FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organization for Registered NBFCs)

101/103, Sunflower, 1st Floor, Rajawadi Road No.2, Ghatkopar (East), Mumbai – 400 077 (India)

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11th June, 2019

Smt. Nirmala Sitharaman Ji
Minister of Finance
Government of India
North Block
New Delhi - 110 001.

Hon'ble Finance Minister Madam,

SUB: PRE-BUDGET MEMORANDUM – SUGGESTIONS FOR ENHANCED CONTRIBUTION OF NON-BANKING FINANCE COMPANIES (NBFCs)

Finance Industry Development Council (FIDC) is a Self-Regulatory Organization (SRO) cum Representative Body of the NBFCs registered with the Reserve Bank of India. FIDC was formed 15 years ago and is the recognized face of the NBFC sector. We have been engaged in regular interaction both with Reserve Bank of India and Govt. of India, which include pre-budget meetings and also important policy related meetings with RBI. Almost all the leading NBFCs and a large number of small and medium sized NBFCs are our members.

Foremost, we salute and heartily congratulate you for being the first woman Finance Minister of India. We deeply appreciate the bold and effective structural reforms undertaken by your Ministry during the last five years which have resulted in India being the fastest growing economy in the world. A quantum jump in India's position in the Ease of Doing Business Index issued by the World Bank, the Sovereign rating upgrade by Moody's and India becoming one of the most preferred destinations for foreign investment and successful implementation of GST were the major achievements.

We take this opportunity to assure our full support to fulfilling the Hon'ble Prime Minister's vision of transforming India to a "Developed Economy".

Realizing PM's Vision of New India By 2022 – NBFCs to Play an Important Role

NBFCs have been the unsung and silent contributors in nation building for the past more than 8 decades now. Moody's have stated that one of the important factors, to this rating upgrade, has been the Govt"s efforts to formalize economic activity. NBFCs have played a significant role in this, by providing financial services to the unbanked segment of the population in the rural, semi urban and urban areas across the country. This has enabled these people to move away from the moneylenders and become a part of the formal economy.

Hon'ble Prime Minister Shri Narendra Modi shared his vision for building a New India by 2022 during his Independence Day speech last year. Some of the key elements of his vision are :

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- promoting entrepreneurship,
- greater focus on the lower strata of the society,
- promoting framers prosperity and
- greater use of technology to bring transparency

NBFCs Promote Financial Inclusion

NBFCs over the years have played a vital role in the development of the economy, be it in financial intermediation in rural and semi urban areas or financing activities that are engines of growth, such as transport sector, SMEs and MSMEs, leasing, hire purchase etc.

For more than 70 years now, NBFCs have been in the forefront of catering to the segment of customers who are un-bankable masses in the rural and semi–urban areas. Through strong linkage at the grassroot level, ability to take quicker decisions and highly personalized customer service, they have created a medium of reach and communication and are very effectively serving the segments that were forced to approach unorganized money lenders for all their credit needs. NBFCs have transformed a borrower, who is "unbanked" into "bankable".

Performance

As per RBI's Financial Stability Report (FSR) dated December 2018 the total Balance Sheet size of the NBFC as on 31 March,2018 stood at Rs. 26.0 lakh crores.

As per this Report, NBFCs growth during the last few years was quite impressive. Moreover, this has been a "healthy" growth as reflected in the better asset quality. Key parameters on Y-o-Y growth are:

Description		Sept (FY18)	March (FY18)
• Growth in Aggregate Balance Sheet size	=	17.20%	(18.60%)
• Net Profit (%age to total income)	=	16.20%	(22.90%)
• Gross NPA (as %age of total advances)	=	6.10%	(5.80%)
• CRAR (minimum prescribed by RBI is 15%)	=	21.00%	(22.80%)
• Leverage Ratio	=	4.00%	(3.40%)

NBFCs have performed well without compromising on compliance to the regulatory framework. Since 2014, the Regulatory Framework for NBFCs has been "harmonised" with that for banks and other financial institutions and the regulatory arbitrage has been plugged to a great extent.

