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Digital Capital Raising

(Person-to-person lending, equity crowdfunding)

India

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Relevant Regulations

1. Credit
2. Investments
3. Data protection
4. Consumer protection
5. AML / KYC
6. Competition
7. Taxation

The Cambridge Centre for Alternative Finance (CCAF) and BFA Global have produced this deck to support fintech startups working in India and those seeking to enter the Indian fintech market in navigating the regulatory environment.

This deck provides **an overview of India's regulation of digital capital raising** which includes **equity crowdfunding and P2P lending**.

Each slide in this deck provides high-level facts about each of the relevant regulations as well as a link to the original source. Not all regulations included in the deck may be relevant based on the nuances of your particular business model.



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01 — Credit



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Credit: NBFCs

- In India, only a bank or a non-banking financial company (NBFC) is allowed to develop a credit business.
- NBFCs are categorized into 8 types based on:
 - the type of liabilities as Deposit and Non-Deposit accepting NBFCs,
 - the kind of the activity they conduct, and
 - for non deposit taking NBFCs, by their size into systemically important and other non-deposit holding companies (NBFC-NDSI and NBFC-ND).
- The categorization of fintech firms is generally dependent on the products and services they offer, and fintechs should apply for a NBFC license under their relevant category. For example, fintech firms that provide either digital lending products or vehicle and consumer loans fall into the NBFC - Investment and Credit Company (NBFC-ICC) category. Other options include NBFC-P2P (as a peer-to-peer lender), NBFC-MFI (microfinance institution) or a general NBFC entity.

Broad Categorization	Features
NBFC - Investment and Credit Company (NBFC-ICC)	<p>Includes Asset Finance companies (AFC), Investment Companies (IC) and Loan Companies (LC).</p> <ul style="list-style-type: none"> • AFC is an institution that finances physical assets supporting productive/economic activity, such as automobiles, tractors, lathe machines, generator sets, earth moving and material handling equipment, and moving on own power and general-purpose industrial machines. These businesses' principal purpose is aggregate financing of real/physical assets supporting economic activity. Income from this lending must not exceed 60% of its total assets and total income respectively. • IC is a financial institution whose principal business is the acquisition of securities. • LC is a financial institution that provides financing by making loans or advances or otherwise for any activity other than its own but does not include an AFC. <p>A deposit taking NBFC-ICC shall invest in unquoted shares of another company which is not a subsidiary company or a company in the same group of the NBFC an amount not exceeding 20% of its owned fund.</p>

Credit: NBFCs (cont.)



Broad Categorization	Features
Systemically Important Core Investment Company (CIC-ND-SI)	<p>CIC-ND-SI is an NBFC whose business is the acquisition of shares and securities that satisfies the following conditions:</p> <ol style="list-style-type: none"> 1. it holds at least 90% of its total assets in the form of investment in equity shares, preference shares, debt, or loans in group companies; 2. its investments in equity shares (including instruments compulsorily convertible into equity shares within a period not exceeding 10 years from the date of issue) in group companies constitutes at least 60% of its total assets; 3. it does not trade its investments in shares, debt, or loans in group companies except through block sale for the purpose of dilution or disinvestment; 4. it does not conduct other financial activity referred to in Section 45I(c) and 45I(f) of the RBI act, 1934 except investment in bank deposits, money market instruments, government securities, and loans to and investments in debt issuances of group companies or guarantees issued on behalf of group companies; 5. its asset size is INR 1 billion (US\$14 million) or above; and 6. it accepts public funding
Infrastructure Debt Fund Non-Banking Financial Company (IDF-NBFC)	<p>IDF-NBFC is a company registered as a NBFC to facilitate the flow of long-term debt into infrastructure projects. IDF-NBFC raise resources through issue of Rupee or Dollar denominated bonds of minimum 5-year maturity. Only Infrastructure Finance Companies (IFC) can sponsor IDF-NBFCs</p>
Infrastructure Finance Company (IFC)	<p>IFC is a non-banking finance company a) which deploys at least 75% of its total assets in infrastructure loans, b) has a minimum Net Owned Funds of INR 3 billion (US\$41.4 million), c) has a minimum credit rating of 'A' or equivalent d) and a CRAR of 15%.</p>

Credit: NBFCs (cont.)



