To,
Mr. Vaibhav Chaturvedi
Chief General Manager
Department of Regulation
Reserve Bank of India

Sub: Representation for inclusion of acquired portfolios as eligible assets for determining the principality of Housing Finance Companies

Dear Sir/Ma'am,

We, Indian Securitisation Foundation, on behalf of the structured finance industry intend to draw your attention to the uncertainty amongst the housing finance industry participants regarding the inclusion of acquired housing finance loans as eligible assets while determining the principality for a non-banking finance company ('NBFC') to be classified as a housing finance company ('HFC').

The principal business criteria (PBC) for HFCs (Refer Annex I) requires the following:

a. At least 60% of the total assets of the company to be financial assets in housing finance; and
b. At least 50% of the total assets to be financial assets in housing finance to individuals.

We have come across situations where market participants have taken a view that the pools of housing loans acquired through direct assignment (DA) transactions shall not be included in the computation of financial assets for the purpose of PBC for HFCs. HFCs have been taking a view that it is only originated loans which are to be included for the purpose of the regulatory minimum ratios (60 and 50% as above).

In this regard, we hereby make the following submissions:

a) Acquisition of home loans may be done either organically, that is, through self-origination, or by acquiring pools of eligible home loans, by Transfer of Loan Exposures as per Master Direction – Reserve Bank of India (Transfer of Loan Exposures) Directions, 2021[1] ('TLE Directions'), which is a permitted mode of building a loan book. Evidently, every player in the housing finance business has geographical limitations, as also limitations in terms of number of branches, customer access, etc. Hence, self-origination mode is not feasible for many HFCs. Even if the HFC is partly originating itself, there seems little reason for the HFC to not acquire a loan pool which is otherwise fitting into the policy and underwriting standards of the HFC. As a part of the requirement of the TLE Directions [para 35], the acquiring lender has to do the same level of credit due diligence and KYC

[1] https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12166

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Website: www.indiansecuritisation.com
Email: info@indiansecuritisation.com; vinod@vinodkothari.com

checks as required at the time of origination, which clearly indicates that the regulator is not distinguishing between self-origination and TLE acquisition.

b) The TLE Directions recognise three modes of transfer of loans, namely assignment, novation and loan participation. Same as in the case of assignment, in case of novation as well, the acquirer shall subrogate the legal rights and obligations of the originator;

c) Transfer of loans puts the acquirer in the position of the originator. Along with the loan portfolio, all the rights and obligations of the originator are transferred to the acquirer through assignment. Hence, the acquirer legally steps into the shoes of the originator and should rightly be treated as such;

d) The acquired pools, irrespective of the mode of transfer, are accounted in the books of the transferee on a loan-by-loan basis. The capital adequacy requirements and prudential norms are also applicable to the transferee as if the portfolio was originated by the transferee;

e) Upon transfer of loans under the TLE Directions, the risks and rewards underlying the portfolio are transferred to the transferee without any recourse to the transferor w.r.t transferred loan exposure. As a result, the assets in the books of the transferor shall get derecognised and be recorded in the books of the transferee. The transferor does not consider such eligible assets for computation of its PBC for being determined as an HFC. Since the said assets are not considered as financial assets in housing finance of the transferor, the same should be considered as financial assets in housing finance for the transferee;

f) The Master Directions – Priority Sector Lending (PSL) – Targets and Classification[2] allow fulfilment of PSL targets by either making investments in securitisation transactions backed by PSL loans or by acquiring a portfolio of PSL loans. The whole intent behind this is to promote PSL lending systemically. Similar treatment must be accorded in case of housing loans because, like priority sectors, housing is also a sensitive sector, the flow of credit in the housing sector should grow systemically.

g) The RBI, being the regulator of the financial sector, has been making several efforts to promote the securitisation and DA market in India. Further, the Harshvardhan Committee[3] has been doing tremendous work in the direction of promoting the securitisation market for housing finance receivables in India. Promoting securitisation and DA has been high on the agenda of the RBI for the last few years. Not recognising acquired pools as eligible housing finance assets may act as a demotivator for HFCs intending to enter into this market. Further, as a result of the loan transfer, the transferor releases its capital, and moves on to originate further loans. By restricting

[2] https://rbidocs.rbi.org.in/rdocs/notification/PDFs/MDPSL803EE903174E4C85AFA14C335A5B0909.PDF
[3] https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=941