Recognition of Increased Funding of MSMEs by NBFCs

NBFCs expertise and potential to finance MSMEs has been duly recognised by the apex International body like World Bank Group, Government of India and leading Financial Institutions :

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- World Bank Group has signed Engagement Letters (MOUs) with FIDC to conduct Training Programs on
  - Commercial Credit Reporting - which aim at development of alternate credit scoring models for unbanked and MSMEs who do not have any reported credit history
  - Movable Asset Based lending - which aim at developing models for financing against the security of "intangible" movable assets. This is best suited for lending to MSMEs who cannot offer any tangible movable assets as security.

- Hon'ble Prime Minister in his address to the nation on 31st December 2016 announced coverage of NBFCs under the Credit Guarantee Fund Trust for Micro and Small Enterprises (CGTMSE) - this shall give the much desired boost to aggressive financing of MSMEs by NBFCs.

Regulation of NBFCs "Harmonised" with Banks & Other Financial Institutions

The Revised Regulatory Framework for NBFCs, issued by RBI in 2014, has largely plugged the regulatory arbitrage between banks, FIs and NBFCs. Today, the regulatory norms for NBFCs in all the following key areas are at par with banks:

- Mandatory Registration with RBI along with prescribed entry level
- Minimum Capital Adequacy (CRAR) of 15% which is even higher than the banks
- Know Your Customer (KYC) Norms and all other provisions of Prevention of Money Laundering Act, 2002
- Code of Fair Business Practices
- Asset Liability Management
- Corporate Governance
- Prudential Norms on Asset Classification (NPA Classification), Income Recognition and Provisioning
- Credit Concentration Norms
- Statutory Liquidity Ratio (SLR)
- Onsite Inspection of books and accounts on annual / bi-annual basis
- Offsite surveillance– submission of Returns to RBI on monthly, quarterly & annual basis

The expert committees in the recent past have all appreciated high levels of compliance being shown by NBFCs, thereby posing lower risk to the system.

Stringent Regulation and high compliance levels, should dispel any doubts regarding the healthy and ethical functioning of NBFCs. As such, let there be no apprehension on how well NBFCs are regulated, while considering our requests.

Recent Developments in the NBFC Sector

With one of the infra financing NBFCs going down in September 2018 and the recent default by one of the large Housing Finance Companies (HFCs), have triggered a sudden change in the sentiments against the NBFC sector, which were otherwise considered a bright spot in the economy. It is important to note that Housing Finance Companies (HFCs) have a totally different business model and have a different regulator in National Housing Bank (NHB). Further, out of the 10,000 odd NBFCs registered with RBI only 08 (eight) are classified as Infrastructure Finance Companies and out of this eight, five are Public Sector Companies. It is therefore, imprudent and unfortunate that the defaults by the above said two companies is being taken as the representative picture of the entire NBFC Sector.

Request

Based on the facts stated above, we hereby request that :

- ***While the regulation relating to Asset Side of NBFCs Balance Sheet have been harmonized with that for banks and other FIs, it is the liability side which needs immediate attention. There is a crying need to create a dedicated liquidity window for NBFCs to tackle the current liquidity crunch. It is equally important to also open up funding avenues on a long term basis. Our detailed suggestions on Short Term and Long Term measures in this regard are given in Annexure -1***

- ***Tax issues as detailed in Annexure- 2 be considered favorably, to bring the much desired parity with banks, FIs including Housing Finance Companies***

- ***Recoveries need to be fast tracked and facilitated by doing away with the rider of minimum loan ticket size of Rs.1.0 cr for Enforcement of Security Interest under the SARFAESI Act , as detailed in Annexure – 3***

We shall be glad to supplement this memorandum with any additional information / clarification that may be required. We thank you in anticipation of a positive response and assure you of our full co-operation always.

