

**July 18, 2006**

**All Primary Dealers in Government Securities Market**

Dear Sir

**Master Circular – Operational Guidelines to Primary Dealers**

As you are aware, the Reserve Bank of India has, from time to time, issued a number of guidelines/instructions/circulars to the Primary Dealers (PDs) in regard to their operations in the Government Securities Market. To enable the PDs to have all the current instructions at one place, a Master Circular incorporating the guidelines/instructions/directives on the subject was issued on July 12, 2005. With a view to capture the changes and new instructions issued by Reserve Bank of India thereafter, this updated Master Circular is being issued. The list of circulars consolidated is given in Annex VII. It may however be noted that the guidelines on Risk Management and Capital Adequacy have not been covered in this circular as a Master Circular on the subject is being issued separately.

2. Please acknowledge receipt.

Yours faithfully

**(G. Mahalingam)**  
**Chief General Manager**

## Master Circular for Operations of Primary Dealers

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## **1. General**

### **1.1 Introduction**

In 1995, the Reserve Bank of India (RBI) introduced a system of Primary Dealers (PDs) in Government Securities Market.

### **1.2 The objectives of Primary Dealer System**

The objectives of the PD system are:

- (i) To strengthen the infrastructure in the government securities market in order to make it vibrant, liquid and broad based.
- (ii) To ensure development of underwriting and market making capabilities for government securities outside the RBI so that the latter will gradually shed these functions.
- (iii) To improve secondary market trading system, which would contribute to price discovery, enhance liquidity and turnover and encourage voluntary holding of government securities amongst a wider investor base.
- (iv) To make PDs an effective conduit for conducting open market operations (OMO).

### **1.3 Eligibility conditions**

The following classes of institutions are eligible to apply for Primary Dealership:

- (i) Subsidiary of scheduled commercial bank/s and all India financial institution/s dedicated predominantly to the securities business and in particular to the government securities market.
- (ii) Company incorporated under the Companies Act, 1956 and engaged predominantly in the securities business and in particular the government securities market.

(iii) Subsidiaries/ joint ventures set up by entities incorporated abroad under the approval of Foreign Investment Promotion Board (FIPB).

The applicant shall have net owned funds of a minimum of Rs. 50 crore. The owned funds will consist of paid-up equity capital, free reserves, balance in share premium account and capital reserves representing surplus arising out of sale proceeds of assets but not reserves created by revaluation of assets. From this the aggregate of the following items will be deducted

- (i) accumulated balance of loss;
- (ii) deferred revenue expenditure; and
- (iii) other intangible items

(iv) In terms of the Annual Policy Statement for the year 2005-06 that the permitted structure of Primary Dealership (PD) business would be expanded to include banks, which fulfill certain minimum eligibility criteria, the following categories of banks would be eligible to apply for PD licence. (RBI's approval would be subject to compliance with all other relevant laws).

(i) Banks which **do not at present have a partly or wholly owned subsidiary** and fulfill the following criteria :

- (a) Minimum net owned funds (NOF) of Rs.1, 000 crore
- (b) Minimum CRAR of 9 per cent
- (c) Net NPAs of less than 3 per cent and a profit making record for the last three years.

(ii) Indian banks which are undertaking PD business **through a partly or wholly owned subsidiary** and wish to undertake PD business departmentally by merging / taking over PD business from their partly / wholly owned subsidiary subject to fulfilling the criteria stipulated above.

(iii) Foreign banks operating in India who wish to **undertake PD business departmentally by merging the PD business** being undertaken by group companies subject to fulfillment of criteria stipulated above.

**Note:** The decision to enlist Primary Dealers will be taken by Reserve Bank of India based on its perception of market needs, suitability of the applicant and the likely value addition to the system.

#### **1.4 PDs' role and obligations**

PDs are expected to play an active role in the government securities market, both in its primary and secondary segments. A Primary Dealer will be required to have a standing arrangement with RBI based on the execution of an undertaking (**Annex-I**) and the authorisation letter issued by RBI each year. The major roles and obligations of PDs are as below:

- i. **Support to Primary Market:** PDs are required to support auctions for issue of Government dated securities and Treasury Bills as per the minimum norms for underwriting commitment, bidding commitment and success ratio as prescribed by RBI from time to time.
- ii. **Market making in Government securities:** PDs should offer firm two-way quotes in Government securities, through the Negotiated Dealing System, over-the-counter telephone market and through recognised Stock Exchanges in India and take principal positions in the secondary market for Government securities.
- iii. A PD should submit periodic returns as prescribed by RBI from time to time.
- iv. PDs should achieve minimum turnover ratio of 5 times for Government dated securities and 10 times for Treasury Bills of the average month-end stocks subject to the turnover in respect of outright transactions being not less than 3 times in government dated securities and 6 times in Treasury Bills (turnover ratio computed as the ratio of total purchase and sales during the year in the secondary market to average month-end stocks) in the secondary market for Government dated securities and Treasury Bills.
- v. PDs' operations are subject to all prudential and regulatory guidelines issued by RBI.
- vi. PDs should maintain adequate physical infrastructure and skilled manpower for efficient participation in primary issues, trading in the secondary market, and to advise and educate the investors.
- vii. A Primary Dealer shall have an efficient internal control system for fair conduct of business and settlement of trades and maintenance of accounts.

- viii. A Primary Dealer will provide access to RBI to all records, books, information and documents as may be required.
- ix. PDs investment in Government Securities and Treasury Bills on a daily basis should be at least equal to its net call borrowing plus net RBI borrowing plus the minimum prescribed NOF.
- x. Bank-PDs will be subject to underwriting and all other obligations as applicable to standalone PDs and as may be prescribed from time to time. Further, the banks will have to maintain separate books of account for transactions relating to PD business (distinct from the normal banking business) with necessary audit trails. It should be ensured that, at any point of time, there is a minimum balance of Rs. 100 crore of Government securities earmarked for PD business.

### **1.5 Facilities from RBI to PDs**

The Reserve Bank currently extends the following facilities to PDs to enable them to effectively fulfill their obligations:

- i. Access to Current Account facility with RBI.
- ii. Access to Subsidiary General Ledger (SGL) Account facility (for Government securities) with RBI.
- iii. Permission to borrow and lend in the money market including call money market and to trade in all money market instruments.
- iv. Access to Liquidity Adjustment Facility (LAF) of RBI.
- v. Access to liquidity support from RBI under a scheme separately notified.

The facilities are however subject to review, depending upon the market conditions and evolution.

- vi. Favoured access to open market operations by Reserve Bank of India.

### **1.6 Procedure for Authorisation of Primary Dealers**

For enlistment as a Primary Dealer an eligible institution should submit its application in the specified proforma to the Chief General Manager, Internal Debt Management Department (IDMD), Reserve Bank of India, Central Office Building, Shahid Bhagat Singh Marg, Mumbai-400 001. Banks eligible for Primary Dealership may approach the Chief General Manager-in-Charge, Department of Banking Operation and Development, Reserve Bank of India, Central Office, 12<sup>th</sup> Floor, Shahid Bhagat

Singh Marg, Mumbai-400 001. The Reserve Bank will consider the application and, if satisfied, would grant approval 'in principle'. The applicant will thereafter submit an undertaking in respect of the terms agreed to. Based on the application and undertaking, an authorisation letter will be issued by RBI. Continuation as a Primary Dealer would depend on the compliance with the terms and conditions in the authorisation letter.

### **1.7 Regulation**

- i. PDs are required to meet such registration and other requirements as stipulated by Securities and Exchange Board of India (SEBI) including operations on the Stock Exchanges.
- ii. PDs are expected to join Primary Dealers Association of India (PDAI) and Fixed Income Money Market and Derivatives Association (FIMMDA) and abide by the code of conduct framed by them and such other actions initiated by them in the interests of the securities markets.
- iii. In respect of transactions in Government securities, a Primary Dealer should have a separate desk and should maintain separate accounts and have an external audit of annual accounts. The Primary Dealer should maintain separate accounts in respect of its own position and customer transactions.
- iv. A Primary Dealer should bring to the RBI's attention any major complaint against it or action initiated/taken against it by authorities such as the Stock Exchanges, SEBI, CBI, Enforcement Directorate, Income Tax, etc.
- v. Reserve Bank of India reserves the right to cancel the Primary Dealership if, in its view, the concerned institution has not fulfilled any of the prescribed performance criteria contained in the authorisation letter.
- vi. RBI's instructions to Primary Dealers will apply to Bank-PDs, to the extent applicable.
- vii. As banks have access to the call money market and the Liquidity Adjustment Facility (LAF) of RBI, Bank-PDs will not have separate access to these facilities.
- viii. RBI will conduct on-site inspection of Bank-PD business.
- ix. Bank-PDs will be required to submit prescribed returns, as advised by RBI from time to time.

- x. A Bank-PD should bring to the RBI's attention any major complaint against it or action initiated / taken against it by the authorities such as the Stock Exchanges, SEBI, CBI, Enforcement Directorate, Income Tax, etc.
- xi. Reserve Bank of India reserves the right to cancel the Bank-PD authorization if, in its view, the concerned bank has not fulfilled any of the prescribed eligibility and performance criteria.
- xii. Reserve Bank of India reserves its right to amend or modify these guidelines from time to time, as may be considered necessary.

## **1.8 Supervision by RBI**

**1.8.1 Off-site supervision:** PDs are required to submit prescribed periodic returns to RBI promptly. The current list of such returns, their periodicity, etc. is furnished in **Annex II.**

**1.8.2 On-site inspection:** RBI will have the right to inspect the books, records, documents and accounts of an authorised PD. PDs are required to make available all such documents, records, etc. to the RBI inspectors and render all necessary assistance.

## 2. Support to primary issues of Government securities

Concomitant with the objectives of PD system, the PDs are expected to support the primary issues of the dated securities of Central Government and State Government and Treasury Bills of Central Government, through underwriting the dated securities and meeting the underwriting/bidding commitments and success ratios. The related guidelines are as under:

### 2.1 Underwriting of Dated Government Securities

#### 2.1.1 Dated securities of Central Government:

- i. On announcement of the notified amount for dated securities of the Central Government, the underwriting commitment will be divided into two parts - i) Minimum Underwriting Commitment (MUC) and ii) Additional Competitive Underwriting (ACU). The MUC of each PD will be computed to ensure that at least 50 percent of each issue is mandatorily covered by the aggregate of all MUCs. The MUC will be uniform for all PDs, irrespective of their capital or balance sheet size. The remaining portion of the notified amount will be open to competitive underwriting through underwriting auctions. Each PD would be required to bid for a minimum of 3 per cent of notified amount. The auctions could be either uniform price-based or multiple price-based depending upon the market conditions and other relevant factors, which will be announced before the underwriting auction for each issue. All successful bidders in the ACU auction will get commission as per auction rules.
- ii. RBI will announce the MUC of each PD and the amount for which ACU underwriting auction will be held. PDs have to bid in the ACU underwriting auction for the remaining portion (notified amount minus MUC) of the notified amount.
- iii. Bids will be tendered by PDs within the stipulated time, indicating both the amount of the underwriting commitments and underwriting commission rates. A PD can submit multiple bids for underwriting.
- iv. Each PD would be required to bid for a **minimum of 3 per cent** of the notified amount.
- v. A PD **cannot bid for more than 30 per cent** of the notified amount.