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secondary market activity in home loans, the aggregate supply of housing finance, crucial for achieving affordable housing finance, is getting curtailed.

h) Inclusion of acquired housing finance pools in computation of financial assets for the purpose of computation of PBC for HFCs will assist affordable housing finance companies to reduce their cost of funds, which in turn would enable flow of housing finance to untapped sectors. The Government of India has a target to ensure 'Housing for All' by 2022. Securitisation and DA have the potential to enable the government to meet this lofty dream in the upcoming years. Taking a view that acquired pools shall not be considered as financial assets for the purpose of computation of PBC for HFCs, may counter the objectives of the Government of India and the RBI.

As mentioned earlier, there is an ambiguity among the market participants whether to classify such acquired loan exposures as eligible housing finance assets. The HFCs are currently transitioning from the old regulatory framework to the new regulatory framework, and the year ending 31st March 2022 is the first complete year of implementation, by which all the HFCs have to ensure that at least 50% of total assets are housing finance assets and 40% of the total assets are housing finance to individuals.

In absence of clarity on whether acquired portfolios shall be considered as eligible assets, several HFCs may fail to meet the criteria by the said timeline of March 31, 2022.

Hence, we request you issue a clarification stating that the acquired housing loans should be considered for the purpose of PBC for HFCs.

In case of any clarifications, please reach out to us.

Thanking you,

For **Indian Securitisation Foundation**

VINITA NAIR

Digitally signed by VINITA NAIR
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Date: 2021.12.10 11:56:26 +05'30'

Vinita Nair
Director
DIN: 08067063

Date: December 10, 2021

INDIAN SECURITISATION FOUNDATION

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Annex I- PBC for HFCs

HFCs are regulated by the Reserve Bank of India ('RBI') *vide* powers conferred by the Finance Act, 2019[4] read with RBI Press Release no. 2019-2020/419 dated August 13, 2019[5]. The RBI has issued Master Direction – Non-Banking Financial Company – Housing Finance Company (Reserve Bank) Directions, 2021[6] ('HFC Directions') which regulates the operations of HFCs.

The HFC Directions define a housing finance company as:

> *4.1.17. "**Housing finance company**" shall mean a company incorporated under the Companies Act, 2013 that fulfils the following conditions:*
>
> *a. It is an NBFC whose financial assets, in the business of providing finance for housing, constitute at least 60% of its total assets (netted off by intangible assets). Housing finance for this purpose shall mean providing finance as stated at clauses (a) to (k) of Paragraph 4.1.16.*
>
> *b. Out of the total assets (netted off by intangible assets), not less than 50% should be by way of housing finance for individuals as stated at clauses (a) to (e) of Paragraph 4.1.16.*
>
> *Note: The above-mentioned conditions shall be treated as Principal Business Criteria for HFCs and are applicable from the date of original instructions issued vide circular DOR.NBFC (HFC).CC.No.118/03.10.136/ 2020-21 dated October 22, 2020.*

In order to qualify as an HFC, a company must fulfil the following conditions:

a) It should be a company registered under the Companies Act, 2013 or erstwhile Companies Act, 1956;

b) It must be an NBFC i.e. it must fulfil the Principal Business Criteria (PBC) applicable to an NBFC. The PBC for an NBFC requires at least 50% of the total assets of the company to be financial assets and at least 50% of the total income to be derived from such financial assets;

c) In addition to fulfilling the above discussed PBC, the company must also fulfil the following additional conditions, hereinafter referred to as PBC for HFCs:
   - At least 60% of the total assets must be financial assets in housing finance;
   - At least 50% of the total assets must be financial assets in the form of housing finance to individuals.

[4] https://egazette.nic.in/WriteReadData/2019/209695.pdf

[5] RBI Press Release no. 2019-2020/419 dated August 13, 2019

[6] Master Direction – Non-Banking Financial Company – Housing Finance Company (Reserve Bank) Directions, 2021

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In order to qualify as an HFC, an NBFC must be involved in '**financing**' of housing loans. For this purpose, housing finance has been defined as follows:

