

Master Circular

on

Investments By Primary (Urban) Co-operative Banks (Updated up to June 30, 2006)

(The Master Circular is also available at RBI website
www.mastercirculars.rbi.org.in
and may be down loaded from there)



RESERVE BANK OF INDIA

**Urban Banks Department,
Central Office
Mumbai**

RBI/2006-07/66

UBD.BPD. (PCB). MC.No 8 /16.20.000/2006-07

July 12, 2006

Chief Executive Officers of
All Primary (Urban) Co-operative Banks

Dear Sir,

Master Circular on Investments by Primary (Urban) Co-operative Banks

Please refer to our Master Circular UBD.BPD.(PCB).MC.No.13/16.20.00/2005-06 dated December 29, 2005 on the captioned subject (available at RBI website www.rbi.org.in). The enclosed Master Circular consolidates and updates all the instructions/guidelines on the subject upto June 30, 2006.

Yours faithfully,

(N.S. Vishwanathan)
Chief General Manager In-charge

Master Circular on Investments by Primary (Urban) Co-op. Banks

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Master Circular on Investments by Primary (Urban) Co-operative Banks

1 RESTRICTIONS ON HOLDING SHARES IN OTHER CO-OPERATIVE SOCIETIES

1.1 Section 19 of the Banking Regulation Act, 1949 (as applicable to co-operative societies) stipulates that no co-operative bank shall hold shares in any other co-operative society except to such extent and subject to such conditions as the Reserve Bank may specify in that behalf. However nothing contained in the section applies to -

1.1.1 shares acquired through funds provided by the state government for that purpose;

1.1.2 in the case of a central co-operative bank, the holding of shares in the state co-operative bank to which it is affiliated; and

1.1.3 in the case of a primary (urban) co-operative bank (pcb), holding of shares in the central co-operative bank to which it is affiliated or in the state co-operative bank of the state in which it is registered.

1.2 In pursuance of the powers conferred by section 19 read with section 56 of the said Act, the Reserve Bank has specified that the extent and conditions subject to which co-operative banks may hold shares in any other co-operative society shall be as follows:

1.2.1 The total investments of a co-operative bank in the shares of co-operative institutions, other than those falling under any of the categories stated at paras 1.1.1 to 1.1.3 above, shall not exceed 2 per cent of its owned funds (paid-up share capital and reserves).

1.2.2 The investment of a bank in the shares of any one co-operative institution coming under para 1.2.1 above shall not exceed 5 per cent of the subscribed capital of that institution.

Note: When more than one co-operative bank contributes to the shares in a co-operative society falling under para 1.2.1, the limit of 5 per cent of the subscribed capital indicated above shall apply not in respect of the investment of each of the banks but in respect of the investment of all the banks taken together. In other words, the total investment of all the co-operative banks should be limited to 5 per cent of the subscribed capital of the enterprise concerned.

A co-operative bank should offer to make its contribution to the shares of a co-operative society coming under para 1.2.1 above only if the by-laws of the recipient society provide for the retirement of share capital contributed by it.

1.2.3 The retirement of the share capital contributed by a bank to the shares of any society coming under para 1.2.1 above should be completed in 10 equal annual instalments commencing from the co-operative year immediately following the year in which the concern commences business or production.

- 1.2.4 A co-operative bank should not, except with the permission of the Reserve Bank, contribute to the share capital of a society coming under category referred to in para 1.2.1 above, if it is situated outside its area of operation.
- 1.2.5 The above restrictions will not apply to holdings by co-operative banks of shares in non-profit making co-operative societies such as those formed for the protection of mutual interests, (e.g. co-operative banks' association) or for the promotion of co-operative education etc. (e.g. state co-operative union), or housing co-operatives for the purpose of acquiring premises on ownership basis, etc.

2 STATUTORY (SLR) INVESTMENTS

2.1 Act Provisions

2.1.1 In terms of provisions of section 24 of the Banking Regulation Act 1949, (As applicable to co-operative societies), every primary (urban) co-operative bank is required to maintain liquid assets which at the close of business on any day should not be less than 25 percent of its demand and time liabilities in India (in addition to the minimum cash reserve requirement).

2.1.2 The banks may hold such liquid assets in the form of cash, gold or unencumbered approved securities.

2.1.3 'approved securities' as defined by section 5(a) (i) & (ii) of the Banking Regulation Act, 1949 (AACS) mean -

- (i) Securities in which a trustee may invest money under clause (a), (b), (bb), (c) or (d) of Section 20 of the Indian Trust Act, 1882.
- (ii) Such of the securities authorised by the Central Government under clause (f) of Section 20 of the Indian Trust Act, 1882 as may be prescribed.

2.2 Holding in Government/other approved Securities

All primary (urban) co-operative banks are required to achieve certain minimum level of their SLR holdings in the form of government and other approved securities as percentage of their Net Demand and Time Liabilities (NDTL) as indicated below :

Sr. No	Category of bank	Minimum SLR holding in government and other approved securities as percentage of Demand and Time Liabilities
1.	Scheduled banks	25%

2.	Non-Scheduled banks a) with NDTL of Rs.25 crore & above b) with NDTL of less than Rs.25 crore	15% 10%
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2.2.1 In terms of notification UBD. PCB. 6657./ 16.26.000 / 2005-06 dated December 26, 2005 published in Part III of Section 4 of the Gazette of India (Extraordinary) dated December 31, 2005, the non-scheduled primary (urban) co-operative banks, having single branch-cum-head-office or having multiple branches within a single district, having a deposit base of Rs.100 crore or less are exempted from maintaining SLR in prescribed assets upto 15% of their DTL on keeping the required amount, in interest bearing deposits, with State Bank of India and its subsidiary banks and the public sector banks including Industrial Development Bank of India Ltd. Such exemption shall be in force upto March 31, 2008 and during this period UCBs should build up adequate infrastructure, risk management practices including human resource and technological up-gradation so as to reduce market related risk.

Manner of Holding Mandatory Investments

2.3.1 The Securities may be held in either of the three forms viz: (a) Physical scrip form, (b) Subsidiary General Ledger (SGL) Account and (c) in a dematerialised account with depositories (NSDL/CDSL, NSCCL). In respect of securities with SGL facility, the SGL account can be maintained in the bank's own name directly with the Reserve Bank of India, or in a Constituent SGL Account opened with any scheduled commercial bank/state co-operative bank/primary dealer (PD) or Stock Holding Corporation of India Ltd. (SHCIL)

2.3.2 Primary (urban) co-operative banks are not permitted to open and maintain CSGIL A/cs of other PCBs / other entities like charitable institutions, trusts etc.

2.3.3 Non-scheduled primary (urban) co-operative banks with DTL of Rs.25 crores & above and all scheduled primary (urban) co-operative banks are required to maintain investments in government securities only in SGL Accounts with Reserve Bank of India or in Constituent SGL Accounts with PDs, scheduled commercial banks, state co-operative banks, depositories and SHCIL.

3 INVESTMENT POLICY

3.1 Keeping in view the various regulatory/statutory and the bank's own internal requirements, primary (urban) co-operative banks should lay down,

with the approval of their Board of Directors, the broad Investment Policy and objectives to be achieved while undertaking investment transactions. The investment policy should be reviewed each year. The Board/Committee/Top Management should actively oversee investment transactions. Banks should not undertake any transactions on behalf of Portfolio Management Scheme (PMS) clients in their fiduciary capacity, and on behalf of other clients, either as custodians of their investments or purely as their agents.

- 3.2 The bank's investment policy should clearly define the authority to put through deals, procedure to be followed for obtaining sanction of the appropriate authority, putting through deals, fixing various prudential exposure limits, and reporting system.
- 3.3 The investment policy of the bank should include guidelines on the quantity (ceiling) and quality of each type of security to be held on its own investment account. Bank should clearly indicate the authority to put through investment deals and the reporting system to be adopted. It should be prepared strictly observing the instructions issued by the Registrar of Co-operative Societies and the Reserve Bank of India from time to time and clearly spell out the internal control mechanism, accounting standards, audit, review and reporting system to be evolved.
- 3.4 All the transactions should be clearly recorded indicating full details. The top management should undertake a periodic review of investment transactions in a critical manner and put up large transactions to the Board, for information.
- 3.5 A copy of the internal investment policy guidelines framed by the bank with the approval of its Board should be forwarded to the concerned Regional Office of the RBI, certifying that the policy is in accordance with the prescribed guidelines and the same has been put in place. Subsequent changes, if any, in the Investment Policy should also be advised to the Regional Office of the RBI.

4 GENERAL GUIDELINES

- 4.1 Primary (urban) co-operative banks should not undertake any purchase/sale transactions with broking firms or other intermediaries on principal to principal basis.
- 4.2 No sale transaction should be put through by banks without actually holding the security in its investment account i.e. under no circumstances banks should hold an oversold position in any security. However, scheduled primary (urban) co-operative banks may sell a government security already contracted for purchase, provided:
 - 4.2.1 the purchase contract is confirmed prior to the sale,
 - 4.2.2 the purchase contract is guaranteed by CCIL or the security is contracted for purchase from the Reserve Bank and,

- 4.2.3 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). Sale of government securities allotted to successful bidders in primary issues on the day of allotment, with and between CSGL constituent account holders is permitted.
- 4.3 For purchase of securities from the Reserve Bank through Open Market Operations (OMO), no sale transactions should be contracted prior to receiving the confirmation of the deal/advice of allotment from the Reserve Bank.
- 4.4 Only scheduled banks, not classified as Grade III/IV, are at present permitted to become members of NDS and participate in DVP III mode for settlement of Government Securities transactions.
- 4.5 Banks should exercise abundant caution to ensure adherence to these guidelines. The concurrent auditors should specifically verify the compliance with these instructions. The concurrent audit reports should contain specific observations on the compliance with the above instructions and should be incorporated in the monthly report to the Chairman and Managing Director/Chief Executive Officer of the bank and the half yearly review to be placed before the Board of Directors. CCIL will make available to all market participants as part of its daily reports, the time stamp of all transactions as received from NDS. The mid office/back office and the auditors may use this information to supplement their checks/scrutiny of transactions for compliance with the instructions. Any violation noticed in this regard should immediately be reported to the concerned Regional Office of Urban Banks Department and the Public Debt Office (PDO), Reserve Bank of India, Mumbai. Any violation noticed in this regard would attract penalties as currently applicable to the bouncing of Subsidiary General Ledger (SGL) forms even if the deal has been settled because of the netting benefit under DVP III, besides attracting further regulatory action as deemed necessary.
- 4.6 Banks successful in the auction of primary issue of government securities, may enter into contracts for sale of the allotted securities in accordance with the terms and conditions as indicated below :
- 4.6.1 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 selling bank should make suitable noting/stamping on the allotment advice indicating the sale contract number etc., the details of which should be intimated to the buying entity. The buying entity

should not enter into a contract to further resell the securities until it actually holds the securities in its investment account. Any sale of securities should be only on a T+0 or T+1 settlement basis.

