Existing & Proposed Guidelines for NBFCs (mainly NBFC-ND)

An Online Seminar for ICAI Members of Western Region on March 13, 2021

What is an NBFC?

A Company

- **NBFC is a company registered under the Companies Act** (which is engaged in activities as defined **u/s 45-I (f) of RBI Act**)

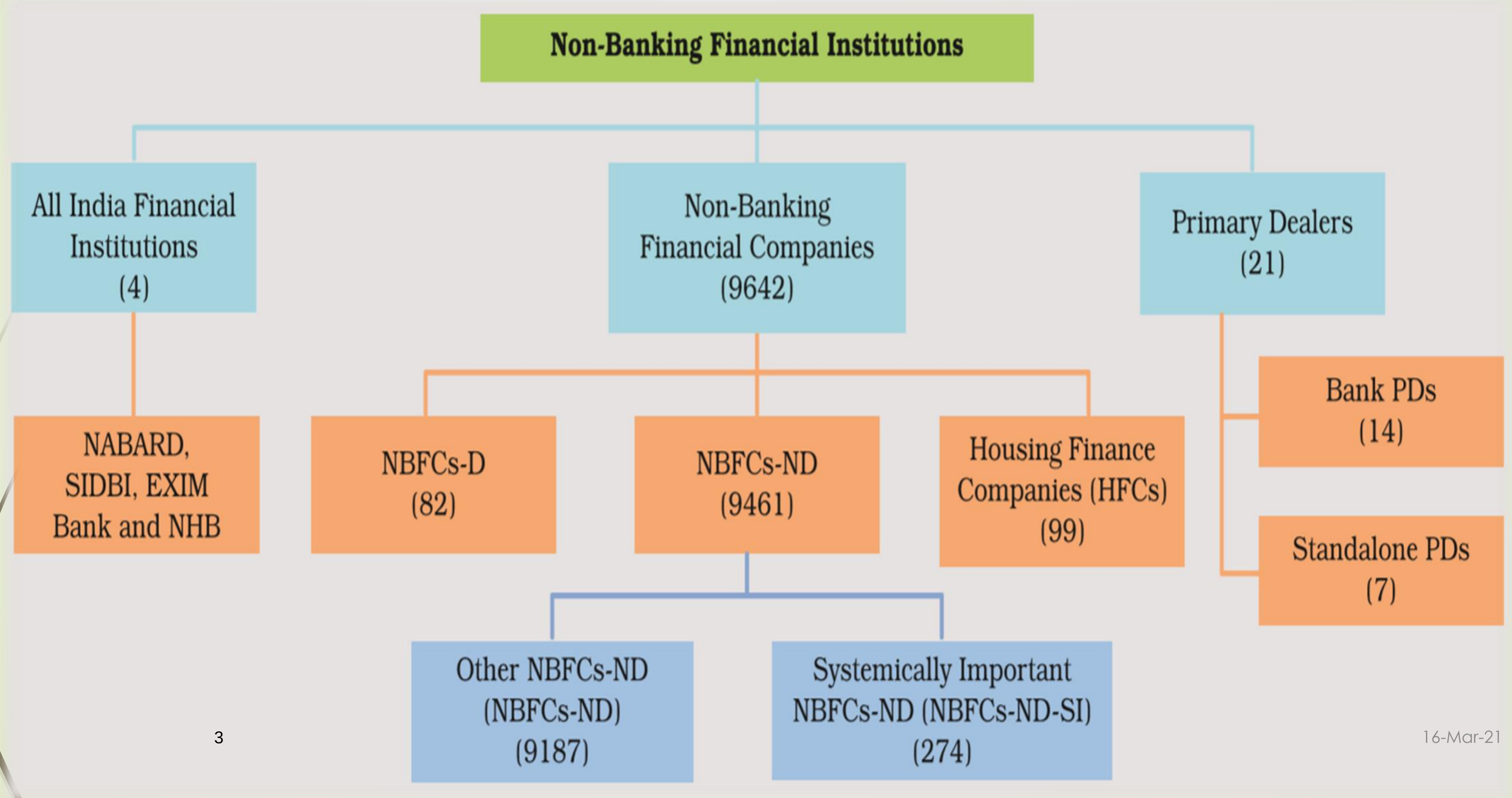
engaged into

- **Principal Business the receiving of public deposits** under any scheme/Arrangement or extending **loans & advances, acquisition of shares, stock, bonds, debentures, G-Sec, other marketable securities, etc.**
- **Leasing/delivering goods to hirer under Hire Purchase Agmt.**
- Any class of **insurance business,**

does not include

- Institutions whose **principal business** is **agriculture activity,**
- **Industrial activity, purchase or sale of any goods** (other than securities)
- **or providing any services and sale / purchase / construction of immovable property**

Structure of NBFIs under RBI Regulation in the Eco System



Why NBFCs are Created?

- Basically, to cater the credit needs of **bank excluded segments**.
- Initially, NBFCs were **complimenting banks** in credit intermediation
- However, over the period, NBFCs have grown significantly in terms of **size, operations, technological sophistication, entry into newer business lines** etc.
- NBFCs are **competing with banks** in providing wide range of financial services to niche sectors.

NBFCs – Basic Criteria for Registration

1) A company must be duly registered as per Companies Act 2013 as a public **limited or private limited company.**
2) The company must have a minimum **Net Owned Fund** of ₹ **2 Crore**
3) Satisfy the Principle Business Criteria (**PBC)**

- What is Principle Business Criteria?
  - Financial Assets **>= 50 % of Total Assets**
  - Financial Income **>= 50% of Total Income**
- Financial Assets will include all assets that are financial in nature except **cash, bank deposits, advance tax payments, deferred tax payments**
- Financial Income is the income generated from **financial assets**

Genre of Shadow Banks with their Min Net Owned Funds Requirements

Type of NBFC	Min NOF to be maintained
NBFCs other than mentioned below	₹ 2 crore
NBFC-MFI [Micro Financial Institution]	₹ 5 crore
NBFC- MFI in NE Region	₹ 2 crore
NBFC- Factor	₹ 5 crore
NBFC-HFC [Housing Finance Company]	₹ 20 crore
NBFC-MGC [Mortgage Guaranteed Company]	₹ 100 crore
IDF – NBFC [Infrastructure Debt Fund]	₹ 300 crore
NBFC- IFC [Infrastructure Finance Company]	₹ 300 crore
All India Financial Institutions (4) **NABARD, EXIM, NHB and SIDBI**	*They are well known for Development Financial Institution*

NBFCs – Criteria for Registration

- Is PBC defined in RBI Act?
- It is adopted while registration to ensure that only companies **predominantly engaged in financial activity** get registered with RBI.
- NBFCs can commence its operations **only after obtaining '*Certificate of Registration*'** from the RBI.

Three Mandates of Regulation & Supervision

Depositor Protection

- RBI is discouraging new entrants
- Existing are being encouraged to convert into non-deposit taking
- Close monitoring by BFS –deposit taking NBFCs inspection report put up to BFS

Customer Protection

- FPC
- NBFC Ombudsman
- Now special attention to conduct – focus area of supervision in addition to Governance and Systems and Controls

Financial Stability

- SI NBFCs identified and subjected to closer scrutiny – on-site and off-site
- Close monitoring of top 50, now top 100 accounting for over 95% of the sector
  - Monitoring involves – watching rating downgrades, adverse media coverage, weekly CRILC reporting, monthly structural liquidity returns, keeping totally up to date – take up the smallest development, a single default
  - 5th Pillar - interaction with stakeholders - SA interaction; MF, Banks, Markets depts.

