

Modernising the Law for Payment Services in India | Preparing for the Future of Retail Payments

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Errors (if any) rest with the authors.

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I. Setting the Context

A safe and well-functioning payments ecosystem is critical to support economic activity. Technological innovations are transforming the financial system, and payments continue to remain the leading sector impacted by such innovations. While the initial impact was seen in the large-value payment systems, the recent years have witnessed efforts by policymakers and the industry to revolutionise the retail payments sector that enables households and businesses to make and receive payments. Such efforts recognise the growing adoption and role of digital payments, that has also been accentuated by the Covid-19 pandemic.

Existing literature refers to the potential of digital payments to enable economies to pursue several policy objectives, including promotion of financial inclusion, ensuring financial transparency and the reduction in costs associated with cash transactions.¹ As the payments sector continue to innovate to meet the consumer demand for more efficient, innovative and faster payment systems, policymakers and central banks are focusing their efforts to develop policies and regulations to support the growth of digital payments. India is not left behind. With the launch of the Unified Payments Interface (“UPI”), India has witnessed a steady adoption of digital payments, indicating the need to support such innovation in the payments sector. Innovative payment solutions also have the potential to drive growth in other sectors of the financial system such as banking and lending.

As per the data released by the Reserve Bank of India (“RBI”), retail digital payments (excluding payments through real time gross settlement (“RTGS”)) in India has shown a year wise growth, both in terms of volume and value.² However, if one includes RTGS payments, the value of total digital payments witnessed a drop of 1.2% in the financial year (FY) 2019-2020 which further got amplified to 13.4% in the FY

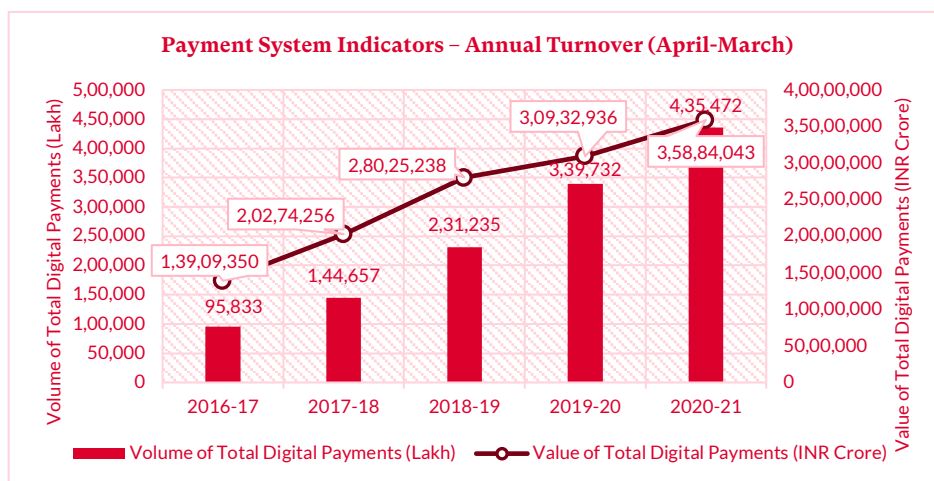


Figure 1: Value and Volume of digital payments transactions in India (RBI)

2020-21.³ RBI notes that the dip is “mainly due to lower growth observed in the large value payment system, viz., Real Time Gross Settlement (RTGS) system”⁴ that “is largely attributable to the subdued economic activity.” To

¹ Committee on Digital Payments, ‘Medium Term Recommendations to Strengthen Digital Payments Ecosystem’ (2016) Pg 77 <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed on 19 March 2021; Ceyla Pazarbasioglu, Alfonso Garcia Mora, Mahesh Uttamchandani, et al, ‘Digital Financial Services’ (World Bank Group, April 2020) <<https://pubdocs.worldbank.org/en/230281588169110691/Digital-Financial-Services.pdf>> accessed 22 August 2021

² RBI, ‘Handbook of Statistics on Indian Economy’, (15 September 2021) <<https://www.rbi.org.in/scripts/AnnualPublications.aspx?head=Handbook%20of%20Statistics%20on%20Indian%20Economy>> accessed 20 September 2021. This comprises of following payment systems: (1) Credit Transfers (AePS (fund transfers), APBS, ECS Cr, IMPS, NACH Cr, NEFT, UPI); (2) Debit Transfers and Direct Debits (BHIM Aadhaar Pay, ECS Dr, NACH Dr, NETC (linked to bank account)); (3) Card Payments (Credit Cards and Debit Cards); (4) Prepaid Payment Instruments. Here, the RTGS system includes customer and inter-bank transactions only. The figures for ‘card payments’ indicate only the payment transaction conducted at point of sale (PoS) terminals and online. UPI and AePS (Fund Transfer) were introduced in FY 2016-17; BHIM Aadhaar Pay and NETC (linked to bank account) were introduced in FY 2017-18.

³ RBI, ‘Annual Report 2020-21’, (27 May 2021) pg. 185 <https://rbidocs.rbi.org.in/rdocs/AnnualReport/PDFs/ORBIAR202021_F49F9833694E84C16AAD01BE48F53F6A2.PDF> accessed 22 August 2021.

⁴ RBI, ‘Annual Report 2020-21’, (27 May 2021) pg. 185

measure the deepening and penetration of digital payments in the country, the RBI has also launched the Digital Payments Index (“DPI”)⁵ that comprises of five broad parameters (further sub-divided into other parameters). The DPI finds a steady growth in the index representing the rapid adoption and deepening of digital payments across the country in recent years.

Despite these developments, India still remains a cash dependent economy. The RBI in its report on “Assessment of the progress of digitisation from cash to electronic”⁶ notes that “India continues to have a strong bias for cash payments” as is evident from the percentage of cash in circulation (“CIC”) to gross domestic product (“GDP”). A high CIC relative to GDP indicates that cash is highly preferred as a payment instrument. While demonetisation brought down the CIC as a percentage of GDP to 8.70% in FY 2016-17, it increased to 10.70% in 2017-18 and to 11.2% in 2018-19. The Bank for International Settlements (“BIS”) has also released data⁷ on the CIC to GDP (%) of countries that are members of the Committee on Payments and Markets Infrastructure (“CPMI”) (formerly the Committee on Payments and Settlement Systems (“CPSS”)), which is an international standard setting body for payments⁸ consisting of senior representatives from various central banks across the world. This data indicates that as compared to many CPMI member countries, the CIC to GDP (%) in India is relatively higher, indicating India’s strong dependence on cash.

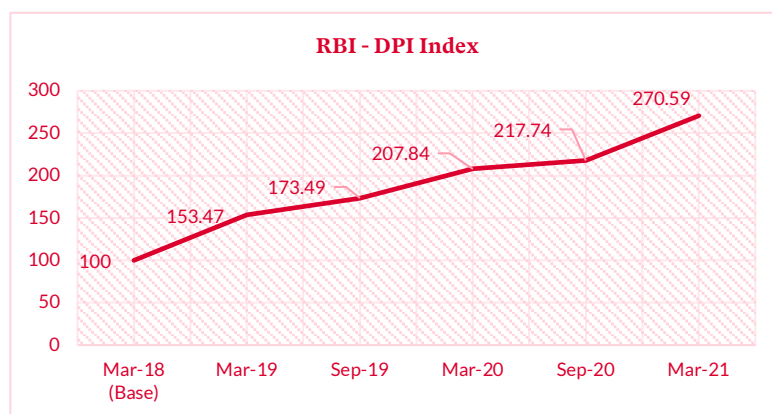


Figure 2: RBI DPI Index

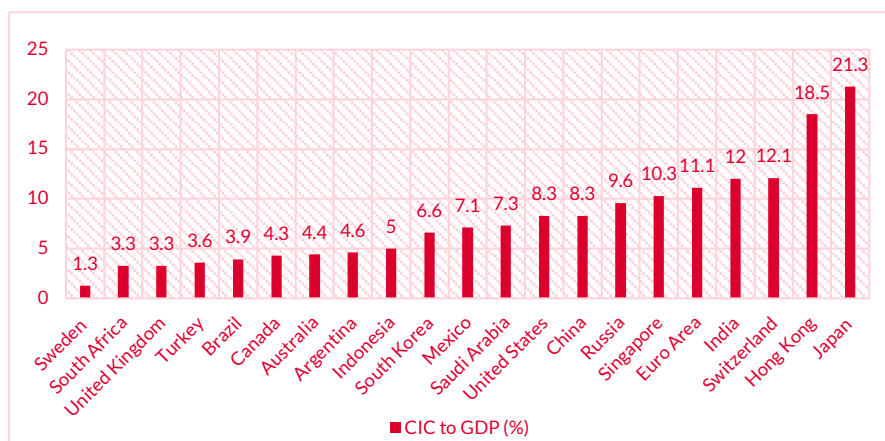


Figure 3: Snapshot of CIC as a percentage of GDP (%) in CPMI countries (2019) (Source: BIS)

<https://rbidocs.rbi.org.in/rdocs/AnnualReport/PDFs/ORBIAR202021_F49F9833694E84C16AAD01BE48F53F6A2.PDF> accessed 22 August 2021.

⁵ RBI, ‘Reserve Bank of India introduces the RBI-Digital Payments Index’ (1 January 2021) <https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=50901> accessed 19 September 2021. RBI, ‘Reserve Bank of India announces Digital Payments Index (RBI-DPI) for March 2021’ <https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=51962> (28 July 2021) <https://www.rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=51962> accessed 19 September 2021. The DPI is comprised of five broad parameters that enable measurement of deepening and penetration of digital payments in the country over different time periods. These parameters along with weightage assigned to them are as follows: (a) Payment Enablers (weight 25%), (b) Payment Infrastructure – Demand-side factors (10%), (c) Payment Infrastructure – Supply-side factors (15%), (d) Payment Performance (45%) and (e) Consumer Centricity (5%). Each of these parameters have sub-parameters which, in turn, consist of various measurable indicators. The DPI has been constructed with March 2018 as the base period, i.e. DPI score for March 2018 is set at 100.

⁶ RBI, ‘Assessment of the progress of digitization from cash to electronic’ (24 February 2020) <<https://www.rbi.org.in/Scripts/PublicationsView.aspx?id=19417>> accessed 20 August 2021.

⁷ BIS, ‘Payments and Financial Market Infrastructures statistics’ (25 March 2021) <https://www.bis.org/statistics/full_data_sets.htm> accessed 20 August 2021.

⁸ The Committee on Payments and Market Infrastructures (CPMI) is an international standard setter that promotes, monitors and makes recommendations about the safety and efficiency of payment, clearing, settlement and related arrangements, thereby supporting financial stability and the wider economy. BIS, CPMI-Overview <<https://www.bis.org/cpmi/about/overview.htm?m=3%7C16>> accessed 20 August 2021.

A pilot study conducted by the RBI on retail payment habits of individuals in six cities between December 2018 and January 2019 reveals that 54.2% of the respondents preferred cash as a mode of payment with 40.9% of respondents indicating digital payments as the preferred mode.⁹ Further, 49.7% of the respondents and 44.2% of the respondents indicated cash and digital payments, respectively, as the preferred mode to receive money for payments. The respondents also indicated cash as the preferred mode of payment for small-value transactions, but indicated preference towards digital modes of payments towards higher amounts. The aforesaid statistics indicate that while India is witnessing a gradual proliferation in digital payments, there is a sustained interest and propensity towards cash transactions, especially for small-value transactions.

Given the value proposition of digital payments and the consumer shift towards such payments, it is important to reassess the key enablers for creating a conducive ecosystem for further uptake and sustained usage of such modes of retail payments. Such an ecosystem should strive to pursue the following goals: (a) safety and soundness of payment systems; (b) protecting the interests of retail consumers from the new forms of risks that are presented by such digital payments; and (c) promoting efficiency in the functioning of payment systems by fostering competitive market conditions and encouraging innovations. This in turn will facilitate the development of more customer centric solutions and improve accessibility and adoption of such solutions.

One of the key enablers to meet these goals is the regulatory framework for payment systems. The principal legislation for payments in India i.e. the Payment and Settlement Systems Act, 2007 (“PSS Act”) was enacted more than a decade back when the digital payments market in India was at its nascent stage. The law was primarily enacted to regulate payment systems from a systemic perspective and to confer the RBI with necessary powers to regulate these systems. Therefore, the PSS Act does not take into account the policy goals stated above that are crucial for the operation of retail payments, resulting in the absence of specific provisions dealing with such issues in the PSS Act. While the RBI has time and again sought to address the existing gaps in the primary law through directions issued from time to time, this may not be the optimal solution to address the existing gaps in the law. Such an approach is also not in line with the international best practices where several countries have, along with policy interventions, undertaken efforts to modernise their payments law to adapt to the rapidly evolving industry. Against this background, this Report argues that India needs to reassess the PSS Act taking into account the developments in the retail payments sector since its enactment in 2007 and the future of digital payments in India. By deconstructing the digital payments value chain, tracing global practices in payment system regulation and identifying the existing gaps in the PSS Act, this report argues for a modern retail payment services law in India that is built on the principles of proportionate regulation and balances regulatory flexibility with well-established statutory mandates that can promote competition, innovation and consumer protection.

⁹ Pradip Bhuyan, Jolly Roy and Raja Ram, ‘Retail Payment Habits in India – Evidence from a Pilot Survey’ (*RBI Bulletin*, April 2021) <https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/04AR_26042021C7C9371E047E4AFCACA834ECCBBB1152.PDF> accessed 20 August 2021.

II. Demystifying the Digital Payments Ecosystem

An Introduction to Payment Systems

Broadly, the term “payment system” refers to a set of instruments, rules, procedures, processes and interbank funds transfer systems that facilitate the transfer of money. It encompasses the entity operating the payment system (“payment system operator” or “PSO”) and the participants.¹⁰

Generally, payment systems are classified as either retail or wholesale. A retail payment system handles a large volume of low-value payments for purchase of goods and services by consumers and businesses.¹¹ This may include person-to-person payments (such as transfer of funds to friends and family), person-to-business payments (payment to merchants), business-to-person payments (salary payments) and business-to-business payments.¹² A wholesale payment system executes large-value payment transactions between financial institutions.¹³ This may include payments to settle securities and foreign exchange trades, payments to and from central counterparties, and other interbank transactions.¹⁴ Due to their systemic nature, wholesale payment systems in most countries are owned and operated by central banks. In India, RTGS is owned and operated by the RBI and processes wholesale payments. Payments processed through UPI, Immediate Payment Service (“IMPS”) and card networks are used for retail transactions and are owned and operated by private-sector players. Payment systems that have “the potential to trigger or transmit systemic disruptions” are often referred to as systemically important payment systems (“SIPS”).¹⁵ It may include the sole payment system in a country or systems that mainly handle time-critical, high-value payments.¹⁶ Typically, the RTGS operated by central banks qualify as SIPS and are subject to specific standards of regulation and oversight.

Payment systems are complex markets with multiple participants. Such participants include banks, clearing and settlement systems and payment service providers that offer payment services to the end user. These players may participate in different stages of a payments value chain. Broadly, a payment system infrastructure consists of “front-end” and “back-end arrangements”.¹⁷ In a typical payment transaction, a payment flows through the “front-end” arrangements which is used by a payer to initiate the payment and multiple “back-end” arrangements for clearing and settling payments.¹⁸

¹⁰ Morten Bech and Jenny Hancock, ‘Innovations in Payments’ (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

¹¹ BIS, ‘Central banks and payments in the digital era’, (BIS Annual Economic Report, 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.pdf>> accessed 18 August 2021.

¹² Morten Bech and Jenny Hancock, ‘Innovations in Payments’ (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

¹³ BIS, ‘Central banks and payments in the digital era’, (BIS Annual Economic Report, 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.pdf>> accessed 18 August 2021.

¹⁴ Morten Bech and Jenny Hancock, ‘Innovations in Payments’ (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

¹⁵ A payment system which has “the potential to trigger or transmit systemic disruptions; this includes, among other things, systems that are the sole payment system in a jurisdiction or the principal system in terms of the aggregate value of payments, and systems that mainly handle time-critical, high value payments or settle payments used to effect settlement in other Financial Market Infrastructures (FMI).” See CPSS, BIS, ‘A glossary of terms used in payments and settlement systems’ <<https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>> accessed 18 August 2021.

¹⁶ BIS, ‘A glossary of terms used in payments and settlement systems’ <<https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>> accessed 18 August 2021.

¹⁷ Johannes Ehrentaud, Jermy Prenio, Codruta Boar, et al, ‘Fintech and payments: regulating digital payment services and e-money’ (BIS FSI Insights on policy implementation No 33, 2021) <<https://www.bis.org/fsi/publ/insights33.pdf>> accessed 18 August 2021.

¹⁸ Morten Bech and Jenny Hancock, ‘Innovations in Payments’ (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

- The front-end arrangements consist of the transaction account that provides the source of funds (e.g., bank account); the payment instrument (e.g., cash, card, cheque) and the service channel used to initiate payment that connects the payer and the payee (e.g., bank branch, point-of-sale (POS) terminal, payment application).¹⁹ Generally, banks and non-bank payment service providers offer retail or consumer facing services in the front-end of a payment transaction through digital wallets or mobile interfaces.
- The back-end arrangements focus on clearing and settlement processes in payments. Clearing involves “transmitting, reconciling and, in some cases, confirming transactions prior to settlement.”²⁰ Typically, clearing operations are undertaken by automated clearing houses that are multilateral arrangements to facilitate exchange of payment instructions between PSOs.²¹ Settlement is the “discharge of an obligation in accordance with the terms of the underlying contract.”²² Payments may be settled on a gross basis individually (as done in the RTGS) or on a net basis as a batch, commonly referred to as deferred net settlement.²³

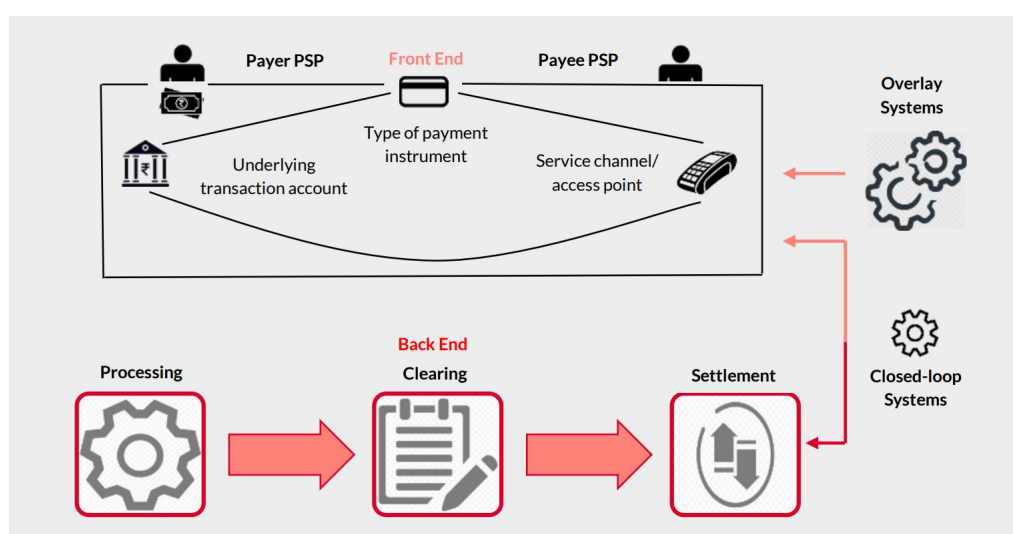


Figure 4: Payments infrastructure elements and arrangements²⁴

Due to technological advancements and changes in consumer preference, the retail payment systems have witnessed entry of new players. The initial changes were witnessed in the front-end arrangements with new ways of initiating payments - mobile payments, contactless payments, etc. This was followed by the development of overlay systems that provide front-end services by using existing instruments (such as credit or debit cards stored in a digital wallet) and payment infrastructure to process, clear and settle payments. This includes services such as Apple Pay, Google Pay, etc.²⁵ Such systems link the front-end application to a consumer’s underlying card or bank account. Advancements in payment technologies have also led to the rise of closed-loop systems (such as Ali

¹⁹ BIS, 'Central banks and payments in the digital era', (BIS Annual Economic Report, 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.pdf>> accessed 18 August 2021.

²⁰ CPSS, BIS, 'A glossary of terms used in payments and settlement systems' <<https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>> accessed 18 August 2021.

²¹ Morten Bech and Jenny Hancock, 'Innovations in Payments' (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

²² CPSS, BIS, 'A glossary of terms used in payments and settlement systems' <<https://www.bis.org/dcms/glossary/glossary.pdf?scope=CPMI&base=term>> accessed 18 August 2021.

²³ Morten Bech and Jenny Hancock, 'Innovations in Payments' (BIS Quarterly Review, March 2020) <https://www.bis.org/publ/qtrpdf/r_qt2003f.pdf> accessed 18 August 2021.

²⁴ BIS, 'Central banks and payments in the digital era' (BIS Annual Economic Report, 24 June 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.htm>> accessed 20 August 2021.

²⁵ BIS, 'Central banks and payments in the digital era', (BIS Annual Economic Report, 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.pdf>> accessed 18 August 2021; Johannes Ehrentraud, Jermy Prenio, Codruta Boar, et al, 'Fintech and payments: regulating digital payment services and e-money' (BIS FSI Insights on policy implementation No 33, 2021) <<https://www.bis.org/fsi/publ/insights33.pdf>> accessed 18 August 2021.

Pay, M-pesa) that provide “front-end to back-end services, have back-end arrangements largely proprietary to their respective firms, and do not interact with or depend much on the existing payments infrastructure.”²⁶

Stages of a Digital Payment Transaction

A retail payment transaction consists of different stages with different players. To break down the front-end and the back-end arrangements discussed above and to examine the stages of a payment chain, this report relies on the five-stage classification outlined by the BIS.²⁷ Stages relating to pre-transaction, authorisation and post transaction usually fall within the front-end arrangements and stages relating to clearing and settlement fall within the back-end arrangements, as discussed above.

| Stage | Description | Indicative list of activities during this stage |
|-------------------------|--|---|
| Pre-transaction | <i>This stage consists of such activities that are required to set up the initial infrastructure to facilitate digital payments transaction. This includes contractual and technological infrastructure to process digital payments.</i> | <ul style="list-style-type: none"> • Provision of payment instruments / devices to consumer (card issuance, delivery and activation, provision of e-money wallet, etc.). • Provision of hardware to accept payment instruments (ATM and POS terminals used for non-cash payments, cheque reader, etc.). • Provision of software to accept payment instruments / devices (web-hosting services, provision of shopping cart software, payment gateway, etc.). • Provision of information security services (digital signature, online transaction security system, etc.). |
| Authorisation | <i>This stage includes such activities that enable payment service providers to authorize / validate payment transactions before it can be completed.</i> | <ul style="list-style-type: none"> • Transaction authorisation (fund verification) - involves activities to verify and confirm if the payer has sufficient funds for the transaction. • Fraud and risk management services to payees - includes verification services (for verifying IP address, card verification), payment instrument authentication, and identity authentication. • Fraud and risk management services to card issuers by monitoring transactions and notifying of potential frauds. |
| Clearing | <i>This stage involves exchange of relevant payment information and claims between the accounts of the payer and the payee, calculation and dissemination of information of claims that needs to be settled.</i> | <i>This includes processes and activities for payments clearing - provision of services to merchants to sort their sales information and submit claims to respective networks; calculation of net positions of members by networks, and transmission of clearing orders.</i> |
| Settlement | <i>This stage relates to final discharge of a valid claim.</i> | <i>It involves the actual movement of funds - i.e., posting of credits and debits in the bank account with the settlement bank and in the accounts of the final payer and payee.</i> |
| Post-transaction | <i>This stage involves processes and activities related to the provision of various value-added services.</i> | <ul style="list-style-type: none"> • Provision of statement for payers such as online bank / card account statements. • Matching invoices and payments. • Provision of dispute processing and chargeback services. • Reporting and data analysis services to merchants and financial institutions. • Ex-post compliance services relating to anti-money laundering and terrorist financing regulation, such as reporting to authorities. |

Table 1: Snapshot of stages of a digital payment transaction²⁸

²⁶ BIS, ‘Central banks and payments in the digital era’ (BIS Annual Economic Report, 2020) <<https://www.bis.org/publ/arpdf/ar2020e3.pdf>> accessed 18 August 2021.

²⁷ CPMI, BIS, ‘Non-banks in retail payments’ (2014) pg.4 <<https://www.bis.org/cpmi/publ/d118.pdf>> accessed 18 August 2021.

²⁸ CPMI, BIS, ‘Non-banks in retail payments’ (2014) <<https://www.bis.org/cpmi/publ/d118.pdf>> accessed 18 August 2021; See also Johannes Ehrentraud, Jermy Prenio, Codruta Boar, et al, ‘Fintech and payments: regulating digital payment services and e-money’ (BIS FSI Insights on policy implementation No 33, 2021) <<https://www.bis.org/fsi/publ/insights33.pdf>> accessed 18 August 2021.

Different entities, including banks and non-banks, participate in different stages of the payments value chain discussed above. The extent of participation of a bank and non-bank may vary depending on the payment instrument in question.

