FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organisation for Registered NBFCs – AFCs)

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

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September 16, 2014

Shri P. Vijaya Bhaskar
Executive Director,
Reserve Bank of India
Central Office Building
17th Floor, Shahid Bhagat Singh Road
Mumbai-400 001.
2262409022660797

Dear Sir,

SUB: RBI circular DNBS(PD).CC.No.399/03.10.42/2014-15 dated July 14, 2014 addressed to all Non Banking Financial Companies/Residuary Non Banking Companies with regard to Levy of foreclosure charges/pre-payment penalty on Floating Rate Loans.

With reference to the above, we have to state as under:

Vide the above circular, RBI has stipulated that as a measure of customer protection and also in order to bring in uniformity with regard to prepayment of various loans by borrowers of banks and NBFCs, it is advised that NBFCs shall not charge foreclosure charges/pre-payment penalties on all floating rate term loans sanctioned to individual borrowers, with immediate effect.

In this regard, we wish to seek your clarification if the above circular is applicable with regard to the new loans to be booked from July 14, 2014, being the date of the circular or is intended to be made applicable with retrospective effect on all the existing loan sanctions.

We would wish to make the following observations for your kind consideration:

- It is a known fact that fixed rate loans are more expensive than the floating rate loans particularly in the case of home equity/home loans, as they are typically longer term loans and hence the funds are also borrowed on long tenors to manage the asset liability appropriately. Hence, while sanctioning such floating rate loans, the rates were kept lower building the foreclosure charges committed in the loan. The rates offered to the customers for floating rate loans are not exorbitant, and the reason for offering lower rates to the customers, including those who do not have a credit history till now, the first to credit customers, was the foreclosure charges. Removing such foreclosure charges all of a sudden with retrospective effect, would cause a spate of premature closure of loans to switch to another Lender with a softer loan, causing significant drop in revenues for the NBFCs besides creating a huge impact on the asset liability management of NBFCs.

- The biggest challenge that the waiver of Foreclosure charges pose, over and above the drop in the income, is the threat of a rapid portfolio depletion with all the NBFCs. This would be caused as there are no exit barriers for the customers with the removal of foreclosure charges and the customer is free to switch as many times as he wants to, from one lender to the another. There will be large numbers of floating rate loan book size with several NBFCs, causing a huge fall in the assets under management and the resulting drop in revenues.

- As you may be aware, the customers that NBFCs as a business have acquired, are mostly first to credit customers, acquired with detailed due diligence on the customer's business model and the collateral offered by the customer as there is no CIBIL or any other credit history. Each and every customer is met and the collateral visited, before disbursing any loan, this stands true for customers with no credit history. After the customer is on our books for 6-12 months, and has built a credit history, the banks poach the customers by offering him lower rates and fees, which we are not able to match in view of the structural differences. As both banks and NBFCs operate in the same market with significantly different interest rates, removal of foreclosure charges, ***retrospectively***, will result in several of our customers being poached by banks who would be able to offer them much attractive interest rates at the cost and efforts of NBFCs who have tested and created a credit history for the customers.

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- Customers could also misuse this move to move on from financier to financier to try and increase their borrowings, thereby putting the loan at risk, if the quantum of the loan amount increases beyond his repaying capacity.

- Any transaction including the Lending rate is a package, based on number of factors, such as credit worthiness, tenor, fixed or floating rate etc., and removing one important factor without looking at the balance of factors is bound to create problems for the existing Lenders. Far reaching moves such as these should be implemented prospectively with proper advance Notice.

While we understand and appreciate the waiver of the foreclosure charges would benefit the customers and can be implemented **for future cases**, since the NBFCs will then structure and price it accordingly, enforcing it with retrospective effect, would greatly inconvenience and shake up NBFCs and create a huge systemic impact on the entire system.

We hope you will consider the above request and issue the necessary clarification.

We look forward to an **immediate positive response** and are confident that we are in the process of a long and beneficial relationship.

Thanking you,

Yours sincerely,

FOR FINANCE INDUSTRY DEVELOPMENT COUNCIL

MAHESH THAKKAR
Director General