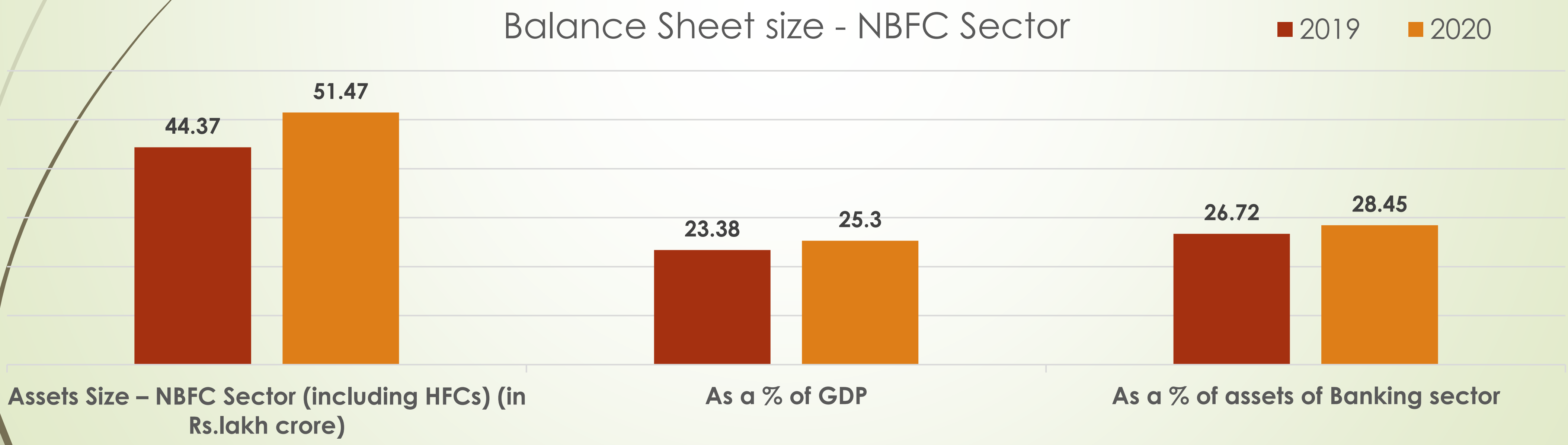
Perspective on NBFC Sector

- Pre-demonetization
  - Period of growth and profits
- Post Demonetization
  - Excess liquidity into the system to Mutual Funds
- From Mutual Funds to NBFCs
- Few NBFCs developed a business model risk i.e. Funding Long term assets with short term liabilities – easy availability at cheaper costs
- Post IL&FS crisis → tapering of excess liquidity and decline in lenders confidence
- Weakness surfaced in ALM followed by rating downgrade and default of some NBFCs

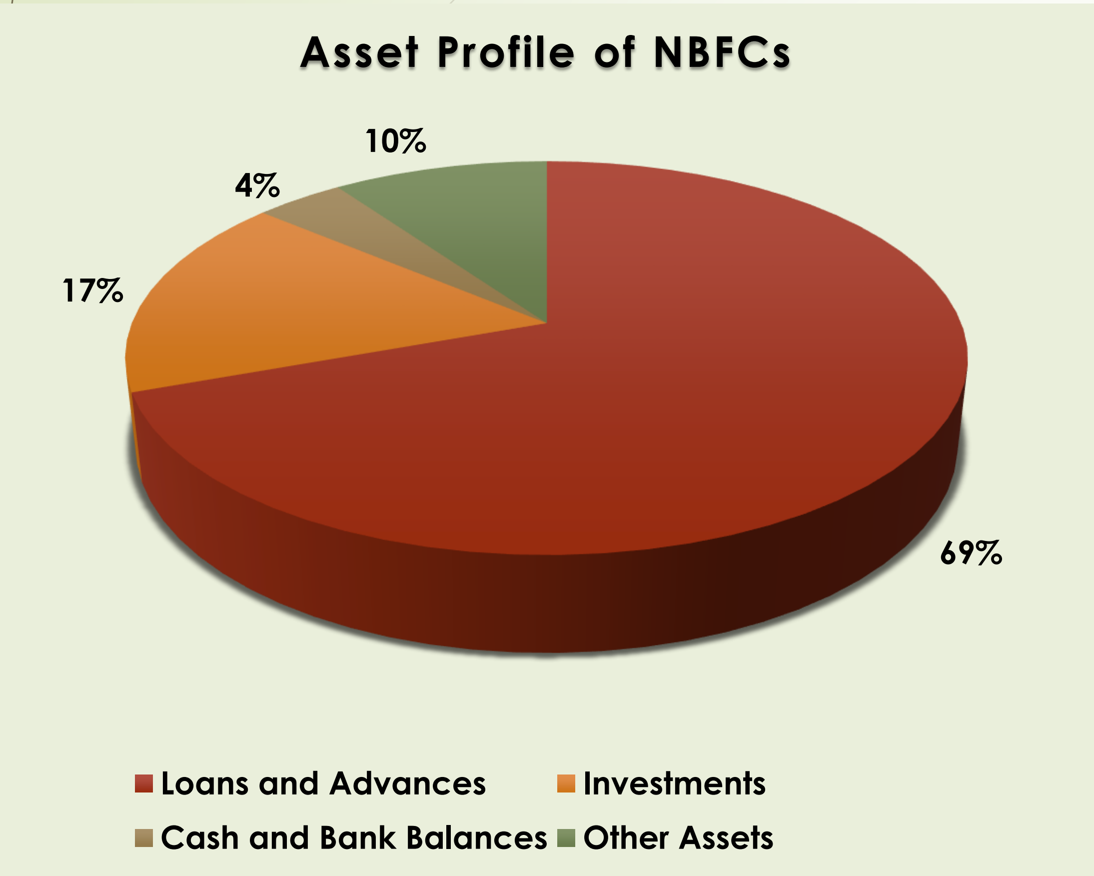
Sector- Overview- Depicting NBFC Population, their Growth, Contribution to Economy and credit penetration etc.

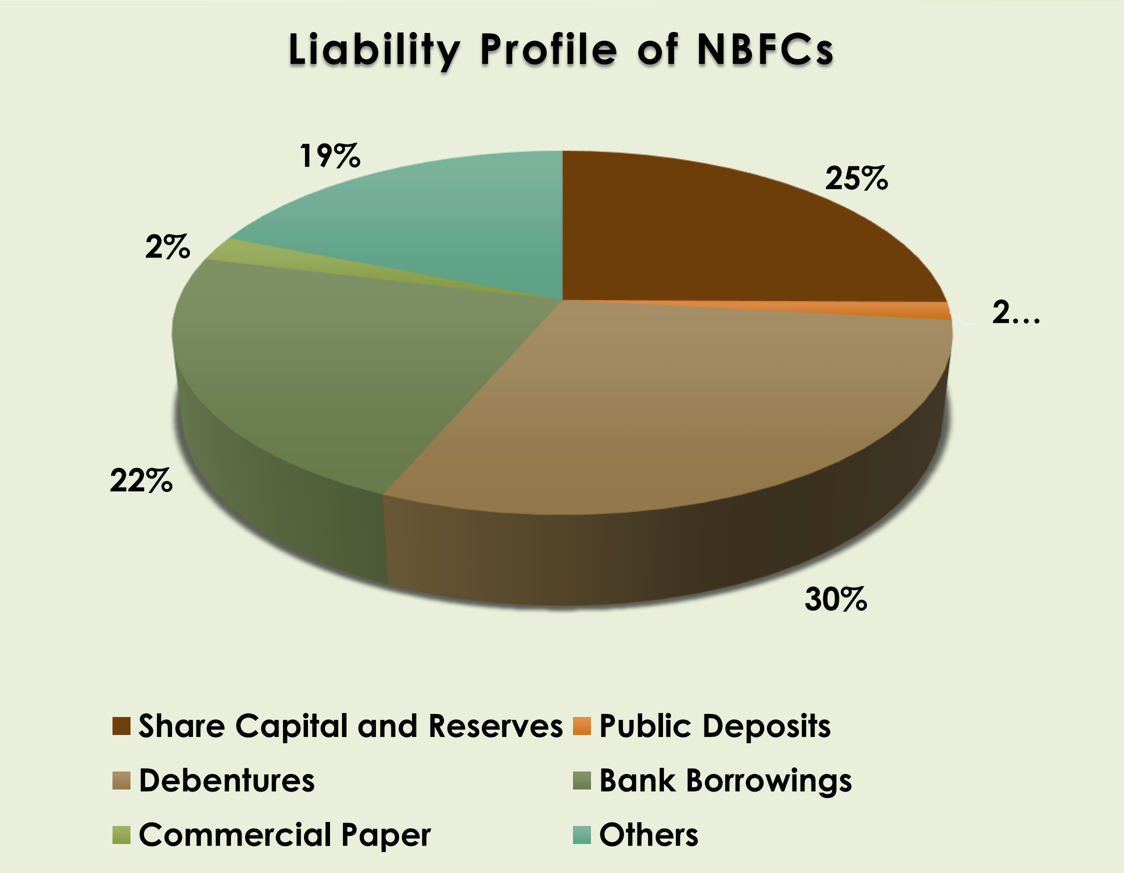
Shadow Banking Complements the banks in **Credit Intermediation** process and offer niche financial Products & Services to under banked clients and a particular group of client

- **9642** NBFCs registered with RBI as on **March 31, 2020** (excl. **99 HFC** as on March 31,2020)
- **82** (**0.9%**) deposit accepting NBFCs (around **20** actively accepting deposits) &**9461(ND)**
- **274 (2.84%)** – Systemically Important Non-Deposit rest **9187 (ND-NSI)** & **ARC -30**
- **Total Public Funds- ₹ 33 trillion as on March 31, 2020**

