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[Please See Annexure:R-3 to R-18, in Vol.II]

IN THE SUPREME COURT OF INDIA
ORIGINAL CIVIL WRIT JURISDICTION
WRIT PETITION (CIVIL) NO. 906 OF 2016

IN THE MATTER OF:

VIVEK NARAYAN SHARMA ..PETITIONER

VERSUS

UNION OF INDIA ..RESPONDENTS

COUNTER AFFIDAVIT ON BEHALF OF THE UNION OF INDIA

The Respondent no. 1 most humbly submits as under:

1. That the present Writ Petition (PIL) has been filed inter alia against Notification dated 08.11.2016 issued by the Respondent no.1 under which the existing series of the value of five hundred rupees (Rs. 500/-) and one thousand rupees (Rs. 1000/-) ceased to be legal tender with effect from 09.11.2016.

2. That the answering Respondent had earlier filed an affidavit dated 01.12.2016 before this Hon'ble Court, which may be treated as part and parcel of this affidavit.

3. That in furtherance to the aforesaid affidavit, the present affidavit is being filed on behalf of the Respondents in above captioned petition pursuant to the direction of this Hon'ble Court in order dated 16.12.2016 and connected petitions pending before this Hon'ble Court with regard to cancellation of legal tender character of Rs. 500 and Rs. 1000 bank notes. Copy of the order dated 16.12.2016 passed by this Hon'ble Court is being annexed herewith and marked as **ANNEXURE R-1 [PAGE 180 to 192]**

4. That it is submitted that vide Notification dated 8.11.2016, issued by the Ministry of Finance (Department of Economic Affairs), the Government of India, exercising powers conferred by sub-section (2) of Section 26 of the Reserve Bank of India Act, 1934 declared that the specified bank notes of denomination of then existing series of the value of five hundred rupees and one thousand rupees shall cease to be legal tender with effect from 09.11.2016 to the extent specified in the aforesaid Notification dated 08.11.2016.

5. That aforesaid notification as also subsequent actions came to be challenged before this Hon'ble Court as also other Hon'ble High Court across the country. This Hon'ble Court *was,* vide order dated 16.12.2016, pleased to admit all the writ petitions and further stay the proceedings of all other proceedings pending before any High Court. This Hon'ble Court further directed that no other Court shall entertain, hear or decide any writ petition/proceedings on the issue or in relation to or arising from the decision of the Government of India to demonetize the old notes of Rs. 500/- and Rs. 1000/ - as the entire issue is pending for consideration before this Hon'ble Court in the present proceedings. This Hon'ble Court further permitted the petitioners before the High Court(s) or any other Court in India in respect of proceedings already instituted on the subject matter to file intervention in the present proceedings. This Hon'ble Court further, after framing certain questions of law, was pleased to

direct that the matters be placed before a larger bench of five Judges.

6. That the answering Respondent had filed transfer petitions seeking transfer of the various writ petitions pending before the High Court. This Hon'ble Court, vide the aforesaid order dated 16.12.2016, was also pleased to issue notice in such transfer petitions and stayed the proceedings in the pending writ petitions before the High Courts.

7. That in the meanwhile, since the Parliament was not in session, the President of India was pleased to promulgate an Ordinance known as 'The Specified Bank Notes (Cessation of Liabilities) Ordinance, 2016', which was published on 30.12.2016 and brought in to force from 31.12.2016. It was necessary to promulgate the said Ordinance since it was incumbent on the Central Government to inter-alia have clarity and finality to the liabilities of the Reserve Bank of India as well as the Central Government arising from such Specified Bank Notes which had ceased to be legal tender.

8. That the aforesaid Ordinance provided for 'grace period' during which the specified bank notes can be deposited in accordance with the Ordinance. Clause 3 of the Ordinance however, provided that with effect from 31.12.2016, the specified bank notes ceased to be liabilities of the Reserve Bank under Section 34 of the Reserve Bank of India Act, 1934 and it shall cease to have guarantee of the Central Government under sub-section (1) of Section 26 thereof. The Ordinance made it further explicitly clear that this was notwithstanding anything contained in the Reserve Bank of India Act, 1934 and or any other law for the time being in force.

9. That the aforesaid Ordinance was replaced by the Specified Bank Notes (Cessation of Liabilities) Act, 2017 passed by the Parliament, which became Act after getting assent of the President on 27.02.2017 and was published in the Official Gazette on 28.02.2017. The aforesaid Ordinance was repealed under sec. 13(1) of the Specified Bank Notes (Cessation of Liabilities) Act, 2017 and the Act

was deemed to have come into force on 31.12.2017 by virtue of sec. 1(2) of the aforesaid Act.

10. That at the outset, it is most respectfully submitted that the present matter is solely within the province of economic policy. This step has been taken by the Government after due deliberations and is in accordance with law. It is well settled that unless the policy is unconstitutional or contrary to any law, the Courts are not to interfere with such economic policy.

11. That it is further most respectfully submitted that after some early issues, the entire policy has been eventually smoothly effectuated and the currencies have been appropriately remonetised. It is submitted that the Indian economy has already comfortably adjusted itself to the new scenario where the earlier series of Rs.500 and Rs.1000 had ceased to be a legal tender and fresh series of Rs.500 were issued and a new denomination of Rs.2000 has been introduced. It is submitted that in such a situation, the present matter, for all practical purposes, has

been rendered purely academic and infructuous and therefore, may accordingly be dismissed.

BACKGROUND AND MISCHIEF SOUGHT TO BE CURBED:

12. That it is submitted that the objective of the decision to cancel the legal tender character of high denomination bank notes of Rs.500 and Rs.1000 denomination w.e.f. the expiry of 8th November 2016 was to curb financing of terrorism through the proceeds of Fake Indian Currency Notes (FICN) and use of such funds for subversive activities such as espionage, smuggling of arms, drugs and other contrabands into India and for eliminating Black Money which casts a long shadow of parallel economy on India's real economy.

13. That FICN in circulation in higher denominations are comparatively larger as compared to those in other denominations. Use of FICN facilitates financing of terrorism and drug trafficking. Use of high denomination for storage of unaccounted wealth has been evident from cash recoveries made by law

enforcement agencies from time to time. FICN have been misused by terrorists and are known to facilitate generation of black money as well as hoarding of black money.

14. That three specific mischiefs, which had serious adverse impact on the Indian economy over the past years have been, (i) fake currency notes; (ii) storage of unaccounted wealth in the form of high denomination notes which happened to be fake in many instances; (iii) use of fake currency to finance subversive activities such as terrorism, etc.

15. It was found that fake currency notes of Rs. 500/- and Rs. 1000/- bank notes were in circulation in large numbers and it was difficult for the public in general to identify the genuine bank notes from the fake ones. The use of fake currency notes was causing adverse effect to the economy of the country. Further, it was found that high denomination bank notes were being used for storage of unaccounted wealth as was evident from the large cash recoveries made by law enforcement agencies. It was also found

that fake currency was being used for subversive activities such as drug trafficking and terrorism, causing serious damage to the economy and security of the country.

16. That currently, India is the second largest producer and consumer of currency notes. Circulation of bank notes has increased from 64.58 billion pieces to 90.27 billion pieces over last five years. The total amount of currency in circulation as on 08.11.2016 was Rs. 17.7 lakh crore which included Specified Bank Notes (SBNs) of Rs. 500 and Rs. 1000 amounting to Rs. 15.44 lakh crore and Rs. 2.33 lakh crore of Rs 100 and lower denominations.

17. That the data maintained by RiM had shown a steep rise in circulation of Rs. 1000 and Rs. 500 banknotes during preceding 5 years. The rise in circulation may be seen in the table below:

Denomination	**Circulation in 2011 (Billion Pieces)**	**Circulation in 2016 (Billion Pieces)**	**Percentage increase**
Rs. 2 & Rs. 5	11.12	11.63	4.59

Rs. 10	21.30	32.01	50.39
Rs. 20	3.02	4.92	63.05
Rs. 50	3.20	3.89	21.71
Rs. 100	14.02	15.78	12.51
Rs. 500	8.91	15.71	76.38
Rs.1000	3.02	6.33	108.98
Total	64.58	90.27	39.78

The growth rate of Rs. 500 and Rs. 1000 notes indicates two major threats viz., infusion of Fake Indian Currency Notes (FICN) and generation of black money.

18. That over the years, there have been reports from various quarters, which reflect upon the causes and the ill-effects of black money. There was need to eliminate the parallel economy or the shadow economy outside the GDP system.

19. That cash transactions do not leave any audit trail and therefore, act as conduit for black money. Elimination of black money will eliminate the long shadow of the parallel economy on our real economy and will be very positive for India's growth outlook. A parallel shadow economy corrodes and eats into the

vitals of the country's economy. It generates inflation, which adversely affects the poor and the middle classes more than others. It deprives Government of its legitimate revenues, which could have been otherwise used for welfare and development activities.

20. The ratio of currency in circulation (CIC) to Gross Domestic Product (GDP) has been 11% or more in the last five financial years beginning from 2011-12 to 2015-16. As per some reports such as BCG Global Payment Models 2015, Reserve Bank of Australia Annual Report 2014 and Euro Monitor Passport 2015, the Cash to GDP percentage ratio for India is approximately 11.55%, which is higher than the USA figure of 7.74%.Copy of the Report of the BCG Global Payment Models, 2015 is being annexed herewith and marked as **ANNEXURE R-2 [PAGE 193 TO 273]**

21. To bring transparency in payments made in the country, efforts have been taken to promote digital mode of payments through number of measures. As

per the Weekly Statistical Supplement (WSS), the notes in circulation as on November 4, 2016 stood at Rs.17, 74,187 crores. Roughly 86% of this value i.e. Rs.15,25,800 crore comprised of notes of denominations Rs.500 and Rs.1000. Copy of the Weekly Statistical Supplement no. 47 and 48 of Vol. 31 issued by the RBI is being annexed herewith and marked as **ANNEXURE R-3 [PAGE 274 TO 281].**

22. As per the Study Report on the 'The Cost of Cash in India' conducted by The Fletcher School, Tufts University, in collaboration with National Institute for Bank Management, Pune in 2014, 87% of all transactions in India were cash-based. The ratio of currency to GDP in India (12.2%) is higher than countries such as South Africa (3.9%), Brazil (4.1%), and Mexico (5.7%). A report by VISA indicates a high volume of cash transactions has positive correlation with percentage of shadow economy (estimated) to GDP. For India the figure is 26%. Copy of the Study Report on the 'The Cost of Cash in India' conducted by The Fletcher School, Tufts University is being

annexed herewith and marked as **ANNEXURE R-4 [PAGE 282 TO 547]**

23. <u>CBDT Report on Black Money, 2012:</u> The Committee was mandated to examine the existing legal and administrative framework to deal with the menace of generation of black money through illegal means. Relevant portions of the Report is being reproduced hereunder:

> "II CONCEPTS AND DEFINITIONS OF BLACK MONEY
>
> 2.1 There is no uniform or accepted definition of 'black' money. Several terms are in use — such as 'black money', 'black income', 'dirty money', 'black wealth', 'underground wealth', 'black economy', 'parallel economy', 'shadow economy', 'underground' or 'unofficial' economy. If money breaks laws in its origin, movement or use, and is not reported for tax purposes, then it would fall within the meaning of black money. The broader meaning would encompass and include money derived from corruption and other

illegal zvays — to include drug trafficking, counterfeiting currency, smuggling, arms trafficking, etc. It would also include all market based legal production of goods and services that are concealed from public authorities for the following reasons-

(i) to evade payment of taxes (income tax, excise duty, sales tax, stamp duty, etc);

(ii) to evade payment of other statutory contributions;

(iii) to evade minimum wages, working hours and safety standards, etc.; and

(iv) to evade complying with laws and administrative procedures.

2.2 There are three sources of black money — crime, corruption and business. The 'criminal' component of black money would normally include proceeds from a range of activities including racketeering, trafficking in counterfeit and contraband goods, forgery, securities fraud, embezzlement, sexual exploitation and prostitution, drug money, bank frauds and illegal trade in arms. The 'corrupt' component of such money would stem from bribery and theft by those holding public office - such as by grant of business, bribes to alter land use or to regularize unauthorized construction, leakages from government social spending programmes, speed money to circumvent or fast-track procedures, black marketing of price controlled services, etc.

2.3 The 'commercial' limb of black money usually results from tax evasion by attempting to hide transactions and any audit trail relating thereto, leading to evasion of one or more taxes. The main reason for such black economy is underreporting revenues / receipts / production, inflating expenses, not correctly reporting workers employed to avoid statutory obligations for their welfare. Opening of the economy permits contracts of all kinds — particularly for allocation of scarce resources such as mineral and spectrum — which, in the absence of transparent rules and procedures for licenses and non compliance of contractual obligations of the persons concerned, leads to increased generation of black money. In all the three forms of black money - 'criminal', 'corrupt' and 'commercial' – subterfuges are created which include false documentation, sham transactions, benami entities, mispricing and collusion. This is often done by layering transactions to hide their origin."

'III. CAUSES & METHODS ADOPTED FOR GENERATION OF BLACK MONEY, MOST PRONE SECTORS OF ECONOMY

Cash economy and use of counterfeit currency

3.25 'Cash' as an asset has its own demand. However, in large cash economies, such as India, counterfeit currency poses a major threat to the economy. Countries have attempted to check counterfeiting of currency notes, as it disrupts smooth commercial transactions and has a multiplier effect on mainstream economy.

India faces this problem, as immigrants become carriers for small amounts. The Indo-Bangladesh, Indo-Pakis tan and Indo-Nepal borders are targeted for this purpose by agencies inimical to the interests of India.

3.26 The demand for currency is determined by a number of factors such as income, price levels and opportunity cost of holding currency. Currency is also used as a store of value, particularly in countries with low inflation or large 'shadow' economies. As per the RBI Annual Report for 2010-11, there was acceleration in currency in circulation in 2010-11 owing to increased demand on account of economic growth, high inflation and low yield on deposits for most part of the year."

"3.29 India has a large cash economy due to dependence on agriculture, and existence of non-formal sector and insufficient banking infrastructure. Further, the RBI has attributed the growth and strength in the cash economy to factors like acceleration in per capita real GDP growth, commercialization of agriculture and urbanization and availability of higher denomination notes. In a recent judgement delivered by Hon'ble Kerala High Court LP.D. Abraham v. CIT (Central), Cochin Cross Objection 112/2008 in ITA 323/2008 dated 15.12.2008], the Court has suggested putting restrictions on possession and handling of cash above certain limits. In an earlier case, Hon'ble Supreme Court had also observed Rajendran Chingaravelu vs. UoI in CA No. 7914 of 2009; ORDER DATED November 24, 2009 (320 ITR 1), that "The nation is facing terrorist threats. Transportation of large sums of money is associated with distribution of funds for terrorist activities, illegal pay offs, etc. There is also rampant circulation of unaccounted black money destroying the economy of the country." Further, "Money which is drawn from a Bank and legitimately belonging to the carrier, may still be used for an illegal purpose, - say to pay for a crime or to fund an act of terrorism. It may also be used for a routine illegal function - to make part payment of sale consideration for a property in cash, so that the full price is not reflected in the sale deed, resulting in evasion of stamp duty and registration charges and evasion of payment of capital gains and creation of black money. The carrying of such a huge sum, itself gives rise to a legitimate suspicion." The Court concluded that, "Any bona fide measures taken in public interest, and to provide public safety or to prevent circulation of black money, cannot be objected as interference with the personal liberty or freedom of a citizen."

"3.32 Demonetization of high denomination currency notes is believed to be one of the methods to 'kill' the extant black economy, and to curb the generation of black money."

"VI. MEASURES TO TACKLE BLACK MONEY

6.13 Government may consider amending existing laws (The Coinage Act 2011, The Reserve Bank of India Act 1934, FEMA, IPC, Cr PC, etc.), or enacting a new law, for regulating the possession and transportation of cash, particularly putting a limitation on cash holdings for private use, and including provisions for confiscation of cash held beyond prescribed limits. This would address the concerns expressed by various courts, and also the Election Commission of India for reducing the influence of money power during elections."

Copy of the CBDT Report on Black Money, 2012 is being annexed herewith and marked as **ANNEXURE R-5 [PAGE 548 TO 782]**

24. White Paper on Black Money: The Ministry of Finance, Department of Revenue, Central Board of Direct Taxes, New Delhi issued a White Paper on Black Money in May 2012 providing a comprehensive view on the prevailing menace of black money in the Indian economy. The relevant portions of the White

Paper, discussing the issue of Cash Economy in India under Chapter V - The Way Forward, are reproduced hereunder:

"B.4 Cash Economy

5.2.24 Cash has always been a facilitator of black money since transactions made in cash do not leave any audit trail. So far, efforts to regulate and control cash transactions have been constrained due to two reasons. The first is that the poor have to deal in cash, particularly in the rural sector, and accordingly payments on account of labour wages or those made to rural artisans and institutions need to be made in cash. Second, the costs of transaction imposed by any regulations are likely to spread across the economy and affect both consumers and producers, thereby leading to resistance and lack of support for such a move.

5.2.25 However, given the primary importance of cash in relation to both generation and use of black money, there is no alternative but to target cash transactions in a way that will not affect those complying with the law, while making it difficult for those intending to generate and utilise black money. This will require keeping fairly high transaction limits and exempting those with a reasonable audit trail at either end of the transactions. Further work needs to be done in this regard in future by way of legal curbs and regulations that can restrict the generation and flow of black money within the economy.

5.2.26 As of now there are no legal restrictions to keeping very large amounts of cash with oneself or transporting it from one place to another. One is neither required to report it nor provide any explanation for it. There have been suggestions that the government may consider amending existing laws, including the Coinage Act 2011, The Reserve Bank of India Act 1934, FEMA, and the

Indian Penal Code, or enacting an entirely new statute aimed at regulating the possession and transportation of cash above a particular threshold limit. This may include creating a limitation on cash holdings for private use, as well as provisions for confiscation of cash held beyond such prescribed limits. However, such laws need a broader political consensus to emerge for their acceptance in Parliament.

5.2.27 Another important measure in this regard could be the promotion of banking channels including use of credit and debit cards, since they leave adequate audit trails and hence disincentivise black money generation. The opposite is true of trade practices that block the audit trail, such as cheque discounting, which can be discouraged applying the same logic. With electronic transfer facilities being available to trade, one can foresee this as one of the major thrusts towards strengthening accountability and discouraging unaccounted activities."

In its Foreword to the White Paper, the then Finance Minister noted as under:

"There is no doubt that manifestation of black money in social, economic and political space of our lives has a debilitating effect on the institutions of governance and conduct of public policy in the country. Governance failure and corruption in the system affect the poor disproportionately. The success of an inclusive development strategy critically depends on the capacity of our society to root out the evil of corruption and black money from its very foundations. Our endeavour in this regard requires a speedy transition towards a more transparent and result oriented economic management systems in India."

The White Paper mentions that cash has always been a facilitator of black money since transactions made in cash do not leave any audit trail. It notes that black money has been estimated to have increased from 15%-18% of GDP to 19%-21% of GDP during 1975-76 to 1983-84. It also quotes the estimates made by the World Bank in July, 2010 wherein the size of the shadow economy for India has been estimated at 20.7% of the GDP in 1999 and rising to 23.2% in 2007. Copy of the White Paper on Black Money in May 2012 is being annexed herewith and marked as **ANNEXURE R-6 [PAGE 783 TO 1185]**

25. <u>Special Investigation Team on Black Money appointed by this Hon'ble Court:</u>

a. In Ram Jethmalani v Union of India, (2011) 8 SCC 1, this Hon'ble Court was pleased to constitute a Special Investigation Team with regard to investigation of black money and passed the following directions:

"57. In light of the above we herewith order:

(i) That the High-Level Committee constituted by the Union of India, comprising of (1) Secretary, Department of Revenue; (ii) Deputy Governor, Reserve Bank of India; (iii) Director (IB); (iv) Director, Enforcement; (v) Director, CBI; (vi) Chairman, CBDT; (vii) DG, Narcotics Control Bureau; (vii) DG, Revenue Intelligence; (ix) Director, Financial Intelligence Unit; and (x) JS (FT & TR-I), CBDT be forthwith appointed with immediate effect as a Special Investigation Team;

(ii) That the Special Investigation Team, so constituted, also include Director, Research and Analysis Wing;

(iii) That the above Special Investigation Team, so constituted, be headed by and include the following former eminent Judges of this Court:

(a) Hon'ble Mr Justice B.P. Jeevan Reddy as Chairman; and (b) Hon'ble Mr Justice M.B. Shah as Vice-Chairman; and that the Special

Investigation Team function under their guidance and direction;

(iv) That the Special Investigation Team, so constituted, shall be charged with the responsibilities and duties of investigation, initiation of proceedings, and prosecution, whether in the context of appropriate criminal or civil proceedings of

(a) all issues relating to the matters concerning and arising from unaccounted for monies of Hassan Ali Khan and the Tapurias;

(b) all other investigations already commenced and are pending, or awaiting to be initiated, with respect to any other known instances of the stashing of unaccounted for monies in foreign bank accounts by Indians or other entities operating in India; and

(c) all other matters with respect to unaccounted for monies being stashed in foreign banks by Indians or other entities operating in India that may arise in the course of such investigations and proceedings.

It is clarified here that within the ambit of responsibilities described above, also lie the responsibilities to ensure that the matters are also investigated, proceedings initiated and prosecutions conducted with regard to criminality and/or unlawfulness of activities that may have been the source for such monies, as well as the criminal and/or unlawful means that are used to take such unaccounted for monies out of and/or bring such monies back into the country, and use of such monies in India or abroad. The Special Investigation Team shall also be charged with the responsibility of preparing a comprehensive action plan, including the creation of necessary institutional structures that can enable and strengthen the country's battle against generation of unaccounted for monies, and their stashing away in foreign banks or in various forms domestically.

(v) That the Special Investigation Team so constituted report and be responsible to this Court, and that it shall be charged with the duty to keep this Court informed of all major developments by the filing of periodic status reports, and follozving of any special orders that this Court may issue from time to time;

(vi) That all organs, agencies, departments and agents of the State, whether at the level of the Union of India, or the State Government, including but not limited to all statutorily formed individual bodies, and other constitutional bodies, extend all the cooperation necessary for the Special Investigation Team so constituted and functioning;

(vii) That the Union of India, and where needed even the State Governments, are directed to facilitate the conduct of the investigations, in their fullest measure, by the Special Investigation Team so constituted and functioning, by extending all the necessary financial, material, legal, diplomatic and intelligence resources, whether such investigations or portions of such investigations occur inside the country or abroad;

(viii) That the Special Investigation Team also be empowered to further investigate even where charge-sheets have been previously filed; and that the Special Investigation Team may register further cases, and conduct appropriate investigations and initiate proceedings, for the purpose of bringing back unaccounted for monies unlawfully kept in bank accounts abroad."

Copy of the judgment of this Hon'ble Court in Ram Jethmalani v Union of India, (2011) 8 SCC 1 is being annexed herewith and marked as **ANNEXURE R-7 [PAGE 1186 TO 1196]**

b. In furtherance to the aforesaid directions, the Special Investigation Team (SIT) was duly constituted by the Government of India vide notification dated 29.05.2014. Copy of the Central Government Notification F. No. 11/2/2009-Ad. E.D. dated 29.05.2014 constituting SIT is being annexed herewith and marked as **ANNEXURE R-8 [PAGE 1197 TO 1203]**

c. The SIT has, while relying upon the aforesaid CBDT Report and White Paper, recently submitted its Fifth Report on 14.07.2016. Relevant portions of the same are reproduced hereunder:

"5. Limit for cash holding:-

(i) For successful implementation of restricting accounted/unaccounted cash transaction, it is absolutely necessary to have reasonable restriction in holding cash and to fix the limit of cash holdings. It is known fact that a number of persons are holding cash of lacs of rupees and such holding is undoubtedly unaccounted.

(iv) In the Second Report, SIT suggested that,

"for regulating the possession and transportation of cash, particularly putting a limitation on cash holdings for private use and including provisions for confiscation of cash held beyond prescribed limits, provision in the Act should be made Further, for holding of cash / currency notes also, there should be a limit, by prescribing a reasonable threshold, may be Rs.10 lacs or Rs.15 lacs.This would control holding of unaccounted money to a large extent. This would also control transfer of unaccounted cash from one destination to other, which at present is rampant, may be by Angadias or by other means."

Law should provide that if any cash amount more than the prescribed limit is found, the same shall vest in the Union of India.

(viii) In the Fourth Report, the issue with regard to limit on cash holding was reiterated by referring to the afore-quoted suggestions made in earlier reports. SIT, in the Fourth Report, observed and suggested that, "It appears that for taking decision, there is inordinate delay on the part of the Department. It should be realized that in almost all cases of illegal transactions, cash is used. At present, cash is transferred from one city to other only by telephonic call. If there is restriction on holding cash, dealing in black money would be to a large extent restricted. It is reported that in some cases, large amount has been found from some officers as corruption amount. Similar is the case for the election purpose, real estate dealing, etc."

