The Legal 500 & The In-House Lawyer
Comparative Legal Guide
India: Fintech
This country-specific Q&A provides an overview to Fintech law in **India**.

It will cover open banking, regulation of data, cryptocurrencies, blockchain, AI and insurtech.

This Q&A is part of the global guide to Fintech. For a full list of jurisdictional Q&As visit **http://www.inhouselawyer.co.uk/index.php/practice-areas/fintech/**

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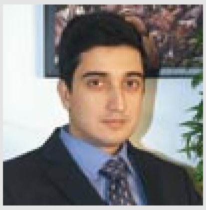

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1. ## What are the sources of payments law in your jurisdiction?

The sources of law regulating payments in India include the Payment and Settlement Systems Act, 2007 (PSS Act) and the Payment and Settlement Systems Regulations, 2008 issued thereunder. The PSS Act and the Regulations provide the necessary statutory basis for India's central bank, the Reserve Bank of India (RBI) to undertake the function of regulating payment and settlement systems in India. Under the PSS Act, the RBI has wide discretion to issue directions and guidelines to payment systems. While there is also a proposal to make changes to the PSS Act and introduce a new regulator called the Payments Regulatory Board (PRB), the necessary amendments to the PSS Act have not been passed yet.

2. Can payment services be provided by non-banks, and if so on what conditions?

Yes, payment services may be provided by non-banks. The PSS Act provides that any person, including non-banking financial companies (NBFC) or any other entity that wishes to operate a payment system, may do so upon receiving authorisation under the PSS Act by the RBI. However, there are certain eligibility criteria to be met in order for an applicant to obtain such authorization from the RBI to issue and operate a payment system. In addition ‘payment gateway service providers’, which merely act as technology service providers between merchants and banks (that process or settle the transaction) may not require an RBI authorization. Examples of such payment gateways operating in India are BillDesk, RazorPay and Instamojo.

3. What are the most popular payment methods and payment instruments in your jurisdiction?

Cash or fiat currency is the most preferred mode of payments in India. Currency circulation accounts for 18 percent of gross domestic product (GDP) as against 3.5-8 percent in developed nations. Approximately, 78 percent of all consumer payments and 97 percent of all retail payments are made in cash as of April 2018. Other than cash, paper and non-paper payment methods and payment instruments are also commonly used in India. Paper-based instruments include cheque and paper based national electronic fund transfer (NEFT) instructions. NEFT can also be used via internet banking facilities offered by banks to their customers. Primary non-paper based modes for retail payments include, immediate payments service (IMPS), Unified Payments Interface (UPI) enabled apps, credit cards, debit cards, prepaid payment instruments (PPIs) such as e-wallets and gift cards, and national automated clearing house (NACH).

What is the status of open banking in your jurisdiction (i.e. access to banks' transaction data and push-payment functionality by third party service providers)? Is it mandated by law, if so to which entities, and what is state of implementation in practice?

4. 'Open banking' as a concept for all kinds of financial data has not been uniformly implemented

in India. However, UPI can be considered to be a form of 'open banking' for digital payments. It is a system developed by India's nodal retail payments organizations, the National Payments Corporation of India (NPCI) and it allows for customers of UPI enabled banks to seamlessly make peer-to-peer and merchant payments through payment apps operated by third parties using the NPCI's infrastructure. Application portability has been provided by separating the 'Payment Services Provider' (PSP) bank with the customer's remitting bank and the recipient receiving bank. For instance, a customer of Bank A can use the UPI application of Bank B to send money to a customer of Bank C. While the payment processing and settlement functions continue to be done by banks, several applications are being designed and marketed by third party app developers after entering into tie-ups with banks. Examples are, Google Pay, WhatsApp Pay and PhonePe who have tied up with a host of banks such as ICICI, HDFC, Axis Bank, Yes Bank etc.

5. How does the regulation of data in your jurisdiction impact on the provision of financial services to consumers and businesses?

Data is heavily regulated in banking and financial institutions; hence banks and financial institutions have strict confidentiality and security obligations with respect to consumer and banking data. In addition, the RBI has recently in April issued a Notification under the PSS Act mandating data localization requirement for payments information. The Notification states that "complete end to end transaction details including information collected, carried or processed as part of the message or payment instruction, to be exclusively stored in a server/system only in India". Only the storage abroad of a 'foreign leg' of a transaction will be permitted. This is likely to require significant investments in local data center capacity, especially by foreign payment service providers.

6. What are regulators in your jurisdiction doing to encourage innovation in the financial sector? Are there any initiatives such as sandboxes, or special regulatory conditions for fintechs?

