ABCUL
Association of British Credit Unions Limited

Payments Consultation
Banking & Credit Team
Floor 1, Yellow
HM Treasury
1 House Guards Road
London, SW1A 2HQ

Dear Sirs,

Setting the strategy for UK payments

We appreciate the opportunity to respond to this consultation. The Association of British Credit Unions Limited (ABCUL) is the main trade association for credit unions in England, Scotland and Wales representing around 65% of British credit unions who in turn serve around 80% of credit union members.

Credit unions are not-for-profit, financial co-operatives owned and controlled by their members providing safe savings and affordable loan facilities. Increasingly credit unions offer more sophisticated products such as current accounts, ISAs and mortgages.

At 30 March 2012, credit unions in Great Britain were providing financial services to 887,965 adult members and held more than £762 million in deposits with more than £604 million out on loan to members. An additional 121,922 young people were saving with credit unions.[1]

Credit unions in Britain are small, co-operative financial institutions which provide inclusive financial services in the communities and workplaces they serve. They are owned and controlled by a restricted membership and are operated for the sole benefit of this membership. The Credit Union Act 1979 sets down these operating principles in law.

In the past decade, British credit unions have trebled their membership and assets have expanded four-fold. As this growth has taken place, the role that credit unions can play – both in providing equitable financial services to the whole of their communities and providing diversity in the financial services sector – has been increasingly recognised by government and policy-makers.

Credit unions have been central to UK Government efforts to promote financial inclusion taking a pivotal role, for example, in delivering the Department for Work & Pensions Financial Inclusion Growth Fund which provided capital for on-lending to those without access to a source of affordable credit.

[1] Figures from unaudited quarterly returns provided to the Financial Services Authority

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Ending in March 2011, the loans provided under the fund totalled 405,000 with a value of £175 million[2] and an independent evaluation of the scheme found that it saved loan recipients between £119 million and £135 million in interest payments compared with high cost alternatives.[3] The great success of this scheme has been central to the Coalition Government's decision to extend £38 million investment through the DWP's Credit Union Expansion Project to help credit unions towards self-sustainability in a 5-7 year period, adding a million new members, in order to provide a viable alternative financial service, particularly to those on a lower income.[4]

Credit union position on payments strategy reform

Credit unions, as deposit-taking financial institutions, are closely tied to the payments system infrastructure since making and receiving payments is a central element of their business. In recent years the sector's involvement has increased through the development of the Credit Union Current Account and the Credit Union Prepaid Card both of which rely upon agency arrangements. As the sector continues to grow, in line with the Government's ambitious vision, credit unions' reliance upon developments in payments systems is likely to increase as they develop collaborative solutions to both increase access to current account and prepaid card services and develop new services based on online, telephone and mobile payment systems. Indeed, the development of, and increased participation in, such services is a central element to the sector's strategy for growth and reaching self-sustainability as supported by the Government. It is in this context that we respond to the current proposals.

Currently the opportunities for the credit union sector to influence the development of payments strategy are limited. The sector is involved, through ABCUL, in the User Forums which go some way to informing the Payments Council's work however, as the consultation document sets out, the powers of these Forums are limited and their influence only marginal.

Given the context set out above, the credit union sector is keen to be more closely involved in the development and promotion of new and existing payments systems. Likewise, the sector is entirely in support of the Government's ambition to have UK payments networks that facilitate competition through open access on reasonable commercial terms.

As such, we would like to express our broad support for the reforms outlined in both Options 1 and 2 in the consultation document to be implemented in tandem.

Option 1 – Enhanced self-regulation

We are in favour of the proposals set out since we believe they will create the basis for a more transparent, accountable and responsive framework for setting and implementing payments strategy. We are in agreement that a wider range of voices ought to be taken into account in respect of developing strategy since, whilst the system providers of course play a central role in

[2] See DWP Growth Fund statistics here: http://www.dwp.gov.uk/other-specialists/the-growth-fund/statistics/
[3] See DWP Growth Fund evaluation: http://www.hm-treasury.gov.uk/d/evaluation_growth_fund_report.pdf
[4] See DWP Credit Union Expansion: http://www.dwp.gov.uk/other-specialists/credit-union-expansion/

payment strategy, payment infrastructure is of increasingly fundamental relevance in the modern economy. Furthermore we agree with proposals to increase transparency through the publication of regular progress reports and independent performance reviews.

That said we are concerned that there is the possibility of undue burdens being placed upon smaller providers and non-provider members of the Council were reform of funding arrangements to expect a significant new contribution from them. Whilst we appreciate that there would appear to be a case for funding to be tied more closely to reformed membership, any new expectations should be based on the principle of proportionality and the recognition that whilst society and the economy as a whole increasingly relies upon efficient, open and effective payments infrastructure (thus necessitating their representation in the Council structures), the proceeds from its use are enjoyed only by the ultimate providers of said infrastructure.

We agree, likewise, that the Payments Council, should focus its efforts entirely upon the development of a fit-for-purpose payments system infrastructure and should not play a lobbying or trade association role – there are various bodies already in existence which represent the interests of the payments service providers and therefore it would seem appropriate that the Council focus on its regulatory and strategy-setting role avoiding any potential for or appearance of a conflict of interest.

Option 2 – Creation of a Payments Strategy Board

We agree that the creation of a Payments Strategy Board taking on the strategy setting functions currently held by the Payments Council, in connection with the reforms put forward in Option 1 to the Payments Council itself, would represent a significant improvement on the current situation. This would allow the Payments Council to focus upon implementation, guided by the Board's direction.

It would seem to make sense, were the creation of a Payments Strategy Board pursued, that it sit within the structures of the Financial Conduct Authority given the obvious relationship between the responsibilities of the two.

We agree with the proposed objectives of such a body, particularly with the promotion of access to payments networks by the industry on reasonable terms. This, as we have seen, is critical to the development of the credit union sector and to ensuring a competitive market for the provision of payment services which are becoming increasingly important in the modern economy. We are also in favour of the proposal to draw a broad membership representing a range of interests on to the group which will be essential if the Board is to achieve its objectives.

Again, we would urge careful considerations of the principles of fairness and proportionality when addressing the funding arrangements for the Board. Small players such as credit unions, though reliant upon payments systems, are less able to meet significant new costs and have seen the burden of regulation steadily increase in recent years. Likewise, as smaller players, the sector's relative position in the payments market is tiny and this should be reflected in any new charge it is expected to meet. As set out above, while the importance of payment systems in the economy necessitate a wide membership base for strategy-setting bodies, the financial benefits of running the systems flow almost entirely to the providers of this infrastructure.

Conclusion

Efficient, effective and reliable payment systems which are available to all providers at a reasonable cost are critical to the future development of the credit union sector. As such we are in broad support of a combination of Options 1 and 2 proposed by the consultation which we agree will enhance the strategy setting arrangements for payments infrastructure.

We are keen that funding arrangements for the reformed regime should be proportionate and thereby reflect the minor position credit unions occupy in using the payment infrastructure.

Yours sincerely,

Mark Lyonette
ABCUL – Chief Executive

The Association of Corporate Treasurers

Comments in response to
Setting the strategy for UK payments
HM Treasury,
July 2012

October 2012

The Association of Corporate Treasurers (ACT)

The ACT is a professional body for those working in corporate treasury, risk and corporate finance. Further information is provided at the back of these comments and on our website www.treasurers.org.

Contact details are also at the back of these comments.

We canvas the opinion of our members through seminars and conferences, our monthly e-newsletter to members and others, *The Treasurer magazine*, topic-specific working groups and our Policy and Technical Committee.

General

The ACT welcomes the opportunity to comment on this matter.

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The ACT is of the opinion that it is not necessary to move from self-regulation of the payments industry to government regulation, rather, strengthen the current self-regulation structure by ensuring users have a stronger voice.

We do not agree with the government's preferred option (Option 2) to establish a public sector body, the Payments Strategy Board (PSB) to oversee the UK payments strategy. Regulation represents a barrier to entry, restricts competition and innovation and increases costs. We believe regulation should only be used as a last resort where there is evidence of an actual or potential market failure and where the public good from regulation far outweighs the costs. Additionally there is a high risk that a separate regulatory body will become remote from the payments industry and not close enough to advise on UK payments strategy.

Our preferred option is (Option 1) enhanced self-regulation which proposes to keep the Payments Council with improvements to enhance the voice of the user. Setting the strategy for future payments networks should take into account the interests of all, including corporates which we represent. Changes to ensure a strong users' voice include changing the composition of the Payments Council Board and enhancing the role and function of the current user forums.

The third option in the consultation document is full statutory regulation similar to other regulated sectors such as gas, electricity and water. This option would be a major increase in the overall regulatory burden with considerable costs and take time to implement. This is not the government's preferred option and we agree this is a step too far.

In addition to answering the consultation questions we have also provided a specific comment on plastic cards. Plastic cards represent a significant portion of payment transactions and that percentage is growing. Historically payment merchants have been owned and operated by a number of the big banks but in recent years there has been a trend to sell off a portion of the payment merchant operations to Private Equity interest and overseas providers, which have no direct accountability to the new regime. With the continued trend from cheque payment to plastic payments it is important that this method of payment is specifically covered and included in the updated UK Payments Strategy and that the Payments Council takes ownership of strategy for the plastic card payments industry.

Question 1

Do you agree that the creation of a Payments Strategy Board:

- *Should be the lead option for reform,*
- *Provides the appropriate balance between Government intervention, impact and cost, and*
- *Effectively tackles the issues the Government has set out?*

The Payments Strategy Board is the government's preferred option, however we do not agree that this should be the lead option for reform. Our key concerns are that:

- Regulation should only be used as a last resort where there is evidence of an actual or potential market failure or in quasi-monopoly areas where competition is insufficient, industry codes etc. have failed and where the public good from regulation manifestly exceeds the costs it engenders. The government has not provided any evidence of these in their consultation to warrant independent regulation.
- The proposal is that the PSB would only publish recommendations to the payments industry rather than requiring action so is not a strong voice
- The PSB, as a separate body, could become distant from the workings of the payments industry and not close enough to advise on strategy
- There is some question over the PSB having a formal information gathering power but without this power it may not be able to understand and verify key trends in the payments industry

- The PSB is to be funded by an FCA levy on the payments industry. This would be an additional cost which may be passed on to consumers/corporates

Question 2

The following relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds with Option 2.

a. *Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?*
b. *How can a clearer separation of the Payments Council's strategy setting and trade body representative functions be best achieved?*
c. *Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?*
d. *Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how payments Council's board can be strengthened further.*
e. *Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?*
f. *How can Payments council funding be put on a long term, secure footing?*
g. *How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?*
h. *How can the membership of the Payments Council be broadened most effectively?*

The ACT is of the opinion that Option 1 to continue with the Payments Council is the preferred option but only where there is a stronger user's voice to act as a real counterbalance to the industry.

The current remit and objectives of the Payments Council: strategic vision; openness and accountability; and integrity are broadly appropriate. However the voting rights of the Payments Council's Board is dominated by the banks with only four out of fifteen directors being independent and having to work together in order to veto a Board decision. From a strategic perspective this gives the banks considerable power to dictate the future direction of the payments industry. The requirement that two independent directors would be able to veto the Board's decisions does provide more of a voice for corporates and consumers and we agree with this proposal.

User forums are currently the main channel for end-users such as corporates to work together with the Payments Council. We do believe that the current format of the user forums is not effective and that the proposed User Councils should have a stronger voice and be able to set their own agendas and strategic views.

Additionally we agree with the following option 1 proposals:

- Clearer functional separation of the strategic function from the trade body or lobbying functions
- Significantly enhance the role and function of the current user forums (the ACT are currently a member of the large users forum)

- The Bank of England would continue to sit on the Payments Council board as a non-voting observer and the new Financial Conduct Authority (FCA) would be invited to also have non-voting observer status.
- Provide transparency by continuing to publish the annual progress report

Question 3

The following relate to the creation of a new public body, (the Payments Strategy Board (PSB)) under Option 2.

a. *Do you agree with the proposed remit for a new payments Strategy Board?*
b. *Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.*
c. *Do you agree that the Payments Strategy board should include senior industry representatives, non industry representatives and independents? What do you consider to be the right composition of the Board?*
d. *Should the Payments Strategy board have a formal information gathering power? If yes, what information should be covered by such a poser, and what should an appropriate enforcement mechanism be?*
e. *Do you agree that the Payments Strategy Board should be funded by the FCA levy on the payments industry?*
f. *Should the FCA have any further controls over the Payments Strategy Board?*

As detailed above we do not agree with the creation of a new public body to regulate the payments industry and hence have not answered the detailed points under Question 3.

Additional comments on the UK payments strategy and plastic card payments

In 2010 plastic card payments represented 23.3%[1] of transactions by volume and in July 2012 had an annual growth rate for spending of 5.2%[2]. Plastic cards are not addressed by the Payments Council but by the UK Cards Association. The UK Cards Association website states that "The UK Cards Association Board is responsible for setting the strategic priorities for the industry."[3] For such a major part of the payments landscape, we believe plastic cards should be specifically included within the remit of the Payments Council and hence the UK payments strategy.

Whilst the 2011 National Payments Plan states that the Payments Council will "Examine our relationships with The UK Cards Association and the international card schemes as part of our forthcoming governance and performance review, and consider how the Payments Council can be most effective in driving change in card payments."[4] we do not believe this action point goes far enough. We urge the Payments Council to take ownership of strategy for the plastic card payments industry.

[1] Source: Calculated from data in table 3.2 of HMT's Setting the strategy for UK payments July 2012 based on Payments Council. UK Payment Statistics 2011. Tables 27.1 and 27.2
[2] The UK Cards Association Card Expenditure Statistics [CES] – July 2012. At a glance key figures for July 2012
[3] http://www.theukcardsassociation.org.uk/board_members/the_board.asp
[4] The 2011 National Payments Plan page 40

Historically payment merchants have been owned and operated by a number of the big banks but in recent years there has been a trend to sell off a portion of the Payment Merchant operations to joint venture structures. WorldPay Business Services is majority owned by Ship Luxco Holdings & CY SCA, registered in Luxembourg. WorldPay trade under the name Streamline in the UK and claim to handle 46%[5] of all UK point of sale transactions. Global payments, which operates under the name of HSBC is wholly owned by Global Payments Inc. a quoted US company. Lloyds provides merchant acquisition through its subsidiary Cardnet which is approximately 50% owned by the First Data Corporation, a company owned by KKR a US Private Equity firm. Elavon Merchant Services processes transactions for Santander and Bank of Ireland and is owned by US Bankcorp, the fifth largest commercial bank in the US. So it is reasonable to conclude that less than 50% of the UK Merchant acquisition market is provided by existing representatives of the Payments Council. We believe it is important that plastic cards should be included directly in the updated UK Payments Strategy and regulated by the Payments Council.

[5] Worldpay Group half year trading update to June 2012 found at http://www.worldpay.com/about_us/content/half-year-trading-june-2012.pdf

The Association of Corporate Treasurers

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Our 4,300 members work widely in companies of all sizes through industry, commerce and professional service firms.

For further information visit www.treasurers.org

Guidelines about our approach to policy and technical matters are available at http://www.treasurers.org/technical/manifesto.

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HM Treasury: Setting the strategy for UK payments

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This consultation follows the Governments response to the Treasury Select Committee report issued in 2011 "The Future of Cheques". The Treasury Select Committee recommended that "The Treasury should make provision in the forthcoming Financial Services Bill to bring the Payments Council formally within the financial regulation system, to be overseen by the regulatory body the Treasury identifies as being most appropriate".[i] In the Government's response to the report, the Government said that it accepted "the case for bringing the Payments Council within the scope of financial regulation. The Government believes this may necessitate going beyond the Committee's recommendation to include the relationship between the Payments Council, its members and inter-bank payment systems."[ii] Although this consultation was therefore prompted by the recent debate on the handling of the cheque withdrawal programme, it follows an on-going discussion on how payments should be regulated. The Cruickshank Report, published in 2000 recommended a new regulator for payments, along the lines of other utility style regulators.[iii] Payments regulation has also been considered by the Independent Commission on Banking also considered the issue in its interim and final reports. The Payments Council itself has recently conducted a governance review examining some of the issues covered by this consultation.

Key points and recommendations

- Payment systems are essential services and must be explicitly recognised as so

- Whatever structure the Government decides to establish, it must include a clear objective to ensure access to payments.

- Option 2 is the most attractive option, but it should be reviewed after 3 years and if insufficient progress has been made Option 3 must be re-considered

- The Payments Council is a membership body and therefore has an inherent conflict in representing groups which are not members

- Most of the changes made as part of Option 1 increase the flow of information into the Payments Council, but do not change the incentives or obligations on the decision makers

- The Payments Strategy Board must be able to effectively challenge the Payments Council; this requires a stronger remit and appropriate resource and a structure which ensures independence from the Payments Council

1. Introduction & general comments

Age UK welcomes this consultation into the future regulation of payments. We recognise that this is a challenging sector to reform, especially because it is highly inter-connected with other regulated industries and already involves a wide range of different regulatory institutions. It is also a highly technical area, which can make it more difficult to design an effective and constructive independent scrutiny function.

Age UK provided a full response to the Payments Council's recent Governance Review which covers many of the points we wish to make in response to this consultation. We therefore attach a copy of the previous response, with key points summarised in this section and responses to specific consultation questions in the section below.

This consultation is important because payment systems are essential services. They are the gateway to other utilities and essential services; everyone needs access to them in order to be able to participate in society. Until relatively recently the importance of access to payment systems was less acute as it was easier to access wages and benefits in cash. However as DWP, HMRC and the private sector modernise their payment systems they increase the importance of access to non-cash based payments for all. Further, changes to delivery of social care as part of the personalisation agenda and the delivery of universal credit will increase the reliance of vulnerable consumers on payment systems.

In 2011 Age UK researched the way older people use payment systems and found that payment systems were not working well for many older people.[iv] Consequences included inappropriate password sharing, keeping large amounts of cash at home, stress and anxiety when undertaking basic tasks and increased dependence on others. Further, new developments have the potential to increase exclusion unless the needs of older consumers are taken into account. We also found that issues experienced by older consumers were often also found among other marginalised groups, such as those living with disabilities or on a low income.

