RBI to Review NBFCs

Source: BL

Why in News?

The **Reserve Bank of India (RBI)** is gearing up to conduct a comprehensive review of the categorisation of Non-Banking Finance Companies (NBFCs) **in 2024.**

- The review is seen as a precursor to potentially granting bank licences to select NBFCs.
- Elevating specific NBFCs could serve as a preliminary and evaluative step towards considering them for the allocation of bank licences in the future.

What are NBFCs?

- **About:** An NBFC is a company registered under the **Companies Act, 1956 or** Companies Act, 2013, involved in various financial activities like lending, investing in securities, leasing, insurance.
    - They offer various banking services but do not have a banking licence.
- **Key Features:**
    - NBFCs provide diverse financial services like personal loans, home loans, vehicle loans, gold loans, microfinance, insurance, and investment management.
    - They can accept public deposits for a minimum of **12 months and a maximum of 60 months.**
        - However, NBFCs **cannot accept demand deposits.**
    - They **do not form part of the payment and settlement system** and cannot issue cheques drawn on itself.
- **Classification:**
    - **On the Basis of Deposits:**
        - Deposit-taking non-banking finance companies
        - Non-Deposit taking Non-Banking Financial Institutions
    - **On the Nature of their Major Activity:**
        - Investment and Credit Company
        - Consumer Durable Loan Finance
        - Core Investment
        - Company (CIC)
        - Infrastructure Finance Company (IFC)/Infrastructure Debt Fund (IDF)
        - Asset Reconstruction Companies (ARC)
        - Factoring Companies
        - Gold Loan Companies
        - Fintech cos: P2P Lenders
- **Licencing:** The company must be registered under the **Companies Act, 2013**, either as a public or private company.
    - The company should have a minimum net owned fund of at least Rs. 10 crores to be eligible for NBFC registration.
    - At least **one-third of the directors** of the company must possess relevant work experience in the finance sector.
    - The company should have a good track record with **CIBIL (Credit Information Bureau India Limited)** regarding its credit history and financial credibility.

    - The company must comply with all the regulations, norms, and guidelines prescribed under Capital Compliances and the **Foreign Exchange Management Act (FEMA) laws.**
- **Regulation:** The RBI has been given the powers under the **RBI Act 1934** to register, lay down policy, issue directions, inspect, regulate, supervise and exercise surveillance over NBFCs that meet the **50-50 criteria of principal business.**
    - The Reserve Bank introduced the Scale Based Regulation (SBR) in October, 2021, categorising NBFCs into **Base Layer (NBFC-BL), Middle Layer (NBFC-ML), Upper Layer (NBFC-UL), and Top Layer (NBFC-TL).**
    - This framework outlines the methodology for identifying NBFCs in the Upper Layer based on their asset size and scoring criteria.

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List of NBFCs in upper layer

1	LIC Housing Finance	9	Shanghvi Finance Pvt Ltd
2	Bajaj Finance	10	M&M Financial Services
3	Shriram Finance	11	PNB Housing Finance
4	Tata Sons Pvt Ltd	12	Tata Capital Financial Services
5	L&T Finance	13	Aditya Birla Finance
6	Indiabulls Housing Finance	14	HDB Financial Services
7	Piramal Capital & Housing Finance	15	Muthoot Finance
8	Cholamandalam Investment and Finance	16	Bajaj Housing Finance

What is the 50-50 Criteria of Principal Business?

- RBI considers a company's principal business to be financial in nature if more than **50% of its total assets and gross income come from financial activities.**
    - This definition ensures that only companies primarily involved in financial operations are registered as NBFCs and fall under RBI's regulatory oversight.
- Companies primarily engaged in non-financial activities, even if they conduct some financial business on the side, are not regulated by RBI.
    - This assessment is commonly referred to as the **"50-50 criteria"** for determining a company's involvement in financial business.

Note

Demand deposits refer to funds deposited in banks or financial institutions that can be **withdrawn by the account holder on demand** without any prior notice.

- They are highly liquid and accessible for day-to-day transactions, making them a preferred choice for individuals and businesses needing frequent access to their funds.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims:

Q. With reference to the Non-banking Financial Companies (NBFCs) in India, consider the following statements: (2010)

1. They cannot engage in the acquisition of securities issued by the government.
2. They cannot accept demand deposits like Savings Account.

Which of the statements given above is/are correct?

(a) 1 only
(b) 2 only
(c) Both 1 and 2
(d) Neither 1 nor 2

Ans: (b)

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