Policy on Co-Lending by Bank and NBFC/HFC to Priority Sector

A. BACKGROUND:

1.1 The Reserve Bank of India (RBI) had issued guidelines on Co-Origination of Loans by Bank and NBFCs for lending to priority sector vide notification dated 21.09.2018. All Scheduled Commercial Banks (except RRBs and Small Finance Banks) were permitted to engage with NBFC-ND-SIs to co-originate loans for creation of Priority Sector Assets, and share risks and rewards. RBI had instructed Banks/NBFCs to formulate Board approved policy for entering into a co-origination agreement.

1.2 In view of the above, Co-Origination Policy was placed for approval to the Board as a part of Credit Policy 2019-20, and was approved.

1.3 Based on the feedback received from the stakeholders and to better leverage the respective comparative advantages of the Banks and NBFC/HFCs in a collaborative effort, RBI decided to provide greater operational flexibility to the lending institutions, while requiring them to conform to the regulatory guidelines on outsourcing, KYC, etc.

1.4 Accordingly, RBI has revised the scheme and rechristened as **"Co-Lending Model" (CLM)** vide notification dated 05.11.2020 to improve the credit flow to the unserved and underserved sector of the economy and make available funds to the ultimate beneficiary at an affordable cost, considering the lower cost of funds from banks and greater reach of NBFC/HFCs. The said circular supersede the RBI notification on Co-Origination of Loans dated 21.09.2018. However, any loans outstanding in terms of the earlier circular would continue to be classified under priority sector till their repayment or maturity, whichever is earlier.

1.5 As per RBI guidelines, Banks shall formulate a Board approved policy for entering into CLM and place the approved policy on the Bank website. Based on the approved policy, a Master agreement shall be entered into between the two partner institutions (Bank and NBFC/HFC) which shall inter-alia include, terms and conditions of the arrangement, the criteria for selection of partner institutions, the specific product lines and areas of operation, along with provisions related to segregation of responsibilities as well as customer interface and protection issues.

1.6 The Master Agreement may provide for the banks to either mandatorily take their share of the individual loans originated by the NBFC/HFC in their books as per the terms of the agreement or to retain the discretion to reject certain loans after their due diligence prior to taking in their books.

1.7 In terms of the CLM, Bank is permitted to Co-lend with all registered NBFC (including HFCs) based on a prior agreement. The co-lending bank will take its share of the individual loans on a back-to-back basis in their books. However, NBFC/HFCs shall be required to retain a minimum of 20% share of the individual loans in their books.

1.8 Bank can claim priority sector status in respect of their share of credit while engaging in the CLM adhering to the specified conditions.

1.9 In terms of the above revised guidelines issued by RBI, we release herewith the Board approved Policy on Co-lending by Bank and NBFC/HFCs to Priority Sector.

B. Policy Guidelines:

1. Broad Criteria for Selection of NBFC (including HFCs) as a Partner Institution under Co-Lending Model (CLM):

- The NBFC/HFC must be a registered with RBI and in business for a period of more than 3 years, with minimum Networth of Rs. 200.00 Crores.
- NBFC/HFC shall be required to retain a minimum of 20% share of the individual loans on their books.
- Credit Rating of the NBFC/HFC by accredited External Rating Agency must conform to the minimum of A and above, for the last 3 years.
- The NBFC/HFC shall have a minimum Capital Adequacy Ratio of 15%
- Other Financial / Non-Financial parameters for each NBFC/HFC individually will be part of Master Agreement to be entered into between bank and NBFC/HFC.

2. Eligible Entities for Co-Lending:

2.1 CLM is applicable to all Scheduled Commercial Banks (excluding Regional Rural Banks, Urban Co-operative Bank, Small Finance Banks and Local Area Banks) and all registered NBFCs (including HFCs) for providing competitive credit to priority sector.

2.2 In terms of the CLM, our Bank may co-lend with all the registered NBFCs including HFCs based on a prior agreement. However, Bank is not allowed to enter into Co-lending agreement with an NBFC/HFC belonging to the promoter group.

2.3 The Master Agreement to be entered into by our Bank and NBFC/HFCs for implementing the CLM may provide either for the Bank to mandatorily take our share of the individual loans as originated by the NBFC/HFC in their books or retain the discretion to reject certain loans subject to our due diligence.

a. If the Agreement entails a prior, irrevocable commitment on the part of the Bank to take into our books the share of the individual loans as originated by the NBFC/HFC, the arrangement shall comply with the extant guidelines on Managing Risks and Code of Conduct in Outsourcing of Financial Services by Scheduled Commercial Banks, issued vide RBI notification dated March 11, 2015 and updated from time to time. In particular, our Bank will conduct due diligence at our end as per our extant guidelines.

