A

Discussion Paper on

Disincentivising Issuance and Usage of Cheques

(Available for comments up to February 28, 2013)

Reserve Bank of India

Department of Payment and Settlement Systems

Central Office, Mumbai

DISINCENTIVISING CHEQUE USAGE – A DISCUSSION PAPER | **RESERVE BANK OF INDIA**

PREFACE

The Reserve Bank of India has been spear-heading reforms in the payment and settlement systems of the country, leveraging on the benefits derived from technological developments. This has facilitated the existence, today, of a bouquet of payment systems to suit the requirements of various types of customers, purposes and segments.

Over the last decade, the Bank has been sharing and signalling the expected developments in line with its objectives for developments in payment and settlement systems for the country, in the form of a Vision Document. The present scenario is such that all payment systems - paper to electronic - need to be developed simultaneously to reduce use of cash in the economy. The current Vision Document for Payment and Settlement Systems (2012-2015) envisages the move towards a ñless-cashò society and greater adoption of electronic modes of payments. This inter alia implies that the role of cheques has to reduce significantly while electronic payments grow significantly.

With the growing trend visible in electronic payments, decline in cheque usage is inevitable. This is already visible in the statistics which show reduction of cheques being cleared. The question of import is whether further developments in this regard should be left to the users themselves (market forces) or whether this declining trend should be ñmanagedò. If the decline in cheque usage is managed and actively discouraged in a structured manner, the results could not only be achieved in a shorter time-span but could also ensure that no particular section of society is marginalised due to these developments. Further, it could also pave the way for a structured migration and adoption of electronic payments by all sections of society.

Given the still high use of cheques, any strategy to discourage the use of cheques by individuals as well as institutional users has to have a multi-pronged approach encompassing cost and time considerations, incentives for use of electronic modes of transactions and disincentives for the use of paper-based instruments. In this direction, it was announced in the Second Quarter Review of Monetary Policy 2012-13 that a discussion Paper on the subject will be placed in the public domain for comments.

Accordingly, this discussion paper has been prepared in consultation with a few stakeholders. Studies conducted by and experiences of other countries in their efforts at reducing cheque usage have also been considered as they provide valuable insights in meeting our endeavor. To this end, we seek views on the matter of disincentivising cheque usage in the country. Specific and actionable feedback would be highly valued.

INTRODUCTION – STATUS OF CHEQUE USAGE IN THE COUNTRY

Developments in the banking and financial sector have been critical in facilitating economic growth, and the role of safe, secure and efficient payment and settlement systems in this regard is well-documented. The payments eco-system in the country is gradually moving from a purely cash and cheque-based scenario to one where electronic payments are slowly but surely taking the lead. With the Reserve Bank of India leading the change and also vocalising its payment system policy objectives through its Vision Document, the payments scenario is set to move towards a ôless-cashô society where everyone has access to various safe, efficient, accessible electronic payment services.

The growth in electronic payments in recent years is quite heartening registering a year-on-year growth of nearly 30% on an average since 2003 (2009-10 being an exception). In terms of volume, while the share of cheque-based payments has begun to decline, the share of electronic payments is increasing. In a scenario of increased turnover in non-cash payments, this trend is significant.

In value terms, electronic payments are certainly the dominant one in the non-cash payments turnover in the country (Chart-1).

