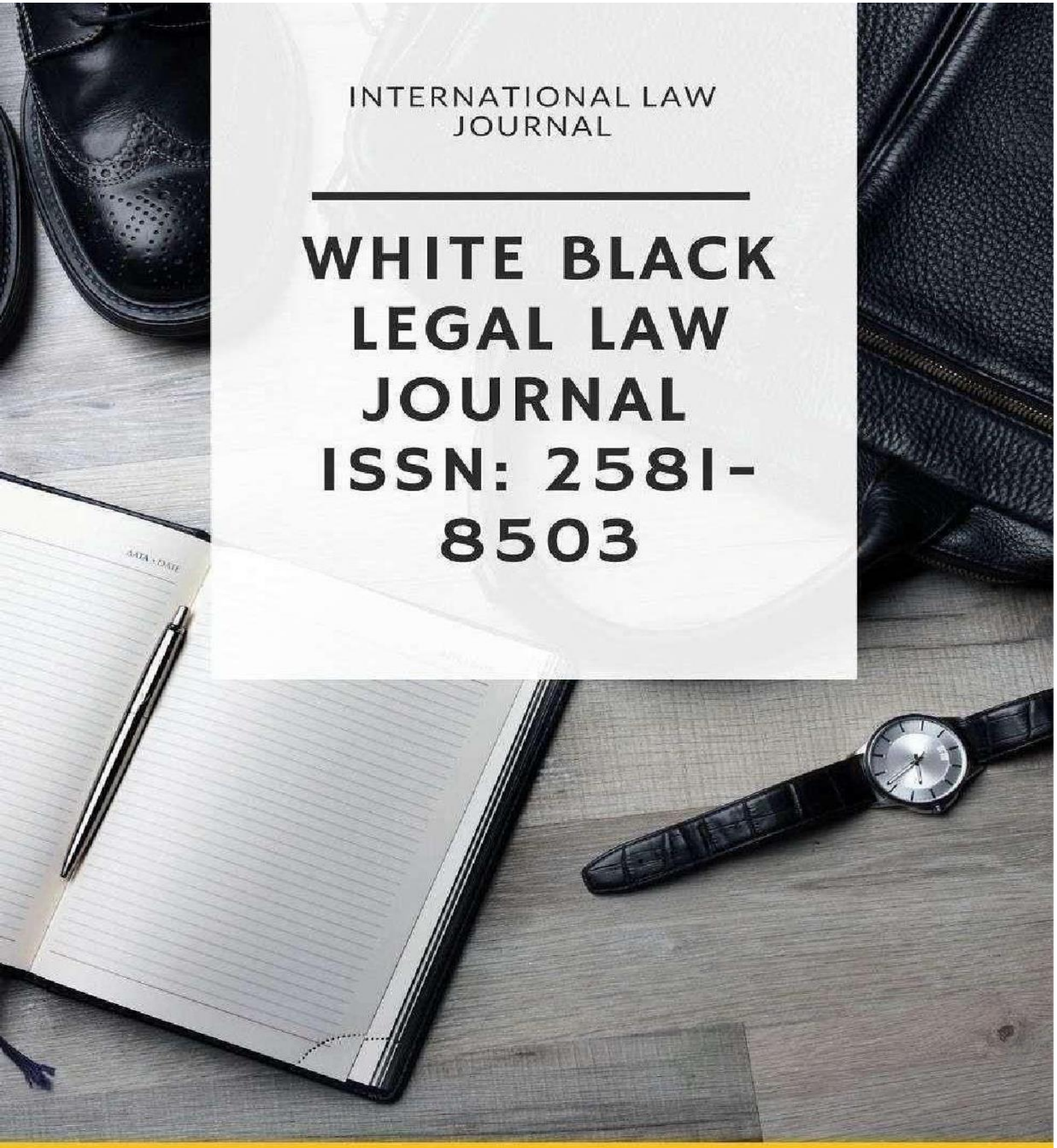


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NBFC CRISIS IN INDIA: CAUSES, REGULATORY FAILURES, AND THE WAY FORWARD