- 4.6.2 The contract for sale of allotted securities can be entered into by banks only with entities maintaining SGL Account with Reserve Bank of India for delivery and settlement on the next working day through the Delivery versus Payment (DVP) system.
- 4.6.3 The face value of securities sold should not exceed the face value of securities indicated in the allotment advice.
- 4.6.3 The sale deal should be entered into directly without the involvement of broker/s.
- 4.6.5 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 Reserve Bank of India for verification. Banks should immediately report any cases of failure to maintain such records.
- 4.6.6 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 Board of Directors of the Bank once every month. A copy thereof should also be sent to the Regional Office concerned of Urban Banks Department.
- 4.6.7 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.
- 4.7 Banks should seek a scheduled commercial bank, a primary dealer, a financial institution, another primary (urban) co-operative bank, insurance company, mutual fund or provident fund, as a counter-party for their transactions. Preference should be given for direct deals with such counter parties. It will be desirable to check prices from the other banks or PDs with whom the primary (urban) co-operative bank may be maintaining constituent SGL Account (CSGL). The prices of all trades done in government securities, including those traded through Negotiated Dealing System, are also available at RBI website (www.rbi.org.in).
- 4.8 Scheduled urban co-operative banks may undertake retailing of Government Securities with non-bank clients, such as provident funds, non banking financial companies, high net worth individuals etc. subject to the following conditions:

- 4.8.1 Banks may freely buy and sell Government securities on an outright basis at the prevailing market prices without any restriction on the period between sale and purchase.
- 4.8.2 Retailing of Government securities should be on the basis of ongoing market rates/yield curve emerging out of secondary market transactions.
- 4.8.3 No sale of Government securities should be effected by banks unless they hold securities in their portfolio either in the form of physical scrips or in the SGL account maintained with RBI.
- 4.8.4 Immediately on sale, the corresponding amount should be deducted by the bank from its investment accounts and also from its SLR assets.
- 4.8.5 These transactions should be looked into by the concurrent/statutory auditors of the bank.
- 4.8.6 Scheduled banks should put in place adequate internal control checks/mechanisms as advised by RBI from time to time.
- 4.9 Banks may take advantage of the non-competitive bidding facility in the auction of Government of India dated securities, provided by RBI. Under this scheme, banks may bid upto Rs. two crore (face value) in any auction of Government of India dated securities, either directly, through a bank or through a primary dealer. For availing this facility, no bidding skill is required, as allotment upto Rs. two crores (face value) is made at the weighted average cut-off rate which emerges in the auction. Primary (urban) co-operative banks may also participate directly or through a bank or a primary dealer in the auctions of state development loans, where coupon is mostly fixed in advance and notified by RBI. An advertisement in leading newspapers is issued 4-5 days in advance of the date of auction. Half yearly auction calender of Government of India securities is also issued by RBI.
- 4.10 CSGL Accounts should be used for holding the securities and such accounts should be maintained in the same bank with whom the cash account is maintained. For all transactions delivery versus payment must be insisted upon by the banks.
- 4.11 In case CSGL account is opened with any of the non-banking institutions indicated above, the particulars of the designated funds account (with a bank) should be intimated to that institution.
- 4.12 All transactions must be monitored to see that delivery takes place on settlement day. The fund account and investment account should be reconciled on the same day before close of business.
- 4.13 Officials deciding about purchase and sale transactions should be separate from those responsible for settlement and accounting.

- 4.14 All investment transactions should be perused by the Board at least once a month.
- 4.15 The banks should keep a proper record of the SGL forms received / issued to facilitate counter-checking by their internal control systems/RBI inspectors/other auditors.
- 4.16 All purchase/sale transactions in Government securities by the banks should necessarily be through SGL account (with RBI) or constituent SGL account (with a scheduled commercial bank/state co-operative bank/primary dealer/Stock Holding Corporation of India) or in a dematerialised account with depositories (NSDL/CDSL/NSCCL).
- 4.17 No transactions in Government securities by a primary (urban) co-operative bank should be undertaken in physical form with any broker.
- 4.18 The entities maintaining the CSGL/designated funds accounts are required to ensure availability of clear funds in the designated funds accounts for purchases and of sufficient securities in the CSGL account for sales before putting through the transactions.
- 4.19 The security dealings of banks generally being for large values, it may be necessary to ensure, before concluding the deal, the ability of the counter-party to fulfil the contract, particularly where the counter-party is not a bank.
- 4.20 While buying securities for SLR purposes, the bank should ensure from the counter parties that the bonds it intends to purchase have and would continue to have SLR status. The bank should also verify this from independent sources in case of doubt.
- 4.21 In order to avoid concentration of risk, the banks should have a fairly diversified investment portfolio. Smaller investment portfolios should preferably be restricted to securities with high safety and liquidity such as Government securities.
- 4.22 The primary (urban) co-operative banks may seek the guidance of Primary Dealers' Association of India/Fixed Income and Money Market Dealers' Association (FIMMDA) on investment in Government Securities.

5 TRANSACTIONS THROUGH SGL ACCOUNT

5.1 SGL Account

- 5.1.1 Transfers through SGL accounts by the banks having SGL facility can be made only if they maintain a regular current account with the Reserve Bank. All transactions in Government securities for which SGL facility is available, should be put through SGL accounts only.

- 5.1.2 Before issue of SGL transfer forms covering the sale transactions, banks should ensure that they have sufficient balance in the respective SGL accounts. Under no circumstances, should an SGL transfer form issued by a bank in favour of another bank, bounce for want of sufficient balance in the SGL account. The purchasing bank should issue the cheques only after receipt of the SGL transfer forms from the selling bank.
- 5.1.3 If the SGL transfer form bounces for want of sufficient balance in the SGL Account, the bank which has issued the form will be liable for the following penal action:
- 5.1.3.1 The amount of SGL form (cost of purchase paid by the purchaser of the bank) will be debited immediately to the current account of the selling bank with the Reserve Bank.
- 5.1.3.2 In the event of an overdraft arising in the current account following such a debit, penal interest will be charged by the Reserve Bank on the amount of the overdraft at a rate 3% points above the SBI DFHI's call money lending rate on the day in question.
- 5.1.3.3 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 date of occurrence of the third bouncing. If after restoration of the facility, any SGL form of the bank bounces again, the bank will be permanently debarred from the use of the SGL facility in all the PDOs of the Reserve Bank.

5.2 SGL Forms

- 5.2.1 The SGL transfer forms should be in the standard format prescribed by the Reserve Bank and printed on semi-security paper of uniform size. These should be serially numbered and there should be a control system in place to account for each SGL form.
- 5.2.2 SGL transfer forms should be signed by two authorised officials of the bank whose signatures should be recorded with the respective Public Debt Office (PDO) of Reserve Bank and other banks.
- 5.2.3 The SGL transfer form received by the purchasing bank should be deposited in its SGL account immediately. No sale should be effected by way of return of SGL transfer form held by the bank.
- 5.2.4 Any bouncing of SGL transfer forms issued by selling bank in favour of the buying bank should immediately be brought to the notice of the Reserve Bank by the buying bank.

5.3 Control, Violation and Penalty Provisions

- 5.3.1 Record of SGL transfer forms issued/received should be maintained. Balances as per the bank's books in respect of SGL accounts should be reconciled with the balances in the books of PDOs. The concerned PDO will forward a monthly statement of balances of SGL/CSGL

account to all account holders. Primary (urban) co-operative banks having SGL/CSGL accounts with PDOs may use these statements for the purpose of monthly reconciliation of their SGL/CSGL balances as per their books and the position in this regard should be placed before the Audit Committee of the Board. This reconciliation should also be periodically checked by the internal audit department. A system for verification of the authenticity of the SGL transfer forms received from other banks and confirmation of authorised signatories should be put in place.

- 5.3.2 Banks should also forward a quarterly certificate to the concerned PDO, indicating that the balances held in the SGL accounts with the PDO have been reconciled and that it has been placed before the Audit Committee of the Board. A copy thereof should be sent to the concerned Regional Office of the Urban Banks Department.
- 5.3.3 Banks should put in place a system to report to the top management on a monthly basis the details of transactions in securities, details of bouncing of SGL transfer forms issued by other banks and review of investment transactions undertaken during the period.
- 5.3.4 All promissory notes, debentures, shares, bonds, etc. should be properly recorded and held under joint custody. A separate register may be maintained to record the particulars of securities taken out/re-lodged. These should be subjected to periodical verification say once in a quarter or half-year, by persons unconnected with their custody.
- 5.3.5 Certificates should be obtained at quarterly/half-yearly intervals in respect of securities lodged with other institutions. Similarly, it is necessary to reconcile the outstanding BRs with the counter-party at monthly intervals and reconciliation of SGL Account balance with the PDO at monthly intervals.
- 5.3.6 The internal inspectors and concurrent auditors should peruse the transactions to ensure that the deals have been undertaken in the best interest of the bank. The Vigilance Cell should also make surprise sample checks of large transactions.
- 5.3.7 The concurrent auditors should certify that investments held by the bank, as on the last reporting Friday of each quarter and as reported to RBI, are actually owned/held by it as evidenced by the physical securities or the out-standings statement. Such a certificate should be submitted to the Regional Office of Urban Banks Department having jurisdiction over the bank, within 30 days from the end of the relative quarter.

6. USE OF BANK RECEIPTS (BRs)

6.1 When to use BRs

- 6.1.1 No BR should be issued under any circumstances in respect of transactions in Government securities for which SGL facility is available.

- 6.1.2 Even in the case of other securities, BR may be issued for ready transactions only, under the following circumstances:
 - 6.1.2.1 The scrips are yet to be issued by the issuer and the bank is holding the allotment advice.
 - 6.1.2.2 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.
 - 6.1.2.3 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.
- 6.1.3 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 mere exchange of BRs held by the banks.
- 6.1.4 BRs may be issued covering transactions relating to bank's own Investment Accounts only, and no BR should be issued by bank covering transactions relating to Constituents' Account including brokers.

6.2 **BR form issue, custody, record**

- 6.2.1 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 control system in place to account for each BR form.
- 6.2.2 There should be a proper system for the custody of unused BR forms and their utilisation.
- 6.2.3 Separate registers of BRs issued / 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.
- 6.2.4 A system for verification of the authenticity of the BRs received from other banks and confirmation of authorised signatures should be put in place.

6.3 **Settlement through BRs**

- 6.3.1 No BR should remain outstanding for more than 15 days.
- 6.3.2 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 Reserve Bank explaining the reasons under which the scrips could not be delivered within the stipulated period and the proposed manner of settlement of the transactions.

6.4 Control, Violation and Penalty Provisions

- 6.4.1 The existence and operation of controls at the concerned offices should be reviewed, among others, by the statutory auditors and a certificate to this effect may be forwarded to Reserve Bank of India, Urban Banks Department, Central Office, Mumbai 400 018 every year.
- 6.4.2 The violation of the instructions relating to the BRs would invite penal action which could include raising of reserve requirements, withdrawal of refinance 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 (AACs).
- 6.4.3 The reconciliation should be periodically checked by the internal audit department.

