



Guidance Note

Pricing of Digital Loans by NBFCs

JAN 2025

Fintech Association for Consumer Empowerment

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1. Context

Pricing (interest rate and other charges regulated entities/NBFCs charge to the customers) is a critical component of a responsible lending framework reinforced by the Reserve Bank of India (RBI). The regulatory framework gives the NBFCs' Board freedom and responsibility in pricing decisions. It expects the NBFCs to be judicious, fair, objective and transparent in formulating pricing that aligns with consumer interests, safeguards overall financial stability,¹ and generates reasonable returns. Pricing is subject to supervisory review.

NBFCs involved in digital lending directly or through FinTechs (LSPs, marketplaces, and other TSPs) have significantly expanded credit access to underserved segments with timely and convenient credit and promoted financial inclusion. Given the diversity of digital lending in terms of scale, business models, segments, risk appetite, and product/ticket size/tenure, pricing in digital lending varies widely. Newness and evolving models mean that industry-level cost and pricing structure benchmarks haven't developed. Equally, there are also concerns about loan pricing in digital loans, including the explainability and performance of risk-based pricing models, governance framework, high interest rates, and non-transparent methods of calculating interest².

This guidance note³ aims to support FACE members in formulating their loan pricing framework. We developed it after consulting with members and understanding regulatory objectives. It builds on long-held principles that require pricing to be context-specific, reasonable, fair, consistent, competitive, transparent, affordable, suitable, and sustainable.

Appropriate pricing frameworks enhance the credibility and long-term value of digital lending. In addition to providing a competitive edge and market reputation, they build customer and stakeholder confidence and prevent predatory behaviours that may overburden customers with unaffordable loans.

The note outlines a framework for setting prices that NBFCs can adapt to their own context. It focuses solely on key indicators and does not include specific formulas or detailed weightings for constructing a pricing model, which is the prerogative of the NBFC board. Current practices in pricing methodologies informed the development of this guidance note.

In this guidance note, we articulate the pricing approach in three elements: governance, approach, and transparency.

2. Governance

NBFC should have robust governance of the pricing framework, which entails the following:

- a. The Board should approve a well-documented pricing policy that is reviewed at least once a year or more frequently to reflect evolving business and macroeconomic conditions. No change in the pricing model can be implemented without Board approval.
- b. The policy should cover the following:
 - Approach to pricing
 - Underlying components (cost of funds, operating costs, risk, margin, etc.) of interest rate models (annex a), in as granular details as possible, separately for different loan products, including minimum and maximum limits on interest rates.

¹ https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=58049

²

<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/106MDNBFCs1910202343073E3EF57A4916AA5042911CD8D562.PDF>, pg 61

³ Approved by the FACE Board through email circulation on 29 Jan 2025.

- For risk-based pricing models, policy should explain the variables, including annual model validation and deviation tolerance.
- Governance framework with a clear delegation matrix and authority to approve exceptions within the ranges approved by the Board (refer to Annex b)
- List of all fees/charges (refer to Annex c), rationale for applying, and underlying calculations.
- Parameters of internal and external audits to check compliance with pricing policy and reporting to the Board.
- Frequency and parameters of board review and reporting (for example, IRR, WALR, APR, charges, cost components, internal/external audit reports⁴, customer complaints⁵, industry/peer benchmarking, regulatory developments, and supervisory observations). Any supervisory observation concerning pricing should be promptly discussed with the Board.
- Besides the interest rate, the policy should define fees and other charges the company will levy customers across product categories, if applicable. This should include the reasoning for levying those charges, computation logic, and minimum and maximum rates or amounts.
- Disclosure to customers and the public (website/marketing collaterals/apps etc). Please refer to Annex d for suggested disclosures.

