RBI issues guidelines for regulating payment aggregators and payment gateways

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Summary

Until recently, the activities of payment intermediaries were governed, albeit indirectly, as per the Reserve Bank of India (RBI) Directions[1]. These directions required banks to maintain a nodal account of intermediaries with permissible credits/debits and prescribed a settlement cycle for credit to merchants.

Given the crucial role played by payment intermediaries in online transaction(s), the RBI issued[2] a Discussion Paper on Guidelines for Payment Gateways (PGs) and Payment Aggregators (PAs) with the intent to regulate the activities of PGs and PAs.

After considering the suggestions on the Discussion Paper, the RBI issued[3] Guidelines on Regulation of Payment Aggregators and Payment Gateways (Guidelines) to regulate the activities of PAs in entirety and to provide baseline technology-related recommendations to PGs. The Guidelines shall come into force from 1 April 2020 other than for activities for which specific timelines are mentioned.

The Guidelines provide a regulatory framework for PAs on the capital requirements, authorisation process, governance, merchant on-boarding, safeguards from money laundering related provisions, on-boarding of merchants, settlement, customer grievance redressal framework, reporting requirements, security and fraud prevention framework etc.

Salient features of the Guidelines

Meaning of PA's and PG's for the purpose of the Guidelines

- **PAs:** PAs are entities that facilitate e-commerce sites and merchants to accept various payment instruments from the customers for completion of their payment

1 dated 24 November 2009
2 on 17 September 2019
3 on 17 March 2020

obligations. PAs facilitate merchants to connect with acquirers. In the process, they receive payments from customers, pool and transfer them on to the merchants after a time period.

- **PGs:** PGs are entities that provide technology infrastructure to route and facilitate processing of an online payment transaction without any involvement in handling of funds.

Applicability of the Guidelines

- The Guidelines are applicable only to PAs. Further, domestic leg of import and export related payments facilitated by PAs would also be governed by the Guidelines. However, Cash on Delivery (CoD) e-commerce model are outside the purview of the Guidelines.

Authorisation

- As per the Guidelines, banks are not required to obtain separate authorisation where they provide PA services. However, non-bank[4] PAs should obtain an authorisation from RBI under Payment and Settlement Systems Act, 2007 (PSSA).
- All existing non-bank PAs are required to apply for authorization till 30 June 2021. Further, all existing e-commerce marketplaces providing PA services are required to set-up a separate entity for providing PA services and obtain authorisation from the RBI under PSSA on or before 30 June 2021.

Net worth requirement

All existing non-bank PAs and new non-bank PAs are required to fulfill following net-worth requirement. Failure to meet net-worth requirement would lead to closure of PA business

- **Existing PAs:** Existing PAs to achieve the net-worth of:
  - INR 15 crore as on the date of application or by 31 March 2021, whichever is earlier **and**
  - INR 25 crore by 31 March 2023
- **New non-bank PAs:** New non-bank PAs to achieve the net-worth of:
  - INR 15 crore on the date of application **and**
  - INR 25 crore by the end of the third financial year of grant of authorisation

[4] Should be a company incorporated under Companies Act, 1956 or 2013. The Memorandum of Association (MOA) of the applicant must cover the proposed activity of operating as a PA.

- Net-worth of INR 25 crore, in either case, to be maintained at all times, thereafter.
- Net-worth to include paid-up equity capital, compulsorily convertible preference shares (CCPS)[5], free reserves, share premium balances, capital reserves representing surplus arising out of sale proceeds of assets[6].
- FDI allowed, subject to extant consolidated Foreign Direct Investment (FDI) Policy and relevant foreign exchange management regulation on this subject.

