Sansad TV Perspective: RBI: Digital Lending Rules

In the series Sansad TV Perspective, we bring you an analysis of the discussion featured on the insightful programme 'Perspective' on Sansad TV, on various important topics affecting India and also the world. This analysis will help you immensely for the IAS exam, especially the mains exam, where a well-rounded understanding of topics is a prerequisite for writing answers that fetch good marks.

In this article, we feature the discussion on the topic: RBI: Digital Lending Rules

Video link: https://youtu.be/rUWt54J7Rgk

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Guests:

- A.K. Bhattacharya, Editorial Director, Business Standard
- Ashok Kumar Jha, Former Secretary, Ministry of Finance, GoI
- Pankaj Mathpal, Founder & CEO, Optima Money Managers

Context:

- Recently, the Reserve Bank of India (RBI) has come up with a framework for regulating the digital lending segment in the Indian economy. It has issued guidelines for digital lending.

Background:

- Recently there has been an uptick in the credit disbursal from NBFCs as compared to the private scheduled banks. This was associated with serious concerns about the functioning of such NBFCs that were increasingly making use of the digital lending segment.

Digital lending:

- Digital lending involves lending through web platforms or mobile apps, utilizing technology for authentication and credit evaluation. Under digital lending, Lending Service Providers (LSPs) act in partnership with Non-Banking Financial Companies (NBFCs) who disburse credit (or a line of credit) to the customer using the former's platform.

Concerns in the digital lending segment:

- A large number of the lending apps available for Indian android users happen to be illegal in that they are either unregulated by the RBI or have NBFC partners with an asset size of less than ₹1,000 crores. There was the absence of a standardised regulatory norm for this segment.

- The Lending Service Providers are found to be resorting to reckless lending practices due to high competitiveness in the segment. They are found to be lending credit beyond a borrower's repayment capacity. This is resulting in higher interest rates for all users.
- There are also serious concerns of mis-selling, unfair business conduct, charging of exorbitant interest rates, and unethical recovery practices by the lending service providers.
- The unbridled engagement of third parties and the sharing of personal information of the borrowers with them amount to a possible breach of data privacy of the borrowers. This is a major concern with respect to this segment.

Significance of digital lending segment:

- Given that digital lending utilizes automated technologies for most of its activities, it has the advantage of lower operating costs and can also help ensure speedy disbursal of loans.
- Small borrowers without a documented credit history and thus, not served by traditional financial institutions have found a credit avenue for their short-term loan requirements through this segment.
- The digital lending segment can play a major role in supplementing the role being played by the existing financial system dominated by banks in meeting the demand for loans across the credit ecosystem given their scalability.

New regulations:

- Lending must be carried out by entities that are either regulated by the RBI or possess permission to operate under relevant law. This will limit the operation of any illegal entities in the segment.
- All loan disbursals and repayments are to be executed directly between the bank accounts of the borrower and the entity and not through any third party. This will help eliminate the participation of third parties.
- Digital lending entities and not the borrowers should pay fees or charges payable to Lending Service Providers in the credit intermediation process.
- Cooling-off period to be provided to the borrower.
- Lenders would compulsorily have to inform the borrower in a standardised format about all fees and charges and LSPs will not be allowed to raise them without prior consent from customers. This would help address concerns of mis-selling, unfair business conduct, and charging of exorbitant interest rates.
- The new regulations mandate a dedicated resolution framework which requires the digital lending entity to appoint a grievance redressal officer. This would come under the purview of the RBI's Integrated Ombudsman Scheme (RB-IOS) and all complaints have to be resolved within 30 days of lodging of the complaint.
- All the data collected by the digital lending apps should be "need-based" and must be with the prior and explicit consent of the borrower. Users are also allowed to revoke previously granted consent.

Significance of the new regulation guidelines:

- Will go a long way in protecting the interests of the borrowers by increasing transparency and accountability in the digital lending segment. This will help incentivize borrowing and help deepen financial inclusion in India.
- Will help increase awareness among the borrowers about the regulation guidelines.

Recommendations going forward:

- Currently, only regulated entities have been brought within the ambit of the new regulations and going forward other entities may also be brought into the regulation ambit to make it more comprehensive.
- There will also be the need for newer agreements between the LSPs and NBFCs to keep in line with the newer guidelines.
- Firm action should be taken against those in breach of the new guidelines to ensure strict adherence. Otherwise, there will be laxity in following these guidelines.