Broad Categorization	Features
Non-Banking Financial Company-Micro Finance Institution (NBFC-MFI)	<p>NBFC-MFI is a non-deposit taking NBFC with at least 85% of its assets meeting the following qualifying criteria:</p> <ul style="list-style-type: none"> a. loan disbursed by an NBFC-MFI to a borrower with a rural household annual income not exceeding INR 1,000,000 (US\$1,381) or urban and semi-urban household income not exceeding INR 1,600,000 (US\$2,209); b. loan amount does not exceed INR 50,000 (US\$138.1) in the first cycle and INR 1,000,000 (US\$1,381) in subsequent cycles; c. total indebtedness of the borrower does not exceed INR 1,000,000 (US\$1,381); d. tenure of the loan is not less than 24 months for loan amount in excess of INR 15,000 (US\$201.75) and allows prepayment without penalty; e. loan is extended without collateral; f. aggregate amount of loans, given for income generation, is not less than 50% of the total loans given by the NBFC-MFIs; and g. loan is repayable in weekly, fortnightly, or monthly installments at the choice of the borrower.
Non-Banking Financial Company-Factors (NBFC-Factor)	<p>NBFC-Factor is a non-deposit taking NBFC engaged in the principal business of factoring. The financial assets in the factoring business should constitute at least 50% of its total assets and its income derived from factoring business should not be less than 50% of its gross income.</p>
Mortgage Guarantee Companies (MGC)	<p>MGC is a financial institution for which at least 90% of the business turnover is mortgage guarantee business or at least 90% of the gross income is from mortgage guarantee business and net owned fund is INR 100 crore (US\$13,500,000).</p>
NBFC-Non-Operative Financial Holding Company (NOFHC)	<p>NBFC-NOFHC is a financial institution through which promoter or promoter groups are permitted to set up a new bank. It's a wholly-owned Non-Operative Financial Holding Company (NOFHC) which holds the bank and all other financial services companies liable to regulations promulgated by the RBI and other financial sector regulators to the extent permissible under the applicable regulatory prescriptions</p>

Credit: NBFC licensing

- NBFCs are required to register with the RBI before commencing operations.
- In order to successfully register, the applicant must:
 - be registered as a company under Section 7 of the Companies Act, 2013 or 1956 (as amended)
 - engage in the activities described on the [FAQ page](#) of the RBI website
 - have minimum net owned funds of INR 20 million (US\$0.28 million)
 - meet the RBI's 'Asset-Income Test', i.e. NBFC's financial assets (such as loans and equity investments) constitute more than 50% of its total assets and income from financial assets constitute more than 50% of its gross income.
- The regulatory approval timelines to apply for different types of NBFC licenses depend on the business activity as set out [here](#).

Exemption

NBFCs can commence business without obtaining a certificate of registration and are not required to meet these requirements if the given NBFCs are regulated by other regulators. For example, Venture Capital Funds/Merchant Banking companies/Stock broking companies registered with SEBI, Insurance Companies holding a valid Certificate of Registration issued by IRDA.

Credit: Digital credit

- All digital lenders must be registered as a bank/NBFC or have a partnership arrangement with an existing bank or NBFC to initiate digital lending activity.
- Due to increased activity in credit intermediation through these digital models, the RBI issued a circular in June 2020 detailing the directions and circulars that digital lending platforms that partner with the concerned NBFCs/Banks must follow. In December 2020, the RBI released a Press Release cautioning the public about unauthorized digital lending platforms in the market. The RBI clarified that legitimate public lending activities could only be undertaken by banks and NBFCs registered with the RBI.
- The RBI set up a Working Group (WG) in January 2021. The objective of the WG is to create a comprehensive framework on digital lending in India to protect consumers from illegal lending and regulate credit intermediation through the digital lenders in the country.

Digital Lending Models in India

- Digital loan platforms by Banks or NBFCs
- Digital lending marketplaces (under the partnership model or as a peer-to-peer lender)
- Buy Now, Pay Later
- Small and Medium Enterprise Financing
- Supply Chain Financing

Credit: P2P lending



Key regulation:

The Master Directions – NBFC – Peer to Peer Lending Platform Directions, 2017 provide a framework for the registration and operation of NBFCs in India that operate a peer-to-peer lending platform. These platforms can also undertake activities relating to debt crowdfunding.