Key Players in the Digital Payments Ecosystem

Traditionally, the payments landscape has been a bank-dominated sector with banks providing most payment services. However, technological innovations have led to the emergence of non-banks that participate in different stages of the payments value chain. The main players offering payment services are: (a) central banks; (b) banks; and (c) non-banks. Non-banks may participate in different capacities - either as an authorised / licensed player providing specific payment services or as an unregulated entity providing support services to authorised players. In India, non-banks participate not only in the front-end arrangement (such as prepaid payment instruments ("PPIs"))²⁹ but also in the back-end services (such as National Payments Corporation of India ("NPCI") for operating UPI, IMPS). A BIS study³⁰ classifies the role of non-banks in a payment transaction into four broad categories based on the stages of the payment chain in which they engage, the type of payment service they provide and their relationship with banks. This report partially relies on such classification to identify the main players in a digital payments ecosystem in India. Needless to say, in any transaction, the payer and the payee, which are the retail consumers and merchants are also important players.

| Category | Description | Illustration |
|---|---|--|
| Front-end providers | <p>They provide an interface between the users of payment services (payers and payees) and traditional clearing and settlement processes.</p> <p>They may participate in the pre-transaction, authorisation or post-transaction stages, but not in the clearing and settlement process.</p> <p>Both banks and non-banks may provide such services.</p> <p>Depending on their role in the actual handling of consumer funds, such entities may or may not require authorisation.</p> | <p>Card acquirers, payment gateway, payment aggregators³¹</p> <p>Third-party application providers, UPI-BHIM App, Google Pay</p> |
| Back-end providers | <p>They provide back-end services to banks or other authorised PSOs, without having any direct relationship with the payer or payee.</p> <p>Such services are provided by way of an outsourcing arrangement. They do not provide clearing and settlement services.</p> <p>Considering such providers provide only back-end services which does not involve handling consumer funds, they are typically not required to be authorised under the law.</p> | <p>Technology service providers; Data center providers</p> <p>Entities that provide data security services or back-office operations, including services relating to audit and compliance</p> |
| Operators of payment systems / issuers | <p>They are licensed / authorised under the payment systems law to provide payment services and / or clearing and settlement services.</p> <p>They work with banks and non-bank payment service providers for clearing and settling transactions in relation to different payment instruments</p> | <p>Central banks operating RTGS</p> <p>Card networks like Visa, Mastercard, etc. that are authorised under the PSS Act in India</p> <p>NPCI, that is authorised under the PSS Act in India, to operate UPI, IMPS, etc.</p> |

²⁹ PPIs are "instruments that facilitate purchase of goods and services, including financial services, remittance facilities, etc., against the value stored therein." RBI, 'Master Directions on Prepaid Payment Instruments (PPIs)' (August 2021) para 2.8 <https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12156> accessed 18 August 2021. (henceforth referred to as "PPI Master Directions")

³⁰ CPMI, BIS, 'Non-banks in retail payments' (2014) pg.4 <<https://www.bis.org/cpmi/publ/d118.pdf>> accessed 18 August 2021.

³¹ 'Payment Aggregators' are "entities that facilitate e-commerce sites and merchants to accept various payment instruments from the customers for completion of their payment obligations without the need for merchants to create a separate payment integration system of their own." 'Payment Gateways' are "entities that provide technology infrastructure to route and facilitate processing of an online payment transaction without any involvement in handling of funds." RBI, 'Guidelines on Regulation of Payment Aggregators and Payment Gateways (Updated as on November 17, 2020)' (2020) paras 1.1.1. and 1.1.2. <<https://rbi.org.in/Scripts/NotificationUser.aspx?Id=11822&Mode=0>> accessed 18 August 2021. (henceforth referred to as "PA Guidelines")

| | | |
|-----------------------------|---|---|
| End-to-end providers | They provide all the services referred to above, with payers and payees maintaining a direct relationship with them. They are in the nature of "closed-loop systems" discussed above. | Operators of three-party card systems Providers of certain e-money services such as PayPal, M-pesa |
|-----------------------------|---|---|

Table 2: Overview of the key players in a digital payment ecosystem³²

Overview of the digital payment systems in India

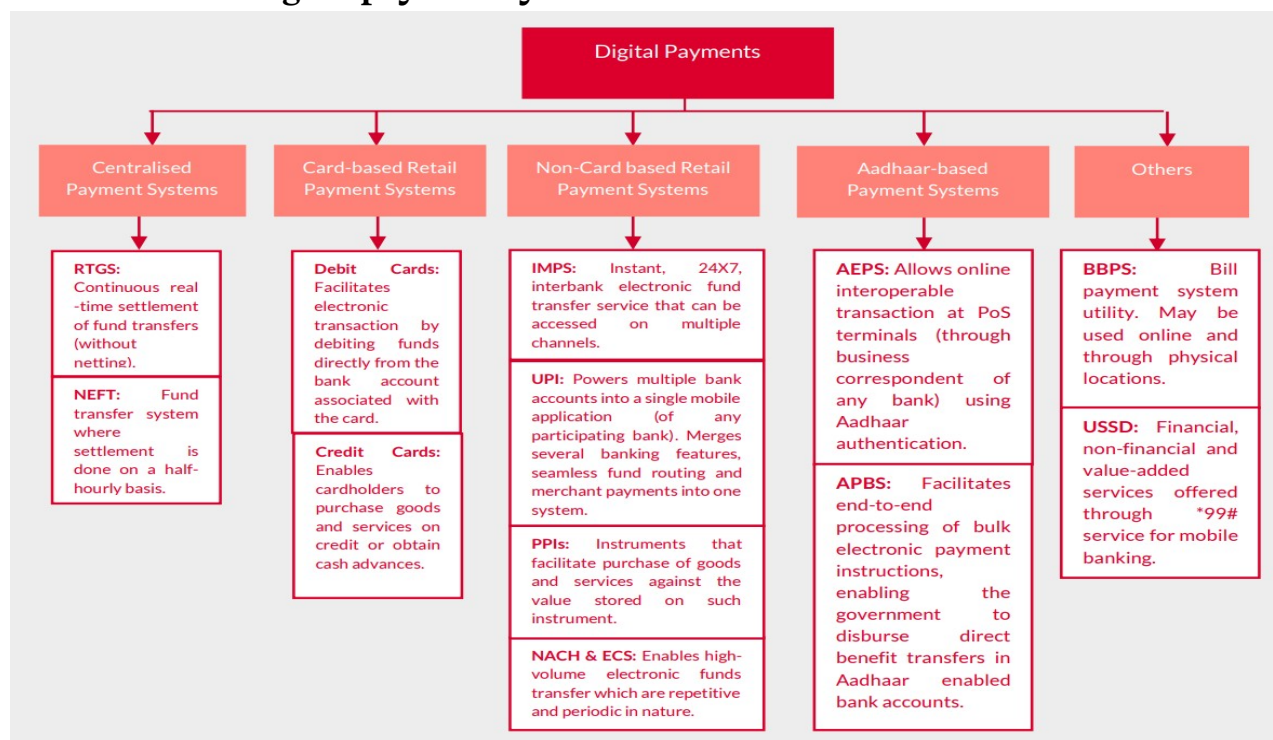


Figure 5: Snapshot of digital payment systems in India

Table 3 below outlines the operators and the participants of some key payment systems in India and also sets out the regulatory status of such systems.³³

| Category | Payment System | Operator | Participants / Membership | | Authorisation under the PSS Act |
|------------------------------------|----------------|----------|---------------------------|-----------------|---|
| | | | Banks | Non-Banks | |
| Centralised Payment Systems | RTGS | RBI | √ ³⁴ | √ ³⁵ | PSS Act exempts RBI operated payment systems from authorisation ³⁶ |

³² CPMI, BIS, 'Non-banks in retail payments' (2014) pg.4 <<https://www.bis.org/cpmi/publ/d118.pdf>> accessed 18 August 2021.

³³ RBI, 'Policy Paper on Authorisation of New Retail Payment Systems' (2019) <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/ANRPS21012019A8F5D4891BF84849837D7D611B7FFC58.PDF>> accessed 18 August 2021.

³⁴ RBI, 'Real Time Gross Settlement (RTGS) System Regulations, 2013' (October 2013) <https://rbidocs.rbi.org.in/rdocs/RTGS/PDFs/RTGSB111013_2013.pdf> accessed 18 August 2021; RBI, 'Master Directions on Access Criteria for Payment Systems (Updated as on July 28, 2021)' (2021) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10833&Mode=0>> accessed 19 August 2021.

³⁵ Non-bank entities with access to centralised payment systems are standalone primary dealers, clearing corporations of stock exchanges, central counterparty (CCIL), retail payment system organisation (NPCI), select financial institutions (NABARD, EXIM Bank) and DICGC. Other non-banks that have been allowed access are PPI issuers, card network and white label ATM operators are permitted direct access subject to guidelines. RBI, 'Access for Non-banks to Centralised Payment Systems' (28 July 2021) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12133&Mode=0>> accessed 18 August 2021.

³⁶ Exemption under the section 4 of the Payment and Settlement Systems Act, 2017 permits the RBI to commence and operate payment systems without requiring authorisation.

| | | | | | |
|------------------------|-----------------------|-----------------------------------|----------------|-----------------|--|
| | NEFT | RBI | ✓ | ✓ ³⁷ | PSS Act exempts RBI operated payment systems from authorisation |
| Cards | Debit Card | Banks ³⁸ | Not applicable | | Banks can issue debit cards as a part of their banking license and no prior approval of RBI is required |
| | Credit Card | Banks and NBFCs ³⁹ | | | Banks meeting certain net worth requirements can issue credit cards. No prior approval is required. Certain NBFCs are allowed to issue credit cards with prior approval of RBI ⁴⁰ |
| | Card Payment Networks | Non-banks | ✓ | ✓ | Authorised under the PSS Act |
| Fund Transfer | IMPS | NPCI ⁴¹ | ✓ | X | NPCI is authorized under the PSS Act to operate the IMPS |
| | UPI | NPCI | ✓ | X | NPCI is authorized under the PSS Act to operate the UPI |
| | PPIs | Banks and Non-Banks ⁴² | ✓ | ✓ | Non-banks must obtain RBI authorisation and banks must take RBI's approval under the PSS Act |
| | ECS ⁴³ | NPCI | ✓ | X | NPCI is authorized under the PSS Act to operate the NACH |
| Aadhaar based payments | AEPS ⁴⁴ | NPCI | ✓ | X | NPCI is authorized under the PSS Act to operate the AePS |
| | APBS ⁴⁵ | | | | |
| | BBPS ⁴⁶ | NPCI | ✓ | ✓ | NPCI is authorized under the PSS Act to operate the Bharat Bill Payment Central Unit. Non-banks have also |

³⁷ Non-bank entities with access to centralised payment systems are standalone primary dealers, clearing corporations of stock exchanges, central counterparty (CCIL), retail payment system organisation (NPCI), select financial institutions (NABARD, EXIM Bank) and DICGC. Other non-banks that have been allowed access are PPI issuers, card network and white label ATM operators are permitted direct access subject to guidelines. RBI, 'Access for Non-banks to Centralised Payment Systems' (28 July 2021) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12133&Mode=0>> accessed 18 August 2021.

³⁸ Co-branded cards can be issued by banks in partnership with a non-bank. Non-bank entity's role is limited to marketing, distribution of the cards or providing access to the cardholder. RBI, 'Master Circular on Credit Card, Debit Card and Rupee Denominated Co-branded Pre-paid Card Operations of Banks and Credit Card issuing NBFCs' (1 July 2015)

<<https://www.rbi.org.in/scripts/NotificationUser.aspx?Mode=0&Id=9838>> accessed 18 August 2021.

³⁹ RBI, 'Master Direction - Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016' (1 September 2016) <<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/45MD01092016B52D6E12D49F411DB63F67F2344A4E09.PDF>> accessed 18 August 2021.

⁴⁰ Notably, issuance of debit and credit cards are regulated under the Banking Regulation Act 1949 (henceforth referred to as "BR Act") and the Reserve Bank of India Act 1934 (henceforth referred to as "RBI Act") and not the PSS Act.

⁴¹ RBI, 'Certificates of Authorisation issued by the Reserve Bank of India under the Payment and Settlement Systems Act, 2007 for Setting up and Operating Payment System in India' (23 August 2021) <<https://m.rbi.org.in/Scripts/PublicationsView.aspx?id=12043>> accessed 30 August 2021.

⁴² Both, the banks and the non-banks may issue Small PPIs and Full-KYC PPIs. RBI, 'Master Directions on Prepaid Payment Instruments (PPIs)' (August 2021) para 2.8 <https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12156> accessed 18 August 2021.

⁴³ Electronic Clearing Service (ECS) is "an electronic mode of payment / receipt for transactions that are repetitive and periodic in nature." ECS facilitates "bulk transfer of monies from one bank account to many bank accounts or vice versa using the services of a ECS Centre at a ECS location". RBI, 'FAQs on Electronic Clearing Service' <<https://www.rbi.org.in/commonman/Upload/English/FAQs/PDFs/ECS140311.pdf>> accessed 18 August 2021.

⁴⁴ Aadhaar Enabled Payment System (AEPS) is "a payment service empowering a bank customer to use Aadhaar as his/her identity to access his/ her respective Aadhaar enabled bank account and perform basic banking transactions like balance enquiry, cash deposit, cash withdrawal, remittances through a Business Correspondent." NPCI, 'AePS FAQs' <<https://www.npci.org.in/what-we-do/aeps/faqs#:~:text=It%20is%20an%20electronic%20way,Aadhaar%20number%20and%20biometrics%2FOTP>> accessed 18 August 2021.

⁴⁵ Aadhaar Payment Bridge System (APBS) is "a component of National Automated Clearing House (NACH) that uses Aadhaar number for electronic crediting of government subsidies and benefits in Aadhaar-linked bank account." RBI, 'Booklet on Payment Systems' (2021) <<https://www.rbi.org.in/Scripts/PublicationsView.aspx?id=20315>> accessed 18 August 2021.

⁴⁶ Bharat Bill Payment System (BBPS) is a "system driven by National Payments Corporation of India (NPCI) that offers interoperable and accessible bill payment service to consumers via digital (bank channels) as well as through a network of agents & bank branches." NPCI, 'Bharat BillPay FAQs' <<https://www.npci.org.in/what-we-do/aeps/faqs#:~:text=It%20is%20an%20electronic%20way,Aadhaar%20number%20and%20biometrics%2FOTP>> accessed 18 August 2021.

Table 3: Payment systems, system providers and system participants in India⁴⁷

Digital Payments Transaction Flow - Illustrations

This section provides an overview of the transaction flow of some commonly used digital payment solutions - debit card transaction, IMPS fund transfer and payment by UPI.

Illustration 1: How does a debit card transaction work?

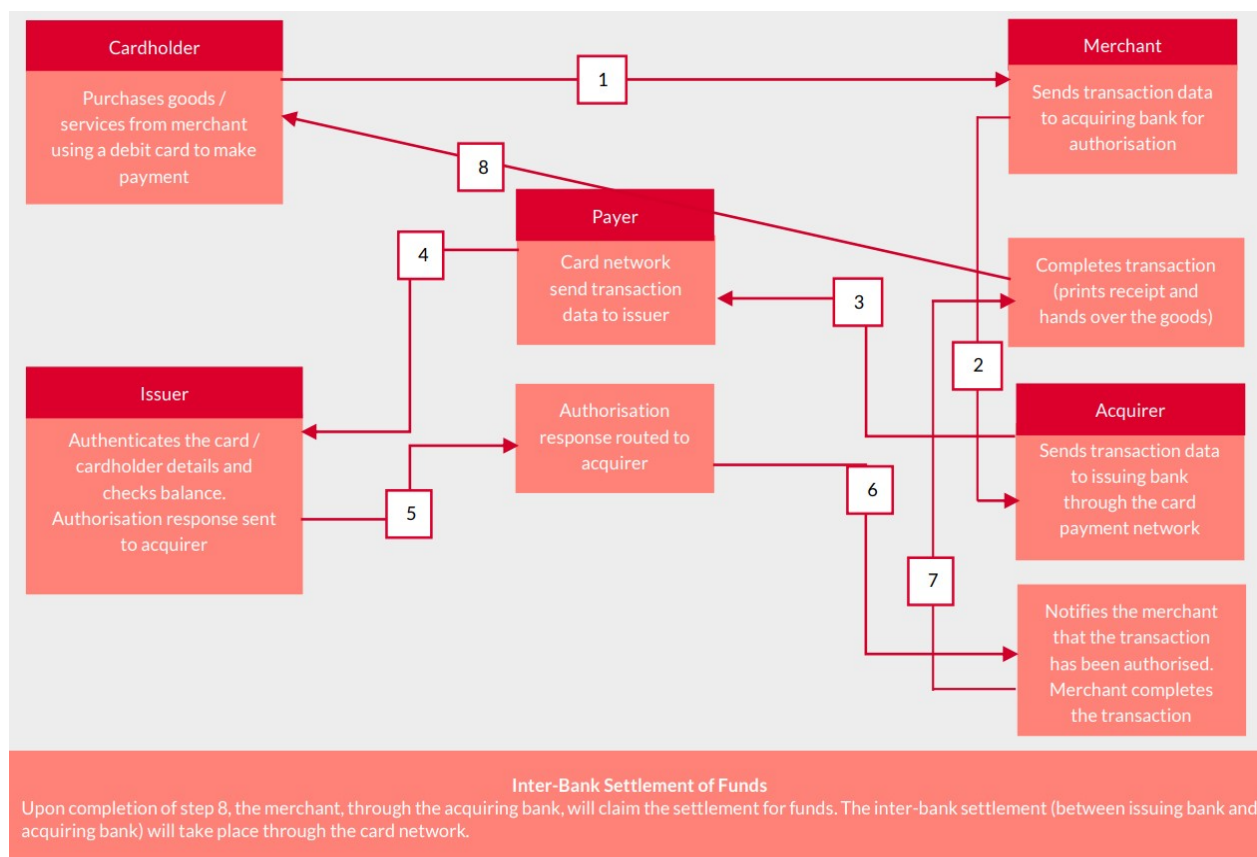


Figure 6: Snapshot of a debit card transaction in a four-party card network model⁴⁸

| Main participants in a debit card transaction for payment to merchant in a four-party model of card networks |
|--|
| Merchant: Entity selling goods and services |
| Cardholder: Consumer purchasing goods and services from a merchant |
| Acquiring Bank: The bank which has installed the POS terminal at the merchant location |
| Card Network: Entities that route and settle funds such as Visa, MasterCard, etc. |
| Issuing Bank: The bank which has issued the card to the consumer |

⁴⁷ RBI, 'Policy Paper on Authorisation of New Retail Payment Systems' (2019) <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/ANRPS21012019A8F5D4891BF84849837D7D611B7FFC58.PDF>> accessed 18 August 2021.

⁴⁸ RBI, 'Concept Paper on Card Acceptance Infrastructure' (2016) <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/MDRDBEDA36AB77C4C81A3951C4679DAE68F.PDF>> accessed 4 April 2020.

Illustration 2: How does an IMPS Transaction work?

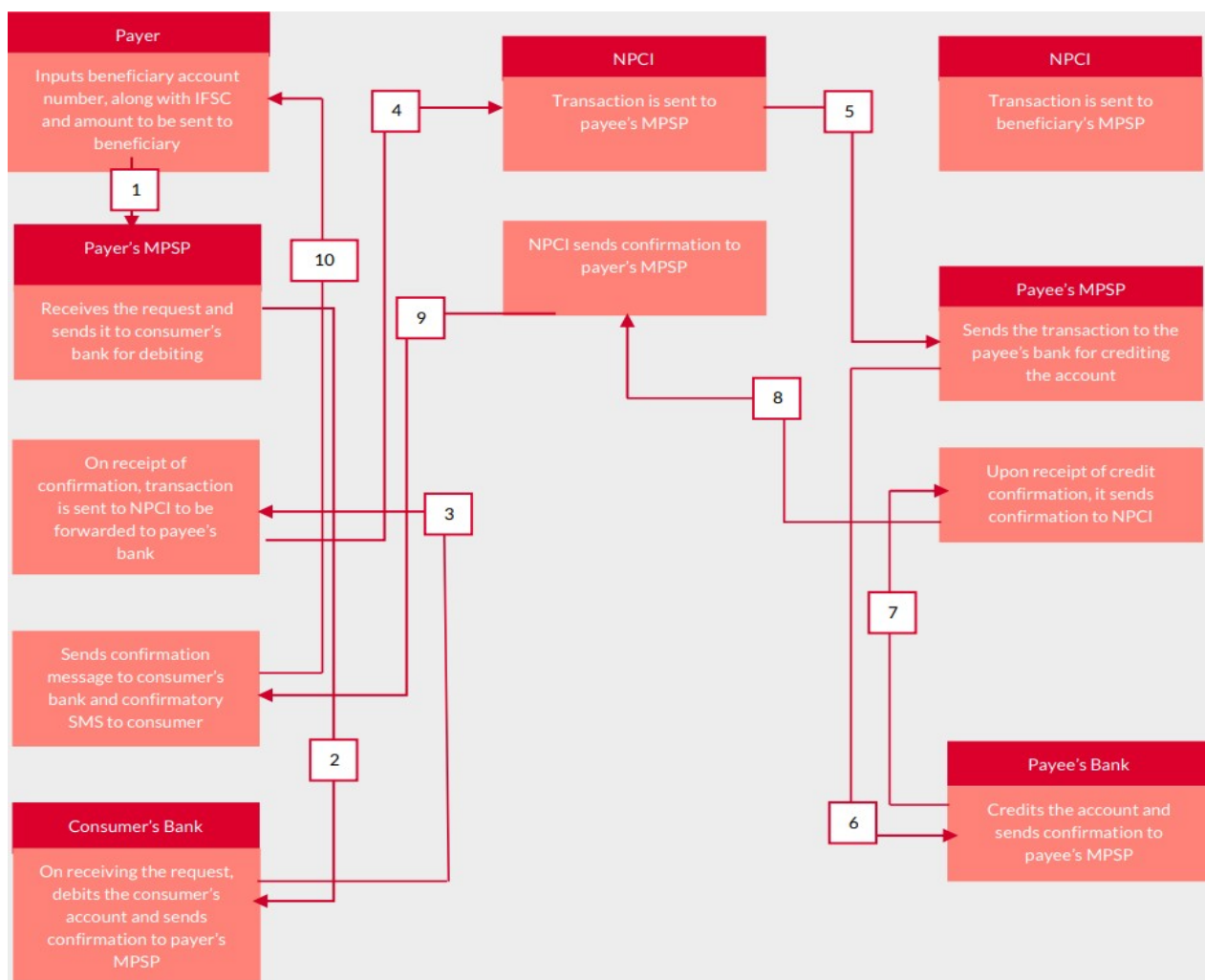


Figure 7: Snapshot of a payment transaction through IMPS⁴⁹

| Main participants in an IMPS transaction for person-to-person fund transfer | |
|---|--|
| Payer: | Person whose account is debited to transfer funds to the payee |
| Payee: | Person whose account is credited with funds from the payer's account |
| Mobile Payment Service Provider ("MPSP"): | Telecom provider of either the payer or payee, as indicated |
| Payer Bank - | Bank of the person making the payment |
| Payee Bank - | Bank of the person receiving the payment |

How does a UPI Transaction work?

A UPI transaction can work on a two, three or four-party model. There can be a maximum of four entities consisting of two payment service providers (referred to as 'PSP' in the Figure 8 below) that will act as the interface providers for end consumers / merchants and two banks acting as remitter and beneficiary bank. Figure 8 describes a typical UPI person to person transaction using a four-party model.

⁴⁹ Please note that this transaction flow is based on the IMPS Procedural Guidelines released by NPCI and that was earlier made available on their website. However, the guidelines have now been removed from the website. We had reached out to NPCI to access the latest procedural guidelines, but have not received any response.

