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Electronic Remittance System in India– Rationalization

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Abstract

Migrating from paper-based payments to electronic payments would improve the overall efficiency of the payment system, and provide meaningful cost savings and efficiency to the entire economy. With a view to expedite migration of payment transactions to electronic mode, this study looks into some prudent measures that are expected to facilitate overall transition from cheque or cash based payments to electronic payments. We highlight that there is a scope for rationalization of overall costs/pricing in the payment system keeping broader objectives of acceptance and financial inclusion in mind. We have the classic example of ATM pricing in India which revolutionized its use. With pricing being based more on well laid out fundamental principles, RBI should carry out a focused review of the bottlenecks in the country's electronic payment system and advocate appropriate directions. Some recommendations are put forth keeping few bottlenecks in forefront.

I. Introduction

1. An efficient payment system acts as a lubricant to the economy. A shift from paper-based payments to electronic payments is essential in order to facilitate quick and secure fund transfer and improve efficiency of our economy. Cheque payment is one such paper-based mode of fund transfer that is inefficient and expensive and should be phased out sooner rather than later. By driving the displacement of cheques through more intensive use of electronic payments, resources involved in manual processing can be redeployed and payment cost can be considerably reduced. Electronic payment, which is a more expedient and efficient means of payment, provide the opportunity to improve productivity levels and lower the cost of doing business.

2. Moreover, electronic payments, being cost efficient, can also enhance financial inclusion by extending financial services to the unbanked communities that were hitherto out of reach due to high operational costs. In so doing, such communities would be brought into the formal financial system and into the economic mainstream. This would enable them to enjoy lower cost of financial services and better means of savings.

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3. The Reserve Bank of India (RBI) has a plan to increase the efficiency of the nation's payment systems by accelerating the country's migration to electronic payments. It has laid a roadmap for migration to electronic payments with a thrust on safety, efficiency and public interests. However, it is felt that the public acceptance for e-payment can be achieved through education on the availability of safe, convenient and cost-effective mode of e-payment. While the transition to electronic payments will be gradual and may span over several months, efforts should be intensified to encourage the public to use electronic payment modes.

4. RBI aims to promote an environment that is conducive for greater use of electronic payments by bringing together relevant stakeholders to address the barriers that have impeded the increased adoption of electronic payments. RBI through its recent notifications dated November 03, 2010 and January 19, 2011 brought in some policy changes in India's National Electronic Funds Transfer (NEFT), Real Time Gross Settlement (RTGS) payment systems and Cheque Collections. NEFT/RTGS systems allow transfer of money from ones bank account, in say Bank A, to any person's bank account, in say Bank B. Unlike cheques, these electronic modes of money transfer are more efficient and cost effective for the country and the users of the system.

5. India's migrant population is on the rise. This increases the need for putting in place an easily acceptable means of money transfer. RBI has envisaged providing avenues for a proper remittance system for the country which is formal, efficient, easy-to-use and addresses the needs of varied customer group, including the large number of migrant remitters.

II. Growth in NEFT and its Pricing

6. RTGS system, as the name suggests, is real time and is primarily envisaged for processing and settling large value payment orders. For this reason, even before the recent policy change, RBI allowed RTGS transfers only for amounts above ₹ 1 lakh[2]. Over the last few years, RBI has made its NEFT system more robust with near real-time settlement finality through its 11 settlement cycles in a day.

7. There are more than 77287 (76089) bank branches participating in NEFT (RTGS). The RBI data on average amount per transaction suggests that NEFT is primarily being used for small value transactions although systems are in place for its use for large value transaction. With NEFT's current 11 batch-settlement cycles in a day, the effective time taken to see an NEFT or RTGS materializing (beneficiary getting the credit) remains very close. For NEFT, the beneficiary can expect to get credit for the first nine batches on week days (i.e., transactions from 9 am to 5 pm) and the first four batches on Saturdays (i.e., transactions from 9 am to 12 noon) on the same day. For transactions settled in the last two batches on

[2] 1 lakh = 0.1 million

week days (i.e., transactions settled in the 6 and 7 pm batches) and the last batch on Saturdays (i.e., transactions handled in the 1 pm batch) beneficiaries can expect to get credit on the next working day morning. The net settlement of the NEFT batch run is routed through the RTGS system. On week days, the RTGS closes at 4.30 pm for customers and at 6 pm for interbank transactions.

