

FIDC

Finance Industry Development Council

(A body incorporated as a Self Regulatory Organisation for Registered NBFCs)

August 16, 2010

Dr.D.Subbarao
Governor
Reserve Bank of India
Central Office Building
Shahid Bhagat Singh Road
MUMBAI 400 001

Respected Sir,

Reg: Discussion Paper on Engagement of 'for-profit' Companies as Business Correspondents (BCs) dated August 2nd, 2010

We would like to place before you the case for NBFCs to be empanelled as business correspondents (BC) to banks. We believe that NBFCs can contribute significantly in achieving RBI's goal of financial inclusion.

Banking Correspondents are to deliver financial services at an affordable cost to the low-income, disadvantaged groups that normally get excluded by the mainstream banking system. Over their long history, NBFCs have been providing financial services precisely to these segments of people that are not covered by banks. Some of their typical customer profiles include:

- Self employed professionals
- Unorganized sectors such as small traders, shop keepers etc.
- Rural entrepreneurs
- Farmers and farm workers
- Micro and small enterprises

In this context, it is pertinent to elaborate on the inherent strengths of NBFCs which match the requirements of BC model, thus making NBFCs an ideal collaborator for banks as BCs. Some of the relevant NBFC strengths are:

I. Regional Presence

- a) Local market knowledge and provision of excellent service levels to the customer, whether in urban, rural or other under banked segments of the country
- b) Well trained field staff who understand the customer's financial needs and can educate new customers on banking and credit. This will minimize the need for investments by banks in training BCs

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II. Operational Effectiveness

1. Low cost and flexibility in the operations which will be an advantage for the sustainability of the BC model
2. An understanding and proven experience in handling cash transactions in rural areas
3. Proven risk mitigation controls and specifically, the ability to assess credit risk in absence of traditional parameters

III. Technology Leverage

1. Most NBFCs today, have experimented and adopted various technology enablers to their operations such as internet based information dissemination, hand held devices, smart cards etc. for customer service. The same can be extended to further the needs of the BC model to ensure safety and ease of banking to customers

IV. Financial Strength

1. The financial strength of the NBFC as compared to an individual or a not-for-profit organization acting as BCs, will help in effective cost sharing with the banks and more importantly result in minimal charges being passed on to the customer

V. Governance and Compliance

1. NBFCs have been adhering to the governance structure and compliance norms set by RBI and have the necessary processes and systems in place for the reporting requirements expected from BC

It is true that there is a potential conflict of interest between the NBFC and bank's operations while implementing such an arrangement. The solution lies in evolving appropriate monitoring and control mechanisms that will mitigate such risks. Some aspects of such a regulatory mechanism could involve:

- 1 Development of a operational guidebook for use by the NBFC staff acting as BCs to separate the bank and NBFC interests
- 2 Setup of minimum/maximum business limits for the NBFCs and banks
- 3 Varying degree of permissions based on size, track record, geographical presence etc. (e.g a pan India NBFC can operate across India whereas a regional NBFC will be restricted to the region of its prominence)
- 4 Non compete agreements between NBFCs and banks after termination of a BC

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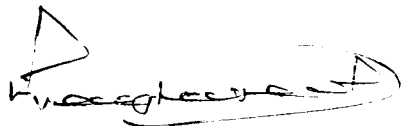
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- 5 Mandatory disclosures for all NBFCs and banks on BC activities. For e.g. customer overlap between normal and BC operations of the NBFC
- 6 Specific organization structures to be setup in the NBFC and bank for monitoring and internal audit of BC activities
- 7 Setup of a scheme for peer audit by banks and NBFCs
- 8 Setup of a banking ombudsman for monitoring all BC activities of NBFC

It has long been our case that the ideal relationship between banks and NBFCs should be that of wholesaler and retailer. It is our submission that the Business Correspondent model provides the ideal framework for both deposit taking and non-deposit taking NBFCs to work with banks under the guidance of RBI to further the financial inclusion goals in a sustainable manner. We trust that this would receive your favourable consideration.

Kind Regards,

Yours sincerely



T.T.Srinivasaraghavan
Chairman

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