# Co-lending Guidelines

## Understanding the borderlines

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# What is co-lending?

Financial interfaces between different financial entities may take the form of securitisation, direct assignment, co-lending, banking correspondents, loan referencing, etc.

Co-lending is coming together of entities in the financial sector – mostly, something that happens between banks and NBFCs, or larger banks and smaller banks for offering a loan/financial product.

There is joint contribution of credit by both lenders at the facility level. It also involves sharing of risks and rewards between the co-lenders.

# Difference between Co-lending, Direct Assignment and Securitisation

## Securitisation

In Securitisation, the originator sells its receivables to an SPV, which then raises funds by issuing PTCs (with receivables as underlying assets

## Direct Assignment

In Direct assignment, the originator sells its receivables (after some seasoning) directly to the assignee, who takes over such assets in its own books

## Co-lending

In Co-lending, the loan is co-originated by the parties at the inception itself

# Why Co-lending?

Leveraging the outreach, tech-based appraisal process, automated processes and specialization of NBFCs

Achieving Priority Sector Lending Targets for Banks

A win-win situation for both the bank and the NBFC

# Benefits to banks

Benefit of the outreach of the NBFC

Automation of lending process, resulting into reduced costs of documentation, due diligence, etc.

Bank may have full recourse on the NBFC on the co-originated loans (hence, complete risk cover) – (under the CLM guidelines)

# Benefits to NBFCs

- Expansion of customer base
- Relaxation from taking the entire exposure in the books (even after having risk over the entire exposure)
- Diversified portfolio
- Alternative to obtaining finance from banks for on-lending to borrowers

# Examples

| Base Case: No Co-lending | | | |
|---|---|---|---|
| Asset/Exposure | Amount | Risk Weight/CCF | Amount of RWA |
| Loan Exposure | 1,00,000 | 100 | 1,00,000 |
| Recourse | 0 | 100 | 0 |
| Total | | | 0 |
| Capital Requirement | | | 15,000 |

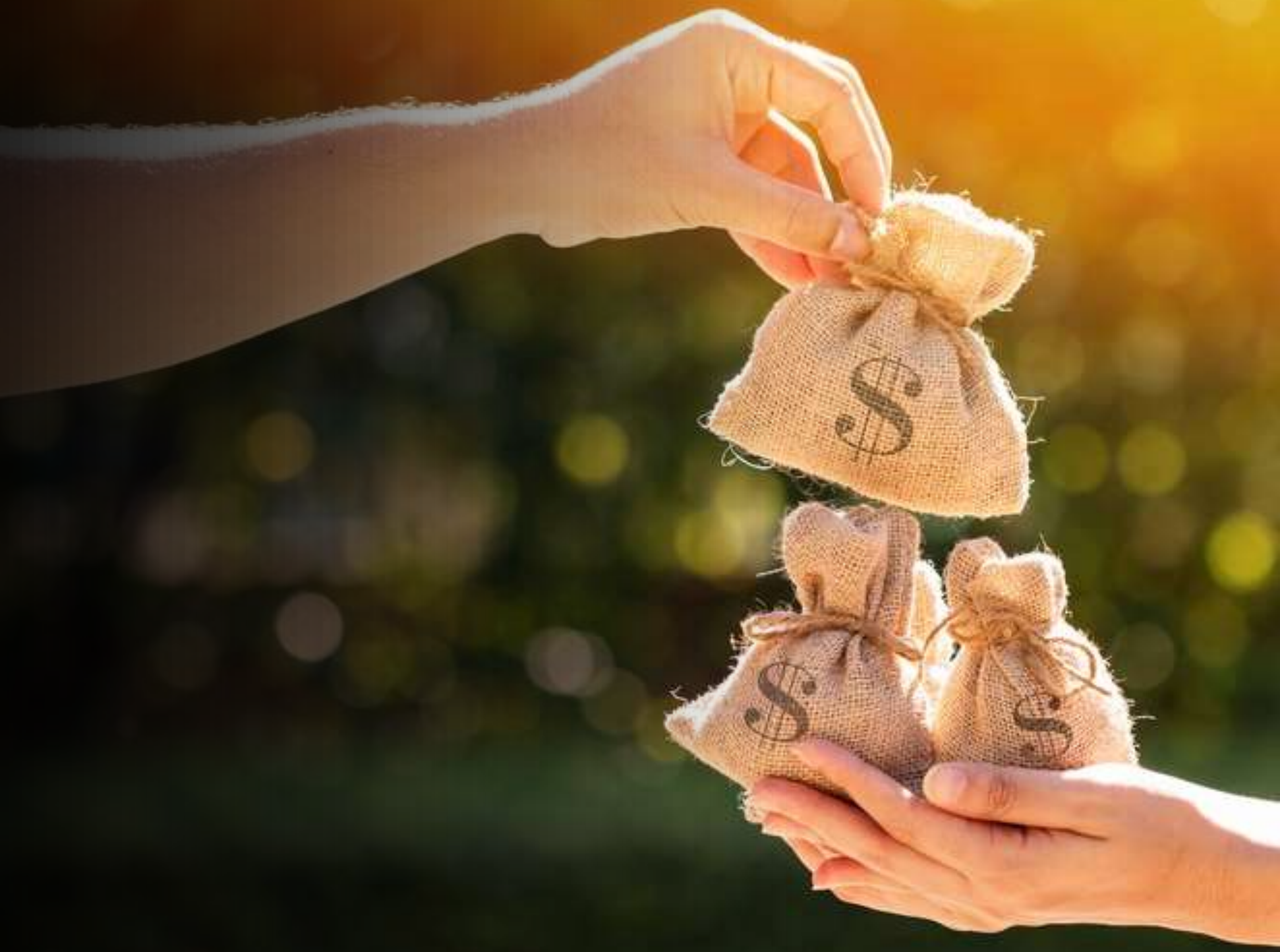
| Case 1: No Recourse | | | |
|---|---|---|---|
| Asset/Exposure | Amount | Risk Weight/CCF | Amount of RWA |
| Loan Exposure | 30,000 | 100 | 30,000 |
| Recourse | 0 | 100 | 0 |
| Total | | | 0 |
| Capital Requirement | | | 4,500 |

