

Directions issued to Primary Dealers

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2	2. Direction on Financial Statements	10-Jan-02
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Attention:

Reference No: 08/24/002/005/01

**Direction on Segregation of Proprietary Government
Securities Accounts**

This direction is issued under Section 10(2) of the Regulations made by the President, dated March 01, 2000 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from 1st January, 2002.

K G D D Dheerasinghe
Superintendent of Public Debt

Colombo
Date: 10.1.2002.

1. With effect from 1st January 2002, Primary Dealers are required to classify their proprietary government securities portfolio under two categories: Investment Account and Trading Account.
2. The criteria for classifying government securities into such categories are given below:

Trading Account

- (a) Government securities acquired for the specific purpose of trading on a regular basis to profit from short-term changes in market prices and yields shall be held in the Trading Account.
- (b) Government securities held in the Trading Account must be revalued or “Marked to Market” on a weekly basis using the weekly report on Weighted Average Market Prices compiled by the Central Bank.
- (c) Any gains or losses on securities held in the Trading Account must be taken to earnings.

Investment Account

- (a) Government securities acquired with the positive intent and ability to hold to maturity shall be held in the Investment Account. The Primary Dealer should intend to earn a regular interest yield from these securities. Securities classified into the Investment Account shall be documented and authorized by the Chief Executive Officer of the Primary Dealer and this statement must be submitted to the Public Debt Department of the Central Bank of Sri Lanka with the monthly financial statements.
- (b) Securities in the Investment Account may be used for repurchase transactions.
- (c) Securities in the Investment Account shall be carried and reported at cost over the period of redemption, with the following exceptions;
 - (i) Carrying values of securities in the Investment Account may be adjusted to account for the accretion of discount (or depletion of premium). The adjustments should be amortised on a straight-line basis over the period to maturity.
 - (ii) Carrying values of securities in the Investment Account may be written down to their fair value to account for any diminution in value which is expected to be other than temporary (i.e. if the decline results in a permanent impairment of the value of the security).
 - (iii) The carrying value of securities in the Investment Account used under temporary switching transactions in repurchase and reverse repurchase transactions, may be adjusted after the reversal or “second leg” of the transaction has been concluded to reflect margin calls.
 - (iv) The carrying value of securities transferred from the Trading Account into the Investment Account shall be marked to market prior to the transfer. Therefore, any gains or losses due to revaluation would have been recognised in earnings prior to the transfer. The market value of the securities at the point of transfer into the Investment Account then becomes the ‘historical cost’ for accounting purposes.

Reclassification of Securities

- (a) Transfer of securities between the Trading Account and the Investment Account must be justifiable, documented and authorized. A statement on portfolio transfers, if any, shall be signed by the Chief Executive Officer of the Primary Dealer and submitted to the Public Debt Department together with the monthly financial statements.

(b) Portfolio transfers shall only be undertaken rarely. The circumstances justifying portfolio transfers into and out of the Investment Account are given below:

- (i) A change in the statutory and regulatory requirements regarding the type or level of permissible investment securities
- (ii) A significant increase in the capital requirements that obliges the Primary Dealer to reduce its investment holdings
- (iii) A major business occurrence that necessitates the sale of securities to maintain the Primary Dealer's risk profile
- (iv) A significant change in risk weights assigned to government securities for the purpose of computing the capital adequacy ratio.

Market Revaluation of Proprietary Securities Accounts

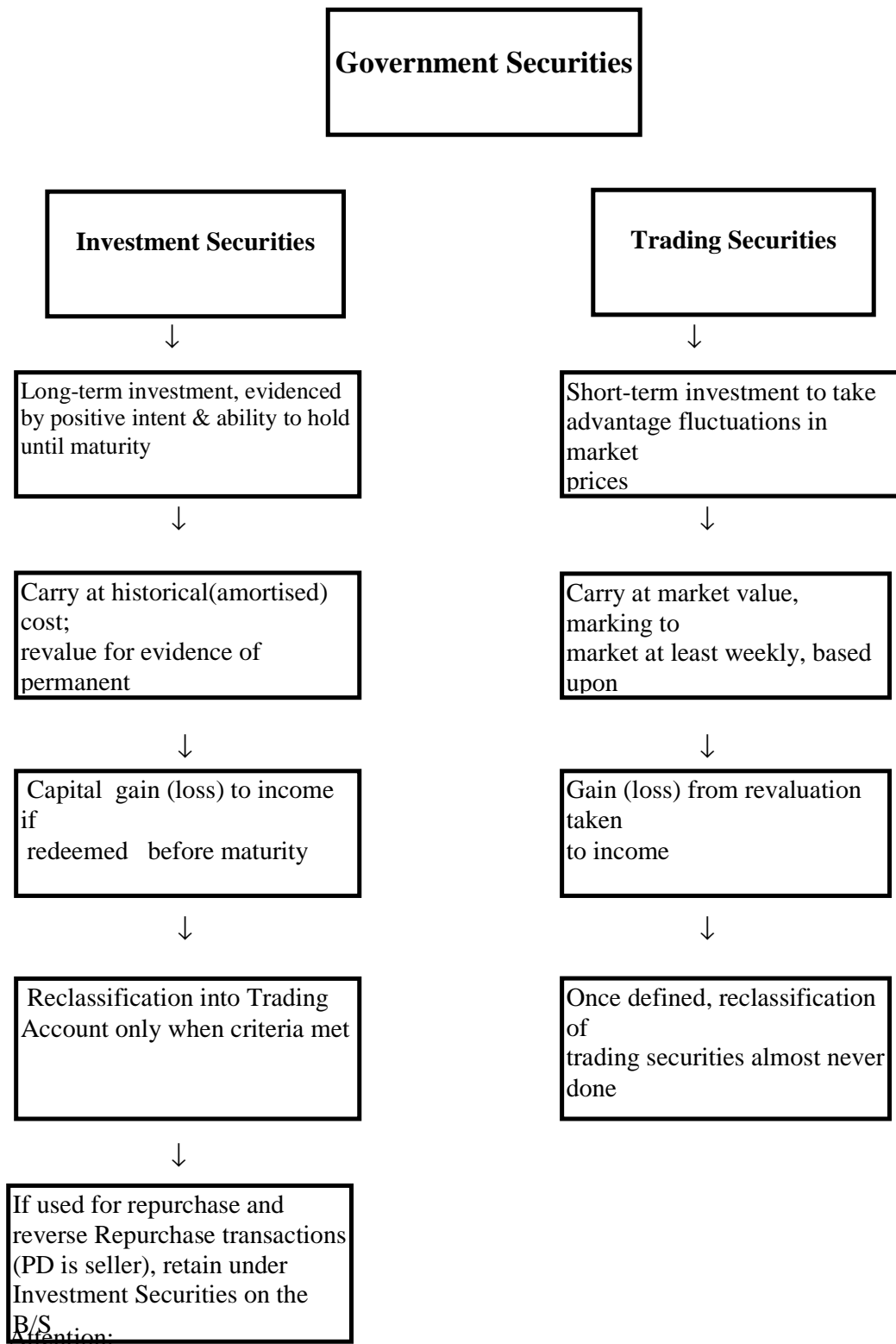
The guidelines on market revaluation and the accounting treatment of the securities accounts are given below.

Table 1

Market Revaluation of Proprietary Securities Accounts

Description	Accounting Treatment
i. Investment Account	Book and maintain at cost Amortise premium or discount over period to redemption Adjust for impairment of value expected to be other than temporary Profit (loss) from sale prior to maturity is charged to capital Gains (losses) on Investment Securities are taken to income
ii. Trading Account	Mark to Market at least weekly using CBSL market rates Profit(loss) from sale prior to maturity is charged to capital Gains (losses) on Investment Securities are taken to income
iii. Securities used in financing transactions (repurchase and reverse repurchase)	Retain securities on the balance sheet The value of securities outstanding (i.e. where the reversal of the repurchase and/or reverse repurchase transaction has not been effected) should be adjusted for margin calls Book interest income/expense, whether explicit or implicit, to the B/S; Interest Income or Interest Expense account
iv. Reclassification of securities from Trading to Investment Account	Book the reclassified security at current market rate That current market rate becomes the 'historical cost' of the security
v. Reclassification of securities from Investment to Trading Account	Take profit (loss) from reclassification to income as the transfer 'in substance' (i.e. the intention) amounts to a sale.

Accounting for Government Securities



Direction on Financial Statements

This direction is issued under Section 10(2) of the Regulations made by the President dated March 01, 2000 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from 1st January, 2002.

K G D D Dheerasinghe
Superintendent of Public Debt

Colombo
Date:10.1.2002.

1. With effect from 1st January 2002, Primary Dealers are required to prepare their annual financial statements, the Balance Sheet and the Profit and Loss Account in accordance with the accounting methodology specified in the Sri Lanka Accounting Standards.
2. In addition, Primary Dealers are required to maintain their proprietary government securities portfolio in one of two separate accounts, the Investment Account and the Trading Account in accordance with the Direction on Segregation of Proprietary Government Securities Accounts.
3. The annual financial statements of the Primary Dealers must be audited by an external auditor registered with the Central Bank of Sri Lanka, in accordance with the Sri Lanka Auditing Standards.
4. Audited annual financial statements of Primary Dealers are required to be submitted to the Public Debt Department of the Central Bank of Sri Lanka, within five (5) months of the end of the financial year to which it relates.
5. Primary Dealers are also required to submit unaudited annual financial statements to the Public Debt Department of the Central Bank of Sri Lanka, within three (3) months of the end of the financial year to which it relates.

6. Primary Dealers are required to publish their Balance Sheet and Profit and Loss Statement for the financial year, in Sri Lankan newspapers preferably in all three languages (Sinhala, Tamil and English) or at least in the English language newspapers within six (6) months of the end of the financial year to which they relate.

7. Primary Dealers are also required to publish their unaudited Balance Sheet and Profit and Loss Statement for each half year, in Sri Lankan newspapers preferably in all three languages (Sinhala, Tamil and English) or at least in the English language newspapers within two (2) months of the end of the half year to which they relate.

08/24/002/005/01

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1

April 9, 2002

[Direction on New Products](#)

The direction is issued under Section 12 of the Regulations made by the President dated February 01, 2002 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from April 12, 2002.

K.G.D.D. Dheerasinghe
Superintendent of Public Debt

Colombo
Date : 12.4.2002

With effect from April 12, 2002, Primary Dealers are required to inform the Public Debt Department of any new product it is intending to launch, prior to its introduction to the market. The details of the structure of the proposed product, price, interest yield, maturity and other relevant information should be submitted for consideration. Any documentation or agreements with customers relating to the proposed product should also be submitted. Primary Dealers are required to obtain the concurrence of the Public Debt Department prior to launching the new product.

This direction is being issued in the interest of consumer protection and to maintain the integrity and safety of the government securities market.

Primary Dealers are required to strictly comply with this direction.

Direction/p2/cn2

Attention:
Reference No: 08/24/002/005/01

Public Debt Department,
No: 30, Janadhipathi Mawatha,
Colombo 01.
March 11, 2002

Attentions: Chief Executive Officers

To: All Primary Dealers

Direction on Secondary Market Quotes (Bid and Offer Prices)

The Primary Dealers are required to be “market makers” in the secondary market for government securities, thereby improving market liquidity. Liquidity is facilitated if there are active market-makers who will undertake to make , on demand and in any trading conditions, continuous and firm (effective) two way prices. The Public should also have easy access to information on the latest bid offer prices of each Primary Dealer.

