

THIRD-PARTY SELL (TPS)

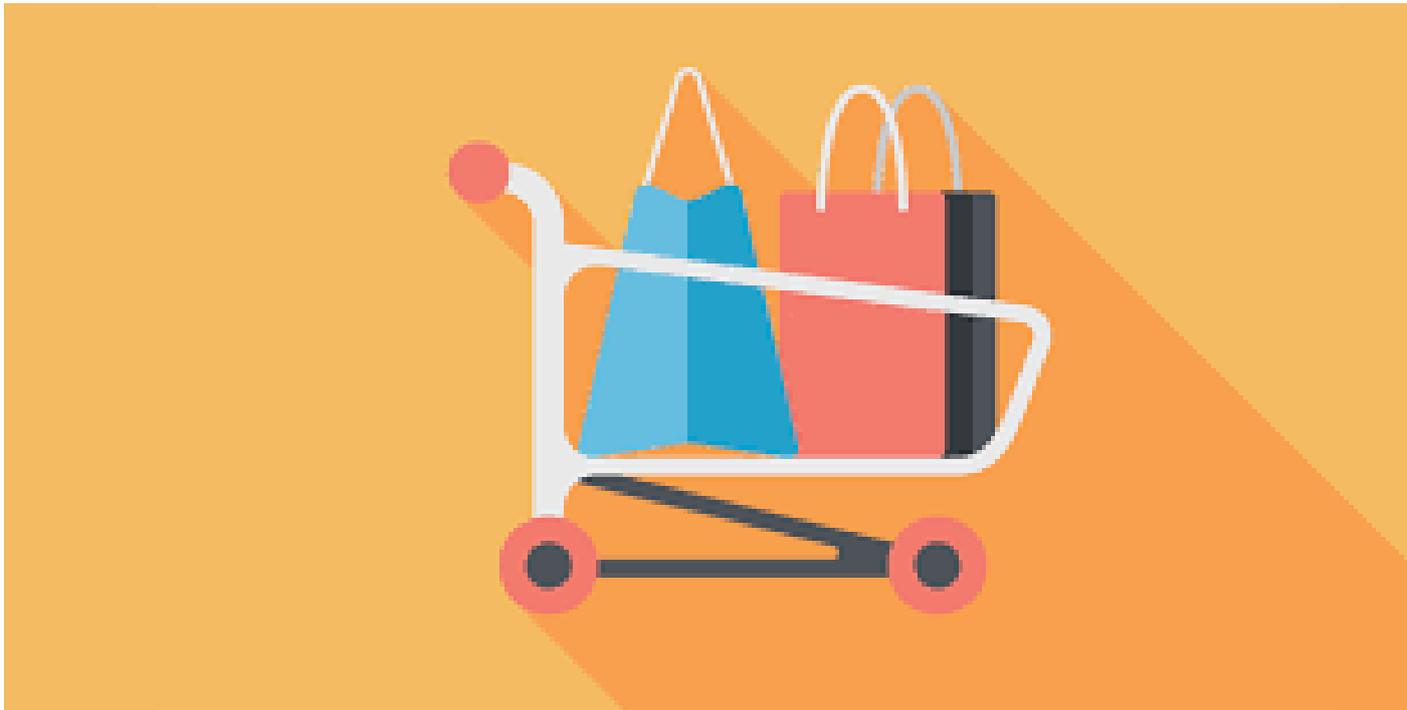


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1. Introduction

NBFC-MFIs, due to their strong connect with customers, have a fair understanding of customer's need for financial and non-financial products. Close customer-connect combined with last-mile connectivity of NBFC-MFIs, offer a powerful channel to facilitate provision of different products and services to low-income market segments.

Consequently, NBFC-MFIs in partnership with different types of providers such as Banks, Insurance Companies, NBFCs and Vendors of house-hold goods are increasingly capitalizing the micro-credit channel to meet demands of the customers beyond micro-credit. An internal review by MFIN on Third-party Sell (TPS) conducted in Oct 18 showed that half of our member NBFC-MFIs are offering TPS covering about 20% of their customer base. From the customer's perspective, there are benefits but instances of forced selling as well as several product quality issues were also documented.