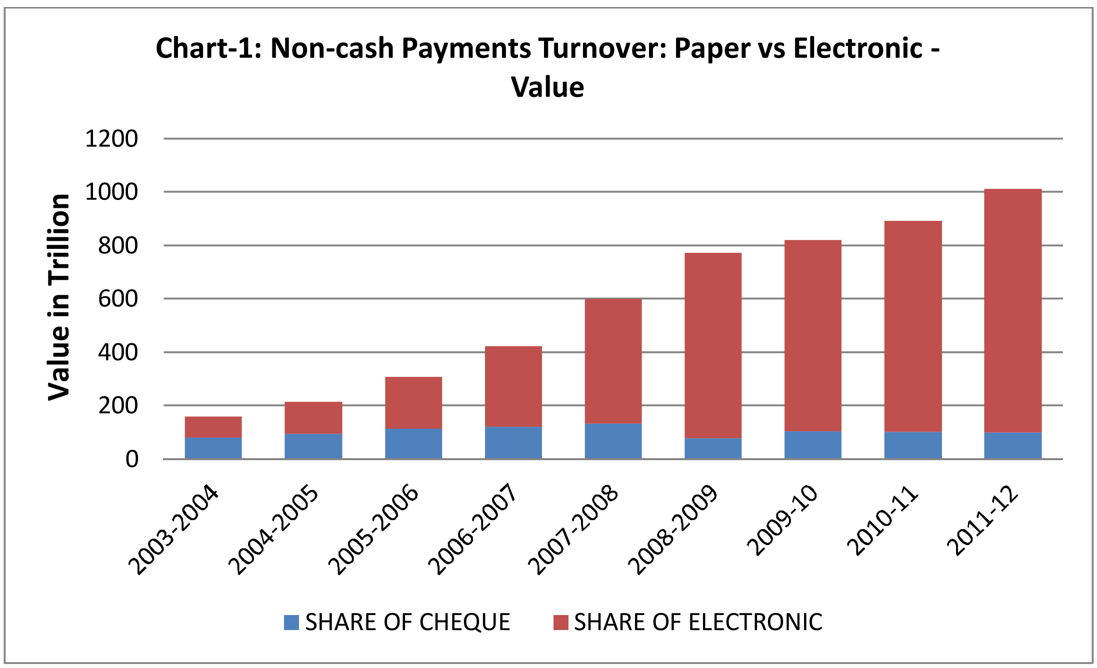
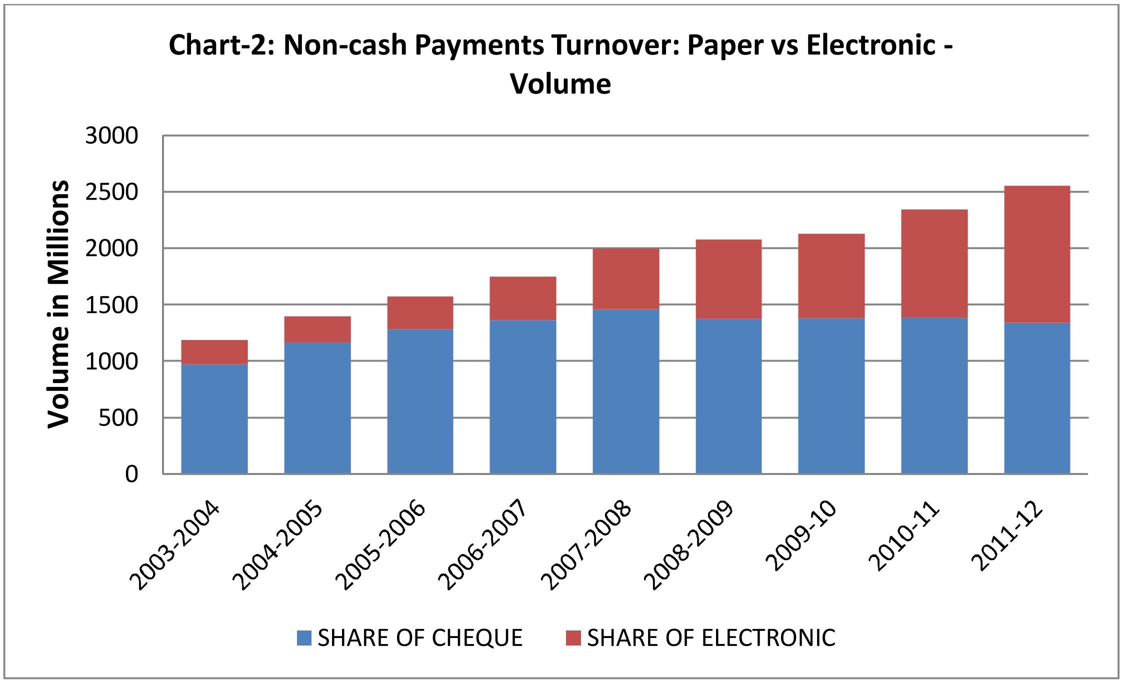


Chart-1: Non-cash Payments Turnover: Paper vs Electronic - Value

Source: RBI Annual Report

In spite of the above, in absolute terms cheque volumes continue to be high at nearly 52% of total payments turnover (Chart-2). Significantly, the share of cheques is showing a declining trend.



Source: RBI Annual Report

While this high cheque volume may be attributed to the vast, low cost and efficient cheque clearing infrastructure in the country as also the overall growth in the economy, it is nevertheless desirable that such incremental transactions take place in electronic form rather than through cheques. Further, it would be desirable to migrate existing cheque usage also to electronic form.

REASONS FOR CHEQUE USAGE

The road to travel towards the migration from cheque usage is easier said than done. Some of the reasons for the continued usage of cheques, despite developments in electronic payments are:

- Cheque was the only alternative to cash for a long time and as such, has paved its way to all segments of the society. Consumer habits / mind set do not change as quickly as changes in technology take place. Migration from cash to cheque is a simple step forward involving move from one physical instrument to another. E-payments on the other hand, are not visible / physical in nature and as such are at a different conceptual level. The most important factor that contributes to the usage of cheque is the comfort of feeling the physical instrument. Hence, even as newer electronic forms of payments are introduced, widespread adoption of such modes takes time.
- The ease with which cheques can be issued - only the name of the beneficiary is required as against e-payment modes requiring additional details such as

account number, name of bank/branch. The beneficiaries are not very comfortable, presently, parting with such details. In many cases, cheques also enable anonymity in payments through use of bearer instruments.

- Further, there has always been a mismatch between the supply and demand for electronic payment modes. Low levels of accessibility and awareness of electronic payment systems hamper adoption of electronic payments. Many users may also be apprehensive of using a ‘new’ mode of payment and as such may resist the movement from their ‘comfort zone’ of using cheques. A lack of knowledge of online transaction process creates apprehensions that the account/transaction information can be accessed by / is shared with others, and can be used fraudulently. This in turn, gives rise to apprehensions regarding security issues in electronic payments, especially since such payments can operate from virtually anywhere across geographic borders.
- Issuing of cheques does not cost much to the drawer, for example, as most banks offer some number of cheques leaves free of cost. Similarly, collection charges are also waived in many cases to the payee. In India, at present there are no charges for collecting local cheques and in case of Speed Clearing cheques up to Rs. 1 lakh are not charged. In contrast, some charges have to be incurred for initiating electronic payments to the originator. Given the lack of awareness, cost considerations influence payments behaviour, overriding other considerations.
- Most electronic payments are ‘credit push’ in nature which per force necessitates the payer to have the requisite funds at the time of initiating the payment. Cheque issuance does not come with any such compulsions! Often, people issue cheques without apprehension regarding fund availability as they are confident of using the ‘time window’ between cheque issuance and cheque collection to deposit the necessary amount in the account from which the cheque has been issued. This ‘time window’ is further extended when the payee delays the collection of the cheque. This delay benefits the payer.
- Further, cheques are also the preferred mode when the payer wants to exercise control over when (timing) the payment is made. In case of electronic payments, since ‘value date’ concept is still not so widespread, the fear is that the payer cannot control the timing of payment once the payment mandate is given.
- Cheques also enable the issuer to maintain a physical record of the payments, which may not be so visible under electronic payments. These fears play on people’s choice of mode of payments, especially among those who are not so comfortable with carrying out on-line transactions.
- In case of online banking / payments, many banks put ceilings on the amount for payment made by users using that mode. At times, the account holders themselves are allowed to set their per transaction / per beneficiary remittance