8. The Indian RTGS and NEFT systems have displayed significant growth in both transaction volumes and values. A glimpse of the 6-monthly data, as below, highlights the same.

Retail Electronic Payment Systems										
6 Month Periods	NEFT / EFT					RTGS System (Customer Remittance)				
	Number (Lakh)	% increase in Number	Amount (₹ crore)	% increase in Amount	Avg. amount per trans. (₹)	Number (Lakh)	% increase in Number	Amount (₹ crore)	% increase in Amount	Avg. amount per trans. (₹)
Apr07-Sep07	48.7		57911		118865	15.1		6801452		44923724
Oct07-Mar08	84.4	73	82415	42	97626	26.3	74	9298721	37	35329487
Apr08-Sep08	125.7	49	106983	30	85123	39.0	48	9702231	4	24903058
Oct08-Mar09	195.9	56	144974	36	73993	73.4	88	10301876	6	14039079
Apr09-Sep09	276.1	41	182960	26	66271	118.6	62	13754954	34	11600703
Oct09-Mar10	387.3	40	226548	24	58493	185.8	57	15761824	15	8481851
Apr10-Sep10	527.5	36	355507	57	67395	225.1	21	16446909	4	7305841
Oct10-Mar11	795.9	51	433261	22	54437	232.2	3	19739384	20	8501027

(Number in lakh and Amount in ₹ crore[3])

9. Effective November 15, 2010, RBI increased the threshold floor value for RTGS transactions from ₹ 1 lakh to ₹ 2 lakhs. Earlier, for the transactions in the range of ₹ 1-2 lakhs, it made more sense for the banks and remitters to prefer RTGS over NEFT because it was faster with no additional cost (it used to uniformly cost ₹ 25 for remittance of above ₹ 1 lakh to ₹ 5 lakhs). A snapshot of the RTGS and NEFT charges pre- and post- November 2010 is given below.

RTGS (Charges ₹)	Pre-Nov10	Post-Nov10
₹ 1 lakh to ₹ 2 lakhs	25	-
above ₹ 2 lakhs to ₹ 5 lakhs	25	25
above ₹ 5 lakhs	50	50
NEFT (Charges ₹)	Pre-Nov10	Post-Nov10
up to ₹ 1 lakh	5	5
above ₹ 1 lakh to ₹ 2 lakhs	25	15
above ₹ 2 lakhs	25	25

10. For the users of the system to move their transactions from RTGS to NEFT, a new value band in the ₹ 1 lakh to ₹ 2 lakh segment has been created for NEFT, with customers having to pay ₹ 15 per transaction. This effectively provides a saving of ₹ 10 per transaction to the customer. Thus, the special niche value band created in NEFT is a value proposition for customers providing funds transfer in a timely manner with wider geographical coverage at a lesser cost.

[3] 1 crore = 10 million

11. Another point to note is that for the individual users, NEFT is cheaper than RTGS for the above ₹ 5 lakhs band. Thus, given the current NEFT efficiency levels the system prompts and induces use of NEFT more in this high band. However, since for the banks the cost to initiate a very high value NEFT or RTGS is same, it is not very clear whether there is a tendency on the part of the banks to route a high value transfer request through the RTGS system even if the remitter applies for a NEFT. If there is no such tendency, the question remains why not? The only possible benefit for banks to prefer NEFT's net settlement in batches, even for a high value remittance, is the advantage of the netting effect. Will it be more meaningful to direct all transfers to RTGS if the transfer amount is more than ₹ 10 lakhs just like one directs transfers upto ₹ 2 lakhs to NEFT? Keeping the full objectives of the payment system, RBI may **consider taking necessary steps for encouraging RTGS over NEFT for high value transactions, say beyond ₹ 10 lakhs**. Irrespective of this move, RBI may relook into extending the operation window for RTGS. Looking ahead, National Payment Corporation of India (NPCI) has plans to develop the one-to-one funds transfer system, 24 × 7 MoneyLine, which when operational, would replace NEFT.

12. All banks (or at least banks with more than 2 lakh NEFT transactions per annum) need to put in place a common standard, enabling *straight through processing* (STP) for all its NEFT / RTGS transactions. Such a processing removes avenues for human delays in parking funds at beneficiary account after every batch run and ensures timely onward transition from remitter bank.

