



पेंशन निधि विनियामक और  
विकास प्राधिकरण

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**PENSION FUND REGULATORY  
AND DEVELOPMENT AUTHORITY**

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## CIRCULAR

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### **Subject: Proper Due Diligence by Pension Funds before making Investments in Corporate Securities**

The Pension funds are allowed to invest in various asset classes including Corporate Bonds in accordance with the investment guidelines issued by the Authority from time to time. As per the investment guidelines, it has been emphasized that the prudent investment of funds within the prescribed pattern is the responsibility of the pension fund and fiduciary duty of NPS Trust which needs to be exercised with proper credit appraisal utmost due diligence.

2. In case of investment in any financial asset, due diligence including proper credit appraisal has to be carried out to assess the risk associated with any particular security/ bond before investment is made by the fund. The risks analyzed should include, inter alia, credit risk, liquidity risk and solvency risk amongst others. Although the requirement of rating has been maintained in the investment guidelines, however complete reliance on the credit ratings should not be a substitute for a comprehensive investment due diligence. The minimum credit rating stipulations are merely intended to limit the risk associated with investments at a broad and general level. Accordingly, it should not be construed in any manner as an endorsement for investment in any asset satisfying minimum prescribed rating or substitute for the due diligence to be carried out by the fund.

3. A complete documentation of the analysis and assessment and due diligence done along with all backing documents, references and research needs to be maintained by the Pension Funds at all times for scrutiny by the Authority or the Auditors etc. The documentation should amongst others deliberate upon the macro economic scenario, the sectoral analysis, the adherence to prudential guidelines stipulated by the Authority, any internal risk management limits stipulated by the Board of Pension Funds, the detailed analysis of the securities sought to be invested in, including the financials, the management of the issuer company etc. As the investments into the corporate bonds necessarily entail credit risk and liquidity risk, therefore the company's liquidity position and other parameters such as liquid investment or cash balances excess to unutilized credit lines, liquid coverage ratio and adequacy of cash flows for servicing maturing debt obligation, need to be analyzed. The PFM should also analyze the deterioration of liquidity and also check the asset liability

mismatch. The PFM should not merely rely on the parentage of the company but rather emphasize on analysis of financial and other parameters. The asset liability management of the issuer company concern should be an important factor while making the decision to invest. The parameters mentioned in this paragraph are illustrative and not exhaustive and a detailed process note is to be developed by each Pension Fund under the guidance of its Board.

4. All the corporate bond portfolio needs to reviewed periodically by the pension funds for all its current holding to satisfy itself about continuing to hold the securities/Bonds. If any of the instruments held by the Pension funds falls below the minimum permissible investment grade prescribed for investment in that instrument when it was purchased, as confirmed by one credit rating agency, the option of exit shall be considered and exercised, as appropriate, in a manner that is in the best interest of the subscribers.

5. The Pension Funds need to develop robust risk management teams headed by Chief Risk Officer and use necessary tools to enable prudential investment which optimize risk adjusted return for the subscriber. The Chief Risk Officer will report to the risk management committee which in turn is accountable to the Board of the Pension Fund.

6. The Pension Funds shall ensure that in case of a downgrade/default or an asset becoming a non-performing asset the Pension Funds must have a robust system of follow up with the issuer with regular reporting to their respective Boards for timely action for recovering the maximum dues from the issuer.



**(Sumeet kaur Kapoor)**  
**Chief General Manager**