

Customers providing benefit to banks through usage of ATM and EDC machines

Ashish Das¹

Department of Mathematics, Indian Institute of Technology Bombay, Mumbai-400076, India
and
Department of Statistics, The University of Akron, Akron, Ohio-44325, USA

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Abstract

The usage of ATM and EDC machines by the customers is a blessing in disguise for banks. The paper attempts to argue on how imposition of a fee for third party ATM transactions serves to be counterproductive to the banking system and makes the payment system inefficient. IBA seems to take steps (keeping banks in the forefront) to generate additional income for the banks by an easy path of levying fees which is against consumer interest. RBI's approach had been to put such issues, after its initial analysis, in the public domain for public comments. Thereafter, a reasoned decision, keeping broader public interests in mind, is taken.

1. Introduction

On December 24, 2007, Reserve Bank of India (RBI) came out with an approach paper on Fair Pricing and Enhanced Access of Bank ATMs. Subsequently, on March 10, 2008, RBI issued a direction to all banks making use of other bank ATMs for balance enquiries and cash withdrawals free effective April 1, 2009. It now appears that Indian Banks' Association (IBA) may be taking this with a pinch of salt since it wants RBI to review its decision on providing free ATM usage. Needless to say, with IBA's stated vision "to work proactively for the growth of a healthy, professional and forward looking, banking and financial services industry, in a manner consistent with public good", it remains to be seen how such a move by IBA is consistent with being forward looking and for public good.

Most of the banks have carried out a transition from only ATM cards to ATM-cum-Debit cards. In short we call such cards as Debit cards. In India we have over 1464 lakh (as of June 2009) debit cards issued by banks (excluding those withdrawn/blocked). By March 2008 end, the number of ATMs deployed in India was 34,789 with the then annual rate of increase in the number of ATMs being 28.4%. Thus considering a reasonable figure of 44000 ATMs deployed currently by the banks, on an average each ATM caters to about 3300 debit cards. In extensively

¹ Dr. Ashish Das is Professor with the Indian Institute of Technology Bombay (presently on sabbatical as Visiting Professor at The University of Akron, Ohio). E-mail: ashish@math.iitb.ac.in

populated locations, the ATMs serve many more debit cards. The advent of ATMs helped to improve customer convenience and reduce costs.

The cost of a bank transaction on manual mode is estimated to be in the range of Rs. 45 to Rs. 50 while it is around Rs. 15 on ATM and Rs. 4 on e-banking². This is consistent with the RBI's December 2007 approach paper which indicated that generally the aggregate charges per ATM transaction range from Rs.10 to Rs. 20 for cash withdrawal and Rs. 5 to Rs. 8 for balance enquiry (these being the cost/charges incurred by the card issuer's bank for use of ATM of other bank). In fact, depending on business strategies adopted, some banks spend as high as Rs. 72 to service a customer at counters while they spend only Rs. 18 to service him at ATM. Realizing the benefits bank get out of use of ATM some banks, in order to push customers to ATM, even offer rewards.

Let us consider the practical situation wherein a bank X does not have an ATM located where it should have one (assuming a number of their own customers would have used it, had there been one). Bank X customers, in that location, may then look for a location where bank X has an ATM or a bank branch. In other words, bank X induces inconvenience to their customers and also carry a risk of incurring more expenditure (through a customer's branch visit) because of its inability to have placed an ATM at the location. Thus, keeping in mind the role of technology in enhancing quality of customer service in banks, RBI came up with an innovative idea of making third party ATM same as customer's own bank ATM thereby considerably reducing the cost (of opening more branches or installing more ATMs) to banks. This way, while increasing efficiency and better utilization of resources, bank X customers can use bank Y ATM while bank Y customers can use bank X ATM with cost saving and convenience to banks and bank customers. The expenditure and income incurred by each of banks X and Y balance out and in fact there is a tremendous gain for banks even after paying Rs. 17-20 by profiting almost Rs. 30 on each ATM cash withdrawal as against carrying out the transaction on manual mode over the branch counters.

As per RBI, international experience indicates that in countries such as UK, Germany and France, bank customers have access to all ATMs in the country, free of charge except when cash is withdrawn from white label ATMs or from ATMs managed by non-bank entities. There is also a move, internationally, to regulate the fee structure by the regulator from the public policy angle. The ideal situation is that a customer should be able to access any ATM installed in the country free of charge through an equitable cooperative initiative by banks.

