PSL & CBG

Policy for Co-lending of Loans

Scope: India

Issuer: **Arvind Sharma** – Head, Priority Sector Lending (PSL)

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Global ID:

1 Guiding Principle

The Reserve Bank of India (RBI), in its circular RBI/2020-21/63 FIDD.CO.Plan.BC.No.8/04.09.01/2020-21 dated November 5, 2020 in supersession of earlier circular RBI/2018-19/49 FIDD.CO.Plan.BC.08/04.09.01/2018-19 dated September 21, 2018 (both attached), introduced Co-Lending Model (CLM)[1] that allows Banks to co-lend with all registered Non-Bank Finance Companies (NBFC) including HFC (Housing Finance Companies). The banks can claim priority sector status in respect of their share of credit while engaging in the CLM adhering to the specified conditions. DBS Bank India Limited (DBIL or Bank), being WOS entity of DBS Bank Limited, Singapore with more than 20 branches, can participate in co-lending of PSL loans as well as non-PSL loans. Under the arrangement, 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 per cent share of the individual loans on their books.

All outstanding co-lending loans (if any) booked under RBI Circular dated September 21, 2018 would continue to be classified under priority sector till their repayment or maturity, whichever is earlier.

Priority Sector Lending (PSL) is lending to those sectors which the Reserve Bank of India (RBI) considers as important for the overall development of the economy – including sectors that are under-banked and/or un-banked and to improve the flow of credit to the un-served and underserved sector of the economy.

RBI regulations require that Scheduled Commercial Banks meet PSL of 40% of the Adjusted Net Bank Credit (ANBC). These regulations are modified periodically by setting limits for sub-sectors and other qualifications for the beneficiary groups (last updated on September 04, 2020).

Co-lending is an important avenue for PSL target achievement as well as for CBG group to extend loans as it allows the Bank to reach out to target client segments in an economically efficient manner with least investment in setting up the distribution channels. The benefits that accrue to stakeholders in co-lending of loans are:

Benefit for the Customer:

- Lower cost of borrowing (blended)

Benefits for DBIL:

- Leverage the network and domain expertise of the NBFC partner - an RBI regulated entity.
- Bank retains credit decisioning right on each customer.
- Operational elements outsourced to the NBFC partner provides a high volume, low cost distribution & scale-up opportunity
- DBIL gets access to proven expertise and infrastructure for origination, distribution, servicing and collections & recovery that can be leveraged profitably for lending and managing the co-lending portfolio. Partnerships allow DBIL to learn about the segment behavior, credit performance etc. without having to invest heavily in the infrastructure required to run such a business
- A co-lending arrangement allows penetration into a market segment and/or consumer borrowing need that is currently not being served by DBIL

[1] Any subsequent amendments in RBI policy from time to time will be automatically applicable to this policy.

- Better economics due to the lower cost structure of the partner and the higher yields available.

Benefits for the NBFC:

- Competitive customer pricing, leveraging lower bank pricing.
- Ability to expand customer base.
- Leverage operating model to take on outsourced work from bank partner.

This document defines the policy governing co-lending partnership arrangements between the Bank and NBFC partners.

2 Policy

2.1 Partner Selection: Given the significant reliance on the partner, it is critical that the partner selection criteria be robust. The NBFC partner shall be assessed basis the appropriate DBIL approved framework for outsourcing including but not limited to the below mentioned:

- Business Experience
- Management / Promoters
- Financial soundness & Capital Adequacy
- Adequacy of Business policies
- Portfolio Credit Quality
- Governance framework
- Credit Rating

2.2 Credit Risk Framework: Credit Risk framework would be unique to each partnership program depending on NBFC partner's products and client segment and would comply to parameters as defined under this policy (para 2.6). It shall detail the credit risk criteria based on which the bank shall co-lend to borrowers. It shall also document the partner level selection assessment envisaged at 2.1 above. For PSL co-originated loans, it shall be approved by CRO, DBIL and Head PSL, DBIL. For co-originated CBG loans, the Credit risk framework would be approved by Head CBG, DBIL and CRO, DBIL. Approved framework shall be reviewed annually or earlier to incorporate any required changes.

2.3 Operating Framework: Bank and NBFC partner shall mutually agree on an Operating Framework including origination & KYC framework, monitoring guidelines, disbursement and collections framework, servicing and escalation matrix, accounting framework, NPA recognition and recovery process for the loans generated under co-lending model in line with parameters as defined under this policy (para 2.6). Framework shall be customized to ensure satisfactory customer delivery under each partnership program. The Operational Framework document will be signed off by Head of respective departments at DBIL and Head PSL or Head CBG, basis the type of colending model. The framework shall be reviewed annually or earlier to incorporate any required changes.

Bank and NBFC partner shall enter into Master Agreement capturing all aspects relating to colending model including credit, operating framework etc. The Master Agreement may provide either for the bank to mandatorily take their share of the individual loans as originated by the NBFC partner in their books or provide for Bank to retain the discretion to reject the loans.

