



Deviating from the BHIM-UPI Law

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Standing on the shoulders of a giant: The impact of UPI



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Abstract

With reference to Section 10A of the Payment and Settlement Systems (PSS) Act, 2007, and the prescribed electronic mode of payment, the Unified Payment Interface (in short UPI), we address a simple query.

Is it that banks and system providers are required by law not to charge *upon any person making or receiving a payment* using the UPI?

An answer to the above question would clarify a simple situation where we two go Dutch (split the bill) over lunch at a restaurant and you pay the full bill.

Should I be confident that the bank cannot charge me (because of the extant law) if I make a payment of Rs 200 to you (the Dutch amount that I owe you) using the UPI?

Or, should my lack of confidence prompt me to pay using the little cash that I kept for an emergency situation (where paying digitally is not an option)?

The paper dwells on the same and provides a guidance for policy.

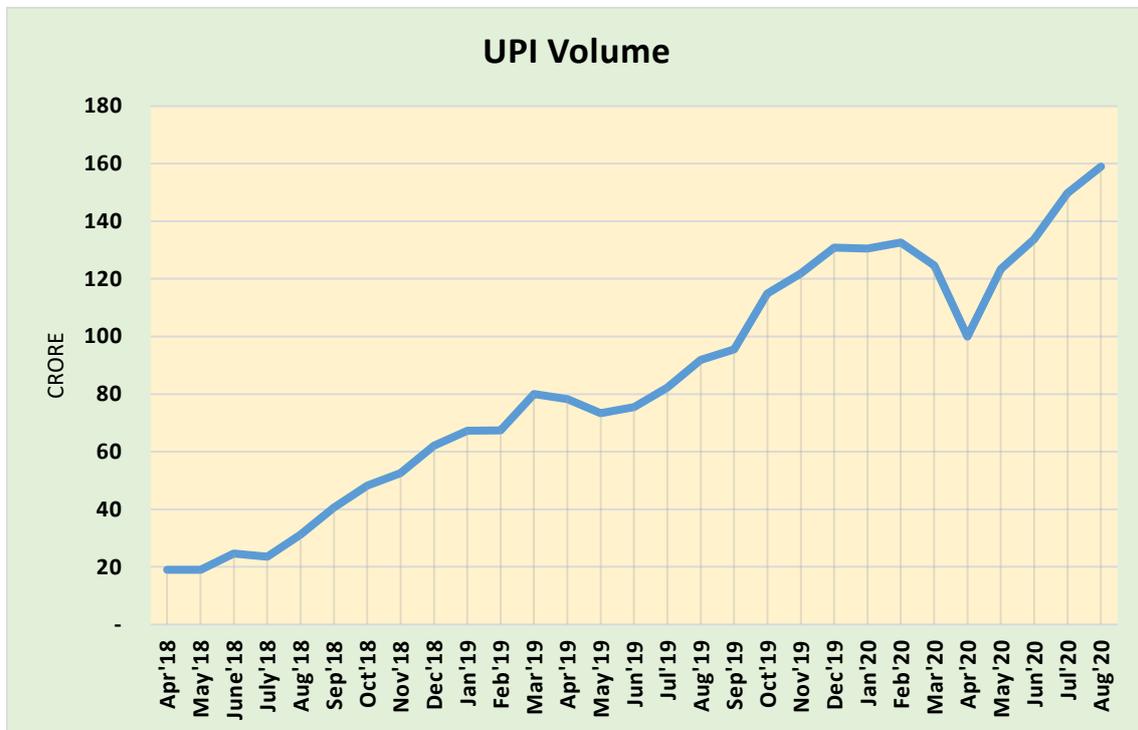
* The views expressed are those of the author and not necessarily of the institution to which he belongs.

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I. Introduction

0. In India, Unified Payment Interface (UPI) is the most commonly used means of payment after cash – a marked difference in the two modes of payment being that UPI is a digital mean unlike cash. In July 2020 alone there were 150 crore UPI transactions. Based on August daily figures till August 23, 2020, the August 2020 projection for UPI transactions is 159 crore. The chart on UPI volume, below, depicts a handsome and consistent growth that demonstrates the potential of UPI to replace cash usage.



