

## Part II

### Strategic Approach

#### 1. New Institutional Structure for Retail Payment Systems

Today, Payment and Settlement system of the country includes retail and large value payments in the form of a variety of paper based and electronic payment instruments. As detailed in the earlier section, there are a large number of institutions operating with different ownership pattern having varied types of functions including processing, clearing, management and settlement.

Due to multiplicity of operators, local practices which vary from place to place, determine the conduct of clearing and settlement and important aspects like safety, efficiency and customer service are often compromised for operational convenience. This limits the scope of product innovation in payment services.

The institutional structure and delivery channels of payment services in other countries differ from the same in India in the sense that the ownership of the retail payment systems in other countries rests with a separate legal entity, whereas in India they are voluntary associations. A point of view which is being increasingly recognized is that the regulator should not be the service provider unless the payment system is systemically important. A survey carried out covering the retail payment systems in 14 countries revealed that the ownership of retail payment systems - both paper-based and electronic, vary from country to country. In some countries they are operated by private companies whose ownership includes participating banks and financial institutions, while in other countries it is operated by bankers' association/ payments association. It is only in very few countries that central banks operate retail payment system.

In accordance with this international trend, it is envisaged that the Indian Retail Clearing function, in its entirety, could be entrusted to a separate legal entity at national level and Reserve Bank can provide settlement services for all the clearing systems, besides being the regulator and supervisor of the payment systems.

The broad framework of the new national entity may be as under:

- This envisioned national entity would be a limited company owned and operated by banks. Indian Banks Association will discuss with a few leading banks and develop consensus on the ownership pattern. Since a few banks have already been running MICR Cheque Processing Centres (MICR CPCs) with substantial investment, they may be consulted for the purpose. .
- The details regarding staffing, ownership of existing infrastructure etc., may have to be worked out.

- All retail clearing operations, both paper-based and electronic will be managed and operated by this limited company.
- The new organization would provide a robust technologically intensive centralized system offering ECS, EFT and SEFT (or NEFT) Services covering the entire country. It may also take initiatives on ATM-switching, multi-application smart card, e-commerce and m-commerce based payment systems.
- The new entity would bring about efficiency enhancements and uniformity in the existing payment products and develop new products taking advantage of technology innovation. Existing MICR centres would be converted into cheque truncation based clearing centres. It would also introduce cheque truncation based inter-city clearing paving the way for T+1 (or even T+0) cheque clearing for the whole country.

The advantage of setting up of the national entity on these lines for running all retail payment system activities will be that this entity will have uniformity in the structure, operations and procedures. The disparate local practices which impede efficiency and customer service in the functioning of the clearing operations would be effectively neutralized. This single entity would deploy professionally skilled and competent personnel to manage and run clearing operations. It will create an enabling environment for bringing out innovative products. It will pave the way for conducting all clearing at national level, leading to better information dissemination and better customer education on various payment services and systems.

Keeping the above in view, it is proposed to initiate the following step towards a new organizational structure for retail payment systems during 2005-08:

**Action Point:**

1. Setting up of an institution at the national level which will own and operate all retail payment systems of the country.