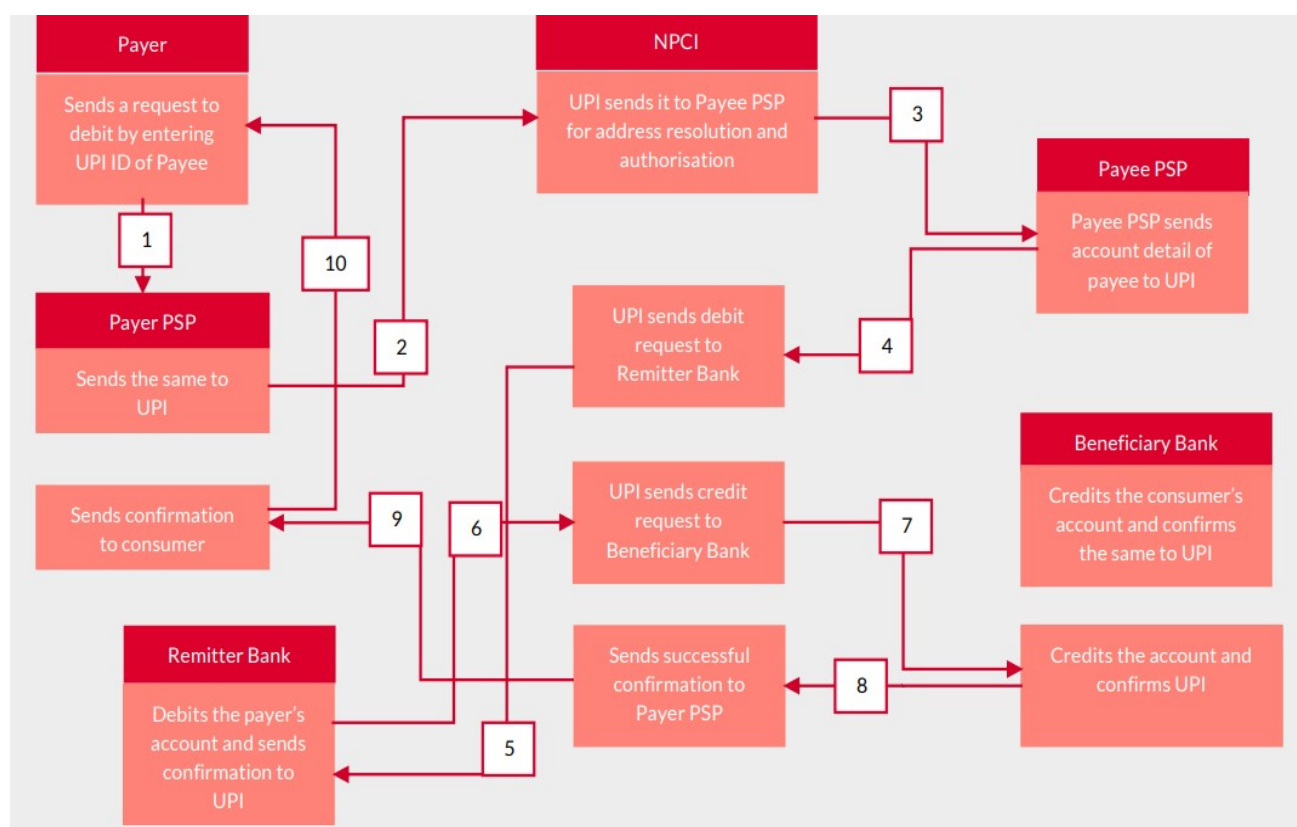


Figure 8: Snapshot of a UPI person-to-person transaction using a four-party model⁵⁰

| Main participants in a UPI Transaction |
|--|
| Payer: Payer is an app user of Payer PSP (say Bank A), but has a bank account with the Remitter Bank (say Bank B) |
| Payee: Payee is an app user of Payee PSP (say Bank C), but has a bank account with the Beneficiary Bank (say Bank D). |
| Payer PSP: It is broadly responsible for on-boarding consumers and creating their UPI ID through which they can carry out relevant transactions. |
| Payee PSP: It is broadly responsible to on-board consumers and allow them to receive funds on the basis of allocated UPI ID. |
| Remitter Bank: All UPI users need to have a bank account with a UPI enabled bank. This is the bank where the payer has an account and which will get debited. The remitting bank is also responsible to issue and store the UPI PIN set by the consumer. |
| Beneficiary Bank: This is the bank, where the payee holds an account for the purposes of receiving funds in a UPI transaction. |
| Third Party Applications – Non-banks that participates in a UPI transaction by partnering with a bank that is already enabled on UPI and develop its own PSP. Example, Google Pay, PhonePe, Amazon Pay, etc. |

Digital Payments and Charges

The retail payment system is a two-sided market. Both merchants (payees) and consumers (payers) in the payment network have different needs, incentives, and reasons for using the network, and the payment service providers in between have to coordinate these needs and incentives.⁵¹ While doing so, the payment service providers

⁵⁰ Please note that this transaction flow is based on the UPI Procedural Guidelines released by NPCI and that was made available on their website. However, the guidelines have now been removed from the website. We had reached out to NPCI to access the latest procedural guidelines, but have not received any response.

⁵¹ Consultative Group to Assist the Poor (CGAP), 'The challenge of two-sided markets in merchant payments' (October 2019) <<https://www.cgap.org/research/publication/challenge-two-sided-markets-merchant-payments>> accessed 1 April 2021.

themselves bear costs and take credit risks to facilitate a digital payment. To an extent, they seek to offset such costs by charging fees from consumers and merchants for facilitating their role in a digital transaction.

Merchant Discount Rate and Interchange Fee

The charges involved in a digital payment transaction are not standard across the world and may vary depending on the commercial arrangement between the parties. Broadly, such charges include merchant discount rate (“MDR”) (also known as ‘merchant service charges’ or ‘merchant service fee’), interchange fee and other service charges / convenience fee.

Currently, there is no standard definition of these charges. Broadly, MDR is the fee charged to a merchant by the acquiring entity, which has set up a POS or card acceptance machine at the merchant location to accept digital payments.⁵² MDR is a major source of revenue in the card business. It comprises of other costs such as the interchange fee, scheme fee payable to the card network, and other costs incurred by the acquirer.⁵³ ‘Interchange fee’ is the fee paid by the acquiring entity to the card issuing bank⁵⁴ to cover handling costs, fraud and the risk involved in approving the payment.⁵⁵ Typically, a portion of the MDR is also paid to the card payment network by the acquiring entity as ‘scheme fee’. After deducting the interchange fee and the scheme fee from the MDR paid by a merchant, the acquiring entity retains the outstanding amount as ‘acquirer’s commission’.

A payment transaction may also consist of additional fees which are imposed by merchants on consumers such as surcharge fee and convenience fee.⁵⁶ Surcharge fee is the fee imposed by a merchant on a consumer for processing a transaction through a particular payment mode, and such fee differs for different payment methods.⁵⁷ Convenience fee is charged to consumers by a merchant for providing online payments facility to consumers, and is payment method agnostic.⁵⁸ The value of ‘convenience fee’ remains standard for all like transactions regardless of the form / method of payment used.

MDR and Interchange fee: Legal Position in India

In India, MDR is regulated by the RBI pursuant to its powers under the PSS Act. It has been imposed to promote acceptance of digital payment modes by a wider set of merchants, especially small merchants. Ceilings on MDR were first introduced in 2012 by the RBI, wherein banks were advised to cap the MDR for debit card transactions.⁵⁹ The MDR rates were temporarily revised in December 2016 to promote the rise in card payments amid the demonetization drive in India.⁶⁰ No MDR limits on transactions made using credit cards have been prescribed given the underlying risk the issuing bank undertakes when fulfilling the credit card transactions.⁶¹

While earlier MDR circulars sought to cap the rates subject to transaction value, in 2017, the RBI issued a circular (“2017 MDR Circular”) to revise the MDR regulatory framework for debit card transactions by determining MDR

⁵² RBI, ‘Concept Paper on Card Acceptance Infrastructure’ (2016)

<<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/MDRDBEDA36AB77C4C81A3951C4679DAE68F.PDF>> accessed 4 April 2021.

⁵³ RBI, ‘Concept Paper on Card Acceptance Infrastructure’ (2016)

<<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/MDRDBEDA36AB77C4C81A3951C4679DAE68F.PDF>> accessed 4 April 2021.

⁵⁴ Committee on Digital Payments, ‘Medium Term Recommendations to Strengthen Digital Payments Ecosystem’ (2016) pg.144 <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed 19 March 2021.

⁵⁵ To illustrate, when a consumer / cardholder swipes a card or makes a payment at POS terminal for purchasing goods and services, the issuing bank is required to transfer the funds from consumer’s bank account to the merchant’s account as held with acquiring institution.

⁵⁶ Ashish Das, ‘To surcharge or not to surcharge! – The plight of small and medium merchants’ (IIT Bombay Technical Report, 2019) <http://www.math.iitb.ac.in/~ashish/workshop/surcharge-2019_03_03.pdf> accessed 10 April 2021.

⁵⁷ Australian Competition & Consumer Commission, ‘Q&A: Payment Surcharges’ <<https://www.accc.gov.au/business/pricing-surcharging/payment-surcharges/qa-payment-surcharges>> accessed 10 April 2021.

⁵⁸ Ashish Das, ‘To surcharge or not to surcharge! – The plight of small and medium merchants’, (IIT Bombay Technical Report, 2019) <http://www.math.iitb.ac.in/~ashish/workshop/surcharge-2019_03_03.pdf> accessed 10 April 2021.

⁵⁹ RBI, ‘Benchmarking India’s Payment Systems’ (2019)

<<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/BIPS04062019CE3C72E9873244ED8BAAE9C8FC5955A8.PDF>> accessed on 19 March 2021.

⁶⁰ RBI, ‘Special Measures up to March 31, 2017: Rationalisation of Merchant Discount Rate (MDR) for Transactions up to Rs 2,000’ (December 2016) <<https://rbi.org.in/Scripts/NotificationUser.aspx?Id=10780&Mode=0>> accessed on 19 March 2021.

⁶¹ RBI, ‘Merchant Discount Rates Structure for Debit Card Transactions’ (June 2012) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=7304&Mode=0>> accessed on 19 March 2021.

caps based on the size of the merchant (by turnover). The RBI hiked the MDR rate citing that the step will help POS infrastructure providers in recovering costs they incur in providing the technology.⁶² Banks have also been advised to ensure that merchants on-boarded by them do not pass on MDR charges to consumers while accepting payments through debit cards. The 2017 circular prescribed the following rates:⁶³

| Merchant Category | MDR for debit card transactions (as a % of transaction value) | |
|--|--|--|
| | Physical POS infrastructure including online card transactions | QR code-based card acceptance infrastructure |
| Small merchants (with turnover upto INR 20 lakh during the previous financial year) | Not exceeding 0.40% (MDR cap of INR 200 per transaction) | Not exceeding 0.30% (MDR cap of INR 200 per transaction) |
| Other merchants (with turnover above INR 20 lakh during the previous financial year) | Not exceeding 0.90% (MDR cap of INR 1000 per transaction) | Not exceeding 0.80% (MDR cap of INR 1000 per transaction) |

Table 4: MDR for debit card transactions

Meanwhile, notifications were also issued by the RBI⁶⁴ and the Ministry of Electronics and Information Technology⁶⁵ to reimburse MDR costs for specific payments. In 2019, by way of the Finance (No. 2) Act⁶⁶ 2019, the government introduced the following provisions in the Income Tax Act, 1961 and the PSS Act:

- Insertion of section 269SU to the Income Tax Act, 1961: This mandated businesses with total sales, turnover or gross receipts exceeding INR 500 million in previous FY to provide their consumers with modes of payment for (i) debit card powered by RuPay, (ii) UPI (BHIM-UPI); and (iii) UPI Quick Response Code (BHIM-UP QR Code).⁶⁷
- Insertion of section 10A to the PSS Act: This prohibited banks and system providers from imposing any charge on a payer, or a beneficiary receiving payment, through the electronic modes of payment prescribed under section 269SU of the Income Tax Act, 1961.⁶⁸ This implied that banks and other system providers could not impose MDR on merchants for accepting payments through the modes discussed above.

Post the introduction of these provisions, many stakeholders have voiced their concerns against the zero MDR policy in relation to select payment products operated by NPCI. They argue that MDR constitutes a major source

⁶² Joel Rebello, 'RBI defends hike in minimum MDR charges' (*The Economic Times*, 13 December 2017) <<https://economictimes.indiatimes.com/industry/services/retail/rbi-defends-hike-in-minimum-mdr-charges/articleshow/62057315.cms?from=mdr>> accessed 8 July 2021.

⁶³ RBI, 'Rationalisation of Merchant Discount Rate (MDR) for Debit Card Transactions' (December 2017) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11183&Mode=0>> accessed 19 March 2021.

⁶⁴ In February 2017, RBI announced its decision to absorb the MDR charges in respect of debit card transactions charged by acquiring banks on payments made to Government of India. RBI reimbursed MDR charges upto INR 0.1 million to acquiring banks in respect of debit card transactions made by consumers to government. RBI, 'Reimbursement of Merchant Discount Rate' (16 February 2017) <<https://rbi.org.in/Scripts/NotificationUser.aspx?Id=10860&Mode=0>> accessed 31 March 2021.

⁶⁵ Following RBI's February 2017 circular, the Ministry of Electronics and Information Technology (MeitY) notified a scheme in December 2017, to exempt MDRs for merchants on low-value transactions, with the aim of promoting digital payments acceptance among the small-scale businesses where the transaction amounts are generally of small size. Pursuant to the scheme, the government reimbursed these MDR costs to acquiring banks for a period of two years starting with effect from 1 January 2018. MeitY, 'Subsidising MDR Charges on Debit Cards/ BHIM-UPI / Aadhar Pay Transactions of Value Less Than or Equal to Rs 2000' (27 December 2017) <http://meit.gov.in/writereaddata/files/gazette_notification_on_subsidizing_mdr_charges.pdf> accessed on 19 March 2021.

⁶⁶ The Finance (No. 2) Act, 2019 <<https://egazette.nic.in/WriteReadData/2019/209695.pdf>> accessed on 19 March 2021.

⁶⁷ The Income Tax Act, 1961, ss. 269SU and 271DB [Section 269SU: Every person, carrying on business, shall provide facility for accepting payment through prescribed electronic modes, in addition to the facility for other electronic modes, of payment, if any, being provided by such person, if his total sales, turnover or gross receipts, as the case may be, in business exceeds fifty crore rupees during the immediately preceding previous year; Section 271DB: Any shops, business firms or companies with an annual turnover of over INR 50 crores who do not provide digital payment facilities to its consumers as prescribed by Section 269SU, will be liable to pay a penalty of INR 5,000/- per day for such failure.]

⁶⁸ The 'prescribed electronic modes' of payment for the purpose of Section 269SU are "(i) Debit Card powered by RuPay; (ii) Unified Payments Interface (UPI) (BHIM-UPI); and (iii) Unified Payments Interface Quick Response Code (UPI QR Code) (BHIM-UPI QR Code)." The Income Tax Rules, 1962, rule 119AA.

of revenue for acquirers, and the zero MDR policy will cause significant revenue losses for them.⁶⁹ This may disincentivise acquirers and hinder the growth of the digital payments industry. Further, there is also a concern that zero MDR could be extended to all NPCI products which may disincentivise banks from adopting NPCI's payment instruments.⁷⁰ Certain industry players have also raised the concern that the zero MDR policy benefits only large merchants (with annual turnover more than INR 50 crore), though it is actually the smaller merchants that need this relaxation to easily adopt digital payments.⁷¹ In the past, several government committees have studied the MDR regulation in India and recommended that perhaps India may reconsider its present stance on regulating MDR caps and should regulate interchange fee. For further details, please see the discussion in the section on the "MDR and Interchange Fee – Indian and International Perspective".

Digital Payments Acceptance: How are merchants and consumers charged?

Merchants

Except for payments through the specified payment modes mentioned above, merchants have to pay MDR to an acquiring entity on every digital payment transaction carried out by a consumer. Such rates are negotiated between merchants and acquiring entities subject to RBI's prescriptions in the 2017 MDR Circular. To enable the acceptance of digital payments for online purchases of goods and services, merchants may also be required to tie-up with different payment service providers, including payment gateways, payment aggregators, non-bank wallet providers, etc. Therefore, in addition to the MDR and applicable goods and services tax ("GST") on MDR, merchants may also be subjected to other charges such as POS setup fee and installation charges, fees for rental and maintenance of POS terminals, payment gateway fee, etc. These are commercially agreed between a merchant and a payment service provider, and are not publicly disclosed. In many cases, such payment service providers may also provide value-added services for which the rates are commercially negotiated between parties.

Consumers

The RBI has instructed banks to ensure that the merchants on-boarded by them do not pass MDR to their end-consumers.⁷² Prior to 1 July 2019, the RBI levied some charges on banks for processing transactions using RTGS and National Electronic Funds Transfer ("NEFT").⁷³ However, with effect from 1 July 2019, the RBI has waived the processing charges levied by it on member banks for transactions processed through RTGS and NEFT systems to provide impetus to digital funds movement. It has further advised banks to pass on these benefits to their

⁶⁹ Samreen Ahmed, 'MDR waiver to hit fintechs, payments companies' business model', (*Business Standard*, 29 January 2021) <https://www.business-standard.com/article/finance/mdr-waiver-to-hit-fintech-payments-firms-business-model-119123001025_1.html> accessed 18 August 2021.

⁷⁰ Anandita Singh Mankotia and Ashwin Manikandan, 'SBI, NPCI seek 'Visa power' for RuPay cards', (*The Economic Times*, 4 January 2020) <<https://economictimes.indiatimes.com/industry/banking/finance/banking/sbi-npci-seek-visa-power-for-rupay-cards/articleshow/73092976.cms>> accessed 18 August 2021.

⁷¹ Arti Singh, "You are helping the rich get richer": The MDR waiver has a chilling message for card swipes', (*The Economic Times*, 24 June 2019) <<https://economictimes.indiatimes.com/prime/fintech-and-bfsi/you-are-helping-the-rich-get-richer-the-mdr-waiver-has-a-chilling-message-for-card-swipes/primearticleshow/70355253.cms>> accessed 18 August 2021.

⁷² RBI, 'Rationalisation of Merchant Discount Rate (MDR) for Debit Card Transactions' (6 December 2017) <<https://rbidocs.rbi.org.in/rdocs/notification/PDFs/MDR06122017317CE333007D406A9002F5A119229563.PDF>> accessed 4 August 2021.

⁷³ HDFC Bank, 'Common Fees and Charges for Savings Account' <<https://www.hdfcbank.com/personal/save/accounts/savings-account/fees-and-charges>> accessed 4 August 2021; Kotak Mahindra Bank, 'Fees and Charges' <<https://www.kotak.com/en/personal-banking/erstwhile-ing-vysya/savings-accounts/orange-savings-account/fees-and-charges.html>> accessed 4 August 2021; ICICI Bank, 'Common Service Charges' (ICICI Bank) <<https://www.icicibank.com/service-charges/common-service-charges.page>> accessed 4 August 2021; State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Non Credit Related Service Charges' <<https://www.pnbindia.in/Non-Credit-Related-Service-Charges.html>> accessed 18 August 2021; Central Bank of India, 'Service Charges and Fees' <<https://www.centralbankofindia.co.in/en/service-charges-fees>> accessed 18 August 2021. See also Nikhil Agarwal, 'NEFT, RTGS, transfer charges to be waived for savings account, RBI issues order' (Livemint, 18 December 2019) <<https://www.livemint.com/money/personal-finance/neft-rtgs-transfer-charges-to-be-waived-for-savings-account-rbi-issues-order-11576579893524.html>> accessed 18 August 2021.

consumers.⁷⁴ This has resulted in many banks waiving the charges for consumers transferring fund using RTGS and NEFT systems through online channels (viz. internet banking and/ or mobile apps of the banks).⁷⁵ In December 2019, the RBI further directed banks to not levy any charges on consumers that transfer funds from their savings account using NEFT system through online channels.⁷⁶

The Report has examined the charges imposed by banks and other payment service providers on merchants and consumers. For this purpose, the Report relies on schedule of charges on payment transactions as publicly displayed by different banks and non-banks payment service providers. Key findings from the review are provided in the Annexure A to the Report.

MDR & Interchange Fee – Indian and International Perspective

For the purposes of this section, the regulatory position related to MDR and interchange fee of thirteen (13) international jurisdictions have been surveyed. The international jurisdictions reviewed are a mix of advanced economies and emerging economies - Australia, Argentina, the United States of America, the United Kingdom, the European Union, Brazil, Canada, China, South Korea, Japan, Mexico, South Africa, and Singapore. These countries have been selected for the review due to the two-fold reasons: (a) the RBI has selected these jurisdictions for its exercise of benchmarking India's payment systems wherein it assessed India's progress against payment systems and instruments in major countries; and (b) the RBI considers payment systems in these countries to be robust, diverse and efficient.⁷⁷ Based on a review of the regulatory frameworks of select jurisdictions, the approaches adopted by countries can be classified into three broad categories.

Jurisdictions that regulate interchange fee

Out of all the surveyed jurisdictions, it has been observed that regulators in the majority of jurisdictions regulate interchange fee as opposed to MDR. Such jurisdictions include Australia, Argentina, Brazil, China, the European Union ("EU"), Mexico, South Africa, the United Kingdom ("UK") and the United States of America ("US"). All these jurisdictions regulate the interchange fee by way of capping it upto certain value of percentage of the transaction amount. Out of these jurisdictions, it has been noted that the US and Mexico cap the interchange fee for debit transactions only.

Most of these jurisdictions appear to have introduced such regulations after witnessing a history of antitrust litigations and investigations against international card schemes that indicated manipulation of interchange fee.⁷⁸

⁷⁴ RBI, 'National Electronic Funds Transfer (NEFT) and Real Time Gross Settlement (RTGS) System' (11 June 2019) available at <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11586&Mode=0>> accessed 4 August 2021

⁷⁵ HDFC Bank, 'Common Fees and Charges for Savings Account' <<https://www.hdfcbank.com/personal/save/accounts/savings-account/fees-and-charges>> accessed 4 August 2021; Kotak Mahindra Bank, 'Fees and Charges' <<https://www.kotak.com/en/personal-banking/erstwhile-ing-vysya/savings-accounts/orange-savings-account/fees-and-charges.html>> accessed 4 August 2021; ICICI Bank, 'Common Service Charges' <<https://www.icicibank.com/service-charges/common-service-charges.page>> accessed 4 August 2021; State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Non Credit Related Service Charges' <<https://www.pnbindia.in/Non-Credit-Related-Service-Charges.html>> accessed 18 August 2021; Central Bank of India, 'Service Charges and Fees' <<https://www.centralbankofindia.co.in/en/service-charges-fees>> accessed 18 August 2021. See also Nikhil Agarwal, 'NEFT, RTGS, transfer charges to be waived for savings account, RBI issues order' (Livemint, 18 December 2019) <<https://www.livemint.com/money/personal-finance/neft-rtgs-transfer-charges-to-be-waived-for-savings-account-rbi-issues-order-11576579893524.html>> accessed 18 August 2021.

⁷⁶ RBI, 'Furthering Digital Payments – Waiver of Charges – National Electronic Funds Transfer (NEFT) System' (16 December 2019) <<https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=11756&Mode=0>> accessed 15 August 2021.

⁷⁷ RBI, 'Benchmarking India's Payment Systems', (2019) pg. 3

<<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/BIPO4062019CE3C72E9873244ED8BAAE9C8FC5955A8.PDF>> accessed on 19 March 2021.

⁷⁸ US Federal Trade Commission, 'Roundtable on Competition and Efficient Usage of Payment Cards' (30 May 2006) <<https://www.ftc.gov/sites/default/files/attachments/us-submissions-oecd-and-other-international-competition-fora/CompetitionEfficiencyUsageUnitedStates.pdf>> accessed 18 August 2021; European Commission, 'Antitrust: Commission welcomes Court judgment confirming that Mastercard's payment card interchange fees are anti-competitive' (11 September 2014) <https://ec.europa.eu/commission/presscorner/detail/en/MEMO_14_528> accessed 18 August 2021; Reserve Bank of Australia, 'Review of Card Payments Regulation' <<https://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/conclusions-paper-may2016/introduction.html>> accessed 18 August 2021; South African Reserve Bank, 'Card results of the Interchange Determination

These jurisdictions witnessed international card schemes dominating the markets as card issuing banks preferred such schemes that offer high interchange fee. Consequently, issuing banks preferred to issue their consumers with the cards of international schemes. Therefore, merchants were left with no option, but to accept cards with these international card schemes.⁷⁹

The European Commission in its memo on 'Payment Services Directive and Interchange Fees Regulation: frequently asked questions' sets out its rationale for capping of interchange fee and its impact on market.⁸⁰ It notes that "the level playing field for interchange fee will facilitate market entry and increase competition to benefit consumers and retailers." It further notes that "due to the competitive pressure domestic acquirers would have an interest in offering acceptance facilities at lower fee to merchants." Notably, it has been observed that in all the select jurisdictions that regulate interchange fee, the value of CIC to GDP (%) is lower than India.⁸¹

Jurisdictions that regulate MDR

Broadly, it may be noted that there are fewer jurisdictions like India that regulate merchant service fee or MDR. Out of all the surveyed jurisdictions, South Korea and Argentina have been found to regulate the merchant service fee or MDR. South Korea caps merchant service fee on credit card transactions.⁸²

As discussed, it is often argued that MDR capping may act as a disincentive for the acquiring entities as higher unregulated interchange fee end up leaving thin margins for acquirers within the capped MDR. For instance, Argentina for long struggled in attracting and incentivizing large numbers of acquiring entities and to promote competition in its digital payments industry.⁸³ In view of this, the 'Banco Central de la Republica Argentina' or 'Central Bank of Argentina Republic' (BCRA) has ultimately introduced regulations on interchange fee in 2017 with the aim to lower barriers to entry to new acquirers and incentivizing them with higher margins and profits.⁸⁴

In case of India, several committees in the past have suggested the Indian government to reconsider regulation of MDR and move towards the regulation of interchange fee. In 2016, the 'Committee on Digital Payments', headed by former finance secretary Ratan P. Watal ("Committee on Digital Payments"), noted that MDR is essential for the sustained growth of the digital payments industry and acts as an incentive for the stakeholders. The committee observed that capping the MDR "may ultimately hamper the growth of the payments industry."⁸⁵ The committee

Project - Phase 2' (20 March 2014) <<https://www.resbank.co.za/en/home/publications/publication-detail-pages/media-releases/2014/6155>> accessed 18 August 2021.