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Abstract

Non-Banking Financial Companies (NBFCs) occupy an important position in India's financial system by extending credit to households, small businesses, infrastructure projects and segments that may not be fully served by conventional banks. Their contribution is accompanied by vulnerabilities arising from maturity transformation, reliance on wholesale funding, concentration of exposures, governance weaknesses and interconnectedness with banks and capital markets. The defaults and distress associated with major entities, particularly Infrastructure Leasing & Financial Services Limited (IL&FS), Dewan Housing Finance Corporation Limited (DHFL) and Reliance Capital Limited, exposed the potential for entity-level weaknesses to transmit stress across the financial system.

This paper examines the legal and regulatory framework governing NBFCs in India, analyses the causes of NBFC distress, and evaluates the regulatory response. It adopts doctrinal and analytical methods, relying on legislation, RBI directions, government materials, judicial decisions and selected case studies. It argues that NBFC crises cannot be explained exclusively as liquidity events: liquidity stress may reveal deeper problems in asset quality, funding strategy, governance, transparency and supervisory effectiveness. The paper considers the Reserve Bank of India Act, 1934, the scale-based regulatory framework, fraud risk management directions and the special insolvency framework for financial service providers under section 227 of the Insolvency and Bankruptcy Code, 2016. It concludes that India has strengthened its framework, but effectiveness depends on timely supervision, credible disclosures, board accountability, robust liquidity planning and coordinated resolution arrangements.

Keywords: NBFCs; RBI; financial stability; liquidity risk; corporate governance; IL&FS; DHFL; insolvency; scale-based regulation.

Introduction

India's financial system comprises banks, non-banking financial companies, insurance institutions, capital-market intermediaries and other regulated entities. NBFCs form an important part of this structure. They provide loans and advances, asset finance, investment services, microfinance and specialised credit. Their business models can reach borrowers, sectors and geographies that are not always served efficiently by banks. This function supports credit availability and financial inclusion, but it also means that distress in a large or interconnected NBFC may affect borrowers, lenders, investors and market confidence.[1]

An NBFC is not simply a bank operating under another name. The statutory definition is contained in section 45-I(f) of the Reserve Bank of India Act, 1934, while section 45-IA establishes the registration requirement for specified NBFC business.[2] NBFCs generally cannot accept demand deposits and their deposits are not covered by the Deposit Insurance and Credit Guarantee Corporation in the same manner as eligible bank deposits.[3] Their funding structure therefore differs from that of banks and may depend more heavily on bank loans, debentures, commercial paper, securitisation and other market sources.

The expression 'NBFC crisis' does not describe one uniform event. It refers to episodes of liquidity stress, defaults, governance failures and insolvency involving particular entities, together with wider market consequences. [4]The 2018 IL&FS defaults were a significant shock to confidence in the NBFC and housing-finance sectors. The resulting reassessment of credit risk and funding availability demonstrated how quickly wholesale funding conditions can tighten. Subsequent distress involving DHFL and Reliance Capital further raised questions about supervision, governance and resolution.[5]

A central distinction is between liquidity and solvency. A solvent entity may be unable to pay obligations when due because its assets are illiquid or its funding is unavailable. An insolvent entity, by contrast, may have liabilities exceeding the value of its assets or may be unable to meet obligations on a sustained basis. The two conditions can interact: a liquidity shock may force asset sales, weaken asset values and turn temporary stress into deeper financial distress.

