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Megha Middha, is working as an Assistant Professor of Law in Mody University of Science and Technology, Lakshmangarh, Sikar (Rajasthan). She has an experience in the teaching of almost 3 years. She has completed her graduation in BBA LL.B (H) from Amity University, Rajasthan (Gold Medalist) and did her post-graduation (LL.M in Business Laws) from NLSIU, Bengaluru. Currently, she is enrolled in a Ph.D. course in the Department of Law at Mohanlal Sukhadia University, Udaipur (Rajasthan). She wishes to excel in academics and research and contribute as much as she can to society. Through her interactions with the students, she tries to inculcate a sense of deep thinking power in her students and enlighten and guide them to the fact how they can bring a change to the society

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Mrs.S.Kalpana

Assistant professor of Law

Mrs.S.Kalpana, presently Assistant professor of Law, VelTech Rangarajan Dr. Sagunthala R & D Institute of Science and Technology, Avadi. Formerly Assistant professor of Law, Vels University in the year 2019 to 2020, Worked as Guest Faculty, Chennai Dr.Ambedkar Law College, Pudupakkam. Published one book. Published 8 Articles in various reputed Law Journals. Conducted 1 Moot court competition and participated in nearly 80 National and International seminars and webinars conducted on various subjects of Law. Did ML in Criminal Law and Criminal Justice Administration. 10 paper presentations in various National and International seminars. Attended more than 10 FDP programs. Ph.D. in Law pursuing.



Avinash Kumar



Avinash Kumar has completed his Ph.D. in International Investment Law from the Dept. of Law & Governance, Central University of South Bihar. His research work is on "International Investment Agreement and State's right to regulate Foreign Investment." He qualified UGC-NET and has been selected for the prestigious ICSSR Doctoral Fellowship. He is an alumnus of the Faculty of Law, University of Delhi. Formerly he has been elected as Students Union President of Law Centre-1, University of Delhi. Moreover, he completed his LL.M. from the University of Delhi (2014-16), dissertation on "Cross-border Merger & Acquisition"; LL.B. from the University of Delhi (2011-14), and B.A. (Hons.) from Maharaja Agrasen College, University of Delhi. He has also obtained P.G. Diploma in IPR from the Indian Society of International Law, New Delhi. He has qualified UGC - NET examination and has been awarded ICSSR - Doctoral Fellowship. He has published six-plus articles and presented 9 plus papers in national and international seminars/conferences. He participated in several workshops on research methodology and teaching and learning.

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BOOM OF DIGITAL LENDING

AUTHORED BY - ARPIT JAIN & SAUMYA TOMAR

Keywords

1. Digital Lending
2. Financial inclusion
3. Technology
4. Traditional Banking
5. Loan process

Abstract:

Digital lending revolutionized the traditional lending geography, using technology for briskly, accessible, and inclusive access to credit. With wide internet penetration and mobile operation, digital platforms have normalized lending, reaching preliminarily underserved populations. According to a 2021 check, digital lending's global request was valued at \$11.3 billion and projected to grow at a CAGR of 18.3 by 2028. These platforms use AI algorithms for threat assessment, reducing processing time and paperwork. By streamlining processes and offering individualized loan products, digital lending has come a catalyst for fiscal addition and profitable growth, serving borrowers and lenders likewise. Our idea is to explore the untapped eventuality of digital lending in India, slipping light on its transformative impact on fiscal addition, advancing practices, and profitable growth. Through in-depth analysis and case studies, we aim to show the unique challenges and openings faced by the Indian digital lending ecosystem, addressing its impact on borrowers, lenders, and non-supervisory aspects. By pressing innovative technologies, arising trends, and unborn prospects, this composition seeks to raise mindfulness and give precious perceptivity into a content that has been overlooked by others. In conclusion, the rise of digital lending has significantly transformed the lending landscape, addressing the inefficiencies of traditional banking and promoting financial inclusion. This modern approach has streamlined the lending process, making it faster, more accessible, and customer-friendly. Through advancements in technology, data analytics, and the establishment of digital ecosystems, digital lending has emerged as a powerful tool for bridging the credit gap, especially for underserved

segments like micro, small, and medium enterprises. While challenges and regulatory concerns exist, the benefits of digital lending in terms of customer satisfaction, operational efficiency, and financial inclusion cannot be ignored. As the digital lending ecosystem continues to evolve, it holds the potential to reshape the financial industry and contribute to economic growth.

