TeamLease® RegTech
Helping India Comply

SIMPLIFYING COMPLIANCE MANAGEMENT FOR NON-BANKING FINANCIAL COMPANIES (NBFCs) IN INDIA

Table of Contents

Introduction 03

Types of NBFCs 04

Nature of Compliances 09
- Categories of Compliances
- Types of Compliances
- Industry-Specific Compliances

Compliance Challenges for Non Banking Financial Companies 23

Industry Perspective 30

Rethinking Compliance Management 31

1 Introduction

Non-Banking Financial Companies have emerged as important sources of commercial credit in the Indian economy. As of 2021, there are over 9462 NBFCs registered with the Reserve Bank of India (Sengupta, Song & Harsh Vardhan, 2021). NBFCs play an important role in serving the underserved sections of the economy where commercial banks are often unable to provide services. Despite the recent NPA crisis of 2018, NBFCs play a pivotal role in stimulating economic growth and "managing the spread of risks during financial duress" (Varun Madan, 2021).

From a regulatory standpoint, NBFCs are not as strictly regulated by the RBI as are commercial banks. However, from a compliance management perspective, NBFCs are no different from any other form of service. There is a high regulatory burden on the compliance officers and the key management persons within these companies which frequently forms bottlenecks in the ease of doing business.

There are hundreds of one-time and ongoing compliances that the company executives must deal with at any given point of time, and very often, these need to be outsourced on an ad-hoc basis given their sheer volume. These include both general and industry-specific compliances. A rapidly changing regulatory environment also adds to the complexity of the problem as the management must routinely keep up with such legal updates and upgrade their compliance management accordingly.

Therefore, the purpose of the present report is to provide an overview of the regulatory environment for NBFCs, to discuss some of the problems encountered by the industry and propose actionable recommendations to reduce the compliance burden on them.

2 Types of NBFCs

The Reserve Bank of India provides a comprehensive description of the types of NBFCs that operate in India and is reproduced below:

NBFCs can be classified on the basis of a) asset/liability structures; b) systemic importance; and c) the activities they undertake. In terms of liability structures, NBFCs are subdivided into deposit-taking NBFCs (NBFCs-D) - which accept and hold public deposits - and non-deposit taking NBFCs (NBFCs-ND) - which source their funding from markets and banks. Among non-deposit taking NBFCs, those with asset size of ₹500 crore or more are classified as non-deposit taking systemically important (NBFCs-ND-SI). Within this broad categorization the different types of NBFCs are as follows:

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, lathe machines, generator sets, earth moving and material handling equipments, moving on own power and general purpose industrial machines. Principal business for this 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.

Investment Company (IC)

IC means any company which is a financial institution carrying on as its principal business the acquisition of securities,

Loan Company (LC)

LC means any company which is a financial institution carrying on as its principal business the providing of finance whether by making loans or advances or otherwise for any activity other than its own but does not include an Asset Finance Company.

Infrastructure Finance Company (IFC)

IFC is a non-banking finance company a) which deploys at least 75 per cent of its total assets in infrastructure loans, b) has a minimum Net Owned Funds of ₹ 300 crore, c) has a minimum credit rating of 'A 'or equivalent and d) and a CRAR of 15%.

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

CIC-ND-SI is an NBFC carrying on the business of acquisition of shares and securities which satisfies the following conditions:-

(a) it holds not less than 90% of its Total Assets in the form of investment in equity shares, preference shares, debt or loans in group companies

(b) its investments in the equity shares (including instruments compulsorily convertible into equity shares within a period not exceeding 10 years from the date of issue) in group companies constitutes not less than 60% of its Total Assets

(c) it does not trade in its investments in shares, debt or loans in group companies except through block sale for the purpose of dilution or disinvestment

(d) it does not carry on any other financial activity referred to in Section 45I(c) and 45I(f) of the RBI act, 1934 except investment in bank deposits, money market instruments, government securities, loans to and investments in debt issuances of group companies or guarantees issued on behalf of group companies.

(e) Its asset size is ₹ 100 crore or above and

(f) It accepts public funds

Infrastructure Debt Fund

IDF-NBFC is a company registered as NBFC to facilitate the flow of long term debt into infrastructure projects. IDF-NBFC raise resources through issue of Rupee or Dollar denominated bonds of minimum 5 year maturity. Only Infrastructure Finance Companies (IFC) can sponsor IDF-NBFCs.

Micro Finance Institution (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. aggregate amount of loans, given for income generation, is not less than 50 per cent of the total loans given by the MFIs

g. loan is repayable on weekly, fortnightly or monthly installments at the choice of the borrower

Non-Banking Financial Company - Factor

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 percent of its total assets and its income derived from factoring business should not be less than 50 percent of its gross income.

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 and net owned fund is ₹ 100 crore.

Non-Operative Financial Holding Company

NOFHC 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 all other financial services companies regulated by RBI or other financial sector regulators, to the extent permissible under the applicable regulatory prescriptions.

RBI - Scale Based Regulations for NBFCs

The sector went through a major regulatory overhaul in 2021, when RBI notified the "Scale Regulation (SBR): A Revised Regulatory Framework for NBFCs" to align the regulatory requirements for NBFCs because of the change in their risk profiles, and their evolution in terms of size and complexity. The framework came into effect from 01.10.2022 and has reclassified NBFCs into 4 layers - Base Layer (BL), Middle Layer (ML), Upper Layer (UL), and Top Layer (TL).

Previous classifications of NBFC- Infrastructure Investment Company, Core Investment Company, Microfinance Institution, Systemically Important/ Non-Systemically Important, Deposit-taking/Non-deposit taking etc. have been done away with.

Sr. No	Layer	Previous Classifications
1	Base (BL)	(a) Non-deposit taking NBFCs below the asset size of ₹1000 crore and (b) NBFCs undertaking the following activities- (i) NBFC-Peer to Peer Lending Platform (NBFC-P2P) (ii) NBFC-Account Aggregator (NBFC-AA) (iii) Non-Operative Financial Holding Company (NOFHC) (iv) NBFCs not availing public funds and not having any customer interface
2	Middle (ML)	(a) all deposit taking NBFCs (NBFC-Ds), irrespective of asset size, (b) non-deposit taking NBFCs with asset size of ₹1000 crore and above and (c) NBFCs undertaking the following activities: (i) Standalone Primary Dealers (SPDs) (ii) Infrastructure Debt Fund - Non-Banking Financial Companies (IDF-NBFCs) (iii) Core Investment Companies (CICs) (iv) Housing Finance Companies (HFCs) (v) Infrastructure Finance Companies (NBFC-IFCs) (vi) Investment and Credit Companies (NBFC-ICCs) (vii) Micro Finance Institutions (MFIs) (viii) NBFC-Factors (ix) Mortgage Guarantee Companies (NBFC-MGCs)
3	Upper (UL)	The Upper Layer shall comprise of those NBFCs which are specifically identified by the Reserve Bank as warranting enhanced regulatory requirement based on a set of parameters and scoring methodology as provided in the Appendix to this circular. The top ten eligible NBFCs in terms of their asset size shall always reside in the upper layer, irrespective of any other factor.
4	Top (TL)	The Top Layer will ideally remain empty. This layer can get populated if the Reserve Bank is of the opinion that there is a substantial increase in the potential systemic risk from specific NBFCs in the Upper Layer. Such NBFCs shall move to the Top Layer from the Upper Layer.

RBI holds the authority to move NBFCs into the top 2 layers based on certain parameters set by them from time to time. In addition, the top 10 eligible NBFCs in terms of their asset size will always remain in the UL regardless of any other factor. The TL will consist of companies from the UL that have seen a substantial increase in their potential systemic risk.

NBFC-BLs are required to put in place a Board-approved policy on the grant of loans to directors, senior officers, and relatives of directors. They must now also make disclosures related to their types of exposure, related party transactions, loans to Directors/ Senior Officers and customer complaints. NBFCs in the BL, ML, and UL are required to make disclosure on their exposure in specific fields in their annual financial statements. These statements also need to present information on related parties and complaints.