7. Suggestions:

....

Limitation on cash holding would have its deterrent effect. Persons holding more unaccounted money would like to disclose the unaccounted money as per the "Income Declaration Scheme (IDS)" which begins from 01st June, 2016 for such disclosure."

Copy of the PIB Press Release dated 14.07.2016 along with the extracts of the Fifth Report of the SIT dated 14.07.2016 is being annexed herewith and marked as **ANNEXURE R-9 [PAGE 1204 TO 1205]**

26. There were certain other issues related to high denomination bank notes. Increase in circulation of bank notes of denominations Rs.500 and Rs.1000 vis-à-vis that of Rs.50 and Rs.100 for preceding 5 years (as per RBI data) had shown a steep rise for the two highest denominations i.e. 76.38% for Rs. 500 and 108.98% for Rs. 1000. Further, as per the data available in the Economic Survey for 2014-15 and 2015-16, the size of the economy has grown less than 30% from 2011-12 to 2015-16. Though inflation may be another reason for enhanced circulation of such notes but the level of growth, even incorporating inflation during 2011-2016, does not explain the increase of circulation of high denomination notes, to the extent mentioned above.

27. Therefore, in view of the menace posed before the country on account of counterfeit notes and activities related to it, and the advantages that likely

to accrue to the country if the legal tender character is withdrawn from Rs. 500 and Rs. 1000, this scheme was introduced. It was felt that the withdrawal of existing high denomination bank notes will curb funding of terrorists with the proceeds of FICN and use of existing FICN network for subversive activities. It will eliminate Black Money, which casts a long shadow of the parallel economy on our real economy. The poor and middle class, who are worst sufferers due to black money, will be benefited. It will help reduce tax avoidance and bring more transactions into the formal economy.

28. That it is relevant to note that the earlier exercise of demonetization undertaken in 1978 declared that the specified high denomination notes cease to be legal tender in payment or on account at any place. The Act was eventually upheld by this Hon'ble Court. Copy of the High Denomination Bank Notes (Demonetization) Ordinance, 1978, is being annexed herewith and marked as **ANNEXURE R-10 [PAGE 1206 TO 1233]**

A true copy of the High Denomination Bank Notes (Demonetization) Act, 1978 and judgment of this Hon'ble Court in Jayantilal Ratanchand Shah v Reserve Bank of India, (1996) 9 SCC 650 is being annexed herewith and marked as **ANNEXURE R-11 [PAGE 1234 TO 1267]**

RATIONALE BEHIND DEMONETISATION, ITS IMPLEMENTATION, PROBLEMS FACED BY GOVERNMENT DURING IMPLEMENTATION, PROBLEMS FACED BY THE PUBLIC AND STEPS TAKEN BY THE GOVERNMENT TO OVERCOME SUCH PROBLEMS

29. That in the last few years, the Reserve Bank, in consultation with the Government of India, had been working on introduction of new series of banknotes. It included changes for improving existing security features, introduction of new security features and new design features including new color scheme and new sizes, besides a new theme. The primary objective behind this entire exercise is to secure our banknotes against counterfeiting.

30. That the Reserve Bank had also embarked since January 2014 on a programme to withdraw all the notes issued before the year 2005 (withdrawal of old series notes periodically is a standard international practice followed by the note issuing authorities). In parallel, Government of India had been taking several steps to curb black money and combat terrorism. There were reports by intelligence and enforcement agencies that availability of the then existing high denomination banknotes made it easier for black money hoarders and counterfeited notes in high denominations were being used for terrorist financing.

31. The Government of India and the Reserve Bank considered that the introduction of new series of notes could provide a very rare and profound opportunity to tackle all the three problems of counterfeiting, terrorist financing and black money by demonetizing the banknotes in high denominations of Rs 500 and Rs 1000 or by withdrawing legal tender status of such banknotes.

32. The Government of India, therefore, on 07.11.2016, advised the Reserve Bank that to mitigate the triple problems of counterfeiting, terrorist financing and black money, the Central Board of the Reserve Bank may consider withdrawal of the legal tender status of the notes in high denominations of Rs 500 and Rs 1000. It was advised in that letter that cash has been a facilitator of black money since transactions made in cash do not leave any audit trail. Elimination of black money will eliminate the long shadow of the ghost economy and will be positive for India's growth outlook. They also observed that in the last five years, there has been an increase in the circulation of Rs 500 and Rs 1000 notes with an increasing incidence of counterfeiting of these notes. There have been widespread reports of the usage of FICN for financing of terrorism and drug financing. The Fake Indian Currency Notes have their origin in a neighboring country and pose a grievous threat to the security and integrity of the country. Hence, the Government recommended that the

withdrawal of the legal tender character of these notes is apposite. The Government of India advised the Bank to place these matters immediately before the Directors of the Central Board of the Reserve Bank of India for consideration in terms of the provisions of Section 26(2) of the Reserve Bank of India Act, 1934.

33. That the Central Board of the Reserve Bank met on 08.11.2016 to consider the Government's advice. The Board was informed that a summary measure with high and lasting impact in the form of withdrawal of legal tender character of these high denomination bank notes to contain the menace of counterfeit notes was proposed by the Government. It was also presented that such a proposal could not have come at a more opportune time than coinciding with the introduction of the MG(new) series of notes; with these, the existing banknotes can be summarily withdrawn, and the new design notes with more counterfeit resistance features be introduced. Thereafter, Government of India, on the

recommendations of the Central Board of the Reserve Bank, withdrew the legal tender status of banknotes of Rs 500 and Rs 1000 denominations effective midnight of 08.11.2016.

34. Since secrecy and confidentiality were the critical requirements of this decision making process, preparations for arranging bank notes of new series in full measure was impossible. Therefore, when scheme started the demonetized bank notes could be exchanged with new available bank notes along with the continuous supply being made from the bank note printing presses. Reasonable restrictions on withdrawal were put in place based on the availability of stock of currency notes of various denominations, past utilisation pattern and considering the needs of the common persons so that hardships are minimised, keeping in view equitable distribution of available cash. These restrictions were only on cash withdrawals. There were no restrictions or limits on non-cash modes of withdrawals like cheques, RTGS, NEFT, cards, mobile banking, internet banking etc.

35. That the GOT notification dated 08.11.2016 envisaged operation of the exchange scheme with the Reserve bank and specified banks along with post offices as primary agencies for withdrawal of the SBNs within limits on cash withdrawals both from ATMs and counters. Arrangements were also made to distribute cash through the Banking Correspondents(BCs) and the Point-of-Sale(PoS) terminals.

36. Operation of the Scheme: Exchange for cash: The initial limit of Rs. 4000 per person, was increased to Rs.4500 and later lowered to Rs.2000 and stopped altogether at 'bank 'branches / post offices with effect from 25.11.2016. However, the exchange facility continued at RBI Offices upto 30.12.2016.

37. Deposit of SBNs into accounts: SBNs were permitted to be deposited into the accounts without any limit. However, limits were placed on deposits into Jan Dhan Yojana accounts. Later, deposits into the credit of loan accounts were also permitted.

38. Cash withdrawal limits: Cash withdrawal limits were set initially at Rs.10,000 per account subject to weekly limit of Rs.20,000/-. The day limit was withdrawn and weekly limit was enhanced to Rs.24,000/- on November 13, 2016 including the ATM withdrawals of Rs 2,500 per day. The daily limit of withdrawal from ATMs was subsequently increased (within the overall weekly limits specified) with effect from January 01, 2017, to Rs 4500/- per day per card and further to Rs. 10,000 per day per card with effect from January 16, 2017. Cash credit/overdraft and current account holders were allowed a withdrawal limit of Rs 50,000 per week, which was increased to Rs. 1 lakh on January 16, 2017. These limits are not applicable to cash withdrawal by a bank, Post Office, Money changers operating at International airports and operators of White Label ATMs. Cash withdrawal up to Rs 2.5 lakhs was also permitted on grounds of marriage. Government Departments were allowed to draw cash beyond the stipulated limit only on production of evidence justifying their cash

requirements. Withdrawals of deposits made in current legal tender notes on or after November 29, 2016 were allowed beyond the current limits. With a view to ensure improvement in cash supply in the rural areas, the banks were advised to supply at least 40% bank notes to the rural areas.

39. Measures to mitigate the impact on certain segments of public: The Government permitted use of SBNs for several exempted type of transactions such as for booking bus, train and air tickets, for treatment at government hospitals, for purchase of medicines from government medical stores, for purchase of petrol! diesel, for buying groceries/ vegetables and milk at government run booths! stores etc. The list, limits and period were modified from time to time keeping in mind the situation, which was being monitored round the clock. Further, deposit of SBN was also allowed (till December 30, 2016) under the Pradhan Mantri Garib Kalyan Deposit Scheme (PMGKDS), 2016. Several facilitation measures like waiver of ATM charges for all

transactions, deployment of Micro ATMs near village Panchayat Offices, use of mobile vans to provide exchange for people in remote/ unbanked areas, introduction of special category of PPLs for merchants with higher domestic transfer limits and enhancement in the undertaken.

In order to avoid inconvenience to road users, collection of user fees was suspended from midnight 08.11.2016 till midnight 02.12.2016. Upon resumption of collection of user fees, road users were provided with the option to pay users fees with old denomination notes of Rs. 500 and Rs. 1000 till 15.12.2016.

40. <u>Measures to meet farmers' requirements:</u>

a. Usage of specified banknotes in the Rs. 500 denomination allowed for making payments towards purchase of seeds and fertilizer from the centres till end of the scheme, etc.

b. Drawals upto Rs 25000/- per week in cash allowed from their loan (including Kisan Credit Card limit) or deposit accounts.

c. Traders registered with APMC markets / mandis permitted to draw up to Rs 50,000/- from their current accounts.

d. Currency chests advised to ensure adequate cash supply to the DCCBs/ RRBs.

e. Opening accounts (in a camp mode) for plantation workers, etc.

f. Prevention of abuse of PMJDY accounts through limits on withdrawals.

g. Initially, an additional 60 days time was given to borrowers of regulated entities to repay their dues on loans and thereby avoid NPA classification. This relaxation extended for another 30 days.

41. <u>ATM Recalibration:</u>

a. The Reserve Bank of India constituted a Task Force on 14.11.2016 for the recalibration and reactivation of ATMs for dispensing the Mahatma Gandhi (New) Series Banknotes of Rs.500/- and Rs.2000/-. The Task Force comprised representatives from Government of India (Ministry of Finance and Ministry of Home Affairs), four banks with largest ATM network (State Bank of India, Axis Bank, ICICI Bank and HDFC Bank), National Payments Corporation of India, Chief General Manager, Department of Currency Management, RBI and Chief General Manager, Department of Payment and Settlement System, RBI (Member Secretary).

b. The Task Force decided that the recalibration work of around 2.18 lakh ATMs in the country be taken up in mission mode so as to complete the process by the end of November 2016.The Task Force decided that a Common Action Plan (CAP) for recalibration of ATMs shall be drawn by the Original Equipment Manufacturers (OEMs) and

Cash Replenishment Agencies (CRAs). Based on the above decision, the OEMs, CRAs and Managed Service Providers (MSPs) set up a control room with representatives from all the vendor entities being present. The Task Force was monitoring the progress in targets and their achievements in ATM recalibration on a daily basis.

c. As a result, nearly 1.80 lakh ATMs were recalibrated by November 30, 2016. Nearly 1.98 lakh ATMs had been recalibrated by January 4, 2017.

d. As per the data available as on 15.05.2017, around 2.08 lakh ATMs had been recalibrated which accounted for 93% of ATMs as on April 30, 2017.

e. The recalibration of remaining ATMs could not be taken up within this time period for various reasons such as - ATMs located in remote areas, being non-operational /under repairs, pending bank approvals etc.

STEPS TAKEN BY THE GOVERNMENT TOWARDS A CASHLESS ECONOMY:

42. Cashless economy describes an economic state whereby financial transactions are not conducted with money in the form of physical banknotes or coins, but rather through the transfer of digital information (usually an electronic representation of money) between the transacting parties.

43. The world is experiencing a rapid and increasing use of digital methods of recording, managing, and exchanging money in commerce, investment and daily life. Transactions which would historically have been undertaken with cash are often now undertaken electronically.

44. India has much higher cash to Gross Domestic Product (GDP) ratio than most of major developing and developed economies. India's large informal

economy is a major factor in the dominance of cash in day-to-day transactions.

45. Key Advantages of Cashless Economy:

a. Convenience for Residents: Cashless ecosystem, with cashless payment and receipt modes is highly convenient for making and receiving payment for everyone with no hassle to carry cash and will also mitigate the risk of loss of money.

b. Better Management of Funds: Using electronic modes, automated accounting, easier to manage funds, expenditure and revenues and ensure controlled budget implementation for individuals, businesses and Government departments.

c. Eradication of Black or unaccountable money: All cashless transactions are above ground, visible, traceable, accountable and thus taxable. So they are taxable (less black money) and also encourage people to transact legally and pay taxes.

d. Increase in Tax Collections: Tax collections will increase significantly and that revenue can be used for the benefit of society - building infrastructure, helping poor and less privileged people, education, health care and other essential activities. It can be used to lift Indians out of poverty and also fuel economic growth.

e. Reduction of Tax Rates: As the result of higher tax collection, tax rates can be reduced as tax net becomes wider with higher number of tax payers.

f. No Middle Man in Social Benefit Transfers: Any social benefit to poor and needy people can be done through direct bank transfers without any inclusion of middle men and their siphoning off the aid and exploiting the poor. It also becomes necessary that after receipts of payments electronically by residents below the poverty line there are enough avenues for spending funds electronically, especially small value transactions.

g. Control on Terrorism Funding Activities: It will be difficult to have counterfeit currency and / or support criminal activities and terrorism.

h. Actual Fund Revenue and Expenditure Records: Much better data of India's GDP including informal and service sector to understand what sectors are growing and where support is needed.

i. Less Cash Minting Costs: Usage of digital payments will result into less need to print paper currency and replace it thereby reducing associated costs.

j. Reduction in Friction of economy with No Unused cash: Funds stored with banks as savings accounts, deposits or investments can be used for productive use by investing in public and private sector by their banks instead of wealth lying unused as stacks of currency bills hidden under mattresses and in cupboards.

k. Digital payment methods bring transparency in the system and help track transactions, thus reducing leakages in the welfare schemes.

l. Digital payments reduce the cases of tax evasion and broaden the tax net.

m. The total cost of cash to the Indian economy is estimated to be Rs. 200 billion. The cost is borne by the customers, banks and financial institutions and by the Government. A move to digital economy lowers cost associated with printing, handling and transportation of the currency notes and opportunity cost of time spent in collecting cash. The security threat associated with handling cash is eradicated in case of digital modes of payment.

n. Digital payment modes increase financial inclusion and help reach the unbanked population at a much faster pace without the need for establishing physical infrastructure.

o. Indian society being a predominantly patriarchal society, finances of the house are handled and sometimes mishandled by the male members. Digital payment modes increase female participation by enabling the benefits of the schemes designed for their well-being and reach them directly. This results in empowerment of women.

p. Digital society with better transaction records of individuals and higher availability of capital with the banks makes access to credit easier. This not only helps in improving the living standards of people but also strengthens the financial system by early detection of non-performing assets.

46. The users prefer digital transactions to cash transactions for a variety of purposes. Some of the factors are as listed below:

a. Ease of completing payments - The payment service providers (PSPs) are working towards making payments easier and faster for the end customer. Starting with cleaner user interfaces to one click payments to multiple loading and payment options, digital payments eliminate the need to carry cash and the hassles one has to undergo for getting change. The ease of making payments through UPI has boosted its usage 100 times since its launch in August, 2016.

b. Faster transfer of funds - Fund transfers are instantaneous and safer when done through digital modes.

c. Tracking of expenses - Expense tracking becomes earlier with the transaction history and user friendly dashboard functionalities provided by the PSPs.

d. Easy refunds - With the boom in the e-commerce industry, order returns and cancellations and subsequent refund of transaction amount have become a part and parcel of the daily urban life. Transactions made through digital payment modes provide quick and easy refunds to the source of fund.

47. With the increase in merchant adatation, the use of the new age modes of a further innovation as competition intensifies in the digital payments area. Social media payments is a new phenomenon and digital payments are permeating into the lives of the common man.

48. Cashless economy is based upon four pillars and three building blocks:

a. <u>Availability of Easy To Use Systems for Cashless Transactions:</u> Government has to ensure that residents and business have 'Easy to Use' options for electronic payments.

b. <u>Penetration of Banking Infrastructure at the Last mile:</u> For achievement of goal of Casifiess economy, it is important that every resident is included in the formal financial system and have convenient access to banking infrastructure especially residents at the bottom of the pyramid.

c. <u>Financial and Technical Literacy Levels to Use Cashless Modes:</u> In order to ensure that each segment of users is able to complete digital transactions securely, it becomes critical that Government ensures availability of adequate financial literacy channels for users.

d. <u>Government's Focus and Regulatory Support for Promotion of Cashless modes:</u> The regulations may facilitate promotion and incentivize the usage of electronic modes and should ensure that there are sufficient security measures and support to banks for secure banking environment to ensure high trust levels in banking. The Three building blocks, Security and Confidentiality, Quality Connectivity and Multi modal Electronic payments should be ensured for qualitative, accurate, timely and transparent digital payments

49. That the Digi Dhan Abhiyaan was undertaken to get people and merchant onboard digital platform through CSC SPV of the Ministry of Electronics and information Technology. Starting from 04.12.2016, 58.6 lath people and 1.60 lakh merchants were enabled till 22.12.2016.

50. That the Digi Shaala, an education channel, was initiated from 09.12.2016 to educate people regarding various facets of digital payments. The channel is available on DD Free Dish which caters to nearly 2-2.5 crore rural households.

51. That the CashlessIndia.gov.in has been launched on 09.12.2016 to provide official authentic information regarding various digital payment systems.

52. That the National Institute of Electronics and IT (NIELIT) conducted workshops and reached out to its student community- approx. 3 lath students! merchants were promoting digital payments.

53. That the Software Technology Park of India (STPI) has been conducted workshops and reached out of 37 lath employees of IT sector promoting digital payments.

54. That the Digital Payments Division for Cyber Security was set up in Ministry of Electronics and Information Technology (MeitY)/ Certi-In on 13.12.2016.

EFFORTS OF DIFFERENT MINISTRIES IN THE GOVERNMENT OF INDIA:

55. That it is most respectfully submitted that all the Ministries were asked to encourage employees to use debit! credit card for payments in an attempt to move towards cashless economy. The Government on 19.12.2016 had announced benefit of lower rate of Income Tax on digital turnover for small businesses up to a turnover of Rs. 2 crore. The Government of India, including the Ministry of Civil Aviation has been constantly endeavoring to promote cashless transactions for a seamless digital experience to all the stakeholders in the civil aviation sector. In this

regard, steps taken! being taken by various Ministries! Departments of the Government of India have been summarized in the following paragraphs.

56. Ministry of Urban Development: The Ministry of Urban Development has taken measures to promote e-payments by providing suitable incentives for digital payments. Some of the measures taken by the Organizations under the Ministry of Urban Development are as follows.

a. <u>Delhi Development Authority (DDA)</u>

i. Online payment facilities for Land and Housing Department has been on since last one year on DDA website www.dda.org.in. All payments in the Housing A/c Wing are made through e-payment mode. Steps are being taken to bring Credit & Debit cards also.

ii. The salary and remuneration of staff, pension and medical claims (in most cases) are paid through e-payments.

iii. Two training programmes have been organized to promote and create awareness in the staff in respect of various modes of digital payments to the DDA employees and others.

iv. DDA has provided a hyperlink "Digital payments" on the website of DDA (www.dda.org.in) which is directly linked with Awareness material uploaded on NITI Aayog's website for the awareness of the DDA Employees and its other Stakeholders.

b. **Directorate of Estates**

i. It has been decided that w.e.f 01.01.2017 all payments and receipts would be done only through digital options and the office will not accept any cash/cheque. Allottees/ applicants would however be at liberty to deposit the amount online or by cash/cheque directly to the bank and obtain online generated challan.

ii. The office organized an awareness programme on digital payments on 23.12.2016 for its officers and staff.

c. Directorate of Printing

i. All payments to the officers, staff and vendors are made by the Directorate online. Also, most of the clients/ Ministries/ Departments make payment for printing job through online transfer. In order to make payment of salary and other payments to employees to Government of India Presses under this Directorate, all the Managers/ Officers-in charge have been directed to encourage all the members of staff to take salary online. They have also been advised to collect mandate forms from employees who are drawing salary in cash.

d. Land & Development Office

i. All the payments by the office are made digitally. Insofar as receipts are concerned, these are received the office and the bank through cheque/draft. The office is making arrangement to discontinue Cheque/ draft payments and take payments digitally only.

ii. All the payments by the office are made digitally. In so far as receipts are concerned, these are received in the office and the bank through cheque/ draft. The office is making arrangement to discontinue Cheque/draft payments and take payments digitally only.

iii. All out efforts are being made to bring all beneficiaries who are lessee of properties on the digital platform. They are being encouraged to make payments digitally. Suitable clause has been inserted in the demand letter.

iv. The staff is continuously being made aware in respect of digital payment.

e. <u>Central Public Works Department</u>

i. As regards payments and receipts, payments to contractors are being made through electronic payment mode through authorized banks, cash portion of EMD of tenders are received and refunded electronically and salary and allowances to employees are also paid electronically.

ii. Instructions have been issued for identification of groups, beneficiaries, activities where digital payments can be introduced in lieu of physical payments.

iii. In regard to promotion of digital payments amongst the target groups and beneficiaries instructions have been issued to all field offices of CPWD.

iv. Instructions for promotion of Digital Payments in CPWD in partnership with Banks have been issued to all field offices.

v. Payments to the contractors, suppliers etc. from CPWD divisions are now made electronically through PFMS portal implemented by the O/o CCA, MoHUA/CGA, MoF from 01.07.2017 which is integrated with authorized bank of CPWD.

f. National Institute of Urban Affairs

i. The institute is taking steps to ensure that al payments to staff are made digitally.

57. Ministry of Road Transport and Highways:

a. Ministry of Road Transport and Highways with its flagship ETC programme has enabled road users to pay user fees through obboard RFID tags (FASTags) by incentivizing road users to opt for the same with a cashback of 10% for the FY 2016-17 and 7.5% for the FY 2017-18.

b. Further, to promote road users to participate in the drive for a less cash economy, this Ministry has enabled payment of user fees through pre-paid payment instruments such as mobile-wallets and through debit/credit cards.

c. Adoption of digital payment of user fees among road users has shown an encouraging trend since Dec-16. Prior to this, 1.07 lakh FASTags were in use accounting for 0.02% user fees collected monthly through electronic mode, which has soared to 7 lac tages in use amounting to 20% of total user fees being collected electronically.

