प्रेस प्रकाशनी PRESS RELEASE

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March 17, 1998

RBI Seminar on New Regulatory Framework for NBFCs

The Reserve Bank of India today organised a one-day Seminar on the New Regulatory Framework for the Non-Banking Financial Companies (NBFCs). The Seminar was held at the Indira Gandhi Institute of Development Research, Mumbai.

The Seminar was attended by a cross section of NBFCs, their Associations, chambers of commerce and representatives of the Institute of Chartered Accountants of India and credit rating agencies. The purpose behind organising such a Seminar was to effectively disseminate the rationale of the revised regulatory framework for NBFCs for its better appreciation, the need for effective supervision of the NBFC sector and to share major supervisory concerns.

Shri S.P. Talwar, Deputy Governor, Reserve Bank of India delivered the Key Note Address. In his address the Deputy Governor underscored the importance played by the NBFCs and stated that the NBFCs more particularly the leasing and hire purchase finance companies, perform a very important financial intermediation role contributing to the economic development of the country. They supplement the role of banking sector to cater to the increasing financial need of a developing economy and have diversified their activities and expanded intermediation both in the areas of credit and in channelising the savings of the society. They act as agents between the savers and users of funds and offer tailor made services to both the borrowers as also the savers.

The Deputy Governor then briefly outlined the history of Reserve Bank regulations over the NBFC sector. He stated that the RBI Act was amended in January 1997 by effecting comprehensive changes in Chapter III-B and V of the Act vesting more powers with the RBI. The entire gamut of regulation and supervision over the activities of NBFCs has undergone a qualitative change both in terms of thrust and forces in the context of the amendment to RBI Act and in the light of certain disquieting developments in the NBFC sector in the recent past.

Explaining the focus of the New NBFC Policy, the Deputy Governor stated that the regulatory attention would now be on NBFCs accepting public deposit. The RBI has favoured a policy to restrict the short term and the unsecured borrowings of the NBFCs on the strength of their credit rating, the size of NOF and the activities of the companies. This, he said was important as the saving community is the fountainhead of public deposits and it was necessary to persistently maintain their confidence.

The Deputy Governor assured that the Reserve Bank of India had an open mind and was willing to sympathetically consider the genuine difficulties of the NBFCs in compliance with the new regulatory framework. He stated that the new regulations have already been relaxed once in response to the request made by NBFCs.

The Deputy Governor elaborated on the steps taken by the Reserve Bank to put in place an effective supervisory mechanism over NBFCs. He said that the Reserve Bank has brought out a comprehensive Inspection Manual and has devised Special formats for Off-site Reporting/Monitoring. Companies with asset size of Rs.100 crore and above have been asked to furnish an Annual Return giving the comparative position of their operational data for 3 years in regard to various items of their balance sheet, profit and loss account and certain key ratios. It is the intention that the On-site Inspection should be more by exception, than a routine activity. Accordingly, On-site Inspection of NBFCs will be carried out on a random basis taking into account the record of their compliance with the Directions and prudential norms, incidence of complaints, problem companies and will cover the NBFCs having large amounts of public deposits. The remaining companies will be mainly subjected to Off-site Surveillance and scrutiny of Statutory Returns, Balance Sheets, Profit & Loss Account, Auditor's Reports, etc. The Reserve Bank proposes to network Central Office with all the Regional Offices to build up profile of the companies and reduce response time in follow up of the irregularities with the erring NBFCs. All the returns are to be computer compatible and their processing has to be computerised so as to facilitate their scrutiny without any delay. These returns are to serve the objective of off-site surveillance. The Reserve Bank has opened 16 Regional Offices of the Department to serve the NBFC sector at a place nearer to the place of their registered offices.

Stressing on the need for depositors' education, the Deputy Governor stated that the Reserve Bank has a plan for educating general public through media. The purpose of this campaign is to explain to the masses at large that they may look into certain aspects of functioning of the concerned NBFC and certain other features in its deposit schemes while making deposits with it. He, however, pointed out that this is the task which the NBFCs themselves or the Self Regulatory Organisation should undertake.

The Deputy Governor also mentioned that the Reserve Bank of India has taken up the matter of offering insurance to depositors of the NBFCs with General Insurance Corporation of India with a request to consider formulating a scheme for deposit insurance for NBFCs. The Deputy Governor also stressed the need for ensuring the quality of assets created by the NBFCs which has a direct bearing on the financial viability and depositors' confidence.

The Deputy Governor stated that the Reserve Bank had received 37,478 applications from existing companies. Of these, 9074 companies were found to have NOF of Rs. 25 lakh and above. Of these again, 2371 companies were accepting public deposits. The Reserve Bank has already approved 2540 NBFCs for registration and the application of 15 NBFCs have been rejected. It is intended to complete the process of registration by end June 1998. The Deputy Governor advised that it is now enjoined upon the statutory auditors of NBFCs to directly report to the RBI the cases where applications for certificate of registration have not been made to the Reserve Bank. He cautioned that any failure to do so on the part of both the NBFCs and their auditors will attract severe penalties as provided for under the RBI Act.

In conclusion the Deputy Governor reiterated the objective of the regulation and supervision as also the mission of RBI is to ensure that -

i. the financial companies function on healthy lines;
ii. these companies function as a part of the financial system within the policy framework, in such a manner that their existence and functioning do not lead to systemic aberrations;
iii. the quality of surveillance and supervision exercised by the Bank over the NBFCs is sustained by keeping pace with the developments that take place in this sector of the financial system; and that
iv. the depositors' interest is safeguarded.

He hoped that that 3 to 5 years down the line, an efficient, viable and vibrant NBFC sector would emerge.

In their presentations, the associations of the NBFCs and chambers of commerce welcomed the regulations but suggested substitution of mandatory requirement of investment grade credit rating by the supervisory rating as per the recommendations of Khanna Committee for acceptance of deposits from public more particularly for small companies engaged in hire purchase finance and equipment leasing activities. They requested for certain relaxations in regard to provisioning norms on NPAs against lease and hire purchase assets and valuation of unquoted investments or staggering these provisioning norms so as to allow them some time to adjust to the new norms. They urged for a level playing field for NBFCs in the matters of tax reliefs as are available to banks and financial institutions. They also sought a few clarifications on certain provisions of the RBI Directions. The Associations suggested for a developmental role for the RBI to visualise some measures to improve their liquidity position in times of crises so as to avoid any adverse impact on the credibility with the depositors. The NBFCs supported the idea of insurance for NBFC deposits.

(Alpana Killawala)
General Manager

Press Release : 1997-98/847