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NBFCS - TYPES OF NBFCS AND THEIR ROLES

They are progressively evolving into a vital part of our financial system and serving the vital objective of sustained and inclusive economic developments.

NBFCs are typically into funding of:

- Construction equipments
- Commercial vehicles and cars
- Gold loans
- Microfinance
- Consumer durables and two wheelers
- Loan against shares etc.

- **NON-BANKING FINANCIAL COMPANY (NBFCs)**
- The Reserve Bank of India Act, 1934 (RBI Act) defines **a "non-banking financial financial institution which is a company;**
- a non-banking institution which is a **company and which has as its principal business the receiving of deposits, under any scheme or arrangement or in any other manner, or lending in any manner;**
- such other non-banking institution or class of such institutions, as the Bank may, **with the previous approval of the Central Government and by notification in the Official Gazette, specify**.

- As defined under section 45-I(e) of the RBI Act, a "non-banking institution" means a company, corporation or cooperative society.

- Further, the Act defines a "company" as a company as defined in **section 3 of the Companies Act, 1956 and includes a foreign company within the meaning of section 591 of that Act**.

- An NBFC is engaged in the business **of loans and advances, acquisition of shares/ stocks/bonds/debentures/securities issued by the Government or local authority or other marketable securities of a like nature, leasing, hire-purchase, insurance business, chit business** but does not include any institution whose principal business is that of agricultural activity, industrial activity, purchase or sale of any goods (other than securities) or providing any services and sale/purchase/construction of immovable property.

In terms of Section 45-1A of the RBI Act, a non-banking financial **company can commence or carry on the business of non-banking financial institution subject to**

a) Obtaining a certificate of registration from the Bank (RBI)

b) Having a net owned funds of minimum of ₹200 lakh.

EXEMPTIONS FROM REGISTRATION WITH RBI

In terms of powers given to RBI, to obviate dual regulation, certain categories of NBFCs as mentioned below, which are regulated by other regulators are exempted from the requirement of registration with RBI:-

- Venture Capital Fund/Merchant Banking companies/ Stockbroking companies registered with SEBI

- Insurance company holding a valid Certificate of Registration issued by IRDA
- Nidhi companies as notified under section 620A of the Companies Act, 1956
- Chit companies as defined in clause (b) of section 2 of the Chit Funds Act, 1982
- Housing finance companies regulated by NHB
- Stock Exchange or a Mutual Benefit Company.

TYPES OF NBFCs AND THEIR ROLE IN PROMOTING INCLUSIVE GROWTH

a) Liabilities Based Classification

- NBCs are classified on the basis of liabilities into two categories, viz., Category 'A' companies, (**NBFCs having public deposits** or NBFCs-D), and Category 'B' companies, (**NBFCs not having public deposits** or NBFCs-ND).
- NBFCs-D are now subject to requirements of capital adequacy, liquid assets maintenance, exposure norms (including restrictions on exposure to investments in land, building and unquoted shares), Assets & Liability Management (ALM) discipline, reporting requirements

b) Activity Based Classification

Presently NBFCs are classified in terms of activities into five categories, viz., **Loan Companies (LCs), Investment Companies (ICs), Asset Finance Companies (AFCs), Infrastructure Finance Companies (IFCs)** and

Systemically Important Core **Investment Companies** (CICs-ND-SI).

c) Size Based Classification

In 2006, non-deposit taking NBFCs with assets of ₹100 crore and above were labelled as Systemically Important Non-Deposit taking NBFCs (NBFCs-ND-SI), and prudential regulations such as capital adequacy requirements, exposure norms along with reporting requirements were made applicable to them. Capital Market Exposure (CME) and ALM reporting and disclosure norms were made applicable to them at different points of time.

The different types of NBFCs are:

1) Asset Finance Company (AFC) : An AFC is a company which is a financial institution carrying on as its principal business the financing of physical assets supporting productive/economic activity, such as automobiles, tractors, generator sets, earthmoving and material handling equipment's etc. Principal business for the purpose is defined as aggregate of financing real/physical assets supporting economic activity and income arising therefrom is not less than 60% of its total assets and total income respectively.

2) Systemically Important Core Investment Company (CIC-ND-SI) :

CIC-ND-SI is a NBFC carrying on the business of acquisition of shares and securities satisfying the following conditions:

a) It **holds not less than 90% of its total assets in the form of investments in equity shares, preference shares, debts or loans in group companies.**

b) Its asset size is ₹100 crore or above.
c) It accepts public funds.
d) It **does not carry on any other financial activity referred to in section 45-1(c) and 45-I(f) of the RBI Act, 1934 except investment in bank deposits, money market instruments, government securities, loans to and investments in debt issuance** of group companies or guarantees issued on behalf of group companies.
e) Adjusted Net Worth of CIC-ND-SI shall **at no point of time be less than 30% of its aggregate risk weighted assets on the balance sheet date** and risk adjusted value of off-balance sheet items as on the date of the last audited balance sheet.