[1] Reserve Bank of India, 'Non-Banking Financial Companies and Financial Stability' (2021) *RBI Bulletin*.
[2] *Reserve Bank of India Act 1934*, ss 45-I(f), 45-IA
[3] Reserve Bank of India, 'Frequently Asked Questions: Non-Banking Financial Companies' accessed 18 October 2026.
[4] Reserve Bank of India, Report on Trend and Progress of Banking in India 2018–19 (RBI, 2019)
[5] Ministry of Finance, Government of India, 'Firm and Decisive Government Action Taken to Preserve Value and Assets of IL&FS' (Press Information Bureau, 1 October 2018)

Literature Review

The literature on NBFC regulation broadly examines the role of non-bank financial intermediation, systemic risk, prudential supervision and the relationship between market-based funding and financial stability. Regulatory materials emphasise that NBFCs serve specialised credit needs but may be exposed to risks associated with leverage, liquidity transformation and interconnectedness. The Financial Stability Reports of the Reserve Bank of India provide a macroprudential perspective on risks in the financial system, while RBI's scale-based framework reflects a move towards proportionate regulation according to size, activity and systemic significance.

A second strand of literature concerns corporate governance and the role of boards, auditors and credit rating agencies. The IL&FS episode brought attention to group complexity, disclosure quality and the possibility that entity-level information may not adequately reveal risks arising from subsidiaries, guarantees and intra-group relationships. Research on financial distress also highlights that governance weaknesses can delay the recognition of deteriorating asset quality or liquidity pressures.

A third strand concerns insolvency and resolution of financial service providers. Ordinary corporate insolvency mechanisms may not fully address the public-interest dimensions of a financial institution, including customer assets, continuity of financial services and systemic confidence. The Insolvency and Bankruptcy Code, 2016, read with the 2019 Financial Service Provider Rules, creates a special route for notified financial service providers. The DHFL and Reliance Capital proceedings provide practical contexts for examining this framework.

The research gap addressed here is the need to connect these strands. Rather than treating liquidity, governance, regulation and insolvency as separate topics, this paper examines how they interact in selected NBFC crises and whether subsequent legal reforms respond to the vulnerabilities revealed.

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Research Questions

1. What structural and financial factors contribute to recurring NBFC distress in India?
2. How do asset-liability mismatches and dependence on wholesale funding amplify liquidity risk?
3. To what extent has the RBI's regulatory framework been effective in identifying and mitigating NBFC vulnerabilities?
4. What do the IL&FS, DHFL and Reliance Capital cases reveal about corporate

governance, supervision and resolution?

5. Are the existing insolvency and resolution mechanisms adequate for financial service providers?
6. What legal, regulatory and institutional reforms may strengthen financial stability while preserving proportionate regulation?

Research Methodology

This research adopts a doctrinal and analytical methodology. It examines primary legal materials, including the Reserve Bank of India Act, 1934, the Companies Act, 2013, the Insolvency and Bankruptcy Code, 2016, the Financial Service Provider Rules, 2019, and relevant RBI directions. It also considers judicial decisions, official reports and publicly available materials concerning selected NBFC cases.[6]

The study is qualitative and case-study based. IL&FS, DHFL and Reliance Capital are selected because they illustrate different dimensions of financial distress, regulatory intervention and resolution.[7] The paper does not conduct an original survey or quantitative econometric analysis. Accordingly, it does not claim that the selected cases represent every NBFC or establish a single cause for all episodes of distress.[8] Public allegations are distinguished from findings formally established by courts or competent authorities.

The scope is limited to India, with particular attention to developments from 2018 onwards. The research evaluates both the legal design of the regulatory framework and practical implementation challenges. All legal provisions and regulatory directions should be checked against their latest amended or consolidated versions before submission.

Research Hypothesis

The paper proceeds on the hypothesis that recurring NBFC distress is associated not only with market liquidity conditions but also with weaknesses in governance, risk management, funding structures and supervisory implementation. A proportionate, risk-sensitive framework can reduce these vulnerabilities only when supported by reliable data, timely intervention and effective accountability.

[6] Reserve Bank of India Act 1934, particularly ch IIIB; Companies Act 2013; Insolvency and Bankruptcy Code 2016; Insolvency and Bankruptcy (Insolvency and Liquidation Proceedings of Financial Service Providers and Application to Adjudicating Authority) Rules 2019.