Yours Faithfully,
For **FINANCE INDUSTRY DEVELOPMENT COUNCIL**

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Annexure-1

FUNDING SUPPORT TO NBFCs TO ENSURE LIQUIDITY

Important Clarification on the Current Situation

The IL&FS default in September 2018 resulted in a sudden change in the perception of the strength of the entire NBFC sector. As is typical in such situations, it is the negativity in the sentiments which plays the key role rather than the actual performance. As the representative body of the NBFC sector, we would like to clarify the following:

1. *The core issue today relates to the sudden and great impact on the growth of NBFC sector and is not a solvency issue.*
2. *This has heavily impacted the flow of credit to the key sectors of the economy like Automobiles, MSMEs and Consumer Goods, which have suffered heavily.*
3. *Defaults by one Infrastructure Financing NBFC and a Housing Finance Company do not represent the actual picture of the NBFC sector*
4. *The typical NBFC model is a heavily retail and small business focused lending model with an average asset tenure of 2-5 years.*
5. *Therefore, asset liability mismatch is practically a non-issue for NBFCs and is more relevant for long term infra project financing and housing finance companies.*
6. *While the flow of bank funds to NBFCs has dropped since October 2018, the recent data released by RBI on sectorial deployment of bank credit presents a different picture. This is because the figure for bank credit to NBFCs includes Government owned NBFCs.*

Banks are the Major Contributors to Funding NBFCs

Banks continue to be the major source of funding for NBFCs. When it comes to Small and Medium NBFCs, (which comprise of 95% of the total number of NBFCs) banks are the only option. The major concern arising as a fall out of this negativity has been a sudden change in attitude and the perception that majority of the public-sector banks have shown towards NBFCs. The most disturbing aspect has been the apprehension and reluctance on the part of the banks to continue with the existing lending arrangements to NBFCs. Instances of banks withdrawing the unutilized lines of credit or showing apprehension / reluctance in renewal/rolling over the existing credit lines have been reported by some of our members. While they are willing to buyout NBFC portfolios but that is merely a band aid solution which does not ensure growth of NBFCs.

RBI has taken measures to address overall liquidity in the system by way of open market operations and other means. However, the liquidity thus created naturally ends up with the banks. It is the hesitation and reluctance on the part of banks to ensure percolation of this liquidity down to NBFCs which needs to be addressed immediately. The same may be done by

- incentivizing banks to fund NBFCs
- Creating a window for flow of bank credit dedicated to NBFCs

- Excluding PSU NBFCs while calculating sectoral bank exposure to NBFCs.

Funding Avenues Are Restricted

NBFCs raise most of their fund requirements through bank loans, non-convertible debentures and commercial paper. Banks are the most important source of funding for the sector, accounting for well over 50% of the resources raised by NBFCs.

In the aftermath of higher reporting of NPAs and the subsequent entry of several banks into the PCA mechanism and especially post the events of September 2018, NBFCs have found it difficult to raise growth capital from the banking system and have therefore been forced to either shrink business or resort to securitisation of their high quality assets. This has contributed to a sharp slowdown in the automobile, MSME and similar sectors which have had direct implications on capital formation, GDP growth and employment generation.

Funding avenues for NBFCs outside the banking system are heavily restricted, as

- Public Deposits are not allowed/ encouraged by RBI
- Bond Market is not developed in India
- Securitization guidelines by RBI are restrictive in nature
- There is no refinance window available to NBFCs

Refinancing of Small and Medium Sized NBFCs by MUDRA

There are a large number of small and medium sized NBFCs providing last mile credit delivery in urban, semi urban and rural areas across the country. They have been complying to the RBI norms. These companies are primarily dependent on banks for fund raising, since they do not have access to Capital markets and neither do they have any ECBs. They are feeling the real heat of the recent situation and there is an immediate need to provide a refinance window to these companies.

MUDRA was setup with the prime objective of refinancing banks, NBFCs and MFIs for on-lending to non corporate small businesses. For this purpose three categories of loans were prescribed – Shishu (upto Rs.1.0 lakh), Tarun (Rs.1.0-5.0 lakhs) and Kishore (Rs. 5.0-10.0 lakhs). While the "Shishu" category is primarily the forte of MFIs, it is the "Tarun" and "Kishore" categories which are a perfect fit for Non- Banking Finance Companies (NBFCs).