*4.1.16. "**Housing Finance**" shall mean financing, for purchase/ construction/ reconstruction/ renovation/ repairs of residential dwelling units, which includes:*

a. *Loans to individuals or group of individuals including co-operative societies for construction/ purchase of new dwelling units.*
b. *Loans to individuals or group of individuals for purchase of old dwelling units.*
c. *Loans to individuals or group of individuals for purchasing old/ new dwelling units by mortgaging existing dwelling units.*
d. *Loans to individuals for purchase of plots for construction of residential dwelling units provided a declaration is obtained from the borrower that he intends to construct a house on the plot within a period of three years from the date of availing of the loan.*
e. *Loans to individuals or group of individuals for renovation/ reconstruction of existing dwelling units.*
f. *Lending to public agencies including state housing boards for construction of residential dwelling units.*
g. *Loans to corporates/ Government agencies for employee housing.*
h. *Loans for construction of educational, health, social, cultural or other institutions/ centres, which are part of housing projects and which are necessary for the development of settlements or townships (see note below).*
i. *Loans for construction meant for improving the conditions in slum areas, for which credit may be extended directly to the slum-dwellers on the guarantee of the Central Government, or indirectly to them through the State Governments*
j. *Loans given for slum improvement schemes to be implemented by Slum Clearance Boards and other public agencies.*
k. *Lending to builders for construction of residential dwelling units.*

All other loans including those given for furnishing dwelling units, loans given against mortgage of property for any purpose other than buying/ construction of a new dwelling unit/s or renovation of the existing dwelling unit/s as mentioned above, will be treated as non-housing loans and will not be falling under the definition of "Housing Finance".

***Note**: Integrated housing project comprising some commercial spaces (e.g. shopping complex, school, etc.) can be treated as residential housing, provided that the commercial area in the residential housing project does not exceed 10 per cent of the total Floor Space Index (FSI) of the project.*

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Timelines for meeting thresholds

HFCs which are not currently meeting the PBC are required to fulfil the eligibility conditions as per the following timelines:

Timeline	Minimum percentage of total assets towards housing finance	Minimum percentage of total assets towards housing finance for individuals
March 31, 2022	50%	40%
March 31, 2023	55%	45%
March 31, 2024	60%	50%

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Annex II - About Indian Securitisation Foundation

Indian Securitisation Foundation (ISF) is a not-for-profit organisation incorporated under section 25 of the Companies Act, 1956, a representative body of the securitisation industry in India. ISF is formed with the objective of developing, promoting and protecting the securitisation, structured finance markets in India in particular, and market for fixed income securities in general.

Securitisation in India is not just a fixed income investing instrument, but essential for the idea of financial inclusion, in form of priority sector lending. Banks meet their priority sector targets partly through portfolio acquisitions and securitisation, thereby putting securitisation at par with the banking book.

Infrastructure sector also depends substantially on securitisation for equity extraction. In essence, the significance of securitisation to India's financial sector cannot be under-estimated.

Over time, credit default swaps are also expected to be prevalent as ways of synthetically replicating credit risk. It is a clear policy choice to have a strong market for fixed income securities in India: structured finance securities are an essential part of that market, to provide variety, choice and alignment to investor needs.

In this background, ISF was conceptualised to provide direction, leadership, advocacy and support to the securitisation and structured finance industry.

Some of the functions of the Foundation include:

- **Advocacy** – making representation to various authorities from time to time on matters as may concern securitisation and similar capital market instruments.
- **Industry forums and networking** - holding periodic conventions and educational courses.
- **Development of industry standards** - framing self-regulatory standards on disclosures, reporting, servicing reporting, DOs and DONTs for securitisation and direct assignment transactions, etc. Development of standards such as standard assignment agreements, assignment procedures, notification procedures, etc. on the lines of ISDA agreements and encouraging members over period to start using such standard templates.
- **Information exchange** – on matters of common interest, collateral performance, etc.

