

Responses to Consultation Paper PSR CP14/1 – A new regulatory framework for payment systems in the UK

Respondents - R to Y

Respondent (<i>non-confidential responses</i>)
Raphaels Bank
RBS
Ripple Labs
Santander UK
Secure Trust Bank PLC
SWIFT
TechUK
Tesco Bank
The Investment Association
TISA
Transpact.com
TSB Bank PLC
UK Cards Association
Virgin Money
Visa Europe
VocaLink
Which
Yorkshire Building Society
YourCash Europe

RAPHAELS BANK

RAPHAELS BANK

Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper and Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

We broadly support your approach but we are concerned that regulation needs to be joined up between yourselves, the PRA, FCA, CMA and BoE. We have heard and read that this will be the case, however, we have seen major disruption through withdrawal of banking support in the market for payments providers in the past two years which appears to be continuing without any apparent regulatory intervention.

You have rightly identified access to payment systems as an important area for your involvement, however, if indirect access is to work, there has to be a range of sponsoring banks providing such services. This market is limited and apparently contracting, exacerbated by the closure and non-availability of bank accounts from clearing banks to the sector.

Some sponsoring banks have made significant moves to close bank accounts on policy grounds to UK payments providers and this is continuing today partly, we believe, in response to increased regulation.

Unless there is a significant shift in the regulatory approach to this issue, then competition and innovation will be diminished in UK payments.

The proposed powers and positioning of the PSR looks like a positive step to us, of course implementation and application of the principles laid out will be key to the impact that you have.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper and Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

We agree with your approach as opposed to the alternatives, but would like to understand the steps you intend to take to ensure effectiveness of the Forum.

We support your approach in administering the Forum, but would like to understand more what will be your approach if it takes decisions you don't agree with or the industry fails to adopt or implements too slowly.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum?

In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

Broad representation is essential and it must be possible for representatives to own and control the agenda.

We believe the agenda should be based on strategy and be holistic. There needs to be input into the way payment systems integrate with each other and the services they provide, as well as identification and solution-finding on related issues such as sponsorship and settlement.

We believe the Forum will need to have around 20 members to incorporate all the necessary representation which should definitely include an independent chair, the regulated payment systems, end user representatives for consumers, SMEs and major corporates as well as the smaller banks / building societies, EMI, PI and emerging payments provider sectors. Some form of futurist to look across emerging channels would also be helpful.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

As we state elsewhere in this response, the issues around the UK payments systems are made up of a complex jigsaw of issues on which, we believe, no one is taking a holistic view.

This would seem a good agenda for the Forum as opposed to tactical and short term issues driven by other agendas.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

We have had some difficulty in accessing a bank offering sponsorship for Euro payments (particularly Euro denominated direct debits and credits) originated in the UK which has limited our ability to provide payments services in Europe on a cross border basis, forcing us to (attempt to) open accounts elsewhere in Europe rather than in the UK as we would wish. We believe this should form part of your considerations.

It appears that the whole UK domestic payments structure was built by the big banks and operated largely by them and their nominees for their own benefit. We believe the long term future for payments should not be based on historical systems but more on current, emerging and future payment methods.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you

disagree with our proposed approach, please give your reasons.

We support this approach and will be interested to see what you believe "good" looks like in this respect and what will be made public in the disclosures and your responses.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes to the first question; no to the second.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

Whilst we do not object to this approach, or think that it is without merit, the key is in the behaviour of individuals and the instructions they are working under from their employers. For example, your rule could be followed, but representatives from one big bank on multiple bodies could still coordinate their activity or work to their bank's policy.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

Yes, but we believe you should be vigilant in looking out for behaviour arising from possible conflicts.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes to the first question; no to the second.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Yes, minutes will need to be carefully reviewed and interpreted in detail by the PSR.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you

provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes to the first question; no to the second.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

Yes.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper and Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

We would like to make a few generic points on access.

We support many partners in payments, including over 20 clients running 170, mostly prepaid, card programmes. We have had many discussions with various parties around integrating card payment functionality with domestic banking infrastructure and we are working with three partners in delivering current account type products tapping into Faster Payments and direct debits but based on a core prepaid platform accessing domestic clearing via middleware through an agency banking relationship.

Many of the parties we work with are not regulated but are nevertheless investing in payment services and payments technology. Many of them are doing this specifically with their own products and services in mind rather than as service providers to third parties. This kind of company, wishing to bring payments products and services to market, is not of a scale to consider gaining separate direct access to multiple systems and possibly associated regulatory status, they look to us and to others to sponsor them.

Referring back to our opening points in question 1, we consider that the market for sponsoring services is inadequate and needs a significant overhaul. Under your intended market review in combination with the other steps you are taking, we believe that meaningful results may take too long to deliver.

There is a fundamental problem with the current sponsorship model, in that:

- Sponsor banks are perceived / perceive themselves as responsible for the AML / Terrorist Funding (particularly these days, the latter) of the financial institutions that use their services, which threatens their business through local regulatory action around the world (and particularly in the USA);
- Most sponsor Banks do not see sponsorship activity as core to their business model and therefore will put investment in it as a lower priority;
- In the past bigger banks have not seen the level of competition arising from sponsorship activity as impacting on their business, but as the payments world

diversifies and an individual consumer's requirements become increasingly disassociated from a branch banking environment, this is likely to change, again this is likely to lead to sponsor banks de-prioritising this line of business which is helping to increase competition.

As such we do not believe that improving direct access and making sponsoring banks more accountable will provide a long term solution, a more radical approach is needed to encourage or promote an alternative solution to access which works for smaller players but does not rely on the incumbent sponsors. We think that addressing this problem in a pro-active way should be a core goal of the PSR and that the Strategy Forum should be given this as a first task. Raphaels Bank would welcome the opportunity to work with the PSR on this agenda, through representation on the Forum or otherwise.

The innovative / smaller operator sector of the payments industry is reasonably well served in terms of access to capital (it often doesn't need overdrafts or bank loans) but is currently underserved in proactive and helpful access to payments through suitable sponsors and availability of bank accounts. As such it needs a new banking model.

Without appropriate sponsored access to payment solutions, we believe that the innovative end of the payments market will continue to get squeezed out.

As such, the Access Rule has value and may prove to be worthwhile, but it is part of a bigger jigsaw which is not currently being contemplated by a single entity able to piece together the bigger picture, and hence runs the risk of being ineffective.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes – we would be interested to learn if there will be a fines or penalties regime for rule-breaking.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes, however the way in which operators and their owners behave will be the key.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Yes to the first question. No to the second. We are concerned that sponsors will continue to exit / restrict activity in the market and use costs as a justification.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

Of course the fullest possible set of information will be helpful. However, as outlined earlier, we are concerned that increased regulation in this area without the provision of an alternative to the current few active sponsor banks, will increase the exit / restriction of activity of sponsor banks in this market, including the withdrawal of banking facilities to financial institutions. The PSR, PRA, CMA, and FCA need to have a clear idea of what "good" looks like in the sponsor market and to understand how they are going to steer proactively the sponsor banks in this direction and / or support the rapid development of an alternative.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes, we believe you should take action to ensure this happens rather than leave it to industry to implement.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes, broadly, however the key will be what is in the code and the extent to which it is enforced and the way in which it operates in practice.

The biggest issue we have seen in the past few years, which continues actively today, is the withdrawal of banking facilities to FIs by high street clearing banks regardless of the actual activity of the FI concerned. Unless the code addresses this fundamental point, it will improve service provision around the margins without addressing the root cause.

We are also concerned that the code will end up reflecting sponsor banks' behaviour towards the high street challenger banks, such as Metro and Virgin, which in reality are not the issue when it comes to innovation in the payments arena.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes, although the key aspect here is that this part of the jigsaw supports commercial viability of the whole. Technical access without sponsorship is of little value to many.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

Yes to the first question. No to the second. A holistic review of the actual costs and benefits of the whole package would be an interesting exercise in April 2016.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

Interchange has received a lot of attention as it is the part of the charging structure which impacts merchants and therefore they have successfully lobbied to ensure it is fully aired and now regulated via the EU. However issuers, particularly smaller issuers like ourselves, get no voice and no input over the scheme fees and charges made to us, some of which we regard as disproportionate and we propose that their charging mechanisms also need to be reviewed. In particular we believe charges on inter-regional transactions are significantly higher than the cost of the transaction in some cases.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Yes. We would be interested to know what level of transparency will be in place on reporting them.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Yes.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

Yes.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply?

Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

No, we do not think any of these additional measures should be used at this stage, but should be kept under review.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Yes to the first question. No to the second.

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

Yes. We believe you should consider integrating your approach with the new senior managers regime, possibly to include key positions in Operators and infrastructure providers.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

No, although we believe you should review penalties actually imposed periodically to check they are proportionate and fit for purpose, together with stronger action on repeat offenders.

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

One of the things we have added to many of our commercial contracts is that liability caps should exclude actual direct losses of any description. We would welcome consideration of an appropriate redress regime alongside penalties.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

Yes.

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Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper and Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed regulatory approach.

We recognise that the UK Government has committed to developing a regulatory regime for the payments industry that makes it even more responsive to the needs of service users, promotes innovation, and facilitates effective competition between Payment Service Providers. We fully support these objectives, and look forward to working with the PSR to ensure that they are delivered.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper and Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach of setting up a Payments Strategy Forum where the views of Schemes and Users are represented in the setting of the industry agenda.

We understand that it is the PSR's intention to establish a Working Group to consider in detail how the Payments Strategy Forum, and any subsidiary groups, would be governed – we would be very pleased to join any such Working Group, and contribute to the thinking in that respect.

The payments industry, through both Payments Council and the UK Cards Association, has a strong track record in collaboration particularly in delivering innovation and change to the market alongside positive engagement with regulators and other stakeholders. We believe the proposed forum could build on this success.

Examples of such collaboration include Faster Payments, the launch of Chip and PIN, the Current Account Switch Service, and Paym.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

The proposed design of the Forum includes representatives from consumer and business groups. Whilst RBS supports that approach, on the basis that effective representation of all constituencies is a prerequisite if the Forum is to fully achieve its aims, we believe that careful consideration should be given to how these groups are represented. There can be significant divergence in agenda and goals between constituencies, potentially making it difficult to reach a consensus on what needs to be done, and to what timescales. In a worst case scenario, involving too many representatives from a very wide array of stakeholders may have the unintended effect of stifling innovation.

Separately, careful consideration will need to be given to the role of the Card Schemes as stakeholders in the proposed forum, particularly as they operate in strong competition with each other. Ideally, the cards-related agenda of the forum should be focussed on development of infrastructure and standards (which in turn allow participants to compete) in order to be effective.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

RBS believes that working groups which feed into the forum with proposals for consideration and debate are sensible. It will, however, be important to consider the process by which proposals will be approved, on which entities they will be binding (Payments Council has a mechanism whereby smaller members can seek a waiver in respect of certain Board decisions), and, once agreed, how the Forum will track and report delivery, and hold participants to account.

As indicated above, we would be happy to work with the PSR/others to consider in detail how the Payments Strategy Forum, and any subsidiary groups, would be governed.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

None at this time, although clearly further such issues might arise as detailed consideration is given to the working of the Forum.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

RBS agrees that it is important that the views of service users are represented in decision making in the Schemes, and that decisions taken in Scheme governance or advisory groups continue to be taken with sound commercial and service improvement as a basis. While decisions will sometimes impact differently on particular groups of stakeholders

(e.g. due to technical work needed to comply) the end goal is improvement and enhancement to the effectiveness of the broader payments landscape.

As mentioned in relation to the Payments Strategy Forum (see SP2-Q2 above), it is important for the Schemes to balance the desire to ensure all interests are represented with the need to keep meeting numbers to within manageable proportions. We believe that the Independent Directors perform a useful role in that respect.

Specifically in relation to cards, it is not our view that small players are under represented in Card Scheme decision making. The make up of governance groups (for example the Visa UK Board) is such that all member institutions have the opportunity to stand for election.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

RBS supports the proposed direction on Operators to ensure that there is appropriate representation of the interests of service-users (and, indeed, of all parties with an interest in the operation of a particular system).

Provided that such representation is proportionate (and we'd welcome further discussion on how best to ensure that this is the case), we do not believe that significant additional costs would be incurred. The electronic schemes, in particular, have worked hard over recent years to ensure that the interests of users are fully represented, including via the appointment of independent chair/directors with, inter alia, a public interest objective.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach – we believe that the Schemes have established processes in place to identify and address such conflicts.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously

act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

RBS supports the proposed approach – we do not believe that any significant costs would be incurred as a result.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

RBS supports the principle of timely publication of board minutes, as already happens in respect of Payments Council board meetings.

We do, however, believe that Operators should be permitted to exercise a sensible redaction policy, i.e. to avoid an obligation to publish material which might, for example, compromise the security or integrity of systems, or legitimate confidentiality interests of third parties. Unredacted minutes might contain commercially sensitive data relating to tendering for contracts, employee contracts/data etc, where there is no public interest benefit arguing for publication.

That said, we would suggest that arrangements could be made for the PSR to have confidential access to unredacted minutes (subject to FOIA considerations) – we understand that some of the electronic schemes already operate such arrangements with the Bank of England.

We are not convinced that publishing details of all votes, and the rationale for each Director voting in the way that they did, is necessarily helpful (e.g. if it resulted in a reluctance, for any reason, to speak freely on a particular issue) – again, this information could be made available to the PSR on a private basis if required.

Specifically in respect of the card schemes, whilst still supporting the principle of requiring Schemes to publish minutes of decision making meetings (on the basis that this would increase transparency and trust while making the Schemes more accountable to their wider membership and eventual end users), we are not sure that, when redacted to remove commercially sensitive data, they will prove to be entirely helpful. In the case of MasterCard it may be difficult to achieve disclosure via this approach, i.e. given their incorporation in the United States and status as a public company.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

RBS does not believe that the proposed approach would lead to a significant increase in costs.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our

proposed approach, please give your reasons.

RBS supports the proposed approach in respect of Payments Council reserved matters – indeed, we are aware that Payments Council’s Board has already voted to terminate the relevant contracts.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach.

We would be keen to ensure that, whether an Operator is subject to Regulation 97, or to the proposed Access Rule, there is a ‘level playing field’ for all Operators.

We would also be keen that the PSR and Bank of England liaise to ensure that their interpretation/application of Principle 18 is aligned.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach.

We would again be keen to ensure that there is a level playing field for current Operators, or those which might become subject of this regulatory regime in the future.

We assume that the process for assessing compliance would be similar to that undertaken by the Bank of England in respect of CPMI IOSCO – hopefully the two could be co-ordinated to avoid potential duplication of effort.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposal.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

RBS supports the proposed Access Package.

Whilst we don't believe that this will result in additional costs for Operators, it should be noted that some (e.g. Faster Payments, with 5 FTE's) are already investing significant resource/budget in addressing Access related issues.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach, i.e. that appropriate information should be published, with a view to providing guidance to PSPs which are contemplating Indirect access to one or more payment systems.

This information however needs to be defined in conjunction and agreement with all Sponsor Banks to ensure that the key elements are consistent across the banks, i.e. to enable high level comparison of individual offerings, notwithstanding that each sponsor will wish to adopt its own branding, formats etc.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed development of an Information Hub, and would suggest that it is developed so as to be complementary to the information provided by Sponsor Banks (see SP4-Q5 above).

We would recommend that information provided by the Hub is kept at high level, and aims primarily to point PSPs in the direction of the further information required to enable them to make the right decisions to meet their own individual circumstances.

The Hub should avoid the inclusion of commercially sensitive detail, or any attempt to construct a simplistic 'comparison table', of the kind provided in certain consumer markets. It should clearly be kept up to date, and comply with Competition Law requirements, at all times.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach, and, in common with those other banks which currently act as Sponsor Banks, has already commenced work on creating a draft Code of

Conduct for approval/delivery within the timescales proposed.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

RBS supports the proposed approach to the development of a variety of competitive Technical Access Solutions. We are participating fully in the workstream being led by the Faster Payments Scheme in this respect (see their press announcement dated 8 December 2014).

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

Whilst marketing collateral/webpage creation will clearly require development activity, as will introduction of a new Code of Conduct, RBS does not consider the costs involved to be material.

The Operators (particularly Faster Payments) will also incur costs in taking forward the Indirect Access work, but these are substantially in place already, and included in budgets going forward.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

RBS is pleased that the PSR has given careful consideration to the subject of interchange fee regulation, and note that it is broadly observing as EU regulation comes to a conclusion over the coming months.

Irrespective of the arguments about the correct level of interchange fees, arguments which are now broadly settled, a fundamental feature of interchange rates has been the ability to incentivise desirable behaviour. This has included financial benefit for retailers in moving to secure methods of payment such as Chip and PIN or Verified by Visa/MasterCard SecureCode and has been an effective tool in achieving change in the market. The PSR should consider how it can allow or encourage similar measures in the future – particularly where a strategic direction or programme is identified by the proposed Strategy Forum.

It is our view that some merchants will, as the paper identifies, be subject to 'blended' pricing where they have little visibility of the difference between the interchange fee for the transaction type and the merchant service charge applied by the acquirer. We believe that it would be desirable to encourage greater transparency in this area to encourage competition between providers of acquiring services as well as to ensure that smaller retailers see the same benefit of reduced interchange as the larger retailers. Furthermore,

we have genuine concerns that reduced interchange fees will not result in lower costs to consumers (as desired) by virtue of retailers reducing prices. Instead, we believe that consumers may in the longer term be the net losers by virtue of increased fees for banking services and a reduced appetite amongst banks to invest in innovation in card products.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Principle 1: RBS agrees

Principle 2: RBS agrees

Principle 3: RBS agrees but would query the means by which the PSR will make its judgement in determining whether or not an Operator or Infrastructure provider has adequate financial resources. Rather than develop its own means, it is recommended that the PSR accesses financial and/or operational data already made available to other regulatory bodies such as the FCA. Where regular additional information is required that goes beyond current requirements, consideration should be given to extending the requirements laid-down by other regulatory bodies in order to gain commonality of approach and ensure efficiencies of scale in its production and delivery.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

RBS agrees with this approach noting that this is essential primarily for the purposes of the Personal and Non-Personal customer experience as well as maintaining commercial competition and encouraging innovation.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

RBS agrees with the proposed approach, albeit that we believe that the Operators, which are already subject to CPMI IOSCO principles, and to Companies Act responsibilities, will already be compliant.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed

Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

As above, we believe that the Operators, which are already subject to CPMI IOSCO principles, and to Companies Act responsibilities, will already be compliant with the proposed Principles. Whilst we don't disagree with the PSR's proposed approach, we would welcome a recognition of the current position.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

RBS agrees but restates what was said in response to SP6-Q1 regarding the re-use of existing information as doing so will help restrict cost impacts for firms without compromising the PSR's objectives.

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

RBS agrees with the proposed approach for the PSR's Objectives Guidance. RBS in particular welcomes the PSR's acknowledgement of the importance of collaboration across the industry and how this can ensure added efficiencies, further innovation and enhanced competition. RBS would urge the PSR to seek an appropriate balance of regulatory intervention and continuing organic development within the industry which will further support and ensure the achievement of the overall aims of the core objectives of the PSR.

RBS notes the PSR will in due course publish further guidance on the operation of its concurrent competition powers. RBS looks forward to reviewing this guidance and engaging with PSR further if required on this topic.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

RBS agrees with the proposed approach here. In particular the overarching consideration that in formulating specific priorities and workstreams the PSR will consider the balance between how specific action will advance its own objectives against potentially constraining factors (in particular surrounding resourcing for undertaking such workstreams in light of the likely benefit of potential outcomes).

In addition to the importance of fairness and the proportionality of any action taken, RBS would add that ensuring transparency in any decision making processes is equally important. RBS recommends that the PSR engages with industry stakeholders sufficiently before undertaking any significant workstreams to ensure these are appropriately framed to deliver maximum benefit in light of the inevitable resource costs which will be incurred, both by PSR and the industry generally.