All Primary Dealers are hereby directed to submit their daily buying and selling quotes for securities with maturity upto 3 years on the screen provided by the Public Debt Department of the Central Bank of Sri Lanka (CBSL). The first quotes for the day should be submitted by at least 10.00 a.m. These quotes will be disseminated to the public via CBSL web page, Public Debt Department web page, other electronic media and published in the newspapers. Primary Dealers are also required to disseminate information on there daily two-way prices to the public through there own information dissemination systems.

This direction is issued under Section 12 of the Regulations made by the Minister of Finance dated February 1, 2002 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from 11th March ,2002.

Dr. H. N. Thenuwara

Superintendent of Public Debt

Reference No: 08/24/002/005/01

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1

April 9, 2002

Direction on the Establishment of a Branch Office by Primary Dealers

The direction is issued under Section 12 of the Regulations made by the President dated February 01, 2002 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from April 12, 2002.

Colombo
Date: 12 .4.2002

K.G.D.D. Dheerasinghe
Superintendent of Public Debt

With effect from April 12, 2002, Primary Dealers are required to inform and obtain the prior concurrence of the Public Debt Department for the establishment of a branch or any other type of office which proposes to engage in trading in government securities and primary dealer business.

The following details relating to the proposed branch should be submitted to the Public Debt Department for consideration.

- (1) Type of Establishment.
- (2) Location and Address.
- (3) Type of Activities.
- (4) Manager and Qualifications.
- (5) Staff Numbers and Duties.
- (6) Organization Structure and Internal Control System.
- (7) Operating Systems.
- (8) Risk Management Systems.
- (9) Proposed date for commencement of business.

Primary Dealers are required to strictly comply with this direction.

Directioin/cn2
Attention:

Direction on Repurchase and Reverse Repurchase Agreements

This direction is issued under Section 12 of the Regulations made by the Minister of Finance dated February 1, 2002 in terms of the Local Treasury Bills Ordinance and the Registered Stocks and Securities Ordinance and will come into effect from 1 June, 2002.

Colombo
Date 2.5.2002

Signed
K.G.D.D.Dheerasinghe

Definition and Structure

A repurchase (repo) is a sale and repurchase agreement. For example, Party A sells securities to Party B with a legally binding agreement to purchase *equivalent* securities from Party B for an agreed price at a specified future date, or at call. Legal ownership to the securities changes giving Party B full (“unfettered”) title to the securities. Party B may use or dispose of them as it pleases, but it has an obligation to deliver equivalent securities to Party A at the end of the repo. Party A’s spot sale and forward purchase (repo) is matched by Party B’s spot purchase and forward sale (“reverse repo”).

The interest rate implied by the difference between the sale price and “repurchase” price is the repo rate. If Party A is selling securities to Party B in order to raise finance for itself, then the repo rate is, in effect, the cost to Party A of raising secured funds. Party B can “lend” money to Party A for a “repo rate” of interest, and receive government securities. This is a “*general collateral, or GC repo*” (see Annex 1) and is normally initiated by the party which wants to borrow money i.e. the cash taker.

Alternatively, Party B may have a short position in a particular government security, which it covers by obtaining (reversing in, thus “reverse repo”) that security from Party A. As Party B is initiating the transaction, A has more negotiating power over the repo rate he will pay on the cash received. The repo rate may therefore be lower (and may even be zero). This allows party A to invest the cash which it receives – perhaps via GC repo – at a higher rate than he is paying B, and earn a net return. This is a “*special repo*”, ie a repo in a specific government security (see Annex 2) and is normally initiated by the cash provider.

Since the secondary market value of securities provided as “collateral” can vary, the cash taker in GC repo may give a margin to protect the cash provider against adverse movements in the market price of the collateral. For instance, if the expected price volatility of the securities used was V% over the period from initial payment of the margin to its next normal. revaluation, then a repo loan of 100 would require “collateral” of 100 plus V%¹. The securities should be revalued every day or at least every week .

Accrued Interest and Pricing of the Securities

The market value of a security will be affected by accrued interest. In the case of coupon bonds - other things being equal – the market value including accrued interest (the “dirty” price³) will increase steadily in between coupon

payment dates, and drop by the amount of the coupon on coupon date. In the case of a zero coupon bond, the market value will tend to rise steadily, other things being equal, up to redemption. Similarly, the exposure of a cash lender in a repo transaction will increase over time as interest accrues on the loan.

In the case of most short-term repo transactions, this means that the secondary market value of the collateral increases broadly in line with the value of the loan plus accrued interest. With longer –term transactions, particularly if the yield curve is significantly sloped (whether positively or negatively) the collateral: loan ratio can change over time. This may require a periodic adjustment in the amount of collateral provided⁴.

If a coupon is payable during the life of a repo, there may be a need for a simultaneous adjustment to the level of collateral, as there will be a step adjustment to the market value of the collateral without a corresponding change to the value of the loan plus accrued interest. In practice, most short-term repo transactions will try to use securities where the coupon payment dates fall outside the period of the repo transaction.

Hold-in-custody (HIC) Repo

In some cases, the cash taker may retain the security – in a segregated account – rather than transferring it. For instance, a large bank might borrow cash by repo, but in order to reduce transactions costs and facilitate substitution (see annex 1), the repo is not registered with the (central bank’s) government securities registry/depository. While the cash provider is the beneficial owner of the securities, it is still registered in the name of the cash taker. The cash provider takes on some credit risk in order to obtain a higher overall return.

Tri-partite Repo

One of the parties in the repo may not have an account in the (dematerialised) settlement system, or may lack the necessary back-office infrastructure to manage the administration of repo. If the cash provider does not wish to assume credit risk on the cash taker by using HIC repo, he could ask a third party – perhaps a custodian bank with good credit rating, or an international clearing organisation – to stand in the middle, effectively acting as an agency broker.

Blocked Repo

Where repo is essentially being used as a form of secured lending, the securities taken as “collateral” may be put into a blocked account. Although the form of repo means that legal ownership passes to the “cash provider”, they cannot be

on-sold or otherwise pledged unless there is an event of default. In this case it is necessary to clarify who has the power to un-block the securities, and in what circumstances. In the event of default, it is important that the cash provider can access the securities quickly (to minimize price risk).

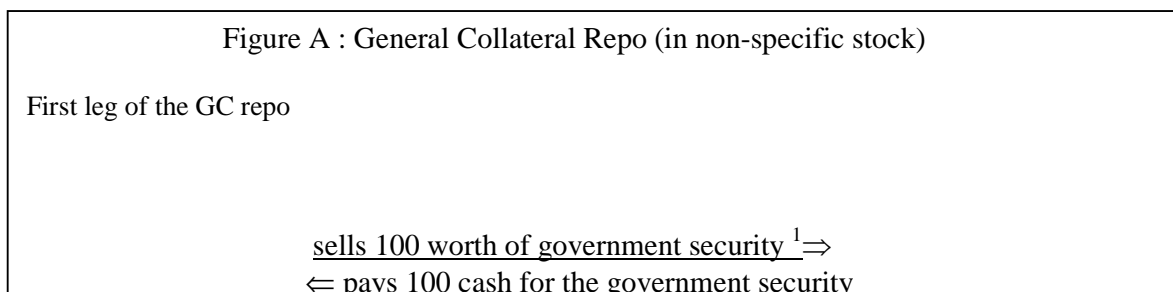
Blocked repo reduces the liquidity of the transaction for the cash provider, as it is not possible in this case to on-sell or repo out the securities received. This will tend to discourage the use of longer-term contracts and may prove a major deterrent to the use of repo. In some countries blocked repo is preferred by the authorities, at least in the initial stages of the market, because it prevents a chain of transactions involving a single security, and where a default could precipitate a chain reaction. (If Bank A does not return securities to Bank B, then Bank B cannot in turn pass them back to Bank C, and so on.)

Blocked repo also prevents the cash provider from taking a short position by selling outright a security which has been repoed in. However, it is not clear that this reduces risk in the market, since any position, whether long or short, entails a measure of risk.

FOOTNOTES

- ¹ Strictly speaking, the collateral would be $100/(1 - V\%)$; but for low values of V the difference is insignificant.
- ² The repo interest is calculated as size of the “loan”*interest rate (here 0.065 as the rate is 6.5%)* period of the repo (e.g. 7/365 for a 7 day repo). $100 * 0.065 * (7/365) = 0.125$
- ³ It is normal market practice to quote securities prices excluding accrued interest (“clean” prices), as this facilitates comparison between different securities and across time; but accrued interest is of course taken into account when calculating the actual payment for any transaction.
- ⁴ Account must also be taken of ex-dividend dates (if these apply) when valuing the collateral.

Annex 1



Party
A

Party B

Party
A

Party
B

Annex 2

Figure B : Special Repo (in a specific government security)

First leg of the special repo

Party
A

sells 100 worth of government security¹ →
← pays 100 cash for the government security

Party B

¹ with a nominal value of X

Party B now has 100 worth of government security (to cover its short position) and Party A has the use of 100 of cash.

Second leg of the special repo :

pays 100 cash plus repo →

Party
A

Party
B

Annex 3

Classic repo vs Sell and Buy-Back

A sell and buy-back is in many respects similar to repo, though more “primitive”. The key similarities and differences, are summarised below :

- **Purchase and Sale** : Both involve purchase and sale, i.e transfer of ownership, rather than the use of the security as collateral (where ownership is only transferred in the event of default).
- **Margin maintenance** : Sale and buy-back typically does not involve margin maintenance. While this simplifies the transaction, because there is no need to provide

additional margin if the secondary market price of the security changes, it can give rise to increased credit risk – see annex 6.

- **Coupon :** With repo, the cash taker retains the right to any coupon payments. If coupon is paid during the life of the repo (to the cash provider as legal owner), it must be immediately passed to the cash taker. Failure to do so would constitute an event of default. In a sell and buy-back, the value of the coupon is factored in to the repurchase price. This gives rise to credit exposure against the cash provider for the period between payment of the coupon and maturity of the repo.
- **Substitution :** In a repo transaction, the security repoed can in principle be substituted for another security of the same value. Assume for instance that a market-maker repos out a security, and then has demand from a client to buy that particular security. The market-maker could conclude the deal with the client, and substitute a different security for the one repoed. The client obtains the specific security he wants, and the repo cash provider still has satisfactory “collateral”. (in practice, the cash provider may charge a few basis points for the inclusion of the substitution clause, since this gives the cash taker rather than the cash provider the chance to benefit if the security goes “special”.) There is no right of substitution in sell and buy-back transactions.
- **Industry-approved contract :** This exists for repo, normally the PSA/ISMA contract, providing greater legal certainty to both participants. There is no standard documentation with sell and buy-back transactions.

CLASSIC REPO vs SELL/BUY-BACK

	<u>Repo</u>	<u>Sell/Buy-Back</u>
Purchase and Sale	X	X
Margin Maintenance	X	X
Coupon passed	X	X
Coupon added to end price Substitution	X	X
Industry-approved contract	X	X

Attention:
08/24/002/0005/001

Public Debt Department
Central Bank of Sri Lanka
No.30, Janadhipathi Mawatha
Colombo 1

July 15, 2002

Chief Executive Officer,

- Ceybank Securities Ltd.
- Commercial Bank Primary Dealer Ltd.
- NSB Fund Management Co. Ltd.
- HNB Securities Ltd.
- First Capital Treasuries Ltd.
- Sampath Surakum Ltd.
- Seylan Bank Asset Management Ltd.
- Ceylinco Shriram Securities Ltd.

Direction on Secondary Market Actual Rates

The Public Debt Department is setting up a system to monitor actual secondary market rates on a real time basis. In this regard, Primary Dealers are required to submit actual buying and selling rates for all maturities of securities transacted during the day, in the

format provided below. As an initial step, it is compulsory to provide actual rates of short term securities traded.