- vi. Depending upon the bids submitted for underwriting, RBI will decide the cut-off rate of commission and inform the PDs.
- vii. Underwriting commission will be paid on the amount accepted for underwriting by the RBI, irrespective of the actual amount of devolvement, by credit to the current account of the respective PDs at the RBI, Fort, Mumbai, on the date of issue of security.
- viii. PD should bid for an amount not less than the amount successful in the ACU and MUC. If two or more issues are floated on the same day, the minimum bid amount will be applied to each issue separately.
- ix. In case of devolvement, PDs would be allowed to set-off the accepted bids in the auction against their underwriting commitment accepted by the Reserve Bank. Devolvement of securities, if any, on PDs will take place on pro-rata basis, depending upon the amount of underwriting obligation of each PD after setting off the successful bids in the auction.
- x. An illustration pertaining to the underwriting procedure is given in **Annex III** .

#### **2.1.2 Dated securities of State Governments:**

- i. On announcement of the notified amount for dated securities of the State Governments for which auction is held, RBI may invite PDs to collectively bid to underwrite up to 100 per cent of the notified amount in respect of any of such issues.
- ii. A PD can bid to underwrite up to 30% of the notified amount of the issue. If two or more issues are floated on the same day, the limit of 30% is applied by taking the notified amounts separately.
- iii. The total amount offered for underwriting by a PD on any single day should not exceed five times of its net owned funds.
- iv. Bids will be tendered by PDs within the stipulated time, indicating both the amount of the underwriting commitments and underwriting commission rates. A PD can submit multiple bids for underwriting.
- v. Depending upon the bids submitted for underwriting, the RBI will decide the cut-off rate of commission and the underwriting amount up to which bids would be accepted and inform the PDs.

- vi. RBI reserves the right to accept any amount of underwriting up to 100 per cent of the notified amount or even reject all the bids tendered by PDs for underwriting, without assigning any reason.
- vii. In case of devolvement, PDs would be allowed to set-off the accepted bids in the auction against their underwriting commitment accepted by the Reserve Bank. Devolvement of securities, if any, on PDs will take place on pro-rata basis, depending upon the amount of underwriting obligation of each PD after setting off the successful bids in the auction.
- viii. Underwriting commission will be paid on the amount accepted for underwriting by the RBI, irrespective of the actual amount of devolvement, by credit to the current account of the respective PDs at the RBI, Fort, Mumbai, on the date of issue of security.

## **2. 2. Bidding in Primary auctions of Treasury Bills**

- i. Each PD will individually commit, at the beginning of the year, to submit bids for a fixed percentage of the notified amount of Treasury Bills in each auction.
- ii. The minimum bidding commitment amount / percentage for each PD will be determined by the Reserve Bank, in consultation with the PD. While finalising the bidding commitments, the RBI will take into account the net owned funds (NOF), the offer made by the PD, its track record and its past adherence to the prescribed success ratio. The amount/percentage of minimum bidding commitment so determined by the Reserve Bank will remain unchanged for the entire financial year or till the conclusion of agreement on bidding commitments for the next financial year, whichever is later.
- iii. If a PD in any auction of Treasury Bills, fails to submit the required minimum bid or submits a bid lower than its commitment, the Reserve Bank will reduce assured liquidity support to the extent of shortfall/ failure in submission of bids for a period of three months from the date so specified by the Reserve Bank.
- iv. A PD would be required to achieve a minimum success ratio of 40 percent of bidding commitment for Treasury Bills auctions on an annual basis.
- v. The success ratio requirement of 40 percent of bidding commitment in respect of Treasury Bills auctions will be monitored on a half yearly basis. A PD is required to achieve the minimum level of success ratio in each half

year (April to September and October to March) separately. **(For illustration please refer to Annex IV).**

### **2.3 Sale of securities allotted in Primary issues / OMO on the same day**

**2.3.1** PDs which are successful in the auctions of Government dated securities and Treasury Bills, may enter into contracts for sale of the allotted securities in accordance with the following terms and conditions:

- i. Sale deal can be entered into only once by the allottee on the basis of authenticated allotment advice issued by RBI. The seller should make suitable noting/stamping on the allotment advice indicating the sale contract number etc. the details of which should be intimated to the buyer.
- ii. The face value of securities sold should not exceed the face value of the securities indicated in the allotment advice.
- iii. The sale contract can be entered into only between entities having SGL and CSGL accounts with RBI and settled through CCIL.
- iv. 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, the date of delivery and face value of securities sold, sale consideration, the date and details of actual delivery, transaction ID No. etc. This record will be made available to RBI for verification when required.
- v. The services of brokers should not be used for such sale contracts.
- vi. PDs will be responsible for any failure of contracts due to securities not being credited to their SGL Account on account of non-payment/bouncing of cheques etc.
- vii. Any sale of securities allotted in primary auctions, in terms of this permission, should only be on the basis of permitted settlement cycles.
- viii. This type of sale transactions should be subjected to concurrent audit and the relative report should be placed before the CEO. Instances of deviations reported by concurrent auditor, if any, should also be reported to IDMD, RBI.

**2.3.2** No sale transaction should be contracted in respect of the securities purchased from Reserve Bank of India through open market operations, prior to receiving the confirmation of the deal/advice of allotment from the Reserve Bank.

## 2.4 Intra-day short selling

Intra-day short selling is being permitted subject to the following conditions:

- i. Intra-day short sale transaction and also the covering of short position should be executed only on the Negotiated Dealing System – Order Matching (NDS-OM) platform.
- ii. Under no circumstances should the short position be left uncovered at the end of the day. Inability to cover a short position during the trading day itself shall be treated as an instance of 'SGL bouncing' and will be liable to the disciplinary action prescribed in respect of SGL bouncing, besides attracting such further regulatory action as necessary.
- iii. At no point of time should a bank/PD accumulate a short position in excess of 0.25 per cent of the outstanding stock of a security. The information regarding the outstanding stock of each Government of India dated security is being made available on the RBI website (URL: [www.rbi.org.in](http://www.rbi.org.in)) with effect from March 1, 2006 to facilitate monitoring in this regard.
- iv. Gilt Accounts Holders (GAHs), under CSGL facility are not permitted to undertake intra-day short selling. Those entities providing CSGL facility are required to ensure that no short-sale is undertaken by the GAHs.

## 2.5 When Issued transactions in Central Government Securities

As part of restructuring the debt issuance framework in light of Fiscal Responsibility and Budget Management (FRBM) Act, 2003, the Internal Technical Group on Central Government Securities had recommended introduction of 'When Issued' markets in Central Government Securities. 'When Issued', a short form of "when, as and if issued", indicates a conditional transaction in a security authorized for issuance but not as yet actually issued. All "when issued" transactions are on an "if" basis, to be settled if and when the actual security is issued.

2.5.1 'When Issued' market has two basic advantages: -

i. It facilitates the distribution process for Government securities by stretching the actual distribution period for each issue and allowing the market more time to absorb large issues without disruption.

ii. 'When Issued' market also facilitates price discovery process by reducing uncertainties surrounding auctions.

2.5.2. Accordingly, it has been decided to permit 'When Issued' transactions in Central Government securities. Such 'When Issued' transactions shall be undertaken **only on** NDS-OM platform. Detailed guidelines on 'When Issued' transactions are given in the **Annex V**. 'When Issued' operations will commence after the required system is developed on NDS-OM.

2.5.3. The terms and conditions mentioned in the guidelines will be the relevant terms and conditions referred by the Reserve Bank of India under its Notification No. S.O. 551(E) dated 17<sup>th</sup> April 2006 issued in exercise of the powers conferred on the Reserve Bank of India under Section 16 of the Securities Contracts ( Regulation) Act, 1956 (42 of 1956) vide Government of India Notification No. 183(E) dated March 1, 2000 issued under Section 29 A of the Act, *ibid*.

2.5.4. These guidelines will be reviewed periodically to consider modifications and continuance, as appropriate.

### **3. Primary Dealers operations - Sources of funds**

**3.1** PD's investments in Government securities/Treasury Bills from its own funds should be at least Rs. 50 crore i.e., minimum prescribed NOF at all times.

**3.2** PDs are permitted to borrow funds from call/notice money market and repo market. They are also eligible for liquidity support from RBI. The funds raised from call/notice/repo markets (on net basis) and also the funds obtained by availing liquidity support from RBI, should necessarily be invested in Government securities/Treasury Bills.

**3.3** PDs are allowed to borrow from call/notice market, on average in a reporting fortnight, up to 200 percent of their net owned funds (NOF) as at the end March of the preceding financial year.

**3.4** PDs may lend up to 25 percent of their NOF in call/notice market. The limit will be determined by PDs on an average basis during a 'reporting fortnight'.

**3.5** These limits on borrowing and lending are subject to periodical review by Reserve Bank of India.

### **3.6 Liquidity Support from RBI**

**3.6.1** In terms of the "Guidelines for Primary Dealers in the Government Securities Market", PDs are provided with liquidity support by the Reserve Bank of India through repos /refinance against Central Government securities. In view of the revised scheme of underwriting commitment, the methodology of calculation of liquidity support to individual PDs has been changed. The liquidity support will be provided to stand-alone PDs only. The parameters based on which liquidity support will be allocated are given below:

- i. **Liquidity Adjustment Facility** : The stand-alone PDs will be able to access the Liquidity Adjustment Facility as hitherto.
- ii. **Liquidity support**: Of the total liquidity support, half of the amount will be divided equally among all the stand-alone PDs. The remaining half (i.e. 50%) will be divided in the ratio of 1:1 based on market performance in primary market and secondary market. Performance in primary market will be computed on the basis of bids accepted in the T-Bill auction and G-sec auction in the proportion of 1:3. Similarly, the secondary market performance

will be judged on the basis of outright turnover in T-Bills and G-secs in the proportion of 1:3.

- iii. The PD-wise quantum of liquidity support will be revised every half-year (April-September and October-March) based on the market performance of the PDs in the preceding six months.

**3.6.2** The liquidity support to PDs will be made available at the 'repo rate' announced by Reserve Bank.

**3.6.3** The liquidity support availed by a PD will be repayable within a period of 90 days. The penal rate of interest payable by PDs if liquidity support is repaid after 90 days is Bank Rate plus 5 percentage points for the period beyond 90 days.

### **3.7 Inter-Corporate Deposits**

**3.7.1** Inter-Corporate Deposits (ICD) may be raised by Primary Dealers sparingly and should not be used as a continuous source of funds. After proper and due consideration of the risks involved, the Board of Directors of the PD should lay down the policy in this regard, which among others should include the following general principles:

- i. While the ceiling fixed on ICD borrowings should in no case exceed 50% of the Net Owned Funds (NOF) of the PD, it is expected that actual dependence on ICDs would be much below this ceiling.
- ii. ICDs accepted by PDs should be for a minimum period of one week.
- iii. ICDs accepted from parent/promoter/group companies or any other related party should be on "arms length basis" and disclosed in financial statements as "related party transactions".
- iv. Funds raised through ICDs are subject to ALM discipline.