In spite of registering an impressive growth, *a study of MUDRA loans reveals that a vast majority of this growth has been in the Shishu (upto 1 lac category) while both Tarun and Kishore categories have performed far below the expectations*. Ministry of MSME, Ministry of Finance, RBI and SIDBI have all voiced their concern over this important aspect. The underlying reason for this gap is due to the fact that till date MUDRA's exposure to the NBFC sector has been negligible. Only a handful of NBFCs (out of the total number of 11,000) have been able to avail refinance from MUDRA.

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Eligibility Norms to Avail Refinance from MUDRA – A Stumbling Block for Small & Medium NBFCs

MUDRA's future expansion plans have to involve NBFCs in a big way. On the other hand small and medium sized NBFCs' future growth plans must involve MUDRA as the Refinancing body. In other words, both are an answer to each other's problems.

The major stumbling block between the two are the eligibility norms prescribed for NBFCs to avail refinance from MUDRA. If this is taken care of, then it shall not only cater to the funding needs of small and medium sized NBFCs, but also incite them to shift from acceptance of public deposits and thus save on the high regulatory compliance cost and burden.

The three key norms which are keeping NBFCs away from MUDRA are:

- Entry level Net Own Funds (NOF) prescribed by MUDRA is much above the RBI's prescribed entry level to set up an NBFC. This has resulted a large chunk of RBI registered NBFCs being ineligible

- MUDRA has prescribed a minimum investment grade credit rating for NBFCs. All the accredited Credit Rating Agencies follow the same rating model and scale, irrespective of the company's size. Therefore, obtaining a minimum investment grade credit rating for these companies is a big challenge, simply because of their size.

- MUDRA prescribes a cap on the lending rates, by prescribing a maximum spread between borrowing and lending rates of NBFCs. This has discouraged large, small and medium sized NBFCs, since any such cap makes the business uncompetitive and in some cases unviable.

MUDRA may Refinance Big NBFCs for On Lending to Small & Medium NBFCs

With funding avenues for small and medium sized NBFCs restricted, they are heavily dependent on banks, which has also been of concern to RBI. As a result, some of the big NBFCs undertake refinancing the smaller ones, especially, in case of asset financing NBFCs. Such arrangements have shown great promise and comfort and reduce the risk for any outside funding agency (including banks) whose exposure is only on the better governed and more stringently regulated NBFCs only.

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Measures to Address the Funding / Liquidity Concerns of the NBFC Sector

Short Term Measures – Need Immediate Action

1. *The crying need of the hour is to create a dedicated liquidity window for NBFCs through the banking channels. The same may be provided for a period of one year. Precedence may be drawn from a special repo window created by RBI in 2008 for banks under the liquidity adjustment facility (LAF) for on lending to NBFCs.*

2. *Since 1999, RBI had allowed all bank lending to NBFCs for on-lending to the priority sector, to be treated as priority sector lending by banks. This gave a huge incentive to banks to lend to NBFCs. While it ensured sufficient bank funding to NBFCs at a reasonable cost, it also facilitated banks to meet their PSL targets. However, this was abruptly withdrawn in 2011. The same arrangement may be restored urgently.*

3. *For Small &Medium sized NBFCs, eligibility norms for NBFCs for availing refinance from MUDRA should be made favorable by:*

    - *Allowing all RBI registered NBFCs to avail refinance*
    - *External Credit Rating criteria may be replaced by prescribing some additional financial parameters to be met, which may be more realistic and doable.*
    - *The cap of 6% on the maximum spreads allowed should be done away with, since market forces ensure that the rates are within acceptable limits*

    Systemically Important NBFCs should be Allowed to Act as Aggregators by availing refinance from MUDRA for on lending to small and medium sized NBFCs.

Long Term Measures

1. *Setup up a Permanent Refinance Window for NBFCs*

    A dedicated "Refinance window for NBFCs", on the lines of National Housing Bank (which provides refinance to Housing Finance Companies) has been a long-standing demand of the NBFC sector. The Parliamentary Standing Committee on Finance in their 45th Report dated June 2003 (relating to The Financial Companies Regulation Bill, 2000) had recommended setting up of a new refinance institution for NBFCs.