All Primary Dealers are therefore required to send **actual buying and selling rates** for 91 day and 364 day Treasury Bills by fax to the Public Debt Department by 4.00 p.m. daily. The fax numbers are 477718/9.

Name of Primary Dealer

Instrument /Period	Buying Yield Rate (Range)	Selling Yield Rate (Range)
3 month Treasury Bill		
12 month Treasury Bill		
2 Year Treasury Bond		
3 Year Treasury Bond		
4 Year Treasury Bond		
5 year Treasury Bond		
6 Year Treasury Bond		

All Primary Dealers should strictly comply with this direction which is issued under Section 12 of the Regulations of 2002 under the Registered Stock & Securities Ordinance and the Local Treasury Bills Ordinance.

K.G.D.D.Dheerasinghe
Superintendent of Public Debt

Attention:

CHIEF EXECUTIVE OFFICERS, PRIMARY DEALERS

DIRECTION ON CAPITAL ADEQUACY

This direction is issued under Section 12 of the Regulations made by the Minister of Finance dated 1 February, 2002 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect on January 1, 2002.

Colombo
Date : 30.10.2002

K.G.D.D.Dheerasinghe
Superintendent, Public Debt

1. In order to promote the safety, soundness and stability of the primary dealer system, it has been decided to introduce a capital adequacy requirement for primary dealers.
2. With effect from January 1st, 2003 primary dealer companies are required to maintain a minimum capital to assets ratio (capital adequacy) of 5 % with Tier 1 capital constituting not less than 70% of total capital funds.

3. For the purpose of the Capital Adequacy Ratio, capital is defined as follows :

Tier-1 Capital

- (a) Issued and paid up ordinary share capital.
- (b) Issued and paid up non-cumulative preference shares (non-redeemable or redeemable at issuer's option).
- (c) Share premium account.
- (d) Reserves created or increased by appropriations of retained earnings or other surpluses eg. retained profits and other reserves (excluding fixed assets revaluation reserves and retained profits on unaudited financial statements. Retained profits on unaudited financial statements can be included if the certification of a statutory auditor is provided).

Less

Goodwill and other intangible assets accumulated losses, investments in shares of subsidiaries and affiliate companies.

Tier-2 Capital

- (a) Short term subordinated debt (maturity period of more than 3 years).
- (b) Long term subordinated debt (maturity period of more than 5 years).
- (c) Cumulative preference shares.
- (d) Perpetual subordinated debt.

Less

Investment in subordinated debt of other companies, debentures and any debt instrument issued by subsidiaries, associate and affiliate companies and loans and advances granted to subsidiaries, associate and affiliate companies.

4. For the purpose of this Direction, assets shall mean:

- (a) Trading Securities Account – Balance Sheet Value (Market Value)
 - (i) Treasury Bills.
 - (ii) Treasury Bonds.
- (b) Investment Securities Account – Balance Sheet Value (Amortised Value at Historical Yield Rates).
 - (i) Treasury Bills.
 - (ii) Treasury Bonds.
- (c) Money lent under Reverse Repurchase Agreements (Securities Purchased under Agreements to resell) – Balance Sheet Value (Leg – 1/Leg – 1 plus Accrued Interest).
- (d) Cash & Bank Balances.
- (e) Fixed Assets – Balance Sheet Value (Net of Depreciation).
- (f) Other Assets – Those not included in the above and excluding items deducted from the capital calculation – Balance Sheet Value.

5. Returns on the Capital Adequacy position should be submitted to the Public Debt Department, at the end of each month in the format already provided by the Public Debt Department.

Attention:

Reference No. 08/24/002/005/01

**DIRECTIONS ON CUSTODIAL & TRUST HOLDINGS OF SCRIP
SECURITIES**

This direction is issued under section 10 of the Regulations made by the President dated 1 March 2000 under the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance and will come into effect from 1 January 2002.

Colombo

K.G.D.D. Dheerasinghe

February 14, 2003.

Superintendent of Public Debt

- (1) A dealer direct participant shall deposit any securities purchased, received or retained by the dealer direct participant for the account of a customer in a custodial securities account in the name of the customer, provided that where a security purchased, received or retained by a dealer direct participant on behalf of more than one customer the dealer direct participant shall maintain accounts to show the rights of each such customer in the security and such security shall be maintained in a custodial securities account on behalf of all such customers.

- (2) A dealer direct participant shall deal with securities held on behalf of a customer by the dealer direct participant only in accordance with instructions given by the customer to the dealer direct participant in writing.
- (3) Where securities are physically held by a dealer direct participant on behalf of a customer such securities shall be physically segregated from the securities of the dealer direct participant or of other customers of the dealer direct participant, and shall be held in safe and secure custody.
- (4) Securities held by the dealer direct participant on behalf of a customer shall be clearly identified in the records of the dealer direct participant as being held for the customer, and shall not form part of the assets of the dealer direct participant.
- (5) The dealer direct participant's records relating to securities held on behalf of customers shall be available for inspection by the Central Bank and to the customer or the customer's authorised representative at reasonable times, subject to applicable laws.
- (6) A dealer direct participant shall furnish to the Central Bank returns in respect of custodial holdings of securities on a monthly basis in the format at Schedule – I.
- (7) A dealer direct participant shall issue to its customers confirmations in respect of purchases and sales of securities on behalf of the customer in the format at Schedule – II and shall, in addition, issue to the customers a monthly statement with respect to the securities held by the dealer direct participant on behalf of the customers. Where a dealer direct participant holds a security on behalf of more than one customer, the dealer direct participant shall issue a confirmation to each such customer at the time that the customer acquires a right in the security, specifying the serial number of the security due to the customer and the coupon rate, if any, payable to the customer on such security in the format at Schedule – II.

Schedule 1

Register of Securities held in Custody/Trust on behalf of Customers for the month of

Purchase Date	Name of Customer	Reference No. of Confirmation Letter	Purchase Amount (Face Value)	Maturity Date	T.Bill/ T.Bond	Part/Full Owner-ship/ Beneficial Ownership	Face Value of T.Bill/Bond	Securities			
								In		Out	
								Signature	Date	Signature	Date

Table Register/cn2

Schedule – II

CONFIRMATION ADVICE
Purchase of Treasury Bills under Custodial Arrangements

Reference No. :

Date :

Name of Customer :

Address :

Dear Sir/ Madam,

Purchase of Treasury Bills

With reference to your application, we confirm that the following Treasury Bill/s is/are held in our custody on your behalf. On maturity you will receive the face value of the Treasury Bill/s.

1. Face Value :

2. Treasury Bill No. :

3. Purchase Date :

4. Yield :

5. Price :

6. Maturity Date :

Yours Faithfully,

.....
Manager

.....
Authorised Officer

Schedule – II

CONFIRMATION ADVICE
Purchase of Treasury Bonds under Custodial Arrangements

Reference No. :

Date :

Name of Customer :

Address :

Dear Sir/ Madam,

Purchase of Treasury Bonds

With reference to your application, we confirm that the following Treasury Bond/s is/are held in our custody on your behalf. On maturity you will receive the face value of the Treasury Bond/s and on coupon payment dates you will receive semi-annual interest payments

1. Face Value :

2. Treasury Bond No. :

3. Coupon Rate :

4. Yield :

5. Purchase Date :

6. Coupon Payment Dates :

7. Interest Payment Amounts :

8. Maturity Date :

9. Accrued Interest Paid :

10. Clean Price :

11 Total Price Paid :

Yours Faithfully,

.....
Manager

.....
Authorised Officer

Schedule – II

CONFIRMATION ADVICE
Purchase of Treasury Bills under Trust Arrangements

Reference No. :

Date :

Name of Customer :

Address :

Dear Sir/ Madam,

Treasury Bills Held in Trust

With reference to your application, we confirm that the following Treasury Bill/s is/are held in trust by us and that your beneficial ownership in the Bill/s is as stated in Item 1 below . On maturity you will receive the said value of the Treasury Bill/s as stated in Item 1 below.

1. Value of Beneficial Ownership :

2. Treasury Bill No. & Face Value:

3. Purchase Date :

4. Yield :

5. Price :

6. Maturity Date :

Yours Faithfully,

.....
Manager

.....
Authorised Officer

Schedule – II

CONFIRMATION ADVICE

Purchase of Treasury Bonds under Trust Arrangements

Reference No. :

Date :

Name of Customer :

Address :

Dear Sir/ Madam,

Treasury Bonds held in Trust

With reference to your application, we confirm that the following Treasury Bond/s is/are held by us in trust and that your beneficial ownership of the Bond is as stated in Item 1 below. On maturity you will receive the said value of the Treasury Bond/s as stated in Item 1 and on coupon payment dates you will receive semi-annual interest payments as stated in Item 7.

1. Value of Beneficial Ownership :

2. Treasury Bond No and Face Value. :

- 3. Coupon Rate :
- 4. Yield :
- 5. Purchase Date :
- 6. Coupon Payment Dates :
- 7. Value of Interest Payment :
- 8. Maturity Date :
- 9. Accrued Interest Paid :
- 10. Clean Price Paid :
- 11. Total Price Paid :

Yours Faithfully,

.....
Manager

.....
Authorised Officer

Attention:

Direction on Forward Rate Agreements and Interest Rate Swaps

This Direction is issued under Section 12 of the Regulations made by the Minister of Finance dated February 1,2002 under the Local Treasury Bills Ordinance and the Registered Stocks and Securities Ordinance and will come into effect from April 1, 2003.

Colombo

K.G.D.D.Dheerasinghe

April 1,2003

Superintendent of Public Debt

Financial derivatives such as Forward Rate Agreement (FRA) and Interest Rate Swaps (IRS) are useful for managing interest rates risks.

Description of the Product

1. A Forward Rate Agreement (FRA) is a financial contract between two parties to exchange interest payments for a 'notional principal' amount on settlement date, for a specified period from start date to maturity date. Accordingly, on the settlement date, cash payments based on contract rate (fixed) and the settlement rate, are made by the parties to one another. The settlement rate is the agreed bench-mark/reference rate prevailing on the settlement date.
2. An Interest Rate Swap (IRS) is an agreement between two parties to exchange a stream of interest payments for a 'notional principal' amount on multiple occasions during a specified period. Such agreements generally involve the exchange or swapping of future fixed rate interest payments for future floating rate interest payments or the exchange of future floating rate interest payments for future floating rate interest payments. Accordingly, on each payment date that occurs during the swap period, cash payments based on the fixed/floating and floating rates, are made by the parties to one another.

Participants

3. Primary Dealers (PDs) can undertake FRAs/IRS as a product for their own balance sheet management and for market making. PDs can offer these products to Licensed Commercial Banks, Licensed Specialised Banks, Registered Finance Companies, Registered Leasing Companies, Registered Insurance Companies, institutional investors and corporates for hedging their own balance sheet exposures.

Product Policy and Internal Control System

4. Prior to undertaking FRAs/IRS, PDs are required to inform Public Debt Department (PDD), Central Bank of Sri Lanka and abide by such reporting and any prudential requirements as prescribed by the Central Bank of Sri Lanka, from time to time.
5. PDs are required to ensure that appropriate infrastructure and risk management systems such as ability to price the product and to “mark to market ” their positions, monitor and limit exposures on an ongoing basis, etc., are put in place.
6. A copy of the document detailing Product Policy and Internal Control System should be submitted to the Public Debt Department, Central Bank of Sri Lanka .

Types of FRAs/IRS

7. PDs can undertake different types of basic FRAs/IRS. Swaps having explicit/implicit option features such as caps/floors/collars are not permitted.

Bench Mark Rate

8. The benchmark rate shall be the Treasury Bill or Treasury Bond rate

Size

9. There will be no restriction on the minimum or maximum size of ‘notional principal’ amounts of FRAs/IRS. Norms with regard to size are expected to emerge in the market with the development of the product.