**3.7.2** PDs are prohibited from placing funds in ICD market.

### **3.8 FCNR (B) loans /External Commercial Borrowings**

**3.8.1** PDs may avail of FCNR(B) loans up to a maximum of 25% of the NOF and subject to the foreign exchange risk of such loans being hedged at all times at least to the extent of 50 per cent of the exposure.

**3.8.2** PDs are not permitted to raise funds through External Commercial Borrowings.

## **4. Diversification of activities by stand-alone Primary Dealers**

**4.1.** In accordance with paragraph 122 of the Annual Policy Statement for the year 2006-07, it was proposed to permit stand-alone Primary Dealers (PDs) to diversify their activities, as considered appropriate, in addition to their existing business of Government securities, subject to limits.

**4.2.** Accordingly, PDs may bifurcate their operations into core and non-core activities.

**4.2.1.** The following activities are permitted under core activities:

- i. Dealing and underwriting in Government securities
- ii. Dealing in Interest Rate Derivatives
- iii. Providing broking services in Government securities
- iv. Dealing and underwriting in Corporate / PSU / FI bonds/ debentures
- v. Lending in Call/ Notice/ Term/ Repo/ CBLO market
- vi. Investment in Commercial Papers
- vii. Investment in Certificates of Deposit
- viii. Investment in Security Receipts issued by Securitization Companies/ Reconstruction Companies, Asset Backed Securities (ABS), Mortgage Backed Securities (MBS)
- ix. Investment in debt mutual funds where entire corpus is invested in debt securities

**4.2.2.** PDs are permitted to undertake the following activities under non-core activities:

**4.2.2.1.** Activities, which are expected to consume capital such as:

- i. Investment / trading in equity and equity derivatives market
- ii. Investment in units of equity oriented mutual funds
- iii. Underwriting public issues of equity

**4.2.2.2.** Services, which do not consume capital or require insignificant capital outlay such as:

- i. Professional Clearing Services
- ii. Portfolio Management Services
- iii. Issue Management Services

- iv. Merger & Acquisition Advisory Services
- v. Private Equity Management Services
- vi. Project Appraisal Services
- vii. Loan Syndication Services
- viii. Debt restructuring services
- ix. Consultancy Services
- x. Distribution of mutual fund units
- xi. Distribution of insurance products

**4.2.3.** For distribution of insurance products, the PDs may comply with the guidelines contained in the circular No.DNBS(PD)CC No.35/10.24/2003-04 dated February 10, 2004 issued by the Department of Non-Banking Supervision.

**4.2.4.** Specific approvals of other regulators, if needed, should be obtained in respect of the activities detailed above.

**4.2.5.** PDs are **not** allowed to undertake broking in equity, trading / broking in commodities, gold and foreign exchange.

**4.3.** The investment in Government Securities should have predominance over the non-core activities in terms of investment pattern. All PDs are required to ensure predominance by maintaining at least 50 per cent of their total financial investments (both long term and short term) in Government Securities at any point of time. Investment in Government securities will include the PD's Own Stock, Stock with RBI under Liquidity Support / Intra-day Liquidity (IDL)/ Liquidity Adjustment Facility (LAF), Stock with market for repo borrowings and Government Securities pledged with Clearing Corporation of India Ltd. (CCIL).

**4.4.** The exposure to non-core activities shall be subject to the guidelines on regulatory and prudential norms for diversification of activities by stand-alone PDs, which are as under:

**4.4.1** The minimum Net Owned Fund (NOF) requirement for a PD, proposing to undertake non-core activities, as detailed in para 4.2.2.1, should be Rs.100 crore as against Rs.50 crore for a PD, which does not diversify into these activities.

**4.4.2** The exposure to non-core activities, as defined in paragraph 4.2.2.1 *ibid*, shall be subject to risk capital allocation as prescribed below.

**4.4.2.1.** PDs may calculate the capital charge for market risk on the stock positions / underlying stock positions/ units of equity oriented mutual funds using Internal Models (VaR based) based on the guidelines prescribed vide RBI circular No. IDMD.1/ (PDRS) 03.64.00 / 2003-04 dated January 07, 2004 on Capital Adequacy and Risk Management. PDs may continue to provide for credit risk arising out of equity, equity derivatives and equity oriented mutual funds as prescribed in the circular mentioned above.

**4.4.2.2** The guidelines for both credit risk and market risk in respect of Commercial Paper, Corporate / PSU / FI bonds / Underwriting are contained in the RBI circular IDMD 1/(PDRS) 03.64.00 /2003-04 dated January 07, 2004.

**4.4.2.3** The capital charge for market risk (VaR calculated at 99 per cent confidence interval, 15-day holding period, with multiplier of 3.3) for the activities defined in para **4.2.2.1.** above should not be more than 20 per cent of the NOF as per the last audited balance sheet.

**4.4.3** Those PDs, which at present, have taken position beyond the prescribed limit under paragraph 4.4.2.3 above, should ensure adherence to the prescribed limit within a period of six months from the date of the circular.

**4.5.** It has also been decided that PDs will not be permitted to set up step-down subsidiaries. PDs that already have step-down subsidiaries (in India and abroad) may restructure the ownership pattern of these subsidiaries. If the PD is a subsidiary of a holding company, the step-down subsidiary of the PD may become another direct subsidiary of the holding company. In case the PD itself is a holding company, then the step-down subsidiary may take up the PD activity and the holding entity may take up activities other than those permitted for the PDs. The restructuring, as above, should be completed and compliance with the above guidelines may be reported within a period of six months from the date of this circular together with complete details of organizational structure and activities undertaken by the PD. The

PDs involved in activities other than those defined above in para 4.2.2 should either fold back or hive-off these activities to other subsidiaries as detailed above.

## **5. Investment Guidelines**

**5.1 Investment policy** – PDs should frame and implement investment and operational policy guidelines on securities transactions which should be approved by their Boards. The guidelines should contain the broad objectives to be followed while undertaking transactions in securities on their own account and on behalf of clients, clearly define the authority to put through deals, and lay down procedure to be followed while putting through deals, various prudential exposure limits, policy regarding dealings through brokers, systems for management of various risks, guidelines for valuation of the portfolio and the reporting systems etc. Operational procedures and controls in relation to the day-to-day business operations should also be worked out and put in place to ensure that operations in securities are conducted in accordance with sound and acceptable business practices. While laying down these guidelines, the PDs should strictly observe Reserve Bank's instructions, issued from time to time. The effectiveness of the policy and operational guidelines should be periodically evaluated.

**5.2** PDs should necessarily hold their investments in Government securities portfolio in either SGL (with RBI) or a gilt account (with a scheduled commercial bank/State Cooperative Bank/PD/FI or SHCIL) or in a dematerialised account with depositories (NSDL/CDSL). Only one gilt account can be opened by any PD for this purpose. In case this gilt account is not with NSDL/CDSL, additional gilt account is permitted with NSDL/CDSL to enable the PD to settle the trades in government securities concluded on exchanges. All purchase/sale transactions in Government Securities by PDs should be compulsorily through SGL/CSGL/Demat accounts.

**5.3** PDs should make fresh investments and hold Commercial Papers, bonds and debentures, privately placed or otherwise and investments in equity instruments, only in dematerialised form.

**5.4** All securities transactions (including transactions on account of clients) should be subjected to concurrent audit by internal/external auditors to the extent of 100% and the results of the audit should be placed before the CEO/CMD of the PD once every month. The compliance should be monitored on ongoing basis and reported directly to the top management. The concurrent audit should also cover the business done through brokers and include the findings in their report.

**5.5** All problem exposures, which are not backed by any security or backed by security of doubtful value, should be fully provided for. Where a PD has filed suit against another party for recovery, such exposures should be evaluated and provisions made to the satisfaction of auditors. Any claim against the PD should also be taken note of and provisions made to the satisfaction of auditors.

**5.6** The profit and loss account should reflect the problem exposures if any, and also the effect of valuation of portfolio, as per the instructions issued by the Reserve Bank, from time to time. The report of the statutory auditors should contain a certification to this effect.

**5.7** PDs should formulate, within the above parameters, their own internal guidelines on securities transactions in both primary and secondary markets, with the approval of their Board of Directors.

**5.8** PDs should publish their audited annual results in leading financial dailies and on their website in the format prescribed (**Annex VI**). The following minimum information should also be included by way of notes to the Balance Sheet: -

- i. Net borrowings in call (average and peak during the period),
- ii. Basis of valuation,
- iii. Leverage Ratio (average and peak),
- iv. CRAR (quarterly figures), and
- v. Details of the issuer composition of non-Government securities investments.

PDs may also furnish more information by way of additional disclosures.

**5.9** Any change in the shareholding pattern of a PD needs prior approval of RBI. PDs should report any other material changes such as business profile, organization, etc. affecting the conditions of licensing as PD to RBI immediately. PDs should bring to the RBI's attention any major complaint against it or action initiated/taken against it by authorities such as the Stock Exchanges, SEBI, Central Bureau of Investigation, Enforcement Directorate, Income Tax, etc.

## **6. Prudential systems/controls**

### **6.1 Internal Control System in respect of securities transactions**

- i. All the transactions put through by the PD either on outright basis or ready forward basis should be reflected on the same day in its books and records i.e. preparation of deal slip, contract note, confirmation of the counter party, recording of the transaction in the purchase/sale registers, etc.
- ii. With the approval of their Board of Directors, PDs should place appropriate exposure limits / dealing limits, for each of their counter- parties which cover all dealings with such counter parties including money market, repos and outright securities transactions. These limits should be reviewed periodically on the basis of financial statements, market reports, ratings, etc. and exposures taken only on a fully collateralized basis where there is slippage in the rating/assessment of any counterparty.
- iii. With the approval of their Boards, PDs should put in place reasonable leverage ratio for their operations, which should take into account all outside borrowings as a multiplier of their net owned funds.
- iv. There should be a clear functional separation of (i) trading (front office) (ii) risk management (mid office), and (iii) settlement, accounting and reconciliation (back office). Similarly, there should be a separation of transactions relating to own account and constituents' accounts.
- v. For every transaction entered into, the trading desk should generate a deal slip which should contain data relating to nature of the deal, name of the counter-party, whether it is a direct deal or through a broker, and if through a broker, name of the broker, details of security, amount, price, contract date and time and settlement date. The deal slips should be serially numbered and controlled separately to ensure that each deal slip has been properly accounted for. Once the deal is concluded, the deal slip should be immediately passed on to the back office for recording and processing. For each deal, there must be a system of issue of confirmation to the counter-party. The timely receipt of requisite written confirmation from the counter-party, which must include all essential details of the contract, should be monitored by the back office. With respect to transactions matched on the NDS-OM module, since CCIL is the central counterparty to all deals, exposure

of any counterparty for a trade is only to CCIL, and not to the entity with whom a deal matches. Besides, details of all deals matched on NDS-OM are available to the counterparties as and when required by way of reports on NDS-OM itself. In view of the above, the need for counterparty confirmation of deals matched on NDS-OM does not arise.

- v. Once a deal has been concluded, there should not be any substitution of the counter-party by the broker. Similarly, the security sold/purchased in a deal should not be substituted by another security under any circumstances.
- vi. On the basis of vouchers passed by the back office (which should be done after verification of actual contract notes received from the broker/counter-party and confirmation of the deal by the counter party), the Accounts wing should independently write the books of account.
- vii. PDs should periodically review securities transactions and report to the top management, the details of transactions in securities, details of funds/securities delivery failures, even in cases where shortages have been met by CCIL.

