

June 22, 2004

To Residuary Non-Banking Companies (RNBCs)

Dear Sirs,

Maintenance of directed investments by RNBCs

Please refer to the Notification No. DFC. 55/DG(O)-87 dated May 15, 1987 containing directions titled as 'Residuary Non-Banking Companies (Reserve Bank) Directions, 1987' (RNBC Directions). As a measure of security for depositors of RNBCs, these directions require RNBCs to invest the amount of deposits in the manner prescribed therein.

2. In terms of the directions mentioned above, the RNBCs are presently required to invest the amount of aggregate liabilities to the depositors (**ALD**) in the following manner:

- | | |
|--------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| (i) Directed investments | Not less than 70 per cent of their aggregate liabilities to depositors (ALD) in the manner prescribed by RBI under Paragraphs 6 (1)(a) and (b) of the RNBC Directions. |
| (ii) Discretionary investments | Not more than 20 per cent or ten times the net owned fund (NOF), whichever is lower as per decision of the board of directors of RNBCs under paragraph 6 (1) (c) of the RNBC Directions. |

The market value of all the above investments should not be less than the ALD outstanding as at the last working day of the second preceding quarter.

3. Reserve Bank of India has recently reviewed the current regulations on investments by RNBCs. The review has brought out the need for rationalization of the pattern of directed investments of RNBCs and reduce the overall systemic risk in the financial sector. It has, therefore, been considered necessary in the public interest and the interest of the RNBCs to modify and rationalise the directed and discretionary investments by RNBCs. Details of the rationalised measures are given below. These measures are expected to impart greater liquidity and safety to the investments of RNBCs and thus enhance protection available to the depositors.

4. The investment pattern of the directed investments and discretionary investments as contained in the RNBC Directions have since been modified as under:

(i) Fixed Deposits /Certificates of Deposit of Scheduled Commercial Banks and Certificates of Deposit of Financial Institutions (10% component)

The RNBCs may presently invest an amount not less than 10 per cent of the ALD in the Fixed Deposits (FDs) and Certificates of Deposit (CDs) of scheduled commercial banks (SCBs) and Financial Institutions (FIs). It has been decided that the RNBCs may invest only in (i) the FDs and CDs of SCBs; and (ii) CDs of specified Financial Institutions (FIs) provided such CDs are rated not less than AA+ or its equivalent by an approved credit rating agency. However exposure of the RNBC to one scheduled commercial bank may not exceed 1% of the aggregate deposit liabilities of the bank as on 31 March of the previous accounting year. Exposure to any one specified FI may not exceed 1% of the ALD of the RNBC.

(ii) Government Securities/Bonds/debentures/units of Mutual Funds (70% component)

(a) Investment in securities issued by Central or State Governments as part of their market borrowing programme.

Presently RNBCs are required to invest in approved securities (not less than 10% of ALD) under Section 45-IB of the RBI Act. In order to further strengthen the protection available to the depositors, it has been decided that, the RNBCs should further invest as part of their investments under the RNBC Directions, in Central and State Government securities issued by the Governments in the course of their market borrowing programme; an amount which shall not be less than 15% of the outstanding ALD.

(b) Requirement of rating and listing of the bonds and debentures

In order to enhance the liquidity and safety of the portfolio, it has been decided that investment in debt securities should be confined to those having minimum AA+ or equivalent grade rating and listed on one of the stock exchanges. However bonds/debentures of holding companies/subsidiary companies/companies in the same group will not be eligible for investment under this category. If the rating of any instrument is downgraded below the prescribed grade or it is delisted, the instrument shall be taken out of the eligible securities and the shortfall, if any, due to the above in compliance with investment requirements in the 70% category would have to be made good before making any other investments.

(c) Investment in units of only debt oriented Mutual Fund schemes

The investment in units of mutual funds would be in those fund schemes only which are debt oriented, subject to the aggregate investment in the mutual funds not exceeding 10% and in one mutual fund not exceeding 2% of ALD. The investments in equity oriented mutual fund schemes would not be eligible under directed investments in securities.

(iii) Discretionary Investments

Presently RNBCs are permitted to invest not more than 20 percent of the aggregate amount of liabilities to the depositors or ten times the net owned fund of the company, whichever is less, in any manner which in the opinion of the company is safe as per the approval of its Board of Directors. It has been seen that the aggregate amount of discretionary investment of the RNBCs has been generally not more than three times the Net Owned Funds (NoF). It is felt that such companies should use their own funds for discretionary investments and the present limit of discretionary investment from the deposits may be gradually phased out and the entire deposits may be invested in the manner stated above in paragraphs (i) and (ii). In this regard the following road map is prescribed.

(a) From the quarter April to June 2005 and onwards, RNBCs will be permitted to invest only to the extent of 10% of the ALD as at the second preceding quarter (i.e. for the quarter April to June 2005, ALD as on December 31, 2004), or one time their NoF, whichever is lower, in the manner which in the opinion of the company is safe as per the approval of its Board of Directors.