7 ENGAGEMENT OF BROKERS

7.1 Dealing through Brokers

- 7.1.1 The inter-bank securities transactions should be undertaken directly between banks and no bank should engage the services of any broker in such transactions. Banks may, however, undertake securities transactions among themselves or with non-bank clients through members of the National Stock Exchange (NSE), the Stock Exchange, Mumbai (BSE)/OTC Exchange of India wherein the transactions are transparent. In case any transactions in securities are not undertaken on NSE, OTC Exchange of India or the Stock Exchange, Mumbai (BSE), the same should be undertaken by the banks directly without the use of brokers.
- 7.1.2 Purchase of permissible shares and PSU bonds in the secondary market (other than inter-bank transactions) should be only through recognised stock exchanges and registered stock- brokers.
- 7.1.3 The SBI DFHI has been permitted to operate as a broker in the inter-bank participation market. This would enable the banks to seek intermediation of SBI DFHI for borrowing/lending, if required. However, the banks shall be free to settle transaction in the inter-bank participations market directly, if so desired.
- 7.1.4 It should be ensured that the applications of the banks in respect of their own subscription to Central/State Government loans are submitted directly to the receiving offices of the RBI/State Bank of India and intermediaries or brokers should not be used for the purpose.
- 7.1.5 Similarly, where the investments are made by the banks on account of their clients, the relative applications bearing the bank's own stamps should be tendered direct to the receiving offices.
- 7.1.6 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. Under no circumstances banks should give power of attorney or any other authorisation to the brokers/ intermediaries to deal on their behalf in the money and securities markets.

- 7.1.7 Disclosure of counter party should be insisted upon on conclusion of the deal put through brokers.
- 7.1.8 Contract confirmation from the counter party should be insisted upon.
- 7.1.9 The brokers should not be involved in the settlement process at all i.e. both the fund settlement and delivery of security should be done with the counterparty directly.

7.2 **Empanelment of Brokers**

- 7.2.1 The banks should prepare a panel of brokers with the approval of their Board of Directors.
- 7.2.2 Brokers should be empanelled after verifying their credentials e.g. :
 - (a) SEBI registration
 - (b) Membership of BSE/NSE/OTCEI for debt market.
 - (c) Market turnover in the preceding year as certified by the Exchange/s.
 - (d) Market reputation etc.
- 7.2.3 The bank should check websites of SEBI/respective exchanges, to ensure that the broker has not been put in the banned list.

7.3 **Broker Limits**

- 7.3.1 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, and ensure that these limits are not exceeded. A record of broker-wise details of deals put through and brokerage paid should be maintained.
- 7.3.2 A limit of 5% of total transactions (both purchases and sales) entered into by the banks during a year should be treated as the aggregate upper contract limit for each of the approved brokers.
- 7.3.3 This limit should cover both the business initiated by the bank and the business offered/brought to the bank by a broker.
- 7.3.4 It should be ensured that the transactions entered through individual brokers during a year normally do not exceed the prescribed limit. However, if 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. In such cases, post-facto approval of the Board may be obtained after explaining the circumstances under which the limit was exceeded.

Note : Clarifications on certain issues raised by the banks in this regard are furnished in Annexure I.

8 SETTLEMENT OF GOVERNMENT SECURITIES TRANSACTIONS –THROUGH CLEARING CORPORATION OF INDIA LTD.

- 8.1 With effect from 1st April, 2003, all Government Securities transactions (both Outright and Repo) are being settled compulsorily through Clearing Corporation of India Ltd. (CCIL) only. Any transactions in Govt. Securities for settlement by the banks outside the NDS-CCIL system are not being entertained by Reserve Bank of India since that date.
- 8.2 Primary (urban) co-operative banks, which are not a member of NDS-CCIL system, should undertake their transactions in Government securities through gilt account/de-mat account maintained with a Negotiated Dealing System (NDS) member.
- 8.3 With effect from May 25, 2005, all outright secondary market transactions in Government Securities will be settled on T+1 basis. However, in case of repo transactions in government securities, the market participants will have the choice of settling the first leg on either T+0 basis or T+1 basis as per their requirement.

9 TRADING OF GOVERNMENT SECURITIES ON STOCK EXCHANGES

- 9.1 With a view to encouraging wider participation of all classes of investors, including retail, in government securities, trading in government securities through a nation-wide anonymous, order driven, screen-based trading system of the stock exchanges, in the same manner in which trading takes place in equities, has been introduced. This facility of trading of government securities on the stock exchanges, in the dematerialized mode only, would be available to banks in addition to the present NDS of the Reserve Bank, which will continue to remain in place.
- 9.2 The primary (urban) co-operative banks have the option to undertake transactions in dated Government of India (GOI) securities in dematerialized form on automated order driven system of the National Stock Exchange (NSE), The Stock Exchange, Mumbai (BSE) and Over the Counter Exchange of India (OTCEI) in addition to the existing mode of dealing through SGL accounts with Reserve Bank of India or Constituent SGL accounts with the designated entities such as Scheduled Commercial Bank/Primary Dealer/State Cooperative Bank etc.
- 9.3 As the trading facility on the above stock exchanges will operate parallel to the present system of trading in government securities, the trades concluded on the exchanges will be cleared by their respective clearing corporations/clearing houses. However, trading members of the stock exchanges shall not be involved in the settlement process for any RBI regulated entity. All stock exchange trades of banks have to be settled either directly with CCIL/clearing house (in case they are clearing members) or else through a clearing member custodian.

- 9.4 Banks, as institutional investors on the stock exchanges, may undertake transactions only on the basis of giving and taking delivery of securities. In other words, short selling of government securities, even on an intra-day basis, is not permissible.
- 9.5 With a view to facilitating participation on the stock exchanges within the regulations prescribed by RBI, SEBI and the exchanges, banks are being extended the following facilities:
- 9.5.1 Opening de-mat accounts with a bank depository participant (DP) of NSDL/CDSL or with SHCIL in addition to their SGL/CSGL accounts with RBI/authorized entities.
- 9.5.2 Value free transfer of securities between SGL/CSGL and demat accounts is being enabled at Public Debt Office (PDO), Mumbai, subject to operational guidelines issued separately by our Department of Government and Bank Accounts (DGBA) to all SGL account holders.
- 9.6 The balances in government securities maintained by the banks in the depositories will be included for SLR purpose. Any shortfall in maintenance of CRR/SLR resulting from settlement failure (on either the NDS-CCIL market or the stock exchanges) will attract the usual penalties.
- 9.7 The Boards of primary (urban) co-operative banks may take a conscious decision in regard to using the stock exchange platform for making investments in government securities in addition to the existing NDS-CCIL market and the direct bidding facility. As regulations of SEBI will also apply insofar as trading of government securities is concerned, the Board should frame and implement a suitable policy to ensure that operations are conducted in accordance with the norms laid down by RBI/SEBI and the respective stock exchange. Prior to commencing operations, the dealing officials should also familiarize themselves with the basic operating procedures of the stock exchanges.
- 9.8 **Operational Guidelines**
- 9.8.1 Banks should put in place appropriate internal control systems catering to stock exchange trading and settlement before commencing operations on the exchanges. The back office arrangement should be such that trading on the NDS/OTC market and on the stock exchanges can be tracked easily for settlement, reconciliation and management reporting. Banks should, therefore, install enabling IT infrastructure and adequate risk management systems.
- 9.8.2 Only SEBI registered brokers who are authorized by the permitted exchanges (NSE, BSE or OTCEI) to undertake transactions in government securities can be used for placing buy/sell orders. A valid contract note indicating the time of execution must be obtained from the broker at end of day.

- 9.8.3 The dealing officials should independently check prices in the market or on the stock exchange screens before placing their orders with the brokers. The decision-making processes cannot be delegated to brokers by the banks.
- 9.8.4 The transactions done through any broker will be subjected to the current guidelines on transactions done through brokers.
- 9.8.5 Brokers/trading members shall not be involved in the settlement process; all trades have to be settled through clearing member custodians. Hence, it will be necessary for primary (urban) co-operative banks to enter into a bilateral clearing agreement with such service providers before hand.
- 9.8.6 All transactions must be monitored with a view to ensuring timely receipt of funds and securities. Any delay or failure should be promptly taken up with the concerned exchange/authorities.
- 9.8.7 At the time of trade, securities must be available with the banks either in their SGL or in the de-mat account with depositories.
- 9.8.8 Any settlement failure on account of non-delivery of securities/non-availability of clear funds will be treated as SGL bouncing and the current penalties in respect of SGL bouncing will be applicable. The stock exchanges will report such failures to the respective Public Debt Offices.
- 9.8.9 For the limited purpose of dealing through the screen based trading system of the stock exchanges the condition that a primary (urban) co-operative bank should seek a scheduled commercial bank, a primary dealer, a financial institution, another primary (urban) co-operative bank, insurance company, mutual fund or provident fund as a counterparty, while undertaking transactions in Government securities, will not apply.
- 9.8.10 Banks should report on weekly basis to their Audit Committee of the Board, giving the details of trades on aggregate basis done on the stock exchanges and details of any "closed-out" transactions on the exchanges.
- 9.8.11 The banks should take all necessary precautions and strictly adhere to all instructions/guidelines issued by the Reserve Bank relating to transactions in Government securities as hitherto.

10. READY FORWARD CONTRACTS IN GOVERNMENT SECURITIES

- 10.1 In terms of the notification No. S.O. 131(E) dated January 22, 2003 issued by Reserve Bank of India under powers derived from Section 29A of the Securities Contracts (Regulation) Act (SCRA), 1956, the primary (urban) co-operative banks may enter into ready forward contracts (including reverse ready forward contracts), only in (i) Dated Securities and Treasury Bills issued by Government of India and (ii) Dated Securities issued by State Governments.

- 10.2 Ready forward contracts in the above mentioned securities may be entered into with :
- 10.2.1 Persons or entities maintaining a Subsidiary General Ledger (SGL) account with Reserve Bank of India, Mumbai ; and
- 10.2.2 The following categories of entities who do not maintain SGL accounts with the Reserve Bank of India but maintain gilt accounts (i.e gilt account holders) with a bank or any other entity (i.e. the custodian) permitted by the Reserve Bank of India to maintain Constituent Subsidiary General Ledger (CSGL) account with its Public Debt Office, Mumbai:
- (i) Any scheduled bank,
 - (ii) Non-scheduled Primary (Urban) Co-operative Banks
 - (iii) Any primary dealer authorised by the Reserve Bank of India,
 - (iv) 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,
 - (v) Any mutual fund registered with the Securities Exchange Board of India
 - (vi) Any housing finance company registered with the National Housing Bank, and
 - (vii) Any insurance company registered with the Insurance Regulatory and Development Authority.
- 10.3 All persons or entities specified at 10.2.2 above can enter into ready forward transactions among themselves subject to the following restrictions:
- 10.3.1 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.
- 10.3.2 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
- 10.3.3 Primary (Urban) Cooperative banks may not enter into ready forward contracts with the non-banking financial companies. However, this restriction would not apply to repo transactions with Primary Dealers in Government Securities.
- 10.4 All ready forward contracts should 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).
- 10.5 All ready forward contracts shall be settled through the SGL Account / CSGL Account maintained with the Reserve Bank of India, Mumbai with

the Clearing Corporation of India Ltd. (CCIL) acting as the central counter party for all such ready forward transactions.