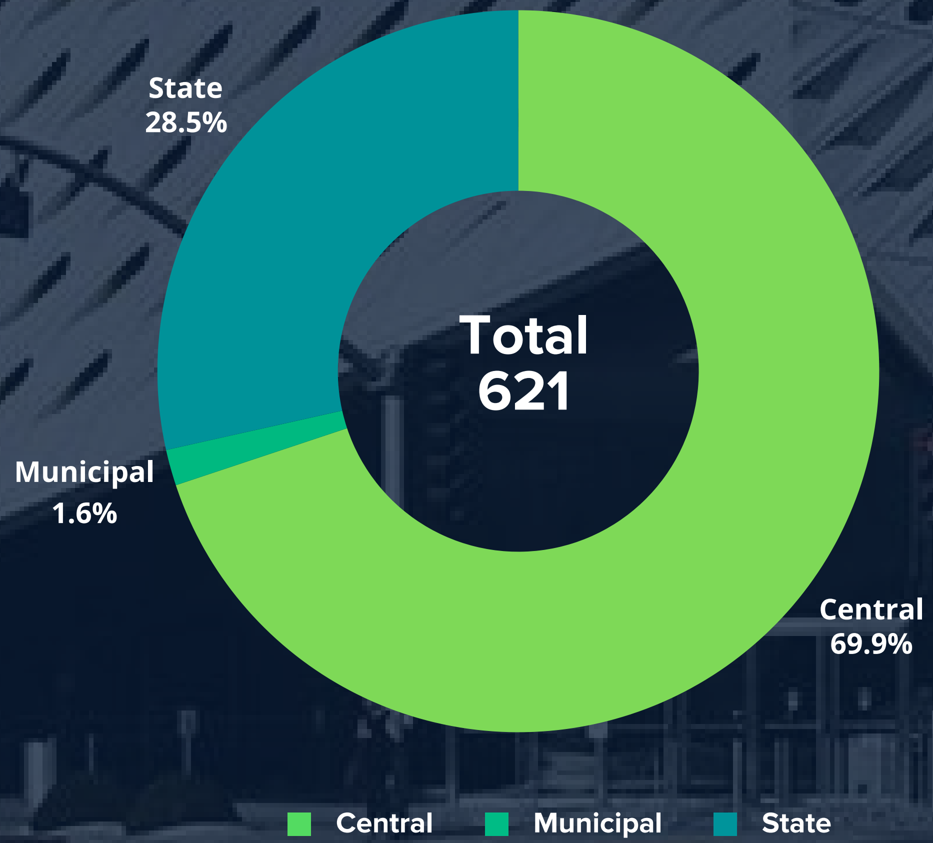
NBFC-ULs must determine internal exposure limits on important sectors to which credit is extended. These institutions are also required to maintain Common Equity Tier 1 Capital of at least 9% of the Risk Weighted Assets. There needs to be a Board approved policy in place for the adoption of the enhanced regulatory framework with an implementation plan. The implementation plan has to be shared with RBI. In addition, both UL and ML institutions are required to put in place a Compliance Function and appoint a Chief Compliance Officer (CCO) by 01.10.2023.

3 Nature of Compliances

NBFCs in India have to stay abreast with two kinds of compliances: one-time and ongoing. A single company is subject to over 35 one time registrations and approvals in a single state. These are further split into four stages viz., Setting Up, Pre-Commissioning stage, Post-Commissioning Stage and Post-Production stage. One-time compliances typically deal with incorporation of the entity, land allotment, project related approvals, construction-related approvals, approvals related to labour, safety and health, tax-related registrations, industry-specific approvals, etc.

Besides these one-time registrations and approvals, an NBFC is further subjected to a host of ongoing compliances at the Central, State and Local levels. For example, Labour Laws fall in the Concurrent List where both the Union and State are entitled to legislate. This means that at any given point in time, a company would have to ensure compliance with a parent legislation drafted by the Centre along with state rules and regulations.Similarly, under Environmental Laws there is a Central Pollution Control Board and there are State Pollution Control Boards to regulate compliance. Thus, every company has the task of ensuring that it is simultaneously compliant with the laws falling under the three legislative lists of the Constitution respectively.

Central, State and Local Level Compliances



Data on the number of compliances for a single NBFC operating in a single state at the Central/State/Municipal level
Source: Teamlease Regtech

Categories of Compliances

Labour

Labour typically includes around 29 central laws (now condensed into four labour codes). Being a concurrent subject, labour laws are further legislated upon by the states and each parent act is then accompanied by a host of state legislations, alongside the central and state rules. Legislations under the labour category include Apprentices Act, 1961 and Apprenticeship Rules, 1992; Contract Labour (Regulation & Abolition) Act, 1970; Employees Compensation Act, 1923; Equal Remuneration Act, 1976 and Equal Remuneration Rules, 1976; State Shop & Establishment Acts; Sexual Harassment of Women at Workplace (Prevention, Prohibition & Redressal) Act, 2013 & Sexual Harassment of Women at Workplace (Prevention, Prohibition & Redressal) Rules 2013; Payment of Wages Act, 1936; Maternity Benefit Act, 1961.

EHS (Environment, Health & Safety)

EHS is predominantly constituted by the Environment Protection Act, 1986 and its related rules such as Environment (Protection) Rules, 1986; Battery Waste Management Rules, 2022; Bio-Medical Waste Management Rules, 2016; E-Waste (Management) Rules, 2016; Plastic Waste Management Rules, 2016 etc. Other important legislation include the Air (Prevention and Control of Pollution) Act, 1981; Water (Prevention and control of pollution) Act 1974; Explosives Act, 1884, and Gas Cylinders Rules, 2016 etc.

Corporate Laws

Under Corporate Laws, the main legislation include, Companies Act, 2013 & Companies (Incorporation) Rules, 2014 along with other rules and regulations.

