / or interest into equity, debentures, bonds, etc., such instruments should be treated as NPA abinitio in the same asset classification category as the loan if the loan's classification is substandard or doubtful on implementation of the restructuring package and provision should be made as per the norms.

3.10.3 State Government guaranteed investments

For the year ending March 31, 2005, investment in State Government guaranteed securities would attract prudential norms for identification of NPI and provisioning, if interest and/or principal or any other amount due to the bank remains overdue for more than 180 days. With effect from the year ending March 31, 2006, investment in State Government guaranteed securities, including those in the nature of 'deemed advance', will attract prudential norms for identification of non- performing investments and provisioning, when interest/ instalment of principal (including maturity proceeds) or any other amount due to the bank remains unpaid for more than 90 days.

4. Uniform accounting for Repo / Reverse Repo transactions

4.1 The revised accounting guidelines effective from April 1, 2010 are applicable to market repo transactions in government securities and corporate debt securities. These accounting norms will, however, not apply to repo / reverse repo transactions conducted under the Liquidity Adjustment Facility (LAF) with RBI.

4.2 Market participants may undertake repos from any of the three categories of investments, viz., **Held For Trading, Available For Sale and Held To Maturity**.

4.3 The economic essence of a repo transaction, viz., borrowing (lending) of funds by selling (purchasing) securities shall be reflected in the books of the repo participants, by accounting the same as collateralized lending and borrowing transaction, with an agreement to repurchase, on the agreed terms. Accordingly, the repo seller, i.e., borrower of funds in the first leg, shall not exclude the securities sold under repo but continue to carry the same in his

investment account (please see the illustration given in the Annex) reflecting his continued economic interest in the securities during the repo period. On the other hand, the repo buyer, i.e., lender of funds in the first leg, shall not include the securities purchased under repo in his investment account but show it in a separate sub-head (please see the Annex). The securities would, however, be transferred from the repo seller to repo buyer as in the case of normal outright sale/purchase transactions and such movement of securities shall be reflected using the Repo/Reverse Repo Accounts and contra entries. In the case of repo seller, the Repo Account is credited in the first leg for the securities sold (funds received), while the same is reversed when the securities are repurchased in the second leg. Similarly, in the case of repo buyer, the Reverse Repo Account is debited for the amount of securities purchased (funds lent) and the same is reversed in the second leg when the securities are sold back.

4.4 The first leg of the repo transaction should be contracted at the prevailing market rates. The reversal (second leg) of the transaction shall be such that the difference between the consideration amounts of first and second legs should reflect the repo interest.

4.5 The accounting principles to be followed while accounting for repo / reverse repo transactions are as under:

(i) Coupon /Discount

The repo seller shall continue to accrue the coupon/discount on the securities sold under repo even during the repo period while the repo buyer shall not accrue the same.

In case the interest payment date of the security offered under repo falls within the repo period, the coupons received by the buyer of the security should be passed on to the seller of the security on the date of receipt as the cash consideration payable by the seller in the second leg does not include any intervening cash flows.

(ii) Repo Interest Income / Expenditure

After the second leg of the repo / reverse repo transaction is over, the difference between consideration amounts of the first leg and second leg of the repo shall be reckoned as Repo Interest Income / Expenditure in the books of the repo buyer / seller respectively ; and

the balance outstanding in the Repo Interest Income / Expenditure account should be transferred to the Profit and Loss account as an income or an expenditure . As regards repo / reverse repo transactions *outstanding on the balance sheet date*, only the accrued income / expenditure *till the balance sheet date* should be taken to the Profit and Loss account. Any

repo income / expenditure for the remaining period should be reckoned for the next accounting period.

(iii) Marking to Market

The repo seller shall continue to mark to market the securities sold under repo transactions as per the *investment classification of the security*. To illustrate, in case the securities sold by banks under repo transactions are out of the **Available for Sale** category, then the mark to market valuation for such securities should be done at least once a quarter. For entities which do not follow any investment classification norms, the *valuation for securities sold under repo transactions may be in accordance with the valuation norms followed by them in respect of securities of similar nature*.

4.6 Accounting Methodology

The accounting methodology to be followed along with the illustrations is given in **Annexes VIII-1 and VIII-2**. Participants using more stringent accounting principles may continue using the same principles. Further, to obviate the disputes arising out of repo transactions, the participants should enter into bilateral Master Repo Agreement as per the documentation finalized by Fixed Income Money Market and Derivatives Association of India (FIMMDA).

4.7 Classification of Accounts

Banks shall classify the balances in Repo A/c under Schedule 4 under item I (ii) or I (iii) as appropriate. Similarly, the balances in Reverse Repo A/c shall be classified under Schedule 7 under item I (ii) a or I (ii) b as appropriate. The balances in Repo interest expenditure A/c and Reverse Repo interest income A/c shall be classified under Schedule 15 (under item II or III as appropriate) and under Schedule 13 (under item III or IV as appropriate) respectively. The balance sheet classification for other participants shall be governed by the guidelines issued by the respective regulators.

4.8 Disclosure

The disclosures as prescribed in **Annex VII** should be made by banks in the “Notes on Accounts’ to the Balance Sheet.

4.9 Treatment for Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR)

(i) Government securities:

The regulatory treatment of market repo transactions in Government securities will continue as hitherto, i.e., the funds borrowed under repo will continue to be exempt from CRR/SLR computation and the security acquired under reverse repo shall continue to be eligible for SLR.

(ii) Corporate debt securities:

In respect of repo transactions in corporate debt securities, as already advised vide IDMD.DOD.05/11.08.38/2009-10 dated January 8, 2010,

- a. The amount borrowed by a bank through repo shall be reckoned as part of its Demand and Time Liabilities (DTL) and the same shall attract CRR/SLR.
- b. The borrowings of a bank through repo in corporate bonds shall be reckoned as its liabilities for reserve requirement and, to the extent these liabilities are to the banking system, they shall be netted as per clause (d) of the explanation under section 42(1) of the RBI Act, 1934. Such borrowings shall, however, be subject to the prudential limits for inter-bank liabilities.

5. General

5.1 Income recognition

i) Banks may book income on accrual basis on securities of corporate bodies/ public sector undertakings in respect of which the payment of interest and repayment of principal have been guaranteed by the Central Government or a State Government, provided interest is serviced regularly and as such is not in arrears.

ii) Banks may book income from dividend on shares of corporate bodies on accrual basis provided dividend on the shares has been declared by the corporate body in its Annual General Meeting and the owner's right to receive payment is established.

iii) Banks may book income from Government securities and bonds and debentures of corporate bodies on accrual basis, where interest rates on these instruments are pre-determined and provided interest is serviced regularly and is not in arrears.

iv) Banks should book income from units of mutual funds on cash basis.

5.2 Broken Period Interest

Banks should not capitalise the Broken Period Interest paid to seller as part of cost, but treat it as an item of expenditure under Profit and Loss Account in respect of investments in Government and other approved securities. It is to be noted that the above accounting treatment does not take into account taxation implications and hence the banks should comply with the requirements of Income Tax Authorities in the manner prescribed by them.

5.3 Dematerialised Holding

Banks should settle the transactions in securities as notified by SEBI only through depositories. After the commencement of mandatory trading in demat form, banks would not be able to sell the shares of listed companies if they were held in physical form. In order to extend the demat form of holding to other instruments like bonds, debentures and equities, it was decided that, with effect from October 31, 2001, banks, FIs, PDs and SDs would be permitted to make fresh investments and hold bonds and debentures, privately placed or otherwise, only in dematerialised form. Outstanding investments in scrip forms were required to be converted into dematerialised form by June 30, 2002. As regards equity instruments, banks were required to convert all their equity holding in scrip form into dematerialised form by December 31, 2004.

Short sale in Government Securities

Banks may undertake short sale of Central Government dated securities, subject to the short position being covered within a maximum period of five trading days, including the day of trade. In other words, the short sale position initiated today (trade date, T+0) will have to be covered on or before close of T+4 day. Such short positions shall be covered only by outright purchase of an equivalent amount of the same security. The short positions may be reflected in 'Securities Short Sold (SSS) A/c', specifically created for this purpose. For the purposes of this circular short sale and notional short sale are defined as under:

'Short Sale' is defined as sale of securities one does not own. A bank can also undertake 'notional' short sale where it can sell a security short from HFT even if the security is held under its AFS/HTM book. The resultant 'notional' short position would be subject to the same regulatory requirements as in the case of a short sale. For the purpose of these guidelines, short sale would include 'notional' short sale as well. The short sale by banks and the cover transaction shall not affect the holdings and valuation of the same security in AFS/HTM categories in any way.

Short sale transactions can be undertaken by banks, subject to the following conditions:

Minimum requirements:

In respect of short sales, banks shall ensure adherence to the following conditions:

- a) The sale leg of the transaction should be executed only on the Negotiated Dealing System – Order Matching (NDS-OM) platform. The cover leg of the short sale transaction can, however, be executed either on or outside the NDS-OM platform.
- b) The sale leg as well as the cover leg of the transaction should be accounted in the HFT category.
- c) Under no circumstances, should participants fail to deliver, on settlement date, the securities sold short. Failures to deliver securities short sold shall be treated as an

instance of 'SGL bouncing' and the concerned banks will be liable to disciplinary action prescribed in respect of SGL bouncing, besides attracting such further regulatory action as may be considered necessary.