RBS welcomes the fact that the PSR intends to closely work with other regulators (notably the European Commission, the Competition and Markets Authority and FCA) when considering any workstreams to ensure regulatory duplication is avoided.

RBS notes the intention of PSR to publish a Memorandum of Understanding with the CMA and looks forward to reviewing this in due course.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

RBS agrees with the proposed approach in so far as they are intended to be largely consistent with the FCA's Decision Procedure and Penalties Manual (DEPP) and Enforcement Guide (EG). Any proposal to vary these powers and procedures in the future should be the subject of consultation by the Payment Services Regulator or at the very least be based on a publicised "read-across" (e.g. relevant amendments to FCA DEPP and EG that have been consulted upon).

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

RBS welcomes the proposals regarding dispute resolution and the transparent process that the PSR intends to apply. However, where the PSR has sought commercially sensitive information from firms, it should be treated in confidence and not distributed further without the prior consent of the firm. Once a determination is made again, commercially sensitive information should be withheld.

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

RBS welcomes the proposals regarding Super-Complaints and their having been modelled on the existing Super-Complaints mechanism for the CMA. It is recommended that where other organisations such as the CMA seek to vary their Super-Complaints process that the PSR is mindful of these and maintains model similarities where it is appropriate to do so.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

RBS broadly agrees with the principles and methodology i.e. a disgorgement element plus a penalty element with mitigating/aggravating factors and a provision for discount. This mirrors the existing FCA/PRA enforcement regimes.

If there is to be a cap on penalty amounts, our preference is for the cap to be in respect of revenues derived from the failure as opposed to funds transferred through the relevant system e.g. CHAPS system. The magnitude of compliance failures should not, in our view, be measured by the total amount paid through the transaction(s) at issue. Uncapped penalties could lead to disproportionality. Applying a cap delivers greater certainty and acts

as a safeguard against over-zealous assessment of culpability.

The PSR has provided guidance as to the factors which it may take into account when determining the level of a penalty. This list is not exhaustive but it does include consideration of the participant's previous disciplinary record and compliance history. It is not clear if this is intended to cover only their disciplinary record with the PSR or whether it would also take into account regulatory action taken by other regulators e.g. FCA or PRA. We would argue that it should be limited to the firm's compliance history with the PSR; regulatory regimes vary in their approach and it would be inappropriate to seek to collate all findings across multiple regulators in calculating a PSR penalty.

Otherwise, the PSR's suggested approach is broadly in line with the FCA and PRA regimes and we have no further comments.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

[See our response to SP6-Q11.](#)

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

[See our response to SP6-Q11.](#)

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

[See our response to SP6-Q11.](#)

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Submission to the Payment Systems Regulator
Consultation (CP 14/1)

Submission by:

Ripple Labs Inc.
San Francisco, CA USA



11 January 2015

Submission to:
UK Financial Conduct Authority
Payment Systems Regulator
psrconsultations@psr.org.uk



300 Montgomery Street, 12th Floor
San Francisco, CA 94105

11 January 2015

Financial Conduct Authority
Payment Systems Regulator

Submitted via: psrconsultations@psr.org.uk

Dear Madam/Sir:

I am pleased to submit a response to PSR CP14/1 on behalf of Ripple Labs, Inc.

Ripple Labs is a technology company that conceived and developed the Ripple protocol, an open payments infrastructure for real-time clearing, netting and settlement of financial transactions. Our objectives in building the Ripple protocol are to facilitate more transparent and efficient payments systems, reduce friction between financial institutions and currencies, and broaden access to financial services.

We commend the PSR's transparency, thoughtfulness, and inclusion in its approach to regulation, and are grateful for the opportunity to submit this letter.

Ripple Labs fully supports and shares the PSR's objectives of fostering a competitive, innovative, and inclusive payments system. As the Ripple protocol embodies many of the PSR's goals, Ripple Labs writes to ensure that it and other emerging technologies are accounted for in the PSR's approach to oversight.

We respond to your questions from the perspective of an infrastructure provider. The Ripple protocol is not currently designated for oversight by the PSR; however, as an emerging technology with interest in UK payment systems, Ripple Labs aims to proactively engage with the PSR and other regulators.

We discuss four primary points that we believe will be essential to the PSR's success:

- 1. Ensure regulations account for the new technologies that will be necessary for creating a more competitive, innovative, and inclusive payment system.**
- 2. Enable startups and smaller companies to contribute to payment system innovation.**
- 3. Take a holistic view of risk and consider the cumulative impact of regulations.**

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- 4. Consider how new infrastructure technology can minimize payment, operational, and systemic risks while improving anti-money laundering (AML) efforts.**

We thank you for considering our comments and are happy to assist with any questions.

Understanding Ripple and Its Benefits

Opportunities to improve today's payment systems

Today, banks largely rely on a patchwork of intermediaries to clear, net and settle transactions for domestic and cross-border currency payments.

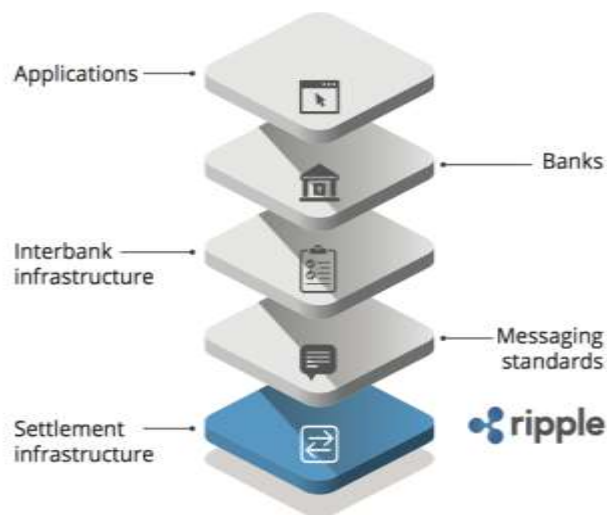
The reliance on intermediaries concentrates risk and control in a handful of large institutions while adding costs, delays and inefficiencies to funds exchange for the entire ecosystem (operators, participants, administrators).

The increased demand for faster and more global payments has highlighted structural inefficiencies and inherent risk in today's system. There's an opportunity to build a safer, faster and more efficient system.

Ripple: Infrastructure to minimize or eliminate structural inefficiencies

Ripple is infrastructure technology that is the foundational layer for a payments system. Ripple is designed to be a neutral settlement layer, meaning it incorporates the existing messaging standards, governance, and rules of the networks that adopt the protocol. As an infrastructure technology, Ripple does not replace existing networks, rather it aims to increase efficiency and connect separate networks.

Ripple: The Foundational Layer of an Interbank Payments Network



As basic infrastructure, Ripple is a technology can be used by payment networks, banks, central banks, and clearing houses. Similar to today's existing payment rails, Ripple is not intended to be used directly by consumers.

What makes Ripple different?

The first neutral payments protocol

Ripple is an Internet protocol-based technology, meaning it is a set of standards to enable connectivity and interoperability between financial institutions. The standard is formally referred to as the Ripple Transaction Protocol (RTXP).

Payments today are made in manner that is akin to the early days of email. Each email domain was siloed, restricting communication between users belonging to separate domains. To resolve these structural barriers, email providers adopted the SMTP Internet protocol, which underpins the interoperable email system we know and use today.

The Ripple protocol is an open standard that enables systems and banks to connect seamlessly, much like SMTP has done for email.

A record of balances without a central counterparty

Ripple features a ledger that clears and settles payments between banks and payment systems bilaterally - without intermediaries - in real-time. Unlike today's networks which typically rely on a central counterparty, Ripple transactions are cleared via consensus, the process (native to Ripple) by which a collection of authorized counterparties validate transactions.

Having many parties engage in consensus on the distributed network maximizes operational redundancy, thereby minimizing risk of systemic downtime and the concentration of control within any one party. No longer are network participants restricted to the technical capabilities and settlement hours of the one central counterparty.

A competitive market for funds exchange and delivery

When making cross-border transactions today, a bank is subject to the FX rate dictated by its correspondent. This lack of competition adds significant costs to cross-border payments.

Ripple rethinks funds-exchange by hosting a competitive market of authorized liquidity providers to post FX bids. Ripple routes transactions through the lowest FX rate, reducing a material cost and minimizing a bank's risk associated with having only one FX provider.

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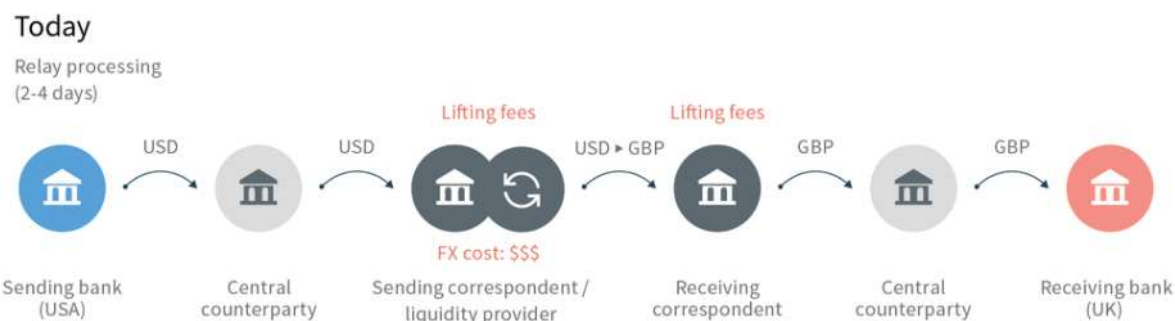
Benefits of Ripple

Ripple's unique characteristics and capabilities provide numerous benefits for network operators, payment service providers, end users, and regulators. Below are some benefits we feel are of particular interest to the PSR. The Ripple protocol:

1. Reduces fragmentation and concentration risk; increases competition

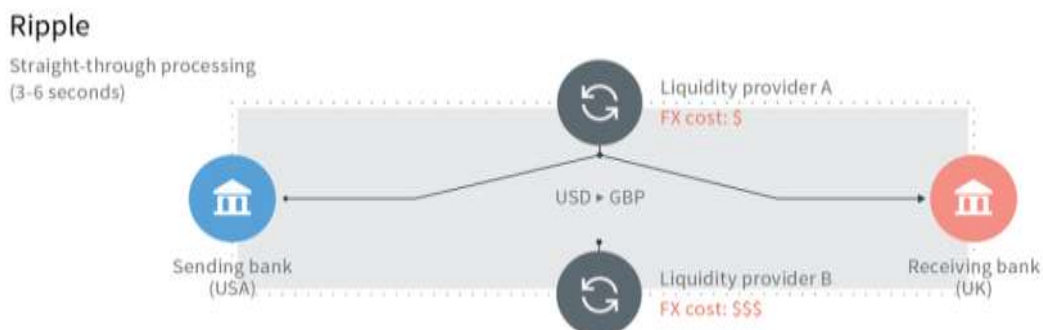
For cross-border transactions today, banks send payment messages through a global network provider (ex: SWIFT) but must rely on a complex patchwork of correspondents and intermediaries for settlement. This fragmented settlement infrastructure adds costs, delays, and risks, resulting in a system that is feasible for only high-value payments.

Given that only a handful of institutions have the size and international presence to serve as a correspondent, settlement of cross-border payments is largely concentrated in a small group of global money center banks, leaving most banks with few alternatives if their correspondent ceases operations.



The Ripple protocol enables bilateral payments in real-time, circumventing the chain of intermediaries along with their costs, delays, and risks. As a result, Ripple can vastly broaden access to cross border payments, lowering barriers for banks (and their customers) who previously lacked the size or payment volume to facilitate transactions themselves.

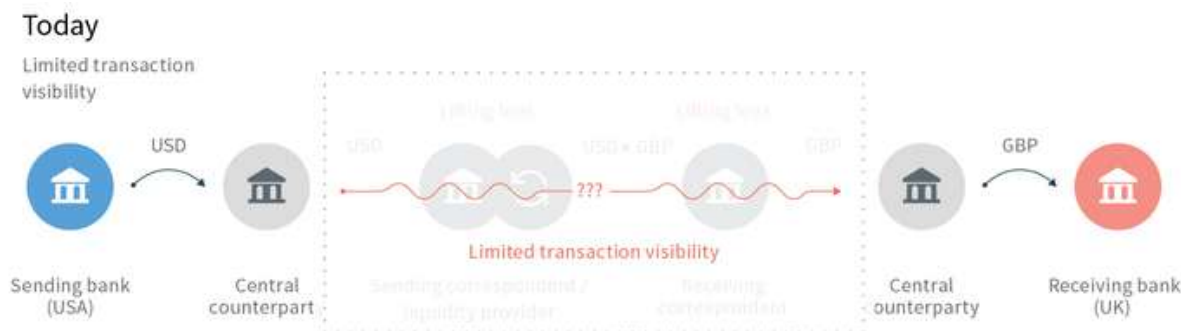
Ripple has the potential to lower the cost of transactions by increasing competition. Instead of only one FX provider as in today's system, Ripple hosts a competitive marketplace of liquidity providers who bid on the currency exchange. Ripple sources FX from the lowest-cost liquidity provider, minimizing a significant cost of cross-border payments.



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2. Enables fund traceability and transaction visibility

Today's system provides little transaction visibility for sending and receiving banks, complicating balance confirmations, audits and AML compliance. Banks have little to no insight into the transaction path and counterparties as funds move across borders.



Bilateral connectivity simplifies the transaction path, improving traceability between sender and receiver. Further, banks can exchange more payment information (e.g. fee pre-disclosure; balance validation; confirmation) before and after settlement.

The transparency offered by the Ripple protocol has the potential to greatly improve the industry's AML efforts while lowering banks' cost of compliance. (Importantly, the ledger does not include any personally identifiable information like account numbers or customers' unique identifiers.)

3. Reduces systemic risk: no single point of failure

The distributed network created by the Ripple protocol maximizes redundancy across the parties on Ripple. This process means that systemic operation does not rely on any single party, rather it is shared across the participants on the network. A large majority of independent participants would need to fail for the system to cease operating.

Unlike today's networks, which rely on a central operator, it is impossible for control or power within Ripple to become concentrated in any one or few parties. Ripple's distribution minimizes systemic risk and improves operational resiliency - essential aspects of a trusted payment system.

4. Eliminates conflicts of interest as a neutral infrastructure layer

Ripple is designed to be a neutral payments infrastructure, meaning it is currency agnostic and, like email and other standards, shows no preference to any country, jurisdiction, or system.

Ripple leverages the governance and messaging standards of the payment networks that adopt the protocol, making it flexible infrastructure without conflicting interests.

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5. Improves capital efficiency and liquidity management

To minimize counterparty risk, a bank must place reserves or collateral at its correspondent. As each correspondent typically only serves select markets, a bank must maintain multiple correspondent relationships to maximize geographic reach, tying up significant amounts of working capital.

Ripple's bilateral settlement obviates the need for correspondents, minimizing the costly reserve requirements and allowing banks to more efficiently deploy their capital. Instead of holding reserves with each correspondent, banks only have to hold one reserve on Ripple and can access all the currencies and market makers on the protocol.

Instead of FX provision limited to a single correspondent, the competitive market of currency providers bid on transactions, minimizing costs and maximizing currency liquidity.

6. Decreases operational and settlement risk

On Ripple, payments are either fully settled and completed in real-time or they do not occur at all -- a process called atomic payments. This process eliminates or reduces many of the risks that plague today's reliance on intermediaries for cross-border payments, including:

- Principal risk (also called *Herstatt Risk*) - since payments settle bilaterally, in real-time, Ripple eliminates the risk of failure along the chain of intermediaries
- Replacement cost risk - since payments cannot fail as they pass through the intermediaries, sending institutions do not have to account for replacing a failed transaction with a new intermediary and a new market price
- FX risk - with the FX conversion and settlement occurring in real-time, Ripple minimizes the foreign currency risk arising from the timing gap between the agreement of the rate and the actual conversion of currency
- Operational risk - the sending and receiving institution having a direct connection provides real-time transaction confirmation and minimizes the cost and time of error resolution. Today banks rely on intervention from their correspondent to resolve errors, a process that results in costs and can take several days.

The reduction in risk on Ripple lowers the cost of sending payments and improves the safety of the system.

7. Enables new products and improved consumer experience

Because Ripple enables banks to offer faster payments at a lower cost, the benefits of Ripple's payments infrastructure can flow through to the end user via access to new products and services.

Ripple enables banks to introduce new payment products, specifically low-value payments that aren't feasible today and more efficient interbank payment products. Banks can offer their customers increased geographic reach for remittances, faster payment confirmation and additional transparency not possible today.

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8. Improves information security and reduces cyber threats

Cyber security is a top priority for the financial services industry. Today, personal information is sent through a chain of intermediaries, each of which could compromise the security of the information to either bad actors or governments that require visibility into bank transactions.

Ripple's bilateral payments - direct from sender to receiver - eliminate the intermediaries and many opportunities for data breach. Ripple helps safeguard information and improve information security within payments.

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Who is Ripple Labs?

Named one of the 50 Smartest Companies by MIT Technology Review, Ripple Labs is the technology company that conceived and developed the Ripple protocol. The Ripple protocol is an open architecture, thus not owned by any one party, yet Ripple Labs exists to support its adoption by developing tools for financial institutions and payment networks.

Our staff of over 80 professionals has experience in financial services (E-loan, Goldman Sachs); payment networks (Fiserv, Visa); security (Jumio, United States National Security Agency); technology (Apple, Google); and policy (Federal Reserve, Promontory Financial Group).

Ripple Labs is uniquely positioned to create a modern payments infrastructure as it is (a) developing a technologically advanced and extensible global transaction protocol and (b) cooperating with regulators and incumbent financial institutions to enhance and connect existing systems.

Ripple Labs has engaged with dozens of regulators, central banks, banks, payment networks, and liquidity providers globally (Americas, Europe, Asia-Pacific). Public engagements include: CBW Bank (US), Cross River Bank (US) Fidor Bank (Germany), Earthport (global interbank payment network operating in 65 countries). Private engagements include: top-20 EU and US banks, EU and US bank consortiums, multibillion-dollar hedge funds and quantitative trading firms, top-10 global remittance operators, top-15 global telcos.

Ripple Labs is backed by prominent investors including Google Ventures, Andreessen Horowitz, Lightspeed Venture Partners and IDG Capital Partners.

Ripple Labs is based in San Francisco, CA.

1. Regulatory Approach

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

The PSR's regulations will apply to payment system operators, infrastructure providers and payment service providers within each designated entity.

Ripple is a settlement infrastructure that can be used by system operators and service providers. Ripple is not currently designated for PSR's oversight; yet, as an emerging technology that can underpin future payment systems, we strive to be an active participant in regulatory and industry discussions.

Our goal in responding to the PSR's request is to ensure the regulatory approach takes into consideration the emerging technologies that will enable a competitive, innovative and inclusive payment system.

We share several points that we believe are essential to the PSR's regulatory approach:

1. Ensure regulations account for the new technologies that will be necessary for creating a more competitive, innovative, and inclusive payment system.

The PSR is building on the UK's history of being an innovation leader in banking, as demonstrated in its implementation of the Faster Payments initiative. To continue this important effort, we urge the PSR to ensure its rules accommodate the new technologies and governance models that can underpin a more efficient, inclusive, and safer payments system.

The PSR's proposal and supporting papers describe regulatory efforts in the context of the existing system, which assumes the continued use of a centralized operator. Certain new technologies, such as open protocols and distributed networks, may not rely on a central operator.

This alternative governance model offers many benefits to payment systems. A distributed network eliminates the systemic risk of relying on one central operator. Ripple's distributed network maximizes operational redundancy, meaning a large majority of independent participants would need to fail before operations are interrupted. This model improves resiliency, while making it impossible for any one party to acquire dominant control over the system.