58. Ministry of Rural Development:

a. Mahatma Gandhi National Rural Employment Guarantee Scheme (MGNREGS): In the last 2 years, the Department of Rural Development has moved very swiftly in adopting electronic Fund Management System (eFMS) for its programmes. 95% of wages under MGNREGS go to the accounts of workers. In 22 States including 1 UT the money is transferred under the National eFMS directly from the Central Government to the account of the workers, once the Fund Transfer Order has been generated by the States. In rest of the States money is transferred to the accounts of the workers from the State Employment Guarantee Fund through the eFMS system. 8.57 crore (79%) of MGNREGS active workers have the Aadhaar details seeded into NREGASoft. 3.8 crore workers' accounts are on the Aadhaar details seeded into NREGASoft. 3.8 crore workers' accounts are on the Aadhaar Payment Bridge Systems (APBS). Through out concerned campaign for collecting consent of workers, the Department is attempting to have over 7 crore Aadhaar linked Bank accounts by March. Efforts have been made to speed up Aadhaar seeding in Bthar. Assam, Meghalaya and Jammu & Kashmir need to expedite the process. West Bengal and Odisha have reached about 70% Aadhaar seeding. All the others are above 80% and near universal Aadhar seeding for active workers. The Aadhaar Bank link facilitates Aadhaar enabled payment wherever Point of Sale (POS) machine or Micro ATMs are available. A number of MGNREGS workers also have RuPay Cards and feature phones for other forms of digital transactions.

b. Pradhan Mantri Awaas Yojana - Gramin (PMAY-G): Under the Rural Housing programme, PMAY-G as also the earlier Indira Awaas Yojana (IAY), 100% payments are made into Bank accounts of beneficiaries through a similar process of generation of Fund Transfer Order. Over 1 crore beneficiaries would be covered under PMAY-G. The Awaasoft-MIS for Housing Programme allows disbursal of funds to beneficiary Bank accounts from the single nodal account at the State level.

c. Deen Dayal Antyodaya Yojana: National Rural Livelthood Mission (DAY:NRLM): 29 lath Self Help Groups (SHGs) covering 3.44 crore women

SHG members are covered under the DAY:NRLM. SHGs received revolving fund and community investment fund into their accounts electronically. Bank loans to SHGs are also transferred electronically to these accounts or through the Panchayat level federations or other arrangement of on lending.. The challenge has been to link the SHG account to the individual accounts of the members of SHGs. The Department is also focusing on bringing small lending in SHGs to electronic forms of transfer. Programmes for financial literacy has been designed for SHG women and are going on in States. Pilot projects for financial inclusion through use of mobile phones have also been undertaken in 4 states. The pace of linking all 3.44 crore SHG Women to Aadhaar linked accounts and mapping these individual accounts with the SHG account is going on in full swing. Dual authentication to enable SHG account operations through Micro ATMs at village level will go a long way in bringing those components of SHGs' transactions which are outside formal Banking institutions at present to the digital.

d. National Social Assistance Programme (NSAP): the digitization of all beneficiaries under the National Social Assistance Programme for old age, widows, and disabled persons have been completed in all the States and UTs. Currently, efforts to link all digitized accounts with Aadhaar numbers is going on in the States. Over 55% beneficiaries have Aadhaar seeding and efforts are being made to provide for near universal coverage by March. Aadhaar linking of accounts of NSAP beneficiaries will facilitate cash drawal or Aadhaar enabled cashless transactions through P05 machines, with bio-metric readers and Micro ATMs available at the village level with PDS, Common Service Centres (CSCs), Banking correspondents and other Gram Panchayat level persons authorized in this regard.

e. Impact of Demonetization: Since all major programmes of the Department like MGNREGS and PMAY-G were already near universal IT/ DBT enables, reaching the money to the account of the worker or beneficiary was not an issue at all. In programmes like Pradhan Mantri Gram Sadak Yojana (PMGSY), contractors' payments to causal workers may have been temporarily affected. Analysis of the performance of the programmes indicates that whatever little impact demonetization may have had after 08.11.2016, has largely been covered up thereafter. Under MGNREGA, on an average over 50 lakh workers are coming to worksites every day and the total person days generated so far has already crossed 160 crores. This means that the confidence of workers in receiving payment for work done through their Bank accounts has been restored in large measure. It is also important to point out that historically work demand in September to November period has always been low especially in year of good monsoon. Under the PMAY-G and the IAY, the performance does not appear to have been affected so far. Under the IAY, 20.1 lath houses have been completed in the current year so far and statistics for November and December indicate no slowing down of the process of completion of houses. Similarly, under the PMGSY, over 28,800 km of roads have already been constructed in the current Financial Year so far. Over the last 15 days, the pace of construction has considerably picked up. The seasonality factor in PMGSY historically, has also confirmed that by middle of December the pace picks up and goes on till the end of Financial Year. In all the three programmes mentioned above while the targets for the year were very steep with 48,812 km (133 km per day) of PMGSY roads to be completed, 217 crore person days of MGNREGS work, and 33 lakh Rural Housing completion by March 2017, all the three are likely to be met fully by March. This shows that the overall impact on Rural Development programmes have not been very significant

f. Initiatives for Enabling Digital Payments in Rural India: After Video Conference with Chief Secretaries and District Magistrates under the Chairmanship of CEO, NITI Aayog, the Department of Rural Development had a detailed Video Conference with all the Principal Secretaries of Rual Development and followed up with a detailed request to all Chief Secretaries of States. A comprehensive Training Module on enabling digital payments in rural India has been made with NIRD & PR, Hyderabad, as the nodal institution. The training of all master trainers at the State level has already been completed except in States like West Bengal, Uttarkhand and Goa (these State are also being covered up at the earliest). States in turn have started and many have completed their District/Block Resource Persons' training. The Department's effort is to train all the nearly 6 lakh Gram Rozgar Sewaks, Housing Programme functionaries, Livelihood Mission functionaries and Community Resources Persons of Livelihood Mission to reach out to our 10.88 crore active workers of MGNREGA, 1 crore identified beneficiaries of PMAY-G, 3.44 crore women members of SHGs by March 2017. We are confident of reaching out to most of these households by the end of January 2017. Training Module on Enabling Digital Payments in Rural India is available on our website.

g. With 3.8 crore MGNREGA workers already on the Aadhaar payment bridges account, large scale transactions through POS machines, with biometric readers and Micro ATMs has been made possible with simplification of Unstructured Supplementary Service Data (USSD), bio-metric reader with Android phone for Aadhaar enabled transaction, and simplification of Unified Payment Interface (UPI) which are now all at an advanced stage. The pace of enabling digital payments in rural India will go much faster. The workers and the beneficiaries of the Rural Development Department constitute a proxy for poverty in rural areas as these are the poorest households requiring States' support.

59. Ministry of Finance, Department of Expenditure:

a. The approval of the Union Finance Minister has been obtained that all payments including salary to Government employees shall be made through electronic mode only, subject to availability of banking facilities. Relevant provisions under Central Government Accounts (Receipt & Payment) Rules, 1983 are being amended to facilitate 100% payment including salary to all Central Government employees through electronic mode only. Section 44AD of the Income Tax Act, 1961 has been amended in the Finance Act 2017, to promote and encourage small unorganized business for digital transaction wherein the existing rate of deemed total income of eight percent has been reduced to six percent in respect of turnover arising out of digital transactions.

b. The relevant provisions under the Central Government Accounts (Receipt & Payment Rules) 1983 have been amended wherein all payments to Government servant, including salary payments, shall be made by electronically signed advices for direct credit to their bank accounts, subject to availability of banking facilities. Gazette notification to this effect has also been issued on 27.04.2017.

c. The threshold limit for payment to vendors/suppliers electronically has been lowered from Rs.25,000/- to Rs.5000/-. As on date for all payments beyond Rs.5000/- made by Central Government Ministries/Departments to its suppliers/vendors of Goods and Services, payment shall be made through electronic mode only.

d. Advisory has been issued to all Ministries/Departments to encourage its employees to make use of Debit Cards for personal transactions instead of cash.

e. Guidelines on the Accounting procedure have been formulated for payment of applicable MDR (Merchant Discount Rate) charges on Government dues below Rs.1 Lakh for taxes, non-taxes and other payments through Cards and Digital means and all Ministries! Departments have been directed to take necessary action on:

i. For all Utility Bill payments, customer should get 1% cash back, subject to certain ceiling to be decided by the Department. Cash back may also be provided in the form of discount. The expenses shall be borne by the Utility

Company. Nodal Ministry/ Department shall issue appropriate advisory in this regard to the State Governments for Utility services provided by Undertakings of State Government.

ii. All Convenience Fee/Charges for digital payments levied on customers by Ministries/Departments of the Union Government for various should be waived.

f. Promotion of payments through Cards and Digital means- implementation thereof.

i. Cabinet has approved various measures for promotion of payments through cards and digital means for incentivisation of digital transactions and removal of present disincentive for such transactions. Department of Economic Affairs vide their OM No. F No.-01/02/2015-Cy.II - Vol. V/278-371 dated 29th February 2016 has already issued detailed guidelines in this regard.

ii. In compliance of these directives of Cabinet, a package for promotion of digital and cashless economy has been announced vide press Note released on 08.11.2016 as per letter no. 10/3/2016-Cy.I of Secretary DEA. Controller General of Accounts, Department of Expenditure vide OM No. 1(1)/2006/ ECS/TA/325 dated 14.11.2016 has earlier issued certain guidelines towards payment of Govt. money through debit/credit cards and net banking facility.

60. **Ministry of Agriculture:**

a. Out of the budgetary allocation of Rs. 1060.50 crore made available for post-demonetisation relief measures, based on the demand received from NABARD, the Department has already released a sum of Rs.838.50 crore to NABARD, i.e., (i) towards provision of additional resources of Rs.660.50 crore for meeting the cost of interest waiver of 2 months (November and December, 2016) for crop loans disbursed by Cooperative Banks between 01.4.2016 and 30.09.2016; and, (ii) Rs.178 crore for meeting the cost of interest subvention and administrative cost to be paid to NABARD on account of short term borrowing to be made by them at prevailing market rate of interest for a sum uptoRs.20,000 crore for on-lending to Cooperative Banks at 4.5 percent rate of interest.

b. Post demonetization measures taken by Department of Agricultural Cooperation& Farmers Welfare: Consequent to the cancellation of legal tender character of old Rs.500 and Rs.1000 notes and the resulting difficulties faced by the farmers in encashing the cheques received against sale proceeds of their Kharif produce in the mandis and also constraints faced by them due to inadequacy of cash in carrying out Rabi operations and servicing the interests of the short term crop loans, especially in view of the restrictions imposed on Cooperative Banks, the Department of Agriculture, Cooperation and Farmers Welfare, Government of India has taken the following actions post demonetization in this regard.

i. In the aftermath of Demonetization, the Govt. decided that an additional grace period of 60 days for prompt repayment incentive @3% will be provided to such of the farmers whose crop loan dues fall due between 1.11.2016 to 31.12.2016 and if such farmers repay the same within 60 days from their due date in this period.

ii. The Department also moved a Cabinet proposal under Rule 12 of Government of India (Transaction of Business) Rules, 1961 seeking approval for relief measures for farmers. The Prime Minister approved the proposal of the Department on 20.12.2016 to grant interest waiver for two months (November and December, 2016) for all short term crop loan availed from Cooperative Banks between 01.04.2016 to 30.09.2016 and upfront deposit of the same in the accounts of the concerned farmers. Additional resources of Rs.660.50 crore were approved towards interest payment in the farmers' account.

iii. As part of the above Cabinet proposal, Hon'ble Prime Minister also approved provision of interest subvention at the rate of about 1.8% p.a. and 0.2% administrative cost of NABARD in 2016-17 on short term borrowing up to Rs.20,000 crore at market rate for onward lending to Cooperative Banks at 4.5% p.a. provided Cooperative Banks made available short term crop loans up to Rs.3.00 lakh to farmers at 7% p.ä. The Govt. approved provision of Rs.400 crore towards this proposal in 2016-17.

iv. Post-demonetization, the Department through its many organizations viz. Cooperative Banks, including Urban Cooperative Banks and Multi-State Cooperative Banks, RRBs, IFFCO, KRIBCO, NABARD, National Seed Corporation, Mother Dairy NAFED, Krishi Mandies, etc. organized training and awareness camps for farmers, dealers and retailers and disseminated information through posters and pamphlets in regional languages for promotion of cashless transaction, opening of Mobile accounts, use of RuPay card, Debit card, use of PoS (Point of Sale Machine), promotion of digital payment between farmers etc. Reportedly, IFFCO has since directed 250 of its Farmer Sale Centres of install PoS machines and tied up with Airtel to initiate mobile bank accounts for 5 crore active members of its 50000 committees. KRIBHCO tied up with ICICI and Yes Bank to install 61 PoS 50000 committees. KRIBHCO tied up with ICICI and Yes Bank to install 61 PoS machines at Farmers Service Centres/ fertilizer retail outlets. National Seed Corporation installed PoS machines in Lucknow and New Delhi at 12 of its 77 Sale counters and directed State Bank of India to install PoS at remaining sale counters. Facilities have been installed at all 77 sale counters to use UPI/e-Wallet through mobiles for purchase of seeds. At AMUL while 28 lath farmers supply milk only 11.5 lakh accounts were in operation and post demonetization 9.01 lath new account have been opened. Similarly only 500 booths of Mother Diary had facilities for cashless transactions earlier, which have been extended to remaining 603 booths; SBI cash card are accepted at 777 booths and it is reported that daily transactions worth Rs.35 lakhs are being conducted through pre-paid card and e-Wallet. NAFED has from earlier on been procuring pulses and oil seeds at MSP from farmers under the Price Support Scheme of GoI through RTGS and account payee cheques. Likewise till 9th of January, 2017 at various APMCs 88.27% transactions have been cashless and 6673 new bank accounts were opened farmers.

61. Ministry of Labour and Employment

a. This Ministry has taken several steps to encourage cashless economy and digitization of bank transactions.

b. Ministry of Labour& Employment is organizing Camps through its organizations i.e. ESIC/EPFO/Labour Officers in coordination with District Magistrates of the Districts for opening of Bank Accounts.

c. Hon'ble Minister has also addressed a letter to all the Chief Ministers and State Labour

Ministers about the campaign for opening of bank accounts.

d. The officials of Labour Department have also been instructed to organize camps especially in clusters where concentration of construction worker and Beedi workers are there.

e. As per reports received from the field officers of the Ministry of Labour & Employment, the updated status on comps organized and bank account opened in pursuant of demonetization as per reports received from the field officers of the Ministry of Labour & Employment up to 12.05.2017 total 1, 66,874 camps held for opening of Accounts, 53, 61,772 Bank Accounts opened.

f. The Payment of Wages (Amendment) Ordinance, 2016 (No. 9/2016) has been promulgated on 28.12.2016 amending

Section 6 of the "Payment of Wages Act, 1936", vide which all wages shall be paid incurrent coin or currency notes or by cheque or by crediting the wages in the bank account of the employee with provision that the appropriate Government may, by notification in the Official Gazette, specify that an industrial or other establishment shall pay the wages only by cheque or by crediting the wages in his bank account. This will ensure payment of Minimum wages to workers and consequent social security benefits.

62. Telecom Regulatory Authority of India:

a. In order to promote Mobile based Banking and payments through cards and digital means, Telecom Regulatory Authority of India (TRAI)has notified the Telecommunication Tariff (Sixty First Amendment) Order, 2016 on 22.11.2016 and also amended the Mobile Banking (Quality of

Service) (Second Amendment) Regulations 2016 on 22 November 2016 thereby: -

i. Reducing the ceiling tariff for the use of USSD for USSD-based mobile banking and payment services from Rs 1:50 to Rs.0.50.

ii. Making USSD session open for banking services as well as all kind of third party payments. Therefore, the 'USSD session for mobile banking service' has been renamed as 'USSD session for mobile banking and payment service'.

iii. Increasing the number of stages from 5 to 8 per USSD session.

b. TRAI has also made the following suggestions to RBI/ DFS to popularize the service apart from the regulatory interventions:

i. RBI/DFS/NPCI may undertake a deep 'drill-down' of the factors responsible for transaction failures and take appropriate steps to address them.

ii. National Payments Corporation of India and the banks may constantly strive to improve the software features and design to create a more user friendly menu for USSD based mobile' banking services as it would help in improving the customer experience and also the success rate of mobile banking transactions.

iii. Though the number of stages has been increased from 5 to 8, effort should be made to further improve the software design so as to let the consumer complete the transactions in minimum number of stages. This would lead to consumer convenience and greater uptake of the service.

iv. Effort should be made to put in place a smoother mechanism of linking bank accounts with mobile phones through a simplified process so that the success rate of transactions can improve.

v. In the long run, NPCI/banks /other stakeholders need to evolve a policy framework where the consumer does not have to pay for the transactions, particularly the failed ones and the cost of transactions is borne either by NPCI/ banks/other stakeholders.

vi. Last but not the least, increasing consumer awareness about this send through a time-bound, targeted communication strategy is of paramount importance.

vii. Some of the above suggestions have already been addressed by Reserve Bank of India. NPCI has been given approval for launching the revised version of *99# known as USSD 2.0 which is integrated with the Unified Payment Interface (UPI) and addresses the issues flagged above.

63. **<u>Ministry of Electronics & UIDAI:</u>**

a. <u>Mahatma Gandhi National Rural Employment Guarantee Scheme</u> (MGNREGS):The MGNREGS pursuant to the MGNREG Act, 2005 assures livelihood security to the rural poor by guaranteeing a minimum of 100 days of wage employment annually to every household whose adult members volunteer to do manual unskilled work. There are 10.38 crore active workers registered in the MGNREGS. Of these, 4.20 crore have bank accounts and job cards linked with their Aadhaar number. Using these, 15.84 crore payment transactions transferring wages have been already remitted. Those who are entitled to receive MGNREGS wages and have Aadhaar linked bank accounts can authenticate their identity at their doorstep/ neighborhood.

This is done through a handheld device known as micro ATM carried by Business Correspondents (BCs) of the banks. There are over 2.48 lath micro ATMs operating across the country. Micro ATM allows beneficiaries to withdraw money using Aadhaar Enabled Payment System (AEPS) with ease thereby furthering the end of financial inclusion. AEPS saves them the trouble of going to the nearest bank, often at distances in excess of 40 km, thereby saving loss of a day's wages. Further it prevents instances of "ghost" intermediaries, i.e. fake beneficiaries from claiming wages that rightfully belong to genuine workers.

b. <u>National Social Assistance Programme (Old Age Pensions, Widow Pensions, Disability Pensions): In </u>the aforementioned pension schemes of the Government of India, of over 2.83 crore beneficiaries, about 1.47

crore have their pension accounts linked with Aadhaar. Using such facility, over 2.10 crore payment transactions have been made and over Rs.2,196 crore electronically remitted directly to beneficiary's Aadhaar linked savings accounts. These accounts are then accessible by visiting the branches or through handheld devices using Aadhaar Enabled Payment System (AEPS). These devices are known as microATM and currently more than 2.48 Lath banking correspondents (of banks/ India Post) go from village-to-village/ neighbourhood to neighbourhood offering basic banking services. This saves old-age pensioners, widows and the disabled the trouble of going to their bank branch to receive their pensions, which is onerous particularly in far-flung rural areas.

c. <u>Prime Minister's Tan DhanYojana (PMJDY):</u> The PMJDY is a scheme for financial inclusion of the marginalized sections of society who do not have access to formal credit. The scheme permits the opening of zero-balance bank accounts and dispenses with the requirement of onerous documentation required for account opening. Over 28.44 crore accounts have been opened under PMJDY. Of these over 18.97 crore individuals have presented Aadhaar for linking to their PMJDY bank accounts or as identity proof to open the PMJDY accounts. Since PMJDY is directed primarily at BPL families and those who are financially excluded, the Aadhaar number is crucial for accessing benefits via the bank account for several social benefits and government schemes. Pertinently, one pension and two insurance schemes of the Government of India, the Atal Pension Yojana (APY), the PM Suraksha Bima Yojana (PMSBY) and the PM Jeevan Jyoti

Bima Yojana (PMJJBY) are in design, linked with PMJDY accounts. These schemes provide wide insurance coverage with small premiums thereby furthering the goal of financial inclusion. As an illustrative example, for PMSBY, paying a premium of Rs. 12 per annum, the insured is entitled to coverage for Rs. 2 lakh. When the Aadhaar number is linked, the claim amounts can be directly transferred to the bank accounts of the beneficiaries. This cuts out middlemen and ensures quicker transfer of funds at times of need to persons who otherwise would have no access to formal credit and insurance.

d. <u>Employees' Provident Fund Organization (EPFO):There</u> are over 11.18 crore contributory members to the EPFO. Currently, when employees change companies, multiple PF accounts, which are not linked to each other, are created. It is onerous to withdraw money from these accounts as they may be situated in different locations, in several cities. Due to this, deposits in several PF accounts remain unclaimed as the process for withdrawal is time-consuming and inconvenient. The linkage of Aadhaar numbers with PF accounts provides employees with a lifelong Universal Access Number (UAN), which is a Unique Identifier. Using the UAN, employees can make a single application irrespective of location to the relevant authority for withdrawal. All PF accounts also have overarching linkage thereby making it easier for the person to transfer money between accounts and withdraw money. This facilitates movement of persons for employment across India and access to PF funds with ease across locations. Currently, over 1.71 crore persons have linked their Aadhaar to their UAN in order to avail these benefits.

e. <u>AEPS and Demonetization:</u> Aadhaar Enabled Payment System (AEPS) was launched on 23.12.2012. AEPS has enabled residents to carry out banking transactions over handheld devices (microATM) carried by Business Correspondents (BCs). Micro ATMs provide doorstep services using Aadhaar and finger-prints of the resident. The basic idea was to provide banking services to remote area, thus, ensuring Financial Inclusion. The four Aadhaar enabled basic types of banking transactions are as follows:

i. Balance Enquiry

ii. Cash Withdrawal

iii. Cash Deposit

iv. Aadhaar to Aadhaar Funds Transfer

f. At present, 131 banks are live on AEPS ON-US and 91 banks are on OFF-US (inter-operable). As on 30.09.2017, over 87.45 crore transactions have taken place using AEPS across the banks. At present (last month), 7.86 crore transactions/month are happening across 3.06 lakh micro ATMs in the field.

g. After the demonetization, use of AEPS has increased significantly. From 09.11.2016 till 31.05.2017, over 62.78 crore AEPS transactions have happened in the field. This can also be seen in the monthly trends where, from 2.57 crore transactions in October 2016, 2.69 crore in November 2016, 3.73 crore transactions in December 2016 and transactions increased to 7.84 Crore in September, 2017.

h. UIDAI has already been running a micro ATM incentive scheme which incentivizes Banks and Post Offices for deploying Micro

ATM devices to carry Aadhaar enabled Banking transactions that also includes e-KYC based account opening and doing Bank Account Aadhaar linking through biometric authentication. As of 31st March 2017, over 18,502 micro ATMs have been incentivized by paying out Rs. 27.75 crore. The scheme has since been closed w.e.f. 01.04.2017.

i. Further, as per a report prepared by the Ministry, the following can be noted:

  i. The Direct Benefit Transfer (DBT) system in India which started on pilot basis in 2013 and took off in a massive way under the current government has led to savings of approximately Rs.50,000 crores in last 3 years. The Government has saved Rs. 14,000 cr its Public Distribution System by deleting 2.33 cr fake ration cards and Rs. 26,408 cr under the LPG subsidy payout till December 31, 2016. The

LPG subsidy scheme qualifies as the world's largest cash transfer program.

ii. In 2006, Andhra Pradesh became the first state in India to introduce electronic payments through a smart card system. The system was introduced in 158 sub-districts and 19 million people. Research shows, implementation of electrpnic payment system significantly reduced the leakage of funds between the Government and target beneficiaries. According to World Bank estimates in 2012, the State Government could save 1% of its GDP by digitizing subsidy flow.

iii. The incidents of demanding bribes for making social security payments has reduced to 1.8% when payment is made via smart cards rather than manual cash payout. In case of manual payments, the incidents of bribe demands stand at 3.8%. Digital transactions have thus led to a 47% reduction in bribe demands. Also, the incidents of ghost recipients have fell by 1.1%.

RESTRICTION PLACED ON THE DCCB TO ACCEPT DEPOSITS OR EXCHANGE OF DEMONETIZED CURRENCY OF RS. 500/- AND RS. 1000/-

64. The District Cooperative Banks (DCCBs) are part of Short Term Cooperative Credit Structure (STCCS), which is 3-Tier structure, i.e., generally DCCBs provides loans through PACS (Primary Agriculture Credit Society) and other societies. DCCBs also provide financial services directly to members as well.

65. In a 3 Tier Structure, primarily StCBs at State level functions through the DCCBs at the district level and Primary Agricultural Credit Societies (PACS) and other societies at village level. The District Central

Cooperative Banks (DCCBs) through the PACS are one of the key players in surveying agricultural credit. Thus, the PACS are the member-owned institutions which collectively own DCCBs and are federated as StCBs. Thus all the three tiers of institutions are owned by the individual members in the rural areas.

66. That as on 31.03.2016, there are 367 licensed DCCBs having 13,943 branches, with a large network of about 90000 affiliated PACS. Of the total loan outstanding of Rs.2.74 lakh crore, the agricultural loan outstanding is Rs.1.27 lakh crore towards 499 lath borrowing farmers (through PACS), majority of whom are small and marginal. Incidentally, there are close to 13.8 crore operational land holdings in the country. As on 30.09.2016, there are nearly *7.57* crore Kisan Credit Cards (KCCs), of which the co-operative banks are having 3.75 crore KCCs in operation. Besides providing credit, the DCCBs support several institutions operating in inputs industry both in farm

sector like seed, fertilizers, pesticides, agro-service, etc., allied sectors like dairy, fisheries, etc., and non-farm rural activities like weavers, pisciculture, etc,. In addition they provide credit support to whole range of postharvest industry like marketing societies, processing societies. Further, DCCBs play key role in Agriculture insurance, farmer benefit schemes, etc. Thus, the role of DCCBs in farmer oriented programs is very critical.