- d) At no point of time should a bank accumulate a short position (face value) in any security in the HFT category in excess of the following limits:
 - i) 0.25% of the total outstanding stock issued of each security in case of securities other than liquid securities.
 - ii) 0.50% of the total outstanding stock issued of each security in case of liquid securities.
- e) Banks shall be entirely responsible for ensuring strict compliance with the above prudential limits on real time basis for which they may put in place appropriate systems and internal controls. The controls provided in the trading platform (NDS-OM) are merely in the nature of additional tools and should not be cited as a reason for any breach of internal or regulatory limits. The information regarding the outstanding stock of each Government of India dated security is being made available on the RBI website (URL: <http://rbi.org.in/Scripts/NDSUserXsl.aspx>). The list of liquid securities for compliance with the limits shall be provided by FIMMDA from time to time.
- f) Banks which undertake short sale transactions shall mark-to-market their entire HFT portfolio, including the short positions, **on a daily basis** and account for the resultant mark-to-market gains / losses as per the relevant guidelines for marking-to-market of the HFT portfolio.
- g) Gilt Accounts Holders (GAHs), under CSGL facility, are not permitted to undertake short sales. Entities maintaining CSGL Accounts are required to ensure that no short sale is undertaken by the GAHs.

Borrowing security (through the repo market) to meet delivery obligations:

Since securities that are short sold are to be **invariably** delivered on the settlement date, participants are permitted to meet their delivery obligations by acquiring securities in the repo market. Accordingly, with a view to enable participants to run short positions across settlement

cycles, banks have been permitted to use the securities acquired under a reverse repo to meet the delivery obligation of the short sale transaction. While the reverse repos can be rolled over, it is emphasised that the delivery obligations under the successive reverse repo contracts are also to be invariably met, failing which the concerned banks shall attract the regulatory action as specified above. It may, however, be noted that the permission to use securities acquired under reverse repo as above applies only to securities acquired under market repo and **not** to securities acquired under RBI's Liquidity Adjustment Facility.

Policy and internal control mechanisms:

Before actually undertaking transactions in terms of this circular, banks shall put in place a written policy on short sale, which should be approved by their respective Boards of Directors. The policy should lay down the internal guidelines which should include, *inter alia*, risk limits on short position, an aggregate nominal short sale limit (in terms of Face Value) across all eligible securities, stop loss limits, the internal control systems to ensure adherence to regulatory and internal guidelines, reporting of short selling activity to the Board and the RBI, procedure to deal with violations, etc. Banks shall also put in place a system to detect violations if any, immediately, certainly within the same trading day.

In addition to the internal control mechanisms, the concurrent auditors should specifically verify compliance with these instructions, as well as with internal guidelines and report violations, if any, within a reasonably short time, to the appropriate internal authority. As part of their monthly reporting, concurrent auditors may verify whether the independent back/mid office has taken cognizance of lapses, if any, and whether they have reported the same within the required time frame to the appropriate internal authority. Any violation of regulatory guidelines noticed in this regard should immediately be reported to the respective Public Debt Office (PDO) where the SGL account is maintained and Internal Debt Management Department, Reserve Bank of India, Mumbai.

When Issued Market - Guidelines

Definition

'When, as and if issued' (commonly known as 'when-issued' (WI)) security refers to a security that has been authorized for issuance but not yet actually issued. 'WI' trading takes place between the time a new issue is announced and the time it is actually issued. All 'when issued' transactions are on an 'if' basis, to be settled if and when the actual security is issued.

Mechanics of Operation

Transactions in a security on a 'When Issued' basis shall be undertaken in the following manner:

- a) 'WI' transactions can be undertaken in the case of securities that are being reissued as well as newly issued, on a selective basis.
- b) 'WI' transactions would commence on the issue notification date and it would cease on the working day immediately preceding the date of issue.
- c) All 'WI' transactions for all trade dates will be contracted for settlement on the date of issue.
- d) At the time of settlement on the date of issue, trades in the 'WI' security will be netted off with trades in the existing security, in the case of reissued securities.
- e) The originating transactions (sale or purchase of 'WI' securities) shall be undertaken only on NDS-OM. Any reversal of a When Issued transaction can, however, be undertaken on or outside the NDS-OM platform.
- f) Only PDs can take a short position in the 'WI' market. In other words, non-PD entities can sell the 'WI' security to any counterparty only if they have a preceding purchase contract for equivalent or higher amount.
- g) Open Positions in the 'WI' market are subject to the following limits:

Category	Reissued security	Newly issued security
Non-PDs	Long Position, not exceeding 5 per cent of the notified amount.	Long Position, not exceeding 5 per cent of the notified amount.
PD	Long or Short Position, not exceeding 10 per cent of the notified amount	Short Position, not exceeding 6 per cent and Long Position, not exceeding 10 per cent of the notified amount.

h) In the event of cancellation of the auction for whatever reason, all 'WI' trades will be deemed null and void *ab initio* on grounds of force majeure.

Internal Control

All banks participating in the 'WI' market are required to have in place a written policy on 'WI' trading which should be approved by the Board of Directors. The policy should lay down the internal guidelines which should include, inter alia, risk limits on 'WI' position (including, in the case of reissued securities, overall position in the security, i.e., 'WI' plus the existing security), an aggregate nominal limit (in terms of Face Value) for 'WI' and in the case of reissued securities, 'WI' plus the existing security, the internal control arrangements to ensure adherence to regulatory and internal guidelines, reporting of 'WI' activity to the top management, procedure to deal with violations, etc. A system should be in place to detect violations immediately, certainly within the trading day.

The concurrent auditors should specifically verify compliance with these instructions and report violations on the date of trade itself, within a reasonably short time, to the appropriate internal authority. As part of their monthly reporting, concurrent auditors may verify whether the independent back/mid office has taken cognizance of all such lapses and reported the same within the required time frame. Any violation of regulatory guidelines noticed in this regard should immediately be reported to the Public Debt Office (PDO), Mumbai and IDMD, Reserve Bank of India.

**Investment portfolio of banks – Transactions in securities –
Conditions subject to which securities allotted in the auctions for primary issues can be
sold**

(i) The contract for sale can be entered into only once by the allottee bank on the basis of an authenticated allotment advice issued by Reserve Bank of India. The buyer from an allottee in a primary auction is also permitted to re-sell the security subject to compliance with the terms and conditions stipulated in our circular No.RBI/2005-06/ 73 IDMD.PDRS. 337 /10.02.01/2005-06 dated July 20, 2005 and IDMD.PDRS.05/10.02.01/2003-04 dated March 29, 2004 Any sale of securities should be only on a T + 0 or T + 1 settlement basis.

(ii) The contract for sale of allotted securities can be entered into by banks with entities maintaining SGL Account with RBI as well as with and between CSGl account holders for delivery and settlement on the next working day through the Delivery versus Payment (DvP) system.

(iii) The face value of securities sold should not exceed the face value of securities indicated in the allotment advice.

(iv) The sale deal should be entered into directly without the involvement of broker/s.

(v) Separate record of such sale deals should be maintained containing details such as number and date of allotment advice, description and the face value of securities allotted, the purchase consideration, the number, date of delivery and face value of securities sold, sale consideration, the date and details of actual delivery i.e. SGL Form No., etc. This record should be made available to RBI for verification. Banks should immediately report any cases of failure to maintain such records.

(vi) Such type of sale transactions of Government securities allotted in the auctions for primary issues on the same day and based on authenticated allotment advice should be subjected to concurrent audit and the relative audit report should be placed before the Executive Director or the Chairman and Managing Director of the Bank once every month. A copy thereof should also be sent to the Department of Banking Supervision, RBI, Central Office, Mumbai.

(vii) Banks will be solely responsible for any failure of the contracts due to the securities not being credited to their SGL account on account of non-payment / bouncing of cheque etc.

Guidelines on Stripping/Reconstitution of Government Securities

Stripping is a process of converting periodic coupon payments of an existing Government security into tradable zero-coupon securities, which will usually trade in the market at a discount and are redeemed at face value. Thus, stripping a five-year security would yield 10 coupon securities (representing the coupons), maturing on the respective coupon dates and one principal security representing the principal amount, maturing on the redemption date of the five-year security. Reconstitution is the reverse of stripping, where, the Coupon STRIPS and Principal STRIPS are reassembled into the original Government security.

2. In terms of Explanation to section 11(2) of the Government Securities Act 2006, “A Government security may be stripped separately for interest and principal or reconstituted on the application of the holder subject to such terms and conditions as may be specified”. Accordingly, the terms and conditions for stripping and/or reconstitution of Securities issued by the Government of India have been notified by Reserve Bank of India vide Notification IDMD.1762/2009-10 dated October 16, 2009 (**Annex I-D-1**)

Process of Stripping/Reconstitution

3. Stripping/Reconstitution will be carried out at RBI as an automated process within the Negotiated Dealing System (NDS). The process of stripping/reconstitution will be a straight-through process without any manual intervention. Requests for stripping/reconstitution will be generated and approved by market participants on the NDS and the same will, thereafter, flow to a Primary Dealer (PD) of their choice for authorization. After authorization by the PD, such requests would be received and processed by the system (PDO-NDS) and necessary accounting entries posted in the accounts of the requesting participant for the STRIPS

created/securities reconstituted. The NDS will do necessary validation check like eligibility of securities, balances available, etc., on the requests for stripping/reconstitution made by participants. However, participants are required to ensure that sufficient balances are available in their accounts before putting through requests for stripping/reconstitution.

4. Normally, ISIN for Government securities are assigned at the time of auction of the securities. However, in the case of STRIPS, as these securities are created at the request of the participant, ISIN as well as nomenclature for STRIPS are created automatically based on a predefined algorithm (see **Annex I-D-2**).