## **6.2. Purchase/Sale of securities through SGL transfer forms**

With the commissioning of Negotiated Dealing System (NDS), all PDs are expected to be the members of NDS and conclude/report all outright and repo transactions on NDS and clear/settle them through CCIL as central counter-party. In such cases where exceptions have been permitted to tender physical SGL transfer forms, following guidelines should be followed:

- i. Records of all SGL transfer forms issued/received should be maintained and a system for verification of the authenticity of the SGL transfer forms received from the counter-party and confirmation of authorised signatories should be put in place.
- ii. Under no circumstances, a SGL transfer form issued by a PD in favour of a counter-party should bounce for want of sufficient balance in the SGL/Current Account. Any instance of return of SGL form from the Public Debt Office of the Reserve Bank for want of sufficient balance in the account should be immediately brought to the notice of the PD's top management and reported to RBI with the details of transactions.

- iii. SGL Transfer forms received by purchasing PDs should be deposited in their SGL Accounts immediately. No sale should be effected by way of return of SGL form held by the PD.
  - iv. SGL transfer form should be in a standard format prescribed by the Reserve Bank and printed on semi-security paper of uniform size. They should be serially numbered and there should be a control system in place to account for each SGL form.
- 6.3.** Bank Receipt or similar receipt should not be issued or accepted by the PDs under any circumstances in respect of transactions in Government securities.
- 6.4. Accounting Standards for securities transactions**
- i. PDs should adopt the practice of valuing all securities in their trading portfolio on mark to market basis, at appropriate intervals.
  - ii. Costs such as brokerage fees, commission or taxes incurred at the time of acquisition of securities, are of revenue/deferred nature. The broken period interest received/paid also get adjusted at the time of coupon payment. PDs can adopt either the IAS or GAAP accounting standards, but has to ensure that the method should be true and fair and should not result in overstating the profits or assets value and should be followed consistently and be generally acceptable especially to the tax authorities.
  - iii. Broken period interest paid to seller as part of cost on acquisition of Government and other securities should not be capitalised but treated as an item of expenditure under Profit and Loss Account. The PDs may maintain separate adjustment accounts for the broken period interest.
  - iv. The valuation of the securities portfolio should be independent of the dealing and operations functions and should be done by obtaining the prices declared by Fixed Income Money Market and Derivatives Association of India (FIMMDA) periodically.
- 6.5. Reconciliation of holdings of Government securities etc.**
- Balances as per PDs books should be reconciled at least on monthly intervals with the balances in the books of PDOs. If the number of transactions so warrant, the

reconciliation should be undertaken at more frequent intervals. This reconciliation should be periodically checked during audit.

#### **6.6. Transactions on behalf of Constituents:**

- i. The transactions on behalf of constituents and the operations in the Constituent SGL accounts should be conducted in accordance with the guidelines issued by RBI on the Constituent SGL accounts.
- ii. All transaction records should give a clear indication that the transaction belongs to constituents and does not belong to PDs' own account.
- iii. The PDs should be circumspect while acting as agent of their clients for carrying out transactions in securities on behalf of clients.
- iv. PDs should not use the constituents' funds or constituents' assets for proprietary trading or for financing of another intermediary's operations.
- v. PDs who act as custodians (i.e. CSGIL account holders) and offer the facility of maintaining gilt accounts to their constituents, should not permit settlement of any sale transaction by their constituents unless the security sold is actually held in the gilt account of the constituent.

#### **6.7 Failure to complete delivery of security/funds in an SGL transaction**

Any default in delivery of security/funds in an SGL sale /purchase transaction undertaken by a PD will be viewed seriously. A report on such transaction even if completed through the securities/funds shortage handling procedure of CCIL, must be submitted to Internal Debt Management Department, Reserve Bank of India immediately. The occurrence of third default in a period of 6 months (April - September and October-March) in funds and/or securities delivery will result in debarment of the PD for period of 6 months from the third occurrence, from trading with the use of SGL facility. If after restoration of the facility, any default occurs again, the PD will be debarred permanently from the use of SGL facility.

## **7. Trading of Government Securities on Stock Exchanges**

**7.1** With a view to encouraging wider participation of all classes of investors, including retail in Government securities, trading in Government securities through a nationwide, anonymous, order driven screen based trading system on stock exchanges, in the same manner in which trading takes place in equities has been permitted. Accordingly trading of dated Government of India securities in dematerialized form is allowed on automated order driven system of the National Stock Exchange (NSE) of India, The Stock Exchange Mumbai (BSE) and the Over the Counter Exchange of India (OTCEI). This trading facility is in addition to the reporting/trading facility in the Negotiated Dealing System. Being a parallel system, the trades concluded on the exchanges will be cleared by their respective clearing corporations/clearing houses. The trades of PDs should be settled either directly with clearing corporation/clearing house (in case they are clearing members) or through clearing member custodian.

**7.2** PDs are expected to play an active role in providing liquidity to the Government Securities Market and promote retailing. They may, therefore, make full use of proposed facility to distribute Government securities to all categories of investors through the process of placing and picking-up orders on the exchanges. PDs may open demat accounts with a Depository Participant (DP) of NSDL/CDSL in addition to their accounts with RBI. Value free transfer of securities between SGL/CSGL and demat accounts would be enabled by PDO-Mumbai subject to guidelines issued by RBI's Department of Government and Bank Accounts (DGBA) in this behalf separately.

### **7.3 Operational Guidelines**

- i. PDs should take specific approval from their Board to enable them to trade in the Stock Exchanges.
- ii. PDs may undertake transactions only on the basis of giving and taking delivery of securities.
- iii. Brokers/trading members shall not be involved in the settlement process; all trades have to be settled either directly with clearing corporation/clearing house (in case they are clearing members) or else through clearing member custodians.

- iv. The trades done through any single broker will also be subject to the current regulations on transactions done through brokers (please see para 8.1).
- v. At the time of trade, securities must be available with the PDs either in their SGL or in the demat account.
- vi. A standardized settlement on T+1 basis of all outright secondary market transactions in Government Securities has been adopted to provide the participants more processing time for transactions and to help in better funds as well as risk management.
- vii. In the case of repo transactions in Government Securities, however, market participants will have the choice of settling the first leg on either T+0 basis or T+1 basis, as per their requirements.
- viii. 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 transactions will be applicable. Stock Exchanges will report such failures to the respective Public Debt Offices.
- ix. PDs who are trading members of the Stock Exchanges may have to put up margins on behalf of their non-institutional client trades. Such margins are required to be collected from the respective clients. PDs are not permitted to pay up margins on behalf of their client trades and incur overnight credit exposure to their clients. In so far as the intra day exposures on clients for margins are concerned, the PDs should be conscious of the underlying risks in such exposures.
- x. PDs who intend to offer clearing /custodial services should take specific approval from SEBI in this regard. Similarly, PDs who intend to take trading membership of the Stock Exchanges should satisfy the criteria laid down by SEBI and the Stock Exchanges.

## **8. Business through brokers**

### **8.1 Business through brokers and contract limits for approved brokers -**

PDs may undertake securities or derivative transactions among themselves or with clients through the members of the BSE, NSE and OTCEI. A disproportionate part of the business should not be transacted through only one or a few brokers. PDs should fix aggregate contract limits for each of the approved brokers. A limit of 5%, of total transactions (both purchase and sales) entered into by a PD during a year should be treated as the aggregate upper contract limit for each of the approved brokers. However, if for any reason it becomes necessary to exceed the aggregate limit for any broker, the specific reasons therefor should be recorded and the Board should be informed of this, post facto.

**8.2** With the approval of their top management, PDs should prepare a panel of approved brokers, which should be reviewed annually, or more often if so warranted. Clear-cut criteria should be laid down for empanelment of brokers, including verification of their creditworthiness, market reputation, etc. A record of broker-wise details of deals put through and brokerage paid, should be maintained.

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

**8.4** The role of the broker should be restricted to that of bringing the two parties to the deal together. Settlement of deals between PDs and counter-parties should be directly between the counter-parties and the broker will have no role in the settlement process.

**8.5** While negotiating the deal, the broker is not obliged to disclose the identity of the counter-party to the deal. On conclusion of the deal, he should disclose the counter-party and his contract note should clearly indicate the name of the counter-party.

## **9. Norms for Ready Forward transactions**

Primary Dealers are permitted to participate in Ready Forward (Repo) market both as lenders and borrowers. The terms and conditions subject to which ready forward

contracts (including reverse ready forward contracts) may be entered into by PDs will be as under:

- i. Repos may be undertaken only in i) dated securities and Treasury Bills issued by the Government of India and ii) dated securities issued by the State Governments.
- ii. Repos may be entered into only with scheduled commercial banks, Urban Cooperative banks, other PDs, NBFCs, mutual funds, housing finance companies, insurance companies and any listed company, provided they hold either an SGL account with RBI or a Gilt account with a custodian.
- iii. Listed companies can enter into repo transactions subject to the following conditions:
  - (a) The minimum period for Reverse Repo (lending of funds) by listed companies is seven days. However, listed companies can borrow funds through repo for shorter periods including overnight;
  - (b) Where the listed company is a 'buyer' of securities in the first leg of the repo contract (i.e. lender of funds), the custodian through which the repo transaction is settled should block these securities in the gilt account and ensure that these securities are not further sold or re-repoed during the repo period but are held for delivery under the second leg; and
  - (c) The counterparty to the listed companies for repo/reverse repo transactions should be either a bank or a Primary Dealer maintaining SGL Account with the Reserve Bank.
- iv. A PD may not enter into a repo with its own constituent or facilitate a repo between two of its constituents.
- v. PDs should report all repos transacted by them (both on own account and on the constituent's account) on the Negotiated Dealing System (NDS). All repos shall be settled through the SGL Account/CSGL Account maintained with the RBI, Mumbai, with the Clearing Corporation of India Ltd (CCIL) acting as the central counter party.
- vi. Securities acquired under a reverse repo cannot be traded/sold/further repoed before the reversal date.
- vii. The purchase/sale price of the securities in the first leg of a repo should be in alignment with the proximate market rates prevalent on the date of transaction.

- viii. Repo transactions, which are settled under the guaranteed settlement mechanism of CCIL, may be rolled over, provided the security prices and repo interest rate are renegotiated on roll over.
- ix. 'The Global Master Repos Agreement' on repos, with suitable schedules, as proposed by FIMMDA may be entered into by PDs with their counter parties to repos transactions.

## **10. Portfolio Management Services**

**10.1** PDs may offer Portfolio Management Services (PMS) to their clients under the SEBI scheme of PMS, subject to the following conditions. Before undertaking PMS,

the PD must have obtained the Certificate of Registration as Portfolio Manager from the SEBI and also a specific approval from the RBI.

- i. PMS cannot be offered to any RBI regulated entity. However advisory services can be provided to them with suitable disclaimers.
- ii. Where applicable, the clients regulated by any other authority should obtain clearance from the regulatory or any other authority before entering into any PMS arrangement with the PD.
- iii. PDs are required to comply with the SEBI (Portfolio Managers) Regulations, 1993 and any amendments issued thereto or instructions issued there under.