3) Loan Company (LC): LC refers to any firm that is a financial institution that provides finance, whether through loans or advances or otherwise, for any activity other than its own, but does not include an asset finance company.

4) Investment Company (IC) : IC means any company which is a financial institution **carrying on with the acquisition of securities** as its principal business.

5) Infrastructure Finance Company (IFC): IFC is a non-banking finance company which **deploys at least 75% of its total assets in infrastructure loans, has a minimum net owned funds (NOF) of ₹300 crore**, and has a minimum credit rating of 'A' or equivalent and a Capital to Risk Weighted Assets Ratio (CRAR) of 15%.

6) Infrastructure Debt Fund (IDF) - Non Banking Financial Company (IDF-NBFC) : IDF-NBFC is a company registered as NBFC to facilitate **the flow of long term debt into infrastructure projects**. IDF-NBFC raises resources through issue of Rupee or Dollar denominated bonds of minimum 5 years maturity. Only Infrastructure Finance Companies can sponsor IDF-NBFCs.

7) Non-Banking Financial Company-Micro Finance Institutions (NBFC-MFI) : NBFC-MFI is a non deposit taking NBFC **having not less than 85% of its assets in the nature of qualifying assets** which satisfy the following criteria:

a) Loan disbursed by an NBFC-MFI to a borrower with a rural household annual income not exceeding ₹1,00,000 or urban and semi-urban household income not exceeding ₹1,60,000;
b) Loan amount does not exceed ₹50,000 in the first cycle and & ₹1,00,000 in subsequent cycles;
c) Total indebtedness of the borrower does not exceed ₹1,00,000;
d) Tenure of the loan not to be less than 24 months for loan amount in excess of ₹15,000 with prepayment without penalty;
e) Loan to be extended without collateral;
f) Loan is repayable in weekly, fortnightly or monthly instalments; vii. Aggregate amount of loans given for income generation, is not less than 50% of the total loans given by the MFIs.

8) Non-Banking Financial Company-Factors (NBFC-Factors): NBFC-Factor is a non-deposit taking NBFC engaged in the principal business of factoring**. The financial assets in the factoring business should constitute at least 50% of its total assets and its income derived from factoring business should not be less than 50% of its gross income.**

9) Mortgage Guarantee Companies (MGC): **MGC are financial institutions for which at least 90% of the business turnover is mortgage guarantee business or at least 90% of the gross income is from mortgage guarantee business, with net owned funds at ₹100** crore at the time of commencement of business, which shall be reviewed for enhancement after 3 years.

10) NBFC-Non-Operative Financial Holding Company (NOFHC): NOF-HC is financial institution through which **promoter/promoter groups will be permitted to set up a new bank**. It is **a wholly owned Non-Operative Financial Holding Company (NOFHC) which will hold the bank as well as other financial services companies regulated by RBI or other financial sector regulators.**

11) NBFC-Account Aggregator: RBI (the Bank) in exercise of the powers conferred under section 45JA of the RBI Act has issued directions for compliance by every non-banking financial company undertaking the business of Account Aggregator vide Master Direction - Non-Banking Financial Company - Account Aggregator (Reserve Bank) Directions, 2016. Account Aggregator' means a non-banking financial company as

stated in sub-clause (iii) of clause (f) of Section 45-1 of the RBI Act that undertakes the business of an account aggregator for a fee or otherwise

12) **Residuary Non-Banking Companies (RNBCs):** Residuary Non-Banking Company is a company the principal business of which is acceptance of deposits, under any scheme or arrangement or in any other manner and not being Investment, Asset Financing or Loan Company.

REGULATORS OF NBCs

Overview of Regulators of Non-Banking Companies

Companies
(Registered under Section 3 of the Companies Act 1956)

NBFCs registered with RBI
Regulation. Supervision. Surveillance & Enforcement under RBI

NBFCs Registered by Other Regulators

Type of Financial Institutions	Authority for Regulation, Supervision, Surveillance & Enforcement
Housing Finance Institutions	National Housing Bank
Merchant Banking Company, Venture Capital Fund Companies, Stock Broking, Collective Investment Schemes (CIS)	SEBI
Nidhi Companies, Mutual Benefit Companies	MCA
Chit Fund Companies	State Government
Insurance Companies	IRDA

Non Banking Non Financial Companies
Regulation. Supervision and Surveillance under the Companies Act 1956.
Regulator : Ministry of Corporate Affairs (MCA)
Enforcement Agency : State Governments