b. Bank will also be required to comply with the Master Directions - Know Your Customer (KYC) Direction, 2016, issued vide RBI notification dated February 25, 2016 and updated from time to time, and our own extant guidelines in this regard, which permits regulated entities, at their option, to rely on customer due diligence done by a third party.

c. However, if our Bank exercises its discretion regarding taking into its books the loans originated by NBFC/HFC as per the Agreement, the arrangement will be akin to a direct assignment transaction. Accordingly, Bank shall ensure compliance with all the requirements in terms of Guidelines on Transactions Involving Transfer of Assets through Direct Assignment of Cash Flows and the Underlying Securities issued vide RBI notifications dated May 07, 2012 and August 21, 2012, and as updated from time to time, with the exception of Minimum Holding Period (MHP) which shall not be applicable in such transactions undertaken in terms of this CLM.

d. MHP is defined as the number of instalments to be paid prior to Securitisation / Direct Assignment of Loans assets, and is counted from the date of full disbursement of loans.

e. The MHP exemption shall be available only in cases where the prior agreement between the Bank and NBFC/HFCs contains a back-to-back basis clause and complies with all other conditions stipulated in the guidelines for direct assignment.

3. Generation of Loans under CLM:

The loan accounts will be generated in the following process:

a. The NBFC will perform loan origination activities, i.e., starting with the selection of borrowers in conformity with the product lines decided as per Master Agreement, and recommend the proposal to the Bank along with verified KYC documents and other due-diligence activities completed at its end, viz.,
   i. Verification of Borrower’s Place of Residence/Business/Work
   ii. Verification of IT Returns / Financial Statements / GST returns, Bank Statements and other documents as prescribed in the Master Agreement.
   iii. Verification of property proposed to be purchased/mortgaged, along with LSR and EVR from duly empanelled Advocates/Valuers, in case of loans where mortgage of property is involved.
   iv. Verification of Credit Bureau reports, CERSAI search reports etc.

b. The Bank will assess the proposal independently with regard to conformity with product guidelines and applicable risk assessment. The proposal will be co-lent only on conformation with laid-out guidelines.

c. The lending parties enter into a three-way agreement with the client. The Bank and NBFC will pool their funds into an escrow account to be maintained with the Bank, from which the loan shall be disbursed. Although both lenders will maintain the client’s accounts, they must share information and collaborate to generate a unified statement of accounts for the borrower for easier repayments.

d. Bank will also do due diligence at its end as per our laid down guidelines or with the help of Connect Perfect module prior to sanction of their facilities. The due diligence may include all the facilities provided to us vide the Connect Perfect module, viz., verification of KYC documents, CIC (CIBIL, CRIF etc.) scores extraction, ITR verification, etc.

4. Customer related issues:

4.1 The NBFC/HFC shall be the single point of interface for the customers and shall enter into a loan agreement with the borrower, which shall clearly contain the features of the arrangement and the roles and responsibilities of NBFC/HFCs and bank.

4.2 All the details of the arrangement shall be disclosed to the customers upfront and their explicit consent shall be taken.

4.3 Interest rates and Chargeability: The ultimate borrower may be charged an all-inclusive interest rate as may be agreed upon by both the lenders conforming to the extant guidelines applicable to both.

4.4 The extant guidelines relating to customer service and fair practices code and the obligations enjoined upon the banks and NBFC/HFCs therein shall be applicable mutatis mutandis in respect of loans given under the arrangement.

4.5 The NBFC/HFC should be able to generate a single unified statement of the customer, through appropriate information sharing arrangements with the bank.

4.6 With regard to grievance redressal, suitable arrangement must be put in place by the co-lenders to resolve any complaint registered by a borrower with the NBFC/HFC within 30 days, failing which the borrower would have the option to escalate the same with the concerned Banking Ombudsman/Ombudsman for NBFC/HFCs or the Customer Education and Protection Cell (CEPC) in RBI.

5. Sharing of Risks and Rewards:

5.1 Bank shall co-lend with NBFCs/HFCs under a CLM involving sharing of Risks and Rewards, ensuring appropriate alignment of respective business objectives, as per mutual agreement, subject to the NBFC/HFC being required to retain a minimum of 20% share of the individual loans in their books.

5.2 However, CA certificate should be obtained from the NBFCs/HFCs stating that its contribution towards the loan amount is not funded out of borrowing from Our Bank or any other group company / subsidiary of our Bank.

6. Priority Sector Status:

The Bank will claim priority sector status in respect of our share of credit while engaging in the co-lending arrangement, without recourse to the NBFC.

7. Other Operational Aspects:

7.1 Bank and NBFC/HFCs shall maintain each individual borrower's account for their respective exposures. However, all transactions (disbursements/ repayments) between the Bank and NBFC/HFCs relating to CLM shall be routed through an escrow account maintained with the Bank, in order to avoid inter-mingling of funds. The Master Agreement shall clearly specify the manner of appropriation between the co-lenders.