5. Individual STRIPS (Coupon as well as Principal) will have a face value of Rs.100.

Eligibility

6. Any entity, including individuals, holding balances of Government securities that are eligible for stripping/reconstitution (as notified by RBI from time to time) can strip/reconstitute these securities. However, a participant (non-PD) desirous of stripping/reconstituting his balance of eligible Government securities/STRIPS should generate a request on the NDS for stripping/reconstitution by choosing any one of the Primary Dealers. Such requests for stripping/reconstitution by non-PD members shall be authorized by the PD and thereafter flow to the NDS for appropriate action (stripping/reconstitution). Requests for stripping/reconstitution by gilt account holders (GAH) shall be placed by the GAH with their respective custodians, who, in turn, will place the requests, on behalf of its constituents, in the NDS. Since stripping/reconstitution is permitted only in respect of securities held in electronic form, any participant desirous of stripping/reconstituting Government securities should have a SGL Account with the RBI or a Gilt Account with a custodian maintaining a CSGIL Account with the RBI. In the case of Primary Dealers, they can place requests directly in the NDS for stripping/reconstitution and need not route the same through another PD.

7. Initially, all PDs would be eligible to authorize stripping/reconstitution requests. However, Reserve Bank, at its discretion, can exclude any PD from authorizing such requests. Market participants will have the flexibility to choose a PD of their choice while submitting requests for stripping/reconstitution. PDs will act as market makers in STRIPS and provide two-way quote in the market.

Timings

8. Requests for stripping can be submitted by participants between 9.00 am and 2.00 pm only. All requests for stripping, received by the system (PDO-NDS), will be processed at 2.00 pm and necessary book entries will be passed in the SGL account of the participants to credit the due amount of STRIPS (coupon as well as principal) on account of stripping. All requests that have not been authorized by 2.00 pm will be rejected by the system. Stripping requests cannot be approved/ authorized after 2.00 pm on any business/working day.

9. Similarly, requests for reconstitution can be submitted between 9.00 am and 2.00 pm only. However, the requests for reconstitution would be processed online i.e., as and when such requests are authorized by the PD, and the necessary accounting entries would be passed in the SGL account of the requesting participant immediately subject to availability of sufficient and necessary balances. However, as indicated at paragraph 8 above, requests for reconstitution that are not authorized by 2.00 pm will be rejected by the system. No reconstitution request can be approved/authorized after 2.00 pm on any business/working day. Since reconstitution requests are processed online, such requests, whenever routed through a PD, must be authorized by the PD within 15 minutes of the receipt of the system notification (authorization request).

Eligible Securities

10. RBI will notify, from time to time, the securities that are eligible for stripping/reconstitution. To begin with, securities issued by Government of India, other than floating rate bonds, with coupon dates as 2nd January and 2nd July, will be eligible for stripping/reconstitution. Thus, all outstanding securities issued by Government of India, except floating rate bonds, with coupon dates/maturity date as 2nd January and 2nd July, irrespective of the year of maturity, will be eligible for stripping/reconstitution.

Minimum amount for stripping/reconstitution

11. The minimum amount of securities that needs to be submitted for Stripping/Reconstitution will be Rs.1 crore (face value) and multiples thereof.

Accounting and Valuation

12. STRIPS, being zero coupon securities, trade at a discount and are redeemed at face value. Thus, STRIPS will have to be valued and accounted for as zero coupon bonds and in the manner prescribed vide para 3.7.2 in the DBOD Master Circular dated July 1, 2009 on prudential norms for classification, valuation and operation of investment portfolio by banks.

13. The discount rates used for valuation of STRIPS at inception should be market-based. However, in case traded zero-coupon rates are not available, the zero coupon yields published by FIMMDA should be used instead.

14. Accounting entries in the SGL accounts as a consequence of stripping/reconstitution, will be passed at the face value. Thus, when a participant places a request for stripping, his SGL account will be debited by the face value of the Government security submitted for this purpose, and will be simultaneously credited with the aggregate face value of Coupon STRIPS (equal to the aggregate coupon amounts) as well as the face value of Principal STRIPS (equal to the face value of the government security). An illustration is given in **Annex I-D-3**.

15.1 However, on the day of stripping, the STRIPS should be recognised in the books of account of the participant at their discounted value and at the same time, the Government security in question should be derecognised. The accounting treatment for reconstitution should be exactly the opposite of stripping. The detailed procedure for accounting of STRIPS is given below.

15.2 The stripping/reconstitution, per se, should not result in any profit or loss. As the present value of the STRIPS (coupon as well as principal) discounted using the ZCYC will not be equal to the book value/market value of the security, the value of STRIPS shall be normalized using a factor that will be the ratio of the book value or market value of the security (whichever is lower) to the sum total of the market value of all STRIPS created out of the security (illustration given in **Annex –I-D-4**). This will ensure that the sum total of the market value of STRIPS equals the book value/market value of the security, whichever is lower.

15.3 Banks can strip eligible Government securities held under the AFS/HFT category of their investment portfolio. However, if strips are to be created out of securities held in the HTM category, then the security first needs to be transferred to AFS/HFT category. The shifting of securities from HTM category for the purpose of stripping, will be as per the relevant guidelines prescribed vide DBOD Master Circular dated July 1, 2009 on prudential norms for classification, valuation and operation of investment portfolio by banks.

15.4 In case STRIPS are created from securities held in the HTM portfolio, the securities should be transferred from the HTM category to the AFS/HFT category (as per the shifting discipline from HTM, i.e., once a year at the beginning of the year as per the above-mentioned master circular dated July 01, 2009) and the shifted security shall be carried at the least of the book value/market value. Depreciation, if any, shall be provided for and appreciation, if any, ignored as hitherto. Thereafter, the lower of the book value/market value will be used for normalizing the market value of individual STRIPS to the book value/market value. Post-stripping, the book value/market value of the existing securities will be derecognized and replaced by the normalized value of STRIPS whose sum total shall exactly equal the book value/market value of the extinguished security (thereby ensuring that there is no profit or loss on account of stripping). Any appreciation, arising due to the shifting of the security from HTM shall be ignored. The same methodology would follow for securities that are stripped from the AFS/HFT portfolio.

SLR Status of STRIPS

16. STRIPS will be reckoned as eligible Government securities for SLR purposes and retain all the characteristics of Government security. They will be eligible securities for market repo as well as repo under LAF of RBI but with appropriate haircut.

Trading in STRIPS

17. To begin with, STRIPS will be tradable only in the OTC market. Hence, trades in STRIPS will have to be undertaken in the OTC market and reported on NDS for clearing and settlement through CCIL.

18. Short sale of STRIPS shall not be permitted.

19. Participants shall not sell STRIPS/securities upfront based on the requests placed by them for stripping/reconstitution. Accordingly, sale transaction in STRIPS/securities shall be undertaken by participants only after the securities are stripped/reconstituted and the same is reflected in the SGL account of the participant.

Fees & Charges

20. Reserve Bank will not charge any fees for stripping/reconstitution of Government Securities. Further, to begin with, PDs, who are the “authorized entities” for authorizing requests for stripping/reconstitution in the PDO-NDS may also not charge the participants for carrying out this activity.

Annex I-D-1

I. Definitions

a) “STRIPS” (Separate Trading of Registered Interest and Principal of Securities) are distinct, separate securities that are created from the cash flows of a Government security and shall consist of –

- (i) Coupon STRIPS, where the single cash flow of the STRIP represents a coupon flow of the original security
- (ii) Principal STRIP, where the single cash flow of the STRIP represents the principal cash flow of the original security.

Explanation: Stripping of a security shall result in Coupon STRIPS for all outstanding coupon payments and one Principal STRIP for the redemption payment. Each STRIP accordingly becomes a zero coupon bond since it has only one cash flow at maturity. Each STRIP shall be a distinct Government security and shall have a separate and distinct International Securities Identification Number (ISIN).

b) “Stripping” means the process of separating the cash flows associated with a regular Government security i.e., each outstanding semi-annual coupon payment and the final principal payment into separate securities.

c) “Reconstitution” means the reverse process of stripping, where the individual STRIPS i.e., both coupon STRIPS and Principal STRIPS are reassembled to get back the original security.

d) “Authorized entity” means a Primary Dealer or any other entity recognized by the RBI to accept requests from the holders of Government securities for stripping/reconstitution of the securities and submission to the RBI.

II. Terms and Conditions for STRIPS

1. The process of stripping/reconstitution of Government securities shall be carried out at RBI, Public Debt Office in the PDO-NDS (Negotiated Dealing System).

2. All dated Government securities other than floating rate bonds having coupon payment dates on 2nd January and 2nd July, irrespective of the year of maturity shall be eligible for Stripping/Reconstitution.
3. All Coupon STRIPS with the same maturity date shall have the same ISIN, regardless of the underlying security from which the interest payments were stripped, and coupon STRIPS of the same cash flow shall be fungible (interchangeable). The ISIN of Coupon STRIPS shall be different from the ISIN of Principal STRIPS, even if they have the same maturity date, and shall not be fungible.
4. Stripping/reconstitution may be done at the option of the holder at any time from the date of issuance of a Government security till its maturity.
5. Stripping/reconstitution shall be permitted only in the eligible Government securities held in the Subsidiary General Leger (SGL)/Constituent Subsidiary General Ledger (CSGL) accounts maintained at the Public Debt Office, RBI, Mumbai. Physical securities shall not be eligible for stripping/reconstitution.
6. Holders of Government securities shall place their requests for stripping/reconstitution only with an "Authorized entity".
7. Reserve Bank will not charge any fees on stripping/reconstitution.
8. The amount of securities that could be tendered for stripping/reconstitution shall be a minimum of Rs.1 crore and multiples thereof.
9. These terms and conditions shall come into effect from the date of this Notification.

