

## Digital lending directives by Reserve Bank of India

### Background

India has witnessed tremendous growth in the digital payments environment recently and moreover in the covid period, where quick and contactless payments flourished. Banks and non-banking financial companies ('NBFC') have outsourced various digital lending applications (DLA or the DL Apps) to third parties to enable their 'loan management' function right from initiation to repayment. As per the working group on digital lending (WGDL) constituted by the Reserve Bank of India (RBI), the overall volume of loan disbursement in India through digital mode (in the years 2017 – to 2020) grew by more than 12 times, and the share of NBFCs in such disbursements increased by almost 5 times!

### Introduction

Concerns were raised about the risks of the digital lending apps (DLAs) outsourced by the NBFCs or Fintech companies like:

- a. Lack of regulated digital lending
- b. Uncontrolled engagement of third parties
- c. Unfair business conduct
- d. Charging of exorbitant interest rates
- e. Unethical recovery practices
- f. Mis-selling and breach of data privacy and security

### Certain data published by the WGDL

- India had the highest FinTech adoption rate of 87 % as of 2020 and the growth is around 24.56% in terms of CAGR.
- Number of illegal DLAs (1 January 2021 – 28 February 2021): 600
- Complaints against the DLAs received by RBI portal 'Sachet': More than 2,500; of the above complaints, most pertain to the DLAs promoted either by non-regulated entities or small NBFCs (asset size of less than INR 1,000 crore).

The pandemic-led growth of digital lending and unbridled extension of financial services to retail individuals is susceptible to many unethical conduct and governance issues. The burgeoning growth of technology companies facilitating financial services has made the regulatory role more challenging. At present, the disruptions due to the unregulated services may be negligible, but they need to be checked on the background of India's huge potential for technology adoption.

On 10 August 2022 the RBI, decided to implement many of WGDL's suggestions with immediate effect. The remaining suggestions will be implemented in due course.

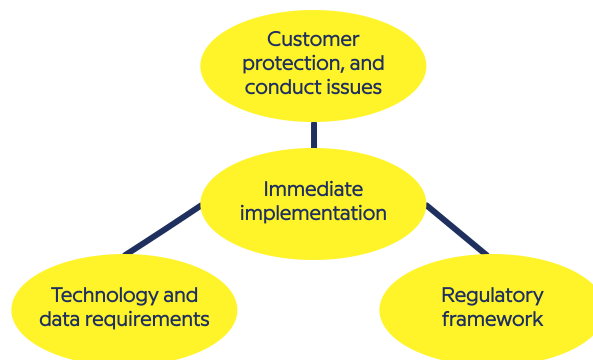
### How will the digital lending system be regulated?

The entire digital lending universe is categorised into three groups and the WGDL has recommended the following way to regulate such entities.

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Category of digital lenders	Proposed regulatory mechanism	Some important issues addressed (the list is not exhaustive)
RBI regulated entities (RE) and the lending service providers (LSPs) engaged by the REs	RBI's own regulatory framework for the REs and LSPs	<ul style="list-style-type: none"> <li>• Direct lending from the REs to the borrowers without any pass-through account.</li> <li>• The REs and the LSP to mandatorily have a nodal redressal grievance officer (including the redressal of complaints against the DLAs) and the details to be disclosed mandatorily on their websites.</li> <li>• DLAs to have a restricted access to the borrower's device.</li> <li>• Government to announce the legal and institutional framework for Balance Sheet Lending using DLAs which will be restricted to REs of RBI and to entities registered under any other law.</li> <li>• Digital India Trust Agency (DIGITA) will be set up to verify the DLAs before making them available to the public.</li> </ul>
Entities regulated by any other statutory laws/provisions (i.e., other than RBI)	Rules/regulations on digital lending to be formulated by the respective regulator/controlling authority based on the recommendations of WGDL	
Unregulated entities	Government to curb illegal lending activity based on the suggestions of WDGL	A regulatory framework will be brought in to ban all unregulated lending.

### Core areas of implementation



## Weblink

<https://rbidocs.rbi.org.in/rdocs/PressRelease/PDFs/PR689DL837E5F012B244F6DA1467A8DEB10F7AC.PDF>

## Therefore

There was a need to check the unethical practices in the recovery process of various lending apps and lenders. The multi-fold growth in the digital payments environment simultaneously increased the risk of unregulated lending and the recovery process threatening the soundness of the financial system. The RBI's timely move to bring digital lending under a stringent regulatory framework will strengthen and help positively grow India's digital revolution.