limits. While the reasons behind this could be to ensure the safety for the users, it also creates undue hassles when the user wants to make payments (in case of urgency) beyond the set limits. In such cases, the users may prefer to issue cheques, rather than go through the time-taking process of making changes in the limits, which has to be authorised by the bank.

Further, in the Indian context, there are possibly two other important reasons which tend to drive the continued usage of cheques:

- Preference of the lenders for Post Dated EMI cheques rather than other electronic modes of collection under the strong belief that the lender gets protection under NI Act only if the payments are made through cheques. This is despite the protection given under the Payment and Settlement Systems Act 2007. A random check with a few banks revealed that in case of one bank, atleast 10% of its loan recoveries were through PDCs while another bank indicated that around 20% of its monthly cheque volumes presented in outward clearing comprised PDCs. One other major banks indicated that about 4% of its monthly outward volume is in the form of PDCs. Even this indicative data shows that PDCs constitute a sizeable segment of cheques in usage, and these can certainly be migrated to electronic means.
- Availability of faster cheque clearing infrastructure through more than 1200 clearing houses in India with a very small ócooling periodô[1] as compared to that prevalent in advanced economies, is another reason. Customers are comfortable and generally content with the present system, wherein, the local cheques and majority of the outstation cheques are cleared (through speed clearing) with T+1 clearing cycle.

In addition to the above, surveys conducted in various countries seeking to reduce/eliminate cheque usage, has also brought to fore other reasons for people/organisations continuing to use cheques. For instance, the review commissioned by Payment NZ (done by Ernst & Young) in 2011 on the use of cheques in New Zealand, revealed that home-bound individuals (due to age or illness) continued to use cheques or that cheques are considered to be a more personal form of gift or donation, etc. The survey also revealed that organisations continued to accept cheques for following reasons ï it is easier to match payments with applications / invoices, making it as easy as possible for customers to make a payment, etc. Organisations issued cheques to facilitate making of irregular or large or on-off payments, an opportunity for payment float, etc.

[1] Cooling period is the time up to which collecting banks should wait after receiving provisional credit for the amount of cheque presented by them for possible return of the cheque by the drawee bank under the provisions of the applicable laws in the country, before giving credit to the customers, which, varies from 5-21 days.

THE NEED FOR 'MANAGING' THE DECLINE IN CHEQUE USAGE

The Report "Target 2013: Modernising Payments in Ireland" prepared by the National Irish Bank in September 2010 outlines the unique characteristics of the payments industry which justify the need for intervention in reducing the cheque usage in that country:

- ***Social cost of cheque usage***: Paper-based systems such as cheques and cash come with a considerable cost to the society, particularly in those countries where high usage of cheques persists. Besides the obvious financial costs related to cheque usage such as printing, security, postage, clearing and handling costs etc., high cheque (and cash) usage also bring other non-financial costs to the users/society such as growth of a shadow economy, environmental damage, security risks, etc.
- ***Payments services is a network good***: The success of any payment product depends upon the number of other people who use and accept it. Thus, if no one were to use cheques, then cheques would decline just as they would thrive if people continued to accept cheques even if they are inefficient and expensive. Hence, a 'managed' decline of cheques could nudge the payments choice into electronic mode.
- ***Choice of payment mode is secondary***: Since payment services are not consumed for their own sake, a person's preference for a given mode of payment is usually dependent on the mode accepted by the seller of the goods and services that is primarily being bought (and for which payment is being made). Regardless of the customer's own preference, payment will be made using a particular mode depending on the seller acceptance. The receipt of fees by academic institutions by demand draft which is also a paper instrument is a testimony of this fact. Thus, if the seller accepts cheques, then cheques will continue to exist. Conversely, electronic payments will get a boost, if sellers are disincentivised to use cheques (and cash) as they would move to electronic payments.

Broadly, these reasons can be held to be universally true and provide the rationale as to why it is essential to 'manage' the extent and speed of decline in cheque usage as well as monitor the direction in which such payments get re-directed (preferably into electronic payments).

Thus, even as these factors are well-appreciated, it has not been possible to push-the-envelope insofar as ensuring that cheque usage is seriously discouraged. It is perhaps appropriate to do so now that alternate means of payments in the form of easy, accessible, low-cost and efficient electronic systems are available.

