Digital Payments
Level the Playing Field to Leverage the Potential
Competing with Cash in Retail Payments
OUTLINE

• Retail payments in India

• Competition assessment in digital retail payments industry

• Plausible impact of sub-optimal competition

• Recommendations to level the playing field

• Areas for further interventions
RETAIL PAYMENTS IN INDIA
CASH IS THE KING

Preferred modes of payments

UNTAPPED POTENTIAL OF DIGITAL PAYMENTS

Retail payments: 2016-17 (vol in mn)

COMPETITION ASSESSMENT IN DIGITAL RETAIL PAYMENTS INDUSTRY
Growth in transaction volumes in Tanzania owing to competition & interoperability with non-banks

Source: GSMA (2016)
METHODOLOGY FOR COMPETITION ASSESSMENT

CUTS Competition Impact Assessment Toolkit:

- Is the level playing field between competitors distorted?
- Are there entry barriers?
- Is the free and fair market process limited?
- Is monopoly and its abuse prevalent?
- Is the scope to introduce new products or supply existing products in new ways limited?
- Is institutional independence limited?
- Is a subsidy or state aid distortionary?
- Is the measure driven by vested interests promoted by the government?
- Is anti-competitive conduct not effectively prevented?
# Limited Role for Non-Banks in India

| PPIs | Allowed to issue select closed and semi-open PPIs  
|      | Not allowed to issue open system PPIs, among others  
|      | Direct and interoperable payments to other PPIs not allowed  |
| IMPS | Act as banking correspondents (BCs) to facilitate inter-bank fund transfer, and enable transactions with bank as counterparty  
|      | Payments inter-se non-banks not allowed  |
| AEPS | Engage in authorisation, best finger detection, e-KYC, demographic authentication and as BCs to facilitate withdrawal and transfer  
|      | Payments between banks and non-banks not allowed  |
| UPI  | Can partner with banks to develop apps, and participate in non-UPI leg of transaction  
|      | Cannot directly access UPI inhibiting seamless transactions with banks  
|      | Inter-se non-bank PPI payments not allowed  |
| BBPS | Can act as payment operating unit and facilitate bill payments  
|      | Need a sponsor bank to enable settlement  |
GOVERNMENT PREFERENCE TO BANK LED MODES

<table>
<thead>
<tr>
<th>BHIM</th>
<th>AEPS</th>
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<tbody>
<tr>
<td>• Merchant cashback scheme and customer referral bonus scheme</td>
<td>• Subsidy for adoption of biometric sensors</td>
</tr>
<tr>
<td>• Six months outlay ~ INR 500 crore</td>
<td>• Tax exemptions on specific acceptance infrastructure</td>
</tr>
<tr>
<td>• Expansion to Bank UPI applications and bank merchants</td>
<td>• Waiver of merchant discount rate</td>
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<tr>
<td>• Other service providers not eligible</td>
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</table>
INCREASING ROLE OF NPCI WITHOUT ADEQUATE CHECKS

- Private non-profit owned and governed by banks
- Sole retail payments organisation
- Operator of IMPS, UPI, AEPS and BBPS
- Provides clearance and settlement services
- Acts as standard setter and thus acts as quasi-regulator
- Issuer and operator of BHIM mobile application
- Received in-principle approval to operate National Electronic Toll Collection system
- Has access to substantial data
PLAUSIBLE IMPACT OF SUB-OPTIMAL COMPETITION
IMPACT OF SUB-OPTIMAL COMPETITION: INSUFFICIENT UPTAKE IN Q1

**TOTAL**
- Target met: 63%
- Target unmet: 37%

**UPI + BHIM**
- Target met: 75%
- Target unmet: 25%

**UPI**
- PhonePe: 35%
- BHIM: 26%
- Banks: 10%
- Target unmet: 29%

*Source: NPCI (Speech by former CEO)*
IMPACT OF SUB-OPTIMAL COMPETITION: LOW QUALITY

<table>
<thead>
<tr>
<th>AEPS transaction failure (%)</th>
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<tr>
<td>OFF-US</td>
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<tr>
<td>ON-US</td>
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</tbody>
</table>

- Banks refusal to transact with small banks and non-banks (ICICI Bank – PhonePe; SBI – Paytm)
- User unfriendly product design (Raman & White)
- Difficulties in navigation (Microsave)
- Limited features (Cashless Consumer)
- Inadequate disclosure (Omidyar/ Dalberg)
- Security and privacy concerns (Aggarwal and Chandorkar)

Source: Economic Survey
# Impact of Sub-Optimal Competition: Inadequate Redress

## Complaints Mix

<table>
<thead>
<tr>
<th>Category</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Deficiency in service</td>
<td>22%</td>
</tr>
<tr>
<td>Payments related</td>
<td>33%</td>
</tr>
<tr>
<td>Others</td>
<td>45%</td>
</tr>
</tbody>
</table>