Governance of PA

The Guidelines provides following guidance for governance of a PA:

- PAs to be professionally managed
- Promoters to satisfy 'fit and proper' criteria prescribed by the RBI
- Directors to submit a declaration to the RBI
- The RBI to examine 'fit and proper' status of Applicant and its management by obtaining inputs from other regulators, government departments, etc.
- Any takeover/acquisition of control/change in management of a non-bank PA to be communicated to the RBI within 15 days. The RBI to examine 'fit and proper' status of the management and may place suitable restrictions on such changes
- PAs to disclose info regarding merchant policies, customer grievances, privacy, and other terms and conditions on website and mobile application
- PAs to appoint a nodal officer for regulatory and customer grievance functions

Safeguards against money laundering

- Extant Know Your Customer (KYC)/Anti-Money Laundering (AML)/Combating Financing of Terrorism (CFT) related guidelines to apply to PAs
- Provisions of Prevention of Money Laundering Act, 2002 to also apply to PAs

Merchant on-boarding

The Guidelines provide following guidance for the purpose of on-boarding a merchant:

- PAs to have a board approved policy for merchant on-boarding

[5] CCPS can be either cumulative or non-cumulative and they should be compulsorily convertible into equity shares and the shareholder agreement should specifically prohibit any withdrawal of this preference capital at any time.

[6] not those created by revaluation of assets adjusted for accumulated loss balance, book value of intangible assets and deferred revenue expenditure, if any

- PAs to undertake background and antecedent check of the merchants, to ensure that such merchants do not have malafide intent of duping customers, do not sell fake/counterfeit/prohibited products, etc.
- PAs to check Payment Card Industry-Data Security Standard (PCI-DSS) and Payment Application-Data Security Standard (PA-DSS) compliance of the infrastructure of the merchants on-boarded
- Merchant not to be allowed to store/save customer card related data
- Merchant agreement to provide for security/privacy of customer data

Escrow account management

- Amount collected by non-bank PAs to be maintained in an escrow account, with only one scheduled commercial bank at any point of time
- Escrow account not to be operated for CoD transactions
- Settlement of funds with merchants not to be co-mingled with other business
- Interest not to be paid by bank on balance maintained in escrow, except when the PA enters into an agreement with bank and subject to certain conditions
- Permitted credits/debits to the escrow account:

Permitted credits	• Payment from various customers towards purchase of goods/services • Pre-funding by merchants/PAs • Transfer representing refunds for failed/disputed/returned / cancelled transactions • Payment received for onward transfer to merchants under promotional activities, incentives, cash-backs, etc.
Permitted debits	• Payment to various merchants/service providers • Payment to any other account on specific directions from merchant. • Transfer representing refunds for failed/disputed transactions • Payment of commission to intermediaries[7] • Payment of amount received under promotional activities, incentives, cash-backs, etc.

Settlement

- Amounts deducted from the customer's account (including wallet) shall be remitted to the bank maintaining escrow account within the prescribed time

[7] at pre-determined rates / frequency

- Final settlement with merchant to be completed within the prescribed time
- Credits towards reversed transactions and refund transactions to be routed through the escrow account, unless otherwise.

Customer grievances

- PAs to have, a formal and publicly disclosed, customer grievances redressal and dispute management framework.

Security, fraud prevention and risk management framework

- PAs to put in place adequate information and data security infrastructure and systems for prevention and detection of frauds
- PAs to set-up a mechanism to monitor, handle and follow-up on cyber security incidents and breaches
- PAs not to store the customer card credentials within their database or server accessed by merchant(s)

General instructions

- Extant instructions on Merchant Discount Rate (MDR) to be followed
- Information on other charges such as convenience fee, handling fee, etc., levied to be displayed upfront by PAs
- PAs not to place limits on transaction amount for any payment mode
- Refunds to be made to original payment method, unless agreed by customer

Our comments

With the constant evolution of the fin-tech and e-commerce industry in India, it was crucial to have clear guidelines in place to increase transparency and efficiency. With the introduction of this Guidelines, existing PAs will be directly regulated by the RBI.

The Discussion Paper had suggested three alternate ways to regulate the activities of PGs and PAs: (i) Continue with extant instructions; (ii) Limited regulations; and (iii) Full and Direct Regulations. Out of these three alternatives, the RBI favoured the third alternative i.e., to have full and direct regulations for regulating PAs and PGs in India.

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