INTRODUCTION

Digital lending is a modern form of borrowing of money by modern customers via websites, apps with the combination of two generations of banking systems. The most effective part was that these platforms provide loan really fast with less paper procedures that helps business and group of people to take loan on urgent basis or in urgent situations. During the COVID-19 time when banks were close these fin tech companies became the back bone of lending system. This portmanteau allows whole process so fast that it completes within 10 minutes without any collateral. This also skyrocket the demand of 'pay later' platforms which promotes not making upfront payments.

The Reserve Bank of India voluntarily come into play to analyses the functioning of lending apps and website because of miss-selling to unsuspecting consumers a lot of data breaching cases were being reported also unethical business activities are increasing day by day.

For this Working Group was also formed which mainly focused on conduct, technology and charges which work as bedrock and all analysis were dependent on that. This further support RBI to release of RBI implementation of recommendation and digital lending guidelines. The guideline were issued under ambit of banking regulation act 1949, the RBI Act 1934, The national housing bank act 1987 and credit information (regulation) act 2005.

Now the importance of digital lending is finance penetration which assist in meeting huge credit need which rarely meet and it mainly focuses in micro enterprises and low income branch of India. Up to the most extent it help in saving time as it decreases the overhead cost by 30%-50%. Digital lending is also called alternative lending. It has aimed different borrowing needs like consumer loans, small and medium business loans, capital loans, etc. Digital lending companies have better possession of higher returns than banks. Digital lending has great opportunities to grow in country like INDIA because of the digital loan system. Industry estimates say the digital lending market is expected to grow to a whopping USD 515 billion by 2030. Tho, it has so many advantages but

at the same time great technology brings great risks also and in country like India its very difficult to make people trust the process of digital lending Risks involved in digital lending are –there are changes of leakage on dark web, take over of accounts, Fraud campaigns. Another problem with Indian crowd is despite significant advancements in technology, a considerable portion of the Indian population still lacks digital literacy. Fin tech companies need to invest in educational initiatives to make their products more accessible and user-friendly for a broader audience.

STATEMENT OF PROBLEM

In this era of 21st century the formal financial institutions ,lending is happening through offline mode. We can say that the lending process is of early age, right from the identifying blueprint of borrower to confirmation of loan or credit is being carried out traditionally which is really mundane and slow for urgent basis creditors. Most of the bank still use stereotypical guidelines to issue loan such as **CIBIL** credit score to discover the credit worthiness of a borrowers. These credit scores have limitations that facts presented by the borrowers is not given enough value and that's not enough bank provide loans provide loans to only those borrowers who have the bank account in their bank and customer who have GOOD CREDIT SCORE.. As a result, the individualities and the businesses do not have access to the banks irrespective of larger number of fiscal addition enterprise of the Government of India and those who are short of persuading credit scores come financially barred. therefore, the traditional banking system makes the individualities and the businesses financially barred and it has clumsy and time consuming lending process .Now for this a bridge is here called digital lending .Digital lending is really smooth in nature and loans are sanctioned in less time comparatively by the help of technology and basic credit score at pocket friendly rate of interest .Few of the digital lenders provide credit in such a short span of time just after submitting of respective documents and they provide wide range of credit to reach diversified needs of different people and group of peopleThat is why is need of the hour to study about the boom of digital lending in the world of 21st century.