- 10.6 The custodians should put in place an effective system of internal control and concurrent audit to ensure that :
 - 10.6.1 ready forward transactions are undertaken only against the clear balance of securities in the gilt account,
 - 10.6.2 all such transactions are promptly reported on the NDS, and
 - 10.6.3 other terms and conditions referred to above have been complied with.
- 10.7 Primary (urban) co-operative banks can undertake ready forward transactions only in securities held in excess of the prescribed Statutory Liquidity Ratio (SLR) requirements.
- 10.8 No sale transaction should be put through without actually holding the securities in the portfolio by a seller of securities in the first leg of a ready forward transaction.
- 10.9 Securities purchased under the ready forward contracts shall not be sold during the period of the contract.
- 10.10. **Prohibition against buy-back arrangements**
 - 10.10.1 Banks should not undertake double ready forward deals in Govt. securities, including treasury bills.
 - 10.10.2 No ready forward and double ready forward deals should be put through even among banks and even on their investment accounts in other securities such as public sector bonds, units of UTI, etc.
 - 10.10.3 No ready forward and double ready forward deals should be entered into in any securities including the Government securities, on behalf of other constituents including brokers.

11 UNIFORM ACCOUNTING FOR REPO/REVERSE REPO TRANSACTION

- 11.1 In order to ensure uniform accounting treatment for repo/reverse repo transactions and to impart an element of transparency, the banks should follow the uniform accounting principles detailed below:
 - 11.1.1 The uniform accounting principles are applicable from the financial year 2003-04. Market participants may undertake repos from any of the three categories of investments, viz. Held for Trading, Available for Sale and Held to Maturity.

- 11.1.2 The legal character of repo under the current law, viz. as outright purchase and outright sale transactions will be kept intact by ensuring that the securities sold under repo (the entity selling referred to as “seller”) are excluded from the Investment Account of the seller of securities and the securities bought under reverse repo (the entity buying referred to as “buyer”) are included in the Investment Account of the buyer of securities. Further, the buyer can reckon the approved securities acquired under reverse repo transaction for the purpose of Statutory Liquidity Ratio (SLR) during the period of the repo.
- 11.1.3 At present, repo transactions are permitted in Central Government securities including Treasury Bills and dated State Government securities. Since the buyer of the securities will not hold it till maturity, the securities purchased under reverse repo by banks should not be classified under Held to Maturity category. The first leg of the repo should be contracted at prevailing market rates. Further, the accrued interest received/paid in a repo/reverse repo transaction and the clean price (i.e. total cash consideration less accrued interest) should be accounted for separately and distinctly.
- 11.2 The other accounting principles to be followed while accounting for repos/reverse repos will be as under:

11.2.1 Coupon

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 on the date of receipt as the cash consideration payable by the seller in the second leg does not include any intervening cash flows. While the buyer will book the coupon during the period of the repo, the seller will not accrue the coupon during the period of the repo. In the case of discounted instruments like Treasury Bills, since there is no coupon, the seller will continue to accrue the discount at the original discount rate during the period of the repo. The buyer will not, therefore, accrue the discount during the period of the repo.

11.2.2 Repo Interest Income/Expenditure

After the second leg of the repo/reverse repo transaction is over,

- (a) the difference in the clean price of the security between the first leg and the second leg should be reckoned as Repo Interest Income/Expenditure in the books of the buyer/seller respectively;
- (b) the difference between the accrued interest paid between the two legs of the transaction should be shown as Repo Interest Income/Expenditure account, as the case may be; and
- (c) 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 subsequent period in respect of the outstanding transactions should be reckoned for the next accounting period.

11.2.3 **Marking to Market**

The buyer will mark to market the securities acquired under reverse repo transactions as per the investment classification of the security. To illustrate, for banks, in case the securities acquired under reverse repo transactions have been classified under Available for Sale category, then the mark to market valuation for such securities should be done at least once a quarter. For entities who do not follow any investment classification norms, the valuation for securities acquired under reverse repo transactions may be in accordance with the valuation norms followed by them in respect of securities of similar nature.

- (a) In respect of the repo transactions outstanding as on the balance sheet date the buyer will mark to market the securities on the balance sheet date and will account for the same as laid down in the extant valuation guidelines issued by the RBI.
- (b) the seller will provide for the price difference in the Profit & Loss account and show this difference under "Other Assets" in the balance sheet if the sale price of the security offered under repo is lower than the book value.
- (c) the seller will ignore the price difference for the purpose of Profit & Loss account but show the difference under "Other Liabilities" in the balance sheet if the sale price of the security offered under repo is higher than the book value; and
- (d) similarly the accrued interest paid/received in the repo/reverse repo transactions outstanding on balance sheet dates should be shown as "Other Assets" or "Other Liabilities" in the balance sheet.

11.2.4 **Book value on re-purchase**

The seller shall debit the repo account with the original book value (as existing in the books on the date of the first leg) on buying back the securities in the second leg.

11.2.5 **Disclosure**

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

(Rs. in crores)

Particulars	Outstanding during the year			As on March 31
	Minimum	Maximum	Daily Average	
Securities sold under repos				
Securities purchased under reverse repos				

11.3 Accounting methodology

The accounting methodology to be followed along with illustrations are given in the Annexure I and II of our circular UBD.BPD.PCB. Cir.44/09.80.00/2002-03 dated May 12, 2003. While market participants, having different accounting systems, may use accounting heads different from those used in the illustration, there should not be any deviation from the accounting principles enunciated above. Further, to obviate disputes arising out of repo transactions, the participants may consider entering into bilateral Master Repo Agreement as per the documentation finalised by FIMMDA.

12. NON SLR INVESTMENTS

12.1 Holding Shares & Debentures in Private Sector Companies or Institutions other than Co-operative Sector

The primary (urban) co-operative banks should not subscribe to the initial or subsequent issue of shares/debentures of private sector companies or bodies or organisations other than in co-operative sector unless specifically permitted by the Reserve Bank.

12.2 Deposits with other institutions and other primary (urban) co-operative banks

12.2.1 Scheduled primary (urban) co-operative bank should not place deposits with any other primary (urban) co-operative bank.

12.2.2 Non-scheduled primary (urban) co-operative banks may place deposits with strong scheduled primary (urban) co-operative banks, fulfilling following norms:

- (i) The bank is complying with the prescribed level of CRAR.
- (ii) Net NPA of the bank is less than 7%
- (iii) The bank has not defaulted in the maintenance of CRR/SLR requirements for the last two years.
- (iv) The bank has declared net profits for the last three consecutive years.

- (iv) The bank is complying with prudential norms on income recognition, asset classification and provisioning, exposure ceilings and loans & advances to directors.

12.2.3 Primary (urban) co-operative banks should not park their funds as deposits with other institutions/companies/corporations etc. save as provides above (para 12.2.2) as the funds mobilised by them are intended for lending to the community of the area of operation from where such funds are mobilised, provision of credit at reasonable rates to small borrowers, etc.

12.2.4 Acceptance of deposits from non-scheduled UCBs by the scheduled UCBs will be subject to the following conditions:

- (i) The total of all such deposits accepted by a scheduled bank should not exceed 10% of its deposit liabilities as on 31 March of the previous financial year.
- (ii) The rate of interest offered on such deposits should be market related.
- (iii) The total amount of deposits placed by a non-scheduled primary (urban) co-operative bank with a scheduled bank should not exceed 15% of its capital funds so as to be in consonance with the extant exposure norms.

12.2.5 Primary (urban) co-operative banks may, however, maintain balances in current accounts with other banks for meeting their clearing and remittance requirements.

12.3 **Non-SLR Debt Securities - Guidelines**

In order to contain risks arising out of the non-SLR investment portfolio of banks, the banks should adhere to the following guidelines :

12.3.1 **Coverage**

- (i) These guidelines cover investments by urban co-operative banks in the bonds issued by public sector undertakings, unsecured redeemable bonds floated by nationalized banks, bonds / shares issued by All India Financial Institutions and units of Unit Trust of India. The guidelines will apply to investments both in the primary market as well as in the secondary market. It may be noted that banks should not invest in Non-SLR debt securities of original maturity of less than one year.
- (ii) It is further clarified that these guidelines apply to capital gains bonds, bonds eligible for priority sector status and bonds issued by central or state public sector undertaking, with or without government guarantees.

- (iii) Definitions of a few terms used in these guidelines have been furnished in Annexure II with a view to ensure uniformity in approach while implementing the guidelines.

12.3.2 Regulatory Requirements

- (i) 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.
- (ii) Banks should not invest in unrated debt securities except bonds of nationalised banks, unlisted securities, unlisted shares of All India Financial Institutions and privately placed debt securities.
- (iii) The debt securities shall 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 public sector undertakings which comply with the requirements of the SEBI circular dated September 30, 2003.

12.3.3 Internal Assessment

Since non-SLR securities are mostly in the form of credit substitutes, banks should :

- (i) subject all their investment proposals relating to the above 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 that they should not 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.

12.3.4 Fixing of Prudential limits

12.3.4.1 The Board of Directors of banks should fix a prudential limit for their total investment in non-SLR securities and sub-limits for the following debt securities:

- (i) bonds of public sector undertakings,

- (ii) bonds /equity of All India Financial Institutions listed in Annexure III*
- (iii) Infrastructure bonds floated by All India Financial Institutions,
- (iv) unsecured redeemable bonds floated by nationalised banks,
- (v) units of UTI and
- (vi) certificates of deposit issued by scheduled commercial banks and other financial institutions approved by RBI.

12.3.4.2 The total investment in (i) to (vi) above should not exceed 10 per cent of the banks' total deposits as on March 31 of the previous year, with a sub-ceiling of 5 per cent of incremental deposits of the previous year for investments covered under (v)

12.3.4.3 Banks should ensure that exposure, to a single issuer of debt securities is within the individual exposure ceiling prescribed by RBI for grant of advances, based on capital funds of the bank.

12.3.4.4 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.

12.3.4.5 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 liquidity.

12.4 **Investment in Certificates of Deposit (CDs)**

Primary (urban) co-operative banks are permitted to make investments in CDs issued by scheduled commercial banks and other financial institutions approved by the Reserve Bank, subject to fulfilment of the following conditions:

- (a) The banks should have reached the level stipulated by the Reserve Bank for lendings to priority sector at the time of making investment in CDs.
- (b) The banks should, with the approval of their Board of Directors, evolve policy guidelines governing their investments and obtain the approval of their Boards for placing funds in CDs.
- (c) The investments in CDs should not result in resource crunch necessitating borrowings from higher financing agencies. In other words, the banks should not resort to borrowings from higher financing agencies while making investments in CDs, except for temporary periods to meet exigencies. It should, however, be ensured that the borrowings are need-based and cost-effective.