As scale of TPS is increasingly growing, it is important to have defined policies and processes to do TPS in a manner which is beneficial to all the participants, particularly the customers. Many NBFC-MFIs offering products through TPS have already put in place several good practices and measures focusing on safeguarding customers interests. This Guidance Note is formulated building on the experience of NBFC-MFIs.

This note covers various aspects of TPS like selection of the right product and vendor, process vis a vis customer & third-party vendors and internal control. ***It may be noted that TPS, based on product, context and nature of contract between NBFC-MFI and third-party vendor can have significant variations and complexities. Hence, this Guidance Note rather than being too specific and prescriptive, gives broad common-sense principles and factors which should be considered by NBFC-MFIs while doing TPS.***

This Guidance Note can be used by NBFC-MFIs to frame and align their policies and practices on TPS to focus on customer interests.

For any clarification/suggestion, please feel free to connect with us. We also invite you to send us your feedback and suggestion to improve this Guidance Note. You can connect with us at sheetalprasad@mfinindia.org

2. Overview

2.1 TPS is defined as sale of physical product (such as water purifiers, consumer goods, mobile phones, solar products linked to micro-credit by NBFC-MFIs or directly without micro-credit) or financial products (such as opening of bank accounts, wallets, life and non-life insurance, pension etc) by NBFC-MFI where the NBFC-MFI partners with third-party vendor (s) to facilitate sale of such products to their customers.

2.2 In commonly prevailing model for non-financial products, NBFC-MFI partners with a third-party vendor and negotiates price/delivery mechanism/warranty/service contracts etc. NBFC-MFIs also have a commercial agreement outlining a margin fee per product and support for training/marketing etc. Micro-credit is also provided to the customers for purchase of third-party products (for non-financial products).

It may be noted that TPS (for non-financial products) is usually coupled with micro-credit by the NBFC-MFIs. For micro-credit part, NBFC-MFIs are required to follow regulatory and industry norms as required under RBI Directions for NBFC-MFIs, RBI Fair Practices Code, Industry Code of Conduct (CoC) and Compendium of MFIN Directive and Advisories.

2.3 A key requirement and challenge in TPS is to ensure that

- product offered is suitable to the customers and meets quality standards
- customer is fully and correctly informed
- customer is not forced to buy such products

2.4 This Guidance Note outlines the key principles for the NBFC-MFIs in TPS to ensure the above. This Guidance Note is organized around five sections as under:

- a. Selection of product/s
- b. Selection of vendor
- c. Factors vis a vis third-party vendor
- d. Factors vis a vis customer
- e. Internal controls

2.5 It may be noted that TPS (for non-financial products) is usually coupled with micro-credit by the NBFC-MFIs. For micro-credit part, NBFC-MFIs are required to follow regulatory and industry norms as required under RBI Directions for NBFC-MFIs, RBI Fair Practices Code, Industry Code of Conduct (CoC) and Compendium of MFIN Directive and Advisories. This Guidance Note does not capture required processes with respect to micro-credit and only covers aspects related t to TPS.

3. Before beginning

3.1 As a first step, NBFC-MFIs should strategically and critically evaluate its objective and reason, financial as well as non-financial for starting TPS. NBFC-MFIs must strategically evaluate its branch network to offer third-party products to its customer segment. TPS opens new revenue stream for NBFC-MFI and allows it to deepen its engagement with the customers. However, TPS entails setting-up new process, has demands on management and employee time and may create new risks. NBFC-MFIs exploring the TPS should carefully consider all the pros and cons related to TPS and decide.

3.2 Before going for full-scale implementation, NBFC-MFIs should consider piloting TPS on a small scale with few branches in select regions. This helps in evaluating and fine-tuning various requirements in terms of training employees, awareness amongst customers, internal processes, reporting etc. NBFC-MFIs should also explore to learn from experiences of other NBFC-MFIs, if relevant and possible.