The RBI and the Securities Exchange Board of India (SEBI) have set up the Working Group on Fintech and Digital Banking and the Committee on Financial and Regulatory Technologies respectively. These committees have been tasked with assessing the opportunities, risks and challenges presented by the rapid growth of FinTech in India. The RBI's Working Group, in its report has recognized that there is a need to 'provide an environment for developing FinTech innovations and testing applications/APIs developed by Banks and FinTech Companies'. Recent media reports also state that the RBI is working on a regulatory sandbox for financial technology.

7. Do you foresee any imminent risks to the growth of the fintech market in your jurisdiction?

The most imminent risk would be the fate of the national 'Aadhar' biometric identification system. As the vast majority of Indians already possess an Aadhar number, the system had become an indispensable tool in the hands of fintech enterprises as it allowed for a seamless, instant electronic KYC using the fingerprint and iris scans of individuals. A recent ruling by the Supreme Court of India has now ruled that Aadhar can no longer be used for purposes of electronic authentication by private entities (including fintech enterprises) for KYC purposes. Thus, there has been an adverse short term impact on the fin-tech space especially smaller fintech players and start-ups, that almost exclusively relied on the use Aadhaar for low-cost digital customer verification and acquition.

Next, regulatory authorities in India have also taken a very strict view on crypto-assets. The Government and the RBI have taken steps which could affect the future of cryptocurrency businesses in India. These steps have been discussed in detail in question 14 below.

8. What tax incentives exist in your jurisdiction to encourage fintech investment?

The Indian government has launched the 'Start-up India' initiative under which various incentives (such as a three year income tax holiday) subject to the start-ups meeting certain conditions. Some additional financial incentives are also there for digital payments. While these are not *per se* tax incentives, they are more geared towards the users of these services as opposed to the providers of such services. Two such notable incentives are the recent subsidization of Merchant Discount Rate (MDR) paid by merchants on debit cards for transactions lesser than INR 2,000 and the subsidy on Goods and Service Tax (GST) to the users of the RuPay card or the BHIM UPI App, which have been developed by the National Payments Corporation of India (NPCI).

9. **Which areas of fintech are attracting investment in your jurisdiction, and at what level (Series A, Series B etc)?**

Due to the large amount of cash in circulation and resulting market potential, the Payments segment has attracted the majority of fintech investment in India. Several international companies such as Softbank, Amazon, Google and WhatsApp have invested in the Indian payments space. While Amazon has made greenfield investments into India by setting up and licensing its own payment system in India, Softbank and Berkshire Hathaway have invested a combined 1.7 billion dollars in One 97 Communications Private Limited ((the operator of the ‘Paytm’ mobile payments platform)) for its 10th and 11th funding rounds respectively. Google and WhatsApp have tied up with Indian banks to facilitate digital payments on the UPI platform through the launch of their own apps. India is now the largest user of mobile data in the world. This has facilitated massive growth in digital payments. The volume of digital payments in India is estimated to grow beyond USD 500 billion (approx. 15% of GDP) by 2020. Aside from digital payments, 27% of fintech companies that have obtained funding are in the alternative lending segment, out of which 27% have raised Series A capital. As per some reports, for the first 9 months of 2018, Fintech startups in India raised a combined 1.6 Billion USD across 99 deals at various stages.

10. **If a fintech entrepreneur was looking for a jurisdiction in which to begin operations, why would it choose yours?**

India is now the largest user of mobile data in the world and smartphone ownership is rapidly rising. This has enabled mass adoption of digital technologies. India provides a unique opportunity for Fintech entrepreneurs to begin operations as the largest under-served population in banking and other financial sectors. India’s deep talent pool for software engineers and developers also makes it a ready base from which to develop fintech applications. Government support, especially in the payment segment has been significant with the financial incentives (which have been discussed above) being provided to individuals and merchants to adopt digital payments.

11. **Access to talent is often cited as a key issue for fintechs – are there any immigration rules in your jurisdiction which would**

help or hinder that access, whether in force now or imminently? For instance, are quotas systems/immigration caps in place in your jurisdiction and how are they determined?

There is no *per se* quota system which is applicable for immigrants into India. However, the minimum salary for a prospective employee to get a visa in India is in excess of USD 25,000 per year. Apart from certain exemptions, visas are given only to individuals with skills which are unavailable in India (such as highly qualified technical experts, senior executives in a managerial position, etc.) While there is no specific validity specified for employment visas for the Fin-Tech industry, for individuals working in the Information Technology enabled sectors, the validity of a visa is limited to three years at a time. However, this is extendible. Generally, employment visas for most other sectors are valid for only 2 years at a time, which is extendible.

12. If there are gaps in access to talent, are regulators looking to fill these and if so how? How much impact does the fintech industry have on influencing immigration policy in your jurisdiction?