67. That the three-tier structure of StCBs is functioning in 20 States and the rest of smaller states are having 2 Tier structure where StCBs (State Cooperative Banks) are having direct link with PACS. There are no DCCBs in 2 tier structure. Besides, 3 StCBS in States (Himachal Pradesh, Jammu & Kashmir and West Bengal) are also having direct link with PACS for financing. There are about 90000 PACS in the country linked to DCCBs in 20 States having membership of about 12 crore in the rural areas. The PACS are normally collecting deposits from members, though small, as part of internal resource generation

and also maintain deposits with DCCI3s. *PACS* level deposits amounted about to Rs.84,600 crore as on 31.03.2015. Copy of 3 Tier structure of Short Term Cooperative Credit Structure (STCCS) is being annexed herewith and marked as **ANNEXURE R-12 [PATE 1268 TO 1486]**

The State Cooperative Societies Acts:

68. The State Cooperative Banks, the DCCBs, Urban Cooperative Banks and Primary Societies are registered up under the State Cooperative Societies Acts. They are under the administrative control of the State Govt. for which rules have been framed under respective State Cooperative Societies Act. However, the StCBs, DCCBs and Urban Cooperative Banks are also covered within the meaning of "Banking Companies" and therefore brought under the purview of Banking Regulation Act. 1949 (As applicable to Cooperative Societies.

Registration, Licensing, Supervision, Statutory Inspection, Regulation and liquidation of Cooperative Banks:

69. The table on authority for registration of societies, licensing, supervision, statutory Inspection and regulation over the DCCBs by the various agencies viz., RBI, Registrar of Cooperative societies and NABARD is indicated below:

Activity	**Authority**
Registration of DCCBs and StCBs	Registrar of Cooperative Societies (RCS) of State Govt.
Licensing under section 22 of the BR Act 1949 (AACS)	RBI on Recommendation of NABARD
Statutory Inspection under Section 35 (6) of BR Act 1949 (AACS)	NABARD
Regulation under BR Act 1949 (AACS) Various	RBI

provisions	
Regulation under provisions of State Cooperative Societies' Act / Rules	Registrar of Cooperative Societies (RCS) of State Govt.
Liquidation of DCCBs / StCBs By RCS on recommendation of NABARD and RBI	

Thus, registration and liquidation of Societies is vested with RCS of the respective state Government, the Inspection and supervision of DCCBs and StCBs is with NABARD and the Regulation is with RBI. Copy of the major features of DCCBs is being annexed herewith and marked as **ANNEXURE R-13 [Page 1487 to 1489]**

Board of Supervision (BOS):

70. The supervisory responsibility is guided by an independent Board of Supervision. The Board of Supervision (BoS) is established in NABARD since 1996. The BoS is chaired by Chairman of NABARD with members drawn from RBI, ED RBI and other

experts of Banking, Accounting, and Rural Credit. It reviews the financial position of banks and functioning of StCBs, DCCBs and RRBs at Quarterly intervals. The review of functioning of BoS is put up the Board of Directors of NABARD in the Board agenda for their information.

Regulatory control of RBI over DCCBs:

71. The DCCBs are regulated by the Reserve Bank of India under the provisions of Banking Regulation Act, 1949 (AACS):

a. Minimum Capital Requirement under provisions of Section 11 of BR Act 1949 (AACS),

b. Capital Adequacy Ratio (CRAR): Maintenance of minimum CRAR as prescribed by RBI,

c. Cash Reserve Ratio (CRR): Maintenance of CRR under provisions of Section 18 of BR Act 1949 (AACS)

d. Statutory Liquidity Ratio (SLR): Maintenance of SLR under provisions of Section 24 of BR Act 1949 (AACS)

e. Know Your Customer (KYC/AML): Master Directions on KYC issued by RBI.

72. Under Section 22 of the BR Act 1949 (AACS), the RBI issues license to Rural Cooperative Banks DCCBs after due consideration of statutory compliances and financial soundness. 367 out of 370 DCCBS are issued license by RBI. Only 3 DCCBS from Jammu and Kashmir did not attain licensing criteria. The licensing is reviewed periodically at annual / biennial inspection carried out by NABARD under provisions of BR Act 1949 (AACS). Based on Statutory inspections NABARD forwards to its recommendations for issue/continuation or otherwise of license issued to banks to RBI.

Amendment Notification (Rules) regarding acceptance of SBNs from DCCBs and post offices:

73. The Rules notified in the Gazette Notification dated 20.06.2017 provide for deposition of the SBNs received by banks, post offices and District Central Cooperative Banks (DCCBs) during the period specified in the Rules. The validity of the Rules is upto a period of 30 days from 20.06.2017. RBI has thus been statutorily empowered and authorized to accept such SBNs which are covered by the said Rules. RBI has issued operational guidelines to its Issue offices for implementation of the Rules vide Circular dated June 29, 2017 emphasizing that the process be completed expeditiously to ensure its completion within the stipulated time-frame. DCCBs have been apprised of the Rules and have been advised to approach RBI for tender of those SBNs within the time limit and subject to the conditions evident in the Rules. All 19 issue offices of RBI have been designated for the purpose. Banks in other sectors have also been kept informed. Copy of the Circular dated 29.06.2017 is annexed herewith and marked as **ANNEXURE R-14 [Page 1490 to 1492].**

74. That an assurance was given by the Ld. Attorney General (and accepted by this Hon'ble court) in the captioned matter that SBNs collected by DCCBs between 10th and 14th November 2016 might be exchanged with their linked currency chests after a 100% audit of the veracity of the KYC documents of SBN depositing customers of DCCB is conducted by NABARD, the supervisor and to the extent of such verified SBNs only. Accordingly, a notification No. S.O. 4086(E) dated 17.12.2016 was issued by the Government of India in conformity with the stand taken in regard to KYC audit of the SBNs by NABARD. RBI issued a detailed advice to NABARD in this regard for conducting the audit as contemplated by the GOI/RBI. Meanwhile Government of India passed the Specified Bank Notes (Cessation of Liabilities) Ordinance, 2016 under which RBI had no authority to pay the exchange value of SBNs to anyone after December 30, 2016, except to the extent permitted under the said Ordinance. Subsequently, Government of India passed the Specified Bank Notes (Deposit by

Bank, Post Offices and District Central C-operative Banks) Rules, 2017 vide Gazette Notification dated 20th June 2017 and RBI was empowered to pay the exchange value to the DCCBs. The aforesaid Rules provide statutory power and authority to RIM to actually accept the SBNs, which satisfy the conditions specified in the Rules and the above-referred Notification. An issue of concern to this Hon'ble Apex Court about the financial stress on the DCCBs because of freezing of the deposited SBNs received by them between 10th and 14th November 2016 stands duly resolved by the provisions of the Rules and the steps taken by RIM in accordance with the Rules.

Compliance to Know Your Customer (KYC) directions by RBI:

75. The DCCBS have approved policy of KYC-AML incorporating the various aspects covered in the Master Direction of RBI. They have been registered with FIU-md. They submit periodical returns such as

Cash Transaction Reports (CTRs) and Suspicious Transaction Reports (STRs) to FIU-md.

76. A special scrutiny of compliance to KYC -AML guidelines and adherence to provisions of section 114B of IT Rules 1962 regarding obtaining copy of PAN for cash deposits of Rs. 50000 and above in SBNs was undertaken by NABARD, at the instance of RBI during December 2016. The scrutiny was taken up in the Branches of DCCBs which have received deposits / exchanged SBNs of Rs. 100 lakh and above during the period 10 to 14th November 2016. The scrutiny reports indicate that the DCCBs, in general, have adhered to the KYC-AML guidelines of RBI and provisions of IT Act. The observations in the scrutiny reports of SBNs have been sent to RBI.

SBNs collected by DCCBs:

77. The RBI notification No RBI/2016-17/112 DCM (Plg) No. 1226/10.27.00/2016-17 dated 08.11.2016 on "Withdrawal of Legal Tender Character of Existing Rs. 500 and Rs. 1000 Bank notes" issued to Public

Sector Banks, private Sector Banks, Foreign Banks, Regional Rural Banks, Urban Cooperative Banks and State Cooperative Banks, did not, specifically mentioned the District Central Cooperative Banks (DCCBs), although as per the Government of India's Gazette Notification No 2652 dated 08.11.2016 (S.O 3407 (E), para. 1(1), all Banking companies were required as under:

> "Every Banking Company defined under Banking Regulation Act 1949 (10 of 1949) and every Govt. treasury shall complete and forward a return showing the details of specified bank notes held by it at the close of business as on 8th November 2016, not later than 10th November 2016 to the designated Regional Office of the Reserve Bank of India (here in after referred to as Reserve Bank) in the format specified by it."

78. Subsequently, Ministry of Finance (Department of Economic Affairs) issued a corrigendum vide No.

S.O 3418(E) dated 09.11.2016 to include DCCBs also. The RBI circular No. RBI/2016-17/130 dated 14.11.2016 states that no exchange facility against the Specified Bank Notes (SBN) or deposit of such notes should be entertained by the DCCBs. Copy of the RBI Circular No. RBI/2016-17/130 dated 14.11.2016 is being annexed herewith and marked as **ANNEXURE R-15 [PAGE 1493 TO 1494].**

79. It is pertinent to mention here that the said RBI circular dated 14.11.2016 subsequently stood ratified by Government of India vide its letter F.No.10/03/2016-Cy.1(Vof II) dated 24.11.2016 read with Gazette Notification S.O. 3543(E) dated 24.11.2016.

80. The SBNs held by DCCBs as on 8th November and 14th November 2016 is as under:

Date	SBNs amount (Rs. crore)
8 November 2016	4136.89
14th November 2016	12083.79

(provisional)	

Source: DCCBs through ENSURE -NABARD

81. As per the data reported by DCCBs on SBNs collected by DCCBs, 89.6% of SBN tenderers were individuals, 2.3% were PACS and other societies and 8.1% have exchanged the SBNs during the period 10th to 14th November 2016. Thus, a large share of SBNs were deposited by Individuals. Copy of the State wise details of SBNs collected by DCCBs during the period 10th - 14.11.2016 are given is being annexed herewith and marked as **ANNEXURE R-16 [page 1495 to 1504]**

BLACK MONEY:

82. There is no official estimation of the amount of black money either before or after the Government's decision of 8th November 2016 declaring that bank notes of denominations of the existing series of the value of five hundred rupees and one thousand rupees shall cease to be legal tender with effect from 9th November 2016.

83. The searches conducted by the Income Tax Department during the period 01.04.2014 to 30.09.2017, in 2370 groups of assessees have led to admission of undisclosed income of Rs.44,224 crore. Besides 24,360 surveys conducted during the same period, resulted in detection of undisclosed income of Rs.37,879 crore. Further, during the period 01.04.2014 to 31.08.2017, the Income Tax Department prosecuted 2886 persons before criminal courts, besides compounding of offences in 3548 cases. 86 persons were convicted by trial courts for offences under direct taxes during the same period.

84. That 648 disclosures involving undisclosed foreign assets worth Rs.4164 crore, were made in the one-time three months' compliance window closed on 30th September 2015, under the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015. The amount collected by way of tax and penalty in such cases was about Rs.2476 crore. Further, under the Income Declaration Scheme, implemented by the Government during

June to September 2016,71,726 declarants made declarations of undisclosed income of Rs. 67,382 crore.

85. That whenever a case of undisclosed income/ asset is detected, the Income Tax Department takes necessary action under provisions of direct taxes laws which include investigation, assessment of income, levy of tax, interest & penalty and filing of prosecution complaints before criminal courts, wherever applicable. Other law enforcement agencies such as Enforcement Directorate, Central Bureau of Investigation, etc. also take action under laws administered through them, in relevant cases, depending upon facts of each case. The Government has taken several steps, both by way of policy initiatives as well as through more effective enforcement action on the ground, to more effectively tackle the issue of black money. These steps include putting in place robust legislative and administrative frame works, systems and processes

with due focus on capacity building and integration of information and its mining through increasing use of information technology. It is pertinent to mention here that section 51 of the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015 is a schedule offence appended to PMLA, 2002 and the Directorate of enforcement has taken up a few cases of investigation as well.

Estimation of Black Money:

86. That there is no official estimate of the amount of black money inside and outside the country.

a. Study on estimation of unaccounted income and wealth: The Standing Committee on Finance on Demand for Grants (2009-10) in its second report, presented in Parliament on 2nd December 2009, had made certain observations, which included the following:

> "Unaccounted money
>
> 8. Parallel economy and generation and sustenance of unaccounted money / wealth have

been a bane afflicting this country for long. However, what is most damaging about this phenomenon is its innate relationship with tax evasion as also lax tax enforcement. The disquieting fact that the Ministry of Finance (Department of Revenue) have no assessment available with them on the extent of unaccounted income / wealth, can only compound the problem further. They have instead tried to turn away from their responsibility by pleading that since most of the transactions generating black money are unrecorded, the credibility of any estimate of black money is doubtful. When pressed on the issue, they cited a 1999 study by Shri Arun Kumar, Professor of JNU in his book 'Black Economy in India' wherein the quantum of black money has been estimated as Rs.4,87,185 crore i.e. 40% of the GDP. The Department have further maintained that keeping in view the nature of Indian economy and also the fact that a large number of transactions are entered in cash, it is not possible to arrive at the correct assessment of the quantum of unaccounted money in the country. Neither is there any proposal under consideration of the Ministry for getting any fresh study conducted on the quantum of unaccounted money in the country. Such an indifferent response of the Ministry is not acceptable to the Committee. It has become imperative that the Ministry conducts a thorough assessment / survey on unaccounted income / wealth, particularly bringing out the nature of activities engendering money laundering both inside and outside the country with its ramifications on national security."

The Standing Committee, in another observation in the same report, had also desired to know the quantum of non-payment of tax due to evasion by registered corporate bodies.

b. On 28.10.2010, Hon'ble Finance Minister accorded in-principle approval for the study in respect of the above. The study was assigned to NIPFP, NCAER and NIFM to be conducted by them separately and independently. The study commenced on 21st arch, 2011. Terms of Reference (ToRs) of the study are as under:

i. To assess / survey unaccounted income and wealth both inside and outside the country.

ii. To profile the nature of activities engendering money laundering both inside and outside the country with its ramifications on national security.

iii. To identify important sectors of economy in which unaccounted money is generated and examine causes and conditions that result in generation of unaccounted money.

iv. To examine the methods employed in generation of unaccounted money and conversion of the same into accounted money.

v. To suggest ways and means for detection and prevention of unaccounted money and bringing the same into the mainstream of economy.

vi. To suggest methods to be employed for bringing to tax unaccounted money kept outside India.

vii. To estimate the quantum of non-payment of tax due to evasion by registered corporate bodies.

c. That the timeline was extended from time to time on the request of the institutes on various grounds including the nature of complexities involved in the subject matter. An Expert Group under the chairmanship of Member(Inv.), CBDT and including Principal Economic Advisor, Department of Economic Affairs; Economic Advisor, DEA; Commissioner (Inv.); Joint Secretary (TPL-I), Joint Secretary (FT & TR-I);

Commissioner (IT&CT); Commissioner (ITA); Commissioner(Vig.) and Dy. Director, DEA was constituted to, inter alia, firm up the Government's view/response on these reports, for submission to Finance Minister.

d. Present status: The final reports from National Institute of Public Finance and Policy(NIPFP), National Council of applied economic Research (NCAER) and National institute of Financial Management(NIFM) have been received in December 2013, July 2014 and August 2014 respectively. They have been examined and the response of the Government has been prepared by CBDT in consultation with the other Ministries, Agencies and Departments such as CBEC; ED; SEBI; Ministries of Rural Development, Health, Corporate Affairs, Petroleum and Natural Gas. The final reports and the Government's response have been submitted to the Lok Sabha Secretariat on 21.07.2017 for placing the same before the Standing Committee on Finance.

Recent major initiatives to further tackle the issue of black money:

87. In recent times, the Government has taken several steps to tackle the issue of black money, particularly black money stashed abroad. They include legislative and administrative measures, setting up of more advanced system and processes with due focus on capacity building and greater use of information technology. Recent major initiatives in this regard include the following:

a. <u>Enactment of the Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act, 2015:</u> The Government enacted a comprehensive and a more stringent new law to deal with foreign undisclosed income and assets of Indians that has come into force w.e.f.

01.07.2015. First assessment year under the new law is 2016-17. Its salient features are:

i. Separate taxation of undisclosed foreign income and assets.

ii. More stringent provisions for concealment penalties (equal to three times the amount of tax payable) and prosecutions (rigorous imprisonment up-to 10 years with fine for willful attempt to evade taxes etc. in relation to undisclosed foreign income/ assets).

iii. The offences under this law are not compoundable.

iv. Issues under the new law are out of the purview of the Income- tax Settlement Commission.

v. Offence of wilful attempt to evade tax etc. in relation to undisclosed foreign income! assets has been made a Scheduled Offence under the Prevention of Money-laundering Act, 2002 (PMLA).

vi. This enables attachment and confiscation of the proceeds of crime of wilful attempt to evade such tax, etc. i.e. the black money stashed abroad. Further, PMLA has been amended through the Finance Act, 2015 enabling attachment and confiscation of property equivalent in value held within the country.

vii. A one-time compliance window of 3 months, inter alia, provided an opportunity to taxpayers to make declarations of their undisclosed foreign assets before they were subjected to more stringent provisions of the new law. 648 declarations were filed disclosing undisclosed foreign assets worth Rs.4164 crore. An amount of about Rs.2476 crore has been collected as tax and penalty in such cases.

b. <u>Comprehensive amendment to the Benami Transactions (Prohibition) Act, 1988 with a view to further address the issue of domestic black money:</u> Though the Benami Transactions (Prohibition) Act, 1988 has been on the statute book since last 28 years, the same could not be made operational so far because of certain inherent defects. The Benami Transactions (Prohibition) Amendment Act, 2016 has been enacted w.e.f. August 2016 by the Government to curb the menace of domestic black money and the amended law has come into force w.e.f 1st November, *2016.* The Act, inter-alia, seeks to specify the implementation authorities, empower them to conduct investigation, create appellate machinery and provide for management of confiscated property. The Benami Transactions (Prohibition) Amended Act of 2016 empowers the specified authorities to provisionally attach benami properties which can eventually be confiscated. Besides, if a person is found guilty of offence of benami transaction, he shall be punishable with rigorous imprisonment for a term not less than one year but which may extend to 7 years and shall also be liable to fine which may extend to 25% of the fair market value of the property.

c. Income Tax Department has issued show cause notices for provisional attachment of benami properties in 517 cases. Out of these, provisional attachment has been made in 475 cases with properties worth more than Rs.1626 crore. Benami properties attached include deposits in bank accounts, agricultural land, jewellary etc.

88. Other significant anti-evasion legislative measures taken in recent years: The significant legislative measures taken in

recent years with a view to curb the menace of back money include the following:

a. <u>Tracking & curbing cash transactions and strengthening third party reporting mechanism:</u>

i. In order to curb black money in domestic immovable property transactions, section 269SS, section 269T, section 271D and section 271E of the Act were amended to prohibit acceptance of any payment, or repayment of advance, of Rs.20,000 or more otherwise than by an account payee cheque or account payee bank draft or by electronic clearing system through a bank account, in relation to transfer of an immovable property by providing penalty of an equivalent amount. [Finance Act, 2015].

ii. Suitable amendment in rule 114B of the Income Tax Rules (the Rules) has been made vide Notification No. 95/2015 dated 30th December, 2015 whereby quoting of PAN has been made mandatory for transactions of sale or purchase of goods or services of any nature above Rs. 2 Lakh. [2015].

iii. The AIR has been replaced with a new reporting regime- the Statement of Financial transaction (SFT) w.e.f 1.4.2016. The SFT has enabled streamlining of the process and enlarging of the coverage of reportable high value transactions in select sectors.

iv. The new regime would help achieve multiple benefits of widening of tax base through identification of new tax payers, non-filers and stop filers, curb tax evasion in non-intrusive manner, improve compliance of tax laws and encourage use of non-cash payments. It will also tackle the problem of splitting of transactions as annual aggregate transaction value will also trigger reporting.

b. <u>Post demonetisation, there are significant changes as under:</u>

i. CBDT issued a notification dated 15.11.2016 amending Rule 114B of the Income Tax Rules, 1962, mandating PAN for all cash deposits above Rs. 50,000 and aggregating to more than Rs.2.5

lakh. Rule 114E of the Income Tax (I.T.) Rules, 1962 was also amended to mandate the prescribed reporting entities to report all cash deposits above Rs. 2.5 lakh in savings accounts and Rs. 12.5 lakh in current account during 9 November and 30 December, 2016.

ii. Mandatory linking of PAN with bank accounts: RBI, vide Circular dated 15.12.2016, directed all Regulated Entities (RE) to strictly comply with the extant instructions including in respect of 'Small Accounts' [Basic Savings Bank Deposit / Pradhan Mantri Jan Dham Yojana accounts which are non-KYC compliant accounts are treated as 'Small Accounts'] for which the prescribed limits/

conditions should not be breached and compliance therewith should be strictly monitored. It further stated that in respect of KYC compliant accounts where the required 'Customer Due Diligence' procedure had been complied with, REs should ensure compliance regarding quoting of PAN/ obtaining of Form 60 for all transactions in terms of I.T. Rule 114 B which includes opening of accounts with banks, NBFCs, etc. No debit transaction, transfer or otherwise should be allowed in accounts which do not comply with these requirements.

iii. Restriction of cash transaction of Rs.2 lath or more (Section 269ST of I.T. Act), no deduction under section 80G if cash donation exceeds Rs. 2000 effective from 01.04.2018, restriction of donations of Rs.2000/- or more to political parties otherwise than by a bank account or through electoral bonds, widening of the scope of taxability of receipt of the sum of money or the property by any person without consideration or for inadequate consideration in excess of Rs.50,000 and deeming of prescribing fair market value as full value of consideration for computation of capital gains in case of transfer of shares other than quoted shares (Section 50 of I.T. Act). [Finance Bill; 2017].

iv. Vide notification no. 2 of 2017, dated 6.1.2017, Rules 114B to

114E of the I.T. Rules, 1962, were further amended as under:

(i) A proviso has been inserted in the Rule 114B providing that a person who has an account (other than a time deposit and a Basic Saving Bank Deposit Account) maintained with a banking company or a cooperative bank and has not quoted his PAN or furnished Form No.60, as the case may be, at the time of opening of such account or subsequently, he shall furnish his PAN or Form No.60, on or before 28 February 2017.

(ii) A sub-Rule has been inserted in Rule 114C making it mandatory to the person referred to in sub-rule (1) or sub-rule (2) thereof who has received any document

(Banks etc) in which PAN is mentioned or, as the case may be, a declaration in Form No.60 has been furnished, shall ensure that the valid PAN or the fact of furnishing of Form No. 60, is duly mentioned in the records maintained for the transactions referred to in rule 114B and the PAN or the details of Form No. 60 are linked and mentioned in any information furnished to the Income-tax authority or any other authority or agency under any provision of the Act or any rule prescribed therein.

(iii) Another proviso has been added to the Rule 114D providing that statement in respect of prescribed transactions under Rule 114B shall be furnished on or before the 15.1.2017.

v. Rule 114E has been amended to include a banking company, a co-operative bank and the Post Master General, as reporting persons, for reporting cash deposits during the period 1st April, 2016 to 9th November, 2016, in respect of reportable accounts.

vi. Under SFT, the Form 61A has been amended to include furnishing of details about Aggregate gross amount credited to the account in cash from 1st day of April, 2016 to 8th November, 2016 and from 9th day of November, 2016 to 30th day of December, 2016, apart from Aggregate gross amount credited/ debited to the account in cash during the F.Y.

vii. Linking of Aadhar with PAN has been made mandatory for filing Income Tax Returns and for applying for new PAN from 1 July 2017 [Finance Act, 2017].

c. <u>Plugging loopholes in transactions through foreign connections:</u>

i. In the context of section 6 of the Income-tax Act, with a view to check the creation of shell companies which are incorporated outside but controlled from India for the purpose of avoidance of tax payment in India, enabling provision relating to "place of effective management" (POEM) has been provided which is an internationally recognized concept for determination of residence of a company incorporated in a foreign jurisdiction. [Finance Act, 2016].

ii. Country-by-country reporting requirement in respect of international group has been introduced to address issues relating to base erosion and profit shifting - Section 286 of the Income-tax Act, 1961. [Finance Act, 2016].

d. <u>Higher rate of tax & penalty on undisclosed income:</u>

i. The Taxation Laws (Second Amendment) Act, 2016 was enacted to enable levy of tax at a higher rate of tax on the undisclosed income (tax, surcharge and penalty of about 77.25 if disclosed in the Return of Income and 85% if not disclosed at all, besides penalty and prosecution) and provide for the taxation and investment regime for Pradhan Mantri Garib Kalyan Yojana, 2016 (PMGKY).

ii. The scheme of PMGKY allowed a person to declare undisclosed cash by paying tax, surcharge and penalty totalling to 50% of the sum so declared. Besides, 25% of the undisclosed income would have to be mandatorily deposited in Pradhan Mantri Garib Kalyan Deposit Scheme for 4 years, bearing zero interest. The scheme was open till 31 March, 2017.

e. <u>The Special Investigation Team (SIT) on Black Money:</u>

The SIT on Black Money was constituted by the Government in May 2014 under Chairmanship and Vice-Chairmanship of two former Judges of Hon'ble Supreme Court, Hon'ble Justices Shri M.B. Shah and Shri Arijit Pasayat. Members of the SIT include-Secretary (Revenue); Dy. Governor, RBI; Chairman, CBDT; Director, IB; Director, CBI; Director, RAW; Director, ED; DG, NCB; DG, DRI; Director, FIU; JS(FT&TR-I), CBDT. SIT has been monitoring investigations into cases involving substantial black money/ undisclosed income, particularly black money stashed abroad. It also reviews the legal and administrative framework to curb the menace of black money. The SIT has so far submitted 5 reports to Hon'ble Supreme Court.