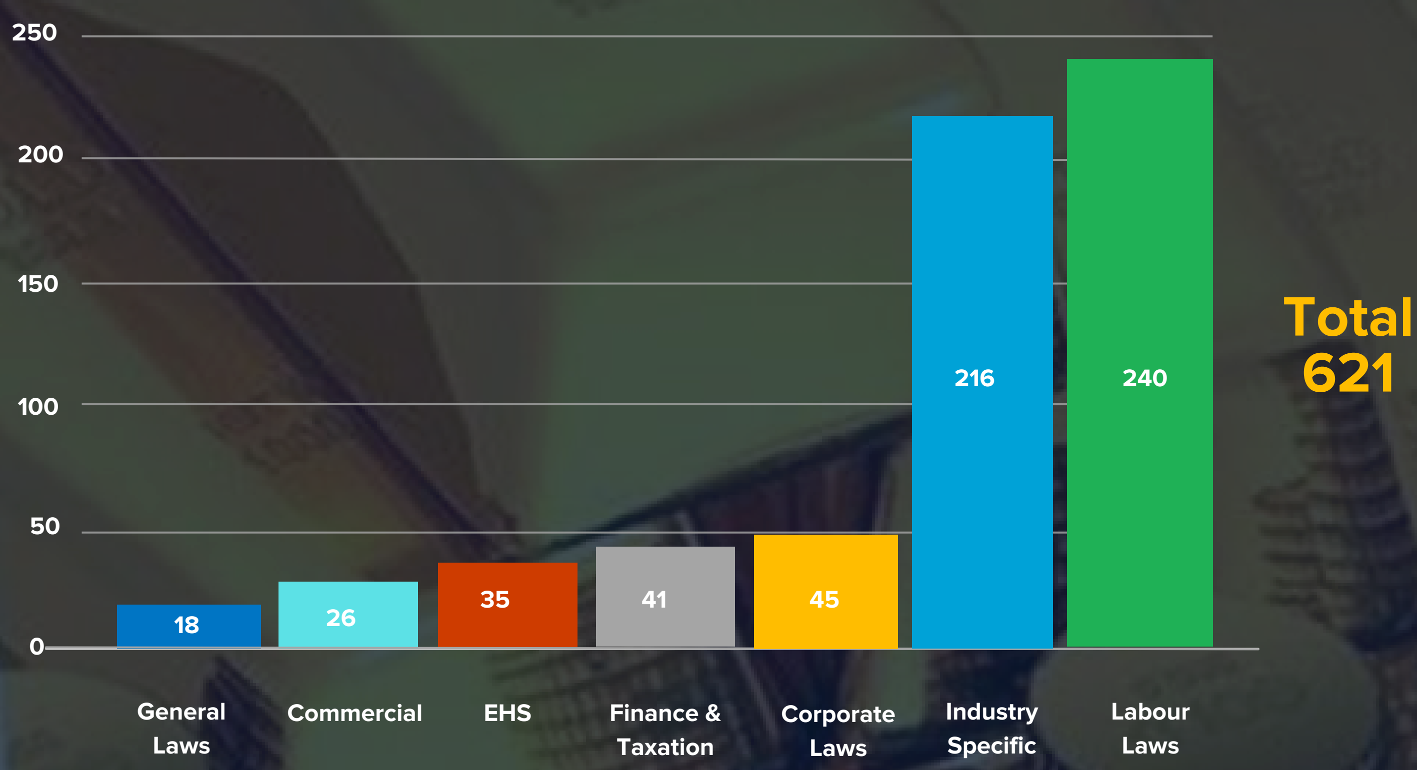
Commercial Laws

These include the Electricity Act, 2003 and Central Electricity Authority (Measures Relating To Safety and Electric Supply) Regulations, 2010; Bureau of Indian Standards Act, 2016 and Bureau of Indian Standard Rules, 1987; Collection of Statistics Act, 2008 and Collection of Statistics (Central) Rules, 1959; Motor Vehicles Act, 1988 and Central Motor Vehicle Rules, 1989, etc.

Finance and Taxation Laws

This category includes the Central Goods and Services Tax Act, 2017 and state specific legislations on indirect taxation. It also includes the Income Tax Act 1961 and Income Tax Rules 1962 along with state government taxes on professions and trades.

Categories of Compliances



Data on the number of compliances for a single NBFC operating in a single state
Source: Teamlease Regtech

Types of Compliances

Audit and Accounts

As per Companies Act 2013, an NBFC which is required to comply with Indian Accounting Standards has to file a financial statement with the ROC via Form AOC-4 NBFC (Ind AS) u/s 137 of the Act. Under Central Goods and Services Tax Act, 2017 and Central Goods and Services Tax Rules, 2017 a company is required to get its accounts audited and furnish a certified copy of the statement through Form GSTR-9C. Under Information Technology Act 2000 and Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules, 2011, a company is required to carry out an annual audit of reasonable security practices and procedures. There are also several auditing and accounting compliance requirements which will be covered in the Industry-specific section that follows.

Committees

As per the Industrial Disputes Act, 1947 every employer is required to constitute a Works Committee as well as set up a grievance redressal committee. Under Sexual Harassment of Women at Workplace (Prevention, Prohibition & Redressal) Act, 2013, there are requirements with respect to the constitution of the internal committee in dealing with incidents of sexual harassment. There are also Industry-specific compliances related to committees.

Employee Safety & Welfare

These typically include compliances under the various labour laws such as the Maternity Benefit Act, 1961 and Minimum Wages Act, 1948 as well as legislations such as Rights of Persons with Disabilities Act, 2016 and Rights of Persons with Disabilities Rules, 2017.

Display Requirements

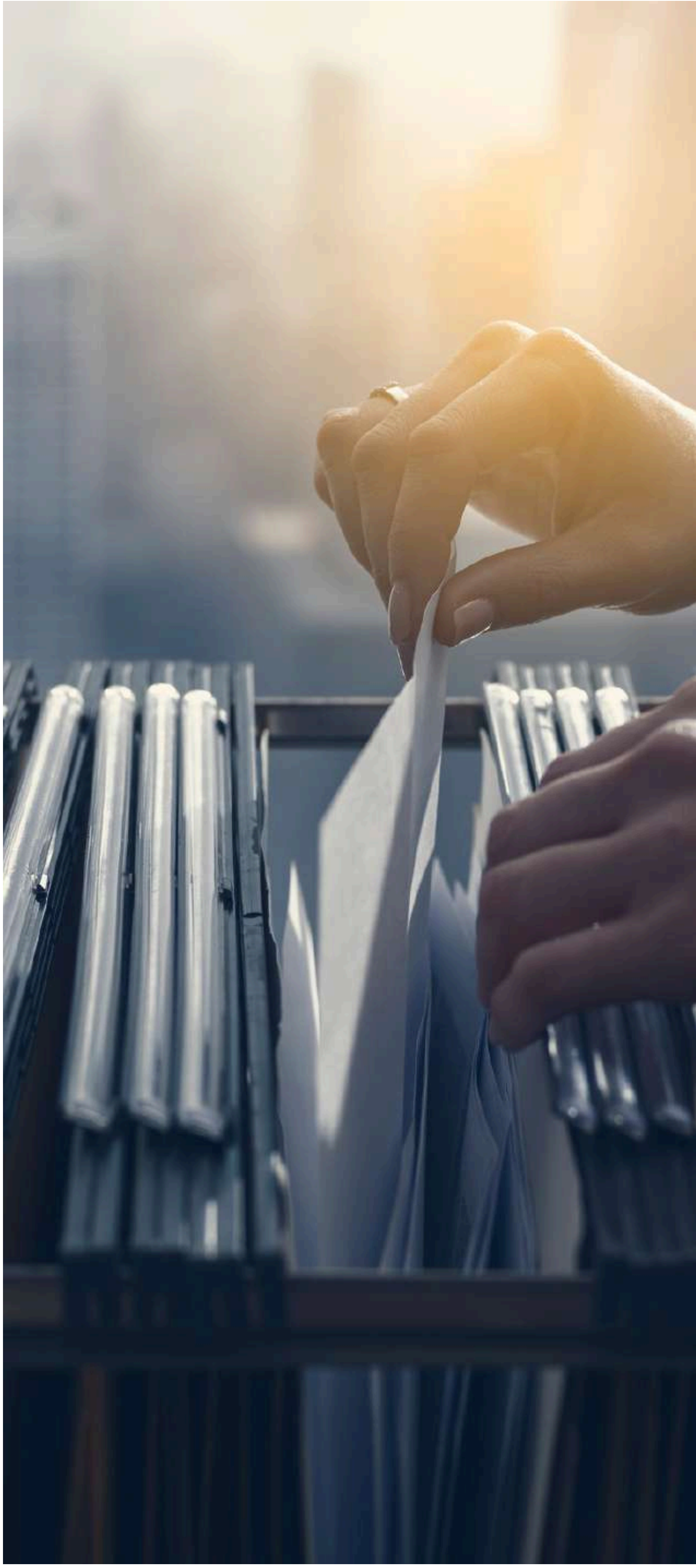
As per Central Goods and Services Tax Act, 2017 and Central Goods and Services Tax Rules, 2017, a NBFC is required to display its certificate of registration at the business premises. Under Legal Metrology Act, 2009 a company making use of weights and measures for any purpose must display its certificate of verification. Several Industry-specific compliances such as those contained in RBI's Master Circulars/Directions also contain display requirements. For example, under Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016, an NBFC-MFI is required to display the effective rate of interest charged to its borrowers on loans in all its offices in the vernacular language. Similarly, as per RBI Guidelines on Fair Practices Code for NBFCs Employee Welfare & Safety, every NBFC shall ensure that that the effective rate of interest charged and the grievance redressal system set up is prominently displayed in all its offices and in the literature issued by it (in vernacular language) and on its website.

Payments

As per Apprentices Act, 1961 and Apprenticeship Rules, 1992 an employer (NBFC) is required to pay a stipend to any apprentice in the manner and mode as may be prescribed. A company is also required to make monthly contributions in accordance with the Employees State Insurance Act, 1948 and the related rules. Under Payment of Bonus Act,1965 & Payment of Bonus Rules, 1975, a company is required to pay the bonuses within 8 months from the closing of the accounting year.

Register and Records

This category is typically covered under various labour laws and Industry-specific compliances. On an average, an NBFC can easily accrue well over 100 compliances only related to maintenance of registers. For example, under Apprentices Act, 1961 and Apprenticeship Rules, 1992 a company is required to maintain registrations and records pertaining to attendance and work done by an apprentice. Employees State Insurance Act, 1948 requires a company to maintain a register of employees under Form 6. Under the Bureau of Indian Standards Act, 2016 an NBFC is required to maintain records of maintenance, inspection and testing of fire extinguishers. As per RBI's Master Direction - Know Your Customer (KYC) Direction, 2016, an NBFC shall maintain and preserve all necessary records of transactions with customers.