[7] Reserve Bank of India, Master Direction – Non-Banking Financial Company – Scale Based Regulation Directions, 2023 (as amended).

[8] Ministry of Corporate Affairs, Report on the Financial and Operational Performance of Infrastructure Leasing & Financial Services Limited (where relevant, consult official IL&FS disclosures and proceedings).

The NBFC Crisis in India: Causes, Regulatory Failures, and the Way Forward

1. Conceptual and Legal Framework of NBFCs in India

1.1 Nature and Functions of NBFCs

NBFCs undertake financial activities such as lending, asset financing, investment, factoring and microfinance, subject to their registration and regulatory category.[9] Their contribution lies partly in specialisation: an asset-finance company may understand a particular borrower segment, while a microfinance institution may use group-based lending models.[10] This diversity makes a single uniform regulatory intensity inappropriate. [11]At the same time, differences in business model do not eliminate common risks such as leverage, liquidity mismatch, credit concentration and governance failure.[12]

1.2 Banks and NBFCs: Regulatory Distinction

Banks are governed principally by the Banking Regulation Act, 1949 and the RBI Act, alongside prudential and supervisory directions. [13]NBFCs are regulated primarily under Chapter IIIB of the RBI Act and applicable RBI directions.[14] NBFCs generally cannot accept demand deposits and are not part of the deposit-taking and payment architecture in the same way as banks.[15] Their funding may instead depend on bank finance, debentures, commercial paper, securitisation, public deposits where legally permitted, and other market sources. [16]The difference in funding structure affects the speed and form in which liquidity stress can arise.

1.3 Statutory Framework

The RBI Act is the central statute. Section 45-I contains definitions relevant to NBFC

[9] Reserve Bank of India, Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 (19 October 2023, as amended); Reserve Bank of India Act 1934, s 45-I(f); Factoring Regulation Act 2011, ss 2–4.
[10] Reserve Bank of India, Master Direction – Reserve Bank of India (Regulatory Framework for Microfinance Loans) Directions, 2022 (14 March 2022, as amended); Reserve Bank of India, 'Harmonisation of Different Categories of NBFCs', RBI/2018-19/130, DNBR (PD) CC No 097/03.10.001/2018-19 (22 February 2019).
[11] Reserve Bank of India, 'Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs', RBI/2021-22/112, DOR.CRE.REC.No.60/03.10.001/2021-22 (22 October 2021).
[12] Reserve Bank of India, Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 (19 October 2023, as amended), provisions concerning capital adequacy, liquidity risk management, credit concentration and corporate governance.
[13] Banking Regulation Act, No. 10 of 1949, §§ 5–6 (India); Reserve Bank of India Act, No. 2 of 1934 (India).
[14] Reserve Bank of India Act, No. 2 of 1934, ch. IIIB, §§ 45-IA, 45-IB, 45-IC, 45JA–45L (India); Reserve Bank of India, Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023, as amended (India).
[15] Reserve Bank of India, Frequently Asked Questions on Non-Banking Financial Companies.
[16] Reserve Bank of India, Master Circular – Bank Finance to Non-Banking Financial Companies (NBFCs) (Apr. 1, 2025); Reserve Bank of India, Master Direction – Non-Banking Financial Companies Acceptance of Public Deposits (Reserve Bank) Directions, 2016, RBI/DNBR/2016-17/38 (Aug. 25, 2016), as updated Feb. 27, 2025.

regulation; section 45-IA addresses registration and net-owned-fund requirements; and sections 45JA, 45K, 45L and 45M provide important powers relating to policy, directions, information and regulation. [17]The precise scope of each power must be read with the text of the Act and the relevant direction. RBI's regulatory framework is therefore a combination of statutory authority and subordinate directions.

The Companies Act, 2013 is also relevant. Sections 128 and 129 concern books of account and financial statements; section 134 addresses board responsibility and the board's report; section 177 concerns audit committees; and section 188 regulates specified related-party transactions. These provisions matter because sound prudential regulation cannot substitute for accurate accounts, effective boards and independent oversight.

