RBI / 2009-10/18

DNBS (PD) CC No. 157 / 03.10.001 / 2009-10 **July 1, 2009**

To

All Non-Banking Financial Companies (NBFCs)

Dear Sir,

Master circulars- miscellaneous instructions to NBFC- ND-SI

In order to have all current instructions in one place, the Reserve Bank of India has consolidated all the instructions issued during the year ended June 30, 2009. The circular seeks to consolidate all instructions issued exclusively to NBFC-ND-SI i.e. other than those which have been consolidated in Master Notification on Prudential Norms and Master Circular - compendium of instructions issued to NBFCs. A consolidated list of all instructions issued under various subjects is compiled for ready reference. The compendium of circulars has also been placed on the RBI web-site (http://www.rbi.org.in). A copy of the compendium is enclosed.

Yours sincerely

(P. Krishnamurthy)
Chief General Manager-in-charge

Quarterly Return on important financial parameters of Non-Banking Financial Companies (NBFCs) not accepting/holding public deposits and having assets size of Rs.500 crore and above

It was decided in November 2004 to introduce a reporting arrangement for Non Banking Financial Companies not accepting/holding public deposits and having assets size of Rs.500 crore and above as on March 31, 2004. Accordingly, all such companies were required to submit a quarterly return in the prescribed format.

(The details are given in DNBS(PD) C.C. No.45/02.02/2004-05 dated November 13, 2004)

2. In September 2005, it was felt that the intervening period of a quarter does not help in quick assessments of the dynamic financial system. Therefore, it was been decided to change the periodicity to a month and all NBFCs with assets size of Rs 100 crore and above will be required to submit the return.

About time of reporting and manner of reporting, the following changes are proposed.

a) The return should be submitted within seven days of the month following the month to which it pertains. The return certified by statutory auditors may ,however, be submitted within seven days of finalisation of final accounts.

b) So far companies were not indicating clearly categories viz: Loan, Investment, Hire Purchase, Leasing, etc. Hence forth the companies will be required to indicate clearly their classification in return under company profile item 7.

c) The return will be submitted to the Regional Office under whose jurisdiction the company is located. A copy of the return may also be submitted by e-mail to DNBS, CO, Mumbai immediately followed by a hard copy. The e-mail address of DNBS, Central Office, Mumbai is given below:- helpdnbs.@rbi.org.in

The format of the return has also been revised which is enclosed with this circular. Non submission of the return will be viewed seriously and penal action will be taken for such non compliance.

(The details are given in DNBS(PD) C.C. No.57 /02.05.15/ 2004-05 dated September 6, 2005)

3. In April 2006 certain additional parameters were added to the information being called from non-deposit taking NBFCs with Asset size of Rs 100 crore and above. The changes proposed in the format of return are on a) Requirement relating to Profit and Loss Account b) Asset Classification, c) Bank's/FIs exposure on the company, d)Part VIII: Capital Market Exposure, e**)** Foreign Sources of Funds

It was also decided that revised reporting arrangement may be given effect to after two months. Accordingly, data submission in the old format was to continue up to the month of June 2006 and the first monthly return in the revised format was to be required to be submitted for the month of July 2006.
(The details are given in DNBS (CMDI) C.C. No. 67 /21.05.15/2005-06 dated April 5, 2006 and DNBS (CMDI) C.C. No. 69 /21.05.15/2005-06 dated June 2, 2006 .

Financial Regulation of Systemically Important NBFCs and Banks' Relationship with them

4. Non Banking Financial Companies (NBFCs) play a crucial role in broadening access to financial services, enhancing competition and diversification of the financial sector. They are increasingly being recognised as complementary to the banking system, capable of absorbing shocks and spreading risks at times of financial distress. The application of different levels of regulations to the activities of banks and NBFCs, and even among different categories of NBFCs, has given rise to some issues arising out of this uneven coverage of regulations. The Reserve Bank of India had, therefore, set up an Internal Group to examine the issues relating to level playing field, regulatory convergence and regulatory arbitrage in the financial sector. Based on the recommendations of the Internal Group and taking into consideration the feedback received thereon, it was decided to put in place a revised framework to address the issues pertaining to the overall regulation of systemically important NBFCs and the relationship between banks and NBFCs. Accordingly, a draft of the proposed guidelines

were issued vide letter DBOD.No.FSD.556/ 24.01.02/ 2006-07 dated November 3, 2006, seeking feedback from banks and NBFCs. Based on the feedback received, the draft guidelines were suitably revised and second draft guidelines issued for further comments vide DBOD.No.FSD.5046/24.01.028/2006-07 dated November 30, 2006. On the basis of the feedback received, final guidelines are now issued for implementation.

