Article

Financial asset aggregators: RBI issues draft regulatory directions

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The Reserve Bank of India, on 3rd March, 2016[1], announced the release of the draft guidelines[2] (Draft Guidelines) to put in place a regulatory framework for carrying out the business of Accounts Aggregator (AA). This press release is in furtherance to the press release of the RBI dated 2nd July, 2015[3] where it had, for the first time, expressed its intent to set up new kind of Non-Banking Financial Company (NBFC) which would carry out the business of accounts aggregator. The concept of account aggregation however was a brain child of the Financial Stability and Development Council, and the same has been doing its rounds from 2014 in the 10th meeting[4] of FSDC Secretariat and the matter was confirmed only in the 12th meeting[5] of FSDC in 2015.

Let us first understand what is asset aggregation.

Meaning of asset aggregators:

The Draft Guidelines defines "*business of an account aggregator*" in the following manner:

> *"business of an account aggregator" means the business of providing under a contract, the service of, retrieving or collecting information of its customer pertaining to such financial assets, as may be specified by the Bank from time to time; and consolidating, organizing and presenting such information to the customer or any other person as per the instructions of the customer;*
> *Provided that, the consolidated statement/ report of the financial assets of the customers, shall not be the property of the Account Aggregator, for any further use. The consolidated statement/ report will be only for use of the customer.*

The term *financial asset* for this purpose includes the following –

a) bank deposits including fixed deposits, saving deposits, recurring deposits and current deposits;
b) Deposits with NBFCs;
c) Structured Investment Product (SIP);
d) Commercial Paper (CP);
e) Certificate of Deposit (CD);
f) Government Securities (Tradable);
g) Equity Shares;
h) Bonds;
i) Debentures;

[1] https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=36394
[2] https://rbidocs.rbi.org.in/rdocs/content/pdfs/DNBFCA030316.pdf
[3] https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=34345
[4] http://finmin.nic.in/fsdc/Press_release_10th_meeting_FSDC.pdf
[5] http://finmin.nic.in/fsdc/Press_release_12th_meeting_FSDC.pdf

j) Mutual Fund Units;
k) ETFs;
l) Indian Depository Receipts;
m) CIS (Collective Investment Schemes) units;
n) Alternate Investment Funds (AIF) units;
o) Insurance Policies;
p) Balances under the National Pension System (NPS);
q) Units of Infrastructure Investment Trusts;
r) Units of Real Estate Investment Trusts;

Any other asset as may be identified by the Bank for the purposes of these directions, from time to time.

Asset aggregators and lead generators:

The AAs as per the Draft Guidelines are different from lead generators, sometimes also called loan aggregators. Loan aggregators or lead generators assist in obtaining finance by the prospective borrower, by aggregating his financial position and scouting for funding, mostly using web technology. This is also largely what is happening in P2P market.

The concept is widely used UK and USA have already turned out to be lucrative markets for the lead generators, where the scope of lead generation is not only restricted to financial services but extended to non-financial services as well. Lead generators bring in more focused approach to connect between the borrowers and lenders.

Some of the leading players engaged in the business of financial lead generation in UK are - MVF Global, Reactive, Call Credit, Chartered Developments.

Some of the leading players engaged in the business of financial lead generation in USA are – OnPath, eGENTIC, The List Partners, Talk2Rep.

Asset aggregators and portfolio managers:

While the AA is yet to be notified as a separate class of companies by the RBI, we must not forget about portfolio managers which also deals with portfolio of securities. Let us understand how does the two differ from each other.

The SEBI (Portfolio Managers) Regulations, 1993[6] defines portfolio managers in the following manner –

> *"portfolio manager" means any person who pursuant to a contract or arrangement with a client, advises or directs or undertakes on behalf of the client (whether as a*

[6] http://www.sebi.gov.in/cms/sebi_data/commondocs/pmregu1993_p.pdf

discretionary portfolio manager or otherwise) the management or administration of a portfolio of securities or the funds of the client, as the case may be;

As is evident from the above definition, the scope of the portfolio managers includes both advising and undertaking, on behalf of the customer, management and administration of portfolio of securities. This absolutely contrary to the scope of AA, which is restricted only up to aggregation of information of a portfolio of financial assets of the customer.

Therefore, we can say that the scope of portfolio managers starts from where the scope of AA ends.

Financial aggregators: global scenario

Financial aggregation is not a new concept and has been used widely world-wide for quite some time now. Financial aggregation is same as asset aggregation where financial information from multiple sources are collected and presented together so as to enable the investors to report and analyse the data with ease.

In USA, the market has been flourishing for over a decade and half until lately when leading banks like JPMorgan Chase, Wells Fargo and Bank of America cut off data to some of the financial aggregators[7].

Unlike USA, this concept could penetrate the market in UK only a couple of years back. The concept is commonly known as account aggregation in UK. The most popular app in UK is OnTree. Most of the UK-based accounts aggregators in UK rely on a US-based platform called the Yodlee for aggregation accounts for their customers[8].

In Australia, the Australian Securities and Investments Commission, came out with a consultant paper on account aggregation in the financial services sector in 2001[9] to provide a skeleton to the account aggregation business.

How is asset aggregation an NBFC activity?

The definition of the term "Account Aggregator" refers to section 45-I (f) (iii) of the Reserve Bank of India Act, 1934 which says –

(f) ''non-banking financial company'' means–
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[7] http://www.pymnts.com/news/2015/bank-of-america-joins-financial-data-aggregator-battle/
[8] http://www.theguardian.com/technology/2014/jul/26/personal-finance-apps-ontrees-yodlee-privacy
[9] http://download.asic.gov.au/media/1933166/what-do-you-want-to-do-with-acctaggreg_issues.pdf

> *(iii) such other non-banking institution or class of such institutions, as the Bank may, with the previous approval of the Central Government and by notification in the Official Gazette, specify;*
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> *XXX*

While the RBI Act confers sufficient powers on the RBI to notify further classes of non- banking institutions as non-banking financial companies, however, it would be really inappropriate for the RBI to call this particular class of company as an NBFC. The justification for the same is below.