⁷⁹ It may be observed that in opinion of these jurisdictions, the interchange fees were found to constitute a floor for merchant fees that were set out by issuing banks, below which there remains no scope for smaller merchants to negotiate, resulting in higher costs to them. It was further found out that in these jurisdictions such high interchange fees have contributed in past as an entry barrier for new domestic card schemes that are unable to offer such higher interchange fees unlike internationally dominant card schemes. Reserve Bank of Australia, 'Questions and Answers- Card Payment Regulation' <<https://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/q-and-a/card-payments-regulation-qa-conclusions-paper.html#interchange-fees-q3>> accessed 18 August 2021; European Commission, 'Payment Services Directive and Interchange Fee Regulation: frequently asked questions' (24 July 2013) <https://ec.europa.eu/commission/presscorner/detail/en/MEMO_13_719> accessed 18 August 2021.

⁸⁰ European Commission, 'Payment Services Directive and Interchange Fee Regulation: frequently asked questions' (24 July 2013) <https://ec.europa.eu/commission/presscorner/detail/en/MEMO_13_719> accessed 18 August 2021.

⁸¹ BIS, Red Book Statistics, "Payments and financial market infrastructures statistics' (2021) <https://www.bis.org/statistics/full_bis_rb_csv.zip> accessed 21 March 2021.

⁸² Not much information is available in translated version about South Korea's regulation of interchange fee. Financial Services Commission, 'FSC Reforms Card Processing Fee Rates' (26 November 2018) <<https://www.fsc.go.kr/eng/pr010101/22195?srchCtgr=4&curPage=&srchKey=&srchText=&srchBeginDt=&srch>> accessed 18 August 2021. We have relied on machine-translated English version.

⁸³ Argentina regulated MDRs at 3% for credit cards and 1.5% for debit cards. The country struggled in attracting large number of acquirers as they were being excessively charged by VISA and MasterCard that maintained a huge proportion of the market and continued offering higher interchange fees to issuing banks leading to anti-competitive interchange pricing in overall. Organisation for Economic Cooperation and Development (OECD) Regional Centre for Competition in Latin America, 'Newsletter No. 1' (June 2020) pg.24-29 <<https://www.oecd.org/daf/competition/june-2020-rcc-lima-newsletter.pdf>> accessed 18 August 2021.

⁸⁴ Directorate for Financial and Enterprise Affairs Competition Committee, 'Working Party No. 2 on Competition and Regulation: Co-operation between Competition Agencies and Regulators in the Financial Sector' (OECD, 2017) Pg 6 Para 20 <https://www.argentina.gob.ar/sites/default/files/cooperation_between_competition_agencies_and_regulators_in_the_financial_sector.pdf> accessed 18 August 2021.

⁸⁵ Committee on Digital Payments, 'Medium Term Recommendations to Strengthen Digital Payments Ecosystem' (2016) Pg 77 <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed on 19 March 2021.

also observed that MDR caps are one of the reasons for less deployment of POS terminals in India.⁸⁶ Hence, it recommended that MDR should be market driven, and suggested that interchange fee may be regulated on an evidence-based approach. Similarly, the RBI's committee on 'Deepening Digital Payments', chaired by Nandan Nilekani, recommended that "the regulator should adjust the interchange rate and let the market compete on MDR ultimately growing the acceptance ecosystem rather than inhibiting it."⁸⁷

Jurisdictions that do not regulate MDR and interchange fee

Out of the surveyed jurisdictions, there are jurisdictions like Japan, Singapore and Canada where the card acceptance charges are unregulated. In these jurisdictions, there is no legislation or regulation that prescribes any cap for either MDR or interchange fee. In Singapore and Japan, it may be observed that currently card payment network operators themselves set the default interchange fee rate and the rate is used when a 'bilateral interchange fee' is not set between an issuer and an acquirer.⁸⁸

The Reserve Bank of Australia ("RBA") notes that the tendency for interchange rates to rise to high levels is most apparent in such unregulated jurisdictions.⁸⁹ In Canada, the dispute between merchants and card payment networks on high interchange fee resulted in the Canadian Department of Finance intervening to secure voluntary commitments from Visa and MasterCard to reduce interchange fee for domestic consumer cards and narrow the range of interchange rates charged to businesses.⁹⁰

⁸⁶ Committee on Digital Payments, 'Medium Term Recommendations to Strengthen Digital Payments Ecosystem' (2016) Pg 116 <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed 19 March 2021.

⁸⁷ RBI, 'High Level Committee on Deepening of Digital Payments' (2019) Pg. 13 <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/CDDP03062019634B0EEF3F7144C3B65360B280E420AC.PDF>> accessed 21 March 2021.

⁸⁸ Japan Fair Trade Commission, Survey on Credit Card Market' (March 2019) <<https://www.jftc.go.jp/en/pressreleases/yearly-2019/March/SurveyonCreditCardMarketReport.pdf>> accessed 18 August 2021 (Japan); Jamie Lee, 'Visa to reinstate card payments on Comfort cabs from January 2016 (Amended)' (*The Business Times*, 16 December 2015) <<https://www.businesstimes.com.sg/banking-finance/visa-to-reinstate-card-payments-on-comfort-cabs-from-january-2016-amended>> accessed 9 April 2021 (Singapore).

⁸⁹ Till the time Department of Finance, Canada, had not intervened to secure voluntary commitments from Visa and MasterCard to reduce interchange fees, Canada had among the highest card payments acceptance fees in the world such that Canadian merchants that accepted Visa and MasterCard credit cards paid a card acceptance fee from 1.5 to 3% of each purchase. Government of Canada, 'Visa and MasterCard's anti-competitive rules' (8 May 2012) <<https://www.competitionbureau.gc.ca/eic/site/cb-bc.Nsf/eng/03467.html>> accessed 18 August 2021; The United States where there is no regulation of card payments acceptance charges on credit cards, the credit card interchange rates in the MasterCard system are as high as 3.25 per cent plus 10 cents, implying that – after scheme fees and acquirer margin – some merchants may pay over 3½ per cent in merchant service fees for high rewards cards. RBA, 'Questions and Answers- Card Payment Regulation' <<https://www.rba.gov.au/payments-and-infrastructure/review-of-card-payments-regulation/q-and-a/card-payments-regulation-qa-conclusions-paper.html#interchange-fees-q3>> accessed 18 August 2021.

⁹⁰ Government of Canada, 'New Agreements to Deliver Lower Credit Card Costs for Small and Medium-Sized Businesses' (9 August 2018) <<https://www.canada.ca/en/department-finance/news/2018/08/new-agreements-to-deliver-lower-credit-card-costs-for-small-and-medium-sized-businesses.html>> accessed 18 August 2021.

III. Regulating Payment Services - Indian and Global Perspective

A conducive legal framework is a key enabler for promotion of digital payments. Taking into account the rapid transformation of the digital payments sector, many jurisdictions have reassessed and modernized their legal and regulatory framework for payment services, using activity-based and risk-based approaches. Modernization efforts have aimed to foster safety, efficiency, innovation and competition in the retail payments space.⁹¹ This section examines the legal and regulatory framework applicable to payment systems in India as well as the select jurisdictions.

Regulating Payment Systems - Indian Perspective

In India, the payment systems are governed by the RBI under the PSS Act. As per section 4 of the PSS Act, a PSO (other than RBI) must be authorised by RBI to commence or operate a payment system in India. RTGS, NEFT and Securities Settlement Systems for the government securities, which are owned and operated by the RBI, do not require authorization. To qualify as a 'payment system' under the PSS Act, two conditions must be met: (a) the system must enable payment to be effected between a payer and a beneficiary; and (b) it must be involved in clearing, payment or settlement service or all of them. While the term 'settlement' has been defined,⁹² the terms 'payment' and 'clearing' have not been defined. Pursuant to section 4 of the PSS Act, the RBI has authorised different categories of PSOs to operate different payment systems - retail payment organisation (NPCI), card payment networks (Visa, MasterCard, etc), cross-border money transfers entities - in bound (Western Union, Moneygram, etc.), ATM networks (NPCI, Euronet Services, etc.), PPI issuers (Amazon Pay, Mobikwik, etc.), white label ATM operators, Instant Money Transfer operators, trade receivable discounting system (TReDs) platform providers and BBPOUs.⁹³ All these entities are governed by the provisions of the PSS Act.

The PSS Act was primarily enacted to "provide for the regulation and supervision of payment systems in India and to designate the RBI as the authority for the purpose and for matters connected therewith or incidental thereto." A review of the provisions of the PSS Act indicates that it focuses on the following issues:

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|--|
| <i>Empowers the RBI to regulate and authorise payment systems. The scope of the Act is limited to regulation of "payment system", "system provider" and "system participant".⁹⁴</i> |
| <i>Outlines the conditions and procedure for being authorised as a payment system under the PSS Act.</i> |
| <i>Empowers the RBI to determine standards for payment systems and guidelines for efficient management of such systems.</i> |
| <i>Empowers the RBI to call for information, inspect system providers and participants and carry out audits.</i> |
| <i>Empowers the RBI to issue directions to regulate the payment systems or in the interest of management or operation of any of the payment systems or in public interest.</i> |
| <i>Outlines duties of system provider:</i> |

⁹¹ Tanai Khiaonarong and Terry Goh, 'Fintech and Payments Regulation: Analytical Framework' (*International Monetary Fund*, 29 May 2020) <<https://www.imf.org/en/Publications/WP/Issues/2020/05/29/Fintech-and-Payments-Regulation-Analytical-Framework-49086>> accessed 18 August 2021.

⁹² "Settlement" means settlement of payment instructions and includes the settlement of securities, foreign exchange or derivatives or other transactions which involve payment obligations. The PSS Act, section 2(1)(n).

⁹³ RBI, 'Certificates of Authorisation issued by the Reserve Bank of India under the Payment and Settlement Systems Act, 2007 for Setting up and Operating Payment System in India' (23 August 2021) <<https://m.rbi.org.in/Scripts/PublicationsView.aspx?id=12043>> accessed 30 August 2021.

⁹⁴ "Payment System" means a system that enables payment to be effected between a payer and a beneficiary, involving clearing, payment or settlement service or all of them, but does not include a stock exchange. The PSS Act, section 2(1)(i); "System Provider" means a person who operates an authorised payment system. The PSS Act, section 2(1)(q); "System Participant" means a bank or any other person participating in a payment system and includes the system provider. The PSS Act section 2(1)(p).

- *Duty to disclose terms and conditions to system participants.*
- *Duty to keep documents confidential.*
- *Duty to obtain the RBI's authorisation for change in the payment system which would affect the structure or the payment operation of the payment system.*

Provisions on netting and finality of settlement and protection of consumer funds held by certain payment systems.

Procedure for the settlement of disputes between system participants, between any system participant and the system provider or between system providers.

Offences and penalties for contravention of the provisions of the Act.

Pursuant to its powers under the PSS Act, the RBI has issued the Payment and Settlement Systems Regulations 2008 ("PSS Regulations 2008") that lays down the procedural requirements for commencing or carrying on a payment system. It covers matters like form of application for authorization under the PSS Act and lays down the regular compliance requirements, such as furnishing of returns / documents / other information, furnishing of accounts and balance sheets by system provider etc. to the RBI. However, most of the substantive legal prescriptions for payment systems and PSOs have been issued by the RBI through circulars / notifications pursuant to its power to determine standards and power to issue direction, generally, under section 10 and section 18, respectively, of the PSS Act. Such a position is contrary to payment systems law in many countries where substantive provisions and obligations on payment service providers are provided in the primary statute with the subordinate legislation being relied on for clarifying or giving effect to such substantive obligations set out in the primary statute.

Regulating Payment Services | Comparing Global and Indian Regulatory Approach

This section outlines the key findings from the review of the legal frameworks governing payments across the UK, Singapore, Australia, Canada, Hong Kong, Indonesia and Brazil ("Surveyed Jurisdictions"). The key findings from the review of the Surveyed Jurisdictions were then studied against the Indian framework discussed above. The Surveyed Jurisdictions include countries with low cash transactions, high volume of cashless payments as well as countries that have in recent years undertaken efforts to modernise their payment systems law. To evaluate the digital payments penetration, the report relies on data relating to the following:

- Value of CIC as a percentage of GDP: This indicates the extent of use of cash as a payment instrument in the economy. It is assumed that having high CIC to GDP (%) indicates cash is preferred as a payment instrument.⁹⁵
- Volume of cashless payments: Volume of cashless payments is the indicator of overall figure of retail payments (in value and numbers) transacted using payment services / instruments (card and e-money payments only)⁹⁶ other than cash.⁹⁷

Principal legislation governing payment services

Position in Surveyed Jurisdictions

- *Many Surveyed Jurisdictions (UK, Singapore, Canada, Australia and Brazil) have two legislations governing payment systems and services, with one law governing payment services (consumer facing retail payment services) and the other law focusing on SIPS / large-value payment systems or systemically important clearing and settlement systems from a financial stability perspective.*
- *Singapore has two principal legislations:*

⁹⁵ RBI, 'Benchmarking India's Payment Systems', (2019) pg. 21

<<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/BIPS04062019CE3C72E9873244ED8BAAE9C8FC5955A8.PDF>> accessed on 19 March 2021.

⁹⁶ For the purposes of this report 'cashless payments' constitute the overall retail payments transacted using card and e-money payments inside the country. It is important to note that in the BIS Red Book, 'cashless payments' also include retail payments transacted using credit transfers, direct debit, and cheques other than card and e-money payments.

⁹⁷ CPMI, BIS, 'Methodology of the statistics on payments and financial market infrastructures in the CPMI countries (Red Book statistics)' (August 2017) <<https://www.bis.org/cpmi/publ/d168.pdf>> accessed 18 August 2021.

- The Payment Services Act 2019 ("Singapore PS Act") regulates payment systems and payment service providers. The law seeks to provide legal certainty, consumer safeguards and encourage innovation in the payments sector.⁹⁸ The law also empowers the Monetary Authority of Singapore ("MAS") for closer supervision of SIPS and "systems wide payment system" ("SWIPS").⁹⁹
- The Payment and Settlement Systems (Finality and Netting) Act ("Singapore FN Act") provides a framework for protection of designated payment and settlement systems from disruptions that may generate systemic risks and protect transactions netted and settled in these designated systems. Notably, the law does not directly cover the regulation of consumer-facing retail payment service providers.¹⁰⁰
- Similarly, Australia also has two principal legislations:
 - The Payment Systems (Regulation) Act, 1998 ("Australia PSR Act") empowers the RBA to regulate designated payment systems where it considers such designation to be in the public interest. Since Australia adopts a co-regulatory model of payments regulation, the extent of regulation is minimal. Designated payment systems are subject to an access regime, regulatory standards, dispute resolution and directions as issued by the RBA.
 - The Payment Systems and Netting Act 1998 ("Australia PSN Act") allows the RBA to exercise its powers where it is necessary in the interest of systemic stability of the financial system. Under this law, the RBA has the power to grant approvals to RTGS systems and to multilateral netting arrangements. These approvals provide certain legal protections for transactions undertaken in such systems.
- The UK also has two principal legislative frameworks:
 - The Financial Services (Banking Reforms) Act, 2013 ("UK FSBR Act") created the Payment Systems Regulator ("PSR") to promote competition, innovation and protect user interest in the payments market. It empowers the PSR to regulate payment systems designated by the Her Majesty's Treasury ("HM Treasury") under the UK FSBR Act ("Regulated Payment Systems") to promote the objectives highlighted above.
 - The Payment Services Regulation 2017 ("UK PS Regulation") that was enacted to transpose the second European Union Payment Services Directive into the national legislation seeks to regulate "payment service providers".
- In Brazil, the primary laws only provide the principles that the Banco Central Do Brasil ("BCB") i.e. the Central Bank of Brazil, needs to observe to regulate different payment systems and its constituents. This is supplemented by allied BCB circulars and Brazilian National Monetary Council ("CMN") Resolutions that provide prescriptive rules on authorisation and regulation of such payment systems and its constituents:
 - The Law no. 10,214/ 2001 (the "Brazil Payment Systems Law") read with the CMN Resolution 2882 and the BCB Circular 3057 provides regulation for the Brazilian payment, clearing and settlement system.¹⁰¹
 - The Law no. 12,865/ 2013 (the "e-Payments Law") along with a set of circulars¹⁰² and CMN resolutions provides the authorisation framework for "payment schemes" (i.e., the set of rules governing payment services, such as credit or debit card transactions), and "payment institutions" (i.e., entities providing services such as issuance of electronic money and associated services).¹⁰³
- Both Hong Kong and Indonesia has one primary legislation to regulate payment systems. In case of Hong Kong, the Payment Systems and Stored Value Facilities Ordinance (cap. 584) ("PSSVF Ordinance") empowers the Hong Kong Monetary Authority ("HKMA") to regulate clearing or

⁹⁸ MAS, 'Payment Services Act' (15 April 2019) <<https://www.mas.gov.sg/regulation/acts/payment-services-act>> accessed 19 August 2021.

⁹⁹ MAS, 'Payment Systems' <<https://www.mas.gov.sg/regulation/payments/payment-systems>> accessed 19 August 2021.

¹⁰⁰ Ong Ye Kung, "Payment and Settlement Systems (Finality and Netting) (Amendment) Bill" - Second Reading Speech by Mr Ong Ye Kung, Minister for Education (Higher Education and Skills) and Second Minister for Defense on behalf of Mr. Tharman Shanmugaratnam, Deputy Prime Minister and Minister-in-charge of the Monetary Authority of Singapore' (8 January 2018) <<https://www.mas.gov.sg/news/speeches/2018/payment-and-settlement-systems-finality-and-netting-amendment-bill>> accessed 16 August 2021.

¹⁰¹ Law no. 10214, of March 27, 2001 (2001)

<https://www.bcb.gov.br/content/financialstability/paymentssystem_docs/Laws/Law10214.pdf> accessed 19 August 2021 (henceforth referred to as 'Brazil Payment Systems Law'); BCB Circular no. 3057, of August 31, 2001 (2001)

<https://www.bcb.gov.br/content/financialstability/paymentssystem_docs/Laws/Circular3057amended.pdf> accessed 19 August 2021. CMN Resolution 2882, effective August 30, 2001 (2001)

<<https://www.bcb.gov.br/Pom/Spb/Ing/InstitucionalAspects/Resolution2882amended.pdf>> accessed 19 August 2021. We have relied on the machine-translated English versions of these laws as provided by the BCB on its website.

¹⁰² CMN Resolutions. 4,282 and 4,283, and Circulars Nos. 3,680, 3,681, 3,682 and 3,683. We have relied on the machine-translated English version of these CMN Resolutions and BCB Circulars; Walter Stuber, 'The New Rules for Payment Institutions and Payment Arrangements In Brazil' (Mondaq, 20 November 2013) <<https://www.mondaq.com/brazil/financial-services/275958/the-new-rules-for-payment-institutions-and-payment-arrangements-in-brazil>> accessed 19 August 2021.

¹⁰³ Law no. 12,865, of October 9, 2013 (2013)

<https://www.bcb.gov.br/content/financialstability/paymentssystem_docs/Laws/Law12865.pdf> accessed 19 August 2021.

settlement systems or retail payment systems and stored value facilities ("SVFs").¹⁰⁴ Indonesia has recently passed the BI Regulation No. 22/23/PBI/2020 on restructuring of the regulatory framework of payment systems ("Indonesia BI Regulations").¹⁰⁵

- Canada has enacted the Retail Payment Activities Act 2021 ("Canada RPA Act") which is yet to come into force.¹⁰⁶ The Canada RPA Act seeks to build a new retail payments oversight framework to ensure the protection of end users and to build confidence in the retail payments ecosystem in Canada. This will work in tandem with the Payment Clearing and Settlement Act ("Canada PCS Act") that provides the legislative authority and power to Bank of Canada to oversee clearing and settlement systems (also called financial market infrastructures or FMIIs).

Position in India

- The legal framework in India can be traced back to the PSS Act. The legal framework of most of the Surveyed Jurisdictions focuses on ensuring safety and soundness of payment systems, with a specific framework for transactions processed through SIPS. Contrary to the Indian position, the laws of most of the Surveyed Jurisdictions also focus on promoting competition and protection of consumer interest. Further, unlike India most of the Surveyed Jurisdictions (other than Brazil) set out the substantive provisions governing payment systems and payment services, including positive obligations on entities providing such services in the primary statute.

Who is regulated under the law?

Position in Surveyed Jurisdictions

- Many Surveyed Jurisdictions recognise different players in the payments value chain. In the case of UK and Singapore, the law makes a distinction between payment systems and payment service providers. Broadly, 'payment systems' refer to systems that facilitate fund transfer. Payment service providers usually include players that provide new and emerging forms of consumer facing retail payment services, such as payment gateways, e-wallet providers, etc.
- For instance, in Singapore:
 - The Singapore PS Act provides for licensing and regulation of "payment service providers" and oversight of "payment systems". "Payment service providers" are defined to mean any person who provides such "payment services" that are specified in the Singapore PS Act. These services are - account issuance, domestic money transfer, cross-border money transfer, merchant acquisition, e-money issuance, digital payment token and money-changing. On the other hand, a "payment system" means a "funds transfer system or other system that facilitates the circulation of money, and includes any instruments and procedures that relate to the system."
 - Under the Singapore PS Act, the MAS also has the power to designate SIPS, against which it can exercise specific powers. For further details, please see the discussion below.
 - The Singapore FN Act regulates designated systemically important systems. These "systems" are established for "clearing or settlement of payment obligations" or "clearing, settlement or transfer of book-entry securities".
- In the UK:
 - Like the Singapore PS Act, the UK PS Regulations also regulates "payment services". This includes services relating to the execution of payment transactions (such as direct debits, credit transfers and card payments), issuing of payment instruments (credit or debit cards), acquiring payment transactions, money remittance, "account information services"¹⁰⁷ and "payment initiation services".¹⁰⁸ The UK PS Regulations also define "payment system" to mean a funds transfer system with formal and standardised arrangements and common rules for the processing, clearing and settlement of payment transactions.

¹⁰⁴ The PSSVF Ordinance (2015) <<https://www.elegislation.gov.hk/hk/cap584>> accessed 18 August 2021.

¹⁰⁵ This regulation is effective from 1 July 2021. Bank Indonesia, 'BI Reform Regulation of Indonesia's Payment System' (8 January 2021) <https://www.bi.go.id/id/publikasi/ruang-media/news-release/Pages/sp_230621.aspx> accessed 19 August 2021. Indonesia BI Regulations (2020) <https://www.bi.go.id/id/publikasi/peraturan/Documents/PBI_222320.pdf> accessed 18 August 2021. We have relied on the machine-translated English version of the law.

¹⁰⁶ 'Division 7 of the Bill C-30: Retail Payment Activities Act' (Parliament of Canada, 2021) <<https://www.parl.ca/DocumentViewer/en/43-2/bill/C-30/royal-assent#ID0E0WIOEA>> accessed 19 August 2021. Bank of Canada, 'Retail Payments Supervision' (2021) <<https://www.bankofcanada.ca/core-functions/financial-system/retail-payments-supervision/#:~:text=Under%20the%20Retail%20Payment%20Activities,protecting%20users%20from%20certain%20risks>> accessed 18 August 2021.

¹⁰⁷ "An Account Information Service Provider (AISP) lets you see all your account information from different bank accounts in one place online or in a mobile app". Financial Conduct Authority (FCA), 'Account information and payment initiation services' (8 December 2017) <<https://www.fca.org.uk/consumers/account-information-and-payment-initiation-services>> accessed 19 August 2021.

¹⁰⁸ "A Payment Initiation Service Provider (PISP) lets you pay companies directly from your bank account rather than using your debit or credit card through a third party such as Visa or MasterCard." FCA, 'Account information and payment initiation services' (8 December 2017) <<https://www.fca.org.uk/consumers/account-information-and-payment-initiation-services>> accessed 19 August 2021.

- The regulations do not cover inter-bank settlement. It does not apply to payment transactions carried on within a payment or securities settlement system between payment service providers and settlement agents, central counterparties, clearing houses, central banks or other participants in the system.
- The UK FSBR Act regulates payment systems designated by the HM Treasury under the Act. The HM Treasury may designate a payment system only if it is satisfied that deficiencies in the design of the system, or disruption in its operation, would be likely to have serious consequences for “service users”. Currently, there are 8 Regulated Payment Systems, out of which 6 are inter-bank systems and 2 are card networks.¹⁰⁹
- In Australia, under the Australia PSR Act, the RBA regulates designated payment systems and “purchased payment facilities”.¹¹⁰ Payment system is defined to mean “a funds transfer system that facilitates the circulation of money, and includes any instruments and procedures that relate to the system.” Such payment systems are designated if such designation is necessary in public interest to do so. Regulation is sparingly applied as there is a presumption in favour of industry-led regulation. Participants of designated payment systems are subject to an access regime, standards, dispute resolution and directions issued by the RBA.
- In Hong Kong, the PSSVF Ordinance provides for a licensing framework for SVFs (which includes e-wallets) as well as a designation framework for clearing and settlement systems or retail payment systems on specific grounds.¹¹¹
- The Canada RPA Act empowers the Bank of Canada to supervise “payment service providers”. These include a variety of entities that perform electronic payment functions, such as payment processors, digital wallets, currency transfer services and other payment technology companies that offer any of the following services - providing and maintaining a payment account for fund transfer, holding funds, initiating electronic funds transfer, authorizing or transmitting instructions about an electronic funds transfer, clearing or settling electronic funds transfers.
- The Indonesia BI Regulations also makes a distinction between payment systems, payment service providers and payment infrastructure providers. As per the regulations:
 - “payment system” is defined as a system that includes a set of rules, institutions, mechanisms, infrastructure, sources of funds for payments, which are used to carry out the transfer of funds in order to fulfil obligations arising from economic activity.
 - “payment system service providers” can be classified into: (a) payment service providers i.e., banks or non-bank entities that provide services to facilitate payment transactions to users; and (b) payment system operators i.e., parties that operate infrastructure as facilities that can be used to move funds for the interests of their members.
 - Bank Indonesia is empowered to supervise and regulate such payment service providers (such as electronic money issuers, e-wallet providers, and payment gateway providers) and payment system infrastructure operators (“PIP”) (such as switching providers, clearing providers, and settlement providers).¹¹²
- In Brazil, the BCB regulates the authorized “Brazilian Payment Systems”, as provided under Article 1 of the Brazil Payment Systems Law.¹¹³ The “Brazilian Payment Systems” comprises of the entities, systems and procedures related to the clearing and settlement systems processing funds transfers and transactions, including the instant payment system (PIX).¹¹⁴ Under the e-Payments Law, the BCB regulates (i) the payment schemes (card networks such as Brasil Card, MasterCard and Visa)¹¹⁵ and (ii) payment institutions (BCB licensed entities providing services such as

¹⁰⁹ These are Bacs, C&C (Cheque & Credit), CHAPS, Faster Payments Scheme (FPS), LINK, Northern Ireland Cheque Clearing (NICC), MasterCard, Visa Europe (Visa).

