Digital Banking Unit (DBU) – A Boost to the Digital Economy*

Introduction

Promotion of digital payments ecosystem is a necessary aspect of Digital India programme and is aimed at digitizing the financial sector and economy with consequent benefits of efficiency, transparency and quality. Digital Payments transactions have been gradually increasing over last few years, as a part of Government of India's strategy to digitise the financial sector and economy. Over the past four years, digital payment transactions have grown multi-fold from 3,134 crore in FY 2018-19 to 5,554 crore in FY 2020-21. During current financial year i.e. FY 2021-22, the total number of 7422 crore digital transactions have been reported till 28th February, 2022. Bharat Interface for Money-Unified Payments Interface (BHIM-UPI) has emerged as the preferred payment mode of the citizens and has achieved a record of 452.75 crore digital payment transactions with the value of Rs. 8.27 lakh crore till 28th February 2022. Covid-19 pandemic has established that digital payments enable access to healthcare as well through contactless payment modes like BHIM-UPI QR code in consonance with the "new normal" of social distancing.

Several marketing expressions like "challenger banks"[1], "neo-banks"[2] in addition to "digital banks" are used interchangeably in financial / fintech[3] discourse in India and elsewhere, without regard to whether these fintechs actually function as "banks" as the applicable law defines them.

1. **Challenger banks** are mobile, online and tech-based small retail banks that offer financial services and digital offerings. These banks have no physical branches.
2. A **neo-bank** (also known as an online bank, internet-only bank, virtual bank or digital bank) is a type of direct bank that operates exclusively online without traditional physical branch networks.
3. **Financial technology (abbreviated fintech or FinTech**) is the technology and innovation that aims to compete with traditional financial methods in the delivery of financial services.

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Article

Banks and fintechs offering digital banking services (also called, neo-banks) rely primarily on digital channels that organically have high efficiency metrics related to incumbent commercial banks. This structural feature makes them a potentially effective channel through which policymakers can achieve social goals like empowering the hitherto under-banked small businesses, and enhancing trust among retail consumers.

While giving a boost to the digital economy, Union Minister of Finance Nirmala Sitharaman in her Budget Speech 2022-2023 stated that:

In recent years, digital banking, digital payments and fintech innovations have grown at a rapid pace in the country. Government is continuously encouraging these sectors to ensure that the benefits of digital banking reach every nook and corner of the country in a consumer-friendly manner. Taking forward this agenda, and to mark 75 years of our independence, it is proposed to set up 75 Digital Banking Units (DBUs) in 75 districts of the country by Scheduled Commercial Bank.

In line with the above Union Budget, Reserve Bank of India has released the guidelines on "Establishment of Digital Banking Units (DBUs)".

Digital Banking Unit (DBU)

A specialised fixed point business unit / hub housing certain minimum digital infrastructure for delivering digital banking products & services as well as servicing existing financial products & services digitally, in both self-service and assisted mode, to enable customers to have cost effective/ convenient access and enhanced digital experience to/ of such products and services in an efficient, paperless, secured and connected environment with most services being available in self-service mode at any time, all year round.

Opening of DBUs

Scheduled Commercial Banks (other than RRBs[4], PBs[5] and LABs[6]) with past digital banking experience are permitted to open DBUs in Tier 1 to Tier 6 centres, unless otherwise specifically restricted, without having the need to take permission from Reserve Bank of India in each case.

The DBUs of the banks will be treated as Banking Outlets (BOs). For the purpose of compliance with regulatory requirements on opening of BOs during a financial year, the DBUs will be treated as opened in a centre from where the significant parts of its new business are proposed to be sourced, regardless of its physical location.

4. **Regional Rural Banks (RRBs)** are government owned scheduled commercial banks of India that operate at regional level in different states of India. These banks are under the ownership of Ministry of Finance, Government of India. They were created to serve rural areas with basic banking and financial services.

5. A **Payments Bank (PB)** is like any other bank, but operating on a smaller scale without involving any credit risk. In simple words, it can carry out most banking operations but can't advance loans or issue credit cards. It can accept demand deposits (up to Rs. 2 lakh), offer remittance services, mobile payments/transfers/purchases and other banking services like ATM/debit cards, net banking and third party fund transfers.

6. **Local Area Banks (LAB)** can be defined as banks that were set up by the Government of India solely with the purpose of enabling the local institutions to pool and mobilize the rural savings and ensuring that these savings are made available for investment concerning needs or in other words, these banks help in bridging the existing gaps with respect to the credit availability and thus, strengthening the credit mechanism in the local areas (rural as well as semi-urban areas).

Infrastructure and Resources

Each DBU shall be housed distinctly, with the separate entry and exit provisions. They will be separate from an existing Banking Outlet with formats and designs most appropriate for digital banking users.

For front-end or distribution layer of digital banking, each bank would choose suitable smart equipment, such as Interactive Teller Machines, Interactive Bankers, Service Terminals, Teller and Cash Recyclers, Interactive Digital Walls, Document uploading, self -service card issuance devices, Video KYC[7] Apparatus, secured and connected environment for use of own device for digital banking, Video Call / Conferencing facilities, to set up an DBU. These facilities can be insourced or outsourced while complying with relevant regulatory guidelines.

The back-end including the Core Banking System (CBS)[8] and other back office related information systems for the digital banking products and services can be shared with that of the incumbent systems with logical separation. Alternatively, banks can adopt more core-independent digital-native technologies offering better scalability, flexibility in creating new / reusable digital environments through continuous development / software deployment and interconnectivity specifically for this business segment, based on their digital strategy.