Return Filing, Disclosures and Intimations

There are extensive filing and disclosure requirements under labour law. For example under Contract Labour (Regulation & Abolition) Act, 1970 an employer is required to send annual return in Form XXI to Registering Officer; Under Payment of Bonus Act,1965 an NBFC must upload the annual return on the web portal of the Ministry of Labour and Employment in Form D.

There are also Industry-Specific compliances such as submission of a certificate from the Statutory Auditors on half yearly basis under Compliance with FDI norms-Half yearly certificate from Statutory Auditors of NBFCs, Notification No. RBI/2009-10/304 DNBS (PD).CC. No 167 /03.10.01 /2009-10 dated February 04, 2010; or disclosing the details of average interest charged/ paid on borrowings in the balance sheet Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016. Such compliances will be covered in greater detail in the section below:

Industry-Specific Compliances

There are over 200 Industry-Specific compliances that are typically applicable to an NBFC operating at a single location within the country. Some of these compliances are outlined below:

RBI Circulars

- NBFCs have to meet a plethora of return filing requirements and disclosure related compliances under RBI circulars such as the Master Circular- 'Non-Banking Financial Company-Micro Finance Institutions' (NBFC-MFIs) - Directions, dated July 1, 2015; and Master Direction - Know Your Customer (KYC) Direction, 2016, Master Direction DBR.AML.BC.No.81/14.01.001/2015-16, February 25, 2016.

- There are display requirements such as those contained in Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016. For example, under the foregoing Master Direction, "Every registered Systemically Important Non-Deposit taking Non-Banking Financial Company (NBFC-ND-SI) having customer interface shall display the Fair Practice Code with the approval of its board of Directors on its website preferably in the vernacular language or a language as understood by the borrower."

- Besides these general compliances RBI circulars also contain specific particulars such as the asset classification norms applicable to NBFCs. Under **Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016**, every NBFC having an asset size of Rs. 500 crores is required to adopt the following asset classification:

(i) Standard asset means the asset in respect of which, no default in repayment of principal or payment of interest is perceived and which does not disclose any problem nor carry more than normal risk attached to the business; ii. Non-performing asset means an asset for which, interest/principal payment has remained overdue for a period of 90 days or more

- Under the same Master Direction mentioned above, the interest rate cap is also set. Thus, every NBFC-MFI having an asset size of 500 crore or more must ensure that the interest rates charged to its borrowers are lower of the following: (a) *The cost of funds plus margin i.e. margin not exceeding 10 % for large MFIs (loans portfolios exceeding Rs. 100 crore) and 12 % for the others; or (b) The average base rate of the five largest commercial banks by assets multiplied by 2.75. The average of the base rates of the five largest commercial banks shall be advised by the Bank on the last working day of the previous quarter, which shall determine interest rates for the ensuing quarter.*

- Then there are other compliance requirements under the 2016 Direction such as Sanctioning and disbursing loans from a central location; Prohibition on having complicated loan application procedure for the borrowers; Code of Conduct for field staff to have minimum qualifications, training tools etc; Provision for outstanding assets by NBFC-ND-SI; Classification of the lease/hire purchase assets, loans and advances and any other forms of credit on the considering credit weaknesses and security for realization by NBFC-ND-SI and so on.

Prevention of Money Laundering Act, 2002 and Prevention of Money Laundering (Maintenance of Records) Rules, 2005

Under this Act, an NBFC is subjected to compliances such as Maintaining information of transactions with clients; Communicating the details of the Designation Director and the Principal Officer to Director; Furnishing of information of cash transactions, series of cash transactions integrally connected or transactions involving receipts by non-profit organisations, to the Director; Verifying identity of clients during commencement of an account-based relationship; Furnishing information of suspicious transactions to the Director; Closing the accounts of the existing clients where no records are present; Exercising ongoing due diligence with every client and examine transactions; Reporting entity to review the due diligence measures in certain cases.

Reserve Bank of India Act, 1934

According to the Master Directions - Information Technology Framework for the NBFC Sector, 2017, under the RBI Act, 1934, NBFCs must have the IT Strategy Committee work in partnership with other Board committees and senior management to review and approve the IT strategy. The Chief Information Officer must ensure implementation of IT policy to the operational level involving IT strategy, value delivery, risk management and IT resource management. As per the Ombudsman Scheme for Non-Banking Financial Companies, 2018, an NBFC must display the particulars of the scheme in all the offices and branches.

Key RBI Regulations in 2022 for NBFCs

In January, RBI issued the Master Circular - Bank Finance to NBFCs, DOR.CRE.REC.No.77/21.04.172/2021-22. This provided for banks to extend working capital facilities and term loans to NBFCs that are engaged in activities like: infrastructure financing, equipment leasing, hire-purchase, loan, factoring, and investment. However, they cannot grant bridge loans or interim finance. Banks can only invest in Zero Coupon Bonds (ZCBs) if the issuing NBFC has built up a sinking fund for the accrued interest and the same is invested in liquid investments/ securities such as Government bonds. The circular also allowed banks to invest in Non-Convertible Debentures (NCDs) whose original/initial maturity was up to 1 year.

In February, RBI issued a notification, DoS.CO.PPG.SEC/10/11.01.005/2021-22, regarding the implementation of 'Core Financial Services Solution' (CFSS) by NBFCs. NBFCs with more than 10 'Fixed Point service delivery units' in the Middle and Upper layers are mandated to implement the CFSS. It also provided for the timeframe for implementation for NBFCs across the 4 layers.

In April, RBI notified the Net Owned Fund (NOF) requirement for NBFCs to commence or continue operations. The notification, *DOR.CRE.060.CGM(MM) 2022*, provided that Investment and Credit Companies (ICCs), Micro Finance Institutions (MFIs), and Factors must have a NOF of 10 crore rupees. For existing institutions that fall below the threshold, a glide path is provided. All such NBFCs are required to reach the NOF threshold by 31.03.2027. While ICCs and MFIs in the North-East region need to reach 5 crore rupees NOF by 31.03.2025, other MFIs and Factors need to have a NOF of 7 crore rupees in the same timeframe.

RBI also issued a notification, Ref.No.DoS.CO.PPG/SEC.01/11.01.005/2022-23, regarding the Compliance Function and Role of the Chief Compliance Officer in NBFCs in the Upper and Middle layers. These NBFCs are required to put in place a board-approved policy based on the provided framework by 01.04.2023 and 01.10.2023 respectively. The framework provides for the responsibility of the Board, as well as the appointment, responsibilities, and tenure of the CCO.

In addition, RBI issued the guidelines, DOR.CRE.REC.24/21.01.003/2022-23, for the Large Exposures Framework for NBFC-UL to address the credit risk concentration of the companies in the Upper layer. The guidelines provide instructions on identifying large exposures and put in place reporting norms for the same. Capital requirements for NBFC-ULs were also notified, DOR.CAP.REC.No.21/21.06.201/2022-23, which provided for the elements of Common Equity Tier 1 capital.

In May, RBI made NBFCs engaged in providing microfinance loans, non-deposit taking, and having asset size of less than 100 crore rupees exempt from sections 45IA, 45IB, and 45IC of the RBI Act, 1934 vide notification DoR. FIN. REC. 95 /CGM (JPS)-2022. RBI then notified, vide notification DOR.FIN.REC.No.30/03.10.001/2022-23, that the deposits of NBFCs will receive a minimum investment grade credit rating of 'BBB-' by registered Credit Rating Agencies. RBI also issued a notification, FIDD.CO.Plan.BC.No.5/04.09.01/2022-23, on lending by commercial banks to NBFCs and Small Finance Banks (SFBs) to MFIs. Bank credit to NBFCs for on-lending was limited to the overall limit of 5% of an individual bank's total priority sector lending. SFB credit to MFIs (members of 'Self-Regulatory Organisation') was limited to 10% of the bank's total priority sector lending.