1. The genesis of this paper is an observation relating to disarray in service charges during the recent past and which prevails even today. We highlight two instances,

- (i) Major Private banks have introduced charges on person-to-person (P2P) payments¹ using UPI beyond 20 transactions a month. The charges are Rs 2.50 for transactions under or equal to Rs 1000, and Rs 5 for transactions above Rs 1000. Additionally, goods and services tax (GST) are applied on these charges.

¹ Also referred to as peer-to-peer payments.



(ii) The largest Public sector bank imposed a charge @ Rs 17.70 (inclusive of GST) for every unassisted digital means of payment beyond four debits a month. This applied more specifically to our vast section of underprivileged depositors holding Basic Savings Bank Deposit (BSBD) Accounts (and all Pradhan Mantri Jan Dhan Yojana (PMJDY) Accounts are BSBD Accounts). This persisted during the past few years and even in Q4 of FY20 (despite Reserve Bank of India (RBI) and the PSS Act prohibiting, direct or indirect, charges for NEFT- and UPI-based electronic transactions, respectively).²

2. This may mislead other banks in the banking industry. We list India's top private sector banks along with the links to their schedule of service charges for payments made using UPI in excess of 20 P2P transactions per month. Each of the links were last accessed on August 19, 2020.

HDFC Bank: Rs 2.75 + GST for ticket size upto Rs 1000, and Rs 4.75 + GST for ticket size in excess of Rs 1000

<https://www.hdfcbank.com/personal/pay/money-transfer/unified-payment-interface/fees-and-charges>

ICICI Bank: Rs 2.50 + GST for ticket size upto Rs 1000, and Rs 5.00 + GST for ticket size in excess of Rs 1000

<https://www.icicibank.com/service-charges/common-service-charges.page?>

Axis Bank: Rs 2.50 + GST for ticket size upto Rs 1000, and Rs 5.00 + GST for ticket size in excess of Rs 1000

<https://www.axisbank.com/docs/default-source/default-document-library/change-in-charges-for-upi.pdf>

Kotak Mahindra Bank: Rs 2.50 + GST for ticket size upto Rs 1000, and Rs 5.00 + GST for ticket size in excess of Rs 1000

<https://www.kotak.com/en/digital-banking/ways-to-bank/bhim-upi/charges.html>

² This was taken up by the author with the government and RBI during early April 2020 and immediately thereafter the bank had reverted back indicating that they have initiated necessary steps to waive these charges. In this regard, in a recent follow-up communication (dated August 14, 2020), the bank has indicated that “*The waiver of service charges was approved by the Bank in view of the COVID-19 pandemic. However, we are in the process of allowing all non-cash debits transactions free of cost to the BSBD BC Channel customers. Necessary IT development is underway. All non-cash debit transactions shall be allowed free of cost shortly.*”.



The BHIM-UPI law

3. UPI is also known by BHIM-UPI, where BHIM is the acronym for ‘Bharat Interface for Money’. Effective November 1, 2019, the government brought in a law under Section 10A of the Payment and Settlement Systems (PSS) Act, 2007 which says that “... no bank or system provider shall impose, whether directly or indirectly, any charge upon a person making or receiving a payment by using the electronic modes of payment prescribed under section 269SU of the Income-tax Act, 1961.”

4. Effective January 1, 2020, UPI (BHIM-UPI) was notified as a prescribed electronic mode of payment under Rule 119AA of the Income-tax Rules, 1962. Thus, banks and system providers were prohibited to impose any charges to a person for payments made or received through BHIM-UPI. However, a question arose as to whether Section 10A, in any way, inherently qualifies such a person, when the Section mentions “... a person making or receiving a payment...”? Does “a person” mean “any person” and includes any two persons making and receiving a payment using BHIM-UPI?

Related insight

5. When the law got implemented, the banks and system providers had tried to interpret the law in a way that suited them. They tried to make the law mean that no bank or system provider shall impose any charge upon the merchant whose annual turnover exceeds Rs 50 crore, and that the banks and system providers have the freedom to charge the merchants whose annual turnover *does not* exceed Rs 50 crore. This idea was put forth since Section 269SU of the Income-tax Act, 1961 sets a law mandating every person, carrying on business, to provide facility for accepting payment through prescribed electronic modes, if his annual turnover in business exceeds Rs 50 crore.