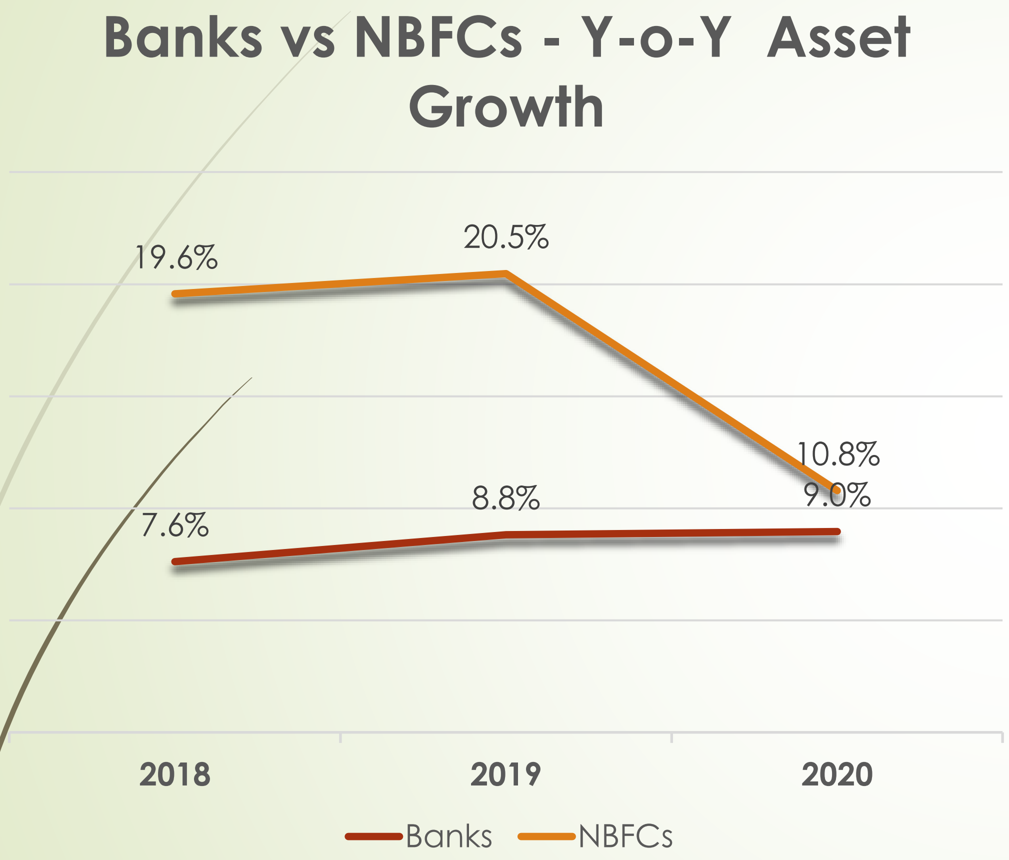


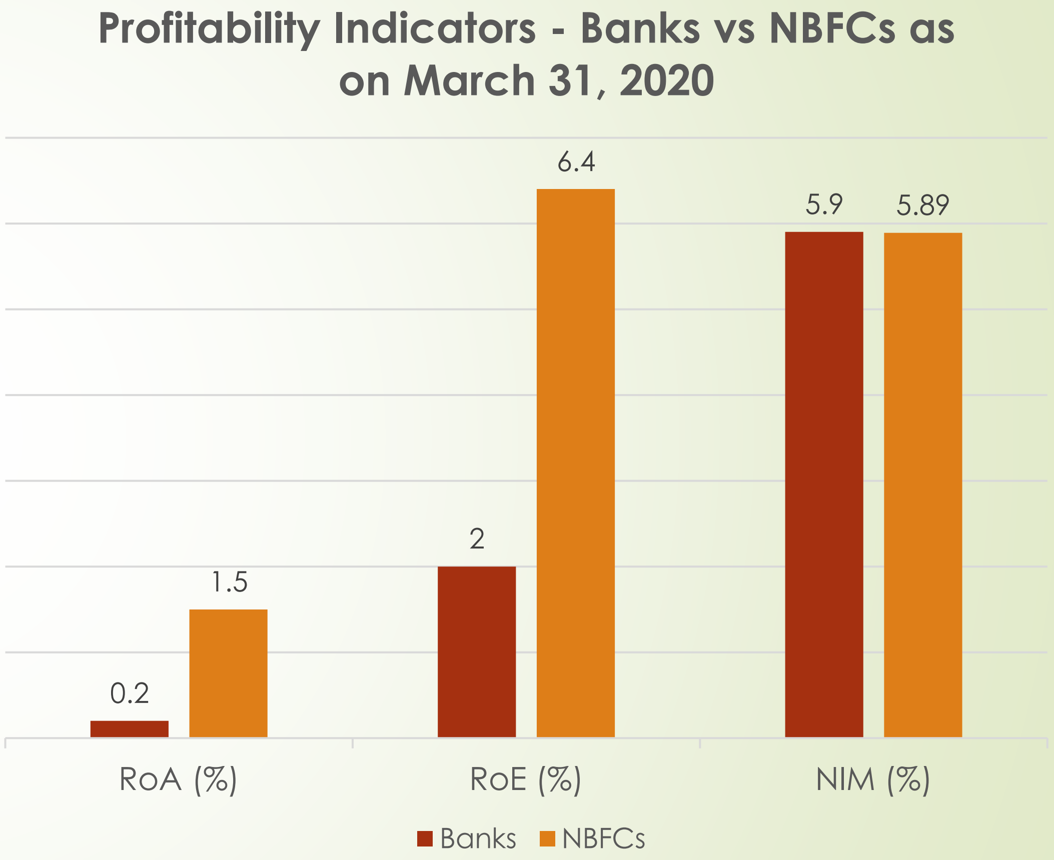
Assets and Liabilities – Profile of NBFC sector as on March 31, 2020





NBFCs Vs. Banking sector (Asset Growth & Profitability Ratio)