**10.2** In addition, PDs should adhere to the under noted conditions:

- i. A clear mandate from the PMS clients should be obtained and the same strictly followed. In particular, there should be full understanding on risk disclosures, loss potential and the costs (fees and commissions) involved.
- ii. PMS should be entirely at the customer's risk without guaranteeing, either directly or indirectly, any return.
- iii. Funds/securities, each time they are placed with the PD for portfolio management, should not be accepted for a period less than one year.
- iv. Portfolio funds should not be deployed for lending in call/ notice/term money/Bills rediscounting markets, badla financing or lending to/ placement with corporate/non-corporate bodies.
- v. Client-wise accounts/records of funds accepted for management and investments made there against should be maintained and the clients should be entitled to get statements of account at frequent intervals.
- vi. Investments and funds belonging to PMS clients should be kept segregated and distinct from each other and from those of the PD. As far as possible, all client transactions should be executed in the market and not off-set internally, either with the PD or any other client. All transactions between the PD and any PMS client or between two PMS clients, if any when necessary, should be strictly at market rates.

## **11. Guidelines on interest rate derivatives**

**11.1** PDs are permitted to undertake transactions in both specified Over-the-Counter (OTC) and Exchange Traded Interest Rate Derivatives (IRDs).

### **11.2 OTC Derivatives**

PDs may undertake transactions in Forward Rate Agreements (FRA) and Interest Rate Swaps (IRS) for their own balance sheet management or for market making purposes in terms of RBI's Monetary Policy Department (MPD) circular MPD.BC.187/07.01.279/1999-2000 dated July 7,1999. The guidelines contained in that circular should be strictly observed. It is, however, not necessary for the PDs to get the prudential limits on swap positions vetted by IDMD after approval of respective boards.

### **11.3 Exchange Traded Derivatives**

**11.3.1** PDs can transact only in interest rate futures on notional bonds and T-Bills both for hedging the risk in their underlying investment portfolio and trading position. PDs desirous of transacting in IRDs on the stock exchanges should formulate the policy framework and appropriate risk control measures which their respective Boards should approve before they undertake trades in interest rate futures on the stock exchanges. PDs should take specific approval from their Board covering, *inter alia*, the products that they may transact, size/composition of the investment portfolio intended to be hedged, clear demarcation of trading portfolio from that of hedging portfolio, organizational set-up to monitor, rebalance, report, account and audit such transactions. Further, it is desirable that derivative desks are created within the Treasury and the management level responsibility clearly assigned.

**11.3.2 Stock exchange regulation:** PDs desirous of taking trading membership of the Stock Exchanges should satisfy the membership criteria and also comply with the regulatory norms laid down by SEBI and the respective stock exchanges (BSE/NSE). Those not seeking membership of Stock Exchanges can transact IRDs through approved F & O members of the exchanges.

**11.3.3 Settlement:** As trading members of the F&O segment, PDs should settle their derivative trades directly with the clearing corporation/clearing house. PDs participating through approved F & O members shall settle proprietary trades as a

participant clearing member or through approved professional / custodial clearing members. Broker / trading members of stock exchanges cannot be used for settlement of IRD transactions.

#### 11.3.4 Hedging positions

- i. **Eligible underlying:** For the present, only the interest rate risk inherent in the portfolio of Government securities can be hedged. For this purpose, the securities intended to be hedged must be identified and carved out for monitoring purposes.
- ii. **Hedge criteria:** IRD transactions undertaken on the exchanges shall be deemed as hedge transactions, if and only if,
  - a. The hedge is clearly identified with the underlying Government securities in the investment portfolio.
  - b. The effectiveness of the hedge can be reliably measured.
  - c. The hedge is assessed on an ongoing basis and is “highly effective” throughout the period.
- iii. **Hedge Effectiveness:** The hedge will be deemed to be “highly effective” if at inception and throughout the life of the hedge, changes in the marked- to-market value of the hedged items with reference to the marked-to- market value at the time of the hedging are “almost fully offset” by the changes in the marked-to-market value of the hedging instrument and the actual results are within a range of 80% to 125%. If changes in the marked-to-market values are outside the 80% to 125% range, then the hedge would not be deemed to be highly effective.

The hedged portion of the investment portfolio should be notionally marked-to-market, at least at monthly intervals, for evaluating the efficacy of the hedge transaction.

**11.3.5 Trading positions:** Primary Dealers may hold trading positions in exchange traded IRDs subject to the following prudential regulations:

- i. **Construction of trading portfolio:** The trading portfolio of the participants comprising IRS, FRAs, exchange traded IRDs etc. should be clearly demarcated from that of the hedging portfolio.
- ii. **Interest rate sensitivity of trading portfolio:** The interest rate derivatives should be split into basic building blocks and PV01 / VaR limits on the trading portfolio of interest rate derivatives (comprising OTC as well as exchange

traded) be approved by the ALCO. For the purpose, the floating rate leg of MIFOR linked swaps should be adjusted against the gap limits and the fixed leg included in the rupee trading positions. ALCO should also consider placing similar limits on the composition of trading positions comprising balance sheet and off-balance sheet products.

**11.3.6 Accounting Standards:** The Accounting Standards Board of the Institute of Chartered Accountants of India (ICAI) is in the process of developing a comprehensive Accounting Standard covering various types of financial instruments including accounting for trading and hedging. However, as the formulation of the Standard is likely to take some time, the Institute has brought out a Guidance Note on Accounting for Equity Index Futures as an interim measure. Till ICAI comes out with a comprehensive Accounting Standard, PDs may follow the above guidance note *mutatis mutandis* for accounting of exchange traded IRDs also.

**11.3.7 Accounting for Hedging Positions:** The following norms will apply in relation to hedging positions of PDs.

- i. If the hedge is “highly effective”, the gain or loss on the hedging instruments and hedged portfolio may be set off and any net gain / loss treated as per the accounting practice adopted for the investment portfolio.
- ii. If the hedge is not found to be "highly effective", no set-off will be allowed and the underlying securities will be marked to market as per the accounting practices adopted for the portfolio.
- iii. A hedge may be temporarily rendered as not “highly effective”. Under such circumstances, the relevant futures position will be deemed as a trading position. All deemed trading positions should be marked to market as a portfolio on a daily basis and losses should be provided for and gains, if any, should be ignored for the purpose of Profit & Loss Account. PDs should strive to restore their hedge effectiveness at the earliest.
- iv. Any gains realized from closing out / settlement of futures contracts can not be taken to Profit & Loss account but carried forward as "Other Liability" and utilized for meeting depreciation provisions on the investment portfolio.

**11.3.8 Accounting for trading positions:** The following should be used as general principles for accounting of trading transactions:

- i. Trading positions in interest rate derivatives (OTC and Exchange traded) should be marked to market on a daily basis.

- ii. Profits and Losses arising out of trading positions should be taken to the Profit & Loss Account.

**11.3.9 ALM classification:** The ALM classification will apply differently to the hedging positions and trading positions in IRDs. In case of hedging, interest rate futures may be treated as a combination of a long and short position in a notional Government security. The maturity of a future will be the period until delivery or exercise of the contract, as also the life of the underlying instrument. For example, a short position in interest rate future for Rs. 50 crore [delivery date after 6 months, life of the notional underlying Government security 3½ years] is to be reported as a rate sensitive asset under the 3 to 6 month bucket and a rate sensitive liability in four years i.e. under the 3 to 5 year bucket. Trading positions should be classified as rate sensitive asset or liability, as the case may be, under 0-30 day maturity bucket.

**11.3.10 Client Trades:** PDs who are trading members of the Stock Exchanges may have to put up margins on behalf of their non-institutional client trades. Such margins are required to be collected upfront from the respective clients. PDs are not permitted to pay up margins on behalf of their client trades and incur overnight credit exposure to their clients. In so far as the intra day exposures on clients for margins are concerned, the PDs should be conscious of the underlying risks in such exposures.

**11.3.11 Disclosures and reporting:** The PDs undertaking interest rate derivatives on exchanges may disclose as a part of the notes on accounts to balance sheets the following details:

(Rs. Crore)		
Sr.No.	Particulars	Amount
1	Notional principal amount of exchange traded interest rate futures undertaken during the year (product-wise) a) b) c)	
2	Notional principal amount of exchange traded interest rate futures outstanding as on 31 <sup>st</sup> March _____ (product -wise) a) b) c)	
3	Notional principal amount of exchange traded interest rate futures outstanding and not "highly effective" (product -wise) a)	

	b) c)	
4	Mark-to-market value of exchange traded interest rate futures outstanding and not “highly effective” (product -wise) a) b) c)	
5.	Notional Principal Amount of trading positions in Interest Rate Futures outstanding as on 31 <sup>st</sup> March _____ (product -wise) a) b) c)	

## **12. Guidelines on investment in non-Government Securities**

**12.1** These guidelines cover PDs' investments in non-Government securities (including capital gains bonds, bonds eligible for priority sector status, bonds issued by Central or State public sector undertakings with or without Government guarantees and bonds issued by banks and financial companies) generally issued by corporates, banks, FIs and State and Central Government sponsored institutions, SPVs etc. These guidelines will, however, not be applicable to (i) units of equity oriented mutual fund schemes where any part of the corpus can be invested in equity, (ii) venture capital funds, (iii) commercial paper, (iv) certificate of deposit, and (v) investments in equity shares. The guidelines will apply to investments both in the primary market as well as the secondary market.

**12.2** PDs should not invest in non-Government securities of original maturity of less than one-year, other than Commercial Paper and Certificates of Deposits, which are covered under RBI guidelines.

**12.3** PDs should undertake usual due diligence in respect of investments in non-Government securities.

**12.4** PDs must not invest in unrated non-Government securities.

**12.5** The PDs will abide by the requirements stipulated by the SEBI in respect of corporate debt securities. Accordingly, while making fresh investments in non-Government debt securities, PDs should ensure that such investment are made only in listed debt securities, except to the extent indicated in paragraphs 12.6 and 12.7 below.

**12.6** PDs' investment in unlisted non-Government securities should not exceed 10% of the size of their non-Government securities portfolio on an on-going basis. The ceiling of 10% will be inclusive of investment in Security Receipts issued by Securitization Companies/Reconstruction Companies and also the investment in Asset Backed Securities (ABS) and Mortgage Backed Securities (MBS). The unlisted non-Government debt securities in which PDs may invest up to the limits specified above, should comply with the disclosure requirements as prescribed by the SEBI for listed companies.

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

- i. Investment in units of only such mutual fund schemes that have an exposure to unlisted securities of less than 10 per cent of the corpus of the fund will be treated on par with listed securities for the purpose of compliance with the prudential limits prescribed in the above guidelines.
- ii. Only PDs whose investment in unlisted non-Government securities are within the prudential limits prescribed in the above guidelines may make fresh investment in such securities and up to the prudential limits.

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

**12.9** Boards of PDs should review the following aspects of non-Government investment at least at quarterly intervals:

- i. Total business (investment and divestment) during the reporting period.
- ii. Compliance with the prudential limits prescribed by the Board for investment in non-Government securities.
- iii. Compliance with the prudential guidelines on non-Government securities prescribed above.
- iv. Rating migration of the issuers/ issues held in the PDs' books and consequent diminution in the portfolio quality.