¹¹⁰ This may include gift cards and pre-paid mobile phone accounts.

¹¹¹ Clearing and settlement system’ means “a system established for — (a) the clearing or settlement of payment obligations; or (b) the clearing or settlement of obligations for the transfer of book-entry securities, or the transfer of such securities.” ‘Retail payment system’ means “(a) a system or arrangement for the transfer, clearing or settlement of payment obligations relating to retail activities (whether the activities take place in Hong Kong or elsewhere), principally by individuals, that involve purchases or payments; and (b) includes related instruments and procedures”. The PSSVF Ordinance, section 2.

¹¹² Ahmad Fikri Assegaf and Indira Yustikania, ‘Regulating How We Pay, Bank Indonesia Issues New Rule On Payment System’ (Mondaq, 3 February 2021) <<https://www.mondaq.com/shareholders/1032486/regulating-how-we-pay-bank-indonesia-issues-new-rule-on-payment-system>> accessed 18 August 2021. Baker McKenzie, ‘Indonesia: Digital “stargazing” through 2021: Bank Indonesia overhauls payment system regulations’ (11 January 2011) <<https://www.lexology.com/library/detail.aspx?g=9d8fe513-ccfc-4ebe-bd36-01ce2eced894>> accessed 19 August 2021.

¹¹³ The Brazil Payment Systems Law, art 1. We have relied on the translated English versions of the law as provided by the BCB on its website.

¹¹⁴ BCB, ‘Brazilian Payments System’ <<https://www.bcb.gov.br/en/financialstability/paymentsystem>> accessed 18 August 2021; Banco Central do Brasil, ‘What is Pix?’ <<https://www.bcb.gov.br/estabilidadefinanceira/pix>> accessed 18 August 2021.

¹¹⁵ BCB, ‘List of authorized SPB member arrangements’ (27 July 2021) <<https://www.bcb.gov.br/estabilidadefinanceira/relacaoarranjosintegrantes>> accessed 18 August 2021.

issuance of electronic money, issuance of prepaid instruments, issuance of post-paid payment instruments like credit cards; acquiring services; and payment initiation service provider (PISP)).¹¹⁶

Position in India

- Most Surveyed Jurisdictions recognise the distinction between consumer facing retail payment services and payment systems operators or infrastructure providers that provide only the infrastructure for processing payments. Unlike many Surveyed Jurisdictions, the PSS Act does not make a distinction between the different players and roles played by each player in the payments value chain. The PSS Act is also silent on the concept of SIPS and the same is sought to be covered through the "Oversight Framework for Financial Market Infrastructures (FMIs) and Retail Payment Systems (RPSs)" ("RBI FMI Oversight Framework").¹¹⁷
- The PSS Act provides a broad definition of the term "payment system" along with an indicative list of activities that may fall within the definition of payment systems. This includes retail payment organisations, card payment networks, cross-border money transfer, PPI issuers, ATM networks, white label ATM operators, etc. By placing reliance on the expansive definition of "payment system", the PSS Act fails to recognise the role of each player in the payments value chain and the risk posed by such activity. This coupled with the absence of a risk-based regulatory approach in the provisions of the PSS Act, has led to a situation where the RBI has to rely on subordinate legislations to bring new and emerging payment services within the ambit of the PSS Act and to create a framework for its regulation.

Who is required to be authorised or licensed under law?

Position in Surveyed Jurisdictions

- Most Surveyed Jurisdictions follow an authorisation framework for payment service providers and designation framework for SIPS.
- Depending on the nature and size of activities, the UK PS Regulations may require a payment service provider to apply for authorisation or registration, as the case may be.
 - A "payment service provider" can be required to be (a) authorised as an authorised payment institution; (b) registered as a small payment institution; (c) registered as an account information service provider ("AISP"); or (d) registered as an agent of (a) to (c).¹¹⁸
 - Registration framework for "small payment institutions" is relevant to firms executing payment transactions with a monthly average of 3 million euros (or an equivalent amount) or less, over a 12-month period. Small payment institutions are not subject to specific provisions relating to capital requirements, protection of consumer funds, audit and outsourcing. These provisions are applicable to an "authorised payment institution".
 - Inter-bank payment systems are subject to a designation framework under the UK FSB Act.
- Unlike the UK that has two different frameworks for regulating payment systems and payment service providers, Singapore has a comprehensive framework under the Singapore PS Act. The Singapore PS Act envisages a licensing framework with three types of licenses: (a) money-changing license; (b) standard payment institution license; and (c) major payment institution license. Notably, the 'major payment institution license' requirement is primarily triggered where the entity carries on business crossing a specific threshold.
- Under the Canada RPA Act, payment service providers are required to be registered. A designation framework for SIPS is provided in the Canada PCS Act.
- The PSSVF Ordinance in Hong Kong is similar to Singapore's framework to the extent that it envisages a licensing framework for SVFs. Clearing and settlement systems and retail payment systems are subject to a designation framework.

¹¹⁶ Marcelo Padual Lima, Aaron Papa de Moraes and Thassila Victoria Nogueira, 'Brazil: Fintech', (The Legal 500 Country Comparative Guides, 2020) <<https://www.legal500.com/guides/chapter/brazil-fintech/>> accessed 18 August 2021; Alina Miyake, Diego Gualda, Érica Sumie Yamashita, et al, 'First-step analysis: fintech regulation in Brazil', (Lexology, 22 June 2020) <<https://www.lexology.com/library/detail.aspx?g=7ec5cc84-a2b3-47e3-8487-6c0ebe964a84>> accessed 18 August 2021.

¹¹⁷ An FMI is defined as a multilateral system among participating institutions, including the operator of the system, used for the purposes of clearing, settling, or recording payments, securities, derivatives, or other financial transactions. The term FMI generally refers to SIPS, Central Securities Depositories, Securities Settlement Systems, Central Counter Parties, and Trade Repositories that facilitate the clearing, settlement, and recording of financial transactions. ¹¹⁷ RBI, 'Oversight Framework for Financial Market Infrastructures (FMIs) and Retail Payment Systems (RPSs)' (13 June 2020)

<https://rbidocs.rbi.org.in/rdocs/Content/PDFs/OVER13062020_FF0CC640BA0CC434C83A1E847B4FB3FD6.PDF> accessed 18 August 2021.

¹¹⁸ An "agent" means "a person who acts on behalf of an authorised payment institution, a small payment institution or a registered account information service provider in the provision of payment services." The UK PS Regulations, regulation 2.

- Under the Australia PSR Act, a corporation seeking to hold purchased payment instruments must be authorised as a deposit taking institution under the Banking Act, 1959. Further, the Australia PSR Act provides for a designation framework for payment systems.¹¹⁹
- In Indonesia, the regulations envisage a licensing requirement for payment service providers.¹²⁰ For payment infrastructure providers, the Indonesia BI Regulations envisage a designation framework.¹²¹
- In Brazil, Article 5(II) of the CMN Resolution 2882 empowers the BCB to authorise the functioning of clearing houses and clearing and settlement providers that facilitate transfer of funds. The BCB Circular 3057 sets out the substantive provisions regarding authorisation of such providers. Article 9 of the e-Payments Law empowers the BCB to authorise payment schemes that operate in the country and authorise operation of payment institutions. The owners of payment schemes are required to request authorisation for the payment scheme that they operate, such as Visa do Brasil Empreendimentos Limited is authorized to operate Visa Direct in Brazil.¹²² Similarly, payment institutions, such as merchant acquirers like Cielo, Rede and Stone, are required a license to operate upon reaching specific operational thresholds.¹²³

Position in India

- Unlike most of the Surveyed Jurisdictions that envisage a registration / authorisation requirement for payment service providers and designation for SIPS, the PSS Act requires operator of a "payment system" i.e., a "system provider" (irrespective of nature of services provided) to obtain authorisation. Under the PSS Act, various non-bank entities have been authorised to operate retail payment systems and other payment services. Notably, by way of subordinate legislation, it has been clarified that banks while operating as payment aggregators or PPI issuers only need to obtain an approval as opposed to an authorisation.

Does the payment system law clarify if certain services are exempt from the provisions of the law?

Position in Surveyed Jurisdictions

- The Singapore PS Act and the UK PS Regulations expressly outlines a list of services that fall outside the definition of payment services. For instance, cash transactions not involving any intermediary, payment transactions through certain documents like cheque, service of transporting currency, services provided by a technical service provider, without the provider holding any funds, etc. are excluded.
- The Singapore PS Act also exempts some payment services that do not pose sufficient risk to warrant regulation. Significant carve outs include – a payment service that is provided by any person only in respect of any limited purpose e-money, any service of dealing in, or facilitating the exchange of, any limited purpose digital payment tokens, and any payment service solely incidental to or necessary for regulated activities carried out by a regulated financial services company (such as banks).
- In Hong Kong, the PSSVF Ordinance also exempts certain SVFs from the provisions of the ordinance, including provisions relating to licensing. This includes SVFs used for certain cash reward schemes, purchasing certain digital products, used within a limited group of a good or service's providers, etc. Such SVFs are exempted where the risks posed by the facility to a user, potential user, the payment system and financial system of Hong Kong is immaterial.
- The Canada RPA Act is not applicable to SIPS designated under the Canada PCS Act, payment functions performed by banks and other regulated entities, "prepaid payment instruments" (does not include open PPIs as defined in India), ATM withdrawals, etc.
- In Brazil, the Article 9(1) of the e-Payments Law empowers the BCB to define situations for exemption from authorisation. It exempts from authorisation the payment services providers with a small transaction volume or providing payment services within a limited scope, including (i) acquirers and post-paid payment instruments whose transaction volume does not exceed BRL 500 million (within a period of 12 months); (ii) pre-paid or post-paid instruments only accepted in one chain store; (iii) pre-paid or post-paid instruments for payment of specific public utilities,

¹¹⁹ Designated systems include card payments (EFTPOS, American Express, Visa and MasterCard) and the ATM system.

¹²⁰ Erwandi Hendarta, Mahardikha Sardjana, Eddie Prabowo Dewanda and Johan Kurnia, 'Indonesia: Digital "stargazing" through 2021: Bank Indonesia overhauls payment system regulations' (Lexology, 11 Januray 2021) <<https://www.lexology.com/library/detail.aspx?g=9d8fe513-ccfc-4ebe-bd36-01ce2eced894>> accessed 18 August 2021.

¹²¹ Erwandi Hendarta, Mahardikha Sardjana, Eddie Prabowo Dewanda and Johan Kurnia, 'Indonesia: Digital "stargazing" through 2021: Bank Indonesia overhauls payment system regulations' (Lexology, 11 Januray 2021) <<https://www.lexology.com/library/detail.aspx?g=9d8fe513-ccfc-4ebe-bd36-01ce2eced894>> accessed 18 August 2021.

¹²² Alina Miyake, Diego Gualda, Érica Sumie Yamashita, et al, 'First-step analysis: fintech regulation in Brazil' (Lexology, 22 June 2020) <<https://www.lexology.com/library/detail.aspx?g=7ec5cc84-a2b3-47e3-8487-6c0ebe964a84>> accessed 18 August 2021.

¹²³ Payment institutions that are issuers of post-paid payment instruments and/or acquirers are only obliged to file for an authorization with the BCB if/when the regulatory threshold is reached: BRL 500 million in payment transactions, aggregated in the previous 12 months period. Marcelo Padual Lima, Aaron Papa de Moraes and Thassila Victoria Nogueira, 'Brazil: Fintech', (The Legal 500 Country Comparative Guides, 2020) <<https://www.legal500.com/guides/chapter/brazil-fintech/>> accessed 18 August 2021.

such as public transportation services; (iv) payment services related to the granting of employment law benefits, such as pre-paid cards distributed by the employer to its employees for payment of meals.¹²⁴

- In both Singapore and Hong Kong, banks that have been granted a banking license are not separately required to obtain a license / registration for providing payment services.

Position in India

- Unlike many Surveyed Jurisdictions, the PSS Act does not specifically provide a list of services that are exempted from the provisions of the PSS Act. Such a clarification may be relevant given the complex payment transaction that involve multiple players, especially players that may just provide technological services without handling any consumer funds.
- The PSS Act exempts the RBI operated payment systems from obtaining authorisation under the law. Unlike Singapore and Hong Kong, the PSS Act does not clarify if banks are required to obtain authorisation for providing payment services. However, the 'Master Directions on Prepaid Payment Instruments (PPIs)' ("PPI Master Directions") provide that banks which meet the eligibility criteria can be permitted to issue small and fully-KYC PPIs after obtaining the approval of the RBI. As per the 'Guidelines on Regulation of Payment Aggregators and Payment Gateways' ("PA Guidelines"), while non-banks have to obtain authorisation under the PSS Act from the RBI for operating as a payment aggregator, banks need not obtain such authorisation.

Does the law incorporate a risk-based framework for payment service providers and SIPS?

Position in Surveyed Jurisdictions

- The Singapore PS Act comprises of two parallel regulatory frameworks - (a) a designation regime that enables the MAS to regulate SIPS for financial stability as well as efficiency reasons, and (ii) a licensing regime that focuses on retail payment services provided to consumers and merchants.
- Under the licensing regime, the Singapore PS Act envisages three types of licenses for payment service providers to create a risk-based framework. A payment service provider may apply to be a money-changing licensee, standard payment institution or a major payment institution. Money-changing licensees can conduct only money-changing services. Standard payment institutions may conduct any combination of regulated activities that are below specified thresholds. Both will be regulated primarily for money laundering and terrorist financing risks. Only major payment institutions may carry out payment services above specified thresholds, and will be regulated more comprehensively.¹²⁵
- Under the Singapore PS Act, the MAS also has the power to designate a payment system under the law if it is considered to be SIPS or SWIPS, or where it is otherwise in the public interest to do so. Under the law, SIPS are payment systems whose disruption could trigger, cause or transmit further disruption to participants or cause systemic disruption to the financial system. SWIPS are systems whose disruption could affect public confidence in payment systems or the financial system of Singapore.
- For such SIPS and SWIPS, the MAS may impose such conditions and restrictions on the operator, participant or settlement institution of such a payment system, as the authority thinks fit. Such conditions or restrictions may be related to activities that the operator or settlement institution of such designated payment system undertakes, the standards to be maintained by them. An operator or settlement institution of a designated payment system is mandated to notify the MAS of the occurrence of any of the following events - intention to make material change in operating rules, settlement procedures, material function being outsourced, the operator or settlement institution being, becoming or being likely to become insolvent, etc.
- The Singapore PS Act and the UK FSB Act also envisage an access regime for designated payment systems. The UK PS Regulations can require the operator of a Regulated Payment System to enable a person who has made an application to the regulator, to become a payment service provider in relation to the payment system. It can also require a payment service provider with direct access to the Regulated Payment System to enter into an agreement with the applicant to become a payment service provider in relation to the system.
- In line with the Singapore PS Act, the PSSVF Ordinance in Hong Kong envisages a designation framework for clearing and settlement systems and retail payment systems. Such systems are designated by the regulator if it is of the opinion that the system is, or is likely to become, a system whose proper functioning is material to the monetary or financial stability of Hong Kong, or to the functioning of Hong Kong as an international financial centre or the system should be so designated, having regard to matters of significant public interest. Therefore, SIPS are covered in this

¹²⁴ BCB Circular 3,682 of 4 November 2013, art.2 and BCB Circular 3,885 of 26 March 2018, art.6. We have relied on machine-translated English version of the BCB Circulars; Luiz Roberto de Assis and Fabio Kupfermann Rodarte, 'FinTech in Brazil: overview' (Thomson Reuters Practical Law, 1 December 2020)

<[https://uk.practicallaw.thomsonreuters.com/w-014-5181?transitionType=Default&contextData=\(sc.Default\)&firstPage=true](https://uk.practicallaw.thomsonreuters.com/w-014-5181?transitionType=Default&contextData=(sc.Default)&firstPage=true)> accessed 18 August 2021.

¹²⁵ MAS, 'Explanatory Brief on the Payment Services Bill' (19 November 2018) <<https://www.mas.gov.sg/news/speeches/2018/explanatory-brief-on-the-payment-services-bill>> accessed 18 August 2021.

designation framework. To date, HKMA has designated six retail payment systems which includes Visa, MasterCard, UnionPay International and American Express.¹²⁶

- For such designated retail payment systems - (a) HKMA may impose conditions or restrictions on activities carried out through designated systems; (b) every operator or settlement institution of a designated system must ensure that it is operated in a safe and efficient manner; (c) transfers and settlements with respect to the designated retail payment systems are final (provisions on the netting and settlement finality are applicable to designated payment systems); etc.
- The Indonesia BI Regulations adopts a risk-based classification of “payment service providers” and “payment infrastructure operators”.
 - These entities can be classified into three categories based on the potential risk that their system failure or disruption could cause to the payment system and / or financial system, i.e. (i) systemic payment companies (ii) critical payment companies, and (iii) general payment companies i.e. payment system operators that do not pose any significant impact.
 - Such classification is done on the basis of size, interconnectedness, complexity and / or substitutability of the payment system operators. Bank Indonesia will periodically evaluate the classification of payment service providers and payment infrastructure providers. Based on such classification, it may set certain requirements in relation to the operators' capitalization, risk and information system management, as well as other aspects.
 - The Indonesia BI Regulations has also updated the regulatory approval mechanism for new products/ services and cooperation arrangements between payment service providers. Bank Indonesia has introduced a self-assessment system by which payment service providers must assign risk rating to the proposed product / service or cooperation arrangement. Product approval applications that are deemed to be of low risk only need to be reported to Bank Indonesia, while those that are determined to be of medium or high risk must be approved by Bank Indonesia prior to launching. The same principle goes for cooperation arrangements with other payment service providers and support providers. Bank Indonesia reserves the right to re-examine the risk rating assigned by the payment service provider and require a prior approval to be sought in the event of a difference.¹²⁷
- In Brazil, Article 8 of the BCB Circular 3057 provides that all systems clearing and settling securities and other financial assets, including foreign currency and financial derivatives, as well as funds transfer and cheque clearing and settlement systems with average daily turnover as specified in the circular are considered as systemically important. Further, it empowers BCB to authorise a clearing and settlement system as the systemically important system, if such a system in the discretion of BCB offers risk to the flow of Brazilian Payment Systems.¹²⁸ The CMN Resolution 2882 specifies that the BCB may apply specific provisions to those systems that are considered systemically important.¹²⁹

Position in India

- The PSS Act does not specifically recognise a risk-based framework. Unlike many Surveyed Jurisdictions that expressly recognise SIPS in the parent statute and empower the regulator to exercise specific powers against such systems, the PSS Act is silent on the same. The same is sought to be addressed through the RBI that has issued the RBI FMI Oversight Framework. Amongst other things, the framework seeks to designate FMI, including “Retail Payment Systems” and PPIs on the basis of risk posed by it.¹³⁰ Notably, the framework refers to the provisions of the PSS Act to trace its powers to govern such designated systems.

Does the primary statute provide for consumer protection measures?

Position in Surveyed Jurisdictions

- The UK PS Regulations prescribe different consumer protection measures such as disclosure of specific information to consumers prior to or post transaction, including disclosure about charges and consent requirements; provisions relating to security of transactions; liability for unauthorized transactions; consent for use of personal data; and consumer authentication safeguards. The rights and obligations in relation to payment services are applicable based on transaction sizes outlined in the regulations.¹³¹

¹²⁶ Hong Kong Monetary Authority, ‘Regulatory Regime for Retail Payment Systems’ (11 September 2018) <<https://www.hkma.gov.hk/eng/key-functions/international-financial-centre/stored-value-facilities-and-retail-payment-systems/regulatory-regime-for-retail-payment-systems/>> accessed 18 August 2021.

¹²⁷ Erwandi Hendarta, Mahardikha Sardjana, Eddie Prabowo Dewanda and Johan Kurnia, ‘Indonesia: Digital “stargazing” through 2021: Bank Indonesia overhauls payment system regulations’ (Lexology, 11 Januray 2021) <<https://www.lexology.com/library/detail.aspx?g=9d8fe513-ccfc-4ebe-bd36-01ce2eced894>> accessed 18 August 2021.

¹²⁸ The BCB Circular no. 3057, art. 8 of section V. We have relied on the machine-translated English versions of the law as provided by the BCB on its website.

¹²⁹ The CMN Resolution 2882, art.5. We have relied on the machine-translated English versions of the law as provided by the BCB on its website.

¹³⁰ RBI, ‘Oversight Framework for Financial Market Infrastructures (FMIs) and Retail Payment Systems (RPSs)’ (13 June 2020) <https://rbidocs.rbi.org.in/rdocs/Content/PDFs/OVER13062020_FF0CC640BA0CC434C83A1E847B4FB3FD6.PDF> accessed 18 August 2021.

¹³¹ The UK PS Regulations, regulation 65.

- Under the Singapore PS Act, licensed payment service providers and settlement institutions are required to designate a person to address consumer complaints. The MAS which apply to all financial institutions that issue or operate protected accounts.¹³²
- In Hong Kong, the PSSVF Ordinance does not expressly set out consumer protection safeguards, though licensing conditions may prescribe certain safeguards.
- In Indonesia, the Bank Indonesia has issued a separate regulatory framework for consumer protection related issues - BI Regulation No. 22/20/PBI/2020 on Consumer Protection. These regulations impose consumer protection requirements on operators of payment systems and other Bank Indonesia regulated entities.¹³³ These regulations require regulated entities to follow core principles of consumer protection such as equality and fair treatment; openness and transparency; protection of consumer data and personal data in digital transactions; and effective complaint handling and resolution of complaints. The regulations also envisage a grievance redressal mechanism where consumers can approach the Bank Indonesia for resolution of their grievances.
- In Brazil, the Article 7(IV) of the e-Payments Law provides that the payment schemes and payment institutions must meet end-users needs, in particular with respect to freedom of choice, safety, protection of their economic interests, non-discriminatory treatment, privacy and personal data protection, transparency and access to clear and complete information about their services.¹³⁴

Position in India

- The PSS Act does not set out any consumer protection principles or obligations for payment service providers. Most of the consumer protection obligations relating to unauthorised transactions, risk management, consumer grievance redressal, etc. has been introduced through subordinate legislation in the form of notifications issued by the RBI from time to time.

Does the law envisage requirements for access and interoperability?

Position in Surveyed Jurisdictions

- Under the UK PS Regulations, payment systems must have access requirements which are objective, proportionate and non-discriminatory.¹³⁵ The UK FSBR Act further empowers the PSR to require the operator of a Regulated Payment System to enable an applicant to become a payment service provider in relation to the system.
- Under the Singapore PS Act, the MAS has the power to impose an access regime to a "relevant payment system". Such an access regime may be granted to a participant, operator or settlement institution of that payment system or any other person that determines access to that payment system. The MAS has a statutory obligation to ensure that such an access regime is fair and non-discriminatory.
- Similarly, under the Singapore PS Act, the MAS has the power to take such steps as specified in the law to ensure interoperability between a payment account or accounts and a payment system.
- In Indonesia, the law requires both payment service providers and payment infrastructure providers to ensure interconnectedness and interoperability, including standards set by the Bank Indonesia in this regard.
- In Brazil, the e-Payments Law sets out that payment schemes and payment institutions shall promote the non-discriminatory access to infrastructures and services, and observe interoperability within the payment scheme and between different payment schemes.¹³⁶ In case of Brazilian Payment Systems, the Brazil Payment Systems Law does not provide the access criteria and interoperability requirements. The CMN Resolution 2882 requires payment systems to observe general terms to be imposed by the BCB which also includes that the access criteria of the payment system must be public, objective and clear, to enable the broad participation.¹³⁷

Position in India

- The PSS Act does not recognise the concept of open access and interoperability. Access requirements to centralized payment systems have been set out in Master Directions on Access Criteria for Payment Systems which further allows 'Non-Bank Payment System Providers' to participate

¹³² MAS, 'Guidelines for E-Payments User Protection' (05 December 2019) < <https://www.mas.gov.sg/regulation/guidelines/guidelines-for-e-payments-user-protection> > accessed 18 August 2021.