There is currently no body with responsibility for ensuring access to payment systems. Payments are often seen as opaque and difficult to engage with, cheques were the exception. It is difficult for consumers, especially vulnerable consumers, to achieve adequate representation, given the imbalance of power. **Whatever the structure the Government decides to use to set the strategy for UK payments it must have a clear objective to ensure access to safe, convenient and affordable payment systems for consumers.**

We note that in the Government's response to the Treasury Select Committee's 'Future of Cheques' report, it was stated that:

"The Government has ensured that the FCA will be able to require banks and building societies to take or refrain from specified action, such as withdrawing cheque services for both new and existing customers."

We are concerned that drafting changes to the Financial Services Bill may mean that this statement is no longer effective. Whilst the Financial Conduct Authority (FCA) does have rule making powers which technically allow it to require regulated firms to take or refrain from specified action, we do not see how the FCA's current objectives would allow it to make rules in respect of access to payment systems, as described above. We would welcome a clear statement from the Government or the Financial Services Authority/FCA on whether the new Financial Services Bill would have allowed it to intervene in the cheque withdrawal programme. If the FCA does not have objectives which allow it to consider access to services in this way, then it becomes more important that the Payment Strategy Board (PSB) has a strong remit for access.

2. Response to specific questions

Q1: Do you agree that the creation of a Payment Strategy Board:

- **Should be the lead option for reform**

We agree that the PSB should be the current lead option for reform, largely for the reasons set on in the consultation document. Although we view payments as an essential service, we do not think this necessarily requires a ‘Paycom’ style regulator. We consider this would be especially challenging to make sense of this kind of regulation unless it is joined up with other approaches to access to banking and financial services more widely.

However, whilst we recognise that it is preferable to avoid establishing a new regulator, we note that the industry has failed over an extended period of time to put in place measures to ensure payments work for consumers or meet the other objectives specified by the Government in this consultation. We therefore recommend that Option 2 is reviewed after 3 years and that Option 3 stays firmly on the table.

- **Provides the appropriate balance between Government intervention, impact and cost; and**

We agree that Option 2 is attractive in terms of the balance of intervention and cost, and that it has the potential to further the aims specified in this consultation. However we are not convinced that it will have the necessary impact, this will depend both on the detail of the implementation and the will with which industry approaches the challenge.

- **Effectively tackles the issues the Government has set out?**

It depends on the detail of the PSB, comments on which we include in the answer to Question 3. Without more detail, and access to clear sanctions, we do not think the PSB will tackle the issues set out by the Government. In particular, it will be important that the PSB is able to effectively challenge the Payments Council. This requires true independence of the PSB.

Q2: The following questions relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds with Option 2.

We have answered this question on the assumption that these changes will be put in place alongside Option 2. If the PSB is not established, then the Payments Council would need much more radical overhaul, however we do not think that tinkering with the Payments Council alone will ever achieve the Government’s objective.

a. **Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?**

   The current Payments Council objectives, as stated in its memorandum of association are:

‘(a) to lead the future development of co-operative payment systems in the UK in order to ensure that the payment system as a whole meets the needs of payment service providers, users and the wider economy....

...

(b) to ensure that the payment system is open, accountable and transparent.....’[v]

This is potentially a very limited set of objectives. In terms of leadership, the Payments Council is restricted to ‘future development of co-operative payments systems’. In practice, this has meant that questions raised about standards of existing payment systems have been met with the response that this is outside the Payments Council’s remit and within the ‘competitive space’.

The Payments Council does seem to be interpreting its remit more broadly, describing itself on its website as:

“......the organisation that sets the strategy for UK payments. It was set up by the payments industry in 2007 to ensure that UK payment systems and services meet the need of payment service providers, users and the wider economy.”

However, it is also unclear what ‘the needs of payment service providers, users and the wider economy’ means. It is only since the public pressure applied during the cheque withdrawal process that the Payments Council has started to ensure vulnerable consumers are properly represented in their research, an essential step to effective representation.

The extent to which these objects should be enhanced depends on the role the Government envisages for the Payments Council in the new arrangements. If it is to continue to have a key strategy setting role, we recommend that its mandate be clarified to ensure:

- The Payments Council looks at all consumer groups
- The Payments Council considers how well existing payment systems are working, as well as leading the design of new systems
- The Payments Council plays a greater role in setting minimum standards for consumer experience of different payment systems
- The issue of the ‘co-operative v competitive’ space is examined.

b. How can a clearer separation of the Payments Council’s strategy setting and trade body representative functions be best achieved?

We would add to this question the issue of the limited membership of the Payments Council. The Payments Council is not able to represent the entire payments industry and this has the potential to add another conflict within its strategy setting function.

In our view the Payments Council has an inherent conflict of interest when setting strategy as an industry membership based body is being asked to weigh the interests of industry, consumers and the wide economy. This is best addressed by ensuring strong independent external challenge through the PSB.

Whilst removing the trade representation/lobbying functions may improve appearances, we are unconvinced that it resolves the fundamental issue that consumers are required to trust the part of the industry to balance needs appropriately.

Other changes, such as increased in independent representation at board level could assist, however we consider that such change will always have limited impact in an organisation which works by consensus. These changes may, therefore, have some limited ongoing impact and will most often be felt when major decisions need to be made, however they are likely only to change the outcome at crisis points.

c. Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?

If the Payments Council is to continue to set the strategy for UK payments we would support this commitment. The report should not just be against its objectives, but also against the performance of the payments systems themselves, set against agreed criteria, which should include accessibility. The PSB could have a role in agreeing the criteria and also in responding to the Payments Council's progress report.

d. Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council's board can be strengthened further.

We agree that any two independent directors should have a right of veto over board decisions. We note that independent directors are currently required to:

'..act in the best interests of the payments sector as a whole and not any sectional interest of different objective, or as a representative of a particular viewpoint, and shall act in line with the objectives.'

Whilst we support the idea that independent directors should not be aligned to any particular user group, we would review the use of words 'payments sector as a whole' which suggests an emphasis on the already well represented payments industry.

If the Payments Council is required to set a strategy in the interests of payments providers, users and the wider economy we suggest that these last two groups should have greater representation at Board level, or that there be greater numbers of independents. Alternatively, the PSB could be used to provide this counter-balance.

e. Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?

Age UK is a member of the Consumer User Forum. Whilst we support the intentions behind the suggestion that existing user forums be strengthened we have two concerns:

(i) Capability of the User Forums to provide significantly more challenge than they currently do. A typical user forum has a full agenda which it is not always possible to cover in sufficient detail. Attendees are generally not payments experts and payments will be a relatively small part of their work. It is not realistic to expect this type of group to make up for an imbalance of power and incentives at Board level.

(ii) User Forums would then also need to be reviewed in order to ensure they represented a wide enough range of user interests.

g. How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?

The Payments Council is currently unable to enforce decisions at all. We anticipate that in practice it will continue to be difficult for the Payments Council to do so. We would also be concerned that this could make it even more difficult for the Payments Council to take decisions.

If it is unrealistic to expect the Payments Council to enforce decisions, it may be possible to give it the tools to require members to report on progress with relevant initiatives. If this was made public, it would be possible for this to be taken into account by consumers when making decisions about which systems to use and also by Government and the Regulators, so that they are able to employ any existing applicable sanctions. It could also help to clarify exactly what sanctions it would be helpful for the Payments Council to have and to demonstrate how well the self-regulatory environment is working.

Question 3

a. Do you agree with the proposed remit for a new Payments Strategy Board?

We recommend that the PSB remit is significantly strengthened to give it a remit to ensure that consumers have access to safe, convenient and affordable payment systems.

The PSB should seek to do more than ‘promote/encourage’ the industry to take action. It should have a clear set of expectations of what the UK needs from its payment systems and should work to ensure that these expectations are reached. Although it will not be able to compel the industry to comply with its recommendations, it should publish clear reports on how well the industry is delivering for the UK.

We strongly support the Government’s expectation that the PSB would carry out research into the operation of payment systems. Whilst we do not want the PSB to replicate the Payments Council, it is important that it can challenge the Payments Council effectively. We view the PSB as having a challenge, rather than advisory role and therefore consider it should have a stronger remit. It should also be appropriately staffed and resourced.

It may also be appropriate to give the PSB an explicit remit to oversee the Payments Council, especially in respect of the Payments Council's strategy setting function. However if this is added, it should not remove the wider remit currently given to the PSB. It is important that the PSB should consider the whole of the payments landscape, not just that segment represented by the Payments Council.

Although we do not want the PSB to replicate the Payments Council, we are concerned that there is a risk it could have its remit limited in a way which makes it difficult to operate effectively. One way to draw a boundary could be to specify that the PSB is focused on 'public interest issues'. It should be clear that public interest does not mean 'something which interests the general public' or 'consumer facing'. The PSB may rightly need to consider issues which the general public would never otherwise be aware of. We think that a remit along the lines suggested by the Government in this consultation, strengthened as described above would cover this. However we can see some advantages to using 'public interest', appropriately understood as a guide to issues of concern to the PSB.

The PSB must also be able to react to changes in the payments landscape and take up issues on its own initiative. It should not be restricted to reviewing strategies already determined by the Payments Council.

b. Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.

As there is no single regulator for the payments industry it is difficult to see how the PSB can effectively require action. We therefore agree that initially the PSB should work by recommendations and transparency, but that this should be reviewed and if appropriate improvements are not seen then the Government should give more thought to mandating action. One way this could work would be to pass Payments Council funding through the PSB.

c. Do you agree that the Payments Strategy Board should include senior industry representatives, non-industry representatives and independents? What do you consider to be the right composition of the Board?

As the PSB is not mandating action and is not seeking to replicate the Payments Council we recommend that the PSB has either no or token representation from the industry. Industry will be well able to represent its views through the Payments Council. We in theory support the inclusion of non-industry representatives, however in practice we see a very limited number of possible candidates from a consumer perspective. It may therefore, be more appropriate that the majority of the PSB are independents. This may also help to keep the PSB to a manageable size.

d. Should the Payments Strategy Board have a formal information gathering power? If yes, what information should be covered by such a power, and what should an appropriate enforcement mechanism be?

We would support a formal information gathering power, especially as this would add to the PSB's ability to act as a check and balance to the Payments Council. The power could be contained in the legislation setting up the PSB and for payment providers regulated by the FSA, existing sanctions examined to see whether they could be used for enforcement. Where payment service providers are not currently regulated by another regulator we anticipate that these will usually be smaller providers who have more to gain by providing information than not complying. If this is not the case, the Government could consider giving the PSB the power to issue fines and to publicly censure.

e. Do you agree that the Payments Strategy Board should be funded by an FCA levy on the payments industry?

No answer

f. Should the FCA have any further controls over the Payments Strategy Board?

We are sensitive to the fact that the FCA should not have responsibility for a body it does not have control over. The FCA could be asked to review the effectiveness of the PSB a regular intervals, however this may be better done by an independent review reporting to the Treasury.

We do not forsee equivalent issues with the PSB as have been experienced with the Money Advice Service, as the PSB will be operating on a much smaller budget and will not be delivering services directly.

We do see a challenge for the FCA, in that its role is primarily to stop bad conduct, whereas the PSB will be looking more positively to require payments providers to take action to improve systems or develop new ones. This is a fundamentally different approach and may make integrating the PSB into the FCA more difficult.

It also makes it more difficult for the FCA to play the role of 'backstop' if the PSB is not able to achieve the results it is seeking, or allow it to intervene even when serious service issues, such as the ending of a service relied on by vulnerable consumers' is at stake.

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[i] The Future of Cheques, 2011, Treasury Select Committee
[ii] Government response to Future of Cheques
[iii] Competition in UK Banking: A Report to the Chancellor of the Exchequer, Don Cruickshank, March 2000 (The Cruickshank Report).
[iv] The Way We Pay: payment systems and financial inclusion, Age UK, 2011
[v] Article 3.1, Memorandum of Association of Payments Council Limited

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Setting the Strategy for UK payments

Dear Sirs

Thank you for inviting Aldermore Bank plc. to respond to your consultation brief on UK Payments. As a "Challenger Bank" we are keen that the UK payments systems work in an efficient and transparent manner that benefit end customers and promote innovation and cost effectiveness.

We have recent experience in securing greater access to the payments infrastructure in the role of an Agency Bank including allocation of our own sort codes for customers. While we believe this process to have been successful for us and our customers, there is still a lack of transparency of costing between the large players dominating the market, and there is still a major dependency between ourselves and our sponsor bank to provide continuity of service. Recent disruptions in service for major players highlight the disruption this can cause for downstream institutions and customers and for general systemic failure.

An efficient payments system is vital to customer choice and also innovation in payments as customers choose digital channels such as Internet and mobile payments solutions. We encourage steps that allow individual organisations to innovate and promote new solutions without the constraints that may result from slower changes in the payments infrastructure or sponsor banks. Challenger Banks may therefore be held back to the pace of change of the wider industry rather than being at the vanguard of change. Longer term we also believe there should also be a fuller review into the portability of account numbers akin to mobile phone portability between different sponsor banks.

We have also recently attended sessions with the UK Payments Council that point to greater openness to work across the Industry, and not just the large players, although we remain concerned that this must be effective engagement that delivers on solutions and commitments for the Industry and consumers as a whole, and does not in itself become a substitute for real action.

We welcome greater industry consultation and certainty. While broadly supportive of option 2 and the establishment of a strategic body, we also support greater openness and transparency through Option 1 if this can be achieved to meet the same aims with less overhead.

We have responded to your detailed questions as requested and look forward to hearing of your conclusions.

Yours faithfully

Paul Myers

COO Aldermore Bank plc.

Question 1
Do you agree that the creation of a Payments Strategy Board:

- should be the lead option for reform;
- provides the appropriate balance between Government intervention, impact and cost; and
- Effectively tackles the issues the Government has set out?

Please provide evidence where appropriate to support your answer.

Response:

Aldermore supports the need for greater transparency in the area of payments.

We agree that the establishment of a new regulator (Option 3) is likely to be costly and may in fact slow down innovation in the Industry.

We support the creation of a Payment Strategy Board if it is also coupled to greater transparency and change within the Payments Council – we do not believe that one can exist without the other. Recent steps from the Payments Council to be more open are welcome developments which need to be built upon as opposed to lip-service to true reform.

We also believe that a Payments Strategy Board needs to truly help drive innovation in digital payments and greater cost transparency/efficiency while maintaining a key role ensuring the integrity and resilience of the overall payments networks in the UK.

We therefore support the establishment of a lean Strategy Board than can help drive the strategic agenda across the industry without undue overhead, but fully supported by greater openness from the Payments Council.

Question 2

The following questions relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds with Option 2.

A Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?

B How can a clearer separation of the Payments Council's strategy setting and trade body representative functions be best achieved?

C Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?

D Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council's board can be strengthened further.

E Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?

F How can Payments Council funding be put on a long term, secure footing?

G How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?

H How can the membership of the Payments Council be broadened most effectively?

Response:

A) We agree the current remit and objectives are clear, though prone to interpretation. We welcome wider and effective consultation across the Industry and greater competition – through innovation and greater cost transparency. De-mystification of the workings of the payments council is welcomed, as well as greater inter-working of the payments networks to reduce the cost of entry (most Financial organisations have to create differing systems and operational interfaces to work with the many and varied payments networks).

B) We believe that the roles of strategy and implementation can be effectively split by constituting separate "Boards" within the Payments Council to effectively challenge between customer needs/strategic innovation, and their delivery across the wider trade bodies.

C) We welcome greater openness but would suggest that annual reporting does not reflect the increasing pace of innovation across the industry and would welcome more focused quarterly updates.

D) We welcome appropriate checks and balances to ensure that decisions are grounded in the wider needs of customers. We'd encourage greater challenge to Board decisions and therefore in principle support veto by two independent directors so long as this does not lead to paralysis on decision making.

E) We encourage greater communication – as long as these lead to increased traction without adding delay or bureaucracy around improving services.

F) The current funding mechanism by volume of payments is sensible and proportionate. We believe this does not need changing given the relative stability of volumes within the larger banking organisations.

G) There needs to be a "contract for change" that is agreed by the key members as part of the reconstitution of the Payments Council. This can be self-regulated with peer reviews to ensure that there is a broad drive for change without individual players slowing down innovation due to perceived self-interests and priorities (e.g. as in the implementation of Faster Payments)

H) We believe the inclusion of further financial organisations, such as Challenger Banks, as well as some business/consumer advocates can bring a fresh perspective to the Payments Council so long as they are given an effective voice and vote to help drive change forward.

Question 3

A Do you agree with the proposed remit for a new Payments Strategy Board?

B Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.

C Do you agree that the Payments Strategy Board should include senior industry representatives, non-industry representatives and independents? What do you consider to be the right composition of the Board?

D Should the Payments Strategy Board have a formal information gathering power? If yes, what information should be covered by such a power, and what should an appropriate enforcement mechanism be?

E Do you agree that the Payments Strategy Board should be funded by an FCA levy on the payments industry?

F Should the FCA have any further controls over the Payments Strategy Board

A) We agree with the remit, and encourage a lightweight approach to ensure that this helps drive positive movement with the Payments Council, rather than creating an additional layer for negotiation of change.

B) We believe a process of strong recommendation to be appropriate, although these should be backed up with more direct compulsion where it is evident that progress is being hampered by self-interests. We would encourage the Strategy Board to be mindful and proportionate in actions and especially to consider the downstream costs of change within smaller organisations.

C) We believe a broad spectrum of informed representatives is correct, especially where this can include smaller organisations and the voice of the end customer. This composition should be fresh and not encumbered by the size of the major players.

D) We strongly support the information gathering power where this supports greater transparency on costs and performance to allow informed choices for both the industry and end consumers.

E) We believe the current model of the Payments Council, based on volumes of payments to be an effective “tax” based on consumption and would encourage extension of this to the Payments Strategy Board.

F) We believe the FCA should maintain an effective oversight on the Payments Strategy Board to ensure integrity and resilience of the UK payments networks as well as ensuring transparency of operation across regulated entities.