Advisory Committee

Mr. M.R. Umarji	Mr. Madhukar R Umarji, Former Chief Advisor - Legal of the Indian Banks' Association is acknowledged as an authority on Secured Transactions Law in India. He began his career as a Legal Assistant for the state government simultaneously pursuing his Masters in law. Following his Masters, he shifted to being a Legal Advisor in commercial banks and completed his transition to a commercial banker by becoming Executive Director of a public sector bank. Later he was taken on deputation at Reserve Bank of India as Executive Director in charge of Department of Non-Banking Supervision. He has been a part of several Expert Committees set up by the Government and Working Groups concerned with Banking Sector Reforms in India. His pivotal role in the drafting of secured transactions legislation in India shaped the way for a path-breaking reform for the Indian banking industry.
Mr. D.K. Vyas	Mr. D K Vyas, MD and CEO, Srei Equipment Finance Limited, demonstrates a judicious balance between growth and prudence in lending. He is a B.Com graduate from the Ajmer University. Being a strategist, Mr. Vyas is known for his innovative ideas which have reshaped India's infrastructure equipment financing industry.
Mr. Sanjay Chamria	Mr. Chamria founded Magma (Now part of Poonawalla group) in 1988, along with Mr. Mayank Poddar. As the Executive Vice Chairman, he anchors policy formation, strategy planning and execution. He was born and educated in Kolkata, and graduated as one of the country's youngest chartered accountants in 1985 with national ranking. For the past 23 years, he has steered the organization from a three-employee, one-office set up to a company with 225+ branch offices and more than 6000 employees Mr. Chamria uses his position as one of the foremost leaders in India's asset financing industry to articulate his views on critical issues facing the industry and its future. He has represented the BFSI and NBFC industry at various forums, including RBI, and before the finance ministry and other government bodies. He has also chaired committees at the FICCI, the Hire Purchase & Lease Association of India, the CII, the Finance Industry Development Council (FIDC) and the Indian Merchants Chamber in Mumbai.
Mr. V. S. Rangan	Mr. V. Srinivasa Rangan is Executive Director at Housing Development Finance Corporation Limited (HDFC Ltd). He has been associated with the company since

1986. Mr. Rangan is a Graduate in Commerce, CWA and an Associate member of the Institute of Chartered Accountants of India with national ranking.

Mr. Rangan has worked on international consulting assignments in housing finance in countries such as Ghana and the Maldives. He has also been a member of various committees constituted by the regulators in the areas of development of Mortgage Backed Securitisation and Secondary Mortgage Markets which includes RBI's Committee on Asset Securitisation and Mortgage Backed Securitisation and Technical Group formed by National Housing Bank for setting up of a Secondary Mortgage market institution in India.

Mr. Rangan was also conferred the "Best CFO in the Financial Sector for 2010" by "The Institute of Chartered Accountants of India" (ICAI) for exceptional performance and achievements as CFO in the Financial Sector for the year 2010.

Mr. T.T Srinivasraghavan	Mr. T. T. Srinivasaraghavan is the Managing Director at Sundaram Finance Ltd. He served as Joint Managing Director of Sundaram Finance Ltd. Mr. Srinivasaraghavan also serves as Chairman of Infreight Logistics Solutions Ltd. He serves as an Executive Director of Sundaram Finance Ltd, and Director of Sundaram BNP Paribas Home Finance Limited and Sundaram BNP Paribas Asset Management Co. Ltd. Mr. Srinivasaraghavan has a vast experience in the Banking and Finance sectors. He serves as President of International Finance & Leasing Association, United Kingdom. Mr. Srinivasaraghavan holds an M.B.A. in Finance Degree.

Directors

Mr. Vinod Kothari	Mr. Vinod Kothari is a noted scholar on securitisation and has lectured all over the World on securitisation. Vinod Kothari has been consulted by regulators in various countries, and has structured transactions in several markets. Vinod Kothari is the author of several books on the subject including Securitisation: Financial Instruments of Future, and Introduction to Securitization, (co-author with Frank Fabozzi), Credit Derivatives and Structured Credit Trading, etc. For detailed profile of Mr. Vinod Kothari, see: http://vinodkothari.com/profile/

Ms. Vinita Nair Dedhia	Ms. Vinita Nair Dedhia holds a degree in Bachelor of Management Studies (BMS) from Sydenham College of Commerce and Economics, Mumbai University, Maharashtra, MS(Finance) from ICFAI university and is a Fellow Member of the Institute of Company Secretaries of India (ICSI). She is a Senior Partner in M/s Vinod Kothari & Company, Practising Company Secretaries. In 2020, she was one of the awardee of 'Best Secretarial Audit Report' Award at the ICSI National Awards for Corporate Governance, 2019 for the secretarial audit carried out for HDFC Ltd. She has co-authored several books including Law & Practice relating to Corporate Bonds and Debentures published by Taxmann Publications, Companies Act viz. Your queries on Companies Act, 2013 and The Companies (Amendment) Bill, 2017.

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