6. Surely, such an interpretation is flawed since Section 10A of the PSS Act explicitly mentions that “... no bank or system provider shall impose, whether directly or indirectly, any charge *upon a person making or receiving a payment* by using the electronic modes of payment



prescribed under section 269SU of the Income-tax Act, 1961”. It explicitly mandates no imposition of charge, upon a person (without qualifying such a person), for using certain prescribed electronic modes and no leeway has been provided to banks and system providers in this regard.

7. In section 10A of the PSS Act, for the information regarding “the electronic modes of payment”, a reference has solely been made to section 269SU of the Income-tax Act, 1961, to simply identify the prescribed electronic modes, and nothing else (certainly not the merchant categorization). The prescribed electronic modes are defined in Rule 119AA in the Income-tax Rules, 1962, and include “Unified Payments Interface (UPI) (BHIM-UPI)”.

8. In a related development, to give further impetus to digital retail payments, effective January 1, 2020, RBI invoked the PSS Act and made online payments/transactions using National Electronic Funds Transfer (NEFT) free. RBI mandated that “, ... banks shall not levy any charges from their savings bank account holders for funds transfers done through NEFT system which are initiated online (viz. internet banking and/or mobile apps of the banks).”.



II. NPCI, banks and RBI

9. We look into the role and stance taken by some key stakeholders to address the impasse on an answer to the core question, “Is it that banks and system providers are required by law not to charge *upon any person making or receiving a payment* using the UPI?”.

The NPCI

10. BHIM-UPI is powered by National Payments Corporation of India (NPCI) that engineered to make it a giant payment infrastructure for the country. NPCI has not put any business restrictions onto the banks for P2P payments using BHIM-UPI other than years of moral suasion to keep the charges zero. Technically speaking, as on date, NPCI has not put any bar on banks to reasonably charge for P2P BHIM-UPI based digital payments, though NPCI is clear that the responsibility to meet the extant laws, rules and regulations of the country vests with banks for such acts of charging for payments carried out using BHIM-UPI.

11. In this context, it may be noted that in the approved minutes of a meeting of banks with NPCI dated February 14, 2020, the UPI Steering Committee of NPCI concurred to limit free P2P fund transfer transactions to 20 per month. However, we observe that NPCI does not explicitly indicate in the said minutes that the banks charge beyond 20 P2P transactions in a month. Therefore, the decision to charge for UPI transactions is that of banks and not of NPCI.

The banks

12. Coming to technicalities again, banks insist that they do not levy any charges to customers for making “PAYMENTS” using BHIM-UPI and are completely compliant to the regulations under Section 10A of the PSS Act. Their claims rest on a premise that payments are different from funds transfer. Banks try to justify that there is a clear distinction of a UPI funds transfer, restricted to P2P, and the UPI merchant payments, i.e., person-to-merchant (P2M) transactions, which are identified based on MCC (Merchant Category Code). However, these are business related superficial distinction created by NPCI for UPI, with the sole purpose of charging merchants for UPI transactions.



13. In this context, one needs to see what these P2P and P2M UPI transactions are as per the PSS Act. Section 2 of the PSS Act defines some terms and includes subsection 2(c), which says “2(c) “*electronic funds transfer*” means any transfer of funds which is initiated by a person by way of instruction, authorisation or order to a bank to debit or credit an account maintained with that bank through electronic means and includes point of sale transfers, automated teller machine transactions, direct deposits or withdrawal of funds, transfers initiated by telephone, internet and card payment”.

As per this definition even card payments and their usage at point of sale are fund transfer transactions. This implies that even the P2M payments are actually nothing but funds transfer.

The RBI

14. For the benefit of all and to technically understand the situation, a query (as in the Abstract of this paper) was put to the administrator of the PSS Act, which is the RBI.³ The RBI in a written response indicated that the instructions on zero charges for prescribed electronic modes have been issued by the Government of India. RBI did not provide an explicit answer to the explicit question related to the Section 10A of the PSS Act. RBI indicated that they do not have any comments to offer in this regard.

15. Though we respect RBI’s response, such a response from the administrator of the PSS Act, goes against the institution’s own medium-term strategy framework ‘Utkarsh 2022’. The framework was launched in mid-2019 to achieve excellence in the performance of RBI’s mandates and strengthening the trust of citizens and other institutions. The strategic framework reiterates RBI’s commitment to the Nation and includes “Excellence in performance of statutory and other functions” and “Strengthened trust of citizens and other Institutions in the RBI”. It is felt that not providing explicit answer relating to an Act implemented by RBI dwarfs the spirit behind Utkarsh 2022 and inhibits promotion of consumer education and protection.

