RBI issues co-lending norms by banks and NBFCs to the priority sector.

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Overview

The Reserve Bank of India (RBI) has issues co-lending norms to priority sector. All scheduled commercial banks (excluding Regional Rural Banks and Small Finance Banks) are allowed to co-lend with all registered NBFCs (including Housing Finance Companies) for the creation of priority sector assets under co-lending model (CLM) based in prior agreement. Earlier in September 2018, RBI had allowed all SCBs to co-originate loans with only non-deposit taking systemically important (ND-SI) finance companies. The RBI took over the regulations of the Housing Finance Companies (HFCs) from National Housing Bank (NHB) in August 2019.

As per the RBI notification the guidelines are to provide greater operational flexibility to lending institutions, to improve credit flow to unserved and underserved sector of the economy and make funds available at affordable cost, considering lower cost of funds from banks and greater reach of NBFCs.

Highlights of Co-lending norms:

1) The co-lending banks will take their share of the individual loans on a back-to-back basis in their books. However, NBFCs shall be required to retain a minimum of 20% share of the individual loans on their books.

2) The banks and NBFCs shall formulate Board approved policies for entering into CLM and place the approved policies on their websites.

3) The Master Agreement may provide for the banks to either mandatorily take their share of the individual loans originated by the NBFCs 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.

4) The CLM shall not be applicable to foreign banks with less than 20 branches.

The below features are common in Co-Origination and Co-Lending norms-

1) Banks and NBFCs shall have to put in place suitable mechanism for due diligence by bank as credit sanction process cannot be outsourced.
2) Banks shall not be allowed to enter into co-lending arrangement with an NBFC belonging to the promoter Group.
3) 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 within 30 days.
4) The co-lending banks and NBFCs shall maintain each individual borrower's account for their respective exposures and all transactions shall be routed through an escrow account maintained with the banks.
5) The co-lenders shall establish a framework for monitoring and recovery of the loan and shall arrange for creation of security and charge, as mutually agreed upon.
6) Each lender shall adhere to the asset classification and provisioning requirement.
7) Any assignment of a loan by a co-lender to a third party can be done only with the consent of the other lender. Both banks and NBFCs shall implement a business continuity plan to ensure uninterrupted service to their borrowers till repayment of the loans under the CLM and Co-Origination agreement.

The below features are as per the latest norms –

Co-Origination	Co-Lending	Comments
The co-originating lenders shall adhere to applicable KYC guidelines.	The lenders are required to comply with the KYC directions which already permit regulated entities at their option to rely on customer due diligence done by a third party.	Expected to save time and operational cost of lenders especially banks as they can rely on NBFC due diligence after following appropriate protocols
NA	Banks can exercise its discretion regarding taking into its books the loans originated by NBFC as per the agreement, the arrangement will be akin to a direct assignment transaction (exception of Minimum Holding Period which shall not be applicable in such transactions).	Provides operational ease and flexibility for taking joint exposure for a customer originated by the NBFCs

CARE Ratings View

The Co-Lending Model is aimed at leveraging the reach of NBFCs to unserved segment of the economy and to aid banks meet their priority sector lending targets. The CLM need a joint contribution of credit at the facility level by both the lenders and also sharing of risks and rewards. The scheme is expected to bring down the cost of funds for the borrowers, considering the lower cost of funds from banks compared with NBFCs. As per RBI's sectoral deployment of credit from September 2018 to September 2020, priority sector credit by banks grew by 11.0% and in absolute terms it has increased by Rs.2.97 lakh crore. Further, in FY20 banks, PSL declined to 40.8% as compared with 42.6% in FY19.

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