89. Specific enforcement actions in the context of demonetization:

a. Enforcement actions by the Income Tax Department: Following intelligence of large scale misuse of opportunities of deposit of cash in specified bank notes post demonetization enforcement actions were intensified by the ITD Summary of actions and preliminary outcome is as under:

i. More than 1,100 search, seizure and survey actions were taken by the ITD during the period 9th November 2016 to 10th January 2017.

ii. These actions led to seizure of valuables of more than Rs.610 crore, which includes cash of Rs.513 crore (including new currency of more than Rs 110 crore).

iii. The undisclosed income detected in these actions (as on 10th January 2017) was more than Rs.5,400 crore.

iv. Besides, more than 5,100 notices were issued for verification of suspicious transactions of high value cash deposits.

v. More than 400 cases have been referred to ED and CBI between 9 November, 2016 and 10 January, 2017. These agencies have taken appropriate actions in large number of such case

b. <u>Operation Clean Money initiated by ITD on 31.01.2017:</u>

i. A huge cache of information on cash deposits in banks post demonetization was shared with the ITD post demonetization by various government agencies.

ii. Operation Clean Money was launched on 31st January 2017 to use this information effectively and in a short span of time for non-intrusive verification of such data, both to optimize government resources and cause minimum inconvenience to the taxpayers. It entailed collection of relevant information on cash transactions, its collation and analysis, extensive use of information technology and data analytics tools for identification of high risk cases based on approved criteria, expeditious verification of suspect cases and enforcement actions in appropriate cases, which include searches, surveys, enquiries, assessment of income, levy of taxes, penalties, etc. and filing of prosecution complaints in criminal courts, wherever applicable.

iii. In the first phase of the Operation 17.73 lakhs suspicious cases (No. of PANs) were identified through use of advanced data analytics. Such cases were those where cash transactions did not appear to be in line with the tax profile of PAN holders.

The total cash deposit involved in these cases was Rs. 3.68 lakh crores in 23.22 lakh bank accounts. The responses on such cash deposits were solicited from account holders in a non-intrusive manner by sending SMS/emails. 11.18 lath persons have submitted response for 16.92 lath bank accounts.

c. <u>Investigation in HSBC foreign bank accounts cases:</u>

i. That the information regarding certain Indians holding bank accounts in HSBC bank in Switzerland was obtained from the Government of France under the Double Taxation Avoidance Convention (DTAC) between India and France in 2011. The following have been the broad outcomes of ITD actions in these cases:

(i) Undisclosed income of about Rs.8448 crore has been brought to tax on account of deposits made in unreported foreign bank accounts. This includes an amount of Rs.1687 crore assessed on protective basis. Tax demand of about Rs. 5447 crore has been raised in such cases which includes demand in protective assessments.

(ii) Out of the above-mentioned 412 cases in which assessments have been completed, concealment penalty of about Rs.1290.2 crore has been levied in 164 cases. Besides, in 69 cases concealment penalty proceedings initiated are pending.

(iii) So far, 199 prosecution complaints in HSBC cases have been filed in 84 cases.

d. Investigation in ICIJ cases: During FY 2013-14, International Consortium of Investigative Journalists (ICIJ) released in public domain information about offshore entities with several persons of different countries were associated. Investigations were conducted by ITD in cases of Indians appearing in the said disclosures. Summary of findings, so far, is as under:

(i) Out of 700 cases, 298 have been found actionable so far.

(ii) Verification of Income-tax returns in these cases shows that in a large number of cases, such offshore entities/ transactions were not disclosed to the Income-tax Department.

(iii) Despite the major constraint of non-availability of information relating to financial transactions/ bank accounts on the website of ICIJ, sustained investigations in these cases have yielded encouraging results. Undisclosed credits of about 11010 crore has been detected in the bank accounts [includes income declared under Compliance window of BMA [Black Money (Undisclosed Foreign Income & Assets) and Imposition of Tax Act, 2015].

(iv) So far, 72 Prosecution complaints have been filed in 31 cases, which include complaints filed under section 277 (false statement in verification, etc.) and under section 181 of IPC.

(v) Further expeditious investigation in these cases is in progress.

e. Investigation in the cases revealed in 'Panama Papers Leaks:

i. Background: Certain information, reported to be outcome of investigation by International Consortium of Investigative Journalists (ICIJ), a Washington based organization; Suddeutsche Zeitung, Munich based newspaper; and Indian Express newspaper appeared in public domain including website of ICIJ and Indian Express of Delhi edition of 04.04.2016 and subsequent dates. In the context of India, the information, inter alia, indicated apparent linkage between certain Indian persons and various offshore entities created in low-tax or no tax foreign jurisdictions as also with assets acquired abroad.

ii. The Government constituted a Multi-Agency Group (MAG) on 04.04.2016, inter alia, for facilitating co-ordinated and speedy investigation in the cases.

The Group consist of the officers of the Central Board of Direct Taxes (CBDT), Enforcement Directorate (ED), Financial Intelligence Unit (FIU) and Reserve Bank of India, and its Convenor is Member (Investigation), CBDT. So far, the MAG has submitted 7 reports to the Government. SIT has been kept informed of the progress.

iii. Summary of the outcome: The Panama papers contained details of 426 persons, prima facie, Indians or persons of Indian origin. The Income Tax department conducted enquiries in all 426 cases. About 316 references were made to 22 foreign jurisdictions under Tax Treaties. In 5 cases criminal prosecution complaints have been filed and in 7 cases notices under section 10 of the Black Money (Undisclosed Foreign Income & Assets) and

Imposition of Tax Act, 2015 have been issued. Investigations so far have detected undisclosed credits of about Rs.792 crore (approx). Further investigation in all the above cases is in progress.

f. <u>Taxation Laws (Second Amendment) Act, 2016:The</u> Taxation Laws (Second Amendment) Act, 2016 was enacted to enable levy of tax at a higher rate of tax on the undisclosed income and provide for the taxation and investment regime for Pradhan Mantri Garib Kalyan Yojana, 2016 (PMGKY).

g. <u>Enforcement actions taken by the Enforcement Directorate (ED):</u>

i. ED conducted searches under FEMA at 67 places across India on Full Fledged Money Changers (FFMC) on 11 November, 2016

During the search Rs 3 crores (aprox.) of old currency notes and foreign currency worth Rs 1.7 crores were seized. Action under FEMA has been initiated against the contraveners.

ii. Searches under FEMA at 36 Hawala Operators in Delhi, Mumbai, Chennai, Bangalore, Guwahati and Kolkata were conducted on 29 November, 2016, leading to recovery of Rs.1 crore of old currency notes and Rs.20 laths of new Indian currency notes and foreign currency of about Rs 50 Laths. Action under FEMA has been initiated against the offenders.

iii. The Directorate maintained close coordination with various LEAs and any scheduled offence registered in connection with post demonetization was followed up with recording of ECIR under PMLA. Information for registration under scheduled offences was also gathered from open sources viz electronic/print media and internet.

iv. The ED has so far recorded 33 ECIRs under PMLA in connection with cases relating to demonetization. 18 persons have been arrested by the ED in these cases.

h. <u>Enforcement actions taken by CBI:</u> CBI has registered cases/ enquiries at various places all over India pertaining to demonetization. The number of such cases, the amount involved therein, number of arrests made and searches conducted in these cases are as under:

a.	Number of cases registered	33 (31 RCs & 02 Preliminary Enquiries)
b.	Departments involved	Banks, Post offices, Railways
c.	Amount involved as per FIR	Rs.157.12 crore (approx.)
d.	Number of Public Servants involved so far	47
e.	Number of arrests made so far	38
f.	Searches conducted so far	52
g.	Amount seized by CBI so far (New/ valid currency Rs. 26,21,70,670/-)	Rs. 26.35 crore (approx.) (Invalid/ demonetized currency Rs. 13,95,000/-)
h.	Cases involving public sector/ private sector/ cooperative Banks	21

i. <u>Summary of approach to dealing with data on cash deposits:</u>

Objective		*Action Point*	*Remarks*

Encourage online submission of correct explanation of source of cash deposit	1.	Electronic Communication (SMS/Email) to target segment	Preliminary analysis of >Rs.1 cr+ accounts Two rounds of communication sent • 17,92,467 target segment • 10,39,193 PAN holders in the target segment have logged in • 8,71,509 PAN holders have submitted online response.
	2.	Push high risk cases (including cases with no response) to field formation	• 3,78,230 high risk cases (including 1,96,280 cases with no response) pushed in two batches
		Selective enforcement action (Survey) on high risk persons not submitting response	• 2000+ surveys u/s 133A conducted on persons not submitting response
	4.	Closure of low risk cases	• Under Process
Gather additional information	5.	Ensure complete	• 57.05 Lakh

related to cash despites leveraging data analytics		and accurate reporting of SFT (Form 61A/61) by banks	reports submitted by 1819 banks. • Reporting compliance is being monitored.
	6.	Collect STR/ CTR data from FIY-IND	FIU has agreed to share data dump of ~15,000 STRs
	7.	Collect additional information (latest KYC and fund *flow* information) from banks in specific cases (wrong PAN, invalid PAN, Not registered on e-filing portal, no response)	Under Process
Target high risk persons for PMGKY	8.	Calibrated release of actionable cases for Assessment! Investiga tion wing	High risk FIU data shared with Investigation Wing/I&CI 3,78,230 high risk cases (including 1,96,280 cases with no response)

			pushed in two batches
	9.	Identification of high risk groups/cases using advanced data analytics	Thematic Analysis Reports under preparation
Create on- going buzz around Operation Clean Money and PMGKY	10.	Targeted media campaign	Initiated
	11.	Press releases about voluntary compliance & enforcement action	Initiated
	12.	Activate influencers (Industry chambers, CAs, market association, banks etc) by outreach	Initiated
	13	Launch dedicated web portal with social media integration and dashboards	

Effective process implementation by ITD	14	Detailed Standard Operating Procedure (SOP) for online verification without any need to visit IT office	Issued
	15.	Online monitoring and supervision	On going

j. Action taken by Enforcement Directorate in Panama Leaks Case:

i. ED has initiated open inquiries in 210 cases out of list of 381 individuals received from CBDT.

ii. ED has initiated open inquiries in 42 cases out of list of 46 cases received from RBI where prima facie contravention has been observed.

iii. In one case, ED has seized Rs. 7 Crore (aprox.) of the accused lying with different banks under Section 37A of FEMA, 1999.

k. <u>Tax treaties with foreign countries:</u>

i. Tax Treaties are the means to enable effective investigation in cases of black money stashed abroad as they provide access to information from foreign countries/ jurisdictions in the form of admissible evidence. The Government has entered into tax treaties with a number of countries/jurisdictions for exchange of information for tax purposes. As on 30.06.2017, India had such treaties with 148 countries/ jurisdictions.

ii. Amending treaties enabling sharing of banking information: Since 2009 onwards, a number of tax treaties have been modified through amending Protocols, e.g., DTAAs with Switzerland, Singapore, Australia, Sweden, U.K. Mauritius, etc. In the modified/ renegotiated DTAAs as also in the new DTAAs entered after 2009, the banking information and information for domestic tax purposes can also be exchanged. Further, generally the information received may be used for non-tax purposes if such use is permitted under the laws of both the supplying and receiving State and with the consent of the supplying State.

iii. Amendment of India-Mauritius DTAA: The Protocol for amendment of the Convention for the avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income and capital gains between India and Mauritius was signed by both countries in May 2016, which provides for source-based taxation of capital gains on shares and interest income of banks. The Protocol would help tackle treaty abuse and round tripping of funds attributed to the India-Mauritius treaty thus curbing revenue loss. It would also improve transparency in tax matters and help curb tax evasion and tax avoidance.

iv. Amendment of India-Singapore Treaty: India and Singapore amended the DTAA for avoidance of double taxation and prevention of fiscal evasion with respect to taxes on income, by signing a Third Protocol in December 2016. The Third Protocol has amended the DTAA with effect from 1st April, 2017 to provide for source based taxation of capital gains arising on transfer of shares in a company. This would curb revenue loss, prevent double non-taxation and streamline the flow of investments. The Third Protocol would also enable application of domestic laws and measures concerning prevention of tax avoidance or tax evasion. This would be in line with India's treaty policy to prevent double non-taxation, curb revenue loss and check the menace of black money through automatic exchange of information.

v. Significant increase in investigations in recent years: As a result of these efforts in recent years, there has been a significant increase in the number of exchange of information (EOI) requests sent in foreign assets cases to foreign jurisdictions in the last three years. A total of 4059 requests were made in the last 3 financial years (2014-2015 and 2016-2017) against 2093 made in earlier 6 years (2008-2009 to F.Y 2013-2014).

vi. Treaty Negotiation with Panama: At present, India does not have any EOI relationship with Panama, although India has been pursuing with Panama to enter into an agreement for exchange of information for tax purpose. Negotiations were entered into with Panama in 2009 for a Tax Information Exchange Agreement (TIEA). Panama initially insisted on negotiating a Double Taxation Avoidance Agreement (DTAA), but agreed to negotiate TIEA in April 2012. For this purpose both sides exchanged their positions in 2013, but substantial differences persisted on the positions of two sides, as Panama was neither willing to agree to International standards, nor to the Indian proposals in respect of several provisions. The process could not be carried forward in

2014 and 2015 due to a change in Government in Panama and restructuring of its negotiating team. In late 2015, after Panama agreed to resume the negotiations, both sides have exchanged their proposals, and an integrated document containing proposals of both sides have been prepared. The views of Panama on the proposals made by India are awaited at this stage. Panama has not signed the Multilateral Convention through which information can also be exchanged. However, on 14.07.2016, Panama has officially expressed interest in becoming a party to the Convention on Mutual Administrative Assistance in Tax Matters.

m. <u>Search and Seizure, Surveys and Prosecutions:</u> Statistics on search & seizure, surveys & prosecutions conducted by the

ITD in the last three years and current year and preliminary outcome thereof are as under:

i. Search and Seizures:

ii. Surveys:

Financial Year	Number of groups searched	Total assets seized (In Rs. crore)	Undisclosed income admitted u/s. 132(4) of the Income-tax Act, 1961 tin Rs.crore]
2013-14	569	808.66	10792
2014-15	545	761.70	10288
2015-16	447	712.32	11226
201617*	1152	1469.45	15497
2017-18(Upto Sep._2017)*	226	485.57	7213

*Figures are provisional

Financial Year	No. of surveys conducted	Undisclosed income detected (in Rs. Crores)
2013-14	5327	90390

2014-15	5035	12820
2015-16	4428	9699
2016-17	12526	13716
2017- 18 (Upto Sep. 2017)*	2371	1643

*Figures are provisional

iii Prosecutions & compounding: Various measures have been taken in the recent past to strengthen the prosecution mechanism with a view to identify the prosecutable cases at the earliest and pursue the same with due seriousness. Relevant statistics for prosecution in this regard for last 4 financial years and the current year is as follows:

F. Year	No. of cases in which Prosecutions complaints filed	No. of cases disposed off by the Court	No. of persons convicted	No. of Compounding Applications filed	No. of cases compounded	Total of Prosecution and Compounding (2+6)

		s				
(1)	(2)	(3)	(4)	(5)	(6)	(7)
2013-14	641	103	41	849	561	1202
2014-15	669	76	34	1131	900	1569
2015-16	552	66	28	1089	1019	1571
2016-17*	1252	46	16	1920	1208	2460
2017-18 Upto Aug, 2017	413	33	8	659	421	834

*provisional figures upto 31st January 2017

n. <u>Proactive role in promoting Automatic Exchange Of Information (AEOI) from Offshore Jurisdictions and Common Reporting Standards (CRS):</u>

i. India has played a proactive and prominent role in development and implementation of the new global standards on automatic exchange of information, which would enable the tax authorities to receive information about taxpayers hiding their money in offshore financial centres and tax havens through multi-layered entities with non-transparent ownership, on an automatic basis.

ii. The Common Reporting Standards (CRS) on Automatic Exchange of Information (AEOI) was developed by OECD working with all G20 countries and Indian delegates contributed to the same. The framework is known as CRS Multilateral Competent Authority Agreement (MCAA). About 83 jurisdictions have already signed the MCAA till June 2016 and over 100 jurisdictions have committed to exchanging information under the CRS by 2017 or end 2018. India has joined a group of 48 countries as early adopters to the new global standards and will be exchanging information automatically as per these standards from 2017. Information sharing arrangement with USA under its Foreign Account Tax Compliance Act (FATCA) has been entered into on 9th July 2015. Exchange of information under FATCA has started from 30th September 2015.

iii. For implementation of these standards in India and with a view to provide information to other countries, necessary legislative changes have been made through Finance (No. 2) Act, 2014, by amending section 285BA of the Income-tax Act, 1961, and necessary rules and guidelines are being formulated in consultation with financial institutions.

90. THE INCOME DECLARATION SCHEME, 2016:

The Government brought in the Income Declaration Scheme (IDS) in the Budget 2016 to provide opportunity to Indian persons to declare their undisclosed income during 1st June 2016 to 30th September, 2016 and pay 45% tax, surcharge and penalty on such undisclosed income declared. About 71,726 declarations disclosing undisclosed income of Rs.67,382 crore were made under this scheme.

91. INCREASING USE OF INFORMATION TECHNOLOGY FOR ENFORCEMENT OF COMPLIANCE:

Availability of information in electronic form has provided an opportunity to the Income Tax Department to develop a wide range of non-intrusive methods for promoting voluntary compliance and deterring tax evasion. Some of the important measures include the following:

a. Selection of Cases for Scrutiny -Computer Assisted Scrutiny Selection (CASS): The Department has been implementing a centralized, rule- based mechanism for selecting cases for scrutiny, wherein the rules and parameters are reviewed every year.

b. Non-filers Monitoring System (NMS): The Non-filers Monitoring System (NMS) has been rolled out for pilot implementation to prioritize action on non-filers with potential tax liabilities. Data analysis was carried out to identify non-filers about whom specific information was available in the AIR, CIB and TDS/TCS Returns database. As a result of this initiative, 94.05 Lakh non-filers filed their Income-tax returns and paid self-assessment tax of Rs. 16,566 crore.

c. Income Tax Business Application (ITBA): ITBA is an ambitious venture of the Income Tax Department aimed at improving service delivery to tax payers and raising tax revenues, inter alia, by helping in curbing tax evasion through putting in place end to end IT processes for all verticals of the Department. These verticals include Investigation, Central & Intelligence & Criminal Investigation (I&CI). The project is being implemented in phases.

d. Project Insight: The existing database of the Income Tax Department is fragmented on the basis of the source and method of collection of the information. Project insight has been conceptualized as a robust and comprehensive data warehousing and business intelligence system. Upon implementation, the Project would play a key role in data mining to track tax evaders and widening of the tax-base. The new technical infrastructure will also be leveraged for implementation of Foreign Account Tax Compliance Act Inter Governmental Agreement (FATCA IGA) and Common Reporting Standard (CRS).

e. The contract for implementation of the Project has been signed in July 2016 and it will be rolled out in a phased manner during the period 2017-18.

AMENDMENT NOTIFICATION (RULES) REGARDING ACCEPTANCE OF THE SEIZED/CONFISCATED SPECIFIED BANK NOTES (SBNS):

92. The Central Government notified the Specified Bank Notes (Deposit of Confiscated Notes) Rules, 2017 vide Gazette Notification No.G.S.R.460 (E) dated 12.05.2017 providing for tender of the SBNs seized/ confiscated on or before December 30, 2016. The Rules came into effect from the 12.05.2017. In pursuance of these Rules, RBI issued procedural guidelines to its Regional offices vide Circular dated 25.05.2017 to facilitate tender and acceptance of the SBNs within the ambit of the Rules. Copy of the Specified Bank Notes (Deposit of Confiscated Notes) Rules, 2017 is being annexed herewith and marked as **ANNEXURE R-17 [PAGE 1503 TO 1505]**. Copy of the Circular dated 25.05.2017 issued by the Reserve Bank of India is annexed herewith and marked as **ANNEXURE R-18 [Page 1506 To 1509].**

93. The RBI offices are under instructions to accept the SBNs tendered by an eligible person and / or Central/State Government Departments as defined in terms of clause 2(a), (b), and (c) of the Rules and

pay exchange value of the SBNs so tendered in the manner provided in the Rules, i.e. either by credit into bank account or in cash as desired by a tendered of the SBNs.

94. For purpose of clarity, RBI has also provided a list of documents expected to be submitted by a tenderer, and the manner of payment, within the ambit of the Rules. The Rules and the Circular thus address the issue of cognizance of the SBNs held by courts of law across the country for various reasons and accord an opportunity to them to get the value in terms of the banknotes which are legal tender. The initiative by the Go/ and RBI is a step towards fulfillment of the expectation expressed in the order dated November 30, 2011 by the Hon'ble High Court, Madras,(Madurai Bench) in the matter of the suo motu Writ Petition (MD) No. 21985 of 2016.

CASE STUDIES OF FOREIGN COUNTRIES SHOWING ADVANTAGES OF DIGITIZATION

95. <u>Use of digital payment modes lower costs:</u>

a. Nigeria: Evaluation of social transfer program revealed that the cost is 20% lower in case of mobile transfer compared to manual cash distribution.

b. South Africa: Cost of disbursing social grants by smart cards in 2011 was one-third that of by manual cash disbursement (R13.50 compared to R35.92).

c. Mexico: Shift to digital payments beginning in 1997, reduced Mexico Government's spending on social welfare, wages and pensions by nearly $1.3 billion or 3.3% annually.

d. Brazil: In Brazil, the BolsaFaniulia program reduced its transaction costs from 14.7 percent of total payments to 2.6 percent when it bundled several benefits onto one electronic payment card

96. <u>Speed of transfer</u>

a. <u>Nigeria:</u> Social transfers by mobile reduced overall travel and wait time for cash transfers to a quarter of what it took for manual cash transactions. The travel time to cash-out point was reduced by 40 minutes compared to manual cash distribution. This excludes 3 hours of wait time involved in manual cash transfer.

97. Increased Control

a. Rome: A field experiment with Filipino migrants in Rome showed that 27% of the sample were interested in a product for direct remittance transfer to schools in the Philippines. In another lab trial, it was found that a "soft" commitment of tagging remittances as one for education increases remittances by 15%

98. Increased security

a. United States: Introduction of Electronic Benefit Transfer (EBT) and thus switching from social cash transfers by paper checks (which need encashment) to electronic debit cards reduced the overall crime rate by almost 10% over next 20 years or 47 fewer crimes per 100,000 population per county over month. This was a direct result of switching social benefits from cash to electronic credit.

99. <u>Increased financial inclusion and increase in women's economic participation and empowerment</u>

a. Nigeria:-There is a suggestive evidence from the social cash transfer program in Niger that the control and greater privacy in case of mobile transfers compared to manual cash transfers, shifts the power and decision making in favour of women who are usually the recipients of the benefit transfers.

b. Kenya: The arrival of mobile money or m-Pesa empowered the women by making it easier for them to receive remittances from husbands working in urban areas.

100. <u>Increased risk management</u>

a. <u>Kenya:</u> According to results of several research, m-Pesa users were more resilient to income shocks (such as job loss, severe illness, or harvest failure) and their household consumption remained the same. In other households, the consumption decreased by 6-10% as a result of such shocks. One of the reasons for the same was that, the m-Pesa users received money from a large number of senders located far away. Digital payments strengthen the informal insurance network among poor households.

b. Rwanda: Results similar to Kenya were observed where people transferred money through mobile to individuals affected by financial shocks. This made it easier for the families using mobile money to absorb such shocks.

101. Increased availability of financial data Malawi:

As a part of an experiment in Malawi fingerprints were collected while applying for loans, in order to obtain positive and negative credit information. This helped the lenders in providing better terms to good borrowers while withholding future loans for defaulters. This directly led to increase of repayment rates of loans.

102. That leave is sought for making any further submissions if so required at the time of hearing. The present affidavit may be read as reply to all the other writ petitions connected to the present writ petition.

