CAB Training Cards

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A ten-point guide for UCBs for investments in Certificate of Deposits

UCBs earlier were keeping term deposits with public sector banks mainly as part of their SLR maintenance, liquidity management and also for earning income. Even after withdrawal of eligibility of these deposits from being reckoned for SLR with effect from April 01, 2015, UCBs continue to place their excess funds in term deposits with the public sector banks, private banks and more recently with small finance banks for their liquidity management and also to earn income. There are basically two challenges with these term deposits i.e. (a) these deposits cannot be sold in the market and (b) its pre-mature withdrawal could lead to loss of interest. As alternative to the term deposits, an option available to UCBs is Certificate of Deposits (CDs). The following key points in respect of CDs may be helpful for UCBs in taking decision regarding investments in them: -

(i) CDs are negotiable money market instruments and are issued in dematerialized form or as a Usance Promissory Note against funds deposited at a bank or other eligible financial institutions. CDs in physical form are freely transferable by endorsement and delivery. CDs in demat form can be transferred as per the procedure applicable to other demat securities. There is no lock-in period for the CDs.

(ii) CDs can be issued by (i) scheduled commercial banks {excluding Regional Rural Banks and Local Area Banks} based on their funding requirements; and (ii) select All-India Financial Institutions (FIs) that have been permitted by RBI to raise short-term resources within the umbrella limit fixed by RBI.

(iii) Investment in CDs by UCBs are subject to the applicable gross inter-bank and single bank exposure ceilings of 10% and 5% respectively of their deposits as on March 31st of the previous year.

(iv) UCBs can invest a minimum amount of ₹1 lakh and in multiples of ₹1 lakh thereafter in a CD issued by a permitted entity.

(v) The maturity period of CDs issued by banks cannot be less than seven days and not more than one year, from the date of issue. However, FIs can issue CDs for a period not less than one year and not exceeding three years from the date of issue.

(vi) CDs are being issued at a discount on face value. The issuing bank / FI is free to determine the discount / coupon rate. CDs may also be issued on floating rate basis and the interest rate on these floating rate CDs are reset periodically.

(vii) All OTC trades in CDs have to be reported within 15 minutes of the trade to the Financial Market Trade Reporting and Confirmation Platform (“F-TRAC”) of Clearcorp Dealing System (India) Ltd. (CDSL).

(viii) All OTC trades in CDs have to necessarily be cleared and settled under DVP-I mechanism through the authorised clearing houses {National Securities Clearing Corporation Limited (NSCCL), Indian Clearing Corporation Limited (ICCL) and MCX Stock Exchange Clearing Corporation Limited (CCL)} of the stock exchanges.

(ix) The investments in CDs are subject to market rate fluctuation. Investments in CDs are classified under the non-SLR investments.

UCBs also have to consider that, unlike loan against term deposits, here banks /FIs are not permitted to grant loan against their own CDs. Furthermore, they cannot buy-back their own CDs before maturity. However, the RBI may relax these restrictions for temporary periods through a separate notification.

(x) The investments in CDs issued in physical form are signed by two or more authorised signatories but are freely transferable by endorsement and delivery, therefore possibility of tampering with the document could not be ruled off. Further, physical certificates have to be presented for payment by the last holder. In case of loss of physical certificates, duplicate certificates can be issued only after complying with few laid down requirements. Therefore, it may be better if UCBs invest only in CDs issued in demat form.

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