Question 1
Do you agree that the creation of a Payments Strategy Board:
• should be the lead option for reform,
• provides the appropriate balance between Government intervention, impact and cost, and
• effectively tackles the issues the Government has set out?
Please provide evidence where appropriate to support your answer.

This should be the lead option. It strikes the right balance between tackling the issues identified in the consultation and imposing greater costs through a regulator. It would be an effective complement to a reformed Payments Council. Option 1 and 2 together are the most appropriate reforms.

Question 2
The following questions relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds with Option 2.
a Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?
b How can a clearer separation of the Payments Council's strategy setting and trade body representative functions be best achieved?
c Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?
d Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council's board can be strengthened further.

The narrower any board is, the more likely that problematic proposals are to be overlooked. In these circumstances, giving a right of veto to two members with strong objections is sensible.

But we feel this is unnecessary if the board is indeed broadened in the sorts of ways discussed in the consultation. With a membership that represents the broad range of payments providers and consumers, the board will be much more likely to reach sensible, generally agreeable decisions in the first place. Where proposals had achieved this broader support, having been road-tested by this board, we feel a further right of veto for a mere two members would make it very difficult for good but nonetheless controversial proposals to succeed.

There is a balance to be struck between ensuring the full breadth of interests is accounted for and preventing any one interest overriding all others. We feel a broader board will be more effective in achieving this than an effective requirement of almost total unanimity.

e Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?
f How can Payments Council funding be put on a long term, secure footing?
g How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?
h How can the membership of the Payments Council be broadened most effectively?

We believe the interests of consumers should be taken into account, and they should be represented on the Payments Council. The best consumers representatives would be economically trained. Maintaining antiquated technology and payment solutions may be against consumers' interests if the costs of doing so are high and widely dispersed among all consumers, for the benefit of a small few.

The industry as a whole, without a bias towards the largest banks, should also be properly represented.

Question 3

a Do you agree with the proposed remit for a new Payments Strategy Board?

b Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.

The Payments Strategy Board should make recommendations rather than mandate actions. The idea of the industry either adopting the PSB's recommendations or explaining their reasons for rejecting them is proportionate.

c Do you agree that the Payments Strategy Board should include senior industry representatives, non industry representatives and independents? What do you consider to be the right composition of the Board?

This mixture of representatives will ensure a broader balance of interests and priorities is represented. But we take issue with the potential for 'senior industry representatives' to mean only the very largest payments providers are representative of a much larger industry. allpay processes £3.8 billion a year, across 46.8 million transactions, for 750 public sector clients - including 2 million transactions a year for the Ministry of Justice. But if 'senior industry representative' means HSBC, Santander, JP Morgan, RBS, Lloyds Banking Group and Barclays – all currently on the Board of the Payments Council – then firms like allpay would not appear to qualify. On some issues companies across the industry will be in agreement, and 'senior industry representatives' can represent the whole industry - but on others, they may be better only at representing the largest.

Rather than including "senior industry representatives, non industry representatives and independents", we suggest that the Payments Strategy Board should "include a broad range of industry representatives, non industry representatives and independents".

d Should the Payments Strategy Board have a formal information gathering power? If yes, what information should be covered by such a power, and what should an appropriate enforcement mechanism be?

e Do you agree that the Payments Strategy Board should be funded by an FCA levy on the payments industry?

f Should the FCA have any further controls over the Payments Strategy Board?

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8 October 2012

HMT CONSULTATION "SETTING THE STRATEGY FOR UK PAYMENTS"

Introduction

Bacs Payment Schemes Limited (Bacs) is pleased to respond to the above consultation. Founded in 1968 Bacs is a not-for-profit, membership-based industry body is owned by sixteen of the leading banks and building societies in the UK, Europe and US[1]. Bacs is responsible for the schemes behind the clearing and settlement of automated payments in the UK including Direct Debit and Bacs Direct Credit and has been maintaining the integrity of payment related services for over 40 years.

The Government acknowledges that the Bacs payment system is of critical importance to the UK financial system and has confirmed that it meets the recognition criteria set out in the Banking Act 2009. Bacs is, therefore, regarded as an FMI recognised as systemically important by HMT and overseen by the Bank of England.

Since its inception, over 90 billion transactions have been debited or credited to British bank accounts via Bacs. And in 2011 over 5.7 billion UK payments were made this way with a total value of £4.3 trillion.

Bacs works closely with the Payments Council under a 'contracted scheme' arrangement for the benefit of the UK payments industry and the end users of the UK payment systems. In addition to this response Bacs has contributed to, and supports, the Payments Council's response to this consultation.

Response

Question 1: Creation of a Payments Strategy Board

Bacs supports the Payments Council's views regarding the desired outcome for a new strategy setting function (under a governance structure envisaged with both options one and two) that – in particular:

[1] The members of Bacs have contributed to this consultation response although the Bank of England have not participated in the formation of Bacs' view.

- Clearly defines a strategy that encompasses all types of payments used by all sectors of users in the UK.

- Ensures strategic prioritised decision making that is balanced, based upon sufficient analysis, has credibility over the long term and is made with regard to the wider public interest.

- Ensures that focus is placed on areas of genuine need or innovation opportunities that are deliverable both over the short and long term.

- Ensures that an appropriate balance between innovation and preserving the integrity of the payment system is maintained.

Question 2: Proposed changes under option 1

We agree that the current remit and objectives of the Payments Council remain broadly appropriate and support the Payments Council's view that there is benefit in ensuring that their objectives fully reflect their role and responsibilities following the conclusions of this consultation.

In particular we believe that there would be benefit in reviewing the role and responsibility of the Payments Council in respect of the integrity of all payment services in the UK.

Question 3: Proposed remit and strategy for a new Payments Strategy Board

To fully meet the objectives of the new Payments Strategy Board as set out in paragraph 5.24 we believe that all methods of payment used in the UK should be encompassed along with their respective payment scheme operators (Financial Market Infrastructures (FMI)) treated on an equal basis.

In agreeing a Target Operating Model (TOM) and to ensure the successful implementation of any revised model for the strategic direction of payments in the UK we would:

- Seek clarity as to the nature and operation of the relationship between Bacs (as an FMI recognised as systemically important by HMT, overseen by the Bank of England and in a 'contracted scheme' arrangement with the Payments Council) and the proposed Payments Strategy Board.

- Seek to ensure that for FMIs in a 'contracted scheme' arrangement with the Payments Council that the chosen operating model respects the rights, responsibilities and relationships of all entities (including System Operator responsibilities of schemes that have been recognised by HMT as Systemically Important under the Banking Act 2009).

We are pleased to note that the Banking Reform white paper (paragraph 4.39) states that the current statutory oversight regime is preserved for systemically important systems.

The need for a clear TOM may also be required for UK payment systems that are not currently in a contractual arrangement with the Payments Council.

Michael Chambers
Managing Director

HM Treasury Consultation
Setting the Strategy for UK Payments
Response on behalf of Barclays Bank plc

Executive Summary

Barclays Bank plc welcomes the opportunity to respond to HM Treasury consultation 'Setting the Strategy for UK Payments'.

The payments system provides a service for the general public, SMEs and large corporates so it is critically important that it operates with users' interests at heart. As a founding member of the Payments Council we remain supportive of its work but recognise the need for reform. Our preferred policy outcome is Option 2 - the creation of a new Payments Strategy Board (PSB).

Option 2 provides a welcome fresh start, and could be put in place swiftly and cost effectively. It is important, however, to ensure that a new governance structure is stable, effective and workable. To this end, we would like to offer the following comments and recommendations.

- The credibility and effectiveness of the PSB depends in great part on the ability of the Independent Directors to provide appropriate challenge. The reaction to the proposed phasing-out of cheques in 2011 illustrated a stark divergence between public opinion and the industry. It is therefore essential that the Independent Directors appointed to the PSB are able to provide that all-important 'external voice'. The expertise and experience of the Independents is far more important than voting structures. The priority should be to ensure that the Independent Directors have sufficient understanding and experience of the UK payments sector to ensure discussions and decisions always take account of the full range of perspectives. In doing so, stakeholders will have confidence that the strategic direction of the PSB reflects the needs of users. If this cannot be achieved, the PSB is likely to face the same challenges as the Payments Council.

- Allied to this, the reaction of politicians to the proposed phasing-out of cheques highlights the importance of a close dialogue between the PSB and Government. We believe the PSB should act as a conduit between the industry and Government, ensuring that each is aware of the others' concerns and priorities. This dialogue could be facilitated by ensuring HM Treasury is consulted on key decisions.

- Likewise, the relationship between regulators and the PSB is also critically important, so we agree that the Bank of England should have observer status on the Board. We also believe the Bank of England should have ultimate responsibility for maintaining the integrity and effectiveness of the payments system, which proved so critical during the financial crisis and continues to be paramount. It is appropriate that this oversight role belongs to a regulator rather than the PSB.

- As proposed in the consultation document, we would like to see the PSB offer strategic direction at a high level, leaving implementation to the payments industry. If the PSB is to perform this visionary function effectively, the industry representatives must be suitably senior. One of our primary concerns about a revised Payments Council under Option 1 is that it may remain overly operational, rather than focusing on strategy.

- We support the proposed objectives of the PSB and agree that the payments system must operate for the benefit of users. Although driving change should be included in the PSB's objectives, innovation in payments is often best delivered through competition. Rather than deciding on which innovations to promote, a core PSB role should be to ensure that there is the right framework in place to enable innovation and investment. In fulfilling this role, it will be important that there is a dialogue between the PSB and the Government and regulators, as outlined above.

The creation of the PSB provides a great opportunity to restore confidence by ensuring it can make the right decisions for users of the payments system. For the reforms to be effective and lasting, the challenges faced by the Payments Council must be addressed at the outset.

Consultation Questions

Question 1

Do you agree that the creation of a Payments Strategy Board:
- **should be the lead option for reform,**
- **provides the appropriate balance between Government intervention, impact and cost, and**
- **effectively tackles the issues the Government has set out?**

Barclays supports the creation of a new Payments Strategy Board and believes this should be the lead option for reform.

The creation of the PSB represents a sensible and proportionate policy response, capable of achieving the Government's objectives. We believe this option provides a welcome fresh start, and could be put in place swiftly and cost effectively.

The payments industry would benefit from more senior level strategic input via a Strategy Board, and the Board could be strengthened by the appointment of Independent Directors with sufficient expertise in payments to offer appropriate challenge.

Question 2

a) Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?

The Payments Council has three main objectives, all of which we broadly support:

- To have a strategic vision for payments and lead the future development of co-operative payment services in the UK
- To ensure payment systems are open, accountable and transparent
- To ensure the operational efficiency, effectiveness and integrity of payment services in the UK

We would also suggest that the Payment Council's objectives are broadened to include ensuring that the payments networks should operate for the benefit of all users, as proposed for the PSB under Option 2.

In addition, we note that the Payments Council has a key role in representing the UK payments industry at a European level. It will be important to dovetail any changes in UK payments governance with those taking place in Europe.

b) How can a clearer separation of the Payments Council's strategy setting and trade body representative functions be best achieved?

There is a tension between the Payments Council's role in fulfilling the remit given to it by the Government in 2007 and the role of a traditional trade association inherited from APACS. The creation of the PSB would provide the best opportunity for this tension to be resolved, though it could be possible to separate out these types of activity within the current governance structure under Option 1. The Payments Council could continue to have a strategy-setting and implementation role, and also a separate trade body of committees made up of payment institutions and banks.

If Option 2 is pursued, it would be most appropriate for the PSB to provide high level strategic vision, leaving implementation to the industry. The Payments Council could combine strategy implementation with a more traditional trade association role. The costs of payments regulation may increase significantly with the creation of the PSB, so it is important to avoid duplication of activities.

c) Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?

Yes. This approach would build on existing activity, as the Council currently reviews its progress every two years and publishes an Annual Report which includes a section written by the Independent Directors.

d) Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council's board can be strengthened further.

We understand the rationale behind giving any two independent directors a right of veto, but this is a considerable power to award any minority group. Arriving at good decisions is more likely to come through discussion and compromise rather than minority veto (or threat of veto).

Far more than voting structures, the most important consideration is the expertise and experience of the Independent Directors. Despite best intentions, the ability of the Independent Directors to provide sufficient counterbalance to the industry has been limited to date. In order for reforms to be effective and lasting, the selection process must be sufficiently robust to ensure the Independent Directors and Chairman have sufficient knowledge, experience and understanding of the UK payments sector to provide an appropriate degree of input and, if needed, challenge. This is where efforts should be focussed.

e) Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?

While the User Forums provide an effective forum for stakeholders, we agree that they could be further improved by being upgraded to User Councils. This would require additional resource and the Government would have to be confident that there is sufficient appetite among stakeholders for regular engagement of this nature.

If Option 2 is taken forward, it would be advisable for the User Councils to have close dialogue with the Strategy Board.

f) How can Payments Council funding be put on a long term, secure footing?

If Option 2 is taken forward and the PSB funded by an industry levy, our preference would be to leave the Payments Council's funding model as is, befitting a voluntary membership organisation.

g) How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?

The challenge for the Payments Council is not how to enforce a decision but how to reach the right decision in a timely manner. The best way to address this would be to have more senior level strategic input to the Board and to appoint independent directors with sufficient knowledge of payments.

h) How can the membership of the Payments Council be broadened most effectively?

The Payments Council's membership criteria were deliberately drafted to be as inclusive as possible. We agree that the membership base of the Payments Council should be opened to payment service users and organisations with an interest in payments by creating different categories of membership.

Question 3

a) Do you agree with the proposed remit for a new Payments Strategy Board (PSB)?

We agree with the objective to promote access to payments networks by the industry on reasonable terms .

We also agree that the payments system needs to operate for the benefit of all users, as it provides a service for businesses of all sizes and the general public. However, it is also important that changes are only mandated following an appropriate Impact assessment, which takes into account the costs and benefits of all participants. For example, a new payment service that benefits end users could offer only a marginal return on investment or present a poor business case for the industry.

Although driving change should be part of the PSB's objectives, innovation in payments is often best delivered through competition. Rather than deciding which innovations to promote, the PSB should ensure that there is the right framework in place to enable innovation and investment. In some cases, a watching brief may be sufficient.

In order to provide useful direction, we would like to see the PSB set out a high level vision for the payments industry, focusing on 'big ticket' items such as account switching. The more detailed lower level developments sit most appropriately with industry associations, such as the Payment Council, or the payment schemes.

We agree that the PSB should be accountable to the FCA. However, it will be important for the respective powers/responsibilities of the FCA, HM Treasury and the Bank of England to be clarified so as to avoid the potential for duplication and/or potential conflicts of interest e.g. the priorities of the Bank of England and the FCA might differ in relation to the priority expectations placed on the recognised payment schemes.

The OFT commented in its review in March 2009 that the UK payment system had continued to function reliably throughout the financial crisis. This remains a critically important priority, so we believe the Bank of England should have a responsibility to maintain the integrity of the payments system.

It is difficult at this stage to offer any comment on the future role of the Payments Council, as this will depend on role of the PSB.

b) Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.

We agree that the PSB should make recommendations to the payments industry rather than requiring action. Following a PSB decision, we envisage implementation delivered by the industry.

As the conduit between Government/regulators and the payments industry, it might also be appropriate for the PSB to make recommendations to the regulators and to Government.

We are concerned that giving the PSB formal powers to require action would effectively turn it into a regulator, which would stray into Option 3 of the consultation

c) Do you agree that the Payments Strategy Board should include senior industry representatives, non industry representatives and independents? What do you consider to be the right composition of the Board?

The PSB should include senior level representation so that it can provide clear, strategic direction. We would recommend that it meets no more than twice a year to ensure that it attracts sufficiently senior representatives. We envisage representatives drawn from all types of payment services providers, including the largest providers, the smaller banks with experience of agency arrangements, and non-bank institutions. The Payments Council has been criticised for domination by the largest banks, so it is essential that this perception is not carried forward into the PSB. However, the success of future payment systems depends on achieving reach and investment - as demonstrated by the new Faster Payments Service - so it is important to include the largest banks in the process.

It is critical that Independent Directors have expertise and experience in the UK payments sector, and are provided with sufficient resource/briefing by the PSB. Despite best intentions, the ability of the Independent Directors to provide sufficient counterbalance to the industry on the Payment Council has been limited to date. If the PSB is to achieve the Government's objectives, it is essential that the Independent Directors provide an effective counterbalance to the industry.

Although the role of Independent Directors is extremely important on the PSB, we do not believe it is necessary or realistic to include them at all levels of the Industry structure (e.g. the Payments Council, other trade associations, and the Schemes, many of which are independent commercial organisations) as finding a sufficiently wide pool of willing candidates would be challenging. If the PSB focuses on strategy and the Payments Council essentially executes the strategy, it follows that the PSB is where the independents can provide most value.

We agree that the Bank of England and the FCA should be given observer status, and would like to see HM Treasury fulfil a consultative role. The reaction of politicians to the proposed phasing-out of cheques highlights the importance of a close dialogue between the PSB and Government. We believe the PSB should act as a conduit between the industry and Government, ensuring that each is aware of the others' concerns and priorities. This dialogue could be facilitated by ensuring HM Treasury is consulted on key strategic decisions.

Linked to this suggestion, experience demonstrates that effective stakeholder engagement and communication is crucial, so we suggest that the User Councils have a close dialogue with the PSB.

d) Should the Payments Strategy Board have a formal information gathering power? If yes, what information should be covered by such a power, and what should an appropriate enforcement mechanism be?

We are concerned that giving the PSB formal information gathering powers would effectively turn it into a regulator, which would stray into Option 3 of the consultation. If these powers are required on occasion, they would be available to the FCA.

e) Do you agree that the Payments Strategy Board should be funded by an FCA levy on the payments industry?

An FCA levy may be appropriate and, in any event, the creation of the PSB would provide an opportunity to review the balance of funding across the industry. The five largest banks currently provide in excess of 80% of the Payments Council's funding. This is partly because cost allocation follows size in terms of qualifying UK payment volumes and partly because the Payments Council has followed a deliberate policy of keeping costs to a minimum for smaller players so as to be as inclusive as possible.

f) Should the FCA have any further controls over the Payments Strategy Board?

