

NBFCs Outside Regulatory Ambit may Pose Risk to Financial System

Non-regulated non-banking financial companies (NBFCs) could pose risk to the financial system, the Reserve Bank of India said in its Financial Stability Report (FSR).

A Shadow Banking Implementation Group carried out a preliminary study of such institutions and recommended that they be brought under some regulation. It found that there was a high degree of heterogeneity in business models and risk profiles across various non-banking financial entities in the organised as well as the unorganised (informal) sectors.

It also identified “exempted” provident funds, unregulated chit funds, co-operative and credit societies and primary agricultural credit societies as groups of institutions that need a greater degree of oversight.

“The study stresses on the need for a large scale survey by the National Sample Survey Organisation (NSSO) or other such agencies to estimate the size of the informal financial sector,” the RBI said in its report.

The central bank also said that government-owned entities discharging the functions of special NBFCs that are exempt by statute from adherence to prudential regulations, are an area of concern.

Reviewing framework

The Reserve Bank said that it is in the process of reviewing the extant regulatory framework for NBFCs, based on the recent developments in the sector and also the recommendations made by the Nachiket Mor Committee.

The proposed review, the central bank said, will cover among other things the corporate governance guidelines, including ‘fit and proper’ criteria for their directors, regulation of deposit acceptance activity and consumer protection measures.

The current regulations focus only on deposit-taking NBFCs and large systemically important non-deposit taking NBFCs. Those NBFCs, which are below the asset size threshold of ₹50 crore, are not under the surveillance of the RBI.

The RBI said such entities might be playing an important role in furthering financial inclusion, but there needs to be a mechanism to regulate such entities.

(Business Line)