- (d) The banks should have achieved the requisite level of investments in Government and other approved securities

12.5 Bonds/ Debentures received through SC/RC

- 12.5.1 The bonds/ debentures received by the banks as sale consideration towards sale of financial assets to Securitisation / Reconstruction Companies will be classified as non-SLR investments in the books of the banks and accordingly the valuation, classification and other norms applicable to non-SLR investments of banks as prescribed by RBI from time to time would be applicable to the instruments received by the banks from the sale consideration from SC/ RC. Primary (urban) co-operative banks are allowed to hold these investments, over and above the limit of 10% of its deposits as on 31 March of the previous year, for non-SLR securities. Primary (urban) co-operative banks are not permitted to make any direct investment in the security receipts, pass-through certificates, or bonds/ debentures issued by SC/RC.
- 12.5.2 When a bank sells its financial assets to SC/RC, on transfer the same would be removed from the books of the bank.
- 12.5.3 If the sale to SC/RC is at a price below the net book value (NBV) (i.e. book value less the provision held), the shortfall should be written off/ debited to P&L A/c of that year, subject to the provisions of co-operative societies acts/rules/administrative guidelines in regard to write-off of debts.
- 12.5.4 If the sale is for a value higher than the NBV, the excess provision will not be reversed but will be utilized to meet the shortfall/loss on account of sale of other financial assets to SC/RC.

12.6 Role of Board of Directors

- 12.6.1 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 investment. 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.
- 12.6.2 The Board should devise a system to ensure that the limits prescribed in paragraph 12.3.4 above are scrupulously complied with. 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.
- 12.6.3 Boards of banks should review the following aspects of non-SLR investment twice a year:

- (i) Total business (investment and divestment) during the reporting period
- (ii) Compliance with the prudential limits prescribed by the Board for non-SLR investments
- (iii) Rating migration of the issuers/ issues held in the bank's books and consequent diminution in the portfolio quality
- (iv) Extent of non-performing investments in the non-SLR category and sufficient provision thereof.

12.7 **Demat form**

12.7.1 Primary (Urban) co-operative banks should make investments in non-SLR securities in dematerialised form only.

12.7.2 In addition to one SGL/CSGL A/c, banks may open a demat account with a bank depository participant of NSDL/CDSL or with SHCIL for holding PSU Bonds.

12.8 **Trading and settlement in 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 securities are reported on the NDS and settled through the CCIL from a date to be notified by RBI.

12.9 **Disclosures**

Presently, banks having deposits of Rs. 100 crore and above are required to disclose certain information as 'Notes on Accounts' to their balance sheet effective from the year ending March 31, 2003. In addition to these disclosures, the banks (i.e. banks having deposits of Rs.100 crore & above) should also disclose the details of 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 Annexure IV.

12.10 **Pre-requisites**

12.10.1 These non-SLR investments may be made by the banks subject to the following conditions/safety measures:

- a. A provision should exist for such investments in respective State Co-operative Societies Act/Multi State Co-operative Societies Act and a general or specific permission should be obtained from the Registrar of Co-operative Societies of the concerned State.
- (b) Banks should comply with the instructions regarding investment policy and the dealings in securities transactions.
- (c) There should be no default by the banks in maintenance of statutory cash reserve and liquid assets requirements as prescribed by the Reserve Bank of India Act, 1934/Banking Regulation Act, 1949 (AACS).

- (d) Banks should have achieved the targets fixed by the Reserve Bank from time to time for lending to priority sectors/weaker sections.
- (e) Overdues of banks should not be more than 15% of their outstanding loans and advances.
- (f) Banks should comply with the Reserve Bank instructions regarding income recognition, asset classification and provisioning.

12.10.2.1 While investing in long term debt instruments, the banks should thoroughly satisfy themselves about the terms & conditions of issue, namely payment of interest and repayment of principal, and ensure that there are no clauses permitting the issuer for rescheduling such repayments.

13 INTERNAL CONTROL AND INVESTMENT ACCOUNTING

13.1 Internal Control

13.1.1 For every transaction entered into, a deal slip should be prepared which should contain details relating to name of the counter-party, whether it is direct deal or through a broker, and if through a broker, details of security, amount, price, contract date and time. For each deal, there must be a system of issue of confirmation to the counterparty.

13.1.2 The Deal Slips should be serially numbered and controlled separately to ensure that each deal slip has been properly accounted for.

13.1.3 On the basis of vouchers passed after verification of actual contract notes received from the broker/counter-party and confirmation of the deal by the counter-party the Accounts Section should independently write the books of accounts.

13.1.4 A record of broker-wise details of deals put through and brokerage paid, should be maintained.

13.1.5 The Internal Audit Department should audit the transactions in securities on an ongoing basis and monitor compliance with the laid down management policies and prescribed procedures and report the deficiencies directly to the management of the bank.

13.2 Investment Accounting

13.2.1 Accounting Standards

In order to bring about uniform accounting practice among banks in booking of income on units of UTI and equity of All-India Financial Institutions, as a prudent practice, such income should be booked on cash basis and not on accrual basis. However, in respect of income from Government securities/bonds of public sector undertakings and All-India Financial Institutions, where interest rates on the instruments are

predetermined, income may be booked on accrual basis, provided interest is serviced regularly and is not in arrears.

13.2.2 Broken Period Interest - Government and Other Approved Securities

13.2.2.1 With a view to bringing about uniformity in the accounting treatment of broken period interest on Government securities paid at the time of acquisition and to comply with the Accounting Standards prescribed by the Institute of Chartered Accountants of India, the 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 & Loss Account.

13.2.2.2 It is to be noted that the above accounting treatment does not take into account taxation implications and hence the bank should comply with the requirements of income tax authorities in the manner prescribed by them.

14 RECOMMENDATIONS OF GHOSH COMMITTEE

The following recommendations made by the Ghosh Committee should be implemented by the banks to prevent frauds and malpractices:

14.1 Concurrent Audit

14.1.1 In view of the possibility of abuse, treasury functions viz. investments, funds management including inter-bank borrowings, bills rediscounting, etc. should be subjected to concurrent audit and the results of audit should be placed before the Chairman and Managing Director of the bank at prescribed intervals.

14.1.2 It is the primary responsibility of the banks to ensure that there are adequate audit procedures for ensuring proper compliance of the instructions in regard to the conduct of investment portfolio.

14.1.3 The concurrent audit should cover the following aspects:

- (i) Ensure that in respect of purchase and sale of securities the concerned department has acted within its delegated powers.
- (ii) Ensure that the securities other than those in SGL and in demat form, as shown in the books, are physically held.
- (iii) Ensure that the Accounting Unit is complying with the guidelines regarding BRs, SGL forms, delivery of scrips, documentation and accounting.
- (iv) Ensure that the sale or purchase transactions are done at rates beneficial to the bank.
- (v) Scrutinise conformity with broker limits and include excesses observed in their periodical reports.

14.1.4 Banks should formulate internal control guidelines for acquisition of permissible shares, debentures and PSU bonds in the secondary market duly approved by their Boards.

14.2 **Internal Audit**

Purchase and sale of government securities etc. should be separately subjected to audit by internal auditors (and in the absence of internal auditors by Chartered Accountants out of the panel maintained by the Registrar of Co-operative Societies) and the results of their audit should be placed before the Board of Directors once in every quarter.

14.3 **Review**

Banks should undertake a half-yearly review (as of 31st March and 30th September) of their investment portfolio, which should, apart from other operational aspects of investment portfolio, clearly indicate and certify adherence to the laid down internal investment policy and procedures and RBI guidelines, and put up the same before the Board within a month. Such review reports should be forwarded to Regional Office of Urban Banks Department by 15 May / 15 November respectively.

14.4 **Penalties for Violation**

Banks should scrupulously follow the above instructions. Any violation of these instructions will invite penal action against defaulting banks which could include raising of reserve requirements, withdrawal of refinance from the Reserve Bank, denial of access to money markets, denial of new branches/extension counters and advising the President of Clearing House to take appropriate action including suspension of membership of the Clearing House.

15 **CATEGORISATION OF INVESTMENTS**

15.1 Primary (urban) co-operative banks are required to classify their entire investment portfolio (including SLR and non-SLR securities) under three categories viz. -

- (i) Held to Maturity (HTM)
- (ii) Available for Sale (AFS)
- (iii) Held for Trading (HFT)

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

15.2 **Held to Maturity**

15.2.1 Securities acquired by the banks with the intention to hold them up to maturity will be classified under "Held to Maturity" category.

15.2.2 The investments included under "Held to Maturity" category should not exceed 25 per cent of the bank's total investments. However, banks are permitted to exceed the limit of 25 per cent of their total investments under HTM category provided,

- a) the excess comprises only of SLR securities

- b) the total SLR securities held in the HTM category is not more than 25 per cent of their NDTL as on the last Friday of the second preceding fortnight.
- 15.2.3 Primary (urban) co-operative banks are not permitted to invest in bonds and debentures of private sector companies. Their investments in bonds of PSUs and shares (as permitted by RBI) should be classified under 'Held to Maturity' category but these will not be counted for the purpose of specified ceiling under this category.
- 15.2.4 Profit on sale of investments in this category should be first taken to the P&L Account and thereafter be appropriated to the Investment Fluctuation Reserve. Loss on sale will be recognised in the P&L A/c.
- 15.3 **Held for Trading**
- 15.3.1 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' category.
- 15.3.2 If banks are not able to sell the security within 90 days due to exceptional circumstances such as tight liquidity conditions, or extreme volatility, or market becoming unidirectional, the security should be shifted to the 'Available for Sale' category, subject to conditions stipulated in paragraphs 15.5.3 and 15.5.4 below.
- 15.4 **Available for Sale**
- 15.4.1 Securities which do not fall within the above two categories will be classified under 'Available for Sale' category.
- 15.4.2 Banks have the freedom to decide on the extent of holdings under 'Available for Sale' category. This may be decided by them considering various aspects such as basis of intent, trading strategies, risk management capabilities, tax planning, manpower skills, capital position, etc.
- (Profit or loss on sale of investments in HFT & AFS categories should be taken to P&L Account).
- 15.5 **Shifting of investments**
- 15.5.1 Banks may shift investments to/from 'Held to Maturity' category with the approval of the Board of Directors once in a year. Such shifting will normally be allowed at the beginning of the accounting year. No further shifting to/from this category will be allowed during the remaining part of that accounting year.
- 15.5.2 Banks may shift investments from 'Available for Sale' category to 'Held for Trading' category with the approval of their Board of Directors. In case of exigencies, such shifting may be done with the approval of the Chief Executive of the Bank, but should be ratified by the Board of Directors.

15.5.3 Shifting of investments from 'Held for Trading' category to 'Available for Sale' category is generally not allowed. However, it will be permitted only under exceptional circumstances such as mentioned in paragraph 15.3.2 above, subject to depreciation, if any, applicable on the date of transfer, with the approval of the Board of Directors/Investment Committee.

15.5.4 Transfer of scrips from one category to another, under all circumstances, should be done at the acquisition cost/book value/market value on the date of transfer, whichever is the least, and the depreciation, if any, on such transfer should be fully provided for.

15.6 Classification of Investments in the Balance Sheet

For the purpose of Balance Sheet, the investments should continue to be classified in the following categories:

- (i) Government securities
- (ii) Other approved securities
- (iii) Shares
- (iv) Bonds of PSUs
- (v) Others

16 VALUATION OF INVESTMENTS

16.1 Valuation Standards

16.1.1 Investments classified under 'Held to Maturity' category 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.

16.1.2 The individual scrip in the 'Available for Sale' category will be marked to market at the year-end or at more frequent intervals. The book value of the individual securities would not undergo any change after the revaluation.