We agree with the proposed powers for the FCA, which would include the power to appoint and remove members of the PSB.

Payments Consultation
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BBCCL

Belfast Bankers' Clearing Company Limited

5 October 2012

Dear Sirs

<u>Setting the Strategy for UK Payments</u>

Thank you for giving us the opportunity to respond to your consultation on Setting the Strategy for UK Payments. We do not intend to respond to each individual question in detail, rather provide you with some general views we believe to be relevant to our Scheme Company in the context of the options for the future. Our member banks may, of course, wish to submit their own responses to the consultation.

We would firstly just like to clarify that in Annex B (Glossary) you make reference to the Cheque & Credit Clearing Company Limited managing the cheque clearing system. That is certainly true as far as Great Britain is concerned but it is not true for Northern Ireland (NI) and as the consultation is UK wide we feel it is important that this fact is recognised. It is the Belfast Bankers' Clearing Company Limited which has responsibility for overseeing the cheque and credit clearing systems in NI. While there are many similarities in cheque / credit processing in GB & NI there are some notable differences and we would be happy to discuss these with you if required.

We would be entirely happy to comply with and work with a Payments Strategy Board if the government determines that to be the best solution to resolve the issues highlighted in your document. Nevertheless, since the Payments Council will still exist, we have some concerns at the prospect of another layer of regulation and oversight being added to our industry. As such we feel that Option 1 (Enhanced Self Regulation) under a strengthened, more accountable, more representative Payments Council would be capable of meeting the government's aims.

From our perspective membership of the Payments Council has, for the first time, enabled NI to gain a higher profile and to 'have a voice' on key industry decisions. It has also helped create awareness that UK initiatives may need to eg, take account of practices in NI or the prevalence of particular market segments, and we would appreciate if any proposed new regime made provision for NI representation in some form.

We do recognise that in terms of overall UK payments, NI represents a very small percentage of the activity and indeed the cheque clearing volumes for NI only amount to around 2% of the whole UK cheque market. As such we would not expect to be able to influence key decisions to any great extent but would be satisfied with a mechanism to ensure our voice is heard and that due consideration is given to NI, where appropriate.

A brief response to each of the consultation questions is included below.

Please do not hesitate to contact me if you would like any clarification on any of our responses or would like more information on our Scheme.

Yours faithfully

Ivan Laird
Chairman

Responses to Individual Questions

1. While we are relatively relaxed as to this question, on balance, we do not think that there is a need for a Payments Strategy Board as this will inevitably duplicate the existing Payments Council management and governance structure with the associated cost there-of. In addition there is the potential for "turf wars" between a Strategy Board and the Council which would only dilute the capacity of both to achieve their objectives.

Instead we consider that a Strategy Advisory Council should be established by the Payments Council, which should have a majority of non-service providers, and which would be tasked with the responsibility of producing strategic initiatives that would advance the services provided by service providers to users/consumers.

2a. No - See I above.

2b. By establishing a Strategy Advisory Council as set out in 1 above. This Council should have a majority of non-services providers and should contain user representatives.

2c. Yes

2d. No, as this would put too much power in the hands of two people. While we believe the Payments Council should have a substantial number of independent directors, which should include user/consumer representatives, the majority should be service providers as it is they who have to meet the cost of all service enhancements. The chairman should be selected from the independent directors and, as a safeguard where it was established as being in the public interest, a majority of the independent directors should have a right to refer board decisions to an independent arbitrator for review. However there should be no process which would permit coercion of the payments industry except any that is legislative.

2e. Yes, subject to them only having advisory powers.

2f. Funders should commit to a minimum contribution of say 75% of their 2012 funding for five years with the balance of funding required being negotiated annually.

2g. We do not agree that the Payments Council should have coercive powers. There will no need for these, provided it brings forward initiatives that have real and lasting benefits for both providers and users.

2h. It should have user/consumer representation.

3. W e do not consider that it is necessary or desirable to establish a Payments Strategy Board but have responded to the questions posed on the basis that a decision was taken to establish such a Board.

3a. No

3b. Yes

3c. Yes

3d. No

3e. No

3f. No

Response to HM Treasury Consultation on the future of the UK Payments Council

This paper is contributed to the government debate on the future of the regulation of the UK payments industry. It is firstly a reaction to the HM Treasury report and secondly a partial response to the HMT request for consultation.

It has been compiled by a group of consultants and people with significant knowledge of the payments industry.

It is authored by Peter Miller, an independent consultant, with 20 years experience of the industry, gained initially from providing payment systems to banks and latterly by working on the buy side of the payments industry, for example leading the sale of the Faster Payments Service and also working for two years as Director of Strategy for VocaLink.

Contributions to the thought process have been gained from several experienced people in Peter Miller's network, by discussion and by written contribution. This includes David Macfarlane – previously general manager of the CHAPS Clearing Company, previously with Clydesdale Bank.

And it has been externally reviewed by:

- Bryan Foss - Bryan Foss, Visiting Professor Business Markets, Bristol Business School (also ex independent board member DWP and DCLG) and
- Alison Bond, founder The Halo Works Ltd a market research company.

The paper is provided as a serious and knowledgeable view of the problem addressed. We would be happy to discuss its contents further.

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Right idea, wrong structure?

Synopsis.

The purpose of this paper is to reflect an opinion on the future of the UK Payments Council ("the Council"), as a response to the consultation paper produced by HM Treasury ("the Report"). This is, first of all, an article which presents a point of view on the whole topic but it also contains responses to the consultation on the preferred approach to change for the Council.

This paper agrees that the Council needs to improve its performance. The Report suggests a range of options for its governance and favours an externally appointed and new Payment Strategy Board. This paper agrees with many of the ideas presented in the Report but disagrees with the proposed structure for their implementation; and recommends that the Council be reformed instead, and that it should also be accountable to HMT, the OFT and the FCA on its progress.

Introduction

In its review of the Council, the inevitable conclusion has arrived from HM Treasury (HMT). The payments industry needs new and better regulation. This conclusion has been directly caused by:

- The controversy surrounding the attempt to get rid of cheques. It is important to remember that this was driven by the Council from an industry-wide consultation, and even if it was badly run, the Treasury Select Committee's reasoning against it was less informed than it might have been;
- but also the supposedly botched implementation of Faster Payments;
- and the banking industry's failure to address internet and mobile payment platforms. (The owning banks have not always been able to agree on collaborative initiatives.)

Thus, HMT concludes that the "payment industry" needs better direction than is currently being given by the Council, in order to achieve the world class money transmission market the government desires. It also sets out a consultative process, which is designed to agree the reforms to be made to the Council.

The Report is to be found on the following link.

httpwww.hm-treasury.gov.uk/d/setting_strategy_uk_payments190712.pdf

The Regulatory Proposal

The Report is presented as a consultative step on the way to the "right" answer. It offers three options, and a consultation process designed to select the second of them. The options are:

1. Reform of the Council to achieve better control, continuing to operate as a self-regulatory body. Specifically, this should offer bank account users greater input into the process of developing strategy and limit the ability of banks, individually or collectively, to block progress and change;
2. A Payment Strategy Board. This would be a new body reporting into the Financial Conduct Authority. It would have the power to make recommendations to the industry. But recommendations are not binding and can be blocked by the industry! Thus a relatively narrow part of the banking industry would be directed by political will rather than by the institutions which run it and pay for it. This is the option recommended by the Report;
3. A new regulator, a "Paycom" to direct the payments industry. Thankfully, the Report rejects this approach, first put forward in the Cruikshank Report of 2000.

There is (and quite rightly) no "do nothing" option. It is presented as a consultative paper. This paper is a response to the Report, firstly written as an argument and secondly, completing the questions asked in the Report on the option preferred by this paper, provided as an Annex.

Foreword

We should not belittle the problem in addressing it.

Self-regulation, which is the preferred option put forward in this paper, is not often successful. But, externally driven regulation on commercial entities (think about the decades of controversy surrounding the rail industry) is scarcely more so. And this is not just about regulation, it is about providing direction for as well as securing the payment infrastructure upon which the UK economy depends. Many interests have to be satisfied.

- Regulating it, or directing it, must satisfy the needs and interests of all sorts of customers - from the largest users of the infrastructure (Government in the shape of HMRC and the DWP), large and mid-sized corporates and SMEs, as well as the millions of us retail account holders.
- The infrastructure must not break. The economy stops if it does. This must be the top priority for government interest and concern. The integrity of the infrastructure cannot be compromised in the name of innovation or pandering to wacky ideas of the moment.
- And then there are governments and other regulators which demand change, either at a functional level (for example, the Payment Services Directive) or at a technical level;
- And then there are the banks which own the infrastructure – it provides their bread and butter – as well as being intrinsically linked to the accounting and product processing systems which banks use to conduct their daily business for their customers. It is these banks which have logically owned direction of the industry to date, and whose grip upon the infrastructure the Report is seeking to lessen, in the interests of all parties. Whilst we might be brutally and incisively critical of the behaviour of certain individuals and groups in banks in recent times, few misdeeds fall at the door of transaction bankers; in contrast, it is they who have sustained the integrity of the financial system, and it is their efforts and actions which provide sustainable economic growth.

In an ideal world, these interests need satisfying by discussion and collaboration, under strong leadership and on a publicly accountable basis, rather than being forced into shape by a regulatory dictate.

Electronic payments processing is part of banking, it is not some separate thing. It is therefore also important to ensure that the future shape of regulation or industry direction has a precise and well-defined scope.

This scope is confined to areas of co-operation between financial institutions, where electronic account-to-account payments provide legal finality of the movement of money - settlement. This is distinct from the world occupied by Payment Service Providers, who facilitate purchases and trade, but who do not themselves facilitate the final movement of money across a registered settlement system. Thus, if a collaborative infrastructure is required for mobile payments, then it is limited to the facility to clear and settle instructions across accounts, and does not include the competitive level of payment capture, where big commercial beasts (Visa, Mastercard, Google, PayPal and others) are currently competing, both to find the right "wallet" product for their customers, and to win market share. Natural selection is occurring in this part of the market place.

The scope however must not be confined to sustaining the as-is state. It cannot be assumed that innovation in clearing and settlement will occur through natural competitive forces. Furthermore, deeply networked economic systems in developed economies have a strong inertia against innovation. Absence of (appropriate) innovation risks regulators imposing change, and core skills and services moving offshore. As in all successful businesses, it is essential to scrutinise what needs to be done to maintain a leadership position – and to enforce the implementation and adoption of necessary change.

Recommendation

This paper supports the first option presented in the report, the improvement of the structure and the operation of the Council. Self-regulation, bringing all of the parties together to achieve consensus on industry development is argued as preferable to the creation of a new body attempting to force change from an external position. The banks own the payments infrastructures and fund them for the benefit of their customers. They must have a major say in their future development.

Increasing scale and scope of regulation should be a last resort. Others have commented that the current scale of regulation imposes a near-unmanageable burden on the banking industry; incrementing this burden is unlikely to have the effect the regulator desires.

Some aspects of management of the payments industry, for example the maintenance of its integrity and the avoidance and dissipation of systemic risk, will be better governed by responsible industry experts than through regulation, inasmuch as regulators are unlikely to have the detailed hands-on knowledge required.

How the Payments Council should be regulated and managed depends on its goals. Whilst it is important to recognize the aspirations of the customer, these must be tempered by the need to solve problems and drive future development from the perspective of what is safe, effective and reliable. Keeping the economy going is more important than nice-to-have innovation. The original remit of the Payments Council falls short, is not detailed enough and fails to prioritise. It is currently stated as:

- *"To have a strategic vision for payments and lead the future development of co-operative payment services in the UK*
- *To ensure payment systems are open, accountable and transparent*
- *To ensure the operational efficiency, effectiveness and integrity of payment services in the UK"*

It could be restated as:

The Payments Council sets direction and takes responsibility for the development of UK electronic payments, with the aim of creating a world-class and open payments infrastructure for £ sterling. This is led by a vision and clear principles, which are well-communicated. It should liaise, as frequently as is required, with such bodies as required, such as HM Treasury, the FCA and the OFT to present its approach and progress.

1. *Firstly, to ensure the operational efficiency, effectiveness and integrity of the existing payment networks in the UK, and to continue to develop them as both customers and banks require;*
2. *Secondly, to ensure payment systems are open, accountable and transparent. This includes the requirement to envision such common facilities and standards, which may be necessary to improve the safety, security and legal use of the payment networks;*
3. *Thirdly, to set out a vision for the contribution that the payments industry should make to sustaining and growing the UK's position as a major financial centre.*
4. *Fourthly, to lead the future development of new co-operative electronic payment services in and beyond the UK for the benefit of UK businesses and the UK economy. This includes the reasoning of what is, as well as what is not, in scope for collaboration or a common approach ;*
5. *Fifthly, to increase the ease with which bank account users can transact with other currencies, countries and economies as international trade and movement increases.*

In achieving its remit, the governance structure should ensure that it is not exploited as a forum to prevent or postpone innovation. Consensus decisions work well for the common good, but can be exploited, and must not be, by individual stakeholders to preserve competitive advantage. A separate decision-making process may be appropriate for innovations.

In other words, the remit should recognize that stability and transparency of the existing infrastructure are more important than its future development. Keeping it running is essential and more important than making it better, faster, cheaper, important though all of these are. Change must be approached carefully and consensually. This remit recognizes that:

1. The Council is a self-regulatory body, but must both present its case to government and fully answer government criticisms and questions. It must be largely self-regulated, because financial integrity cannot simply be mandated. The complex relationship between the different systems and processes can only be understood by industry experts; they must be empowered.

2. It sets a vision of the future, which the government can clearly see, which the industry, partially or wholly buys into (not all account providers are members of all clearings) , and in which bank account users can understand both the services they get now and the services they may get in the future;
3. Common concerns are dealt with. The development of security standards, and more particularly the requirements of many regulatory bodies on banks to police their systems can be addressed centrally. This is, for example, relevant to Anti Money Laundering requirements, set by many governments internationally, which are currently addressed at huge cost and with both practical and political difficulty by individual banks.
4. Customers' needs to make payments in other currencies to bank account users in other countries are taken into account. This addresses the growing needs of UK citizens working abroad, the need for UK companies to trade internationally and the needs of citizens of other countries working in the UK to send money home.

If the Council has not operated to date either well or in the way that the politicians wanted, it remains as the right sort of forum to achieve consensus, in which it is preferable to achieve progress by all players buying in rather than responding to a regulatory fiat.

The Report suggests, as its first option, changes to the remit of the Council, in order to do the government's bidding. But it should be remembered that the payments market is a free market, dependent for its future on the continued operation and funding of the existing players. Would it not be preferable, for example, to add an HMT representation to the existing structure rather than remove the ability of the industry to develop at a safe pace? It is worth noting that HMG's Departments of State are the biggest users of the payment schemes in the UK, by a distance, and as such have a significant interest in the Council achieving its objectives. This interest applies to both the Council and to the schemes which it runs.

It is clear that the Council is operating in the government's and the customer's interests anyway. One of the most frequently heard and recent chirps from politicians , as part of a general bank-bashing tendency, that the banking industry needs to provide the ability to customers to switch banking suppliers easily, seems to miss the point that the Council is already sponsoring an account switching program. Whilst this is not entirely a payments issue, the Council has provided the collaborative forum for this hugely difficult programme to happen (at an industry cost of an estimated £850 million.)

If this restated remit sets out the Council's objectives, the methods of achieving them within a changed Council structure are discussed later in the paper. BUT, these must all be subject to an independent audit to recognised international standards, with details made available as appropriate to Council stakeholders and to the general public.

Report Commentary

The HMT Report is incomplete. Some questions and issues are not covered.

1. The first is an obvious general one. Banks payment operations are subject to much regulation already, too much one might argue. They are operating in a supposedly free market, but are required:
    a. to operate to standards (UK, European and global);
    b. to work as government policemen to ensure that dirty money and terrorist funds are not transferred through them;
    c. they will be required to detect tax avoiders (soon FATCA from the US, but European legislation is also expected);
    d. to operate to the rules and levels required by the central bank supervisor;
    e. subject to the usual anti-competitive regulation (the OFT);
    f. to be responsive to new laws (such as the Payment Services Directive).

   Now the politicians want to impose an external strategy body to set direction, to replace the collaborative one which recognises the complexity of the existing market. These banks and their systems are supposed to both offer service and be profitable, at the same time as incurring huge cost. If challenger banks are complaining that the investment in the payment business is too high, then this is hardly the banks' fault. Mid-size banks (as opposed to challengers) have been considering and practicing the outsourcing of their clearing and settlement functions through agency arrangements for a long time, absolutely because the scale of their businesses does not justify the level of investment necessary to remain in the business let alone to be competitive. The risk of further regulation is that it will extinguish any vestige of free market operation. If you were a bank being asked to fund yet another regulator which limited its ability to compete, then the simple answer would be "why?" (As an aside, the US has recently imposed new regulation on its banks, in the form of the Dodd-Frank Act. Faced with near-impossible (and hence barely credible) demands, some banks elected to withdraw from some banking services. The regulator has responded by relaxing some minor aspects. But this has left a bad taste, and an unnecessarily adversarial position between the banking industry and the regulators.)

2. The second is that stability in the existing systems is more important than the overly required wish to innovate. They are presented here as equally important drivers. The Report recommends the introduction of a new body to direct a free market enterprise, which is currently regulated, mostly for the all-important safety, efficiency and stability purposes, by the Bank of England. The requirement to support UK plc innovation is not currently required at infrastructure level but in the channels that enable customers to input and commit their payment instructions, i.e. in the competitive areas of the market.
    a. The Report goes out of its way to approve of the Bank's role, as overseer. The clearing and settlement functions work very well, are funded and owned entirely by the banks, and operated in order to move money as cheaply, safely and quickly as possible.
    b. The interconnectedness, huge cost and potential fragility of the clearing and settlement infrastructure, composed as it is of both central infrastructure and the banks' payment systems, militate against external meddling and fast change. These systems don't

simply send messages, they move money and the daily completion of their clearing and settlement duties is essential to the operation of the UK economy. And they work.