3. Approach

- c. The interest rate, processing fee, and other charges, such as penal charges, should follow the RBI Fair Practices Code.
- d. Pricing methodology and model should accurately and consistently include and calculate various pricing components.
- e. Arrive at pricing calculation (interest rate, fee etc) based on the company's data, benchmarking with the industry for specific product/market segments and considering customers' affordability.
- f. Pricing calculations to follow a steady-state model to cover regular, continuous costs and not include outliers that distort the pricing in the short-medium term. For example, a sudden spike in credit costs due to idiosyncratic risks, fraud losses, credit decisions or investment in company infrastructure to support growth should be proportioned appropriately. Similarly, the costs arising from business decisions, such as higher liquidity/provisions, should not invariably be passed on to the customers.
- g. While it is acceptable to reflect increases in risk weights, liquidity premiums, and the cost of borrowing within the pricing model, the Board and delegated authority should evaluate whether and how these are incorporated into the pricing model to be absorbed by the company and the customers.
- h. The Board and management should make company-wide efforts to optimise costs to improve returns, pass on operational efficiencies, rating upgrades, and risk management benefits to customers, and benchmark their performance with peers and the industry.
- i. There should be a SoP for the multiple scenarios in the loan cycle, such as part-prepayment, foreclosure, delay in repayment, and early repayment of EMI, and how they will impact the interest and charges calculation.

⁴ Any deviations and material audit findings should be placed before the board.

⁵ Customer grievance redressal should include the pricing-related complaints received directly from customers or other stakeholders, including the RBI ombudsman, for consideration by the board.

- j. There should be objective criteria and delegation of authority to approve any exceptions, deviations and waivers from standard policy within the limits approved by the Board.
- k. Information on the pricing policy and any subsequent changes should be communicated to all relevant departments, including IT systems/process, audit, operations, and communication for uniform implementation within the company with effective timelines.
- l. The general expectation for post-tax Return on Assets (RoA) should align with the volatility of returns and normalised industry profitability. This can vary depending on the company-specific business model and risk-return expectations.
- m. The committee empowered with pricing should closely monitor the costs (operations, credit, finance) and review them quarterly to incorporate them into the pricing model to arrive at the interest rate.
- n. Evaluates rates offered by competitors in the market to stay competitive.
- o. Macroeconomic sensitivity towards various components can be made based on how changes in interest rates affect customer demand for loans.

4. Annexures

Annex a: Pricing Model

The main components of a company's pricing policy are costs and expected profit or RoA, which may vary for different products. These can vary depending on the products being offered by the NBFC in which case, NBFCs are required to draw pricing the individual products as appropriate. The company can have differential models for credit costs linked to product/customer profiles.

- a. Finance cost: This includes all the financial costs, such as borrowing costs of debt from banks, financial institutions, or through market instruments like debentures, processing fees and other costs associated with borrowings⁶, liquidity premium⁷ and equity/capital costs. The upfront cost incurred by the entity finance should be amortised over the term for which finance has been availed.
- b. Operational costs: This includes administrative expenses, marketing, technology, salaries, rent, GST losses/government levies, and other day-to-day costs that the rate charged must cover.
- c. Credit risk: Provisions for non-performing assets (NPAs) and potential loan defaults are factored into the interest rate as a buffer against credit losses. For companies doing risk-based pricing, this can have multiple variables (some examples described below). The same can be validated, stress-tested and documented to ensure that the ranges are accounted for while building the pricing model.
 - Creditworthiness of customers: Higher-risk customers (e.g., those with lower credit scores or inconsistent financial histories) are generally charged a higher interest rate to compensate for the increased risk of default.
 - Collateral and Loan-to-Value (LTV) Ratios: Loans with collateral may have lower interest rates due to the reduced risk. The LTV ratio helps determine the risk profile and, subsequently, the interest rate.

⁶ Costs directly related to raise the funding such as intermediation services, advisory, rating, hedging, legal, documentation, market listing etc.

⁷ NBFCs should have a rationale for if and when to factor the liquidity costs into the pricing model and be judicious to avoid invariably burdening the customers with liquidity costs due to higher liquidity buffers.