(b) From the quarter April to June 2006 and onwards this limit would stand abolished and RNBCs would not be permitted to invest any amount out of the ALD as at the second preceding quarter, as per their discretion. Thus from the quarter April to June 2006 and onwards the RNBCs will be required to invest entire amount of ALD as at the second preceding quarter, in the directed investments.

5. Transitional Provisions

The provisions during the transition period would be as under:

(i) The revised pattern of investments will come into force from the quarter beginning July 2004. However, the reduction in discretionary investments shall come into effect in a phased manner from April 1, 2005.

(ii) The existing investments may continue to be held till their sale/maturity but are not permitted to be renewed / rolled over.

(iii) The companies may submit to Regional Offices of the Department of Non-Banking Supervision, Reserve Bank of India, under the jurisdiction of which their Registered office is located, the status of their investments

as on March 31, 2004 in terms of the revised pattern and also submit an action plan within 30 days of the notification for compliance with the revised requirements. The Central Office of RBI will take a view on the proposed action plan and communicate appropriately.

6. The changes in the directions have been explained in the chart given in the Annexure. A copy of the amending Notification No. DNBS. 178 / CGM (DSN) - 2004 dated June 22, 2004 issued by the Bank for giving effect to the above changes is enclosed for your compliance.

7. Please acknowledge receipt to the Regional Office under whose jurisdiction the registered office of your company is located.

Yours faithfully,

(D.S. Nagi)
Chief General Manager

Encls: As above

AnnexureChart showing the revised investment pattern for RNBCs

Investments	As % of Aggregate Liabilities to Depositors (ALD) from quarter beginning April 2005 up to quarter ending March 2006	From Quarter beginning April 1, 2006
1	2	3
(i) Investments in (a) **FDs/CDs of SCBs (b) **FDs of FIs (c) **CDs of FIs	Not less than 10% <i>Nil</i> <i>Rating not less than AA+ or its equivalent</i>	Not less than 10% <i>Nil</i> <i>Rating not less than AA+ or its equivalent</i>
(ii) investments in (a) *Central/State Government securities (b) bonds/debentures <i>rated minimum AA+ grade or equivalent by an approved rating agency and listed on a stock exchange.</i> (c) Units of debt oriented mutual funds (under SEBI Regulations)	<i>Aggregate investment not less than 70%</i> Not less than 15% Not more than 10% subject to not more than 2% in any one mutual fund.	<i>Aggregate investment not less than 80%</i> Not less than 15% Not more than 10% subject to not more than 2% in any one mutual fund.
Total	Not less than 80%	Not less than 90%
(iii) Other investments (Discretionary Investments)	Not more than 10% of the aggregate deposit liabilities or equal to NoF, whichever is lower.	Nil
(iv) Balance of the aggregate deposit liabilities	In any of the above mentioned categories at (i) and (ii) above	
Grand Total the deposit liabilities	Not Less than 90%	Not less than 90%

* Securities issued by Central or any of the State Governments in the course of their market borrowing programme.

** Exposure of the RNBC to one scheduled commercial bank may not exceed 1% of the aggregate deposit liabilities of the bank as on 31 March of the previous accounting year. Exposure to any one FI may not exceed 1% of the deposit liabilities of the RNBC.

Notes:

- a) **The existing investments, not in conformity with the above directions, may continue till their sale / maturity but are not permitted to be renewed / rolled over.**
- b) **If the rating of any security is downgraded below the required rating of AA+ grade or is delisted, the security shall be taken out of the eligible security. The shortfall if any shall be made good before making any other investment.**
- c) **Bonds/debentures of holding /subsidiary companies or companies in the same group would not qualify for investments under paragraph (ii) above.**

RESERVE BANK OF INDIA
DEPARTMENT OF NON-BANKING SUPERVISION
CENTRAL OFFICE
CENTRE I, WORLD TRADE CENTRE
CUFFE PARADE, COLABA
MUMBAI 400 005

NOTIFICATION No. DNBS. 178/CGM (DSN)-2004 dated June 22, 2004

The Reserve Bank of India, having considered it necessary in the public interest and being satisfied that, for the purpose of enabling the Bank to regulate the credit system to the advantage of the country, it is necessary to amend the Residuary Non-Banking Companies (Reserve Bank) Directions, 1987, hereby, in exercise of the powers conferred by Sections 45J, 45JA, 45K and 45L of the Reserve Bank of India Act, 1934 (2 of 1934) and all the powers enabling it in this behalf, directs that the said Directions contained in Notification No.DFC.55/DG(O)-87 dated the 15th May 1987 shall, with immediate effect, be amended as follows, namely :-