Tenor

10. There will be no restriction on the minimum or maximum tenor of the FRAs/IRS.

Capital Adequacy

11. PDs are required to maintain capital for FRAs/IRS, as per the stipulations contained in **Annex 1**.

Exposure Limits

12. In order to set exposure limits for counterparties, PDs may apply the conversion factors to notional principal amounts as per the exposure method prescribed in **Annex 1**.

13. Furthermore, while dealing with corporates and institutions other than Licensed Commercial Banks, PDs should exercise due diligence to ensure that they are undertaking FRAs/IRS only for hedging their own rupee balance sheet exposures. PDs are advised to also obtain a certificate from the authorised signatory/signatories of corporate/s to the effect that the transactions undertaken by them are meant for hedging balance sheet exposures only, i.e., size and tenor of the transactions undertaken are not in excess of their underlying rupee exposures.

Swap Position

14. Preferably, PDs should undertake FRAs/IRS only for hedging underlying genuine exposures. However, recognising the crucial role played by the market maker in development of the product and creating of the market itself, PDs have been allowed to undertake market making activity, which would involve at times dealing in the market without underlying exposure. **However to ensure that market makers do not over extend themselves, market makers are required to place prudential limits on swap positions, which may arise on account of market making activity.**

Accounting and Valuation

15. Transactions for hedging and market making purposes should be recorded separately. **While transactions for market making purposes should be “marked to market” (at least at weekly intervals), those for hedging purposes could be accounted for on accrual basis.** PDs should adopt accounting treatment on the basis of the International Accounting Standards (IAS 32 & 39) . PDs may refer to **Annex 2,**

Documentation

16. For uniformity and standardisation, PDs should use International Swap Dealers Association (ISDA) documentation, as suitably modified to comply with these Directions for undertaking FRAs/IRS transactions. Institutions should further evaluate whether the counterparty has the legal capacity, power and authority to enter into FRAs/IRS transactions.

Reporting

17. PDs are required to report, as per the proforma indicated in **Annex – 3** their FRAs/IRS operations on a monthly basis to Public Debt Department, Central Bank of Sri Lanka.

18. These directions are intended to form the basis for development of Rupee derivative products such as FRAs/IRS in the country. The directions are subject to review, on the basis of development of FRAs/IRS market.

Annex - I

Capital Adequacy for Primary Dealers on Interest Rate Contracts for Credit Risk

Primary Dealers undertaking Forward Rate Agreements and Interest Rate Swaps, will be required to fulfill the following minimum capital/capital adequacy requirements:

Over and above the minimum capital requirements and the capital adequacy ratio required by the Direction on Capital Adequacy, Primary Dealers will have to maintain additional capital at 12 per cent of Risk Weighted Assets (RWA) towards credit risk on Interest Rate Contracts.

The methodology for these off-balance sheet items will be as follows :

(i) The notional principal amount will be multiplied by the conversion factors given below to arrive at the adjusted value.

@ 0.5 per cent of notional principal value for original maturity of less than 1 year.

@ 1.0 per cent for original maturity of one year and less than two years.

@ 1.0 per cent for each additional year.

(ii) The adjusted value thus obtained shall be multiplied by the risk weight applicable to the counter party as specified below.

Primary Dealers/Licensed Commercial Banks/	20 per cent.
All others	100 per cent.

Annex 2

Accounting Norms

Accounting for Hedge Swaps

(i) Interest Rate Swap which hedges interest bearing asset or liability should generally be accounted for like the hedge of the asset or liability.

- (ii) The Swap that is accounted for like a hedge should be accounted for on accrual basis except the swap designated with an asset or liability that is carried at market value or lower of cost or market value in the financial statements. In that case the swap should be marked to market with the resulting gain or loss recorded as an adjustment to the market value of designated asset or liability.
- (iii) Gains or losses on the termination of swaps should be recognised when the offsetting gain or loss is recognised on the designated asset or liability. This implies that any gain or loss on the terminated swap would be deferred and recognised over the shorter of the remaining contractual life of the swap or the remaining life of the asset/liability.

(iv) Redesignation of Hedge Items

If a hedge is redesignated from one item of asset/liability to another item of asset/liability such redesignation should be accounted for as the termination of one hedge and acquisition of another. On the date of redesignation the swap should be marked to market and the mark to market value would be amortized over the shorter period of the remaining life of the swap or remaining life of the asset/liability. The offsetting mark to market entry adjustments would be treated as premium received or paid for hedge on the newly designated item of asset/liability and this would be amortized over the life of the redesignated asset/liability or remaining term of the swap whichever is shorter.

- (v) When a PD is acting like a broker for matching parties and is not a Principal to the contract itself, then the fee should be recognised immediately as an income. In case where the bank acts like a Principal the fee should be amortized over the life of the contract.

Accounting for Trading Positions

The following should be used as general principles for accounting of trading transactions.

- (i) Trading swaps should be marked to market with changes recorded in the income statement.
- (ii) Income and expenses relating to these swaps should be recognised on the settlement date.
- (iii) Fees should be recognised as immediate income or expenditure.
- (iv) Gains or losses on the termination of the swaps should be recorded as immediate income or expenses.

Disclosures

The following should be disclosed in the note to the balance sheet:

- the notional principal of swap agreements;
- nature and terms of the swaps including information on credit and market risk and the accounting policies adopted for recording the swaps;
- quantification of the losses which would be incurred if counterparties failed to fulfil their obligation under the agreement;
- collateral required by the entity upon entering into swaps;

- any concentration of credit risk arising from the swaps. Examples of concentration could be exposures to particular industries or swaps with highly geared companies; and
- the “fair” value of the total swaps book. If the swaps are linked to specific assets, liabilities or commitments, the fair value would be estimated amount that the entity would receive or pay to terminate the swap agreements at balance date. For a trading swap the fair value would be its mark to market value.

Annex - 3

Monthly Return on Forward Rate Agreement/Interest Rate Swaps

Name of the Institution :

Month and Year :

1. Gross Notional Amount (Rs.) :

Total :

Of which for

Hedging :

Market Making :

2. FRAs/IRS contracted during the month of 200

Original Maturity	No. of Contracts	Notional Amount (Rs.)	Floating # Rate (Range)	Fixed Rate (Range)	Floating @ # Rate (Range)
Upto 3 Months					
3 – 6 Months					
6 – 12 Months					
1-2 Years					
2-3 Years					
3-4 Years					
4-5 Years					
5-6 Years					
6-7 Years					
7-8 Years					
8-9 Years					
9-10 Years					
10-11 Years					
11-12 Years					
12-13 Years					
13-14 Years					
14-15 Years					

along with rates bench marks should also be mentioned in bracket.

@ rate pertaining to second leg, if the swap is 'floating to floating' in nature

3. FRAs/IRS outstanding as at the end of the month of 200

Residual Maturity/ Repricing Date*	No. of Contracts	Notional Amount (Rs.)	Floating # Rate (Range)	Fixed Rate (Range)	Floating @ # Rate (Range)
Upto 3 Months					
3 – 6 Months					
6 – 12 Months					
1-3 Years					
2-3 Years					
3-4 Years					
4-5 Years					
5-7 Years					
6-7 Years					
7-8 Years					
8-9 Years					
9-10 Years					
10-11 Years					
11-12 Years					
12-13 Years					
13-14 Years					
14-15 Years					

* Residual maturity or repricing date, whichever is earlier, is to be reported.

along with rates bench marks should also be mentioned in bracket.

@ rate pertaining to second leg, if the swap is 'floating to floating' in future.

Attention:

08/24/002/0005/001

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1
July 23, 2003.

Chief Executive Officer

- Ceybank Securities Ltd.
- Commercial Bank Primary Dealer Ltd.
- NSB Fund Management Co. Ltd.
- HNB Securities Ltd.
- First Capital Treasuries Ltd.
- Sampath Surakum Ltd.
- Seylan Bank Asset Management Ltd.
- Ceylinco Shriram Securities Ltd.
- Peoples' Bank
- Hongkong & Shanghai Banking Corporation Ltd
- Capital Alliance Ltd

**Direction on Firm Two Way Quotes (Bid and Offer Prices)
for Benchmark Maturities**

We refer to the Direction on Secondary Market Firm Two Way Quotes issued on July 2, 2002 where PDs are required to make firm two way quotes for 12 month Treasury Bills.

In order to promote the liquidity of medium and long-term market, it is necessary to expand the firm two- way quote requirement for selected benchmark maturities.

In this regard, the Public Debt Department has selected four benchmark maturities, that cover short to medium- term securities.

All PDs are hereby required make **firm (effective) two- way quotes** for the following benchmark maturities for trading with the public.

Firm Two Way Quotes for Selected Benchmark Maturities

- a) 3 month Treasury Bills
 - b) 12 month Treasury Bills
 - c) 2 year Treasury Bonds
 - d) 5 year Treasury Bonds
- All PDs required to submit their effective buying and selling quotes for securities in the benchmark maturities to the Public Debt Department in the specimen format provided in the

Annex. The firm two way quotes should be e-mailed to the Public Debt Department by at least 10.00 a.m. daily. The e-mail address is pdebt@cbsl.lk

- All PDs are also required to put their effective buying and selling quotes for securities in the benchmark maturities on the Bloomberg Screen by 10 a.m. daily.

PDs are also encouraged to make two way quotes for securities in other maturities.

All PDs are required to comply with this direction with immediate effect and non compliance may result in prohibition to participate in auctions conducted by the Public Debt Department in the future.

This direction is issued under Section 12 of the Regulations made by the Minister of Finance dated February 1,2002 in terms of the Registered Stocks and Securities Ordinance & the Local Treasury Bills Ordinance.

K.G.D.D. Dheerasinghe
Superintendent of Public Debt

ANNEX

SPECIMEN FORMAT

FIRM & EFFECTIVE

TWO WAY QUOTES

Name of Primary Dealer

Instrument /Period	Buying Yield Rate	Selling Yield Rate
--------------------	-------------------	--------------------

	(Range)	(Range)
3 Month Treasury Bill		
12 Month Treasury Bill		
2 Year Treasury Bond		
3 Year Treasury Bond (optional)		
4 Year Treasury Bond (optional)		
5 Year Treasury Bond		
6 Year Treasury Bond (optional)		
10 Year Treasury Bond (optional)		
15 Year Treasury Bond (optional)		



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இலங்கை மத்திய வங்கி

CENTRAL BANK OF SRI LANKA

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ஜனாதிபதி மாவத்தை,
த. பெ. இல. 590,
கொழும்பு - 1, ஸ்ரீ லங்கா
கந்தி : 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

_ Attention:

08/24/002/0005/003

Public Debt Department
Central Bank of Sri Lanka
No.30, Janadhipathi Mawatha
Colombo 1
August 15, 2003

Chief Executive Officer of Primary dealers

[Direction on Minimum Subscriptions Levels for Treasury Bill and Bond Auctions](#)

This direction is issued in terms of Section 12 of the Regulations dated February 1, 2002 issued by the Minister of Finance under the Registered Stocks and Securities Ordinance and the Local Treasury Bills Ordinance. In terms of this direction each Primary Dealer is hereby required to subscribe a minimum 10% of the amount offered for each maturity at each Treasury Bond auction and Treasury Bill auctions in order to ensure that the auctions are fully subscribed.

All Primary Dealers are required to comply with this direction with immediate effect.