Modifications to the Regulatory Framework

16. In the light of the concerns that arise out of the divergent regulatory requirements for various aspects of functioning of banks and NBFCs and keeping in view the broad principles for the proposed revision, the following modifications are being made in the regulatory framework for NBFCs.

A. Regulatory Framework for Systemically Important NBFCs – ND (NBFC – ND – SI)

(i) Determination of NBFC – ND – SI

All NBFCs – ND with an asset size of Rs. 100 crore and more as per the last audited balance sheet will be considered as a systemically important NBFC **–** ND.

(ii) Capital Adequacy Ratio for NBFCs – ND – SI

NBFCs – ND – SI shall maintain a minimum Capital to Risk-weighted Assets Ratio (CRAR) of 10%. The present minimum CRAR stipulation at 12 % or 15%, as the case may be, for NBFCs – D shall continue to be applicable.

(iii) Single / Group Exposure norms for NBFCs – ND – SI

Exposure norms were laid down for NBFC-ND-SIs.

Further, the NBFCs – ND – SI are advised to have a policy in respect of exposures to a single entity / group. NBFCs-ND-SI not accessing public funds both directly and indirectly may apply to the Reserve Bank for an appropriate dispensation consistent with the spirit of the exposure limits.

B. Additional Single Exposure norms for Asset Finance Companies

(iv) In terms of circular DNBS.PD.CC.No.85/03.02.089/2006-2007 dated December 6, 2006, companies financing real/physical assets for productive /economic activity will be classified as Asset Finance Companies (AFCs) as per the criteria prescribed therein.

In addition to the single party and single group of parties exposure norms prescribed for NBFCs-D and NBFCs-ND-SI, AFCs are permitted to exceed the exposure to a single party and single group of parties up to a further 5 percent of their owned fund in exceptional circumstances with the approval of their Boards.

C. Expansion of activities of NBFCs through automatic route

(v) NBFCs set up under the automatic route will be permitted to undertake only those 19 activities which are permitted under the automatic route. Diversification into any other activity would require the prior approval of FIPB. Similarly a company which has entered into an area permitted under the FDI policy (such as software) and seeks to diversify into NBFC sector subsequently would also have to ensure compliance with the minimum capitalization norms and other regulations as applicable.

Effective date and transition

17. Taking into account the likelihood that some of the NBFCs may not be in compliance with some of the elements of the revised regulatory framework it has been decided to provide for a transition period up to end March 2007. Accordingly, NBFCs should comply with all elements of the revised framework with effect from April 1, 2007. In case any NBFC – ND – SI needs more time for compliance, it should apply to DNBS before the close of business on January 31, 2007 clearly indicating the reasons for

which it is not able to ensure compliance within the above period and the time frame within which it would be able to comply with all the relevant elements. This will enable the Reserve Bank to take a view on the requests by end March 2007.

Scope of application to certain categories

18. The guidelines contained in this circular will be applicable to the NBFCs as specified in the relevant paragraphs except the categories mentioned below:

i) The Residuary Non Banking Companies (RNBCs) and Primary Dealers (PDs) are subject to a separate set of regulations. The Reserve Bank will constitute an Internal Group to review the existing guidelines applicable to these entities in the light of the guidelines contained in this circular and examine the need for prescribing supplementary guidelines which will be issued separately. Till then, these entities will continue to be governed by the existing regulations.

ii) Government owned companies, as defined under Section 617 of the Companies Act, which are registered with the Reserve Bank of India as NBFCs, are exempted from certain provisions of Non-Banking Financial Companies Prudential Norms (Reserve Bank) Directions, 1998, at present. It is proposed to bring all deposit taking and systemically important government owned companies under the provisions of the said Directions which will be in conformity with the existing guidelines, including those contained in this circular. However, the date from which they are to fully comply with the regulatory framework will be decided later. These companies are, therefore, required to prepare a roadmap for compliance with the various elements of the NBFC regulations, in consultation with the Government, and submit the same to the Reserve Bank (Department of Non Banking Supervision – (DNBS)), by March 31, 2007.

