NPCI/UPI/Rupay/OC-118/2021-22 **08th September, 2021**

To
All UPI and Rupay Members,

Sir/Madam,

Subject: Reference Guidelines for members on Merchant acquisition standards

The obligation to acquire, manage and monitor "Merchant/ Aggregator/ Marketplace/ Master -Merchant/ Sub-Merchant" (hereinafter "**Merchant**") relationships has been a long-standing responsibility of the Acquiring Member Banks (the "**Acquiring Member Bank**") to ensure balance in the ecosystem.

As per the procedural guidelines, the Acquiring Member Bank takes full liability for merchants on-boarded by them either directly or through aggregator/partners. Hence a proper process on the merchant acquisition & portfolio monitoring along with necessary due diligence is required to mitigate risks. In this regard, NPCI is providing the reference guidelines (Ref Annexure A) on merchant acquisition with a set of controls for processing P2M (Person to Merchant) based transactions.

Reference is given to Acquiring Member Bank's key risk responsibilities and accountabilities when managing Merchants. This document nowhere conflicts, and only supplements the regulatory directions in this regard, if any.

Acquiring Member Banks are requested to adhere to the Guideline as appropriate.

Yours sincerely,

SD/-
Dilip Asbe
Managing Director & CEO

Annexure A – Reference Guidelines for Merchant acquisition standards

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An Acquiring Member Bank must monitor its Merchant activity (viz., on-boarding criteria, transaction monitoring & control, training, assessment of the portfolio metrics, etc.) periodically. These monitoring standards for merchants is a baseline for the level of oversight on Merchant performance. Acquiring Member Banks can use both manual as well as digital modes of merchant due diligence.

Acquiring Member Bank should ensure the following points are in place and the same is adequately addressed:

- Board approved policy for Merchant acquisition
- Agreements with various stakeholders (as appropriate)
- Merchant underwriting
- Merchant portfolio and risk monitoring
- Merchant training
- Third party agent risk oversight and governance

The abovementioned key responsibilities are described in detail:

1. Board approved policy for Merchant acquisition:g

i. Implement policies that include standards to ensure quality / business conduct to mitigate risk to the NPCI operated payment system in terms of financial or reputational risk.

ii. The policies must be approved by the Acquiring Member Bank's Board of Directors and should have a periodic review mechanism.

2. Agreements with various stakeholders:

i. Merchant agreement in place with each merchant/aggregator (as appropriate) before any service is provided.

ii. Appropriate agreements to be in place with any third party service provider (as may be required) in case any of the activities pertaining to the merchant acquiring portfolio is outsourced.

iii. Merchant agreements are reviewed from time to time and updated appropriately with changes, if any.

3. Merchant underwriting:

i. Suggested acceptable criteria for Merchant/Aggregator/Master merchant underwriting:

a. Acquiring Member Bank to verify the Merchant (or its mobile application) on origin country and ownership for "foreign official/stakeholder" to ensure no conflict with Regulatory / Government guidelines.
b. The underwriting process should provide clarity on permitted merchant types, segments and allocation of Merchant Category Codes (MCC) basis nature of business.
c. Validation of Merchant key information.
d. Website/mobile merchant information screening to ascertain the nature of business.
e. Quantifying a new Merchant's financial risk exposure (e.g., sales volume, bureau checks, dispute history, delivery method, contingent liability) wherever applicable.
f. KYC validation, sanction screening, other verifications, wherever applicable, as may be required.
g. Assessing compliance with applicable data security standards and requirements.
h. Conditions that require a Merchant to be re-underwritten (location, change in ownership, change in average sales volume/ transaction amount, change in products/ services offered, etc.)

ii. Merchant Criteria - An Acquiring Member Bank shall also classify merchants into Critical, High, Medium & Low risk segments so that appropriate oversight, monitoring and due diligence is suitably carried out on a periodic basis. It is also recommended that the Acquiring Member Bank has a clearly defined prohibited merchant categories / lines of businesses.

iii. Prohibited Merchants:

a. Exclusion of Merchant categories that have been banned under the Central or State laws and regulations as may be applicable.
b. Exclusion of Merchant operating such business that is not specifically permitted by the regulator, statutory or any other competent authority.
c. Exclusion of Merchant posing a high brand (or reputational) risk.
d. Exclusion of merchant operating in financial products / services that are not regulated.

4. **Merchant portfolio and risk monitoring:**

It is recommended that Acquiring Member Bank suitably incorporates and follows the below points as appropriate towards meeting portfolio risk monitoring objectives.

i. An Acquiring Member Bank shall monitor the merchants/sub-merchants on-boarded by Aggregator.
ii. Use of predetermined Merchant sales volume, transaction amount parameters for risk monitoring purposes.
iii. Monitor sudden increase and dips in merchant volumes, including cross border volumes.
iv. Monitor merchant level fraud to sales, chargeback to sales, reversal and refunds.
v. Website (or information available online) verification for online merchants to review product / service offering, refund/ cancellation polices, delivery mechanism and other Terms and conditions.
vi. Use of 'Hold funds' and 'deferred settlement' for suspicious transactions / merchants.
vii. Carry out investigations for suspicious or questionable transactions.
viii. Inactive / Dormant merchant review.

a. Web-crawling: It is recommended to deploy web crawler scan services to determine whether the products or services offered are inconsistent with the Merchant's transaction activity, wherever its applicable.
    i. Changes in the type of products offered that effectively alter the Merchant's MCC.
    ii. Transaction laundering by misusing the credential and resulting in illegal sale of products / services.
    iii. To identify potential violations involving sale of banned goods / controlled substances / illegal services and unethical business by the merchant.

b. Investigation: If the investigation reveals Merchant involvement in illegal and/ or fraudulent activity or in any other brand damaging activity, the Acquiring Member Bank must:
    i. Take appropriate legal action to minimize losses and explore other legal remedies
    ii. Cooperate with networks, issuers and law enforcement agencies, as appropriate
    iii. Hold any and all available settlement funds, if possible.

It is suggested that Acquiring Member Banks ensure that their Merchant agreements are robust enough to cover these scenarios.

5. **Merchant training:**

    i. Acquiring Member Bank to create ongoing training modules with Merchants on the acceptance methods and guidelines.

    ii. Training to be conducted physically / virtually with adequate information in line with the policy of the Acquiring Member Bank.

    iii. FAQ's along with Do's and Don'ts to be published by the Acquiring Member Bank

6. **Third party agent oversight and governance**:

    i. Acquiring Member Bank shall do necessary underwriting as may be required for on-boarding of any third party service provider.

    ii. The Acquiring Member Bank shall conduct a periodic review/audit of the third parties engaged by the Merchant/s as required by its internal procedures.

    iii. Acquiring Member Bank shall remain responsible for outsourcing of all security system related activities by the Merchant to any third Party. When using services of third parties, the Acquiring Member Bank must establish controls in line with outsourcing guidelines advised by the regulator.