

Reserve Bank of India (Amendment) Act, 2006

February 15, 2013

RESERVE BANK OF INDIA (AMENDMENT) ACT, 2006 ¹

[No. 26 OF 2006]

[June 12, 2006]

An Act further to amend the Reserve Bank of India Act, 1934

Be it enacted by Parliament in the Fifty-seventh Year of the Republic of India as follows:-

Prefatory Note-Statement of Objects and Reasons. – Financial sector reforms are marking steady progress in India. The Indian financial markets now have more products, participants and better liquidity than before. For more operational flexibility, the Reserve Bank of India needs to have enabling powers to use a larger variety of financial instruments than hitherto.

2. The volatility in the influx of foreign exchange and the market conditions in a fast changing economy can be expected to continue in future as the financial sector makes more and more progress. To cope with any unforeseen eventualities in future, such as excess or lack of liquidity in the banking system and for effective conduct of monetary policy, there is a need to enable Reserve Bank of India to determine the Cash Reserve Ratio (CRR) for scheduled banks without any floor or ceiling. Globally, many Central Banking authorities have such powers. Further, in the context of the conduct of monetary policy becoming more market-based through progressive use of indirect instruments, the Reserve Bank of India needs more flexibility to set Cash Reserve Ratio, which is one of the two statutory pre-emptions in respect of the resources of banks.

3. Over-the-counter derivatives play a crucial role in reallocating and mitigating the risks of corporates, banks and other financial institutions. The ambiguity regarding their legal validity has inhibited the growth and stability of the market for such derivatives. It has become essential to provide for clear legal validity of such contracts.

4. At present, under Section 29-A of the Securities Contracts (Regulation) Act, 1956, the Central Government has delegated to the Reserve Bank of India, by a notification, the powers exercisable by it under Section 16 of that Act, for regulating the transactions in money market and other instruments. Therefore, more effective regulation of the markets for interest rate contracts, including Government securities and money- market instruments as also derivatives, it is necessary to confer specific powers on the Reserve Bank of India, under the Reserve Bank of India Act, 1934, to lay down policy and to issue directions to agencies operating in these contracts, securities and derivatives.

5. It is, therefore, considered necessary to suitably amend the Reserve Bank of India Act, 1934. The salient features of the Bill which seeks to amend the RBI Act are as follows:-

(a) define the expressions, 'derivative', 'repo' and 'reverse repo' in Section 17 for the purposes of the business of the Bank and differently in new Chapter III-D for the purposes of regulatory powers of the Bank;

(b) empower the Reserve Bank of India to deal in derivatives, to lend or borrow securities and to undertake repo or reverse repo;

(c) remove the lower floor and upper ceiling of Cash Reserve Ratio (CRR) and to provide flexibility to RBI to specify CRR;



(d) remove ambiguity regarding the legal validity of derivatives;

(e) empower RBI to lay down policy and issue directions to any agency dealing in various kinds of contracts in respect of Government securities, money-market instruments, derivatives, etc., and to inspect such agencies.

6. The Bill seeks to achieve the above objects.

1. Received the assent of the President on June 12, 2006 and published in the Gazette of India, Extra., Part II, Section 1

1. Short title and commencement.

(1) This Act may be called the Reserve Bank of India (Amendment) Act, 2006.

(2) It shall come into force on such date as the Central Government may, by notification in the Official Gazette, appoint; and different dates may be appointed by different provisions of this Act.

2. Amendment of Section 17.

In Section 17 of the Reserve Bank of India Act, 1934 3f 1934) (hereinafter referred to as the principal Act),-

(i) after clause (6), the following shall be inserted, namely:

“(6-A) dealing in derivatives, and, with the approval of the Central Board, in any other financial instrument.