(For details please refer to DNBS.PD/ CC No. 86/ 03.02.089/2006-07 dated December 12, 2006.)

Misuse of Bank Finance for hoarding – Status and Action

19. Concerns were expressed that some of the corporates / entities may be hoarding foodgrains which could have had the benefit of resources from the NBFC finance. NBFC-ND-SI (all non-deposit taking NBFCs with asset size of Rs. 100 Crore and above) were advised in February 2007 to undertake a scrutiny of their financial exposures to large borrowers for procurement of foodgrains.

The above class of NBFCs may also consider a quick scrutiny of the accounts on whom they have large exposure and confirm to themselves that funds have not been diverted for procurement of foodgrains with a view to hoarding.

NBFC-ND-SI were sensitized to this issue and hence requested to provide a comprehensive report on the above by March 10, 2007.
(As per DNBS (PD) CC. No.90/ 03.10.001/ 2006-07 dated February 23, 2007)

Supervisory Framework for Systemically Important non-deposit taking/holding NBFCs (NBFC-ND-SI)

20. To ensure adherence to compliance with the regulatory framework for Systemically Important NBFCs – ND such companies are advised to put in place a system for submission of an annual statement of capital funds, risk asset ratio etc., as at end of March every year in form NBS-7 as per prescribed format. The first such return may be submitted for the year ending March 31, 2007. The return may be submitted within a period of three months from the close of the financial year, every year.

21. Such returns may be submitted electronically and for the purpose, NBFC-ND-SI may approach the Information Division of Central Office of this Department for assignment of user-id and password for web-enabled submission of the return . A hard copy of the return duly signed by the designated authority may be filed with the Regional Office of the Department of Non-Banking Supervision in whose jurisdiction the company is registered.

(Details are in DNBS.PD/ CC.No. 93 / 03.05.002 /2006-07 April 27, 2007)

Guidelines for NBFC-ND-SI as regards capital adequacy, liquidity and disclosure norms

22. To protect the interests of the depositors, deposit taking NBFCs (NBFC-D) were subject to prudential regulation on various aspects of their functioning. However, non-deposit taking NBFCs (NBFCs-ND) were subject to minimal regulation. In the light of the evolution and integration of the financial sector, it was felt that all systemically relevant entities offering financial services ought to be brought under a suitable regulatory framework to contain systemic risk. Therefore, as a first step, it was advised vide DNBS.PD/ CC. No. 86/ 03.02.089 /2006-07 dated December 12, 2006 that all NBFCs – ND with an asset size of Rs. 100 crore and more as per the last audited balance sheet would be considered as systemically important NBFC **–** ND (NBFC-ND-SI) and specific regulatory framework involving prescription of capital adequacy and exposure norms was put in place from April 01, 2007 for such NBFCs-ND-SI.

23. On a review of the experience with the regulatory framework since April 2007, it is felt desirable to enhance the capital adequacy requirement and put in place guidelines for liquidity management and reporting, as also norms for disclosures. Accordingly, the Bank had placed on its web-site on June 2, 2008, the draft guidelines for NBFCs-ND-SI as regards the above aspects for receiving the comments of the

public. After considering the comments received from public/ NBFCs/ Associations/ banks, the guidelines have been modified suitably.

Capital adequacy

24. NBFCs – ND – SI were advised to maintain a minimum Capital to Risk- Assets Ratio (CRAR) of 10% with effect from April 01, 2007. However, in view of recent international developments, the risks associated with highly leveraged borrowings and reliance on short term funds by some NBFCs to fund long gestation assets, concerns have arisen regarding the enhanced systemic risk associated with the activities of these entities. Keeping in view the importance of providing adequate capital charge for the same in order to enhance the cushion for any shocks, it has been decided to increase the minimum capital to risk assets ratio (CRAR) for NBFCs-ND-SI from the present prescription of 10%. They are advised to achieve 12% CRAR by March 31, 2009 and further 15% CRAR by March 31, 2010.