Another emerging technology that could drive greater efficiency and connectivity within UK payment systems is digital currencies. The Ripple protocol includes a native digital currency (referred to as XRP) to serve operational and security functions.¹ Ripple Labs recently submitted

¹Specifically, XRP acts as a bridge between illiquid currencies so banks can easily and efficiently make cross-border payments to areas not feasible today. Importantly, banks do not have to use XRP as a bridge currency and have full control to only send payments with traditional fiat currencies. Additionally, XRP acts as a "postage stamp" when sending payments across the protocol. This process attaches a small cost to each payment, making it unfeasible and costly to spam the protocol. (continued on next page)

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a letter in response to HM Treasury's request for information on digital currencies, a copy of which is attached to this document.

To advance the UK's payment system, the PSR should ensure its rules and guidance accommodate the alternative governance structures and new technologies that will drive innovation.

2. Enable startups and smaller companies to contribute to payment system innovation.

We commend the PSR's effort to build a flexible regulatory framework, rather than issuing proscriptive guidance. Putting forth inflexible or one-size-fits-all regulation will exclude startups and smaller companies -- typically the drivers of innovation -- from participating in the payments system.

To create a more competitive and innovative system, we stress the need for a tiered, risk-based regulatory scheme that considers the size and unique circumstances of each participant.

We are encouraged by regulators' recent acknowledgment of this concern. In December 2014, the New York Department of Financial Services announced revisions to its BitLicense proposal to include a 2-year transitional operating license for startups and small companies. Without this provision, startups would not have been able to meet the expectations for mature companies and would be excluded from contributing innovation and competition. We applaud such efforts to balance inclusion and innovation with oversight and consumer protection.

3. Take a holistic view of risk and the cumulative impact of regulations.

We acknowledge that new technologies present new risks and deserve careful consideration before implementation. However, many of these risks are known and can be mitigated.

We urge the PSR to take a holistic view, also considering the risks from continued reliance on antiquated infrastructure. The risks of not modernizing one's infrastructure and capabilities are not always as apparent as the risks that come with a new technology. Yet, the risks of outdated technology increase over time and pose real threats to a system's operational resiliency.

Further, we urge the PSR to be mindful of the cumulative impact that regulations will have on network operators, infrastructure providers, and end users. As regulations may create unintended consequences, the PSR should strive for coordination between rules and weigh the aggregate effects of its guidance.

The cost increases exponentially if a user attempts to attack or overwhelm the network, essentially bankrupting the bad actor of its reserves. This feature protects the network from denial of service attacks and bolsters the resiliency and security of the protocol.

4. Consider how new infrastructure technology can minimize payment, operational, and systemic risks while improving anti-money laundering (AML) efforts.

We support and share the PSR objectives of creating a more competitive, innovative and inclusive system. However, we urge the PSR to also consider how to build a safer system with greater risk monitoring capabilities.

The distributed network created by the Ripple protocol can reduce certain systemic risks and can help ensure that no one party will gain dominant control and suppress competition. Ripple further supports increased competition by replacing one FX provider with a marketplace of providers bidding on FX spreads. This arrangement incentivizes the most efficient management of FX liquidity and minimizes transaction costs.

Specifically, the Ripple protocol:

- Increases network connectivity and interoperability while lowering liquidity costs;
- Enables more-complex transactions via higher visibility and funds traceability; and
- Increases transaction speed and volume while lowering credit, operational, and systemic risk.

Minimizing risk, enabling greater AML capabilities and reducing compliance costs

We fully support and contribute to the PSR's three objectives, yet we also urge the PSR to consider how to create a safer system with greater risk management capabilities. With the global economy becoming increasingly interconnected and new payment services extending the reach of payments, greater risk management and transaction monitoring capabilities will be critical aspects of a modern payment system. The failure to adopt enhanced risk management tools becomes a risk itself.

Unlike payments sent through correspondent banks today - which are opaque at best - Ripple's ledger provides complete end-to-end transaction traceability, greatly improving banks' visibility into payments and their AML monitoring capabilities.

At present, banks must pay correspondents for audit and account balance reports. Ripple's transparent ledger is updated in real-time and available 24/7/365. This functionality offers the possibility of significantly lower compliance and operational costs while empowering management and regulators with greater information.

2. Payments industry strategy

SP2-Q1: Do you agree with our proposed approach of Option 1: (Option 1) set up a Payments Strategy Forum to establish the industry strategy; (Option 2) maintain the Payments Council's or a successor body's role in setting industry strategy; (Option 3) PSR develop high-level priorities for the industry ourselves.

Ripple Labs applauds the PSR's efforts to build consensus around industry strategy, drive forward change, and spur innovation. In considering which approach to pursue, we encourage the PSR to take into account the need to make discussions of industry strategy transparent. Creating an open environment that welcomes new or alternative perspectives will be key in driving innovation.

Discussions of industry strategy should be inclusive of both existing payment industry entities and firms outside of the payments industry and outside the UK who are developing innovative technology. An interested party's inability to access discussions and share ideas will stifle the PSR's innovation efforts. Ripple Labs fully supports the PSR's intention to increase service-user representation in discussion of industry strategy.

While we offer these overarching themes and support for PSR's general direction, we opt to leave the decision on how best to incorporate these points to UK firms and those designated for oversight.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

The PSR has proposed a series of well-informed infrastructure themes for the industry to address. Ripple Labs offers these additional themes for consideration:

- 1. Improving interoperability through infrastructure** - The retail and commercial market is increasingly demanding the ability to move funds between payment systems more seamlessly and swiftly. The success of a future payment system hinges on its ability to meet this demand and enable more efficient funds movement.

We would like to emphasize the role of infrastructure in setting standards for enabling interoperability between payment systems domestically as well as internationally. Investing in infrastructure that is designed to maximize interoperability will establish the UK as a leader in payments innovation.

- 2. Improving information security and personal data privacy**

We are developing the Ripple technology with compatibility with messaging standards and information security standards in mind. In light of the recent escalation of database

breaches and compromised identity information, we have given serious thought to addressing and integrating measures to include digital security on an infrastructure level.

Bilateral payments via Ripple means that banks no longer have to send private customer information through a chain of intermediaries who each increase the risk of a breach. End-to-end payments via Ripple gives banks and investigators greater visibility and control over funds information, and allows individuals to have agency over their personal information, minimizing the risk of a data breach.

3. Improving compliance and risk management

Ripple's ledger operated via a distributed network brings complete transaction transparency for sending and receiving banks, whereas today visibility is opaque at best.

The ledger provides opportunities to collect richer data and vastly improves banks' and regulators' AML capabilities while lowering cost of compliance. Transaction data will be more visible and stored in a common ledger, improving the process of conducting audits and investigations. Rather than tracking funds through each intermediary's own books, investigators can simply reference the Ripple ledger for funds traceability.

Focusing on ways to improve risk management capabilities while lowering compliance costs can create significant advantages for UK payments systems and regulators.

4. Identity portability and privacy

Ripple technology supports the principle of individual identity ownership. Ripple Labs is developing the protocol with a framework to give users control over how their personal identity data is used and shared. We applaud the PSR's initiative to take number portability into account. However, we believe that efforts to build an effective digital payment structure must include digital identity standards on an infrastructure level. Such a system would also protect individual privacy, ensure user authenticity and provide transparency capabilities.

Furthermore, this identity framework enables tiered Know-Your-Customer standards and provides possibilities for greater financial inclusion. Integrating secure digital identity standards at the infrastructure level reduces anonymity and ensures greater AML compliance and technical access to participation in the payments system.

3. Ownership, governance and control of payment systems

(see Supporting Paper 3: Ownership, governance and control of payment systems for more details)

The PSR has voiced concern that the effective control of today's payment systems is concentrated in a small number of participants. This concentration has limited openness, innovation, and the representation of service-users in industry discussions.

Ripple Labs urges the PSR to consider how alternative governance models - like open architecture and distributed networks - can directly address concerns of control and limited access.

Distributed networks vastly decrease concentration of effective control

Unlike network governance today, which relies on one central operator, distributed networks rely on the individual participants in the network to facilitate primary functions.

For instance, today all the payment service providers within a network rely on one central counterparty to clear and settle transactions. However, distributed networks like Ripple decentralize these primary functions to participants in a process called consensus.

Having multiple, individual parties facilitate the primary functions maximizes redundancy across the network, minimizing the systemic risk of relying on one central operator. A large majority of the individual members on a distributed network would each have to stop working to disrupt the network's operations.

As processes are decentralized across many participants, it is inherently impossible for any one party to gain effective control over the network.

As a neutral architecture, Ripple enables inclusiveness and accessibility

The Ripple protocol is designed to be a neutral settlement architecture, meaning it supports and treats all currencies equally. This structure enables accessibility and promotes inclusiveness globally.

As an open standard, the Ripple protocol is not owned or controlled by any one party. (Ripple Labs exists to promote the use of the protocol but does not own it.) Just as no one owns the protocol that underpins email (SMTP), no single entity owns or controls the Ripple protocol. It exists to increase interoperability and reduce friction between its users.

Structuring the Ripple protocol as a distributed network and an open standard minimizes the possibility of vested or conflicting interests exerting undue influence over its use. This allows networks and payment service providers to use the protocol with confidence that it will remain a neutral standard for connecting payment systems.

Success of other open protocols in and beyond payments

The accessibility, utility, and neutrality of open protocols are already being used to improve payments and banking globally. One primary example is the development and adoption of the Advanced Message Queuing Protocol (AMQP), a standard used to order, translate and route payment messages across diverse programming languages that were not previously interoperable.

AMQP was started and developed by the banking industry as an alternative to proprietary standards that did not allow connectivity across systems. J.P. Morgan Chase led the development of AMQP in 2003, organizing a working group of international banks including Bank of America, Credit Suisse, Deutsche Bank, Barclays, and Goldman Sachs.

AMQP has been adopted globally to enable connectivity in banking. J.P. Morgan Chase sends one billion messages using AMQP each day.² The Deutsche Borse became the first financial exchange to adopt AMQP, enabling users to better monitor positions and risks.

Being an open standard has allowed non-banking sectors to adopt and benefit from the protocol as well. AMQP is currently being used by the defense, telecommunication, and manufacturing sectors at organizations including Google, NASA, the Government of India, AT&T, and the U.S. National Science Foundation.

The adoption of open protocols has proven them to be a successful way to enable connectivity and interoperability between participants.

Ensuring consumer safety and security on the protocol

Although the protocol is neutral, Ripple Labs takes certain measures to maintain standards to keep the network safe and secure. As such, Ripple Labs defines and encourages best practices and standards for financial institutions and banks (referred to as “gateways”) that adopt the protocol.

Although Ripple Labs does not control gateway activity, we are implementing a program through which gateway risk is ranked and monitored. We also engage with gateways on topics related to technical development, risk and compliance. Ripple Labs promotes gateways that implement best practices around consumer protection and KYC, among others. Generally, established banks already implement best practices consistent with the regulatory requirements in the countries in which they operate.

Gateways using the Ripple protocol to settle transactions are encouraged to adhere to best practices around consumer protection. This includes full disclosure of terms of service, pricing

² Source: Advanced Message Queuing Protocol. <http://www.amqp.org/product/realworld>

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information and fees. We encourage gateways to audit their financials and disclose to customers their dispute resolution rights and policies around accessibility of funds.

As part of this program, we monitor whether gateways are registered with the proper authorities as money service businesses, as applicable, and if they implement an anti-money laundering program and onboarding procedures (i.e. Know-Your-Customer rules) as required by law.

Through these means, Ripple Labs encourages an open, neutral and inclusive protocol, while also setting standards that promote consumer safety and trust.

4. Access to payment systems

Increasing Access

While Supporting Paper 4 is primarily focused on network operators, Ripple Labs would like to take the opportunity to discuss how modern infrastructure technology can further the PSR's goal of increasing access to payment systems.

Integration of Ripple does not impact a network operator's rules or governance. However, the benefits of using Ripple as payment infrastructure enables more banks to participate directly in payment networks.

Ripple's bilateral settlement eliminates the costs and risks of relying on intermediaries to facilitate payments. Atomic transactions via real-time settlement on Ripple's ledger minimize settlement and counterparty risk, while the competitive marketplace of FX providers reduces the cost of exchanging currencies.

Altogether these benefits can lower the marginal costs of transacting and participating in a payment network, making direct integration economical for payment service providers who may lack the volumes to justify direct participation today.

6. Regulatory tools

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence?

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants?

SP6-Q3: Do you agree with our proposed approach that our PSR Principle of Financial Prudence should apply to Operators and Central Infrastructure Providers?

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles?

Ripple Labs supports the PSR's efforts to set high-level behavioral standards, rather than issuing prescriptive rules. This approach takes into consideration the unique circumstances and size of a variety of companies that contribute innovation and competition.

Ripple Labs agrees with the expectation that all participants pursue a clear and cooperative relationship with regulators, keeping them apprised of developments in a timely manner.

Further, Ripple Labs supports the expectation that companies who are designated for oversight fully observe and comply with rules, regulations, and standards of conduct.

Ripple Labs recognizes the importance of a strong compliance program. We have invested in a team of risk and compliance analysts led by Karen Gifford, Chief Compliance Officer. Gifford previously served as an AML prosecutor at the Federal Reserve Bank of New York and worked as a regulatory and compliance consultant at Promontory Financial Group. Greg Kidd, the Chief Risk Officer of Ripple Labs, covered payments systems at the Federal Reserve Board and also served as a risk consultant at Promontory Financial Group.

Ripple Labs applauds the PSR for considering systemic risk in its proposal, evident in the third principal: financial prudence. Ensuring the safety and soundness of the system itself is a product of safe and sound participants. ***However, we underscore the need for flexibility in applying this principle and ask the PSR to define the particular risks that the regulation is aiming to address.***

Ensuring companies have sufficient funds to meet their liabilities and properly carry out their functions is vital, yet we urge a tiered approach that acknowledges the size, age, and growth stage of companies, particularly startups and smaller entities. Holding startups and smaller companies to the same expectations as large companies may prohibit them from participating and undermine the PSR's efforts to foster an innovation and competitive system.

A tiered approach would grant greater flexibility to startups and then increase expectations as they mature or begin to serve crucial functions within the system. Ensuring rules enable firms of

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all sizes to participate helps foster a diverse and vibrant ecosystem necessary for the UK to develop a leading payment system.

As previously mentioned, the New York Department of Financial Services' recent decision to allow a transitional digital currency license for startups is a great example of a tiered approach to regulation that balances oversight and safety with innovation.

The PSR's proposal calls for operators and infrastructure providers to identify, monitor and manage their business risk. While Ripple Labs agrees that managing business risk is essential, we urge the PSR to ensure the risks they are seeking to address are not already covered by other regulations, such as third-party vendor management requirements that may be imposed by other financial regulators.

Duplicating efforts or regulations, especially in an inconsistent way, will unnecessarily increase the cost and burden of compliance. If the PSR feels that some business risks have not been properly addressed in existing regulations, Ripple Labs urges the PSR to clearly define these risks so industry participants can ensure they are fully accounted for.

Ripple Labs appreciates the opportunity to submit this letter. We are pleased to assist with any questions and look forward to future participation in the PSR's efforts.

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Santander UK: A new regulatory framework for payment systems in the UK: PSR CP 14/1

Overview

1. Santander UK Plc (Santander) welcomes the opportunity to respond to the Payment Systems Regulator's (PSR) consultation on a new regulatory framework for payment systems in the UK. Santander encloses our responses to the questions detailed in CP14/1 in an annex attached to this document.
2. As a scale challenger in the UK banking market, Santander welcomes measures which improve competition, innovation and the experience of customers. We are therefore broadly supportive of the PSR's proposed approach, particularly to ensure that payment systems are operated and developed in a way that considers and promotes the interests of all service users.
3. Santander supports the PSR's three statutory objectives (competition, innovation and working in the interest of service-users) and believes the PSR will (i) ensure payment systems operate in the best interest of all and (ii) build upon significant improvements, such as CASS, Faster Payments, Paym, and contactless cards, made in recent years.
4. One of the greatest obstacles for challenger banks is accessing the parts of payment systems which are essential to giving customers the way to pay which they expect. We acknowledge there is complexity and cost in joining payment schemes directly – driven mainly through the technical requirements of connectivity – and as a result challenger banks tend to enter into agency access agreements. One way to tackle this would be to create a Single Access Point (SAP) which would allow challenger banks to access the faster payment infrastructure without the complexity and cost of direct access.

Our response to the consultation questions includes the following key points:

5. Santander stresses the importance of the PSR working closely with other regulators such as the Financial Conduct Authority (FCA), the Competition and Markets Authority (CMA), the Bank of England and the Prudential Regulation Authority (PRA). A collaborative approach will be fundamental to the sector's future viability, particularly with regard to the implementation of ring-fencing which will result in significant and material changes to UK banks' structure, operating models and systems. The impact of ring-fencing on the industry must be taken into account by the PSR during the course of its market studies and wider work, so that it fully considers the demands placed on banks' technology platforms and their ability to best serve customers.
6. In addition to ring-fencing, there is a significant regulatory burden facing retail banks. This relates to both the regulatory change agenda, through reforms such as ring-fencing, and to the depth and tight timeframes attached to regulatory data requests from PRA and FCA supervision teams, the FCA's competition department and the CMA's Retail Banking Market Investigation. This means the amount of change already in plan is significant and future initiatives will need careful coordination to ensure conflicts are minimized; this would also apply to information requests. We urge regulators to

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coordinate appropriately with each other in an effort to minimise the burden on firms. We also believe there is a need to monitor and align to EU developments, such as the Payment Services Directive 2, as appropriate to ensure consistency.

7. Santander welcomes a more open model and the opportunity for other parties to become direct participants of payment schemes. We are supportive of the creation of a Payments Strategy Forum, considering it important that a balance of stakeholder representation exists, and that the role of the independent Chair will be central to the Forum's success. We would note that the approach taken to date by the PSR in engaging a wide stakeholder group has been positive, and believe this could bring significant benefits going forward, so would support an on-going 'town-hall' opportunity to bring as many interested parties together regularly for briefings.
8. Santander supports the notion of openness and transparency and therefore, agrees with the publication of board minutes. However, we do ask that caution is exercised and particular sensitivities are taken into consideration. Independent Directors of the Operators should be a key focal point to encourage wider engagement; we believe this is a simple and personal engagement model that could be offered to stakeholders.
9. We hope you find our response to CP14/1 useful. We welcome the opportunity to discuss the content of our response with you and are happy to answer any queries you may have.

Santander UK plc
12 January 2015

Annex: Santander's response to detailed questions raised in PSR CP14/1

Question in relation to our proposed regulatory approach (see Part B of our Consultation Paper and Supporting Paper 1: The PSR and UK payments industry for more details)

SP1-Q1:

Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

10. Santander agrees with the proposed approach outlined, but stresses the importance of the PSR working closely with other regulators. Santander welcomes the PSR's intention to work closely with the FCA, CMA, Bank of England and PRA and is hopeful that the PSR will do their utmost to relieve any regulatory burden that may be caused as a result of duplication.
11. In particular, we would like to understand whether the PSR is working actively with the CMA in their market investigation into the PCA and SME markets, and note that the CMA has identified access to payments systems and account switching and shopping around as areas of interest for their on-going Market Investigation (see pages 41 and 72 of CMA Personal current accounts Market Study update, 18 July 2014).

Questions in relation to our proposed approach to payments industry strategy (see Part D of our Consultation Paper and Supporting Paper 2: Payments industry strategy and areas for collaboration for more details)

SP2-Q1:

Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in Supporting Paper 2: Payments industry strategy and areas for collaboration? If you disagree with our proposed approach, please give your reasons.