³ Section 3 of the PSS Act states “The Reserve Bank shall be the designated authority for the regulation and supervision of payment systems under this Act.”. The query to RBI was addressed to Executive Director, RBI (overseeing the Department of Payment and Settlement Systems of RBI).



III. Answer lies in “Payments”

16. Banks have tried to highlight “PAYMENTS”, as if it is different, for sure, from fund transfer transactions. There is no ambiguity in the definition of ‘payments’. Payments can be effected in a number of ways using ‘common modes of payment’ and that includes bank transfers.

17. UPI – the “Unified PAYMENTS Interface” – is simply facilitating transfer of funds from one bank account to another bank account. This activity of UPI does not change with what the purpose of the transaction is. Similarly, BHIM – Bharat Interface for Money – is only an interface for money transfer from the books of account of one bank into the books of account of another bank. The initial name UPI, of the payment interface, got also known as BHIM-UPI, after NPCI launched its own UPI app called BHIM. So long as a transaction is done through UPI, by virtue of UPI being a payments interface, there is no ground (as per extant laws) to consider an account-to-account funds transfer as not being a payment.

18. The Section 10A of the PSS Act only mentions payment by using UPI as an electronic mode of payment (through Rule 119AA in the Income-tax Rules, 1962). It does not mention how UPI works and its internal nomenclatures of “P” for a person and “M” for a merchant. So long as UPI is used as a means of payment, it cannot be charged for and it is not necessary that “PAYMENTS” can be made only to a merchant or a person registered as a merchant as per the definition of “M” in UPI. Section 10A of the PSS Act simply mentions “a person making or receiving a payment by using UPI”. The Section does not mention the word “merchant”.

19. Returning a small person-to-person loan amount is a payment. Similarly, giving a gift money is also a payment. A small roadside cobbler receiving payments or a student making a payment to a tuition teacher can all be done using UPI, where the law does not make it mandatory for the beneficiary to become a merchant (in the UPI sense) to receive such a payment.

20. It cannot be that only merchants can receive payments. A UPI beneficiary is not required to register himself as a merchant to receive just a single payment in the whole month. For



receiving a loan repayment of Rs 100, one need not become a merchant just to satisfy UPI's business architecture. A fund transfer transaction (in a bank's parlance), in most situations, can be attributed to a payment, and of course, such payments are common when we receive salary payments through account-to-account fund transfers.

21. A non-merchant or a merchant receiving payments (through fund transfer or otherwise) is independent of the associated tax liability, if any, at the hands of the receiver.

Misusing 'misuse of UPI'

22. The concept of penalty or setting up restraints, in case of misuse of UPI, is good. With that in mind NPCI has already, at a system level, restricted P2P transactions to a maximum of 10 per day from a bank account. The initial misuse of UPI was based on a business model where every UPI handle⁴ strived to acquire more customers with a prospect of returns under the then UPI's commission for every transaction. More the transactions, more the earnings for the UPI handle. This prompted the UPI handles to lure UPI users to transact more through cash-back incentives. In other words, induced P2P UPI transactions through UPI handle's instigation led to several transactions that were really not genuine.

23. Such a situation requires more of restraining the UPI handles who in their vested interest had toyed the UPI product. We are not aware of any sort of penal charges that have been advocated by NPCI onto a UPI handle for misusing the UPI platform via inducing (unnecessary) transactions through cash-backs or similar attractions. With the minimized commissions, the extensive cash-backs have faded but still the UPI transactions – more for its genuine use case – have increased manifolds.

24. While declaring the P2P UPI transaction charges, the banks do not indicate that their charges are the penal charges (since P2P payments using UPI beyond 20 a month, necessarily amounts to misuse). Thus, it appears that the sole objective and the consequence of imposing

⁴ UPI handles are UPI IDs of the mobile apps of Payment Service Providers (PSPs) and Third Party App Providers (TPAPs) like that provided by banks' own apps and other apps like BHIM, PhonePe, Google Pay, Bharatpe, Amazon Pay, Paytm, etc.



such charges is to inhibit free genuine P2P UPI transactions among users and to generate some revenue for the bank.