16.1.3 The individual scrip in the "Held for Trading" category will be marked to market at monthly or at more frequent intervals. The book value of individual securities in this category would not undergo any change after marking to market .

Note: *Securities under AFS and HFT categories shall be valued scrip-wise and depreciation/appreciation shall be aggregated for each classification as indicated at para 15.6 above separately for AFS and HFT. 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. Similarly net depreciation for any classification in one category should not*

be reduced from appreciation in similar classification in another category.

16.1.4 The provisions required to be created on account of depreciation in the "Available for Sale" and "Held for Trading" category in any year should be debited to the Profit & Loss Account and an equivalent amount (net of tax benefit, if any, and net of consequent reduction in the transfer to Statutory Reserve) or the balance available in the Investment Fluctuation Reserve / Investment Depreciation Reserve Account, whichever is less, shall be transferred from the Investment Fluctuation Reserve/Investment Depreciation Reserve Account to the Profit & Loss Account. In the event provisions created on account of depreciation in the "Available for Sale" and "Held for Trading" category 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 the Investment Fluctuation Reserve/Investment Depreciation Reserve Account to be utilised to meet future depreciation requirement for investments in this category. The amounts debited to the Profit & Loss Account for provision and the amount credited to the Profit & Loss Account for reversal of excess provision should be debited and credited respectively under the head "Expenditure - Provisions & Contingencies". The banks should segregate quantum of provisions required for diminution/depreciation in investments and park under "Contingent provisions against depreciation in investment" to clearly define provisions and reserves and facilitate transfer of funds from/to Investment Fluctuation Reserve/Investment Depreciation Reserve. The amounts appropriated from the Profit & Loss Account and the amount transferred from the Investment Fluctuation Reserve/Investment Depreciation Reserve to the Profit & Loss Account should be shown as 'explanatory note' after determining the profit for the year.

- 16.1.5 It is clarified that while the individual scrips in the Held for Trading category will continue to be marked at monthly or at more frequent intervals, the book value of the individual securities in this category would not undergo any change after marking to market. While the net depreciation in the value of investments, if any, shall be provided for ; the net appreciation, if any, should be ignored. Net depreciation required to be provided for in any one category should not be netted with net appreciation in any other category.
- 16.1.6 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.

16.1.7 The relaxations extended to UCBs during the year 2004-05 in respect of shifting of securities to HTM category and provisioning norms are detailed in Annexure V.

16.1.8 The relaxations extended to UCBs during the year 2005-06 in respect of shifting of securities to HTM category and provisioning norms are detailed in Annexure VI

16.2 **Market Value**

16.2.1 **Quoted Securities**

The 'market value' for the purpose of periodical valuation of investments included in the "Available for Sale" and the "Held for Trading" categories 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.

16.2.2 **Unquoted SLR Securities**

In respect of unquoted securities, the procedure as detailed below should be adopted.

(i) Central Government Securities

(a) The Reserve Bank of India will not announce the YTM rates for unquoted Government securities, for the purpose of valuation of investments by banks. The 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.

(b) The 6.00 per cent Capital Indexed Bonds may be valued at "cost" which may be reckoned by using the index ratio calculated by taking the Wholesale Price Index (WPI) with a three months' lag. For example, the WPI for the month of November 1997 may be used to calculate the index ratio for month of March 1998. An illustrative example is given below:

The bonds were issued in December 1997 at par. The Wholesale Price Index (WPI) for August 1997 was taken as the Base WPI. Similarly, the Reference WPI for payment of redemption value in December 2002, is taken as the WPI for August 2002. Thus, a clear 3 months' lag is followed for indexation of capital. The same principle can be applied for arriving at 'Cost' for the purpose of valuation of Capital Indexed Bonds. If the valuation of the bond is to be done in March 1998, the index ratio can be calculated by taking the WPI for November 1997 as the Reference WPI. While for every quarter ending March of a year, the numerator will take WPI of November of the previous year, for other quarters ending in months viz. June, September and December, every year, the index ratio will take in the numerator WPI for February, May and August of the respective years.

Assuming that the Monthly Average Index of Wholesale Prices (1981 - 82 = 100) for November 1997 is 329.90. The Reference WPI is 329.90. The base WPI, i.e. the WPI for August 1997 is 326.00. The calculation of 'Cost' of Capital Indexed Bonds is illustrated below:

$$\begin{aligned} \text{Index Ratio} & & & \text{WPI for November 1997} \\ \text{for} & = & \frac{\text{-----}}{\text{Base WPI}} \\ \text{March 1998} & & & \\ & & & \\ & & & 329.9 \\ & = & \frac{\text{-----}}{326.00} = 1.01196 \text{ or } 1.01 \text{ (rounded to two decimal} \\ & & & \text{places)} \end{aligned}$$

Cost of the bonds for valuation as on 31 March 1998 Rs. 100 x 1.01 = Rs. 101.00.

- (a) It is clarified that the reckoning of number of years for the purpose of deciding upon appropriate YTM Rate be done by rounding off the fractional period of a year to the nearest completed year.

As regards valuation of other unquoted securities including PSU bonds, banks should uniformly follow 'Yield to Maturity' method for arriving at valuation of unquoted securities.

- (ii) Treasury Bills should be valued at carrying cost.

(iii) 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.

(iv) 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.

16.2.3 Unquoted non-SLR securities

(i) Debentures/Bonds of AIFIs and PSUs

All debentures/bonds other than debentures/ bonds which are in the nature of advance should be valued on the YTM basis. Such debentures/bonds may be of 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,

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

(c) Where interest/principal on the debenture/bonds is in arrears, the provision should be made for the debentures as in the case of debentures/bonds treated as advances. The depreciation/provision requirement towards debentures where the interest is in arrears or principal is not paid as per due date, shall not be allowed to be set-off against appreciation against other debentures/bonds.

(ii) Where the debentures/bond 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.

(iii) Shares of Co-operative Institutions

If primary (urban) co-operative banks have regularly received dividends from co-operative institutions, then their shares should be valued at face value. In a number of cases, the co-operative institutions in whose shares the primary (urban) co-operative banks have made investments have either gone into liquidation or have not declared dividend at all. In such cases, the banks should make full provision in respect of their investments in shares of such co-operative institutions. In cases where the financial position of co-operative institutions in whose shares banks have made investments is not available, the shares have to be taken at Re. 1/- per co-operative institution.

16.2.4 Shares of All India Financial Institutions

Primary (urban) co-operative banks are allowed to invest in the shares of all India Financial Institutions.

Where stock exchange quotations are available, the shares should be valued accordingly. 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.

16.2.5 Units of UTI

Investments in quoted Mutual Fund Units should be valued as per stock exchange quotations. Investments in non-quoted Mutual Funds Units are to be valued on the basis of the latest re-purchase price declared by the Mutual Funds in respect of each particular Scheme. In case of funds with a lock-in period, or where repurchase price/market quote is not available, Units could be valued at NAV. If NAV is not available, then these could be valued at cost, till the end of the lock-in period.

17 INVESTMENT FLUCTUATION RESERVE (IFR)

With a view to build up adequate reserves to guard against market risks:

- 17.1 Banks should build up Investment Fluctuation Reserve (IFR) out of realised gains on sale of investments, and subject to available net profit, of a minimum of 5 per cent of the investment portfolio by March 2008. This minimum requirement should be computed with reference to investments in two categories, viz., 'Held for Trading (HFT)' and 'Available for Sale (AFS)'. It will not be necessary to include investment under 'Held to Maturity' category for the purpose. However, banks are free to build up a higher percentage of IFR up to 10 per cent of the portfolio depending on the size and composition of their portfolio, with the approval of their Board of Directors.
- 17.2 Banks should transfer maximum amount of the gains realised on sale of investment in securities to the IFR. Transfer to IFR shall be as an appropriation of net profit after appropriation to Statutory Reserve.
- 17.3 The IFR, consisting of realised gains from the sale of investments from the two categories, viz., 'Held for Trading' and 'Available for Sale', would be eligible for inclusion in Tier II capital.
- 17.4 Transfer from IFR to the Profit & Loss Account to meet depreciation requirement on investments would be a 'below the line' extraordinary item.
- 17.5 Banks should ensure that the unrealised gains on valuation of the investment portfolio are not taken to the Income Account or to the IFR.
- 17.6 Banks may utilise the amount held in IFR to meet, in future, the depreciation requirement on investment in securities.
- 17.7 Creation of IFR as per the above guidelines is mandatory for primary (urban) co-operative banks having aggregate Demand and Time Liabilities of Rs. 100 crore and above, and optional for smaller banks.

17.8 Distinction between IFR and IDR

It may be noted that Investment Fluctuation Reserve (IFR) is created out of appropriation from the realised net profits / out of profits earned on account of sale of investments initially held under HTM category but subsequently shifted to AFS or HFT category, and forms part of the reserves of the bank qualifying under Tier II capital, whereas Investment Depreciation Reserve (IDR) is a provision created by charging diminution in investment value to Profit & Loss Account. While the amount held in IFR should be shown in the balance sheet as such, the amount held in IDR should be reported as Contingent provisions against depreciation in investment.

18 REPORTING

Scheduled primary (urban) co-operative banks are required to submit a statement containing information on their investments in approved securities and money market instruments, etc. on quarterly basis. The statement as at the end of each calendar quarter should reach RBI, Central Office, Urban Banks Department within 10 days from the close of the quarter.

Master Circular on Investments
Certain clarifications on brokers' limits
[Ref: Para 7.3]

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, if it is consistently followed in future.
2.	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.
3.	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
4.	Whether central loan/state loan/treasury bills etc. purchased though direct subscriptions/auctions will be included in the volume of total transactions?	No, as brokers are not involved as intermediaries.
5.	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 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 and the reasons therefore recorded and approval of the competent authority/Board obtained post facto.
6.	Whether the transactions conducted on behalf of the clients would also be	Yes, if they are conducted through the brokers.

	included in the total transactions of the year?	
7.	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 inasmuch as Board's post facto approval can be obtained.
8.	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.
9.	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 crore	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 instructions are considered necessary.
10.	Whether the limit is to be observed with reference to total transactions of the previous year as the total transactions of the current year would 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 be 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.

Master Circular on Investments - Certain Definitions
[Vide para 12.3.1(iii)]

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.
 - v) 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' debt security is a security which is listed in a stock exchange. If not so, it is an 'unlisted' debt security.
5. A non performing investment (NPI), similar to a non performing advance (NPA), is one where :
 - a. Interest/ instalment (including maturity proceeds) is due and remains unpaid for more than 180 days. The delinquency period has become 90 days with effect from 31st March 2004.
 - b. 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.