DEVELOPMENTS IN ELECTRONIC PAYMENTS

Gradually, many options of electronic payments have been made available in the country which can easily be adopted by the cheque using public ï both institutional and individual users. These include systems such as:

- Electronic Clearing Service - While the ECS is generally operated at local levels, the National ECS (NECS) system, operated from a central location at Mumbai, is a pan-India system facilitating crediting of accounts of beneficiaries across bank branches. It leverages on Core Banking Solutions (CBS) of member banks. The Regional ECS (RECS) covers all CBS-enabled bank branches within a state or a group of states, thus facilitating state-wide payments/receipts to be processed at a centralised location. There are two variants of ECS - (i) ECS (Credit) which can be used by corporates and governments for making bulk and repetitive payment requirements like salary, interest, dividend payments etc. It facilitates crediting the beneficiaries account on the appointed date without involvement of any paper instruments (ii) ECS (Debit) enables utility companies, insurance and loan companies, etc. to effect the periodic and repetitive collections from consumers (EMIs) directly from their bank accounts, based on the mandates given by them. In case of EMI payments, the ECS (Debit) system greatly obviates the need for using Post-dated cheques (PDCs) by lenders for collecting the periodic instalments from the borrowers.
- National Electronic Funds Transfer (NEFT) system facilitates near-real-time funds transfer facility with its twelve batch settlements at hourly intervals, which can be best used for domestic fund transfer requirements. Some salient features of the system include ï acceptance of cash for originating transactions by walk-in customers, positive confirmation to the sender regarding successful credit of funds to the beneficiary account, provision for penal interest for delayed credit to beneficiary account or delayed return of funds to originator, no minimum or maximum amount limitations, facilitating outward transfers to Nepal to enable migrants from that country to remit funds to their families using the formal banking channel,etc.
- Real Time Gross Settlement (RTGS) system, facilitates both inter-bank and customer transactions with transfer of money taking place from one bank to another on a "real time" and on "gross" basis. Settlement in "real time" means payment transaction is not subjected to any waiting period. "Gross settlement" means the transaction is settled on one to one basis without bunching or netting

with any other transaction. All inter-bank payments and customer transactions above Rs. 2 lakh can be processed through this system.

- Inter-bank Mobile Payments (IMPS) operated by NPCI facilitating inter-bank transfer of funds through mobile phones. This leverages on the high penetration rate of mobile phones and is built around the convenience and ease of use among mobile phone users. Further, the IMPS also provides the convenience of using the IMPS for internet-based on-line transactions.
- National Automated Clearing House (NACH) operated by NPCI is similar to the ECS payment service enabling pan-India processing of bulk payments and receipts. The system has just been operationalized towards the end of December 2012. It also has the capacity to electronically manage Debit mandates and holds great promise for substituting the cheque system.
- Introduction of second factor authentication for card not present transactions in order to make card transactions more secure.
- The Aadhaar Bridge Payment Systems (ABPS) has been put in place by NPCI as a payment bridge in order to facilitate direct credit of government benefit payments to beneficiary accounts based on the Aadhaar number, Amount and Transaction reference number. Account number and Aadhaar number mapping has been done by each beneficiary bank and uploaded to the NPCI central system. Thereafter, through Aadhaar Enabled Payment System (AEPS), the funds are withdrawn by the intended beneficiary at Business Correspondent (BC) locations by providing Aadhaar number and validation of biometric identification.

All efforts are being made by both the RBI and the banks to create awareness about the safety, security and ease of operations of electronic modes, using various platforms including customer interactions during town hall meetings etc. Similarly, in recent times, the charges structure for most of these products have been rationalised even as the necessary payments infrastructure in the eco-system is being strengthened.

MULTI-PRONGED APPROACH FOR CHEQUE DISINCENTIVISATION

Given the reasons for continued existence of cheques as a payment means, it is a moot point that positive reinforcements for electronic payments alone will not lead to reduction in cheque reduction, but it has to be reinforced unequivocally through certain measures which will disincentivise the usage of cheques quite forcefully. Needless to state, in line with the Vision Document for Payment Systems, this process of disincentives has to be built around a multi-pronged strategy so as to ensure that there is no negative slippage towards cash-based payments. In this endeavour, banks, which are not only the major players in electronic payments but having considerable stake in cheques and their usage, have a significant role to play.

Based on the inputs received during consultations with stakeholders, the ***following strategies*** can be considered which not only focus on reducing cheque usage but also envisages paving the way for ódirectingô the users towards adoption of electronic payment services.

(A) Segment the users and set suitable targets

In order to ensure that the plan of disincentivisation works well in meeting the objective of reducing cheque usage in the country, it is essential to identify the cheque using segments of the population, their reasons for doing so including identifying the transactions / purposes for which cheques are being used and then build necessary disincentives even as they are ódirected and managedô towards electronic payments most suited to their requirements. Education and Awareness of alternate payment means would go a long way in ensuring the success of this plan. The on-going financial literacy efforts through Electronic Banking Awareness and Training (e-BAAT) would play a very significant role in this context.

The segments may be classified broadly into individual users, institutional users and Government departments so as to encompass all the categories of payments such as - Person to Person(P2P), Person to Business(P2B), Business to Person(B2P), Business to Business(B2B), Person to Government(P2G), Government to person(G2P), Business to Government(B2G), Government to Business(G2B). All the segments, including the banks, need to work together to achieve the objective of reducing cheque usage in the country and migrate towards electronic payments. Illustratively,

<u>Individual users</u>: should be discouraged from using cheques to meet their requirements and encouraged to migrate towards electronic payments

- P2P funds transfer requirements could be done through the use of RTGS, NEFT, IMPS, Internet Banking etc.
- P2B payments can be made using NEFT, ECS, NACH etc. (for instance utility bills payments, insurance premia etc)
- P2G payments can be made using Internet Banking, card payments, etc.

<u>Institutional users</u>: all B2P payments can be met using ECS, NACH and NEFT payment services while B2B payments can be made using either RTGS or NEFT depending on the value and time criticality of payments. B2G payments are also best routed using NEFT and RTGS along with online payments using net banking as well as through card payments.