Immigration policy is not a topic which is paid significant attention by regulators in India as the country has a significant labour surplus. The domestic fintech industry does not seem to have sought any specific changes to the immigration policy in India.

13. What protections can a fintech use in your jurisdiction to protect its intellectual property?

Contractual safeguards can be implemented in IP agreements, such as IP Transfer Agreements or IP Licensing Agreements. Specifically, for Trademarks and Patents (if eligible), fintech service providers can make the appropriate filings with the Office of the Controller General of Patents, Designs and Trademarks. Copyright registration with the Copyright Office is optional and not mandatory to establish copyright in a work. Depending on the specific facts and circumstances, parties can also incorporate arbitration clauses into their contracts. India is a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958 (New York Convention) as well as the Geneva Convention on the Execution of Foreign Arbitral Awards, 1927 (Geneva Convention). If a party receives a binding award from a country which is a signatory to the New York Convention or the Geneva Convention and the award is made in a territory which has been notified as a convention country by India, the award would then be enforceable in India. Out of the 196 countries in the world only 48 countries have been notified by the Indian Government as reciprocating countries (With major countries such as US, UK, France, Germany, Netherlands, Singapore being notified territories) with the most recent addition being Mauritius.

14. How are cryptocurrencies treated under the regulatory framework in your jurisdiction?

Currently there is no clear definition for cryptocurrencies / virtual currencies in India and till recently, there was also no law which specifically regulates cryptocurrencies. For this reason, under the existing regulatory framework and judicial precedents, the classification of cryptocurrencies such as Bitcoin is likely to be 'goods' in the nature of software. The consequence of this is that any cross-border trade in the token is likely to be deemed as an import or an export of the good viz. in the nature of a software and attract applicable exchange control and Goods and Service Tax (GST) regulations.

Further, on April 6, 2018, RBI issued a circular titled "Prohibition on dealing in Virtual Currencies" (VC Circular). The VC Circular prohibited regulated financial institutions from "dealing with VCs or providing services for facilitating any person or entity in dealing with or settling VCs". This has resulted in entities dealing in crypto-assets from being cut off from the Indian financial system. This circular has been challenged in the Supreme Court of India on the grounds of being unconstitutional. (Disclosure: Nishith Desai Associates is acting for some of the parties who have challenged the VC Circular in the Supreme Court).

15. How are initial coin offerings treated in your jurisdiction? Do you foresee any change in this over the next 12-24 months?

There are no specific laws on initial coin offerings in India. However, in the absence of any specific definition for the term 'Virtual Currency', all initial coin offerings in India are likely to be impacted as they will be cut off from the Indian financial system as a result of the RBI's circular discussed above.

The chances of any change over the next 12-24 months would be subject to the ruling of the

Supreme Court of India on the constitutionality of the VC Circular. In addition, as per a Government press release, on October 30, 2018, FSDC "*deliberated on the issues and challenges of crypto-assets/ cryptocurrency and was briefed about the deliberations in the High-level Committee to devise an appropriate legal framework to ban the use of private crypto currencies in India and encouraging the use of Distributed Ledger Technology (DLT)*". In the absence of a clear definition of crypto-currencies or VCs in India, this is likely to affect the growth of the virtual currencies and ICOs in India. Even blockchain platforms which depend on some level of tokenization for their functioning are likely to be affected.

Other factors which could change this position are the results of the General Elections, which are scheduled for 2019 and the composition of the new government.

16. Are you aware of any live blockchain projects (beyond proof of concept) in your jurisdiction and if so in what areas?

Numerous innovative blockchain startups are present in India such as Elemential, which is a blockchain middleware that is sector agnostic and are being used to create a KYC utility by National Stock Exchange (NSE), enable instant allotment for asset registries, manage royalty payments for media licenses. Sofocle is another company that designs and develops blockchain powered enterprise solutions for Smart Contracts, Supply chain, Finance, Insurance, Healthcare, and Manufacturing. EzyRemit is a startup that enables blockchain powered solutions to the remittance market and StaTwig is a company that is leveraging Internet of Things (IoT) and blockchain to provide real-time tamper-proof end-to-end tracking that identifies problems and inefficiencies in the supply chain industry. Further, IBM has introduced an invoice management blockchain solution for manufacturing companies to enable their Goods and Sales Tax (GST) compliance. Recently, HSBC India has also executed a trade finance transaction involving an export shipment sent by Indian company Reliance Industries Limited to a US buyer.

While Distributed Ledger Technology (DLT) cannot always be equated to blockchain, India's telecom regulator (Telecom Regulatory Authority of India) has also issued regulations recently which mandate the use of DLT by telecom companies to restrict the flow of unsolicited commercial communication to Indian telecom consumers.