3. The Report makes no suggestions as to the way in which the current account-to-account clearing infrastructure is deficient, but merely suggests that there is no “do nothing” option for its regulation, as it cannot be left to a bank-dominated Payments Council. In reading the various papers, it is also apparent that, for example, Visa and Mastercard might be brought into the same industry focus. This might be a bigger step than those producing theoretical papers in HM Treasury could possibly imagine. The credit card world actually competes with the banking world, whilst only the debit card accesses a bank current account. And the card industry has its own separate trade association.

4. It does not seem to have occurred to the report-writers to observe that some of the individuals who direct, staff and manage the Payments Council were not up to the job, in other words that performance of duty, rather than the nature of the duty itself is the problem. Anyone who watched the Council Chairman’s appearance in front of the Treasury Select Committee would have been struck both by his woeful performance but also by the inability of the TSC to properly understand the problems with which it was grappling.
    a. It is also notable that the level of bank representation in the Council is of substantially lower quality and seniority than was the case in the days of the old APACS Council.
    b. The UKPC needs directors who understand the industry and staff who are high quality experts and the external directors have been so far virtually invisible to outsiders in the relatively short life of the Council.
    c. It should have been hoped that the appointment of Adrian Kamellard on the organization as CEO and the introduction of new directors, notably Claire Spottiswoode, started to add sufficient weight to the Council. But HMT cannot wait for piecemeal improvement in the current self regulatory body.

5. What is the nature of strategy? The Council publishes its own. It has been criticised as it lacks a vision, but rather provides tactical plans which cover all of the bases. This is inevitable, in the sense that the future has to be built upon what we have, upon the huge investment which has already been made and upon which the economy depends, and what the various regulators demand, rather than being driven by a blue-sky strategy from Whitehall. The unqualified implementation by Parliament of the European Payment Services Directive (a directive with laudable objectives) in the UK, which failed to recognize that UK clearing already offered a choice to customers (immediate or three day clearing of credits) and demanded a D+1 standard for all direct credits, failed to take account of what was already there in the UK, ironically shaped by the demands of the OFT. The banks could not win. But, absent a clear long term vision and plan for execution, it is inevitable that short-termism will dominate. We will muddle through but that is unlikely to achieve a broader goal, such as sustaining and growing the UK's position as a major global financial centre.

6. What is the point of an externally appointed body to set strategy, which cannot impose its strategy and directions on the banking community? The Report admits that such a body can only recommend - it cannot mandate change. How can this be represented as an improvement upon a self regulatory body which tries to square away the different interests involved? How is this preferable to a body which would produce strategy properly and includes all of the players necessary to get agreement on it?
7. This approach also seems to have the effect of doubling up the resource requirement at the beginning of an enterprise for change. The envisaged Strategy body would do good things and after much work and resource effort come up with a brilliant new idea. Then it would be passed to the Council which will then go through the same process and after much work and resource effort suggest perhaps that there are inherent risks which make the enterprise unworkable and then under the "MoU" knock it back. (This is similar to the effect of separating the schemes from the infrastructure, which resulted in doubled resources in for example the Bacs scheme and VocaLink.)

   If the process is contained within the Council, all stakeholders would do this once and hence the need for HMT representation. There is a learning curve to be negotiated but a strong regulatory hand needs to be applied to the Council, especially at the outset of its reform.

8. If such an external strategy body is invented, how will the banks respond? They fund the Council. Why would they continue to do anything other than manage the existing infrastructure? A return to the old APACS structure would be the obvious consequence.

9. It also fails to take account of the difference between Payment Service Providers, who provide a channel to the customer to initiate and receive payment instructions (Paypal, Visa and Mastercard are the most obvious of these), and the banking suppliers which offer clearing <u>and settlement</u> facilities to customers and other PSPs through bank accounts and the established clearing and settlement schemes and thus provide the final and irrevocable completion of payments using central bank money. It is these clearing and settlement schemes which are essential to the smooth operation of the UK economy.

The banks and the Bank of England have to run and control the clearing and settlement systems, since their operation is a combination of the bank payment systems, the clearing infrastructure and the Bank of England settlement systems and processes.

They run well, and their failure would be far more damaging than the absence of an innovation or two. Some of these innovations are best left to the private sector to bring to market, and the banks must have the right to refuse them or to adopt them, not just on marketing and competitive grounds, but more importantly dependent upon the risk they pose to the smooth operation of the flows of money around the UK economy through the clearing and settlement systems upon which money transmission depends. The Report bears testimony to this in quoting the trillions of value which are transacted daily through them and which cause them to be listed as part of the National Critical Infrastructure.

The Problem

Several interests are managed by the establishment of the Council, coming as it does from its original APACS home. And these problems largely break down into two categories.

- The operation, the safety and integrity of the existing infrastructure, which are more important than;
- New customer requirements, presented as new developments and innovations and developed as an industry strategy.

The main concern must be the safety and integrity of the bank payment and the associated clearing and settlement systems, which are designed to settle defined payment instruments between financial institutions which offer them, through whatever method. As the Report rightly points out, these are hugely important methods for settling payments and keeping the economy rolling. The Bacs failure of a few years ago, shortly after VocaLink implemented a new technology infrastructure, demonstrates this. The successful operation of these clearing and settlement systems is intrinsically linked to the accounting systems of the financial institutions that use them, as the recent failure of RBS systems also demonstrates. You might estimate that RBS is involved in 40-50% of sterling payments as they are involved in the sending or receiving leg of at least 20% of total traffic. The unavailability of one bank in the clearing and settlement systems because its accounting or payment systems fail to function represents a systemic risk, which has to be taken into account. Requiring change implies risk, which has to be carefully managed. And the risk is posed largely by the sheer volume and value of the transactions being processed, and the interconnectedness of the complete infrastructure (bank systems, clearing infrastructure and settlement process) rather than by the nature of the participants in clearing and settlement.

The key mechanisms here are CHAPS, Bacs, Faster Payments and the cheque clearing. And the key systems are the clearing and settlement systems themselves, and the accounting systems of the banks to which they are linked and the Bank of England systems which provide the settlement capability. It is this interconnectedness which makes change slow and meddling risky.

The key role of APACS was to ensure the continued and safe development of facilities which were collective responsibilities. This role was and is performed well, as both the quality and the performance of UK clearing remains high. This perhaps underlines the need for independent external audit, to demonstrate to all that this continues to be run well.

The LINK system is also an important service provider. It offers a method for any debit card user to take cash from most ATMs irrespective of which institution owns the ATM. So it links the ATM networks of financial institutions and encourages other payment service providers to build their own networks. It is valuable, however it is not systemically important, in the same way that Bacs, FPS and CHAPS are.

These are the systems which move our money electronically between accounts and which the Council and its members are bound to safeguard, direct and improve.

So, you have a variety of instruments, each with an important set of rules associated:

- Direct Credits (systemically significant through CHAPS, three day through Bacs)
- Immediate Payments
- Direct Debits
- Standing Orders
- Cheques
- As well as cash card transactions

These instruments are automated through secure settlement systems, funded and owned by banks. They run well and offer the cheapest and safest means of moving money electronically between accounts. They are systemically significant, in that their failure to operate damages consumers, businesses and the economy as a whole. Change to them must be managed carefully and slowly. A good example of this was recognized by government in the passing before Parliament of the Payment Systems Regulations in 2009 (the UK implementation of the PSD) and its most onerous requirement, the provision of D+1 settlement for consumer-initiated direct credits, which was required to happen by Jan 1st 2012, over two years later.

And the change has to be collaborative in that many banks use the clearing and settlement systems, and for all of their functions to be used by all banks, agreement has to be sought. This is the reason that some change must take place at the speed of the slowest, which should not, of itself, be a criticism.

Payment Methods

It is likely that one or any of these existing payment instruments and the associated clearing and settlement systems will be used for the clearing and settlement of new payment METHODS such as mobile payments (note the distinction between instruments and methods) or credit cards. A mobile payment will (probably) be a direct credit issued from a mobile phone rather than a new instrument in its own right.

So, in the light of current industry striving (and huge competition) to provide mobile wallets we need to clearly define what we mean by a mobile payment as against a transfer of a token value between two mobile phones across the same or different mobile networks. In this instance, the mobile phone becomes the input channel to instruct a bank, in real-time or after the event at the PSPs risk, to execute a payment from bank account to bank account.

New payment methods will undoubtedly need to use the existing clearing and settlement infrastructures to achieve the final movement of money between accounts, as existing ones do. But these methods represent the competitive element of the market, in which collaboration either at a partial level or at a complete one is not always valuable, and could be anti-competitive.

The Charges

It is also worth noting the issues which led to the political demand for further regulation, in which the Council's failure is not as clear cut as it is presented. If ultimately, the government didn't get what it wanted or as fast as it wanted, then it was not entirely without cause. The three issues quoted are as follows.

1. The abolition of cheques.

It is undeniable that the cheque is the most unreliable, slowest mechanism which is most subject to fraud. It is thus being driven down in its usage.

- Less usage of cheques is good for customers and for banks. A similar drive to reduce the use of cash is also promoted.
- Cheque volumes are falling dramatically. Thus the unit cost of processing is increasing.
- It is also a mechanism used by small businesses in particular to protect their own cash flow. Post a cheque on a Friday and it will be ten calendar days before the value passes to the beneficiary, even if it looks as if the bill is paid.
- Further encouragement to find alternative methods of payment are being sought and in the interests of all parties.

BUT….. The cheque remains as the payment method of last resort, the use of which has not been entirely replaced by new mechanisms. Charities would have been the most obviously affected by the departure of the cheque.

As was recognised by the Treasury Select Committee, the banking community had no obvious plan in place ready to replace the cheque. But the TSC failed to recognize that the long date (2018) for the possible abolition was dependent upon the provision of alternatives, which if they weren't actually visible and planned, were being actively considered. And failure to develop them would have resulted in the continued existence of the cheque.

It was the Council's problem that it failed to communicate its plans and objectives at all well. The cheque would probably have survived anyway.

2. Faster Payments.

The success of Faster Payments has been under-played. The UK is one of the very few economies, and the only major economy which has implemented a real-time payment service for consumers. If you read North American papers on their payments industry, they are looking on with envy and are currently considering the implementation of a similar service.

Its development was fast (two years) to meet the political imperative. Payment systems take a long-time to develop, test and implement safely as is only to be expected for systems which move money finally and irrevocably, and this was too fast.

The main problem with its implementation, was the ability of the different member banks to introduce it safely and accurately, which was of greater concern than the need to implement a new service completely. The politicians are at least partly wrong here too.

3. Innovation.

Banking (and payments is part of banking) is a competitive market, in which the clearing and settlement mechanisms form a collaborative part. Some strategic issues and innovations for the industry are collaborative and some are a competitive matter. The debate as to whether mobile payments or internet payments are part of a competitive market will run and run. The Council has started to build a low level of competitive infrastructure for mobile payments at the same time as individual banks are competing with their own branded product or are ignoring the mobile element of the payments market. If banks see the mobile as another means of extending their electronic banking capability rather than as a discrete payment method, leaving the likes of Mastercard, Visa, Google and others to implement globally acceptable payment mechanisms using mobile technology, then that is their competitive choice. Not all markets, thank goodness, are driven by political wish. They are driven by the ability of the market players to invest, the viability of the plans they are investing in and the wishes of their shareholders.

Thus, this paper argues that the motives behind the creation of an external Payment Strategy Board are a little over-stated.

Is the Council fit for purpose today?

This paper should not be read as an unqualified support for the existing Council. As these bodies go, it is still relatively new and it has faults. This section concentrates on those faults.

- The most obvious one is that in all parts of its structure and governance, banks and even individual banks can block progress on almost any topic. Examples of this within the industry are legion, but hearsay. But, for example, it should have been obvious to even the most naïve outsider that discussions of a mobile initiative have been on an off the slate for several years. It was ironic, if hardly coincidental, that the final announcement of an industry initiative, which defined a competitive boundary, and the announcement of Barclays new Pingit service occurred within days of one another, some three or four years after the production of an industry requirement was first mooted. One large bank can stymie progress on an individual issue somewhere within the governance structure of the Council. This must above all be changed.
- The original National Payments Plan of 2008 is much improved by the 2011 update. It is improved in the sense that it is more obviously reacting to customer demand, even if that demand is calibrated from a small sample. But it is still a plan and not a strategy. There is much verbiage on the Council web-site of a strategic vision of the market being held. But there is no picture anywhere of what the future might look like, what is desirable or possible and therefore no target at which the Plan is being aimed. It covers lots of known bases, but fails to answer the question as to where it may all end up – and why. In one sense, this explains the cheque saga. The desire to get rid of the cheque was not reflected in an overall vision, which had to include how it might be replaced. A strategic vision is required, as a target for the Council and its members to aim at, and into which all initiatives proposed in the Plan can be fitted. And it should be remembered that a vision is not fixed – it changes as events and

developments change the view of the possible. Who, but the odd visionary, would have considered the mobile phone as a viable device for making payments ten years ago?

- All of the plans fail to cover the question of cost. How much does it cost to process a direct debit or a credit transfer, beyond the penny cost of clearing? It is in the industry's interests to be open about the huge cost of payment processing. The free banking principle obscures costs. It is desirable to make the substantial cost of processing visible to one and to all. As examples:
    a. one UK bank has an operational staff of in excess of 500 people to administer its AML checking to inspect the large numbers of transactions which might involve dirty money in its many forms. They review large numbers of payments for fear that they might infringe, and in practice stop less than 2% of the filtered transactions;
    b. the costs of implementing the Faster Payments Service were in the tens of millions for most of the banks.

  This kind of regulatory or operational investment/cost is invisible to consumers and the direction of travel for the industry has to be influenced by the unit cost of processing the various instruments. In the interests of transparency, some metric to establish cost has to be established.

- And there is no doubt that the work of the Council, and indeed of some of the schemes which report to the Council is limited by the dominance of the banks in the number of bank members and their combined strength in the voting structure. It is also clear that the level of bank representative on the Council has to be improved for many of the industry's members. The banks need to be represented by people who will consider a broader interest than simply what is in their own bank's payment business interests. "What do they know of cricket, who only cricket know?" What is in the industry interest and what is in the customers' interest have to be questions which enter the equation more strongly. Looking back at the old APACS Council it was clear that this representation used to be of greater seniority. Less so now.
- And the other players have a role to play. To the outsider, the performance of the external directors is not at all visible. The chairman is widely criticized. And the executive is led by people from the old APACS mould, more used to managing something which exists and less able to envision strategic change, let alone convince of it. Where is the leadership?
- The Council today only has MOUs in place between itself and the various schemes, so that control of each scheme remains with the banks. Real change to this is required. The Council must have full ownership of the payment schemes. The chairmen of the schemes should attend Council and be accountable for their responsibilities. Full ownership means full public accountability for the performance of PCR and Payment Schemes. Subsidiarity should replace the MOUs.

In reading the minutes of the Council over time and watching its performance, it should be recognized that it has achieved much that it is to be approved. That does not mean that it couldn't be better. And the performance of the external directors and chairman are not visible.

How should the Council be improved?

The government criticism of the Payments Council is partly justified. This paper argues that it is the performance of the Council which needs to be improved and that the industry should have the opportunity to get this relatively new house into the right order.

This is a function of organizational structure, of voting structure and of people, all of which need review.

First of all, this is about leadership.

The Chairman must be a leader with a senior banking background, commanding respect from all elements of the organization. Names such as Martin Taylor's come to mind, as this is an important appointment, providing governance to a large part of the banking industry.

Secondly, it is about public accountability.

If the industry is to avoid the imposition of full scale regulation then it must be transparent as to its performance and delivery and this transparency must be independently audited and attested by an external firm of auditors.

With public accountability must come ownership. There is currently an agreement or memorandum of understanding between the Council and each of the payment scheme companies. This is not strong enough. Subsidiarity would be a better way forward, a visible change. The reformed Council takes ownership of and ultimate accountability for Payments Schemes Limited which has its own CEO, reporting to the Chairman. In turn Payment Schemes Ltd owns each of the payment scheme companies.

Supporting that visible change would be independent external audit. Separate and fully detailed SOC type audits and reports on Payments Council, Payments Schemes Limited and the payment scheme companies for stakeholders on the Boards, and a SOC 3 type report designed as a general use report demonstrating to users that these organisations have all necessary controls in place, the levels of performance achieved and delivery against plan. These general reports should be openly available on appropriate web sites for public consumption.

With the CEO, the Chairman must bring through the reform of the Council required, and separate the operation of the Council into two halves.

The first half is the strategic part. Its function is to gather the requirements for the industry, to interpret regulatory direction of all types, to own and drive the production of industry data, to create the future vision required, and to allow the connection between vision and current plans to be built. This function must be able to clearly differentiate and declare which areas of the market are competitive and which would benefit from collaboration. This function does not properly exist today and is not a million miles away from the Strategy Board envisaged by the Report. Ultimately, a proper strategy is required, providing the vision which drives every working member of the Council, and which exists as a message communicating the direction this important part of the banking industry is headed in to the public in general.

The second is the schemes part. Payment Schemes Limited is led by its CEO, and the scheme companies, each of which already has its own MD. The scheme companies should have a planning function to direct the known future of the existing schemes, which should be managed in parallel, avoiding competition, overlap and unnecessary cannibalization of existing volumes between schemes. This will continue to be directed by the banks through the steering boards associated with each scheme. It would have been ideal to have undone the separation of scheme from infrastructure at the same time, but for the fact that the main infrastructure provider, VocaLink, is probably too far down the path of operating as a commercial supplier.

A third element is the consultative function, designed primarily to manage and resource the implementation of changes, of projects and procurements.

As today, all three are supported by an administration company (UK Payments Administration Ltd) responsible for providing facilities and support functions.

This is not to say that the Council should be directed and staffed entirely by payments and banking specialists. Indeed, the skill-sets required are accounting, research and strategy skills, leavened by payments and banking knowledge, with some experience of regulation itself as well as the abilty to represent areas of the user market-place.

