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ENGAGING WITH DIGITAL LENDING PLATFORMS – STRICTER COMPLIANCES FOR BANKS AND NBFCS

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On 24 June 2020, the Reserve Bank of India (RBI) issued directions on "*Loans Sourced by Banks and NBFCs over Digital Lending Platforms: Adherence to Fair Practices Code and Outsourcing Guidelines*" (Directions) to scheduled commercial banks (Banks) and non-banking financial companies (NBFCs) in relation to their engagement with digital lending platforms for disbursement of loans to borrowers.

The Directions have been issued primarily to reiterate requirements relating to compliance with the existing regulatory framework for outsourcing of services and the fair practices code by Banks and NBFCs (both traditional NBFCs utilising brick and mortar channels for credit delivery, and NBFCs registered to operate as 'digital-only' lending entities). According to the RBI, the need for these Directions has arisen on account of an increase in complaints received by the RBI against the lending platforms. Such complaints primarily relate to exorbitant interest rates, non-transparent methods of calculating interest, harsh recovery measures, unauthorised use of personal data, and bad behaviour. The RBI has also observed that lending platforms often tend to portray themselves as lenders without disclosing the name of the Bank or the NBFC in question to the customer, as a consequence of which, customers are unable to access grievance redressal avenues available under the regulatory framework.

To ensure transparency for customers, RBI has stressed on the primary responsibility of Banks and NBFCs in outsourcing of financial and information technology related services and has sought meticulous compliance by Banks and NBFCs with the instructions in existing regulatory framework.

Some of the key aspects highlighted by the RBI for compliance are: (a) disclosing the names of the digital lending platforms engaged as agents on the website of Banks/NBFCs; (b) directing the digital lending platforms to disclose the name of the Bank/NBFC to the customer on an upfront basis; (c) issuance of the sanction letter to the borrower on the letterhead of the Banks/NBFCs immediately after sanction but before execution of the loan agreement; (d) furnishing a copy of the loan agreement and all annexures to such agreement at the time of sanction or disbursement of loans; (e) ensuring effective oversight and monitoring of the digital lending platforms engaged by the Banks/NBFCs; and (f) making adequate efforts towards creation of awareness about the grievance redressal mechanism.

While the RBI has not prescribed specific penal consequences for breach of the aforesaid requirements, it has stated that any violation by Banks and NBFCs will be viewed seriously.

Comments

Increase in proliferation of mobile internet and smartphones has boosted the growth of fintech lending businesses in India. A completely digital financial services experience is being offered by fintech players, enabling the new age customer to avail loans in a matter of minutes. After the RBI imposed severe restrictions on the operation of peer-to-peer (P2P) lending platforms in 2017 (and brought such platforms within its regulatory ambit by requiring them to register as NBFC-P2Ps), various online lending platforms restricted participation of unregulated retail lenders. The RBI had also clarified that electronic platforms which only assisted Banks, NBFCs and other regulated financial institutions to identify borrowers would not be treated as NBFC-P2Ps. Consequently, fintech lending platforms limited their lender base only to regulated entities, and acted as business correspondents or selling agents of Banks and NBFCs. Consequently, such lending platforms provided various facilitation services to Banks and NBFCs, including services in relation to customer on-boarding and know-your-customer (KYC) verification, credit risk analysis, loan disbursement, and loan recovery for Banks and NBFCs.

The existing regulatory framework applicable to Banks and NBFCs on outsourcing of services to third parties and compliance with fair practices already contains a robust set of instructions. With these Directions, the RBI is seeking a greater interface between the lenders (Banks and NBFCs) and their customers who are sourced through such lending platforms. It is pertinent to note that the RBI does not intend to bring such digital lending platforms within its regulatory ambit and views them as mere intermediaries providing technology-based solutions. Instead, the RBI has only reiterated that the onus of regulatory compliance lies solely with the Banks and NBFCs, who are directly regulated by the RBI.

In terms of impact of these Directions, Banks and NBFCs operating in the digital lending segment may see increased inspection of their outsourcing arrangements with lending platforms. The RBI may also require changes to existing outsourcing agreements executed by Banks and NBFCs including providing the customers access to grievance redressal system of the Banks and NBFCs. Digital lending platforms may need to review and modify their customer on-boarding and related technological processes to ensure that a specified lender is identified upfront prior to disbursement of loans (while ensuring customer exclusivity in their arrangements with the lenders). Lenders are also likely to insist on technology-based solutions from the digital lending platform to ensure that they comply with the specific loan documentation requirements prescribed under the Directions.

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