K.G.D.D.Dheerasinghe



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கந்தி : 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Superintendent of Public Debt

Attention:

Ref:08/24/002/0005/003

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1
November 28, 2003

Chief Executive Officers of Primary Dealers

[Direction on Minimum Capital Requirement](#)

In terms of the direction dated December 23, 2002 issued under the section 7 of the Local Treasury Bills Ordinance and the Registered Stock and Securities Ordinance, all Primary Dealers (PDs) are required to maintain a minimum capital requirement of Rs. 200 million of which a minimum of Rs. 150 million should be maintained as Tier-I capital.

However, in view of the current financial status and having considered the viability and stability of the primary dealer system and the interest of the national economy, the Central Bank of Sri Lanka has decided that the minimum capital maintained by a primary dealer should be increased to Rs. 400 million of which minimum Rs. 350 million should be maintained as Tier-1 Capital with in the timeframe specified below.

Minimum Capital Funds Required	<u>Before 31/12/2004</u> Rs.350 million.	<u>Before 1/7/2005</u> Rs.400 million.
--------------------------------	---	---

Tier I capital and Tier II capital are defined as follows :

Tier-1 Capital

- (e) Issued and paid up ordinary share capital.
- (f) Issued and paid up non-cumulative preference shares (non-redeemable or redeemable at issuer's option).
- (g) Share premium account.
- (h) Reserves created or increased by appropriations of retained earnings or other surpluses eg. retained profits and other reserves (excluding fixed assets revaluation reserve).

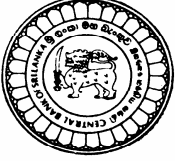
Less

Goodwill and other intangible assets accumulated losses, investments in shares of subsidiaries and affiliate companies.

Tier-2 Capital

- (e) Short term subordinated debt.
- (f) Long term subordinated debt.
- (g) Cumulative preference shares.
- (h) Perpetual subordinated debt.

K.G.D.D.Dheerasinghe
Superintendent of Public Debt



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கந்தி: 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Attention:

Ref:08/24/002/0005/003

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1
November 28, 2003

Chief Executive Officers of Primary Dealers

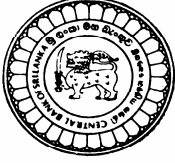
Direction on Special Risk Reserve

In order to promote the safety, soundness and the stability of the Primary Dealer(PD) system and to build up PD capital base, with effect from July 1, 2004, Primary Dealers (PDs) are required to transfer a percentage of their profit after tax annually to a Special Risk Reserve as follows.

- 50% of the profit after tax annually by the PDs who maintain capital funds less than Rs.400 million
- 25% of the profit after tax annually by the PDs who maintain capital funds in excess of Rs.400 million.

This direction is issued in terms of Section 12 of the Regulations dated February 1, 2002 issued by the Minister of Finance under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance.

Please acknowledge receipt.



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ஜனாதிபதி மாவத்தை,
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கந்தி : 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

K.G.D.D.Dheerasinghe
Superintendent of Public Debt

Attention:
08/24/002/0005/003

Public Debt Department,
December 19, 2003.

CEO's of Primary Dealers ,

Direction on Accounting for Repo Transactions

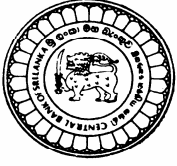
All Repurchase and Reverse Repurchase transactions should be recorded to reflect the true commercial effect or substance of the transaction. As all Repo transactions are in effect collateralized borrowings / lending, they should be accounted for as follows.

1. Repurchase Transactions
Dr. Cash/Bank
Cr. Repurchase A/C
2. Reverse Repurchase Transactions
Dr. Reverse Repurchase A/C
Cr. Cash

Carrying value/Book value of securities given as Collateral for Repo borrowings should also be taken out of the Trading/Investment portfolio account and put into a separate encumbered Trading/Investment portfolio account. When preparing the Balance Sheet, Primary Dealers should report the encumbered and unencumbered securities together but a note to the accounts should disclose the value of encumbered securities included in the Trading /Investment portfolio. A note to the accounts should also disclose the market value of securities obtained as collateral on Reverse Repurchase transactions and the policy on haircuts on the collateral taken on Reverse Repurchase transactions.

Yours faithfully,

Superintendent of Public Debt



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ஜனாதிபதி மாவத்தை,
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கந்தி : 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Ref:08/24/002/0005/004

Public Debt Department
No.30, Janadhipathi Mawatha
Colombo 1
January 6, 2004

Chief Executive Officers of Primary Dealers

Direction on Short Selling of Securities

This direction is issued in terms of Section 12 of the Regulations dated February 1, 2002 issued by the Minister of Finance under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance. In terms of this direction Primary Dealers (PDs) are required to refrain from short selling of securities. No PD should sell any securities without actually holding the relevant securities in its portfolio. Securities obtained as collateral on reverse repo transactions are not considered as PD's own securities and hence they cannot be sold.

Please acknowledge receipt.

K.G.D.D.Dheerasinghe
Superintendent of Public Debt

Attention:

Reference No: 08/24/002/0005/004

Public Debt Department,
No: 30, Janadhipathi Mawatha,
Colombo 01.
June 7, 2004

Chief Executive Officers of Primary Dealers,

Direction on Adjusted Trading (Away Prices)

Primary Dealers are hereby required to refrain from having adjusted trading or using away prices for recording their transactions. They should use current market prices, for recording their transactions.

Adjusted trading is a practice involving the sale of a security at a price above the prevailing market value and the simultaneous purchase and booking of a sale or different security at a price greater than its market value. Such transactions inappropriately differ the recognition of losses on securities sold while establishing an excessive reported value for acquired securities.

This direction is issued in terms of Section 12 of the Regulations dated February 1, 2002 issued by the Minister of Finance under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance.

Please acknowledge the receipt of this direction.

Dr. H. N. Thenuwara
Superintendent of Public Debt



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ஜனாதிபதி மாவத்தை,
த. பெ. இல. 590,
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தந்தி : 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Ref:08/24/002/0005/005

Public Debt Department

January 18, 2005

Chief Executive Officers of Primary Dealers,

[Direction on Enhancement of Minimum Capital Requirement of Primary Dealers](#)

This direction is issued in terms of section 12 of the Regulation dated February 1, 2002 issued by the Minister of Finance under the Registered Stocks and Securities Ordinance and the Local Treasury Bills Ordinance.

In terms of the direction on Minimum Capital Requirement issued on 28th November 2003 Primary Dealers (PDs) were required to maintain Rs 350 million as minimum capital before 31 December 2004. However, some PDs were unable to meet this requirement by 31 December 2004. Considering this situation and the current market conditions, the Monetary Board decided to extend the deadline from 31 December 2004 to 1 July 2005 for the PDs to comply with the minimum capital requirement of Rs 350 million.

PDs are required to comply with the above requirement subject to the condition that any PD who wishes to declare profits as dividends during the period from 31 December 2004 to 1 July 2005 shall obtain the prior approval of the Central Bank to do so.

Dr W M Hemachandra

Superintendent of Public Debt



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CENTRAL BANK OF SRI LANKA

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Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Ref:08/24/002/0005/005

Public Debt Department

April 18, 2005

Chief Executive Officers of Primary Dealers,

Direction on Enhancement of Minimum Capital Requirement, Dividend Distribution and Maintenance of Tier II Capital by Primary Dealers

This direction is issued in terms of section 12 of the Regulation dated February 1, 2002 issued by the Minister of Finance under the Registered Stocks and Securities Ordinance and the Local Treasury Bills Ordinance.

1. Primary Dealers (PDs) are required to increase minimum capital from,
 - a. Existing Rs 200 million to Rs 250 million from 1 July 2005 and
 - b. Rs 250 million to Rs 300 million from 1 July 2006instead of Rs 350 million as per the CBSL directions on 28 November 2003 and 18 January 2005.
2. PDs who maintain a capital between Rs 250 million – Rs 300 million are allowed to declare 25% of profits as dividends with effect from 1 July 2005.
3. PDs who maintain a capital above Rs 300 million are required to allocate 25% of profits annually to a special reserve with effect from 1 July 2005. Direction on special risk reserve issued on 28 November 2003 will be lapsed after 30 June 2005.
4. PDs are allowed to maintain up to a maximum 50% of Tier –I capital as Tier – II capital with effect from I July 2005.
5. PDs are required to implement the Risk Weighted Capital Adequacy Framework with a minimum capital requirement of Rs 300 million with effect from 1 July 2006.

Superintendent of Public Debt



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CENTRAL BANK OF SRI LANKA

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தந்தி: 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

08/25/001/0034/001
Circular No. SSSS/01/2005

September 30, 2005

To: All Participants of LankaSettle System.

Amendment to LankaSettle System Rules, August 2003.

You are hereby informed that the first paragraph of Clause 5.8 of Volume 3 of LankaSettle System Rules issued in August 2003 is amended to read as follows with effect from October 1, 2005.

"LankaSecure will accept Securities Instructions for settlement on future Value Dates and will store such instructions until such Value Date. The System will accept Securities Instructions for up to 31 calendar days in advance of current date and Securities Instructions with future Value Dates greater than 31 calendar days in advance will be rejected."

Accordingly, clause 5.8 of Volume 3 of the LankaSettle System Rules will read as follows with effect from October 1, 2005.

"5.8 Forward Dated Transactions

LankaSecure will accept Securities Instructions for settlement on future Value Dates and will store such instructions until such Value Date. The System will accept Securities Instructions for up to 31 calendar days in advance of current date and Securities Instructions with future Value Dates greater than 31 calendar days in advance will be rejected.

If a Securities Instruction is received by LankaSecure that has a value Date that has already passed it will be rejected.

At the start of each Business Day LankaSecure checks that each stored Securities Instruction has a valid Value Date. If a stored Securities Instruction has a value date that has already passed it will be rejected.

In the event that a Business Day is "cancelled", e.g. a day on which due to extraordinary circumstances the Central Bank is not open for business, it is the responsibility of the Participant to cancel stored Securities Instructions for that Value Date or re-send them following rejection with a new Value Date."

C.Premaratne
Superintendent of Public Debt

K.R.M.Siriwardhane
Director/Payments and Settlements



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CENTRAL BANK OF SRI LANKA

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ஜனநிபதி மாவத்தை,
த. பெ. இல. 590,
கொழும்பு - 1, ஸ்ரீ லங்கா
தந்தி: 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

08/24/021/001/005

September 29, 2005

Circular No : SSSS/02/2005

To: All Participants of LankaSettle System

Cancellation of the Primary Dealer License of Commercial Bank Primary Dealer Ltd. and Appointment of Commercial Bank of Ceylon Ltd. as a Primary Dealer

Commercial Bank Primary Dealer Ltd. of No.21, Bristol Street, Colombo 01 has been permitted by the Monetary Board of the Central Bank of Sri Lanka to transfer its Primary Dealer business to its parent company, Commercial Bank of Ceylon Ltd. (Dealer Direct Participant) of the same address which will be appointed as a Primary Dealer with effect from October 01, 2005.

Accordingly, we wish to inform you that with effect from October 01, 2005 Commercial Bank Primary Dealer Ltd. will cease to be a Primary Dealer.

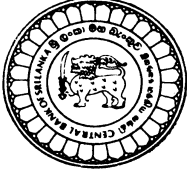
Consequently, SWIFT User Identification Code (BIC) No. CBPDLKLXXXX and RTGS Settlement Account Number CBPDLKLXXXX010004552 of Commercial Bank Primary Dealer Ltd. will cease to be operative with effect from October 01, 2005. The following current SWIFT User Identification Code (BIC) and RTGS Settlement Account Number of Commercial Bank of Ceylon Ltd. will be used for all Primary Dealer operations of Commercial Bank of Ceylon Ltd.

