PAYMENTS BANKS:  
THE CONCEPTUAL FRAMEWORK

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INTRODUCTION

The payments bank is registered as a public limited company under the Companies Act, 2013, and licensed under Section 22 of the Banking Regulation Act, 1949, with specific licensing conditions restricting its activities mainly to acceptance of demand deposits and provision of payments and remittance services. It is governed by the provisions of the Banking Regulation Act, 1949; Reserve Bank of India Act, 1934; Foreign Exchange Management Act, 1999; Payment and Settlement Systems Act, 2007; Deposit Insurance and Credit Guarantee Corporation Act, 1961; other relevant Statutes and Directives, Prudential Regulations and other Guidelines/Instructions issued by RBI and other regulators from time to time. The payments bank is given scheduled bank status once it commences operations, and is found suitable as per Section 42 (6) (a) of the Reserve Bank of India Act, 1934.

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ELIGIBLE PROMOTERS

The existing non-bank Pre-paid Payment Instrument (PPI) issuers authorised under the Payment and Settlement Systems Act, 2007 (PSS Act); and other entities such as individuals / professionals; Non-Banking Finance Companies (NBFCs), corporate BCs, mobile telephone companies, super-market chains, companies, real sector cooperatives; that are owned and controlled by residents; and public sector entities may apply to set up payments banks.

Existing PPI licence holders could opt for conversion into payments banks. It is not mandatory for an existing PPI issuer to apply for a payments bank licence and it may continue as a PPI issuer as per the guidelines issued by RBI from time to time.

A promoter / promoter group can have a Joint Venture with an existing scheduled commercial bank to set up a payments bank. However, scheduled commercial bank can take equity stake in a payments bank to the extent permitted under Section 19 (2) of the Banking Regulation Act, 1949.

If a Government entity desires to set up a payments bank, it should first obtain necessary approvals from the Government and submit its application.

If the promoter succeeds in obtaining a payments bank licence from the RBI after due process, it would be required to set up the payments bank under a separate corporate structure unless it is an existing PPI licence holder opting for conversion into a payments bank.

The entities and their Promoters / Promoter Groups as defined in the SEBI (Issue of Capital & Disclosure Requirements) Regulations, 2009 should be ‘fit and proper’ in order to be eligible to promote payments banks. RBI would assess the ‘fit and proper’ status of the applicants and group entities on the basis of their past record of sound credentials and integrity; financial soundness and...
successful track record of at least 5 years professional experience or in running their businesses.

**SCOPE OF ACTIVITIES**

The payments bank will be set up as a differentiated bank and shall confine its activities to further the objectives for which it is set up. Therefore, the payments bank would be permitted to set up its own outlets such as branches, Automated Teller Machines (ATMs), Business Correspondents (BCs), etc. to undertake only certain restricted activities permitted to banks under the Banking Regulation Act, 1949, as given below:

i. Acceptance of demand deposits, i.e., current deposits, and savings bank deposits from individuals, small businesses and other entities, as permitted. No NRI deposits should be accepted. The eligible deposits mobilised by the payments bank would be covered under the deposit insurance scheme of the Deposit Insurance and Credit Guarantee Corporation of India (DICGC). Given that their primary role is to provide payments and remittance services and demand deposit products to small businesses and low-income households, payments bank will initially be restricted to holding a maximum balance of Rs. 100,000 per individual customer. After the performance of the payments bank is gauged, RBI may consider raising the maximum balance limit. However, payments bank can accept a large pool of money to be remitted to a number of accounts provided at the end of the day the balance does not exceed Rs. 100,000. If the transactions in the accounts conform to the “small accounts”1 transactions, simplified KYC/AML/CFT norms will be applicable to such accounts as defined under the Rules framed under the Prevention of Money-laundering Act, 2002. The payments bank will have to undertake its own KYC/AML/CFT exercise as any other bank.

ii. Issuance of ATM / Debit Cards. Payments banks, however, cannot issue credit cards.

iii. Payments and remittance services through various channels including branches, Automated Teller Machines (ATMs), Business Correspondents (BCs) and mobile banking. The payments/ remittance services would include acceptance of funds at one end through various channels including branches and BCs and payments of cash at the other end, through branches, BCs, and ATMs. Cash-out can also be permitted at Point-of-Sale terminal locations as per extant instructions issued under the PSS Act. Payments banks can be part of any card payment network (other than credit cards) that is authorised under the PSS Act. In the case of walk-in customers, the bank should follow the extant KYC guidelines issued by the RBI.