**12.10** In order to help in the creation of a central database on private placement of debt, a copy of all offer documents should be filed with the Credit Information Bureau (India) Ltd. (CIBIL) by the PDs. Further, any default relating to interest/ installment in

respect of any privately placed debt should also be reported to CIBIL by the investing PDs along with a copy of the offer document.

**12.11** 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 these SEBI guidelines, (as and when applicable) PDs should ensure that all spot transactions in listed and unlisted debt securities are reported on the NDS and settled through the CCIL from a date to be notified by RBI.

### 13. Guidelines on declaration of dividends

PDs should follow the following guidelines while declaring dividend distribution:

- i. The PD should have complied with the regulations on transfer of profits to statutory reserves and the regulatory guidelines relating to provisioning and valuation of securities, etc.
- ii. PDs having Capital to Risk Weighted Assets Ratio (CRAR) below the regulatory minimum of 15 per cent in any of the previous four quarters cannot declare any dividend. For PDs having CRAR between the regulatory minimum of 15 per cent during all the four quarters of the previous year, but lower than 20 per cent in any of the four quarters, the dividend payout ratio should not exceed 33.3 per cent. For PDs having CRAR above 20 per cent during all the four quarters of the previous year, the dividend payout ratio should not exceed 50 per cent. Dividend payout ratio should be calculated as a percentage of dividend payable in a year (excluding dividend tax) to net profit during the year.
- iii. The proposed dividend should be payable out of the current year's profits. In case the profit for the relevant period includes any extraordinary profit income, the payout ratio should be computed after excluding such extraordinary items for reckoning compliance with the prudential payout ratio ceiling of 33.3 per cent or 50 per cent, as the case may be.
- iv. The financial statements pertaining to the financial year for which the PD is declaring dividend should be free of any qualifications by the statutory auditors, which have an adverse bearing on the profit during that year. In case of any qualification to that effect, the net profit should be suitably adjusted downward while computing the dividend payout ratio.
- v. In case there are special reasons or difficulties for any PD in strictly adhering to the guidelines, it may approach Reserve Bank in advance for an appropriate *ad hoc* dispensation in this regard.
- vi. All the PDs declaring dividend should report details of dividend declared during the accounting year as per the prescribed proforma. The report should be furnished within a fortnight of payment of dividend.

#### 14. Guidelines on Issue of Subordinated Debt Instruments

In continuation to RBI circular IDMD.No.01/PDRS/03.64.00/2003-04 dated January 07, 2004, the guidelines relating to issue of Subordinated Debt Instruments under Tier II and Tier III Capital are furnished below:

- i. The amount of Subordinated Debt to be raised may be decided by the Board of Directors of the PD.
- ii. The interest rate spread of the instrument over the yield of equal residual maturity of the Government of India dated security at the time of issue shall not exceed 200 bps.
- iii. The instruments should be 'plain vanilla' with no special features like options, etc.
- iv. The debt securities shall carry a credit rating from a Credit Rating Agency registered with the Securities and Exchange Board of India.
- v. The issue of Subordinated Debt instruments should comply with the guidelines issued by SEBI vide their circular SEBI/MRD/SE/AT/36/2003/30/09 dated September 30, 2003 as amended from time to time, wherever applicable.
- vi. In case of issue of unlisted issues of Subordinated Debt, the disclosure requirements as prescribed by the SEBI for listed companies in terms of the above guidelines should be complied with.
- vii. Necessary permission from the Foreign Exchange Department of the Reserve Bank of India should be obtained for issuing the instruments to NRIs/FIIs. PDs should comply with the terms and conditions, if any, prescribed by SEBI/other regulatory authorities in regard to issue of the instruments.
- viii. Investments by PDs in Subordinated Debt of other PDs/banks will be assigned 100% risk weight for capital adequacy purpose. Further, the PD's aggregate investments in Tiers II and III bonds issued by other PDs, banks and financial institutions shall be restricted upto 5 percent of the investing PD's total capital. The capital for this purpose will be the same as that reckoned for the purpose of capital adequacy.
- ix. The PDs should submit a report to the Internal Debt Management Department, Reserve Bank of India giving details of the capital raised,

such as, amount raised, maturity of the instrument, rate of interest together with a copy of the offer document, soon after the issue is completed.

**Notes:**

Other general guidelines prescribed in RBI circular IDMD. No. 01/PDRS/03.64.00/2003-04 dated January 07, 2004 on Capital Adequacy Standards and Risk Management Guidelines for Primary Dealers may also be kept in view.

**15. Violation/Circumvention of Instructions**

Any violation/circumvention of the above guidelines would be viewed seriously and such violation would attract penal action including the withdrawal of liquidity support, denial of access to the money market, withdrawal of authorisation for carrying on the business as a Primary Dealer, and/or any other penalty the Reserve Bank may deem fit.

**UNDERTAKING**

To

The Chief General Manager-in-Charge,  
Internal Debt Management Department,  
Reserve Bank of India,  
Central Office Building,  
Mumbai-400 001.

By

.....  
Registered Office .....

WHEREAS the Reserve Bank of India (RBI) has offered in principle to admit us as a Primary Dealer in Government securities in accordance with the Guidelines dated January 1, 2002 for the Primary Dealers in Government Securities Market.

AND WHEREAS as a precondition to our being authorised as a Primary Dealer we are required to furnish an undertaking covering the relative terms and conditions

AND WHEREAS at the duly convened Board of Directors meeting of \_\_\_\_\_ on \_\_\_\_\_, the Board has authorised Shri/Smt./Kum. \_\_\_\_\_ and Shri/Smt./Kum. \_\_\_\_\_ to execute and furnish an UNDERTAKING to the Reserve Bank of India jointly and severally as set out below:

NOW, THEREFORE, in consideration of the RBI agreeing to admit us as a Primary Dealer, we hereby undertake and agree:

1. To commit to aggregatively bid in the auction of Treasury Bills and Government of India Dated Securities to the extent of .....per cent of each issue of auction Treasury Bills and for a minimum amount equal to the underwriting commitment (allotted under Minimum Underwriting Commitment and Additional Competitive Underwriting) for Government of India Dated Securities and to maintain the success ratio in aggregate winning bids at not less than 40 per cent for Treasury Bills.
2. To offer to underwrite primary issues of Government of India dated securities, Treasury Bills and State Government securities, for which auction is held, and accept devolvement, if any, of any amount as may be determined by RBI in terms of prevalent scheme for Bidding, Underwriting.
3. To determine prudential ceilings, with the prior approval of the Board of Directors of the company, for reliance on borrowings from the money market including repos, as a multiple of net owned funds, subject to the guidelines, if any, issued by the Reserve Bank in this regard.

4. To offer firm two-way quotes through the Negotiated Dealing System/ over the counter telephone market/ recognised Stock Exchanges in India and deal in the secondary market in Government dated securities and Treasury Bills of varying maturity from time to time and take principal positions.
5. To achieve a sizeable portfolio in Government securities and to actively trade in the Government securities market.
6. To achieve an annual turnover of not less than 5 times in Government dated securities and not less than 10 times in Treasury Bills of the average of month-end stocks subject to the turnover in respect of outright transactions being not less than 3 times in government dated securities and 6 times in Treasury Bills. To maintain the capital adequacy standards prescribed by the Reserve Bank of India, Internal Debt Management Department vide circular IDMD.No.01/(PDRS) 03.64.00 /2003-04 January 07, 2004 and to subject ourselves to all prudential and regulatory guidelines as may be issued by the Reserve Bank of India, Internal Debt Management Department from time to time.
7. To maintain infrastructure in terms of both physical apparatus and skilled manpower for efficient participation in primary issues, trading in the secondary market, and for providing portfolio advice and education to investors.
8. To continue to have in place the "Guidelines on Securities Transaction to be followed by Primary Dealers" issued under cover of IDMC.No.PDRS/2049-A/03.64.00/99-2000 dated December 31, 1999 and Master Circulars issued from time to time as also other necessary internal control systems for fair conduct of business and settlement of trades and maintenance of accounts.
9. To comply with all applicable Reserve Bank of India/Securities and Exchange Board of India (SEBI) requirements under the guidelines existing, and which may be laid down from time to time in this behalf, failing which RBI would be at liberty to cancel the authorisation as a Primary Dealer.
10. To abide by the code of conduct as laid down by RBI/SEBI or the Primary Dealers' Association of India.
11. To maintain and preserve such information, records, books and documents pertaining to our working as a Primary Dealer as may be specified by the RBI from time to time.
12. To permit the RBI to inspect all records, books, information, documents and make available the records to the Inspectors and render all necessary assistance.
13. To maintain at all times a minimum net owned funds of Rs. 50 crore in Government securities and that the liquidity support, if any, availed and net borrowings from call money market and net repo borrowings are dedicated exclusively to the Government securities business.

14. To maintain an arms length distance from parent company/promoters.
15. To obtain prior approval of Reserve Bank of India for any change in the shareholding pattern of the company.
16. To submit in prescribed formats periodic reports including daily transactions and market information, monthly report of details of transactions in securities and risk position and performance with regard to participation in auctions, annual audited accounts and an annual performance review and such statements, certificates and other documents and information as may be specified by RBI from time to time.
17. To report the matter immediately to RBI and abide by such orders, instructions, decisions or rulings given by the RBI if and when any kind of investigation/inquiry/inspection is initiated against us by statutory/regulatory authorities, e.g. SEBI/RBI, Stock Exchanges, Enforcement Directorate, Income-tax authorities, etc.

We do hereby confirm that the above undertakings will be binding on our successors and assigns.

Dated this        day of                    Two Thousand .....

Signed, sealed and delivered by the within named,        )  
 being the authorized persons, in terms of the                )  
 Resolution No. \_\_\_\_\_ of the Board of Directors        )  
 at the duly convened Meeting held on \_\_\_\_\_        )  
 in the in the presence of \_\_\_\_\_                                )

Signatory        (i)  
                       (ii)  
 Witness         (i)  
                       (ii)

## Annex II

## A. Statements / Returns required to be submitted by Primary Dealers to IDMD

Sr. No.	Return/Report	Periodicity	Last date for submission	Reference under which required
1.	PDR-I*	Fortnightly	Next working day of the reporting fortnight	PD Guidelines
2.	PDR-II*	Monthly	10th of the following month	
3.	PDR-III*	Quarterly	15 of the month following the reporting quarter	
4.	PDR IV*	Quarterly	15 <sup>th</sup> of the month of the month following the reporting quarter	
5.	Annual Report & Annual Audited A/cs	Annual	As soon as annual accounts audited and finalised	
6.	Auditor's Certificate on Net Owned Funds	Yearly	30th June	
7.	Reconciliation of holdings of Govt. Securities in own A/c and constituent A/c	Yearly	One month from the close of accounting year	IDMC.No.PDRS/2049A/03.64.00/99-2000 dated December 31, 1999
8.	Return on FRAs / IRS*	Fortnightly	As prescribed by MPD	MPD.BC.187/07.01.279/1999-2000 dated July 7, 1999.
9.	Deviations, <b>if any</b> , reported by Concurrent Auditors on sale transactions of securities allotted in Primary Issues on the same day	Monthly	15th of the month following the reporting month	IDMC.PDRS.No. PDS.1/03.64.00/2000-2001 dated October 6, 2000
10.	Statement of Transactions effected between Gilt A/c holders	Weekly	Next working day following the reporting week	PDO/SGL/CIRR. No. 07.01.13/2950/2000-2001 dated November 8, 2000.
11.	Investments in non-Government securities	Yearly	Disclosures in the 'Notes on Accounts' of the balance sheet, with effect from	IDMD.PDRS.No.3 /03.64.00/ 2003-04

			the financial year ending 31 March 2004.	March 08, 2004
12.	Details of dividend declared during the accounting year	Yearly	Within a fortnight from the payment of dividend	IDMD.PDRS.No 6 /03.64.00/ 2003-04 June 03, 2004

