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The UPI Merchant Discount Rate Framework and Consumer Payment Behaviour in India

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Abstract

India's Unified Payments Interface (UPI) supports routine payments and transfers across a wide range of users and merchants. This paper examines the September 2026 merchant discount rate (MDR) framework and its potential implications for consumer payment behaviour. It uses a descriptive policy analysis of official publications and illustrative calculations to assess how the framework distributes costs across transaction categories. The design preserves free personal transfers and protects low-value merchant payments and qualifying small merchants. Potential effects on consumers arise mainly through changes in merchant acceptance, prices and perceptions of payment charges. The analysis identifies conditions that may influence continued UPI use and indicators for evaluating those effects after implementation.

Keywords *Unified Payments Interface, merchant discount rate, digital payments, consumer behaviour, merchant acceptance*

Introduction

Developed by the National Payments Corporation of India (NPCI) and launched in 2016, UPI enables real-time transfers through interoperable mobile applications [1]. QR codes and virtual payment addresses simplify acceptance for merchants and allow customers to pay exact amounts without exchanging account details. UPI recorded 16.58 billion transactions in October 2024, illustrating its scale before the September 2026 announcement [1].

As usage expands, participating institutions must maintain processing capacity, cybersecurity and fraud controls. The September 2026 framework introduces a charge within the merchant payment system for specified transactions while retaining free use for individuals [2]. Its effect on consumers depends partly on how merchants respond to those costs.

Research Objectives

- To describe the rates, thresholds and exemptions in the UPI MDR framework.
- To examine how merchant costs, payment acceptance and consumer perceptions could influence UPI use.
- To identify indicators for evaluating changes in merchant and consumer behaviour.

Research Methodology

The study uses a descriptive and analytical design based on secondary sources. It reviews the Ministry of Finance's announcement of 15 September 2026 and uses historical payment statistics to establish context [1, 2]. The analysis compares the announced treatment of personal transfers, standard merchant payments, qualifying small merchants and selected sectors. The charges in Table 1 are arithmetic illustrations. The study uses no primary survey or post-implementation transaction data, so it cannot estimate causal effects or quantify behavioural changes.

Policy Framework and Illustrative Charges

Person-to-person transfers remain free. Standard person-to-merchant payments up to ₹2,000 carry zero MDR. The framework also exempts qualifying merchants in the person-to-person-merchant (P2PM) category that receive up to ₹1 lakh per month through UPI QR codes. The Ministry of Finance states that banks have been advised to prevent merchants from passing MDR on to consumers and that UPI app providers are prohibited from levying platform fees or hidden charges [2].

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Table 1. Announced MDR rates and illustrative charges

Transaction category	Amount	Merchant MDR	Illustrative charge
Standard merchant payment	Up to ₹2,000	0%	₹0 on a ₹1,500 payment
Eligible standard merchant payment	Above ₹2,000	0.4%	₹20 on a ₹5,000 payment
High-value standard merchant payment	₹75,000 and above	Capped at ₹300	₹300 on ₹1,00,000 after the cap
Specified essential sectors	Above ₹2,000	Flat ₹5	₹5 on an eligible ₹10,000 fuel or insurance payment
Capital-market payment	Eligible transactions	0.02%, capped at ₹300	₹10 on an eligible ₹50,000 mutual fund payment

Source. Ministry of Finance [2]. Illustrative charges are calculated using the announced rates.

Findings and Discussion

1 Routine payments and financial inclusion

The ₹2,000 threshold and the exemption for qualifying small merchants preserve the cost conditions for many routine purchases. This can help sustain QR acceptance at neighbourhood shops and street vendors, where customers benefit from the ability to pay exact amounts. The effect on financial inclusion will also depend on connectivity, digital literacy and access to reliable grievance channels.

2 Higher-value payments and indirect pass-through

An eligible merchant may absorb the MDR, adjust general prices or steer customers toward another payment method. Even where a separate surcharge is prohibited, changes in prices or acceptance could influence how consumers pay for larger purchases. The size of any effect will depend on merchant margins, competitive conditions and enforcement. Misunderstanding the MDR threshold could also discourage transactions that remain free to consumers.

3 Sector differences and payment infrastructure

The flat fee in specified essential sectors gives merchants a predictable payment cost. The lower percentage rate in capital-market transactions limits the charge on covered payments, with any indirect impact on investors depending on changes in broader service pricing. MDR revenue could support processing capacity and security. The scale of any resulting improvement depends on how the revenue is used.

4 Merchant costs and pricing decisions

A merchant's exposure depends on the share of eligible transactions, the typical bill amount and the category in which payments are processed. Consider a store with 100 standard UPI merchant payments of ₹5,000 each. Under the announced rate, the illustrative MDR is ₹20 per payment, giving a total of ₹2,000 on ₹5 lakh of receipts. If the same store also receives 200 standard UPI merchant payments of ₹1,000 each, those payments add ₹2 lakh in receipts and carry zero MDR. Across the full ₹7 lakh in this example, the merchant's MDR averages about 0.29% of UPI receipts. The calculation illustrates why two stores with similar UPI turnover can face different costs [2].