iv. Issuance of PPIs as per instructions issued from time to time under the PSS Act. However, the outstanding balances in PPIs will be deployed as per the pattern of deployment of funds indicated at paragraph 5 below.

v. Internet banking - The RBI is also open to payments bank offering Internet banking services. The payments bank is expected to leverage technology to offer low cost banking solutions. Such a bank should ensure that it has all enabling systems in place including business partners, third party service providers and risk management systems and controls to enable offering transactional services on the
internet. It may be clarified that RBI does not envisage payments banks to be “virtual” banks or branchless banks. Therefore, while offering internet banking services, the payments bank will be required to comply with RBI instructions on internet banking; and information security, electronic banking, technology risk management and cyber frauds.

vi. Functioning as Business Correspondent (BC) of another bank – A payments bank may choose to become a BC of another bank, subject to the RBI guidelines on BCs.

vii. As a channel, the payments bank can accept remittances to be sent to or receive remittances from multiple banks under a payment mechanism approved by RBI, such as RTGS / NEFT / IMPS.

viii. Payments banks will be permitted to handle cross border remittance transactions in the nature of personal payments / remittances on the current account. All facilities / approvals incidental to undertaking such transactions in foreign exchange will be enabled by RBI on an application made to it.

ix. Payments banks can undertake other non-risk sharing simple financial services activities, not requiring any commitment of their own funds, such as distribution of mutual fund units, insurance products, pension products, etc. with the prior approval of the RBI and after complying with the requirements of the sectoral regulator for such products.

x. The payments bank may undertake utility bill payments etc. on behalf of its customers and general public.

The payments bank cannot set up subsidiaries to undertake non-banking financial services activities. The other financial and non-financial services activities of the promoters, if any, should be kept distinctly ring-fenced and not comingled with the banking and financial services business of the payments bank.

The payments bank will be required to use the words “Payments Bank” in its name in order to differentiate it from other banks.

**DEPLOYMENT OF FUNDS**

The payments bank cannot undertake lending activities. Apart from amounts maintained as Cash Reserve Ratio (CRR) with RBI on its outside demand and time liabilities, it will be required to invest minimum 75 per cent of its “demand deposit balances” in Government securities/ Treasury Bills with maturity up to one year that are recognized by RBI as eligible securities for maintenance of Statutory Liquidity Ratio (SLR) and hold maximum 25 per cent in current and time / fixed deposits with other scheduled commercial banks for operational purposes and liquidity management. The “balances outstanding under the PPIs issued” by the payments bank should be flexibly invested / deployed between SLR eligible Government securities/Treasury Bills and bank deposits (both demand and time) in such a manner that it is able to comply with the requirements of CRR and SLR on its “overall outside demand and time liabilities” including its deposit balances and outstanding balances in PPIs issued.

The payments bank will participate in the payment and settlement system and will have access to the inter-bank uncollateralised call money market and the collateralized repo and CBLO market for purposes of temporary liquidity management.
**CAPITAL REQUIREMENT**

The payments bank will not have significant credit and market risks. However, it will be exposed to operational risk. The payments bank will also be required to invest in technological infrastructure for its operations. Capital will be needed to buffer against operational risk and also utilised for creation of such fixed assets. Therefore, the minimum paid-up equity capital of the payments bank shall be Rs. 100 crore.

The payments bank shall be required to maintain a minimum capital adequacy ratio of 15 per cent of its risk weighted assets (RWA) on a continuous basis, subject to any higher percentage as may be prescribed by RBI from time to time. Tier I capital should be at least 7.5 per cent of RWAs. Tier II capital should be limited to a maximum of 100 per cent of total Tier I capital. However, as payments banks are not expected to deal with sophisticated products, the capital adequacy ratio will be computed under Basel Committee’s standardised approaches.

As the payments bank will not have significant risk weighted assets, its compliance with a minimum capital adequacy ratio of 15 per cent would not reflect the true risk. Therefore, as a backstop measure, the payments bank should have a leverage ratio of not less than 3 per cent, i.e., its outside liabilities should not exceed 33.33 times its net worth (paid-up capital and reserves).