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Some of the important regulations/guidelines relating to acceptance of deposits by NBCs are:

a) The NBCs are allowed to accept/renew public deposits for a **minimum period of 12 months and maximum period of 60 months.** They cannot accept deposits repayable on demand.
b) NBFCs **cannot offer interest rates higher than the ceiling rate prescribed by RBI from time to time**. The interest may be paid or compounded at rests not shorter than monthly rests.
c) NBFCs cannot offer gifts/incentives or any other additional benefit to the depositors.
d) NBFCs **should have minimum investment grade credit rating**.
e) The deposits with **NBFCs are not insured.**
f) The repayment of deposits by NBFCs is not guaranteed by RBI.
g) Certain mandatory disclosures are to be made about the company in the Application Form issued by the company soliciting deposits.
h) Only those NBFCs to which the Bank had given a specific **authorisation and have an investment grade rating are allowed to accept/hold public deposits to a limit of 1.5 times of its Net Owned Funds**
i) If an NBFC defaults in repayment of deposit, the depositor can approach the Company Law Board or the Consumer Forum or file a civil suit in a court of law to recover the deposits.
j) **There is Ombudsman for hearing complaints against NBFCs**. However, in respect of credit card operations of an NBFC, which is a subsidiary of a bank

k) Deposit taking NBFCs may get itself rated by any of the six rating agencies **namely, CRISIL, CARE, ICRA, FITCH Ratings India Pvt. Ltd, Brickwork Ratings India Pvt. Ltd. and SMERA.** Liquid assets requirement for the deposit taking

COMPANIES ACT, 2013 - RECENT CHANGES

The 2013 Act introduces major changes relating to governance, compliance and enforcement, disclosure norms, e-management, auditors and mergers and acquisitions. It has also introduced several new concepts **like one-person company, small company, dormant company, class action suits, registered values and Corporate Social Responsibility (CSR).**

Some of the major changes are:

a) **One Person Company (OPC)** : The Act has introduced a company with only one person as a member.

b) **Private Company:** The upper limit on the number of members of a private company has been raised from 50 to 200.

c) **Small Company :** The Act has introduced the concept of a small company, which is a company other than a public limited company with a paid-up capital not exceeding ₹50 lakh or such higher amounts as may be prescribed, which shall not be more than ₹5 crore and a turnover as per last profit and loss account not exceeding ₹2 crore or such higher limit prescribed which shall not be more than ₹20 crore.

d) **Dormant Company:** This is a company formed for a future project or to hold an asset or intellectual property and has no significant accounting transaction.
e) **Financial Year:** Uniform accounting year for all companies with period ending on 31st March of every year, with certain exceptions included has been introduced.
f) **Consolidated Financial Statements (CFS) :** CFS is now mandatory for companies having a subsidiary or an associate or a joint venture in addition to standalone financial statements.
g) **Mandatory Auditor Rotation and joint auditors:** The 2013 Act mandates the rotation of auditors after the specified time period. It includes provision for joint audits.
h) **Secretarial Audit For Big Companies:** Companies with paid up capitals ₹100 crore would be required to annex a secretarial audit report given by a Company Secretary in practice with its Board's report.
i) **National Financial Reporting Authority (NFRA):** The 2013 Act requires constitution of NFRA, which has been bestowed with significant powers in issuing authoritative pronouncements and regulating the audit profession
j) **Corporate Social Responsibility (CSR):** It requires a Board approved corporate social responsibility policy to be formulated by the company and incur a minimum expenditure on social activities. The CSR expenditure has to be **at least 2% of the average net profits of the immediately preceding 3 years and in the event of not spending the amount**. Explanation has to be given for the reasons thereof in the directors report.

k) **Class action suits:** It introduces a new concept of class action suits which can be initiated by shareholders against the company and the auditors.

l) **Woman Director:** The 2013 Act requires at least one woman Director on the Board to encourage gender diversity.

m) **Acceptance of deposits and Enhancing the protection of depositors:** The 2013 Act states that only those companies which meet such net worth or turnover criteria as may be prescribed can accept deposits from individuals. Such companies will also be required to obtain credit rating from a recognised credit rating agency, shall have to provide deposit insurance and maintain deposit reserve account.

n) **Registered Valuers:** The 2013 Act has introduced a new concept of registered valuers for providing valuation under various sections.

o) **Number of Directorship:** The 2013 Act increases the limit of the number of directorships that can be held by an individual from 12 to 15. One director has to be resident in India.

p) **Appointment of key managerial personnel:** The 2013 Act requires mandatory appointment of following whole time key managerial personnel for every listed company and other companies having a paid-up share capital of ₹5 crore or more.

- Managing Director, or Chief Executive Officer or Manager and in their absence a Whole time Director
- Company Secretary
- Chief Financial Officer

HIGHLIGHTS OF THE COMPANIES (AMENDMENT) ACT, 2015

a) Requirement of minimum paid up share capital has been done away with.
b) Common Seal made optional
c) **Declaration of dividend :** No company shall declare dividend unless carried over past losses and depreciation in previous years are set off against profit of the company for the current year.
d) Punishment for Contravention of provisions of Sections 73 and 76 (pertaining to acceptance of deposits by a company) by introducing Section 76A.

- As per the amendment, in addition to payment of amount of deposit or part and the interest due, the company shall be punishable with a fine not less than ₹1crore which may extend to ₹10 crore.
- In addition, every officer of the company who is in default shall be liable to be punished with imprisonment which may extend to seven years or with a fine not less than 25 Lakh extendable to 2 Crore or both.