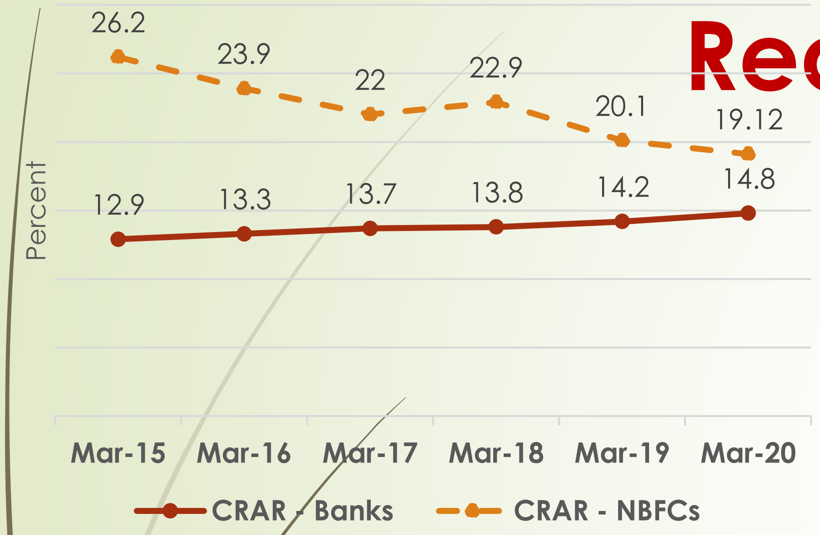


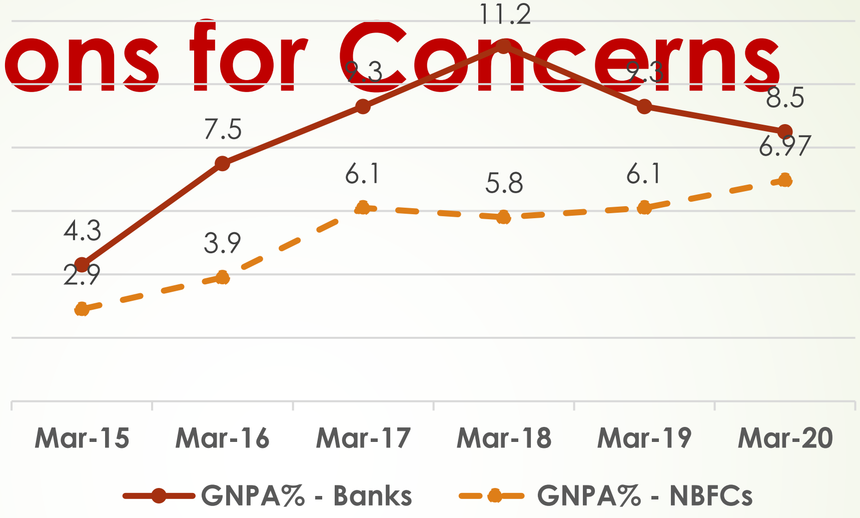


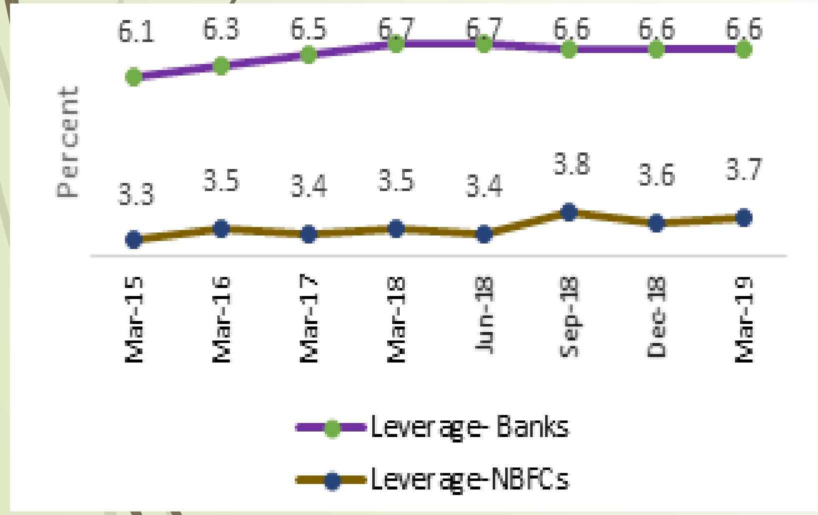
Reflections

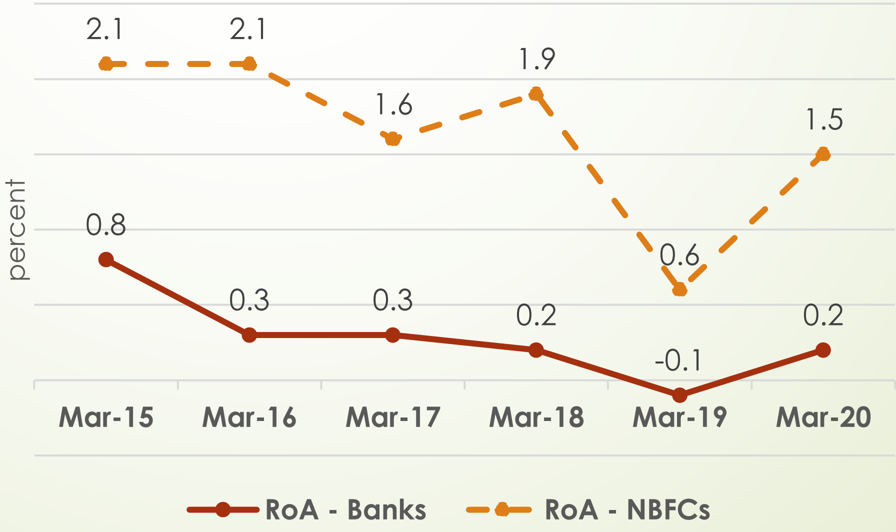
- **Earnings for NBFCs are higher in comparison to the average earnings by Banks**

