Prepaid transit instruments: Step to a 'less-cash society'

By Sawant Singh and Aditya Bhargava, Phoenix Legal

PHOENIX LEGAL

New Delhi
Second Floor,
254, Okhla Industrial Estate
Phase III
New Delhi – 110 020, India
Tel +91 11 4983 0000
Fax: +91 11 4983 0099
Email: delhi@phoenixlegal.in

Mumbai
Vaswani Mansion, 3rd Floor
120 Dinshaw Vachha Road
Churchgate
Mumbai – 400 020, India
Tel: +91 22 4340 8500
Fax: +91 22 4340 8501
Email: mumbai@phoenixlegal.in

Following up on the government's initiative to encourage Indians to move to electronic payment methods, the Reserve Bank of India (RBI) has issued guidelines on the use of "prepaid payment instruments" (PPIs). A PPI facilitates the purchase of goods and services against value stored on it.

The rationale for encouraging electronic payment methods is that the Indian economy is overwhelmingly based on cash transactions and this has been recognized to cause revenue leakage. Further, the import of paper and technologies to print new currency notes (and destroy old ones) substantially adds to the exchequer's bill.

With this in mind, the government is strongly promoting a "less-cash society", where electronic payment methods predominate. Further, the finance minister in this year's budget speech noted that cash transactions had to be discouraged to curb black money, and proposed to introduce measures that "will incentivize credit or debit card transactions, and disincentivize cash transactions".

Through a circular dated 9 July, the RBI introduced a PPI for mass transit systems (PPI-MTS), which allows mass transit system operators (such as bus operators, taxi service providers, and metro and rail operators) to issue PPIs. The circular notes the importance of PPIs by recognizing that "the migration of micro and small value cash payments can play a significant role in achieving the vision of less-cash society. One such area where a large number of small value cash payments take place relates to mass transit systems".

Features of a PPI-MTS

A PPI-MTS has to be semi-closed, which means that it can be used for purchasing goods and services (including financial services) from "a group of clearly identified merchant locations/ establishments" that have a specific contract with the PPI issuer (in this case, the mass transit operator) to accept the PPI. A semi-closed PPI does not permit withdrawal of cash against the PPI or redemption of the PPI by the PPI holder. The circular also provides that no cash-out or refunds can be obtained in respect of a PPI-MTS.

A PPI-MTS has to contain the "automated fare collection application" related to the transit service of the issuer. A PPI-MTS can also be used with merchants whose activities are allied to the issuer or are carried on within the premises of its transit system.

The instruments can be "reloadable", which means that the balance in the PPI-MTS can be topped up on a continuing basis without the need to purchase a new PPI-MTS. However, a PPI-MTS can only be issued for a value of up to ₹2,000 (US$30) and the balance on a PPI-MTS (including reloads) cannot exceed ₹2,000. Presumably, this limit will be raised once the government and the RBI can gauge the effectiveness of the PPI-MTS.

PPI-MTS issuers have been granted the discretion to determine the level of any know-your-customer requirements applicable to PPI-MTS purchasers.

The validity of a PPI-MTS must be at least six months from the date of issue. While no maximum validity period has been prescribed, this would need to be examined in light of the Companies (Acceptance of Deposits) Rules, 2014, which require companies to provide services within 365 days of receiving an advance so that it is not reckoned as a "deposit".

Clarity on issues such as maximum value and time limits would go a long way in encouraging the use of PPIs.

What's next?

While the RBI circular does not contemplate using a PPI-MTS for more than one transit service, this might be made possible by standardizing the fare collection/attribution mechanisms across various transit services, particularly ones operated by group companies or subsidiaries of the issuer. Such standardization should not affect classification of the PPI-MTS as a semi-closed payment system, and would also help increase the prevalence of the PPI-MTS.

It is reported that the government proposes to encourage the use of PPIs by providing a tax waiver. There is a good business case for doing so, as conducting transactions through electronic payment methods saves costs such as printing and security of physical currency, environmental upkeep, and tracking of cash transactions from a taxation and anti-money laundering perspective. From a policy perspective, talks have already started on whether the future role (and revenue stream) of banks will revolve around providing technology for facilitating electronic payment systems, and clearinghouse-related services.

Payment systems operators are also much in demand, particularly for foreign direct investment, as foreign investors see great value in an industry which is nascent but has great untapped potential. Such investors are motivated by success stories such as the Paytm payment gateway, which has reported crossing the 100 million-customer mark, and provides a vast variety of services such as payments for electricity and water, mobile phone recharges and cab fares.

Phoenix Legal is a full-service law firm with offices in New Delhi, Mumbai and Chennai. Sawant Singh is a partner and Aditya Bhargava is a principal associate in the Mumbai office.