In October, RBI launched, vide Press Release 2022-2023/1004, the Advanced Supervisory Monitoring System (DAKSH). It is an end-to-end workflow application that will allow RBI to monitor the compliance requirements of all supervised entities including NBFCs. RBI also notified, DOR.CRE.REC.No.78/03.10.001/2022-23, the classification of various NBFCs in the Middle Layer. NBFC-ICCs (Investment and Credit Company), NBFC-MFIs (Micro Finance Institution), NBFC-Factor, and NBFC-MGCs (Mortgage Guarantee Company) were all drafted in to the Middle Layer.

KYC Guidelines for NBFCs

The Master Direction – Know Your Customer (KYC) Directions, 2016 provide for critical compliances related to the KYC processes for NBFCs. These directions mandate the formulation of a policy to adopt a risk-based approach for periodic updation of KYC. This approach needs to be approved by the Board of Directors and added to the internal KYC policy of the institution. In addition, the companies need to conduct tests of the V-CIP (Video Customer Identification Process) application software and its relevant APIs before it can be used for the KYC process. As part of the requirements for operating a V-CIP software, companies need to formulate a clear flow and standard operating procedures (SOP) and ensure variability in the sequence and types of questions during video interactions. This will help companies avoid instances wherein the interactions are pre-recorded and verify the authenticity of the V-CIP process.

In addition, the V-CIP software must be able to deny connection requests from spoofed and outside-of-India IP addresses. The video recordings must have geo-tagging enabled and contain the live coordinates along with the date-time stamp for the customer undertaking the V-CIP. The application has to be able to detect spoofs and face liveness as well as do face matching. AI can also be used to ensure the robustness of the V-CIP. The directions mandate that only trained officials should operate the process and that the activity log of the officers along with their credentials need to be preserved. Periodical testing of the entire infrastructure is also mandated and the NBFCs must maintain the data and recordings of V-CIP.

Fair Practices Guidelines/ Code of Conduct for NBFCs

The RBI Guidelines on Fair Practices Code for NBFCs, Appointment of Internal Ombudsman by NBFCs, the Integrated Ombudsman Scheme, and the RBI (Regulatory Framework for Microfinance Loans) Directions, 2022 together provide for the framework of ethical and fair practice guidelines for NBFCs.

The guidelines on fair practices code provide that the companies must mention the penal interest for late repayment in bold letters in the loan agreement. The companies must undertake periodical review of their compliance of the fair practices code as well as the grievance redressal mechanism. In addition, the fair practices code must be published on the company website. The borrowers must be informed in vernacular language about the terms and conditions, interest, and amount of loan sanctioned. Any changes in the terms and conditions must also be notified to the borrowers. Companies are also required to train the field staff on the appropriate debt recovery behavior towards borrowers. The field staff must also not harass the borrowers by using muscle power, bothering/calling borrowers at odd hours, among other things.

The Appointment of Internal Ombudsman regulations are applicable on deposit taking NBFCs with 10 or more branches and non-deposit taking NBFCs with asset size of over 5000 crore rupees. Stand-alone Primary Dealers, Infrastructure Finance Companies, Core Investment Companies, Infrastructure Debt Funds, Account Aggregators, NBFCs under corporate insolvency resolution process, NBFCs in liquidation, and those with only captive customers are exempted from these regulations. The regulations provide for the appointment of an internal ombudsman (IO) every 5 years with the IO responsible for all complaints examined by the company. The IO is required to do quarterly reporting to the RBI on the total number of complaints received and the number of complaints partly or wholly rejected. In addition, the IO must also submit the total number of cases wherein the decision of the IO has been rejected and the number of cases closed annually. The companies are also required to formulate a standard operating procedure (SOP) for auto-escalation of complaints rejected by the internal grievance redressal mechanism to the IO.

In 2021, RBI introduced the Integrated Ombudsman Scheme, which integrated the Banking Ombudsman Scheme, 2006, the Ombudsman Scheme for NBFCs, 2018, and the Ombudsman Scheme for Digital Transactions, 2019. The new scheme is applicable on all NBFCs except Core Investment Companies, Infrastructure Debt Funds, Infrastructure Finance Companies, and companies in the winding up/liquidation process. The NBFCs are required to appoint a Principal Nodal Officer at the head office and display the name and contact details of the officer along with the details of the complaint lodging portal of the ombudsman in its branches. The scheme also provides for the display of the salient features of the scheme in all offices and places of business and a copy of the scheme of also has to be available in all branches. The scheme further mandates that the companies must file the written version in reply to the averments in complaints received within 15 days before the ombudsman.

RBI has also issued guidelines for recovery of microfinance loans under the RBI (Regulatory Framework for Microfinance Loans) Directions, 2022. The guideline provides for the NBFCs to put in place mechanisms to identify borrowers facing difficulties with loan repayment and guiding them on the available resources. Recovery of the loan can only be made at a designated place. If the borrower fails to appear on two or more successive occasions, field staff can make recovery from the place of residence or work of the borrower. Even then, the field staff or any loan recovery agent of the institution is not allowed to engage in coercive/ harsh methods for recovery. They cannot use threatening or abusive language or harass the borrower with persistent calling or calling at odd hours. Use or threat of violence as well as misleading the borrower on the consequences of non-repayment is also barred. In addition, the companies are required to provide the details of recovery agents to the borrower when the recovery process is initiated. Harassing the relative, friends or co-workers of the borrowers as well as harming their reputation is also not allowed by the guidelines. If the recovery agent is found in violation of any of the recovery guidelines, the NBFC is required to change the agent and inform the borrower of such change.

Many more such Industry-Specific as well as general compliances have to be managed by compliances officers in NBFCs. The following section will deal with some of the challenges faced by NBFCs in managing their compliance.

Details of some of the return to be submitted by systemically important NBFC (Having Asset size of ₹ 500/- Crore or more)

<table>
<tr><th>Sr. No</th><th>Act</th><th>Name of the Return</th><th>Frequency</th><th>Penalty</th></tr>
<tr><td>1</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS04B -SL&IRS</td><td>Monthly</td><td>Contravention shall be punishable with imprisonment upto 3 years. [Section 58(5)(aa) and Para 5 of Chapter II]</td></tr>
<tr><td>2</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS10 - SAC</td><td>Anually</td><td>Contravention shall be punishable with imprisonment upto 3 years. [Section 58(5)(aa) and Para 5 of Chapter II]</td></tr>
<tr><td>3</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS01-Important Financial Parameters</td><td>Quarterly</td><td rowspan="5">A) Contravention shall be punishable with i) fine not exceeding Rs. 10,00,000/-; or twice the amount involved in such contravention or default, where the amount is quantifiable, whichever is more;
ii) in case of continuing contravention fine which may extend to Rs. 1,00,000/- for every day, after the first, during which the contravention or default continues. [Section 58B (5)(aa) read with Section 58G(1)(b) of Reserve Bank of India Act, 1934].

B) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 58C of Reserve Bank of India Act, 1934].</td></tr>
<tr><td>4</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS03 -Important Prudential Parameters</td><td>Quarterly</td></tr>
<tr><td>5</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS04A - STDL</td><td>Quarterly</td></tr>
<tr><td>6</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>CRILIC</td><td>Quarterly</td></tr>
<tr><td>7</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>DNBS-13-Overseas Investments</td><td>Quarterly</td></tr>
<tr><td>8</td><td>Master Circular - Non-Banking Financial Companies - Corporate Governance (Reserve Bank) Directions, 2015</td><td>Change in Directors</td><td>Quarterly</td><td>Any contravention of or non-compliance with the circulars or directions may attract penalties as prescribed under the provisions of Chapter V of the RBI Act, 1934.</td></tr>
<tr><td>9</td><td>Master Direction - Monitoring of Frauds in NBFCs (Reserve Bank) Directions, 2016, RBI/DNBS/2016-17/49 Master Direction DNBS. PPD. 01/66.15.001/2016-17, Dated 29th September 2016</td><td>FMR-2&3</td><td>Quarterly</td><td rowspan="3">A) Contravention shall be punishable with i) fine not exceeding Rs. 10,00,000/-; or twice the amount involved in such contravention or default, where the amount is quantifiable, whichever is more;
ii) in case of continuing contravention fine which may extend to Rs. 1,00,000/- for every day, after the first, during which the contravention or default continues. [Section 58B (5)(aa) read with Section 58G(1)(b) of Reserve Bank of India Act, 1934].