SWIFT User ID Code (BIC) : CCEYLKLXXXX

RTGS Settlement Account : CCEYLKLXXXX010004404

Mrs. C. Premaratne
Superintendent of Public Debt

Mrs. K.R.M. Siriwardhane
Director/Payments and Settlements



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CENTRAL BANK OF SRI LANKA

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தந்தி: 'மத்தியவங்கி'

Janadhipathi Mawatha,
P.O. Box 590,
Colombo 1, Sri Lanka.
Telegrams: 'CENTRABANK'

Circular No: SSSS/01/2006

February 28, 2006

To: All Participants of LankaSettle System

Reporting Securities Transactions in the Central Depository System

As stipulated under custodial responsibilities of the system rules of LankaSettle, it is the sole responsibility of the Dealer Direct Participants in the Central Depository System (CDS) to record the legal ownership of a security promptly and accurately. There are different types of accounts in the system to record different types of transactions. However, it has been observed that most participants are recording security transactions in incorrect accounts in the CDS of the Central Bank in particular for repos and reverse repos.

The following denotes the meanings of the four types of repo and reverse repo accounts available in the system from the participants' point of view.

- | | |
|---------------------------------------|-----|
| 1. Tradable Repo Account | CRE |
| 2. Non- Tradable Repo Account | CRR |
| 3. Tradable Reverse Repo Account | CRP |
| 4. Non- Tradable Reverse Repo Account | REP |

Participants must record their repo and reverse repo transactions in the following manner.

- a) A repo transaction by a participant with a customer

Securities must be held in the participant's CRE or CRR account giving legal ownership to the customer

- b) A reverse repo transaction by a participant with another participant or with a customer

Borrowing party (repo party) must transfer securities to the lending party's (rev.repo party) CRP or REP account.

In addition to the above, outright sales of securities by a participant to a customer should be recorded in the account type of CSL and no other securities transactions be recorded in this account. The details of accounts type available in LankaSecure are given in Annex I.

Accordingly, all participants are kindly requested to report above securities transactions in correct accounts as per System Rules of LankaSettle issued by the Central Bank of Sri Lanka (CBSL).

C. Premaratne

Superintendent of Public Debt

Account Types Available in LankaSecure

The following Account Types are used in LankaSecure. The Central Bank may, at its discretion, restrict the Account Types that may be available to any Participant or category of Participant as well as the transaction types that may be applied to each Account Type.

Account Type	Code	Purpose
Participant's/ Central Bank's Own Account	OWN	Holds securities owned by the Participant/ Central Bank
ILF Account	ILF	Holds securities, in the case of participants, to be transferred to the Central Bank as collateral for ILF, and, in the case of the Central Bank, transferred by the participants to the Central Bank as collateral for ILF.
Pledge Account	PLG	Holds securities that have been pledged to the Participant (in the case of an Approved Credit Agency) or an entity for whom the Participant is acting. The name of the Pledgor is recorded in the Owner field. Securities in these accounts cannot be traded except in accordance with applicable Regulations.
Customer Account (Resident)	CSL	Holds securities owned by a "person resident in Sri Lanka" Customer of a Participant. The account is created by specifying a resident Owner in securities transactions. This Account Type is available only to Dealer Direct Participants.
Customer Account (Non-Resident)	CSF	Holds securities owned by a "person resident outside Sri Lanka". The account is created by specifying a non-resident Owner in securities transactions. This Account Type is available only to Dealer Direct Participants.
Tradable Repo Account	CRP	Holds securities that are transferred under a Reverse Repo Agreement by a Participant or a Customer to a counterparty that are to be returned at a future date under the terms of such agreement. Securities in this Account are tradable.
Non-Tradable Repo Account	REP	Holds securities that are transferred under a Reverse Repo Agreement by a Participant or a Customer to a counterparty that are to be returned at a future date under the terms of such agreement. Securities in this account cannot be traded.
Tradable Customer Reverse Repurchase Account	CRE	Holds Securities that are transferred under a Reverse Repurchase Agreement by a Participant or a customer to a customer that are to be reversed at a future date under the terms of such agreement. Securities in this account are tradable.
Non-Tradable Customer Reverse Repurchase Account	CRR	Holds Securities that are transferred under a Reverse Repurchase Agreement by a Participant or a customer to a customer that are to be reversed at a future date under the terms of such Agreement. Securities in this account cannot be traded.
Statutory Investment Account	STI	Securities that are held by Participant to meet statutory requirements imposed on the Participant.
Primary Auction Purchase Account	PAP	Holds securities purchased at Primary Auction (Primary Dealer and Designated Non Dealer Bidder use only).
Domestic Operations Repo Account	DOP	Holds securities transferred to a Participant by the Central Bank under a Repo Agreement that are to be returned to the Central Bank at a future date. Securities in this Account are not tradable.
Domestic Operations Reverse Repo Account	DRP	Holds securities transferred to the Central Bank by a Participant under a Reverse Repo Agreement that are to be returned to the Participant at a future date.

June 22, 2006

To: Chief Executive Officers of Primary Dealers,

[Direction On Risk Weighted Capital Adequacy Framework \(RWCAF\) for Primary Dealers \(PDs\)](#)

This direction is issued in terms of section 12 of the Regulation No.01 of 2002 dated February 1,2002 issued by the Minister of Finance under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance.

1. With effect from July 01, 2006 PDs are required to maintain:

- a. A required minimum capital which is the higher of Rs.300 million (minimum capital) or the capital sufficient to meet the interest rate sensitivity of the trading portfolio including reverse repos and risk on disallowances (capital charge), and counterparty credit risk;
- b. Net capital [Capital (Tier I and Tier II) minus capital for counter party risk], which should be equal to or higher than the capital charge; and
- c. A minimum risk weighted capital adequacy ratio (CAR) of 8%

The methodology of calculating sensitivity of the PD portfolios to an assumed change in yields along with the risk exposure for long/short positions (capital charge), and counterparty credit risk requirement are given in [Schedule 1 &2](#).

2. PDs are required to comply with the following regulatory requirements for reporting of capital adequacy with effect from July 01, 2006.

All PDs are required to report the positions of their capital adequacy in the specified format on a monthly basis, which is given in [Schedule 3](#) in electronic format (via email/soft copy). The reporting format for the respective month has to be completed by each PD and submitted to the Public Debt Department (PDD) on or before 15th of the subsequent month. These reporting formats would cover, inter alia,

- a. Whether the minimum absolute capital requirement is being satisfied; and
- b. Whether the CAR is above or below its required minimum capital adequacy ratio.

All PDs on a daily basis are required to maintain the above-mentioned minimum capital and capital adequacy ratio requirements including a proper mechanism to monitor those requirements.

3. Definition of Capital Funds, Net Capital, Minimum Capital, Required Minimum Capital, Capital Adequacy Ratio and Minimum Capital Adequacy Ratio

3.1 Capital Funds

Capital Funds would include the followings:

Tier-I Capital

- (i) Issued and paid up ordinary share capital.
- (j) Issued and paid up non-cumulative preference shares (non-redeemable or redeemable at issuer's option).
- (k) Share premium account.
- (l) Reserves created or increased by appropriations of retained earnings or other surpluses, eg., retained profits and other reserves (excluding fixed assets revaluation reserves and retained profits on unaudited financial statements. Retained profits on unaudited financial statements can be included, if the certification of a statutory auditor is provided).

Less

Goodwill and other intangible assets, accumulated losses.

Tier-II Capital

Tier-II capital includes the following and will be limited to 50% of Tier-I capital.

- (i) Medium term subordinated debt (maturity period of more than 3 years).
- (j) Long term subordinated debt (maturity period of more than 5 years).
- (k) Cumulative preference shares.
- (l) Perpetual subordinated debt.

To be eligible for inclusion in Tier II capital, the instrument should be fully paid-up, unsecured, subordinated to the claims of other creditors, free of restrictive clauses, and should not be redeemable at the initiative of the holder or without the consent of the Central Bank of Sri Lanka (CBSL). This instrument should carry a fixed maturity, and as it approaches maturity, it should be subject to progressive discount, for inclusion in Tier II capital.

Instruments with an initial maturity period of equal or less than 3 years should not be included as part of Tier II capital. The subordinated debt instruments included in Tier II capital shall be subject to discount at the rates shown below:

Remaining Maturity of Instruments	Rate of Discount (%)
Less than one year	40.00
One year and above but less than two years	20.00
Two years and above but less than three years	0
Three years and above	0

3.2 Net Capital

Net Capital includes Tier-I and Tier II capital, less counter party risk capital requirements.

3.3 Minimum Capital

Minimum capital is Rs. 300 million, which is imposed by the CBSL and required, to be maintained by a PD.

3.4 Required Minimum Capital

A required minimum capital is the higher of Rs.300 million (minimum capital) or the capital sufficient to meet the interest rate sensitivity of the trading portfolio plus rev.repo and capital for disallowances (capital charge), and capital for counterparty credit risk.

3.5 Capital Adequacy Ratio

Capital Adequacy Ratio is the ratio computed by dividing available capital by the risk-weighted assets.

3.6 Minimum Capital Adequacy Ratio

Minimum Capital Adequacy Ratio is the ratio computed by dividing minimum required capital by the risk-weighted assets.

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C. Premaratne

MEASUREMENT OF MARKET RISK (CAPITAL CHARGE)**A. Fixed Income Instruments**

PDs are required to calculate capital charges based on the standardised duration based method as follows.

- i. First calculate the price sensitivity of all instruments in terms of a change in interest rates of between 3.0 and 1.8 percentage points (adjusted Basle rates) depending on the duration of the instrument as per Table 1 given below. (For rev.repo portfolio, take maturity of the rev.repo instead of the security maturity)
- ii. Slot the resulting sensitivity measures into a duration-based ladder with the thirteen time-bands set out in Table 1;
- iii. Calculate the capital charge for trading plus rev. repo as follows;
Market value of the individual security * modified duration * assumed change in yield.
(Please see the schedule 3, Page 12 for calculation of Modified Duration for Trading and Reverse Repo)
- iv. Subject the lower of the long and short positions in each time-band to a 5% capital charge towards vertical disallowance designed to capture basis risk; (Please see the schedule 3, Page 15)
- v. Carry forward the net positions in each time-band for horizontal offsetting across the zones subject to the disallowances set out in Table 2. (Please see the schedule 3, Page 15)

Table- 1
Assumed Yield Changes in each Maturity Category

Zone	Time Period	Assumed Change in Yield	Weight
1	1 month (or less)	3.0	0
	1 to 3 months	3.0	0.2
	3 to 6 months	3.0	0.4
	6 to 12 months	3.0	0.7
2	1 to 2 years	2.7	1.25
	2 to 3 years	2.4	1.75
	3 to 4 years	2.25	2.25
3	4 to 5 years	2.25	2.75
	5 to 7 years	2.1	3.25
	7 to 10 years	1.95	3.75
	10 to 15 years	1.8	4.5
	15 to 20 years	1.8	5.25
	over 20 years	1.8	6.0

Source: Basle standard bands with treble Basle yield changes

In line with the Basle methodology, long and short positions within the same time band may be 95% offset against each other, with 5% of the smaller of the long or short position within a time band being required as a basis reserve. The remaining position (i.e., the residual after offset) is carried through to Table 2 below, which gives the horizontal disallowances to be applied to different time bands within zones, between adjacent zones, and finally between zones 1 and 3.

Table- 2
Zone Netting Disallowance Table

Zones	within the zone	between adjacent zones	between zones 1 and 3
Zone 1	40%	40%	100%
Zone 2	30%		
Zone 3	30%	40%	

Source: Basle standard

Price sensitivity can be calculated in two different ways:

- 1. Modified Duration * Change in yield; or**
- 2. Explicit calculation of the price change based on the formula outlined below which will be used in the risk weighted capital adequacy calculations..**

Both approaches will give the same result for small (e.g. 1 to 50bp) changes in yields; however, in the case of larger assumed changes in rates, the latter approach will be more accurate due to the impact of convexity (which measures the sensitivity of duration itself to the change in the level of yield).