4. Selection of product

4.1 The foremost aspect related to TPS is the selection of right product for the customer. Selection should be done by genuinely understanding the needs of the customers and their ability and willingness to pay for it. Right selection of the product for TPS ensures that there is a popular demand for the product alleviating obstinate incentive for force-selling to the customers.

4.2 The product should be selected based on evaluation of customer needs, alignment of NBFC-MFI's strategic objectives and internal capacity. Accordingly, the NBFC-MFI should factor in the following:

- **Need and Suitability:** Customer's need should be the primary factor in the selection of product as it ensures acceptability of the product. Survey amongst customers should be done to assess most sought-after products. Products which increases the well-being of customer and her household (such as those enhancing livelihoods, improving access to health or clean drinking water, increasing productivity, reduce drudgery, reduce vulnerability) should be prioritized in TPS.
- **Prince range:** Given that micro-credit customers are from low-income households and they have limited purchasing power, their ability and willingness on the price-point to purchase such products should be reasonably evaluated.
- **Segments/Area/Location:** A relevant product for one segment of customers or an area/location may not be a relevant product for other customer segments or other locations where NBFC-MFI operates. Hence, any product identified for TPS should be properly assessed before being offered to different customer segments and different operating areas of the NBFC-MFI. Products which customer already have or have easy access to in the local market at a competitive rate should generally be avoided.
- **Product features:** Ease of selling is an equally important factor to be considered. Product features should be simple which can easily be understood by the customers and the employees of the NBFC-MFI. For example, a complex investment product may require a lot of customer education and NBFC-MFI may lack time and capacity to offer such product to the customer.
- **Alignment with strategic objectives:** Products preferred by customer to be assessed for alignment with strategic objectives of NBFC-MFI.
- **Process flow:** Product should be logistically and administratively manageable for the NBFC-MFI considering location of branches, infrastructure available, security, process flow, documentation etc.

As per RBI Charter of Customer Rights, 'The products offered should be appropriate to the needs of the customer and based on an assessment of the customer's financial circumstances and understanding'.

Right selection of the product for TPS ensures that there is a popular demand for the product alleviating obstinate incentive for force-selling to the customers.

4.3 Short-listed product(s) should be finalized by the Senior management team/Board of the NBFC-MFI.

5. Selection of third-party vendor

5.1 After the relevant product(s) is identified, NBFC-MFIs should have well-laid out process to select third-party vendor based on transparent and objective parameters.

5.2 If possible, company should invite proposals from multiple agencies for fair comparison and competitive deal.

5.3 Selection of partner(s) for TPS should consider the following:

- **Market position:** NBFC-MFI should consider the market position of the vendor and its brand. It is always advisable to go with a vendor who has reputed brand and established network in NBFC-MFI's area of operations. This ensures customer's acceptability, ease of selling and established network for product availability and servicing.
- **Quality:** Quality of product is another important factor which should be carefully evaluated. A poor-quality product leads to dissatisfaction and inconvenience amongst the customers and can snowball into reputational risk for the NBFC-MFI. NBFC-MFIs must check if products offered by the third-party partners conform to the acceptable standards for such product¹.
- **Existing relationships:** Third-party vendor's previous and existing partnerships in the micro-credit industry should be examined to learn about the experience.
- **Warranty and post-sale service:** Third-party vendor's post-sale network, warranty offered on the product are other critical factors should be factored while selecting a third-party vendor.
- **Support:** Some social-good products by some third-party vendors such as sanitation products, water purifiers, renewable energy products facilitate technical and financial support. Such additional supports available should be explored to pass on the benefit to the customers.
- **Pricing:** Finally, vendors offering most competitive price is a critical factor. Based on potential volume, a lower price must be negotiated for the customers and in no case the product offered to the customers should be at a price which is higher than the Maximum Retail Price (MRP).

A significant percentage of customer complaints on the Customer Grievance Redressal Mechanism (CGRM) of NBFC-MFIs as well as MFIs are related to product quality/service issues. Therefore, choosing good quality product is important to ensure customer pull for product and satisfaction.