A merchant may continue accepting UPI if quick settlement, simpler reconciliation or reduced cash handling offsets some of the fee. A merchant with tight margins and customers willing to use cash may have a stronger incentive to steer larger payments away from UPI. Merchants that absorb MDR incur the cost directly. Merchants that adjust posted prices may spread the cost across customers using several payment methods, making changes in consumer prices harder to attribute to MDR.

5 Consumer choice at the point of payment

The choice between UPI and cash depends on whether the merchant accepts the payment method, how quickly the transaction can be completed and whether the customer expects an additional charge. A regular customer at a grocery shop may continue paying digitally if the shop keeps accepting UPI on the same terms. A customer making an occasional high-value purchase may switch if the retailer asks for cash or offers a different price depending on the payment method. Such a response could appear first in the average value of UPI purchases even if consumers continue using UPI frequently for small transactions.

The ₹2,000 threshold may be misunderstood as the point at which customers start paying an additional fee. The Ministry's announcement assigns MDR to the merchant payment ecosystem and provides safeguards against passing the fee to consumers [2]. A survey should therefore ask what customers believe the rule says, whether a merchant requested a different payment method, and what the customer ultimately paid. These measures distinguish a change driven by misunderstanding from a change driven by the terms offered at checkout.

6 Differences across merchants and locations

The P2PM exemption depends on merchant classification and monthly UPI QR receipts, so business size alone is an incomplete indicator of eligibility [2]. A neighbourhood shop with frequent small sales may rely mainly on the per-transaction threshold, while a qualifying vendor may benefit from the category-based exemption. A comparison by location should also account for the mix of businesses. A rural market with many low-value purchases and an urban shopping district with a larger share of high-value purchases may show different payment patterns even when merchants respond similarly to the same fee.

Connectivity, access to cash and the reliability of QR payments shape the choices available in each location. Where a consumer has limited alternatives, a merchant's decision to discourage UPI may impose extra time or travel costs. Where several payment options are readily available, the same decision may produce a switch at checkout with little disruption. Evidence from local markets would help identify where changes in merchant acceptance matter most.

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Policy Implications and Further Research

Clear communication should distinguish the merchant-side charge from the price paid by a customer and explain the small-merchant exemption. Consumer complaint data can help identify reported surcharges and refusals to accept UPI. An empirical follow-up could compare merchant acceptance and UPI use just below and above ₹2,000 before and after implementation, accounting for seasonality, merchant category and other payment options. A consumer and merchant survey could help distinguish changes driven by price, acceptance and misunderstanding of the rules.

1 Data and indicators for an empirical follow-up

A follow-up study could combine anonymised transaction records, merchant surveys and consumer responses. Transaction records should distinguish standard merchant payments from exempt and special-rate categories and retain the bill amount, payment date and merchant category. Merchant surveys could record QR availability, accepted alternatives, fee awareness and changes in posted prices. Consumer surveys could record the intended and actual payment method, whether the merchant suggested an alternative, and whether a charge was displayed or requested.

Useful measures include UPI's share of all completed payments by count and value, the proportion of merchants accepting UPI for higher-value bills, and the share of surveyed customers reporting a requested surcharge. The denominator matters. A drop in UPI transactions may reflect weaker sales overall. Comparing UPI transactions with all completed payments for the same merchants helps distinguish changes in payment choice from changes in customer demand. Complaint counts should be interpreted alongside transaction volumes and awareness of reporting channels.

2 Evaluating changes around the payment threshold

For standard merchant transactions, researchers could compare narrow bands of bill amounts immediately below and above ₹2,000. Using the same merchants before and after a verified implementation date would help account for differences in business type and location. Examining several weeks on either side and checking for holidays, promotional periods and price changes would help interpret any difference. Exempt merchants and special-rate sectors should be identified in the data because their costs may follow different rules [2].

Researchers should also check for clustering of bills just below the threshold. Clustering can arise from ordinary pricing, promotions or changes in how purchases are recorded. Where possible, invoice totals should be compared with payment records to identify split payments. A shift around the threshold is easier to interpret when it is accompanied by evidence from merchants and consumers about what happened at checkout.

3 Scope and limitations

This paper evaluates the announced policy and uses numerical examples to explain its design. It does not observe merchant costs, price adjustments, payment refusals or household spending after implementation. The October 2024 transaction figure illustrates the prior scale of UPI and provides no estimate of the framework's effects [1]. The expected channels described here can guide data collection and hypothesis testing. The direction and magnitude of behavioural changes remain empirical questions.

Conclusion

The framework combines limited cost recovery on specified merchant payments with protections for individuals, routine purchases and qualifying small merchants. The analysis suggests that indirect effects are more plausible for larger payments, where a merchant may change prices or steer customers towards other payment methods. Actual changes in payment behaviour require evidence on transaction patterns, merchant acceptance and consumer complaints after implementation.

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Conflicts of interest

The authors declare that there are no conflicts of interest regarding the publication of thesis paper.

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