Master Circular on Investments
List of All India Financial Institutions

[Vide para 12.3.4.1 (ii)]

1. IFCI Ltd.
2. Industrial Investment Bank of India Ltd.
3. Tourism Finance Corporation of India Ltd.
4. Risk Capital and Technology Finance Corporation Ltd.
5. Technology Development and Information Company of India Ltd.
6. Power Finance Corporation Ltd.
7. National Housing Bank.
8. Small Industries Development Bank of India
9. Rural Electrification Corporation Ltd.
10. Indian Railways Finance Corporation Ltd.
11. National Bank for Agriculture and Rural Development.
12. EXIM Bank of India.
13. Infrastructure Development Finance Co. Ltd.
14. Housing & Urban Development Corp. Ltd

Master Circular on Investments

Disclosures Requirements

[Vide para 12.9]

i) Issuer composition of Non SLR investments

(Rs. in crore)

No.	Issuer	Amount	Extent of 'below investment grade' Securities	Extent of 'unrated' securities	Extent of 'unlisted' securities
1.	2.	3.	4.	5.	6.
1	PSUs				
2	FIs				
3	Nationalised Banks				
4	Others				
5	Provision held towards depreciation		X X X	X X X	X X X
	Total *				

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

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 1 st April	
Reductions during the above period	
Closing balance	
Total provisions held	

Xxxx

**Master Circular on Investments
Special concessions to UCBs during the year 2004-05
[Vide para 16.1.7]**

UCBs were permitted, as a one-time measure, to exceed the limit of 25% of total investments under HTM category and to shift SLR securities to the HTM category one more time (cf para 15.5.1) during the accounting year 2004-05 vide RBI circular dated September 2, 2004) provided the excess investments are in SLR securities and the total SLR securities held in the HTM category is not more than 25 per cent of their NDTL as on the last Friday of the second preceding fortnight. Banks were also advised that such shifting should be done at the acquisition cost/book value/ market value on the date of transfer, whichever is the least, and the depreciation, if any, on such transfer should be fully provided for. Further, the Non-SLR investments in bonds of PSUs and shares (as permitted by RBI) classified under HTM category may remain in that category and no fresh non-SLR securities are permitted to be included in the HTM category.

In view of the representations made by Federations of UCBs expressing difficulties in meeting with the provisioning requirements consequent to shifting of securities to HTM category, the issue was reexamined and decided, as a special case, to relax the requirements, as under:

1. Scheduled UCBs:

Scheduled UCBs were allowed to crystallize the provisioning requirement arising on account of shifting of securities from HFT/AFS categories to the HTM category consequent to the issue of our guidelines dated 02.09.2004 and amortize the same over a maximum period of five years commencing from the accounting year ending 31.03.2005, with a minimum of 20 % of such amount, each year.

II. Non Scheduled UCBs:

Shifting of securities from HFT/AFS categories to the HTM category by Non-Scheduled UCBs consequent to the issue of the circular dated 02.09.2004 may be done at book value, subject to the following conditions:

(a) In case the book value is higher than the face value, the difference between the book value and the face value i.e., the premium may be amortized in equal installment over the period remaining to maturity. If the security was obtained at a discount to face value, the difference should be booked as profit only at the time of maturity of the security.

(b) The securities transferred under this special dispensation should be kept separately under the HTM category, and should not be transferred back to the AFS/HFT category in future as per the extant instructions on transfer of securities from HTM category.

(c) In normal course, such securities under HTM category should not be sold in the market and are to be redeemed on maturity only. However, in case of exceptional circumstances if such securities are to be sold, profit/loss on sale of investments in this category should be first taken to the Profit & Loss Account and thereafter, the profit if any, should be appropriated to the 'Capital Reserve'.

(d) The banks were advised to build up sufficient provisions and adhere to extant investment norms for UCBs by 31.03.2009 without any relaxations.

It may be noted that the above relaxation is s a one time measure for the accounting year ended March 31, 2005 and for all fresh investments made on or after 01.04.2005, extant guidelines should be followed. The banks are not allowed to write back provisions already made on investments as on 31.03.2004.

Master Circular on Investments
Special concessions to UCBs during the year 2005-06
[Vide para 16.1.8]

The primary (urban) cooperative banks are allowed to shift securities from AFS/HFT to HTM category and vice versa once at the beginning of the year. It was represented by the Federations of UCBs that the banks were facing difficulties in meeting the provisioning requirements as a result of a further fall in the prices of securities.

2. Taking into consideration the representations received further relaxations were allowed as under for the year ended March 31, 2006:

- (a) as a special case, the banks may shift securities from and to HTM once more on or before March 31, 2006.
- (b) where the market value is lower than the face value, the provision required would be the difference between book value and face value. Further, the provisioning may be made over the remaining period to maturity instead of five years. It may, however be noted that, if the security was acquired at a discount to face value i.e. the book value is lower than the face value, the difference should be booked as profit only at the time of maturity of the security as hitherto
- (c) The revised valuation norms outlined in para (b) above will apply only to transfers to HTM made during the financial year 2005-06
- (d) In case as a result of valuation as above the provision already held by the bank is rendered surplus, the same should **not** be taken to the Profit and Loss account.



Appendix

Master Circular

on

Investments by Primary (urban) Co-op. Banks

A. List of Circulars consolidated in the Master Circular

No.	Circular No.	Date	Subject
1.	UBD BPD No: 41/ 16.20.000/2005-06	29-03-2006	Investment portfolio of UCBs - valuation
2.	UBD BPD No: 31/ 13.01.000/2005-06	17-02-2006	Investment in Government Securities
3.	UBD BPD No: 41/ 16.20.000/2004-05	28-03-2005	Investment portfolio of UCBs - valuation
4.	UBD BPD No: 16/ 16.20.000/2004-05	02-09-2004	Investments – classification and valuation
5.	UBD BPD No: 49/ 09.80.00/2004-05	20-06-2005	Ready Forward Transactions
6.	UBD BPD No: 50/ 09.80.00/2004-05	20-06-2005	Govt Sec- T + 1 settlement
7.	UBD BPD No: 51/ 09.80.00/2004-05	20-06-2005	Settlement of securities on primary issues
8.	UBD.BPD.No.37/12.05.01/2004-05	26.02.2005	Investment portfolio of banks – Reporting system
9.	UBD.BPD.SUB.CIR.5/09.80.00/2003-04	28-04-2004	Transactions in Government Securities (DVP III)
10.	UBD.BPD.PCB.Cir.45/16.20.00/2003-04	15-04-2004	Investment in non-SLR debt securities by UCBs
11.	UBD.BPD.PCB.Cir.44/09.29.00/2003-04	12-04-2004	Sale of Govt. Securities allo UBD BPD No: 41/16.20.000/2004-05cated during the auctions for primary issues on the same day.
12.	UBD.BPD.PCB.Cir.42/09.11.00/2003-04	1-04-2004	Maintenance of CSGL Accounts
13.	UBD.BPD.PCB.Cir.35/13.05.00/2003-04	27-02-2004	Placement of deposits by NSCBs with strong sch UCBs
14.	UBD.BPD.PCB.Cir.34/13.05.00/2003-04	11-02-2004	Maximum limit on advances – limits on exposure to individual/group borrowers – Computation of capital funds
15.	UBD.BPD.PCB.Cir.33/09.11.00/2003-04	11-02-2004	Maintenance of CSGL Accounts
16.	UBD.BPD.PCB.FIR.26/16.20.00/2003-04	2-12-2004	Investment in shares of ICICI Bank Ltd.
17.	UBD.BPD.PCB.Cir.12/09.29.00/2003-04	04-09-2003	Investment Portfolio of UCBs – Guidelines for Investment Fluctuation Reserve
18.	UBD.BPD.Cir.No.11/09.29.00/2	02-09-	Investment Portfolio of UCBs – Classification &

No.	Circular No.	Date	Subject
	003-04	2003	Valuation of investments
19.	UBD.BPD.PCB.Cir.8/9.2900/2003-04	16-08-2003	Trading of Government Securities in Stock Exchanges
20.	UBD.BPD.Cir.No.1/09.11.00/2003-04	08-07-2003	Settlement in respect of Government Securities Transaction – Compulsory settlement through CCIL
21.	UBD.BPD.PCB.Cir.No.2/09.80.00/2003-04	08-07-2003	Scheme for Non-Competitive Bidding Facility in the Auction of Government of India dated securities
22.	UBD.PCB.56/09.29.00/2003-04	02-07-2003	Investment Portfolio of Banks – Transactions in Securities
23.	UBD.BPD.PCB.Cir.No.46/16.20.00/2002-03	17-05-2003	Placement of deposits by non-scheduled UCBs with Scheduled UCBs
24.	UBD.BPD.PCB.No.44/09.80.00/2002-03	12-05-2003	Guidelines for uniform accounting for Repo/Reverse Repo transactions
25.	UBD.BPD.PCB.Cir.No.39/09.29.00/2002-03	13.03.2003	Trading of Government Securities on Stock Exchange
26.	UBD.BP.No.35/16.26.00/2002-03	18-02-2003	Prices of Government Securities in the Secondary Market
27.	UBD.BPD.SPCB.Cir.No.9/09.29.00/2002-03	27-01-2003	Reconciliation Procedure for Government Loans
28.	UBD.POT.PCB.Cir.No.06/09.29.00/2002-03	06-08-2002	Investment Portfolio of UCBs – Transactions in Government Securities
29.	UBD.POT.PCB.Cir.No.5/09.29.00/2002-03	22-07-2002	Investment portfolio of banks – transaction in securities
30.	UBD.POT.No.49/09.80.00/2001-02	17-06-2002	Ready Forward Contracts
31.	UBD.CO.POT.PCB.Cir.No.48/09.29.00/2001-02	11-06-2002	Certification of holding of securities in banks' investment portfolio
32.	UBD.BR.No.47/16.26.00/2001-02	07-06-2002	Investments in Government and other approved securities by Urban Co-op Banks
33.	UBD.PCB.Cir.No.46/09.29.00/2001-02	06-06-2002	Investment Portfolio of Banks – Transaction in Securities
34.	UBD.Plan.SCB.Cir.No.10/09.29.00/2001-02	26-04-2002	Investment Portfolio of Urban Banks – Transactions in Government Securities
35.	UBD.Plan.PCB.Cir.No.41/09.29.00/2001-02	20-04-2002	Investment Portfolio of Banks – Transactions in Securities
36.	UBD.BR.Cir.No.19/16.26.00/2001-02	22-10-2001	B,R.Act, 1949 (AACS) Section 24 – Investment in Government and other approved securities
37.	UBD.No.BR.6/16.26.00/2000-01	09-08-2001	B.R. Act, 1949 (AACS) Section 24 – Investment in Government and other approved securities
38.	UBD.No.CO.BSD.I.PCB.44/12.05.05/2000-2001	23-04-2001	Guidelines for Classification and Valuation of Investments by Banks
39.	UBD.No.BR.Cir/42/16.26.00/2000-01	19-04-2001	Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) - Section 24 - Investment in Government and other approved Securities by Urban Co-operative Banks (UCBS)