**PROMOTERS’ CONTRIBUTION**

Since a payments bank cannot undertake lending activities, it is not mandatory for it to have a diversified ownership structure. Therefore, no maximum shareholding limit for promoters is prescribed. However, the promoters of the payments bank should hold at least 40 per cent of its paid-up equity capital for the first five years from the commencement of its business. If the payments bank is set up as a joint venture with equity partnership with a scheduled commercial bank, the scheduled commercial banks can take equity stake in a payments bank to the extent permitted under Section 19 (2) of the Banking Regulation Act, 1949. When the payments bank reaches the net worth of Rs.500 crore, and therefore becomes systemically important, diversified ownership and listing will be mandatory within three years of reaching that net worth. However, payments banks having net worth of below Rs.500 crore could also get their shares listed voluntarily, subject to fulfillment of the requirements of the capital markets regulator.

**FOREIGN SHAREHOLDING**

The foreign shareholding in the payments bank would be as per the Foreign Direct Investment (FDI) policy for private sector banks as amended from time to time. As per the current FDI policy, the aggregate foreign investment in a private sector bank from all sources will be allowed up to a maximum of 74 per cent of the paid-up capital of the bank (automatic up to 49 per cent and approval route beyond 49 per cent to 74 per cent). At all times, at least 26 per cent of the paid-up capital will have to be held by residents. In the case of Foreign Institutional Investors (FIIs) / Foreign Portfolio Investors (FPIs), individual FII / FPI holding is restricted to below 10 per cent of the total paid-up capital, aggregate limit for all FIIs /FPIs / Qualified Foreign Investors (QFIs) cannot exceed 24 per cent of the total paid-up capital, which can be raised to 49 per cent of the total paid-up capital by the bank concerned through a resolution by its Board of Directors followed by a special resolution to that effect by its General
Body. In the case of NRIs, the individual holding is restricted to 5 per cent of the total paid-up capital both on repatriation and non-repatriation basis and aggregate limit cannot exceed 10 per cent of the total paid-up capital both on repatriation and non-repatriation basis. However, Non-Resident Indian (NRI) holding can be allowed up to 24 per cent of the total paid-up capital both on repatriation and non-repatriation basis provided the banking company passes a special resolution to that effect in the General Body.

VOTING RIGHTS AND TRANSFER/ACQUISITION OF SHARES

As per Section 12 (2) of the Banking Regulation Act, 1949, any shareholder’s voting rights in private sector banks are capped at 10 per cent. This limit can be raised to 26 per cent in a phased manner by the RBI. Further, as per Section 12B of the Act ibid, any acquisition of 5 per cent or more of paid-up share capital in a private sector bank will require prior approval of RBI. This will also apply to the payments banks.

PRUDENTIAL NORMS

As the payments bank will not have loans and advances in its portfolio, the prudential norms and regulations of RBI as applicable to loans and advances, will therefore, not apply to it. However, the payments bank will be exposed to operational risk and should establish a robust operational risk management system. Further, it may face liquidity risk, and therefore is required to follow RBI’s guidelines on liquidity risk management, to the extent applicable.

BUSINESS PLAN

The applicants for the payments banks licence will be required to furnish their business plans and project reports with their applications. The business plan will have to address how the bank proposes to achieve the objectives of setting up of payments banks. The business plan, inter alia, should cover aspects relating to business model proposed to be used; bank’s access points in rural and semi-urban areas; control over its BCs and customer grievance redressal; joint venture partnership with a scheduled commercial bank, if any; etc. The business plan submitted by the applicant should be realistic and viable. Preference will be given to those applicants who propose to set up payments banks with access points primarily in the under-banked States / districts in the North-East, East and Central regions of the country. However, to be effective, the payments banks should ensure widespread network of access points particularly to remote areas, either through their own branch network, ATMs or BCs or through networks provided by others. The payments bank is expected to adapt technological solutions to lower costs and extend its network.

In case of deviation from the stated business plan after issue of licence, RBI may consider restricting the payment bank’s expansion, effecting change in management and imposing other penal measures as may be necessary.

CORPORATE GOVERNANCE

i. The Board of the payments banks should have a majority of independent Directors.

ii. The bank should comply with the corporate governance guidelines including ‘fit and proper’ criteria for Directors as issued by RBI from time to time.
OTHER CONDITIONS

i. The payments bank shall operate in remote areas mostly through BCs, ATMs and other networks. Therefore, the requirement of opening at least 25 per cent of branches in unbanked rural centres (population up to 9,999 as per the latest census), is not stipulated for them. However, the payments bank will be required to have at least 25 per cent of physical access points including BCs in rural centres. Further, a controlling office for a cluster of access points should also be established for control over various outlets and customer grievance redressal.

ii. The operations of the bank should be fully networked and technology driven from the beginning, conforming to generally accepted standards and norms; while new approaches (such as for data storage, security and real time data updation) are encouraged, a detailed technology plan for the same should be furnished to RBI.

iii. The bank should have a high powered Customer Grievances Cell to handle customer complaints. The payments banks will come under the purview of RBI’s Banking Ombudsman Scheme, 2006.

iv. The compliance of terms and conditions laid down by RBI is an essential condition of grant of licence. Any non-compliance will attract penal measures including cancellation of licence of the bank.