The Insolvency and Bankruptcy Code, 2016 provides a general insolvency framework for corporate persons, but financial service providers require special treatment because they hold or manage assets and funds connected with customers and the financial system. Section 227 empowers the Central Government, in consultation with the appropriate regulator, to notify financial service providers or categories for a special process. The 2019 FSP Rules provide the procedural framework for notified entities.

1.4 RBI's Scale-Based Regulatory Framework

RBI's scale-based regulatory framework classifies NBFCs into Base, Middle, Upper and Top Layers, taking account of size, activity and perceived risk. The framework seeks to apply regulation proportionately: entities with greater systemic significance or complexity are subject to more intensive requirements.[18] The Top Layer is intended for entities that may pose extreme systemic risk and is expected to remain empty ordinarily. The Master Direction issued in 2023 consolidates the framework and has since been updated.[19]

The framework is a move away from a purely activity- or registration-based approach. It recognises that systemic importance may arise from size, interconnectedness, substitutability and complexity. However, classification is only a starting point. Effective regulation also requires accurate data, supervisory capacity, credible enforcement and the ability to respond before distress becomes irreversible.

[17] Reserve Bank of India, Financial Stability Report (December 2018).
[18] Reserve Bank of India, 'Scale Based Regulation (SBR): A Revised Regulatory Framework for NBFCs' (22 October 2021) RBI/2021-22/112, DOR.CRE.REC.No.60/03.10.001/2021-22.
[19] Reserve Bank of India, Master Direction – Reserve Bank of India (Non-Banking Financial Company – Scale Based Regulation) Directions, 2023 (19 October 2023) RBI/DoR/2023-24/106, DoR.FIN.REC.No.45/03.10.119/2023-24 (as updated on 10 October 2024)

2. Causes of the NBFC Crisis in India

2.1 Asset-Liability Mismatch

Asset-liability mismatch arises when the timing or repricing characteristics of an institution's assets and liabilities differ. An NBFC may fund long-term loans with short-term borrowings. Even where loans are expected to perform, the company must refinance maturing liabilities before the underlying assets generate cash. If lenders refuse to roll over funding, the NBFC can face a cash shortfall. The risk becomes more acute when many liabilities mature within a short period or when assets cannot be sold without substantial discounts.

For example, an NBFC may borrow for six months and lend for five years. It depends on repeated refinancing. A market-wide loss of confidence can interrupt that refinancing and create liquidity pressure. This example does not itself prove insolvency; it demonstrates why cash-flow maturity analysis and contingency funding plans are essential.

2.2 Wholesale Funding Dependence

Many NBFCs rely on bank finance, debentures and short-term money-market instruments. Such funding can be efficient during stable conditions, but it is sensitive to market sentiment, ratings and collateral values. When investors reassess an issuer's creditworthiness, the cost of funding may rise or access may disappear. This creates a procyclical dynamic: the institution most in need of refinancing may find it least available.

2.3 Credit Risk and Asset Quality

Credit risk arises when borrowers fail to repay. Weak underwriting, inadequate due diligence, poor monitoring, concentrated exposure and optimistic assumptions about collateral can increase the probability and severity of loss. Deteriorating asset quality reduces cash inflows and may require additional provisioning, weakening capital. A funding shock and a credit shock can therefore reinforce one another.

2.4 Corporate Governance and Internal Controls

Governance failures may include ineffective board challenge, inadequate independent oversight, conflicts of interest, weak audit functions and insufficient scrutiny of related-party transactions. A board cannot manage every loan, but it must ensure that management has reliable systems for risk identification and escalation. Where risk information is incomplete or not acted upon, formal compliance structures may exist without providing meaningful control.