Licensing process:

- An NBFC-P2P requires a Certificate of Registration from the RBI (Section 5)
- It must have a net owned fund greater than INR 20 Million (US\$276,260.20) .
- Registration is required by filling out this [form](#).
- The RBI created a [webpage](#) to help new entrants navigate the registration requirements and document checklists to facilitate registration and commencement of business

Capped exposures:

- The P2P Directions cap the aggregate exposure of a lender to all borrowers across all P2P platforms to INR 5 Million (US\$69,020).
- The exposure of a single lender to the same borrower across all P2P platforms is capped at INR 50,000 (US\$691).
- Aggregate loan taken by a borrower at any point of time, across all P2Ps is also subject to a cap of INR 1 Million (US\$13,804). Additionally, the maturity of loans provided must not exceed 36 months.

Credit: Microfinance banks and businesses

Key regulation:

Non-Banking Financial Company-Micro Finance Institutions (Reserve Bank) Directions, 2011.

NBFC Framework:

Microfinance institutions are categorized as a non-deposit-taking NBFC and are regulated as NBFC-MFIs.

The Directions provide for certain eligibility criteria for the NBFC to enter the Microfinance business (Section 1) and provide requirements for the loans disbursed by the MFI (Section 1).

Trusts/Co-ops:

Microfinance institutions that take the form of a trust or co-operative society are not specifically governed by the RBI but by the respective State or provincial Registrar of cooperatives societies or the underlying regulating authority, with which the trust or co-operative society is registered.

Small finance banks

As an extension to the provision of microfinance and low-cost, small-sized loans, the RBI has allowed for 'on tap' licensing of Small Finance Banks that provide savings opportunities to the underserved and supply credit to small business units, marginal farmers, and micro and small industries. These banks provide these services through high technology and low-cost operations.

Further details regarding eligibility criteria and application procedures can be found in the [Guidelines](#) for 'on tap' Licensing of Small Finance Banks in the Private Sector

Credit: Credit Bureaus

- Credit Reference Bureaus also known as Credit Information Companies (CIC) are governed by **Credit Information Companies (Regulation) Act, 2005** (CICRA) and the **Credit Information Companies Regulation, 2006**.
- Entering the credit information business requires registration and approval from the RBI. The Regulations provide for the process of registration and the requisite forms that are needed to be filled can be found on Section 4 of the Regulations.
- The Regulations also describe privacy principles that the CICs are required to follow while collecting and working with the personal data as well as the accountability of CICs when conducting their business (Section 17 of the Regulations).
- Per Section 15 of the CICRA, every credit institution must become member of at least one CIC. Section 17 of CICRA stipulates that a CIC may seek and obtain credit information from its members (Credit Institution/CIC) only.
- In 2015, the RBI set up a committee to recommend the data format for furnishing credit information to CICs. After receiving the report, it issued a Directive mandating all credit Institutions to become members of all CICs.

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02 — Investment



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Investment: Licensing process & sandboxes

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Key regulation: Securities and Exchange Board of India Act, 1992

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Main regulator: The Securities and Exchange Board of India (SEBI)

—
Licensing process*:

There are separate registrations required for each type of investment activity:

- SEBI (Investment Advisers) Regulations, 2013 regulate Investment Advisers and SEBI (Alternative Investment Funds) Regulations, 2012 regulate various types of Investment Funds
- The Depositories Act, 1996 provides for regulation of depositories in securities. It mandates all depositories to obtain a Certificate of Registration from SEBI before commencing business. The SEBI (Depositories and Participants) Regulations, 2018 created the requisite form along with associated fees.

—
Sandboxes:

- SEBI created the Innovation Sandbox Framework to enable fintech firms and entities not regulated by the SEBI to conduct 'offline testing' of their products or services based on market data provided by stock exchanges, depositories, and qualified registrars and share transfer agents.
- SEBI developed the Regulatory Sandbox Framework which permits entities regulated by SEBI to experiment with fintech solutions in a live environment and on a limited set of real customers for a fixed time frame.