RBI will adopt a cautious approach in licensing payments banks in the initial years, and with experience gained, may suitably revise the approach.
The Line up of Players Eyeing the Payments Bank Arena

The Reserve Bank of India received 72 applications for small finance banks and 41 applications for payments banks. Notable applicants for payments banks include: AB Nuvo Ltd, Airtel M Commerce, Cholamandalam, FinoPayTech, India Post, ItzCash, NSE Strategic Investment Corp, Reliance Industries, Sun Pharma, Kalpataru, Future Group, NSDL, Tech Mahindra, Videocon d2h, Vodafone m-pesa, Aditya Birla Group, Bharti Enterprises Ltd. the State Bank of India (SBI), the country’s largest private sector conglomerate Reliance Industries Ltd (RIL) has applied for it. Others in the fray include a Bharti group company (with Kotak Mahindra Bank Ltd), Aditya Birla Nuvo Ltd, Vodafone Group Plc’s Indian arm, Tech Mahindra Ltd, Department of Posts, and individuals such as Kishore Biyani of the Future Group, Dilip Shanghvi of Sun Pharmaceuticals Industries Ltd and M.G. George Muthoot of the Muthoot group among others.

Advantage Mobile Telephone Companies (MTC)

One can dissect this model into its constituent parts of infrastructure, banking backend and service delivery. Of the players permitted to run a Payments Bank, it is the MTCs, which have the infrastructure and the service delivery components in place. Some of the MTCs a real ready offering a partial banking service through their PPI services which can give the man early bird advantage. The missing piece is the ‘banking backend’. While MTCs are reasonably equipped from a people, processes and technology triangle perspective, they need to close certain gaps. The point is that the MTCs are already a head in the race. A mapping of a few key Payments Bank success factors (KSF) to the inherent strengths of a mobile telephone company will make this point clear:

KSF1: Customerbase
KSF2: Widenational network
KSF3: Strong salesforce on the ground
KSF4: Solid technology infrastructure
KSF5: High growth industry (subscribersto growto 1160,000,000 by 2017 - Source TRAI)

The following figure shows operator-wise rural subscribers. (Source: COAI Report).
State Bank of India, a behemoth in the Indian banking industry, has over 170 million customers. The rural subscribers for Airtel and Vodafone add up to 188 million. The combined rural subscribers sum up to more than 300 million. Assuming about 25% open accounts with Payments Banks, the opportunity number is 75 million, a staggering figure. One can compute business and value per account through extrapolation. The business case for the MTCs is strengthened by growth in mobile wallet adoption, improving customer loyalty and independence from banking intermediaries. This also presents a significant alternative revenue source for the industry which is currently struggling with per capita profitability. Credit Suisse suggested that restrictive mobile payments could yield 1-1.2% additional revenue for telecom operators, while for liberal mobile payments this number could be 7-8%.

Banks tried to do this, but building branches and ATMs has not been efficient. That’s because there’s a fundamental difference in the way banks work, and PPIs [Pre-Paid Instruments, such as virtual wallets]. They’ve [banks have] got existing processes and investments, so they can’t change completely and reach out now.

A mobile based system can become ubiquitous. Unlike virtual wallets, Payment Banks will be interoperable - if one has money saved with one bank, one can transfer it to another.

The barriers to setting up an account are also very simple - all one needs is an Aadhaar card, which is linked to one’s account with the Payments Bank, the government can use the card as a means of easily disbursing benefits, grants and subsidies.

The Payments Bank Business Model for Mobile Telephone Companies

A Mobile Telephone Company looking to transform into a Payments Bank requires a few foundational additions, the most important of which are

a. A strong backend core banking system
b. An Internet banking solution
c. A payments system
d. A digital commerce solution and
e. Access to switch (ATM etc.)

A generic solution architecture for a Payments Bank:
CONCLUSION

So, a mobile based payment is defined as a payment (transfer of funds) where the mobile phone is involved in the initiation and confirmation of the payment. The location of the payer is not important: he may or may not be 'mobile' or 'on the move' or at a Point of Sale. The mobile payment would make use of cash redundant.