Explanation.-For the purposes of this clause, “derivative” means an instrument, to be settled at a future date, whose value is derived from change in one or a combination of more than one of the following underlying, namely:-

(a) interest rate,

(b) price of securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government,

(c) price of foreign securities,

(d) foreign exchange rate, index of rates of prices,

(e) credit rating or credit index,

(g) price of gold or silver coins, or gold or silver bullion, or

(h) any other variable of similar nature;

(ii) after clause (12-A), the following shall be inserted, namely:-



'(12-AA) lending or borrowing of securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities;

(12-AB) dealing in repo or reverse repo:

Provided that lending or borrowing of funds by way of repo or reverse repo shall not be subject to any limitation contained in this section.

Explanation.- For the purposes of this clause,-

(a) "repo" means an instrument for borrowing funds by selling securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to repurchase the said securities on a mutually agreed future date at an agreed price which includes interest for the funds borrowed;

(b) "reverse repo" means an instrument for lending funds by purchasing securities of the Central Government or a State Government or of such securities of a local authority as may be specified in this behalf by the Central Government or foreign securities, with an agreement to resell the said securities on a mutually agreed future date at an agreed price which includes interest for the funds lent;'

3. Amendment of Section 42.

In Section 42 of the principal Act, -

(i) in sub-section (1),-

(a) for the words, brackets and figure "three per cent of the total of the demand and time liabilities in India of such bank as shown in the return referred to in sub-section (2)", the words, brackets and figure "such per cent of the total of the demand and time liabilities in India of such bank as shown in the return referred to in sub-section (2), as the Bank may from time to time, having regard to the needs of securing the monetary stability in the country, notify in the Gazette of India" shall be substituted;

(b) the proviso shall be omitted;

(ii) sub-sections (1-AA) and (1-B) shall be omitted.

4. Insertion of new Chapter III-D.

After Chapter III-C of the principal Act, the following Chapter shall be inserted, namely:-

'Chapter III-D

REGULATION OF TRANSACTIONS IN DERIVATIVES, MONEY MARKET INSTRUMENTS, SECURITIES, ETC.

45-U. Definitions.- For the purpose of this Chapter,-

(a) "derivative" means an instrument, to be settled at a future date, whose value is derived from change in interest rate, foreign exchange rate, credit rating or credit index, price of



securities (also called "underlying"), or a combination of more than one of them and includes interest rate swaps, forward rate arrangements, foreign currency swaps, foreign currency-rupee swaps, foreign currency options, foreign currency-rupee options or such other instruments as may be specified by the Bank from time to time;

(b) "money market instruments" include call or notice money, term money, repo, reverse repo, certificate of deposit, commercial usance bill, commercial paper and such other debt instrument of original or initial maturity up to one year as the Bank may specify from time to time;

(c) "repo" means an agreement for borrowing funds by selling securities with an agreement to repurchase the securities on a mutually agreed future date at an agreed price which includes interest for the funds borrowed;

(d) "reverse repo" means an instrument for lending funds by purchasing securities with an agreement to resell the securities on a mutually agreed future date at an agreed price which includes interest for the funds lent;

(e) "securities" means securities of the Central Government or a State Government or such securities of a local authority as may be specified in this behalf by the Central Government and, for the purposes of repo" or "reverse repo", includes corporate bonds and debentures.

45-V. Transactions in derivatives.

(1) Notwithstanding anything contained in the Securities Contracts (Regulation) Act, 1956 (42 of 1956) or any other law for the time being in force, transactions in such derivatives, as may be specified by the Bank from time to time, shall be valid, if at least one of the parties to the transactions is the Bank, a scheduled bank, or such other agency falling under the regulatory purview of the Bank under the Act, the Banking Regulation Act, 1949 (10 of 1949), the Foreign Exchange Management Act, 1999 (42 of 1999), or any other Act or instrument having the force of law, as may be specified by the Bank from time to time.

(2) Transactions in such derivatives, as had been specified by the Bank from time to time, shall be deemed always to have been valid, as if the provisions of subsection (1) were in force at all material times.

45-W. Power to regulate transactions in derivatives, money market instruments, etc

45-X. Duty to comply with directions and furnish information.-It shall be the duty of every director or member or other body for the time being vested with the management of the affairs of the agencies referred to in Section 45-W to comply with the directions given by the Bank and to submit the information or statement or particulars called for under that section.'