*Foreign investment must additionally comply with the requirement of investment under the Foreign Exchange Management Act, 1999 and the annual consolidated Foreign Direct Investment Policy Circular issued by the Department for Promotion of Industry and Internal Trade

Investment: Wealthtech & InvestTech

SEBI issued the following guidelines and regulations to regulate the wealthtech/InvestTech platforms and activities:

- The SEBI Broad Guidelines on Algorithmic Trading, 2012 and SEBI Broad Guidelines on Algorithmic Trading for National Commodity Derivatives Exchanges, 2016 permit stockbrokers to provide **algorithmic trading** with the prior permission of the stock exchange. Stockbrokers must have risk controls and proper systems to carry out algorithmic trading in compliance with the guidelines.
- SEBI Investment Advisor Regulations, 2013 mandate all entities/individuals providing **robo-advisory services** get registered as an investment advisor
- **Equity crowdfunding** remains to prohibited in India (See next slide).



Investment: P2P equity crowdfunding

Different types of crowdfunding are regulated under different regulations:

- A consultation paper on crowdfunding was released by SEBI in 2014 which proposed a regulatory framework for governing **security-based crowdfunding** methods for startups and MSMEs. However, SEBI did not subsequently release any guidelines. Therefore, equity crowdfunding remains prohibited in India.
- The other recognized forms of crowdfunding that are permitted in India are **donation/social-based lending** crowdfunding, **pre-order** crowdfunding, **reward-based** crowdfunding, and **debt-based** crowdfunding as P2P lending (see section on 5.3 on Credit)
- Additionally, **pooled managed investment funds** are currently regulated under the SEBI (Alternative Investment Funds) Regulations, 2012 (as amended)



Investment: Virtual and crypto assets

Crypto assets trading and currency usage is not systematically regulated in India and the regulatory status is unclear:

- In April 2018, the RBI promulgated a circular prohibiting all entities regulated by RBI to provide services to entities involved in trading virtual currencies. However, in March 2020, the Supreme Court of India declared the circular to be constitutionally invalid.
- The central government plan to introduce the Cryptocurrency and Regulation of Official Digital Currency Bill, 2021, whose purpose is to create a framework to facilitate an official digital currency issued by the RBI and to “prohibit all private cryptocurrencies in India”.
- According to a notification released by the Ministry of Corporate Affairs (MCA), every company that has participated in cryptocurrency transactions will have to disclose the following facts from financial year 2021-2022: (a) Cryptocurrency holdings by the date of the financial statements, (b) The total profit or loss on transactions involving these crypto or virtual currencies, (c) Deposits or advances received from any person for the purpose of trading or investing in these currencies



03 — Data protection



Data protection: National provisions

Key Laws:

Information Technology Act, 2000 ("IT Act") and its corresponding Information Technology (Reasonable Security Practices and Procedures and Sensitive Personal Data or Information) Rules, 2011 ("IT Rules"), and the Indian Constitution

Main provisions:

India does not currently have national legislation governing data protection or privacy. Therefore, regulation is fragmented:

- Personal data is recognized as a fundamental right under Article 21 of the **Indian Constitution**, as ruled by the Supreme Court of India.
- The **IT Act** provides legal recognition of transactions carried out via electronic data interchange and other means of electronic communication.
- Section 43A of the IT Act confers liability on companies which possesses, deals, or handles any sensitive personal data in a computer for any wrongful loss or gain to any person caused due to negligence in implementing and maintaining reasonable data security practices and procedures
- Section 72A of the IT Act states that if any person secures access to personal information while providing contractual services and discloses the data without the consent of the concerned person(s) to any other person shall be punished with a fine and/or imprisonment.
- IT Rules provides individuals with the right to access and correct their information on online platforms. It also mandates that any company collecting sensitive personal information publishes an online privacy policy to which users must agree. Companies must obtain consent of the individual before disclosing sensitive personal information except in the case of law enforcement.
- A comprehensive data protection law - the Personal Data Protection Bill 2019 is currently pending before Parliament

Data protection: Sectoral provisions

The primary legal instruments that address data protection in the financial sector include:

Credit:

- The Credit Information Companies (Regulation) Act, 2005 (CIC Act) and the Credit Information Companies Regulation, 2006 (CIC Regulations) recognize credit information companies (CICs) as collectors of information and requires they adhere to privacy principles at the collection stage and uphold those principles during use and disclosure of credit information. CICs are further required to ensure the credit information they hold is accurate, complete, and protected against loss or unauthorized use, access, and disclosure.