2.3.1 If the Master Agreement entails a prior, irrevocable commitment on the part of the Bank to take into its books its share of the individual loans as originated by the NBFC, the arrangement will comply with the RBI guidelines on Managing Risks and Code of Conduct in Outsourcing of Financial Services by Banks issued vide RBI/2014-

15/497/DBR.No.BP.BC.76/21.04.158/2014-15 dated March 11, 2015 and updated from time to time. Bank will adhere to its credit assessment guidelines as part of ex-ante due diligence.

2.3.2 If, as part of the Master Agreement, the Bank retains its discretion regarding taking into its books the loans originated by NBFC partner, the arrangement will be treated as akin to a direct assignment transaction and 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/2011-12/540 DBOD.No.BP.BC-103/21.04.177/201112 dated May 07, 2012 and RBI//2012-13/170 DNBS. PD. No. 301/3.10.01/2012-13 August 21, 2012 respectively, as updated from time to time, with an exception of Minimum Holding Period (MHP) which shall not be applicable in such transactions undertaken under CLM. The MHP exemption shall be available only in cases where the prior agreement between the Bank and the NBFC partner contains a back-to-back basis clause and complies with all other conditions stipulated in the guidelines for direct assignment.

2.4 Pilot approach: The partnership can be rolled out as a pilot to understand and resolve teething issues/test the Operating & Risk framework; and to make the Outsourcing Risk Review (ORR) more robust. Subject to an acceptable cap (to be documented in the Credit Risk Framework at 2.2) on the pilot size and compliance to RBI guidelines on outsourcing.

2.5 Partnership Agreement: The bank and NBFC partner shall enter into a prior partnership commercial master agreement, including the Credit Risk/Operating Frameworks as envisaged at 2.2 and 2.3 above and the partnership features as detailed in section 2.6. The Agreement will be signed by Head PSL, DBIL or Head CBG, DBIL, basis the type of co-lending model. The Agreement will mandatorily include terms and conditions of the arrangement, the specific product lines and areas of operation, along with provisions related to segregation of responsibilities as well as customer interface and protection issues.

2.6 Partnership Features: Partnerships should incorporate all features of Co-lending model as per RBI guidelines including those summarized below:

Sharing of Risk and Rewards: Bank at its own discretion and in agreement with NBFC partner can decide upon credit risk by way of direct exposure that it intends to take on its book subject to maximum of 80% of loan amount. As per agreement Bank can decide to have different credit risk exposure ratio for different business/product segment with same co-lending NBFC partner subject to maximum of 80% of loan amount. Bank shall ensure that it does not enter into co-lending arrangement with an NBFC belonging to the promoter group.

Interest Rate: Basis respective risk appetite, credit assessment of the borrower and the RBI regulations issued from time to time, both Bank and NBFC partner would have flexibility to price their part of the exposure. The ultimate borrower would be charged an all-inclusive interest rate as may be agreed upon by both the lenders conforming to the extant guidelines applicable to both.

Know Your Customer (KYC): Bank shall comply with Master Directions - Know Your Customer (KYC) Direction, 2016, issued vide RBI/DBR/2015-16/18 Master Direction DBR.AML.BC.No.81/14.01.001/2015-16 dated February 25, 2016 and updated from time to time , which already permit regulated entities, at their option, to rely on customer due diligence done by a third party, subject to specified conditions.

Credit Sanction: Both Bank and NBFC partner shall be entitled to independently assess the risks and requirements of the applicant borrowers. Bank shall not outsource credit decisioning/ underwriting of the proposal. NBFC partner may recommend a proposal as found relevant for joint lending (as per parameters agreed with the NBFC partner) but final decision with regards to Bank's portion of exposure to be taken independently by bank depending on terms defined in the Master Agreement.

Documentation: The NBFC 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 NBFCs and banks. All the details of the arrangement shall be disclosed to the customers upfront and their explicit consent shall be taken.

Escrow Account: The Bank and NBFC partner shall open an escrow account for routing all transactions (disbursements/ repayments) between the banks and NBFCs relating to CLM, in order to avoid inter-mingling of funds.

Data Maintenance: Individual borrower's loan account details shall be maintained with Bank and NBFC partner to reflect their respective exposures. The NBFC partner would be generating a single unified statement of the customer, through appropriate information sharing arrangements with the Bank. The Master Agreement shall clearly specify the manner of appropriation between the co-lenders.

Monitoring & Recovery: The Bank & NBFC partner shall establish a framework for monitoring and recovery of the loan, as mutually agreed upon, as part of its operating framework.

Security and Charge Creation: Bank and NBFC partner would follow a mutually agreed framework for creation of security and charge filing, as part of its operating framework.

Provisioning/Reporting Requirement: Bank and NBFC partner shall adhere to the asset classification and provisioning requirements, as per the respective regulatory guidelines applicable including reporting to Credit Information Companies, under the applicable regulations for its share of the loan account.