2.5 Concentration, Contagion and External Conditions

A firm may be exposed to a narrow set of borrowers, sectors, geographies or funding counterparties. Concentration makes the institution vulnerable to correlated shocks. NBFCs are also linked to banks, mutual funds, insurers, investors, borrowers and other intermediaries. A default can cause direct losses and indirect effects, including higher funding spreads and reduced credit availability. Macroeconomic slowdown and rising borrowing costs can expose weaknesses that were less visible during expansion. These conditions are triggers or amplifiers, not complete explanations.

3. Major NBFC Crises: Case Study Analysis

3.1 IL&FS Crisis

Infrastructure Leasing & Financial Services Limited (IL&FS) was a large infrastructure and financial-services group with complex corporate structures and extensive links to infrastructure financing. Defaults by group entities in 2018 triggered a sharp reassessment of risk and confidence. The episode highlighted the interaction between leverage, project cash flows, group complexity and market funding. It also demonstrated that stress in a large group can affect funding conditions beyond the legal entity that first defaults.

The government moved to replace the board, and the episode prompted scrutiny of governance, disclosures, credit ratings and supervisory coordination. The legal significance of IL&FS lies not in treating every public allegation as a proven finding, but in examining what the crisis revealed about group-wide risk visibility and the capacity to identify stress early. A regulator's entity-level view may be insufficient where risks are transmitted through subsidiaries, guarantees, common funding channels or reputational links.

The principal lesson is that consolidated supervision and credible group-level information are important. Boards and auditors must understand not only the financial position of an individual company but also material exposures within the group. Supervisors need timely information on inter-company transactions, contingent liabilities and maturity concentrations.

3.2 DHFL Crisis

Dewan Housing Finance Corporation Limited (DHFL), a housing finance company, experienced severe financial distress and entered a special insolvency process. The case is significant because it tested the application of the FSP framework and raised questions about protection of creditors and customers while preserving continuity of financial services. RBI

superseded the board and initiated the process that led to appointment of an administrator and proceedings before the adjudicating authority.

Public investigations and proceedings raised allegations of financial irregularities. Such allegations must be distinguished from final judicial findings. The case is relevant to the relationship between supervisory intervention, investigation, creditor treatment and resolution. It also illustrates why a financial service provider cannot always be treated exactly like an ordinary company: its assets may include loans and securities, and abrupt disruption may have wider effects.

3.3 Reliance Capital Crisis

Reliance Capital's insolvency proceedings provide another illustration of the use of the special FSP framework. RBI initiated proceedings and an administrator was appointed. The case provides a basis for examining how an adjudicating authority, administrator, creditors and regulator interact in the resolution of a financial service provider. It also raises questions about valuation, continuity, regulatory approval of a proposed resolution applicant and the time required to achieve a final outcome.

The case should not be reduced to a simple success-or-failure label. A careful assessment should consider the time taken, creditor recoveries, regulatory safeguards, continuity of services and treatment of customers where relevant. These are distinct measures and may not move in the same direction.

3.4 Comparative Analysis

The three cases differ in business structure and legal trajectory. IL&FS primarily demonstrates the systemic implications of a complex group and funding stress; DHFL illustrates supervisory intervention and the special insolvency regime; and Reliance Capital provides further experience with resolution of a financial service provider. Their common analytical themes include reliable information, timely intervention, governance, funding resilience and a resolution mechanism that accounts for the special character of financial businesses.

4. Regulatory Failures and Institutional Challenges

4.1 Supervision and Early Detection

A regulatory framework may contain extensive powers yet fail to prevent distress if information arrives late, is incomplete or is not analysed effectively. Supervisory challenges

include complex group structures, rapid changes in funding conditions, differences in business models and limited visibility into off-balance-sheet or connected exposures. The relevant question is not simply whether RBI had legal authority, but whether supervisory tools, data and intervention thresholds were adequate in the circumstances.