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<tr><td>10</td><td>Master Direction - Monitoring of Frauds in NBFCs (Reserve Bank) Directions, 2016, RBI/DNBS/2016-17/49 Master Direction DNBS. PPD. 01/66.15.001/2016-17, Dated 29th September 2016</td><td>FMR-1</td><td>On occurance : 21 days from date of detection</td></tr>
<tr><td>11</td><td>Master Direction- Non-Banking Financial Company Returns (Reserve Bank) Directions, 2016</td><td>Submission of Certificate on compliance with FDI norms</td><td>Half Yearly</td></tr>
<tr><td>12</td><td>Company Profile Return - RBI letter No. DNBS.MRO.No. 8013/22.24.03/2007-08 dated February 26, 2008</td><td>Company Profile</td><td>Quarterly</td><td>Concerned authority will take appropriate action against the person in default.</td></tr>
</table>

Details of some of the returns to be submitted by non-deposit taking HFCs, with asset size of ₹100/- Crore & above but less than ₹5,000/- Crore

Sr. No	Act	Name of the Return	Frequency	Penalty
1	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	Schedule-V	Monthly	1) Contravention shall be punishable with a fine which may extend to Rs. 5,000. [Section 52A(1)(a) of The National Housing Bank Act, 1987] 2) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 50 of The National Housing Bank Act, 1987].
2	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	Schedule-IV	Quarterly	
3	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	ALM-I (STDL)	Quarterly	1) Contravention shall be punishable with a fine which may extend to Rs. 5,000. [Section 52A(1)(a) of The National Housing Bank Act, 1987]. 2) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 50 of The National Housing Bank Act, 1987].
4	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	20 Major Exposures	Quarterly	
5	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	SARFAESI	Quarterly	1) Contravention shall be punishable with a fine which may extend to Rs. 5,000. [Section 52A(1)(a) of The National Housing Bank Act, 1987]. 2) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 50 of The National Housing Bank Act, 1987].
6	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	Statement on Change of Directors	Quarterly	
7	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	Overseas Investment Report	Quarterly	1) Contravention shall be punishable with a fine which may extend to Rs. 5,000. [Section 52A(1)(a) of The National Housing Bank Act, 1987]. 2) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 50 of The National Housing Bank Act, 1987].
8	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021+B10:B11	ALM-II (SL&IRS)	Half yearly	
9	National Housing Bank Act, 1987 and Master Circular on Returns to be submitted by Housing Finance Companies (HFCs) NHB(ND)/DOS/Sup. Circular No.7/2021-22 dated December 31, 2021	Schedule-II	Half yearly	1) Contravention shall be punishable with a fine which may extend to Rs. 5,000. [Section 52A(1)(a) of The National Housing Bank Act, 1987]. 2) In case offence is committed by a company, every person in charge of the company or director, manager, secretary or other officer of the company shall be deemed to be guilty of the offence. [Section 50 of The National Housing Bank Act, 1987].

Details of some key critical compliances for Microfinance and Gold Loan Companies

Microfinance

- Submission of Statutory Auditor's Certificate
- NBFC-MFIs shall maintain a capital adequacy ratio consisting of Tier I and Tier II Capital which shall not be less than 15 percent of its aggregate risk weighted assets.
- All NBFC ensures to maintain margin caps not exceeding 10 per cent for large MFIs (loans portfolios exceeding Rs.100 crore) and 12 per cent for the others.
- NBFC-MFIs shall ensure that the average interest rate on loans during a financial year does not exceed the average borrowing cost during that financial year plus the margin.
- NBFC-MFI shall provide timely and accurate data to Credit Information Company (CIC)
- NBFC-MFIs shall review their back office operations and make the necessary investments in Information Technology and systems to achieve better control, simplify procedures and reduce costs.
- Ensuring minimum period of moratorium between the grant of the loan and the due date of the repayment of the first installment.
- NBFC-MFI shall provide a loan card to borrower reflecting-

  (i) the effective rate of interest charged;

  (ii) all other terms and conditions attached to the loan;

  (iii) information which adequately identifies the borrower; and

  (iv) acknowledgements by the NBFC-MFI of all repayments including installments received and the final discharge

Gold Loan

- NBFC-ND-SI to maintain Loan-to-Value (LTV) Ratio not exceeding 75 per cent for loans granted against the collateral of gold jewellery
- Every Systemically Important Non-Deposit taking Non-Banking Financial Company (NBFC-ND-SI) primarily engaged in lending against gold jewellery (such loans comprising 50 percent or more of their financial assets) shall maintain a minimum Tier I capital of 12 percent.
- Auction of the gold pledged to be held in the same town or taluka in which the branch of NBFC-MFIs has extended the loan
- Disclosure in balance sheet regarding the loans granted against the collateral of gold jewellery and their total assets by NBFC-MFIs
- NBFC-ND-SI to keep the record of verification of the ownership of gold jewellery of more than 20 grams
- Issuing certificate to the borrower while accepting gold as a collateral against loan by NBFC-ND-SI
- Every NBFC shall ensure to put in place Board approved policy for lending against gold that should inter alia, cover adequate steps to ensure that the KYC guidelines stipulated by RBI are complied with and to ensure that adequate due diligence is carried out on the customer before extending any loan.
- Every NBFC shall ensure that on lending against collateral of gold jewellery the loan agreement shall also disclose details regarding auction procedure.

4

Compliance Challenges for Non Banking Financial Companies

Between the Prevention of Money Laundering Act, 2002 and the Integrated Ombudsman Scheme, 2021 compliance officers of NBFCs' have to comply with several hundred acts and thousands of rules depending on the size of the business.

Depending on the type of NBFC, between the several acts by the state, and centre, there is also an additional pressure of keeping up with the policies and rules of the Reserve Bank of India (RBI) and NHB Regulations.

Given below are some of the major compliance challenges faced by the NBFC sector. Many of these are in congruence with a larger survey of clients conducted by Teamlease Regtech on regulatory complexity and the Ease of Doing Business in India (forthcoming in the India Compliance Report, 2022).

Increase in Compliance Burden due to new Prompt Corrective Action (PCA) Framework for NBFCs

RBI has vide notification dated December 12, 2021, newly introduced Prompt Corrective Action(PCA) Framework for NBFCs which will come into force on October 1, 2022 based on the financial position of NBFCs on or after March 31, 2022.To monitor the financial sustainability of the banking sector, RBI has come up with stricter supervisory norms under the PCA Framework.

What are the PCA risk thresholds for NBFCs

PCA refers to restrictions imposed by the banking regulator on a lender's operations if the key financial parameters of these entities fall below a certain limit. There will be three risk thresholds and three yardsticks to measure them. The restrictions against an NBFC get progressively tightened as it breaches higher threshold levels.

The first risk threshold of the PCA will be triggered when the capital adequacy ratio of the NBFC falls below the regulatory minimum of 15 per cent. If the ratio falls below 12 per cent, the second risk threshold will be triggered, while the ratio falling below 9 per cent triggers the third.

What happens if PCA framework is imposed

For an NBFC under threshold-1, the RBI will impose restrictions on dividend distribution/remittance of profits; also there will be restrictions on the issue of guarantees or taking on other contingent liabilities on behalf of group companies. Upon hitting risk threshold 2, the NBFC will be prohibited from opening branches, while on risk threshold 3, capital expenditure will be stopped other than for a technological upgrade.

Increase in Compliance Burden due to Revised Regulatory Framework for NBFCs: Scale-Based Regulations

Reserve Bank of India vide Notification dated 22.10.2021 announced its new scale- based regulations for the NBFC. The new guidelines will be applicable from 1st October 2022, which cover a wide range of revisions in the applicable NBFC Framework including but not limited to a structure based on scale, net owned fund requirements, board structure, corporate governance, capital requirements, prudential regulation, and other compliances.