Government departments: all G2P payments can be made through direct transfer to the beneficiary accounts using ECS, NEFT, ABPS and NACH at present. Similarly, G2B payments can be routed through RTGS, NEFT, ECS suite, NACH etc. But the greater need is develop an infrastructure and capability of the government departments to enable P2G and B2G payments also. This can be done through a targeted approach of government departments establishing Point-of-Sale (POS) machines wherever large number of cash payment is received, for instance, RTO offices, Octroi nakas etc.

(B) Total stoppage of cheques above a threshold limit

A cut-off in value terms could be prescribed for cheques, especially current account cheques. Some countries have already initiated such measures which are indicated below by way of illustration:

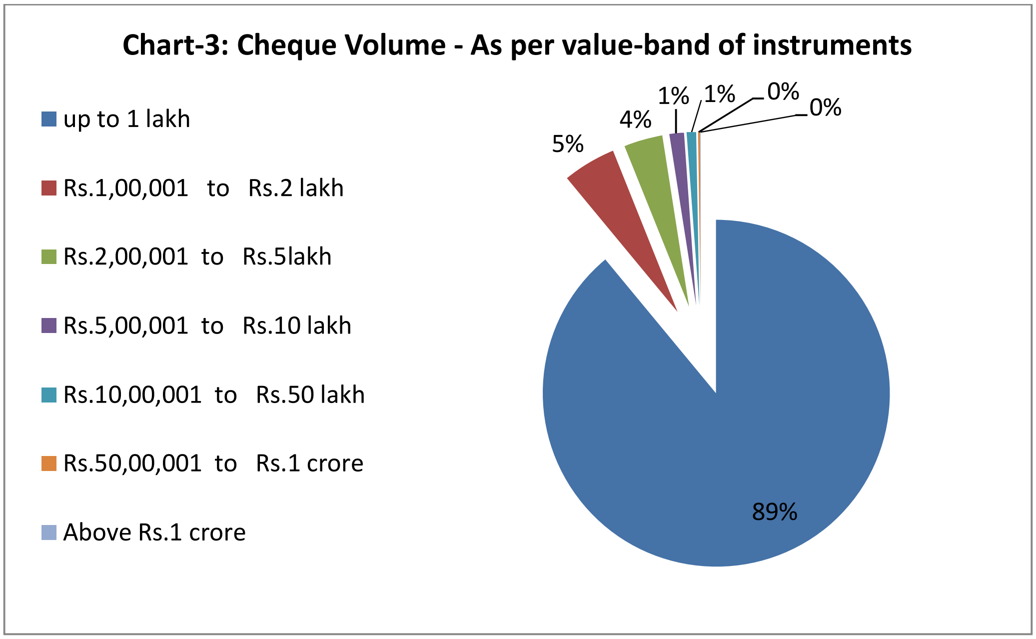
- **Canada**: The country had introduced a $25 million ceiling for cheques, bank drafts and other paper-based items to be processed through Canada's clearing system, effective February 3, 2003.
- **South Africa:** The maximum value payable per cheque has been kept at R5 000 000- (Five Million Rand/Rs.3.05Crore). In case the cheque amount exceeds this limit, it has to be cleared through bilateral exchange between the banks.
- **Nigeria :** For amounts exceeding N10 million, payments should be made through the e-payment mode such as the Central Bank Inter-Bank Funds Transfer System (CIFTS i.e. RTGS) and Nigeria Inter-Bank Settlement System Electronic Fund Transfer (NEFT).
- **Tanzania:** Cheques with value of above TZS 10 Million are not accepted for processing in the clearing houses. Payments exceeding the limit shall be processed through the Tanzania Interbank Settlement System (TISS). However, exception was made in the case of Government cheques.
- **Namibia:** No payments above N$500,000 are accepted by banking institutions through cheque.

In India, the RBI has already mandated since August 2008[2] that all payments above Rs. 10 lakh between RBI regulated entities and in RBI regulated markets are to be mandatorily made through electronic modes of payments.

However, prescription of any cut-off amount limit on issuance of cheques would have a positive impact depending upon the general values/amounts for which cheques are usually written in the country. For instance, an analysis of the volume of cheques cleared through the MICR Cheque Processing Centres (CPCs) across the country

[2] RBI Circular DPSS No.2096/04.04.007/2007-2008 dated June 20, 2008

during the first half year of the financial year 2012-2013 reveals that around 89% of the cheques cleared in these centres were below Rs.1 lakh under various categories (Chart-3).



Source: Data from MICR CPCs

However, the same analysis also reveals that, out of the cheques cleared in the first half (Apr-Sep) of 2012 across all MICR CPCs in the value band of cheques issued up to Rs. 1 lakh, about 54% of the cheque volume belong to current account related accounts, whereas in all other value bands the share of current account related cheques is nearly 64% (Chart-4). The rest of the cheques pertain to savings bank account, government accounts, demand drafts etc.