The price sensitivity of any instrument may be estimated by using the formula given below, where the discount rate to be used is the valuation rate used in marking that specific security to market.

Price Sensitivity

$$NPV = \sum_i \left(C_i \left(\frac{1}{1+S_i} \right)^{t_i} \right)$$
$$= \frac{NPV - \sum_i \left(C_i \left(\frac{1}{1+S_i} \right)^{t_i} \right)}{NPV}$$

Where

$$NPV = \sum_i \left(C_i \left(\frac{1}{1+R_i} \right)^{t_i} \right)$$

\sum_i = Sum over all cashflows

C_i = Cashflow amount at time t

R_i = Valuation rate as derived from Primary Dealer Department quoted rates (interpolating and adding off-the-run spread where necessary)

S_i = Valuation rate as defined above + assumed change in yield (see Table 2 below)

t_i = Value date of the cashflow (expressed in days from now)

t_0 = Settlement date of the security (expressed in days from now)

T_i = Time, in years, from t_0 to t_i calculated on an Actual/Actual basis.

B. Interest Rate Derivatives

The measurement procedure should include all interest rate derivatives and off-balance sheet instruments (e.g., forward rate agreements (FRAs), other forward contracts, interest rate swaps etc.)

in the trading book, which are reacted to changes in, yield rates. The following procedure outlines the general valuation procedure in the event that such activity exists. The derivatives should be converted into positions of the relevant underlying instrument and should be subject to market risk charges as described in Schedule 1.

i. Forward Contracts, including Forward Rate Agreements (FRA)

These instruments are treated as combinations of long and short positions. The maturity of a FRA is the period until it is delivered or the contract is exercised, plus - where applicable - the life of the underlying instrument. For example, a long position in a June three-month interest rate futures entered in April has to be reported as a long position in a government security with a maturity of five months and a short position in a government security with a maturity of two months.

ii. Swaps

Swaps are treated as two notional positions in government securities with relevant maturities. For example, an interest rate swap under which a PD is receiving floating rate interest and paying fixed will be treated as a long position in a floating rate instrument and a short position in a fixed-rate instrument. Tenor of the floating rate instrument is treated as equivalent to the period until the next interest fixing while the tenor of the fixed rate instrument is treated as equivalent to the residual life of the swap.

Until a direct source is available, discount rates could be derived from the bid/off prices published by the PDD to value the swap transactions with appropriate additions for spreads, and applied similar to the bond pricing methodology described in Schedule 1. In most of the cases, an appropriate margin has to be added to the government securities yield curve to obtain an accurate curve for swap valuation.

Appropriate valuation techniques may be developed for more complex financial market products when the need arises.

CALCULATION OF GENERAL MARKET RISK FOR INTEREST RATE

RELATED INSTRUMENTS (Example extracted from Amendment to the Capital Accord to Incorporate Market Risks-Basle Committee on Banking Supervision, January 1996 page 51 & 52)

1. A bank may have the following positions:

- Qualifying bond, \$ 13.33 mn market value, residual maturity 8 years, coupon 8%;
- Government bond, \$ 75 mn market value, residual maturity 2 months, coupon 7%;
- Interest rate swap, \$ 150 mn¹ bank receives floating rate interest and pays fixed, next interest fixing after 9 months, residual life of swap 8 years;
- Long position in interest rate future, \$ 50 mn¹, delivery date after 6 months, life of underlying government security 3.5 years.

2. Table- 3 shows how these positions are slotted into the time-bands and are weighted according to the weights given in Table 1 of A.1. After weighting the positions the next steps in the calculation will be:

(a) The *vertical disallowance* in time-band 7-10 years has to be calculated: The matched position in this time-band is 0.5 (the lesser of the absolute values of the added (weighted) long and (weighted) short positions in the same time-band) which leads to a capital charge of 5% of 0.5 = 0.05 = \$ 25,000. The remaining net (short) position is -5.125.

(b) The *horizontal disallowances within the zones* have to be calculated: As there is more than one position only in zone 1, a horizontal disallowance can only be calculated in this zone. In doing this, the matched position is calculated as 0.2 (the lesser of the absolute values of the added long and short positions in the same zone). The capital charge for the horizontal disallowance within zone 1 is 40% of 0.2 = 0.08 = \$ 80,000. The remaining net (long) position in zone 1 is +1.00.

(c) The *horizontal disallowances between adjacent zones* have to be calculated: After calculating the net position within zone 1 the following positions remain: zone 1

+1.00, zone 2 +1.125, zone 3 -5.125. The matched position between zones 2 and 3 is 1.125 (the lesser of the absolute values of the long and short positions between adjacent zones) The capital charge in this case is 40% of 1.125 = 0.45 = \$ 450,000.

(d) The *horizontal disallowance between zones 1 and 3* has to be calculated: The remaining net (long) position in zone 1 is +1.00, in zone 3 the net (short) position is -4.00. If there were no offsetting between zones 1 and 3 allowed the capital charge would be 5.00 = \$ 5,000,000. However, the horizontal disallowance between the distant zones is 100% of the matched position which leads to a capital charge of 100% of 1.00 = 1.00 = \$ 1,000,000.

(e) The overall net position is 3.00 leading to a capital charge of \$ 3,000,000.

¹ The position should be reported as the market value of the notional underlying. Depending on the current interest rate, the market value of each leg of the swap (i.e., the 8 year bond and the 9 months floater) can be

either higher or lower than the notional amount. For sake of simplicity the example assumes that the current interest rate is identical with the one the swap is based on.

Table- 3

(\$ mn)

	Zone 1				Zone 2			Zone 3					
Time-band	0-1	1-3	3-6	6-12	1-2	2-3	3-4	4-5	5-7	7-10	10-15	15-20	over 20
	Months				Years								
Position		+75 Gov.	-50 Fut.	+150 Swap			+50 Fut.			-150 Swap +13.33 Qual.			
Weight (%)	0.00	0.20	0.40	0.70	1.25	1.75	2.25	2.75	3.25	3.75	4.50	5.25	6.00
Position x Weight		+0.15	-0.20	+1.05			+1.125			-5.625 +0.5			
Vertical Disallow.										0.5 x 10% = 0.05			
Horizont. Disallow. 1	0.20 x 40% = 0.08												
Horizont. Disallow. 2					1.125 x 40% = 0.45								
Horizont. Disallow. 3	1.0 x 100% = 1.0												

3. The total capital charge in this example is:

- for the vertical disallowance	\$	50,000
- for the horizontal disallowance in zone 1	\$	80,000
- for the horizontal disallowance between adjacent zones	\$	450,000
- for the horizontal disallowance between zones 1 and 3	\$	1,000,000
- for the overall net open position	\$	<u>3,000,000</u>
	\$	4,580,000

Note- Vertical Disallowance under section 2 (a) is 5%. Accordingly, Vertical Disallowances in the Table- 3 and capital charge in the section 3 above to be adjusted.

Weights in the Table-3 are respective price sensitivities.

CAPITAL ADEQUACY FOR COUNTER PARTY CREDIT RISK

PDs are required to arrive at the credit equivalent amount for the purpose of reckoning exposure to a counter party on. For this purpose, PDs should consider the market value of respective repo/rev.repo to find out the net exposure of the investment.

Step 1

The net exposure of the repo and rev. repo find out using the following formulae.

$$\text{Repo} = (\text{market value} - \text{leg 1})$$

$$\text{Rev.repo} = (\text{leg 1} - \text{market value})$$

Step 2

The net exposure thus obtained shall be multiplied by the risk weightage allotted to the relevant counter-party as specified below:

1. Government/guaranteed by the government	0%
2. Banks/PDs, EPF and ETF	20%
3. Insurance companies, provident funds	50%
3. Corporates	75%
4. Others	100%

Step 3

Capital utilization by counterparty is obtained using the following formulae. It is clear that same security used for repo and rev. repo transaction would have only one-way exposure for calculation.

$$\text{Repo} = (\text{market value} - \text{leg 1}) * \text{risk weight} * 8\%$$

$$\text{Rev.repo} = (\text{leg 1} - \text{market value}) * \text{risk weight} * 8\%$$

Risk Weighted Capital Adequacy - Calculation

Capital Charge	Trading Portfolio	=	Table 1 ,	Modified Duration * Assumed Changes in yield rates% * Market Value
	Reverse Repo	=	Table 2 ,	Modified Duration * Assumed Changes in yield rates% * Market Value
	Disallowances	=	As Seen in Table 3	
Trading Portfolio	→		To calculate Modified Duration, identical security maturity considered	
Reverse Repo	→		To calculate Modified Duration, Rev.Repo maturity considered	
Capital Utilization by Counterparty Credit				
	Reverse Repo	=	Table 4 ,	(Leg 1 - Market Value) * Risk weight% * 8%
	Repo	=	Table 5 ,	(Market Value - Leg 1) * Risk weight% * 8%

Yield Rates and Counterparty risk weights use for calculations

1) For Capital Charge

Assumed Change in Yield (Basel)	Time Period
3.00%	1 month (or less)
3.00%	1 to 3 months
3.00%	3 to 6 months
3.00%	6 to 12 months
2.70%	1 to 2 years
2.40%	2 to 3 years
2.25%	3 to 4 years
2.25%	4 to 5 years
2.10%	5 to 7 years
1.95%	7 to 10 years
1.80%	10 to 15 years
1.80%	15 to 20 years
1.80%	Over 20 years
1.80%	

2) Counter Party Risk

Counter Party	Risk Weight
Government and Government guaranteed	0%
Banks / PDs, EPF and ETF	20%
Insurance Companies & Approved Provident Funds	50%
Corporates	75%
Others	100%

Name of the PD:
Capital Adequacy Report as at

Amounts in Rs million

		* Risk Weighted Assets
1. Available Capital	0.0	
2 Less : Capital utilization by Counterparty credit	0.0	-
3. Net Capital (1+ 2)	0.0	
4. Capital Charge For Trading & Reverse Repo	0.0	
5. Capital charge for disallowances	0.0	
6. Total Capital Charge (4+5)	0.0	0.00
7. Regulatory Minimum Capital	300	
8. Unused Capital (3 - 6) if 3>=6	0.0	
9. Required minimum capital (higher of Rs. 300 M or sum of capital charge and counter party risk)	300	
10. Whether the total Capital in excess of required minimum capital	0	
11. Npv of Portfolio (Trading & Reverse Repo)	0.0	
12.Total Risk Weighted Capital (Capital charge+Counterparty risk+capital for disallowances)	0.0	
13.Risk weighted other assets (Weighted Assets in balance sheet without trading portfolio and reverse repo)		0.0
14.Total Risk Weighted Assets (2+6+13)		0.0
15.Risk Weighted Capital Adequacy Ratio (Minimum 8%) 1/14		0.0%

*** Risk Weighted Assets**

Amounts in Rs million

1. Capital Charge For Trading & Reverse Repo	-	
2.Capital charge for Disallowances	-	
3.Risk weighted Assets for total Capital Charge	(1+2)/8%	-
4.Risk Weighted Assets for Counter Party		-
5.Risk weighted other assets (Weighted Assets in balance sheet without trading portfolio and reverse repo)		-
6.Total Risk Weighted Assets	3+4+5	-
7.Available Capital		-
8.Risk Weighted Capital Adequacy Ratio (Minimum 8%)	7/6	0.0%