KYC data:

- KYC norms limit the categories of information that banks and financial institutions can seek from their customers. Once such information is collected, there is an obligation on banks to keep it confidential. Any such information collected must not be divulged by the regulated entities under the RBI's purview for the purpose of cross-selling or for any other purpose without the explicit permission of the customer.
- There are similar regulations such as the Master Circular on Credit Card, Debit Card and Rupee Denominated Co-branded Prepaid Card Operations of Banks and Credit Card issuing NBFCs, the Master Circular on Customer Services, 2009, and the Code of Banks Commitment to Customers etc. These create restrictions on the cross-selling of information and impose customer confidentiality obligations

Sources: [The Credit Information Companies \(Regulation\) Act, 2005](#), [the Credit Information Companies Regulation, 2006](#), [Master Direction - Know Your Customer \(KYC\) Direction, 2016](#), [Master Circular on Credit Card, Debit Card and Rupee Denominated Co-branded Prepaid Card Operations of Banks and Credit Card issuing NBFCs](#), [the Master Circular on Customer Services, 2009](#), [the Code of Banks Commitment to Customers](#)

Data protection: Sectoral provisions (cont.)

Insurance:

- In the Insurance sector, Insurance Act, 1938 and regulations issued thereunder by the IRDAI, such as IRDAI (Maintenance of Insurance Records) Regulations, 2015, IRDAI (Health Insurance Regulations), 2016, IRDAI (Protection of Policyholders' Interests) Regulations, 2017, and IRDAI (Outsourcing of Activities by Indian Insurers) Regulations, 2017 impose confidentiality provisions.
- Intermediaries in the insurance sector such as corporate agents, third party administrators (TPAs), and web aggregators serve as a bridge between customers and insurance companies by facilitating the process of purchasing insurance products and assisting in the servicing of policies and assessment of claims. These intermediaries also bear confidential information and thus are subject to obligations relating to data protection and preservation of confidentiality, as prescribed by the IRDAI. Each type of intermediary is subject to its own regulations and Code of Conduct. With relation to TPAs, the IRDAI (Third Party Administrators – Health Services) Regulations, 2016 prohibits TPAs from sharing the data and personal information of customers they receive from servicing insurance policies or claims.

A [report](#) by the Ministry of Electronics and Information Technology has mapped the various financial sector laws that contain data protection provisions.

Data protection: Data localization & cybersecurity

Data localization:

As there is no comprehensive framework, data localization requirements can be found in sectoral regulations on data protection:

- Per India's 2013 Companies Act, Indian registered companies must maintain their books of account for audit and inspection only in India.
- The IRDAI mandates that all original policyholder records be maintained in India.
- On April 6, 2018, the RBI issued a circular titled Storage of Payment System Data, which mandated that all payment system providers store their payment systems data on servers located within the territorial jurisdiction of India. However, for the foreign leg of the transaction, it is permitted to store the data in the foreign country, if required.

Cybersecurity:

- The RBI, under the Guidelines on Regulation of Payment Aggregators and Payment Gateways, provides comprehensive baseline technology recommendations for Payment Gateways.
- The SEBI released Master Circulars on creating Cyber Security Resilience Framework for Stockbrokers and for Asset Management Companies.