13. Finally, with more than 1300 lakh transactions through NEFT and more than 450 lakh transactions through RTGS (customer remittance) during 2010-11, the banking sector, based on prevailing NEFT/RTGS charges, generated revenue of the order of ₹ 270 crore (13 × 10 + 4.5 × 30 = 265) from bank customers. Moreover, with the number of transactions (from among the 1750 lakh customer transactions) attributed to 1-2 lakh band being of the order of 300 lakh, this (until revision) generated a revenue of Rs 75 crore alone. On the other hand for handling 14000 lakh cheques, during 2010-11, that passes through the clearing houses, the banking sector would spent about ₹ 280 crore just to pay off the clearing house charges (₹ 2 per cheque). Considering the elaborate and tedious processes involving printing/distribution of MICR cheque books and handing of cheques at payee/drawee banks, the banking sector engages lots of its resources leading to considerable additional expenses for the cheque based remittance system of the country.

III. Rationalization in NEFT Pricing

14. The flip side of pricing ₹ 15 per NEFT transaction is in its potential of inducing forced inefficiency in the system. Users of the ₹ 1-2 lakhs NEFT band are being prompted to do two NEFT transactions (each of amounts within ₹ 1 lakh) for ₹ 5 per transaction, rather than one

transaction of an amount in the band ₹ 1-2 lakhs. This desirably calls for financial education on how to manage ones remittances in a most cost effective way. However this leads to forced inefficiency and cost to the payment system in terms of twice the paper work to handle NEFT requests, twice the data inputs/outputs and twice the use of the NEFT network.

15. The two main types of vertical equity are proportional and progressive taxation. In proportional taxation, the amount of taxes paid increases directly with income. For example, a 5% increase in earnings will cause a 5% increase in taxes. Progressive taxation includes tax brackets, where people pay taxes based on the tax bracket into which their income places them. Each tax bracket will have a different tax rate, with higher income brackets paying the higher percentages. The question that arises then is whether progressive taxation has been the principle behind RBI's fixing of ₹ 15 fee and if so how well can this justify RBI's existing and declared principle of levy of service charge based on "reasonableness" and as per cost. Though RBI advocates banks to ensure that service charges are reasonable and are not out of line with the average cost of providing these services, it could not make the costing analysis transparent with respect to what component of service fees attributed to true cost and what attributed to profit margin. Thus, unreasonableness in fixing the service charges persists with RBI's fixing ₹ 15 for NEFT lacking rationale.

16. In case the banking sector is very particular in their claim of *ad valorem* increase in actual cost in carrying out such NEFT transactions, RBI, *at best*, should **consider pricing the NEFT value band in the ₹ 1 lakh to ₹ 2 lakhs segment at ₹ 10 per transaction**. With majority of NEFT transactions being in the sub-2 lakhs segments, such a move by RBI would remove the existing confusion and lacuna in the NEFT payment system in the sub-2 lakhs segments.

17. In order to disincentivize the use of NEFT for high value remittances, RBI may **consider keeping the charges same on NEFT and RTGS above ₹ 10 lakhs.**

IV. Remittance Facility for Migrants

18. India's migrant population is more than 100 million people and with an average of 4 persons being dependents, back home, a proper remittance system in place affects about half of India's population. A proper remittance system is one which is formal, efficient and easy to use. One would on a regular basis see long queues outside bank branches. Such a queue, with waiting time averaging 1 to 2 hours, consists of regular remitters (mostly from poor or lower middle class) in a formal system. The pain of standing in long queues is well experienced by the elite while trying to apply/service a Passport or Visa. However, if the elites are asked to stand in such queues on a monthly basis one would surely see quick reforms. Such long queues acts as a deterrent for use of the formal banking system.

19. It is well acknowledged that Know Your Customer (KYC) norms are important for the banking system. However, this acts as a deterrent for most of the migrant population to open bank accounts. With the Indian economy being predominantly cash-based, majority of the migrant population remit cash through the Core Banking Network of the bank by standing in long queues. Post-offices allow such a remittance in form of money-orders. However, it usually takes a minimum of 7 days for the money to reach the beneficiary. Moreover, it costs the remitter ₹ 250 to remit ₹ 5000. Due to such drawbacks, migrants get encouraged to use the informal channels of remittance. The use of India Post or the informal means for money transfer do not require any KYC documentation and can be used by remitter and beneficiary even if they do not have bank accounts. The money being remitted through such systems remains outside the banking system.