² Speech of Shri M. D. Mallya, Chairman and Managing Director of Bank of Baroda and the Deputy Chairman of IBA, on "Role of Technology in Enhancing Quality of Customer Service in Banks" at a function organized by the All-India Bank Depositors' Association, on June 30, 2009.

2. Bank's cost on ATM

Assuming that it indeed costs the bank around Rs. 15-18 when a customer of the same bank uses its own ATM machine, it will cost the bank around Rs. 17-20 when a different bank's ATM is used. This is due to a component of the cost called the switch (inter-connectivity of ATM Networks) fee which is the fee levied by the switch providers like National Financial Switch (NFS), Mitr, Cashnet, VISA, MasterCard etc. and varies from 'Nil' to Rs. 3 per transaction. In order to reduce the cost of operations for banks, the Institute for Development and Research in Banking Technology (IDRBT), which is administering the NFS, has waived the switching fee since December 2007. Furthermore, the recently established National Payments Corporation of India (NPCI), while handling all retail payments and settlement activities in the country, is expected to soon procure Financial Switch and go the IDRBT way. Thus, even if RBI covers for the switch fees, the ATM usage (cash withdrawal) cost pre-April 2009 was worked out by the banks and this figure has been claimed to be around Rs. 15-18. It is not known what had been the method adopted while arriving at this figure.

It becomes imperative to understand the actual cost for setting up and running an ATM unit. Apart from the cost of the ATM instrument itself, the major recurring cost involves expenditure on location rent, electricity (air conditioner), network/communication, security, stationary, maintenance and cash transportation (for off-site locations) and a possible switch (inter-connectivity of ATM Networks) fee. Thus, it is now clear that once a bank X installs an ATM unit, to break even on the initial expenditure of the ATM instrument, it would want (a) more of their own customers to use the ATM rather than use the branch counters which on the long run cost more than 3 times to disburse cash or make a balance inquiry and (b) more of other bank's customers to use their ATM to generate revenue. Now, it should be understood that when a customer of a different bank uses the ATM, that other **bank saves almost Rs 30 even after shelling out around Rs. 17-20 as interchange and switch fees.**

With the number of third party transactions surging post-April 2009, it is imperative to re-work the costing aspects (currently perceived at around Rs. 15-18) and revisit the basis of the ATM policy. The cost per transaction would nearly half if the number of usage of an ATM is doubled. This aspect need to be kept in mind while RBI attempts to identify the true cost of running an ATM machine post-April 2009.

After the ATM transactions fees on using other banks' ATMs was scrapped in April 2009, the IBA studied the entire gamut of ATM transactions. The study found that a majority of the ATM transactions were in the range of average withdrawals of Rs. 3,500-4,000, and 90% of all transactions were below Rs. 10,000. Hence, the intended purpose to serve the common man was achieved. However, the study point out that there was a small minority of users who withdrew very large sums on account of high card limits given by some banks to privileged customers. At the other extreme, there were some customers who withdrew miniscule amounts. This could

create logistics problems for banks at the cost of the common user. However, these problems need to be looked at more closely. IBA's solution in form of limiting the number of free third party withdrawals to 5 a month is not reasoned enough and it would lead to limiting freedom to draw any amount (within Rs. 10,000) more than 5 times in a month. The number 5 appears arbitrary. If need be, for free third party ATM withdrawals, one can possibly think of limiting the total amount to, say, Rs. 1.5 lakh a month. Furthermore, if there are severe logistic issues involved just because a small minority of users tends to withdraw very large sums on account of high card limits, RBI may think of discouraging such users by additionally limiting free third party ATM withdrawals to a total of Rs. 20,000 per day, say. Such a move would achieve eliminating the difficulties encountered by the banks and alongside also achieve the intended purpose to serve the common man.

However, the banks seem to take steps to generate additional income by an easy path of levying fees which is against consumer interest and usurping of consumer surplus. Easy availability of ATM, free of cost, will reduce the demand for reserve cash, thereby enabling the economy to save some resources. However, IBA is free to make such a move for reintroducing third party ATM fees provided it is based on complete and fully worked out facts related to cost data on ATM and manually servicing customers over counters. It should clearly establish that third party ATM is a costlier proposition vis-à-vis branch counters. RBI's approach had been to put such issues, after its initial analysis, in the public domain for public comments. Thereafter the RBI takes a reasoned decision, keeping broader public interests in mind. For this case too public would expect similar practice to prevail.