Data sharing: Open banking

- Under India's Open Banking approach, customers control their data via NBFCs called Account Aggregators (AAs). AAs act as licensed intermediaries that are responsible for the customers' consent management and consolidate customers' financial information held with different financial entities and spread across financial sector regulators. AAs act as an intermediary between Financial Information Provider (FIP), such as banks, non-banking financial companies, insurance companies, insurance repositories, pension funds, etc., and Financial Information User (FIU), which are entities regulated by any financial sector regulator. The flow of information occurs through Application Programming Interfaces (APIs).
- The transfer of information requires explicit customer consent and with appropriate agreements/authorizations between the AAs, the customers, and the FIPs. Data cannot be stored by the AA or used by it for any other purpose. The regulations also set out explicit and robust data security and customer grievance redressal mechanisms. To protect customers' interest, the AAs are not permitted to undertake any other activity.
- Further, to facilitate seamless movement of data and consent-based sharing, a set of core technical specifications were framed in November 2019 by the Reserve Bank Information Technology Private Limited (ReBIT), a wholly owned subsidiary of the RBI, for adoption by all regulated entities acting either as FIPs or FIUs.
- To protect users' critical financial information and enforce a mechanism for obtaining proper consent from customers, AAs must obtain consent through a standardized electronic consent format as prescribed under regulations. AAs must inform the customer of all the necessary attributes contained in the consent format and the customer's rights to file complaints. Customers are able to revoke consent, following which a new consent would have to be obtained. Explicit onus has also been placed on FIPs to verify the validity of the consent, its specified date and usage, and the credentials of the AA.

04 — Consumer protection



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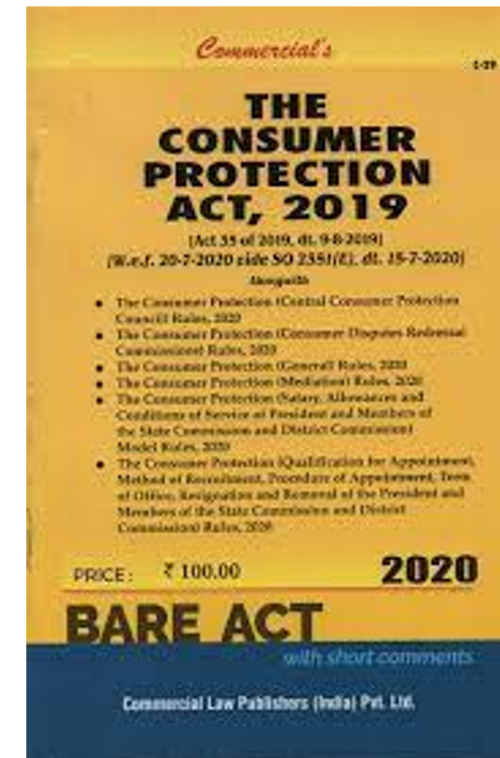
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Consumer protection: National provisions

Key Laws: Consumer Protection Act, 2019

Main provisions:

- The Consumer Protection Act provides for speedy redressal of all consumer complaints through designated consumer protection redressal forums at the District, State, and National levels.
- The Act vested wide-ranging powers with these redressal forums, starting from search, seizure, and summons to meet the needs of the changing times.
- The Consumer Protection Act also includes e-commerce platforms and electronic service providers under its purview to apply more accountability to online platforms and service providers.



Consumer protection: Sectoral provisions

Each financial sector regulator has issued its own consumer protection provisions:

RBI:

- The RBI has formulated a "Charter of Customer Rights" for banks based on global best practices around consumer protection. Banks are required to either prepare their own board-approved policy incorporating the five rights of the Charter or suitably integrate their existing customer service policy with the "Model Customer Rights Policy" formulated by Indian Banks' Association (IBA) / Banking Codes and Standards Boards of India (BCSBI).
- The RBI has three ombudsman schemes - one for banks, a second for NBFCs and a third for digital transactions. The RBI has suggested a potential new ombudsman scheme to unify these schemes to make the mechanism simpler, efficient, and more responsive.
- The ombudsman scheme for digital transaction is implemented by the RBI to enable a protection mechanism for digital payments service providers with relation to unauthorized electronic fund transfers (EFTs) and other digital transaction issues. The scheme contains detailed complaint procedures and a dispute resolution mechanism with a strict timeline for resolving issues. The Ombudsman can award monetary damages for any breach of regulations.

IRDAI:

- The IRDAI issued the IRDAI (Protection of Policyholders' Interests) Regulations, 2017 to ensure the interests of insurance policyholders are protected. Per Regulation 17, every insurer must have in place proper procedures and effective mechanisms to resolve complaints and grievances of policyholders and claimants efficiently and speedily.