Annex I-D-2

ISIN for STRIPS

Structure:

I	N			M	M	Y	Y				
Country code		Issuer type/state code		Month and year of maturity of the STRIP				Security type	Subsequent strips/series serial number		Checksum digit

Example of a CG Principal STRIP maturing in March 2011:

I	N	0	0	0	3	1	1	P	0	1	
Country code		Issuer type/state code		Month and year of maturity of the STRIP				Security type	Subsequent strips/series serial number		Checksum digit

Example of a CG Coupon STRIP maturing in March 2011:

I	N	0	0	0	3	1	1	C	0	1	
Country code		Issuer type/state code		Month and year of maturity of the STRIP				Security type	Subsequent strips/series serial number		Checksum digit

Nomenclature for Coupon STRIPS

GSDDMONYYYYC; where GS=Government Security, DDMONYYYYY=date of maturity of the STRIPS and C=Coupon STRIP. (Ex. A coupon STRIP maturing on March 25, 2011 would be written as **GS25MAR2011C**)

Nomenclature for Principal STRIPS

x.xx%GSDDMONYYYYYP; where x.xx is the coupon of the parent security from which the principal STRIP has been generated, GS=Government Security, DDMONYYYYY=date of maturity of the STRIPS and P=Principal STRIPS. (Ex. A principal STRIP generated from, say, 7.99%2019 maturing on 02 July 2019 will be written as **7.99%GS02JUL2019P**)

Stripping of securities – An illustration

Stripable Securities

Security	Date of Maturity
9.39% 2011	02-Jul-11
12.30 % 2016	02-Jul-16

Investor "A"

Portfolio as on October 16, 2009 (in the books of PDO, Mumbai)

Security	Rs. (Cr) {Face Value}
9.39% 2011	100.00
12.30 % 2016	250.00

On March 17, 2010, investor "A" strips Rs.5 Cr worth of 9.39%2011 & Rs.10 Cr worth of 12.30%2016

STRIPS generated

9.39% 2011		
	02 July 10	2,347,500
	02 Jan 11	2,347,500
	02 July 11	2,347,500
Principal STRIP (PS)	02 July 11	50,000,000

Each coupon strip = {9.39%/2} x 5 Cr.

12.30 % 2016		
	02 July 10	6,150,000
	02 Jan 11	6,150,000
	02 July 11	6,150,000
	02 Jan 12	6,150,000
	02 July 12	6,150,000
	02 Jan 13	6,150,000
	02 July 13	6,150,000
	02 Jan 14	6,150,000
	02 July 14	6,150,000
	02 Jan 15	6,150,000
	02 July 15	6,150,000
	02 Jan 16	6,150,000
	02 July 16	6,150,000
Principal STRIP (PS)	02 July 16	100,000,000

Each coupon strip = {12.30%/2} x 10 Cr.

Portfolio as on March 17, 2010 after stripping (in the books of PDO, Mumbai)

Security	Amount (Rs.) {Face Value}
9.39% 2011	950,000,000
12.30 % 2016	2,400,000,000
CS 02 July 10	8,497,500
CS 02 Jan 11	8,497,500
CS 02 July 11	8,497,500
CS 02 Jan 12	6,150,000
CS 02 July 12	6,150,000
CS 02 Jan 13	6,150,000
CS 02 July 13	6,150,000
CS 02 Jan 14	6,150,000
CS 02 July 14	6,150,000
CS 02 Jan 15	6,150,000
CS 02 July 15	6,150,000
CS 02 Jan 16	6,150,000
CS 02 July 16	6,150,000
PS 02 July 11	50,000,000
PS 02 July 16	100,000,000

CS=Coupon STRIPS; PS=Principal STRIP

Annex I-D-4

Procedure for normalization of STRIPS(at stripping/reconstitution) to ensure no profit/ loss

(For illustration only)

Security 12.30% 2016
Date of maturity 02-Jul-16
Coupon 12.30%
Date of Stripping 03-Mar-10

(1) Market value of 12.30% on 03-Mar-10 129.96
(2) Book Value 120.00
(3) Sum total of PV of STRIPS 127.87
(4) Normalization Factor [(2) ÷ (3)] 0.9385

	Maturity Date	Maturity amount	ZCYC	PV of STRIPS (Market Value)	Normalized value of STRIPS
	(a)	(b)	(c)	(d)	[0.9385 x (d)]
1	2/ Jul/ 10	6.15	4.0683	6.0274	5.6564
2	2/ Jan/ 11	6.15	4.6948	5.8711	5.5098
3	2/ Jul/ 11	6.15	5.3212	5.6841	5.3343
4	2/ Jan/ 12	6.15	5.6128	5.5055	5.1666
5	2/ Jul/ 12	6.15	5.9044	5.3174	4.9901
6	2/ Jan/ 13	6.15	6.1339	5.1305	4.8147
7	2/ Jul/ 13	6.15	6.3633	4.9392	4.6352
8	2/ Jan/ 14	6.15	6.4744	4.7663	4.4730
9	2/ Jul/ 14	6.15	6.5855	4.5946	4.3118
10	2/ Jan/ 15	6.15	6.7227	4.4187	4.1467
11	2/ Jul/ 15	6.15	6.8599	4.2439	3.9827
12	2/ Jan/ 16	6.15	6.9971	4.0707	3.8201
13	2/ Jul/ 16	106.15	7.1343	67.3029	63.1606
TOTAL				127.87	120.00

Note:

1. The security is presumed to be held in HTM category and hence is to be shifted to AFS/ HFT before stripping, marked-to-market and the lower of the book value or market value will be used to arrive at the normalization factor.
2. In case the market value of 12.30% 2016 is less than the book value then the market value, instead of the book value, will be used to normalize the STRIPS i.e., the normalization factor would be **market value ÷ sum total of PV of STRIPS**, where the PV of STRIPS are arrived at by discounting the cash flow using the ZCYC.
3. Securities in AFS/ HFT will be normalized using the same principle (i.e., lower of market value/ book value).

Annex I – E

Repo in Corporate Debt Securities (Reserve Bank) Directions, 2010

1. Short title and commencement of the directions

These directions are called the Repo in Corporate Debt Securities (Reserve Bank) Directions, 2010 effective from **March 01, 2010**.

2. Definitions

- a. **‘Corporate Debt Security’** means non-convertible debt securities, which create or acknowledge indebtedness, including debentures, bonds and such other securities of a company or a body corporate constituted by or under a Central or State Act, whether constituting a charge on the assets of the company or body corporate or not, but does not include debt securities issued by Government or such other persons as may be specified by the Reserve Bank, security receipts and securitized debt instruments”
- b. **‘Security Receipts’** means a security as defined in clause (zg) of section 2 of the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (54 of 2002)
- c. **‘Securitized debt instrument’** means securities of the nature referred to in sub-clause (ie) of clause (h) of section 2 of the Securities Contracts (Regulation) Act, 1956(42 of 1956).

3. Eligible securities for repo in Corporate Debt Securities

- a. Only listed corporate debt securities which are rated ‘AA’ or above by the rating agencies, that are held in the security account of the repo seller, in demat form, shall be eligible provided that Commercial Papers (CPs), Certificates of Deposit (CDs) and other instruments including Non-Convertible Debentures (NCDs) of less than one year of original maturity, shall not be eligible securities for undertaking repo.

4. Eligible Participants

The following entities shall be eligible to undertake repo transactions in corporate debt securities:

- a. Any scheduled commercial bank excluding RRBs and LABs;
- b. Any Primary Dealer authorised by the Reserve Bank of India;
- c. Any non-banking financial company registered with the Reserve Bank of India (other than Government companies as defined in section 617 of the Companies Act, 1956);
- d. All-India Financial Institutions, namely, Exim Bank, NABARD, NHB and SIDBI;
- e. Other regulated entities, subject to the approval of the regulators concerned, viz.,
 - i. Any mutual fund registered with the Securities and Exchange Board of India;
 - ii. Any housing finance company registered with the National Housing Bank; and
 - iii. Any insurance company registered with the Insurance Regulatory and Development Authority
- f. India Infrastructure Finance Company Limited (IIFCL)
- g. Any other entity specifically permitted by the Reserve Bank

5. Tenor

Repos in corporate debt securities shall be for a minimum period of one day and a maximum period of one year.

6. Trading

Participants shall enter into repo transactions in corporate debt securities in the OTC market.

7. Reporting of Trades

- a. All repo trades shall be reported within 15 minutes of the trade on the FIMMDA reporting platform.
- b. The trades shall also be reported to any of the clearing houses of the exchanges for clearing and settlement.

8. Settlement of trades

- a. All repo trades in corporate debt securities shall settle either on a T+1 basis or a T+2 basis under DvP I (gross basis) framework.
- b. Repo transactions in corporate debt securities shall settle in the same manner as outright OTC trades in corporate debt securities.
- c. On the date of reversal of repo trades, the clearing houses shall compute the obligations of the parties and facilitate settlement on DvP basis.

9. Prohibition on sale of repoed security

The security acquired under repo shall not be sold by the repo buyer (lender of the funds) during the period of repo.

10. Haircut

- a. A haircut of 25% (or higher as maybe decided by the participants depending on the term of the repo) shall be applicable on the market value of the corporate debt security prevailing on the date of trade of 1st leg.
- b. Participants may refer to the rating-haircut matrix that may be published by the Fixed Income Money Market and Derivatives Association of India (FIMMDA), to determine the appropriate haircut.

11. Valuation

For arriving at the market value of the corporate debt security, the participants undertaking repo in corporate bonds may refer to the credit spreads published by the FIMMDA.

12. Capital Adequacy

The repo transactions in corporate debt securities shall attract capital charge in terms of para 7.3.8 of the Master Circular DBOD No.BP.BC.21/21.06.001/2009-10 dated July 01, 2009.

13. Disclosure

The details of corporate debt securities lent or acquired under repo or reverse repo transactions shall be disclosed in the “Notes on Accounts” to the Balance Sheet. 4

14. Accounting

The repo transactions in corporate debt securities shall be accounted as per the revised guidelines on uniform accounting for repo/reverse repo transactions in Government securities.