Aerial view of the sector- Inbuilt Strength or Reasons for Concerns







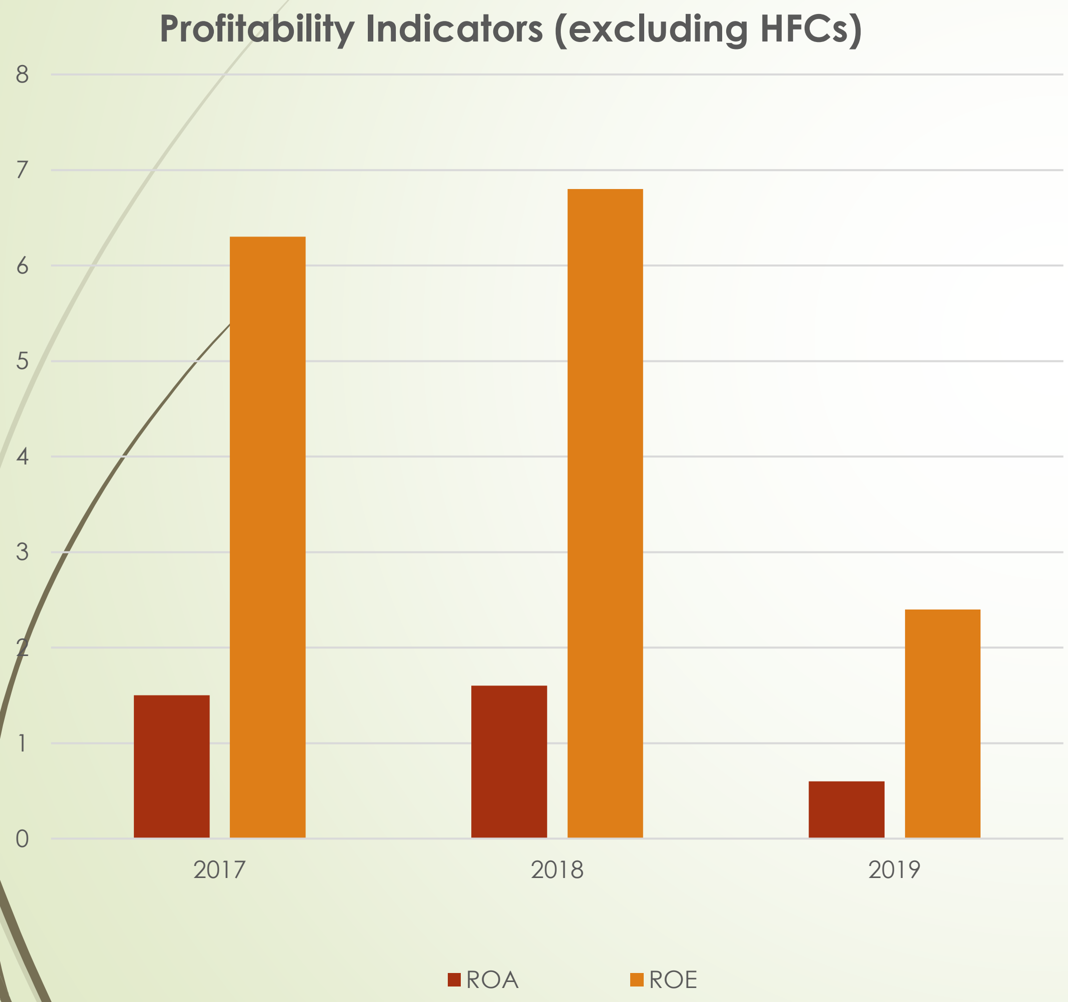


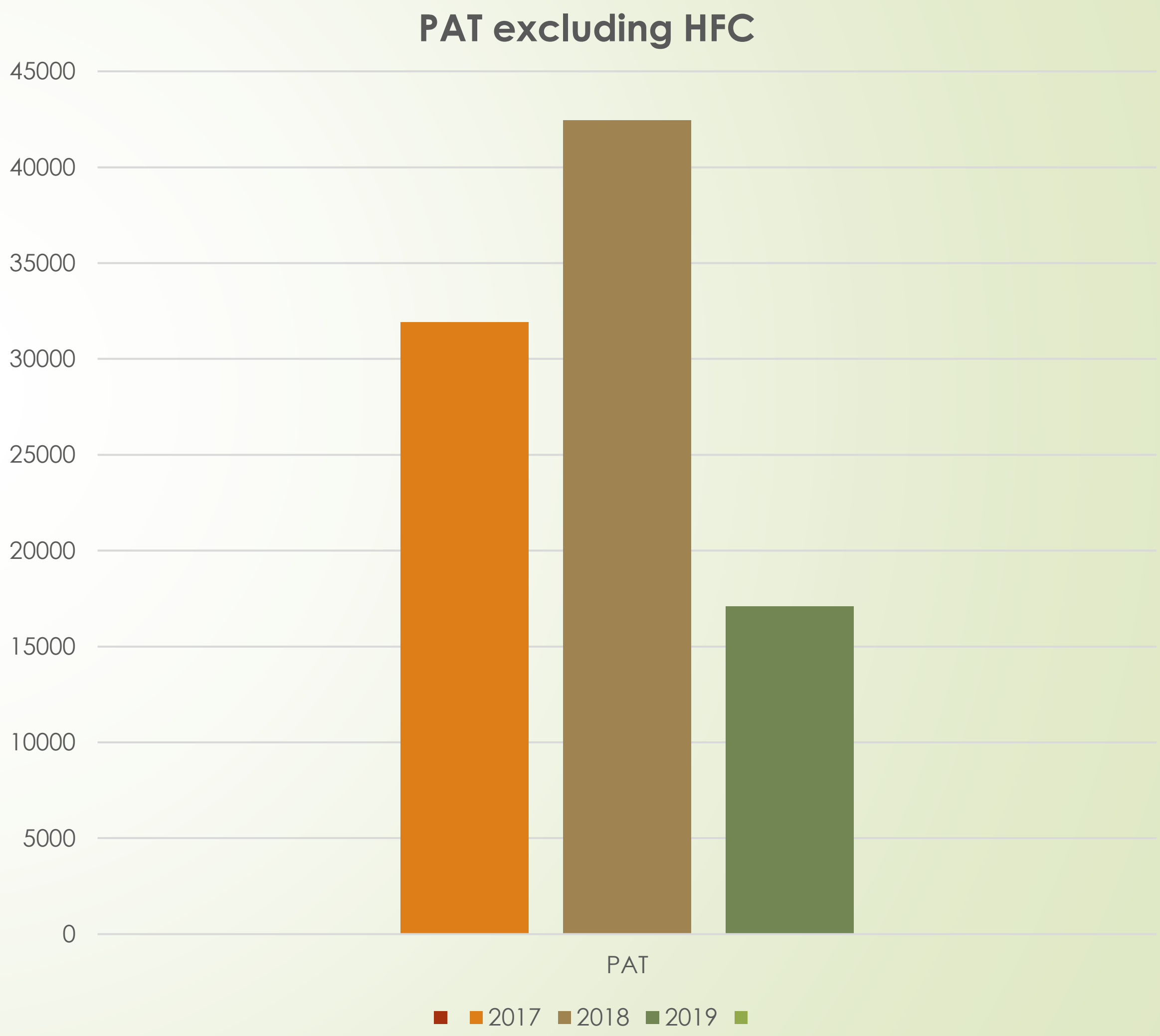
Data Reflection

- The requirement of capital maintenance though majorly non-deposit taking is higher in case of NBFCs
- Difference in the GNPA of banks and NBFCs reflect quality of NBFCs loan asset
- Banks though deposit taking are more leveraged than NBFCs
- Profitability indicators for NBFCs better than banks

Profitability and Profit After Tax (excl. HFC)

As evident from the chart below, an adverse event having significant interconnectedness, impacted sentiments and threat financial stability and erode the confidence of the stakeholders





Evolution of Legal or Regulatory Framework/Amendments with their objects

Time [Year]	Regulatory Purposes
1963	Regulatory and Supervisory Powers over NBFCs conferred with the insertion of *Chapter III-B [Through Banking Laws (Misc. Provision) Bill 1963* in the Reserve Bank of India Act, 1934 (**'RBI Act'**)
1974	Add on powers including the power to **inspect NBFCs**, enhanced **penalties** for contravention of RBI directions, **obligations on statutory auditors,** etc.
1997/98	Categorisation of NBFCs **(i) Public Deposit Accepting,** (ii) **Non-Public Deposit Accepting but engaged in loan, investment, hire-pur & Leasing**; **Définition of Core Investment Company [CIC]** **Deposits was made function of Credit Ratings & NOF; Widening the Scope of Auditors' Certificate**
2014	▪ Requirement of Minimum NOF of **₹ 2 crore** for legacy NBFCs ▪ **Harmonisation of Deposit** Acceptance Requirements Across NBFC categories ▪ Revision of the threshold of systemic importance from ₹100 crore **[firstly introduced in 2006]** to ₹ 500 crore ▪ **Differentiated Regulatory Approach [1st introduced in 2006] was the linked with Customer Interface and Source of Funds.**

Structural & Prudential Arbitrage Between Banks and NBFCs & Concerns Arising out due to such Regulatory Arbitrage and Causing Systemic Risk

- The Banks are regulated under **BR Act 1949 & NBFCs** are regulated by **RBI Act 1934**
- The premise of '**less rigour**' regulation has empowered NBFCs to resort to have ample **business and operational flexibilities** and several regulatory and supervisory circumventions, posing several challenges to Regulator to shift its Regulatory gears.
- Arbitrage induced by '**On Size Fit all & Light Touch Regulations**' was perceived as NBFCs' **scale of operations** would be low in comparison to banks, posing no **significant systemic** risk. But the idea conceived went another way round as evident in slides below
- Contrary, the balance sheet of NBFC (including HFCs) became more than **doubled** from ₹20.72 trillion (2015) to ₹**49.22 trillion (2020).**
- **Total Public Funds- ₹ 33 trillion as on March 31, 2020**
- 28.45% of Assets of Banking Sector @ March 31, 2020

Instances of Structural and Prudential Arbitrages between Banks & NBFCs- Instances Below…

Structural Arbitrage

- Maintenance of CRR & SLR
- Cap on Voting Rights of Shareholders
- Prohibition of buying, selling and bartering of goods
- Prohibition in holding non-banking assets
- Mandatory Board Expertise for Banks
- RBI Control Over Management
- Deposit Insurance
- The requirement to hold a certain % percentage of assets in India
- Restriction on investment in other companies
- Entry Point Norm and Listing Requirements [LODR]

Prudential Arbitrage

- *CRAR – Basel I – Only for Credit Risk – Tier-1- 10% (Also for HFC)*
- *Leverage – No Prescription… Yet to figure out*
- *NPA Classification – 90 DPDs and 180 days*
- *Provision of Standard Assets –flat 0.40% for all assets*
- *Priority Sector Lending Targets – No Target*
- *Risk Weights under Capital Adequacy – One size fit all 100% across all types of Loan assets*
- *Liquidity Guidelines- Granularity in 10 maturity buckets*
- *Lending Against Shares- Higher Exposure vis-à-vis Banks*

Need for strengthening extant Legislative Regime through Scale Based Approach

1. Complex Web of Inter-connectedness with Banks, Capital Market, Money Market & Other Financial Institutions on both side of the balance sheet.

2. Exponential Growth in Size, Leverage, Operations and Technological Sophistications etc.

3. 12 % of the Banks Balance Sheet (2010), Now Over 25% of the Banks B/S (2020)

4. Unbridled growth and degree of complexity fuelled by Light Touch Regulation- A series of crisis viz. IL&FS, DHFL, Alticao and Reliance Capital etc. nudged RBI to review the extant regulatory prescriptions.

5. 5. IL&FS default created a crisis of confidence for NBFC sector which led to Liquidity crunch in the market & consequent ALM mismatch at entity level

Regulatory Arbitrage and Structural Arbitrage of NBFCs vis-à-vis banks

6. A wide scope for regulatory and supervisory circumventions

Need for strengthening extant Legislative Regime through Scale Based Approach

- **Calibrated Regulation has bee adopted by several International Regulatory Agencies such as G-SIB developed by BCBS, G-SII by International Association of Insurance Supervisors (IAIS)**
- **Banks & Market Borrowings of NBFC**– 70% of total outside liabilities (TOL)
- With the waning of market confidence, **NCDs borrowings** declined to **40.8% (December, 2019) from 49.1% (at March 2017). (NBFC Bonds sale (Apr-Aug): 2017 - ₹1100 Bn; 2018 - ₹600 Bn; 2019 - ₹500 Bn; 2020 - ₹860 Bn**
- As such bank borrowings rose to **28.9% (December 31, 2019)** from 23.1% **(at March 31, 2017**), amplifying liquidity risk of the NBFC from **potential to accentuated**, a threat to the entity as well the financial Sector.
- Lending to NBFCs by many banks have either reached or breached their internal exposure or risk appetite limit.
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Extant Regulation- Dashboard

Category	Entry point norm	Capital Adequacy	PBC	Provisioning norms	Credit Concentration norms	Composite (Credit plus investment)	SLR
	Rs.2 crore	15%	50:50 90 days	Same as banks	15% and 25% (add. 5% & 10% for infra)	25% and 40%	15% (NBFC-D)
IC/ LC	✓	✓	✓	✓	✓	✓	✓
AFC	✓	✓	60:60	✓	✓	✓	✓
CIC	100 cr assets	ANW 30% of RWA	90:60	✓	✓	✓	NIL
IFC	300 cr	✓	75:75	✓	✓	✓	NIL
Factors	5 cr	✓	✓	✓	✓	✓	NIL
IDF	300 cr	✓	100%	✓	✓	✓	NIL
MFI	2 cr NE and 5 cr	✓	85%	different	Rs.60000-100000	NIL	NIL
MGC	100 cr ✓	10%	90%	✓	✓	NIL	NIL
AA and P2P		NIL	NIL	NIL	NIL	NIL	NIL

Policy objectives for regulating the sector

Protecting Customers Interest viz. Depositors, Creditors, Investors, Lenders etc.