12. Santander agrees with the option to set up a Payments Strategy Forum (PSF) (Option 1) and feels this delivers a sensible approach to the strategic development of the UK payments infrastructure. We are keen to be represented on what will be a fundamental forum for decision making on the future of payments. The support offered by the PSR will be of critical importance to ensure that all stakeholders are considered and the plans to be implemented are not seen by some to be "big bank" focused only. It will also be important for the regulator not just to observe but also to 'steer' the Forum's activity so that it operates on a transparent and 'no surprises' basis, particularly if it does not feel that the outcomes it is looking for are being pursued.
13. In addition, the right candidate as independent chair is central to the PSF functioning well. It will be important for the Chair to maintain a balanced view and to have adequate knowledge of the payments industry so that strategy setting is realistic while spurring innovation. In addition, the balance of panel representation will be important to ensure views are represented by banks, consumers and innovators. It is clear the change needs to ensure the needs

of all are understood and dealt with, but the balance of the PSF should reflect those who pay for and execute the future developments to ensure that delivery and economic return requirements cannot be ignored.

14. Santander is supportive of the PSF's formation and looks forward to further information on the details of this forum.

SP2-Q2:

Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

15. Santander believes that the PSF has a critical role to play in the future development of projects and should, if well-structured, deliver speedier and constructed decision making. It is therefore important that wider stakeholder representation is included. To ensure the PSF works effectively, we believe an organised and engaging structure of Working Groups feeding into the PSF would be sensible to ensure that it is used as a strategic-thinking body, supported by the detail coming from the Working Group layer. The PSF also needs to maintain control on a wider vision of innovation and collaboration-needs to ensure that the industry deliveries help to create a simpler and fairer model for all Users.
16. By way of a simple definition we would suggest the PSF acts as a board to the programmes and working groups, providing the direction and leadership you would expect from a senior leadership body. Under the board would be relevant standing groups and project working groups to deliver the proposals. It will be essential to have engagement from the Operators to support the work and ensure that they are able to elaborate in key areas. There is a clear need to ensure that the governance and responsibilities of parties involved are clearly understood from the outset – the Operators would then be best placed to lead the development and change models forward to completion; the PSF would be well placed to provide senior direction and support in areas of challenge for example.
17. We recognise the Payments Council provides useful, thorough and extensive MI and data from most Operators, and the provision of this should continue bringing a level of consistency from all the regulated Operators to support better understanding for Service Users of trends and opportunities to innovate. Through a co-ordinated model, the Operators are probably best placed to do this in future.

SP2-Q3:

Do you have any comments on our indicative model for how the Payments Strategy Forum (PSF) could operate in practice?

18. Santander advocates the importance of an independent chair, and recognise the intention to create a working group to design and define the PSF model, which should bring clarity to the following:
 - How will banks with payments and distribution/acquiring be represented, given their representation could affect majority voting if applicable

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- How will new entrants be included in the forum as they enter the UK market?
- How will Direct PSPs procuring agency bank services be protected? In addition, will guidance be created for banks offering white label solutions?

SP2-Q4:

Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

19. Santander believes that one key objective from the PSF needs to be consideration of the future strategy, including the tougher decision about decommissioning or migration to new models.
20. The customer must remain at the heart of the PSF's work. Santander recommends that the industry continues to focus on the work that has started to create a world leading Payment System for the UK, with wider stakeholder engagement essential, and ensure that individual project delivery or workstreams deliver to that new vision of the payments landscape which is seeing competition or entrants globally. The PSR needs to support the PSF by ensuring it is aligned and sighted on the implications for payments from work by other regulators (CMA/PRA etc). We believe the powers that the PSR has should support not needing to mandate banks, Direct PSP's, indirect PSP's to deliver the clear objectives once agreed, and this will support new infrastructures to ensure SME and consumer benefits are driven forward.
21. At this time we would particularly recognise the potential impacts from projects including Banking Reform, and significant European Regulations such as the Payment Services Directive 2, as examples where a medium term sighted vision is important to ensure we make the transition to these regulations more straight-forward for all users.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our Consultation Paper and Supporting Paper 3: Ownership, governance and control of payment systems for more details)

SP3-Q1:

Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

22. Santander is aware that a number of Schemes have introduced Independent Directors and Chair to their model and believe this is a sensible approach to be consistently followed. This is a relatively recent change and in our opinion is bringing some benefits to the groups. One area we feel needs to be improved is Users access to and engagement with the INEDs. This could initially be via a link from the website to pose questions or provide input to debates, as well as the INEDs providing outputs through a consistent and readily available channel - in itself this should not be too much of a burden on

the INEDs and effective support for the Operators would reduce the administrative burden. This straightforward change supports the need for greater transparency and openness and could encourage more direct engagement. The INEDs should have relevant non-bank experience to ensure that the right balance is brought to the Boards. We also feel the cross-sharing of interests between INEDs is an important feature to ensure that cross-scheme collaboration and integration features heavily on their agenda. We consider it important that the representation on Boards is for the interest of the Scheme company and not member institutions. Those represented at Board level should be experienced and knowledgeable with a good detail of the end-to-end payment model and they should be able to support both operational and strategic decision making.

SP3-Q2:

Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

23. Santander is supportive of the proposed direction on Operators to ensure that there is appropriate representation of the interests of service users. The proposal provides a sensible control mechanism. The incremental cost is unlikely to be significant and should provide the underlying benefit that a non-interested party on the Board can support the decision making process.
24. We would caution though that recently the annual budgeting process from Schemes has increased considerably, albeit with justification, and the on-going demands are placing further financial calls on Member banks, which in turn may be passed onto Service Users. The proposed changes therefore always need to be measured and subject to a robust cost benefit analysis to ensure that costs are not allowed to continue to escalate and create another perceived barrier to entry.

SP3-Q3:

Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

25. Santander agrees with the PSR's proposed direction and believes that unintended conflicts of interest will be removed. Santander also suggests that each director must be clear in understanding the need to create separation within their own institutions to ensure they are not personally conflicted by discussions around CIP or Scheme strategy.

SP3-Q4:

Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

26. Yes – Santander agrees that this is a sensible approach with an intention for the PSR to review in the future.

SP3-Q5:

Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

27. Yes – Santander believe that the segregation of responsibility between CI and Scheme is important to recognise commercial and industry needs.

SP3-Q6:

Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

28. Santander believes that the publication of board minutes, including a record of votes and reasons for decisions made, needs to be considered carefully and the sensitivity of voting needs to be considered on a case-by-case basis. The PSR needs to recognise that individual institutions may not always take a positive approach in widely available minutes. Santander queries whether the expectations of published Board minutes are similar to those of the FCA's published Board minutes, i.e. anything commercially sensitive can be redacted. Consistency across the various Operators would also be sensible.
29. Santander would also like to know whether the published Board minutes will be actively shared with other regulators.
30. Santander also believes that to ensure effective decision making around payment systems, and the control thereof, it is crucial to have a clear, transparent view of the key risks; and to complement the approach to risk management which the payments industry currently has in place.

SP3-Q7:

Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

31. Yes – Santander agrees that well documented and accurate minutes should not drive any additional costs and delivers added benefits of openness and clarity.

SP3-Q8:

Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

32. Yes – Santander understands that the Payments Council reserved matters are currently being reviewed between Schemes and the Payments Council and the approach of leaving them to resolve matters in a controlled way is most appropriate.

Questions in relation to our proposed approach to access to payment systems (see Part F of our Consultation Paper and Supporting Paper 4: Access to payment systems for more details)

SP4-Q1:

Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

33. Santander welcomes a more open access model which will further support the aspirations of the industry to drive a fair and open availability of payment systems which in turn will drive innovation for customers.
34. As a scale challenger bank, we see this as a great opportunity for other parties to become direct participants of Schemes and support the payment environment.
35. We consider it critically important that the rules around access continue to consider customer experience, security and stability at the forefront of the approvals process - without these features consumer confidence will be reduced and the perceived benefits of more PSPs will be negated.

SP4-Q2:

Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

36. Yes – we agree.

SP4-Q3:

Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

37. Yes – we agree.

SP4-Q4:

Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

38. Yes – we agree.

SP4-Q5:

Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

39. Yes – we agree that clear and transparent pricing is an important feature in the "new" model.

SP4-Q6:

Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

40. Yes – Santander see the information hub as a sensible tool in the communication model for users. However, the hub should not remove responsibility from Sponsor banks to provide their agency banks with clear communications and support as would be appropriate in any commercial service provided.

41. To date, Santander has not been engaged in any detailed discussions relating to the Hub so we would welcome clarity on issues such as who will own the information hub and therefore ensure that the information presented is accurate and up to date.

42. We would advocate that the hub is coordinated with the Bank of England and clarity about access is provided from the PSR. The PSR should also set out

clearly its expectations of firms' usage of the hub in its March Policy Statement to the Consultation Paper.

43. In addition, we would advocate that the hub would need redaction/ proprietary data protection if it is to be offered outside of an operator/direct PSP/ indirect PSP discrete relationship. The hub should also include the provision of clear Risk and Control Indicators for appropriate users. Industry/cross payment system levels and specific payment system level risks should be identified to ensure adequate focus is maintained over the management of these risks.

SP4-Q7:

Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

44. Yes – we agree that a code of conduct is a sensible and proactive approach. This can be assessed and commented on annually by users of the PSP services to ensure accurate and thoughtful responses.

SP4-Q8:

Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

45. Yes – we see this as a sensible approach which the Schemes should adopt. In respect of the supplier side of the code of conduct we believe there should be basic standard expectations provided, but allow the commercial and competitive space to determine the more detailed and prescriptive positions suppliers wish to take.

SP4-Q9:

Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

46. Yes – we see there is benefit for the Industry in developing this approach.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our Consultation Paper Supporting Paper 5: Interchange fees for more details)

SP5-Q1:

Are there other matters regarding interchange fees that you think we should consider at this stage?

47. Given the Regulation on Multilateral Interchange Fees is still subject to political discussion at an EU level and the regulation has not yet come into force, Santander believes there are no further actions for the PSR to take at this point.

48. With the expectation being that the PSR will be the competent authority for enforcing Interchange Fee Regulations, we welcome the PSR's commitment to engage with relevant stakeholders to inform and share thinking on how it will approach this role.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our Consultation Paper Supporting Paper 6: Regulatory tools for more details)

49. Santander supports the regulatory approach set out by the Payment Systems Regulator. We are committed to good regulation and to the highest standards of conduct in the markets in which we operate. As an economic regulator, we welcome the objective economic analysis the PSR will be able to bring to the high profile issues it will be considering.
50. We would also suggest that in its relations and regulation of payment systems, the PSR takes an approach which is forward looking and proportionate to the users involved.

SP6-Q1:

Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

51. Yes – we agree. The first two principles form what should be standard behaviour for any PSP, the third is a sensible approach to take for Operators or Infrastructure Providers.

SP6-Q2:

Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

52. Yes – we agree. Santander does not believe the approach would create an unfair burden and we consider it critically important to ensure that all participants are expected to behave in a consistent and appropriate way. We believe that for regulation to be successful the regime should be consistent and seek to create a level playing field among participants.
53. Nevertheless, it may be beneficial for the PSR to take into consideration proportionality and the size of an organisation as entry players may not have the resources to adhere to full routine/ obligations.

SP6-Q3:

Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

54. Yes, we agree.

55. The financial prudence and stability of Operators and Providers is of critical systemic importance to customer expectation and we support a reasonable, financially sound approach to this matter.

SP6-Q4:

Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

56. Santander agrees in principle to the proposal, however, we feel more detail is needed to ensure there are no unintended consequences to the participants.

57. We consider that it may be appropriate for the Principles of "Integrity" and "Skill, care & diligence" to apply to indirect participants as well. Whilst these can be carried over into the Terms & Conditions of the sponsor agreement, as PSPs there should be an expectation that they have the skill sets required within these principles

58. Separately however, we would like to understand if the PSR will have a link to the PRA and FCA Accountability regimes so we can better understand the obligations individuals will be under once the regimes are formalised.

SP6-Q5:

Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

59. Yes, we agree with the anticipated costs and benefits identified.

60. To ensure rigour is instilled in the process additional resource may be required, however, we believe but this is not a proportionally significant cost.

SP6-Q6:

Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

61. Yes, we agree.

62. As with any new business plan, we would suggest this area is reviewed regularly to ensure it captures all aspects intended.

SP6-Q7:

Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

63. Yes, we agree. Santander believes this is a sensible approach to take. The proposed approach also supports the PSPs in ensuring that there are not too many initiatives launched at the same time which would create issues for individual PSPs capacity to manage deliveries.

SP6-Q8:

Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

64. Yes – we agree. We consider it critical that the expectations are set out clearly at the start of the engagement so all parties are aware of the requirements.

SP6-Q9:

Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

65. Santander would like further clarity on whether information on dispute resolution will be revealed within board minutes. For instance, could there be an adverse publicity risk if one party is able to levy a complaint against a PSP?

SP6-Q10:

Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

66. Yes – we agree. We see there is benefit in consumer groups raising awareness of potential customer detriment.

SP6-Q11:

Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

67. Yes, we agree.

68. However, Santander does have a concern that, particularly in the case of some Payment schemes where there are many users failure to comply with agreed requirements could be out of the direct control of participants. For example, BACS has 100k+ direct submitters and if a required change to the process was expected, it may be the case that not all submitters would be able to comply. We query whether this would be considered as non-

compliance by the PSR. We believe setting penalties on a case by case basis would be the most sensible approach.

SP6-Q12:

Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

69. Santander acknowledges that the value of transactions varies dramatically between Schemes, so we consider it sensible to base penalties on the revenue generated by the activity or relevant Operator.

[ENDS]

SECURE TRUST BANK PLC

SECURE TRUST BANK PLC

Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper* and *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

Yes.

When determining preferred strategic options and associated timescales the PSR should remain mindful of the limited and finite resources of the multitude of small non-direct participants and their total reliance on the co-operation of the direct participants to enable them to comply with any regulatory changes.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

Yes.

The ongoing CMA investigation of the Current Account market implies that the Payments Council, amongst others, has failed to encourage material levels of new entrants into key UK payments markets. Given the ownership of the Payments Council this is not altogether surprising. A new approach to formulating a macro strategy that promotes effective competition is desirable.

We are supportive of efforts to improve competition by making it easier for small players to access payments infrastructures at a fair cost that should be transparent, governed by term contracts that are non-discriminatory which include appropriate service level agreements to protect the interests of the customers of non-direct participants.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

Whilst the PSF will inevitably be dominated by the large incumbent clearing banks and direct participants, an appropriate mechanism should be created which ensures that ideas, views and concerns of the small non-direct and potential new participants are heard and considered.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

Clarity on the theme of account number portability should be provided at an early stage given the potential ramifications of such a move.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

We are too small to provide any meaningful input into this and some other questions in this Consultation Paper.

SP3-Q5:

Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

This has no impact on Secure Trust Bank PLC given our modest size. However the PSR should seek to find the balance between promoting transparency and requiring larger participants to divulge publicly, at any early stage, innovative steps and potential new products.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

Yes

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

Yes

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes. We believe this will be helpful to small and potential new participants. It may well highlight the absence of any real hunger amongst the larger banks to compete aggressively to provide sponsorship / agency services in the UK.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes. This code of conduct could also consider fairness in the context of the costs levied by sponsoring banks onto agency banks and other non-direct participants.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We would recommend that the PSR reserves judgment here. As it gains greater

knowledge with the passage of time it may determine that a more prescriptive approach will better support delivery of the PSR's statutory objectives.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Yes

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Yes but the approach should be proportionate and not a one size fits all, noting the huge diversity in the scale and scope of the participants.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

In determining whether it is appropriate to levy penalties one would hope that the PSR will take into account whether non-direct participants are themselves guilty of non-compliance or have been exposed to such by their sponsors.

SWIFT

SWIFT



Payment Systems Regulator
Consultation Response Team
25 The North Colonnade
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London E14 5HS

12 January 2015

Dear Sir, Madam,

A new regulatory framework for payment systems in the UK: PSR CP 14/1

SWIFT has reviewed the Payment Systems Regulator's consultation on "New regulatory framework for payment systems in the UK: PSR CP 14/1" of November 2014, and welcomes the opportunity to provide feedback. SWIFT fully supports the Regulator's objectives in promoting competition and innovation, and in ensuring that payment systems are developed and operated in the interests of service-users.

As a member-owned, member-governed cooperative, SWIFT provides the communications platform, products and services to connect more than 10,500 banking organisations, securities institutions and corporate customers in over 200 countries and territories. SWIFT enables its users to exchange automated, standardised financial information securely and reliably, thereby lowering costs, reducing operational risk and eliminating operational inefficiencies. SWIFT also brings the financial community together to work collaboratively to shape market practice, define standards and debate issues of mutual interest.

Beyond the comments set out in the attached annex, we believe additional items could be and will be raised in upcoming discussions. As well as connectivity and access solutions, we believe it will also be important to carefully calibrate the investment and ongoing running costs involved in any eventual solution, particularly given the demands of real-time 24x7 payment operations. The Regulator may also want to give further consideration to issues such as access to the payment system from other jurisdictions and currency zones.

During its forty-year history of serving the global financial community, SWIFT has been involved in many key financial market infrastructure projects both in the United Kingdom and world-wide. This has allowed us to establish best practices, perspectives and acquire unique expertise. Our message templates, protocols and platform have become the industry standard and, as a result, more than a hundred payment market infrastructures and seventy securities market infrastructures currently use them across the world. Amongst others, the Japanese Securities Depository Centre (JASDEC), the Singapore Exchange (SGX), the Australian Stock Exchange (ASX), TARGET2 (T2) and TARGET2-Securities (T2S) in Europe, the Single Euro Payments Area (SEPA) and the first ISO 20022 RTGS in Asia in Brunei, have all embarked on major projects with SWIFT.

Most recently SWIFT was appointed to host and manage the UK's SEPA IBAN Only migration infrastructure platform and to provide the infrastructure for Australia's New Payments Platform (NPP) project, a new fast payments infrastructure.

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SWIFT



The UK's new SEPA IBAN Only platform is a cost-effective open access platform which is designed to both enable full compliance with the SEPA directive and to accommodate the growth of other services and functions in line with the pace of change in the UK payments landscape. NPP, an innovative new platform, will provide Australian businesses and consumers with a fast, versatile, data-rich payments system for everyday payments. The NPP is being developed collaboratively with local financial institutions. It is the local industry's response to the Reserve Bank of Australia's strategic objectives on payments innovation, and implements the former Real Time Payments Committee's proposal on innovation in the domestic payments system.

SWIFT has a long history in the United Kingdom and collaborates closely with the UK financial community to ensure our products, services and standards best support its needs. We would very much welcome the opportunity to contribute to these developments and remain engaged in these discussions as they continue.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

SWIFT believes that a collaborative industry-led approach to the development of technical access solutions is preferable and therefore supports the adoption of this approach by the Payments Systems Regulator (PSR). This said, for a collaborative approach to be implemented successfully, a basic model should first be identified. There are useful prior examples of collaborative approaches in payment systems development and innovation, and SWIFT would welcome the opportunity to discuss these further with the PSR.

Another important factor which needs to be addressed is the issue of harmonisation of message formats and standards for technical access to the UK payment systems. We would strongly recommend that the adoption of open industry standards be mandated in the new payment system. This is because, whenever there is a need to communicate – as indeed there is in any payments solution – there is a need for a shared frame of reference by which different industry actors and systems can understand each other.

By way of background, standards are either open meaning that they are “free of levy” and can be used by all, or they are proprietary, meaning that they are subject to usage restrictions and/or that they can be subject to some sort of usage charge or fee. Open standards support the free interchange of information, whilst proprietary standards can be (and often are) used to restrict information interchange and/or access to infrastructures. Open standards are defined by the industry for the industry in a collaborative way. They are free of charge, facilitate investor choice and provide cost-effective tools to achieve the policy objectives of market resiliency and transparency, as well as sustainable compliance with such objectives. As an important tool for longstanding, robust recovery and for growth, we believe that regulators and policy-makers should expressly require at least the option to use them in the context of the regulatory reforms now underway.