| Case 2: Recourse in the form of guarantee | | | |
|---|---|---|---|
| Asset/Exposure | Amount | Risk Weight/CCF | Amount of RWA |
| Loan Exposure | 30,000 | 100 | 30,000 |
| Guarantee | 70,000 | 100 | 70,000 |
| Total | | | 1,00,000 |
| Capital Requirement | | | 15,000 |

| Case 3: Recourse in form of any other contingent liability | | | |
|---|---|---|---|
| Asset/Exposure | Amount | Risk Weight/CCF | Amount of RWA |
| Loan Exposure | 30,000 | 100 | 30,000 |
| Indemnity/other contingent liability | 70,000 | 50 | 35,000 |
| Total | | | 65,000 |
| Capital Requirement | | | 9,750 |

# Getting into the details of CLM guidelines

New concepts introduced, old ones retained and everything in between



# Applicability

- APPLICABLE FROM THE DATE OF PUBLICATION (NOVEMBER 5, 2020)

  (NO TIMELINE SPECIFIED)
- PSL CLASSIFICATION OF EXISTING LOANS UNDER THE ERSTWHILE GUIDELINES TO CONTINUE
- EXISTING ARRANGEMENTS MAY HAVE TO BE REVIEWED
- APPLICABLE TO CO-LENDING BETWEEN SCBS AND NBFCS (INCLUDING HFCS)
- APPLICABLE IN CASE OF NON-PSL LOANS AS WELL IN PARI-MATERIA

# Salient Features

- Provides two different options for manner of co-lending i.e. Co-origination and DA

- Nature of transactions to be determined based on the discretionary power of the bank to take loan in its books

- Allows NBFCs to bear the risk on the entire exposure of the loans originated by them

# From Co-origination to Co-lending

Earlier, the guidelines dealt only with co-origination of loans

Now, co-Lending gets three faces with introduction of the CLM guidelines-

| | | |
|---|---|---|
| Co-origination | Co-Lending (With outsourcing) | Direct Assignment |

# Outsourcing or DA?

- **Bank**
  - Originates along with the NBFC
    - CLM guidelines applicable. In case sourcing function is outsourced, outsourcing guidelines shall be applicable
  - Irrevocable commitment to take loans originated by the NBFC in its books
    - This is same as Outsourcing the sourcing function to NBFC- Hence, outsourcing guideline shall be applicable
  - Option to cherry-pick the loans originated by the NBFC
    - This is akin to a DA transaction (except for the fact that the loan is shared at the time of origination only)- Hence, DA guidelines, other than MHP requirement shall be applicable

# Defining the roles

- NBFC to be the face of transaction- Hence, the NBFC shall
  - be the single point of interface for the customers
  - generate a single unified statement of the customer, through appropriate information sharing arrangements with the bank
  - Carry out KYC compliances on behalf of the bank (as on outsourced agent)
- Bank will be responsible for funding the loan as per the agreed share and other responsibilities as fixed under the agreement.

# Individual Responsibilities of each Co-Lender

**01**

ASSET CLASSIFICATION AND PROVISIONING AS PER APPLICABLE NORMS ON THEIR RESPECTIVE SHARE OF THE LOAN

**02**

DEVELOP AND MAINTAIN BUSINESS CONTINUITY PLANS WITH RESPECT TO LOANS GRANTED UNDER THE ARRANGEMENT

**03**

ACCOUNTING AND REGULATORY REPORTING WITH RESPECT TO THEIR SHARE OF THE LOANS

**04**

COMPLIANCE WITH FAIR PRACTICES CODE AND GUIDELINES ON CUSTOMER SERVICE

# Responsibilities which may shared as agreed

01

MONITORING AND RECOVERY FUNCTION

02

CREATION OF SECURITY

03

MANAGEMENT OF ESCROW ACCOUNT

# Actionables

| Adoption | Conduct | Execution | Establish |
|---|---|---|---|
| Formulate and adopt a Board approved Policy on Co-lending (existing policy may be revised if required) | Conduct due-diligence of the co-lending party | Execution of Master Agreement | Establish escrow mechanism |

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