ANNEX

Guidelines on investments by RRBs
in Non-SLR Debt Securities

Coverage

1.These guidelines cover banks' investments in Non-SLR debt instruments/ securities issued by corporates, banks, All-India Financial Institutions and State and Central Government sponsored institutions, etc. The guidelines will apply to investments both in the primary market as well as the secondary market.

a) These guidelines apply to all types of bonds, including

i. Capital gains bonds;

ii. Bonds eligible for priority sector status;

iii. Bonds issued by Central or State public sector undertakings, with or without government guarantees; and

iv. Bonds issued by banks and financial institutions.

b) These guidelines will not apply to the following categories of non-SLR investment:

i.Units of equity oriented mutual fund schemes, viz. those schemes where any part of the corpus can be invested in equity;

ii. Venture Capital funds;

iii. Commercial paper; and

iv. Certificates of deposit.

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

2.Definitions of a few terms used in these guidelines have been furnished in Appendix I with a view to ensure uniformity in approach while implementing the guidelines.

Regulatory requirements

3. Banks should not invest in Non-SLR debt securities of original maturity of less than one-year other than commercial paper and certificates of deposits.

4. 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.

5. Banks must not invest in unrated debt securities, unlisted securities and unlisted shares of All-India Financial Institutions (AFIs)

6. The Securities Exchange Board of India (SEBI), vide their circular dated September 30, 2003, have stipulated requirements to be complied with by listed companies for issuing 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. Further, the debt securities should carry a credit rating of not less than investment grade from a Credit Rating Agency registered with the SEBI. Banks should ensure that they make all fresh Non-SLR debt investments only in listed debt securities of companies which comply with the requirements of the SEBI circular dated September 30, 2003.

Internal assessments

7. Since non-SLR securities are mostly in the form of credit substitutes, banks are advised to (i) subject all their investment proposals relating to non-SLR securities to credit appraisal on par with their credit proposals, irrespective of the fact that the proposed investments may be in rated securities, (ii) make their own internal credit analysis and rating even in respect of rated issues and not to entirely rely on the ratings of external agencies, and (iii) 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.

Fixing of prudential limits

8. The Board of Directors of banks should fix a prudential limit for their total investment in non-SLR securities subject to existing limits prescribed by RBI and sub-limits for the following listed debt securities:

a) bonds of public sector undertakings

b) bonds of All-India Financial Institutions

c) unsecured redeemable bonds floated by nationalised banks

d) infrastructure bonds floated by All India financial Institutions

e) units of UTI.

While there will be no ceiling on investments covered under a) to d) above as per our circular RPCD.No.RRB.BC.76/03.05.34/96-97 dated December 13, 1996, the investments covered under e) should not exceed 5 per cent of incremental deposits at the end of the preceding financial year.

9. Banks which have exposure to investments in non-SLR securities in excess of the prudential limit prescribed above as on 31st March 2003 should not make any fresh investment in such securities till they ensure compliance with the above prudential limit.

10. 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 illiquidity.

Role of Boards

11. 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 non-SLR investments. Banks should put in place proper risk management systems for capturing and analysing the risk in respect of non-SLR investments 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.

12. The Board should devise a system to ensure that the limits prescribed in paragraph 8 above are scrupulously complied. The Boards should appropriately address the issue of ensuring compliance with the prudential limits on an ongoing basis, including breaches, if any, due to rating migration.

13. Boards of banks should review the following aspects of non-SLR investment twice a year:

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

Disclosures

14. In order to help in 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. When banks themselves raise debt through private placement, they should also file a copy of the offer document with CIBIL.

15. 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 Appendix II.

Demat Form

16. RRBs should make investment in non-SLR securities in dematerialized form only.

Trading and settlement in debt securities

17.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.

18. Considering the time required by issuers to get their existing unlisted debt issues listed on the stock exchanges, the following transition time is provided :

i. Investment by banks in units of mutual fund schemes where the entire corpus is invested in debt securities will be outside the purview of the above guidelines until December 31 ,2004.

ii. 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% 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.

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Appendix I

Guidelines on investments by RRBs in non-SLR investments portfolio – Definitions
(Vide paragraph 2 of the Guidelines)

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 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 <u>unrated securities</u>.

3. The <u>investment grade ratings</u> 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' debt security is a security which is listed in a stock exchange. If not so, it is an 'unlisted' debt security.

5. A <u>non-performing investment</u> (NPI), similar to a non-performing advance (NPA), is one where

   i) Interest/ instalment (including maturity proceeds) is due and remains unpaid for more than 180 days. The delinquency period would become 90 days with effect from 31st March 2004.

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 , 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 issued by the same issuer would also be treated as NPI.

Appendix II

Prudential guidelines on management of the non-SLR investment portfolio by RRBs – Disclosures requirements

(vide paragraph 15 of the Guidelines)

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)

No. (1)	**Issuer** (2)	**Amount** (3)	**Extent of private placement** (4)	**Extent of 'below investment grade' Securities already invested** (5)	**Extent of 'unrated' securities, already invested** (6)	**Extent of 'unlisted' securities** (7)
1	P S Us					
2	F I s					
3	Banks					
4	Private corporates					
5	Others					
6	Provision held towards depreciation		X X X	X X X	X X X	X X X
	Total *					

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

a. Shares
b. Debentures & Bonds
c. Others

2. Amounts reported under columns 4, 5 and 6 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	