The term NBFC signifies a company which is not a bank but carries out financing activities. To understand what a financing activity means, we can again go back to the section 45I of the RBI Act, which defines the term "business of a non-banking financial institution" in the following manner –

> *(a) ''business of a non-banking financial institution'' means carrying on of the business of a financial institution referred to in clause (c) and includes business of a non-banking financial company referred to in clause (f)*

In this regards, it must be noted the clause (f) of the said section defines the term "non-banking financial company", the definition of which includes non-banking institutions as well. So to understand the actual meaning of non-banking financial activity we should refer to definition of *financial institution* as per clause (c) of the said section, which is as follows –

> *(c) ''financial institution'' means any non-banking institution which carries on as its business or part of its business any of the following activities, namely:*
>
> *(i) the financing, whether by way of making loans or advances or otherwise, of any activity other than its own:*
> *(ii) the acquisition of shares, stock, bonds, debentures or securities issued by a Government or local authority or other marketable securities of a like nature:*
> *(iii) letting or delivering of any goods to a hirer under a hire-purchase agreement as defined in clause (c) of section 2 of the Hire-Purchase Act, 1972:*
> *(iv) the carrying on of any class of insurance business;*
> *(v) managing, conducting or supervising, as foreman, agent or in any other capacity, of chits or kuries as defined in any law which is for the time being in force in any State, or any business, which is similar thereto;*
> *(vi) collecting, for any purpose or under any scheme or arrangement by whatever name called, monies in lumpsum or otherwise, by way of subscriptions or by sale of units, or other instruments or in any other manner and awarding prizes or gifts, whether in cash or kind, or disbursing monies in any other way, to persons from whom monies are collected or to any other person, but does not include any institution, which carries on as its principal business –*

(a) agricultural operations; or
(aa) industrial activity; or
(b) the purchase or sale of any goods (other than securities) or the providing of any services; or
(c) the purchase, construction or sale of immovable property, so however, that no portion of the income of the institution is derived from the financing of purchases, constructions or sales of immovable property by other persons;

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Notably each of the businesses above is a fund based business. The activity of asset aggregation is a fee based business and does not involve any movement of money either to or from the aggregator. The aggregator is simply aggregating information, and not the financial assets of the customer. There is no pooling of money at all with the AA. In that scenario, it is questionable as to how a fee based activity as this could be an NBFC activity, requiring registration with the RBI?

The RBI's powers of registration of NBFCs come from Chapter III-A of the RBI Act. While there is no doubt that the RBI may try to encourage aggregators of financial assets, however, the regulatory tone of the directions sets one thinking as to how does the RBI get the powers to direct the registration of the asset aggregators.

Functions of an aggregator

Economics of aggregation business:

Evidently, aggregation business is technology-enabled, and therefore, the business will require strong technology support. In fact, the Draft Guidelines say that after getting a temporary registration, an AA will have to demonstrate ability of entering into aggregation business by technology capabilities.

The potential sources of revenue of asset aggregators may be from customers. While AAs are not portfolio managers as they do not have any discretion in terms of management of financial assets, it is doubtful if an AA may generate source of revenues from the investees. AA obviously will not be allowed to pass on the fiduciary information about the assets of the client to any potential investee, and hence, it is unlikely that an AA may generate revenues from mutual funds, banks or other potential investees.

In all likelihood, AA business may align well with the business of wealth management. An AA may be a part of a financial conglomerate that has presence in other financial services as well.

Fire walls needed

AAs will be sitting with confidential fiduciary information. AA may be tempted to use the information for their own gain or for that of the financial conglomerate. Hence it will be very important for the AAs to create a proper firewall to ensure the safety and confidentiality of the information collected by them on behalf of their clients.

In fact, the Draft Guidelines itself has highlighted, at several parts, several checks and balances that the AAs must take care of, the same have been listed down below –

a. Account Aggregator shall share information only with the customer to whom it relates or any other person authorized by the customer. Further, the process of authentication of the authorization should be robust.

b. In order to ensure that the information so collected is not used by the AAs for their own gain, the Draft Guidelines provides restrictions upon the AAs so that they cannot undertake any other business other than the business of account aggregator.

c. No financial asset related customer information pulled out by the AAs from the financial service providers should reside with the AAs.

d. AAs should have a Citizen Charter that will explicitly guarantee protection of the rights of a customer. The AAs shall not part with any information that it may come to acquire from/ on behalf of a customer.

e. The AAs should have adequate safeguards built in their IT systems to ensure that they are protected against unauthorised access, alteration, destruction, disclosure or dissemination of records and data.

Other requirements under the Draft Guidelines

We have already discussed in the write-up that the AAs are required to obtain registration with the RBI as NBFCs, consequently, several directions applicable to the NBFCs have been listed down in the Draft Guidelines. Among the long list of directions applicable to the NBFCs, the following have been incorporated in the Draft Guidelines –

a. Portions of Corporate Governance Directions dealing with formation of committees like Audit Committee, Nomination Committee and Risk Management Committee, determination of fit and proper criteria of the directors.

b. Provisions with respect to change/ acquisition of control over the management of the companies.

In addition to the above, the Draft Guidelines also talk about returns to be filed by the AAs, which the RBI will prescribe in times to come and also that the affairs of the AAs shall be subject to audit by the RBI.

To read more resources on NBFCs- Click here
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