Maintain orderly growth of the sectors

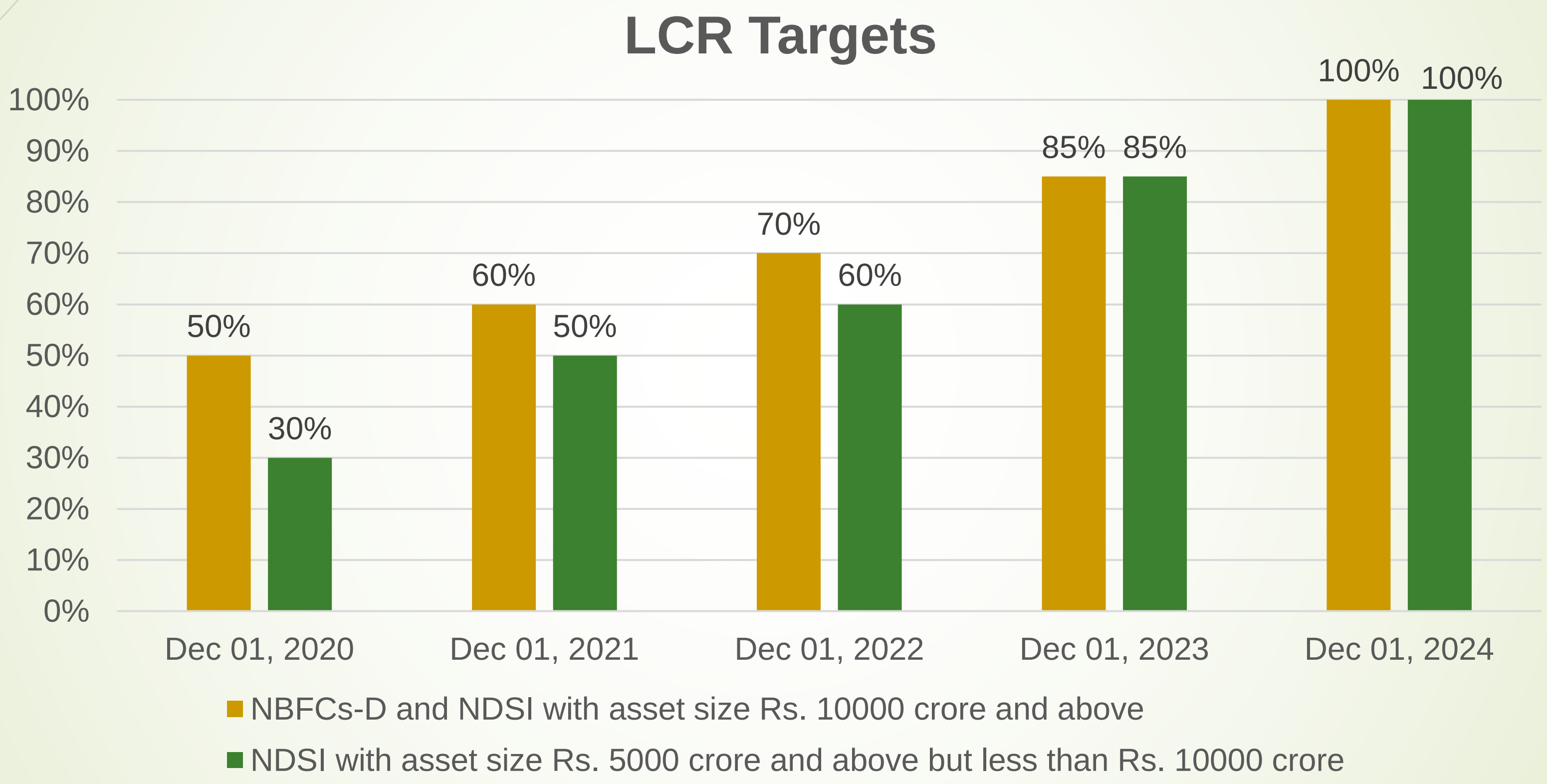
In view of large interconnectedness, RBI to ensure that financial stability not compromised as it has cost to the Economy

Liquidity Risk has been the main face of recent NBFCs fiascos. Interestingly, Liquidity risk is basically a By-Product risk of Credit Risk, Business or Model Risk, Higher Leverage & Governance Risk etc. caused disruption to the financial stability..

Certain Recent Regulatory Measures Of RBI to tightened the regulation for NBFCs Instilling Long term resilience

- *Liquidity Risk Management Framework (LCR)* All non-deposit taking NBFCs with asset size of Rs.5000 crore and above and all deposit taking NBFCs irrespective of their asset size shall maintain a minimum LCR of 100% by December 1, 2024; CIC are exempted
- *CIC Guidelines (Tapan Ray Committee)*
- *CRO Appointment- Post IL&FS fiasco*
- *IND-AS Implementation*
- *NBFC Ombudsman 2018*
- *Co-lending Framework*
- *Harmonisation of different categories of NBFCs- LC, AFC and IC merged with name ICC*
- *Risk Based Internal Audit (Latest One February 3, 2021)*
- *Review of Regulatory framework for HFCs (definition of HFC, NOF and others)*

Timelines for compliance with LCR norms for NBFCs



Steps to tackle the recent challenges – Legislative Amendments

RBI Act, 1934

Section 45-IA

Increase in RBI specified NOF ceiling

- Net owned funds ceiling (to be specified by RBI) increased from ₹2 crore to ₹ 100 crore => RBI can now specify any minimum NOF requirement up to ₹ 100 crore

45-ID and 45-IE (new sections)

Power to remove directors and supersede Board

- Empowers RBI to remove a director (45-ID) or supersede the entire Board of Directors (45-IE)
- However, this section is not applicable to Government Companies

45MAA (new section)

Power to take action against auditor

- If an auditor fails to comply with direction given by RBI u/s 45MA, RBI can remove/ debar the auditor from auditing RBI regulated entities for up to 3 years, at a time

45MBA (new section)

Resolution of NBFC

- RBI can frame scheme of amalgamation, reconstruction or splitting of an NBFC.
- It may establish "Bridge Institutions" so that the splitting of the NBFC is not disruptive to its depositors, creditors and customers

45NAA (new section)

Power in respect of Group Companies

- RBI can call for information relating to group companies and also inspect them

NHB Act, 1987

Regulation of Housing Finance Companies (HFCs) shifted to RBI

- RBI empowered to register HFCs, regulate HFCs, cause an inspection of an HFC (through NHB), prohibit acceptance of deposits and prohibit alienation of assets

Scale based Regulatory Framework for NBFCs

- Extant Regulatory regime – Based on **Principle of Proportionality**– Excessive Operational Flexibility
- '**Light-touch'** Regulation on **premise of low scale of operations** and **Insignificant Systemic Risk** led to Regulatory Arbitrage.
- **Significant increase** in size and interconnectedness and complexities etc.
- Extremely large NBFCs functioning like banks in terms of scale and complexity.
- **7 NBFCs (including HFCs) with asset size more than ₹ 1 lakh and above**.
- During the last 10 years, size of NBFCs has grown from **₹ 6.83 Lakh crore to ₹ 35.13 Lakh crore**.