One could pay a vegetable vendor/kirana shop payment, who displays a mobile Number and MMID at shop, instantaneously. In India, it has been decided to adopt the bank-led model.

National Payments Corporation of India (NPCI), a company under Companies Act, incorporated in December 2008 is facilitating the Interbank Mobile Payment Service (IMPS). IMPS is a money transfer system in which one can send money to other bank accounts instantly, the sender should use mobile banking to send money, the receiver mobile number should be registered with his bank and the money is credited to receivers account instantly.

For registration the Remitter must register for mobile banking and get Mobile Money Identifier (MMID) & Mobile Banking Pin (MPIN) for initiation of a transaction. MMID is a 7 digit number, to be issued by the bank to the customer upon registration and the Beneficiary must Register his / her mobile number with the bank account and get MMID. A remitter can initiate an IMPS transaction by sending a SMS to his bank typing the Beneficiary Mobile Number, Beneficiary MMID and Amount. The receiver will get a SMS confirmation for the credit of his account.

Banks and telcoswill will have to play a complementing role to further the benefits of benefit mobile banking to banked and unbanked. For Telcos it is more about extending its reach and capability to handle large volume low value transactions. For Bank.s it provides that extra reach to extend its catchments beyond conventional branch channel.

Hence, it becomes an effective service delivery channel for Banks to use the Telco network to serve both high and low value customer segment.

Other important role that Bank has in terms of product innovation specifically targeting low value credit. Mobile can be an effective means of credit delivery based on the consumption patterns

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INTERNET SOURCES

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2. Afì-global.org (A quick guide to Maya Declarationon Financial Inclusion)

3. www.trai.gov.in

## ANNEXURE 1

### Comparison of Commercial Bank, Telcoe-wallet and Payments Bank on a Few Key Parameters

<table>
<thead>
<tr>
<th>Parameter</th>
<th>Commercial Bank</th>
<th>Major Telcoe-wallet</th>
<th>Payments Bank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lending</td>
<td>Yes</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Accept deposits</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Cashout</td>
<td>Yes</td>
<td>Yes and No (Depends on the product)</td>
<td>Yes</td>
</tr>
<tr>
<td>Cashin</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Makepayments</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Remittances</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Monetarycontrol–CRR</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Monetarycontrol–SLR</td>
<td>Yes</td>
<td>No</td>
<td>Yes</td>
</tr>
<tr>
<td>Businessmodel</td>
<td>Use delta between lending and deposit rate for revenue</td>
<td>Uses crow account/corporate account for revenue</td>
<td>Use delta between deposits and investments in SLR backed securities as investment revenue</td>
</tr>
<tr>
<td>Businessentity</td>
<td>ScheduledBank</td>
<td>Telco</td>
<td>NBFC/Telco/PPI/etc</td>
</tr>
<tr>
<td>Regulatedby</td>
<td>RBI/BRA etc.</td>
<td>PaymentsandSettlementAct</td>
<td>RBI/BRA/etc.</td>
</tr>
<tr>
<td>Initialcapital</td>
<td>INR5,000,000,000</td>
<td>Notrequired</td>
<td>INR1,000,000,000</td>
</tr>
<tr>
<td>Defaultrisk</td>
<td>Yes</td>
<td>Yes</td>
<td>Minimal</td>
</tr>
</tbody>
</table>

### CLEARING THE AIR

**Payment Bank guidelines**

**Dos**
- Have to use the word ‘Payment Bank’ in their name.
- Can accept demand deposits: that is, current deposits and savings bank deposits, from individuals, small businesses and other entities.
- Can hold a maximum balance of Rs 1 lakh per individual customer.
- Will be allowed to set up branches, ATMs, business correspondents.
- Will be allowed to issue debit cards and offer internet banking.
- Can accept a large pool of money to be remitted, but the balance should not exceed Rs 1 lakh at the end of the day.
- Can accept remittances to be sent to, or receive remittances from, multiple banks.
- Permitted to handle cross-border remittances in the nature of personal payments on the current account.
- Allowed to distribute mutual fund, insurance and pension products.
- Can undertake utility bill payments.

**Don’ts**
- No NRI deposits should be accepted.
- Cannot issue credit card.
- Not allowed to set up arms to undertake NBFC activities.
- Other financial and non-financial services of promoters should not be mingled with the working of payment banks.