Open standards can enable:

- The transport of financial data using standardised processes and languages that cannot be misinterpreted or manipulated by users;
- The standardisation of reporting, enabling supervisors to more efficiently monitor markets and facilitate the exchange of information;
- Easier data capture and better transparency of data delivery;
- Greater cost efficiency for most data exchange, collection and dissemination requirements, including for processing as a whole.

The use of proprietary formats would, in comparison:

- Reduce efficiency in data collection;
- Prevent a comprehensive analysis of financial data by authorities;
- Create unnecessary extra costs for end-users;
- Create barriers to access.

Open standards play a key role in enabling desired regulatory outcomes, whilst delivering cost efficiency and fair competition in the industry. Indeed, in the Recommendations for Financial Market Infrastructures, CPMI-IOSCO recognises the general importance of open standards in the context of the access to, and operations of, financial market infrastructures (defined as; payments systems, CCPs, CSDs and Trade Repositories). Recommendation 22, states that: “An FMI should use, or at a minimum accommodate, relevant internationally

accepted communication procedures and standards in order to facilitate efficient payment, clearing, settlement, and recording.”

In the payments area, standardised protocols using standardised data elements have been developed to provide a common frame of reference (e.g. BIC, IBAN). Similarly, in the broader wholesale financial services sector, standards allow market participants (intermediaries, market infrastructures, investors) to communicate with one another and with their regulators in the same technical language and using common identifiers throughout the transaction life-cycle (trading, clearing, settlement, reporting).

Currently CHAPS, BACS and FPS all use different messaging standards. As a result, UK market participants have to deal with a variety of messaging standards and gateways, communications networks, communications protocols and security methodologies. This adds cost and friction, increases operational risk, and can prove prohibitive for new entrants. Whilst the difficulties can be alleviated in the short term by the use of a technical access hub provider, such divergences of approach should ideally be reduced or eliminated in the future development of the UK payment systems. Of course the deployment of market-wide standards development and migration should be achieved as a result of careful planning and coordination within the industry.¹

For the new payment system, we would strongly recommend the use of the ISO 2022 messaging standard. ISO 2022 is an open international standard which is rapidly emerging as the default choice in the payments industry around the world for high- and low-value, international and domestic schemes. The Australian New Payments Platform (NPP) initiative is based on ISO 2022 formats and the Single Euro Payments Area (SEPA) uses ISO 2022 formats. Many other markets are now implementing, or planning to implement, ISO 2022 to replace multiple local or regional formats for low value and high value payments - for example, the next major step in Euro is for TARGET2 and EBA Euro1 to adopt ISO 2022 for order-by-order payments in 2017.

A further observation on this point: we would also recommend that providers of solutions for the UK seek to harmonise their implementations with those of their peers in other jurisdictions, with the goal of reducing overall costs and promoting interoperability. This would benefit global organisations that connect to multiple payments infrastructures internationally.

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¹ By way of example, the EBA selected the MT103+ message for their SEPA-forerunner service: the Credeuro service. The Credeuro service was the solution to the EU Directive 2560/2001, which required that basic credit transfers in euro up to EUR12,500 should cost the customer the same whether the other endpoint was within their own country or in another EU country.

While this Directive was a stepping stone towards SEPA, it only affected cross-border payments. It was important therefore, that the message type for the Credeuro service be the same as the message type used in other cross-border contexts, albeit adapted to address the issues specific to Credeuro.

The use of code words and the absence of detailed remittance information meant that the business information could be contained in the MT103+ message, rather than the full MT103. The processing cycle meant that bulk processing, rather than order-by-order, was feasible. Over time Credeuro's timecycle was reduced thanks to Payment Services Directive, and then the entire traffic was migrated onto ISO 2022 XML, but without the need to either alter the message type for PSD compliance, nor to alter the communications channel for the migration to ISO 2022 XML.

MT103+ and FileAct proved to be a cost-effective and flexible basis for launching the Credeuro service which the European Commission now views as a vital stepping stone towards SEPA. Following this planning methodology it is logical that high-value euro payments now be migrated onto ISO 2022 and off MT103, as is the plan when TARGET2 and EBA Euro1 move onto InterAct in 2017.

General Comments Relating to Access to UK Payment Systems

In our view there are several other important issues that need to be considered in the context of delivering easier access options to UK payment systems. Amongst other considerations which we would happily discuss further with the Regulator, we would note that Technical Access solutions on their own may not open up the market in the way that the PSR envisages, without accompanying solutions addressing Financial Crime and Settlement issues. We set out some observations on these two matters below.

1. Financial Crime

All financial institutions have a responsibility to ensure that the financial system does not fall victim to terrorist financing or money laundering activities. However, AML rules have been widely cited as a blocker to new entrants setting up banking relationships with Sponsor Banks and obtaining access to payment systems.

New legislation such as the EU's AMLD IV requires that institutions processing payments for their customers implement robust customer due diligence (CDD) measures. New Payments Services Providers (PSPs) should also comply with these AML requirements and perform appropriate CDD on their customers. In the case of indirect access to UK payment systems and schemes, this will be of particular concern to the Sponsoring Banks, since - as Sponsors - they will potentially have no relationships with the customers of the PSPs for whom they are acting.

Where a new entrant is a direct member of a payment system, it acts as its own "Account Servicing Institution" (ASI) and so is fully responsible for the integrity of the traffic it sends into the system. Were the new entrant to breach AML rules, the penalties would fall on them directly.

Where a new entrant has indirect access to a payment system, however, the Sponsor Bank would count as the ASI and carry the risk related to the indirect member's traffic. In such a case, the new entrant's traffic is sent, either to the Sponsoring Bank, or direct to the payment system. In the case that the traffic is sent to the Sponsor Bank, the Sponsor can filter the messages within its own IT environment, before debiting the new entrant's account and sending the traffic to the payment system and performing the necessary checks. Where the traffic is sent direct to the payment system (as per BACS), however, it is unclear how the Sponsor Bank can control the risk, and at what point in the payment process this can be done. Clearly, direct technical access by a new entrant to a payment system makes their Sponsor's AML position more difficult.

The three elements commonly bundled under the term AML are: AML procedures, processes and controls; Know Your Customer (KYC) and Know Your Customer's Business (KYB).

The AML procedures, processes and controls are subject to vetting by the authority, during the PSP licencing process. Assuming that the Sponsor Bank can rely on the licence provision to provide assurance on this first element, it would only need to deal with the other two elements.

"Know Your Customer" rules would require the Sponsor Bank ASI to identify the institution, its owners and ultimate beneficial owners, its directors and officers. The SWIFT KYC Registry addresses for Correspondent Banks is an industry utility which offers a secure portal for exchanging Enhanced Due Diligence (EDD) and Simplified Due Diligence (SDD)

documents and data. Its initial scope focuses on Correspondent Banking, and provides information about institutions, not individual or private customers.

The KYC Registry offers a unique approach compared to current alternatives by providing access to a standard set of due diligence documents and data. All information in the KYC Registry undergoes quality control and transparent validation by a dedicated operational team at SWIFT. Each registry user retains ownership of its data. Registry users can only access each other's data when permission to do so has been granted by the data owner.

There is no reason why such a registry could not cover PIs, eMIs and whatever other classes of new entrant are permitted in the UK, and as a result to effectively solve the second aspect of AML for sponsor banks.

However, the third element – “Know Your Customer's Business” – will likely prove the most intractable for Sponsor Banks. The prevailing view is that it is not possible for a Sponsor Bank to know and then to continuously monitor who the customers of these new entrants are; why they are making the payments; and who the participants in the extended business or payment chain are – all this adds unacceptable risk.

In SWIFT's view there is no way around this issue if the message traffic runs through the Sponsor Bank's IT environment and/or the Sponsor Bank is in any way responsible for the KYB of the new entrant.

One option that could be explored is for the responsibility of the Sponsor Bank to be limited to settlement (and therefore credit risk) only. This option would require that new entrants have direct technical access to payment systems, so that the traffic does not run through the Sponsor Bank environment, and entail a Sponsor Bank arrangement that was limited to the Sponsor Bank underwriting the settlement risk on the new entrant's payments towards the respective payment system (although the Sponsor Bank would still be responsible for performing upfront KYC on the new entrant for whom it acts as sponsor).

In summary, without addressing this issue, we believe that efforts to widen access could be inhibited. Even if new entrants are licenced and can deal with KYC requirements, Sponsor Banks will be very wary of taking the KYB risk; KYB risk is very hard to quantify, but the fines can be extremely high and of such a magnitude that might mean that few PSPs would be able to reimburse their Sponsors.

2. Settlement

The other major obstacle to new entrants wishing to join payment systems, directly or indirectly, is settlement. This is especially true when considering participating in payment systems designed to settle in central bank money.

Whereas many countries allow the equivalent of the Settlement Account to go into overdraft as long as the account holder has placed or pledged eligible bonds to the Central Bank, under the prevailing arrangements in the UK, payments must be covered by cash on a Settlement Account. The Bank of England, of course, permits banks to undertake repurchase agreement operations through which they can sell their eligible bonds to the Bank and buy them back later, thus creating cash on their Settlement Accounts in the interim. The Bank also allows Reserves System banks to use all or part of their Reserves balances as cash balances on their Settlement Accounts during the day, thus reducing their need to obtain liquidity elsewhere to meet their payment settlement obligations.

Many new PSPs, however, neither have Settlement Accounts nor are they part of the Reserves system. As a result, they will need to clear quite a high hurdle if they are to be direct payment system members, or even indirect members. Furthermore, since eMoney institutions may not use customer funds in their own operations, they would have to have separate cash or security of their own with which to back their settlement obligations. Without such resources eMoney institutions will not be afforded direct membership.

However, even those new PSPs seeking indirect access will face significant cost burdens – since they will be passed on the related capital and credit costs incurred by their Sponsors.

It has to be a working assumption that new PSPs will not, in the main, qualify for a Settlement Account at the Bank. Therefore the majority will need a Sponsor Bank. The minority who become direct members and have a Settlement Account are likely to find that:

- They will have to hold relatively large amounts of cash to cover their obligations;
- The amount will not just be their net sender cap during one day, but, in the case of FPS, overnight and – with weekends and Bank Holidays – over several nights;
- Depending upon the exact timing of flows during a settlement cycle, the net sender cap may need to be set nearer to the gross debit turnover, because a new entrant may not be able to predict timing as exactly as an experienced member might be able to, and they would not want to have payments blocked if they were dependent upon incoming funds and unsure exactly when those funds might materialise;
- For this same reason the new entrant would be well advised to own eligible collateral and to be able to regularly use the repurchase facilities with the Bank to create intraday liquidity; to do this the new entrant will have to have the infrastructure for managing this collateral, and the cash accounts and payments that go with it.

All this adds up to a degree of liquidity and net worth, and management effort which may make new entrants' business plans unviable. Over the longer term, a move towards real-time or at least continuous settlement across UK high and low value payments, could be considered as a means of extending all forms of access, but it is clear that settlement questions will require significant immediate focus if the overall objectives of increased competition and prudential safety are to be achieved.

TECHUK

TECHUK

Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper and Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

Type your answer here

Whilst in general the regulatory approach proposed by the PSR is to be welcomed, techUK members are concerned as to whether the PSR will be able to regulate for innovation. It has been suggested that the Regulator should focus on regulation that creates an environment in which innovation thrives.

Too much regulation creates potential unintended consequences, stifling the level of and appetite for innovation. Innovation is most likely to flourish in an environment where industry has the freedom to operate, develop and improve products and services rather than being forced to build innovation into product and service offerings

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper and Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

techUK members agree that Option 1 would be the preferred option; establishing a Payments Strategy Forum with widespread stakeholder participation and involvement. This may help to steer the payments industry in a more service-user focused direction, in terms of its strategy.

As with innovation, payments industry strategy - and strategy development - can only be prescribed to a certain extent. The Supporting Paper talks about the Regulator "taking further action to advance our objectives" if industry strategy and innovation is not forthcoming. It might prove difficult to force "strategy development" onto some of the industry participants, particularly where the strategic direction identified is not necessarily fully aligned with the participants' own objectives.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

techUK members see challenges in ensuring the Strategy Forum is representative of all participants in the payments industry, given that many are competitors, without getting so cumbersome that no direction can be set.

Having representatives from each stakeholder group will ensure the number of Forum members is constrained, but will not necessarily provide a voice for the wider community,

who might then see themselves as “un-represented”.

techUK believes that it could take an extended length of time for all parties to agree a common strategic direction for some of the products and services offered by the payments industry players and that the publication of a high-level roadmap or framework early in the proceedings of the Forum could assist in the management of stakeholder expectations.

The focus of the forum should be to encourage the development of ‘common services’ that enhance the ‘non-competitive’ space and therefore drive strategic direction for the next 5 - 10 years. Success will be dependent on collaboration and a willingness to cooperate with the broader stakeholder community. Most industry representatives will not have had to consider in-depth the views of service-users in the development of their own strategies, apart from ensuring that those strategies accommodate the service-users’ basic requirements.

In designing the Payments Strategy Forum, the PSR could consider the previous approach taken by the Payments Council and set up stakeholder focus groups in order to understand what has worked well and what needs to be improved. This ‘lessons learned’ approach would provide the Payments Strategy Forum working group with valuable input to their design and execution process definition, ensuring the shortcomings of the past are not repeated.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

The Payments Strategy Forum should focus on what the UK Payments Industry needs to look like in 5 to 10 years, with consideration given to the needs of all stakeholders. This will be a challenge given the need to limit the size of the forum.

One option might be to create stakeholder focus groups who meet to prioritise items for the forum, and ‘elect’ a forum member to represent their interests, for a fixed term. The membership would then move to another focus group member on an agreed basis.

The other challenge will be to ensure that proposals accepted by the forum provide a balance between what is the ideal and what is practical. Each proposal should be underpinned by anticipated benefits, high level costs to the industry as a whole and a proposed timescale as to when the change should be available. This will help in prioritising the needs of stakeholders against the expected benefits from any proposed change and allow stakeholders to juggle conflicting priorities.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

techUK members noted that PayM should be included within the review of the infrastructure-related themes, as this makes use of existing designated infrastructure services and provides an excellent framework for the development of future payment services for all stakeholders.

techUK also suggests that some of the existing infrastructure themes are re-visited against a framework of cost/benefit analysis and time to market to ensure they are really delivering benefit for the intended stakeholder groups. This could include the planned review of CASS, and the intention to extend this to include ANP. Will this really make any difference? – do the end users care?

The current remote cheque image capture initiative is perhaps another example where the potential costs, timescale and benefits should be reviewed along with examining the end to end value chain for cheque processing. This would enable the PSR to determine whether there is a more strategic, digital alternative to paper that would meet the needs

of all stakeholders. This approach would sit very much in line with setting the strategic direction for the UK payments industry and driving towards 'World Class'.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Type your answer here

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Type your answer here

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Type your answer here

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

Type your answer here

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q3: Do you agree with our proposal to require public disclosure of Access

Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Type your answer here

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

The Regulator's direction requiring Sponsor Banks to publish certain information relating to access requirements is welcomed by techUK members insofar as it will allow fair access to the relevant information for all indirect PSPs; given the small number of Sponsor Banks which currently service the Agency Bank market. However, it is debatable whether the direction to publish access information will lead to increased competition amongst the Sponsor Banks, although it will ensure that the Indirect PSPs can make an informed choice.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

techUK agrees that the Regulator should not take a more prescriptive approach at this time. As proposed, they should give the industry the opportunity to create the Information Hub in the format, and with the content they believe relevant. Once the PSPs have had an opportunity to use that data to compare Sponsor Bank and Operator offerings and to provide some feedback on the quality of the data being provided to them, the Regulator could then undertake a review of the effectiveness of the Information Hub.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

techUK agrees that the Regulator should not take a more prescriptive approach at this time. However, they should perhaps provide a strategic framework around the development of these solutions to ensure that the PSPs who choose them are not disadvantaged in terms of access, and the associated costs. In many instances today, small PSPs are forced to charge their customers for FPS-related services even whilst larger players provide this for free. This immediately puts smaller players at a disadvantage. The introduction and extension of Technical Access solutions provides a potential answer for this problem if managed properly as part of a wider proposition. The availability and scope of Technical Access solutions should be included within the scope of the Indirect Access Market Review.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

Type your answer here

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

With the likely introduction of the IFR in 2015-16, techUK members anticipate a significant reduction in the fees paid to card issuers by acquirers for payment card transactions, particularly for credit card transactions. Given that one of the stated aims of the Regulator with regard to interchange fee changes is to “(consider) the wider impact of such changes on (...) consumers”, we would welcome assurances from the Regulator that it will work closely with the relevant authority to ensure that one of the objectives of the EC legislation on interchange fees – namely, that “retailers would benefit from lower fees, resulting in savings a portion of which would be passed on to consumers” – is closely monitored and that merchants are seen to pass on these savings by reducing their prices at point of sale. If this reduction in retail prices is not realised, then the legislation will have failed in one of its principal aims and succeeded only in increasing retailer profit margins

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Type your answer here

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

Type your answer here

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

Type your answer here

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Type your answer here

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

Type your answer here

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

Type your answer here

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

Type your answer here

TESCO BANK

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12th January 2015

Tesco Bank aims to be the bank for Tesco customers by rewarding their loyalty and earning their trust. Having taken full control of the business in December 2008, we have invested significantly in building the bank – establishing our banking and insurance platform, migrating customers from The Royal Bank of Scotland and most recently launching our first personal current account in June 2014. We now offer a full range of retail banking and insurance products and serve over 6 million customers from our locations in Edinburgh, Glasgow and Newcastle.

Following a review of the PSR's proposed framework for the regulation of the UK payments industry, Tesco Bank has a number of comments which we trust will be helpful.

1. Architecture of UK Interbank Payments

The current designation of BACS, CHAPS, FPS and Cheque & Credit Clearing Company as system operators, with underlying infrastructure provided by Vocalink, seems to cement the current organisational 'architecture' within UK interbank payments. Through the previous HMT consultation 'Opening Up UK Payments' and also at a number of the PSR's stakeholder events held in 2014, a number of respondents noted that there may be significant benefits available from vertical and/or horizontal consolidation of the UK interbank payment schemes and their infrastructure provider.

Tesco Bank has previously suggested that a robust economic analysis of payments systems in other international markets and of sectors which have faced similar challenges should inform decisions regarding the best 'architecture' for UK interbank payments. From the consultation document and the associated KPMG and Accenture reports, it is not clear whether this analysis has been completed and/or whether future work is intended to consider these questions and, if so, when this might conclude. In the context of the PSR's vision for the UK to have world class payment systems, this seems to be an omission. Tesco Bank would therefore welcome clarification on these points.

TESCO BANK

2. Remit, overlaps with other regulators and Modus Operandi

In our response to the HMT consultation 'Opening Up UK Payments', we suggested that the most practical approach to delivering a new payments economic regulatory regime would be to enhance the role of an existing regulator, such as the Financial Conduct Authority (FCA) or the Office of Fair Trading (OFT). This proposal was motivated by a desire to avoid creating additional financial services regulatory bodies, which may lead to confusion and inefficiency over roles and responsibilities.

To this end, Tesco Bank welcomes the stated intention of the PSR to work 'hand in glove' with the FCA. In many areas, the FCA will already be in possession of detailed information which should reduce the need for the PSR engage directly with Tesco Bank. However, we are not yet clear on the respective remits or how effective co-ordination will be achieved. For example, the FCA is leading the current review of CASS, considering the case for Account Number Portability (ANP) and coordinating the implementation PSD2 in the UK – all of which may have profound implications for payment systems, operators and infrastructure provision. In order to minimise the potential for overlap and/or duplication, we therefore believe that more needs to be done to:

- Explain the respective remits of the FCA and PSR in respect of payments and payment systems (including overlay services such as CASS)
- Clarify the mechanisms for ensuring close co-ordination with EU regulators

Tesco Bank's engagement with the PSR is managed through our regulatory team and is primarily led by technical experts who are experienced industry practitioners, with first-hand knowledge and accountability for the delivery of payment services to our customers. Tesco Bank seeks to engage effectively with all of its stakeholders. However, we have limited bandwidth and we urge the PSR when determining its modus operandi to ensure that the nature of engagement is as inclusive as possible and does not disadvantage non London based financial institutions, while balancing the operational impact of a new regulator.