103. That in view of the aforesaid submissions, the writ petitions and connected matters pertaining to the challenge to the Cancellation of Legal Tender of existing series of Rs. 500 and Rs. 1000 notes by the Government of India and connected issues be dismissed by this Hon'ble Court with costs.

AND FOR THIS ACT OF KINDNESS THE RESPONDENT SHALL EVER BE DUTY BOUND.

DRAWN BY: FILED BY:

[DEVASHISH BHARUKA] **[ANIL KATIYAR]**
Advocate Advocate for the petitioner
Drawn On: 09.2018
Filed on: 10.2018

IN THE SUPREME COURT OF INDIA
ORIGINAL CIVIL WRIT JURISDICTION
WRIT PETITION (CIVIL) NO. 906 OF 2016

IN THE MATTER OF:

VIVEK NARAYAN SHARMA ..PETITIONER

VERSUS

UNION OF INDIA ..RESPONDENTS

AFFIDAVIT

I, Mr. Ganga Kumar Sinha, Under Secretary (C&C) Government of India, Department of Economic Affairs Coin and Currency Division, Ministry of Finance North Block, New Delhi, do hereby solemnly affirm and state as hereunder:-

1. That I am the Answering Respondent and am conversant with the facts of the case and I am competent to swear this counter affidavit.
2. I have read and understood the contents of the accompanying counter affidavit which are true to my knowledge and belief and nothing material has been concealed therefrom .
3. That the annexures annexed with the counter affidavit are true copies of their respectively originals

DEPONENT

VERIFICATION:

Verified at on this ___ day of October, 2018 that the contents of the above affidavit are true and correct to my knowledge and belief, no part of it is false and nothing material has been concealed there from.

DEPONENT

ANNEXURE R-1

REPORTABLE

IN THE SUPREME COURT OF INDIA

CIVIL/CRIMINAL ORIGINAL/APPELLATE JURISDICTION

WRIT PETITION (CIVIL) No.906/2016

Vivek Narayan Sharma ...Petitioner(s)

Vs.

Union of India ...Respondent(s)

WITH

W.P.(C) Nos.908/2016, 913/2016, 916/2016, WP(C) D.No.37946/2016, W.P.(C) No.929/2016, W.P. (C) No. 930/2016, 943/2016, W.P.(Crl.) No.162/2016, W.P.(C) No. 951/2016, 952/2016, 953/2016, 954/2016, 958/2016, 957/2016, T.P.(C) No.2018-2022/2016, W.P.(C)No.971/2016, 972/2016, SLP (C) No. 35356/2016, T.P.(C)No. 2030 - 2038/2016, W.P.(C)No.978/2016, W.P.(C)D.No. 40114/2016, W.P.(C) No.944/2016,

SLP(C) No.35805/2016, W.P.(C)No.996/2016, 997/2016 T.P.(C) No. 1958-1967/2016 & T.P. (C)No. 1982 -1996/ 2016, W.P.(C) Nos. 1006/2016, 1008/2016, 1009/2016, 1010/2016, 1011/2016 and

SLP(C) No. 36757/2016

ORDER

Writ Petitions are admitted.

Issue notice on the Writ Petitions, special leave petitions and other applications. The respondents may file reply affidavit within six weeks. Rejoinder, if any, within three weeks thereafter.

We have heard the learned counsel for the parties at some length. In our opinion, the following important questions fall for our consideration in this batch of petitions:

(i) Whether the notification dated 8th November 2016 is ultra vires Section 26(2) and Sections 7,17,23,24,29 and 42 of the Reserve Bank of India Act, 1934;

(ii) Does the notification contravene the provisions of Article 300(A) of the Constitution;

(iii) Assuming that the notification has been validly issued under the Reserve Bank of India Act, 1934 whether it is ultra vires Articles 14 and 19 of the Constitution;

(iv) Whether the limit on withdrawal of cash from the funds deposited in bank accounts has no basis in law and violates Articles 14,19 and 21;

(v) Whether the implementation of the impugned notification(s) suffers from procedural and/or substantive unreasonableness and thereby violates Articles 14 and 19 and, if so, to what effect?

(vi) In the event that Section 26(2) is held to permit demonetization, does it suffer from excessive delegation of legislative power thereby rendering it ultra vires the Constitution;

(vii) What is the scope of judicial review in matters relating to fiscal and economic policy of the Government;

(viii) Whether a petition by a political party on the issues raised is maintainable under Article 32; and

(ix) Whether District Co-operative Banks have been discriminated against by excluding them from accepting deposits and exchanging demonetized notes.

Keeping in view the general public importance and the far reaching implications which the answers to the questions may have, we consider it proper to direct that the matters be placed before the larger Bench of five Judges for an authoritative pronouncement. The Registry shall accordingly place the papers before Hon'ble the Chief Justice for constituting an appropriate Bench.

We may now advert to the issues which are of immediate concern. The first issue is about the restriction placed on the District Cooperative Banks to accept deposits or exchange of demonetized currency of Rs.500/- and Rs.1000/-. Two broad aspects have been presented before us. The first is about the complete exclusion of the District Cooperative Banks from accepting deposits or exchanging demonetized notes. The second is about the avoidable financial stress on the District Cooperative Banks because of freezing the deposited demonetized notes received by the District Cooperative Banks between 11th and 14th November 2016, which is stated to be around Rs.8000/-Crore (Rupees Eight Thousand Crore).

The first point whether the decision of the Authority to forbid the District Cooperative Banks from accepting deposits and exchanging demonetized notes, may require detailed hearing. It is only upon acceptance of challenge to that decision, that the bar placed on the District Cooperative Banks can be lifted. We are not inclined to suspend that bar as an interim measure. This is especially when the decision is the outcome of financial policy which the respondents claim to have adopted on the basis of experience. In particular, an apprehension has been expressed about the possibility of demonetized notes being converted or exchanged without proper audit, control or supervision. The District Cooperative Banks, it has been urged, are not directly under the control of the Reserve Bank of India but within the purview of NABARD. The dispensation provided by NABARD is, according to the Attorney General, not in conformity with the strict regime provided under the provisions of Banking Regulation Act, 1949 and the Reserve Bank of India Act, 1934.

Reverting to the second aspect, of District Cooperative Banks being precluded from utilizing the demonetized notes deposited with them between 11th to 14th November 2016 (when it was so permitted by the Reserve bank of India), the learned Attorney General has invited our attention to the written instructions received by him from the Under Secretary to the Government of India dated 14th December 2016. The relevant extract of the said letter reads thus:

> "In this regard, it is to inform that as regards the deposits of Specified Bank Notes (SBNs) collected by DCCBs, the RBI has recommended that the

SBNs collected by the DCCBs between 10th and 14th November 2016 may be exchanged with their linked currency chests after a 100% audit of the veracity of the KYC documents of the SBN depositing customers of DCCB is conducted by NABARD, the supervisor and to the extent of such verified SBNs only. For SBNs deposited by Primary Agricultural Credit Societies (PACS) also, similar 100% audit of the KYC documents of the members of the PACS should be conducted by NABARD and to the extent of such verified SBNs only, exchange value will be given by the linked currency chest. In either case, the linked currency chest will subject those SBNs to usual checks, especially relating to finding out FICN."

For that purpose, suitable Notification can be issued by the Competent Authority within two days. We commend to the Competent Authority to do so.

Learned counsel for the District Cooperative Banks, however, submitted that the Reserve Bank of

India must assure that the entire amount offered by the District Cooperative Banks for exchange after due verification in the form of demonetized notes, will be duly replaced by commensurate amount of legal tender notes contemporaneously. The learned Attorney General on instructions submitted that the policy of replacement of legal tender notes as applicable to Public Sector Banks and other Banks will be applied even in the case of District Cooperative Banks for exchange of demonetized currency with the legal tender currency. We accept the assurance given by the learned Attorney General in this behalf.

The other broad point was about extending the time limit for exemption for use of demonetized currency notes of Rs.500/- and Rs.1000/- at specified counters as per the relevant Notifications issued in that behalf by the Reserve Bank of India. It was contended that the exemption period provided in the concerned notification is expiring. Hence, it will not be possible to deposit the demonetized notes at specified counters thereafter, even in case of emergency situation like hospitalization, travel by Railway or Air etc. In our opinion, whether the exemption period should be extended or not must be best left to the judgment of the Government of the day with a hope that the Government will be responsive and sensitive to the problems encountered by the common man. Accordingly, we decline to issue any interim direction to the Government in the matter of extending the period of exemption and leave it open to the Government to take appropriate decision in that behalf, as may be advised.

The other serious grievance made by the petitioners is about the denial of right to withdraw the prescribed amount of Rs.24,000/- per week per account holder, in spite of Notification issued by the Reserve Bank of India permitting such withdrawal. It was submitted that if the Government has issued such Notification after due consideration, it is obliged to ensure that its commitment made under the said Notification is implemented without any exception. The ground reality, however, contends learned counsel, is that the Banks are refusing to pay full amount of Rs.24,000/- per account holder per week on the ground of non-availability of enough volume of legal tender currency. According to the learned Attorney General, the Government has already made it amply clear that it would take around 50 days time to streamline the cash flow. That period is still not exhausted. He submits that as of now the Reserve Bank of India has been able to infuse around Rs.5,00,000/-Crore (Five Lakh Crore) of the new legal tender notes in the form of Rs.500/- and Rs.2,000/-. That is almost over 40% of the amount of demonetized notes already deposited with the Banks. Further, the Authorities are working to the best of their ability to defuse the crisis of cash flow situation by printing new notes. It is further submitted that for the nature of decision taken by the Government - to unearth the black money or unaccounted money and to dry up the terror fund and defeat the attempt of circulation of large scale counterfeit currency, maintaining complete secrecy of such a decision was imperative. For that reason, new currency notes could not be printed well in advance. He submits that the old demonetized notes will be replaced by new legal tender notes in the form of Rs.500/- and Rs.2000/- progressively in right earnest. Considering the stand taken by the learned Attorney General, we may commend to the Authorities to fulfill their commitment made in terms of the stated Notification permitting withdrawal of Rs.24,000/- per account holder of the Bank per week to the extent possible and review that decision periodically and take necessary corrective measures in that behalf.

In our opinion, besides the observations made hitherto, no other direction can be given at this stage by way of an interim relief.

That takes us to the Transfer Petitions filed by the Union of India for withdrawing all Writ Petitions/ proceedings pending in the various High Courts across the country and to hear those cases along with the Writ Petitions pending in this Court. In our opinion, it would be just and proper to withdraw all the Writ Petitions/proceedings pending in different High Courts across the country and to be heard by this Court along with the Writ Petitions which are already pending in this Court raising same or similar issues, to avoid multiplicity of hearing and conflicting decisions on the same subject matter. Accordingly, we issue notice in the respective Transfer Petitions and by way of interim direction, stay the further proceedings of the Writ Petitions/proceedings in the concerned High Court.

We further direct that if any other Writ Petitions/proceedings are pending in any High Court, further hearing of those matters shall also remain stayed in terms of this order.

We further direct that no other Court shall entertain, hear or decide any Writ Petition/proceedings on the issue or in relation to or arising from the decision of the Government of India to demonetize the old notes of Rs.500/- and Rs.1000/-, as the entire issue in relation thereto is pending consideration before this Court in the present proceedings.

We make it clear that petitioners before the High Court(s) or any other Court in India in respect of proceedings already instituted on the subject matter under consideration before this Court, will be free to intervene in the Writ Petitions pending consideration before this Court on the subject matter of demonetization of old currency notes of Rs.500/- and Rs.1000/-, if so advised.

The Registry shall place the matter before the Chief Justice for further orders.

....................................CJI

....................................J
(A.M. Khanwilkar)

....................................J
(Dr. D .Y. Chandrachud)

New Delhi,
Dated: 16th December, 2016

//True copy//

ANNEXURE R-2

BCG

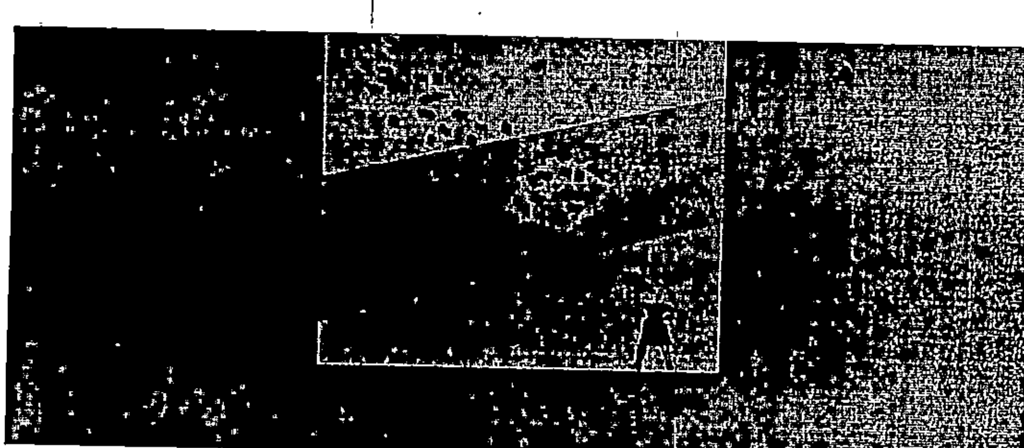
THE BOSTON CONSULTING GROUP

GLOBAL PAYMENTS

2015

LISTENING TO THE CUSTOMER'S VOICE

The Boston Consulting Group (BCG) is a global management consulting firm and the world's leading advisor on business strategy. We partner with clients from the private, public, and not for profit sectors in all regions to identify their highest- value opportunities, address their most critical challenges, and transform their enterprise. Our customized approach combines deep insight into the dynamics of companies and markets with close collaboration at all levels of the client organization. This ensures that our clients achieve sustainable competitive advantage, build more capable organizations, and secure lasting results. Founded in 1963, BCG is a private company with 82 offices in 46 countries. For more information, please visit bcg.com.



SWIFT is a member-owned cooperative that provides the communications platform, products and services to connect more than 10,800 banking organizations, securities institutions and corporate customers in over 200 countries and territories. SWIFT enables its users to exchange automated, standardized financial information securely and reliably, thereby lowering costs, reducing operational risk and eliminating operational inefficiencies. SWIFT also brings the financial community together to work collaboratively to shape market practice, define standards and debate issues of mutual interest. For more information, please visit swift.com.

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GLOBAL PAYMENTS 2015

LISTENING TO THE CUSTOMER'S VOICE

STEFAN DAB

MOHAMMED BADI

LAURENT DESMANGLES

GERO FREUDENSTEIN

ALENKA GREALISH

FEDERICO MUXI

PEDRO RAPALLO

OLIVIER SAMPIERI

YANN SENANT

KUBA ZIELINSKI

CONTENTS

INTRODUCTION

THE PAYMENTS AND TRANSACTION-BANKING businesses are evolving at a dizzying pace. The advance of digital technology, the entry of nontraditional players with compelling value propositions, and changing preferences in the way consumers pay for goods and services in their everyday lives have considerably disrupted the industry landscape.

Which direction will consumer payment habits take in the future? How fast will people and businesses adopt the latest digital technology and leave traditional payment methods behind? How can banks not only handle the arrival of new digital players but also use their own vast infrastructure and customer knowledge to remain competitive in the shifting market climate? Will joining forces with nontraditional players, rather than treating them as adversaries, prove to be a more profitable path forward? These are among the most pressing questions of the moment.

One industry characteristic that has not changed is that payments and transaction- banking businesses remain critical elements of the banking industry and the global financial -services landscape. Because they are a critical source of reliable revenues and a linchpin of customer relationships and loyalty, their importance will continue to grow. But competition will intensify. In order to stand out in a very crowded field, payments players must differentiate themselves digitally, refine their customer- centric strategies, and raise their execution skills. Above all, they must listen to the customer's voice and react accordingly.

In this thirteenth edition of The Boston Consulting Group's Global Payments report, we offer a comprehensive regional overview of the industry. We then discuss the findings of a recent BCG survey of nearly 5,500 consumers in four countries-France, Germany, the U.K., and the U.S. that we conducted with three goals in mind: discovering why the adoption of digital payments has been relatively slow to date; identifying current consumer needs, preferences, and pain points in payments; and formulating the actions that banks can take to unlock the potential of consumer digital payments. Finally, we take a detailed look at the wholesale transaction-banking industry, specifically focusing on how banks can beef up the treasury and trade services that they provide to their clients. In preparing this report, we have for the fourth consecutive year collaborated with SWIFT, the global provider of secure financial- messaging services.

This year also marks the second edition of BCG's Global Payments Model Interactive, available on bcgperspectives.com, which explores how regions and segments of the payments market will shift from year-end 2014 through 2024. This feature provides extensive global detail, including interactive charts on the volume and value of noncash transactions as well as on revenues.

In the Global Payments model, payments revenues include direct and indirect revenues generated by noncash payment services (excluding interbank transfers). They are the sum of the following:-

- Account revenues: spread income on current account balances (also known as checking or demand-deposit accounts) and account maintenance fees

- Transaction revenues: transaction-specific revenues on cards (interchange fees, merchant acquiring fees, and currency conversion fees for cross-border card transactions); fees per transaction on a percentage or fixed basis for non-card payment types; fees for overdrafts and nonsufficient funds; and monthly or annual card membership fees

- Credit card spread (net interest income) and penalty fees

Retail payments are transactions initiated by consumers, and wholesale payments are transactions initiated by businesses or governments.

As always, our aim in Global Payments 2015:

Listening to the Customer's Voice is to provide institutions that are active in the payments and transaction- banking businesses with a clear understanding of the fundamental changes shaping the industry, as well as to offer recommendations on which specific actions should be taken by various types of players in order to achieve or maintain market-leading positions. Today more than ever, no institution can afford to stand pat.

GLOBAL OVERVIEW
DISRUPTION AND OPPORTUNITY

PAYMENTS AND TRANSACTION-BANKING businesses will face both significant disruption and immense opportunity over the next decade, with some $ 900 billion in industry revenue growth up for grabs through 2024. The disruption will have many sources, among them regulatory measures that adversely affect price realization and the customer experience, as well as new market entrants that are gaining traction by leveraging advanced technology to solve pain points and offer creative value propositions. The principal opportunities lie in continuing to capture the migration from cash to electronic payments, adapting to the new digital world, delivering innovative value-adding services, and effectively serving the unbanked and underbanked.

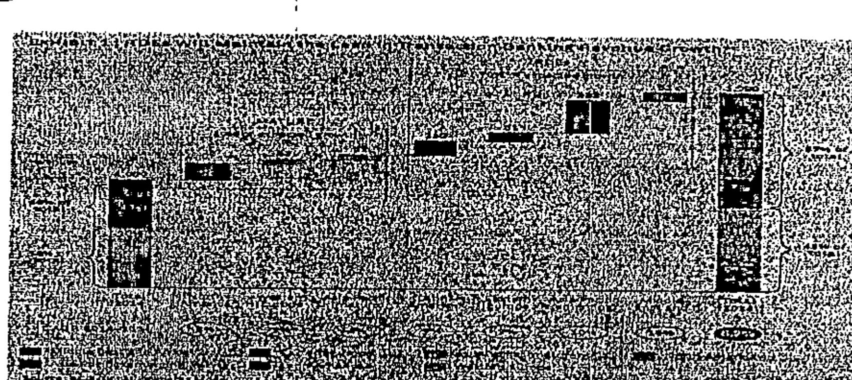
A Dynamic Arena

Transaction banking remains a dynamic arena on a global level, as evidenced by the significant amount of venture capital-roughly $76 billion-that has gone into payments-related businesses since 2010. Moreover, large technology companies are investing heavily in the payments space, ushering in a new world of digital payments as well as spawning a herd of new competitors (and potential partners) for traditional players. Among the primary drivers of change will be digital payment solutions that can be used across different point-of-sale (POS) channels (such as in store, browser, and in-app), new payment rails that deliver so-called instant payments, and perhaps crypto currencies and block chain technology.

Such developments will dramatically change how consumers and businesses select payment-related services (and credit products), how they transact, and how they engage with their providers.

Looking ahead, it's clear that the nimblest stakeholders-those that are quickest to adapt their business and operating models to the shifting landscape-will seize the bulk of the $900 billion revenue-growth prize to be captured over the next decade. Also critical to winning will be a customer-centric strategy, one that truly grasps customer needs, expectations, and pain points, and addresses these issues efficiently and effectively.

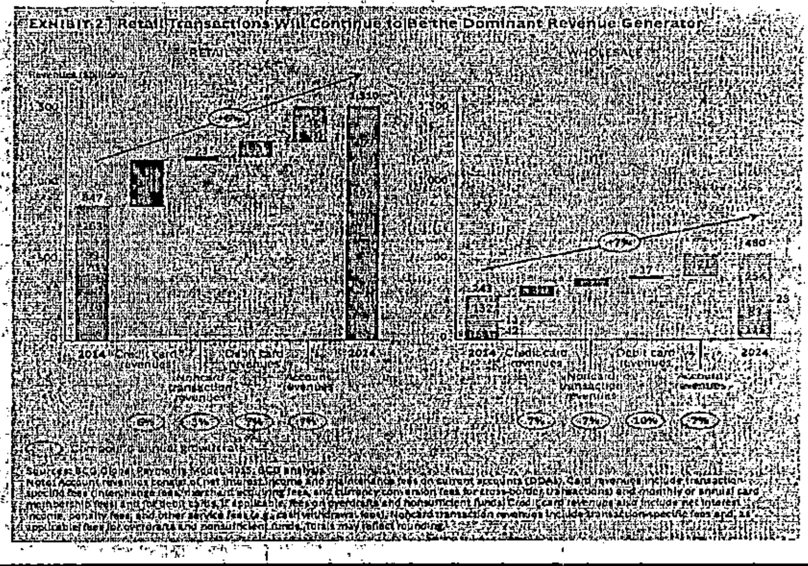
Revenues. In 2014, global transaction-banking revenues were nearly $1.1 trillion, or about 27 percent of total global-banking revenues. (See Exhibit 1.) By 2024, they are projected to reach nearly $2 trillion, with growth driven by a combination of account revenues (40 percent), transaction revenues (34 percent), and non-transaction card revenues (26 percent; these include monthly or annual fees, credit-card net interest income, and other types of fees). Transaction revenues are being propelled by rising transaction values and



Volumes-fueled by macroeconomic growth, migration from cash to e-payments, and broader financial inclusion-which in turn are helping to offset falling revenues per transaction in many regions. Moreover, all variables in the account-revenue equation-the number of accounts, account balances, and spread income-are increasing, driven by positive macroeconomic and interest-rate trends.

Varying Growth Patterns. It's no surprise that rapidly developing economies (RDEs, also commonly referred to as emerging markets), most of which are moving toward higher rates of financial inclusion and greater migration from cash to e-payments, are enjoying stronger growth in all metrics than are mature markets. They will continue to do so. Compared with a year ago, however, retail (consumer-initiated) payments revenue growth in RDEs has been slowed by softening macroeconomic drivers such as GDP and per capita income.

Retail and Wholesale Payments Differences. Although retail payments accounted for a small fraction of global transaction values in 2014 (11 percent), they generated 78 percent of total payments revenues and will account for a projected 73 percent of total revenue growth through 2024. The revenue mix will shift slightly toward account revenues. Wholesale (business- and government-initiated) payments are projected to post stronger annual revenue growth, at a CAGR of 7 percent compared with 6 percent for retail payments, with account revenues generating just over half of that growth. (See Exhibit 2.) Higher wholesale growth is being driven by stronger credit-card and other transaction revenue expansion, owing to lighter price pressure than in retail.