4.2 Credit Rating Agencies

Credit ratings influence funding costs and investor decisions, but they are opinions about credit risk, not guarantees of repayment. Ratings can lag changing conditions, particularly where information is opaque or deterioration is rapid. Conflicts of interest and overreliance on ratings may weaken market discipline. Reforms should support transparent methodologies, timely review, robust surveillance and clear communication of rating assumptions. Investors and lenders should still conduct independent due diligence.

4.3 Governance, Audit and Disclosure

Companies Act duties, audit committees and statutory audits are essential components of accountability. Yet formal compliance does not ensure substantive oversight. Boards require access to accurate, timely and sufficiently granular information. Auditors must exercise professional scepticism and communicate material concerns through legally prescribed channels. Disclosure should enable creditors and investors to understand liquidity, concentration, related-party exposure and material contingent liabilities.

4.4 Liquidity Regulation and Institutional Coordination

Liquidity risk cannot be controlled by capital requirements alone. Capital absorbs losses; liquidity management ensures that cash is available when obligations fall due. A sound framework requires maturity profiling, stress testing, diversified funding, unencumbered liquid assets and board-approved contingency plans. Coordination among RBI, the Ministry of Corporate Affairs, insolvency institutions, securities regulators, auditors and rating agencies is especially important where an NBFC belongs to a complex group or enters insolvency.

4.5 Post-Crisis Regulatory Developments

RBI's scale-based framework is an important development because it calibrates requirements according to risk and systemic significance. RBI also issued dedicated Fraud Risk Management Directions for applicable NBFCs in July 2024. These measures strengthen the formal architecture, but their practical impact depends on implementation, internal escalation and

supervisory follow-through. It would be inaccurate to treat every earlier crisis as proof that the present framework is ineffective: the regulatory framework has changed. The appropriate question is whether reforms address the mechanisms that contributed to past distress.

5. Insolvency and Resolution of NBFCs in India

5.1 Need for a Special Framework

The ordinary corporate insolvency process is designed around resolution or liquidation of a corporate debtor. A financial service provider, however, may hold funds or assets for customers, maintain lending relationships and perform functions whose abrupt termination can affect financial stability. A special framework must reconcile creditor interests with customer protection, regulatory oversight and continuity of critical services.

5.2 Section 227 of the IBC and the 2019 Rules

Section 227 of the IBC empowers the Central Government, in consultation with the appropriate regulator, to notify financial service providers or categories for insolvency and liquidation proceedings under a special framework. The Insolvency and Bankruptcy (Insolvency and Liquidation Proceedings of Financial Service Providers and Application to Adjudicating Authority) Rules, 2019 provide the procedural framework for notified financial service providers. The Rules provide for regulatory involvement, appointment of an administrator and an application to the adjudicating authority.

The Rules recognise that third-party assets held by an FSP should not simply be treated as its own assets. They also provide for regulatory involvement in the resolution process and the suitability of persons who may control or manage the FSP after approval of a resolution plan. These features reflect the special public-interest character of financial businesses.

5.3 Evaluation and Challenges

The special framework is a necessary legal adaptation, but several issues remain. Resolution must be fast enough to preserve value while allowing proper scrutiny. Creditor recoveries must be balanced against customer and systemic interests. Valuation of loan books and other financial assets is sensitive to assumptions about defaults, recoveries and market conditions. Coordination between the administrator, regulator and adjudicating authority must be predictable.

6. The Way Forward: Legal, Regulatory and Institutional Reforms

6.1 Risk-Based and Consolidated Supervision

RBI should continue to strengthen risk-based supervision, with intensity proportionate to systemic importance, complexity and interconnectedness. For large groups, supervision should include a consolidated view of material subsidiaries, intra-group exposures, guarantees and common funding dependencies. Early-warning indicators should combine quantitative measures—such as maturity gaps, leverage, asset quality and concentration—with qualitative information about governance and management.

