

## **RBI Regulations for NBFCs**

Ref.DNBS(PD).CC.No.19/02.01/2001-02

April 22, 2002

To

All Non-Banking Financial Companies  
including Mutual Benefit Financial Companies,  
Mutual Benefit Companies,  
Residuary Non-Banking Companies and  
Miscellaneous Non-Banking Companies

Dear Sirs,

### **RBI Regulations for NBFCs**

As you are aware that the RBI prescribed prudential norms for Non-Banking Financial Companies, vide Notification No.DFC.119/DG(SPT)-98 dated January 31, 1998. These directions were last revised on January 1, 2002. These norms are almost akin to those applicable to banks and financial institutions.

2. In the light of certain developments in the operations of the NBFCs and the need to improve the norms for this sector, it has been decided to modify these norms as per details given hereunder :

#### **(1) Policy on call/demand loans**

(i) It has been observed that some NBFCs were granting demand/call loans with an open period or without any stipulation regarding the rate of interest and servicing due to which difficulty was being experienced in ensuring compliance with prudential norms on income recognition, asset classification and provisioning in respect of such loans. In order to obviate this difficulty and to ensure that all such loans are appropriately classified and the position of non-performing assets is truly reflected in the financial statements of NBFCs, the following directions are issued:

- (A) all NBFCs granting/intending to grant demand/call loans should lay down a policy therefor duly approved by their Board of Directors. The policy should cover the following aspects :
- (a) stipulation of a cut off date within which the repayment of the loan will be demanded/called up. If the cut off date is beyond one year, specific reasons to be recorded by the sanctioning authority;
  - (b) stipulation of the rate of interest and the periodic rests for payment of interest, which shall be at quarterly/monthly intervals. Where no interest is levied or a moratorium is granted, specific reasons to be recorded by the sanctioning authority;
  - (c) stipulation of a cut off date, not exceeding six months from date of sanction of the loan, for review of the performance of the loan; and
  - (d) such loans shall be renewed based on a review covering satisfactory compliance with the terms of sanction.
- (B) all such loans remaining overdue for 6 months from the date of demand/call or loans where interest remained past due for a period of 6 months from the due date would be classified, as non-performing assets.
- (C) The provisioning requirements as applicable to loans, advances and other credit facilities would be applicable to such loans.

(ii) These directions were communicated through a press release on March 4, 2002 and are effective from March 31, 2002 for both the existing and fresh loans. The amending notification is enclosed.

**(2) Asset Classification – Concept of `Past Due' - Removal**

- (i) It has been decided, in consultation with the Informal Advisory Group on NBFCs, to abolish the concept of `past due' from the definition of NPA for NBFCs since the prudential norms for NBFCs are similar to those applicable to commercial banks. Accordingly, the words `past due' wherever appearing in the definition of `non-performing asset' in paragraph 2(1)(xii) of the Non-Banking Financial Companies Prudential Norms (Reserve Bank) Directions, 1998 would be substituted by the words `overdue'. Further, term loan would become NPA when

instalment is overdue for six months instead of 'overdue for more than six months'. Similarly, the Lease and HP assets would also become NPA, if rentals/instalments are overdue for a period of twelve months instead of 'overdue for a period of more than twelve months'.

- (ii) These changes would come into effect from March 31, 2003 and the half yearly return on prudential norms as also the balance sheet as on March 31, 2003 should accordingly reflect the compliance therewith.

**(3) Objective criteria for classification of assets as loss assets**

- (i) In terms of paragraph 2(1) (viii) of the Prudential Norms Directions, the term 'loss asset' has been defined as under :

“(viii) “loss asset” means -

- (a) an asset which has been identified as loss asset by the NBFC or its internal or external auditor or by the Reserve Bank of India during the inspection of the NBFC, to the extent it is not written off by the NBFC; and
- (b) an asset which is adversely affected by a potential threat of non-recoverability due to either erosion in the value of security or non availability of security or due to any fraudulent act or omission on the part of the borrower.”

- (ii) During the course of inspection of some of the NBFCs, it was observed that the companies have been applying divergent yardsticks for identification of potential threat of non-recoverability and consequent classification of assets as loss assets. It is, therefore, clarified that occurrence of any of the following features in the account would be considered as potential threat to the recovery of the assets :

- (a) Non-availability of security either primary or collateral, in case of secured loans and advances.
- (b) Erosion in the value of the security (primary or collateral), is clearly established e.g. security is not marketable, realisable value of the security is not ascertainable or is negligible (less than 10% of outstanding in the account).

- (c) Insurance claim, if any, has been denied or settled in part, as apart from the security, recovery through insurance should be given due consideration.
- (d) Any fraudulent act or omission on the part of the borrower resulting in non-recoverability of the asset.
- (e) Inchoate or defective documentation or where debt is time barred, rendering enforcement impossible.
- (iii) It is further clarified that mere right of the company to file suit against borrower/ guarantor for recovery of dues does not debar the RBI / auditors from treating an asset or part thereof as loss on the above considerations.