15. Computation of CRR/SLR & borrowing limit

- a. The amount borrowed by a bank through repo shall be reckoned as part of its Demand and Time Liabilities (DTL) and the same shall attract CRR/SLR as per the provisions of the Master Circular DBOD.Ret.BC.45/12.01.001/2009-10 dated September 18, 2009.
- b. The borrowings of a bank through repo in corporate bonds shall be reckoned as its liabilities for reserve requirement and, to the extent these liabilities are to the banking system, they shall be netted as per clause (d) of the explanation under section 42(1) of the RBI Act, 1934. Such borrowings shall, however, be subject to the prudential limits for inter-bank liabilities prescribed vide circular DBOD.BP.BC.66/21.01.002/2006-07 dated March 06, 2007.

16. Documentation

The participants shall enter into bilateral Master Repo Agreement as per the documentation finalized by the FIMMDA.

**Investment portfolio of banks - Transactions in securities -
Aggregate contract limit for individual brokers**

Sr. No.	Issue Raised	Response
1.	The year should be calendar year or financial year?	Since banks close their accounts at the end of March, it may be more convenient to follow the financial year. However, the banks may follow calendar year or any other period of 12 months provided, it is consistently, followed in future.
2.	Whether the limit is to be observed with reference to total transactions of the previous year as the total transactions of the current year should be known only at the end of the year?	The limit has to be observed with reference to the year under review. While operating the limit, the bank should keep in view the expected turnover of the current year which may be based on turnover of the previous year and anticipated rise or fall in the volume of business in the current year.
3.	Whether to arrive at the total transactions of the year, transactions entered into directly with counter-parties i.e. where no brokers are involved would also be taken into account	Not necessary. However, if there are any direct deals with the brokers as purchasers or sellers the same would have to be included in the total transactions to arrive at the limit of transactions to be done through an individual broker.
4.	Whether in case of ready forward deals both the legs of the deals i.e. purchase as well as sale will be included to arrive at the volume of total transactions?	Yes. This is however only theoretical as R/F transactions in Govt. security now prohibited except in Treasury Bills and the 3 year dated securities issued by conversion of Treasury Bills recently
5.	Whether central loan /state loan /treasury bills etc. purchased subscriptions/ auction will be, included in the volume of total transactions?	No, as brokers are not involved as intermediaries.
6.	It is possible that even though bank considers that a particular broker has touched the prescribed limit of 5% he may come with an offer during the remaining period of the year which the bank may find it to its advantage as compared to offers received from the other brokers who have not yet done business upto the prescribed limit.	If the offer received is more advantageous the limit for the broker may be exceeded the reasons therefor recorded and approval of the competent authority / Board obtained post facto.
7.	Whether the transactions conducted on behalf of the clients would also be included in the total transactions of the	Yes. If they are conducted through the brokers.

	year?	
8.	For a bank which rarely deals through brokers and consequently the volume of business is small maintaining the broker-wise limit of 5% may mean splitting the orders in small values amongst different brokers and there may also arise price differential.	There may be no need to split an order. If any deal causes the particular broker's share to exceed 5% limit, our circular provides the necessary flexibility in as much as Board's post facto approval can be obtained.
9.	During the course of the year it may not be possible to reasonably predict what will be the total quantum of transactions through brokers as a result of which there could be deviation in complying with the norm of 5% .	The bank may get post facto approval from the Board after explaining to it the circumstances in which the limit was exceeded.
10.	Some of the small private sector banks have mentioned that where the volume of business particularly the transactions done through brokers is small the observance of 5% limit may be difficult. A suggestion has therefore been made that the limit may be required to be observed if the business done through a broker exceeds a cut-off point of say Rs.10 crores	As already observed the limit of 5% can be exceeded subject to reporting the transactions to the competent authority post facto. Hence, no change in our instructions is considered necessary.

Annex III
Para 1.2(ii)

Recommendations of the Group on Non-SLR Investments of Banks

Pro-forma of minimum disclosure requirements in respect of private placement issues - Model Offer Document

All issuers must issue an offer document with terms of issue, authorised by Board Resolution not older than 6 months from the date of issue. The offer document should specifically mention the Board Resolution authorising the issue and designations of the officials who are authorised to issue the offer document. The offer document may be printed or typed "For Private Circulation Only". The 'Offer Document' should be signed by the authorised signatory. The offer document should contain the following minimum information:

I. General Information

1. Name and address of registered office of the company
2. Full names (expanded initials), addresses of Directors and the names of companies where they are Directors.
3. Listing of the issue (If listed, name of the Exchange)
4. Date of opening of the issue

Date of closing of the issue

Date of earliest closing of the issue.
5. Name and addresses of auditors and Lead Managers / arrangers
6. Name address of the trustee - consent letter to be produced (in case of debenture issue)
7. Rating from any Rating Agency and / or copy of the rationale of latest rating.

II. Particulars of the issue

- (a) Objects
- (b) Project cost and means of financing (including contribution of promoters) in case of new projects.

III. The model offer document should also contain the following information:

- (1) Interest rate payable on application money till the date of allotment.
- (2) Security: If it is a secured issue, the issue is to be secured, the offer documents should mention description of security, type of security, type of charge, Trustees, private charge-holders, if any, and likely date of creation of security, minimum security cover, revaluation, if any.
- (3) If the security is collateralised by a guarantee, a copy of the guarantee or principal terms of the guarantee are to be included in the offer document.

- (4) Interim Accounts, if any.
- (5) Summary of last audited Balance Sheet and Profit & Loss Account with qualifications by Auditors, if any.
- (6) Last two published Balance Sheet may be enclosed.
- (7) Any conditions relating to tax exemption, capital adequacy etc. are to be brought out fully in the documents.
- (8) The following details in case of companies undertaking major expansion or new projects :- (copy of project appraisal may be made available on request)
 - (a) Cost of the project, with sources and uses of funds
 - (b) Date of commencement with projected cash flows
 - (c) Date of financial closure (details of commitments by other institutions to be provided)
 - (d) Profile of the project (technology, market etc)
 - (e) Risk factors
- (9) If the instrument is of tenor of 5 years or more, projected cash flows.

IV. Banks may agree to insist upon the following conditionalities for issues under private placements

All the issuers in particular private sector corporates, should be willing to execute a subscription agreement in case of all secured debt issues, pending the execution of Trust Deed and charge documents. A standardised subscription agreement may be used by the banks, inter-alia, with the following important provisions:

- (a) Letter of Allotment should be made within 30 days of allotment. Execution of Trust Deed and charge documents will be completed and debentures certificates will be dispatched within the time limit laid down in the Companies Act but not exceeding in any case, 6 months from the date of the subscription agreement.
- (b) In case of delay in complying with the above, the company will refund the amount of subscription with agreed rate of interest, or, will pay penal interest of 2% over the coupon rate till the above conditions are complied with, at the option of the bank.
- (c) Pending creation of security, during the period of 6 months (or extended period), the principal Directors of the company should agree to indemnify the bank for any loss that may be suffered by the bank on account of the subscription to their debt issue. (This condition will not apply to PSUs).
- (d) It will be the company's responsibility to obtain consent of the prior charge-holders for creation of security within the stipulated period. Individual banks may insist upon

execution of subscription agreement or a suitable letter to comply with the terms of offer such as appointment of trustee, creation of security etc. on the above lines.

(e) Rating: The Group recommends that the extant regulations of SEBI in regard to rating of all debt instruments in public offers would be made applicable to private placement also. This stipulation will also apply to preference shares, which are redeemable after 18 months.

(f) Listing: Currently, there is a lot of flexibility regarding listing required by banks in private placement issues. However, the Group recommends that listing of companies should be insisted upon, (exceptions, if any, to this rule shall be provided in the Investment Policy of the banks) which would in due course help develop secondary market. The advantage of listing would be that the listed companies would be required to disclose information periodically to the Stock Exchanges which would also help develop the secondary markets by way of investor information. In fact, SEBI has advised all the Stock Exchanges that all listed companies should publish unaudited financial results on a quarterly basis and that they should inform the Stock Exchanges immediately of all events which would have a bearing on the performance / operations of the company as well as price sensitive information.

(g) Security / documentation: To ensure that the documentation is completed and security is created in time, the Group has made recommendations, which is contained in this model offer document. It may be noted that in case of delay in execution of Trust Deed and Charge documents, the company will refund the subscription with agreed rate of interest or will pay penal interest of 2% over the coupon rate till these conditions are complied with at the option of the bank. Moreover, Principal Directors of the company will have to agree to indemnify the bank for any loss that may be suffered by the bank on account of the subscription to the debt issue during the period of 6 months (or extended period) pending creation of security.

Annex - IV
Para 1.2.4

**Guidelines on Investments by Banks in Non-SLR Investment Portfolio by Banks -
Definitions**

1. With a view to imparting clarity and to ensure that there is no divergence in the implementation of the guidelines, some of the terms used in the guidelines on non-SLR investments are defined below.

2. A security will be treated as rated if it is subjected to a detailed rating exercise by an external rating agency in India, which is registered with SEBI and is carrying a current or valid rating. The rating relied upon will be deemed to be current or valid if

(i) The credit rating letter relied upon is not more than one month old on the date of opening of the issue, and

(ii) The rating rationale from the rating agency is not more than one year old on the date of opening of the issue, and

(iii) The rating letter and the rating rationale is a part of the offer document.

(iv) In the case of secondary market acquisition, the credit rating of the issue should be in force and confirmed from the monthly bulletin published by the respective rating agency.

Securities, which do not have a current or valid rating by an external rating agency, would be deemed as unrated securities.

3. The investment grade ratings awarded by each of the external rating agencies operating in India would be identified by the IBA / FIMMDA. These would also be reviewed by IBA / FIMMDA at least once a year.