¹³³ 'Operators in the field of Payment Systems' include: (i) issuance of payment instruments using cards; (ii) issuance of electronic money; (iii) issuance of checks; (iv) electronic wallet operation; (v) fund transfers, including fund transfers made through the Bank Indonesia- Real Time Gross Settlement system and the Bank Indonesia National Clearing System; (vi) implementation of payment transaction forwarding; and/or (vii) Operators in the field of other Payment Systems as determined by Bank Indonesia. The BI Regulation No. 22/20/PBI/2020, art. 4. We have relied on the machine translated English version of the law.

¹³⁴ The e-Payments Law, art. 7(IV). We have relied on the machine-translated English version provided by BCB on its website.

¹³⁵ The UK PS Regulations, regulation 103.

¹³⁶ The e-Payments Law, art. 7 (I) & (III). We have relied on the machine translated English version provided by BCB on its website.

¹³⁷ The CMN Resolution 2882, art. 3 (VIII). We have relied on the machine translated English version provided by BCB on its website.

in centralised payment systems such as RTGS and NEFT.¹³⁸ Interoperability has been permitted among PPIs that enables a PPI holder to seamlessly transfer funds between PPIs as provided by different PPI issuers.¹³⁹ It is worth noting that the PPI Master Directions make it mandatory for PPI issuers to give the holders of full-KYC PPIs (KYC-compliant PPIs) interoperability through authorised card networks (for PPIs in the form of cards) and UPI (for PPIs in the form of electronic wallets).¹⁴⁰

¹³⁸ RBI, 'Master Directions on Access Criteria for Payment Systems (Updated as on July 28, 2021)' (2021) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=10833&Mode=0>> accessed 19 August 2021.

¹³⁹ RBI, RBI, 'Master Directions on Prepaid Payment Instruments (PPIs)' (August 2021) para. 11 <https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=12156> accessed 18 August 2021.

¹⁴⁰ RBI, 'Master Direction on Issuance and Operation of Prepaid Payment Instruments (Updated as on November 17, 2020)' (2017) para. 11 <https://www.rbi.org.in/Scripts/BS_ViewMasDirections.aspx?id=11142> accessed 18 August 2021.

IV. The need for redesigning India's Payment Systems Law - Case for Reform

With the evolution of money, the means of payments have also evolved. Payments continue to be the financial service that is most affected by shifts in demand, technology and new entrants. The entry of new players in the payments sector coupled with the evolution of consumer demand has led to innovations in different stages of the payments value chain - more so in case of retail payments. In response to such developments, including the rapid uptake of digital payments by consumers, central banks across several economies have emphasised and taken steps to modernize the retail payments sector. This includes facilitating entry of non-banks, efforts at designing faster payment systems for real-time payments and redesigning payment systems law to focus on risk-based regulation, consumer protection, and promotion of competition and innovation. As the payments sector evolves, there is a need to have a forward looking and flexible regulatory framework that can encourage the growth of this sector and contain risks that may emanate from it.

Given the critical role of payment systems in facilitating economic activity, they are typically subject to an oversight framework. Most modern economies have designed laws to regulate payment systems, their operators and participants. While historically, concerns regarding systemic risks guided the oversight of payment systems, with the evolution of retail payment systems, policy objectives surrounding promotion of innovation, competition and consumer protection have become relevant. A review of the Surveyed Jurisdictions in the previous chapter indicates that typically regulation and oversight of payment systems and services are guided by three primary policy objectives - ensuring safety and soundness of payment systems, promoting efficiency in the functioning of payment systems and the protection of user interests.

- **Safety and soundness:** Payment systems are the backbone of an economy. Any disruption in such systems has the potential to send shocks across the entire financial system or to dent public confidence in payment systems. Therefore, the payment systems must have necessary safeguards for risk management. Given that risks posed by different payment systems vary depending on factors such as size, value and volume of transactions processed, and interconnectedness with other systems, most of the modern payment systems law argue for a risk-based framework where regulation is proportionate to the risks posed by a payment system.
- **Efficiency:** An efficient payments sector determines how effectively payments, clearing and settlements processes are carried out to meet the needs of consumers, as well as to ensure efficient allocation of resources to deliver the service. Therefore, a retail payments oversight framework must be able to foster competitive market conditions and help remove barriers to entry to drive cost reductions and innovation.
- **Consumer Protection:** Given the consumer facing nature of retail payments, it is critical that such services should be designed keeping in mind the needs, interests and vulnerabilities of consumers. Given that payments often act as the relevant entry point for consumers into the financial system, having a robust consumer protection framework is essential to support financial inclusion objectives.

In most modern payment systems laws, the aforesaid policy objectives are sought to be achieved through different legislative provisions in the primary law. For instance, safety and soundness of payment systems is sought to be achieved through provisions relating to netting, settlement finality, segregation of consumer funds from the assets of the payment service provider, etc. Similarly, efficiency in payment systems is sought to be achieved through the provisions that seek to promote competition and innovation in the payments sector - such as provisions relating to the risk-based regulation, mandating open access, interoperability, etc. Consumer interest is sought to be protected through provisions on grievance redressal mechanisms, transparency, protection of privacy, etc.

As the retail payments space rapidly evolves, regulators face oversight challenges. In response to such evolving payment services, business models and entry of new players, many jurisdictions have redesigned their payment systems laws to account for such developments in the retail payments sector. Against these developments, it is important to critically analyse the PSS Act to assess if it is well-equipped to create a framework to promote the policy objectives that underpin most modern payment systems laws.

PSS Act - Tracing its origin

The PSS Act was enacted on 12 August 2008. A review of the report of the Committee of Payment Systems constituted by the RBI¹⁴¹ and headed by Dr. R.H. Patil and the report of the Standing Committee¹⁴² on “the Payment and Settlement Systems Bill, 2006” clearly indicates that the PSS Act was primarily enacted to regulate payment systems, more particularly SIPS, to designate the RBI as the relevant authority for the “regulation and supervision of payment systems” and to give legal recognition to netting procedure. Prior to the enactment of the PSS Act, the RBI relied on its powers under the RBI Act (section 58(2)(p) and 58(2)(pp)) to frame the regulations for “netting” and “settlement finality”. As financial markets were becoming more sophisticated, it was felt that reliance on subordinate legislation for such critical issues must be revisited. A statutory provision on “netting” and “settlement finality” was also necessary for India to comply with the international best practices i.e. the “Core Principles for Systemically Important Payment Systems” formulated by the CPMI, BIS.¹⁴³ Further, the need for a law was felt to expressly empower the RBI to regulate newer payment systems such as money transfer schemes and the operation of card network companies.

Against these developments, the Payment and Settlement Systems Bill 2006¹⁴⁴ was drafted to empower the RBI to regulate and supervise payment systems. Pertinently, the bill only sought to empower the RBI to regulate payment systems, without setting out any specific obligations for operators of such payment systems.

Evolution of the payment systems regulations over the years

Since the initial objective of the PSS Act was to supervise SIPS and empower the RBI to regulate payment systems, the focus has been on regulation from a systemic point and to confer regulatory powers on the RBI, without setting out corresponding obligations on operators of such payment systems and the new and emerging retail payment services. To deal with these gaps, the RBI has entirely relied on its powers under the PSS Act, more particularly, its power to issue directions under section 10 and section 18. Since its enactment, the RBI has issued around 280 circulars / notifications under the PSS Act. For instance, the regulatory framework applicable to PPIs and payment aggregators that have to obtain authorisation under the PSS Act have been issued through such directions issued under the PSS Act. Similarly, obligations relating to risk management, consumer protection, interoperability, MDR, etc. have been issued through directions under the PSS Act. In the absence of any specific statutory mandate on these issues, the RBI has resorted to its directions issuing power to deal with the emerging issues. This has led to a situation where the entire regulatory framework for payment systems in India has evolved through subordinate legislation. Interestingly, the PSS Act was specifically enacted to ensure that RBI did not have to rely on subordinate legislation to regulate payment systems. While regulatory flexibility is necessary for an evolving market, the entire regulatory framework cannot be carved out of subordinate legislation. Such an approach often leads to uncertainty for businesses, that may be a disincentive for businesses to innovate. Even in other jurisdictions, while regulators typically have the flexibility to issue circulars / guidelines, the primary statute also have set out the positive obligations for payment service providers as well as for the regulator.

¹⁴¹ RBI, ‘Committee on Payment Systems’ <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/32827.pdf>> accessed 19 August 2021.

¹⁴² Standing Committee on Finance (2006-07), Fourteenth Lok Sabha, ‘The Payment and Settlement Systems Bill, 2006’ Fifty Sixth Report, (May 2007) <https://prsindia.org/files/bills_acts/bills_parliament/scr1186992340_paymentsettlement.pdf> accessed 19 August 2021.

¹⁴³ CPSS, BIS, ‘Core Principles for Systemically Important Payment Systems’ (2001) <<https://www.bis.org/cpmi/publ/d43.pdf>> accessed 30 August 2021.

¹⁴⁴ The Payment and Settlement Systems Bill, 2006 (2006) <https://prsindia.org/files/bills_acts/bills_parliament/1167468260_The_Payment_and_Settlement_Systems_Bill_2006.pdf> accessed 19 August 2021.

Given the initial focus of the law on regulation from a systemic point, other policy objectives that are critical for the regulation of payments in modern times have not been accounted for in the PSS Act. However, over the course of years, the RBI has acknowledged the role of a regulator in promoting other policy objectives in the payments space such as promotion of competition and protecting the interests of users of retail payments. For instance, the “Payment and Settlement Systems in India - Vision 2019-2021” released by the RBI focuses on such key enablers for adoption of digital payments, including the need to promote competition, convenience and confidence in payment systems.¹⁴⁵ The need for competition in the payments market has also been underscored by the RBI in its “Policy Paper on Authorisation of New Retail Payment Systems” where the RBI has noted that payment systems in India is “characterized by a few operators while there is a wide array of payment systems.” This has given rise to certain questions which range largely around the concerns of concentration and its impact on economic efficiency and financial stability. In the absence of specific statutory provisions, the RBI to its credit has sought to promote such policy objectives by relying on its power to issue directions under the PSS Act - through directions on mandating the interoperability and introduction of the new umbrella entities (“NUEs”) for retail payment systems.

In the past, several committees have suggested reforms to deal with the gaps in the PSS Act, including the Financial Sector Legislative Reforms Commission,¹⁴⁶ the Committee on Digital Payments¹⁴⁷ and the Inter-Ministerial Committee for Finalisation of Amendments of the PSS Act, 2007 (“Inter-Ministerial Committee”).¹⁴⁸ One common theme emerging from the recommendations of these committees is that the PSS Act should include provisions on open access, interoperability and proportionate or risk-based regulation - issues which are yet to be incorporated in the primary statute.

Existing Gaps in the PSS Act

Since the enactment of the PSS Act, the payments landscape has undergone extensive changes due to the emergence of disruptive technologies leading to technology led payment solutions. Due to these technological disruptions, new types of payment services in the form of UPI, IMPS, PPIs, payment aggregators, etc. have emerged. This in turn has led to the emergence of financial technology (fintech) companies and new business models in the payments ecosystem. Despite such developments, the PSS Act has not undergone any significant changes since its enactment almost a decade back except for certain amendments regarding the protection of consumer funds and finality of payment and settlement instructions. To account for these developments, most regulatory interventions in the payments sector have been introduced through subordinate legislation. The introduction chapter already highlights the role of a robust payments market in an economy. While several demand and supply side factors determine the adoption of digital payments, a key enabler for promotion of digital payments is the regulatory framework that is conducive for sustained use of such modes of digital payments. For retail payment systems, such a framework requires an increased focus on consumer protection, innovation and competition. This section highlights that the PSS Act has not been able to provide such an enabling framework due to the existing gaps.

Policy objectives of the PSS Act do not align with the requirements of a modern retail payments law

The payments sector has transformed rapidly, both in India as well as globally. As the growth dynamic of the payments industry has changed over the years, the policy objectives and perspectives governing the future of this

¹⁴⁵ RBI, ‘Payment and Settlement Systems in India: Vision – 2019-2021’ (15 May 2019) <<https://www.rbi.org.in/Scripts/PublicationVisionDocuments.aspx?Id=921>> accessed 19 August 2021.

¹⁴⁶ Financial Sector Legislative Reforms Commission, ‘Report of the Financial Sector Legislative Reforms Commission’ (22 March 2013) <https://www.icsi.edu/media/webmodules/linksofweeks/fslrc_report_vol1.pdf> accessed 19 August 2021; Financial Sector Legislative Reforms Commission, ‘Report of the Working Group on Payments’ <https://macrofinance.nipfp.org.in/fslrc/documents/wg_payments_report.pdf> accessed 19 August 2021.

¹⁴⁷ Committee on Digital Payments, ‘Medium Term Recommendations to Strengthen Digital Payments Ecosystem’ (December 2016) <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed on 19 March 2021.

¹⁴⁸ Inter-Ministerial Committee for Finalisation of Amendments of the PSS Act, 2007, ‘Recommendations to Consolidate and Amend the Law Relating to Payments’ (August 2018) <<https://dea.gov.in/sites/default/files/Payment%20and%20settlement.pdf>> 19 August 2021.

industry need to be markedly different from those which guided it in the past. As discussed earlier, the PSS Act focuses on creating an oversight framework for the RBI over “system providers” and “system participants”. In doing so, it has mostly focused on issues related to supervisory powers of the RBI from a systemic point of view, but has remained silent on key enablers for proliferation of retail digital payments such as the consumer protection and promotion of competition and innovation. In the absence of the same, the RBI has relied on policy documents or subordinate legislation to pursue such objectives. To create more certainty for emerging businesses and to clearly set out the scope of the powers of the RBI under the PSS Act, it may be useful to revisit the purposes / objectives of the PSS Act and, specify the creation of an efficient payments market and protection of consumer interest as objectives that will guide the PSS Act.

Absence of a risk-based framework

A risk-based approach is the hallmark of a modern payment systems law. Such a framework promotes 'proportionate regulation' that is useful to promote competition and innovation as it allows emerging businesses to innovate without undue regulatory intervention, while requiring businesses undertaking higher risk activities to be subjected to stronger regulatory oversight. By directing regulatory resources towards high-risk activities, a risk-based approach also makes optimal utilization of regulatory resources. Such a framework argues that regulatory burden or oversight for a small payment service provider should not be same as that of a critical payment infrastructure. Several of the Surveyed Jurisdictions have adopted a similar approach where the regulatory framework makes a distinction between designated payment systems (that typically includes the SIPS and the SWIPS) and payment service providers (that typically includes retail payment services) on the basis of the risk posed by their activities. As compared to payment service providers, the designated systems are subject to a stringent oversight regime by the regulator. Such an approach is necessary to not only regulate large payment systems from the perspective of systemic risks, but also from a competition point of view. Even in the context of payment service providers, jurisdictions like Singapore and the UK adopt a risk-based approach as is evident from the different licenses issued to the payment service providers based on potential risk posed by the activity proposed to be undertaken by such provider.

In the case of the PSS Act, there is a conspicuous absence of such a risk-based approach. The PSS Act does not make any distinction between the different types of payment service providers, and clearing and settlement systems. In the absence of such a risk-based framework, the RBI has issued the RBI FMI Oversight Framework for designation of SIPS and SWIPS. Notably, the RBI relies on the existing provisions of the PSS Act that broadly outlines the general powers of a regulator to regulate all payment systems, irrespective of the risk posed by it.

Need to relook at the definition of 'payment system' to account for the constantly evolving payments sector

The retail payments sector has been constantly evolving. At the time of the enactment of the PSS Act, the payments sector saw participation by select non-bank entities providing card network and money transfer services. Over the years, new players, primarily non-bank entities with new business models such as PPI issuers, retail payment organisations (like NPCI), merchant acquirers, payment gateways, payment aggregators, and other overlay systems built using UPI have emerged. To account for such advancements and to bring different entities within the purview of the PSS Act, the RBI has time and again issued standalone directions / guidelines. This was last seen in the creation of a regulatory framework for PPIs and payment aggregators, where the RBI through subordinate legislations has clarified that such entities will be brought within the ambit of payment systems under the PSS Act and will accordingly be subject to authorisation requirement.

Under the PSS Act, a payment system must meet two conditions: (a) it must enable a payment to be effected between a payer and a beneficiary; and (b) it must be involved in clearing, payment or settlement service or all of them. While the term 'settlement' has been defined, the terms 'payment' and 'clearing' have not been defined. The absence of a definition of 'payment service' is an important regulatory gap that must be addressed. This is particularly relevant to capture new and emerging services enabled by evolving technology. Further, absence of such a definition in the principal legislation is also likely to cause uncertainty for businesses regarding the applicability of the PSS Act. Complete reliance on subordinate legislation for creating standalone framework for

new and emerging payment services providers is not an ideal solution from legal as well as business certainty perspective.

Globally, Surveyed Jurisdictions like the UK, Singapore, Hong Kong, Thailand, etc. have sought to maintain a distinction between the payment systems and the payment service providers. Typically, payment systems include retail payment systems or the infrastructure providers to transfer funds and that are typically involved in clearing and settlement activities. Payment services generally refers to retail payment services that may include overlay systems and closed-loop systems.

Does not specifically recognise SIPS

Typically, payment systems that are high risk and systemic (often referred to as systemically important payment systems or SIPS) are subject to a more heightened regulatory framework because they have the potential to trigger systemic disruptions. In determining which systems should be regulated as SIPS, central banks rely on objective criteria. In most Surveyed Jurisdictions, the statute provides for a designation framework for SIPS. The designation framework seeks to identify SIPS, impose specific obligations on them and empower the regulator with specific powers to regulate them over and above the powers that regulators exercise vis-à-vis other payment systems and services. Such provisions are necessary to ensure the safety and soundness of SIPS as well as regulate them in a manner to promote more competition, leading to an efficient payments market. The PSS Act does not recognise the concept of SIPS or SWIPS as has been done in other Surveyed Jurisdictions.¹⁴⁹

Provisions to promote competition in the payments space

The PSS Act does not impose any positive obligation on PSOs to provide access to the participants on a fair and transparent basis or ensure interoperability. The provisions of open access and interoperability are significant to create a level playing field for all the players (irrespective of whether it is a bank or non-bank) providing similar payment services. The RBI itself notes that the payments market in India is “characterized by a few operators while there is a wide array of payment systems.”¹⁵⁰ Significant market concentration may lead to a high dependency on select payment and settlement system operators, without readily available alternatives. Such market concentration has the potential to give such operators the market power that leads them to provide lower levels of services at higher prices, lower investment in risk reduction and a lower level of innovation. In light of this, promotion of competition is essential for creating an efficient payments market.

In networked markets such as payments, the lack of open access to payment systems can cause significant entry barriers for the new players.¹⁵¹ Based on the global experience, it has been noted that the non-bank payment service providers, innovative businesses and technological approaches have contributed to expanding the access to payment services.¹⁵² Accordingly, any legal framework for the payment systems must encourage the participation of such non-bank entities and discourage any entry barriers for such entities. Therefore, the many Surveyed Jurisdictions like the UK, Singapore, Hong Kong, etc. statutorily impose open access obligations on a non-exclusive basis. Such open access obligations would lead to a greater interoperability, which refer to the ability of consumers to transact across commercially and technically independent payment platforms.¹⁵³ This is also in line with the recommendations of the CPMI, which has recently recommended that the payment

¹⁴⁹ The same is sought to be undertaken through subordinate legislation i.e., the RBI FMI Oversight Framework. From a legal certainty perspective, power to designate such systems, objective criteria for such designation, and specific powers vis-à-vis such systems should emanate from the primary statute and not from a policy document.

¹⁵⁰ RBI, ‘Policy Paper on Authorisation of New Retail Payment Systems’ <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/ANRPS21012019A8F5D4891BF84849837D7D611B7FFC58.PDF>> accessed 19 August 2021

¹⁵¹ Wilko Bolt, ‘Retail Payment Systems: Competition, Innovation and Implications’ (De Nederlandsche Bank Working Paper No. 362, December 2012) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2192046#> accessed 19 August 2021.

¹⁵² World Bank and CPMI, BIS, ‘Payment aspects of financial inclusion’ (April 2016) <<https://www.bis.org/cpmi/publ/d144.pdf>> accessed 19 August 2021.

¹⁵³ Committee on Digital Payments, ‘Medium Term Recommendations to Strengthen Digital Payments Ecosystem’ (December 2016) <https://dea.gov.in/sites/default/files/watal_report271216.pdf> accessed on 19 March 2021.

infrastructures, including those operated by the central banks, should have objective, and risk-based participation requirements that permit fair and open access to their services.¹⁵⁴

In the absence of such a statutory framework, the RBI has relied on subordinate legislation and has issued directions from time to time on the interoperability for PPIs, allowing entry of NUEs in the payments sector and allowing non-banks to access the centralised payment systems like RTGS and NEFT, etc. While such initiatives are a welcome move, it may be useful to incorporate well-recognised principles / best practices for promoting the competition in the payments sector through provisions on open access and interoperability in the primary statute. The RBI may continue issuing directions to set out the procedural requirements for implementing such obligations, but the primary obligation should stem from the parent statute.

Provisions on consumer protection

Considering the fast-evolving nature of the retail payments, entry of new players and emergence of new models, the consumer protection measures are significant for a country like India which is struggling with issues relating to digital and financial literacy. The issues relating to the disclosure requirements, effective grievance redressal mechanism, protection of consumer data, information security requirements, etc. are critical, especially in the case of consumers facing the payment service providers. Despite this, the PSS Act does not envisage any positive obligation on PSOs for protecting the interests of the end users. Some of these issues are sought to be addressed through directions that have been issued by the RBI from time to time. Recognising such consumer protection safeguards in the parent statute is essential to not only inspire public confidence in the payment systems, but also for business certainty.

Dispute Redressal Mechanism

The presence of an effective and efficient grievance redressal mechanism for payment transactions is essential for the consumer and the merchant confidence. While the RBI has issued circulars requiring some consumer facing payment service providers to have an effective grievance redressal mechanism, the PSS Act is silent on consumer grievance redressal mechanism. While regulatory flexibility may be provided to payment service providers to design their dispute redressal mechanism, it is important that the statute lays down the basic features of such a mechanism. Such a framework is also necessary to increase consumer trust in the payment systems. The legal recognition of the grievance redressal mechanism in the primary statute is also significant so that the legal recourse available for consumers in case of a failure of a payment service provider to resolve such grievance is adequately provided for in the statute.

Excessive reliance on subordinate legislation and legal risks

As discussed above, the PSS Act provides a skeletal framework that essentially sets out the basic regulatory powers of the RBI. To deal with the existing gaps in the PSS Act, the RBI has been issuing directions / guidelines from time to time covering various substantive obligations that should ideally emanate from a statutory framework. This includes:

- The consumer protection obligations on system providers relating to the dispute resolution, liability for unauthorised transactions, etc. emanate from subordinate legislation without any reference to the same in the parent statute.
- The entire framework for adjudication of penalties under the PSS Act is determined through subordinate legislation. This includes appointment of adjudication officers, principles and procedure to be followed for determining penalties, etc. This approach is contrary to the other financial sector laws such as the Securities

¹⁵⁴ World Bank and CPMI, BIS, 'Payment aspects of financial inclusion' (April 2016) <<https://www.bis.org/cpmi/publ/d144.pdf>> accessed 19 August 2021.

and Exchange Board of India Act, 1992, the Insurance Regulatory and Development Authority of India Act, 1938 and the Pension Fund Regulatory and Development Authority Act, 2013.

- Creating a regulatory sandbox framework that empowers the RBI to provide relaxation from the parent statute to encourage innovation in the financial sector is also done through the subordinate legislation without the parent statute envisaging such relaxation or exemption.
- To deal with new and emerging payment services that are sought to be brought within the ambit of the PSS Act, the RBI has issued notifications / circulars to create a standalone framework for the same. The entire regulatory frameworks for PPIs and payment aggregators in India have been issued through notifications issued by the RBI.

While the legal framework for a rapidly evolving sector must allow some flexibility to the regulator to issue specific directions, setting out substantive rights and obligations through subordinate legislation may be an over-reach that will expose such subordinate legislation to legal risks.

Multiple regulatory instruments

The RBI issues different types of regulatory instruments pursuant to section 10 and section 18 of the PSS Act. It has often been pointed out that this practice of issuing several regulatory instruments is complex and may be confusing in relation to the scope and enforceability of such instruments.¹⁵⁵ Currently, the RBI issues notifications, circulars, Master Circulars, Master Directions and guidelines for regulation of the payment systems and the operators of such systems. The distinction between the nature of Master Circular and Master Directions is not clear. While the RBI issued the Master Directions for designing a consolidated regulatory framework for PPIs, the RBI issued guidelines for the purposes of issuing a regulatory framework for payment aggregators.

The aforementioned deficiencies in the existing regulatory framework for digital payments means that the digital payments in India are caught up in the low-equilibrium trap. This has in turn resulted and has potential to result in poor services for the consumers, lack of choice of means of the payment, continued reliance on cash with its high costs and the consequent possibility of money laundering and tax evasion. The challenges with the existing framework as discussed in the preceding chapters and the issues highlighted above call for a renewed and streamlined regulatory architecture for the digital payment services in India.

