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Who Pays for Free? The Proposal to Bring Back MDR on Large-Merchant UPI

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Every fact web-verified against primary sources

> *The Ministry of Finance proposed, in reports on August 3, 2026, amending Section 10A of the Payment and Settlement Systems Act, 2007, to replace the blanket statutory prohibition on Merchant Discount Rate for UPI and RuPay debit transactions with a framework allowing the Centre to notify which payment modes remain exempt.*

WHAT MDR IS, AND WHAT CHANGED IN 2020

Merchant Discount Rate (MDR) is the fee a merchant pays to accept a digital payment, shared among the acquiring bank, the issuing bank and the payment network. It is the revenue that funds payment infrastructure: fraud systems, dispute resolution, settlement rails and the acquiring business that signs merchants up.

PERIOD	REGIME
Before January 2020	MDR applied to UPI and RuPay debit transactions, at regulated rates
From January 2020	**Section 10A** of the Payment and Settlement Systems Act, 2007 imposed a **statutory zero-MDR** requirement on UPI and RuPay debit card transactions
Proposed now	Replace the blanket statutory bar with an enabling provision letting the **Centre notify** which modes stay MDR-exempt

THE REPORTED CONTOURS OF THE PROPOSAL

ELEMENT	DETAIL
Merchants expected to remain exempt	Annual turnover up to **Rs 1.5 crore**
Proposed cap on large-merchant UPI MDR	Not above **0.5 per cent** of transaction value
Mechanism	Executive notification rather than statutory prohibition

The enabling legislation was reported as being prepared at the time of this edition; the proposal, not an enacted change, is what is described here.

THE UNDERLYING POLICY PROBLEM

Zero-MDR achieved its intended objective. Removing the merchant's cost of acceptance was decisive in driving UPI adoption to a scale unmatched anywhere, particularly among small merchants for whom even a modest per-transaction fee is a real deterrent.

But a payment system has running costs regardless of whether anyone is charged for it, and those costs have been met in two ways, both of which have limits.

FUNDING ROUTE	LIMITATION
Budgetary incentive schemes	The government has made annual allocations to compensate banks and payment providers for zero-MDR; this converts a private transaction cost into a recurring fiscal commitment
Cross-subsidy from other business	Banks absorb costs and recover them elsewhere, which distorts pricing and gives providers little incentive to invest in acceptance infrastructure for low-value merchants

The result is a system that is free at the point of use, expensive to run, and dependent on either the exchequer or opaque cross-subsidy to survive. A turnover-threshold MDR attempts to hold the adoption gain for small merchants while asking large merchants, for whom a 0.5 per cent fee is a normal cost of doing business, to fund the rails they use most heavily.

THE ARGUMENTS

FOR A THRESHOLD-BASED MDR	AGAINST
Restores a revenue base for payment infrastructure without touching small merchants	Any MDR risks slowing acceptance growth, and merchants may pass the cost to consumers through surcharging
Reduces the recurring fiscal cost of incentive schemes	The government has repeatedly affirmed zero-MDR as policy; reversal affects predictability for a sector that invested on that basis
Aligns India with international practice, where interchange fees fund card networks	A turnover threshold creates a cliff-edge and invites structuring to stay below it
Improves incentives to expand acceptance in underserved segments	UPI's scale advantage derives substantially from being free; pricing it changes the product

THE INSTITUTIONAL MAP

BODY	ROLE
Reserve Bank of India	Regulator of payment systems under the Payment and Settlement Systems Act, 2007
National Payments Corporation of India (NPCI)	Operates UPI, RuPay, IMPS and other retail payment systems; a not-for-profit company under Section 8 of the Companies Act
Ministry of Finance	Proposes the statutory framework and funds incentive schemes
Board for Regulation and Supervision of Payment and Settlement Systems (BPSS)	The RBI board committee overseeing payment system regulation

UPSC RELEVANCE

GS Paper 3: Indian economy; effects of liberalisation; awareness in the field of IT; inclusive growth and issues arising from it; government budgeting.

Prelims pointers:

- **MDR**: the fee a merchant pays to accept a digital payment, shared among acquiring bank, issuing bank and network.
- **Section 10A, Payment and Settlement Systems Act, 2007**, imposed **zero MDR** on UPI and RuPay debit from **January 2020**.

- **NPCI** operates UPI and RuPay; it is a **not-for-profit company under Section 8** of the Companies Act.
- Payment systems are regulated by the **RBI** under the Payment and Settlement Systems Act, 2007.
- Reported proposal: merchants with turnover up to **Rs 1.5 crore** exempt; large-merchant UPI MDR capped at **0.5 per cent**.

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THE PROPOSAL:

Amend Section 10A of the Payment and Settlement Systems Act, 2007, replacing the statutory zero-MDR bar with an enabling power for the Centre to notify exempt modes.

Merchants with annual turnover up to Rs 1.5 crore expected to stay exempt; large-merchant UPI MDR proposed at not above 0.5 per cent.

BACKGROUND: MDR ON UPI AND RUPAY DEBIT WAS ABOLISHED FROM JANUARY 2020 BY SECTION 10A. SINCE THEN THE RUNNING COST HAS BEEN MET THROUGH BUDGETARY INCENTIVE SCHEMES AND BANK CROSS-SUBSIDY.

INSTITUTIONS: RBI REGULATES PAYMENT SYSTEMS UNDER THE PSS ACT, 2007; NPCI OPERATES UPI AND RUPAY AS A SECTION 8 NOT-FOR-PROFIT COMPANY.

Sources: *Reserve Bank of India, National Payments Corporation of India, Ministry of Finance*

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