# OVERVIEW OF RESERVE BANK'S DIRECTIONS TO AUDITORS OF NBFCs

**Ashhok Saxena, Company Secretary**

Reserve Bank of India has issued fresh directions to the auditors of Non-Banking Financial Companies (NBFCs) called Non-Banking Financial Companies Auditor's Report (Reserve Bank) Directions, 2008[1] after superseding the earlier directions issued in the year 1998. These Directions are applicable to every auditor of a NBFC who is required to make a separate report to the Board of Directors of the Company on the matters specified in the Directions apart from the Report made by him under Section 227 of the Companies Act, 1956. The Directions also make it obligatory for the auditor to state the reasons in case his report contains unfavourable or qualified statements regarding any of the specified matters required to be covered in the Report. If, however, the auditor is unable to express any opinion on any of the specified matters, his report shall indicate such fact together with reasons therefor. This article seeks to discuss the matters contained in the present Directions.

**Auditor's Report: Matters to be included**

The Directions specify various matters for inclusion in the auditor's report on the accounts of a NBFC. Certain general matters are required to be included in case of all NBFCs whereas certain other matters are to be included in the Report based on the fact whether the NBFC is accepting public deposits or not. A statement is also to be included in respect of those NBFCs which are exempted from holding certificate of registration (CoR) subject to certain conditions. The matters to be specified in the Report are discussed in the following paragraphs:

***General Matters for inclusion in case of all NBFCs:*** Specified matters to be covered by the auditor in his report in respect of all NBFCs, irrespective of their classification are as under:

- Statement regarding engagement of NBFC in the business of non-banking financial institution and that the concerned company has obtained a Certificate of Registration (CoR) from the RBI.

  ***Note:*** In the case of a company which is engaged in the business of non-banking financial institution but is not required to hold CoR subject to certain conditions as stipulated by the RBI, the auditor is required to state in the report if the company is complying with the stipulated conditions as advised by the RBI.

- Statement indicating the entitlement of the NBFC to continue to hold CoR in terms of its asset/income pattern as on March 31 of the applicable year.

[1] Issued vide Notification No. DNBS (PD)201/DG(VL)/2008, dated 18.9.2008.

- Statement reflecting the correct classification of the NBFC as Asset Finance Company (AFC) with reference to the business carried on by it during the applicable financial year.

***Specified Matters for inclusion in case of NBFCs accepting/holding Public Deposits:*** Following matters, in addition to general matters stated above, are to be covered by the auditor in his report in respect of those NBFCs which are accepting/holding public deposits:

- Statement indicating that the public deposits accepted by the company together with other borrowings are within the limits admissible to the company as per the provisions of the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998.

- Statement regarding the regularization of excess public deposits (held in excess of the permissible quantum) in the manner provided in the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998.

- Statement indicating if the AFC having CRAR less than 15% or the Investment Company or the Loan Company is accepting "public deposit" without minimum investment grade credit rating obtained from an approved credit rating agency.

- Statement mentioning that the credit rating assigned for each of the fixed deposits schemes of the NBFC by the approved Credit Rating Agency is in force. And further, whether the aggregate amount of deposits outstanding as at any point during the year has exceeded the limit specified by such Credit Rating Agency.

- Statement indicating if the NBFC[2] holds public deposits in excess of the permissible quantum in terms of Notification No. DNBS. 199/CGM (PK) - 2008, dated 17.6.2008. And if yes,
    - whether it has frozen its level of deposits as on the date of that Notification; or
    - whether it has brought down its level of deposits to the level of revised ceiling of deposits in terms of that Notification.

- Statement reflecting the fact if the NBFC has defaulted in paying to its depositors the interest and /or principal amount of the deposits after such interest and/or principal became due.

- Statement regarding compliance with the prudential norms on income recognition, accounting standards, asset classification, provisioning for bad and doubtful debts, and concentration of credit/investments.

[2] Applicable in case of NBFCs having NOF of Rs 25 lakh and above but less than Rs 200 lakhs.

- Statement mentioning that the capital adequacy ratio as disclosed in the return submitted to the RBI is correctly determined and further, such ratio is in compliance with the minimum prescribed CRAR.

- Statement regarding compliance with the prescribed liquid assets requirement and further that the details of the designated bank in which the approved securities are held is communicated to the concerned office of the RBI.

- Statement indicating that the NBFC has furnished to the RBI within the stipulated period the return on deposits as specified in the NBS-1.

- Statement indicating that the NBFC has furnished to the RBI within the stipulated period the half-yearly return on prudential norms as specified in the Non-Banking Financial (Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007.

- Statement regarding compliance with the requirements contained in the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998, in the case of opening of new branches or offices to collect deposits or in the case of closure of existing branches/offices or in the case of appointment of agents.

***Specified Matters for inclusion in case of NBFCs NOT accepting Public Deposits:*** Following matters, in addition to the general matters only, are to be covered by the auditor in his report in respect of those NBFCs which are not accepting public deposits:

- Statement indicating that the Board of Directors has passed a resolution for non-acceptance of any public deposits.

- Statement mentioning if the NBFC has accepted any public deposits during the relevant period/year.

- Statement regarding compliance with the prudential norms relating to income recognition, accounting standards, asset classification and provisioning for bad and doubtful debts.

- Statement mentioning that the Systemically Important Non-deposit taking NBFC has correctly calculated the capital adequacy ratio which is disclosed in NBS-7, and further, such ratio is in compliance with the minimum CRAR prescribed by the RBI. In addition, it is also to be stated that the company has furnished to the RBI the annual statement of capital funds, risk assets/exposures and risk asset ratio (NBS-7) within the stipulated period.

**Submission of an Exception Report to the RBI**

The Directions make it obligatory on the part of the auditor of NBFC to submit a Report to the RBI also, in case he makes an unfavourable or qualified statement regarding any of the specified matters to be covered in his report or if in his opinion the company has not complied with:

- the provisions of Chapter III B of the RBI Act, 1934; or
- the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998; or
- the Non-Banking Financial (Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007; or
- the Non-Banking Financial (Non- Deposit Accepting or Holding) Companies Prudential Norms (Reserve Bank) Directions, 2007.

The Report containing the details of qualified statements and the non-compliances shall be submitted to the concerned Regional Office of the Department of Non-Banking Supervision of the Bank under whose jurisdiction the registered office of the company is located as per Second Schedule to the Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 1998. It is to be noted that such report shall not contain any statement with respect to compliance of any of the provisions.