25. As announced in the Annual Policy Statement for 2008-09 a review of CRAR for NBFCs-ND-SI was done and it was raised from 10 per cent to 12 per cent by March 31, 2009 and further to 15 per cent by March 31, 2010, in terms of circular DNBS (PD). CC. No. 125/03.05.002 / 2008-2009 dated August 1, 2008. Taking into account the difficulty in raising equity capital in the current economic environment, it has been decided to defer the implementation of CRAR of 12 per cent and 15 per cent to March 31, 2010 and March 31, 2011 respectively. (modification made vide Circular DNBS.PD/CC.No.138 /03.02.002 / 2008-2009 dated April 24, 2009)

Disclosure in the Balance Sheet

26. In the light of the concerns as expressed above, the disclosure norms in respect of NBFCs-ND-SI have been reviewed and it has been decided that such Systemically Important NBFCs-ND shall make additional disclosures in their Balance Sheet from the year ending March 31, 2009 relating to:

Capital to Risk Assets Ratio (CRAR)

Exposure to real estate sector, both direct and indirect; and

Maturity pattern of assets and liabilities

The format of disclosure of this additional information is furnished in Company Circular DNBS (PD). CC. No. 125/03.05.002 / 2008-2009 dated August 1, 2008

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Asset Liability Management (ALM) – Reporting

27. To address concerns regarding Asset Liability mismatches and interest rate risk exposures, an ALM System was introduced for the Non-Banking Financial Companies (NBFCs) as part of their overall system for effective risk management in their various portfolios vide Company Circular DNBS (PD).CC.No.15 /02.01 / 2000-2001 dated June 27, 2001. While it was stated therein that the guidelines would be applicable to all NBFCs irrespective of whether they are accepting / holding public deposits or not, to begin with, NBFCs meeting the criteria of asset base of Rs.100 crore (whether accepting / holding public deposits or not) or holding public deposits of Rs. 20 crore or more (irrespective of their asset size) as per their audited balance sheet as of March 31, 2001 were required to put in place the ALM System. The companies were advised that the guidelines should be fully operationalised by the year ending March 31, 2002. A system of half yearly reporting was also put in place for NBFCs holding public deposits.

28. In view of the possibilities of leveraged investments, and asset liability mismatches resulting from use of short term sources to fund NBFC activities, it has now been decided to introduce a system of reporting for NBFCs-ND-SI in the format as prescribed. The return will comprise of:

(i) Statement of short term dynamic liquidity

(ii) Statement of structural liquidity and

(iii) Statement of Interest Rate Sensitivity.

To enable the above class of NBFCs to fine tune their existing MIS to meet the requirement of the reporting dispensation, such compilation would commence with effect from the period ending September 30, 2008. The periodicity of the Statement of short term dynamic liquidity [NBS-ALM1] shall be monthly and that of Statement of structural liquidity [NBS-ALM2] half-yearly. It shall be submitted within 10 days of the close of the month to which it relates and half yearly statement within 20 days of the close of the half year to which it relates to the Regional Office of the Department in whose jurisdiction the NBFC is registered. However, to enable the NBFCs to fine tune the system, the first return for the period ended September 2008 would be submitted by the 1st week of January 2009.

The compilation frequency of Statement of Interest Rate Sensitivity [NBS-ALM3] would be half yearly. As a first step, the same shall be put up to the Board of Directors of the NBFC at half yearly intervals. The statement shall be filed with the Bank later from the date to be announced.

(Details are given in DNBS (PD).CC.No.125/03.05.002/2008-2009 dated August 1, 2008)

Enhancement of NBFCs' capital raising option for capital adequacy purposes

29. Taking into consideration, the need for enhanced funds for increasing business and meeting regulatory requirements, it has been decided that Systemically Important Non-Deposit taking Non-Banking Financial Companies (NBFCs-ND-SI) may augment their capital funds by issue of Perpetual Debt Instruments (PDI) in accordance with the guidelines contained in the circular. Such PDI shall be eligible for inclusion as Tier I Capital to the extent of 15% of total Tier I capital as on March 31 of the previous accounting year.

(Details are given in DNBS (PD) CC. No.131 /03.05.002 / 2008-2009 dated October 29, 2008)

Raising of Short Term foreign currency Borrowings - NBFCs-ND-SI

30. Systemically Important Non-Deposit taking NBFCs (NBFCs-ND-SI) have been permitted, as a temporary measure, to raise foreign currency short term borrowings under the approval route subject to certain conditions in terms of RBI Press Release: 2008-2009/602 dated October 31, 2008. In this connection, all the NBFCs-ND-SI that have availed short term foreign currency loans are advised to furnish a monthly return as per the enclosed format within 10 days from the end of the month to which it pertains. The first such return may be furnished for the month of December 2008 so as to reach Reserve Bank of India, DNBS, Central Office latest by January 10, 2009.

