Payment & Settlement Systems in India

Payment and settlement systems in India are regulated by the Payment and Settlement Systems Act, 2007 (PSS Act), legislated in December 2007.

The Reserve Bank of India continually strives towards ensuring the smooth progress of the payments system. In India it is the BPSS (Board for Regulation of Payment and Settlement Systems) which is in charge of regulating these systems.

India has multiple payments and settlement systems. RBI Still continues to evolve new payment methods and slowly revamping the payments and settlement capability in India.

India supports a variety of electronic payments and settlement system, both Gross as well as Net settlement systems.

The Gross systems is

- Real Time Gross Settlement (RTGS)

The Net settlement systems are;

- ECS - Credit
- ECS - debit
- Credit cards and Debit cards
- National Electronic Funds Transfer (NEFT)
- Indo-Nepal Remittance Facility Scheme
- Immediate Payment Service

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Traditional Systems

Paper-based Payments

Use of paper-based instruments (like cheques, drafts, and the like) accounts for nearly 60% of the volume of total non-cash transactions in the country. In value terms, the share is presently around 11%. This share has been steadily decreasing over a period of time and electronic mode gained popularity due to the concerted efforts of Reserve Bank of India to popularize the electronic payment products in preference to cash and cheques.

Since paper based payments occupy an important place in the country, Reserve Bank had introduced Magnetic Ink Character Recognition (MICR) technology for speeding up and bringing in efficiency in processing of cheques.

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Later, a separate High Value Clearing was introduced for clearing cheques of value Rupees one lakh and above. This clearing was available at select large centres in the country (since discontinued). Recent developments in paper-based instruments include launch of Speed Clearing (for local clearance of outstation cheques drawn on core-banking enabled branches of banks), introduction of cheque truncation system (to restrict physical movement of cheques and enable use of images for payment processing), framing CTS-2010 Standards (for enhancing the security features on cheque forms) and the like.

While the overall thrust is to reduce the use of paper for transactions, given the fact that it would take some time to completely move to the electronic mode, the intention is to reduce the movement of paper – both for local and outstation clearance of cheques.

Credit cards and Debit cards -

As mentioned above India is one of the fastest growing countries in the plastic money segment. Already there are 130 million cards in circulation, which is likely to increase at a very fast pace due to rampant consumerism. India's card market has been recording a growth rate of 30% in the last 5 years. Card payments form an integral part of e-payments in India because customers make many payments on their card-paying their bills, transferring funds and shopping.

Ever since Debit cards entered India, in 1998 they have been growing in number and today they consist of nearly 3/4th of the total number of cards in circulation.

Credit cards have shown a relatively slower growth even though they entered the market one decade before debit cards. Only in the last 5 years has there been an impressive growth in the number of credit cards- by 74.3% between 2004 and 2008. It is expected to grow at a rate of about 60% considering levels of employment and disposable income. Majority of credit card purchases come from expenses on jewellery, dining and shopping.

Another recent innovation in the field of plastic money is co-branded credit cards, which combine many services into one card-where banks and other retail stores, airlines, telecom companies enter into business partnerships. This increases the utility of these cards and hence they are used not only in ATM's but also at Point of sale (POS) terminals and while making payments on the net.

Payment Banks

Reserve Bank of India (RBI) on 27 November 2014 released guidelines for Licensing of Payments Banks.

These guidelines will allow mobile firms and supermarket chains, among others, to enter the banking arena to cater to individuals and small businesses.

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The objectives of payments banks will be to further financial inclusion by providing small savings accounts and payments or remittance services to migrant labour workforce, low income households, small businesses, other unorganised sector entities and other users.