Agreement of future direction is first achieved at working level in dialogue between the two main halves, to cut out ideas which are by discussion agreed to be too risky, too difficult or involve impractical levels of investment.

It is the Council board function to agree the strategy, and to which both the main halves must report. Its structure and its staffing also need change.

- The voting structure of the Council board needs to be equalized, to reduce the possibility that individual banks, or groups of banks block change unreasonably or in their own interest;
- Council Board representatives should be more senior than they are today and should be senior to the bank representation on the schemes' boards;
- The performance of today's external board members needs to be reviewed so that ineffective directors, who do not properly represent their sponsored areas, are changed.
- Other representation at board level should be considered. In most organizations, the CEO is a board member. Under the current model, both the CEO and the Bank of England are observers of the Council board, which presumably means that they have no voting rights and that they are silent participants, unless called upon. This is less than ideal. Also, taking into account HMG's vested interests both as a hugely significant user of the schemes, a body whose Departments of State have hugely significant reliance upon the robustness and resilience of the schemes and as the instrument of government, it is appropriate, at the very least, at this stage of a regenesis of the Council, that there should be proactive Treasury representation on the Council Board, and Payment Schemes Limited.

The Council's operation should be open. This openness should be evidenced to the public, personal, retail and commercial sectors by making available on the Scheme Company websites relevant documentation including inter-alia;

- Criteria for membership
- Scheme Rules
- Scheme Operational Procedures
- A general report on performance of the system, annual and quarterly.

and all updated on a regular basis should any changes be undertaken with the relevant documentation clearly annotating the changes.

Substantial improvement in the Council's structure and operation is required in order for the Council to meet the criticisms, and to retain its self-regulatory role. Above all, this is a question of leadership, in which robust management of all of the conflicting interests has to be actively managed. It can be argued that the performance of the Council has improved in its relatively short life. But it still has a way to go.

Conclusion

The Payments Council is the forum in which these market issues are discussed and for which solutions are put together, for those that have to provide them to agree upon or not. The obvious thing to do is to make it better at what it does. Grace under pressure is required. And it is the business of the Payments Council to present its changes and reforms to the wider public.

The second option, to create a Payment Strategy Board feels more like the kind of elegant idea that Sir Humphrey might have pushed in front of his minister, to get him off the hook and to create the appearance of solving a problem by asserting greater political control, but in reality merely increasing the probability that future directions will not be agreed.

- There used to be APACS, which was bank-owned and run.
- Now we have a Payments Council, set up to achieve greater external input into the future of electronic payments.
- And now we are supposed to welcome a government-implemented strategy body, leading a Council, which leads the old APACS schemes, for fear that the Council doesn't achieve what the government desires.
- What is the elastoplastic structure required when this one fails? There is surely nowhere else to go beyond nationalizing the industry!

Progress in this area is neither easy, nor simple. Many parties are involved. It is far better to continue to try to improve the infrastructure by all parties, notably those organizations which fund it and depend upon it for the running of their account businesses.

The financial services sector is crucial to the UK economy, and the payments business is fundamental to financial services. It is far harder to win back a leadership position once lost. Regulators typically prevent, a role which is crucial following the financial crisis. But, whilst mistakes have been made, none of the major transgressions in recent years fall at the door of transaction bankers. It would be wrong to enforce risk-averse behaviour on a business area whose worst crime is to have been, arguably, not entirely competent; and whose upside potential is national competitive advantage. It would be better to establish a governance model, which encourages and enables best practice. Reform does that; a new strategy board does not, and indeed risks repeating the mistakes of the past.

You might take the view that there are plenty of real problems in the finance sector which need solving. This one would not be at the top of many peoples' lists.

Annex

The following questions relate to the changes the Government would expect the Payments Council to implement to improve its self-regulatory function. Most of these questions are handled in the paper. And the argument of the paper, that a Payment Strategy board is not an appropriate model means that the questions relating to it are not answered.

- Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?

The following is an attempt to rewrite the remit.

The Payments Council sets direction and takes responsibility for the development of UK electronic payments, with the aim of creating a world-class and open payments infrastructure for £ sterling. This is led by a vision and clear principles, which are well-communicated. It should liaise, as frequently as is required, with HM Treasury and the OFT to present its approach and progress.

1. *Firstly, to ensure the operational efficiency, effectiveness and integrity of the existing payment networks in the UK, and to continue to develop them as both customers and banks require;*
2. *Secondly, to ensure payment systems are open, accountable and transparent. This includes the requirement to envision such common facilities and standards, which may be necessary to improve the safety, security and legal use of the payment networks;*
3. *Thirdly, to set out a vision for the contribution that the payments industry should make to sustaining and growing the UK's position as a major financial centre.*
4. *Fourthly, to lead the future development of new co-operative electronic payment services in the UK;*
5. *Fifthly, to increase the ease with which bank account users can transact with other currencies, countries and economies as international trade and movement increases;*

- How can a clearer separation of the Payments Council's strategy setting and trade body representative functions be best achieved?

  By organizing the Council's activity around the two separate functions, recognising the difference between strategy and tactical planning ;

  - *a substantial strategy function*
  - *and a scheme management company, run and owned by the banks*
  - *by re-organising the voting structure;*
  - *and to increase the likelihood of success, by increasing the quality of the people involved.*

- Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?

  Yes.

- Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council's board can be strengthened further.

  Not really. This paper has no detailed recommendations on the changes required in governance. The Council and the banks have this right, as the banks own the existing networks, and fund their future development, as important parts of their own businesses. And they will be called upon to fund new ones. This paper presents its own ideas, in which a reform of the organizational structure, described in the paper is key.

  1. *The schemes should be run, owned and developed by the Council. They should be run collectively, with their own planning function;*
  2. *The strategic function works at executive level to determine:*
     - *The strategic vision and future requirements. And these must be held at the first level as requirements without predetermined solutions;*
     - *The areas at the time which can be seen as viable for collaboration.*

  The Schemes board has the prime say in how these requirements can be implemented and when, and has the right to refuse them, on the grounds of risk, complexity or unreasonable cost.

  But the Council Board supervises both functions and must work to both create strategy and facilitate plans to agree the tactical plans which lead towards the strategy. Leadership is required, rather than complexities of voting structures.

  And the authority of the board will be seen to be greater if the voting power between bank and external directors is equalized and if some form of majority voting (say 75% as in the US) is required to approve any initiative.

- Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?

  Creating valuable customer input to future plans is essential to success. Again, the method used to gain wide samples of meaningful opinion is a matter for the Council board, and specifically its external directors to implement. But there are plenty of research opinions that can run meaningful surveys of target customer audiences. These need to be run separately from the narrower consultation with interested parties.

- How can Payments Council funding be put on a long term, secure footing?

  In what sense is it insecure today? If the budgets to achieve more are required then they must be justified. It is not appropriate to create an organization which is larger than it needs to be by the establishment of excessive tithes on the banking industry, which will inevitably be translated into higher bank charges, borne mostly by industry. And dipping into the public purse is absolutely to be avoided.

- How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?

  Authority is earned not given. The authority of the Council will only be achieved by successful industry leadership, in other words over time. The organizational, governance and people changes described in this paper would, in the author's opinion, be the most likely way in which this authority might be achieved.

- How can the membership of the Payments Council be broadened most effectively?

  The Report has little to say on how HMT would like to see membership broadened. Any organization which manages a current account should get value from the Council, as a source of information and direction. And it becomes a more attractive organization to the industry's customers by owning and publishing properly researched data on the industry and its different customer segments. But companies and people do not join associations unless there is value in the membership, they won't be compelled.

BRITISH RETAIL CONSORTIUM
for successful and responsible retailing

BRC Response – HM Treasury Consultation Paper:
Setting the strategy for UK payments

The British Retail Consortium (BRC) represents the whole range of retailers including independent shops, department stores and large multiples, selling a wide selection of products through centre of town, out of town, rural and online stores. The retail sector employs around 3 million people (10%+ of the workforce) and retail sales were £303 billion in 2011. The retail sector consists of 284,490 outlets, contributing an estimated over 5% to Gross Domestic Product (GVA).

Current BRC Payments Position

The BRC welcomes the opportunity to respond to the consultation document "Setting the strategy for UK payments".

The BRC has provided answers to specific questions, but we would first like to set out members' overall position and key priorities on payments. It is worth doing so, because any proposed changes to payments policy governance in the UK must demonstrate the ability to address these key concerns. It is not possible to discuss how payments policy should be governed if there is not also a focus on the impact this has on market cost and practice and consumer benefit or detriment.

BRC members' experience has shown that having an integrated payment strategy for all payment methods accepted by retailers would be highly desirable. The proposal to have an integrated payment strategy for the UK payments market that pays due regard to both European and International payment developments should deliver real value and benefit to retailers and consumers. Integration of standards for the end to end acceptance, processing and settlement of all payment types from whatever sales channel they emanate is required to satisfy retailers' requirements.

From a wider perspective, an integrated payments market is urgently needed to support development of a digital single market, in turn helping to complete the internal market, and so help create the growth and jobs so vital to European economic recovery.

Retailers' key requirements are:

1. The cost of handling payments, particularly cards, is too high and should be a fixed cost per transaction independent of card or product type. For a retailer, processing ANY and ALL cards requires the equivalent process and functions, but not cost. There is no justification for the large differences in cost to retailer and consumer. The European High Court has found cross border multi-lateral interchange fees in violation of EC competition law and ruled for their removal. The key challenge for this consultation will be the ability of any new payments governance system in the UK to affect meaningful cost change to the domestic interchange fee structure, based on the strength of the European ruling. An enhanced body, new body or regulator will be judged on their ability to drive beneficial change for the market and consumers.

2. The cost of handling a payment should be known by the retailer at the time the payment is accepted – not after the event as it is today for cards. This is the only part of the supply chain where costs are non-negotiable, lack transparency and accountability. In addition, the Honour All Cards Rule means that retailers have no ability to contest any given price increase.

3. All payment-related costs and products accepted should be fully negotiable by retailers – there is a severe lack of competition and innovation in the cards market. In recent years new cards did enter the market – Switch and Maestro – but were quickly consumed. Any new structure should shift the balance of power, so that policy supports new entrants in the payment arena. This would drive competition for the benefit of consumers.

4. The retailer does not want to influence how a customer pays for their goods as it is the customer that should determine how they want to pay.

Key UK Retail Stats

- In 2011 UK retail sales were over £303 billion.
- The BRC-Bond Pearce Retail Employment Monitor showed that, in quarter two of 2012, retail employment was 0.5% higher than in the same quarter a year earlier, equivalent to 4,074 more jobs.
- 9% of all VAT-registered businesses in the UK are retailers, with the total number currently at 187,390
- More than a third of consumer spending goes through shops
- Consumer spending makes up two-thirds of GDP
- The retail sector generates over 5% of the Gross Domestic Product of the UK

Annex A: The BRC Cost of Payments Collection survey issued in 2012. This covers 59% of total UK retail sales (£178 billion) and highlights the large differences in the costs of cash, debit and credit. Retail does not support any payment method over the other; the key concern is why there should be such a large (and increasing) difference in cost where there is no evident difference in merchant process or associated benefit.

Summary of BRC Response to Key Questions

While answers have been given to all the specific questions raised, retailer's position on the key issues can be summarised as below. The retail sector's key observation and position in relation to Government's proposed options again relates to effect not form of any proposal. If a new Payments Board or regulator is capable of re-dressing the balance of power in financial services policy towards all of the market (not just banks) and consumers, and in turn drives lower market and consumer cost, then the retail sector supports government policy. If no change is the result, then retail is unable to support government policy.

The key observations and views are:

- That a Payments Strategy Board (PSB) must have a mandate to consider and recommend payment strategies for all payment types that generate and provide effective competition and innovation in payments. Included within that mandate must be a directive to ensure all payment types are charged and processed in a cost efficient and cost effective way that enables all elements within any payment charge to be transparent and fully negotiable by retailers and consumers. For clarity, this means banks and card schemes must fall under the governance structure, but decision-making powers are spread more broadly across the market and consumers.

- The PSB must have the power to ensure that such directives and strategies that are developed for change are either implemented through a re-vamped Payments Council or mandated through one of the existing regulatory bodies.

- Without these two additional mandates for the PSB the BRC would not be able to support the introduction of a PSB since this would merely be an extension of a less than satisfactory position as is today.

- That the PSB encompasses and is fully inclusive of all key bodies and users, including retailers, involved in payments. Inclusion should mean being representative of all the different categories of users and their different needs in the payment market today and in the future.

BRC Response to the specific Questions raised in the Consultation Paper

For simplicity the BRC will use the same numbering convention as that used in the original document.
EC will be used as a standard abbreviation for the European Commission.
FCA will be used as a standard abbreviation for Financial Conduct Authority.
OFT will be used as a standard abbreviation for the Office of Fair Trading.

Question 1: ***Do you agree that the creation of a Payments Strategy Board:***

- ***should be the lead option for reform;***
- ***provides the appropriate balance between Government intervention, impact and cost; and***
- ***effectively tackles the issues the Government has set out?***

Subject to our detailed responses to the other questions raised, the straight-forward answer is supportive of the creation of a Payments Strategy Board (PSB). However it is important that more emphasis is added and placed on the following within the mission statement for the proposed PSB:

- Provide an improved and clearer definition of exactly what/who industry users are in order to identify and include (encompass) all acceptors of payments and, in our case, their merchant/retailer representation.

- Provide a clearer definition of the interface with existing regulatory bodies and the ability /mandate to request such organisations to enforce immediate action within their individual regulatory mandates. The PSB must be given an enforceable mandate to instigate immediate change so negating any delaying tactics that may be employed by those delivering the required changes, e.g. instruct the OFT to resolve card payment pricing issues immediately.

- Need to recognise the impact and requirement to change / augment UK regulatory requirements will not solely be influenced by UK requirements given that the EC currently has significant influence on the UK payments market and also the key international card schemes MasterCard and Visa. We also consider that American Express should be included, as well as consideration of emergent payment systems which will impact the European and UK market, i.e. China Union Pay. A key requirement is for the PSB to ensure that UK market innovation is protected for example from arbitrary international card scheme rules that may inhibit grow of alternative payment products that are cost effective and efficient for retailers to implement.

- The undue influence on the UK market of the major international card schemes is driven by their outside interests and quest for profits. This must be considered and reviewed by the PSB in terms of their applicability to the UK market especially given that the card schemes control how and on what terms cards are accepted at retailers' point of sale.

- The role of the largest issuer of payment instruments, the Bank of England, should be better represented within the PSB.

- Creation of a PSB must coincide with a revised brief for the Payments Council particularly as to their future mandated functions, the make up of their representation as a whole and on individual user groups. In addition, the Payments Council should be responsible for acting as the keeper of all payment standards to ensure that there is a consistency of approach and implementation at retailers' point of sale wherever that may occur be that in a face-to-face or an electronic environment.

The following is provided to support our comments:

- During recent years representations made by payment acceptors (of which retailers are major players) at User Forums in respect of protection against a cartel approach have to a greater extent been ignored which has resulted in falling attendance and participation at those events.

- Historically the Payments Council has given minimal credence to the comments or proposals made by retailers, merchants and payment acceptors to proposed changes within documents or consultations issued. Even within this consultation paper as presented retailers, merchants and payment acceptors are not mentioned.

- The market value attributed to the establishment of UK Cards Association card standards needs to be maintained as this has enabled retailers to ensure that their suppliers adhere to common pre-defined industry standards.

- Given that the UK banks have, in recent years, allowed the card schemes to become solely international for profit companies the impact on UK retailers has been the creation of a much more complex business model. This has given rise to the unacceptable position where retailers no longer know the payment fee for a handling a card at the time the retailer processes the card payment. Retailers have no room to negotiate these costs.

- The weakness of the current structure is that too much is considered and dealt with in isolation of the impact on other payment methods. It appears that the Payments Council has created a silo mentality rather than managing an integrated payments strategy. For retailers, management of an integrated strategy is a key requirement together with delivering one that is cost effective whilst maintaining or becoming more efficient at point of sale.

- Retailers need to be represented on PSB as a key group of payment acceptors and processors.

- All payment types accepted in the UK should be included within the remit of the PSB to enable any movement initiated by consumers or banks to be closely monitored and the impact assessed on other payment handling or acceptance trends in the UK market. The changes in payment mix should be reviewed and their future impact assessed within the remit of the PSB. *(The BRC annual Cost of Collection survey has been used specifically by our members to assist in their payment strategies. A copy of the most recent survey using 2011 data is included as Annex 1 to this response.)*

From a BRC perspective an enhanced PSB role and responsibilities to that proposed in the consultation paper together with a re-vamped Payments Council should deliver a significantly improved payments market for our members and would be fully supported if it produces real reform.

Question 2: The following questions relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds with Option 2.

a Do you agree that the current remit and objectives of the Payments Council are broadly appropriate? If not, how should they be enhanced?

No. It is fundamentally incompatible to have a membership based organisation, with incumbent member interests, to set the strategy for UK payments. The Council states its remit as, “the organisation that sets the strategy for UK payments. It was set up by the payments industry in 2007 to ensure that UK payment systems and services meet the need of payment service providers, users and the wider economy”. This has led to failure in policy making. The best example is cheque replacement. Moving cheques out of circulation has clear benefits for the banking system, as processors of financial transactions. Retailers have no payments agenda, we sell products and services and merely wish for fair cost and a secure system. Consumers lead how they pay. While one agenda was being aggressively promoted, the result was that this did not in any way reflect the true interests of either retailers or, more importantly, consumers. The Treasury Select Committee and other consumer lobby groups were quick to understand and act on this, resulting in a chaotic and probably expensive withdrawal of the policy. The Payments Council are understandably acting in the interests of their members, however this means they cannot genuinely represent interests of consumers or retailers, as demonstrated by the cheque replacement experience.

The Payments Council should cover all payment types not just the ‘owned’ products as it does today and include all owners in its infrastructure. Cash is a prime example where there is minimal membership where the keepers of the nations’ purse, the Bank of England, must be more active not just in a passive observation role. The BRC believes the Payments Council’s members are insufficiently joined up in their approach and do not adequately reflect the payments market as it is today, e.g. no mention of the Cards Association in the Glossary.

b How can a clearer separation of the Payments Council’s strategy setting and trade body representative functions be best achieved?