Consumer protection: Sectoral provisions (cont.)



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SEBI:

- SEBI set up the Office of Investor Assistance and Education to protect the interests of investors. It issued SEBI (Aid for Legal Proceedings) Guidelines, 2009 to help investors raise complaints and the SEBI (Investor Protection and Education Fund) Regulations, 2009 whose funds are used to protect investors and promote investor education and awareness.
- SEBI also established online investor complaints redressal system called “SCORES” to address investor complaints against listed companies or regulated entities in the securities market.

Unified complaints forum:

- All the financial regulators, along with state and law enforcement authorities, created a single consumer awareness and complaints forum where consumers can lodge complaints against any illegal activity carried out by the offending entities.
- The forum can be accessed [here](#).

05 —

Anti-money laundering (AML)/know your customer (KYC)



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AML/KYC: Key laws & main provisions

Key Laws:

- Prevention of Money Laundering Act, 2002 (PMLA, as amended)
- PML (Maintenance of Records) Rules, 2005
- Aadhaar Act
- Master Direction - Know Your Customer (KYC) Direction, 2016

Master Direction KYC:

- Applies to all entities regulated by RBI.
- These directions lay out KYC guidelines (Sec. 5), Customer Identification procedures (Sec. 13 and 14), and Customer Due Diligence procedures (Chp. 6) for each type of customer.
- RBI's officially valid KYC documents include passports, permanent account number cards issued by income tax authorities, driving licenses, voter identity cards, and job cards issued under the rural employment guarantee scheme.

Digital KYC:

On February 25, 2016, RBI introduced “Digital KYC” mechanisms in Section 3 of its amended Master Direction on KYC.

- Digital KYC involves capturing a live photo of the customer and an officially valid document or the proof of possession of Aadhaar where offline verification cannot be completed.
- RBI has further introduced Video based Customer Identification Process (V-CIP) which involves a customer-consent requirement to undertake the Customer Identification Process (CIP).
- Digital KYC and V-CIP KYC is permitted for all entities regulated by RBI.

AML/KYC: Key laws & main provisions (cont.)

PML Rules:

- Lay out the procedure and manner of maintaining, and time for furnishing, information and verification of records of the client identity.
- Mandate record maintenance of and allow sectoral regulators to issue their own procedures for maintenance of records.

Aadhaar Act (EKYC):

- Aadhaar Act established the Unique Identification Authority of India (UIDAI), which manages the specific data collected about Indian citizens. The UIDAI permits the instant verification of biometric and demographic details of the holder through e-verification which is routed via the Aadhaar database (i.e., e-KYC).
- However, the Supreme Court's judgement in *Justice Puttaswamy (Retd.) v. Union of India* denied private entities access to the UIDAI server for e-verification of holder information for KYC. It also restricted the use of Aadhaar as a mandatory KYC document for a limited number of services and permitted banks' access to Aadhaar only with the consent of the holder.

- In collaboration with the industry, the UIDAI released new e-KYC systems to ensure smooth continuation of business. These include the use of XML files, masking of data, and use of QR codes. The accounts opened through these e-KYC mechanisms have certain restrictions on usage.

AML/KYC: Securities, outsourcing & confidentiality



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SEBI issued Guidelines on Anti-Money Laundering (AML) Standards and Combating the Financing of Terrorism (CFT)/ Obligations of Securities Market Intermediaries. This Master Circular requires all SEBI-registered entities have AML policies in place and lays out the manner and procedure to maintain records.

Outsourcing KYC

Banks, NBFCs, and other Regulated Entities (RE) may engage third parties for data collection for KYC purposes and rely on the third party's customer due diligence. However, REs are required to ensure that decision-making to determine compliance with KYC norms is not outsourced.

Confidentiality

There are Secrecy Obligations and restrictions on sharing KYC information (Section 56 of Master Directions). Information collected from customers for the purpose of opening an account is treated as confidential and related details cannot be divulged for the purpose of cross selling or for any other purpose without the express permission of the customer.