(For further details please refer to DNBS. PD. CC . No.132/22.10.72/ 2008-09 December 23, 2008)

Ratings of NBFCs

31. NBFCs also issue financial products like Commercial Paper, Debentures etc. to which rating is assigned by rating agencies. The ratings assigned to such products may undergo changes for various reasons ascribed to by the rating agencies. It has therefore been decided that all NBFCs (both deposit taking and non-deposit taking) with asset size of Rs 100 crore and above shall furnish the information about downgrading / upgrading of assigned rating of any financial product issued by them, within fifteen days of such a change in rating, to the Regional Office of the Bank under whose jurisdiction their registered office is functioning.

[DNBS (PD) CC. No.134/03.10.001 / 2008-2009 dated February 04, 2009]

32. **Framework for addressing the liquidity constraints of NBFCs**

The Government of India has approved a scheme for providing liquidity support to eligible NBFCs-ND-SI through a Special Purpose Vehicle (SPV) for meeting the temporary liquidity mismatches in the operations. NBFC-ND-SI

(i) should have CRAR as per extant guidelines

(ii) should have made net profit in the preceding two years

(iii) Net NPAs as on last Balance Sheet date should not be more than 5 percent

IDBI SASF Trust has been notified as Special Purpose Vehicle for undertaking this operation. The SPV will purchase the short term papers from eligible NBFCs-ND-SI to meet temporary liquidity mismatches.
(Details are given in DNBS (PD) CC.No.136 /03.10.001/2008-09 dated February 18, 2009)

Criteria for deciding NBFC-ND-SI status

33. A non-deposit taking NBFC with an asset size of less than Rs. 100 crore as on balance sheet date might subsequently add on assets before the next balance sheet date due to several reasons including business expansion plan. It is clarified that once an NBFC reaches an asset size of Rs. 100 crore or above, it shall come under the regulatory requirement for NBFCs-ND-SI as stated above, despite not having such assets as on the date of last balance sheet. Therefore, it is advised that all such non-deposit taking NBFCs may comply with RBI regulations issued to NBFC-ND-SI from time to time, as and when they attain an asset size of Rs. 100 crore, irrespective of the date on which such size is attained.

It is further observed that in a dynamic environment, the asset size of a company can fall below Rs 100 crore in a given month, which may be due to temporary fluctuations and not due to actual downsizing. It is clarified that in such a case the company may continue to submit the Monthly return on Important Financial Parameters to Reserve Bank of India and to comply with the extant directions as applicable to NBFC-ND-SI, till the submission of their next audited balance sheet to Reserve Bank of India and a specific dispensation is received from the Bank in this regard.
(Details are given in DNBS (PD) CC.No. 141 /03.10.001/2008-09 dated June 4, 2009)

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Appendix

List of circulars

Sl. No.	Circular No.	Date
1.	DNBS (PD) C.C. No. 45/ 02.02/ 2004-05	November 13, 2004
2.	DNBS (RID) C.C. No. 57/02.05.15/2005-06	September 6 , 2005
3.	DNBS (CMDI) C.C. No. 67 /21.05.15/2005-06	April 5, 2006
4.	DNBS (CMDI) C.C. No. 69 /21.05.15/2005-06	June 2, 2006
5.	DNBS.PD/ CC. No. 86/ 03.02.089 /2006-07	December 12, 2006
6.	DNBS (PD) CC. No.90/ 03.10.001/ 2006-07	February 23, 2007
7.	DNBS.PD/ CC. No. 93 / 03.05.002 /2006-07	April 27, 2007
8.	DNBS (PD). CC. No. 125/03.05.002 / 2008-2009	August 1, 2008
9.	DNBS (PD). CC.131 / 03.05.002/2008-09	October 29, 2008
10.	DNBS. PD. CC . No. /132/22.10.72/ 2008-09	December 23, 2008
11.	DNBS (PD) CC. No.134/03.10.001 / 2008-2009	February 04, 2009
12.	DNBS (PD) CC.No.136 /03.10.001/2008-09	February 18, 2009
13.	DNBS.PD/ CC. No. 138 / 03.02.002 /2008-09	April 24 ,2009
14.	DNBS (PD) CC. No. 141 /03.10.001/2008-09	June 4, 2009