4. A 'listed' security is a security which is listed in a stock exchange. Investment in non-SLR debt securities (both primary and secondary market) by banks where the security is proposed to be listed on the Exchange(s) may be considered as investment in listed security at the time of making investment.

**Annex - V
Para 1.2.20**

Prudential Guidelines on Management of the Non-SLR Investment Portfolio by Banks - Disclosures Requirements

Banks should make the following disclosures in the 'Notes on Accounts' of the balance sheet in respect of their non-SLR investment portfolio, with effect from the financial year ending 31 March 2004.

(i) **Issuer composition of Non SLR investments**

(Rs. in crore)						
Sl. No	Issuer	Amount	Extent of private placement	Extent of 'below investment grade' securities	Extent of 'unrated' securities	Extent of 'unlisted' securities
1	2	3	4	5	6	7
1.	PSUs					
2.	FIs					
3.	Banks					
4.	Private Corporates					
5.	Subsidiaries / Joint ventures					
6.	Others					
7.	Provision held towards depreciation		XXX	XXX	XXX	XXX
	Total *					

Note: 1. * Total under column 3 should tally with the total of investments included under the following categories in Schedule 8 to the balance sheet:

- (a) Shares
- (b) Debentures & Bonds
- (c) Subsidiaries / joint ventures
- (d) Others

2. Amounts reported under columns 4, 5, 6 and 7 above may not be mutually exclusive.

(ii) **Non-performing Non-SLR investments**

Particulars	Amount (Rs. Crore)
Opening balance	
Additions during the year since 1st April	
Reductions during the above period	
Closing balance	
Total provisions held	

RETURN/STATEMENT NO. 9

Proforma Statement showing the position of Reconciliation of Investment Account as on 31st March

Name of the bank/ Institution: _____

(Face value Rs. in crore)

Particulars of securities	General Ledger Balance	SGL Balance		BRs held	SGL Forms held	Actual Scrips Held	Outstanding deliveries
		As per PDO Books	As per bank's / institution's books				
1	2	3	4	5	6	7	8
Central Govt							
State Government							
Other approved securities							
Public Sector Bonds							
Units of UTI (1964)							
Others (Shares & Debenture etc)							
TOTAL							

Signature of the Authorised Official
with the Name and Designation

Note : Similar statements may be furnished in respect of PMS client's Accounts and other constituents' Accounts (including Brokers). In the case of PMS/other constituents' accounts, the face value and book value of securities appearing in the relevant registers of the bank should be mentioned under Column 2.

General instructions for compiling reconciliation statement

a) Column - 2 (GL balances)

It is not necessary to give complete details of securities in the format. Only aggregate amount of face value against each category may be mentioned. The corresponding book value of securities may be indicated in bracket under the amount of face value of securities under each category.

b) Column - 3 and 4 (SGL balances)

In the normal course balances indicated against item three and four should agree with each other. In case of any difference on account of any transaction not being recorded either in PDO or in the books of the bank this should be explained giving full details of each transaction.

c) Column - 5 (BRs held)

If the bank is holding any BRs for purchases for more than 30 days from the date of its issue, particulars of such BRs should be given in a separate statement.

d) Column - 6 (SGL forms held)

Aggregate amount of SGL forms received for purchases, which have not been tendered with PDO, should be given here.

e) Column - 7

Aggregate amount of all scrips held in the form of bonds, letters of allotments, subscription receipts as also certificates of entries in the books of accounts of the issuer (for other than government securities), etc. including securities which have been sold but physical delivery has not been given should be mentioned.

f) Column - 8 (outstanding deliveries)

This relates to BRs issued by the bank, where the physicals/scrips have not been delivered but the balance in General Ledger has been reduced. If any BR issued is outstanding for more than thirty days the particulars of such BRs may be given in a separate list indicating reasons for not affecting the delivery of scrips.

g) General

Face value of securities indicated against each item in column two should be accounted for under any one of the columns from four to seven. Similarly, amount of outstanding deliveries (BRs issued) which has been indicated in column eight will have to be accounted for under one of the columns four to seven. Thus the total of columns two and eight should tally with total of columns four to seven.

Disclosures

The following disclosures should be made by banks in the 'Notes on Accounts' to the Balance Sheet.

(Rs. in crore)				
	Minimum outstanding during the year	Maximum outstanding during the year	Daily Average outstanding during the year	As on March 31
Securities sold under repos				
Securities purchased under reverse repos				

Recommended Accounting Methodology for accounting of Repo / Reverse Repo transactions

- i The following accounts may be maintained , viz. i) Repo Account, ii) Reverse Repo Account, iii) Reverse Repo Interest Income Account, iv) Repo Interest Expenditure Account v) Reverse Repo Interest Receivable Account and vi) Repo Interest Payable Account.
- ii In addition to the above, the following 'contra' accounts may also be maintained, viz. i) Securities Sold under Repo Account, (ii) Securities Purchased under Reverse Repo Account, (iii) Securities Receivable under Repo Account and (iv) Securities Deliverable under Reverse Repo Account.

Repo

- iii In a repo transaction, the securities should be sold in the first leg at market related prices and re-purchased in the second leg at the same prices. The consideration amount in the second leg would, however, include the repo interest. The sale and repurchase should be reflected in the Repo Account.
- iv Though the securities are not excluded from the repo seller's investment account and not included in the repo buyer's investment account, the transfer of securities shall be reflected by using the necessary contra entries.

Reverse Repo

- v In a reverse repo transaction, the securities should be purchased in the first leg at prevailing market prices and sold in the second leg at the same prices. The consideration amount in the second leg would, however, include the repo interest. The purchase and sale should be reflected in the Reverse Repo Account.
- vi The balances in the Reverse Repo Account shall not be a part of the Investment Account for balance sheet purposes but can be reckoned for SLR purposes if the securities acquired under reverse repo transactions are approved securities.

Other aspects relating to Repo/Reverse Repo

- vii In case the interest payment date of the securities sold under repo falls within the repo period, the coupons received by the buyer of the security should be passed on to the seller on the date of receipt as the cash consideration payable by the seller in the second leg does not include any intervening cash flows.
- viii To reflect the accrual of interest in respect of the outstanding repo transactions at the end of the accounting period, appropriate entries should be passed in the Profit and Loss account to reflect Repo Interest Income / Expenditure in the books of the buyer / seller respectively and the same should be debited / credited as an expenditure payable/income receivable. Such entries passed should be reversed on the first working day of the next accounting period.
- ix Repo seller continues to accrue coupon/discount as the case may be, even during the repo period while the repo buyer shall not accrue the same.

x Illustrative examples are given in ***Annex – VIII.2***

Illustrative examples for accounting of Repo / Reverse repo transactions

While in the body of the circular, the term "repo" is used generically to include both repo and reverse repo (which is simply a mirror image of a repo transaction), in this Annex the accounting guidelines have been set out separately for repo and reverse repo for clarity.

A. Repo/Reverse Repo of dated security**1. Details of Repo in a coupon bearing security:**

Security offered under repo	6.35% 2020	
Coupon payment dates	02 January and 02 July	
Market Price of security	Rs.90.9100	(1)
Date of the repo	28-Mar-2010	
Repo interest rate	5.00%	
Tenor of the repo	5 days	
Reversal date for the repo	02-Apr-2010	
Broken period interest for the first leg*	$6.35\% \times 86 / 360 \times 100 = 1.5169$	(2)
Cash consideration for the first leg	$(1) + (2) = 92.4269$	(3)
Repo interest**	$92.4269 \times 5/365 \times 5.00\% = 0.0633$	(4)
Cash Consideration for the second leg	$(3) + (4) = 92.4269 + 0.0633 = 92.4902$	

* **Using 30/360 day count convention**

** **Using Actual/365 day count convention**

2. Accounting for Repo Seller (Borrower of Funds)First leg

	Debit	Credit
Cash	92.4269	
Repo A/c		92.4269
Securities Receivable under Repo A/c (by contra)	92.4269	
Securities Sold under Repo A/c (by contra)		92.4269

Second Leg

	Debit	Credit
Repo A/c	92.4269	
Repo Interest Expenditure A/c	0.0633	
Cash A/c		92.4902
Securities Sold under Repo A/c (by contra)	92.4269	
Securities Receivable under Repo A/c (by contra)		92.4269

3. Accounting for Repo Buyer (Lender of Funds)

First leg

	Debit	Credit
Reverse Repo A/c	92.4269	
Cash A/c		92.4269
Securities Purchased under Reverse Repo A/c (by contra)	92.4269	
Securities Deliverable under Reverse Repo A/c (by contra)		92.4269

Second Leg

	Debit	Credit
Cash A/c	92.4902	
Reverse Repo A/c		92.4269
Reverse Repo Interest Income A/c		0.0633
Securities Deliverable under Reverse Repo A/c (by contra)	92.4269	
Securities Purchased under Reverse Repo A/c (by contra)		92.4269

4. Ledger entries for the adjustment accounts

Securities Receivable under Repo A/c

Debit		Credit	
To Securities Sold under Repo A/c (repo 1 st leg)	92.4269	By Securities Sold under Repo A/c (repo 2 nd leg)	92.4269

Securities Sold under Repo A/c

Debit		Credit	
To Securities Receivable under Repo A/c (repo 2 nd leg)	92.4269	By Securities Receivable under Repo A/c (repo 1 st leg)	92.4269

Securities Purchased under Repo A/c

Debit		Credit	
To Securities Deliverable under Reverse Repo A/c (reverse repo 1 st leg)	92.4269	By Securities Deliverable under Reverse Repo A/c (reverse repo 2 nd leg)	92.4269

Securities Deliverable under Repo A/c

Debit		Credit	
To Securities Purchased under Reverse Repo A/c (reverse repo 2 nd leg)	92.4269	By Securities Purchased under Reverse repo A/c (Reverse Repo 1 st leg)	92.4269