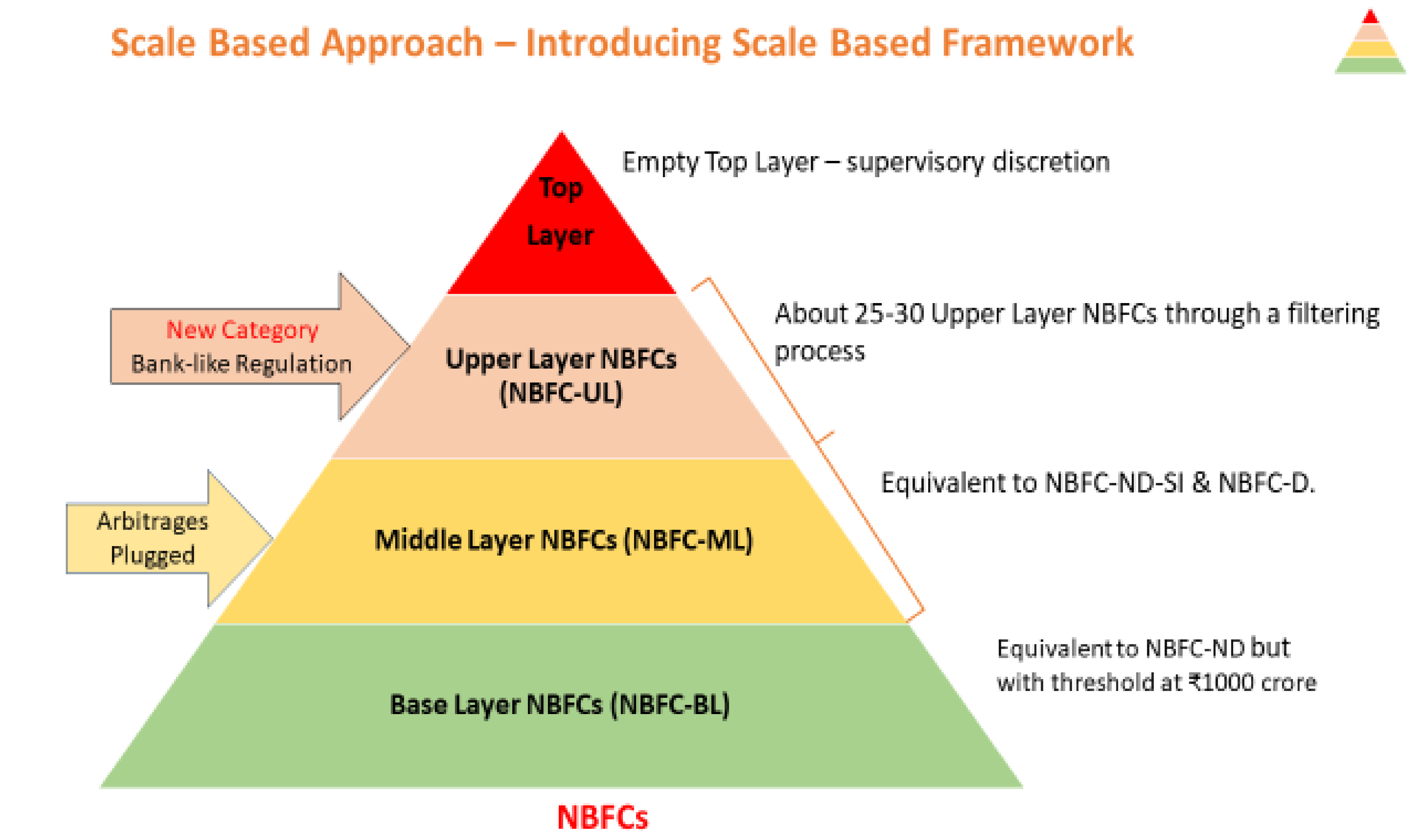
➢ **A need to review the regulatory framework in line with the changing risk profile of NBFCs.**

➢ ***A scale-based regulatory approach linked to the systemic risk contribution of NBFCs could be the way forward.***

➢ *To address risks from large interconnected NBFCs so that risks to the system are moderated.*

➢ *To address adverse arbitrage between NBFCs and banks.*

Introduction of Scale Based Approach (SBA) to Regulation



Population of NBFCs in Layers Hierarchy

Base Layer - Bottom of the Pyramid- NBFC-ND, NBFC-P2P, NBFC-AA, NOFHC & Type I NBFCs [*Not Accepting Public Funds and Not Having Customers interface*]

- Middle Layer-NBFC-D, HFCs, IFCs, IDFs, SPDs and CICs- Adverse regulatory arbitrage vis-à-vis banks can be addressed for NBFCs falling in this layer in order to reduce systemic risk spill-overs, where required.

- Upper Layer- Systemically Important (Criteria–Parametric Matrix)- Will subject to a bank-like regulation, albeit with suitable and appropriate modifications.

- Top Layer- Suppose to be empty, notwithstanding if an entity Posing Extreme Risk, will warrant bespoke ultra regulatory and supervisory attention to contain spill over risk

Criteria for populating NBFCs in their respective Residents under SBA

Scale Based Approach – The Filtering Process

1 SIZE

2 SCALE of Significance

3 ACTIVITY

Upper Layer (NBFC-UL)

- Sample (top 50 NBFCs in terms of asset size) to undergo following filters
  - **Size** – 35%
  - **Inter-connectedness** – 25%
  - **Complexity** – 10%
  - **Supervisory inputs** – 30% (segment penetration, liability mix, group structure)
  - Top 10 to be included in any case

Middle Layer (NBFC-ML)

- Housing Finance Company
- Standalone Primary Dealers
- Infrastructure Finance Company

Always NBFC-ML

- Infrastructure Debt Fund
- Core Investment Company

Base Layer (NBFC-BL)

- Type I NBFC
- Peer to Peer (P2P)
- Account Aggregator (AA)
- NOFHC
- Up to Rs.1000 cr asset size

Identifying NBFC-UL and Methodology for Identification of NBFC-UL

A.) Parameters for UL-

Size, Leverage, Interconnectedness, Substitutability, Complexity and Nature of Activities etc.

B.) Methodology

Quantitative Parameter (70% Weights)

i) Size & Leverage – Total Exposure (On & Off B/S) -20% and Leverage-15%= Total -35%

ii) Interconnectedness (25%)

a.) Intra-financial Assets viz. Lending to FI (10%),

b.) Intra-financial Liabilities viz. FIs-Borrowings (10%) and

c.) Securities O/s with Non-FI –(5%)

iii) Complexity (10%) –a.) Notional Amount of OTC derivatives (5%)

b.) Trading and AFS Securities (5%)

Qualitative Parameter (30%)

i) Nature and Type of Liabilities (10%)- Amount and Types and degree of dependency on ST Findings

ii) Group Structure (10%) – Total entities, number of layers, Intra group exposure

iii) Segment Penetration (10%) – The importance of NBFC as a source of credit to a specific segment or area

Selection of Samples for Identifying NBFC-UL & Scoring Methodology

The Parameter driven measurement approach- Based on sample of NBFCs. Following Criteria included in the sample

i.) **Excluding top 10 -- Basis their asset size**

ii.) Next **50 NBFCs** based on their total exposure (including Off B/S exposure)

iii) **NBFCs-UL** in the previous year (unless supervisors agree that there is a compelling reasons to exclude any one of them)

iv) NBFCs added to the sample by **Supervisors** using their **supervisory judgment**

Scoring Methodology

Based on NBFCs data on Parametric Matrix, **a composite score will be computed for identification of NBFC-UL.** The score for a particular indicator will be calculated by dividing the individual NBFC's amount by the aggregate amount for the indicator summed across all NBFCs in the sample. The systemic significant score of an individual NBFC would represent its relative degree of risk/importance with respect to others in the sample

Implementation Plan & Transition of NBFCs - UL

Identification of NBFC-UL basis parametric analysis shall be conducted **yearly** based on followings

i.) The entity will be subjected to regulation **akin to banks**.

ii.) The entity will be provided a **8 weeks** to chart out a plan for implementation. A Board approved policy for adoption of the enhanced regulatory framework.

iii.) The Board will complies with the **RBI UL** guidelines within a max period of **18** months from the date of its declaration as **NBFC-UL**. During this transition, ***calibrated increment to business may be allowed through supervisory engagements.***

iv) It will subject to enhanced regulation for **4 years** from its last appearance in the category, even where it does not meet the parametric criteria for **4 years** in the subsequent year. If it does not meet criteria for classification for **4 consecutives year**, it will moved out from enhanced regulations. **NBFC-UL will be allowed to exempt from the enhanced regulatory if the movement is Board approved voluntary strategic move.**

Proposed Scale Based Framework

The proposed Regulatory Framework for NBFC In Base Layer

a.) New Threshold **₹1000** crore from Current **₹500 crore.** Out of **9425 NBFC-ND, 9133 having asset size of** ₹500 crore, It increase by 76 to 9209.

b.)**NOF** - **₹20 crore** from **₹2 crore (since 1999)-** Purpose is to eliminate non-serious players and increasing loss absorption capacity against unexpected loss due to business loss and poor governance

c.)**Regulatory Framework**

i) Enhanced **Governance** and **Disclosure Standards** with respect to **Exposure**, **Related Part Transactions**, **Customer Complaints** etc.

ii) NPA **180** days harmonized to **90** days

iii) stipulation for RMC (Risk Management Comm.)

iv) **At least one Directors have expertise in retail**

Regulatory Framework for NBFC In Middle Layer

Structure: NBFC-ND-SI & NBFC-D [**excluding IFCs, IDFs, SPDs and CICs** irrespective of their asset size to be populated in this layer]

- Regulatory prescriptions as applicable to NBFC-ND-SI and D. However, **adverse regulatory arbitrage posing systemic risk will be addressed.**
- Capital- **Status quo- CRAR (15%- Tier I -10% and Tier II- 5%)**
- **Credit Concentration- SBL- (lending 15% + Investment 15%; Total-25%)**

  GBL (**lending 25%, Investment 25 %, Total -40%)**
- **ICAAP-** Capital Assessment based on **Credit+ Market+ Operational + Other Residual Risk**
- **Rotation of Auditors** – Three years then a gap of **6 years (two terms**)
- **Chief Compliance Officer [CCO]- Mandatory**
- **Compensation Guidelines- Constitution of NRC, Principles for Fix/variable pay structure and malus/claw back requirements**
- **Key Managerial Personnel & WTD –To check the Dual Hatting etc.**
- **Corporate Governance and Disclosure Requirements –** Strengthening **Market Discipline**
- **Sectoral Exposure- Board Approved limit for SSE- RBI will leave up to Board of the NBFC**
- **Guidelines for sale of stressed assets – In line with banks (2003 and 2016)**