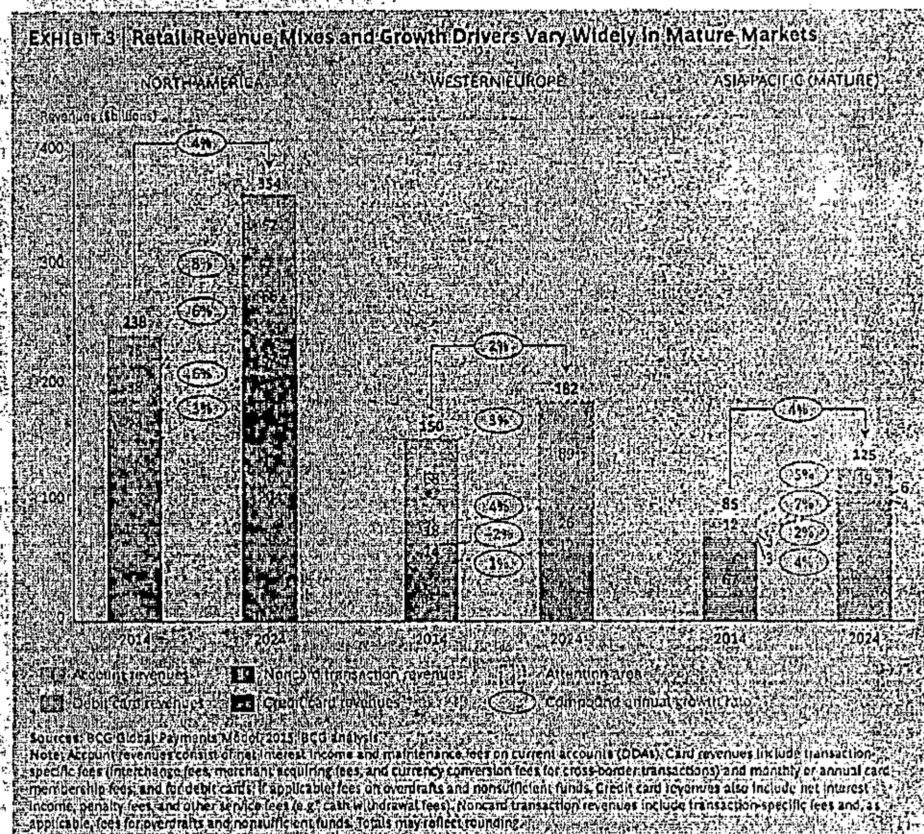
REGIONAL RETAIL TRENDS

There are significant differences in retail payments trends across regions. The greatest diversity is found among mature markets, where revenue mixes and growth drivers differ considerably, although impediments to growth are similar. (See Exhibit 3.) Indeed, most mature markets are grappling with modest macroeconomic growth, regulatory pressure on prices, and persistent flat yield curves.

Nonetheless, some bright spots for revenue growth can be found in mature markets. In North America, for example, credit cards continue to be a highly attractive business and will be the key revenue battleground. In Western Europe, where card revenues have been sharply reduced by regulation, the keys to growth include rethinking daily-banking value propositions and improving price realization to raise account revenues. In mature Asia-Pacific markets, banks should focus on a current-account and credit-card strategy aimed at capturing the ongoing migration away from cash.

North America. North America remains the largest payments and transaction-banking market globally, generating $238 billion in total retail payment revenues in 2014 (28 percent of the worldwide total), with a projected CAGR of 4 percent through 2024.

Credit cards are the dominant revenue engine in the U.S., representing 60 percent of retail payment revenues in 2014. Moreover, credit cards generate the highest return on assets across U.S. retail financial products (close to 2.5 percent, with home-equity loans ranked second at 1.2 percent). Demand deposit account (DDA), debit card, and non-card transaction revenues accounted for the remaining 40 percent. Credit cards are also the lead revenue generator in Canada.



Looking ahead, credit-card revenues-now in a favorable point in the economic cycle, with net interest margins relatively strong and charge-offs low-will be driven by cyclical factors, systemic trends, and competitive shifts. The positive environment may turn negative, however, with a steepening yield curve that will push the cost of funds upward, weakening economic growth and increasing charge-offs. Moreover, several systemic trends will put pressure on average interchange income. For example, merchants may campaign for lower interchange rates if fraud losses drop as a result of the migration to EMV, tokenization, and biometric authentication. Furthermore, m-wallets will drive a move from card-not-present to card-present transactions.

In addition, there will be continued power shifts across the value chain. Co-brand partners are already wielding more clout in their negotiations with issuers, increasing their revenue share and lowering the discount rate that they pay on their co-brand cards. Meanwhile, issuers continue to fuel an arms race in rewards, eroding net interchange. It is looking more likely that at least one bank will launch a three-party network, leveraging its issuing and merchant-acquiring businesses and changing the business model to generate a win for all stakeholders.

To overcome such challenges and capture a healthy share of the expected revenue growth, banks in North America need to pursue a multifaceted strategy. First, as top issuers push their own branded cards, achieving excellence in penetrating core DDA customers will be increasingly important. Banks need to leverage their extensive product and channel platforms and broaden their value propositions to consumers, going beyond traditional cross-selling activities and creating product bundles aimed at specific customer segments (such as aspiring homeowners). They also need to offer relevant products based on "trigger" events such as college graduation or the birth of a child.

Second, issuers need to increase the value-adding services that they bring to their co-brand partners. Doing so will require them to contribute to their partners overall P&L-not just the card component-and will entail working with their partners on sophisticated marketing efforts to increase loyalty and enhance customer engagement.

Other obvious means of improving retail payment economics involve reducing costs and boosting overall efficiency. Cost reduction opportunities lie in slimming down the organizational structure and implementing lean operations, including optimizing both in-sourcing and outsourcing. BCG has found that organizational simplification can result in an 8 to 10 percent savings in total costs, and that improving procurement can reduce related costs by more than 20 percent, depending on the issuer's starting point and willingness to be aggressive.

Clearly, with $116 billion in revenue growth up for grabs over the next decade in North America, there will be numerous competitive battlegrounds. In the short run, one wave of disruption is being generated by mobile payments initiatives, including m-payments at the point of sale, m-commerce, and in-app purchases. Mobile payments-which are unlikely to grow to beyond 30 percent of U.S. retail transactions by 2020 (including card-on-file, POS, and in-app purchases)-will not rapidly replace plastic cards. After 2020, disruption will potentially come from the launch of instant payments solutions and perhaps block chain technology.

Western Europe. Payments revenues are under structural pressure throughout Western Europe. Indeed, interchange regulation set to take effect in October 2015 will result in an estimated total revenue loss of €5 billion per year for card issuers. We are also seeing a significant reduction in interest margins on current accounts (owing to the continued low-interest-rate environment) with no immediate recovery on the horizon. At the same time, increasing e-commerce activity and the gradual elimination of cash from physical points of sale is fueling growth in payments volumes.

Regulation remains a key theme in European payments.

Regulation remains a key theme in European payments, with governments hoping to stimulate further adoption of noncash payment instruments, remove barriers to competition for both banks and other players, and enhance security requirements for both mobile and online payments. Much of this regulation is centered on Payment Services Directive 2 (PSD 2), which aims to spur competition and innovation both through allowing access to customer accounts by third-party payment-service providers and through putting new security rules in place. PSD 2 is set to be submitted to the European Parliament later this year and incorporated into the regulatory framework over the course of 2016.

With the access-to-accounts rule introducing new competition from third-party providers and raising both costs and risks for incumbents, banks should investigate opportunities to strengthen their client relationships through superior interfaces, notably mobile ones, and to introduce value-added services, such as embedding account aggregation into their digital interfaces.

Aside from heightened competition on digital banking interfaces, we expect digital payment solutions at the point of sale to become a key battleground. Very few banks have managed to successfully launch their own digital-payment solutions, owing to delays in product development or an inability to bring a compelling value proposition to consumers and merchants. The fact that global tech giants such as Apple Pay and Android Pay see Europe as a highly attractive territory will force banks to develop an appropriate strategy. In particular, we expect that banks will cooperate more closely with global card networks to develop and promote credible alternatives to the offerings of digital giants. Such cooperation will require banks to support a higher level of standardization to ensure scale and wider adoption. As a consequence, banks will need to rethink how best to differentiate themselves.

India stands out for its bold government-led initiatives to promote financial inclusion.

We're also witnessing greater interest in instant-payment solutions. Many countries- such as the Netherlands, Finland, and Italy- are either implementing or planning to develop a national instant-payment scheme. This trend will gain the most momentum in countries that have a proactive payments regulator, an outdated payments infrastructure, or a critical mass of local banks with real time accounting systems. Yet despite agreement on a common definition of instant payments by the Euro Retail Payments Board, there has been no clear progress toward a pan-European instant-payment scheme. Although likely to become standard in the long run, the business case for instant payments remains questionable in the medium term. Banks will therefore need to carefully think through the prioritization of their payments investments.

Ultimately, we believe that Western European banks are still competitively well positioned because the accounts and payment services they offer enjoy higher levels of trust than those offered by nonbank players. Nonetheless, banks need to act now on three key levers:

- Rethink daily-banking offerings and execute a fundamental review of pricing structures, considering the financial needs and willingness to pay of different customer segments.

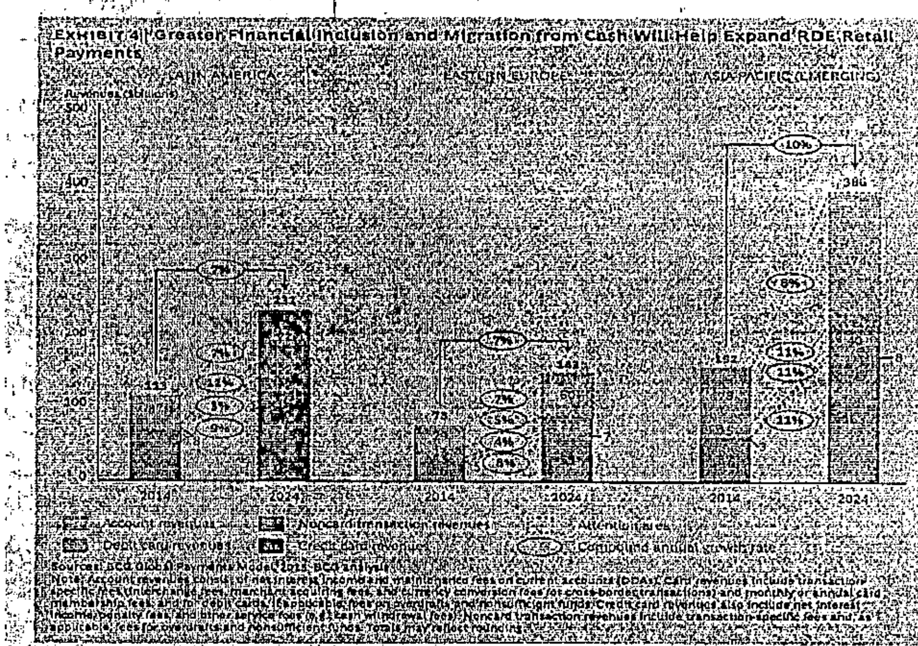
- Beef up digital-banking interfaces in order to be best-in-class relative to local peers.

- Decide on a clearer path for future digital-payments initiatives, such as developing proprietary m-wallets, joining with peers to develop local wallets, or partnering with global card networks or tech giants.

RDEs. Payments-related businesses in RDEs continue to benefit from positive macroeconomic and socioeconomic trends. While many countries have experienced a slowdown in GDP growth, a steady rise in financial inclusion coupled with the push for migration away from cash will continue to generate above-average growth in both payment values and payments revenues. (See Exhibit 4.) Leading the growth will be the emerging markets of Asia-Pacific and Latin America, followed by Eastern Europe.

While the pace of growth will vary across regions, the overall digital future is bright. Ongoing government support, steady investment in payments-related innovation, and increases in smartphone adoption will be key drivers. Both incumbents and new digital-payments players, as well as social media and e-commerce giants, will continue to reshape the payments landscape and ensure the success of new digital platforms.

India. Among emerging markets, India stands out for its bold government-led initiatives to promote financial inclusion and digital innovation, which are driving above-average growth in noncash payments. In 2014, India launched a financial inclusion campaign that generated 125 million accounts within six months. In addition, the Reserve Bank of India (RBI) has established new guidelines to license so-called payment banks-institutions whose objective is to improve financial inclusion by providing basic banking and remittance services to migrant workers, low-income households, small businesses, and other underserved sectors. More than 40 entities have applied, including startups and partnerships between leading telcos and banks, and the RBI has "in principle" approved more than 10.



Such initiatives have fueled the strong adoption of digital payments and the rise of new market entrants. Mobile-banking transactions have increased more than threefold over the past two years, hitting 150 million in 2014. And mobile-wallet transactions have overtaken m-banking transactions. Prepaid payment-instruments providers such as Paytm and MobiKwik (which offer m-wallets) have been gaining traction and have motivated banks to invest in their own digital-payment offerings.

China. The payments market in China is still booming, with growth in noncash payment values expected to range between 10 percent and 15 percent annually over the next decade, depending upon the payment type. Debit and credit cards will continue to be major drivers of growth. In 2014 alone the number of bank cards issued jumped by 21 percent to roughly 5 billion. Mobile-payment values were the hot spot, rising by a reported 134 percent.

The Chinese market is not only growing but opening up as well. In the past, state-controlled China UnionPay was the only player permitted to provide clearing services for renminbi-denominated bank-card payments. But since June 1,2015, other companies-both domestic and foreign-have been able to submit applications for a clearing-services license.

Nonbank players have made a strong entrance in payments with their e-marketplaces and attendant e-wallets-particularly Alibaba with Alipay and Tencent with Ten-pay-and are aggressively trying to extend their acceptance in high-traffic apps (such those related to taxi hailing and online shopping). Moreover, they are encouraging users to link their bank accounts to their e-wallet through special promotions. In 2014, during the Spring Festival, Alibaba and Tencent offered digital "red envelopes" with links to cash coupons worth $97 million and $81 million, respectively, to encourage customers to link their bank accounts.

Looking ahead, there will be several areas of disruption. Smaller cities that are under-served by local banks are prime targets of major nonbank players, which are planning to offer online pay, mobile pay, O2O pay (online ordering with offline service and payment), and other products. China's central bank recently issued guidelines for transaction limits on online payments, triggering strong debate among banks and nonbanks regarding the impact on growth and innovation. As new regulations reshape the competitive landscape, leading players will likely drive further market consolidation.

Central Europe. In central Europe, Poland stands out for being ahead of the curve in innovating and adopting emerging payments technology. For example, 75 percent of POS terminals support near-field communication (NFC), and NFC transactions represent more than a third of the total for global card networks. Competition among banks to innovate has heated up, with m-Bank leading the charge and gaining competitive advantage owing to its superior digital customer experience.

In addition, banks are working together to establish a strong digital infrastructure to spur m-payments. A local payment scheme, Blik, initiated by Poland's six largest banks, was launched in February 2015. The participation of large banks and merchant acquirers means that the scheme has significant adoption potential. In parallel, several Polish banks are piloting the launch of mobile, contactless payment services based on host card emulation.

Latin America. Incumbent banks, which are traditionally slow to innovate, have taken the initiative over the past several years to promote payment electronification and cash substitution, hoping to outcompete new entrants. Examples include m-wallets (such as Stelo in Brazil and Todo Pago in Argentina), the launch of local payments schemes (such as Elo in Brazil), and investments to increase POS penetration-often including NFC. In addition, several governments have been actively promoting e-payments by providing tax incentives, changing regulatory frameworks, and adopting social-transfer e-payments.

One interesting development in some countries is that leading players are leveraging payment -processing platforms owned by bank coalitions in order to develop scalable, system wide, digital innovations (such as Prisma Medios de Pago in Argentina).

RDE Lessons Learned. One harsh lesson learned by incumbents that did not invest sufficiently in digital payments over the past five years is that new entrants are filling the gaps and gaining traction-in some cases significant traction, as in China. Banks that want to regain or improve their market position and adapt to the new world of digital payments must therefore pursue a multifaceted, customer-centric digital strategy, spanning the front-end customer interface to back-end systems. For example, Axis Bank in India has made significant investments in upgrading its payments infrastructure and improving its ability to innovate and go to market rapidly. Elo in Brazil has excelled in customer centricity by understanding the emerging middle class's pain points in payments and solving them. In Poland, m-Bank has reinvented its consumer reward program through digital innovation, with strong results.

UNLOCKING THE POTENTIAL OF CONSUMER DIGITAL PAYMENTS

A **NEW WORLD OF CONSUMER** digital payments is coming into view, spawned by an increasingly connected landscape of people, devices, and social-media platforms. Ubiquitous connectivity, biometrics, tokenization, cloud computing, and the Internet of Things are just a few of the digital trends that will affect the way consumers transact and interact with their banks. These dynamics, moreover, will spur new value propositions that, in turn, will alter the competitive landscape.

There have been myriad digital-payment initiatives, but few have achieved scale.

To better understand how banks can advance in digital payments, BCG carried out a survey of nearly 5,500 consumers in four countries- France, Germany, the U.K., and the U.S. Our objective was to grasp why the adoption of digital payments has been relatively slow to date, as well as to identify current consumer needs, preferences, and pain points. Based on our findings and extensive client work, we are able to outline actions that banks should take to unlock the potential of consumer digital payments, and at the same time successfully adapt to the entry of new and powerful non-bank players into the market. Overall, banks must first understand why traditional payment methods remain resilient, then determine how best to seize the digital opportunity.

Why Traditional Payment Methods Remain Resilient

Over the past ten years, there have been myriad digital-payment initiatives. Few have achieved sufficient scale. Traditional payment methods, notably cards, remain predominant. For example, BCG estimates that barely 1 percent of global retail sales originate from mobile phones. Even online, where the use of new payment forms has been greatest, general-purpose cards continue to prevail with a share of roughly 70 percent.

The primary reasons for the slow uptake of digital payment methods are threefold: a lack of compelling value propositions that outperform traditional payment methods and reward structures; persistent data privacy and security concerns; and, as a consequence, insufficient merchant acceptance and consumer comfort.

Lack of Compelling Value Propositions. There have been few cases of value propositions strong enough to alter consumer behavior in payments. In our survey, three-quarters of respondents, on average, were generally satisfied with currently available means of payment for POS purchases. (See Exhibit 5.) Continued enhancements of card products- such as tighter security with EMV, improved online authorization, tokenization, and innovative reward programs-as well as ever-increasing consumer penetration and merchant acceptance have enabled cards to remain dominant even in new channels (such as in-app).

Data privacy and security concerns remain significant barriers to digital adoption.

Indeed, it's only when banks and payments networks have ignored consumer and merchant pain points that alternative payment methods have managed to take off. PayPal, for example, has gained traction in countries where credit-card penetration is relatively low, where there is no online debit facility (such as Germany), or where small e-mer-chants have struggled to obtain an acquiring account that enables them to accept cards (such as France and the U.S.).

Data Privacy and Security Concerns. Our survey confirmed that worries about data privacy and security remain significant barriers to digital adoption. (See Exhibit 6.) Moreover, we found that if providers do not alleviate these concerns, consumers will not be interested in taking advantage of adoption incentives (such as deals and offers) or trying value-adding functionality (such as spending-management tools), even though they find such features attractive.

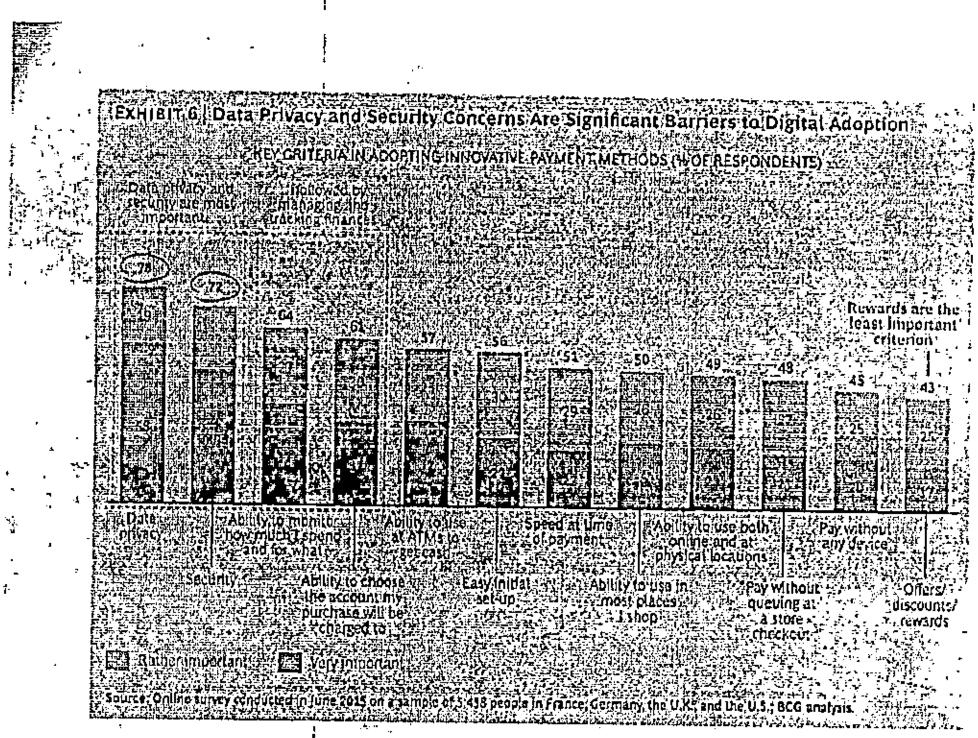
To be sure, when it comes to consumer trust with regard to security and payment privacy, our survey found that banks were the clear winners. This finding has important implications for the leadership role that banks can play-and the negotiating power they can wield-with potential partners.

EXHIBIT 5 | Consumers Are Generally Satisfied with Traditional Payment Methods

SATISFIED RESPONDENTS (%)	POS	BROWSER	SMARTPHONE
Cash (or cash on delivery)	81	63	NA
Credit or debit card	83	79	78
Credit or debit card on file	NA	81	81
Prepaid card	70	77	75
Bank account transfer	NA	85	83
PayPal	65	73	70

Source: Online survey conducted in June 2015 on a sample of 5,438 people in France, Germany, the U.K., and the U.S.; BCG analysis.
Includes responses of "very satisfied" or "rather satisfied" for the specific payment type; NA = not applicable.

Insufficient Merchant Acceptance and Consumer Comfort. As both incumbents and new nonbank entrants know, it is very difficult to generate a virtuous consumer-adoption and merchant-acceptance circle. Important lessons have been learned over the past decade, however. In the online world, achieving sufficient merchant acceptance requires either the ownership of a popular market- place (such as eBay with Paypal, or Alibaba with Alipay) around which to build a strong value proposition, or a consortium of banks deciding early on to cooperate in developing a specific solution (such as iDEAL in the Netherlands). In the physical world (in mature markets), sufficient merchant acceptance requires partnering with card issuers and infrastructure providers.



place (such as eBay with Paypal, or Alibaba leverage the existing payments infrastruc-

Yet merchant acceptance alone will not drive greater consumer adoption. Consumers must find value in using a new payment type or form factor and feel comfortable using it. Even if providers devise compelling value-adding features and alleviate security concerns, adoption will be gradual. As the continued use of cash demonstrates, consumers do not rapidly switch to a new payment type, no matter how attractive it is. Recent large entrants such as Apple Pay, Android Pay, and Samsung Pay have clearly taken note of these lessons. They are offering advanced security, striving to achieve broad acceptance across POS channels, and partnering with banks and global card networks to leverage the existing payments infrastructure. Their future plans include loyalty rewards and broader shopping-related services. Their go-to-market and user-experience expertise, combined with deep funding and a strong drive to expand their broader ecosystems, will help them succeed in spurring adoption (although uptake will likely vary by country).

Looking ahead, new nonbank entrants do not appear to present a significant competitive threat to banks in Europe and North America in the short term because their priorities are not to capture payments revenue streams or to become full-fledged banking-service providers. Their entrance could, however, disrupt the competitive landscape, enabling issuers that excel at harnessing m-wallets' potential to gain greater market share. By contrast, in China, nonbank entrants into the payments arena pose a significant threat to incumbents. Major e-commerce players such as Alibaba and Tencent, for example, are rapidly expanding their financial-services offerings.

There are longer-term risks in mature markets, however, and they are potentially high. For example, if an m-wallet provider becomes a dominant player, it could try to control customer access and influence behavior. The provider could add functionality that enables customers to optimize their use of banking products (such as those related to credit, savings, and rewards), resulting in weaker relationships between customers and their banks and higher switching rates. An m-wallet provider could also offer a reward program superior to those of banks. What's more, it could use the threat of exclusion from its m-wallet to raise its revenue share requirement-say, from 15 to 20 basis points in the U.S.

How Banks Can Seize the Digital Moment

Banks must take decisive action along several dimensions in order to ensure their place as key providers of digital payments and related value-added services. First, the banking industry as a whole must retain a leadership position in standards adoption, advanced security measures, and customer education. Second, banks as individual providers must differentiate themselves.

Banks should focus on smart partnering rather than going it alone.

The Banking Industry as a Whole. Banks (along with card networks and clearing and settlement systems) remain at the center of the payments universe. They bring critical infrastructure, valuable experience (especially in areas such as fraud detection and regulatory compliance), and customer contact. At the highest level, banks need to educate consumers about digital payments and their added value. In BCG's survey, 55 percent of respondents either found no value in m-wallets or had never heard of them. Working with card networks, the banking industry has an important role to play in ensuring that security and communication standards are implemented, protocols are followed, and platforms are open with full transaction visibility.

Security is paramount, of course. Banks, along with card networks and merchant acquirers, need to drive the securing of cards on file through tokenization, create better 3D Secure customer flows, and educate consumers on security and privacy features. While advanced biometric-based security is a powerful tool, our survey found that only 45 percent of respondents found the "pay using biometric identification" option as "rather attractive" or "attractive." Hence, biometrics will require further promotion by m-wallet providers and other stakeholders.

