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WHEN DOES SETTLEMENT BECOME A PAYMENT SYSTEM?

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For more than a decade, power exchanges in India operated within a self-contained regulatory regime under the Electricity Act, 2003 and the CERC (Power Market) Regulations, 2010, with clearing and settlement treated as integral components of an electricity-market framework designed around price discovery, delivery assurance and grid stability. In August 2021, the CERC notified the CERC (Power Market) Regulations, 2021, replacing the earlier framework and introducing, for the first time, a requirement that clearing and settlement of electricity transactions shall be carried out in accordance with the Payment and Settlement Systems Act, 2007 (PSS Act). The introduction of this requirement brought into contact two statutory frameworks that had until then operated within distinct institutional spheres.

Exchanges were initially granted one year to align their clearing frameworks with this requirement. The transition proved more complex than the brevity of the provision suggested, as questions arose on the applicability of the PSS Act within the electricity-market framework, particularly in the absence of a dedicated framework from the Reserve Bank of India (RBI). As consultations amongst the Central Electricity Regulatory Commission (CERC), the Ministry of Finance and the RBI continued, the compliance timeline was extended more than once. In August 2024, the CERC fixed February 2025 as the final deadline for alignment.

In this context, this paper examines whether exchange-based clearing and settlement fall within the statutory conception of a *'payment system'* under the PSS Act, and what that inquiry reveals about the limits of payments law.

Architecture of a Payment System

The PSS Act emerged at a time when India's payment infrastructure had become indispensable to financial stability. Large-value systems such as RTGS, NEFT, CCIL, cheque clearing houses and the retail payment networks were already operating at scale. Yet their legal foundation rested largely on contractual rulebooks and regulatory circulars. Multilateral netting lacked explicit statutory recognition, and settlement did not enjoy insulation from insolvency proceedings. The systems functioned in practice, yet their legal certainty was less assured.

The PSS Act brought payment systems within a formal authorisation framework under the supervision of the RBI and identified them as a distinct category of financial infrastructure. The objective of the PSS Act was neither to regulate commercial activity in general, nor every institutional setting in which funds are ultimately transferred. It addressed organised systems whose defining function is the processing and discharge of payment obligations among participants in a networked environment.

The definitions under the PSS Act reflect that institutional orientation. A *'payment system'* is one that enables payment to be effected between a payer and a beneficiary, involving clearing, payment or settlement services. A *'payment instruction'* is the originating mandate to transfer funds. A *'payment obligation'* arises upon the clearing or settlement of such instructions among system participants. *'Netting'* determines the residual amount payable or receivable after mutual claims are set off. *'Settlement'* discharges the payment obligation so determined. Read sequentially, these provisions describe a structured process in which obligations are generated, compressed and extinguished within the rules of the system.

Within such systems, exposure arises between acceptance of payment instructions and final settlement. Reciprocal claims accumulate, are compressed through netting and extinguished through settlement. Until settlement occurs, each participant remains exposed to the ability of others to perform. It is this interdependence within the clearing chain that gives payment systems their systemic character.

The supervisory architecture of the PSS Act responds to that exposure. No person may operate a payment system without prior authorisation from the RBI. Authorisation brings the system within continuing oversight of its rules, risk-management arrangements and settlement procedures. Section 23 of the PSS Act provides the legal anchor: payment obligations and settlement instructions determined in accordance with the system's approved procedures are final and irrevocable, notwithstanding insolvency or winding up. Netting is validated and discharge within the system cannot be reopened.

Taken together, these features delineate the PSS Act's regulatory perimeter. In simple terms, the statute is directed at organised networks in which payment obligations arise, are processed and extinguished within a supervised multilateral framework capable of transmitting systemic risk.

Clearing and Settlement in Power Exchanges

Power exchanges operate as organised markets for electricity under the framework of the Electricity Act, 2003 and the 2021 regulations, and in accordance with the CERC-approved rules, bye-laws and business rules. Their central function lies in facilitating price discovery and contract formation for defined delivery periods. Members submit bids and offers for specified time blocks and trades arise upon algorithmic matching in accordance with the exchange framework. Upon matching, binding contractual obligations are created under the exchange's rulebook.

