

**November 10, 2008**

To

All Category - I Authorised Dealer Banks

Madam / Sir,

**Remittance related to Commodity Derivative Contract  
Issuance of Standby Letter of Credit / Bank Guarantee**

Attention of Authorised Dealer Category - I (AD Category-I) banks is invited to Regulation 8 of Notification No.FEMA.25/2000-RB dated May 3, 2000 viz. Foreign Exchange Management (Foreign exchange derivative contracts) Regulations, 2000, as amended from time to time, regarding remittance of foreign exchange related to commodity derivative contract undertaken in accordance with the regulations.

2. The Reserve Bank has been receiving requests from banks for issuance of bank guarantee / standby letter of credit, in lieu of making a direct remittance towards payment obligations arising out of commodity derivative transactions entered into by customers with overseas counterparties. With a view to providing greater flexibility to resident entities who have such payment obligations related to commodity derivative contracts, it has been decided that AD Category-I banks may issue guarantees / standby letters of credit to cover these specific payment obligations subject to the conditions / guidelines given in the Annex to this Circular.

3. AD Category-I banks may issue guarantees / standby letters of credit only where the remittance is covered under the delegated authority or under the specific approval granted for overseas commodity hedging by the Reserve Bank.

4. The issuing bank shall have a Board approved policy on the nature and extent of exposures that the bank can take for such transactions and should be part of the credit exposure on the customers. The exposure should also be assigned risk weights, for capital adequacy purposes as per the extant provisions.

5. AD Category-I banks may bring the contents of this circular to the notice of their constituents concerned.

6. Necessary amendments to the Notification No.FEMA.8/2000-RB dated May 3, 2000 viz. Foreign Exchange Management (Guarantees) Regulations, 2000, is being issued separately.

7. The directions contained in this circular have been issued under Section 10(4) and 11(1) of the Foreign Exchange Management Act, 1999 (42 of 1999) and are without prejudice to permissions / approvals, if any, required under any other law.

Yours faithfully,

**Salim Gangadharan**  
**Chief General Manager-in-Charge**

**Conditions / Guidelines for issuance of standby letter of credit /  
bank guarantee - commodity hedging transactions**

1. The standby letter of credit / bank guarantee may be issued for the specific purpose of payment of margin money in respect of approved commodity hedging activities of the company.
2. The standby letter of credit / bank guarantee may be issued for an amount not exceeding the margin payments made to the specific counterparty during the previous financial year.
3. The standby letter of credit / bank guarantee may be issued for a maximum period of one year, after marking a lien on the non-funded facility available to the customer (letter of credit / bank guarantee limit).
4. The bank shall ensure that the guidelines for overseas commodity hedging have been duly complied with.
5. The bank shall ensure that broker's month-end reports duly confirmed / countersigned by corporate's financial controller have been submitted.
6. Brokers' month end reports shall be regularly verified by the bank to ensure that all off-shore positions are / were backed by physical exposures.