Revised Regulatory Framework for NBFCs: Layer-based structure for NBFC

- Base Layer - This includes NBFCs with an asset size below INR 1,000 crore
- Middle Layer - It consists of all deposit-taking and non-deposit taking NBFCs with an asset size of INR 1,000 crore and above
- Upper Layer - The top 10 eligible NBFCs in terms of their asset size shall always reside in the upper layer, irrespective of any other factor
- Top Layer - This layer will remain empty and NBFCs in the upper layer may be moved to the top layer if the potential risk from specific NBFCs in upper layer

Regulatory Changes under SBR for all the layers in regulatory structure

- Net Owned Funds – Regulatory Minimum Net Owned Fund (NOF) for NBFC-Investment and Credit Companies (ICC), NBFC Micro Finance Institution (MFI) and NBFC-Factors would be increased to INR 10 crore. However, for NBFC-P2P, NBFC-AA, and NBFCs with no public funds and no customer interface, the NOF will continue to be INR 2 crore.
- NPA Classification – They will be required to recognise loans overdue for more than 90 days as NPAs by March 2026 and over 150 days by March 2024;
- Experience of the Board – At least one of the directors shall have relevant experience of having worked in bank/NBFC
- Ceiling on IPO Funding – Ceiling of INR 1 crore per borrower for financing subscription of IPOs

The revised regulatory framework being issued will ensure that strong and resilient financial system will be established in view of considerable evolution in terms of size, complexity, and interconnectedness As a financial sector regulator, the RBI has looked to tighten the screws on several regulatory and compliance aspects, so as to ensure that NBFCs are well-funded, efficiently managed, and insulated against various risks.

Fluid Regulatory Environment

India's regulatory environment is fluid. There are over 3,500 regulatory updates annually published on any of the 2,233 websites of Central, State and Local Government websites via notifications, gazettes, circulars, ordinance, master circulars, press releases among others. These changes typically lead to changes in forms, dates, timelines, frequencies, fines, interest rates calculations, applicability threshold values, letters of law among others. These changes are often applicable almost immediately and require a time sensitive interpretation and implementation. Based on a recent study done by TeamLease Regtech, it was found that there were over 1843 regulatory updates that affected a financial company in the last 12 months

Unfortunately, there is no centralized repository of regulatory updates that provides national, realtime, comprehensive and personalised information of all applicable regulatory changes that affects the compliance burden. As a result, the Compliance officer is often expected to periodically visit literally hundreds of websites to ensure that they are not missing any critical update.

Poor Tracking & Managing Applicable Licenses

A typical NBFC in India deals with hundreds of licenses. These include branch licenses, shop and establishment registration, Certification and Standardization requirements by RBI

Each license has many parameters including:

- Issue Date
- Expiry Date
- Categorisation of Industry (Red, Orange, Green, White)
- Conditions of License (Client Specific)
- Days for application for next renewal

Licenses, Registrations, Permissions, Consent Orders & NOCs need to be tracked meticulously to ensure that they are in good order failing which there are serious business consequences. Most organisations lack robust processes which provide adequate assurance for statutory license.

Intricate NBFC Compliances in India

After the NBFC incorporation, it is also needed to address multiple compliances. NBFC compliance differs from one company's type to another for example NBFC can be systematically important (whose asset size is ₹ 500 cr or more as per the last audited balance sheet) or non-systematically important as well deposit-taking and non-deposit-taking. Moreover, it also becomes tedious to know about the filing requirement of the prescribed returns. This is probably one of the most intricate challenges encountered by NBFCs. Increase in compliance for NBFC's notified under Scale Based Regulation (SBR):

For example Small NBFCs are exempted from the maintenance of the Capital Adequacy Ratio (CRAR). But they can't exceed the leverage ratio beyond 7 which is quite restrictive.

NBFC compliances can get complicated as:

- Multiple filing and monitoring requirements once frauds are identified
- Stringent requirements for transfer of loan exposures
- Need to comply with Prevention of Money Laundering Act, 2002 and Prevention of Money Laundering (Maintenance of Records) Rules, 2005
- Multiple audit requirements once cross certain threshold of asset size
- Increase in compliance for NBFC's notified under Scale Based Regulation (SBR): A
- Revised Regulatory Framework for NBFCs 2021
- Stringent timeless set to revert on queries and complains shared by the customers

Lack of an accurate list of Applicable Compliances

A NBFC operating in a single state in India deals with at least 621 compliances in a year. As the company grows its geographical footprint, the number of compliances multiply. These compliances are at three levels; Center, State and Local. In addition, they are in seven compliance categories; Labour, Finance & Taxation, Commercial, Secretarial, EHS, Industry Specific and General. Identification of applicable compliances for a NBFC company requires deep expertise.

The applicability changes based on the location of the NBFC, the number of branches, the type of NBFC(Asset Finance, Investments, Infrastructure Finance, Gold Loans etc) use of specific equipment (vaults, digital security). In addition, there are challenges pertaining to obtaining necessary licenses from RBI. The process involves tedious and complex documentation processes and approval from RBI. Keep in mind that RBI regulates the process which requires to be followed by the applicant to avail of the registration.

In addition, the laws constantly undergo amendments leading to periodic change of applicability. Legislation of new regulations also affect the organisation's compliance obligations management.

Poor tracking of Event Based Compliances

From evolving a cyber crisis management plan to notifying the RBI in case of breach of security and leakage of customer information, NBFCs are riddled with critical event based compliances.

There are many instances where the applicability of licenses and compliances changes based on occurrence of specific business events. As a result, the compliance officer needs to keep his eyes peeled to identify such occurrences and be ready to interpret and implement their impact on the organisation's compliance obligations.

NBFCs companies deal with the challenge of tracking all these applications and their statuses to stay on the right side of the law.

Poor tracking of on-going Compliances

A typical NBFC deals with a large number of compliances that are on-going in nature. From quarterly statement on change of directors to Quarterly submission of Return on Overseas Investment.

Other ongoing compliances also include include displays (licenses, registrations, abstracts of legislations, employee related social security based displays, no smoking, fire exits, danger signs, GST Number, abstract for prohibition of employement of child labour, no smoking area,) In addition, the company also needs to maintain a variety of registers which should be current at any time.

Creating, maintaining, reviewing and certifying that these registers are in compliance with the law of the land is the responsibility of different people across the organization. Unfortunately, there are no enterprise processes to track and maintain the digital copies of these registers and obtain periodic self certification from the relevant stakeholders.

Lack of Awareness at Management Level

Based on a recent survey conducted by TeamLease Regtech, it was discovered that the KMPs (Key Management Personnel) in Indian NBFCs have a poor understanding of compliance obligations in over 75% of the instances. As a result, they are often unpleasantly surprised in the events of show cause notices, instances of financial fines and penalties, canceled licenses, revoked permissions and leaked revenue.

Most executives were found to have very poor handle on the status of key compliances, dates, documentation and residual risk of non-compliance.

Manual, Paper Based & People Dependent Compliance

A typical NBFC company deals with a few thousand compliances in a year. There are at least 50-100 people in different departments (Human Resources, Finance & Tax, Company Secretarial, Administration, Warehouse, credit, customer services, collection, Treasury) directly involved in day to day compliance functions. Unfortunately, while compliance is a key binding constraint in an organisation's growth, a number of Indian organisations are yet to adopt technology platforms for transparent and accountable compliance programs. The compliance officers often use spreadsheets to track status manually. As a result, there are several instances where there are inadvertent misses, delays, lapses, defaults, expired licenses and missed legal updates.

It is not uncommon to see them firefighting and highly stressed during regulatory audits.

Anecdotal Compliance Certification

The Companies Act, 2013 Section requires the issue of Compliance Certificates to the Board. Since the organization is low on technology based tracking systems, the compliance officer has no other choice but to prepare the statutory compliance certificates manually. These certificates often miss key information such as the specific data on an instance of non compliance, delayed filing and the residual risk of poor compliance.

In such instances, the board is often flying blind. They do not have a framework to establish the level of compliance in the company.