**Other important issues**

3. It has been further decided as under :

**(1) Serious action in case of delinquency in submission of returns by NBFCs**

(i) The NBFCs have been directed to submit the following returns / data:

<b>Sr. No.</b>	<b>Type of return/clarifications/data</b>
(a)	Annual Return on deposits as on March 31 every year in form NBS 1 or 1A as may be applicable, to be submitted by September 30 of that year.
(b)	Half yearly return on Prudential Norms in form NBS 2 as on March 31 and September 30 every year, to be submitted by June 30/Decemember 31 respectively.
(c)	Quarterly return on liquid assets in form NBS 3 or 3A as may be applicable, within 15 days of the close of quarter.
(d)	Monthly Return on Repayment of Deposits in form NBS-4 (for NBFCs whose applications for certificate of registration have been rejected).
(e)	Copies of audited balance sheet and profit and loss account with a copy of the report of the Board of Directors as on the last date of each financial year as provided in <ul style="list-style-type: none"> <li>(i) Paragraph 8(1) of the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998</li> <li>(ii) Paragraph 10 of the Miscellaneous Non-Banking Companies (Reserve Bank) Directions, 1977</li> <li>(iii) Paragraph 15 of the Residuary Non-Banking Companies (Reserve Bank) Directions, 1987</li> </ul>
(f)	Auditors' Certificate as provided in paragraph 8 (2) of the Non-Banking

	Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998.
(g)	Auditors' certificate as provided in paragraph 6 (3) of the Residuary Non-Banking Companies (Reserve Bank) Directions, 1987 at quarterly intervals.
(h)	Quarterly Monetary and Supervisory Return in form NBS-5 by NBFCs holding public deposits of Rs. 20 crore or above, within 10 days of the close of quarter.
(i)	Special return /information as may be called for from time to time

(ii) It is observed that the NBFCs have been lax in timely submission of the returns to the Bank. It has, therefore, been decided to take action progressively against NBFCs for non-submission of returns. Such action may include imposing penalties as provided in the Reserve Bank of India Act, 1934 as also launching criminal proceedings against the errant companies, besides considering rejection/ cancellation of the Certificate of Registration. To start with, cases of NBFCs having public deposits of Rs. 50 crore and above and defaulting in submission of the returns are being taken up. This discipline will be extended to other NBFCs also in due course of time.

(iii) NBFCs including mutual benefit financial companies (notified nidhis), mutual benefit companies (potential nidhis), residuary non-banking companies (RNBCs) and miscellaneous non-banking companies (chit fund companies) are advised to ensure strict compliance with the requirement of submission of returns as applicable to them.

**(2) Mechanism for supervision of compliance with ALM guidelines**

(i) In terms of DNBS(PD) CC.No.15/02.01/2001-02 dated January 27, 2001, we had prescribed ALM guidelines for NBFCs having public deposits of Rs. 20 crore and above or asset size of Rs. 100 crore and above as the case may be. Such NBFCs were advised to form ALM Committee (ALCO) and to inform the regional office of the Bank, under whose jurisdiction the registered office of the company is located, of the constitution of the Committee before October 31, 2001. The guidelines have become fully operational as on March 31, 2002. It is expected that such NBFCs have taken adequate steps to institute the system of ALM as part of their overall system for effective risk management. Those NBFCs which are holding public deposits are required to submit the first ALM returns

within a month of close of the relevant half year i.e., before 31 October 2002 and continue thereafter in similar manner.

(ii) The matter of supervision over ALM compliance by the NBFCs not accepting/holding public deposits would be advised in due course of time.

4. The amending notification No. DNBS 157/CGM(CSM) – 2002 dated April 22, 2002 along with updated notification DFC.119/DG(SPT)-98 dated January 31, 1998 (as amended upto date) is enclosed for your scrupulous compliance.

Yours faithfully,

**(C. S. Murthy)**  
**Chief General Manager – in – Charge**

Encls : 2 sheets

#### RBI rationalises prudential norms for NBFCs

The Reserve Bank of India today announced that the past due period of 30 days for identification of non-performing assets by NBFCs would be done away with effective from March 31, 2003. As such, a loan asset would become NPA if the instalment or interest thereon remains overdue for six months and a lease or hire purchase asset would become NPA if the lease rentals or hire purchase instalment remains overdue for twelve months. In order to avoid any ambiguity in classification of NPAs as loss assets, RBI has also set out objective criteria for identification of potential threat of non-recoverability of such assets.

2. The circular and the amending notifications are available on RBI's web-site [rbi.org.in](http://rbi.org.in).

#### **Background**

Keeping in view that the prudential norms for NBFCs are similar to those applicable to commercial banks, the concept of 'past due' has been abolished from the definition of

NPA for NBFCs. It may be recalled that this concept was abolished for banks effective from March 31, 2001. Further, it was observed that some of the NBFCs were using divergent yardsticks for identification of loss assets and as such, objective criteria has been advised to the NBFCs for this purpose.