3. Fees on debit cards

The banks have been given the freedom to decide on the Annual Fees on debit cards. In order to have a feel on the Annual Fees imposed by the banks, we selected 35 banks. The criteria for selecting these banks had been (a) all public sector banks with 900 or more bank branches, (b) all private banks with 300 or more bank branches, and (c) all foreign banks with 10 or more bank branches. Such a selection allows 88% representation of all bank branches in India. Table 1 shows the details on sample coverage while Table 2 gives the full list of the banks.

Table 1: Coverage of sample

Bank group	Total # of offices	% of Total # of offices	# of offices in sample	% of Total Sample Size	Sample %
Foreign (5)	277	0.45	215	0.40	77.62
Private Banks (10)	7975	13.05	6233	11.53	78.16
Public Sector Banks (20)	52880	86.50	47611	88.07	90.04
Total (35)	61132	100.00	54059	100.00	88.43

Source: RBI (<http://www.rbi.org.in/scripts/PublicationsView.aspx?id=9868>)

Annual Fees on debit cards were obtained from each of the banks based on the information provided by the banks on their respective websites (as of Mid-August 2009). Table 2 provides

the Annual Fees for least expensive debit cards (some other premium or brand associated cards or add-on cards may cost more) along with details on number of branches, ATMs and percentage of ATMs to branches for each of the banks. Based on ancillary information on the number of branches, we obtain the weighted mean of Annual Fees. The weights considered are the number of branches since it is closely related to the number of debit cards issued by the banks. (In fact RBI may have bank wise distribution of the 1464 lakh debit cards issued by banks, using which the true mean of the Annual Fees on debit cards can be worked out.) From Table 2, it is observed that the weighted mean of Rs. 40 is about 31% lower than the simple means of Rs. 58. Also, if one looks at the simple mean of the Annual Fees with respect to bank type, public sector banks have a mean of Rs. 37, private banks have mean of Rs. 75 and foreign banks Rs. 106. It is also noted that as high as 15 banks (i.e., 43% of the banks) do not impose any Annual Fees. Thus, it becomes apparent that as such banks want to encourage their customers to take a debit card and use them so that in effect banks can save on manual transactions over the counters which, as mentioned earlier, cost about 3 times more.

Table 2: Debit card annual fees

S.No.	Name of Bank	Bank Type	Branches	ATMs	% ATMs to Branches	Debit Card Annual Fees (Rs.)
1	Corporation Bank	Public	964	956	99	99
2	State Bank of Hyderabad	Public	992	510	51	50
3	Vijaya Bank	Public	1053	272	26	0
4	Dena Bank	Public	1071	313	29	100
5	Oriental Bank of Commerce	Public	1344	741	55	100
6	Andhra Bank	Public	1363	656	48	0
7	Bank of Maharashtra	Public	1365	345	25	0
8	United Bank of India	Public	1399	164	12	50
9	Indian Bank	Public	1524	600	39	0
10	Indian Overseas Bank	Public	1879	451	24	0
11	UCO Bank	Public	1945	305	16	100
12	Allahabad Bank	Public	2135	211	10	100
13	Syndicate Bank	Public	2188	1000	46	0
14	Union Bank of India	Public	2324	1146	49	100
15	Canara Bank	Public	2690	2006	75	0
16	Bank of Baroda	Public	2845	1106	39	0
17	Bank of India	Public	2845	435	15	0
18	Central Bank of India	Public	3324	367	11	0
19	Punjab National Bank	Public	4178	1516	36	0
20	State Bank of India	Public	10183	5848	57	50
21	Catholic Syrian Bank Ltd.	Private	346	125	36	0
22	ING Vysya Bank	Private	398	203	51	150
23	Karnataka Bank Ltd.	Private	436	141	32	0
24	Bank of Rajasthan Ltd.	Private	458	96	21	100
25	Jammu and Kashmir Bank Ltd.	Private	480	210	44	100
26	South Indian Bank Ltd.	Private	489	225	46	50
27	Federal Bank Ltd.	Private	601	516	86	50
28	Axis Bank Ltd.	Private	626	2764	442	100
29	HDFC Bank Ltd.	Private	1150	2345	204	100
30	ICICI Bank Ltd.	Private	1249	3881	311	99
31	Deutsche Bank AG	Foreign	10	31	310	0
32	ABN-AMRO Bank N.V.	Foreign	28	116	414	180
33	Citibank N.A.	Foreign	40	465	1163	0
34	HSBC Ltd.	Foreign	47	177	377	150
35	Standard Chartered Bank	Foreign	90	223	248	200
			54059	30466	56	Mean = 57.9 Weighted Mean = 39.7