To what extent are you aware of artificial intelligence already being used in the financial sector in your jurisdiction, and do you think regulation will impede or encourage its further use?

17. The deployment of AI technologies is currently at a nascent stage in the Indian banking sector,

its competitive advantage over conventional means has been recognised, in the form of setting up of innovation centers and organising hackathons vis-à-vis partnerships between banks and Fintech companies. State Bank of India, the largest bank in India conducted “Code for Bank” hackathon to build solutions leveraging futuristic technologies such as AI into the banking sector. Even the Finance minister of India, in his budget speech for 2018 – 2019, mandated India’s national policy think tank, the NITI Aayog to establish the National Program on AI. In pursuance of this, the NITI Aayog has partnered with several leading AI technology players to implement AI exploratory proof-of-concept projects in numerous areas. It is also formulation a national strategy for building a vibrant AI ecosystem in India in collaboration and consultation with various experts and stakeholders. NITI Aayog unveiled its discussion paper on national strategy on AI focuses on how India can leverage the transformative technologies to ensure social and inclusive growth.

18. Insurtech is generally thought to be developing but some way behind other areas of fintech such as payments. Is there much insurtech business in your jurisdiction and if so what form does it generally take?

Insurtech is at a nascent stage in India however given the scope of new business models, applications, processes and products the Insurance Regulatory and Development Authority (IRDAI) set up a Working Group to examine innovations in insurance involving wearable/portable devices. It is advocating the integration of technology in the process of underwriting risks, processing claims, and the conduct of insurance business itself. While insurance companies have been quick to adopt outreach initiatives, such as, the use of e-forms, remote underwriting calls, etc., considerable effort is required to be made to integrate technological innovations in product design by insurance companies. Although, the IRDAI has de-regulated the tariff-fixing for insurance products, product design continues to be strictly regulated.

19. Are there any areas of fintech that are particularly strong in your jurisdiction?

The fintech landscape in India is dominated by digital payments and lending companies, while other segments, such as personal finance, instant credit and enterprise solutions, are rapidly gaining momentum. Efforts by the NPCI to develop inter-operable payments platforms, as mentioned earlier, have provided significant impetus to the growth of digital payments in India.

The massive amounts of funding received by digital payments startups and government support goes on to show the immense interest in this space.

20. What is the status of collaboration vs disruption in your jurisdiction as between fintechs and incumbent financial institutions?

Incumbent financial institutions are embracing the disruptive changes introduced by fintech and entering into partnerships to expand the range of services offered to their customers and respond to customer demands. Significant collaborations have been witnessed between fintech enterprises and incumbent financial institutions across the digital payments landscape across India. PhonePe, a Flipkart Group company, and Yes Bank have partnered to launch a UPI based mobile payments app. A leading private bank in India, Axis Bank also recently acquired a digital payments company, FreeCharge to boost its exposure in the sector. Even, Google has collaborated with HDFC Bank, ICICI Bank and others to offer the Google Pay app and more recently, instant, pre-approved loans to customers to its users.

21. To what extent are the banks and other incumbent financial institutions in your jurisdiction carrying out their own fintech development / innovation programmes?

Numerous banks and other incumbent financial institutions in India are focusing on innovation in areas, such as artificial intelligence (AI), data analytics and blockchain. Institute for Development and Research in Banking Technology (IDRBT), is the research arm of RBI experimented with blockchain for various trade applications and published the results in a white paper titled “Applications of blockchain technology in banking and financial sector in India”. The white paper, concluded that blockchain is indeed a disruptive technology that can potentially revolutionize the financial industry. Amongst private players, ICICI bank had announced the development of a Stellar-based blockchain application for transactions in a closed network. Axis Bank has partnered with Ripple, to enable cross-border payment services. Thirty banks and NBFCs in India including State Bank of India, ICICI Bank, Axis Bank and Yes Bank have agreed to share corporate KYCs through Primechain Money, which is a blockchain consortium set up by financial technology firm Primechain Technologies.

22. Are there any strong examples of disruption through fintech in your jurisdiction?

Yes. Some key examples of disruption are as follows: (i) Digital only Banks, such as DBS Digibank, IDFC Digital Bank and Kotak Mahindra Bank's 811 Accounts are branchless paperless banks offering a smartphone enabled no-frills banking experience for typically higher interest rates on savings, (ii) Deployment of Chatbots for customer support by leading banks such as HDFC Bank, ICICI Bank and Axis Bank looking to automate customer support. (iii) Peer – to – Peer lending marketplaces such as Faircent have flourished since the RBI brought in regulations for this in 2017 (iv) Non-bank payment intermediaries such as Razorpay, Instamojo, MSwipe have made it much easier for merchants to accept digital payments.