5 Industry Perspectives

In a recent survey conducted by TeamLease Regtech on compliance officers of major NBFC Compliances, here are the key findings:

- 92% agreed to have missed at least one critical compliance during the 12 month period
- 93% agreed to pay fines and penalties in the 12-month period
- 94% believed that they do not have the required visibility and control in their organization's compliance program
- 82% agreed that their Compliance needs a serious rethink
- 79% of Compliance officers believe that third party consultants have better liaisoning experience than they have internally
- 66% agreed to have poor control on their compliance documents
- The average cost of compliance consultants stood at approximately INR 100,000 per month; Labour contributed approximately 35% of the cost
- 56% believed that keeping track of regulatory updates is challenging

6 Rethinking Compliance Management

Conduct a baseline applicability assessment

An accurate list of applicable compliances is the first and perhaps the most important step in streamlining any organization's compliance management. The applicability of compliance changes with the use of specific equipment, input raw material and end products. Stringent timelines to comply the new regulations like the scale based regulation, 2021 and changing reportings further add to the complexity of the compliance. Engaging with a partner vendor to track and create a consolidated assessment of all applicable acts and compliances is critical to effective compliance management.

Companies must engage a partner who brings the depth and width of experience to assess and document the compliance obligations across Union, State and Local laws. In addition, the partner should help classify all the compliance requirements in seven categories; Labour, Finance & Taxation, Environment health and Safety, Secretarial, Commercial and Industry specific. The list should be subclassified by compliance type; licenses, registrations, permissions, consent orders, returns, registers, challans, payments, displays, audits and examinations, committees, exemptions among others.

This checklist should serve as a baseline and should be periodically reviewed and refreshed based on the business changes.

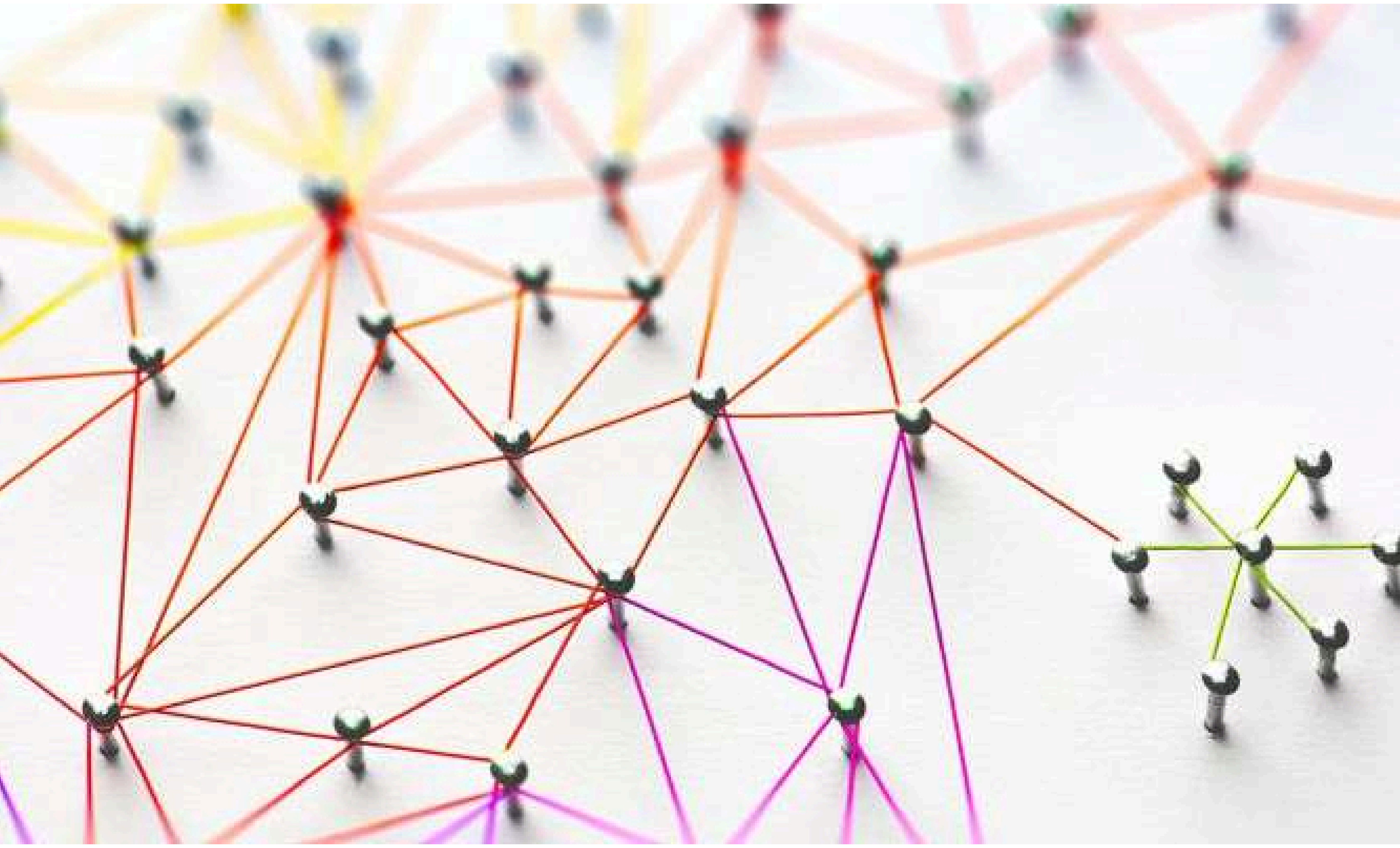
Subscribe to National, Realtime & Personalised Regulatory Updates

It is arduous for a compliance office to browse a few hundred government websites periodically to discover the applicable compliance changes. It is recommended that the company subscribe to national, real time, personalised and comprehensive regulatory updates from a third party vendor. These updates should be available on a daily, weekly and monthly basis; categorized by Act, category of the law, union / state, regulator, nature of change, date of change applicability among others. The update should have search, sort and filter capabilities for easy consumption. Mobile app (IOS and Android) and email based updates are highly recommended.

There are industry leading players such as TeamLease Regtech (www.teamleaseregtech.com) who provide personalised updates in daily / weekly / monthly newsletters and mobile apps.

Create a culture of Compliance

Compliance management becomes a breeze if all the stakeholders hold their end of the stick. While one compliance officer takes responsibility, many key folks within the organisation bring their shoulder to the load. Periodic reviews at department level, functional level and organisational level help make people accountable. In addition, reviews help bubble up issues before they become urgent and important. You should work with your human resources team and add compliance goals as a part of goal setting, mid term assessment and annual assessments. Good compliance behaviour should be rewarded.



Digitize Compliance Management

Technology is transforming key business processes. It is making them faster, easier and cheaper. Technology enables enhanced collaboration and improves human productivity. Data is the new oil. Compliance is a key business process and needs to go digital. Your preferred software solution should have the features given below:

- Smart Dashboards - Easy to use, real time, colour-coded with drill down capabilities
- Native Mobile Apps - IOS & Android based mobile apps
- Flexible Workflows - Configurable workflows which adapt to your business processes
- Integrated Comprehensive Compliance Database - Comprehensive and accurate compliance database covering the law of the land
- Strong Analytics and Reporting - Automated and on-demand analytics and reporting capabilities to flag non-compliance and risks
- Integration with your Office email - Legal updates / alerts / notifications / reminders / escalations / reports on your office email
- Integrated Document Management System - Manage all your compliance documents and working files with version management
- SAAS Based - Quick and Easy to on-board without any additional IT infrastructure and licenses
- Secure & Available - Best in class information security with availability when you need it

Ease of Use

Compliance cuts across your organisation. Employees at various levels of skill, experience and technology-savviness need to feel comfortable using it. You should ensure that your software vendor has a product which has a user-friendly interface for end user adoption.

Quick and easy Deployment

Ensure that end to end on-boarding happens in a few weeks as IT projects are notorious for time and budget overruns. If it takes more than a few weeks to go-live, chances are the project will lose momentum and will cause headaches. In addition, ensure that your vendor has strong capabilities in business discovery, compliance applicability assessment, product configuration and end user training. SAAS and cloud based products should be preferred as they do not require any on-premises technology infrastructure (virtual machines, network resources, storage, firewalls, load balancing among others)

Pay as you go Pricing Option

IT budgets are stretched. There is a constant tussle between CIO and CFO on additional capital allocation for digitisation projects. Perpetual licensing options can be extremely capital intensive. It is highly recommended that you evaluate and prefer ‘pay as you go’ pricing, as budgetary allocation and approval might become a breeze. Such price options are typically cheaper than the salary of a junior compliance officer.

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