Regulatory Framework for NBFC In Upper Layer

- **Broad Structure-** Specifically Identified as Systemically important among NBFCs based on a set of Parametric Matrix above. Not more than **25-30** NBFCs will occupy this layer.
- **Regulatory Framework-** Regulation of NBFC(ML)**+ Additional Regulatory**
- **Capital Regulation-** CET-1 at **9%** within Tier 1
- **Leverage-** Yet to be find **magic** figure, it will act as backstop for further growth to a desired level
- **Standard Asset Provisions**- Currently flat **0.40%-** In line with the banks from **0.25% to 1%**
- **Credit Concentration Norms & Large Exposure Framework(LEF)** with suitable adaption
- **Mandatory LODR-** Listing Obligation & Disclosure Requirements- **Regulatory tools in line of Pvt banks**
- **Qualification of Board Members- Mix of qualification, expertise and experience**
- **Removal of Ind Director– Even before completion of normal tenure sub to RBI app**
- **Group Structure –** It will not allowed to be **complex and opaque s**uch was the case in **IL&FS crisis**
- **Sectoral Exposure –** May fix SSE Ceilings as per Board Approved Policy due to their large size and interconnectedness, may be vulnerable due to concentration risk

Regulatory Framework for NBFC In Top Layer

- It is an emergency residence for a NBFC- Though It is assumed that It will mostly remain empty.
- If the risk emanating has cascading effect to the NBFC industry as well the financial sector, critical in nature etc.
- Very High Risk Supervisory Perceptions would be pushed to Top from Middle
- Will require Higher Capital Charge, including Capital Conservation Buffers. There will be enhanced and more intensive supervisory engagements with these NBFCs
- A comprehensive legislative solution would be required to address the issue of resolution of failing NBFCs to take care of the unique of resolution of financial institution including the need to protect depositors' interest, avoiding moral hazard, ensuring continuity of critical services etc.

Summary Chart - Proposed Regulatory changes for NBFCs – Scale Based Approach

(green)	Proposed changes for NBFC-BL
(yellow)	Proposed changes for NBFC-ML
(peach)	Proposed changes for NBFC-UL

Parameters	NBFC – Base Layer (NBFC-BL)	NBFC – Middle Layer (NBFC-ML)	NBFC – Upper Layer (NBFC-UL)
Capital Regulation			
CET 1	Not stipulated	Not stipulated	9%
Leverage	7	Not stipulated	To be stipulated
Standard Asset provisioning	0.25%	0.40%	Differential Provisioning – Similar as banks
NPA Classification	Harmonisation from 180 days to **90 days** overdue	90 days	90 days
ICAAP	Not stipulated	Board approved policy taking into account all risks	Same as NBFC-ML

Concentration norms			
Computed as a percentage of	Owned funds	Tier 1 capital	Tier 1 capital
Credit Concentration Norms and Applicability of Large Exposure Framework (LEF)	Extant guidelines as applicable for NBFC-NDs	Merger of lending and investment limits into a single exposure limit	(i) LEF as applicable to banks with suitable modification (ii) Transition time for implementation

Governance and Disclosure norms			
Compensation Guidelines – Constitution of Nomination and Remuneration Committee	Not stipulated	(i) Constitution of a Remuneration Committee (ii) Principles for fixed/ variable pay structures (ii) Malus/ claw back requirements	On similar lines as applicable for Private Sector Banks, including guidelines on general compensation policy & remuneration committee.
Rotation of Statutory Auditors/ Firms	Not stipulated	(i) A uniform tenure of three consecutive years (ii) After completion of three years, mandatory cooling period of six years (two tenures) before reappointment.	Same as NBFC-ML

Parameters	NBFC – Base Layer (NBFC-BL)	NBFC – Middle Layer (NBFC-ML)	NBFC – Upper Layer (NBFC-UL)
Key Managerial Personnel (KMP) - whole time employee in the nature of CEO, CFO, CS and WTD	As per Companies Act, 2013	(i) No KMP of an NBFC shall hold office in any other NBFC-ML or NBFC-UL or subsidiaries (ii) An Independent Director cannot be director in more than two NBFCs (NBFC-ML and NBFC-UL) at the same time	Same as NBFC-ML
Appointment of Chief Compliance Officer	Not stipulated	Mandatory	Mandatory
Listing	Not mandatory	Not mandatory	Adequate phase-in-time for mandatory listing. However, disclosure requirements will kick in earlier than actual listing within the broad implementation plan for NBFC-UL
Expertise for Board members	(i) Adequate experience and educational qualification (ii) At least one of the directors should have experience in	Same as NBFC-BL	Same as NBFC-ML Specific expertise may be prescribed in addition

Removal of Independent Directors with Supervisory approval	Not stipulated	Not stipulated	Requires Supervisory approval
Risk Management Committee	(i) Overall role and responsibilities to be laid out (ii) Could be Board or Executive level as to be decided by the Board	Board-level RMC applicable	Board-level RMC applicable
Business Conduct and Disclosure Regulations	(i) Extant guidelines as applicable to NBFC-NDs (ii) Additional disclosures on type of exposures, related party transactions, customer complaints	Additional disclosures	To be at par with banks (SEBI-LODR)

Parameters	NBFC – Base Layer (NBFC-BL)	NBFC – Middle Layer (NBFC-ML)	NBFC – Upper Layer (NBFC-UL)
Other Regulatory Arbitrage			
IPO Financing	Not stipulated	Ceiling of Rs.1 crore per individual	Same as NBFC-ML
Sale of stressed assets	To be at par with banks once guidelines are finalised	To be at par with banks once guidelines are finalised	To be at par with banks once guidelines are finalised
Core Banking Solution for NBFCs	Not mandatory	Mandatory for NBFCs with more than 10 branches	Same as NBFC-ML

Expectation of RBI from the Auditors- **Non-Banking Financial Companies Auditor's Report (Reserve Bank) Directions, 2016**

- Sub-section **(1A) of Section 45MA (Powers and duties of auditors) of the RBI Act, 1934** and of all the powers enabling it in this behalf
- Applies to **every auditor** of a NBFC as defined in section **45 I (f)** of the RBI Act
- Auditor shall also **make a separate report to the Board of Directors of the Company**

Expectation of RBI from Auditors continue….

RBI Act, 1934 – Section 45MA

- (1) duty of an auditor of a NBFC to **inquire** whether or not the non-banking institution has furnished to the RBI **such statements**, **information or particulars relating** to or connected with **DEPOSITS** received by it, as are required to be furnished under this Chapter, and the auditor shall, **except where he is satisfied** on such inquiry that the NBFI has furnished such statements, information or particulars, **make a report to the RBI** giving the aggregate amount of such deposits held by the non-banking institution;

- Whether it is NBFC registered with RBI – **To check CoR**

- If NOT registered
  - ✓ **Ask whether it has sought exemption from RBI – check the documents**

Expectation of Auditors NBFCs- D

The **public deposits** together with **other borrowings** are within the admissible limits **The public deposits held by the company in excess of the quantum of such deposits permissible to it**
Whether the NBFC is accepting "public deposit" without minimum investment grade credit rating from an approved credit rating agency
Reported CRAR is in compliance with the minimum CRAR prescribed therein
Whether the credit rating, for each of the fixed deposits schemes that has been assigned by one of the Credit Rating Agencies listed is in force

Expectation…

- Periodical Engagement **(at least in a quarter)** with the Board/ACB and Senior Management with Exceptional Agenda Items, if any,

- True Fair and Transparency in Annual Report

- It shall be the obligation of the auditor to make a report containing the details of **unfavourable or qualified statements** and/or about the non-compliance, as the case may be

- **4th Pillar** of supervisory process
- Report/Special Report to Board of Director (BOD)
- **Exception Report**
- **Annual Certificate and other certificates**

Reasons to be stated for unfavourable or qualified statements

- Where, in the auditor's report, the statement is unfavourable or qualified viz.

i.) the provisions of Chapter III B of RBI Act (Act 2 of 1934)

ii) NBFC Acceptance of Public Deposits (Reserve Bank) Directions, 2016 and

iii) NBFC–NSI-NDC (Reserve Bank) Directions, 2016 and NBFC–SI-NDC and Deposit taking Company (Reserve Bank) Directions, 2016

- the auditor's report shall state the reasons for such unfavourable or qualified statement, as the case may be.
- Where the auditor is unable to express any opinion on any of the items, his report shall indicate such fact together with reasons therefor.

Thank You All