- Tailored Pricing: Different customer segments (e.g., individuals, SMEs, corporates) may receive varied rates based on their specific risk profile and loan purpose.
 - Preferred Customers: Customers with strong repayment histories or long-standing relationships may be offered lower rates as incentives.
 - Loan Tenure: Short-term loans typically have different pricing structures than long-term ones, as long-term loans involve higher exposure to risk over time.
 - Repayment Flexibility: Loans with flexible repayment schedules might have higher rates to offset the additional risk of payment irregularity.
 - Type of Product: Different loan products (personal, vehicle, and business) will have specific pricing structures due to varying risk and administrative costs.
 - Guarantee: If available, adjustment for government guarantees and first loss by LSPs for specific products/customer segments.
- d. The company incorporates a target profit margin to ensure the rate is financially viable and aligns with strategic business objectives. This is typically a fixed percentage added to the cost of funds and risk premiums. The table below indicates variables considered to determine the pricing at the company and product/cohort level, along with additional risk and macro factors and industry benchmarks to arrive at pricing. Over and above, the company should use the lens of ‘customer affordability’ to ensure the product pricing is not detrimental to the customer’s financial position.

		% of AUM/disbursement value
a	Finance costs (break-up as below)	
	Interest	
	Processing fee	
	Intermediation/administrative charges ⁸	
	Liquidity premium ⁹	
	Capital/equity	
b	Operating costs (break-up as below)	
	Marketing/sourcing	
	Customer acquisition (KYC / Bureau / CKYC etc)	
	Employee	
	Technology	
	Depreciation	
	Collection	
	GST leakage	
	Others	
c	Credit loss	
d	Profit margin/RoA	
e	Lending rate (a+b+c+d)	

⁸ Excluding processing fee

⁹ NBFCs should have a rationale for if and when to factor the liquidity costs into the pricing model and be judicious to avoid invariably burdening the customers with liquidity costs due to higher liquidity buffers.

Annex b: Governance Framework

The governance structure for pricing policy in an NBFC should incorporate multi-tiered accountability and oversight to ensure an effective and compliant pricing strategy. The framework should also adhere to RBI guidelines, risk management, market responsiveness, and strategic objectives. Key components of the governance structure are as follows, which the company may adopt based on the business scale.

- a. Board of Directors (Board) is responsible for approving the overall pricing policy framework, ensuring alignment with regulatory guidelines outlined by the RBI, and conducting periodic reviews of policy efficacy and alignment with strategic goals¹⁰. The Board must review and approve the pricing policy at a defined periodicity. The Board has the final authority to approve major changes to the policy. For operational efficiency, it can delegate certain responsibilities to the Pricing Committee.
- b. Pricing Committee¹¹ should comprise senior executives, including the Directors, CFO, Head of Risk Management, Head of Business Development, and representatives from the compliance team. This committee must formulate and propose pricing strategies to the Board, monitor market trends, competitor pricing, and economic indicators to adapt pricing strategies, and ensure pricing models consider risk-adjusted returns and operational costs. The committee should meet quarterly, with ad hoc sessions as needed. The pricing committee has authority from the Board to recommend/approve pricing changes within specified thresholds and the power to make decisions on regular adjustments, such as interest rate fluctuations within approved ranges. The committee can approve temporary promotional pricing initiatives, subject to Board ratification.
- c. Risk Management Department is responsible for evaluating the risk implications of pricing decisions and ensuring that risk factors are integrated into the pricing policy to mitigate potential financial vulnerabilities. This department should submit risk assessment reports to the pricing committee.
- d. The Compliance Department verifies that pricing policies comply with all relevant RBI regulations and oversees adherence to internal policies and regulatory mandates during implementation. This department should provide compliance audit findings to the Board, including deviations.
- e. Senior Management (e.g., CFO or Head of Business Development) can implement pre-approved pricing strategies and make operational adjustments that do not deviate from the Board-approved framework. Significant market-based pricing deviations must be reported to the Asset Liability Committee (ALCO) for review.
- f. Branch-Level Authorities, if there are branch setups, have limited authority to offer discounts or special rates within a narrow margin for specific customer segments as part of promotional campaigns, provided they adhere to main policy guidelines.
- g. Escalation Matrix defining that critical pricing decisions should be escalated to the Board for approval. The ALCO should review and decide on moderate adjustments, while routine adjustments should be handled by Senior Management and reported quarterly.

¹⁰ Suppose any component of the pricing model changes due to an increase in credit risk. In that case, the board should assess whether adjusting the pricing model assumptions or modifying the credit risk policy is the most sensible approach.

¹¹ Or any other committee which has delegation from the Board.