Assignment: The Bank and the NBFC partner can assign the loans to a third party only with the mutual consent of both the lenders.

Grievance Redressal: Bank will put in place suitable arrangement with the NBFC partner to resolve any complaint registered by a borrower with the NBFC within 30 days and in case, the complaint is not resolved within 30 days, the borrower would have the option to escalate the same to concerned Banking Ombudsman/ Ombudsman for the NBFC partner, or the Customer Education and Protection Cell (CEPC) in RBI.

The Bank will continue to adhere to the extant guidelines relating to customer service and fair practices code and the obligations enjoined upon the banks and NBFCs in respect of loans given under the co-lending model arrangement.

Business Continuity Plan: Bank and the NBFC partner shall implement a business continuity plan to ensure uninterrupted service to the borrowers till repayment of the loans under the colending agreement, in the event of termination of co-lending arrangement between the co-lenders.

The above features shall be appropriately incorporated in the Master Partnership agreement for co-lending entered by the Bank with a NBFC partner.

3 Key Responsibilities

3.1 PSL/CBG Department

DBIL has set-up a separate PSL Department functioning both as a Business Unit and key agent for PSL focus. PSL department will be the Business Unit responsible for PSL loans under co-lending.

CBG Assets and Strategic Alliances team is looking at growth opportunities for lending partnerships including co-lending to Non PSL Loan as well and will be responsible from CBG side.

3.2 RMG

Partner selection and credit risk framework are most important part of establishing any partnership. RMG Credit Risk team will closely work with the PSL/CBG team in partner selection and designing credit risk framework for every partner which will include drafting Risk Acceptance Criteria (RAC) / parameters for on-boarding borrowers under the partnership. RMG Operations Risk team will give guidance over operational risk framework and outsourcing aspects.

3.3 Technology & Operations

Endeavour shall be made for technical integration between the Bank and NBFC partners' systems to optimize on automation, reducing operational cost and streamlining MIS, financial and regulatory reporting. Technology team shall provide the necessary support in this regard. Operations team will provide the support required on the operational aspects.

3.4 Project Team consisting of Supporting Units

Project team comprising of PSL/CBG, RMG & other Support Units (SU) will be set up for executing partnerships on need basis. Support Units are responsible for ensuring that processes are in alignment with the Bank's policy and are efficient.

3.5 Internal / Statutory Audit

The loans under the co-lending agreement shall be included in the scope of Bank's Internal/Statutory audit to ensure adherence to its internal guidelines, terms of the agreement and extant regulatory requirements.

4 Governance

4.1 Ownership and Approving Authority

This Policy is owned by both, the PSL & CBG department and approved by the DBIL Board. Both, PSL Head, DBIL & Head CBG, DBIL may mutually approve and document any changes that are non-substantive in nature.

4.2 Deviations

Deviations from this Policy, if any, should be on an exceptional basis and should be documented, endorsed by both, PSL Head, DBIL and Head CBG, DBIL. The summary of deviations taken during the year will be presented before the IMC for ratification during annual review.

DBS

4.3 Review

This Policy should be reviewed once in three years or when material changes are required / appropriate to ensure continued relevance. However, it may be noted that, any change in the regulatory requirement by RBI shall be made effective from the date of Circular or effective date stipulated by RBI whichever is earlier and the change in the policy shall be carried out and approved in the subsequent IMC meeting.

In instances where an extension is required, approval shall be obtained from both, PSL Head, DBIL and Head CBG, DBIL. A maximum extension of 3 months can be availed in such situations. If the Policy is reviewed with no or non-substantive changes, approval from India Management Committee is required.

Appendix 1 Glossary

NA

Appendix 2 Related Policies and Standards

NA

Appendix 3 Any Additional Information or Materials

RBI circular on Co-lending (RBI/2020-21/63 FIDD.CO.Plan.BC.No.8/04.09.01/2020-21 dated November 5, 2020) and Co-origination (RBI/2018-19/49 FIDD.CO.Plan.BC.08/04.09.01/2018-19 dated September 21, 2018).

RBI Guidelines on Co-Origination.PDF Co-lending by Banks and NBFCs.pdf

Appendix 4 Deviations

Effective Date	Section	Endorsed by & Endorsement date	Approved by & Approval date	Deviation Description	Reason for deviation
dd mmm yyyy	Section in this document where deviation occurs	Endorsement by Group/Country Head of the Unit/Function that applied for the deviation Endorsement date: dd mmm yyyy	Approval by document owner for the deviation Approval date: dd mmm yyyy	This describes the deviation applied to the section	This explains the reasons for the deviation
NA	NA	NA	NA	NA	NA

Appendix 5 Version History

Version	Date of Issue	Summary of Key Changes
1.0	03 Sept 2019	Standard Issued
2.0	15 December 2020	To incorporate certain policy level changes and operational modifications
3.0	28 February 2022	To incorporate factual changes in the policy like change in personnel, change the name of the unit etc.
4.0	17 February 2023	No changes - Annual review