06 — Competition



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Competition: Relevant legislation & regulatory powers



Competition Act:

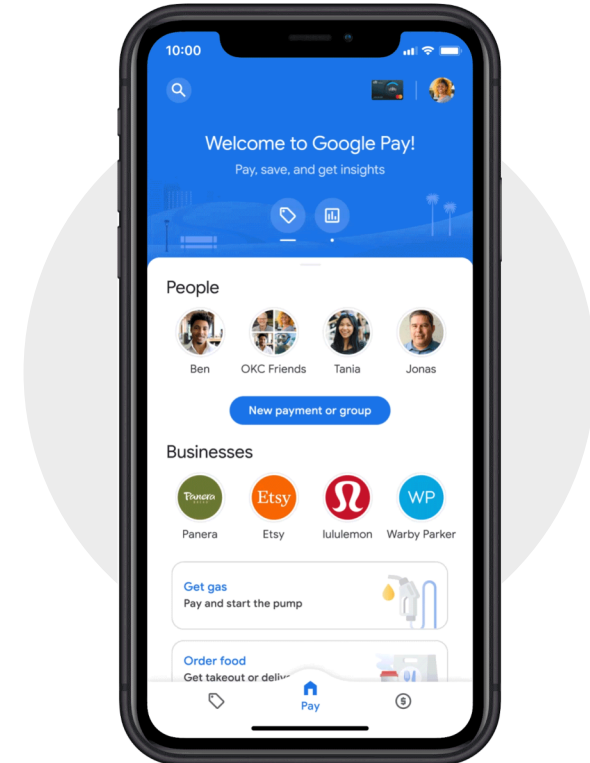
- The Competition Act, 2002 regulates various types of business activities.
- Section 3 of the Act prohibits vertical and horizontal anti-competitive agreements (e.g. between cartels) which causes or is likely to cause an appreciable adverse effect on competition (AAEC).
- Section 4 prohibits market players from abusing their “dominant position” by clearly prohibiting practices like predatory pricing that create a barrier to entry for new players.
- Section 5 regulates combination agreements (i.e. mergers or acquisitions) to prohibit them from hindering fair competition in the market.

Competition Commission of India:

- The Competition Act, 2002 establishes the Competition Commission of India (CCI). The CCI is responsible for eradicating anti-competitive practices, promoting and sustaining competition in markets, protecting consumers’ interests, and ensuring freedom of trade for other participants in markets (Section 18)
- Section 19 of the Act empowers the CCI to initiate an inquiry against a business organization for violation of Section 3 or 4.
- Section 19 also stipulates the factors the CCI will consider in determining if an arrangement or an activity causes an AAEC and if it should be deemed void.
- Section 20 empowers the CCI to initiate an inquiry against combination agreements for violations of Sections 5 and 6 and outlines the factors that must be considered to determine whether an agreement causes an AAEC in the market.

Competition: Focus on fintech

- The NPCI recently released a circular and Standard Operating Procedure mandating all Third-Party Application Providers such as Google Pay and PayPal to not exceed 30% of the overall volume of transactions processed in UPI payments.
- As recently as November 2020, the CCI ordered detailed investigation into Google Pay's activities for possible violations of Section 4 of the Competition Act.



07 — Taxation of financial services



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Taxation: Financial services

Tax incentives:

- The Start-up India initiative seeks to promote and incentivize startups by providing certain tax waivers for startups incorporated after 1 April 2016.
 - This includes a 100% tax rebate on profits for a total period of 3 years within a period of 10 years.
 - The tax incentive scheme has been extended until the end of the financial year 2022.
- A new section 54 EE was inserted in the Income Tax Act for eligible startups to exempt their tax on long-term capital gains within a period of six months from the date of transfer of the asset if such a long-term capital gain or a part thereof is invested in certain funds designated by Central Government as exemptible. To date the Central Government has not designated any funds as exemptible.
- There are tax rebates for merchants accepting more than 50% of their transactions digitally and for merchants providing cash back incentives to consumers for making payments of their GST Bills via prescribed digital modes.

Normal tax rate:

- If the given financial service does not fall within any exemption or promotion scheme of the Government of India, then it shall be subject to corporate tax regime under the Income Tax Act 1960.

For more information and further guidance on engaging with regulators see [Fintech Regulation in India](#)

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