Press Information Bureau
Government of India
Ministry of Finance

09-September-2015 14:49 IST

Introduction of Sovereign Gold Bonds Scheme

The Union Cabinet chaired by the Prime Minister, Shri Narendra Modi, today gave its approval for introduction of the Sovereign Gold Bonds Scheme, as announced in the Union Budget 2015-16.

The scheme will help in reducing the demand for physical gold by shifting a part of the estimated 300 tons of physical bars and coins purchased every year for Investment into gold bonds. Since most of the demand for gold in India is met through imports, this scheme will, ultimately help in maintaining the country's Current Account Deficit within sustainable limits.

The issuance of the Sovereign Gold Bonds will be within the government's market borrowing programme for 2015-16 and onwards. The actual amount of issuance will be determined by RBI, in consultation with the Ministry of Finance. The risk of gold price changes will be borne by the Gold Reserve Fund that is being created. The benefit to the Government is in terms of reduction in the cost of borrowing, which will be transferred to the Gold Reserve Fund.

The salient features of the scheme are:-

i. Sovereign Gold Bonds will be issued on payment of rupees and denominated in grams of gold.

ii. Bonds will be issued on behalf of the Government of India by the RBI. Thus, the Bonds will have a sovereign guarantee.

iii. The issuing agency will need to pay distribution costs and a sales commission to the intermediate channels, to be reimbursed by Government.

iv. The bond would be restricted for sale to resident Indian entities. The cap on bonds that may be bought by an entity would be at a suitable level, not more than 500 grams per person per year.

v. The Government will issue bonds with a rate of interest to be decided by the Government. The rate of interest will take into account the domestic and international market conditions and may vary from one tranche to another. This rate of interest will be calculated on the value of the gold at the time of investment. The rate could be a floating or a fixed rate, as decided.

vi. The bonds will be available both in demat and paper form.

vii. The bonds will be issued in denominations of 5,10,50,100 grams of gold or other denominations.

viii. The price of gold may be taken from the reference rate, as decided, and the Rupee equivalent amount may be converted at the RBI Reference rate on issue and redemption. This rate will be used for issuance, redemption and LTV purpose and disbursement of loans.

ix. Banks/NBFCs/Post Offices/ National Saving Certificate (NSC) agents and others, as specified, may collect money / redeem bonds on behalf of the government (for a fee, the amount would be as decided).

x. The tenor of the bond could be for a minimum of 5 to 7 years, so that it would protect investors from medium term volatility in gold prices. Since the bond, will be a part of the sovereign borrowing, these would need to be within the fiscal deficit target for 2015-16 and onwards.

xi. Bonds can be used as collateral for loans. The Loan to Value ratio is to be set equal to ordinary gold loan mandated by the RBI from time to time.

xii. Bonds to be easily sold and traded on exchanges to allow early exits for investors who may so desire.

xiii. KYC norms will be the same as that for gold.

xiv. Capital gains tax treatment will be the same as for physical gold for an 'individual' investor. The Department of Revenue has agreed that amendments to the existing provisions of the Income Tax Act, for providing 'indexation benefits to long term capital gains arising on transfer of bond'; and for 'exemption for capital gains arising on redemption of SGB' will be considered in the next budget (Budget 2016-17).This will ensure that an investor is indifferent in terms of investing in these bonds and in physical gold- as far as tax treatment is concerned.

xv. The amount received from the bonds will be used by GoI in lieu of government borrowing and the notional interest saved on this amount would be credited in an account "Gold Reserve Fund" which will be created. Savings in the costs of borrowing compared with the existing rate on government borrowings, will be deposited in the Gold Reserve Fund to take care of the risk of increase in gold price that will be borne by the government. Further, the Gold Reserve Fund will be continuously monitored for sustainability.

xvi. On maturity, the redemption will be in rupee amount only. The rate of interest on the bonds will be calculated on the value of the gold at the time of investment. The principal amount of investment, which is denominated in grams of gold, will be redeemed at the price of gold at that time. If the price of gold has fallen from the time that the investment was made, or for any other reason, the depositor will be given an option to roll over the bond for three or more years.

xvii. The deposit will not be hedged and all risks associated with gold price and currency will be borne by GoI through the Gold Reserve Fund. The position may be reviewed in case 'Gold Reserve Fund' becomes unsustainable.

xviii. Upside gains and downside risks will be with the investor and the investors will need to be aware of the volatility in gold prices.

xix. In order to ensure wide availability, the bond will be marketed through post offices/banks/NBFCs and by various brokers/agents (including NSC agents) who will be paid a commission.

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