By making the Payments Council the keeper of the UK payment standards and implementation / controller of the PSB strategy it will also be in a position to act as the co-coordinator to the trade bodies.

c Do you agree that the Payments Council should commit to publishing annual progress reports against its objectives, supported by regular, independent performance reviews?

The BRC agrees that the regular dissemination of information is very important to its members. With the establishment of the PSB care will be needed to ensure that the Payments Council and the PSB do not duplicate or more importantly exclude, intentionally or otherwise, key information during its dissemination. The BRC considers that, as a minimum, the Payments Council should be committing to annual progress reports that are available free of charge to the market.

d Do you agree that any two independent directors should have a right of veto over board decisions? The Government invites views on how the Payments Council’s board can be strengthened further.

The Payments Council in whatever format it takes in the future should be funded, and therefore controlled directly or indirectly, through the FCA. In the future the representative of the PSB on the Payments Council should be the only organisation that has the right of veto over board decisions.

e Do you agree that the existing user forums should be given enhanced functions and autonomy by being upgraded to independent User Councils?

Current user forums do not work effectively. If they continue to exist there is the need for them to be able to exercise power and have a structure to put forward their views and ideas directly into the PSB. What is required is that recommendations from these user groups should either be accepted or rejected with the appropriate rationale for decisions made being provided back to the initiating group rather than the position today of ‘we will consider further’ and the outcome is being to mainly ignore the recommendation. It is this approach that frustrates payment acceptors today as it causes delays and procrastination. In the future it is recommended that the User Forums should be upgraded to Independent User Councils.

f How can Payments Council funding be put on a long term, secure footing?

Funding should be organised and raised by the FCA so ensuring the independence of the structures of the PSB but also the Payments Council. This funding model should ensure that all

relevant parties are represented, not just those within a narrow group, the latter being the representation today on the Payments Council.
The actual methodology used for funding needs to be simple to determine, equitable and cost effective to raise.

g How should a reconstituted Payments Council be given the means to enforce decisions more effectively in a self-regulatory environment?

The BRC considers that the Payments Council will not require an enforcer mandate since this should be within the remit of the PSB.

h How can the membership of the Payments Council be broadened most effectively?

Replacement of the funding methodology used today with one that is universal and obtained from the FCA will ensure that the Payments Council by default broadens its representation and mandate. This change will ensure that the Payments Council has no need to rely directly on its current members for its funding and expertise.

Question 3

a Do you agree with the proposed remit for a new Payments Strategy Board?

No, we consider that the remit should be broader. Namely the proposed remit is not specific enough in terms of its role in resolving / directing issues arising from payment acceptors, in our case retailers. An example of this is the current and on-going debate on transaction pricing and the failure of the payments bodies to address the key issues over many years. Our experience has been that excuses are offered without adequate justification, which is perhaps not surprising in view of the current make up and constitution of the current Payment Council since they are the main beneficiaries of a no change policy. The statement 5.24 “benefit of all users” will only have credibility if future structure and independence is paramount and there is a mandate to enforce change through current channels.

The statement “Promote Access” also needs to be expanded since the market as such is more than “smaller banks” and the remit therefore needs to take into account all the new developments that are either planned or that may be introduced over the coming years. e.g. the option for retailers to self-acquire payment transactions with direct access to card schemes without the need for use of separate acquirers or payment processors; the opportunity for greater direct use of faster payments for handling transactions at point of sale. This aspect of the remit must be future proofed.

b Do you agree that the Payments Strategy Board should make recommendations to the payments industry, rather than requiring action? If you consider mandated action to be appropriate, please set out how such a method could work most effectively.

The PSB should be given the power to make “strong recommendations” (mandate) with the objective of those either being accepted and followed through within the mandated timescales or robustly refuted by the organisations to whom the instructions are addressed with a system in place for subsequent arbitration where rejected.

“No action” – “No response” – “No comment” - Should no longer be acceptable responses.

It should be noted that currently card schemes regularly mandate changes to which retailers’ have to react, at their own cost.

c ***Do you agree that the Payments Strategy Board should include senior industry representatives, non industry representatives and independents? What do you consider to be the right composition of the Board?***

The composition of the Board should represent all the key parties involved in payments. The proposed remit for the FCA to establish, fund and appoint must not be seen or used as a means of creating a PSB of a single mind commercially or politically. This area of concern has been prompted by the fact that key elements of the payments market most importantly payment acceptance, merchants, retailers are not mentioned within any of the documentation.

d ***Should the Payments Strategy Board have a formal information gathering power? If yes, what information should be covered by such a power, and what should an appropriate enforcement mechanism be?***

Number and value of transactions would be a good starting point. A clear definition as to what represents a transaction is required. Past estimates have been shown to be historically unreliable. If a simple definition was established it would not be too burdensome for the market to respond. The availability of data from BRC members continues to be demonstrated in the annual cost of collection survey. For our members the quote "Can't measure - can't manage" sums up as to why accurate information is so important to them.

e ***Do you agree that the Payments Strategy Board should be funded by an FCA levy on the payments industry?***

Yes - but the use of the levy should extend all the way down the food chain so that no party can unduly influence any given outcome. Who will audit the auditors? The fear of retailers is that the FCA could pay too much attention to short-term political consideration without giving long term continuity of purpose and direction that is so important to the development of the future payments market.

f ***Should the FCA have any further controls over the Payments Strategy Board?***

It would appear that the role of the FCA as stated and envisaged is all encompassing and therefore satisfactory.

BRITISH RETAIL CONSORTIUM
for successful and responsible retailing

Cost of Payment Collection Survey 2011

BASE DATA FOR SURVEY

The British Retail Consortium (BRC) announces the results and analysis of its Retail Cost of Payment Collection Survey for the 2011 calendar year.

The response level to the survey covers 58.8% of total UK retail sales (£303 billion) with a combined turnover of over £178 billion.

The respondents to the survey incurred collection costs totaling circa £729 million.

KEY RESULTS

IMPORTANCE OF CASH

Cash is still dominant and accounts for 58.3% of transactions (2010: 55.2%) – customer transactions using cash were up by 5.7% during 2011.

The value of cash still accounts for 32.03% of total turnover compared with 32.8% last year.

YEAR ON YEAR CHANGES IN PAYMENT METHODS USED BY CONSUMERS

During the period 2010 to 2011 as a percentage of transactions handled by retailers there have been changes in the main payment methods used by consumers – these are:

- Cash up 5.7%
- Cards down 10.53%

AVERAGE TRANSACTION VALUE

During 2011 the overall average transaction value has declined from £21.76 to £19.01. The overall number of transactions (closely related to store visits) has increased by over 17.7% now amounting to circa £9.4 billion so reflecting a continued public interest in the high street and online but with a greatly reduced spending power per outing.

COLLECTION COSTS ARE STILL TOO HIGH FOR CARD TRANSACTIONS

Collection costs for 2011 are still out of line with the costs that retailers incur for payment transactions within each category. The cost comparison analysis for the main payment methods are as follows:-

- Cash accounts for **58.27%** of transactions - yet only account for **11.12%** of Costs
- Debit cards account for **29.1%** of transactions - and account for **36%** of Costs
- Credit and charge cards account for only **10.98%** of transactions - but account for a staggering **51.14%** of costs

RISING CARD MERCHANT SERVICE COSTS (MSCS)

- Since 2007 the card merchant service costs for debit cards have risen by over 27% and now account for 0.31% of debit card turnover
- The average MSC on credit and charge cards has risen to 0.95% of turnover compared to 0.91% in 2010.
- Merchant Service Costs still account for circa 97% of the total cost incurred in the acceptance of any type of card by retailers.

It is the interchange cost element within the MSC that has, in the recent MasterCard decision by the European Commission backed by the European Court, been deemed to be anti-competitve and illegal. The UK market currently awaits similar action and ruling by the OFT as interchange equates to more than 90% of the total card MSC retailers pay.

KEY FINDINGS BY PAYMENT METHOD

CASH

- Cash has not lost its appeal – it is still dominant – and now accounts for circa **58.27%** of retail transactions.
    - £32.03 in every £100 spent at retail outlets is by cash
    - Each cash transaction (whatever the value) now costs the retailer an average of 1.5 pence per transaction to handle
    - Average cash transaction value has decreased to £10.45 (2010: £12.93)
- Cash remains the most cost effective method for retailers to accept customer payment

DEBIT CARDS

- Debit cards continue to account for 45.65 % of retail sales by value
    - Each debit card transaction (whatever the value) costs the retailer an average of 9.6 pence per transaction to handle
    - Average debit card transaction value is now £29.83 (2010: £29.58)

CREDIT AND CHARGE CARDS

- Credit and charge cards now account for 21.47% of retail sales value
- The average credit and charge card transaction costs the retailer over 36 pence
- Average credit and charge card transaction value is reducing and is now £37.16 (2010: £41.63)

CHEQUES

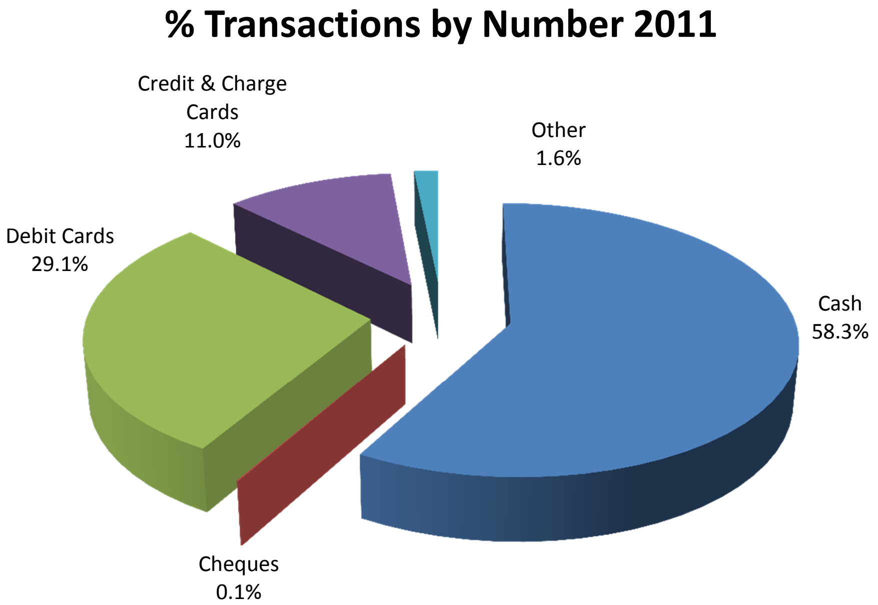
- In this survey the decline in the use of cheques continues with them now accounting for only 0.19% of retail sales turnover
- This category of payment in future surveys will be amalgamated with other non card payments. New payment market developments currently classified as other will undoubtedly increase and be separately identified in future years.

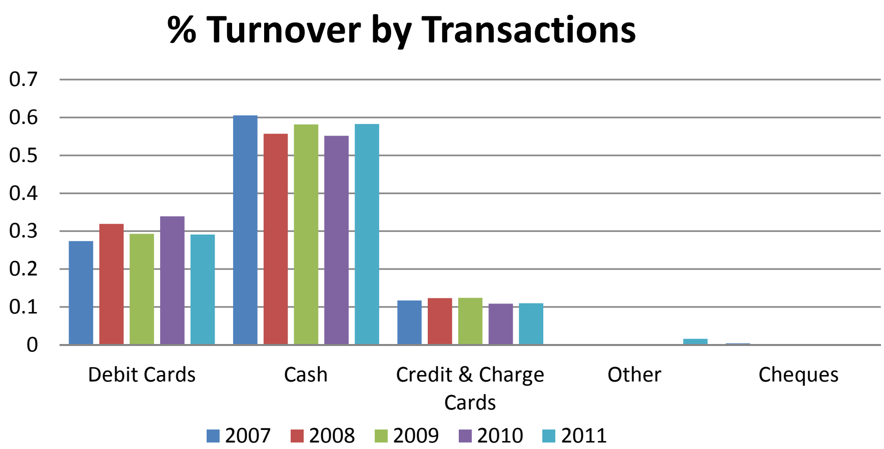
ADDITIONAL INFORMATION OBTAINED

- Survey research has shown that the average time taken to process a cash transaction at point of sale is 27 seconds (2010: 27.2 seconds) compared to 36 seconds (2010: 39 seconds) for handling a card payment.
- Overall the survey showed that 5.69% of the participants' turnover was completed by their customers shopping online.
- Circa 30% of manned tills now have the capability to accept contactless cards. A number of retailers indicated that during the next 12 months they did have plans to roll out and/or consider implementing Near Field Communications (NFC) such as contactless or mobile payments at point of sale.

COST OF PAYMENT COLLECTION SURVEY RESULTS 2011 DATA

TOTAL SALES TURNOVER BY TRANSACTION NUMBER

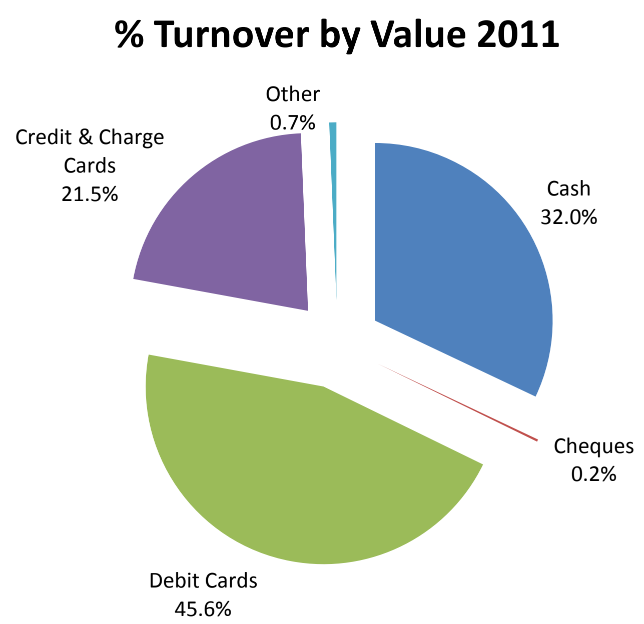


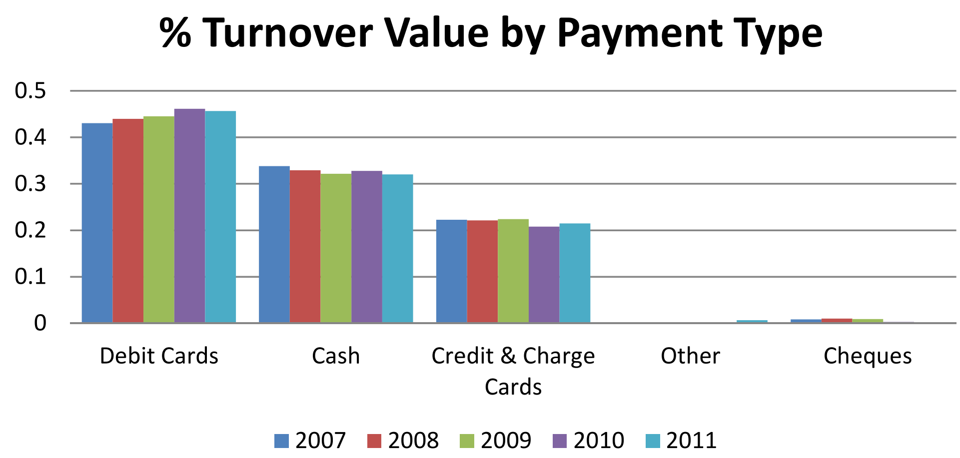


% TURNOVER BY NUMBER OF TRANSACTIONS

	2007	2008	2009	2010	2011
Debit Cards	27.36%	31.92%	29.29%	33.93%	29.09%
Cash	60.56%	55.71%	58.18%	55.15%	58.27%
Credit & Charge Cards	11.69%	12.31%	12.39%	10.86%	10.98%
Cheques	0.38%	0.07%	0.13%	0.06%	0.09%
Other					1.57%
Total	6,680m	6,403m	7,315m	7,957m	9,368m

TOTAL SALES TURNOVER BY VALUE

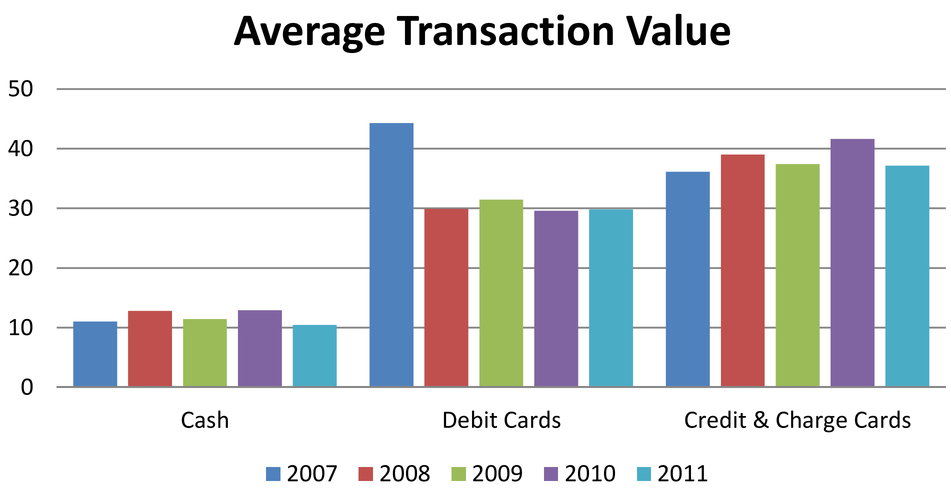




% TURNOVER BY VALUE

	2007	2008	2009	2010	2011
Debit Cards	43.04%	43.97%	44.52%	46.13%	45.65%
Cash	33.81%	32.90%	32.15%	32.78%	32.03%
Credit & Charge Cards	22.29%	22.12%	22.41%	20.78%	21.47%
Cheques	0.85%	1.01%	0.92%	0.31%	0.20%
Other					0.65%
Total	£132 billion	£139 billion	£151 billion	£173 billion	£178 billion

