INDIA’S DIGITAL ARCHITECTURE: FROM INFRASTRUCTURE TO SUPERSTRUCTURE

Relevant for: Developmental Issues | Topic: Issues relating to Growth & Development - Industry & Services Sector incl. MSMEs and PSUs

Factoring enablers and account aggregation can underpin our ecosystem for financial inclusion

Even as India’s asset monetization initiative—the National Monetisation Pipeline—justifiably garnered attention, two recent initiatives which are far more substantive did not get their fair share of it. One was the Factoring Bill amendments passed on 29 July. Moving the Bill in the Lok Sabha, the finance minister promised that thousands of non-banking financial companies (NBFCs) would now be able to buy receivables from Micro, Small and Medium Enterprises (MSMEs). She was not exaggerating. Earlier, the law stipulated that for an NBFC to engage in the factoring business, its: (i) financial assets in the factoring business and (ii) income from the factoring business should both be more than 50% (of gross assets/net income), or more than a threshold as notified by the Reserve Bank of India (RBI). The Bill removed this threshold for NBFCs to engage in this business (bit.ly/3h4EPuZ).

Then, on 3 September, the country announced the launch of its Account Aggregator platform. Eight banks said that they would be rolling it out. Account Aggregators (AAs) are ‘data access fiduciaries’ who act as the front end of its Data Empowerment and Protection Architecture (DEPA). Okay, let me explain this in English. All of us leave various trails of data when we use smartphones and public WiFi. We don’t think about it. But, financial data is different. It needs to be secure and should be accessed only with the consent of the user (data owner) and for purposes the user had consented to. That is what DEPA assures every Indian. It empowers you and I, the folks who generate data when we do any transaction using digital means. AAs are trustees of our data. They do not get to peer into its details. Nor can they use this data. With our consent, however, they can pass on data from financial information providers (FIPs) to financial information users (FIU).

If you are an individual or run a small business and are applying for a collateral-free loan, the lender might ask you to submit reams of documents to establish your credit worthiness. You have to download these from different sources (bank statements, insurance policies, mutual fund holdings, etc.) or give the lender access to the same. Now, upon your approval, AAs will do that. The data in their hands will be encrypted and can only be decrypted by FIUs. These are typically financial institutions.

What does account aggregation do? It fills an information gap efficiently, securely and conveniently. This is critical. Most of the time, risk-based lending does not happen because information is either unavailable or not easily retrievable, and hence lenders stick to collateral-based lending. Over time, as all parties get comfortable with the AA platform, that will change. Every formal financial transaction that we do online can be useful information in meeting our own future need for funding. In that sense, AAs can become agents of financial inclusion (pwc.to/38H52eE).

This has been in the making since 2016. It is another important milestone in the amazing digital transformation that the country is going through, most of which started with the PM Jan Dhan Yojana (PMJDY) and Aadhaar. In August, the National Association of Software and Service Companies (Nasscom) had brought out a report on India’s digital public goods. That they are public goods is very important. In the West, and in the US in particular, they are in private hands.

They have become veritable monopolies. They own, control, dictate and manipulate what information goes through the 'highway' that they have monopolized. In India, in contrast, "the Government emerging as an enabler of citizen-centric services is one of the key factors driving the rise of public digital platforms in India." Nasscom added that our digital platforms were developed at low cost, were inter-operable and had been adopted on a large scale. In another report, PwC India mentions that since its launch in April 2016, the Unified Payments Interface has taken the Indian payment ecosystem by storm (pwc.to/38H52eE). In its August bulletin, RBI notes that its Digital Payments Index rose 2.7 times in just three years after March 2018 (bit.ly/3zKDl0d).

It is also gratifying to note that the Goods and Services Tax Network has been given in-principle approval to become an FIP on the AA network. The GST network is such a huge repository of information that its being part of any data network is a big plus for MSMEs to access finance. Quietly, a lot of work has been done in the past seven years to empower and enable MSMEs.

Now, the GSTN and TReDS (Trade Receivables Discounting System) should shake hands and make it automatic that if a buyer accepts an invoice for claiming input tax credit, then the invoice shall be deemed accepted for TReDS purposes too. Further, if the GST Reverse Charge Mechanism were to be applied to MSME suppliers (which are too small to be paying GST), it could give the MSME sector a big boost.

After that, the only thing that would be pending is an amendment to India's MSME Act to allow MSMEs to retain their classification until both sales turnover and investment criteria are exceeded, rather than any one of them. That will serve as an enduring foundation on which a durable edifice of economic growth can be built.

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