5. If the balance sheet date falls during the tenor of the repo, participants may use the transit accounts, i.e., Repo Interest Payable A/c and Reverse Repo Interest Receivable A/c to record the accrued interest and reverse the same the following day. The balances in the repo interest receivable and payable shall be taken to the P & L Account with appropriate entries passed in the Balance sheet, as below:-

Transaction Leg	1st leg	Balance Sheet Date	2nd leg
Dates	28-Mar-10	31-Mar-10	02-Apr-10

a) Entries in the Books of Repo Seller (borrower of funds) on 31-Mar-10

Account Head	Debit	Credit
Repo Interest Expenditure A/c [Balances under the account to be transferred to P & L]	0.0506 (being the repo interest for 4 days)	
Repo Interest Payable A/c		0.0506

Account Head	Debit	Credit
P & L A/c	0.0506	
Repo Interest Expenditure A/c		0.0506

b) Reversal of entries in the Books of Repo Seller (borrower of funds) on 01-Apr-10

Account Head	Debit	Credit
Repo Interest Payable A/c	0.0506	
Repo Interest Expenditure		0.0506

c) Entries in books of Repo Buyer (Lender of Funds) on 31-Mar-10

Account Head	Debit	Credit
Reverse Repo Interest Receivable A/c	0.0506	
Reverse Repo Interest Income A/c [Balances under the account to be transferred to P & L]		0.0506 (Being the repo interest for 4 days)

Account Head	Debit	Credit
Reverse Repo Interest Income A/c	0.0506	
P & L A/c		0.0506

d) Reversal of entries in the Books of Repo Buyer (Lender of Funds) on 01-Apr-10

Account Head	Debit	Credit
Reverse Repo Interest Income A/c	0.0506	
Reverse Repo Interest Receivable A/c		0.0506

B. Repo/ Reverse Repo of Treasury Bill
1. Details of Repo on a Treasury Bill

Security offered under Repo	GOI 91 day Treasury Bill maturing on 07 May 2010	
Price of the security offered under Repo	Rs.99.0496	(1)
Date of the Repo	28-Mar-2010	
Repo interest rate	5%	
Tenor of the repo	5 days	
Total cash consideration for the first leg	99.0496	(2)
Repo interest *	$99.0496 \times 5\% \times 5 / 365 = 0.0678$	(3)
Cash consideration for the second leg	$(2) + (3) = 99.0496 + 0.0678 = 99.1174$	

* **Using Actual/365 day count convention**

2. Accounting for Repo Seller (Borrower of Funds)

First leg

	Debit	Credit
Cash	99.0496	
Repo A/c		99.0496
Securities Receivable under Repo A/c (by contra)	99.0496	
Securities Sold under Repo A/c (by contra)		99.0496

Second Leg

	Debit	Credit
Repo A/c	99.0496	
Repo Interest Expenditure A/c	0.0678	
Cash A/c		99.1174
Securities Sold under Repo A/c (by contra)	99.0496	
Securities Receivable under Repo A/c (by contra)		99.0496

3. Accounting for Repo Buyer (Lender of Funds)

First leg

	Debit	Credit
Reverse Repo A/c	99.0496	
Cash A/c		99.0496
Securities Purchased under Reverse Repo A/c (by contra)	99.0496	
Securities Deliverable under Reverse Repo A/c (by contra)		99.0496

Second Leg

	Debit	Credit
Cash A/c	99.1174	
Reverse Repo A/c		99.0496
Reverse Repo Interest Income A/c		0.0678
Securities Deliverable under Reverse Repo A/c (by contra)	99.0496	
Securities Purchased under Reverse Repo A/c (by contra)		99.0496

4. Ledger entries for the adjustment accounts

Securities Receivable under Repo A/c

Debit		Credit	
To Securities Sold under Repo A/c (repo 1 st leg)	99.0496	By Securities Sold under Repo A/c (repo 2 nd leg)	99.0496

Securities Sold under Repo A/c

Debit		Credit	
To Securities Receivable under Repo A/c (repo 2 nd leg)	99.0496	By Securities Receivable under Repo A/c (repo 1 st leg)	99.0496

Securities Purchased under Repo A/c

Debit		Credit	
To Securities Deliverable under Reverse Repo A/c (reverse repo 1 st leg)	99.0496	By Securities Deliverable under Reverse Repo A/c (reverse repo 2 nd leg)	99.0496

Securities Deliverable under Repo A/c

Debit		Credit	
To Securities Purchased under Reverse Repo A/c (reverse repo 2 nd leg)	99.0496	By Securities Purchased under Reverse Repo A/c (reverse repo 1 st leg)	99.0496

5. If the balance sheet date falls during the tenor of the repo, participants may use the transit accounts, i.e. Repo Interest Payable A/c and Reverse Repo Interest Receivable A/c to record the accrued interest and reverse the same the following day. The balances in the repo interest receivable and payable shall be taken to the P & L Account with appropriate entries passed in the Balance sheet, as below:-

Transaction Leg	1st leg	Balance Sheet Date	2nd leg
Dates	28-Mar-10	31-Mar-10	02-Apr-10

a) Entries in the Books of Repo Seller (borrower of funds) on 31-Mar-10

Account Head	Debit	Credit
Repo Interest Expenditure A/c [Balances under the account to be transferred to P & L]	0.0543 (being the repo interest for 4 days)	
Repo Interest payable A/c		0.0543

Account Head	Debit	Credit
P & L A/c	0.0543	
Repo Interest Expenditure A/c		0.0543

b) Reversal of entries in the Books of Repo Seller (borrower of funds) on 01-Apr-10

Account Head	Debit	Credit
Repo Interest Payable A/c	0.0543	
Repo Interest Expenditure		0.0543

c) Entries in books of Repo Buyer (Lender of Funds) on 31-Mar-10

Account Head	Debit	Credit
Reverse Repo Interest Receivable A/c	0.0543	
Reverse Repo Interest Income A/c [Balances under the account to be transferred to P & L]		0.0543 (Being the repo interest for 4 days)

Account Head	Debit	Credit
Reverse Repo Interest Income A/c	0.0543	
P & L A/c		0.0543

d) Reversal of entries in the Books of Repo Buyer (Lender of Funds) on 01-Apr-10

Account Head	Debit	Credit
Reverse Repo Interest Income A/c	0.0543	
Reverse Repo Interest Receivable A/c		0.0543

List of Circulars consolidated by the Master Circular

No.	Circular No.	Date	Relevant para no. of the circular	Subject	Para no. of the master circular
1.	<u>DBOD.No.FSC.BC.69/C.469- 90/91</u>	Jan 18, 1991	1,2,4	Portfolio Management on behalf of clients	1.3. 3
2.	<u>DO.DBOD.No.FSC.46/C.469- 91/92</u>	July 26, 1991	4(i), (ii), (iii), (iv), (v), (iv)	Investment portfolio of banks- Transaction in securities	1.2 (i)
3.	<u>DBOD.No.FSC.BC.143A/24.48. 001/ 91-92</u>	June 20, 1992	3(I), 3(I)- (ii)- (iii)- (iv)- (v)- (xi)- (xii)- (xvi)- (xvii), 3(II), 3(III), 3(V)- (i)- (ii)- (iii), (3) & (4)	Investment portfolio of banks- Transaction in securities	1.2 (ii), (iii) & (iv), 1.2.2, 1.2.3, 1.2.5, 1.2.6, 1.2.7
4.	<u>DBOD.No.FSC.BC.11/24.01.009/ 92- 93</u>	July 30, 1992	3,4,5,6	Portfolio Management on behalf of clients	1.3.3
5.	<u>DBOD.No.FMC/BC/17/24.48.001. 92/93</u>	Aug 19, 1992	2	Investment portfolio of banks- Transaction in securities	1.3.2
6.	<u>DBOD.FMC.BC.62/27.02.001/ 92-93</u>	Dec 31, 1992	1	Investment portfolio of banks- Transaction in securities	1.2.6
7.	<u>DBOD.No.FMC.1095/27.01.002/93</u>	April 15, 1993	1 & enclosed format	Investment portfolio of banks- Reconciliation of holdings	1.3.1 & Anne- xure VI
8.	<u>DBOD.No.FMC.BC.141/27.02.006/ 93/94</u>	July 19, 1993	Annex	Investment portfolio of banks-	Anne- xure II