*Source: CUTS Grahak Suvidha Kendra*

## Complaint Filing Process with NPCI

- **Transaction ID**: 12 digit no starting with 7
- **Amount**: [Amount]
- **VPA**: Enter virtual payment address eg. abc@upi or abc@xyzbank
- **Bank Name**: [Bank Name]
- **Date of Transaction**: [Month] [Day] [Year]
- **Mobile Number**: [Mobile Number]
- **Math Question**: 4 + 8 = [Answer]

*Source: [https://www.bhimupi.org.in/get-touch](https://www.bhimupi.org.in/get-touch)*
IMPACT OF SUB-OPTIMAL COMPETITION: HIGH COST OF ACCESS

• Potential margin of Rs. 45 per transaction for facilitating indirect access (to non-banks), available with entities having direct access to RTGS (NPCI/Banks)

• Capital and liquidity requirements for indirect access on non-banks

• Non-banks are required to maintain funds equal to outstanding balance in escrow with banks

• Rationalisation of merchant discount rate
RECOMMENDATIONS FOR LEVELLING THE PLAYING FIELD
LEVELLING THE PLAYING FIELD: RISK BASED REGULATION OF RETAIL PAYMENTS SERVICES

• Move away from entity based regulation
• Clearly define risk based criteria for undertaking activities
• Set graded customer identity and authentication requirements
• Allow non-banks direct and interoperable access of payments platforms
• Explore option to allow non-banks indirect access to critical clearance and settlement services
• Adopt activity based grievance redress processes
LEVELLING THE PLAYING FIELD: REFORMING MANAGEMENT OF RETAIL PAYMENTS PLATFORMS

- Create threat of competition for NPCI by putting in place clear regulations of operating retail payment and bill payment systems
- Broad base decision making of NPCI by expanding membership to new differentiated banks and non-banks
- Involve credible consumer organisations and experts in decision making processes of NPCI
- Revive the idea to create Payments System Advisory Council for broader and structured stakeholder consultations
- Regulate NPCI as Financial Market Infrastructure in accordance with relevant CPSS-IOSCO principles
LEVELLING THE PLAYING FIELD: REVISITING REGULATORY FRAMEWORK OF RETAIL PAYMENTS SECTOR

• Constitute the Payments Regulatory Board. Expand membership. Ensure government nominees are independent experts, with one representing consumers interests

• Adopt a new Payments and Settlement Systems Act. Proposed approach:

<table>
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<tr>
<th>Approach to regulation of retail payments</th>
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<tr>
<td><strong>Key risks</strong></td>
</tr>
<tr>
<td>• Operational</td>
</tr>
<tr>
<td>• Financial</td>
</tr>
<tr>
<td>• Market conduct</td>
</tr>
<tr>
<td>• Efficiency</td>
</tr>
<tr>
<td>• Money laundering and</td>
</tr>
<tr>
<td>terrorist financing</td>
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</tbody>
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*Source: Review of retail payments oversight framework in Canada*
ENSURING THAT PLAYING FIELD REMAINS LEVELLED

• Adopt regulatory impact assessment and regulatory sandbox approaches

• Facilitate consumer ownership on data and open banking

• Encourage partnerships between market players and early regulatory engagement

• Institutionalise risk based regulation and ensure coordination between different regulatory agencies
SUMMARY OF RECOMMENDATIONS

• Adopt risk based regulation of digital retail payments services

• Reform regulation and management of digital retail payment platforms

• Revisit regulatory framework of retail payments services sector

• Adequately prepare for the future
**AREAS FOR FURTHER INTERVENTIONS**

- Collecting primary evidence of adverse impact of regulatory and competition distortions in digital payments sector in semi-urban and rural areas, and consequent engagement with government

- Research and advocacy with government to facilitate adoption of medium term recommendations: i) ensuring efficient grievance redress; ii) creating threat of competition for NPCI; iii) regulating NPCI as FMI; iv) allowing non-banks indirect access to RTGS; v) revival of PSAC; vi) regulation of data ownership, sharing and portability; vi) allowing non-banks access to AEPS

- Research and advocacy with government on emerging areas such as: i) P2G and P2GoB transfers at central, state and local level, ii) regulatory sandboxes and regulatory impact assessment; ii) use of distributed ledger technology, artificial intelligence, regtech iv) creation of databases on consumer perception, (availability, efficiency, failures, refund) to measure progress, v) interface between payments and sectors like lending, insurance, investment, pension, toll collection, PAYG models

- Competition assessment in retail digital payments industry in other countries in South Asia and sub Saharan Africa, cross-border retail payments, remittances
THANK YOU

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