If the digital banking segment of a bank uses an API layer (integration layer) to connect with external third-party application providers, the same should be tested in an isolated/ test environment before being integrated to bank's core systems backed by comprehensive risk evaluation and adequate documentation.

Banks are free to adopt an in-sourced or out-sourced model for operations of the digital banking segment including DBUs. The outsourced model should specifically comply with the relevant regulatory guidelines on outsourcing.

As the purpose of DBUs is to optimally blend digital infrastructure with 'human touch', remote or in situ assisted mode arrangements in right proportion should be planned and put in place by the banks.

The establishment of DBUs should be part of the digital banking strategy of the bank. The operational governance and administrative structure of the DBUs will be aligned with that of the Digital Banking Segment of the bank. However, in order to accelerate digital banking initiatives, each DBU will be headed by a sufficiently senior and experienced executive of the bank, preferably Scale III or above for Public Sector Banks (PSBs) or equivalent grades for other banks who can be designated as the Chief Operating Officer (COO) of the DBU.

7. **"Know Your Customer" or KYC** refers to the process of authenticating the identity of the customers and clients either before or during the start of the business relationship. KYC came into existence in 2002 in India. According to the Reserve Bank of India (RBI) notification it has made it mandatory for all banks to carry out KYC of customers since 2004.

8. **Core Banking** is a banking service provided by a group of networked bank branches where customers may access their bank account and perform basic transactions from any of the member branch offices.

Cyber Security

In addition to ensuring physical security of the infrastructure of the DBU, adequate safeguards for cyber security of the DBUs will have to be ensured by the banks.

Products and Services

Each DBU must offer certain minimum digital banking products and services. Such products should be on both liabilities and assets side of the balance sheet of the digital banking segment. Digitally value-added services to conventional products would also qualify as such. The DBUs are expected to migrate to more structured and custom made products, from standard offerings by use of its hybrid and high quality interactive capabilities.

The banks have the freedom to offer any other digital product or service in addition to the minimum bouquet to cater to the specific needs of the service area. Any product or service that can be provided digitally through internet banking or mobile banking can be provided in the DBU. Any product or service which a bank is not permitted to offer as per the provisions of Banking Regulation Act, 1949, as amended from time to time, shall not be offered by the DBU.

Digital Banking Customer Education

In addition to on boarding of customers in a fully digital environment, various tools and methods shall be used by DBUs to offer hands-on customer education on safe digital banking products and practices for inducting customers to self-service digital banking services. This effort has to be clearly translated to incremental digital penetration of the financial services a DBU is catering to and will have to be monitored. The district where the DBU is located will be the catchment area for the purpose.

Digital Business Facilitator / Business Correspondent

The banks will have the options to engage digital business facilitator / business correspondents in conformance with relevant regulation to expand the virtual footprint of DBUs.

Customer Grievances

There should be adequate digital mechanism to offer real time assistance and redress customer grievances arising from business and services offered by the DBUs directly or through Business Facilitators / Correspondents.

Reporting Requirements

Banks shall report the Digital Banking Segment as a sub-segment within the existing "Retail Banking Segment" in the format as specified under paragraph 4 of Annexure II (Part B) of the Reserve Bank of India (Financial Statements – Presentation and Disclosures) Directions, 2021. It is clarified that the digital banking products / services applicable to segments other than 'Retail Banking' need not be reported at this stage.

Performance update with respect to DBU shall be furnished in a pre-defined reporting format (being separately issued) to Department of Supervision, Reserve Bank of India on monthly basis and in a consolidated form in Annual Report of the bank.

Banks shall furnish information relating to opening, closure, merger or shifting of DBUs online through Central Information System for Banking Infrastructure (CISBI) portal to Department of Statistics and Information Management (DSIM).

Role of Board of Directors

Expansion of digital financial services and financial inclusion being primary objectives of DBUs and in view of the operational flexibility given to banks in this domain, the board should ensure provisions of regular on-site and off-site monitoring system covering all aspects of the guidelines.

The Board or a Committee of the Board shall review the progress and key performance indicators of digital banking services including that of DBU separately at suitable periodicity. The review should cover both business and risk aspects of the segment.

International Scenario

Singapore, Hong Kong and Malaysia have issued special DB regulatory regimes. Elsewhere, as in the United Kingdom, regulators have recognized the DB business model by issuing banking licenses to banks offering "digital-first"[9] / "digital-only"[10] propositions within already existing regulations without creating specialist regimes.

Conclusion

Today, digital inclusion is a prerequisite for financial inclusion. Banks need to invest in building more capabilities to enhance service simplicity, availability and interoperability. There is a need for ecosystem players to adopt a holistic approach on going digital and integrating business strategy covering all constituents to create a remarkable customer experience.

9. **Digital first** is a communication theory that publishers should release content into new media channels in preference to old media.

10. A **digital-only** bank provides banking facilities exclusively through digital platforms, such as mobile, tablets, and the Internet.

Digital banking will shape India's banking sector with cheaper banking alternatives and varied innovative financial products and services becoming more readily available. Thus, digital banking will act as a catalyst for achieving greater financial inclusion in India. Access to digital banking services fuel economic growth and improve unemployment rates by creating the means to pay people for work and services.

References:

- *https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12285&Mode=0*
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