Banks as Individual Providers. In order to sufficiently differentiate themselves and prosper in the new digital world, individual banks need to form smart partnerships, enhance consumer engagement linked to payments, optimize the overall consumer banking experience, and experiment with next-generation technology.

- *Form smart partnerships.* In our view, banks should focus on smart partnering rather than going it alone. How banks approach partnering will vary by country, depending on each nation's specific ecosystem, innovation level, customer pain points, and consumer willingness to change payments behavior. In markets with concentrated banking sectors, banks could succeed by working together to build a superior domestic m-wallet or collaborating with a global card network to leverage the latter's experience and global platform. Joint ventures work best in markets where banks have a history of positive collaboration (such as in the Netherlands), and would likely have a strong advantage over third-party wallets. Yet even in these markets, success will depend highly on the ubiquity of NFC and effective customer promotion.

Banks in an increasing number of markets have an opportunity to partner with Apple Pay, Android Pay, and Samsung Pay. While such partnerships enable customers to make their preferred m-wallet choices, banks need to establish a strong negotiating position, leveraging their assets (such as established customer trust and longstanding relationships) to ensure that they deliver value where their partner cannot. In markets where banks have been mobile-payments innovators (such as Australia), they will have a relatively strong negotiating position.

In fragmented markets with low bank concentration and multiple mobile networks, partnering with a dominant network or a device manufacturer may be the best path. Accords with device manufacturers tend to be less challenging than those with mobile network operators because there is less conflict of interest and less ambiguity regarding who "owns" the customer.

The digitization of card credentials and biometric authentication have profound implications for banks.

- *Enhance consumer engagement linked to payments.* The advent of smartphones and mobile apps is providing banks with a unique opportunity to address evolving customer needs, both enhancing and increasing the frequency of interactions and thereby strengthening relationships. Indeed, BCG's survey showed that consumers are hungry for more control over their transactions and greater visibility with regard to their finances. To meet such needs, banks could offer advanced mobile features, such as the ability to dispute or flag a transaction as potentially fraudulent, receive personalized alerts, have flexible rewards redemption, or turn a card on or off. Affluent consumers, in particular, are seeking preferential treatment (for example, promotions for successful mobile apps such as Uber) and unique offers (for example, privileged access to an event) that can be readily delivered through a mobile app.

Banks also have access to valuable new data-such as location-based and context-aware information generated by the use of m-wallets and mobile apps-that they can leverage to improve fraud detection and provide more personalized loyalty programs. Such data can be extremely useful, but banks must be careful not to overstep customer-privacy preferences. BCG estimates that two-thirds of the total value potential of big data is at risk if stakeholders fail to establish proper restrictions and abide by them.

- *Optimize the overall consumer-banking experience.* As long as banks provide the current account (DDA), they have a critical competitive advantage over nonbank players in helping customers manage their finances and maximize their rewards. Banks must ensure, however, that their mobile app delivers a superior mobile experience (such as actionable alerts) and is not merely a miniaturization of online banking. Banks will be required to observe usage patterns and solicit customer input to continually enhance their apps. Our recent work with major banks has demonstrated that there remains vast potential to enhance the consumer offering in mobile daily banking.

Banks can, for example, add various functions to enable customers to readily manage their cash flow and credit needs, including budget management tools such as customized overspending alerts as well as easy calculators to determine the best way to finance a big-ticket item. Banks could also link products, rewards, and offers together in an all-encompassing value proposition. Further, they could deliver new credit products, including consumer loans at the point of sale, through better and faster data analytics that can produce a credit decision in less than 30 seconds.

In addition to mobile banking apps, the digitization of card credentials and biometric authentication have profound implications for banks. Banks can leverage biometric authentication to facilitate origination across products such as credit cards, consumer loans, and insurance. They can also issue digital credentials directly into select m-wallets and mobile applications.

Whether an issuer should have a standalone app (dedicated to credit cardholders) or leverage a broader mobile-banking app will depend upon each bank's payments strategy. A combined app could be optimal for issuers that have built their business primarily through cross-selling to retail banking customers. Stand-alone apps coupled with biometric log-ins have the advantage of providing a strong user experience early in the customer adoption phase, with no competition from other products in determining the app's enhancements. Improvements that offer differentiation-such as fraud detection, personalized alerts, and flexible rewards redemption at the point of sale-will be critical to long-term usage and customer retention.

- *Experiment with next-generation technology.* Banks must also look beyond current technology and the consumer demands of today. They must explore next-generation technology (such as blockchain technology) and data analytics to figure out new sources of value. One possibility is an urgent-credit service enabled by an instant payment system coupled with advanced underwriting. Another might be a credit-card form factor that uses a fingerprint sensor to provide key features such as displays of recent transactions. Such an offering could put banks back in control of the form factor and potentially displace m-wallets.

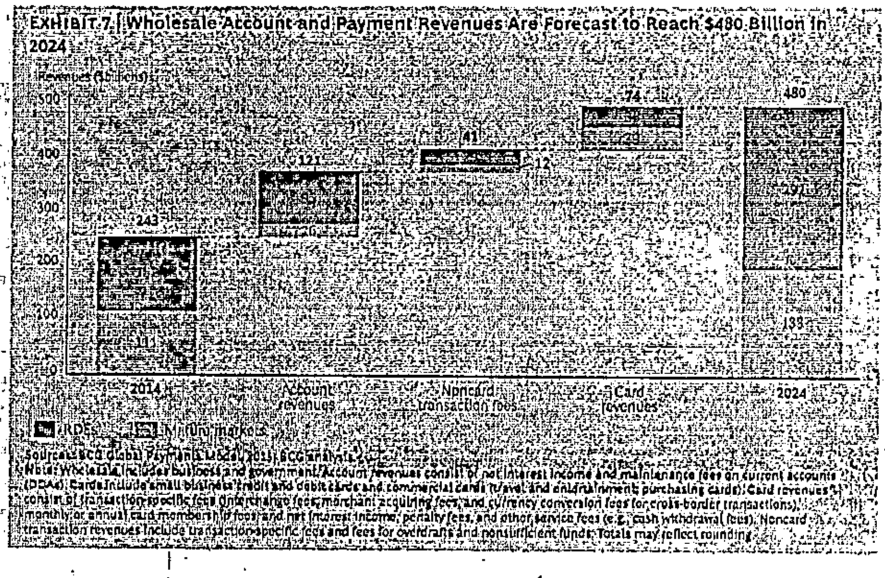
Some banks have effectively established an innovation lab aimed not just at experimenting with new ideas but also at commercializing them. Banks must take an enterprise-wide approach to innovation to assure that all resources and businesses are leveraged and that investments are optimized. Moreover, they must adopt an entrepreneurial approach to product development and marketing. While they still need multiyear technology road maps, they also need to adopt a more agile development approach that allows them to adapt to a shifting competitive landscape and launch new features and functions on a quarterly basis. Many banks are well equipped to be at the forefront of payment innovation-and a few will become disrupters.

WHOLESALE TRANSACTION BANKING BOLSTERING TREASURY AND TRADE SERVICES

WHOLESALE TRANSACTION BANKING- WHICH INCLUDES PAYMENTS, cash management, and trade finance-is an increasingly important business for banks, one critical to building strong client relationships and cross-selling. It also has several structural advantages: moderate cyclically, relatively low risk, and (with the exception of trade finance) low capital requirements.

Further, it is a fairly stable source of low-cost liquidity and funding.

Wholesale transaction banking generated about $330 billion in revenues globally in 2014. Account and payment revenues (covered in this report) generated $243 billion and are expected to nearly double to about $480 billion by 2024, a CAGR of 7 percent. (See Exhibit 7.)



Trade finance added $45 billion, and value-added services (such as information reporting) contributed another $40 billion. Trade finance revenues should reach nearly $100 billion by 2024, a CAGR of 8 percent. (See the sidebar "Being a Champion in Trade Finance.") In general, growth will be driven by increasing volumes and deposit balances, as well as by improving spreads. The importance of all these drivers, however, will vary by region. In RDEs, account revenues stand out as a dominant growth driver.

Treasurers and CFOs cite service quality and process execution as top criteria.

Although revenue-pool growth projections are strong, excelling in wholesale transaction banking is becoming increasingly difficult. For example, the attractiveness of the business has heightened competition among banks, while deficiencies in bank services and the rise of multibank platforms have opened the door to nonbank competitors. In addition, the regulatory compliance burden has grown dramatically, adversely affecting client relationships, bank operations, product development, and international expansion. (See the sidebar "Compliance: A Key Element of Success")

In our view, there are four critical steps to overcoming current challenges and becoming what we call a transaction-banking champion:-

- Focusing on the true needs of treasurers and CFOs
- Excelling in the basics
- Differentiating along key dimensions (such as superior data and analytics; risk management and regulatory advisory services; and flexible

platforms and open architecture)

- Outperforming in go-to-market strategies

Focusing on the True Needs of Treasurers and CFOs

The roles of treasurer and CFO at large corporations and multinationals have evolved considerably since the financial crisis of 2007-2008. Responsibilities have expanded and the stature of these positions has grown. Mandates now encompass a complete balance-sheet mission that includes optimizing working capital and tightening risk management in a time of rising security and fraud threats.

BCG, leveraging a proprietary survey conducted in cooperation with BNP Paribas-a study involving some 500 corporate treasurers and CFOs-has identified critical client needs that offer banks clear opportunities to differentiate themselves. For example, treasurers and CFOs cite service quality and process execution as top criteria for selecting a bank. In addition, we see an overarching theme: companies increasingly want banks to act as advisors and partners in solving their problems and improving their operations. Allowing for some variation by region and client segment, corporate clients ranked having creative ideas and clear solutions either first or second in importance for their relationship managers (RMs). Clients also expect their banks to liaise with other business units (such as retail banking) to help solve difficulties such as inefficient client-to-business or business-to-client payments. (See also "Corporate Treasury Insights 2015: As the Dust Settles," a Focus report by BCG and BNP Paribas, May 2015.)

Further, in financing, treasury needs have gone far beyond traditional credit products. They now require solutions in areas such as integrated working-capital financing, off-balance-sheet financing, and cash optimization.

In terms of service quality, treasurers and CFOs are critical of banks' performance in several areas. They cite inefficiencies and ambiguity in service delivery and an unwillingness to explore nontraditional solutions. They would like to see increases in process efficiency and a reduction in complexity-more straight-through processing (STP), less paperwork, and more automation of administrative tasks. Treasurers and CFOs also expect transaction-banking partners to help them tackle

BEING A CHAMPION IN TRADE FINANCE

Despite the recent slowdown in trade flows, trade finance remains one of the most dynamic businesses in the wholesale transaction-banking arena. Shifts in corporate needs and the rise in demand from small and midsize enterprises (SMEs) are opening numerous opportunities. In addition, trade flows are shifting, with the north-to-south, RDE-to -RDE corridors growing at an above-average pace. These opportunities, however, will be hard won. Increasing regulation and its attendant compliance requirements are hindering banks' ability to respond to new client demands and deliver new services efficiently.

In response, many banks are reviewing and pruning their geographic footprint and client relationships, resulting in service gaps. Rising competition from nonbank providers, which tend to be more nimble and proactive, is threatening banks' market share. Nonetheless, banks can succeed if they deliver a differentiated value proposition and forge smart partnerships.

A differentiated value proposition requires an organizational structure that listens to the voice of the customer and enables coordinated, integrated delivery of trade finance-as well as payment and cash management-services. Two trends have led many corporations to integrate their cash and trade-finance operations more closely first, the rise of open-account trading, and second, working capital constraints. As we have seen, banking clients are seeking holistic solutions, not just individual products.

The Bank Payment Obligation (BPO) is an example of this. Collaboratively developed by the International Chamber of Commerce and SWIFT, the BPO aims to bring together the security of documentary trade with the convenience and efficiency of open-account trade, opening doors to FX and hedge revenue and to direct supply-chain financing. For example, banks can offer lucrative receivables-finance solutions to exporters using BPO-facilitated trade. Developing such solutions will require close coordination across product and sales teams, including FX. Overall, banks are finding that if they can deliver a streamlined, transparent, data-rich FX and payment service, they can compete against the multibank FX platforms.

Within the organization, a differentiated value proposition requires several layers of capabilities. At the foundation, a flexible technological platform that enables integrated services and the easy addition of new functionality is needed. In the middle and at the front end, delivery models must be tailored to target segments, avoiding the "everything to everyone" syndrome. Large corporations need a robust client-service team consisting of product and country specialists as well as industry experts. The middle market can be served by a relationship manager who has strong industry expertise and coordinates well with product and country specialists. At the front end, channels tailored to the needs of specific segments are critical.

As for partnerships, banks are increasingly finding that working with the right collaborator is the most effective means of delivering their value propositions across key regions. Global banks and strong local and regional banks in emerging markets are benefiting from partnerships that combine international infrastructure and sophisticated product suites with local expertise and savoir faire.

Furthermore, while much of banks' energy has been focused on serving large corporate clients, significant opportunity lies in serving the small and midsize market. BCG estimates that SMEs accounted for more than one-third of export trade in 2012 and that their share will likely hit 40 percent by 2020. The increasing digitization of processes has significantly lowered banks' cost-to-serve for this segment.

COMPLIANCE
A Key Element of Success

Amid the tsunami of regulations that has flooded the financial-services industry since the financial crisis, compliance has become a key element of success in all sectors, including transaction banking. Yet many payments providers have invested extensively in compliance without seeing the desired results. This disconnect is often the result of two issues:-

- Deficiencies in "Big C" (the formal compliance organization): typical problems include a lack of top talent, difficulty in implementing regulatory change, and problems with IT systems

- A payments business that does not prioritize compliance or understand how regulations should affect its business model

In order to achieve sustainable compliance, the payments business needs to take the lead. Senior leadership must set and enforce compliance objectives and make them a cornerstone of the company's culture. The focus on compliance must extend to the front line, which needs to understand how daily interactions with clients must be tailored. The right incentives for both management and the front line can help embed a strong culture of compliance.

Moreover, effective compliance must go beyond personnel to include the way products are designed. Operating controls must be robust, and the results of compliance must be continuously measured. Organizations that can identify compliance issues, discuss them candidly, and move to address them effectively will find themselves well positioned to thrive in the ever-evolving regulatory climate. (For more on this topic, see "Enabling Sustainable Compliance at Banks," BCG article, September 2015).

inefficiencies in their own operations. For example, many financial executives are seeking support both in implementing payment factories and in improving electronification of their financial supply chains (such as through e-invoicing).

In terms of engagement and integration, treasurers and CFOs identify numerous pain points. For example, increased regulatory requirements particularly around know-your- customer and anti-money-laundering initiatives-have adversely affected relationships between banks and financial executives, with many treasurers and CFOs believing that banks' compliance processes do not adequately consider the impact on clients. They also find difficulties in the account-opening process and in systems integration and would like to see simpler and faster integration (with fewer tests and iterations) as well as more flexible integration processes. On a continuing basis, they would like to have access to more self-administration tools and a simpler way of managing accounts.

Finally, with both treasurers and CFOs increasingly open to considering third-party, nonbank providers to address their needs, there is real urgency for banks to raise their games. Our survey showed that 20 percent of treasurers and CFOs are already using non-bank providers for at least some transaction-banking services. Moreover, these providers are targeting the most profitable products, such as supply-chain finance, foreign exchange, and cross-border payments. Although banks still possess a competitive edge-higher levels of trust, strong track records in compliance, expertise in running reliable payment systems, and deep relationships built over time (reinforced by high switching costs for clients)-they must still face the probability of losing direct interactions with their clients to nonbank players. Those that successfully address the unmet as well as shifting needs of treasurers and CFOs are likely to establish long-term advisory-based relationships and a greater share of wallet. More cross-selling can translate into more revenue to invest in differentiation and innovation, which in turn can lead to a virtuous circle of more business and still more investment. This potentially virtuous circle is worth an estimated $240 billion in account and payment revenue growth from year-end 2014 through 2024.

Excelling in the Basics

The basics begin with a superior customer experience, an advisory-driven relationship model, and, for those serving international businesses, robust global-coordination capabilities. In addition, transaction-banking champions tend to have advanced pricing strategies and tactics.

A Superior Customer Experience. Customers need to be satisfied across the entire value chain, from on-boarding and systems integration to ongoing interactions across channels. Key goals should include steady improvements in both STP rates and response times-one aim being faster resolution of exceptional items-as well as lower enterprise-resource-planning (ERP) integration time, greater automation of administrative tasks, and clearer service-level agreements. Improving STP rates involves implementing new standards, in particular ISO 20022, the universal financial-industry message scheme. In addition, our survey respondents consistently mentioned that they do not want any single bank to have full visibility into their transaction flows.

The implications of the growing reliance on third-party players are especially profound for banks' technology road maps and their impact on the customer experience. Indeed, the IT and operations side of the business must understand client needs just as much (if not more) as RMs do. Among the questions that banks should address are the following:

- To what degree are clients relying on the bank's online channel?
- Are there certain features and functions of the online portal that no longer serve the needs of large corporate customers?
- To what extent are clients willing to pay for integration services, and should the bank invest

more to enhance integration tools?

An Advisory-Driven Relationship Model. Such a model embodies a problem-solving culture. While a "can-do" attitude starts at the top, hiring RMs with certain qualities solidifies the foundation. RMs need to look at problems from each client's standpoint, understanding their particular working-capital and process-inefficiency challenges. Transaction-banking champions tend to recruit more from industry, finding it easier to train people in payments and cash-management products than in industry-specific domain knowledge. Like their capital-markets colleagues, champions bring industry expertise to commercial pitches.

The IT and operations side of the business must understand client needs as well.

Robust Global-Coordination Capabilities. As treasury decision-making has become more centralized (both at regional and worldwide levels), global-coordination capabilities have become more important than product depth or credit capacity. Transaction-banking champions focus on improving coordination for core customers, avoiding the temptation to try to be everything to everyone. They also strengthen client loyalty through an enhanced service model that features the RM as a single entry point who owns the relationship and leverages the bank's full capabilities. Meanwhile, there is still a role for local banks to serve global companies, much as global banks continue to need specialists in specific countries and regions.

Advanced Pricing Strategies and Tactics. Most banks have room for improvement in their pricing structures. RMs often assume that they must discount in order to win business, so actual pricing is often much lower than the bank's guidelines. On average, we see 30 to 40 percent discounting across products, with wide disparities in price realization per client. Such discounts can rarely be explained by rational criteria. Indeed, expected drivers such as client volumes, the size of the relationship, the number of products bought, or new-versus-renewal business combined typically explain less than 7 percent of price variation. Rather, pricing is often driven by bank cultures that place a higher value on closing the deal than on optimized pricing.

In light of this situation, re-pricing can yield an immediate and much-needed performance lift, often 10 percent or more of total fee revenue, with two-thirds of the increase obtainable within 12 months. Superior pricing capabilities can also help steer both the bank and its clients toward an optimal product mix that better reflects risk, capital, and liquidity factors.

Clients want better data to track payments and accounts payable and receivable.

To support better pricing decisions, banks should move from "pricing as an art," driven by RM perceptions of required discounts, toward "pricing as a science," where the RM is equipped with analytical tools that provide client-specific guidance. One North

American bank, for example, built a detailed pricing algorithm into an RM tool to give guidelines based on specific client situations. If the RM wanted to deviate from the norms, the approval process was automated into the workflow, and specific tools made the impact of different price points on the RM's incentives fully transparent.

Differentiating Along Key Dimensions

There are several areas in which banks can truly stand out and differentiate themselves from competitors, superior data and analytics, risk management and regulatory advisory services, and flexible platforms and open architecture.

Superior Data and Analytics. In the short term, banks should invest in providing more basic data to all client segments. They should then explore demand from key client segments for advanced analytical tools, which they can potentially choose to develop over the medium term. According to our survey, clients need better data to track payments and accounts payable and receivable, as well as to simplify reconciliation. They value analytical tools that help improve working capital and operating efficiency. Such tools can include peer-group metrics as well as customized recommendations for cash velocity, gearing ratios, and bad debts.

Risk Management and Regulatory Advisory Services. There are many opportunities for banks to develop new compliance and risk-management services, with the goal of making compliance an asset rather than a liability. Banks should structure a commercial product that would help treasurers and CFOs with know-your-customer metrics, transaction monitoring, and alert management. Banks with expertise in local regulations, sophisticated systems for assessing counterparty risk, and advanced tools for detecting fraud should evaluate opportunities to commercialize these capabilities as well.

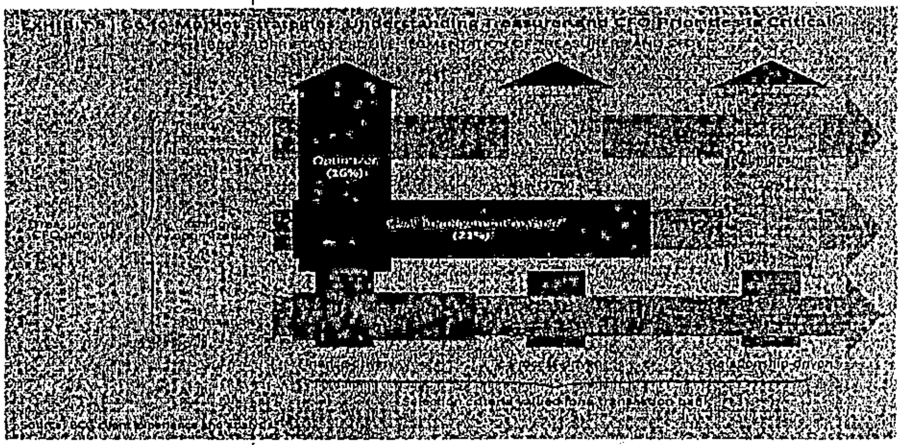
Flexible Platforms and Open Architecture. While treasurers and CFOs of large corporations typically want a consolidated view of their balances across all bank accounts, investments, and open-account trades, they do not necessarily want their bank to provide this view. Instead, they want the bank to readily push the data they need to the system of their choice, which requires easier integration between their systems and those of their banks, as well as the flexibility to make changes to data formats. To meet these demands, banks need to continue their migration to standard formats and open architecture.

By contrast, for small and midsize enterprises (SMEs), the value of a bank's commercial portal and a consolidated view within that portal is relatively high. Hence, banks that can deliver on these needs will deepen their relationships and face less risk of disintermediation by third-party providers with their SME clients. In addition to functionality, banks can make their portals more attractive by improving user-friendliness and providing greater ability to customize.

Outperforming in Go-to-Market Strategies

The final step in becoming a transaction-banking champion is to outperform competitors in go-to-market strategies. BCG has found that the winning combination involves fully understanding both overall client needs and the specific priorities of treasurers and CFOs. Client needs should be examined along four key dimensions: size, industry, region, and financial leverage. Treasurer and CFO needs can be categorized according to whether the priority is process improvement, cash flow optimization, or cost optimization; and within each of these categories, whether the motivation is finance-driven, process-driven, or relationship-driven. (See Exhibit 8.)

N "Corporate Treasury Insights 2015: As the Dust Settles" (a Focus report by BCG and BNP Paribas, May 2015), we observed that transaction banks need to respond to treasurers' expanded roles by elevating the quality and reach of their service offerings. To remain competitive and sustain growth, they must provide smart pricing schemes, become more client centric, and create a richer and more convenient experience. Indeed, the new landscape creates high expectations from treasurers and CFOs and a sense of urgency for banks to close service gaps and differentiate their offerings, providing a combination of service excellence, cyber security leadership, and innovative use of digital technologies.



FOR FURTHER READING

The Boston Consulting Group has published other reports and articles that may be of interest to senior financial executives. Recent examples include those listed here.

Enabling Sustainable Compliance at Banks

An article by The Boston Consulting Group, September 2015.

Global Asset Management 2015: Sparking Growth with Go-To-Market Excellence

A report by The Boston Consulting Group, July 2015

Global Wealth 2015: Winning the Growth Game

A report by The Boston Consulting Group, June 2015

Corporate Treasury Insights 2015: As the Dust Settles

A Focus by the Boston Consulting Group and BNP Paribas, May 2015

Global Capital Markets 2015: Adapting to Digital Advances

A report by The Boston Consulting Group, May 2015

Operational Excellence in Retail Banking 2015: Creating Digital Banks with a Human Touch

A Focus by The Boston Consulting Group, April 2015

The Bionic Bank

A Focus by The Boston Consulting Group, March 2015

Global Corporate Banking 2015: The Look of a Winner

A report by The Boston Consulting Group, March 2015

Overcoming the Digital Dilemma in Wealth Management

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The Emerging Equilibrium in Banking: A Tool Kit for Success

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Global Risk 2014-2015: Building the Transparent Bank

A report by The Boston Consulting Group, December 2014

Time for Rebalancing: Insights from BCG's Treasury Benchmarking Survey 2014

A Focus by The Boston Consulting Group, December 2014

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