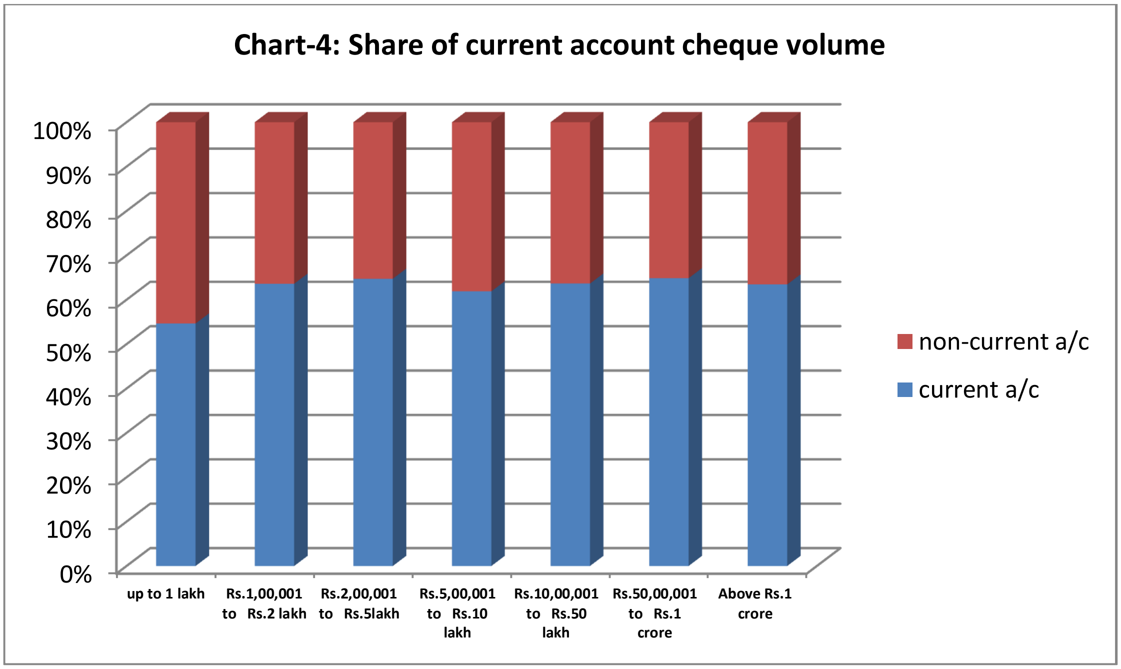


Chart-4: Share of current account cheque volume

As regards Government cheques, the data analysis reveals that government cheques account for 2-3% of all cheques processed during the period in all value bands, except in case of amounts above Rs.1 crore where government cheques account for nearly 5% of the processed cheques.

Therefore, mandating an upper threshold limit will have to be decided taking into the cheque usage pattern by various segments such as individuals, institutions and the Government, so that small users are not immediately inconvenienced even as the objective is largely met.

(C) Set limits or levy charges on issue of cheque books to account holders

This is a classic dilemma and is akin to raising the óchicken or eggô question ï are cheques used because they are available (mostly freely) to the account holders or are cheques given to account holders because it is a widely used payment method? Perhaps, in order to break this riddle and move out of cheques, there should be some limit applied to issuance of cheques to account holders. And even in those cases where it is unavoidable, the charges levied on such cheques should be quite steep so as to discourage its use.

A quick look at the charges being levied by banks shows that generally banks are providing 20 ï 50 cheque leaves to savings bank customers free either on a quarterly basis or annual basis. Few banks do not provide any free cheque books while a few banks provide free of cost cheques every quarter. Beyond this, the charges levied range from Rs.2 ï 3 per cheque leaf. In most banks, current account holding customers are not given any free cheques, though the charges are very nominal ranging between Rs.3 ï 4 per leaf.

One segment of users to whom cheque issuance could be largely curtailed is corporate and institutional users to whom cheques seem to be issued quite liberally for their current accounts. Further, the nominal charges levied by banks on such customers do not act as a deterrent for cheque usage.

(D) Levy of charges on cheque usage- by both issuer of cheque and the beneficiary

Presently, the cheque issuer (drawer) does not bear any charges for issuing a cheque, which makes this method a low-cost means of making payments. This aspect merits some review whereby the drawer is made to bear some charges when cheques are issued. Such charges may be levied on an ad-valorem basis at par with charges applicable in electronic payments systems (such as NEFT/RTGS etc.) as if the drawer had originated such payments through electronic mode.

Similarly, cheque collection charges may also be reviewed and charges levied (on the payee or beneficiary of the cheque) even for local cheques beyond certain amount limits. In case of corporates, charges may be levied irrespective of amount limits for cheques deposited into their current account considering the expenditure incurred by the collecting bank.

(E) Avoid slippage to cash transactions

This is the real apprehension that is often expressed when any plan to discourage use of cheques is discussed. Given the fact that the large volume of cheques issued in the country are of relatively low value, which combined with the accessibility of ATMs (at least in major cities and towns) gives rise to the real worry that if cheque usage is actively discouraged, it would have a negative impact by re-directing these payments to cash-mode. Thus, any strategy to reduce cheque usage should also focus its attention on ensuring that this does not lead to an increase in cash transactions.

Considering the high cost of cash handling, including cash management at ATMs, banks should be active partners in discouraging the use of cash. A sample check was conducted with banks regarding the cost of cash handling including cost of idle cash, maintenance of currency chests, cost of cash movement such as transport, security, insurance, etc. along with the cost of dispensing cash at ATMs. The feedback received from different banks revealed the following - a total cost of Rs.1.95 per Rs.1000/- which excluded the cost of insurance and dispensing cash at ATMs; the cost of dispensing cash through ATMs alone is approximately Rs.17 per transaction; the opportunity loss for holding idle cash would be approximately 9%; the cost per transaction at ATMs ranges from Rs.6.60 to Rs.15.88 in case of fully outsourced operations depending upon the service provider and area of operation. Obviously, in many cases banks have not accounted for the cost of operations where they are handled by their own staff. This could be construed as the ‘social cost’ of cash transactions to the economy as a whole.