Will the creation of NUEs solve the challenges regarding the promotion of a more competitive and innovative payments market?

Concerned that the digital payments ecosystem is primarily concentrated in one entity i.e., NPCI, which operates 11 payment systems in India, the RBI has issued a framework to license NUEs.¹⁵⁶ This sets the stage for more NPCI type entities in the payments ecosystem. The entry of NUEs has been driven by concerns of concentration, need for competition, and the resultant impact on the economic efficiency and financial stability.¹⁵⁷ The RBI's concerns stem from the potential monopoly which NPCI enjoys, that may disincentivize innovation, impact pricing, and limit access to its systems.

¹⁵⁵ Financial Sector Legislative Reforms Commission, 'Report of the Financial Sector Legislative Reforms Commission' (22 March 2013) <https://www.icsi.edu/media/webmodules/linksofweeks/fslrc_report_vol1.pdf> accessed 19 August 2021.

¹⁵⁶ RBI, 'Framework for authorisation of pan-India Umbrella Entity for Retail Payments' <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=11954&Mode=0>> accessed 19 August 2021.

¹⁵⁷ RBI, 'Policy Paper on Authorisation of New Retail Payment Systems' <<https://rbidocs.rbi.org.in/rdocs/PublicationReport/Pdfs/ANRPS21012019A8F5D4891BF84849837D7D611B7FFC58.PDF>> accessed 19 August 2021.

While the RBI's concern that NPCI's monopoly may result in market inefficiencies is genuine, introduction of NUEs may not be the ideal solution to address these issues. A quick look at global developments also indicates that it is not uncommon for jurisdictions to have one or few PSOs operating major payment systems.

- Single operator approach

Contrary to India's position, the UK has consolidated its three large PSOs - Bacs Payment Schemes Ltd., Cheque Credit and Clearing Company Ltd. and Faster Payments Schemes Ltd. into one payment system operator under the name of Pay.uk.¹⁵⁸ Through this consolidation, the UK seeks to bring in standardization, improve efficiency and drive down costs. It notes that multiple operators result in different rules and requirements to access different payment systems. Navigating these rules is time consuming and costly for payment service providers. This may also lead to a duplication of efforts across different operators.

While the RBI introduced NUEs due to its concerns about concentration risk, the UK appears to have taken a different approach. It notes that consolidation will allow concentration of operational and risk management resources and a single approach to risk management will enhance security and resilience. It also enables simpler and more effective regulatory oversight.¹⁵⁹

- Multiple operators' approach

In the United States, the roadmap for faster payments¹⁶⁰ released by the taskforce constituted by the Federal Reserve notes that while globally a number of countries have adopted a national payments system with a single operator, the US will take a market-driven approach to the payment system innovation that will rely on the collaboration between "multiple solution operators" and other stakeholders. However, in doing so, the US taskforce also cautions that this model poses certain challenges relating to interoperability which can be inhibited by business and technical processes. Further, it refers to the security concerns when multiple solution operators pass payments and share information.

The relationship between market concentration and financial stability, despite a growing body of research, remains ambiguous.¹⁶¹ Perhaps this is the reason why different jurisdictions have adopted different approaches. However, a review of the operators of large-value payment systems (excluding card networks) in select jurisdictions with high volume of cashless payments indicates that it is not uncommon for jurisdictions to have the central bank along with a single or few PSOs operating its major payment systems. For instance, in Singapore, the Network for Electronic Transfers ("NETS") Group operates several major inter-bank payment systems, including Singapore's fast payment system. Similarly, Payments Canada, a statutory body in Canada owns and operates the large-value payment system in Canada. In Hong Kong, the Hong Kong Interbank Clearing Limited, a private company jointly owned by the HKMA and the Hong Kong Association of Banks owns and operates the RTGS and the Faster Payment System ("FPS").

While multiple PSOs like the NPCI have its advantages, especially to promote competition, it comes with a set of challenges that has also been acknowledged by the RBI in its 'Policy Paper on Authorisation of New Retail Payment Systems' that sets out the case for introducing NUEs.

¹⁵⁸ Payments Strategy Forum, 'A Payments Strategy for the 21st Century' (November 2016) - < <https://www.accc.gov.au/system/files/public-registers/documents/47.%20Payments%20Strategy%20Forum%2C%20%E2%80%98A%20Payments%20Strategy%20for%20the%2021st%20Century%20Putting%20the%20needs%20of%20users%20first%E2%80%99%2C%20November%202016.pdf>> accessed 19 August 2021. Payment Systems Regulator, 'Delivery plan announced for the consolidation of the operators of BACS, Faster payments Service and Cheque and Credit Clearing' (May 2017) <<https://www.psr.org.uk/news-updates/latest-news/news/delivery-plan-announced-for-the-consolidation-of-the-operators-of-bacs-faster-payments-service-and-cheque-and-credit-clearing/>> accessed 19 August 2021.

¹⁵⁹ Payment System Operator Delivery Group, 'New Payment System Operator' (4 May 2017) <<https://www.psr.org.uk/media/11cnqu0e/psodg-report-2017.pdf>> accessed 19 August 2021

¹⁶⁰ Faster Payments Task Force, 'Final Report Part Two: A Call to Action' (July 2017) <<https://fedpaymentsimprovement.org/wp-content/uploads/faster-payments-task-force-final-report-part-two.pdf>> accessed 19 August 2021.

¹⁶¹ Pietro Calice and Leone Leonida, 'Concentration in the Banking Sector and Financial Stability: New Evidence' (October 2018) <https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3267682> accessed 19 August 2021.

- Multiple operators may add to the complexity and administrative costs for payment service providers who have to navigate through the rules of different operators, impacting the end consumer.
- Business and technical processes may inhibit interoperability as has been admitted by the RBI and the US Faster Payment Task Force. This runs counter to the purpose of promoting competition.
- The governance of multiple NPCI type entities will be challenging for the RBI from an enforcement perspective and will require investment on institutional resources.
- Creation of NPCI type entities will require additional investments along with the creation of suitable institutional infrastructure, which will be costly and time consuming.
- The UK's study indicates that a single operator may lead to the concentration of operational and risk management resources which will enhance the overall management of the risk and resilience in the system.

Undoubtedly, the challenges highlighted by the RBI regarding the concentration in India's payments market and its impact on the competitive landscape, innovation and interest of consumers require consideration. However, in the absence of any cost-benefit analysis in favour of introducing NUEs, it is worthwhile to deliberate if introduction of NUEs is the optimal solution for addressing the challenges identified by the RBI. This is particularly true since the RBI itself notes that "even when there are multiple system providers, the risk of lack of substitution and market failure in a product may not get addressed because the capacity, efficiency, availability, accessibility of systems and services of different payment service providers would not be similar. The feature of facilitating interoperability would have to be built in the new payment systems being created." Accordingly, it may be worthwhile to explore if the policy focus should be moved on from creating NUEs to encouraging more competition at the payment service provider level and designing a framework that takes into account such principles that promote competition in the payments sector. The recommendations discussed in the succeeding chapter may be relevant to design this framework. To deal with the concerns regarding market concentration by NPCI, other measures to improve governance of NPCI may also be considered. This may include measures to separate the standard setting powers of NPCI from its operational functions by establishing a separate standard setting body backed by law.¹⁶² This body must have representatives from all stakeholders, including non-banks and domain experts. Further, the decision making at NPCI may be broad-based to ensure equal representation of all stakeholders. In line with the recommendations of the Committee on Digital Payments (2016), NPCI should have: (a) a time bound plan to move towards diffused shareholding where no individual shareholder along with persons acting in concert hold more than 5% of the equity share capital; and (b) have majority independent directors.

¹⁶² This may be a self-regulatory organisation ('SRO') recognised by the RBI under the Framework for Recognition of a Self-Regulatory Organisation for Payment System Operators issued by RBI on 22 October 2020. RBI, 'Framework for Recognition of a Self-Regulatory Organisation for Payment System Operators' (22 October 2020) <<https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=11986&Mode=0>> accessed 19 August 2021.

V. Redesigning India's Payment Systems Law | Recommendations

The preceding chapter highlights that the PSS Act fails to effectively account for three primary policy objectives that underpin most modern payment services laws. The regulatory framework for digital payments under the PSS Act must be re-designed, to allow it to adapt to new payment products and services and to account for the evolving nature of the payments sector. This will require an amendment to the PSS Act to create a new and modern payment systems law built on a risk-based approach that distinguishes between payment services and clearing and settlement systems from a systemic perspective and imposes regulation in a proportionate manner. This will lower the barrier of entry for low-risk products and services, and allow regulatory resources to be focused on the most systemically important actors. Further, the critical issues pertaining to obligations of payment service providers towards consumer protection, open access, and interoperability that are currently scattered across different sets of subordinate legislations should be addressed through such a statutory framework.

Pertinently, similar efforts to introduce provisions to promote competition and protect interests of consumers was done by the Committee on Digital Payments and the Inter-Ministerial Committee. However, along with these recommendations, both the committees also recommended creation of a new regulator for payment systems known as the Payments Regulatory Board ("PRB"). The PRB will not be a part of the RBI and will be set up as a separate regulator and, accordingly, the power to regulate payment systems will be exercised by such a regulator. The RBI had issued a dissent note against these recommendations.¹⁶³ Post the release of the report by the Inter-Ministerial Committee and the issuance of the dissent note, there has been no steps taken in this regard. Except for the creation of a separate regulator and the composition of NPCI, all the members of the Inter-Ministerial Committee were in agreement with the suggested amendments to the PSS Act.

Possible Approaches

To deal with the challenges discussed in the preceding chapter, this Report recommends redesigning the payment systems law in India to take into account the developments in the payments sector. The approaches and recommendations suggested in this chapter is guided by the three primary policy objectives discussed in the preceding chapter - ensuring safety and soundness of payment systems, promoting efficiency in the functioning of payment systems and the protection of user interests. To achieve an appropriate balance between these objectives, the Report relies on the following principles for suggesting the design of a new payment services law for India - (a) level of regulatory oversight should be commensurate to the risk posed by a payment activity; (b) provide legal certainty to businesses and consumers by setting out the broad contours and mandate under the principal law; and (c) provide flexibility to RBI to design subordinate regulations taking into account the evolving payments landscape.

This section highlights the two possible regulatory designs for modernising India's payment systems law. Irrespective of the regulatory design adopted, this section also highlights the approach that must be adopted while implementing the law.

¹⁶³ RBI, 'Reserve Bank of India releases Dissent Note on Inter-Ministerial Committee for finalization of Amendments to PSS Act' (19 October, 2018) <https://rbi.org.in/Scripts/BS_PressReleaseDisplay.aspx?prid=45287> accessed 19 August 2021.

1. **Approach A: Enact a separate legislation to streamline the governance of payment services in India (“Proposed Law”) and amend the PSS Act:** *The Proposed Law must provide a clear and graded framework within which emerging products and services along the payments value chain can be brought. It must incorporate a risk-based framework that distinguishes payments activities on the basis of the risk that they pose to the financial system. Unlike the PSS Act that focuses on empowering the RBI to regulate payment systems without specifying any significant obligations for system providers, the Proposed Law will regulate “payment service providers” and “payment systems” with a view to promote safety of the payment systems, as well as promotion of other policy objectives relating to competition, innovation and consumer interest. The enactment of the Proposed Law will also require an amendment to the existing PSS Act to carve out such services from the ambit of the PSS Act. The PSS Act may continue to regulate clearing and settlement systems from a systemic perspective.*
2. **Approach B: Enact a new law to create two parallel regulatory frameworks for payment services and systemically important systems and repeal the PSS Act:** *Alternatively, the PSS Act may be repealed and in its place a new law (also referred to as “Proposed Law”) may be enacted to create a two-tiered structure which provides for an authorisation framework for payment service providers as well as a designation framework for SIPS and SWIPS. All other features and provisions discussed in approach A will be incorporated in this approach also.*
3. **Principles-based primary statute with flexibility to the RBI to issue subordinate legislation:** *Given the evolving nature of the payments sector, the Proposed Law should adopt a principles-based approach where the primary statute sets out the broad principles to set the standards by which regulated entities must conduct their businesses.¹⁶⁴ The Proposed Law should provide flexibility to the RBI to set out the detailed and prescriptive rules through the directions. This will ensure that key enabling provisions for promoting competition and protecting consumers stem from the parent statute and are not scattered through notifications that are issued from the RBI time to time. Such an approach promotes certainty for businesses, inspires confidence of consumers, and protects lawmakers from potential legal risks that emanate from excessive delegation where all substantive provisions are set out in the subordinate legislation without any specific power or guidance set out in the primary statute. This is also in line with the global best practices as is evident from a review of the legal framework of Surveyed Jurisdictions.*

Key Features of the Proposed Law

Irrespective of the approach adopted, this section provides a list of indicative provisions that may be incorporated in the Proposed Law. Since the PSS Act already contains provisions relating to finality of netting and protection of consumer funds, the same is not reiterated here and the redesigned legal framework must continue with these provisions.

¹⁶⁴ There is a strong concern that the interpretation of broadly stated principles could lead to the risk of over-zealous and over-broad interpretation at the end of judicial authorities as well as regulators. Accordingly, it is required that such a principle-based regulatory framework must provide adequate flexibility to the regulator to issue formal subordinate legislation / guidance to support the main framework. Such a framework along with the guidance / subordinate legislation will provide rules that set out in more detailed form what conduct is required for the implementation of principle.

Introduce a definition for payment services

In some Surveyed Jurisdictions (such as the UK and Singapore), the law makes a distinction between the payment services and the large-value payment systems. Payment services mainly relate to services provided by a payment service provider to the end consumer (as opposed to a payment system). Such a definition seeks to cover new and emerging types of retail payment services. The identification of such services in the law is useful to design an effective regulatory framework while avoiding the overlaps or duplication in the efforts. The regulation of such services requires policymakers to take into account policy objectives relating to consumer protection, competition and innovation, in addition to regulations designed for systemic risks that underpin regulation of SIPS and SWIPS.

Typically, payment service providers provide five core functions:¹⁶⁵ (a) provision and maintenance of a payment account for electronic fund transfer; (b) enable initiation of payment at the request of a user; (c) provision of services to authorise, approve a payment transaction and / or enable the transmission of payment messages; (d) enable end user to hold funds in an account held with a payment service provider until it is withdrawn by the end user or transferred to a third party through an electronic funds transfer; and (e) enable the processes of clearing and settlement. The experience in Surveyed Jurisdictions indicate that such payment service activities may be divided into certain categories such as account issuance, electronic money issuance, domestic funds transfer, cross-border funds transfer and merchant acquisition. An explicit definition will help to provide clarity on what constitute payment services.

- 1. The Proposed Law should introduce a definition for payment services. In determining the definition, following characteristics may be considered: the services have a clear payments nexus, the service providers process funds or acquire transactions for merchants, and the service providers contract or deal with the consumers or the merchants.*
- 2. Similar to the UK, Singapore and Hong Kong, a list of activities that qualify as payment services may be outlined. However, the RBI should be given the flexibility to recognise other activities as payment services as long as it meets the criteria defined above.*
- 3. The definition of 'payment system' may be amended to confine it to infrastructure providers that facilitate transfer of funds and other clearing and settlement systems, but that does not necessarily interact with the end consumer.*
- 4. The Proposed Law should also introduce definitions for clearing services that are currently absent in the PSS Act.*

Outlining services that are exempted from the provisions of the Proposed Law

Any specific entity or activity that is sought to be exempted from the scope of the Proposed Law or certain provisions of the law should be expressly spelt out. The PSS Act empowers the RBI to exempt any person from the requirement to obtain authorisation under the PSS Act on specific grounds. For PPIs issued by banks and payment aggregator services provided by banks, the RBI has noted that such banks must obtain an approval from the RBI (as opposed to an authorisation). With the evolution of payment services and the emergence of overlay systems relying on existing payments infrastructure to process payments, questions have emerged regarding the need to regulate service providers that in many cases may be only providing support services (such as technology service

¹⁶⁵ Government of Canada, 'Archived - A New Retail Payments Oversight Framework' (2017) <<https://www.canada.ca/en/department-finance/programs/consultations/2017/new-retail-payments-oversight-framework.html>> accessed 19 August 2021.

providers) to facilitate payments, without being involved in the actual handling of consumer funds. In the past, confusion has often arisen regarding the regulatory status of third-party application providers that develop services over UPI.

Some Surveyed Jurisdictions expressly clarify that the technology service providers, and the payment activities involving cash, paper-based payment instruments (cheques, drafts, vouchers, postal money orders, etc.) are excluded from the purview of law. As payment services evolve and with the emergence of different overlay systems, there is a need to identify possible exclusions to provide certainty to the businesses.

- 1. The Proposed Law may consider clarifying the exemptions and the relaxations that will be provided under the law.*
- 2. Possibility of providing exemptions to certain services may be considered - including services for only technological support without any access to consumer funds, execution of a payment transaction on behalf of the payer or the payee, if performed by a commercial agent authorised to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee, and payment service providers that process small volume transactions.*
- 3. The Proposed Law must clarify the nature of exemptions or relaxation. For instance, the existing practice of allowing banks to provide payment services with an approval as opposed to an authorisation must also be recognised in the parent statute. In doing so, it is important to clarify the provisions that continue to apply to such banks.*
- 4. The Proposed Law may also consider including a provision enabling the RBI to provide relaxation or exemption from the law for experimentation on innovative solutions in a regulatory sandbox.*

Introduce a risk-based framework for regulating payment services and payment systems

The Proposed Law should incorporate a risk-based regulatory framework where regulation of payment service providers, and clearing and settlement systems is commensurate to the level of risk posed by them. To design such a framework, following measures may be considered:

Incorporate principles-based requirements: Since the payments landscape is constantly evolving, it may not be possible to have detailed prescriptive provisions in the primary statute. The provisions of the Proposed Law should be principles-based to accommodate the diversity of business models in the retail payments sector and to provide the regulator and the payment service providers with the flexibility to implement the measures in a way that fits the size, business model and the level of risk associated with a payment service provider. For instance, as a part of the operational standards, the Proposed Law may mandate a payment service provider to have a risk management policy, including a business continuity plan. However, the requirement in the Proposed Law will not prescribe how such a policy or business continuity plan designed by a payment service provider must look. The Proposed Law will only require that each payment service provider has a robust risk management policy to identify, monitor and manage operational risks and that a business continuity plan should be tailored to its operations. Details (if any) required maybe supplemented by the RBI through a subordinate legislation. A principles-based approach also allows flexibility to more effectively address business models that are currently unforeseen. In doing so, the Proposed Law will empower the RBI to specifically issue subordinate legislation to give effect to such provisions.

Tiering of measures for authorisation / licensing framework: Regulation for payment service providers should be proportionate and should be done with the intention to promote competition and innovation. The authorisation requirement should continue to apply to an entity that wants to provide payment services. Even within the authorisation framework, a risk-based approach and different authorisation may be envisaged for different types of payment services depending on the risk associated with such payment service. As discussed earlier, the MAS adopts a risk-based approach in the licenses issued to payment service providers. In such a case, the eligibility criteria¹⁶⁶ as well as regulatory requirements applicable to the payment service providers may vary

according to the risks posed by the scale and scope of payment services provided by such payment service providers. While creating such risk-based tiers, different factors such as functions performed by the entity (whether it has access to consumer funds), value and volume of payments, exposure to consumers, and its degree of interconnectedness with other retail payment systems or payment service providers may be considered.

Recognition of designation framework: The Proposed Law should envisage a designation framework for such payment systems whose disruption may trigger systemic risks or dent public confidence in the payment systems - i.e., SIPS and SWIPS. Generally, this may include systems that are the sole payment system in a country or those systems which process large value and are time critical. Most of the modern payment systems laws, including that of the Surveyed Jurisdictions that adopt a risk-based approach expressly recognise such SIPS (and SWIPS in some cases) in the primary legislation and create a specific oversight framework for such systems. Such systems are highly regulated given their potential to trigger or transmit systemic disruptions. In most Surveyed Jurisdictions, the payment systems are designated based on objective criteria. Such criteria may include (i) the number and value of transactions processed; (ii) the number and type of participants; (iii) the markets served; (iv) the market share controlled; (v) the interconnectedness with other FMIs and other financial institutions; etc.¹⁶⁷ Typically, such systems are subject to stringent oversight by regulators. Powers of the regulator vis-à-vis such designated systems include the power to call for information, imposing access obligations, power to ensure that such systems continue to function smoothly during times of disruption, power to impose conditions, and obligations of such systems to notify the regulator about events and changes.

MAS Payment Services Licenses - Risk-based Framework

Money-changing licence: Licensees can provide only money-changing services. The regulation is quite narrow in scope as these services are often provided by small businesses such as sole proprietors offering over-the-counter services with limited risks.

Standard Payment Institution licence: Licensees may provide any combination of the seven regulated payment services, if they process payment transactions or hold e-money float below specified thresholds. Standard Payment Institutions are subject to lighter regulations to encourage innovation and enterprise in smaller businesses.

Major Payment Institution licence: Licensees may provide payment services above the specified thresholds. As the scale of their operations would pose more risk, they are subject to more comprehensive and robust regulation.

1. *The Proposed Law should introduce a risk-based approach and a two-tiered regulatory structure: (a) an authorisation framework for payment service providers; and (b) a designation framework for SIPS and SWIPS.*
2. *In designing the authorisation framework, a risk-based approach may be adopted by introducing different types of authorisation for different payment services - the higher the risk a payment service pose, it should be subject to more stringent regulatory requirements.*
3. *The designation framework should be applicable to such payment systems whose disruption may trigger systemic implications on the financial system, affect public confidence in payment systems, or where such designation is necessary to ensure*

¹⁶⁶ This may include criteria relating to capital requirements, fit-and-proper person criteria, operational requirements, etc.

¹⁶⁷ Tanai Khiaonarong, Terry Goh, and Jihad Alwazir, 'Fintech and Payments Regulation: Analytical Framework' (International Monetary Fund 020/075, 29 May 2020) <<https://www.elibrary.imf.org/view/journals/001/2020/075/article-A001-en.xml>> accessed 19 August 2021.

better efficiency and competition in the financial system. Objective criteria for the designation framework should also be spelt out in the Proposed Law.

4. *Upon designation of a payment system under the Proposed Law, the RBI should be empowered to exercise specific powers against such designated payment systems. These powers can include the power to specify the basic structure of the system rules, power to vary certain terms and conditions of payment system agreements, the power to impose an access regime on a designated payment system, obligation of such systems to notify the RBI of specific changes, etc.*

Incorporate principles to manage operational risks

The technological innovations in the payments sector give rise to new forms of risks leading to operational failure. A payment service provider could experience an operational failure in various ways, including instances where a system is not working, is compromising the data transmitted, or if the system is prone to inaccuracies. It is critical to manage such risks as a safeguard against fraud, financial loss (for both the payment service provider and the consumer), and for maintaining privacy. From a payment service provider's perspective, such operational failures can damage its reputation, lead to legal disputes and result in financial losses. In case such payment services are intrinsically connected to other payment services, the disruption may have a negative effect on the financial system. From a central bank's perspective, managing such operational risks is a key to safeguarding public confidence in payment services. To mitigate these operational risks, the RBI has time and again issued circulars to regulate on different aspects of operational risks, including requirements relating to risk management. However, the PSS Act does not expressly recognise the obligation of payment service providers to have such risk management policies and procedures.

The Proposed Law may consider including a principles-based framework to address operational risks inherent to the retail payments. While the RBI may be empowered to issue subordinate legislation to set out detailed requirements for implementation of these principles, the establishment of these principles in the primary statute will provide legal certainty to regulated entities and also inform subordinate legislation on this issue. This may include the following principles.

1. *A payment service provider should establish a robust operational risk-management framework, including technology risk management policies, with appropriate systems, policies, procedures and controls to identify, monitor and manage operational risks.*
2. *A payment service provider's management should clearly identify and define the roles and responsibilities of officers responsible for addressing operational risks.*
3. *The operational risk management framework must be ratified by the management of the payment service provider.*
4. *The operational risk management framework, including policies, systems and procedures should be reviewed, tested and audited periodically.*
5. *A payment service provider should have a business continuity plan to deal with events posing a significant risk of disrupting operations of the provider. The key features of the plan may be spelt out in the primary statute leaving enough flexibility to businesses to design a plan suitable to their risk profile.*
6. *A payment service provider should identify, monitor, and manage the risks that end consumers, participants, or other third parties may pose to its operations. It should*

also identify, monitor, and manage the risks that its operations might pose to others.

Introduce consumer protection provisions

The PSS Act is silent on the consumer protection mandate for payment service providers. Provisions relating to the same have been provided by the RBI through different notifications issued from time to time. For payment service providers dealing with end consumers, the protection of consumer interest is critical and a scattered framework may not be the best approach to deal with this issue. It may be useful to set out broad based principles on consumer protection in the primary statute leaving details to be set out in the subordinate legislation.

Indicative list of consumer protection provisions that may be introduced in the Proposed Law are set out below.