20. When one sees long queues outside banks it usually involves cash being remitted into some bank branch account at a different location. Here the remitter need not have a bank account and transacts in cash to remit money into the beneficiary's bank account. A simple cash deposit form is filled by the remitter providing his own details (name, address, phone number) and the account name and number of the beneficiary. This is most welcome since it at least allows cash entering the banking system. Keeping this in mind, the RBI has allowed cash transactions in a bank, for an amount less than ₹ 50000, without any KYC documentation[4].

21. Almost all banks in India facilitate NEFT. Individuals, firms or corporates maintaining accounts with a bank branch can transfer funds using NEFT. Even such individuals, firms or corporate who do not have a bank account (walk-in customers) can also deposit cash (less than ₹ 50000) at the NEFT-enabled branch with instructions to transfer funds using NEFT. A separate Transaction Code has been allotted by RBI, in the NEFT system, to facilitate walk-in customers to deposit cash and transfer funds to a beneficiary. 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. NEFT, thus, facilitates originators or remitters to initiate funds transfer transactions even without the need for having a bank account (opening of which requires KYC documents which one may not have readily).

[4] The Government of India vide its Notification No.13/2009/F.No.6/8/ 2009-ES dated November 12, 2009, has amended the Prevention of Money-laundering (Maintenance of Records of the Nature and Value of Transactions, the Procedure and Manner of Maintaining and Time for Furnishing Information and Verification and Maintenance of Records of the Identity of the Clients of the Banking Companies, Financial Institutions and Intermediaries) Rules, 2005. Rule 9, now requires banks / financial institutions to verify identity of the non-account based customer while carrying out transaction of an amount equal to or exceeding rupees fifty thousand, whether conducted as a single transaction or several transactions that appear to be connected.

V. Remittance Reforms for Migrants and Others

22. In order to clearly understand the need for any reforms, we have to address few unanswered questions. The issues that one needs to focus on are:

- For an individual / firm / corporate intending to originate cash transfer of funds (less than ₹ 50000) through NEFT in person, does the bank branch need anything more than just a filled-in 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 contact details (complete address and telephone number, etc.) of the remitter?
- Many banks appear to discourage such small amount electronic remittances through their demanding KYC documents which neither RBI nor Government of India is insisting upon. If this is true, it is important to understand why some banks would like to take such a step without their appreciating the potential of NEFT for the unbanked population to carry out small amount electronic remittances?
- It is well acknowledged that KYC documents are not being sought for an unbanked walk-in customer when a request is made for a Demand Draft of say, ₹ 1000 (against cash of ₹ 1000 + commission charges).

23. How does the bank's present policy help in providing remittance service to one who is in real need of the banking service rather than pushing the person towards informal or less efficient means of money transfer? The following points have been highlighted by RBI and Government of India in context with KYC and Anti-Money Laundering (AML) norms.

- It is important to bear in mind that the adoption of customer acceptance policy (related to the KYC norms) and its implementation should not become too restrictive and must not result in denial of banking services to general public, especially to those, who are financially or socially disadvantaged.
- ...banks should keep in mind the spirit of instructions (on KYC norms) issued by the Reserve Bank and avoid undue hardships to individuals who are, otherwise, classified as low risk customers.
- In case of transactions carried out by a non-account based customer, that is a walk-in customer, where the amount of transaction is equal to or exceeds rupees fifty thousand, whether conducted as a single transaction or several transactions that appear to be connected, the customer's identity and address should be verified. However, if a bank has reason to believe that a customer is intentionally structuring a transaction into a series of transactions below the threshold of ₹ 50000 the bank should verify identity and address of the customer and also consider filing a suspicious transaction report to Financial Intelligence Unit-India.

(The above three points make it clear that the bank should first entertain the cash NEFT and then invoke KYC if it believes misuse. Thus a bank cannot and should not start with a KYC requirement for small remittances.)