5.4 A senior management team or designated sub-committee of the Board of the NBFC-MFI should evaluate the proposals based on clear and objective criterion and make the final decision.

5.5 Selection process of third-party vendors should be documented and kept for records.

¹ As an example, for solar products, NBFC-MFI can check Lighting Global Quality Standards available at <https://www.lightingglobal.org/products/>

6. Factors vis a vis third-party vendor

6.1 A service level contract between NBFC-MFI and third-party vendor must be executed for capturing obligations of both the parties.

6.2 Following aspects, with clear turn-around time, wherever applicable, should be factored in formulating processes with respect to the third-party vendor:

- **Logistics:** There should be well-defined and documented logistic arrangements between the NBFC-MFI and the third-party vendor. If products are stored by the NBFC-MFI, inventory management should be clearly spelled out including requirements of stock keeping, reconciliation, safety, insurance, storage facilities, obligation for damage/theft etc.
- **Delivery:** NBFC-MFIs should have clear terms with the third-party vendor/partner in terms of turnaround time for delivery of products. For financial products, this could be activation of the product such as insurance policy, wallet etc.
- **Payments:** Structure and schedule of payments between the NBFC-MFI and third-party vendor for sale, commission fee, support services should be clearly defined including penalty if any for delayed payments.
- **Customer grievances:** NBFC-MFIs should agree with third-party vendors on redressing customer grievances arising out of product sold through TPS including time-lines to resolve customer complaints.
- **Anti-competition:** Restrictions, if any, with respect to sale of similar products from competition or online platform by the NBFC-MFI should be clearly laid out.
- **Support:** Other support services required by NBFC-MFIs such as marketing/advertising material, training of employee etc should be mentioned in a quantifiable manner.
- **Reporting:** Requirement in terms of reporting with respect to customer (KYC details), products sold (name of the product, product ID, price, date of purchase, warranty etc), monthly reports (total sale across products, location, service issues, payments, pending deliveries, inventory etc) should be clearly laid out.
- **Confidentiality of information:** NBFC-MFI and third-party vendor should lay out mutual responsibilities with respect to confidentiality and privacy of information related to customers, business information, sale volumes and commercials etc.
- **Customer interface:** If third-party vendor has interface, contours of interface with customers should be well defined in line with NBFC-MFI's own code of conduct for customer interaction. This, amongst other things should include acceptable behaviours with customers and respect for their choices etc.

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6.3 **Termination:** Clear terms and conditions should be laid out for terminating the contract/services if both parties agree for the same. This should ensure that customers do not face any inconvenience and harassment due to termination.

7. Factors vis a vis customer

7.1 NBFC-MFIs should clearly lay out a separate process for the TPS to the customers.

7.2 If third-party product is purchased by customer through micro-credit from NBFC-MFI, NBFC-MFI should follow the RBI Directions for NBFC-MFIs, RBI Fair Practice Code and Industry Code of Conduct for credit. This among other things include appropriate loan application process, underwriting including credit bureau check for compliance with norms of moratorium period, multiple/over lending, pricing, loan agreement and disclosure to customers.

7.3 NBFC-MFIs should make appropriate pre/post-sale disclosures to the customers as under:

- Eligibility criterion for customers to avail TPS
- Purchase of third-party product is not compulsory
- Details of the products including price, warranty, name of third-party vendor etc
- Delivery mechanism
- How to access NBFC-MFI or third-party vendor in case of defects with the product or servicing requirements

NBFC-MFI should clearly disclose (in its marketing material as well as in branches, loan documents) that grant of loan is not linked to any other product/services offered by the NBFC-MFI or third party

7.4 NBFC-MFIs should take explicit customer consent from the customer for purchase of third-party product. For financial products, necessary KYC details and other documents as required by the third-party vendor (Bank or Insurer) should be captured from the customers by the NBFC-MFIs as required by the Bank or Insurer.

