

Regulatory Update on RBI's Consolidated Digital Lending Framework – May 2025

The Reserve Bank of India (RBI) has issued comprehensive and consolidated guidelines titled *Reserve Bank of India (Digital Lending) Directions, 2025* vide circular RBI/2025-26/36 dated May 8, 2025¹. These Directions supersede and replace earlier regulations including:

- The Guidelines on Digital Lending dated September 2, 2022 [RBI/2022-23/111/DOR.CRE.REC.66/21.07.001/2022-23], and
- The Guidelines on Default Loss Guarantee (DLG) dated June 8, 2023 [RBI/2023-24/41/DOR.CRE.REC.21/21.07.001/2023-24].

These new Directions aim to consolidate the digital lending framework while introducing important clarifications and refinements that strengthen customer protection, transparency, data privacy, and governance of Lending Service Providers (LSPs).

Background

The RBI had constituted a Working Group on Digital Lending in 2021 to address growing concerns around unregulated digital lending practices, mis-selling, data misuse, and recovery malpractices. Based on its recommendations, the initial guidelines were rolled out in 2022 and 2023, covering key areas such as outsourcing standards, transparency through Key Fact Statements (KFS), and loss-sharing arrangements (DLG/FLDG).

ELP had issued a detailed Booklet² on Digital Lending Guidelines in India, providing structured analysis and compliance guidance based on those earlier frameworks.

Key Highlights of the 2025 Directions

- **Unified Framework:** The 2025 Directions integrate and replace multiple past guidelines, ensuring regulatory clarity and reducing overlaps.
- **Expanded Definitions & Coverage:** Clearer definitions for *Digital Lending*, *Lending Service Providers (LSPs)*, *Digital Lending Apps (DLAs)*, and *Default Loss Guarantee (DLG)* have been included. Coverage now includes multi-lender LSP arrangements and improved DLA oversight.
- **DLG (Default Loss Guarantee) Provisions Rationalized** DLG permitted only up to 5% of the loan portfolio. It must be backed by legally enforceable contracts. **DLG** could be in cash, fixed deposits (with lien), or bank guarantees. DLG cannot result in synthetic securitisation or loan participation.
- **Cooling-off Period:** Borrowers are allowed to exit digital loans without penalty during a minimum look-up period of 3 days (for loans > 7 days) or 1 day (for short-tenure loans).
- **Loan Disbursal & Servicing Rules:** Loan disbursal must be directly into the borrower's account. All repayments must be made into the RE's account only. No pass-through of borrower funds via LSPs is permitted except in cases where it occurs by way of recovery of defaulted loans.
- **Mandatory Disclosures & Digital Document Delivery:** Regulated Entities (REs) must issue digitally signed documents to borrowers.
- Enhanced disclosure norms under the KFS and APR guidelines are reinforced.

¹ <https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12848&Mode=0>

² <https://elplaw.in/leadership/indias-road-map-for-digital-lending-action-points-for-the-lenders/>

- Grievance Redressal: A robust grievance redressal mechanism with designated nodal officers is mandated for REs and LSPs. Links to RBI's CMS and Sachet Portals are to be displayed prominently.
- Implementation Timeline:
 - Para 17 (directory of DLAs): Effective from June 15, 2025
 - Para 6 (multi-lender LSP arrangements): Effective from November 1, 2025

Summary of the Guidelines

Aspect	RBI Digital Lending Directions, 2025 (Effective May 8, 2025)
Definition of DLG	A contractual arrangement between a Regulated Entity (RE) and a third party (usually an LSP) to compensate the RE for credit losses up to a pre-agreed percentage of a specified loan portfolio, whether explicit or implicit.
Eligibility to Offer DLG	DLG may only be provided by: <ul style="list-style-type: none"> ▪ A Lending Service Provider (LSP), or ▪ Another RE, subject to: <ul style="list-style-type: none"> - valid outsourcing arrangement between the RE and LSP - LSP is a company incorporated under the Companies Act, 2013.
Permissible Forms	DLG must be backed by one or more of the following: <ul style="list-style-type: none"> ▪ Cash deposit with the RE ▪ Fixed Deposit with lien in favour of the RE ▪ Bank Guarantee in favour of the RE.
Cap on DLG Exposure	The DLG cap remains 5% of the total loan portfolio covered under the arrangement. This includes explicit or implicit support linked to portfolio performance.
NPA Recognition	Individual loans must be classified as NPA by the RE based on prudential norms. Invocation of DLG does not alter NPA status or provisioning requirements for individual loans.
Regulatory Capital Treatment	No capital relief on loans covered under DLG. The DLG does not qualify as Credit Risk Mitigation (CRM). Capital adequacy is governed by extant capital computation norms.
Invocation Timeline	DLG must be invoked by the RE within 120 days of default, unless the borrower cures the default.
Tenor of DLG Arrangement	The DLG arrangement must remain valid for not less than the longest tenor of the loans within the covered portfolio.
Disclosure Requirements	Extensive disclosure obligations apply to ensure borrower awareness and regulatory transparency. These include listing DLG arrangements and the parties involved, and recording them appropriately.
Restrictions	Synthetic securitisation and structured credit risk transfer mechanisms remain prohibited. The DLG must not result in indirect loan participation or violate asset transfer norms.

ELP Booklet on the Topic³

ELP's previously published Booklet on Digital Lending Guidelines in India comprehensively addressed the regulatory landscape under the 2022 and 2023 RBI circulars. While those circulars now stand repealed, the foundational insights, definitional clarity, and compliance structure outlined in the booklet continue to remain relevant for understanding the transition and ongoing regulatory expectations. A revised edition incorporating the 2025 framework will follow shortly.

We trust you will find this an interesting read. For any queries or comments on this update, please feel free to contact us at insights@elp-in.com or write to our authors:

Mukesh Chand, Senior Counsel – Email – mukeshchand@elp-in.com

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³ Ibid