It is understood that there are certain segments of corporate users who are large depositors and users of cash, and as such these cash transactions in current accounts needs to be discouraged/charged heavily. This has to be done by all banks otherwise the corporates may just shift their activities from one bank to another. Perhaps, this requirement could also be mandated by RBI.

ACTION POINTS

I. General comments

There are some issues which need to be addressed – both regarding disincentivising cheque usage as well as incentivising greater adoption electronic payment products and services. While it is difficult to build an exhaustive list of such issues, some of them are highlighted below:

- ✓ Setting of targets for implementation: It would be advisable to set a target date by which majority of the cheque users are disincentivised from this mode and migrate towards electronic payment methods. However, keeping in mind the diversity of users and the disparity in availability and accessibility to alternate payment services, these target dates can be further divided into phases for better implementation and monitoring. Some of these target dates could commence immediately by the beginning of the financial year i.e., April 2013 while others could be phased for implementation. Targets can also be set suitably for urban areas and rural areas within each segment of users – individuals, institutions and governments.

- ✓ Dispute resolution and complaints redressal - In parallel, the practices and procedures in electronic payment services should be geared to meet not only the technological requirements but also the operational expectations of the users who migrate from cheque usage to these systems. As indicated earlier, one of the important factors influencing persistent cheque usage relates to needs for documentation, customer grievance redressal, etc. Towards this end, various entities, such as system providers, intermediaries and payment gateway providers, corporate users including educational institutions and utility companies, etc. should ensure that the payment processes are simple to use by the "least aware" of users, reconciliation and reporting mechanisms are efficient, and complaints are handled quickly and efficiently with least inconvenience to the users. For instance, if schools begin to use electronic payment services to collect fees from students, then it is imperative that their systems are capable of matching the incoming payments with respective students, and parents/students must not be inconvenienced because the reconciliation system at the school is not efficient. Such "bad experiences" may ill-dispose the users to move away from cheques (where they can control the documentary requirements) to electronic payment services.

It, therefore, becomes imperative that some sort of functionality (e-invoicing for instance) is built within the institutions such as companies, schools and educational institutions, etc which receive payment and provide an immediate documentary evidence to the payer in the form of printable receipts and also facility automatic reconciliation at the institution's end. In the event of any dispute, the payer will at least have some record evidencing the payments made by him/her. Another feature which could aid dispute resolution and provide evidence of payment is the system of providing electronic confirmations when transactions are initiated and completed, along with the transaction reference number. At present, many utility companies provide such confirmations through e-mail and SMS so that some trail is built around the transaction. Similarly, the NEFT system also provides for a system of positive confirmation to the sender which enables him/her to be aware regarding the time the funds were credited to the beneficiary account. Incorporation of such payment details in bank account statements / pass books would also facilitate record-keeping requirements of customers.

- ✓ <u>Protection for bouncing of "electronic payments"</u> - Section 25 of the Payment and Settlement Systems Act, 2007 accords the same rights and remedies to the payee (beneficiary) against dishonour of electronic funds transfer instructions for insufficiency of funds in the account of the payer (remitter), as are available to the payee under section 138 of the Negotiable Instruments Act, 1881. The sub-section (5) of the section 25 of the Payment and Settlement Systems Act, 2007 provides for punishment of two years and twice the amount of electronic funds transfer instruction, or both for dishonour of such electronic funds transfer on par with the penalties stipulated for dishonour of cheques under the Negotiable Instruments Act, 1881. However, awareness of these provisions have not been sufficiently created amongst users of electronic payments, which needs to be done by all entities especially banks, so as to ensure that users of these systems are aware of their legal responsibilities and rights.

- ✓ Widespread accessibility to electronic payments – As stated earlier, payments are "network goods" and as such high growth in electronic payments can be witnessed when the network effect is strong and there is no skewness in demand and supply of such services. Card payments are generally considered as a more convenient form among all electronic payments. As such, the card acceptance infrastructure needs to be further enhanced to ensure that it is geared up for all types of payments. Greater awareness also needs to be created about the availability of such payment options.
- ✓ Customer liability – another factor of equal importance which is very crucial in ensuring greater adoption of electronic payments relates to the matter about the responsibilities and obligations of customers as well as banks and service providers. For instance, in case of an unauthorised transaction taking place using a customer's credentials, the customer needs to know to what extent he/she would be protected, what is the extent of liability to be borne by him/her and what is his/her obligation towards the bank/service provider. In the absence of such clarity, there would always be an apprehension that in case of any unauthorised transaction, the customer would have to "shoulder the loss" while the bank/service provider may go away free.

Keeping the above issues and strategies outlined in view, few "action points" are indicated below which seek to discourage cheque usage. Segment specific approach is used to outline the action points and targets which is more "actionable" and also "identifiable" in terms of implementations and monitoring.

