

RBI/2009-10/15

DNBS (PD) CC No. 153 / 03.10.042 / 2009-10

July 1, 2009

To

All Non-Banking Financial Companies (NBFCs)
and Residuary Non-Banking Companies (RNBCs)

Dear Sir,

Master Circular - Fair Practices Code

In order to have all current instructions in one place, the Reserve Bank of India has consolidated all the instructions issued on the topic as at end of June 30, 2009. It may be noted that the Master Circular consolidates and updates all the instructions contained in the notifications listed in the Appendix in so far they relate to the subject. The Master Circular has also been placed on the RBI web-site (<http://www.rbi.org.in>).

Yours sincerely

(P.Krishnamurthy)
Chief General Manager-in-Charge

The Reserve Bank of India, being satisfied that for the purpose of enabling it to regulate the credit system of the country to its advantage, it is necessary to do, hereby, in exercise of powers conferred under Section 45 L of the Reserve Bank of India Act, 1934 (Act 2 of 1934) and of all the powers enabling it in this behalf, hereby prescribes the broad guidelines on fair practices that are to be framed and approved by the Board of Directors of all Non- Banking Financial Companies (including RNBCs). The fair practices code so framed and approved by the Board of Directors should be published and disseminated on the web-site of the company, if any, for the information of the public. The Fair Practices Code based on guidelines given below were to be put in place by all NBFCs with the approval of their Boards within one month from the date of issue of the circular dated September 28, 2006.

Guidelines on Fair Practices Code for NBFCs

(i) Applications for loans and their processing

- (a) Loan application forms should include necessary information which affects the interest of the borrower, so that a meaningful comparison with the terms and conditions offered by other NBFCs can be made and informed decision can be taken by the borrower. The loan application form may indicate the documents required to be submitted with the application form.
- (b) The NBFCs should devise a system of giving acknowledgement for receipt of all loan applications. Preferably, the time frame within which loan applications will be disposed of should also be indicated in the acknowledgement.

(ii) Loan appraisal and terms/conditions

The NBFCs should convey in writing to the borrower by means of sanction letter or otherwise, the amount of loan sanctioned along with the terms and conditions including annualised rate of interest and method of application thereof and keep the acceptance of these terms and conditions by the borrower on its record.

It is understood that in a few cases, borrowers at the time of sanction of loans are not fully aware of the terms and conditions of the loans including rate of interest, either because the NBFC does not provide details of the same or the borrower has no time to look into detailed agreement.

Accordingly, it was advised that not furnishing a copy of the loan agreement or enclosures quoted in the loan agreement is an unfair practice and this could lead to disputes between the NBFC and the borrower with regard to the terms and conditions on which the loan is granted.

NBFCs are, therefore, advised to invariably furnish a copy of the loan agreement along with a copy each of all enclosures quoted in the loan agreement to all the borrowers at the time of sanction / disbursement of loans.

(iii) Disbursement of loans including changes in terms and conditions

- (a) The NBFCs should give notice to the borrower of any change in the terms and conditions including disbursement schedule, interest rates, service charges, prepayment charges etc. NBFCs should also ensure that changes in interest rates and charges are effected only prospectively. A suitable condition in this regard should be incorporated in the loan agreement.
- (b) Decision to recall / accelerate payment or performance under the agreement should be in consonance with the loan agreement.
- (c) NBFCs should release all securities on repayment of all dues or on realisation of the outstanding amount of loan subject to any legitimate right or lien for any other claim NBFCs may have against borrower. If such right of set off is to be exercised, the borrower shall be given notice about the same with full particulars about the remaining claims and the conditions under which NBFCs are entitled to retain the securities till the relevant claim is settled/paid.

(iv) General

- (a) NBFCs should refrain from interference in the affairs of the borrower except for the purposes provided in the terms and conditions of the loan agreement (unless new information, not earlier disclosed by the borrower, has come to the notice of the lender).
- (b) In case of receipt of request from the borrower for transfer of borrowal account, , the consent or otherwise i.e. objection of the NBFC, if any, should be

conveyed within 21 days from the date of receipt of request. Such transfer shall be as per transparent contractual terms in consonance with law.

(c) In the matter of recovery of loans, the NBFCs should not resort to undue harassment viz. persistently bothering the borrowers at odd hours, use of muscle power for recovery of loans , etc..