6.2 Stronger Liquidity Management

NBFCs should maintain board-approved liquidity risk frameworks that identify cash-flow gaps across time horizons and test severe but plausible scenarios. Stress tests should include non-renewal of wholesale funding, rating downgrades, collateral haircuts and correlated borrower defaults. Firms should diversify funding sources and maintain credible contingency funding plans. The regulator should assess not merely the existence of a policy but the quality of assumptions, governance and actual execution.

6.3 Board Accountability, Transparency and Market Discipline

Boards should receive regular reports on liquidity, concentration, related-party exposures, fraud indicators and stress-test results. Audit and risk committees must have sufficient expertise and independence to challenge management. Disclosure should make material risks intelligible to lenders, investors and customers, including information on asset quality, funding concentration, maturity profiles and significant related-party exposures. Credit rating agencies should explain material rating changes and the limitations of their assessments.

6.4 Effective Fraud Prevention and Resolution Planning

Fraud risk frameworks require clear responsibility, protected escalation channels, timely investigation, accurate reporting and cooperation with law-enforcement agencies. Internal systems should distinguish suspected irregularity from established fraud and ensure that classification decisions follow applicable legal standards and procedural safeguards. For systemically important NBFCs, proportionate recovery and resolution planning could identify critical functions, data needs, operational dependencies and treatment of customer assets before distress occurs.

6.5 Consumer Protection, Proportionate Regulation and Technology

Financial stability should not be pursued at the cost of fair treatment of borrowers and depositors. Clear disclosure, fair recovery practices, accessible grievance redressal and appropriate handling of customer data are essential. Requirements should be calibrated so that smaller, lower-risk NBFCs are not burdened with rules designed for systemically important institutions. Technology can improve supervisory timeliness through standardised reporting, data validation and analytics, but must be supported by data governance, cybersecurity and human supervisory judgment.

7. Findings and Conclusion

7.1 Findings

The analysis indicates that NBFC distress is multi-causal. Maturity mismatch and wholesale funding dependence can create immediate liquidity pressure; weak underwriting and concentration can reduce asset quality; and governance failures can delay recognition or response. The IL&FS, DHFL and Reliance Capital experiences demonstrate different aspects of these risks and the importance of group-level information, timely intervention and specialised resolution.

The legal framework has evolved through scale-based regulation, enhanced prudential requirements, fraud risk management directions and the special FSP insolvency regime. These reforms provide a stronger architecture, but the existence of rules is not equivalent to effective supervision. Their success depends on reliable data, capable boards, internal controls, enforcement and coordination among institutions.

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7.2 Conclusion

NBFCs are essential to India's diverse credit ecosystem, but their contribution depends on public and market confidence. The crises examined in this paper show that financial distress cannot be understood as a temporary shortage of liquidity alone. Funding structure, asset quality, corporate governance, transparency and systemic interconnectedness are closely related. A regulatory response must therefore be comprehensive and preventive as well as remedial.

India's scale-based framework is a significant step towards proportionate regulation, while the 2019 FSP Rules recognise the special nature of financial service provider insolvency. The 2024 fraud risk management directions further strengthen prevention and reporting expectations for

applicable NBFCs. The continuing challenge is implementation: regulators must identify vulnerabilities early; boards must act on risk information; auditors and rating agencies must provide credible scrutiny; and resolution arrangements must preserve value while protecting customers and financial stability.

The way forward is not indiscriminate regulation or the assumption that all NBFCs pose equal risk. It is a risk-sensitive framework combining consolidated supervision, robust liquidity management, board accountability, transparent disclosure, consumer protection and credible resolution planning. Such an approach can support both financial stability and the continued role of NBFCs in widening access to credit.

Footnotes

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2. Reserve Bank of India Act, 1934, §§ 45-I, 45-IA, 45-JA, 45-K, 45-L, 45-M.
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D. Official Websites

- Reserve Bank of India, https://www.rbi.org.in/.
- Insolvency and Bankruptcy Board of India, https://ibbi.gov.in/.
- Ministry of Corporate Affairs, https://www.mca.gov.in/.
- Supreme Court of India, https://www.sci.gov.in/.

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