

Guidelines on Commercial Paper for Banks



Bangladesh Bank

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1. Introduction

Commercial paper (CP) is a short term money-market security issued/sold by usually large corporations for financing working capital such as account receivables and inventories.

As an alternative to bank financing, commercial paper market is experiencing rapid growth in Bangladesh for the last couple of years. It promotes diversification of sources of funds in the economy as well as competitiveness of the financial sector.

Bangladesh Bank (BB), as the central bank of Bangladesh, has the statutory task of regulating and supervising the financial system of Bangladesh. In order to deepen and facilitate the effective and efficient functioning of the money market, it is desirable that participants practice uniform and standard procedures. These guidelines are issued to introduce a regulatory framework for banks when dealing with commercial paper. The guidelines also serve to clarify the regulatory expectations on the risk management issues related to commercial paper.

2. Definitions

For the purpose of these guidelines, unless the context otherwise states:

- a) **Commercial Paper (CP)** is defined as a secured/ unsecured promissory note which has an original maturity between a minimum of seven days and a maximum of one year.
- b) **Credit Enhancements** means credit facilities provided in relation to the issuance of Commercial Paper.
- c) **Issuing and Paying Agent (IPA)** means a bank that delivers CPs to the investors against the proof of payment and at maturity repays the investors after receiving funds from the issuer.
- d) **Investor** means a person/institution that purchases CPs.
- e) **External Credit Assessment Institution (ECAI)** is a credit rating agency registered with Bangladesh Securities & Exchange Commission.

3. Permissible activities for banks

Banks are allowed to invest in CPs, provide credit enhancements to CP issuers and act as an IPA of CPs in the manner set forth in this guideline. However, Banks shall not issue CP in any form or provide any guarantee for CPs.

4. General Instructions:

Banks shall ensure that the following conditions are fulfilled when they act as an investor, an IPA and provide credit enhancements:

- a) The banks shall have written guidelines approved by their Board of Directors for dealing with CPs.
- b) Banks shall obtain and examine the following documents from the intending CP issuers:
 - i. A written request indicating the nature of support sought along with board resolution for the issue of CP;
 - ii. Detailed company profile;
 - iii. Comprehensive financial information including a projected cash flow statement;
 - iv. The value of CP already issued and outstanding;
- c) The net worth of the issuer shall not be less than BDT 30 crore as per the latest audited balance sheet and the net profit after tax shall be positive for the last three (3) years.
- d) The current status shown in the Credit Information Bureau (CIB) report of the issuer company shall be 'standard' and have no track record of classified status for last two (2) years.
- e) The issuer shall have credit rating from an ECAI. The minimum credit rating of the issuer shall not be lower than BB Rating Grade-"2" and "S2" (short-term) as per Risk Based Capital Adequacy (in line with Basel III) guidelines.
- f) Accounting and reporting of investment in CPs should be in line with applicable standards; and support in the form of credit enhancements should be accounted for accordingly.
- g) Banks shall follow the instructions regarding Credit Risk Management Guidelines, Risk Management Guidelines and all other related prudential policies issued by Bangladesh Bank from time to time.

5. Specific Guidelines for Issuing And Paying Agent (IPA)

- a) All certified copies of original documents shall be held in the custody of IPA.
- b) In the offering document, IPA shall make it clear to the investors that the respective CP is subject to credit and other related risks as well as not protected under Deposit Insurance Act, 2000.
- c) In the offering document, it shall be clearly stated that the payment will be made to the investors provided that the issuer has made the funds available to IPA.
- d) IPA is required to inform the prospective investors that in case of default, it will not be held responsible for seeking recovery from the issuers or initiating any action against the issuer on its own or on behalf of the investors.
- e) If the issuer fails to pay, partially or in full, the IPA shall be held responsible to notify the matter of such default to the investors without any delay.
- f) The IPA shall distribute the received funds as per terms and conditions of the underlying agreements if the issuer makes the partial payment.
- g) IPA shall not invest in the respective CP.