- Information accompanying all domestic wire transfers of ₹ 50000 and above must include complete originator information i.e. name, address and account number etc., unless full originator information can be made available to the beneficiary bank by other means.
- If a bank has reason to believe that a customer is intentionally structuring wire transfer to below ₹ 50000 to several beneficiaries in order to avoid reporting or monitoring, the bank must insist on complete customer identification before effecting the transfer.
- While filing Cash Transaction Report, details of individual transactions below ₹ 50000 need not be furnished.
- Customer Education: Implementation of KYC procedures requires banks to demand certain information from customers which may be of personal nature or which have hitherto never been called for. This can sometimes lead to a lot of questioning by the customer as to the motive and purpose of collecting such information. There is, therefore, a need for banks to prepare specific literature/ pamphlets etc. so as to educate the customer of the objectives of the KYC programme. The front desk staff needs to be specially trained to handle such situations while dealing with customers.
- Employee's Training: Banks must have an ongoing employee training programme so that the members of the staff are adequately trained in KYC procedures. Training requirements should have different focuses for frontline staff, compliance staff and staff dealing with new customers. It is crucial that all those concerned fully understand the rationale behind the KYC policies and implement them consistently.

24. All the points above give sufficient direction towards Bank's requiring not to refuse small amount remittances on the pretext of KYC. A bank requiring a copy of the photo ID is different from bank desiring a copy of photo ID. If an unbanked (or even banked) person is desiring to do a ₹ 2000 cash NEFT and is also providing his complete address, telephone number, signature/thumb impression, and does not have a photo ID, how best could the bank facilitate in absorbing this cash into the banking system? There is an acknowledgement slip provided by the bank for every across the counter NEFT request. This acknowledgement slip should suffice, in case of a return, for the person to claim. Let us relook into all the questions with respect to small amount (upto ₹ 10000) remittances carried out by the migrant population base of the country.

25. The NEFT initiator is already required to give his name, address and phone number. The only way one can associate transactions as "several transactions that appear to be connected" is if the remitter's name/address/phone number and the beneficiary details match. If it does not match, there could be no grounds for transactions appearing connected. Thus, banks should not have any serious concern- more so since the RBI and the Government of India are not insisting on any need of identity verification for small amount remittances.

26. For majority of the banks, the cost to users to deposit cash (i.e., remit cash) into a bank account, from a non-home branch location, is more than what it costs to do cash NEFT. With

RBI mandating a low ₹ 5 for even cash NEFT, it may not be sustainable for the banks to handle cash NEFT. This invariably leads to banks resorting to varied tactics to avoid accepting cash under NEFT. To harness the potential of the NEFT for cash deposits using the full resources of the banking infrastructure and also keeping the issue of currency management difficulties in the forefront, RBI in the interest of the payment system and in the interest of the banking policy should consider rationalizing the present rate of ₹ 5 for cash NEFT. RBI should **establish suitable benchmarks on charges for cash remittances through NEFT**. **One option could be to price the cash NEFT at ₹ 15 (instead of the current ₹ 5). RBI should also disseminate knowledge among the public (more specifically, unbanked migrant population) to exercise their right to enter any bank branch (preferably any less crowded bank branch) to harness the facility of cash NEFT.** This would reduce the considerable time taken to stand in long queues of non-home branches of specific banks by the remitter- the one end of the remittance system. **Unless the bank can establish potential fraud beforehand, the information filled in the application form (for cash NEFT) by the remitter should not call for any documentary evidence if the amount is within ₹ 10000.**

27. Banks (or RBI) usually do not allow NEFT between two of its own bank branches. However, if allowed, such a facility (under the present service charge structures) could have an added incentive for the remitter in terms of lower service charge. Many banks have higher charges (than NEFT charges) for within-bank between-accounts fund transfer. RBI should **consider relooking into the service charges for within-bank and between-banks electronic fund transfers and establish sensible parity**.

28. Currently National Financial Switch (NFS) of the NPCI facilitates off-us ATM withdrawals (say positive entries) with the exception being for transaction reversals. Thus, with standards for interoperable micro-ATM already in place, a proactive role by NPCI is solicited for efficient use of these micro-ATMs in bank branch counters for on-us and off-us transactions. For this to take shape NPCI needs to facilitate negative entries (i.e., facilitate deposits) in their existing NSF platform. With a clear process in mind, technologically this can be executed quickly. Once operational, this would be very helpful in improving the existing remittance system where one invariably sees long queues of migrant population trying to deposit cash. With no involvement of paperwork, it would also enhance efficiency through increased speed for deposit transactions. The use of micro-ATM for on-us deposit transactions would be restricted to the bank's core banking network.