RBI Guidelines

- Existing non-bank **Pre-paid Payment Instrument** (PPI) **issuers**, **mobile firms** and **supermarket** chains, among others existing **NBFCs** and **micro finance lenders** are promoters who are eligible to **set up payment banks**.
- **Large public sector enterprises and big industrial houses** are **not allowed** to establish Payment banks.
- A promoter or promoter group can have a joint venture with an existing scheduled commercial bank to set up a payments bank. But they should have a sound track record of five years period of running businesses.
- Payment Banks will initially be restricted to holding a maximum balance of 1 lakh rupees per individual customer. It can issue ATM or debit cards but not credit cards.
- Payment bank cannot undertake lending activities but can distribute the non-risk sharing simple financial products such as mutual fund units and insurance products, etc.
- These banks also should maintain Cash Reserve Ratio (CRR) with the Reserve Bank, it will be required to invest minimum 75 percent of its demand deposit balances in Statutory Liquidity Ratio (SLR) with maturity up to one year and hold maximum 25 per cent in current and time or fixed deposits with other scheduled commercial banks for operational purposes and liquidity management.
- The minimum capital for payments banks is 100 crore rupees and it should have a leverage ratio of not less than 3 percent that is its outside liabilities should not exceed 33.33 times its net worth (paid-up capital and reserves).
- The promoter's minimum initial contribution to the paid-up equity capital for payments bank shall at least be 40 percent for the first five years from the commencement of its business.
- The foreign shareholding in the payments bank should be as per the Foreign Direct Investment (FDI) policy for private sector banks as amended from time to time.
- The operations of the bank should be fully networked and technology driven from the beginning, conforming to generally accepted standards and norms. It should have a high powered Customer Grievances Cell to handle customer complaints
- Those who are interested can apply before January 16 for first round of such permits however these guidelines are subjected to periodic review and revision.
- External Advisory Committee (EAC) of RBI will evaluate the applications and decision to issue an in principle approval for setting up of payment bank will be taken by RBI.
- The validity of the in-principle approval issued by the Reserve Bank will be eighteen months.

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Electronic Mode of Payments

Electronic Clearing Service (ECS) Credit

The Bank introduced the ECS (Credit) scheme during the 1990s to handle bulk and repetitive payment requirements (like salary, interest, dividend payments) of corporates and other institutions. ECS (Credit) facilitates customer accounts to be credited on the specified value date and is presently available at all major cities in the country.

During September 2008, the Bank launched a new service known as National Electronic Clearing Service (NECS), at National Clearing Cell (NCC), Mumbai. NECS (Credit) facilitates multiple credits to beneficiary accounts with destination branches across the country against a single debit of the account of the sponsor bank. The system has a pan-India characteristic and leverages on Core Banking Solutions (CBS) of member banks, facilitating all CBS bank branches to participate in the system, irrespective of their location across the country.

Regional ECS (RECS)

Next to NECS, RECS has been launched during the year 2009.RECS, a miniature of the NECS is confined to the bank branches within the jurisdiction of a Regional office of RBI. Under the system, the sponsor bank will upload the validated data through the Secured Web Server of RBI containing credit/debit instructions to the customers of CBS enabled bank branches spread across the Jurisdiction of the Regional office of RBI. The RECS centre will process the data, arrive at the settlement, generate destination bank wise data/reports and make available the data/reports through secured web-server to facilitate the destination bank branches to afford credit/debit to the accounts of beneficiaries by leveraging the CBS technology put in place by the bank. Presently RECS is available in Ahmedabad, Bengaluru, Chennai and Kolkata

Electronic Clearing Service (ECS) Debit

The ECS (Debit) Scheme was introduced by RBI to provide a faster method of effecting periodic and repetitive collections of utility companies. ECS (Debit) facilitates consumers / subscribers of utility companies to make routine and repetitive payments by 'mandating' bank branches to debit their accounts and pass on the money to the companies. This tremendously minimises use of paper instruments apart from improving process efficiency and customer satisfaction. There is no limit as to the minimum or maximum amount of payment. This is also available across major cities in the country.