- 1. The absence of adequate information about a payment service may lead to unfair or unanticipated outcomes for consumers. To protect consumers from harm that emanate from failure to disclose any or sufficient information, the Proposed Law should mandate payment service providers to disclose to end consumers key terms and conditions applicable to the usage of the payment service, including the main features, charges, risks associated with the service, rights and liabilities of the consumer, liability in case of unauthorised transactions and grievance redressal mechanism.*
- 2. While the Proposed Law may provide flexibility to issue subordinate legislation to spell out the detailed areas on which disclosure must be made and the manner in which such information may be disclosed, it may be useful to set out the broad principles that payment service providers must adhere to while making disclosures under the Proposed Law.*
- 3. In making such disclosures, the Proposed Law should require payment service providers to ensure that the disclosure is (a) provided in a language that is clear, simple and not misleading; (b) easily accessible; and (c) provided in a timely manner. Any change to the key terms and conditions must be specifically brought to the notice of the consumer.*
- 4. The RBI may encourage payment service providers to adopt standardised key facts documents to disclose key information to users relating to the service concisely and in local language.*
- 5. The Proposed Law should specifically require payment service providers to disclose all costs, fees, and charges that arise or may arise from a payment service and a breakdown of such charges. While many payment service providers negotiate final fee for certain services with merchants, it may be useful to clearly disclose the heads of charges.*
- 6. An efficient mechanism for handling consumer grievances is critical to inspire consumer confidence. Separate notifications issued by the RBI deal with guidelines relating to such consumer grievance redressal mechanism. However, the Proposed Law should expressly mandate payment service providers to have in place an effective and efficient consumer grievance redressal mechanism with key features / principles set out in the Proposed Law. Key principles that may be recognised in the Proposed Law include: (a) designation of a senior official that will be responsible for handling consumer grievances; (b) designation of officers who will receive and deal with grievances; (c) clearly outlining the scope of the grievance redressal mechanism; (e) provide clients*

with an easily accessible and free complaint mechanism; (f) adhere to timelines specified by the RBI for dealing with such complaints; and (g) procedure for recourse in case the payment service provider is not able to resolve the grievance.

Incorporate provisions for open access requirements

In networked markets like that of payments, the obligations relating to open access are critical for efforts to promote competition and innovation. This becomes relevant with the entry of new players in the payments space that seek to build the overlay systems. Surveyed Jurisdictions like the UK, Singapore, Hong Kong and Brazil prescribe open access requirements. It has been noted that access provisions could “improve the diversity of payment arrangements (particularly non-bank payment service providers), reduce single points of failure, widen the type of transactions that can be settled in central bank money (considered a safe and ultimate settlement asset that mitigates disruption risk from the failure of a private settlement service provider), and mitigate credit risks.”¹⁶⁸ Provisions in the primary statute requiring payment systems to provide open access to their systems can be instrumental to promote competition and innovation, which in turn could enhance the efficiency. Undoubtedly, provision of such open access should take into account operational, financial and legal consideration. Recognising this, the RBI has recently opened up centralised payment systems (i.e., RTGS and NEFT) to certain non-banks such as card networks, white label ATM operators and PPI issuers. Such a requirement is also significant for other retail payment systems, especially those operated by NPCI.

- 1. The Proposed Law should mandate payment service providers and designated payment systems to provide access to its systems on objective and non-discriminatory criteria.*
- 2. Such a framework must be ownership neutral, technology neutral and proportionate to the risk posed by such access. It is necessary to ensure that such requirements do not unnecessarily expose a payment system to risks such as data security risk, settlement risk, operational risk, business risk and to protect the financial and operational stability of the payment system.*
- 3. The Proposed Law may consider a mechanism to allow any person to approach the RBI for access to designated payment systems who is aggrieved by non-compliance of such designated payment systems with such access criteria set out in the Proposed Law.*

Introduce provisions on interoperability

Broadly, interoperability refers to the ability of consumers to transact across several independent payment solutions. For instance, in India, the RBI introduced interoperability requirements for PPIs that enable consumers to use a PPI to not just make payments to merchants operating a PPI issued by an end consumer’s PPI operator, but also to make payments and transfer funds to PPIs issued by other operators as well as to bank accounts. With the evolution of new payment solutions, ensuring interoperability has become a major issue to avoid the risk of concentration in the payments sector. In the absence of interoperability requirements, all payment services will operate in silos, denying consumers to enjoy the full potential of such payment solutions.

¹⁶⁸ Tanai Khiaonarong, Terry Goh, and Jihad Alwazir, ‘Fintech and Payments Regulation: Analytical Framework’ (International Monetary Fund 020/075, 29 May 2020) <<https://www.elibrary.imf.org/view/journals/001/2020/075/article-A001-en.xml>> accessed 19 August 2021.

1. *The Proposed Law should set out provisions on interoperability for payment service providers and designated payment systems.*
2. *The RBI may be empowered to determine the standards of interoperability for designated payment systems. The standards for interoperability for payment service providers may be undertaken by the RBI or be left to a self-regulatory organisation that has been envisaged by the RBI.*

Recognise role of third-party service providers

The introduction of UPI has witnessed the emergence of many non-banks providing consumer facing services and acting as third-party application providers. Such non-banks partner with banks that can access the UPI's core infrastructure. Notably, such third-party application providers are not required to be authorised by the PSS Act because they merely provide a technology interface and neither handle consumer funds nor provide payment, clearing and settlement services. Given the evolution of the payments sector and the emergence of bank-fintech partnership, the role of such third-party service providers have become crucial especially when they are directly interacting with consumers. Most of these partnerships are structured as outsourcing arrangements and is regulated under the outsourcing guidelines issued by the RBI¹⁶⁹ - both for banks as well as guidelines for outsourcing by non-bank PSOs. The RBI outsourcing guidelines prescribe that it will be the responsibility of the operator to ensure compliance with the law. Considering the evolution of such partnerships and the growing role of such non-bank entities in the payments sector, it may be worthwhile to explore the possibility of recognising their roles and prescribe a light-touch regulatory framework for them under the Proposed Law. Such an approach is not unprecedented. For instance, the Indonesia BI Regulations has provisions for support providers that work with payment service providers to support implementation of payment services activities.¹⁷⁰ Such entities provide support services of a technical nature.¹⁷¹ As per Article 61 of the Indonesia BI Regulations, a payment service provider, if working in cooperation with a support provider, is itself responsible for the conduct and security of that support provider.¹⁷² As part of this responsibility, payment service providers are required to conduct an assessment of the support providers on specified parameters prior to the initiation of cooperation.¹⁷³ For maintaining security and smooth processing of payment transactions, a payment service provider must ensure that there are processes in place to monitor performance of support providers; implement risk management measures by support providers; and that Bank Indonesia has access to support providers.¹⁷⁴ Notably, "cooperation" with such providers are subject to a risk-assessment framework¹⁷⁵ that can be carried out by the payment service provider and in case of any cooperation that is considered to be a high or medium risk, the same must be submitted to Bank Indonesia for the approval.¹⁷⁶ The Canada RPA Act also recognises "third-party service providers". A payment service provider required to submit information about critical providers¹⁷⁷ to the Bank of Canada at the time of application of registration.¹⁷⁸

¹⁶⁹ RBI, 'Guidelines on Managing Risks and Code of Conduct in Outsourcing of Financial Services by banks' (3 November 2006) <<https://www.rbi.org.in/scripts/NotificationUser.aspx?Id=3148&Mode=0>> accessed 19 August 2021; RBI, 'Framework for Outsourcing of Payment and Settlement-related Activities by Payment System Operators' (3 August 2021) <<https://www.rbi.org.in/Scripts/NotificationUser.aspx?Id=12136&Mode=0>> accessed 19 August 2021. The 2006 circular has been amended through other circulars.

¹⁷⁰ Indonesia BI Regulation, art. 1(6). We have relied on the machine translated English version of the law.

¹⁷¹ Indonesia, BI Regulations, art. 14(1). We have relied on the machine translated English version of the law.

¹⁷² Indonesia BI Regulations, art. 61. We have relied on the machine translated English version of the law.

¹⁷³ Indonesia BI Regulations, art. 61. We have relied on the machine translated English version of the law.

¹⁷⁴ Indonesia BI Regulations, art. 61. We have relied on the machine translated English version of the law.

¹⁷⁵ Indonesia BI Regulations, arts. 53 and 54. We have relied on the machine translated English version of the law.

¹⁷⁶ Indonesia BI Regulations, art. 56 read with art. 55. We have relied on the machine translated English version of the law.

¹⁷⁷ Third-party service providers that have or will have a material impact on the payment service provider's operational risks or the manner in which the provider safeguards or plans to safeguard end-user funds.

¹⁷⁸ Canada RPA Act, section 29.

The Proposed Law may recognise the concept and the role of third-party service providers that are engaged by a payment service provider and PSOs to facilitate payment services. Specific provisions regarding such providers that may be considered are:

- 1. The liability of a payment service provider for activities of the third-party service provider may be outlined.*
- 2. The Proposed Law should also specify the payment service provider's obligations, including the need to conduct necessary due diligence and to ensure that such third-party service providers have an adequate risk management strategy commensurate to the role of such providers in the payments process.*
- 3. The outsourcing guidelines may continue to flesh out the detailed requirements with the Proposed Law only specifying the main obligations.*
- 4. A risk-assessment framework that may be undertaken by the payment service provider (subject to review by the RBI in strict cases) may be considered. For any third-party service provider that is categorised as a critical service provider, the payment service provider may be required to specifically inform RBI about the appointment and change in such provider.*

Limit the types of subordinate legislation

As discussed above, currently there are different regulatory instruments that are employed by the RBI to issue directions under the PSS Act. The issuance of multiple instruments may often create uncertainty regarding the enforceability of the directions. The RBI may consider rationalizing the issuance of multiple regulatory instruments. To deal with the complexity and confusion created by multiple regulatory instruments, the Financial Sector Legislative Reforms Commission recommended that regulators should issue only two types of instruments - regulations and guidance.¹⁷⁹ The PSS Act currently recognises directions and guidelines.

The Proposed Law may consider rationalising/streamlining the subordinate legislation that may be issued to regulations and directions.

¹⁷⁹ Financial Sector Legislative Reforms Commission, Government of India, 'Report of the Financial Sector Legislative Reforms Commission' (22 March 2013) <https://www.icsi.edu/media/webmodules/linksofweeks/fslrc_report_vol1.pdf> accessed 19 August 2021.

Annexure A

Key Findings on the Charges Imposed by Banks and Payment Service Providers

The Report has examined the charges imposed by banks and other payment service providers on merchants and consumers. For this purpose, the Report relies on schedule of charges on payment transactions as publicly displayed by different banks and non-banks payment service providers: This comprises of:

- 6 banks (including 3 public sector banks and 3 private sector banks)¹⁸⁰
- 4 payment gateways and aggregators¹⁸¹
- 6 other entities that are engaged in provision of PPIs, facilitating UPI payments or both (this includes both authorised PPI issuers and third-party application providers and entities that act as both).¹⁸²

Review of charges imposed by banks and payment service providers

Charges imposed on merchants

- In most cases, the exact fee charged to merchants are not disclosed upfront. This is left to negotiations between the parties, subject to the regulatory prescriptions of the RBI in relation to MDR.

Payment Gateways / Payment Aggregators

- Besides providing the necessary infrastructure to accept payments, most surveyed payment aggregators also provide value added services to merchants, such as automated customer invoicing, real-time support services, payment analytics services, marketing tools, etc.¹⁸³ For availing such value-added services, merchants and payment aggregators negotiate the rates, which is over and above the standard gateway / platform fee for providing the necessary infrastructure to accept digital payments.¹⁸⁴
- Most entities display some information about their pricing plans. As per the current pricing plans available on the website of three entities for their basic payment gateway services plan, all of them charge a standard platform fee amounting to 2% of transaction amount alongwith applicable GST of 18% of the standard platform fee of the transaction. The platform fee increases to 3% of the transaction amount in case of international cards transactions, EMI transactions, etc.
- Only one payment aggregator does not display on its website any information regarding its pricing plans for merchants.¹⁸⁵ Only one surveyed payment aggregator expressly clarifies that it charges 0% platform fee for UPI transactions and RuPay powered transactions.¹⁸⁶

PPI Issuers and Third-party Application Providers

¹⁸⁰ Three private sector banks are Kotak Mahindra Bank, ICICI Bank, and HDFC Bank. Three public sector banks are State Bank of India, Punjab National Bank, and Central Bank of India.

¹⁸¹ Four payment gateways and aggregators are Razorpay, CCAvenue, BillDesk and PayU.

¹⁸² The surveyed entities engaged in provision of PPIs are Paytm, PhonePe, Mobikwik, and Amazon Pay. The surveyed entities engaged in facilitating UPI payments as Third-party Application Providers ("TPAPs") are Amazon Pay, PhonePe, Paytm, Google Pay, and Whatsapp Payments. Therefore, out of these entities that act as both, PPI issuer as well as TPAPs are Amazon Pay, Paytm, and PhonePe. It is also important to note here that Paytm undertakes these activities as Paytm Payments Bank Limited (PPBL) under its RBI authorisation as payments bank.

¹⁸³ CC Avenue 'Dashboard', <<https://dashboard.ccavenue.com/web/genregistration.do?command=navigateSchemeForm>> accessed 18 August 2021; Razorpay 'Simple and Transparent Pricing' <<https://razorpay.com/pricing/>> accessed 18 August 2021; PayU, 'Pricing' <<https://help.payu.in/knowledge-center/faq-pricing>> accessed 18 August 2021; PayU, 'Terms and Conditions' <<https://www.payu.in/tnc>> accessed 18 August 2021.

¹⁸⁴ For instance, PayU provides value-added services such as logistic support and business growth support, with its Business Plus and Business Premium plans for which a merchant has to pay additional one-time cost over and above the standard / gateway fee. PayU, 'PayU Puts Payment Specialists By Your Side' <<https://payu.in/plans>> accessed 18 August 2021.

¹⁸⁵ The merchants interested in availing BillDesk's services are required to contact to the BillDesk support services to know about the pricing details. BillDesk, 'Partner with BillDesk' <https://www.billdesk.com/part_bill.htm> accessed 18 August 2021.

¹⁸⁶ CC Avenue 'Dashboard', <<https://dashboard.ccavenue.com/web/genregistration.do?command=navigateSchemeForm>> accessed 18 August 2021.

- The surveyed entities do not publicly display the MDR charges payable by merchants. Typically, charges such as processing fee for provision of facility to accept digital payments are negotiated in writing by agreement.¹⁸⁷
- Only one surveyed entity provides a standard break-up of fees, including MDR, which it charges to merchants (small and medium businesses (SMBs)).¹⁸⁸ For UPI transactions and RuPay powered debit card transactions, it charges 0% fee. For merchants that are enterprises other than SMBs, it provides customized plans at price negotiated by written agreement. Other surveyed entities have not made their break-up of charges publicly available and disclose the same to merchants in their merchant acquiring agreements only.¹⁸⁹
- Two surveyed entities that are third-party application providers, charge a “transaction fee” (they do not clarify if this is MDR) to merchants, on every transaction, which is standard across all payment modes.¹⁹⁰ One such entity charges a fixed transaction fee¹⁹¹, while other entity charges such transaction fee that has been negotiated with a merchant in writing by agreement.¹⁹²

Charges imposed on consumers

Banks

- In accordance with the RBI directions, all 6 surveyed banks display a schedule of charges setting out common service charges that are imposed by the bank on retail customers for providing different digital payment services.¹⁹³ Broadly, the schedule contains charges relating to RTGS / NEFT based transactions (through net-banking/ mobile banking), IMPS transactions, debit card and ATM transactions, etc.

For UPI transactions

- Out of the surveyed banks, all the private sector banks impose zero charges on consumers for first 20 P2P UPI transactions of a month.¹⁹⁴ However, after the 20th transaction, they impose a cost, ranging from INR 2.50 to 2.75 on every UPI transaction of value upto INR 1,000 or below, and INR 5 on every transaction of value higher than INR 1,000. An additional 18% GST is also levied. However, these banks do not charge any fee to consumers, irrespective of the number of transactions, on UPI transactions carried out for the purposes of merchant payments, online shopping or bill payments.

¹⁸⁷ MobiKwik, 'Terms and Conditions of Service for Merchants', Clause 9.1 <<https://www.mobikwik.com/termsandconditions/merchants>> accessed 18 August 2021; Paytm, 'Pricing' <<https://business.paytm.com/pricing>> accessed 18 August 2021; Google Pay, 'Google Pay for Business Programs Additional terms of Service', Clause 14 <https://pay.google.com/intl/en_in/about/business/terms/> accessed 18 August 2021; Amazon Pay 'Merchant Agreement for Amazon Pay', Clause S-4 <<https://www.amazonpay.in/help/202125310>> accessed 18 August 2021.

¹⁸⁸ Paytm provides a chart detailing the value of MDR for each different payment mode (Debit transactions, Credit transactions, Netbanking etc.). Paytm, 'Pricing' <<https://business.paytm.com/pricing>> accessed 18 August 2021.

¹⁸⁹ Phonepe, Google Pay and Mobikwik provides that the details of such charges are disclosed to merchants through the written agreement. Amazon Pay provides the information only about the standard 'transaction fee' that it charges to merchants. WhatsApp Payments clarifies that it does not charges any fee to businesses using its services. See WhatsApp Payments, 'WhatsApp India Payments Terms of Service' <<https://www.whatsapp.com/legal/payments/india/terms>> accessed 18 August 2021.

¹⁹⁰ A “transaction fee” of 1.95% of the transaction value along with applicable GST of 18% of transaction fee are charged from a merchant as the standard processing charges which are applicable on merchants for all modes of payments i.e. Amazon Pay Balance, Credit Cards, Debit Cards, EMI and Net-banking. Amazon Pay, 'Amazon Pay Fees' <<https://www.amazonpay.in/help/20212280>> accessed 18 August 2021; Google Pay for business charges certain “Google Fee” on each transaction to merchants along with applicable taxes for providing GP for Business. Google Pay 'Google Pay for Business Programs Additional terms of Service' <https://pay.google.com/intl/en_in/about/business/terms/> accessed 18 August 2021.

¹⁹¹ Amazon Pay, 'Amazon Pay Fees', <<https://www.amazonpay.in/help/20212280>> accessed 18 August 2021; Amazon Pay, 'Merchant Agreement for Amazon Pay', Clause S-4 and 13 <<https://www.amazonpay.in/help/202125310>> accessed 18 August 2021.

¹⁹² Google Pay, 'Google Pay for Business Programs Additional terms of Service', Clause 14 <https://pay.google.com/intl/en_in/about/business/terms/> accessed 18 August 2021.

¹⁹³ RBI, 'Master Circular on Customer Service in Banks' (1 July 2015), para. 8.4 <https://m.rbi.org.in/scripts/BS_ViewMasCircularDetails.aspx?id=9862> as accessed on 8 July 2021.; HDFC Bank, 'Common Fees and Charges for Savings Account' <<https://www.hdfcbank.com/personal/save/accounts/savings-account/fees-and-charges>> accessed 4 August 2021; Kotak Mahindra Bank, 'Fees and Charges' <<https://www.kotak.com/en/personal-banking/erstwhile-ing-vysya/savings-accounts/orange-savings-account/fees-and-charges.html>> accessed 4 August 2021; ICICI Bank, 'Common Service Charges' (ICICI Bank) <<https://www.icicibank.com/service-charges/common-service-charges.page>> accessed 4 August 2021; State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Non Credit Related Service Charges' <<https://www.pnbindia.in/Non-Credit-Related-Service-Charges.html>> accessed 18 August 2021; Central Bank of India, 'Service Charges and Fees' <<https://www.centralbankofindia.co.in/en/service-charges-fees>> accessed 18 August 2021.

¹⁹⁴ Kotak Mahindra Bank, 'Charges' <<https://www.kotak.com/en/digital-banking/ways-to-bank/bhim-upi/charges.html>> accessed 18 August 2021; HDFC Bank, 'FAQs' <<https://www.hdfcbank.com/personal/pay/money-transfer/unified-payment-interface/faqs>> accessed 18 August 2021; ICICI Bank 'Payer UPI FAQs' <https://www.icicibank.com/Personal-Banking/faq/payments/payer-upi-faqs.page?ITM=nli cms_FT_upi_tf_link_linktext> accessed 18 August 2021.

- Contrary to this, the surveyed public sector banks do not mention about imposition of any charge in respect of UPI transactions regardless of the number of transactions.¹⁹⁵ There is no cap on the number of free P2P UPI transactions.

For IMPS transactions

- The surveyed private sector banks¹⁹⁶ charge INR 5 on every transaction of value upto INR 0.1 million and INR 15 on every transaction (regardless of online banking channel or bank branch channel) of value above INR 0.2 million for IMPS based transactions. Additionally, the applicable GST charges are also levied on these IMPS transactions.
- The surveyed public sector banks do not impose any charge for IMPS transactions carried out through online banking channel, except one surveyed public sector bank.¹⁹⁷ However, they impose charges for IMPS transactions carried out using bank branch channel.¹⁹⁸

For debit card transactions

- For debit card usage, most surveyed banks impose charges such as joining fee, annual membership fee, replacement fee, etc.¹⁹⁹ Banks may issue different kinds of debit cards with difference in transaction limits, cash withdrawal limits and range of loyalty points offered. The fee may vary based on the type of the debit card. Some surveyed banks do not charge any issuance or annual fee for some types of debit cards.²⁰⁰

PPI Issuers and Third-party Application Providers

- Most of these apps do not display the exact charges that a consumer will be charged for fund transfer. In case of UPI-based apps, most of these apps clarify that they charge no fee other than what consumer's issuing bank charges for UPI.
- Two surveyed apps clarify that they charge no processing fee to consumers for UPI transactions.²⁰¹
- For bank account to wallet transfers, most of the PPI issuing surveyed entities do not expressly specify the fee. They only mention that the consumers will incur such fee as will be charged by the consumer's issuing bank.²⁰²
- In case of wallet-to-wallet transfers, it has been observed that most of the digital wallet apps do not charge any fee. For wallet to bank account transfers, two surveyed apps clarify the charges they impose on consumers for such transaction.²⁰³

¹⁹⁵ Point 49, It is zero for both P2P transactions as well as merchant payments etc. State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Unified Payments Interface - FAQ' <<https://www.pnbindia.in/UPI-FAQ.html>> accessed 18 August 2021.

¹⁹⁶ HDFC Bank, 'Common Fees and Charges for Savings Account' <<https://www.hdfcbank.com/personal/save/accounts/savings-account/fees-and-charges>> accessed 4 August 2021; Kotak Mahindra Bank, 'Fees and Charges' <<https://www.kotak.com/en/personal-banking/erstwhile-ing-vysya/savings-accounts/orange-savings-account/fees-and-charges.html>> accessed 4 August 2021; ICICI Bank, 'Common Service Charges' <<https://www.icicibank.com/service-charges/common-service-charges.page>> accessed 4 August 2021.

¹⁹⁷ Central Bank of India does not provide any distinction between the charges for IMPS transactions carried out through banking channel and online channel. Central Bank of India, 'IMPS charges with effect from 11.08.2017' <https://www.centralbankofindia.co.in/sites/default/files/Service%20Charges/IMPS_charges_effect_11082017.pdf> accessed 19 August 2021.

¹⁹⁸ State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Non Credit Related Service Charges' <<https://www.pnbindia.in/Non-Credit-Related-Service-Charges.html>> accessed 18 August 2021.

¹⁹⁹ State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021; Punjab National Bank, 'Non Credit Related Service Charges' <<https://www.pnbindia.in/Non-Credit-Related-Service-Charges.html>> accessed 18 August 2021; HDFC Bank, 'Common Fees and Charges for Savings Account' <<https://www.hdfcbank.com/personal/save/accounts/savings-account/fees-and-charges>> accessed 4 August 2021; Kotak Mahindra Bank, 'Fees and Charges' <<https://www.kotak.com/en/personal-banking/erstwhile-ing-vysya/savings-accounts/orange-savings-account/fees-and-charges.html>> accessed 4 August 2021; ICICI Bank, 'Common Service Charges' <<https://www.icicibank.com/service-charges/common-service-charges.page>> accessed 4 August 2021.

²⁰⁰ In case of State Bank of India, the issuance charges are charged on Platinum and Gold category cards only. There is no issuance fee for all other category of debit cards. State Bank of India, 'List of Service Charges' <https://sbi.co.in/webfiles/uploads/index/30082019-UPDATED_LIST_OF_SERVICE_CHARGES.pdf> accessed 18 August 2021.

²⁰¹ MobiKwik, 'About UPI Payments' <<https://www.mobikwik.com/upi>> accessed 18 August 2021; MobiKwik, 'Terms and Conditions' <<https://www.mobikwik.com/termsandconditions>> accessed 18 August 2021; Paytm, 'Paytm UPI FAQ' <<https://paytm.com/offer/paytm-upi-faq>> accessed 19 August 2021.

²⁰² PhonePe, 'Terms of Use of Debit / Credit Cards' <<https://www.phonepe.com/terms-conditions/debit-credit/>> accessed 18 August 2021; MobiKwik, 'Terms and Conditions' <<https://www.mobikwik.com/termsandconditions>> accessed 18 August 2021; Paytm Payments Bank, 'Rates and Charges' <<https://www.paytmbank.com/ratesCharges.html>> accessed 18 August 2021; Paytm Payments Bank, 'Terms and Conditions' <<https://www.paytmbank.com/Terms&Conditions.html>> accessed 18 August 2021.

²⁰³ For instance, two surveyed PPI issuers charge fee of value ranging from 3.95%-5% of the amount transferred along with applicable GST on the amount transferred by consumer from wallet to the bank account.

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