Clearing and settlement are embedded within this market design as mechanisms of trade completion and risk management. Exchanges maintain prefunded margins, collateral and settlement-guarantee mechanisms to manage counterparty exposure. Obligations are aggregated over the settlement cycle and net positions determined under approved rules. Settlement is sequenced with scheduling and dispatch, and default is addressed through defined waterfalls prioritising system stability. The clearing process determines net financial obligations arising from traded positions, and settlement discharges them through designated arrangements. Clearing and settlement, in this setting, are not freestanding services but components of a market architecture supporting price discovery, contract performance and grid stability.

The question, therefore, is not whether funds move through this framework but whether the framework itself answers to the statutory conception of a *'payment system'* under the PSS Act.

Exchange Clearing and the Statutory Definition

The PSS Act defines the term *'payment system'* in specific and functional terms. Embedded within this definition are three elements: there must be a system, that system must enable payment to be effected between a payer and a beneficiary, and it must involve clearing, payment or settlement services.

The first element presents no conceptual difficulty. A power exchange, together with its clearing house and designated clearing banks, operates through an organised arrangement governed by CERC-approved rules, bye-laws and business rules. In that descriptive sense, it constitutes a system. This element, however, is merely threshold. The definitional force lies in the other two elements.

The second element requires that the system *'enable payment to be effected between a payer and a beneficiary'*. The language deliberately does not describe any arrangement in which funds move, rather it points towards systems whose architecture is directed toward effecting payment between parties in that capacity. The accompanying Explanation encompassing credit card, debit card and money transfer operations, confirms the legislative focus on payment infrastructures within the financial system. However, exchange-based clearing operates within a different institutional frame. Fund transfers undoubtedly occur. They arise from trade contracts formed under a sector-specific regime and are administered within a central counterparty structure designed to manage exposure and delivery risk. Settlement is integral to that framework, but it operates as the consequence of market clearing rather than the service around which the infrastructure is constructed. The distinction is structural; it concerns the character of the system, not the mechanics of fund movement.

Among the three expressions used in the third element, only *'settlement'* is furnished with structured content under the PSS Act. Settlement is defined by reference to the discharge of payment obligations arising from payment instructions. A *'payment obligation'* in turn arises as a result of clearing or settlement of one or more payment instructions relating to funds, securities, foreign exchange, derivatives or other transactions. Read together, these provisions contemplate a system in which payment obligations enter through instructions, subsist among system participants within a clearing process, and are ultimately discharged through settlement.

The surrounding definitions situate this structure within the financial system. *'Securities'* are confined to Government securities under the Public Debt Act, 1944; *'derivatives'* refer to interest rate, foreign exchange and RBI-specified financial instruments; and *'other transactions'* appears within that same financial cluster. The statutory scheme thus anchors clearing and settlement within supervised financial infrastructures. That architecture reflects a risk assumption: payment obligations circulate before discharge, creating inter-participant exposure. Section 23 stabilises that exposure by according finality to settlement and protecting netting from insolvency disruption.

Exchange-based clearing proceeds on a different institutional footing. Financial obligations arise upon the matching of trade contracts under a sector-specific regime and are contained within a prefunded central counterparty framework. Margining, collateralisation and defined default waterfalls manage exposure before settlement. Settlement gives effect to liabilities crystallised within that contractual structure. The clearing framework does not generate a circulating chain of unsecured payment obligations requiring statutory stabilisation.

The third element must therefore be read in light of the architecture the PSS Act presupposes. Netting mechanics and banking interfaces do not, by themselves, resolve the inquiry. The question is whether the clearing and settlement involved correspond to the payment-obligation framework and systemic-risk structure the statute was designed to govern. That framework is anchored in financial-system infrastructures within the RBI's supervisory domain and not in every organised market where contractual liabilities culminate in monetary discharge. Classification is determined by institutional character, not by the presence of a cash leg.