				Transaction in securities- Aggregate contract limit for individual brokers- Clarifications	
9	<u>DBOD.No.FMC.BC.1/27.02.001/ 93-94</u>	Jan 10, 1994	1	Investment portfolio of banks- Transaction in securities- Bouncing of SGL transfer forms- Penalties to be imposed.	1.2.2
10	<u>DBOD.No.FMC.73/27.07.001/ 94-95</u>	June 7, 1994	1,2	Acceptance of deposits under Portfolio Management Scheme	1.3.3
11.	<u>DBOD.No.FSC.BC.130/24.76.002/ 94-95</u>	Nov 15, 1994	1	Investment portfolio of banks- Transaction in securities-Bank Receipts (BRs)	1.2.3
12.	<u>DBOD.No.FSC.BC.129/24.76.002/ 94-95</u>	Nov 16, 1994	2 & 3	Investment portfolio of banks- Transaction in securities-Role of brokers	1.2.6
13.	<u>DBOD.No.FSC.BC.142/24.76.002/ 94-95</u>	Dec 9, 1994	1& 2	Do	1.2.6
14.	<u>DBOD.No.FSC.BC.70/24.76.002/ 95-96</u>	June 8, 1996	2	Retailing of Government Securities	1.2.4
15.	<u>DBOD.No.FSC.BC.71/24.76.001/ 96</u>	June 11, 1996	1	Investment portfolio of banks- Transaction in securities	1.2.2
16.	<u>DBOD.No.BC.153/24.76.002/96</u>	Nov 29, 1996	1	Do	1.2.6
17.	<u>DBOD.BP.BC.9/21.04.048/98</u>	29 Jan 1997	3	Prudential norms - capital adequacy, income	5.1 (iii) & (iv)

				recognition, asset classification and provisioning.	
18.	DBOD.BP.BC.32/21.04.048/97	April 12, 1997	1&2	Do	5.1 (i) &(ii)
19.	DBOD.FSC.BC.129/24.76.002-97	Oct 22, 1997	1	Retailing of Government Securities	1.2.4
20.	DBOD.No.BC.112/24.76.002/1997	Oct 14, 1997	1	Investment portfolio of banks- Transaction in securities-Role of brokers	1.2.6
21.	DBOD.BP.BC.75/21.04.048/98	4 Aug 1998	All	Acquisition of Government and other approved securities - Broken Period Interest, - Accounting Procedure	5.2
22.	DBS.CO.FMC.BC.1/22.53.014/98-99	July 7, 1999	1	Investment portfolio of banks – Transactions in securities	1.3.1(i)
23.	DBS.CO.FMC.BC.18/22.53.014/ 99-2000	Oct 28, 1999	2, 3, 4 & 5	Do	1.2.2
24.	DBOD.No.FSC.BC.26/24.76.002/ 2000	Oct 6, 2000	2	Sale of Government securities allotted in the auctions for Primary issues	1.2(i)(b)
25.	DBOD.BP.BC.32/21.04.048/ 2000-01	Oct 16, 2000	All	Guidelines on classification and valuation of investments.	2 & 3
26.	DBOD.FSC.BC.No.39/24.76.002/ 2000	Oct 25, 2000	1	Investment portfolio of banks- Transaction in securities-Role of brokers	1.2.6
27.	Dir.BC.107/13.03.00/2000-01	April 19, 2001	6	Monetary and Credit Policy for the year 2000- 2002 - Interest	5.3

				Rate Policy	
28.	DBOD.BP.BC.119/21.04.137/ 2000-2001	May 11, 2001	Annex - 5 & 12	Bank financing of equities and investments in shares - Revised guidelines	1.2, 1.2.5 1.3, 1.3.1
29.	DBOD.BP.BC.127/21.04.048/ 2000- 01	June 7, 2001	All	Non- SLR Investments of Banks	1.2.8 Anne- xure III
30.	DBOD.BP.BC.61/21.04.048/ 2001-02	Jan 25, 2002	All	Guidelines for investments by banks/Fis and Guidelines for financing of restructured accounts by banks/FIs	1.2.8 (iv)
31.	DBOD.No.FSC.BC.113/24.76.002/ 2001-02	June 7 2002	All	On Investment Portfolio of Banks Transaction in Govt. Securities	1.3.4
32.	DBS.CO.FMC.BC.7/22.53.014/ 2002-03	Nov 7, 2002	Para 2	Operation of investment portfolio by banks- submission of concurrent audit reports by banks	1.2.7(c)
33.	DBOD.No.FSC.BC.90/24.76.002/ 2002-03	March 31 2003	All	Ready Forward Contracts	1.2.1(i), (ii) and (iii)
34.	IDMC.3810/11.08.10/2002-03	March 24 2003	All	Guidelines for uniform accounting for Repo / Reverse Repo transactions	4, Anne- xure VII & Anne- xure VIII
35.	DBOD.BP.BC.44/21.04.141/03-04	Nov 12, 2003	All	Prudential guidelines on banks' investment in non-SLR securities	1.2.8 Annex IV, V
36.	DBOD.BP.BC.53/21.04.141/03-04	Dec 10, 2003	All	do	1.2.8
37.	DBOD.FSC.BC.59/24.76.002 /03-04	Dec 26, 2003	All	Sale of Government securities allotted	Anne- xure

				in the auctions for primary issues on the same day	I C
38.	IDMD.PDRS.05/10.02.01/ 2003-04	Mar 29, 2004	3, 4, 6 & 7	Transactions in Government Securities	1.2(i) (a)
39.	IDMD.PDRS/4777/10.02.01/ 2004-05	May 11, 2005	3	Sale of securities allotted in primary issues	1.2(i) (b)
40.	IDMD.PDRS/4779/10.02.01/ 2004-05	May 11, 2005	2,3,4,5	Ready forward contracts	1.2.1 (b), 1.2.1 (c)
41.	IDMD.PDRS/4783/10.02.01/ 2004-05	May 11, 2005	3	Government securities transactions - T+1 settlement	1.2(i) (c)
42.	DBOD.FSC.BC.28/24.76.002/ 2004-05	Aug 12, 2004	2	Transactions in Government securities	1.2(i)(a)
43.	DBOD.BP.BC. 29/21.04.141/ 2004-05	Aug 13, 2004	2(b) of Annex	Prudential norms - State Government guaranteed exposures	3.5.2
44.	DBOD.Dir.BC.32/13.07.05/ 2004-05	Aug 17, 2004	2	Dematerialisation of banks' investment in equity	5.3
45.	DBOD.BP.BC.37/21.04.141/ 2004-05	Sep 2, 2004	1(i) & (ii)	Prudential norms on classification of investment portfolio of banks	2.1 (ii) & (iii)
46.	DBOD.FSD.BC.No.31/24.76.002/ 2005-06	Sep 1, 2005	2, 3	NDS-OM - Counterparty Confirmation	1.2.5 (i) (c)
47.	DBOD.BP.BC.38/21.04.141/ 2005-06	Oct 10, 2005	All	Capital Adequacy - Investment Fluctuation Reserve	3.4
48.	IDMD.No.03/11.01.01(B)/2005-06	Feb 28, 2006	2,3,4,5	Secondary Market transactions in Government Securities- Intra day short selling	1.2 (i) (a)

49.	IDMD.No.3426 /11.01.01 (D)/ 2005-06	May 3, 2006	All	'When Issued' transactions in Central Government Securities'	1.2 (i) (a)
50	DBOD.No.BP.BC.27/21.01.002/2006-07	Aug 23, 2006	2, 4	Prudential guidelines – Bank's investments in VCF	3.9
51	IDMD.No.2130/11.01.01(D)/2006-07	Nov 16, 2006	All	When Issued transactions in Central Government Securities	1.2(i)(a)
52	DBOD.No.FSD.BC.46/24.01.028/2006-07	Dec 12, 2006	16B(ii)	Financial Regulation of Systemically Important NBFCs and Bank's Relationship with them	1.3.3(i)
53	IDMD.No. /11.01.01(B)/2006-07	Jan 31, 2007	All	Secondary Market transactions in Government Securities- Short selling	1.2.(i)a
54	Mailbox Clarification	July 11, 2007	All	HTM Securities	3.1.(i)
55	DBOD.No.BP.BC.56/21.04.141/2007-08	December 6, 2007	All	Limits on investment in unrated Non-SLR securities- infrastructure bonds	1.2.7
56.	DBOD.No.BP.BC.86/21.04.141/2007-08	May 22, 2008	All	Valuation of securities	3.7.1
57.	Mailbox Clarification	October 10, 2008	All	Transfer of Securities from One Category to Another	2.3 (iv)
58.	Mailbox Clarification	February 6, 2009	All	Non-SLR Securities	1.2.12

59.	<u>Mailbox Clarification</u>	February 5,2009	All	Unlisted Non-SLR Securities	1.2.13
60.	<u>Mailbox Clarification</u>	March 16,2009	All	Classification of Securities	3.2
61.	<u>Mailbox Clarification</u>	February 11,2009	All	Investment Portfolio of Banks	Annex 1(c)(i)
62.	RBI/2009-10/102 IDMD.DOD.No. 334/ 11.08.36/ 2009-10	July 20, 2009	All	Ready Forward contract in G-Sec	1.2.2
63.	<u>Mailbox Clarification</u>	September 3, 2009	All	Waiver of trade confirmation in Government Securities Transactions in OTC market	1.1.5 (c)
64.	RBI/2009-10/184 IDMD No.1764 /11.08.38/2009-10	October 16, 2009	All	OTC trades in Corporate debt securities	1.2.21
65.	<u>Mailbox Clarification</u>	November 6, 2009	All	Clarification on Capital Reserve Account and Special Reserves created under Income Tax Act, 1961	2.1 (vi)
66.	<u>Mailbox Clarification</u>	December 23, 2009	All	Treatment for investment in Rural Housing Development Fund (RHDF) of National Housing Bank	2.1 (iv) (c)
67.	RBI/2009-10/284 IDMD.DOD. 05 /11.08.38/2009-10	January 8, 2010	All	Repo in Corporate Debt Securities	1.2.22
68.	IDMD/4135/11.08.043/2009-10	March 23, 2010	All	Uniform accounting for repo-reverse repo transactions in G-Sec	Para no 4 of master circular

69.	RBI/2009-10/360 IDMD. DOD. 07 /11.01.09/2009-10	March 25, 2010	All	Guidelines on Stripping/ reconstitution of G-Sec	1.1.1
70.	<u>Mailbox Clarification</u>	March 30, 2010	All	Clarification on investment in debentures in the nature of advances	2.1 (ii) (c) and 3.7.1
71.	RBI/2009-10/403 IDMD.DOD.08 /11.08.38/2009-10	April 16, 2010	All	Ready Forward contract in Corporate Debt Securities	1.2.22 and Annex I-E
72.	DBOD.No.BP.BC. 98/ 21.04.141/ 2009-10	April 23, 2010	All	Investment in Unlisted Non-SLR Securities	1.2.10
73.	DBOD.No.BP.BC. 97/ 21.04.141/ 2009-10	April 23, 2010	All	Classification of investments by banks in Bonds issued by Companies engaged in Infrastructure activities	2.1