7.5 NBFC-MFIs should give all necessary documents to the customers with respect to TPS. For example, credit-note, product documents capturing usage guidelines, warranty, servicing, vendor details for defective products etc.

MFID Directive # 8 on Third-party Products: To ensure that customer interests are protected in the sale of third-party product, it is directed that:

- Details of all third-party products offered by NBFC-MFIs should be displayed/disclosed.
- There should not be any bundling of a third-party product with the primary credit product or vice versa.
- There should be a minimum time gap of one month between the disbursement of the primary credit product and the credit for financing the third-party product or vice versa.
- Company's Customer Grievance Redressal Mechanism (CGRM) should cater to complaints related to sale of third-party products.
- Selling price of TPP to the customer, in case of non-financial products, under no circumstances, should exceed the MRP as mentioned on the product.
- Life insurance product linked to the credit is not considered as a third-party product.

7.6 In case of financial products, such as insurance, recurring deposits, wallets, all necessary documents such as policy papers, certificates, passbook, product kit including terms and conditions should be handed over to the customer either by NBFC-MFI or third-party vendor.

7.7 Customer Grievance Redressal Number of the third-party vendor (who is responsible for customer queries/complaints), NBFC-MFI and MFIN should be adequately explained and provided to the customers for dealing with any grievances related to the product or its sale.

7.8 Customer Grievance Redressal Mechanism (CGRM) of the NBFC-MFI should be aligned to handle customer queries and complaints with respect to TPS.

8. Internal controls

NBFC-MFIs should put in place relevant internal controls for TPS.

8.1 **Training to employees:** Employees responsible for TPS (related to sale, quality control, reporting, grievance redressal etc) should undertake adequate trainings covering the following:

- Product information
- Policies and Process
- Communication/disclosures to be made to the customers (including details of grievance redressal and product related queries)
- No mis-selling or forced selling to the customers
- Not linking of purchase of TPS to primary credit product and vice versa

8.2 **Incentives to employees:** Incentives to the employees for TPS should be carefully structured and should not lead to aggressive forced-sell. Customer complaints with respect to forced-sell should be factored in employee's performance appraisal by the NBFC-MFI.

8.3 **Customer choice:** To ensure that TPS is availed by customers based on informed choice, NBFC-MFIs can incorporate the following checks:

- In no case, the micro-credit offered for TPS should be bundled with the primary micro-credit product. There should be a cooling off period of at least 1 month between the primary credit product and micro-credit given for TPS.
- Outbound calls should be made to the customers on a sample basis before processing to ensure and validate their choice and acceptance for the purchase of TPS.

8.4 **Compliance:** If micro-credit is given to customers by the NBFC-MFI to avail third-party product, relevant regulatory and industry norms for micro-credit such loan application process, underwriting including credit bureau check for compliance with norms of multiple/over lending, pricing, loan agreement and disclosure to customers should be followed.

8.5 **Internal audit:** Process with respect to TPS should be audited by the internal audit team for adherence to factors vis a vis third-party vendor and customers. Internal audit should check if customer's choice is mandatorily obtained for TPS. Instances of forced-sell should be highlighted in the audit report.

8.6 **Annual review:** The overall process of TPS including performance of product, vendor, internal processes, customer satisfaction and grievances, defects, TATs etc should be reviewed by the senior management/or any other designated management team of NBFC-MFI to identify lapses for improvement.

9. Annexures: Relevant regulatory/industry norms

9.1 Regulatory guidelines: Relevant regulatory guidelines with respect to TPS are as under:

- RBI Directions on NBFC-MFIs²: Part 1, 4.C.a.iv - Pricing of Credit: 'NBFC-MFIs shall recover only the actual cost of insurance for group, or livestock, life, health for borrower and spouse. Administrative charges where recovered, shall be as per IRDA guidelines.'
- RBI's Guidelines on Fair Practices Code for NBFCs³, Part B. NBFC-MFIs, (ii) Disclosures in loan card,
'(c) v. Non-credit products issued shall be with full consent of the borrowers and fee structure shall be communicated in the loan card itself.'
- Charter of Customer Rights⁴, *point 3*: Right to Suitability: 'The products offered should be appropriate to the needs of the customer and based on an assessment of the customer's financial circumstances and understanding.'