(v) The Board of Directors of NBFCs should also lay down the appropriate grievance redressal mechanism within the organization to resolve disputes arising in this regard. Such a mechanism should ensure that all disputes arising out of the decisions of lending institutions' functionaries are heard and disposed of at least at the next higher level. The Board of Directors should also provide for periodical review of the compliance of the Fair Practices Code and the functioning of the grievances redressal mechanism at various levels of management. A consolidated report of such reviews may be submitted to the Board at regular intervals, as may be prescribed by it.

(vi) Fair Practices Code based on the guidelines outlined hereinabove should be put in place by all NBFCs with the approval of their Boards within one month from the date of issue of this circular. NBFCs will have the freedom of drafting the Fair Practices Code, enhancing the scope of the guidelines but in no way sacrificing the spirit underlying the above guidelines. The same should be put up on their web-site, if any, for the information of various stakeholders.

Complaints about excessive interest charged by NBFCs

(vii) (A) The Reserve Bank has been receiving several complaints regarding levying of excessive interest and charges on certain loans and advances by NBFCs.

Though interest rates are not regulated by the Bank, rates of interest beyond a certain level may be seen to be excessive and can neither be sustainable nor be conforming to normal financial practice.

Boards of NBFCs are, therefore, advised to lay out appropriate internal principles and procedures in determining interest rates and processing and other charges.

In this regard the guidelines indicated in the Fair Practices Code about transparency in respect of terms and conditions of the loans may be kept in view.

NBFCs may confirm having put in place appropriate systems in this regard within a period of one month from the date of this circular to the Regional Office of this Department in whose jurisdiction they are registered.

(B) The Reserve Bank of India, on being satisfied that for the purpose of enabling to regulate the credit system of the country to its advantage, it is necessary so to do, in exercise of powers conferred under Section 45 L of the Reserve Bank of India Act, 1934 (2 of 1934) and of all the powers enabling it in this behalf, hereby issues the following Directions to NBFCs:

- (a) The Board of each NBFC shall adopt an interest rate model taking into account relevant factors such as, cost of funds, margin and risk premium, etc and determine the rate of interest to be charged for loans and advances. The rate of interest and the approach for gradations of risk and rationale for charging different rate of interest to different categories of borrowers shall be disclosed to the borrower or customer in the application form and communicated explicitly in the sanction letter.
- (b) The rates of interest and the approach for gradation of risks shall also be made available on the web-site of the companies or published in the relevant newspapers. The information published in the website or otherwise published should be updated whenever there is a change in the rates of interest.
- (c) The rate of interest should be annualised rates so that the borrower is aware of the exact rates that would be charged to the account.

Clarification regarding repossession of vehicles financed by NBFCs

(vii) It is further clarified to NBFCs excluding RNBCs that, with particular reference to queries raised regarding repossession of vehicles, NBFCs must have a built in repossession clause in the contract/loan agreement with the borrower which must be legally enforceable. To ensure transparency, the terms and conditions of the contract/loan agreement should also contain provisions regarding: (a) notice period before taking possession; (b) circumstances under which the notice period can be waived; (c) the procedure for taking possession of the security; (d) a provision regarding

final chance to be given to the borrower for repayment of loan before the sale / auction of the property; (e) the procedure for giving repossession to the borrower and (f) the procedure for sale / auction of the property. A copy of such terms and conditions must be made available to the borrowers in terms of circular wherein it was stated that NBFCs may invariably furnish a copy of the loan agreement along with a copy each of all enclosures quoted in the loan agreement to all the borrowers at the time of sanction / disbursement of loans, which may form a key component of such contracts/loan agreements.

Appendix

Sr. No.	Circular No.	Date
1.	<u>DNBS (PD) CC No. 80 / 03.10.042 / 2005-06</u>	September 28, 2006
2.	<u>DNBS.PD/ CC.No. 95 /03.05.002 /2006-07</u>	May 24, 2007
3.	DNBS.PD/ CC. No. 107 / 03.10.042 /2007-08	October 10, 2007
4.	<u>DNBS (PD) C.C. No. 133 /03.10.001/ 2008-09</u>	January 2, 2009
5.	<u>DNBS (PD) CC.No.139 /03.10.001/2008-09</u>	April 24, 2009