The growth in digital loan purchases in next 5 years

(1USD= 82INR)

Digital lending growth has been strongly witnessing 30 per cent annual growth in enquiries checking the the departments of the government. Contrary to commercial lending, bad debts in retail lending have held up well and the office score profile of consumers entering loans has

astronomically been stable. With rising influx situations and a burgeoning middle class with advanced disposable inflows, demand for retail credit is anticipated to be robust in the next five times driven by consumption growth across sectors .

Though it is full of advantages but at the same time it has also some negative approaches. According to some researches it may release various problems.

The smoothness and accessibility to digital credit institutions is financially harmful psychologically such as impulsive borrowing and spending .Easy availability of credit may encourage customers to lend the loan without even thinking a bit which would lead to wastage of money on a large scale.

There is a strong competition going on between banks and financial institutions .Some are giving low competitive interest rates because at the end of the day the main motive is profit making . In some corridor of the world, for illustration in developed countries, there are neobanks¹ started launching fiscal products far beyond simple digital lending, while in some developing countries there's only some banks that offer similar services. In Uzbekistan digital lending experience is yet only contains filling online operation to take loans. After filling the operation the client need to go bank with his or her document portfolio to take loan. Not numerous banks offer online microcredit, in addition the interest rate for microcredit is much advanced and conditions are superior. For case in The Joint- Stock Commercial" Aloqa bank" online microloan's interest rate is 109.5 per cent periodic, while it's 32- 35 per cent for simple microcredit. For taking microloan the debtor shouldn't have overdue debt on other loans, a bank card must have at least 9 times pay envelope in the last 12 months, and have a nonstop payroll for the last 3 months. The loan quantum isn't further than 50 of the average payment of the debtor. Only a many banks offer online microloans. Digital lending popular is low fiscal knowledge, access to technological tools and of course the low rate of IT development. Using digital loans and fiscal knowledge are significantly related. In general, the operation of digital fiscal product creates the implicit to make fiscal services available to a wider range of consumers and enterprises, promoting fiscal addition and access to fiscal products. For giving online loans the platform should check the guests ' credit history and score its return capability and in this turn there should be pall database that collects all the information about customer, its plant, payment, former debts and loans. Developing countries need these kind of pall database to apply digital lending, so that the

platform itself will assess the customer and decide whether to give loan or not by twinkles. Regarding the competent operation of online credits, special memorial that sends announcements and warnings about the over operation and help them from wasting to guests who took loan from bank may affect in effective operation of online credits. In small banks or banks in developing countries can achieve nonstop plutocrat coffers for credits by raising the deposit base by attracting further deposits.

WORKING MECHANISM OF DIGITAL LENDING

A .Usage of internet

As I stated we are in the world of 21st century covered all with technology .The usage behaviour of the world is changing in fact the Indian population is extensively using online transactions all thx to e-commerce websites and most importantly efforts of the government to make India a cashless economy.

B .Technological advancements and big data

Again in this era of 21st century there is a new phase of technology like AI, block chain ,cloud computing for the advancement of digital lending .Nation like India is also creating a ecosystem for the advancement and growth of Fin tech start ups .These technologies will bring new form of transections to the country.

C .Digital ecosystem

Parallel to nature of customer its vital to have suitable ecosystem for the growth of digital ecosystem in India. India has somewhere achieve in creating a growing and developing ecosystem for Fin tech and digital transections due to which digital lending is growing through various steps like Bharat bill payment system, cashless economy and Goods and Service Tax(GST).

E .Time saving and customer friendly approach

Getting loans through digital way is not a rocket science but it is a very smooth and simple process .It is fast in terms of tenure ,pricing, and approach. Customer can approach the lender through many ways and give the required documents and get loan any time with 24/7 support system.