SECTION 34 AND THE LEGISLATIVE PERIMETER

The sharpest boundary question raised by applying the PSS Act to exchange-based clearing lies in the statute's own perimeter. Stock exchanges are excluded both within the definition of *'payment system'*, which does not include a stock exchange, and through Section 34, which provides that nothing in the PSS Act shall apply to stock exchanges or their clearing corporations. Power exchanges are not expressly mentioned. That asymmetry sits at the centre of the present inquiry.

The legislative evolution is instructive. The 2006 Bill adopted a transaction-specific formulation that brought within its scope the settlement leg of Government securities trades executed on stock exchanges. Parliamentary scrutiny raised concerns of regulatory overlap with the securities regime. The enacted text replaced that formulation with a categorical institutional carve-out for stock exchanges and their clearing corporations.

The progression from a transaction-based carve-out to an institutional exclusion reflects a deliberate boundary-setting choice. The PSS Act was framed to regulate payment systems within the banking architecture supervised by the RBI. Market infrastructures operating under specialised statutes were not to be subsumed merely because trades entailed movement of funds. Section 34 thus discloses a concern for regulatory coherence and functional demarcation.

Power exchanges did not form part of the statutory landscape in 2007. Exchange-based electricity markets emerged subsequently, with clearing frameworks approved and supervised within its own sectoral regime. The absence of an express exclusion for such infrastructures does not, by itself, determine their position. Section 34 demonstrates that Parliament distinguished between payment systems and exchange-based market infrastructures governed under independent statutes. Whether electricity-market clearing falls within the payments perimeter must therefore be assessed in light of that legislative design, rather than inferred from silence alone.

Concluding Thoughts

The convergence between the PSS Act and exchange-based electricity clearing presents a question of statutory perimeter rather than mechanical inclusion. The payments framework was enacted to stabilise organised financial infrastructures within the RBI's supervisory domain. Exchange-based electricity markets developed later within a distinct statutory ecosystem oriented toward trade formation, collateralised risk management and delivery assurance. Although February 2025 was fixed as the point of regulatory alignment, the institutional position remains unsettled, and power exchanges continue to operate amid uncertainty as to the statute's precise reach.

The definitional structure of the PSS Act and the boundary reflected in Section 34 suggest that the statute was framed with a particular institutional architecture in view. The present intersection arises from regulatory evolution. Where specialised market infrastructures intersect with payments law, classification cannot rest on shared terminology or the mere existence of fund transfers; it must reflect the structural assumptions the statute was intended to govern. If exchange-based electricity clearing is to be brought within the payments perimeter, that would amount to a deliberate enlargement of the statute's scope rather than a matter of interpretation. Settlement becomes a payment system not simply because money moves, but when the law recognises within it a network of payment obligations whose circulation requires systemic stabilisation.

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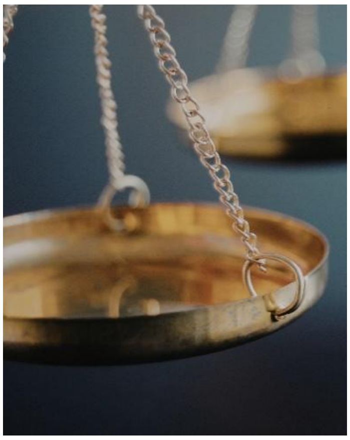

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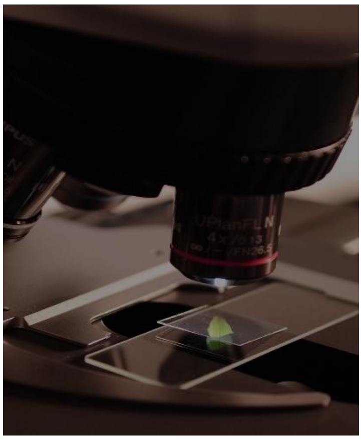

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