

## A P P E N D I X - I X

(See para 4.6 of the Report)

### RBI Circular dated 26.7.1991 regarding transaction in Securities

DEPUTY GOVERNOR

RESERVE BANK OF INDIA  
CENTRAL OFFICE  
BOMBAY

D.O. DBOD NO. FSC. 46/C 469-91/92

26 July, 1991  
4 Sravana, 1913 (Saka)

SECRET

Dear Shri,

#### Investment Portfolio of banks — Transactions in Securities

It is a matter of great concern for us that certain banks are engaged in types of transactions in securities which they should not be undertaking. A list of such transactions is appended:

- (i) Ready forward (buy-back) deals at rates which have no relevance to the market rates, *inter-alia*, with a view to window-dressing their balance sheet/compliance of SLR requirements.
- (ii) Double ready forward deals with a view to covering their oversold position in a specific security.
- (iii) Sale transactions by issue of Bank Receipts (BRs)/SGL forms without actually holding the securities/without having sufficient balance in their SGL accounts.
- (iv) Issuing BRs/SGL forms on behalf of their broker clients without safeguarding banks' interest.

2. You may do away that with a view to helping the banks to overcome various deficiencies in the long-term securities market and to enable them to manage their short-term cash deficit/surpluses more efficiently, we have permitted banks to enter into buy-back deals in Government Securities among themselves (and not with their non-bank clients). It was our expectation that such deals will be undertaken by the selling bank, only if it holds sufficient securities (either in the Physical form or in SGL account), at market related rates and such deals will be properly reflected in their books of account. However, we observe that certain banks have been resorting to this type of transactions, without actually holding sufficient Securities either in physical form or in their SGL account (resulting in substitution of BRs/return of SGL forms for want of sufficient balance), at rates which have no relevance to market, with a view to window-dressing their profitability/maintenance of SLR requirement with the tacit understanding with the counter party banks. Some of the banks appear to be taking outright oversold position in securities and in their desperate bid to cover the oversold position in a particular security/ies enter into double ready forward deals and other banks oblige them in the matter.

3. Another disquieting feature observed is the extensive use of BRs by banks. It has been our intention to ensure that the banks do not undertake sale transactions in securities without actually holding them and do not issue BRs unless they are in a position to deliver the

securities within a reasonable time. Contrary to our above expectation, banks have been issuing BRs freely (without regard to whether they will be in a position to deliver the securities there against within a reasonable time) and against an initial outstanding BRs a series of transactions are put through by further issue of BRs and in the final analysis only the BRs are exchanged and no security is delivered. Some of the banks have also been issuing BRs on behalf of their broker clients, without verifying whether their broker clients hold the securities covered by the relative BRs.

4. It will be absolutely essential for your bank to frame and implement a suitable investment policy to ensure that operations in securities are conducted in accordance with sound and acceptable business practices. While evolving the policy you are requested to keep in view the following guidelines:

- (i) Under no circumstances, the bank should hold a oversold position in any security, that is to say that no sale transactions should be put through without acutally holding the security in its Investment account.
- (ii) All the transactions put through by bank either on outright basis or ready forward basis and whether through the mechanism of SGL Account or Bank Receipt should be reflected on the same day in its Investment Account and accordingly for SLR purpose, wherever applicable.
- (iii) Transactions between your bank and another bank should not be put through the brokers' accounts. The brokerage on the deal payable to the broker, if any, (if the deal is put through with the help of a broker) should be clearly indicated on the notes/memorandum put up to the top management seeking approval for putting through the transaction and amount of brokerage paid, broker-wise, should be maintained.
- (iv) For issue of BRs, the banks should adopt the format prescribed by the IBA and should strictly follow the guidelines prescribed by them in this regard subject to above, the banks should issue BRs covering their own sale transactions only and should not issue BRs on behalf of their constituents including brokers.
- (v) The banks should be circumspect while acting as agents of their broker clients for carrying out transactions in securities on behalf of brokers.
- (vi) 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 our notice with the details of the transactions.

5. We shall also be glad if a copy of the policy framework for undertaking transactions in securities approved by your bank's board, is forwarded to us.

6. Please acknowledge receipt.

Yours sincerely,

(A. Ghosh)