State of Digital lending towards MSME in India

it is well known fact that new technology always have capacity to bridge gap between asymmetrical transfer of information between provider and user of finance . With implementation of digitalisation there is need is of effectiveness in digital lending and clearing the barrier so that lending can be started specially for micro ,small and medium enterprises .

there are a lot of problems faced by MSME such as :

lack of access to finance as there is no formal data for credit assessment specially for MSME, lack of that products which attracts lenders ,usually it takes a lot of time consuming for granting loan.

impediments to credit – It works as middle men processor ,as stated the credit gap for MSME has increased which lead to expanding of formal financing . Also digital lenders definitely have upper hand in traditional banking as because of absence old financial data , new age lender use differentiated credit under writ model to avail creditworthiness of borrower . it is also been estimated that digital lending model have capability to deliver 30-40%over traditional model.

Different type of loans such as business loan and MSME loan for meeting variety of expenses (working capital for day to day funding).

Term loans is for big enterprises , a large amount of money is required for establishing big project huge sum of money is required .Purchase finance offers power to use and provide exactly at that particularly time or point of need for business .Merchant cash advance mainly for attaining receivable.

As India is biggest market for business sphere ,so entities are attempting to penetrate into providing feature that can serve large number of people .

What guidelines are about

1.”third party involvement as central bank have clearly stated that RBI-regulated entities , their LSP, digital lending apps , that all loans need to be clear between bank account holder and RE only “.

2.” Its been clearly stated that digital lending entities and no borrower should pay fees and charges

payable to LSPS in credit intermediation process”.

3.”Credit limit and publishment of list ascertains that borrower on record explicit consent is most important and the entities need to publish list of LSP and DLA indulged in whole process” .

4.”colling off period should be given in with drawl of loan in span of loan contract in which option should be given to exit the digital loan and also by offering proportionate with penalty” .

Industry concerns

The guidelines provided tries to fill the gap highlighted above however on implementation and ground basis a lot have to be categorises .

1. First loss default guarantee :FLDG is basically an arrangement among Fin tech and RE where RE and if issues loan then the Fin tech take responsibility to compensate RE to take responsibility to certain rate if the borrower default in repayment .The most important requisite is that it is always given at pre –decided rate . FLDG works on model of covering motivated RE which offers loan which was previously put in bank in difficult spot at time of recovery and as fact says that 10 %loans are not being repaid .I always represent the guidelines would accept FLDG to follow the provision stated by RBI Mater Direction Of Securitisation Of Standard asset .Although this has not been in FAQs also ,as LSPs are waiting for more description As booming market it gives passage to explore more so that the link can be joined between Fin tech and RE .
2. Buy Now Pay Later Apps :Earlier to issue of guidelines RBI rules on prepaid payment instrument and credit lines (June 2022) non bank PPI was banned . credit lines works on preapproved borrowing limit . Due to banning of BNPC platform was surely affected as whole system was stagnant after sanction of RBI ,company shifted to first model as ne model require loan to be approved and consequently whole process changed. New change of BNPL platform was introduced pass through of loan disbursement which also lead several companies to shutdown.

Indian legal regime

India being a huge country with people full of different opinion and thought process for lending activity there are several laws to regulate the lending activity .

1. Banking regulation (BR)act 1949 :The legislation is applicable to all banking firms in India, come into force in 1949 and implemented in 2020 .All cooperative bank comes

under ambit of RBI additionally small finance bank ,rural ,have also to also fall under this ambit as instructed by RBI guidelines .it also allow lending loan in form of online mode or otherwise as mentioned in sec5(b)of BR act.

2. RBI act 1934 : Apart from bank ,NBFCs also have to comply with RBI act of being registered .NBFC is defined as entity registered in company act 1956/2013 whose mainstream is issuing loan/bond/stock.

Some exemptions are also there as alternative invest fund company /stock exchange/stock broking company and chit funds act.

3. Company act 2013: there are certain rules which need to be comply as according to RBI and lending activity subject to applicable provision of company act 2013 .Sec186 of company act 2013 clearly state restriction on loan amount and minimum internet rate .
4. State money lenders act : The state has power to legislate on matter related to lending .Usually state government appoint registrar general as it is state matter so different state have different provision .
5. Chit funds act 1982: this act maintain chit funds and work as barrier from pre sanction from state government .In this certain amount from time to time is submit into fund .it mainly includes instalment of money and at the end every member got amount turn wise .