3. Strategy Setting Process

We note that the PSR has set out a new proposed approach to industry strategy development. In our experience, the biggest challenge for UK interbank payments in the past has not been an inability to agree strategy, but, in moving from agreed strategy to a funded and mobilised delivery plan in the absence of government intervention. It is not clear from the consultation on how funding and delivery issues will be tackled through the new Payments Strategy Forum and early clarification will be required.

In relation to the strategy setting process for the card schemes, we are conscious that both MasterCard and Visa set their strategies pan-nationally. Priorities are generally agreed across multiple countries. It will therefore be important to understand how the new Payments Strategy Forum can form an effective interface with these international organisations.

Strategy setting is normally an episodic process, rather than a continuous one: with strategy formulation followed by a period of implementation to allow outcomes to be delivered and benefits to be tracked. The concern regarding a Payments Strategy Forum that meets continuously is that there will be an understandable temptation to constantly update the strategy. This creates uncertainty for existing and potential industry participants and may discourage new entrants. For example, while CASS has helped to enable our entry to the current account market, through the development of our personal current account we had to undertake significant additional work to respond to the replacement of ToDDaSO by CASS. To counter this risk, we recommend 'time-boxing' the process for establishing a 3-5 year strategy for payment systems, and establishing mechanisms to ensure that it is reviewed not less than annually.

With regard to representation at the Payments Strategy Forum, we recognise that the PSR needs to strike a difficult balance to ensure appropriate representation while also establishing practical arrangements. Our experience from other industry forums has highlighted a couple of particular areas which may be helpful to the PSR in this regard. Firstly, the views of the UK interbank scheme companies tend to closely align with those of their direct members, resulting in some potential for 'double representation'. Secondly, representatives are well placed to articulate the views of their own institution but are not generally effective at seeking or representing the views of their 'constituency' within industry forums.

TESCO BANK

4. Governance

As noted by the OFT in their July 2013 report on 'How regulation of UK payment systems could enhance competition and innovation', "As the main members and owners of payment systems, large retail banks have a strong position and an ability to control the decisions made by the payment systems". Tesco Bank therefore welcomes the steps to be taken to avoid conflict of interest for individuals at a scheme and operator level, along with the proposals to improve transparency and public interest. However, as recognised by the OFT, within UK payment systems influence is exercised by the organisations who are the main owners and members of the payments systems. Common reporting lines within these organisations therefore seem likely to continue to allow this small number of large organisations to exert undue levels of influence.

5. Access

In its report for the PSR 'UK Payments Infrastructure: Exploring Opportunities' (August 2014), KPMG commented that "the technical standards and requirements for connecting to the payments infrastructure (whether directly or indirectly) can be prohibitively expensive for some PSPs. The existence of multiple payment infrastructures with UK specific standards can require the duplication of infrastructure connectivity, introduce additional technical and operational complexity, and increase the overall setup costs of joining the infrastructure". Tesco Bank agrees with this assessment.

Entering the retail or commercial banking market in the UK requires connectivity to all interbank payment systems in order to support even a limited range of customer propositions. Faced with the existence of multiple layers of operators and infrastructures – each with specific standards, connectivity, rules and operating models – a new entrant has little option other than to utilise the services of a sponsor bank. The cost of agency banking and transactions was highlighted by the FCA as a "non-regulatory barrier to entry" in 2013 in its report 'A review of requirements for firms entering into or expanding in the banking sector'. This topic has also been analysed in a number of other studies and reports.

We recognise that a market review into indirect access will commence in April 2015. However, in view of the considerable body of evidence that access to payments presents a impediment to competition in the banking sector in the UK, Tesco Bank believes that the PSR could have taken a more prescriptive approach to the development of more streamlined and lower cost access solutions. Indeed, from our discussions with potential technology providers of access solutions, it now seems likely that a number will postpone any plans to enter the market pending the outcome of the PSR market review

Separately, at the PSR workshop "Access to UK Payments" held on 6 June 2014, the PSR stated the following principles

"Regardless of the type of access, PSPs should be able to:

- Deliver desired and beneficial outcomes to service users and end users
- Deliver a ubiquitous end user experience
- Compete with rivals within the payments market"

Indirect connection to the UK interbank payment schemes does not currently allow a PSP to deliver a ubiquitous end user experience. In particular, there is no indirect connection to the Faster Payment Scheme which allows a PSP to deliver a 24x7x365 service to its customers – impacting both faster payment processing and overlay services such as PayM. Accordingly, we recommend that the above principles are included within the PSR's framework for the regulation of the UK payments industry.

Kind regards

David McCreadie
Managing Director, Banking

THE INVESTMENT ASSOCIATION

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The Investment Association

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Date: 12 January 2015

Dear Sir

RE: A new regulatory framework for payment systems in the UK

The Investment Association welcomes the opportunity to respond to the Payment Systems Regulator's consultation.

The Investment Association represents the UK asset management industry. Our members manage over £5 trillion in the UK of assets on behalf of UK, European and international clients, both retail and institutional. Collectively, our members make up the second-largest asset management industry in the world.

Below, we have provided our responses to the questions raised in your paper. While your paper is, naturally, primarily banking oriented, it has implications for all users of the payment system, e.g. asset managers, such as the amount of information passed with payments, which can have implications for AML/sanctions purposes. Consequently we seek to ensure that the users of payments services (e.g. our members) get a proper voice in future policy discussions.

Yours

Adrian Hood
Regulatory and Financial Crime Expert

THE INVESTMENT ASSOCIATION

A new regulatory framework for payment systems in the UK

SP2-Q1: Do you agree with our proposed approach to set up a Payments Strategy Forum, as opposed to our Option 2 or Option 3 set out above? If you disagree with our proposed approach, please give your reasons.

Yes, we agree with your preferred Option 1. It represents the best compromise available, allowing for stakeholder involvement in the Forum.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

In general we do agree with the proposed design. It may be necessary to build a certain amount of flexibility into the Forum, from the beginning. There may be occasions where it would be beneficial to co-opt experts from the industry to sit on the Forum for a period, so that the Forum may benefit from their specialist knowledge. I would also support the Working Groups being able to recruit authorities where this would prove to their advantage.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

No comment

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

We have been working with the Payments Council on the Richer Data programme to improve the data transferred with payments, which could have significant beneficial impact on asset management firms' ability to combat money laundering and terrorist financing.

The proposals to phase out cheques has also been of concern to our members.

TISA

TISA

Payment Systems Regulator
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Dear Sirs

Response to PSR CP14/1

A new regulatory framework for payment systems in the UK

TISA is pleased to attach its response to this important consultation

TISA is a not-for-profit membership association operating within the financial services industry.

TISA's membership comprises over 145 member firms involved in the supply and distribution of savings and investment products and services.

These members represent many different sectors of the financial services industry, including banks, stockbrokers, asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, consultants and advisers, software providers, financial advisers and pension providers.

Following an instruction to the industry from the FSA in 2010 to tackle long delays and high costs for re-registration of assets between fund supermarkets, ISA managers and fund managers, TISA established an industry group to tackle the problem and forestall the need for detailed regulation. In 2011 TISA Exchange (TeX) was established.

TeX is a not for profit industry association. Members sign up to a standard published contract and SLA. There is an open standard (ISO20022) message set. Governance is through an elected Board, with 3 Directors elected by asset managers, 3 by service providers (platforms) and three for multi-roles, where businesses combine both activities. TISA provides the Chair and two other additional directors. Interested parties such as solution providers can join as associates (non voting). This structure allows for meaningful access and input from stakeholders. Operationally there is an SLA Council which monitors MI, adherence to SLA and recommends changes and improvements, a Legal Council, for recommending changes to the legal documents and a forum, chaired by TISA, where solution providers can tackle technical issues, particularly around connectivity and interpretation of standards. TISA ensures that these type of meetings cannot become anti-competitive. All members are welcome to attend meetings of the SLA and Legal Councils

We believe that this form of governance, which allows meaningful input from all industry participants, including third party administrators and suppliers, is a good model to adopt.

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We should be very pleased to discuss this approach with you in more detail.

We should like to be considered for a place on the Strategy Forum and associated technical committees that will be formed by you in the coming months, as we believe that our experience in the successful development of cross industry initiatives, such as TeX, would support the regulators objectives.

In addition, as TISA is not tied to a specific part of the financial services industry by its membership - our members are drawn from across the whole of the industry - we can provide an independent perspective on issues and proposals that affect the industry and its end customers - retail consumers and users of payment systems.

I look forward to hearing from you.

Yours sincerely,

Jeffrey Mushens, Technical Director, TISA

TISA RESPONSE TO

Response to PSR CP14/1

A new regulatory framework for payment systems in the UK

12th January 2015

Introduction

TISA is a not-for-profit membership association operating within the financial services industry.

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These members represent many different sectors of the financial services industry, including banks, stockbrokers, asset managers, insurance companies, fund managers, distributors, building societies, investment managers, third party administrators, consultants and advisers, software providers, financial advisers and pension providers.

Following an instruction to the industry from the FSA in 2010 to tackle long delays and high costs for re-registration of assets between fund supermarkets, ISA managers and fund managers, TISA established an industry group to tackle the problem and forestall the need for detailed regulation. In 2011 TISA Exchange (TeX) was established.

TeX is a not for profit industry association. Members sign up to a standard published contract and SLA. There is an open standard (ISO20022) message set. Governance is through an elected Board, with 3 Directors elected by asset managers, 3 by service providers (platforms) and three for multi-roles, where businesses combine both activities. TISA provides the Chair and two other additional directors. Interested parties such as solution providers can join as associates (non voting). This structure allows for meaningful access and input from stakeholders. Operationally there is an SLA Council which monitors MI,

Page 5 of 13

adherence to SLA and recommends changes and improvements, a Legal Council, for recommending changes to the legal documents and a forum, chaired by TISA, where solution providers can tackle technical issues, particularly around connectivity and interpretation of standards. TISA ensures that these type of meetings cannot become anti-competitive. All members are welcome to attend meetings of the SLA and Legal Councils

We believe that this form of governance, which allows meaningful input from all industry participants, including third party administrators and suppliers, is a good model to adopt.

Question in relation to our proposed regulatory approach (see *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

We support the proposed approach. We would particularly like to see the regulator encourage new entrants to the market. There are no physical infrastructure issues, so we do not see why new entrants could not compete with existing systems such as BACS, etc. A governance structure that enabled this and offered meaningful access to all stakeholders would be likely to deliver better outcomes for end consumers, as well as for all market participants.

Questions in relation to our proposed approach to payments industry strategy (see *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

We prefer option 1. Inherently we do not believe it is or should be the business of regulators to develop priorities for the industry. We do not believe that option 2 would work any better in the future than it has to date.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder

representation while still being effective.

As we commented in our summary, TISA has experience in setting up an industry body - TeX - that ensures meaningful stakeholder representation for all industry participants and has delivered meaningful results in the period since establishment. We should be pleased to discuss our experience with you in more detail.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

As we commented above, there are no physical infrastructure constraints on payments systems as there are for, say, railways, or gas and electricity pipes, so we believe that the regulators should look to lower the barriers to entry to potential payment solutions and providers.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

We agree with the proposed direction.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We have no comment on this question.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a

director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

We're not convinced that the conflicts of interest cannot be adequately managed. There are advantages in having knowledgeable industry executives as directors on both sides, not least in being aware of the practicalities and commercials of different courses of action.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

We agree.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We have no comment on this specific question, but see our response to SP3-Q3

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Yes, we agree, provided that the minutes are not neutered so to avoid saying anything useful. In order to encourage meaningful discussion, which industry participants will find useful, we suggest that ascription of comments to individuals in the minutes is avoided.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We cannot comment on the quantum of the likely costs but we cannot believe they are significant.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach,

please give your reasons.

We agree with the approach.

Questions in relation to our proposed approach to access to payment systems (see *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

We agree with the preferred option.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Provided that this requirement does not impose unnecessary costs, which are then bound to be passed on to consumers.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

We agree with this proposal.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

We cannot comment on this question.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

We think this is a matter for the banks to respond on.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We do not believe the regulators should adopt a more prescriptive approach.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We do not believe that the regulators should adopt a more prescriptive approach.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We do not believe that the regulators should adopt a more prescriptive approach. In general terms, we believe it should be the responsibility of industry to develop solutions, whether of Codes of Conduct, Technical Access solutions and the like. The responsibility of the regulators should be that these solutions are published, meet the strategic requirements of the regulators and are developed in accordance with the governance requirements set out for the industry by the regulators. This is likely to ensure that the solutions are more responsive to the needs of the market and consumers, and can also be updated more promptly than if a prescriptive approach is adopted. This is because if the latter approach is adopted, the regulators will have to go through a more formal consultative and rule making approach than the industry would require, certainly based on TISA's experience with TeX, and this will take more time. Also, the prospect of having to go through such a consultative approach will discourage the regulators from making or proposing change. This will be an inhibitor to change and progress. This will be bad for the UK, for the industry and its customers.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

We have no comment on this question.

**Question in relation to our proposed approach in relation to interchange fees
(see *Supporting Paper 5: Interchange fees* for more details)**

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

We have no comment on this question.

**Questions in relation to our proposed approach to our regulatory tools
(including our high-level Principles, and our enforcement and dispute
resolution processes) (see *Supporting Paper 6: Regulatory tools* for more
details)**

We have not sought to comment on this section, except as indicated below, as this seems to us to be a matter for firms. We continue to believe that adoption of the type of governance structure we discussed in relation to TeX, coupled with increasing competition, under the supervision of the regulators, will deliver most of the objectives set out by the regulators.

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial Prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

We are always concerned that regulators will require more capital than necessary from market participants under the rubric of financial prudence. A consequence of this is misallocation of capital, reduced competition, more costs for users and consumers, and increased barriers to entry.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

Market participants are surely already subject to regulatory oversight whether from FCA or PRA, so we should be concerned if the adoption of these Principles imposed further burdens and costs on industry participants.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

SP6-Q10: Do you agree with our proposed approach for our Super-complaints Guidance? If you disagree with our proposed approach, please give your reasons.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

We believe that any penalties imposed should not be retained by the regulators, but paid away to HM Treasury for use in developing financial education.

SP6-Q12: Do you think that we should also take into account metrics other than revenues

when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

Any system has to be fair and objective. What the metrics should be should be for the industry to agree with the regulators.

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

We would dislike the idea of fines being imposed for anything under than anticompetitive behaviour or wilful non compliance. Otherwise firms will become more fearful and risk averse in their decision making, and this will be bad for firms, for customers and, ultimately for the competitive position of the UK.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

As a general rule fines and penalties should only be imposed on objective grounds, calculated on the basis of metrics published in advance with rights of appeal where appropriate.

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Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper* and *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

HM Treasury set up the PSR without any reference to anti-money laundering and counter-terrorist financing (AML/CTF).

This was a fatal error by HM Treasury, as Payment Systems are centred around two core pillars – i) Security and ii) AML/CTF.

Security is adequately captured by one of the PSR's core objectives: 'interest of service users', as only by having a secure and stable payment system environment can the needs of service users (all interested parties) be met.

But AML/CTF should have been within the PSR's core ambit.

That said, it is clearly in the 'interest of service users' that clear and well-functioning AML/CTF obligations are delineated and set. Further, effective 'competition and innovation' can only occur where AML/CTF obligations are clear delineated and understood by all parties.

Therefore, AML/CTF does fall somewhat (albeit obliquely) within the PSR's ambit.

It is disappointing to see that i) the Consultation does not focus at all on AML/CTF, and ii) the PSR has not itself recognised the deficiency in its core objectives, and began a discussion with HM Treasury to rectify this issue.

Please note that we are not suggesting in any way that the PSR should become an AML/CTF regulator – it should not.

But AML/CTF should be recognised implicitly as being at the core of UK Payment Systems, and the PSR should recognise that keeping payment systems free of ML/TF should become a prime objective of the PSR.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum?

In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

Any claim made at the forum by a participant should not be accepted at face value, based on the experience of the commenter.
Otherwise, undue weight will be given to incumbent players, and they need only claim dire repercussions to any move to block it – by scaring the PSR into submission based on the possibility of future non-functional payment systems.

It should be mandatory for forum commenters to substantiate their claims based on clearly documented evidence, and not the say-so of 'the experienced' groupings, who may be using such argument to protect vested interests.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

AML/CTF, as discussed in SP1-Q1

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

Agree

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Agree

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that

payment system? If you disagree with our proposed approach, please give your reasons.

Agree – Chinese walls are proven not to work, and assuming that collusion will not occur by forcing one organisation to present two different personnel is somewhat naive.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Type your answer here

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Agree.
But if meetings are allowed to take place without all comments being minuted (as will invariably occur), then the minutes will not be a full record of the discussions, and the PSR will not have achieved its objective. So the PSR also needs to mandate that all discussions are minuted, without exception.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Agree

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

Type your answer here

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Type your answer here

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

Agree

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a

more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Agree – but wait to see if effective.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Agree – but wait to see if effective.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

Type your answer here

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

As an indirect user who would benefit from being a direct user, but is currently so far distanced from direct use that we have no experience in this matter, we are not able to currently pass comment.

Once the PSR comes into effect, and our route to Direct Access becomes clearer, we (as will many others similar to us) will be able to re-evaluate and answer this question.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Type your answer here

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

Type your answer here

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

Type your answer here

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Type your answer here

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

Type your answer here

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

No

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

It has been reported again and again that banks have flouted regulation and rules, profited massively, and then consider the lesser fines retrospectively imposed as a successful cost of business.

Capping potential fines will enable this approach to continue, and will therefore not prevent continuing abuse.

Only when potential fines to providers are significantly greater in retrospect than the profit otherwise gained, will enforcement be possible.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

Type your answer here

TSB BANK PLC

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Neeta Atkar
Chief Risk Officer

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Consultation response team
25 The North Colonnade
By email: PSRconsultations@psr.org.uk

23rd December 2014

To whom it may concern,

PSR CP14/1: A new regulatory framework for payment systems in the UK

TSB welcomes the opportunity to respond to the Payment Systems Regulator's (PSR) consultation paper (referenced above). We welcome the need for a payment system that operates for the needs of service users, which is innovative and delivers transparency and open and fair access. As a new entrant, one of TSB's objectives is to bring competition to the UK banking industry and we are therefore supportive of the PSR's objective to promote effective competition in the payment systems market which will ultimately benefit customers.

The proposals in the consultation paper will help the payment industry, particularly banks such as TSB, to plan more effectively and to compete and innovate for the benefit of customers.

Whilst the proposals seek to address several issues, particularly access, many of these are not currently a problem for TSB, as we have a good agency payment arrangement with Lloyds Banking Group, and believe that our payments service offering to our customers will rival any payments offering on today's high street. Having access to information of this nature is critical in making the strategic decision of Indirect or Direct membership, which will then inform which sponsor bank or schemes to join. We also see the Sponsor Bank Code of Conduct, as being the right thing to do and should improve further the relationship between an Indirect Bank and Sponsor bank.

In general TSB is supportive of the regulatory approach being taken by the PSR in the consultation paper and therefore our response to the consultation is focused on the areas where we have concerns or want to provide commentary.

Approach to payments industry strategy

We believe the PSR's proposed approach to set up a Payment Strategy Forum and to guide that forum into setting the strategic direction of the payments industry is a positive approach.

However, for the forum to be credible it needs to be clear on how it will appropriately represent and consider the diverse stakeholders in the payments industry. Failure to understand or represent these differences when implementing strategy could adversely impact competition, innovation and the interests of end-users. Therefore, it is crucial that those representing diverse groups on this forum have considered these differences and truly understand the areas they represent. We are hopeful that this will be given due consideration by the working group that is to be set up to consider the forum's design.