29. Cash receiving outlets should be popularized and automation should be ensured to the extent possible. In particular, **each bank branch should have standardized micro-ATM terminals at the manned counters along with cash counting machines**. This would increase the efficiency of depositing (and withdrawing) funds to (from) any bank account by

use of the full banking system. Let Bank A issue a debit card to person X. The processes that one needs to put in place are,

a) Debit card of person X should be usable in Bank B micro-ATM to deposit cash (by a person authorized by X) in the account of X.
b) Debit card of person X should be usable in Bank B ATM and micro-ATM to remit funds to an account of person Y in Bank C.
c) Debit card of person X should be usable in Bank B micro-ATM to withdraw cash.
d) The cost of providing such service is to be correctly identified and paid by Bank A to Bank B.

VI. Effect of Cheque Policy Measures on Transition to Electronic Modes

30. With a view to hasten migration of payment transactions to electronic modes (especially for high-value payments), RBI took some prudent measures that was expected to facilitate overall transition from cheque based payments to electronic payments. In November 2009, RBI completely withdrew the high-value clearing service[5] keeping in mind the risk mitigation measures and migration of such high-value transactions to more efficient electronic modes like RTGS and NEFT.

31. Even after RBI's withdrawal of high-value clearing facility for cheques, a significant quantum of high-value cheques still remains in the system. This follows from the fact that during 2008-09 the total value of cheques was ₹ 1,24,61,135 crore and out of this, the total value under high-value clearing was ₹ 45,50,667 crore. Thus, the percentage of total value of cheques cleared under high-value clearing was 36.5%. Now, when one looks at the cheque data for the one year (post high-value cheque service) period December 2009 – November 2010, the total value of cheques was ₹ 1,02,00,163 crore. This is a decrease of only 18.2%. Thus one could confidently conclude that about 50% of high-value cheques remained in the system even after RBI's withdrawal of the high-value clearing service. In other words only about 50% of high-value payments got migrated to electronic modes.

32. A more detailed analysis of the cheque clearing data (as below) suggests that there has been no significant change in the Non-MICR cheque usage since April 2007. Regarding cheques other than non-MICR cheques, 2007-08 and 2008-09 saw high-value cheques contributing to 47.7% and 43.7% respectively in value terms (though in volume terms this contribution had been only 1.8% and 1.9% respectively). For the one year period December 2009 through November 2010 (by when high-value clearing service had been withdrawn) one would like to monitor the real impact of the measures taken. It is seen that in 2008-09 there had been a 9.7% and 4.8% decrease in MICR (including high-value) cheque in value and volume terms respectively, over previous year. However, when comparing for the one year period December 2009 - November 2010 with the pre- high-value withdrawal period 2008-

[5] It is a facility that allows the cheques of over ₹ 1 lakh to be encashed in one day.

09, it is seen that there had been only 20.4% and 0.4% decrease in MICR cheque value and volume respectively. Adjusting for the annual rate at which MICR cheques and high-value cheques, in value terms, had been decreasing during 2007-09, it is easy to workout (from table on cheque clearing data) that **withdrawal of high-value clearing service has seen no significant effect on cheque volumes and that about 70% of high-value payments, in value terms, did not migrate to electronic modes.** Similar results follow when one looks at the data corresponding to period 2010-11 instead of December 2009 - November 2010.

Cheque Clearing Data								
1 Year Period	Total		Non-MICR		MICR		High Value	
	Number	Amount	Number	Amount	Number	Value	Number	Amount
Apr07-Mar08	14605.6	13396066	2376.0	1867376	12010.5	6028672	219.2	5500018
Apr08-Mar09	13973.9	12469135	2335.7	2060893	11419.7	5857575	218.5	4550667
Dec09-Nov10	13893.9	10200163	2304.0	1914367	11589.9	8285795	0.0	0
Apr10-Mar11	13862.7	10133734	2312.1	1832516	11550.6	8301218	0.0	0

(Number in lakh and Amount in ₹ crore)

33. Why should I and you not use cheques and instead do electronic transfers? For individual users (or even business establishments), other than the convenience of issuing cheques and the inherent deferment of being out of funds, the incentives of issuing cheques and the disincentives for doing an electronic transfer in terms of the attached fee on electronic modes (which does not exist in case of cheques) is very prominent. The advantage of deferment of being out of funds through use of cheques is only system's creation and more of a mindset that would fade with time provided proper measures are taken in the existing design of the payment system. For recipient of a cheque, the inconvenience of depositing it in bank, sort of balances the convenience gained by the issuer of the cheque. Thus, there has to be more convenient ways, harnessing technology like ATM, internet and mobile (not requiring branch visits), to switch money transfers from use of cheques to use of electronic modes.