RBI working group recommendation on digital lending

“Working group was established by RBI in 2021 as the recommendation given was to maintain privacy of system against entities ,standard protocol is provided to maintain customer ,suitability, protection of data .approach was adopted in 3 principle .

:technological neutrality

:principle backed regulation

:addressing regulatory arbitrage

For achieving these working groups have given three measures on near to medium term”.

A. legal and regulating recommendation

“Near term (up to one year) –establishment of nodal agency to verify technological setup and also to maintain public register of apps appeared on website . loan servicing should be directly transfer to bank account of balance sheet however borrower with only PPI account

and no bank account can disburse loan if PPI act are fully KYC compliant” .

“Medium term (above one year): Central government is planning to bring legislation for preventing illegal lending activity by introducing banning of unregulated lending activity act . it is been recommended that RBI should make different framework as agency financial service regulation for outsourced activity including LSPs” .

- B. Recommendation related to technology Near term : compliance with baseline technology is required and publically availability policy should be there by DLA .data should be stored in servers located in Indi itself Medium term :comprehensive regulatory framework should be there for fin tech and tech fins .

Algorithms used should be there auditable and should be made ethical in AI design

- C. Recommendation related to financial consumer protection near term –presentation of fact statement in manner should be provided ,unsolicited commercial communication should be governed by code of conduct .

medium term –anti predatory lending policy should be framed based on character to be defined by RBI.

The reasons why digital lending is becoming more popular

Digital lending satisfies the customers experience: For customer who don't use digital loan system for them offline loan system is really slow and complicated process, less transparent and very less predictable. According to survey conducted by many researches 44 per cent of the customers aren't satisfied with long waiting for credit decision and 43 per cent stated the problem related with complexity of filing a application. Whereas, digital lenders performed well on both counts, with only 15 per cent complaining about long waits and 22 per cent for difficult application process. Digital lending gives them for satisfaction and saves their valuable time.

It increases margin of managing loan: The operating margin percentage of bank is nearly around 5 per cent where they use traditional process, where as its 2 per cent less at non banking institutions. Technology can reduce the duration of banks for writing underwrite loans due to this more loans can be offered. Customers can receive loan approval more smoothly. The American

Bankers Association stated that digital lending in its recent reports that offering financial institutions can improve productivity, close more loans, and importantly increases revenue per loan with cheaper and faster manner. Digital lending is increasing as a business too. Report researches in India stated that the value of digital lending business in the country will exceed 1 trillion USD over the time of 5 years.

RESULTS AND DISCUSSION

The traditional banking system has been inaccessible to many individuals and organisations due to its boring procedures and rules in lending of credit. The digital lending improves financial inclusion by providing access to credit opportunities to those individual and institutions that are out of the traditional banking system due to various reasons like lack of credit scores, collateral, poor past performance etc. Financial inclusion is one of the growing objective of government which could help in the problem of poverty and inequality. The Pradhan Mantri Jan Dhan Yojana (PMJDY) was launched in August 2014 with the objective of providing financial help and services at reasonable cost to the unbanked, unsecured. It is not national approach towards financial inclusion. The no of PMJDY accounts increased at a remarkable rate from 14 crore in March 2015 to 46 crore in August 2022 with a balance of Rs 1,73,954 crore. With the help of Rupay debit cards and mobile based payment systems in digital transaction have reached the milestone of 978 crore in 2016-17 to 7.195 crore during 2021-22. The UPI transaction facilitator have increased transactions from 1.79 crore to 4,596 crore and card transactions and e-commerce increased from 28.29 crore to 151 crore during the same duration of time. Such steps by government are expected to bring the poverty into the system of financial system to save them from exploitation from informal lenders.