2. *Establishment of Alternate Investment Fund*

    An Alternate Investment Fund (AIF) may be established to channelize institutional funds to NBFCs.. Non-convertible debentures (secured by hypothecation of business receivables of NBFCs) could be subscribed to by the AIF for onward lending by NBFCs. These NCDs

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could be administered by investor trustees who could take care of the interests of the AIF and its constituents and would be subject to all extant guidelines in this regard. The manner of constitution of the AIF and the sources of its funds could be discussed further.

3. *"On Tap" Issuance of Secured Bonds/NCDs*

NBFCs have access to Non-Convertible Debentures ("NCDs") having flexible tenure and rates, both through the private placement (with restrictions) and public issue. While private placements have severe restrictions on the number of investors, the frequency of issue etc., public issue of bonds tends to be very expensive, laborious and inflexible.

It is proposed that NBFCs be allowed an on-tap facility for issuance of NCDs to the retail market by making the offering of NCDs through an easy to operate and less costly procedure, but with proper governance to provide investor protection and comfort. The features proposed are:

- *Bonds/NCDs to be rated minimum BBB- (minimum investment grade). Instruments must be secured and should not fall under the definition of "deposit"*
- *Company to file umbrella prospectus (valid for one year) with quarterly financial updates. In no event, can the financials be older than 4 months. This document would lay down the overall limits and the type of NCDs to be issued (deep discount/interest bearing etc.)*
- *Under this, NBFC to be allowed to issue as many NCDs as they wish in whatever frequency they wish to. There should be no need to file an updated prospectus – only updated financials may need to be filed as an addendum.*
- *There should be no need for a specific issue closure date and issue allotment date. The allotment of bonds to be similar to acceptance of deposits – with tenure being determined from the date of the application.*
- *NCDs to be marketed similar to deposits. Intermediaries may be allowed*
- *Tenure may be long term say, 2 or 3 years and upwards*
- *Given that these are secured instruments, there should be no need to maintain SLR.*
- *Governance under SEBI guidelines, with overall borrowing cap being permitted by RBI.*
- *Lead Manager to have responsibility of reporting to SEBI & RBI on quarterly basis*
- *Grievance redressal mechanism similar to deposit acceptance regime; access for investors to SEBI and RBI Ombudsman*
- *Minimum investment amount could be low – say, Rs 10,000/- so that greater retail participation is possible.*
- *Instruments would be listed and tradeable on a recognised stock exchange to provide liquidity to retail investors.*

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4. *Need to Have A Regular Dialogue*

   Today, inspite of playing an important role in the economy, the NBFC sector does not have a platform to engage with Ministry of Finance on a regular basis. In a fast changing scenario, a structured dialogue on a regular basis is an important need of the hour. This acts as a two way flow of information and areas of concern. It also enables the policy makers to get first hand market report.

   It is therefore requested that a mechanism for structured dialogue may be developed to ensure regular meetings (at least twice a year) between senior officials of Department of Financial Services at Ministry of Finance with FIDC as the representative body of NBFCs.

Annexure-2

DIRECT TAX

1. TDS On Interest (Sec 194A) – Request For Exemption

As per section 194A of the Act, any person making payment of interest is required to deduct tax at source ('TDS') @ of 10%. There are certain exemptions given under this section wherein the person making payment to various institutions like Banking Company, Life Insurance Companies and UTI etc., is not required to deduct TDS. Accordingly, any person making payment of interest to Banks is not required to deduct tax

However, no such exemption has been provided to NBFCs from the applicability of section 194A. Accordingly, tax is required to be deducted at the rate of 10 percent from interest paid to NBFCs. This creates severe cash flow constraints since NBFCs operate on a thin spread/ margin on interest which at times is even lesser than the TDS on the gross interest. Further, due to enormous transactions, NBFCs have to face severe administrative hardship in terms of collection of TDS certificates from their thousands of customers.