25. Prior to 2020, just to promote on-boarding of small and medium merchants with less than Rs one lakh worth of BHIM-UPI transactions in a month, a merchant category was created (say 'PM'), for such P2PM transactions. That time, for a P2PM transaction, no fees were imposed onto the 'PM' merchants; unlike for merchants in P2M transactions, where merchants 'M' bore the transaction fee. Starting January 2020, there is no difference between a P2M and a P2PM transaction since the reason behind creating the category 'PM' no longer exists.

26. Now suppose we relax the fact that extant law prohibits banks and system providers to charge for P2P UPI transactions. Though not legally binding, we may see many instances where a potential P2PM and also a P2M transaction getting classified as a P2P transaction. The biggest challenge is the practical need for banks and such small merchants, having annual turnover of less than Rs 5 lakh (say), to necessarily get registered as a 'PM' merchant for the purpose of UPI. On the contrary, there would be a strong commercial reason for banks and system providers not to spend their energy to promote conversion of a true 'PM' from a 'P' to a 'PM'. The payment industry needs to address this first before even thinking of charging for P2P transactions. Converting, for appropriate categorization, of a true 'PM' or 'M' registered as a 'P', through some automatic means, may be a challenge with ample pitfalls.

Need to be technically correct

27. We would like to see that we remain technically correct as per the extant law. That we devise technically specious means to violate the law is different from getting the law changed altogether, if the situation so warrants. And such a change (or even a clarification provided for the same) can be better handled by the government rather than banks trying to come together and thrust a change. However, it is pertinent to mention that if this law for payments, using asset-lite UPI, between two persons is not good, it is difficult to justify as to why RBI's NEFT regulation, on unlimited free online funds transfer, can be considered relatively good.



28. Our horizon is 2000 crore genuine UPI transactions per month (as against the present level of 160 crore UPI transactions).⁵ That would eliminate day-to-day cash usage and bring in a true less-cash economy to the country. As a blessing, the much needed thrust to adopt UPI among the countrymen has now been provided by COVID-19. What even demonetisation could not, COVID-19 has! However, the system inhibitors like the still prevailing concept of interchange received by banks for P2P UPI transactions need to be judiciously eliminated. This section had tried to find the rationale on the payment industry's decision to charge for every P2P payments using UPI, beyond 20 a month. We need to be aware of the details and tread responsibly, more so since this relates to every user, or potential user, of 'Unified Payments Interface' in India.

⁵ Considering 50 crore active savings and current accounts, an average usage of two transaction a day yields 3000 crore UPI transaction a month. Also, considering 30 crore households in India, an average requirement of two transactions a day yields 1800 crore transactions a month.



IV. Costs and prices

29. The payment system of a country is sovereign and it is for public good. It facilitates use of money through transacting. Historically, money created by the government and RBI (mostly in the form of currency) circulated through the banking system and public. The cost of day-to-day usage of cash as a means of money was always borne by the government, RBI and the banks. The people using such money, for their day-to-day usage, never felt burdened to use such a payment mode.

30. Needless to mention, banks incur significant costs on cash management to facilitate financial transactions in the country. Major portion of such costs are not directly passed by the banks to their customers. The cost of servicing UPI, however, is miniscule compared to the costs the banks incur on handling cash.

Who pays for UPI?

31. As mentioned earlier, at present UPI transactions are about 160 crore a month. Even if the UPI transactions increase from the present level to 300 crore transactions a month (i.e., annually 3600 crore UPI transactions), at a reasonable cost of Re one per transaction for such high volumes and asset-lite infrastructure, it would cost the banking industry around Rs 3600 crore only. Now, is this a big amount to manage such a tremendous payments infrastructure, the BHIM-UPI, developed for the country, which has the greatest potential to reduce cash in the country unlike any other digital means of payment?

32. The question of who pays for the associated costs for UPI transactions has to hinge on the spirit of the law under Section 10A. Pricing policy can be ideally based on economic and accounting principles. On accounting principle, **there is no rigorous and impartial study on cost of producing such UPI services** and the likely loss to banks and system providers, should they have to bear it all.