**\* = Indicates that these returns should be submitted in electronic form as an excel file attachment through e-mail.**

**B. Statements / Returns required to be submitted by Primary Dealers to other departments (other than IDMD) of Reserve Bank of India**

Sr. No.	Return/Report	Periodicity	To be filed with Deptt.	Reference under which required
1.	Return on FRAs / IRS	Fortnightly	MPD and IDMD	MPD.BC.187/07.01.27 9/1999-2000 dated July 7, 1999.
2.	Statement showing balances of Govt. Securities held on behalf of each Gilt A/c holder	Half-Yearly	PDO	
3.	Return on Call Money transactions with Commercial Banks	Fortnightly	DEAP, DMB	
4.	Daily Return on Call/Notice/Term Money Transactions	Daily	MPD	For non-NDS members
5.	Call and Notice Money Operations during the Fortnight	Fortnightly		
6.	Total Investments and Resources invested in short-term Instruments	Monthly		
7.	Information for Issue of Commercial Paper	On each issue of CP	MPD	IECD.2/08.15.01/2001-02 dated July 23, 2001

**Note: 1. Return no. 9 is to be submitted to IDMD and MPD as hitherto.**

**2. The last date prescribed for submission of these statements by the concerned departments and/or IDMD should be adhered to.**

## Annex III

## Illustration showing the underwriting amount, cut off rate of underwriting fee accepted by Reserve Bank of India

	Instrument Name	XXXXXXXXXX		
	Auction Type	Multiple		
	Notified amount (NA) (in Rs. crore)	4000		
	No. of Standalone PDs	17		
	No. of Bank-PDs	0		
	Total No. of PDs (n)	17		
a	Minimum Underwriting Commitment (MUC )	2000		
b	Per PD MUC (MUC/ n)	117.65	Rounded off Value	118
c	Adjusted MUC	2006		
d	Additional competitive underwriting ACU = (NA - Adjusted MUC)	1994		
e	Minimum bidding by each PD in ACU (3% of NA)	120		
f	Minimum allotment to a PD to be eligible for higher commission on MUC i.e. min 4% of NA	160		

## Additional Competitive Underwriting (Bids Submitted)

		a	b	c	d		
S. No	PDs participated in U/W	Amount of bid in ACU (Rs. Crore)	Cumulative Amount (Rs. Cr)	Underwriting fee (in paise)	Amount of bid x U/w fee		
1	A	150	150	1.52	228		
2	B	155	305	2.56	396.8	Three lowest bids	
3	A	60	365	3.5	210		
4	C	95	460	3.7	351.5		
5	B	200	660	3.94	788		
6	B	25	685	4	100		
7	D	120	805	4	480		
8	E	95	900	4.49	426.55		
9	F	70	970	4.5	315		
10	G	50	1020	4.75	237.5		
11	E	115	1135	4.9	563.5		
12	C	90	1225	4.94	444.6		
13	F	220	1445	4.95	1089		
14	G	200	1645	5	1000		
15	H	120	1765	5	600		
16	I	120	1885	5	600		
17	I	109	1994	5	545	CUT-OFF	1994
18	I	25	2019	5.5	137.5		
19	J	120	2139	5.94	712.8		

20	K	120	2259	6	720		
21	L	120	2379	6	720		
22	M	55	2434	6.5	357.5		
23	N	120	2554	6.94	832.8		
24	O	120	2674	7	840		
25	P	120	2794	7	840		
26	Q	120	2914	7	840		

Rate of commission payable to Winner(#) PDs on MUC @ 4.20

Rate of commission payable to other PDs on MUC \* 2.29

(three lowest bids)

# Winner PDs are those who have been allotted an amount  $\geq$  4% of ACU amount

@ Weighted Average Commission of all allotted bids

\* Weighted Average Commission of three lowest allotted bids

#### PD Wise eligible commission on ACU and ACU Allotment

[1]	[2]	[3]	[4]=[2] x [3]
Successful PDs	Successful bids in ACU (Rs. Cr)	Underwriting fee bid (in paise)	bid wise comm. payable on ACU (In Rs.)
A	150	1.52	228
A	60	3.5	210
<b>A Total</b>	210		438
B	155	2.56	396.8
B	200	3.94	788
B	25	4	100
<b>B Total</b>	380		1284.8
C	95	3.7	351.5
C	90	4.94	444.6
<b>C Total</b>	185		796.1
D	120	4	480
<b>D Total</b>	120		480
E	95	4.49	426.55
E	115	4.9	563.5
<b>E Total</b>	210		990.05
F	70	4.5	315
F	220	4.95	1089
<b>F Total</b>	290		1404
G	50	4.75	237.5
G	200	5	1000
<b>G Total</b>	250		1237.5
H	120	5	600
<b>H Total</b>	120		600
I	120	5	600
I	109	5	545
<b>I Total</b>	229		1145

## PD Wise eligible commission on MCU, Total commission payable and Total Allotment

						(in Rs.)	(in Rs. cr)
		[1]	[2]	[3]	[4]	[5]	MUC + [1]
Sno	Successful PDs	Total Allotment in ACU Auction to PD (Rs. Cr)	PD Wise Commission on ACU (in Rs.)	Winner PD# if [1] ≥ 4% of NA	Commission payable on MUC (in Rs.)	Total Comm. On MUC & ACU [2] + [4]	Total Allotment in MUC & ACU
1	A Total	210	438.00	YES	495638.47	496076.47	328
2	B Total	380	1284.80	YES	495638.47	496923.27	498
3	C Total	185	796.10	YES	495638.47	496434.57	303
4	D Total	120	480.00	NO	269880.55	270360.55	238
5	E Total	210	990.05	YES	495638.47	496628.52	328
6	F Total	290	1404.00	YES	495638.47	497042.47	408
7	G Total	250	1237.50	YES	495638.47	496875.97	368
8	H Total	120	600.00	NO	269880.55	270480.55	238
9	I Total	229	1145.00	YES	495638.47	496783.47	347
					Total	4017605.804	
	Total	1994				Total allotment to successful PDs	3056

	PDs below cut-off	Total Allotment in ACU Auction to PD (Rs. Cr)	PD Wise Total Commission on ACU (in Rs.)	Commission payable on MUC (in Rs.)	Total Comm.	Total Allotment (in Rs. cr)
1	J	0	0	269880.55	269880.55	118
2	K	0	0	269880.55	269880.55	118
3	L	0	0	269880.55	269880.55	118
4	M	0	0	269880.55	269880.55	118
5	N	0	0	269880.55	269880.55	118
6	O	0	0	269880.55	269880.55	118
7	P	0	0	269880.55	269880.55	118
8	Q	0	0	269880.55	269880.55	118
Total allotment to PDs below cut-off						944
<b>Total coverage of Notified amount (in Rs. crore)</b>						4000
(coverage %age)						1
<b>Total commission payable (before rounding)</b>					6176650.19	

**Illustrations showing adherence by PDs to Commitments on aggregative bidding in auction of Treasury Bills and success ratio**

1. A PD has committed to bid aggregatively Rs. 500 crore GOI Treasury Bills as shown below. The success ratio to be maintained by the PD is 40 per cent in respect of Treasury Bills. Various scenarios in respect of fulfillment of the bidding commitment and the success ratio assuming that the bids tendered and the bids accepted will be as under:

**(1) Treasury Bills:**

**(Rs. crore)**

SCENARIOS	(I)	(II)	(III)
Bidding Commitment (a)	<b>500</b>	<b>500</b>	<b>500</b>
Bids Tendered (b)	600	500	400
Bids Accepted (c)	<b>300</b>	<b>200</b>	<b>100</b>
Success Ratio Achieved (c)/(a)	60%	40%	20%
Fulfilment of Bidding Commitment	Yes	Yes	No
Fulfilment of Success Ratio	Yes	Yes	No
Success ratio in Treasury Bills is the ratio of bids accepted and bidding commitment.			

## When Issued Market - Guidelines

### **Definition**

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

### **Mechanics of Operation**

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

- i. WI transactions will be undertaken only in the case of securities that are being reissued. WI trading for issue of new securities will be considered at a later date.
- ii. WI transactions would commence on the notification date and it would cease on the working day immediately preceding the date of issue.
- iii. All WI transactions for all trade dates will be contracted for settlement on the date of issue.
- iv. At the time of settlement on the date of issue, trades in the WI security can be netted off with trades in the existing security.
- v. ‘WI’ transactions may be undertaken only on **NDS-OM**.
- vi. Any WI trade must have a Primary Dealer (PD) as a counterparty (both counterparties can be PDs). In other words, non-PDs cannot be both buyer and seller in a WI transaction.
- vii. Only PDs can take a short position in the WI market. Non-PD entities can sell the WI security only if they have a preceding purchase contract for equivalent or higher amount.
- viii. Open Positions in the WI market are subjected to the following limits:
  - a. Non-PD entities – Long Position, not exceeding 5 per cent of the notified amount.
  - b. PDs – Long or Short Position, not exceeding 10 per cent of the notified amount.
- ix. In case a PD is unable to deliver securities to the buyer after the auction on the settlement (or issue) date, the transaction will be settled as per the **default settlement mechanism of CCIL**.
- x. In the event of cancellation of the auction for whatever reason, all WI trades will be deemed null and void *ab initio* on grounds of *force majeure*.

**Internal Control**

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

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

**Reporting**

Primary Dealers will report on a daily basis all 'When Issued' transactions, undertaken by them in the format given below.

**Statement of When Issued Operations**

**Date of Transaction:**

**A. Transactions**

<b>Time of Transaction</b>	<b>Purchase</b>	<b>Sales</b>	<b>Net Position of PD</b>
Opening position			
Closing Position			

**B. Position**

<b>Opening Position</b>	<b>Purchases</b>	<b>Sales</b>	<b>Closing Position</b>
WI Security			
Existing Security			
Total			

**The Gazette of India  
EXTRAORDINARY  
Part II – Section 3 – Sub-section (ii)  
Published by Authority  
RESERVE BANK OF INDIA**

**NOTIFICATION**

Mumbai, the 17<sup>th</sup> April 2006

S.O.551(E): - In exercise of the powers conferred on the Reserve Bank of India under section 16 of the Securities Contracts ( Regulation) Act, 1956 (42 of 1956) vide Government of India Notification No. 183(E) dated 1<sup>st</sup> March, 2000, issued under Section 29A of the Act ibid, the Reserve Bank of India –

being of the opinion that it is necessary to prevent undesirable speculation in securities in the whole of India, hereby declares that no person in the territory to which the Act extends, shall, enter into any

(1) contract for the sale or purchase of Government securities, gold related securities and money market securities other than spot delivery contracts or such other contracts traded on a recognised stock exchange, as is permissible under the said Act, rules and bye-laws of such stock exchange.