- h. Review and Audit for pricing policy to undergo a comprehensive annual review by the Board. The internal audit function should assess compliance with pricing guidelines and report discrepancies. External audits may be conducted periodically to ensure adherence to regulatory norms and transparency. In addition, as the company scales up, there shall also be a review to see if the pricing charged to consumers' needs to be adjusted based on evolving macro and internal efficiencies. For instance, with an increase in size and better ratings, if the cost of borrowing falls, there can be a case to reduce the interest rate/APR charged to consumers. Companies operating at a small scale and lacking a full-fledged audit function may conduct the period assessment to document the exceptions/lapses with root cause analysis and prepare a corrective action plan.
- i. Data and pricing methodology/calculations incorporated in the model to arrive at pricing should be accessible to the Board and the RBI for review.

Annex c: Illustrative List of Fees and Charges

Below is the illustrative list of the company's charges, which it may not levy for loan products in different contexts. The company should have a thorough list of all such fees/charges, reasoning for applying such charges, underlying calculations, and caps.

Fee/Charge	Description	Examples of computation
Processing Fees	This is a fee for processing the loan application, including verification and approval. Covers administrative costs for loan origination.	% of the loan amount or a fixed amount subject to a minimum and maximum.
Documentation Fees	Charges for preparing and verifying documents for the loan. It covers paperwork, legal fees, registration costs, etc, but other than those already covered in the processing fee.	% of the loan amount or a fixed amount subject to a minimum and maximum.
Late Payment Charges	Fee for payments made after the due date. Penalises late payment and compensates for delays.	% of the overdue amount or fixed amount, subject to a minimum and maximum
Prepayment Charges	Fee for early repayment of the loan before the agreed tenure. Compensates for the loss of interest revenue.	% of the outstanding balance subject to minimum/maximum amount.
Foreclosure Charges	Charges for repaying the loan before the agreed tenure ends. Covers costs related to early loan closure.	% of the outstanding balance subject to minimum/maximum amount.
Insurance Charges	Charges for insurance products bundled with the loan (e.g., life insurance). Protects both borrower and lender.	On actuals
Bounce Charges	Charges for a bounced cheque or failed payment. Compensates for administrative costs of bounced payments.	A fixed amount for each bounced cheque or failed transaction.
Verification and Inspection Fees	Fees for verifying loan details or inspecting collateral. Covers costs of physical verification or inspection.	A fixed amount for per inspection.
Conversion Charges	Charges for converting a loan type (e.g., fixed to floating rate). Covers administrative work involved in conversion.	A fixed amount or based on % the loan balance.
Renewal Charges	Charges for renewing an existing loan or credit line. Covers administrative work for loan renewal.	A fixed amount or based on % the loan balance.

Annex d: Disclosures

- a. Company must make mandatory disclosures related to applicable interest rates and fees all key documents (marketing collaterals, loan application form, sanction letter, KFS¹², loan agreement) to customers.
- b. Information about the annual percentage rate (APR), which includes both interest and fees as per RBI's KFS, should be easily accessible to customers. Sanction letters and financial documents should outline the rate structure and any changes, particularly for floating-rate loans, and any fees that apply in the event of prepayment or delays in repayment.
- c. Any changes in the pricing of loans (for example, due to floating interest rate) should be promptly communicated to customers through email, sms, app, letters, etc, as appropriate.
- d. If there are loan products with lower pricing that are more favourable to customers, inform the customer of those loan options so that the customer can make the right decision. Existing customers should also be informed of switching to alternative loan options if they are favourable to them.
- e. Loan closure statements must include the final interest calculation and any applicable charges when a borrower settles or forecloses the loan, ensuring complete transparency at the end of the loan lifecycle.
- f. These disclosures across various touchpoints ensure that customers are well-informed about the cost of borrowing, in line with RBI's consumer protection guidelines.
- g. The company should publicly disclose pricing-related information on its website, app and marketing collateral.
- h. Pricing policy should also be available on the company website, as per RBI directions.
- i. Report the pricing-related information to RBI through periodic returns, as required.
- j. Report pricing information to the SROs, as required by them.