33. However, as we work on pricing of UPI, there is an implicit assumption that banks may be at a loss if they are not allowed to charge. If so, why should the government insist on the same?



We should not forget that consumers pay a huge price to banks by implicitly sacrificing interest on savings and current deposits. The implicit price paid by the savings and current account depositors annually (for FY19-20) is of the order of Rs 1.29 lakh crore.⁶ Thus, what is perceived as ‘free’ service of savings/current accounts by banks is actually paid *ex ante* by depositors by agreeing to park their funds in these accounts at a lower return. This is possibly the reason why the government insists on zero charge for a prescribed digital payments product like the UPI. To settle the issue objectively, without taking sides, we need to consider all aspects.

Moving towards a solution

34. Is the government’s decision to make free the digital transactions rational? Given that digitisation through UPI leads to multifaceted savings by banks as compared to providing the same through paper based services (cash and cheques), the government has enough justification for spearheading payments using UPI free of charge. While banks have to contribute their bit for the payment system, it does not mean that the government and RBI do not have to share the cost burden in their endeavour towards furthering the digital payment system in the country and facilitate people to move away from cash for every small, medium or large transaction.

35. The government and RBI have been bearing significant costs on printing and management of cash. Over the past few years they have spent about Rs 5000 crore annually on cash printing alone and even more on cash management. The expenditure towards UPI may be much lower and could even curtail the expenditure on cash. A reduced cash-cost burden must partly get channelized for supporting the UPI ecosystem. While UPI is still in its infancy towards replacing cash, given its rapid progress and future potential, it deserves full support from RBI. Just like RBI provisions for the cost of cash in their books of account, it should also provision for bearing the cost associated with managing the UPI infrastructure.

36. UPI as a digital payments platform increases efficiency towards tax compliance, and provides overall convenience for public good. With the government’s vision of no direct or indirect charge on payments using UPI, an appropriate sharing of cost burden by the

⁶ Das A. (2020), “Merchant transactions through debit cards – costs and prices”, IIT Bombay Technical Report (forthcoming).



government and RBI is called for (with UPI being the simplest alternative to cash in this era of mobile phones).

Concluding Remark

37. With the new law prohibiting banks and system providers to charge users of the prescribed electronic modes of payment, we find a persistent debate on MDR (merchant discount rate), a fee that merchants pay for accepting payments through digital means. Though it is a fact that card based merchant payments has worked well internationally on the principle of MDR, we need to be a bit careful to apply the same principle for the asset-lite UPI, which has the potential to substitute our day-to-day cash requirements. For the present, without advocating anything on the MDR front for UPI, we may at most have a relook at the MDR issue surrounding debit cards. In this connection, we would like to refer to a forthcoming report on the subject by the author as indicated in footnote 6.



References

1. The Finance (No. 2) Act, 2019 inserted section 269SU in the Income-tax Act, 1961, with effect from the 1st day of November, 2019, namely:— “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.”. Acceptance of payment through prescribed electronic modes.
2. In exercise of the powers conferred by section 269SU read with section 295 of the Income-tax Act, 1961, the Central Board of Direct Taxes inserted rule 119AA in the Income-tax Rules, 1962, with effect from the 1st day of January, 2020, namely:— “119AA. Modes of payment for the purpose of section 269SU.- Every person, carrying on business, 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 shall provide facility for accepting payment through following electronic modes, in addition to the facility for other electronic modes of payment, if any, being provided by such person, namely:—
 - (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).”
3. The Finance (No. 2) Act, 2019 inserted section 10A in the Payment and Settlement Systems Act, 2007, with effect from the 1st day of November, 2019, namely:— “10A. Notwithstanding anything contained in this Act, no bank or system provider shall impose, whether directly or indirectly, any charge upon a person making or receiving a payment by using the electronic modes of payment prescribed under section 269SU of the Income-tax Act, 1961.”. Bank, etc., not to impose charge for using electronic modes of payment.
4. RBI notification dated December 16, 2019 on Furthering Digital Payments – Waiver of Charges – National Electronic Funds Transfer (NEFT) System, with effect from January 1, 2020, namely:— “In order to give further impetus to digital retail payments, it has now been decided that member banks shall not levy any charges from their savings bank account holders for funds transfers done through NEFT system which are initiated online (viz. internet banking and/or mobile apps of the banks).”