Capital Charge

Settlement Date

Trading Portfolio

Table 1

Amounts in Rs Millions

Market Value	Security Maturity Date	Coupon Rate	Yield Rate	Mduration	Remaining Maturity Days (Maturity Date-Settlement Date)	Assumed Change in Yield	Capital Charge (Market Value * Mduration * Assume change in yield)
Trading Bonds							
						Total	
Trading Bills							
						Total	
Forward Purchases							
						Total	
- Short sellings							
						Total	
Total NPV((Trading Bonds+Trading Bills+Forward Purchases -Short Sellings)							
Total Capital charge for Trading Portfolio (Trading Bonds+Trading Bills+Forward Purchases -Short Sellings)							-

Reverse Repo

Table 2

Amounts in Rs Millions

Market Value	Rev.Repo Maturity Date	Security Maturity Date	Coupon Rate	Yield Rate	Mduration	Remaining Maturity Days (Maturity Date-Settlement Date)	Assumed Change in Yield	Capital Charge (Market Value * Mduration * Assume change in yield)
-								-

NPV of Trading & Reverse Repo

-

Total Capital Charge for trading portfolio and reverse repo

-

Capital Charge For Disallowances

Rs Mn

Time Band	Zone 1 (Months)				Zone 2 (Years)			Zone 3 (Years)					
	0-1	1-3	3-6	6-12	1-2	2-3	3-4	4-5	5-7	7-10	10-15	15-20	Over 20
	<=1	3<=X >1	6<=X >3	12<=X >6	2<=X >1	3<=X >2	4<=X >3	5<=X >4	7<=X >5	10<=X >7	15<=X >10	20<=X >15	20>
Positions	0	275	150	75	25	50.45	0	150	45.14	100	0	75	0
	0	0	-75	-100	-275	0	0	-125	0	0	0	0	0
Weights %	0.00	0.20	0.40	0.70	1.25	1.75	2.25	2.75	3.25	3.75	4.50	5.25	6.00
Position*Weights		0.55	0.60	0.53	0.31	0.88		4.13	1.47	3.75		3.94	
			-0.30	-0.70	-3.44		0.00	-3.44					
Position*Weights (ABS)		0.55	0.60	0.53	0.31	0.88		4.13	1.47	3.75		3.94	
			0.30	0.70	3.44			3.44					

Verticle Dissallowances

Zone 1	3-6	0.3*5%	0.02
	6-12	0.525*5%	0.03
Zone 2	1-2	0.313*5%	0.02
Zone 3	4-5	3.44*5%	0.172
Total Verticle Disallowances			<u><u>0.23</u></u>

Horizontal Disallowances (Within the Zones)

Time Band	Zone 1 (Months)				Zone 2 (Years)			Zone 3 (Years)					
	0-1	1-3	3-6	6-12	1-2	2-3	3-4	4-5	5-7	7-10	10-15	15-20	Over 20
	>=1	1 >=3	3 >=6	6 >=12	1 >=2	2 >=3	3 >=4	4 >=5	5 >=7	7 >=10	10 >=15	15 >=20	<20
Position*Weights		0.55	0.60	0.53	0.31	0.88		4.13	1.47	3.75		3.94	
			-0.30	-0.70	-3.44		0.00	-3.44					
Net Total	0.00	0.55	0.30	-0.18	-3.13	0.88	0.00	0.69	1.47	3.75	0.00	3.94	0.00
Positives		0.85			0.88			9.84					
Negatives		-0.18			-3.13			0.00					

Zone 1	0.18*40%	0.07
Zone 2	0.88*30%	0.26
Total Horizontal Disallowances (Within)		<u><u>0.33</u></u>

Horizontal Disallowances (Inter Zones)

Time Band	Zone 1 (Months)				Zone 2 (Years)			Zone 3 (Years)					
	0-1	1-3	3-6	6-12	1-2	2-3	3-4	4-5	5-7	7-10	10-15	15-20	Over 20
	>=1	1 >=3	3 >=6	6 >=12	1 >=2	2 >=3	3 >=4	4 >=5	5 >=7	7 >=10	10 >=15	15 >=20	<20
Position*Weights	0.00	0.55	0.60	0.53	0.31	0.88	0.00	4.13	1.47	3.75	0.00	3.94	0.00
	0.00	0.00	-0.30	-0.70	-3.44	0.00	0.00	-3.44	0.00	0.00	0.00	0.00	0.00
Total		0.68			-2.24			9.84					
Total(ABS)		0.68			2.24			9.84					

Zone 1-2	0.68*40%	0.27
Zone 2-3	Remaining	
	Zone 2 2.24+0.68 =-1.567 min	
	Zone 3 9.84 (1.567*40%)	0.63
Total Horizontal disallowances (Inter Zones)		<u><u>0.90</u></u>

Total Disallowances

Verticle Dissallowances+ Horizontal Disallowances (Within the Zones) +Horizontal Disallowances (Inter Zones)

1.4605

Capital Charge for Disallowances

Rs Mn

Time Band	Position		Weight%	Position*Weight				Verticle Disallowances				Horizontal Disallowances (Within the Zones)		Horizontal Disallowances-Inter zone						
	Long	Short		Long*weight	Short*weight	Net Total	Net Total Absolute	Absolute		MIN(Long & Short)	Verticle Disallowances	Net Minimum	Min*%	Inter Zone						
								LONG	SHORT					Net Total	Absolute	Minimum	Rate	Capital Charge	Remaining	
Zone 1 (Months)	0-1		0.00%	0.000	0.000	0.000	0.000	0.000	0.000	0.000	0	0.000	0	1-2,1-3						
	1-3		0.20%	0.000	0.000	0.000	0.000	0.000	0.000	0	0 0									
	3-6		0.40%	0.000	0.000	0.000	0.000	0.000	0.000	0.0000	1-2									
	6-12		0.70%	0.000	0.000	0.000	0.000	0.000	0	Zone 1 0.000 0.000 0.000 0.400 0.000 0.000 Zone 2 0.000 0.000 0.000 0.000 0.000 0.000										
				Total	0.000	0.000	0.000	0.000	0.000	0			1-3							
				Positives			0.000	0.000						Zone 1 Remaining 0.000 0.000 0.000 1.000 0.000 0.000 Zone3 0.000 0.000 0.000 0.000 0.000						
				Negatives			0.000	0.000						1-2,2-3						
Zone 2 (Years)	1-2		1.25%	0.000	0.000	0.000	0.000	0.000	0.000	0	0.000	0	1-2							
	2-3		1.75%	0.000	0.000	0.000	0.000	0.000	0	0 0										
	3-4		2.25%	0.000	0.000	0.000	0.000	0.000	0	Zone 1 0.000 0.000 0.000 0.400 0.000 0.000 Zone 2 0.000 0.000 0.000 0.400 0.000 0.000										
				Total	0.000	0.000	0.000	0.000	0.000	0			2-3							
				Positives			0.000	0.000						Zone2 Remaining 0.000 0.000 0.000 0.400 0.000 0.000 Zone3 FALSE 0.000 0.000 0.000 0.400 0.000 0.000						
				Negatives			0.000	0.000						2-3,1-3						
Zone 3 (Years)	4-5		2.75%	0.000	0.000	0.000	0.000	0.000	0.000	0	0.000	0.000	2-3							
	5-7		3.25%	0.000	0.000	0.000	0.000	0.000	0	Zone 2 0.000 0.000 0.000 0.400 0.000 0.000 Zone 3 0.000 0.000 0.000 0.400 0.000 0.000										
	7-10		3.75%	0.000	0.000	0.000	0.000	0.000	0.00	1-3										
	10-15		4.50%	0.000	0.000	0.000	0.000	0.000	0	Zone 3 Remaining 0.000 0.000 0.000 1.000 0.000 0.000 Zone1 0.000 0.000 0.000 0.400 0.000 0.000										
	15-20		5.25%	0.000	0.000	0.000	0.000	0.000	0	1-3										
	over 20		6.00%	0.000	0.000	0.000	0.000	0.000	0	Zone 3 Remaining 0.000 0.000 0.000 1.000 0.000 0.000 Zone1 0.000 0.000 0.000 0.400 0.000 0.000										
				Total	0.000	0.000	0.000	0.000	0.000	0.000			1-3							
				Positives			0.000	0.000						Zone 3 Remaining 0.000 0.000 0.000 1.000 0.000 0.000 Zone1 0.000 0.000 0.000 0.400 0.000 0.000						
				Negatives			0.000	0.000						0.000						

	Rs mn
Verticle Disallowance	-
Horizontal Disallowance -Within the Zone	-
Horizontal disallowance -Inter Zones	-
	-

Counterparty Risk For Repo and Reverse Repo

Settlement Date

Reverse Repo

Table 4

Amounts in Rs millions

Leg 1 Value	Security Market Value	Security Maturity Date	Remaining Maturity (Days)	Counterparty	Counterparty Weight	Net Value (Leg 1- Market Value)	Net Value (only positive Values)	Risk weighted Assets for Counterparty risk (Net Value*Weight)	Counterparty risk (Net Value*Weight *8%)
0.00	0.00								-

Repo

Table 5

Amounts in Rs millions

Leg 1 Value	Security Market Value	Security Maturity Date	Remaining Maturity (Days)	Counterparty	Counterparty Weight	Net Value ((Market Value-Leg 1)	Net Value (only positive Values)	Risk weighted Assets for Counterparty risk (Net Value*Weight)	Counterparty risk (Net Value*Weight *8%)
0.00	0.00								-

Total Counterparty Risk for reverse repo and repo

-

Total Risk weighted Assets for Counterparty risk (repo & reverse repo)

-

Risk Weighted Other Assets

Table 6

Rs Mn

	As per Balance Sheet	Weight %	Risk Weighted Assets
Balance with Central Bank		0%	
Cash in Hand and with Banks		0%	
Cash with Custodial Agent		0%	
Securities Purchased under agreements to resell		-	
Trading Securities		-	
Investment Securities		100%	
Trading Receivables		100%	
Fails to Deliver		100%	
Securities with Custodial Agent		100%	
Principal and Interest Receivable		100%	
Accounts Receivable		100%	
Loans and Advances		100%	
Investment in Subsidiaries		100%	
Fixed Assets (net of depreciation)		100%	
Other Assets (net)		100%	
Total Assets	-		

June 22, 2006

To: Chief Executive Officers of Primary Dealers,

Direction On Risk Weighted Capital Adequacy Framework (RWCAF) for Primary Dealers (PDs)

This direction is issued in terms of section 12 of the Regulation No.01 of 2002 dated February 1,2002 issued by the Minister of Finance under the Registered Stock and Securities Ordinance and the Local Treasury Bills Ordinance.

1. With effect from July 01, 2006 PDs are required to maintain:

- a. A required minimum capital which is the higher of Rs.300 million (minimum capital) or the capital sufficient to meet the interest rate sensitivity of the trading portfolio including reverse repos and risk on disallowances (capital charge), and counterparty credit risk;
- b. Net capital [Capital (Tier I and Tier II) minus capital for counter party risk], which should be equal to or higher than the capital charge; and
- c. A minimum risk weighted capital adequacy ratio (CAR) of 8%

The methodology of calculating sensitivity of the PD portfolios to an assumed change in yields along with the risk exposure for long/short positions (capital charge), and counterparty credit risk requirement are given in Schedule 1 &2.

2. PDs are required to comply with the following regulatory requirements for reporting of capital adequacy with effect from July 01, 2006.

All PDs are required to report the positions of their capital adequacy in the specified format on a monthly basis, which is given in Schedule 3 in electronic format (via email/soft copy). The reporting format for the respective month has to be completed by each PD and submitted to the Public Debt Department (PDD) on or before 15th of the subsequent month. These reporting formats would cover, inter alia,

- a. Whether the minimum absolute capital requirement is being satisfied; and
- b. Whether the CAR is above or below its required minimum capital adequacy ratio.