Source: RBI (<http://www.rbi.org.in/scripts/PublicationsView.aspx?id=9868>) and individual bank's website

4. Conclusion

RBI had made the cross (third party) ATM usage free from April 1, 2009. However, IBA, representing the banks, has asked RBI to revisit this decision and add conditionality for such free usage. RBI, in the public interest, needs to take a broader view while considering the ATM issue and should have a well reasoned approach while taking such decisions limiting enhanced access to ATMs. In this connection, this paper presents arguments from the customer's point of view.

Firstly, we look at the cost of servicing a customer at bank's counter vis-à-vis at ATM. The banks are obliged to provide free service to their customers for withdrawing cash, making balance enquiries, etc., over the counter and through their own ATMs. However, the cost of providing such services over branch counters (which involves issuing cheque books, processing the cheques and providing service over counters; and this includes the expenditure involved in printing of cheque books) works out to be three times more expensive than that through ATM (their own or other bank's). Thus, effectively with such savings in cost (by use of ATMs), the banks should ideally pass on this gain to their customers. Since the banks earn and save more through more and more cross ATM usage, RBI with a well reasoned decision made such cross ATM usage free. Contrarily, IBA feels otherwise and considers it good to impose a fee for cross ATM usage.

Secondly, limiting the third party usage will be not only a move for inefficiency in payment system but also against the RBI vision on Payment System. Encouraging more and more usage of ATM, by making it free, will help in reduction in cost of servicing customers at bank counters leading to significant savings for bank. In the initial years, most of the bigger foreign and private banks realized the cost benefit of technology and installed more and more ATMs. And now with cross ATM usage made free, these very banks are able to attract more customers at their ATMs leading to generation of extra revenue through enhanced use of their ATM. Thus installing ATM units is an income generating, cost reducing and productivity enhancing activity. However, if a bank gets a fee from their customers in using other banks ATMs, it will have no incentive to setup new ATM for its own customers.

Thirdly, the IBA study indicates that post-April 2009, the intended purpose to serve the common man was achieved through making cross ATM usage free. However, there was a small minority of users who withdrew very large sums (on account of high card limits given by some banks to privileged customers), which could create logistics problems for banks at the cost of the common user. These problems need to be looked at more closely. IBA's solution in form of limiting the number of free third party withdrawals to 5 a month is not reasoned enough and it would lead to limiting freedom to draw any amount (within Rs. 10,000) more than 5 times in a month. If need be, for free cross ATM withdrawals, one can possibly think of limiting the total amount to, say, Rs. 1.5 lakh a month. Furthermore, if there are severe logistic issues involved just because a small minority of users tends to withdraw very large sums on account of high card limits, RBI

may think of discouraging such users by additionally limiting free cross ATM withdrawals to a total of Rs. 20,000 per day, say. Such a move would achieve eliminating the difficulties encountered by the banks and alongside also achieve the intended purpose to serve the common man.

Fourthly, Debit cards are also an important component in the retail payment system. Unlike ATM, where generally money flows out of the bank account of the card holder, in case of debit card usage at merchant establishments, the money flows into the bank account of the merchant using an electronic data capture (EDC) machine installed at the merchant location. In other words, EDC machines acts as a personalized ATM units for merchants. In fact, pin-based debit cards used over an EDC machine behaves in the same manner as an ATM machine where you transfer funds from one of your accounts to another. Thus, the same argument applies to all pin-based debit card transactions over EDC machines whether the merchant is selling merchandise or dispensing cash. Merchants should really not be charged any fees by the banks for such transactions, except for the one-time cost of the EDC machine and possibly 0.2% of the transaction amount with a cap of Rs. 10, say. In this connection, under a research project at IIT Bombay, a merchant survey was launched on August 15, 2009. To know more about the Merchant Survey 2009 and the questionnaire one may see the link http://www.math.iitb.ac.in/events/help_merchantsurvey2009.html

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