7.2 The Master Agreement may contain necessary clauses on representations and warranties which the originating NBFC/HFC shall be liable for in respect of the share of the loans taken into its books by the bank.

7.3 The co-lenders shall establish a framework for monitoring and recovery of the loan as mutually agreed upon, which will be a part of the Master Agreement.

7.4 The co-lenders shall arrange for creation of security and charge as per mutually agreeable terms.

7.5 Each lender shall adhere to the asset classification and provisioning requirement, as per the respective regulatory guidelines applicable to each of them including reporting to Credit Information Companies, under the applicable regulations for its share of the loan account.

7.6 The loans under the CLM shall be included in the scope of internal/statutory audit within the Bank and NBFC/HFCs to ensure adherence to their respective internal guidelines, terms of the agreement and extant regulatory requirements. **C.O. Audit and Inspection to incorporate appropriate aspects in scope of Concurrent Audit and Internal Audit for carrying out Audit of loans under Co-lending.**

7.7 Any assignment of a loan by a co-lender to a third party shall be done only with the consent of the other lender.

7.8 Both the Bank and NBFC/HFCs shall implement a Business Continuity Plan to ensure uninterrupted service to their borrowers till repayment of the loans under the co-lending agreement, in the event of termination of co-lending arrangement between the co-lenders.

8. Exposure ceiling:

8.1 As the Policy is being newly introduced, we propose that the maximum cap of total exposure of Co-lent loans with any Single NBFC/HFC and Group of related NBFCs/HFCs should not exceed Rs.1000.00 crores and Rs.2000.00 crores respectively during any Financial Year. Exposure would inter-alia mean Outstanding plus undisbursed portion of the Sanctioned limit.

8.2 However, the total exposure to Single/Group entity of NBFC/HFC will be guided by Prudential exposure ceiling as per extant Credit Policy guidelines of the Bank.

9. Delegation of Powers:

9.1. Selection of Branches:

Select branches across the country will be identified and authorized to handle such proposals based on the reach and area of operation of individual NBFC/HFC with whom Co-Lending to be done. The authority to select branches will rest with CAC.

9.2. Sanction of Outlay:

Powers to sanction the outlay with regards to Single/Group entity will rest with CAC/MCB.

9.3. Sanctioning Authority:

The authority to sanction individual proposals will be in line with the Bank's extant guidelines on Delegation of Powers for Credit.

9.4. Master Agreement between Bank and NBFCs and related SOPs:

- Based on the Board approved policy on Co-Lending, a Master Agreement will be entered into between the Bank and individual NBFC/HFC, which shall inter-alia include, terms and conditions of the arrangement, the criteria for selection of partner institutions, the specific product lines and areas of operation, provisions related to segregation of responsibilities as well as customer interface and protection issues, Service Charges, Pricing of Loans etc.
- Based on the guidelines enumerated in the Policy document and Master Agreements to be entered into with NBFC/HFC, broad SOPs will be developed in terms of Product creation, Rating and Appraisal mechanisms, Documentation and Creation of Security/Charge on assets, Monitoring & Recovery Mechanisms, Business Continuity Plans, Service Charges, Pricing of Loans etc., and any other aspects relevant to the scheme/process.
- SOPs finalised as such will be placed to CAC for approval.
- Master Agreement with individual NBFC/HFC should be legally vetted by CO: Legal Department and will be placed to CAC for approval. General Manager / DH of the respective vertical will be authorised for tie-ups, signing of agreements with NBFC/HFC.

10. IT Integration / Interface:

The following functions should be integrated / interfaced between Bank and NBFC using IT platforms:

- Seamless sharing of customer data on KYC and Due diligence through shared APIs.
- Integration of all relevant customer data and related Loan fields for opening of Loan accounts in CBS systems of both Bank and NBFC.
- Configuration of multiple repayment and accounting policies, Benchmark RoI of the co-lenders and changes thereof, to arrive at final repayment schedules and account statements for the customer.
- Escrow accounts to be maintained in Bank for all transactions (Disbursement/Repayments etc.) will be parameterised to avoid inter-mingling of funds, i.e., funds related to Disbursement and Repayment should remain separated. Further,

suitable configurations to be made in the Escrow accounts to credit the repayments to respective Loan accounts on a real-time basis.

11. Deviation:

Any deviation from the policy guideline/SOP will be permitted by respective committee (i.e., CAC/MCB) on case to case basis.

12. Validity & Renewal of the Policy:

- The policy will remain valid for FY 2021-22 or till the time it is reviewed/renewed further.
- The Policy shall be modified to give effect to changes in the extant guidelines/directives/initiatives that may be advised by GoI/RBI/IBA, for which action may be called for at short notice by CRMC, and will be placed to the Board for information.