9.2 RBI Charter of Customer Rights⁵

- **Right to Fair Treatment:** Both the customer and the financial services provider have a right to be treated with courtesy. The customer should not be unfairly discriminated against on grounds such as gender, age, religion, caste and physical ability when offering and delivering financial products.
- **Right to Transparency, Fair and Honest Dealing:** The financial services provider should make every effort to ensure that the contracts or agreements it frames are transparent, easily understood by and well communicated to, the common person. The product's price, the associated risks, the terms and conditions that govern use over the product's life cycle and the responsibilities of the customer and financial service provider, should be clearly disclosed. The customer should not be subject to unfair business or marketing practices, coercive contractual terms or misleading representations. Over the course of their relationship, the financial services provider cannot threaten the customer with physical harm, exert undue influence, or engage in blatant harassment.
- **Right to Suitability:** The products offered should be appropriate to the needs of the customer and based on an assessment of the customer's financial circumstances and understanding.
- **Right to Privacy:** Customers' personal information should be kept confidential unless they have offered specific consent to the financial services provider or such information is required to be provided under the law or it is provided for a mandated business purpose (for example, to credit information companies). The customer should be informed upfront about likely mandated business purposes. Customers have the right to protection from all kinds of communications, electronic or otherwise, which infringe upon their privacy.
- **Right to Grievance Redressal and Compensation:** The customer has a right to hold the financial services provider accountable for the products offered and to have a clear and easy way to have any valid grievances redressed. The provider should also facilitate the redress of grievances stemming from its sale of third-party products. The financial services provider must communicate its policy for compensating mistakes, lapses in conduct, as well as non-

² https://www.rbi.org.in/scripts/BS_ViewMasCirculardetails.aspx?id=9827

³ <https://rbi.org.in/scripts/NotificationUser.aspx?Id=7089&Mode=0>

⁴ http://rbi docs.rbi.org.in/rdocs/content/pdfs/CCSR03122014_1.pdf

⁵ https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=32667

performance or delays in performance, whether caused by the provider or otherwise. The policy must lay out the rights and duties of the customer when such events occur.

9.3 Compendium of MFIN Directives and Advisories⁶

a. Directive # 8 on Third-party Products: To ensure that customer interests are protected in the sale of third-party product, it is directed that:

- Details of all third-party products offered by NBFC-MFIs should be displayed/disclosed.
- There should not be any bundling of a third-party product with the primary credit product or vice versa.
- There should be a minimum time gap of one month between the disbursement of the primary credit product and the credit for financing the third-party product or vice versa.
- Company's Customer Grievance Redressal Mechanism (CGRM) should cater to complaints related to sale of third-party products.
- Selling price of TPP to the customer, in case of non-financial products, under no circumstances, should exceed the MRP as mentioned on the product.
- Life insurance product linked to the credit is not considered as a third-party product.

To ensure regulatory compliance on multiple/over lending by member NBFC-MFIs, it is directed that:

b. Directive # 3 on using valid Credit Information Report (CIR)

To ensure regulatory compliance on multiple/over lending by member NBFC-MFIs, it is directed that:

- NBFC-MFIs to use a valid CIR of the customer for all the loans disbursed to customer. CIR should be used for new loans (first cycle or subsequent cycles) as well as any top-up loan or mid-term loan.
- Credit Information Report (CIR) is considered as 'valid' for 15 calendar days from the date of extraction of the CIR. This implies that NBFC-MFIs needs to disburse a loan to the customer within 15 calendar days from date of extracting her Credit Information Report (CIR).
- To extract CIR, NBFC-MFI must accurately input customer's KYC information including Aadhaar, Voter ID, name, spouse name, date of birth and address (pin code, state, district) as required by the CICs to ensure optimum match by the CICs.