6. Specific Guidelines for investment in CP by banks

- a) Before investment to any CP, Banks should assess the issuer's overall debt repayment capacity by taking into consideration the issuer's liabilities with other banks and financial institutions to make sure that the issuer has the ability to repay;
- b) The current ratio of the issuer must be at least 1:1 as per latest audited balance sheet;
- c) The debt-equity ratio of the issuer must be maximum 70:30 as per latest audited balance sheet;
- d) Banks investment in a single issue of CP shall not exceed 20% of the respective issue.
- e) Banks aggregate investment in commercial papers at any point of time cannot exceed 10% of its Tier 1 capital.
- f) Rollover of CP shall be treated as a fresh issue and require complying with all the applicable clauses. Rollover is limited to maximum one time.
- g) Banks shall maintain provision against outstanding balance of the defaulted CPs at the following rates:
 - i. If it is past due/overdue for 03 (three) months or beyond but less than 06 (six) months, the provision requirement is 20%.

- ii. If it is past due/overdue for 06 (six) months or beyond but less than 09(nine) months, the provision requirement is 50%.
 - iii. If it is past due/overdue for 09 months or beyond the provision requirement is 100%.
- h) Endorsements made by the banks on the subsequent purchasers of their holding of CPs shall be strictly on “without recourse” basis.
 - i) Banks investment in an issuer’s CP shall be considered as a ‘funded exposure’ to the issuing company as per BRPD Circular No. 02/2014 on Single Borrower Exposure Limit and any amendments thereafter. Banks shall consider the exposure of the issuing company irrespective of CP being Credit enhanced or not.
 - j) Banks shall not invest in any CP issued by ‘Bank Related Persons’ as defined in section 26Ga of Bank Company Act, 1991 (amended up to 2013).
 - k) Banks shall not purchase/ invest in CPs issued by Non Bank Financial Institutions (NBFI).

7. Specific Guidelines for providing credit enhancement

- a) Banks may, after assessing the issuer’s overall debt repayment capacity by taking into consideration the issuer’s liabilities with other banks and financial institutions, choose to provide credit enhancements by way of standby line of credit, backstop facilities etc.
- b) While providing the above mentioned facilities, banks shall comply with all the legal and regulatory requirements and prudential norms as applicable to them.
- c) Banks shall follow the BRPD Circular No. 02/2014 on Single Borrower Exposure Limit and any amendments thereafter for providing such credit enhancements.

8. Reporting Format:

Details of bank’s involvements in CPs shall be reported to the Department of Offsite Supervision as per Annexure -1 on a quarterly basis or any amendment made therein by that department. The report shall also include information of CPs redeemed within the reporting quarter.

Annexure -1

Name of Bank:
Quarterly Statement of Commercial Paper
 From.....to.....

Amount in core

Issuing company details			Credit Rating of issuer (short & long)	Nature of support	Size of the issue (Face Value)	Amount Subscribed by bank	Amount of credit enhancement	Rate of Interest (%)	Date of Issue (YY/MM/DD)	Date of Maturity (YY/MM/DD)	Present Status of the issue	Existing facilities to the CP issuer (if any)		Capital of the bank
Name	Current Ratio	Debt-Equity Ratio										Funded	Non Funded	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15

Notes:

Column 4: BB equivalent Credit rating of the issuer as per Risk Based Capital Adequacy (in line with Basel III) guidelines.

Column 5: Please indicate using the following Code: Invest - (IN), Issuing & Paying Agent-(IPA), Credit Enhancements - (CE).

Column 6: Total Face value of the respective CP.

Column 7: Please put the value of total amount subscribed/purchased by the bank

Column 8: If the bank is credit enhancement provider: total amount of credit enhancements provided against the respective CP.

Column 9: The interest rate of respective CP.

Column 12: Please indicate following status of the issue:

- a) Redeemed
- b) Not Matured
- c) Defaulted
- d) Rolled over

Column 15: Please put the value of capital held by banks as per clause (1) of section 13 of the Banking Companies Act, 1991 (amended up to 2013).