

Pointers to a future-ready payments policy

Events over the past few weeks have thrown up numerous pointers to what should be included in a future payments-system policy framework.

The Reserve Bank of India's (RBI's) 2017-18 annual report provided the first clue, proving a well-known policy paradigm: competition and freedom of choice are essential tools to avoid distorting markets and the broad economy. An overnight ban on Rs500 and Rs1,000 bank notes—accounting for about 85% of outstanding currency—dealt a body-blow to the economy in terms of jobs, incomes, livelihoods, investment appetite and overall economic growth. The ruinous effects manifested themselves last week: gross domestic product for April-June quarter grew by only 5.7%, the lowest in many quarters.

Demonetisation amounted to suppression of free choice—or freedom to decide how much cash to use, for which transactions—though different reasons were adduced to justify the decision. One of the reasons cited, which has persisted into the post-demonetisation period, is a desire to foster digital payments and to migrate the economy to a less-cash system.

This is a desirable economic objective. However, the policy vectors put in place reveal multiple gaps: lack of a robust competition and innovation policy; uncertainty over the payment regulator's quasi-legislative powers; an unclear road map for achieving financial inclusion; and, an asymmetric preference hierarchy between different payment systems imposed on the consumer. The last one violates democratic principles by coercing the public to move away from a relatively low-cost payment system (such as cash) to a higher cost platform (such as, mobile wallets which involve connectivity costs).

The Supreme Court's (SC's) recent ruling on right to privacy as a fundamental right is likely to complicate the regulatory debate further and might necessitate a systems rethink. The judgement reads: "The balance between data regulation and individual privacy raises complex issues requiring delicate balances to be drawn between the legitimate concerns of the State on one hand and individual interest in the protection of privacy on the other." The nine-judge bench, while acknowledging that the Centre has already appointed a committee under former SC judge B.N. Srikrishna to study the state of India's data privacy and to submit a draft bill, hopes that the Union government will take "all necessary and proper steps".

Still, the right to privacy ruling in itself does set out a future regulatory perimeter for digital financial services. The bench found some pointers in a 2012 report from an [expert group](#) on privacy, appointed by the erstwhile Planning Commission. Specifically, the report mentions a five-pillar conceptual scaffolding for drafting legislation to protect privacy: technological neutrality and interoperability with international standards, which is still lacking; multi-dimensional privacy; horizontal applicability to state and non-state entities to ensure a level-playing field; conformity with privacy principles in line with global best practices; and a co-regulatory enforcement regime which envisages co-existence of independent regulators and self-regulating organizations. Ironically, some of these issues are still being debated in the policy space.

There are multiple views on what to make of SC's judgement; for example, Chennai's IFMR Trust, soon after the SC ruling, [published a blog](#) advocating stakeholder consultation to determine what kinds of data can and should be collected, the desirable regulatory regime for data mining and algorithmic techniques and a legislative terrain to "ensure that use of personal data is tied to legitimate proportional objectives and interests".

There is another critical, and slightly obvious, ingredient necessary in the future regulatory mix:

trust. This was evident when digital payments spiked during November-December 2016 and then tapered off subsequently; people abhor repression and any attempts to increase the value and volume of digital payments must be achieved through trust, not duress. Regulation must have a consumer bias and should not be designed to favour some service providers.

Lack of trust in paper money issued by sovereigns, and controlled by central banks, is growing as is wider acceptance of crypto-currencies. Already six large global banks—Barclays, Credit Suisse, HSBC, Canadian Imperial Bank of Commerce, State Street and the Mitsubishi UFJ Financial Group—have jointly launched a project to use block-chain for clearing and settling financial transactions, reducing time taken for conventional money transfers.

While bitcoins and other crypto-assets are still in an embryonic state in India, the pace of acceptance is slowly picking up. Many community-based initiatives have been advocating block-chain as an alternative to organized finance, viewed as exploitative. The finance ministry appointed a nine-member inter-disciplinary committee to suggest the way forward with crypto-currencies; the committee has submitted its report, which has not been made public yet. Eventually, though, RBI will have to decide whether it will allow money to also exist as crypto-currency, in addition to its role as a commodity (with or without intrinsic value), a financial claim and/or as an accounting entry.

Regulation, almost always, lags technology development. But an opportunity to create a future-ready policy framework now seems close at hand.

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