For the forum to be effective it will need to be viewed by regulators and politicians as the principal body to raise payment issues and take them forward from an industry wide perspective. This is particularly important for new entrants and smaller firms who have less time and resource to deal with such issues.

Whilst the creation and implementation of a payment system strategy will be critical, the PSR could have been more prescriptive in the consultation paper as to how the industry should organise itself to meet the challenge of delivering the strategy. We believe that all industry stakeholders need to clearly understand how the PSR expects them to work together on an inclusive basis and we hope that this will be provided as an outcome of this consultation process.

The creation of the PSR, a Strategy Forum and a payments delivery body all requires funding. We understand why the PSR has not raised this in detail in the consultation paper, however we note that the consultation paper infers that the costs for the Payment Strategy Board will be met by a 'substitution of costs' by the Payments Council. The PSR and the Strategy Forum are additional layers to the current model, which would imply additional costs to the stakeholders within the payments industry. We would hope that the PSR gives this due consideration and ensures that costs do not become prohibitive for smaller stakeholders.

Ownership, governance and controls

We support the direction taken requiring all Interbank and Card Operators to have appropriate representation of service-users in discussions and decision-making at Board.

We have commented above about the need to consider appropriate representation. The service-user community is a wide base that includes: consumers, merchants, corporate, agency, payment institutions etc. Therefore, it is important that there is appropriate representation on the Board that have the ability to represent the views of a wide ranging group of users as there are significant differences between each bank's payments solutions and business activity. Failure to understand/represent these differences when making decisions could adversely impact competition, innovation and the interests of end-users, rather than benefitting them. Therefore, it is crucial that those representing diverse groups on this board have considered these differences and truly understand the areas they represent. We would hope that the Operators take this into consideration when looking at the representation of end-users.

We agree with the proposed direction to Interbank Operators, requiring the Interbank Operator to take reasonable steps to ensure that any individual acting as a director must not simultaneously act as a director of a Central Infrastructure Provider as this removes any conflicts that may occur when a director is acting for the rule setter and technical supplier.

As for the other types of Conflict of Interest particularly an Interbank director also being an employee of a PSP, we are comfortable that the PSR proposes not to issue directions at this time and we observe that there is an expectation of the Operators and PSP's to be mindful of the concerns raised. This may even lead to PSP's ensuring that no single employee should hold a directorship in more than one Interbank Operator. However, we do accept that this would significantly increase resource requirements.

Access to Payment Systems

TSB currently has 'indirect' access to the payments systems through its Sponsor Bank. TSB chose indirect access over direct access for several reasons. These include those listed in the consultation paper e.g. the cost of technical infrastructure, economic considerations, but also because TSB believes that we can serve our customers with all the necessary payment services they require through indirect access.

We understand how some PSP's do not benefit from an indirect access solution that meets their customer needs and they are interested in developments in direct access as this maybe an appropriate solution for them. This is an area that TSB is also mindful of should we choose to change how we access the payments schemes. In view of this we support the preferred option of an access rule aligned to principle 18 of the CPSS-IOSCO Principles. We believe that the Payment Operators will benefit if the PSR provides appropriate guidance on how the rule should be interpreted. Additionally, we support a reporting rule on access as it will ensure that the Operators keep access at the forefront of their thinking.

We agree with the proposal requiring public disclosure of Access Requirements for Operators and Sponsor Banks. This transparency will benefit banks and will provide valuable data that is easily accessible to help make informed decisions. We believe that any public disclosure should be done in a standardised format that enables easy comparison of key requirements across all Operators and Sponsors. Holding both Operator and PSP information in a single hub would be of greater benefit to those considering access, we would envisage that there might be links back to Operator and PSP's websites where they could cover specific areas in greater detail if necessary.

We believe a Sponsor Bank Code of Conduct will give greater comfort to indirect participants, including TSB. Sponsor Banks will have to be clearer on their commitments to providing access and their expectations of the Indirect Bank. The Code of Conduct needs to be quite prescriptive around data requirements, data usage and how the Indirect Bank's payment information is managed e.g. volume and value passed through system Operators.

We agree with the approach being taken by the PSR on Technical Access, however, we support the continued industry developments into technical access and look forward to seeing how the Market Review into the supply of Indirect Access will seek to investigate whether there is a need to be more prescriptive in a technical access solution.

TSB BANK PLC

Summary

In summary, we agree with the broad principles and objectives the PSR is seeking to achieve through the consultation paper, which are designed to improve industry behaviour and promote a world-class payment system in the UK.

We welcome the proposals made in the consultation paper and believe they are the appropriate areas to focus to help encourage competition and innovation, which is in the interest of end-users and will benefit banks, like TSB, who welcome competition and challenge.

Should you have any further questions, please do feel free to get in touch.

Yours sincerely

Neeta Atkar
Chief Risk Officer, TSB

UK CARDS ASSOCIATION

UK CARDS ASSOCIATION

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Payment Systems Regulator: A new regulatory framework
for payment systems in the UK

Response from The UK Cards Association

12 January 2015

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Authors:

Richard Koch

Briony Krikorian-Slade

The UK Cards Association (UK Cards) is the leading trade association for the card payments industry in the UK. Its members account for the vast majority of debit and credit cards in the UK, issuing in excess of 55 million credit cards and 86 million debit cards, and cover the whole of the payment card acquiring market. UK Cards promotes co-operation between industry participants in order to progress non-competitive matters and seeks to inform and engage with stakeholders to advance the industry for the ultimate benefit of its members' consumer and retail customers.

Our response to the April 2014 ['Call for Inputs'](#) sets out the industry's perspective on the extent to which the card payment industry is currently meeting the Payment Systems Regulator (PSR) objectives of competition, innovation and service-user requirements. This response focuses on the role the new PSR could helpfully play in the payment systems landscape in the UK. We have only included responses to questions relevant to the card payments industry, and have not responded specifically to any cost benefit questions.

Executive Summary

- The UK Cards Association is supportive of the aims of the Payment Systems Regulator (PSR) and the positive role that it can play in helping the UK industry to maintain its leading position in payments globally. We believe the PSR can provide a focused and impartial view on how the payment system network should operate across the UK. However, it is important it maintains the following key principles of good regulation in doing so.
- **Proportionate and avoiding unintended consequences.** Various changing layers of regulation apply to different parts of firms' activities, adding to cost. In addition, in card payments an incoming low interchange environment may reduce funds for investment in innovation, security and free banking services. The PSR should carefully consider imposition of further regulatory costs, which could restrict the ability of the UK industry to invest in its competitive features and future infrastructure. The PSR needs to consider payment systems as a whole, rather than looking at parts in silo, and recognise that changes will have consequences across systems. In particular, the PSR should ensure that regulatory burdens do not disadvantage smaller or niche players where disproportionate requirements may ironically put them at competitive disadvantage.
- **Impartial and evidence-based.** The PSR can help payment providers, retailers, consumers and other stakeholders by providing a balanced and impartial view on what is appropriate for the UK industry. It is likely that this will require the PSR to be the ultimate owner of strategy setting, based on a

thorough evidence base and cost-benefit analysis. For example, the PSR's vision of achieving '*world class payment systems*' needs to be supported by robust comparative analysis, benchmarking the UK against other countries and against other industries. Future regulatory requirements should be subject to proper impact assessment where the benefits for certain customers are clearly evidenced and balanced against the costs of delivery; especially as these costs will ultimately be borne by end users. It is also vital that the PSR provides a view that is independent from political influence, and has the long-term interests of the industry and its service-users at heart.

- **Supporting practical, industry-led innovation.** While it is important to encourage a range of innovative products fitting customers' needs, the pace of change in payments so far has reflected the need for resilience, security and consumer trust. Global card schemes themselves are a product of a huge collaborative effort from numerous parties to deliver the standards, rules and technical infrastructure to support a ubiquitous payment product. There is already a high level of innovation in the UK payments industry, which in part has resulted from a flexible regulatory regime, and the PSR should aim to ensure that this continues. The PSR and the proposed Payments Strategy Forum could help set high level principles for innovation and review progress against them, but ultimately the industry needs to lead development and implementation of innovative products.
- **Regulatory delineation.** Within the complex UK/EU regulatory framework the PSR can help make sense of regulation for firms, especially smaller firms, and can help inform and shape relevant regulation to the benefit of the UK industry and consumers. This requires a clear understanding of how its role fits with the other UK regulators, and we would encourage the PSR to prioritise conclusion of the Memoranda of Understanding. There also needs to be a clear delineation in practice between how the FCA operates as a conduct regulator, considering the activities of individual firms, and how the PSR operates as an economic regulator, with regard to the underlying industry conditions and the need to create regulatory certainty that will allow the industry to continue to attract investment.
- **Assisting collaboration with other industries.** A world class payments system needs to be developed in coordination with strategy for relevant industries such as retailer, telecoms, transport, and fintech. The PSR can add huge value through acting as a 'broker' with firms, regulators and associations from these industries, which are increasingly central to future developments.

Regulatory approach

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

- We support the proposed approach of the PSR to be proportionate and effective, avoid unintended consequences, and to be deliberate, transparent and predictable.
- Various changing layers of regulation apply to different parts of firms' activities, adding to cost; sometimes significantly such as the security requirements in the European Payment Services Directive 2. The PSR should carefully consider imposition of further regulatory costs, which could restrict the ability of the UK industry to invest in its competitive features and future infrastructure. This could in turn undermine customer and retailer protection features of card payments that sit over and above legal requirements, such as the chargeback protection for consumers or the payment guarantee for retailers.
- The PSR needs to consider payment systems as a whole, rather than looking at parts in silo, and recognise that changes will have consequences across systems. In particular, the PSR should ensure that regulatory burdens do not disadvantage smaller or niche players where disproportionate requirements may ironically put them at competitive disadvantage.
- The PSR has been set up to operate as an economic regulator, focusing on underlying industry conditions. There needs to be a clear delineation in practice between how it operates and how the FCA operates as a conduct regulator, considering the activities of individual firms. Arguably, the high level Principles that the consultation paper proposes are more similar to those used by a conduct regulator than rules that an economic regulator would use. Pursuing an economic regulatory approach, rather than a case by case approach to individual firms, should create a level of regulatory certainty that would allow the industry to continue to attract investment. This is just as important in the payments industry as in former state-run industries.
- Payment schemes are global in nature and have been designed around strong global interoperability principles. The PSR should therefore be alert to the fact that a divergent UK approach to payment regulation or innovation could have significant adverse impacts on these principles. These principles underpin the provision of products that allow UK consumers to transact internationally in any currency, while providing them with unparalleled

consumer protection if the retailer accepting the card payment does not fulfil its contractual obligations.

- We welcome the approach the PSR is taking to be a regulator that works alongside the industry. However, we see a difficulty in firms adhering at all times to the ‘no surprises culture’. Inherently there is difficulty in giving the regulator information on upcoming developments which are typically commercially sensitive until launch, especially when the PSR has an obligation of transparency to service-users, such as through its statutory Panel. It will also be difficult for firms to know the extent to which something is considered a ‘significant’ development. A pragmatic approach is needed.

Strategy

SP2-Q1: *Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council’s or a successor body’s role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in Supporting Paper 2: Payments industry strategy and areas for collaboration? If you disagree with our proposed approach, please give your reasons.*

SP2-Q2: *Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.*

- We support Option 1. We believe that the Payments Strategy Forum should be responsible for agreeing the high-level industry strategic objectives and outcomes, with the industry developing and co-ordinating a collaborative plan to design and deliver these objectives. However, we believe that Option 1 should be explicit that the outlined approach includes:
- **The PSR owning the vision.** We believe there is a tension between the PSR stating that strategy development by the industry was insufficient in the past, and yet relying on the collective evolution of strategy for the future. If the PSR is to ensure delivery against the vision for world-class payment systems, then arguably it needs to exercise sufficient control over how strategy is developed and set. This is important not least as there is likely to be difficulty in reaching consensus on strategy, with widely differing needs from different payment users; and the liaison that will be required with players from other industries. A lack of clarity over strategy could slow down or prevent investment in the industry. By comparison, Ofcom, which arguably

oversees the industry most similar to payments with various different networks and players, sets out its strategic priorities based on consultation with stakeholders, but nonetheless takes ownership of these and sets them out clearly in its annual plan. We believe the PSR should be clear that it will be the ultimate arbiter of decisions.

- **The PSR taking accountability for ensuring that there is a clear rationale and cost benefit analysis for a proposed development.** We are concerned that the Forum developing strategy without robust underpinning analysis might not result in outcomes that automatically benefit consumers. By analogy Ofgem, which operated a number of service-user groups through its ‘Consumer First’ programme, nonetheless failed to prevent industry dynamics that were found not to be in the interest of service-users.¹ Ofcom meanwhile conducts an in-depth market review on latest developments to inform its annual strategic priorities. We therefore believe that the PSR should have responsibility and accountability for ensuring that strategic direction is underpinned by clear, empirically based rationale.

As mentioned in the consultation paper, public bodies in other countries (the Reserve Bank of Australia, and the Federal Reserve System in USA) take more of an Option 3 approach, namely setting strategic priorities for the industry, based on analysis of gaps and opportunities, and using research, conclusions and stakeholder feedback from consultation processes. While we agree that the conditions in the UK do not necessitate the PSR setting the strategy to the same extent in the UK, we believe it should take the same robust analytic approach.

- We suggest the PSR should use the following tools to inform strategy-setting:
 - Wide-scale and in-depth consumer research. Consumers should continue to decide what works well for them and demonstrate this with their purchasing decisions.
 - Market and technological research. Options for delivery should not be limited to those that are presented by representatives on the Forum/working groups.
 - Overview of regulatory and standard developments internationally, and particularly in Europe. If the PSR’s aim is to grow competition it

¹ See https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/48134/2151-ofgem-review-final-report.pdf for more information.

will presumably want the industry to be open to European providers, which will require a level of European interoperability.

SP2-Q3: *Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?*

- In addition to our comments above, we believe there are further considerations to take into account in terms of constitution and governance of the Forum and related working groups.
- It may be difficult to gather sufficient representation of service-user views. The views and preferences of retailers are often used as a proxy for those of consumers, but they have divergent needs. Consumer representative groups can have particular views that are not necessarily reflective of the average person on the street; and in any case will not reflect the range of demographics that use payment systems.
- It is as yet unclear whether the supporting working groups will be established by the PSR or by other bodies. If they sit outside the PSR's remit, it is questionable how they will have sufficient accountability to the Forum and how outputs will feed coherently into the PSR's strategy. We suggest that any working groups have a clear remit provided by the PSR, in consultation with the Forum.
- There is a question over resourcing of the Forum and the working groups. It seems unlikely that people of the requisite level to steer strategy would be able to meet every 6-12 weeks. In terms of the working groups, to produce cost-benefit analyses and outputs within reasonable timescales and that are consistent across the groups, it seems likely that the PSR would need to both prepare discussion papers for the groups, and collate the outputs.

SP2-Q4: *Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.*

- Standards are key to ensuring interoperability and the PSR can play a vital role in managing the competing standards and protocols coming out of Europe and the USA. The PSR should lead standards discussions with its counterpart regulators and the European Commission, and use the Forum and relevant working group to develop or test proposals that are made at an international/European level.

- The UK currently inputs to global bodies like ISO and EMV, (for example, through the UK Cards Association) which have a direct relevance to the PSR's strategic objectives for the UK. Domestic innovation will often require a global platform; for example, EMV was the direct result of UK lobbying of the card schemes and a pre-requisite for the national Chip & Pin programme.
- Another area for strategic development is in liaison with other industries in the UK. A world class payments system needs to be developed in coordination with a clear strategy for relevant industries, such as such as retailer, telecoms, transport, and fintech. For example, until recently there was limited availability of Near Field Communication (NFC) technology in mobile phones, which was proving a disincentive to implementation of NFC terminals in retailers. The PSR could work with Ofcom and relevant trade bodies such as the GSMA to find a mutual framework that could be made public for MNOs and financial firms to buy into. Another example is transit operators and card schemes looking to roll out contactless cards without a clear and coordinated national strategy, where there is a clear consumer benefit to having a homogenous customer experience. At the moment, individual operators are having discussions with individual card firms, without much strategic direction from the Department for Transport, leaving a potential patchwork of systems across the UK.

Ownership, governance and control

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

- We agree that service-user views should be taken into account in developing new products in the payments industry; indeed the card schemes (and issuers and acquirers) will for the most part already have consumer and retailer consultation built into their product development processes.
- However, there may be difficulties with having service-user representation directly on card payment boards. There are difficulties with this given the need for internationally interoperable systems, which requires decision-making often at a global level. There also will be natural commercial tensions between service-users and the card payment schemes, which could make reaching decisions at a board level challenging. Equally a card company may wish to take a risk backing a specific commercial proposition based on

previous experience, while a service-user representative might take a divergent view. The often-cited example of this is the bringing to market of the smartphone, which on customer testing had little success but has led to the iPhone prototype revolutionising the telecoms market.

- Card schemes already have various service user forums whose remit could be strengthened to feed into board strategy more formally.

SP3-Q4: *Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.*

- There will be a need to ensure that service-user representatives are held to a similar level of account as other directors on boards, including resolving any conflicts of interest.

SP3-Q6: *Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.*

- We support increased transparency in how Operators develop strategy. However, we think there are strong commercial and likely legal reasons why asking global profit-making Operators to publish minutes would be difficult, and in any event would probably not reveal much information once redacted.

Access

SP4-Q3: *Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.*

- In our view, access is key to structuring an environment that will allow innovation to flourish. In particular, we support the publication of access requirements and steps to increase the ease of access to payment systems.
- International card scheme access is complicated because of firms' ability to operate in other Member States under EU passporting regulations. An authorising bank in one country may have lower standards than the card

scheme operators' standards for resilience. For example, the card schemes had to deal with the outcome of various Icelandic bank insolvencies.

Interchange fees

SP5-Q1: *Are there other matters regarding interchange fees that you think we should consider at this stage?*

- Interchange fees are an important component of card payments, ensuring a fair funding balance in the card ecosystem between card companies and retailers, and playing an important role in assisting with the investment necessary to keep electronic payments secure, reliable and convenient.
- The changes that will result from implementation of the EU interchange regulation will have significant impact on the industry and reduce the contribution that retailers make to investment in innovation and security measures. It will be interesting for the PSR to assess the impact of interchange changes on consumers once they have had time to take effect.
- Under the proposed legislation the PSR is likely to be assigned responsibility for determining whether a lower fee should apply for domestic debit transactions than that prescribed by the regulation. As set out, the proposals will already result in a significant reduction, the impacts of which are not yet fully understood. We would encourage the PSR to be careful when considering any variance that goes beyond the regulation, especially as the Commission has indicated that the interchange fee cap will harmonise interchange fees across the EU.

Regulatory tools

SP6-Q1: *Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.*

- Please see previous comments on economic versus conduct regulation.
- Within the complex UK/EU regulatory framework the PSR can help make sense of regulation for firms, especially smaller firms, and can help inform and shape relevant regulation to the benefit of the UK industry and consumers. However, this requires a clear understanding of how its role fits

with the other UK regulators. For example, it will be necessary for the PSR to work closely with the Competition Markets Authority (CMA) on initiatives such as the review into current accounts; and the Financial Conduct Authority (FCA) in relation to Project Innovate. Additional information would be helpful on how the Memoranda of Understanding will operate between relevant regulators, to help the industry understand the regulatory role which will be carried out by the PSR.

SP6-Q9: *Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.*

- Given the experience of regulators in other relevant industries, the PSR should be cautious about getting involved in commercial disputes. Ofcom's intervention in disputes, for example, has resulted in a significant backlog of cases and has placed a huge burden on the regulator's resources. Instead, it would be preferable for the PSR to consider the themes of any disputes and whether it should develop a general approach based on these. Alternatively clear guidance should be provided on the scope of disputes which may be considered by the PSR.