The additional limitations of the existing system are the following:

a) Follow up with every customer for TDS certificates every quarter (details of which are mandatory for claiming the same in the I. T. return) becomes almost impossible. NBFCs have clients who number in thousands and it is practically very difficult to collect details from everyone.

b) Even if the TDS certificate is issued by the customer, if TDS return has not been filed or not filed properly, the credit for such TDS would not be granted to the NBFC as the details of such TDS would not appear in the NSDL system.

c) Once the TDS credit is disallowed, the NBFCs have a hard time following up with the customers and the exchequer has a hard time clearing outstanding demands against NBFCs which, in reality, do not exist.

Co-orgination of Loans by Banks and NBFCs

RBI vide its notification dated 21st September, 2018 has allowed banks and NBFCs on Co-origination of Loans to the priority sector. As per this, a single borrower may be co-funded by bank and a NBFC in a pre-determined ratio. Both bank and NBFC may price the loan independently. However, the borrower shall be offered a single blended rate of interest. All the repayments made by the borrower (including the interest) by way of EMIs shall be made to an escrow account from where the amounts shall be credited to the bank and NBFC in respective proportion.

In such a scenario, the borrower shall not be in a position to determine the exact interest component of the NBFC portion and hence TDS deduction shall be practically impossible. It is therefore important to bring both bank and NBFC at par on the TDS provisions.

<u>Exemption May be Granted to Non-Deposit Taking Systemically Important NBFCs (NBFC-ND-SI) and Deposit Taking NBFCs (NBFC-D)</u>

As per the prevailing Regulatory Framework of RBI, the following two categories of NBFCs are subject to the most stringent regulations:

1. All Deposit Taking NBFCs (NBFC – D) irrespective of their size *–there are total 88 NBFCs-D as on 30th April, 2019*
2. Non-Deposit Taking Systemically Important NBFCs (NBFC-ND-SI) ie., NBFCs which do not accept public deposits and have an asset base of Rs 500 crores and above – *there are total 264 NBFCs –ND-SI as on 30th April, 2019.*

All major aspects of working of above said two categories of NBFCs are regulated and monitored by RBI.

<u>NBFCs are Facing Liquidity Crunch</u>

Exemption from TDS provisions shall also be contributing to ease liquidity for NBFCs.

<u>*Request:*</u>

<u>*Based on the above said facts, it is hereby requested to exempt those NBFCs which are registered with RBI and classified by RBI as Deposit Taking NBFC (NBFCs-D) and Non-Deposit Taking Systemically Important NBFC (NBFCs-ND-SI) from the provisions of TDS on Interest Income. The same may be granted by issuance of Notification u/s 194A(3)(iii)(f) of The Income Tax Act, 1961.*</u>

2. Tax Benefits For Income Deferral u/s.43D Of The Income Tax Act

Section 43D of the Income Tax Act recognises the principle of taxing income on NPAs only in the year in which they are received. It is also logical to recognise income on NPAs on receipt basis and not on accrual basis in order to present the correct picture. In accordance with the directions issued by the RBI, NBFCs like banks and FIs, follow prudential norms and are required to defer income in respect of their non-performing accounts.

However, the provision of Section 43D are only applicable to scheduled banks, public financial institutions, state financial corporations, state industrial corporations and housing finance companies (which are also non-bank entities). Union budget 2017 has extended the coverage of this section to cooperative banks also.

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Request:

NBFCs are the only financial institutions which have been left out. This discrimination against NBFCs is disappointing and discouraging, especially even after the sustained growth and high levels of compliance shown by the sector. This has been one of our long standing demand.We therefore request you to kindly do justice and extend the scope of Sec 43D to RBI registered NBFCs also.

3. Request For Allowing Higher Depreciation Rates For Construction Equipment

The I. T. Act allows depreciation at the rate of 100% in case of certain equipment meant for pollution control, solid waste control, mineral oil concerns, mines and quarries, energy saving devices and renewable energy devices. The Act also allows high rate of depreciation (30%) to motorcars, buses, lorries and taxies used in the business of running them on hire.