AVERAGE TRANSACTION VALUES

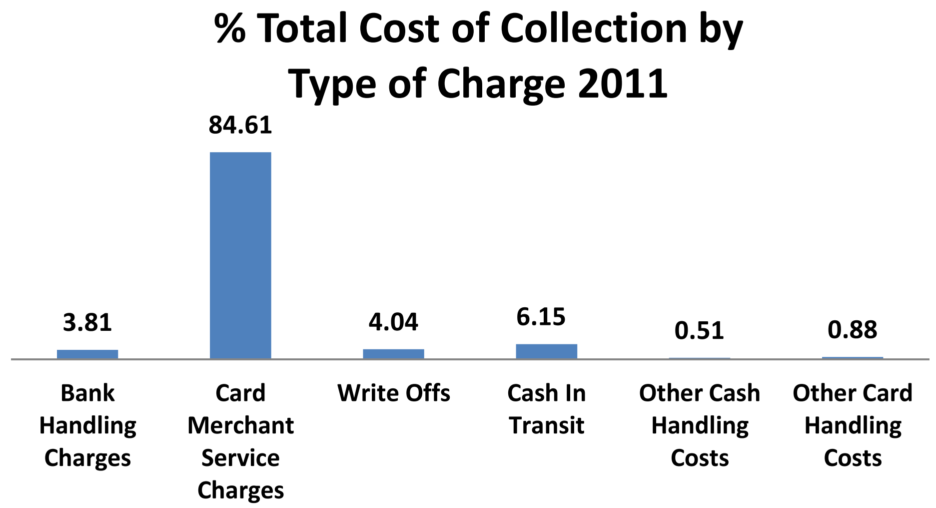


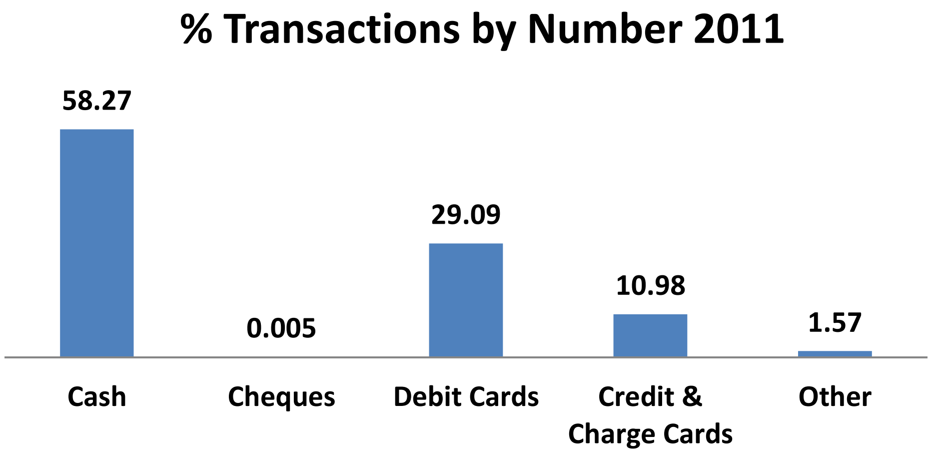
AVERAGE TRANSACTION VALUES

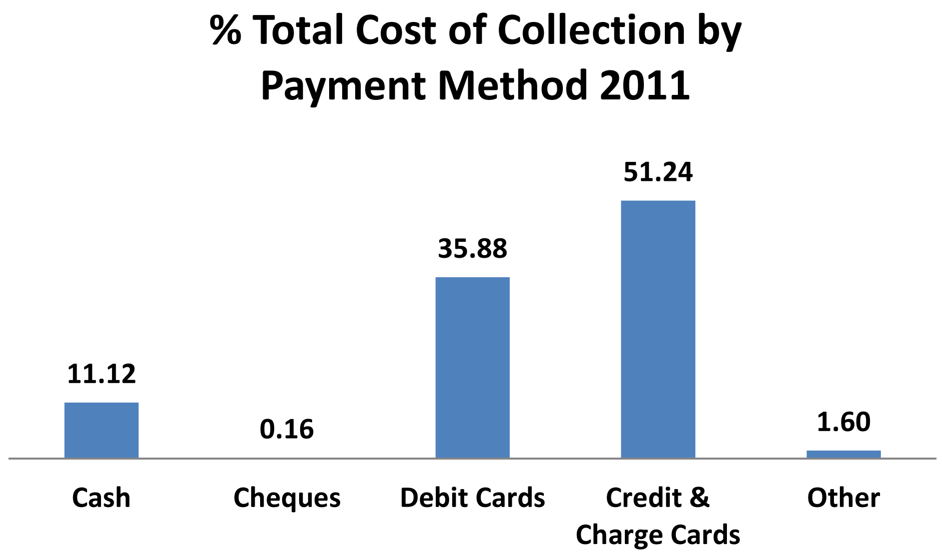
	2007	2008	2009	2010	2011
Debit Cards	£31.05	£29.92	£31.45	£29.58	£29.83
Cash	£11.02	£12.82	£11.43	£12.93	£10.45
Credit & Charge Cards	£36.14	£39.03	£37.42	£41.63	£37.16
Cheques	£44.31	£334.27	£143.58	£111.82	£44.23
Other					£7.89
Overall	£19.74	£21.72	£20.69	£21.76	£19.01

TOTAL COST OF PAYMENT COLLECTION

- Total amount spent by retailers in the survey on payment collection is £729m

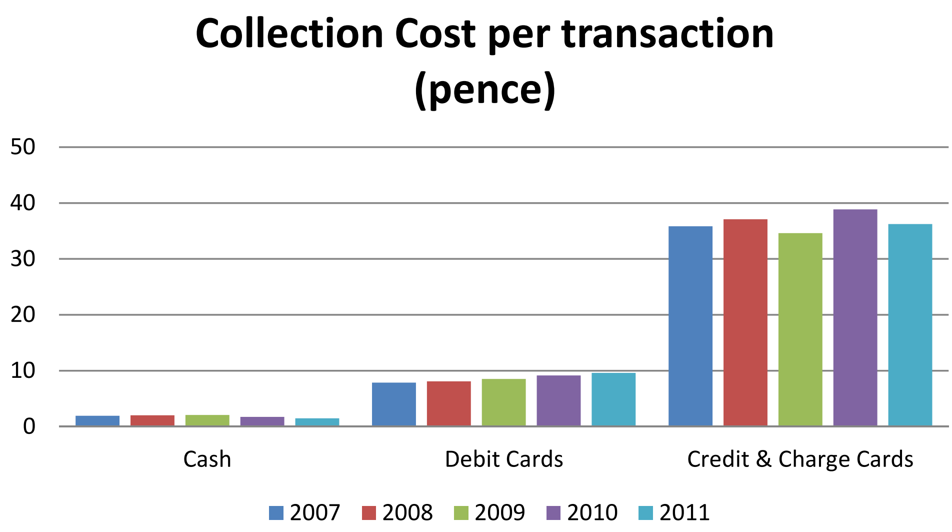






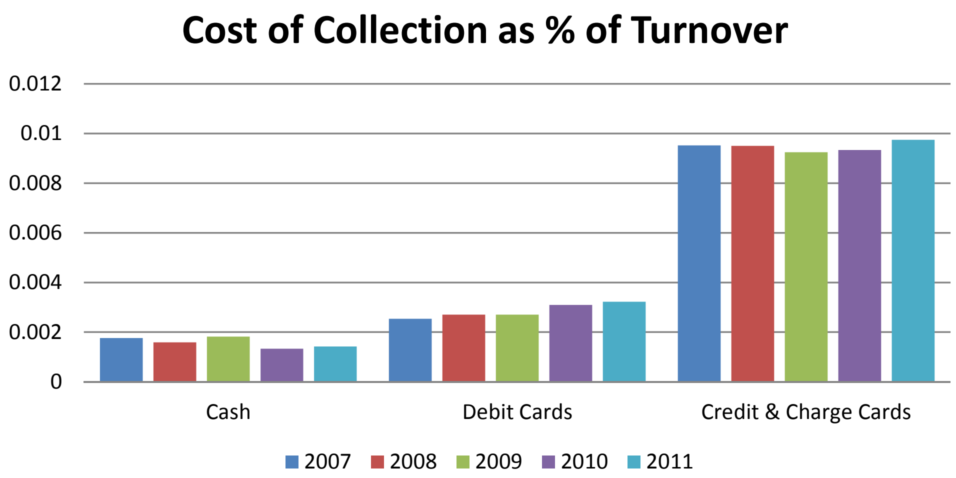
The biggest single cost, 84.6% of total collection costs for retailers accepting cards, continues to be the Merchant Service Charge (MSC) within that cost the fixed element, interchange, accounts for over 90%.

TRANSACTION COLLECTION COSTS



TOTAL COST OF COLLECTION PER TRANSACTION (PENCE)

	2007	2008	2009	2010	2011
Cash	1.9	2.0	2.1	1.7	1.5
Debit Cards	7.9	8.1	8.5	9.2	9.6
Credit & Charge Cards	35.8	37.1	34.6	38.9	36.2
Cheques	53.0	117.5	38.6	14.8	14.6
Other					7.9
Average for all payment types	7.7	8.4	8.0	8.3	7.8



TOTAL COST OF COLLECTION PER TRANSACTION (% OF VALUE)

	2007	2008	2009	2010	2011
Cash	0.18%	0.16%	0.18%	0.13%	0.14%
Debit Cards	0.25%	0.27%	0.27%	0.31%	0.32%
Credit & Charge Cards	0.95%	0.95%	0.92%	0.93%	0.97%
Cheques	1.20%	0.35%	0.27%	0.13%	0.33%
Other					1.01%
Average for all payment types	0.39%	0.39%	0.39%	0.38%	0.41%

COST OF PAYMENT COLLECTION SURVEY 2011

PURPOSE AND METHODOLOGY

PURPOSE

The results from the British Retail Consortium (BRC) Cost of Payment Collection Survey conducted in respect of the 2011 calendar year was completed by retailers that represents 58.8% of UK retail sales annual turnover which in 2011 was £303 billion.

This survey has been compiled on a consistent basis since 1999. It is recognised as providing an independent and definitive view of not only the cost of collection but also the important trends within the UK payments market. It provides the only representative and reliable measure for the cost of payment collection.

The credibility of the findings and results have always proven to be robust despite the past conflicting claims regarding the findings, made more often by the financial industry and card schemes.

The survey collects data that refers to the costs associated with taking payment from customers both at point of sale and through the internet and mail order. Within the different payment types the costs include items such as card acquiring fees (inclusive of the interchange and card scheme fees), fraud, bad debt, losses, cash in transit and related administration costs in all categories. These costs amount to more than £729 million in the responses received and therefore account for one of the key cost elements in retailing operations today.

The primary purpose of the survey is to:

- Provide participating BRC members with a range of figures to allow them to benchmark and improve their own cost structure and components
- Compare the results with previous surveys covering the period 2007 to 2011 in order to analyse how the mix of payment methods and the collection costs have changed
- Keep the BRC informed of payment market trends within its membership to enable the BRC to speak in a knowledgeable way on all payment and related issues
- Position and present the key data in a consolidated format in order for the BRC to communicate selected data to the regulatory authorities within the UK and Europe
- Provide provable data in support of BRC's continuing representation of its members' interests in the ongoing UK and European cases fighting for significant reductions specifically in MasterCard and Visa interchange fees for all card types and any specific card scheme related additional charges.

METHODOLOGY

The BRC circulated a questionnaire to all BRC members including its associated trade associations. Responses were received from members who account for an annual sales turnover in excess of £178 billion, which is circa 58% of total UK retail sales. Most of these retails sales arose from more than 18,800 shops of all types in addition to 5.7% of those total sales having been made via the internet or mail order channels.

The survey covered the following cost items:

Bank Handling Charges	Service charges, night safe costs, etc.
Cash In Transit	Costs incurred in using a Cash-In-Transit service provider to collect cash / cheques and distribute them to the bank and deliver coin (change) to the retailer.
Other Cash Handling Charges	Third party handling costs for prime count, provision of coin.
Card Merchant Service Charges	Card merchant service charges including acquirer processing fees, interchange and card scheme fees.
Write Offs (Losses)	All write-offs including losses arising through till and banking discrepancies, chargebacks, unpaid cheques, bad debt and fraud.
Other Card Handling Costs	For example to include some or all of the following - depreciation of PIN pads and any card specific hardware, maintenance of PIN pads and server costs, specific additional call authorisation costs, terminal rental, storage and filming of signature receipts.

Research has shown that the staff costs involved in handling payments is marginal in terms of the total costs incurred and evenly divided across all payment methods therefore this cost has been excluded from all categories. Responses received have shown that the average time taken to process a cash transaction at point of sale is 27 seconds compared to 36 seconds for a card payment.

Confidentiality of individual retailer submissions has been assured by the method of data collection.

FURTHER INFORMATION

For furher information on the BRC Cost of Payment Collection Survey 2011, please contact:

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HM TREASURY CONSULTATION: SETTING THE STRATEGY FOR UK PAYMENTS RESPONSE BY THE BUILDING SOCIETIES ASSOCIATION

Introduction

The Building Societies Association (BSA) represents mutual lenders and deposit takers in the UK including all 47 UK building societies. Mutual lenders and deposit takers have total assets of over £375 billion and, together with their subsidiaries, hold residential mortgages of £245 billion, 20% of the total outstanding in the UK. They hold more than £250 billion of retail deposits, accounting for 22% of all such deposits in the UK. Mutual deposit takers account for 31% of cash ISA balances. They employ approximately 50,000 full and part-time staff and operate through approximately 2,000 branches.

The BSA welcomes the opportunity to respond to HM Treasury's consultation.

Question 1

Do you agree that the creation of a Payments Strategy Board:

- ***Should be the lead option for reform;***
- ***Provides the appropriate balance between Government intervention, impact and cost; and***
- ***Effectively tackles the issues the Government has set out?***

The Association agrees with the Government's aims as set out in 4.1 of the consultation paper. Having considered the proposed options for changes to the regulatory regime we believe that the most appropriate way to achieve the Government's aims would be a combination of Option 1 (Reform of the Payments Council) and Option 2 (the creation of the Payments Strategy Board). We do not support Option 3 for the reasons set out in 5.48 of the consultation document.

While the creation of the Payments Strategy Board is a necessary step, we believe that the Payments Council should be given adequate opportunity to complete its internal reforms first. Once these internal reforms have been made, it should be clearer what roles and responsibilities both the enhanced Payments Council and the Payments Strategy Board should have. Only after the Payments Council reforms have been implemented and taken into consideration can we be confident that the creation of the Payments Strategy Board would provide an appropriate balance between Government intervention, impact and cost.

Ideally, the Payments Strategy Board would have a narrow remit and focus purely on setting and benchmarking the industry against a small number of key strategic objectives. The enhanced Payments Council would retain all other existing roles and responsibilities, but one of its primary functions would be to seek to achieve the Payments Strategy Board's key strategic objectives.

With regard to the reforming the Payments Council, it should be noted that the majority of our members are not clearing banks/building societies and are not members of the Payments Council. Most building societies rely on agency arrangements with clearing banks for all of their payments related activities. Some of our members have complained that their interests and concerns are not given adequate consideration by the Payments Council or its members and that this can lead to difficulties when seeking to implement industry-wide initiatives. This could be overcome with improved communication between the clearing banks and building societies via better representation at the Payments Council.

We understand that the Payments Council is looking into how best to achieve this and we hope that this is one of the outcomes from its internal reforms.

Given that we believe the best way forward would be a combination of Options 1 and 2, it would not be appropriate for us to answer each of the individual sub-questions under questions 2 and 3. Instead, we have set out or general thoughts on the Government's proposals and highlighted our specific concerns where relevant.

Question 2

The following questions relate to the changes the Government would expect the Payments Council to implement under Option 1. Some of the changes will also be considered if the Government proceeds under Option 2. **[The full set of questions is set out in Annex A of the consultation document.]**

We agree that the current remit and objectives of the Payments Council are broadly appropriate; however, the Payments Strategy Board should have ultimate responsibility for setting payment strategy.

The Payments Council needs to do more to reach out to smaller banks and building societies to ensure that their voices are heard early on in the planning of any new industry-wide initiatives. In the past, members have complained that discussions on the practical aspects of implementing initiatives, such as the introduction of Faster Payments, are slow to filter down to them. As a result, the clearing banks present a 'solution' to their agency clients on a 'take it or leave it' basis very late in the day with very little time for a firm to implement systems changes before an agreed deadline. One of the barriers to becoming full members of the Payments Council is cost. We understand that the Payments Council is looking into options for improving small member representation and we support its efforts in this area. It is important that discussions regarding the implementation of industry-wide initiatives go wider than just the major clearing banks.

We are broadly in favour of the other proposed reforms to the Payments Council.

Question 3

[The full set of questions is set out in Annex A of the consultation document.]

We agree with the proposed remit of the Payments Strategy Board as set out in 5.24 of the consultation document. It should be limited to making recommendations rather than mandating action. These recommendations should be made following prior consultation with the industry via the Payments Council to ensure that they realistic and achievable. It is vital that the recommendations are subject to vigorous cost benefit analysis. The Payments Council has the relevant expertise and resources and would be the most appropriate organisation to ensure that the Payment Strategy Board's recommendations and strategic objectives are met. However, the Payments Council must reform to ensure that smaller firms which rely on agency agreements, such as the majority of building societies, are more involved at an early stage when planning and implementing industry-wide initiatives.

We are generally in favour of the proposals relating to the Payments Strategy Board including its composition and funding. However, before any final decision is made to proceed with the creation of the Payments Strategy Board, we recommend that the Payments Council is permitted to complete its internal reforms. These reforms should be taken into account when deciding the final structure of the Payments Strategy Board and how it will co-operate with the enhanced Payments Council. Further consultation on the introduction of the Payments Strategy Board following the reform of the Payments Council would be welcome.

10 October 2012