34. NEFT has not been created or was aimed at generating additional revenue for the banks. It has been created as a replacement of inefficient and expensive paper based payments. The savings for the banks come as the cost for this electronic funds transfer technology is far less than the corresponding inefficient and cost intensive cheque system. Thus, every transaction which can be done through cheque, if instead is routed through NEFT, the banking system gain even when NEFT charges for the users are kept at par with cheque charges.

35. Finally, RBI should **devise more focused means to incentivize electronic transfers and disincentivize use of cheques**. RBI, through its review of service charges for cheque collections, has signalled discouragement of cheques. Effective April 1, 2011, RBI has mandated increase in Drawee Bank charges by 50 paisa for clearing and settlement of cheques (there being 1150 clearing houses). The intent of the directive is clear - banks have to pass on the clearing house fee and possibly other expenses attached to handling cheques to account holders. Thus one could say that RBI has signalled the banks to discourage excessive

use of cheques by imposing fees, to account holders, beyond certain number of free cheque leaves and free cheque deposits per month. The mandate can also be efficiently translated by charging a fee for high denomination cheques (say above ₹ 50,000). Though RBI has implicitly indicated disincentivizing cheques through pricing them high, as a means to incentivize electronic transfers (facilitating migration of cheques to electronic transfers), and to bring in a sense of balance, RBI should be explicit and **consider allowing 5 free electronic transfers (including deposits and withdrawals) per month for each of the interoperable systems like NEFT, Direct Debit, Interbank Mobile Payment Service (IMPS) and debit card enabled payment transactions at net-banking sites, ATM and Micro-ATM for the low interest bearing basic account**- the savings bank account. **In conjunction with the benefits derived by the users of the payment system through its 5 free payment transactions, RBI should revise the NEFT charges to (i) ₹ 15 for remittances upto ₹ 2 lakhs and (ii) ₹ 25 for remittances above ₹ 2 lakhs.**

VII. Conclusion and Recommendations

36. RBI's pricing structure on electronic and modern payment systems should be based on well laid principles. This note highlights that there is a scope for rationalization of overall costs/pricing in the payment system keeping broader objectives of acceptance and financial inclusion in mind. We have the classic example of ATM pricing in India which revolutionized its use. The same is expected from US Federal Reserve's pricing structure on debit card use at merchant establishments. Thus, with pricing being based more on well laid out fundamental principles rather than on arbitrary policy, RBI should consider revising its current pricing structure.

37. Recommendations:

- RBI may consider taking necessary steps for encouraging RTGS over NEFT for high value transactions, say beyond ₹ 10 lakhs. Irrespective of this move, RBI may relook into extending the operation window for RTGS.

- RBI should consider pricing the NEFT value band in the ₹ 1 lakh to ₹ 2 lakhs segment at ₹ 10 per transaction.

- RBI may consider keeping the charges same on NEFT and RTGS above ₹ 10 lakhs.

- RBI should establish suitable benchmarks on charges for cash remittances through NEFT. One option could be to price the cash NEFT at ₹ 15 (instead of the current ₹ 5).

- RBI should disseminate knowledge among the public (more specifically, unbanked migrant population) to exercise their right to enter any bank branch (preferably any less crowded bank branch) to harness the facility of cash NEFT.

- Unless the bank can establish potential fraud beforehand, the information filled in the application form (for cash NEFT) by the remitter should not call for any documentary evidence if the amount is within ₹ 10000.

- RBI should consider relooking into the service charges for within bank and between banks electronic fund transfers and establish sensible parity.

- Each bank branch should have standardized micro-ATM terminals at the manned counters along with cash counting machines.

- RBI should devise more focused means to incentivize electronic transfers and disincentivize use of cheques.

- RBI should consider allowing 5 free electronic transfers (including deposits and withdrawals) per month for each of the interoperable systems like NEFT, Direct Debit, IMPS and debit card enabled payment transactions at net-banking sites, ATM and Micro-ATM for the low interest bearing basic account.

- In conjunction with the benefits derived by the users of the payment system through its 5 free payment transactions, RBI should revise the NEFT charges to (i) ₹ 15 for remittances upto ₹ 2 lakhs and (ii) ₹ 25 for remittances above ₹ 2 lakhs.

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