No.	Circular No.	Date	Subject
40.	UBD.No.43/16.20.00/2000-01	19-04-2001	Investment of Funds by Urban Co-operative Banks as deposits with other institutions and other Urban Co-operative Banks
41.	UBD.No.POT.Cir.PCB.39/09.29.00/ 2000	18-04-2001	Sale of Government Securities Allotted in the Auctions of Primary Issues
42.	UBD.No.Plan.PCB.Cir/22/09.29.00/ 2000-2001	30-12-2000	Investment Portfolio of banks - Transactions in securities - Role of brokers
43.	UBD.Plan.PCB.Cir/26/09.80.00/99-2000	28-03-2000	Ready Forward Contracts
44.	UBD.Plan.18/09.80.00/1999-2000	30-12-1999	Banks' own investment in State Government Loans -Payment of brokerage commission
45.	UBD.No.Plan.PCB.04/09.80.00/99-2000	25-08-1999	Ready Forward Transactions
46.	Ref. UBD No.BR. 26/18.20.00/98-99	07-04-1999	Investment of funds by primary (urban) co-operative banks In public sector undertakings/ companies
47.	UBD.No.Plan.PCB.DIR.3/09.80.00/98-99	17-08-1998	Reverse Ready forward transactions
48.	UBD.No.BR.1/16.20.00/98-99	10-07-1998	Investment by urban co-op. banks – Valuation of Investments – US – 64 units
49.	UBD No.61/16.20.00/97-98	04-06-1998	Investment of Investment by Urban Cooperative Banks - Valuation of Investment - US- 64 Units funds by primary (urban) co-operative banks in public sector undertakings/companies
50.	UBD.No.Pl.an.PCB/Cir.56/09.60.00/ 97-98	13-05-1998	Investment in Certificates of Deposit (CDs) by primary (urban) co-operative banks
51.	UBD.No.Plan.SUB.20/09.81.00/97-98	19-02-1998	Retailing of Government Securities
52.	UBD.No.BP.37/16.20.00/97-98	29-01-1998	Investment by Urban Co-operative Banks - Valuation of Investments
53.	UBD.No.BSD.I (PCB) 22/ 12.05. 00 / 97-98	26-11-1997	Investment by Urban Co-operative Banks Valuation of Investments
54.	UBD.No.Plan.SUB.No.17/09.83.00/97-98	19-11-1997	Statistical data relating to investments in Money Market Instruments/Government Securities
55.	UBD.No.Plan.PCB/Cir.21/09.60.00/97-98	11-11-1997	Investment in certificates of deposit (CDs) by Urban Co-operative Banks
56.	UBD.No.Plan.PCB.Cir.19/09.29.00/97-98	10-11-1997	Investment Portfolio of banks-Transactions in securities-Role of brokers
57.	UBD.No.Plan.PCB.56/09.60.00/96-97	06-06-1997	Investment in Certificates of Deposit (CDs) by Urban Co-operative Banks
58.	UBD.No.DS.SUB.CIR.7/13.07.00/96-97	07-01-1997	Investment of Surplus Funds by primary co-operative Banks in Bills Rediscounting Scheme
59.	UBD.No.Plan.PCB.34/09.29.07/96-97	30-12-1996	Investment portfolio of banks Transactions in securities
60.	UBD.No.Plan.PCB.No.30/09.82.00/96-97	27-11-1996	Investment by Urban Co-operative Banks in the Units of Unit Trust of India (UTI)
61.	D.No.Plan.PCB.19/09.29.00/96-	11-09-1996	Investment portfolio of banks - System for custody and control of unused B. R. Forms

No.	Circular No.	Date	Subject
62.	UBD.No.Plan.PCB.7/09.60.00/96-97	19-07-1996	Investment in certificates of deposit by Urban Co-operative Banks
63.	UBD.No.Plan/PCB/69/09.29.00/95-96	21-06-1996	Investment portfolio of banks - Transactions in securities
64.	UBD.No.BR.Cir.52/16.20.00/95-96	16-03-1996	Investment of funds by Urban Co-operative Banks in Public Sector Undertakings/Companies
65.	UBD.No.Plan.PCB.47/09.60.00/95-96	29-02-1996	Investment in Certificates of Deposit (CDs) by Urban Co-operative Banks
66.	UBD.No.BR.12/16.20.00/95-96	06-01-1996	Investment of funds by urban co-operative banks in bonds of public sector undertakings
67.	UBD.No.BR.Cir.33/16.26.00/95-96	03-01-1996	Banking Regulation Act, 1949 (As applicable to Co-operative Societies) Section 24-Investment in Government and other approved securities by primary co-operative banks
68.	UBD.No.Cir.63/16.26.00/94-95	16-06-1995	Banking Regulation Act, 1949 (As applicable to Co-operative Societies) Section 24-Investment in Government and other approved securities by primary co-operative banks
69.	UBD.No.BR.CIR.53/16.20.00/94-95	24-04-1995	Investment of funds by Urban Co-operative Banks in Public Sector Undertakings/Companies
70.	UBDNo.Plan.PCB.32/09.29.00/94-95	24-11-1994	Investment Portfolio of Banks - Transactions in Securities - Bank Receipts/Role of brokers
71.	UBD.No.Plan.PCB.29/09.80.00/94/95	09-11-1994	Ready Forward Transactions
72.	UBD.No.Plan.PCB.14/09.80.00/94-95	24-08-1994	Ready Forward Transactions
73.	UBD.BR.10/PCB(CIR)/16.20.00/9495	01-08-1994	Investment of funds by primary co-operative banks in public sector undertakings/companies
74.	UBD.BR.CIR.72/16.20.00/93-94	16-05-1994	Investment of funds by urban co-operative banks in public sector undertakings/companies
75.	UBD.No.PLAN (PCB).CIR.56/09.29.00/93-94	11-02-1994	Investment portfolio of banks - Transactions in Securities.
76.	UBD.No.Plan.51/09.29.00/93-94	20-01-1994	Investment portfolio of banks - Transactions in Securities - Bouncing of SGL transfer forms - Penalties to be imposed:
77.	UBD.No.3/09.29.00/93-94	02-08-1993	Investment port-folio of banks - Transactions in securities - Aggregate contract limit for individuals brokers – Clarifications
78.	UBD.No.Plan.74/UB.81-92/93	17-05-1993	Investment portfolio or banks - Transactions in securities
79.	UBD.No.Plan.13/UB.81/92-93	15-09-1992	Investments portfolio of banks Transactions in securities
80.	UBD.No.BR.1866/A.12(19)-87/88	13-06-1988	Investments of Funds by Urban Co-operative Banks as Deposits with Public Sector Undertakings/ Companies/Corporations/Co-operative Institutions
81.	UBD.No.DC.84 /R.1(B).87/88	13-02-1988	Bills Rediscounting Scheme - Rediscounting of Bills with Banks and Financial Institutions
82.	UBD.No.BR.1455/A12(24)-	31-05-	Banking Regulation Act, 1949 (as applicable to

No.	Circular No.	Date	Subject
	85/86	1986	co-operative societies) - Section 24 - Investment in Units issued by the Unit Trust of India
83.	UBD.BR.871/A.12 (24)-84/85	10-05-1985	Banking Regulation Act, 1949 (as applicable to co-operative societies) - Section 24 - Investment made under national deposit scheme
84.	UBD.BR.498/A.12 (24) -84/85	08-01-1985	Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) Section 24 - Investment in Government and Other Trustee Securities by primary co-operative banks
85.	UBD.NO.DC.597/R.41-84/85	31-10-1984	7% Capital Investment Bonds
86.	UBD.P&O.1121/UB. -63-83/84	01-06-1984	Bank's own investment in central state government loans-payment of brokerage
87.	ACD.ID (DC) 1799/R.36/79/80	10-01-1980	Subscription/purchase of 7 year national rural development bonds
88.	ACD.ID. (DC) 1800/R.36-79/80	10-01-1980	Directive relating to subscription/purchase of 7 year national rural development bonds
89.	ACD.BR.446/A.12 (19)/72-3	01-11-1972	Banking Regulation Act, 1949 (As Applicable to Co-operative Societies) Section 19
90.	ACD.BR.463/A.12 (19)/70-7	09-11-1970	Banking Regulation Act, 1949 (As Applicable to Co-operative Societies): Section 19
91.	ACD.BR.1/A.12 (19)/68-9	01-07-1968	Section 19 of the Banking Regulation act 1949 (as applicable to co-operative societies): Restriction on holding shares in other co-operative societies
92.	ACD.BR.3/A.12 (19)/68-9	01-07-1968	Section 19 of the Banking Regulation Act, 1949 (as applicable to co-operative societies): Restriction on holding shares in other co-operative societies
93.	ACD.BR.903/A.12 (19)/67-8	22-12-1967	Banking Regulation Act, 1949 (as applicable to Co-operative Societies): Section 19: Restriction on holding of shares in other co-operative societies
94.	ACD.BR.388/A.11 (19) 65-6	01-03-1966	Section 19 of the Banking Regulation Act: Restriction on holding shares in other co-operative societies

B. List of Other Circulars from which instructions relating to Investments have also been consolidated in the Master Circular

No.	Circular No.	Date	Subject
1.	UBD.No.POT.PCB.Cir.No.45/09.116.00/2000-01	25-04-2001	Application of Capital Adequacy Norms to Urban (Primary) Co-operative Banks
2.	UBD.CO.No.BSD-I.PCB(Cir)34/12.05.05/99-2000	24-05-2000	Income Recognition, Asset Classification, Provisioning and Valuation of Investments
3.	UBD.No.BSD.PCB./25/12.05.05/ 99-2000	28-02-2000	Income Recognition, Asset Classification, Provisioning and other related matters
4.	UBD.No.I&L(PCBs)42/12.05.00/ 96-97	20-03-1997	Prudential norms - Income Recognition, Assets Classification, Provisioning and other related matters -
5.	UBD.No.I&L(PCBs)68/12.05.00/ 95-96	10-06-1996	Income Recognition, assets classification, provisioning and other related matters Clarifications
6.	UBD.No.I&L(PCB)61/12.05.00/94-95	06-06-1995	Income recognition, asset classification, provisioning and other related matters Valuation of investment and others
7.	UBD.No.I&L86/12.05.00/93-94	28-06-1994	Income recognition, assets classification, provisioning and other related matters
8.	UBD.21/12:15:00/93-94	21-09-1993	Committee to enquire into various aspects relating to frauds and malpractices in banks primary (urban) co-operative banks
9.	UBD.NO.I&L.38/J.1-92/93	09-02-1993	Income recognition, assets classification, provisioning and other related matters
10.	UBD.BR.16/A.6-84/85	09-07-1984	Banking Law (Amendment) Act, 1983
11.	ACD.Plan.358/UB.1-78/9	20-04-1979	Report on the committee on urban co-operative banks
12.	ACD.BR.184/A.12(19)-78/9	23-08-1978	The Banking Regulation Act, 1949 (as applicable to co-operative societies) : Section 10 : Restriction on holding shares in other co-operative societies
13.	ACD.BR.760/A.1/68-9	23-01-1969	The Banking Laws (Amendment) Act, 1968
14.	ACD.BR. 464/A.12(24)/68-9	12-11-1968	Section 24 of the Banking Regulation Act 1949 (As Applicable to Co-operative Societies): Maintenance of Percentage of Assets