II. Individuals as Cheque Users

The following actions are proposed to discourage individuals from cheque usage:

a) Free cheque books may be kept to a minimum number on a per annum basis. The charges levied by banks beyond this number may range from moderate to steep (slab rate) depending upon the cheque usage history of the customer.
b) In case of fresh loans, PDCs should be completely stopped and repayments should be only through electronic payments, with suitable conditions for late payment and non-payments which should be disclosed upfront.
c) Existing PDCs should be converted to electronic payment mandates within a prescribed timeline.
d) Credit card dues should be paid electronically. In case card holders make payments of card dues using cheques, then high convenience charge may be levied by the card issuing bank. This can be implemented after giving due notice and sufficient time to the customers to change to electronic means.

e) It may also be considered to apply some amount/value limit for cheque issuance by individuals. For any cheques issued beyond the stipulated limit, charges may be levied at the time of payment / debit to the account by the paying bank when the cheque is presented for payment through clearing. Such charges may be higher than the charges levied on electronic payments of similar value.
f) In case of individuals who have invested in shares/debentures/bonds etc. and have not opted for receiving dividend/interest directly into their bank accounts, we may consider levying a processing charge when the cheque is deposited into their bank account for collection. To begin with, this may be implemented in major towns and cities where ECS facility is already available and then gradually extended to all areas.
g) In order to avoid increased dependence or slippage to cash-based transactions, high (both in amount and frequency) cash withdrawals and deposits of cash by individuals may also be charged. Implementation of this may however be preceded by conduct of structured research and concerted efforts at customer education.
h) Discourage cheque collection boxes at public places - have it only at bank branches. This will reduce the convenience of using cheques by individuals.

III. Institutions as Cheque Users

Corporates and institutional customers are the largest users of cheques across all value bands accounting for 54% - 64% of cheques processed (Chart-5). Hence, it is imperative that this segment is targeted for moving towards electronic payments.

The following actions are proposed to disincentivise corporate customers from using cheques and also to ensure that there is no slippage to cash:

a) As a first step, access to cheque books should be made costlier for such corporate / institutional customers. There should be no free cheque books given. The charges levied for cheque books issued to such customers may also be increased substantially so that it acts as a deterrent in comparison to alternate electronic payments.
b) Corporates and institutional customers need to stop issuing cheques and make their payments through electronic means, the rationale being that such cheques issued by them have to in any case be encashed by the beneficiaries through the banking system. Hence, logically the beneficiaries should be able to receive the payments from the corporates through electronic payment modes. Therefore, we may consider levying charges for cheques issued by current account holders and these charges may be higher than the corresponding charges if the payment were to be made electronically.

c) Corporates have to also be discouraged from issuing physical interest warrants and dividend warrants. Where such physical instruments are issued, a processing charge (for instance Rs.25/- per instrument) may be levied by the paying bank (on the corporate which has issued the instrument) when the instrument is presented for payment.
d) Further, institutional users are more capable than individuals in moving towards accepting funds electronically. In order to discourage them from accepting cheques from their customers, we may consider levying charges on them when they deposit cheques in their current accounts for collection. This should be made applicable to all institutional users including educational institutions, public utility companies etc. in a phased manner.
e) It is found that even where educational institutions and public utility companies are accepting electronic payments, they are levying certain convenience fees to the payers which need to be stopped.
f) Similarly, cash deposits in current accounts need to be discouraged actively. It is learnt that certain segments of business are heavy users of cash which not only adds to the ósocial cost of paymentsô but also adds to the cost of cash handling at banks, which may be cross subsidised elsewhere to the detriment of other more efficient services. Hence, it is proposed that steep charges should be levied on cash deposits / withdrawals by current account holders into/from their accounts. These charges need to be levied by all banks.

IV. <u>Government departments / agencies as Cheque Users</u>

Given the sizeable nature of Government transactions, they often play a catalyst role in driving the payments in the desired direction. The concept of payment services as a ónetwork goodô can be highly influenced by the payment choices of the government and their agencies. In other words, if government departments / agencies including public sector companies / utilities migrate from cheque-based transactions to electronic payments, it would naturally drive many others to adopt electronic payment services. Similarly, some of the practices and procedures followed by government departments may also influence the choice of payment mode for those dealing with government departments.

Keeping the above in view, the following action points are proposed to ensure government payments/receipts move away from cheques and go fully óelectronicô

a) All government payments to non-individual customers (corporates, business entities, institutions etc.) should be made through electronic mode only. Towards this end, the Ministry of Finance has already issued a memorandum (dated 31st

March 2012) directing all Ministries / Departments of the GOI to make payments to private parties such as suppliers, contractors, grantee / loanee institutions etc. above Rs.25,000/- by payment advices including electronically signed payment advices. This should be implemented immediately by all agencies including state government entities, public sector entities and utility companies too. Further, it should be made applicable to all payments without setting any amount limits.

b) In case of individuals too, government should quickly adopt electronic payments for which a specific timeline should be set for implementation. All benefit transfers and direct cash transfers should be done using electronic payment services as it would also give the necessary fillip to the financial inclusion efforts. Towards this end, the Government has already begun disbursing such payments using the ABPS in many districts in the country on a pilot basis.

c) In case of its receipts, government should enable all types of customers to make payments through electronic modes for which procedures should be simplified. For instance, often people making payments to the government prefer to do so through cheques as it provides them some means of documentary evidence.

d) In due course, if government departments persist in cheque-based payments and receipts then charges need to be levied on those departments/agencies when such cheques are presented for payment from / deposited for collection into government account. These charges have to be borne by the respective government departments / agencies and cannot be recovered from the customers.

e) Most importantly, government departments and agencies should immediately stop levying ćonvenience feeô on customers who prefer to make payments using electronic means such as cards, online banking etc. Unless such extra charges are waived, customers would not be willing to use this method and may continue to use cheques as there is no additional cost involved (customers are already bearing the charges for initiating electronic payment transactions).

f) Government should consider providing tax rebates (for instance, reduce service tax liability etc.) to business establishments, corporates, institutions etc. that are accepting payments through electronic mode. This would not only encourage electronic payments but also actively discourage the present (indirect) advantage that cash payments enjoy.