1. For sub-paragraph (1) of paragraph 6, the following sub-paragraph shall be substituted, namely, -

“6. On and from July 1, 2004 -

(1) Every residuary non-banking company shall invest and continue to invest an amount including the amount invested in assets under Section 45-IB of the Reserve Bank of India Act, 1934 (2 of 1934), which at the close of business on any day of the quarter ending September 30, 2004 and thereafter, on any day of each quarter shall not be less than the aggregate amounts of the liabilities to the depositors, outstanding at the close of business on the last working day of the second preceding quarter (whether or not such amounts have become payable) in securities or in other types of investments which are unencumbered and valued at a price not exceeding the current market price, in the following manner, namely, -

(a) not less than 10 percent of the aggregate amount of liabilities to depositors in fixed deposits/certificates of deposit of scheduled commercial banks; or in certificates of deposit of specified financial institutions, provided the certificates are rated not less than AA+ or its equivalent by an approved credit rating agency, or partly in any of these Fixed Deposits/Certificates of Deposit so rated;

(b) not less than 70 percent of the aggregate amount of liabilities to depositors in securities of any State Government or Central Government issued by them in the course of their market borrowing programme, or in bonds or debentures (rated not less than AA+ or equivalent by an approved credit rating agency and listed on a recognized stock exchange) of any other company incorporated under the Companies Act, 1956 (1 of 1956) or in the manner at clause (a) or in the debt oriented schemes of mutual funds subject, however, to the conditions that

(i) not less than 15 per cent of the aggregate amount of the liabilities to the depositors shall be invested in any securities of any State Government or Central Government issued in the course of market borrowing programme;

(ii) not more than two percent of the aggregate amount of the liabilities to the depositors shall be invested in any one debt oriented Mutual Fund which is governed by the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996 and the aggregate of such investment shall not exceed ten per cent of the aggregate amount of liabilities to the depositors:

Provided that on and from July 1, 2004, a residuary non-banking company which does not comply with the above requirement, shall not make any investment in other securities till the shortfall in this category of investments is made good.

Provided that in the event of downgrading of credit rating below the prescribed grade of any bond or debenture, the bond or debenture shall become ineligible for compliance with the above requirement and shortfall, if any, in the compliance with the above paragraph arising from such downgrading of the rating shall be made good before making any further investments in the securities as provided for in clause (c) or (d)."

Provided that debenture/bonds issued by holding company/subsidiary company/company in the same group shall not qualify for such investment.

(c) for the period prior to March 31, 2005, not more than 20 percent of the aggregate amount of liabilities to the depositors or ten times the net owned fund of the company, whichever is less, may be invested in any manner which in the opinion of the company is safe as per the approval of the board of directors of the company;

(d) on and from April 1, 2005 not more than ten percent of the aggregate amount of liabilities to the depositors or one time the net owned fund of the company, whichever is less, may be invested in any manner which in the opinion of the company is safe as per the approval of the board of directors of the company;

(e) on and from April 1, 2006 the aggregate amount of liabilities to the depositors shall be invested in accordance with sub-paragraph (a) or sub-paragraph (b) only."

2. For the Explanation to paragraph 6, the following Explanation shall be substituted, namely:

“Explanation

- (i) 'net owned fund' means net owned fund as defined under section 45-IA of the Reserve Bank of India Act, 1934 (2 of 1934) including the paid up preference shares which are compulsorily convertible into equity ;
- (ii) "aggregate amounts of liabilities" shall mean total amount of deposits received together with interest, premium, bonus or other advantage by whatever name called, accrued on the amount of deposits according to the terms of contract.
- (iii) "quarter" means the period of three months, ending on the last day of March, June, September or December.
- (iv) "approved credit rating agencies" mean
 - (a) The Credit Rating Information Services of India Ltd. (CRISIL).
 - (b) Investment Information and Credit Rating Agency of India Ltd. (ICRA)
 - (c) Credit Analysis & Research Ltd. (CARE)
 - (d) FITCH Ratings India Private Ltd. (Fitch India)"
- (v) 'scheduled commercial bank' means a bank included in the Second Schedule to the Reserve Bank of India Act, 1934 (2 of 1934) excluding a regional rural bank or a co-operative bank.
- (vi) 'Government company' means a company as defined under section 617 of the Companies Act, 1956 (1 of 1956).
- (vii) 'specified financial institution' means institutions listed in the schedule "D" to this Notification.
- (viii) The words 'holding company', 'subsidiary company', 'company in the same group' shall have the same meaning as assigned to them in the Companies Act, 1956."

(D.S.Nagi)
Chief General Manager

Schedule "D"

List of specified Financial Institutions

(Please see item (vii) in the Explanation to paragraph 2 of Notification No. DNBS.178 / CGM (DSN) - 2004 dated June 22, 2004)

1. IDBI
2. IFCI Ltd.
3. IIBI Ltd.
4. TFCI Ltd.
5. IDFC Ltd.
6. EXIM Bank
7. NHB
8. SIDBI
9. NABARD
10. PFC Ltd.
11. REC Ltd.
12. IRFC Ltd.
13. IREDA Ltd.
14. NEDFi Ltd.
15. HUDCO Ltd.
16. UTI
17. LIC
18. GIC
19. NIC
20. NIA
21. OIC
22. UII

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