Provided that contracts may be entered into on 'when issued basis' in such Government securities and in accordance with such terms and conditions, including the basis on which such contracts may be settled, as may be specified in this regard by the Reserve Bank of India by the following persons or entities

- (a) a scheduled commercial bank
- (b) a Primary Dealer registered with the Reserve Bank of India
- (c) any other person or entity specifically permitted in this regard by Reserve Bank of India,

(2) ready forward contracts in bonds, debentures, debenture stock, securitised debt, and other debt securities issued by any person or any body corporate established by or under a Central or State Act.

Provided that ready forward contracts may be entered into in all Government securities, in accordance with the terms and conditions as may be specified by the Reserve Bank of India, by the following persons/entities

(a) any person or entity holding a Subsidiary General Ledger account with the Public Debt Office of the Reserve Bank of India

(b) a scheduled bank or a non-banking financial company registered with Reserve Bank of India (other than Government Companies as defined in Section 617 of the Companies Act, 1956) or a housing finance company registered with National Housing Bank, or a mutual fund registered with Securities and Exchange Board of India, or an insurance company registered with Insurance Regulatory and Development Authority, holding a Gilt account with any person or entity permitted by Reserve Bank of India to maintain Constituent Subsidiary General Ledger account with Public Debt Office of the Reserve Bank of India or

(c) any other person specifically permitted by Reserve Bank of India, holding a Gilt account with any person or entity permitted by Reserve Bank of India to maintain Constituent Subsidiary General Ledger account with Public Debt Office of the Reserve Bank of India:

Provided further that no ready forward contracts may be entered into between two persons or entities both maintaining Gilt accounts with same person or entity maintaining Constituent Subsidiary General Ledger account with the Public Debt Office of the Reserve Bank of India.

Provided further that no ready forward contracts may be entered into between a person or entity maintaining Subsidiary General Ledger account with Public Debt Office of the Reserve Bank of India with another person or entity maintaining a Gilt account with itself.

Provided further that all ready forward contracts shall be settled through Subsidiary General Ledger account or a Constituent Subsidiary General Ledger account maintained with the Public Debt Office of Reserve Bank of India, in accordance with the terms and conditions as may be specified by the Reserve Bank of India

Provided further that the outstanding ready forward contracts shall continue till termination of the contracts as per the contractual terms:

Provided further that such contracts entered into on the recognized stock exchanges shall be entered in accordance with-

(i) the rules or regulations or the bye-laws made under the Securities Contracts (Regulation) Act 1956, (42 of 1956) or the Securities and Exchange Board of India Act 1992 (15 of 1992) or the directions issued by the Securities and Exchange Board of India under the said Acts;

(ii) the rules made or guidelines or directions issued under the Reserve Bank of India Act, 1934 (2 of 1934) or the Banking Regulation Act, 1949 (10 of 1949) or the Foreign Exchange Management Act, 1999 by the Reserve Bank of India.

(iii) The provisions contained in the notifications issued by the Reserve Bank of India under the Securities Contracts ( Regulation) Act 1956 (42 of 1956)

### Explanation

For the purpose of this notification

- I. "scheduled bank" means a bank included in the second schedule of Reserve Bank of India Act, 1934.
- II. "non-banking financial company" means a company as defined in clause (1) of Section 45-I of the Reserve Bank of India Act, 1934.
- III. "mutual fund" means a fund as defined in clause (q) of the Regulation 2 of the Securities and Exchange Board of India (Mutual Funds) Regulations, 1996.
- IV. "Constituent Subsidiary General Ledger account" means a Subsidiary General Ledger account opened and maintained with the Public Debt Office of the Reserve Bank of India, by a bank or any other person permitted by the Reserve Bank of India, for the purpose of holding Government securities on behalf of its constituents.
- V. "Gilt account" means a securities account opened and maintained by any person with a bank of or any other person permitted by the Reserve Bank of India to open and maintain Constituent Subsidiary General Ledger account with the Public Debt Office of the Reserve Bank of India.
- VI. Entering into contracts on 'when issued' basis means entering into contracts after the notification of issue of any Government security but before the actual issue thereof.

This notification is issued by Reserve Bank of India, in supersession of the notification no. S.O.131 (E) dated 22<sup>nd</sup> January 2003 issued by it.

**(V. K. Sharma)**  
Executive Director  
Reserve Bank of India

No. IDMD/1 /10.02.02/2005-06

**Publication of Financial Results****Name of Primary Dealer**

Audited Financial Results for the year ended 31<sup>st</sup> March .....

**Sources of Funds**

- Capital
- Reserves and Surplus
- Loans
  - Secured
  - Unsecured
  - (of which call money borrowings)

**Application of Funds**

- Fixed Assets
- Investments
  - Government Securities (inclusive of T. Bills)
  - Commercial Papers
  - Corporate Bonds
- Loans and Advances
  - (of which call money lendings)
- Non Current Assets
- Others

**Profits and Loss account**

- Income (business segment wise)
  - Interest
  - Discount
  - Trading Profit
- Expenses
  - Interest
  - Administrative Costs
- Profit before tax
- Net Profit

**Regulatory Capital required** (as per Capital Adequacy Guidelines)

**Actual Capital**

**Return on Net Worth**

## List of circulars consolidated

No	Circular no	Date	Subject
1	IDMC.PDRS.1532. /03.64.00/1999-00	November 2, 1999	Primary Dealers – Leverage
2	IDMC.PDRS.2049A /03.64.00/1999- 2000	December 31, 1999	Guidelines on Securities transactions to be followed by Primary Dealers
3	IDMC.PDRS.5122. /03.64.00/1999-00	June 14, 2000	Guidelines on Securities Transactions by Primary dealers
4	IDMC.PDRS.PDS1. /03.64.00/2000-01	October 6, 2000	Sale of securities allotted in Primary issues on the same day
5	IDMC.PDRS.4135 /03.64.00/2000-01	April 19, 2001	Scheme for Bidding, Underwriting and Liquidity support to Primary Dealers
6	IDMC.PDRS.87. /03.64.00/2001-02	July 5, 2001	Liquidity support to Primary Dealers
7	IDMC.PDRS.1382. /03.64.00/2000-01	September 18, 2001	Dematerialised holding of bonds and debentures
8	IDMC.PDRS.3369. /03.64.00/2001-02	January 17, 2002	Guidelines on Counter party limits and Inter-corporate deposits
9	IDMC.PDRS.4881 /03.64.00/2001-02	May 8, 2002	Guidelines to Primary Dealers
10	IDMC.PDRS.5018. /03.64.00/2001-02	May 17, 2002	Scheme for Bidding, Underwriting and liquidity support to Primary dealers 2001-02
11	IDMC.PDRS.5039. /03.64.00/2001-02	May 20, 2002	Transactions in Government securities
12	IDMC.PDRS.5323. /03.64.00/2001-02	June 10, 2002	Transactions in Government securities
13	IDMC.PDRS.418. /03.64.00/2002-03	July 26, 2002	Publication of Financial results
14	IDMC.PDRS.1724. /03.64.00/2002-03	October 23, 2002	Underwriting of Government dated securities by Primary Dealers
15	IDMC.PDRS.2269. /03.64.00/2002-03	November 28, 2002	Publication of Financial results
16	IDMC.PDRS.2896. /03.64.00/2002-03	January 14, 2003	Trading in Government securities on Stock Exchanges
17	IDMC.PDRS.3432. /03.64.00/2002-03	February 21, 2003	Ready Forward Contracts
18	IDMC.PDRS.3820. /03.64.00/2002-03	March 24, 2003	Availment of FCNR(B) loans by Primary Dealers
19	IDMC.PDRS.1. /03.64.00/2002-03	April 10, 2003	Portfolio Management Services by Primary Dealers – Guidelines
20	IDMC.PDRS.4802. /03.64.00/2002-03	June 3, 2003	Guidelines on Exchange Traded Interest Rate Derivatives

21	IDMC.PDRS.4802 . /03.64.00/2002-03	June 11, 2003	Guidelines on Exchange Traded Interest Rate Derivatives
22	IDMC.PDRS.122. /03.64.00/2002-03	September 22, 2003	Rationalisation of returns submitted by Primary Dealers
23	IDMD. PDRS.No.3/ /03.64.00/2003-04	March 08,2004	Prudential guidelines on investment in non-Government securities
24	IDMD.PDRS.05/ 10.02.01/2003-04	March 29,2004	Transactions in Government Securities
25	IDMD.PDRS. No06/ 03.64.00/2003-04	June 03,2004	Declaration of dividend by Primary Dealers
26	RBI /2004-05/ 66 – IDMD.PDRS. 01 10.02.01/2004-05	July 23, 2004	Transactions in Government securities
27	RBI /2004-05/67 - IDMD.PDRS. 02 /03.64.00/2004-05	July 23,2004	Success Ratio in Treasury Bill auctions for Primary Dealers
28	RBI/2004-05/ 136 – IDMD.PDRS.No/ 03 /10.02.16/2004-05	August 24,2004	Dematerialization of Primary Dealer's investment in equity
29	RBI/2004/218 IDMD.PDRS.No/ 06/ 03.64.00/2004- 05	October 15, 2004	Capital Adequacy Standards – Guidelines on Issue of Subordinated Debt Instruments – Tier II and Tier III Capital
30	RBI/2005/459/IDM D.PDRS/4783/10.0 2.01/2004-05	May 11, 2005	Government Securities Transactions – T+1 settlement
31	RBI/2005/460/IDM D.PDRS/4779/10.0 2.01/2004-05	May 11, 2005	Ready Forward Contracts
32	RBI/2005/461/IDM D.PDRS/4779/10.0 2.01/2004-05	May 11, 2005	Sale of securities allotted in Primary issues
33	RBI/2005/474/IDM D.PDRS/4907/03.6 4.00/2004-05	May 19, 2005	Conduct of Dated Government Securities Auction under Primary Market Operations (PMO) module of PDO-NDS – Payment of Underwriting Commission
34	RBI/2005-06/ 73 IDMD.PDRS. 337 /10.02.01/2005-06	July 20, 2005	Transactions in Government Securities
35	RBI/2005-06/132 IDMD.No. 766/10.26.65A/200 5-06	August 22, 2005	NDS-OM – Counterparty Confirmation
36	RBI/2005-06/308 DBOD.FSD.BC.No. 64/24.92.001/2005-	February 27, 2006	Guidelines for banks' undertaking PD business

	06		
37	RBI /2005-06/309 IDMD.No 03/11.01.01(B)/2005-06	February 28, 2006	Secondary Market Transactions in Government Securities - Intra-day short-selling
38	RBI/2005-06/347 IDMD.PDRS.No.30 07/03.64.00/2005-06	April 4, 2006	Revised Scheme of Underwriting Commitment and Liquidity Support
39	RBI /2005-06/382 IDMD.No/3426 /11.01.01 (D)/2005-06	May 3, 2006	'When Issued' transactions in Central Government Securities
40	RBI/2006-07/49 IDMD.PDRS/26/03. 64.00/2006-07	July 4, 2006	Diversification of activities by stand-alone Primary Dealers-Operational Guidelines