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Electronic Funds Transfer (EFT)

This retail funds transfer system introduced in the late 1990s enabled an account holder of a bank to electronically transfer funds to another account holder with any other participating bank. Available across 15 major centers in the country, this system is no longer available for use by the general public, for whose benefit a feature-rich and more efficient system is now in place, which is the National Electronic Funds Transfer (NEFT) system.

National Electronic Funds Transfer (NEFT) System

In November 2005, a more secure system was introduced for facilitating one-to-one funds transfer requirements of individuals / corporates. Available across a longer time window, the NEFT system provides for batch settlements at hourly intervals, thus enabling near real-time transfer of funds. Certain other unique features viz. accepting cash for originating transactions, initiating transfer requests without any minimum or maximum amount limitations, facilitating one-way transfers to Nepal, receiving confirmation of the date / time of credit to the account of the beneficiaries, etc., are available in the system.

How does the NEFT system operate?

Step-1: An individual / firm / corporate intending to originate transfer of funds through NEFT has to fill an application form providing details of the beneficiary (like name of the beneficiary, name of the bank branch where the beneficiary has an account, IFSC of the beneficiary bank branch, account type and account number) and the amount to be remitted. The application form will be available at the originating bank branch. The remitter authorizes his/her bank branch to debit his account and remit the specified amount to the beneficiary. Customers enjoying net banking facility offered by their bankers can also initiate the funds transfer request online. Some banks offer the NEFT facility even through the ATMs. Walk-in customers will, however, have to give their contact details (complete address and telephone number, etc.) to the branch. This will help the branch to refund the money to the customer in case credit could not be afforded to the beneficiary's bank account or the transaction is rejected / returned for any reason.

Step-2: The originating bank branch prepares a message and sends the message to its pooling centre (also called the NEFT Service Centre).

Step-3: The pooling centre forwards the message to the NEFT Clearing Centre (operated by National Clearing Cell, Reserve Bank of India, Mumbai) to be included for the next available batch.

Step-4: The Clearing Centre sorts the funds transfer transactions destination bank-wise and prepares accounting entries to receive funds from the originating banks (debit) and give the funds to the destination banks(credit). Thereafter, bank-wise remittance messages are forwarded to the destination banks through their pooling centre (NEFT Service Centre).

Step-5: The destination banks receive the inward remittance messages from the Clearing Centre and pass on the credit to the beneficiary customers' accounts.

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Real Time Gross Settlement (RTGS) System

RTGS is a funds transfer systems where transfer of money takes place from one bank to another on a "real time" and on "gross" basis. Settlement in "real time" means payment transaction is not subjected to any waiting period. "Gross settlement" means the transaction is settled on one to one basis without bunching or netting with any other transaction. Once processed, payments are final and irrevocable. This was introduced in in 2004 and settles all inter-bank payments and customer transactions above ₹ 2 lakh.

RTGS vs NEFT

NEFT is an electronic fund transfer system that operates on a Deferred Net Settlement (DNS) basis which settles transactions in batches. In DNS, the settlement takes place with all transactions received till the particular cut-off time. These transactions are netted (payable and receivables) in NEFT whereas in RTGS the transactions are settled individually. For example, currently, NEFT operates in hourly batches. [There are twelve settlements from 8 am to 7 pm on week days and six settlements from 8 am to 1 pm on Saturdays.]

Any transaction initiated after a designated settlement time would have to wait till the next designated settlement time Contrary to this, in the RTGS transactions are processed continuously throughout the RTGS business hours.

Indo-Nepal Remittance Facility Scheme

Indo-Nepal Remittance Facility is a cross-border remittance scheme to transfer funds from India to Nepal, enabled under the NEFT Scheme. The scheme was launched to provide a safe and cost-efficient avenue to migrant Nepalese workers in India to remit money back to their families in Nepal. A remitter can transfer funds up to Indian Rupees 50,000 (maximum permissible amount) from any of the NEFT-enabled branches in India. The beneficiary would receive funds in Nepalese Rupees.