However, construction equipment which contribute immensely to infrastructure development are not given this benefit of higher depreciation rate when they are financed, instead the depreciation rate for such vehicles is only 15%. For other plant and machinery too, the rate is 15%. This acts as a roadblock to infrastructure development.

Request:

In today's age of rapid technological progress, assets like construction equipment and plant and machinery become obsolete faster. Thus, keeping in mind the nature of the asset, its average life-cycle and the pace of technological development, the depreciation rate should be at least at par with commercial vehicles ie; 30%. This will also give an impetus to the infrastructure spend and will incentivize such investments.

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INDIRECT TAX : GST

1. Need to Promote Leasing

World over "Leasing" has been promoted as an important tool for capital formation. Today, the country is making huge investments in the Infrastructure sector and there is a special impetus being given to the MSMEs and the Farm sector. In this scenario, there is a crying need to promote "Leasing" in India, which has suffered a body blow due to imprudent taxation. Prior to the introduction of GST, Lease / Hire Purchase rentals were subject to the levy of VAT @ 4-14% at the state level and in addition, the interest component (to the extent of 10%) of the rental was subject to the levy of Service Tax @ 15%.

While GST has done away with the issue of dual taxation, the rate of GST on rentals of lease of any movable asset is equal to the rate of GST levied on normal sales/purchase of that asset, which does not give any incentive to lease.

Request

- *The interest component of the lease rental may be exempt from the levy of GST on the lines of the exemption given to the interest on loans.*

- *The rate of GST on lease rentals should be reduced to 5% in order to promote and encourage lease as a tool of capital formation.*

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Annexure-3

RECOVERY - ENFORCEMENT OF SEUCRITY INTEREST UNDER THE SARFAESI ACT COMES WITH A RIDER OF MINIMUM LOAN TICKET SIZE OF Rs.1.0 CRORE

Union Budget 2015 had announced coverage of NBFCs (with asset base of 500crs and above) under the SARFAESI Act. This came as a welcome move since the asset classification (NPA) norms for NBFCs were brought at par with banks by RBI. However, in the gazette notification issued on 5th August 2016 to this effect, a clause was inserted whereby sections 13 to 19 of the SARFAESI Act, which cater to the "enforcement of security interest", shall be applicable only in cases where the minimum ticket size of lending is Rs 1crore. This has come as a big surprise to the NBFC sector.

The Underlying Need to Bring Parity with Banks, Housing Finance Companies (HFCs) and Other Financial Institutions (FIs) Is Not Fully Addressed

The prime objective of giving NBFCs coverage under the SARFAESI Act was to bring parity with banks, HFCs and other FIs, and providing NBFCs with an all important tool of recovery. This has been done in the light of the Revised Regulatory Framework for NBFCs, issued by RBI which is aimed to "address regulatory gaps and arbitrage arising from differential regulations, both within the NBFC sector as well as vis a vis other financial institutions". As a result, the Asset Classification (NPA classification norms) were brought at par with banks.

However, the above said rider of Rs 1crore does not fully justify the objective of bringing parity, since no such clause exists for banks, HFCs and other FIs.

Size of The Loan Should Not Be The Criteria

As per the Prudential Norms for Asset Classification (NPA Classification) for banks, HFCs and NBFCs, it is the duration of the overdue period of a loan, and not the ticket size, which determines whether the loan (Asset) is to be classified as "nonperforming" or not. It is therefore, imprudent and unjustified to make the ticket size of the loan as a determining factor for use of tools of recovery of that particular loan.

The Deterrence Factor Gets Diluted

In addition to enable Financial Institutions make recoveries, such recovery tools play a very important role of being a "deterrent to default". The above said rider of minimum ticket size of Rs1crore, dilutes the deterrence factor of an important recovery tool like the SARFAESI Act.

Request

1. *Based on the facts explained above we hereby request you to kindly do full justice by bringing complete parity with banks, housing finance companies and FIs in matters relating to recovery.*

2. *For this , kindly delete the following words from the Notification dated 5th August 2016:*
   "…….with the exception that the provisions of Sections 13-19 shall apply only to such security interest which is obtained for securing repayment of secured debt with principal amount of Rs 1crore and above"