9.4 Industry Code of Conduct: Relevant clause with respect to TPS in the Industry Code of Conduct is as under:

- Products should not be bundled. (Bundling in this context means making purchase of a product or service conditional for provision of another product or service). The only exceptions to bundling may be made with respect to credit life, life insurance & livestock insurance products, which are typically offered bundled with loans. The terms of insurance should be transparently conveyed to the client and must comply with RBI & Insurance Regulatory and Development Authority (IRDA) norms. Consent of the client must be taken in all cases.

9.5 Client Protection Certification Standards: Relevant clauses on TPS from Client Protection Certification Standards⁷ are as under:

⁶ http://mfinindia.org/wp-content/uploads/2016/10/GuidanceNote_CGRM_15th_Oct_2018.pdf

⁷ http://smartcampaign.org/storage/documents/Standards_2.0_English_Final.pdf

- The FI verifies that third parties (agent network managers, etc.) train their own representatives to determine whether products, services and channels are suitable for specific clients, and for lending staff, that collateral policies are understood.
- When insurance is offered through third-party providers, the FI has a transparent process for selecting insurers which involves a competitive bidding and/or market study and a consideration of the value and appropriateness of the products and services offered.
- The FI and/or its agent network provider has a system to monitor third party agent liquidity and network availability and take action in the event of system failures.
- The FI verifies that third parties (agent network managers, etc.) train their representatives not to use aggressive sales techniques and to respect clients' right to refuse products.
- The FI has a mechanism of rigorous and regular monitoring of front-line staff and third-party sales techniques (e.g., agents, insurance companies or money transfer companies) to impede aggressive sales. When 'red flags' are raised, it triggers corrective measures.
- Fees charged by third-party providers or agents are fully disclosed to clients.
- The FI monitors the fees charged to its clients by its third-party providers to ensure that they are in line with peers.
- The code of conduct (or equivalent) clearly spells out organizational values, standards of professional conduct and treatment of clients that are expected of all FI or third-party provider staff or agents. Policies also spell out what sanctions to apply in case of a breach of the code of conduct.
- The FI verifies that third parties (agent network managers, etc.) train their own representatives on policies and processes related to privacy of client data.
- Complaints about the FI's third-party providers can be submitted directly to the third-party providers or to the FI. If submitted to the FI's third-party provider, the FI needs to get reports of the complaints.
- The FI verifies that third parties (agent network managers, etc.) train their own representatives on how the complaints mechanism works, the role of complaints staff, how to appropriately manage complaints until they are resolved, and how to refer them to the appropriate person for investigation and resolution.
- The FI considers design and delivery suitability when products and services are designed or offered through a third-party provider.
- The FI verifies that third parties (agent network managers, etc.) train their representatives not to use aggressive sales techniques and to respect clients' right to refuse products.
- The FI has a mechanism of rigorous and regular monitoring of frontline staff and third-party sales techniques (e.g., agents, insurance companies or money transfer companies) to impede aggressive sales. When 'red flags' are raised, it triggers corrective measures.
- The code of conduct (or equivalent) clearly spells out organizational values, standards of professional conduct and treatment of clients that are expected of all FI or third-party provider staff or agents. Policies also spell out what sanctions to apply in case of a breach of the code of conduct.
- The FI verifies that third parties (agent network managers, etc.) train their own representatives on fair and responsible treatment of clients. The training is aligned with the FI's code of conduct and spells out unacceptable behaviour.
- The FI's agreement with third-party providers that have access to client data specifies that these providers will maintain the security and confidentiality of client data. The FI monitors fulfilment of this agreement and takes action when problems are identified.
- The FI verifies that third parties (agent network managers, etc.) train their own representatives on policies and processes related to privacy of client data

- Complaints about the FI's third-party providers can be submitted directly to the third-party providers or to the FI. If submitted to the FI's third-party provider, the FI needs to get reports of the complaints.
- The FI verifies that third parties (agent, network managers, etc.) train their own representatives on how the complaints mechanism works, the role of complaints staff, how to appropriately manage complaints until they are resolved, and how to refer them to the appropriate person for investigation and resolution.

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