Annex e: Regulations on Pricing and Interest Rate¹³

- a. 45.2.1 NBFCs shall convey in writing to the borrower in the vernacular language as understood by the borrower by means of sanction letter or otherwise, the amount of loan sanctioned along with the terms and conditions including annualised rate of interest and method of application thereof and keep the acceptance of these terms and conditions by the borrower on its record. As complaints received against NBFCs generally pertain to charging of high interest/penal charges, NBFCs shall mention the penalties charged for late repayment in bold in the loan agreement.
- b. 45.2.2 Borrowers may not be fully aware of the terms and conditions of the loans including rate of interest at the time of sanction of loans, either because the NBFC does not provide details of the same or the borrower has no time to look into detailed agreement. Not furnishing a copy of the loan agreement or enclosures quoted in the loan agreement is an unfair practice and this could lead to disputes between the NBFC and the borrower with regard to the terms and conditions. NBFCs, shall furnish a copy of the loan agreement as understood by the borrower along with a copy each of all enclosures quoted in the loan agreement to all the borrowers at the time of sanction / disbursement of loans.
- c. 45.2.3 NBFCs shall comply with the instructions contained in the circular on 'Key Facts Statement (KFS) for Loans & Advances' dated April 15, 2024, as amended from time to time (format of KFS as given in the circular is incorporated in Annex XXVII).

¹² Key fact statement

¹³ https://rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12550

- d. 45.3.1 Penalty, if charged, for non-compliance of material terms and conditions of loan contract by the borrower shall be treated as 'penal charges' and shall not be levied in the form of 'penal interest' that is added to the rate of interest charged on the advances. There shall be no capitalisation of penal charges i.e., no further interest computed on such charges. However, this will not affect the normal procedures for compounding of interest in the loan account.
- e. 45.3.2 NBFCs shall not introduce any additional component to the rate of interest and ensure compliance to these guidelines in both letter and spirit. 45.3.3 NBFCs shall formulate a Board approved policy on penal charges or similar charges on loans, by whatever name called.
- f. 45.3.4 The quantum of penal charges shall be reasonable and commensurate with the non-compliance of material terms and conditions of loan contract without being discriminatory within a particular loan/product category.
- g. 45.3.5 The penal charges in case of loans sanctioned to 'individual borrowers, for purposes other than business', shall not be higher than the penal charges to nonindividual borrowers for similar non-compliance of material terms and conditions.
- h. 45.3.6 The quantum and reason for penal charges shall be clearly disclosed by NBFCs to the customers in the loan agreement and most important terms & conditions/Key Fact Statement (KFS) as, in addition to being displayed on websites of NBFCs under Interest rates and Service Charges. The Board of each NBFC shall adopt an interest rate model taking into account relevant factors such as cost of funds, margin and risk premium and determine the rate of interest to be charged for loans and advances. The rate of interest and the approach for gradations of risk and rationale for charging different rate of interest to different categories of borrowers shall be disclosed to the borrower or customer in the application form and communicated explicitly in the sanction letter.
- i. 45.11.2 The rates of interest and the approach for gradation of risks shall also be made available on the website of the companies or published in the relevant newspapers. The information published on the website or otherwise published shall be updated whenever there is a change in the rates of interest.
- j. 45.11.3 The rate of interest must be annualised rate so that the borrower is aware of the exact rates that would be charged to the account.
- k. 45.12.1 The Reserve Bank has been receiving several complaints regarding levying of excessive interest and charges on certain loans and advances by NBFC. Though interest rates are not regulated by the Reserve Bank, rates of interest beyond a certain level may be seen to be excessive and can neither be sustainable nor be conforming to normal financial practice.
- l. 45.12.2 Boards of NBFCs shall lay out appropriate internal principles and procedures in determining interest rates and processing and other charges. In this regard, the guidelines indicated in the Fair Practices Code about transparency in respect of terms and conditions of the loans are to be kept in view.
- m. 45.4.1 NBFCs shall give notice to the borrower in the vernacular language or a language as understood by the borrower of any change in the terms and conditions including disbursement schedule, interest rates, service charges, prepayment charges etc. NBFCs shall also ensure that changes in interest rates and charges are affected only prospectively. A suitable condition in this regard must be incorporated in the loan agreement.