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Clearing Corporation of India Limited (CCIL)

CCIL was set up in April 2001 by banks, financial institutions and primary dealers, to function as an industry service organisation for clearing and settlement of trades in money market, government securities and foreign exchange markets.

The Clearing Corporation plays the crucial role of a Central Counter Party (CCP) in the government securities, USD –INR forex exchange (both spot and forward segments) and Collaterised Borrowing and Lending Obligation (CBLO) markets. CCIL plays the role of a central counterparty whereby, the contract between buyer and seller gets replaced by two new contracts - between CCIL and each of the two parties. This process is known as 'Novation'. Through novation, the counterparty credit risk between the buyer and seller is eliminated with CCIL subsuming all counterparty and credit risks. In order to minimize the these risks, that it exposes itself to, CCIL follows specific risk management practices which are as per international best practices.In addition to the guaranteed settlement, CCIL also provides non guaranteed settlement services for National Financial Switch (Inter bank ATM transactions) and for rupee derivatives such as Interest Rate Swaps.

CCIL is also providing a reporting platform and acts as a repository for Over the Counter (OTC) products.

Immediate Payment Service

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IMPS - **Immediate Payment Service** is an interbank electronic instant mobile money transfer service through mobile phones in India.

Currently majority of interbank mobile fund transfer transactions are channelized through NEFT mechanism. Under NEFT, the transactions are processed and settled in batches, hence are not real time. Also, the transactions can be done only during the working hours of the RTGS system.

Benefits

- Instant domestic fund transfer
- 24 X 7 (works on holidays also)
- Safe and secure, easily accessible and cost effective
- Channel Independent (can be initiated from Mobile / Internet/ ATM channels)
- Debit & Credit Confirmation by SMS
- Catalyst to Financial Inclusion
- Multiple input options to choose for initiating transactions, such as MMID/ Account /AADHAAR
- Multiple access mechanism to choose from

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Member PPIs

- Oxigen Services (India) Pvt Ltd.(Oxicash)
- ITZ Cash Card Ltd. - (ITZ Cash)
- Airtel MCommerce Services Ltd - (Airtel Money)
- Mobile Commerce Solutions Ltd - (Vodafone M Pesa)
- UAE Exchange & Financial Services - (UAE Exchange)

Bharat Bill Payment System

In the Second Quarter Review of Monetary Policy 2012-13, the Reserve Bank of India announced the setting up of a Committee to finalise the modalities of implementing an electronic GIRO payment system in India.

The Committee was set up under the chairmanship of G. Padmanabhan, Executive Director, Reserve Bank of India to study the feasibility of implementation of an electronic GIRO payment system in the country.

Subsequently, based on the recommendations of the Committee, a GIRO Advisory Group was constituted under the Chairmanship of Prof. Umesh Bellur, IIT Bombay, with the objective of defining a framework that enables the creation of pan India touch points for bill payments by customers in the country, irrespective of the geographical location of the billers.

The Group, which submitted its report on 20 March 2014, had recommended a tiered structure for bill payments system in the country – with a central unit setting the standards and various operating units working in accordance and adherence to the standards set for the BBPS.

Guidelines

- The Reserve Bank of India on 28 November 2014 issued final guidelines for the Bharat Bill Payment System (BBPS). The system will help consumers pay multiple bills like electricity, telephone and school fees at a single point of transaction.
- The BBPS is an integrated bill payment system offering inter-operable and accessible bill payment service to customers through a network of agents, enabling multiple payment modes, and providing instant confirmation of payment.
- The National Payments Corporation of India (NPCI) will function as the authorised Bharat Bill Payment Central Unit (BBPCU) to set the standards for BBPS processes which need to be adhered to by all operating units (Bharat Bill Payment Operating Units - BBPOUs) under the system.
- The prospective participants of the BBPS system are advised to interact with the NPCI to work out the modalities.
- The apex bank has set a 100 crore rupees net worth and domestic registration as qualifying conditions for those seeking to be authorised collection agents.

Source: Ministry of Finance, RBI

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