SP6-Q11: *Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.*

SP6-Q12: *Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?*

SP6-Q13: *What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?*

- As with previous comments, we think a good place to start with penalty setting is the approach that other economic regulators take. The main UK economic regulators have a maximum penalty of 10% of global turnover set in statute (though this will always be with a view to proportionality to the offence).

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Hannah Nixon
Managing Director
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12 January 2015

Dear Hannah

Payment Systems regulator (PSR): A new regulatory framework for payment systems in the UK Consultation Paper (PSR CP14/1)

We welcome the opportunity to respond to the Payment Systems Regulator (PSR) consultation: *A new regulatory framework for payment systems in the UK*.

As a medium-sized challenger bank, we rely on the large banks for access to some payments systems. Whilst we are direct members of Bacs, LINK, Visa and MasterCard, we rely on agency agreements to secure indirect access to Faster Payments, CHAPS and C&CC.

We have been very supportive of the establishment of a new Payment Systems Regulator. We have previously stressed the importance of examining the extent to which the large incumbent banks, which are the principal users of the systems, but also co-operate as the principal owners, have, or could, create barriers to entry and expansion through:

- their membership requirements for the major payment schemes; or
- through the terms and conditions on which they offer indirect access to those schemes.

We view access to payment systems as a key issue holding back competition in UK retail banking, especially in the personal current account market. So we welcome the fact that this issue forms a central part of the PSR Consultation Paper, given our very real interest in the UK payments system being opened up and it made easier for a wider range of parties to access the payments systems.

We are also very supportive of the broad thrust of the PSR's proposals on access to payment systems and on the governance of payment systems. We comment further on these and other matters in our responses to specific questions in the Supporting Papers.

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We note that the FCA is currently reviewing the effectiveness of the CASS and has, alongside this, commenced a study of the costs and benefits of Account Number Portability (ANP). We strongly supported this particular recommendation from the Parliamentary Commission on Banking Standards and are pleased that the PSR will play a central role – working together with the FCA – in taking this work forward.

We believe that the proposals in the Consultation Paper represent an extremely important step forward. However, we believe that adding ANP to the policy mix would amplify the proposals in terms of creating a more effective and dynamic payment services for consumers in the UK.

We believe that ANP is essential to increase competition in the banking sector and, in particular, in the very important personal current account market, as well to bring improved product choice and value to customers, and a much easier, faster and more reliable switching service.

This would be achieved by creating a central portal which would hold bank account numbers at customer level (not by banking institution) – much like national insurance or mobile phone numbers. Each centrally-held account number would control a customer's transactional process, with banking providers linking their products to the central service.

ANP would create a much easier, faster and more reliable switching service. However, importantly for Virgin Money, ANP would also significantly reduce the barriers to entry and expansion for smaller banks associated with the very considerable IT requirements necessary to enter the market. It would also reduce reliance on the agency banking model.

There could also be financial stability benefits associated with a move to portability which should be explored further. The ability to switch customer funds easily and centrally to a "safe haven" could help mitigate the risk of bank runs and ensure customers gain quick access to deposits in the event of bank failure.

We note that many of the large incumbent banks continue to be sceptical about account number portability, and often argue that the cost would be prohibitive. However, our suspicion is that their opposition to account number portability is primarily motivated by their concern that such a portal would act as a catalyst for a new banking model that would reduce the stranglehold of the large incumbent banks on the UK retail market.

We suggest that work should be undertaken to establish the true cost of account number portability, which will, of course, depend on how we transition to such a framework. For example, we could envisage a phased approach towards moving to ANP. However, it is worth noting that the cost of the new infrastructure could be significantly defrayed through cost efficiencies which would result from developing an infrastructure where anti-money laundering checks, PEPs and sanctions checking could take place centrally on an industry wide basis.

So, in summary, we would reiterate our support for a dual track approach to payment systems, namely, for a comprehensive examination of the costs, benefits and technical feasibility of ANP to take place alongside the implementation of the broad thrust of the PSR proposals in this Consultation Paper. We believe that such a solution would successfully

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address problems with payment systems and help create a more competitive and innovative retail banking market.

I attach our responses to the questions in the Consultation Paper on matters of particular importance to Virgin Money – Indirect Access, Direct Access, governance and ownership and strategy and collaboration. Our responses can be summarised as follows:

On Indirect Access to payment systems

- We strongly support the proposal to encourage the development of Technical Access solutions (TAS) which could enable PSPs to gain access to payment systems through a new form of Indirect Access, crucially with direct technical connectivity which could be particularly important in terms of gaining access to FPS;
- We note the suggestion that such Technical Access solutions could support a 'common utility' which would make it easier for new PSPs to gain access to multiple payment systems and which could support a move to account number portability. We would urge the PSR to examine this as part of its work on account number portability;
- We welcome the proposals to require sponsor banks to publish certain access-related information, to encourage the industry to develop an Information Hub and to work with the industry on the development of a PSR-approved Sponsor Bank Code of Conduct. These proposals should make it easier for new or small PSPs to understand the Indirect Access market and to negotiate access arrangements, whilst the Code of Conduct should provide reassurance about certainty of supply and support;

On Direct Access to payment systems

- We support the proposal that Operators of Bacs, C&CC, CHAPS and FPS should be subject to an Access Rule;
- We support the proposal for a requirement that all Operators report to the PSR on compliance with the relevant Access Rules applicable to them annually;
- We also note that the PSR refers to a number of areas where payment systems are reviewing current arrangements with a view to increasing the ability for PSPs to gain access to them. We support them and, in particular, consideration by C&CCCL of allowing sort code portability in relation to cheque processing;
- We also believe that the PSR should examine differences in Access Requirements between payment schemes which serve to increase the cost and complexity for PSPs seeking Direct Access to multiple payment systems which the PSR has itself acknowledged is an issue.

On governance and ownership

- We support proposals to improve the governance of payment systems through requiring that service-users are appropriately represented in decision-making, addressing conflicts of interest and the introduction of a requirement for board minutes and votes to be published;
- We believe that the PSR must seriously examine consideration the ownership of payment systems, given that such banks may gain significant advantages from their dominant position within the payment system and the personal current account

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market. We suggest that the PSR should produce a further paper setting out different alternative ownership options and the pros and cons of each approach.

On Payments industry strategy and collaboration

- We agree with the intention to establish a Payments Strategy Forum, including service-users and infrastructure companies as well as Payment System Providers, Payment System Operators and the PSR and other regulators. However, we believe this Forum should not be in charge of setting strategy. Instead, we would support an approach where the PSR is in clear charge of setting strategy, with the Forum taking on an advisory or consultative function.

We appreciate the considerable volume of work which the PSR has done in a short period, and the many constructive proposals that it has made, to address shortcoming which, we believe, have limited competition and innovation in payments and in current accounts. We would be happy to meet you to expand on our responses and discuss matters further.

Yours sincerely,

Jayne-Anne Gadhia
Chief Executive Officer
Virgin Money

Questions in relation to our proposed regulatory approach (see *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

1. We appreciate the considerable volume of work which the Payment Systems Regulator (PSR) has done in a short period to produce a series of papers which not only set out a comprehensive analysis of matters relating to UK payment systems but also make many constructive proposals to address shortcoming which, we believe, have limited competition and innovation in payments and in current accounts.

2. We agree with the broad thrust of the regulatory approach set out in the consultation and Supporting Paper 1, including the PSR's expectation of a "no surprises" culture, and the approach to using its powers. However, as we outline in paragraph 57 of our response to the questions in Supporting Paper 6, we are keen for additional clarity on the interaction of the PSR's proposed regulatory framework with the existing regulatory framework for individual accountability.

3. We would appreciate it if you could make contact with us prior to the publication of either our response or covering letter.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

4. With regard to question SP2-Q1, we agree with the intention to establish a Payments Strategy Forum, including service-users and infrastructure companies as well as Payment System Providers, Payment System Operators and the PSR and other regulators (2.111).

5. Of the three options for the formation of payments strategy put forward in Supporting Paper 2, we think that Option 2, under which strategy would be set by the Payments Council or a successor industry body (2.94) is less credible, noting previous outcomes such as the implementation of Faster Payments and mobile payments, the decision to abolish cheques and the initial proposals for charging banks for CASS switches.

6. That being said, the Payments Council has a good record recently in terms of programme managing and implementing change (such as CASS) as well as sourcing the required funding from industry participants. Any changes to the organisation of the payments industry should not reduce the industry's capacity for change, or reduce incentives to make appropriate changes in order to benefit customers. We see an important role for the Payments Council in implementing collaborative changes (as is recognised in paragraph 2.24).

7. We support the objectives set out in support of Option 1, under which the PSR will lead the strategy-setting process, in areas where strategic development and innovation require collaboration (2.87-2.88), by launching a Payments Strategy Forum for industry participants and service-users (2.83), supported by a secretariat provided by the PSR (2.85) and with working groups developing proposals at a more detailed level (2.89).

8. However, we think that the Payments Strategy Forum will be too large a group to accommodate all the interested parties set out on the chart in paragraph 2.111. In light of the difficulty of gaining agreement amongst such a large group, and to avoid unnecessary delays, we think that Option 3, under which the PSR would determine high-level priorities for payments and would impose directions on participants to achieve these priorities (2.98), would be a preferable approach to setting industry strategy. We are also interested to learn from the Annex about the approach in various countries including Australia and the United States (2.99), and consider that while these countries may have an acknowledged need for certain developments

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(2.100), gaining consensus on strategy in the UK would by no means be assured without the regulator setting high level direction.

9. In practice, various operational matters have to be addressed, as recognised in questions SP2-Q2 and SP2-Q3, in ways that ensure that the Payments Strategy Forum does not become unwieldy and bureaucratic, and that it does not duplicate aspects of the PSR:

- Forum: As mentioned above (in our paragraph 7) we think that the Payments Strategy Forum will have to be quite large, to accommodate all the interested parties set out on the chart in paragraph 2.111. We therefore suggest that the Forum should be regarded as an advisory body rather than an executive body, with the PSR retaining responsibility for strategy but taking proper account of input from the Forum. We also suggest that, to avoid duplication or even conflict between the Forum and the PSR, the chair of the Forum should be a senior member of the PSR rather than an independent person.
- Working groups: With the Forum meeting only every 6 to 12 weeks, there is a danger that progress by working groups will not be properly managed and/or that there may be some drift between meetings. We therefore suggest that each working group should be led by a member of the PSR, preferably with experience in strategic development, and that the working groups should report to the PSR, while updating the Forum on progress at each meeting and putting forward all fully-worked proposals for consultation with all members of the Forum. We also prefer the term "Task Force" to "working group" since it implies a greater sense of urgency and because the OFT-led Task Force on Faster Payments demonstrates a successful model that can be replicated.

10. We note the intention of the PSR to convene a working group to develop terms of reference for the Forum (2.109), and the subsequent message from the PSR, dated 22 December, inviting expressions of interest to participate in the Working Group, describing relevant experience and expertise and the contribution that interested parties believe they could make to the development and design of the Forum.

11. To ensure openness and inclusiveness, we suggest that the PSR should take account first of the feedback they receive to questions SP2-Q2 and SP2-Q3, and then issue its final proposals on the governance and terms of reference of the Forum for a short period of consultation with all interested parties.

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12. With regard to question SP2-Q4, we have referred to Account Number Portability and related matters in our covering letter to this response. We believe that the PSR and the Payment Strategy Forum should examine Account Number Portability as part of its work agenda.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems for more details*)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give

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reasons.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

13. With regard to question SP3-Q1 and Q2, we support the proposals set out to improve the governance of payment systems by requiring that service-users are appropriately represented in decision-making, addressing conflicts of interest and requiring board minutes and votes to be published, and by requiring Operators to report to the PSR annually on their compliance with its service-user direction. We think that the costs and benefits seem reasonable.

14. With regard to questions SP3-Q3, Q4, and Q5, we support the direction set out on Interbank Operators requiring all reasonable steps to be taken to ensure that any individual acting as director of that Operator must not simultaneously act as a director of a Central Infrastructure Provider. Again, we think that the costs and benefits seem reasonable.

15. In paragraph 53 of 'Changing banking for good', the Parliamentary Commission on Banking Standards said, in June 2013, "The Government's proposed reforms will, however, continue to leave ownership of the payments system largely in the hands of the large incumbent banks. Continued ownership of the payments system by the large banks could undermine the proposed reforms, in view of the scope such ownership gives them to create or maintain barriers to entry. The Commission therefore recommends that the merits of requiring the large banks to relinquish ownership of the payments system be examined and that the Government report to Parliament on its conclusions before the end of 2013."

16. We regret that more consideration has not been given to the ownership of payment systems, given the widespread perception that in the UK an effective oligopoly of large banks gains significant advantage from their dominant position in payment systems and current accounts. As a result, new entrants and smaller banks face significant barriers to entry and expansion, particularly in these areas which enable banks to establish long-term relationships with their customers and to cross-sell other products.

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17. Paragraph 3.45 in Supporting Paper 3 says that, "Some stakeholders believe decisions are made in the interests of Direct PSPs, rather than other service users. Some stakeholders expressed their views that the governance arrangements for Interbank Operators operate as a closed shop or are bank-centric. These views echo those from the Child Report and the Cruickshank Report as well as the OFT's Payment Systems Task Force."

18. In Supporting Paper 3, reasons given to support the PSR's view that no proposals regarding ownership are necessary at this stage include:

- in paragraph 3.22, the view that, under different ownership, prices might be higher than if the payment systems continue to be run as not-for-profit entities, controlled and owned by the larger PSPs. However, owners with commercial incentives may reduce costs through efficiency savings and/or increase income through innovation - and this has been the case for the privatisation of utilities, within a regulated framework including price controls to protect consumers. Also, in Supporting Paper 3, paragraph 3.8 says that the Cruickshank Report noted that in some other 'shared utility' industries there had been a trend away from mutual governance arrangements, and footnote 2 quotes views expressed in the Cruickshank Report about drawbacks in mutual governance arrangements in payment systems, which will be only partly addressed by the establishment of the Payments Strategy Forum.
- in paragraph 3.125, reassurances given to the PSR by directors employed by PSPs that they act in the interest of the Operators first and foremost. However, these reassurances about employees of the large banks properly handling conflicts of interest do not carry much weight, given that the same large banks have clearly failed to do so in matters including LIBOR manipulation and derivatives mis-selling.

19. As a consequence of the concerns over ownership, and the possibility that banks may gain significant advantages from their dominant position within the payment systems and the personal current account market, we would suggest that the PSR produce a further paper setting out different alternative ownership options and the pros and cons of each approach.

20. With regard to questions SP3-Q6, Q7, and Q8, we agree with the PSR's proposed direction relating to board minutes, and see no reason for these published minutes not to include a record of votes and reasons for decisions made. We think that the costs and benefits seem reasonable, and agree with the proposed approach in relation to Payments Council reserved matters.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

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SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

21. With regard to question SP4-Q1, we agree that Operators not subject to Part 8 of the PSRs 2009 - Bacs, C&CC, CHAPS and FPS - should be subject to an Access Rule that is aligned with Principle 18 of the CPSS-IOSCO principles (4.123), which says that, "A financial market infrastructure (FMI) should have objective, risk-based and publicly disclosed criteria for participation, which permit fair and open access."

22. Of the three options suggested for the Access Rule, we prefer Option 1: "An Operator should have objective, risk-based, and publicly disclosed Access Requirements, which permit fair and open access." We prefer it because it follows Principle 18 and because it covers the key points in a way that is short and easy to remember.

23. However, in Option 1, we suggest that "proportionate" might be more appropriate than "risk based", because 'risk-based' has a particular meaning for bankers in the context of the Basel regulations, and because some requirements, such as the CHAPS requirement to provide a legal opinion (4.70), are not risk-based. Also, we suggest that some of the longer text in Option 2 might be incorporated in brief guidance to ensure proper understanding of the Access Rule.

24. With regard to question SP4-Q2 and Q3, we agree that all relevant pan-GB Operators, including those not subject to Part 8 of the PSRs 2009, should be subject to a Reporting Rule that requires them to:

- publish their Access Requirements, at a minimum on their website, and to provide the PSR with a copy and a link to the relevant website (4.157); and to
- provide the PSR with an annual report on compliance of their Access Requirements with relevant regulatory access obligations, and to inform the PSR of any material changes to their Access Requirements (4.153).

25. With regard to question SP4-Q4, we think that the costs and benefits identified for the Access Package seem reasonable.

26. In relation to Direct Access, we note in Supporting Paper 4 a number of areas where payment systems are reviewing matters with a view to improving access to them:

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- The Operator of Bacs is considering whether it is necessary for PSPs to be authorised credit institutions (4.45).
- CHAPS Co is considering whether to adopt a more risk-based approach, under which smaller PSPs may face less onerous technical and operating criteria and requirements (4.54).
- The Operators of Bacs and FPS intend to introduce pre-funding arrangements as a new means of managing credit and settlement risk, in a move away from loss-sharing arrangements that would make Direct Access to Bacs and FPS more attractive for smaller PSPs (4.71).
- C&CCCL is considering options to allow sort code portability in relation to cheque processing (4.91).

27. Also, separately from Supporting Paper 4, Faster Payments' recent White Paper 'A Vision for a New Access Model' puts forward a target operating model that would allow more PSPs to access FPS and offer real-time online payments to their customers.

28. We welcome the initiatives set out in paragraph 25 above - particularly the last two, relating to pre-funding of BACS and FPS, and for C&CCCL to allow sort code portability in relation to cheque processing, since they may address the two specific problems we have experienced with access to payment systems. However, we consider it important that the PSR ensures that these initiatives are finalised and implemented in ways that achieve the objective of making access easier.

29. These initiatives show good intent by the Operators of payment systems in reducing the burden of Access Requirements for smaller PSPs. However, it remains the case that differences in Access Requirements between payment systems (illustrated in paragraphs 4.33 to 4.75 of Supporting Paper 4) increase the cost and complexity for any PSP seeking Direct Access to multiple payment systems, as noted in paragraph 4.30.

30. We suggest that efforts should be made to harmonise Access Requirements as far as possible, and that this task could be led by the PSR-led Technical Access solutions Task Force, which we suggest in paragraph 38 of our response. This matter is relevant to developing a Technical Access solution that would allow a PSP to access multiple payment systems.

31. We note that Supporting Paper 4 says that PSPs using Indirect Access are generally satisfied with the service that they receive from their Sponsor Banks

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(4.194) and that there are not widespread concerns about fees for Indirect Access (4.230). These findings are in accordance with our own experience. We have found Sponsor Banks helpful and supportive, and consider it important that Sponsor Banks are allowed to earn fair returns from providing this service, which enables smaller PSPs and new banks to avoid the costs associated with the investments that would they would otherwise have to make in systems and processes to qualify for Direct Access.

32. Despite our generally positive experience with Indirect Access, we have experienced some specific problems:

- Customer service: Our inability to offer the same levels of service in FPS as PSPs with Direct Access (4.252), and the possibility of being excluded from innovative new industry initiatives such as Zapp due to the inability to service payments in real-time – although we note the target operating model set out in the recent Faster Payments White Paper 'A Vision for a New Access Model', which we are currently reviewing.
- Certainty of supply: The inconvenience to our customers who received new sort codes and our own costs and effort, all as a result of the decision of Co-operative Bank to withdraw from providing Indirect Access to C&CC (4.23).

33. We also recognise that new PSPs, which could add to competition and choice for consumers, may suffer from information asymmetry and may find it hard to understand the Indirect Access market and to negotiate arrangements with Sponsor Banks (4.220).

34. With regard to questions SP4-Q5, Q6, and Q7, we therefore welcome the proposals to require Sponsor Banks to publish certain access-related information (4.280-4.281), to encourage the industry to develop an Information Hub (4.291-4.292) and to work with the industry on the development of a PSR-approved Sponsor Bank Code of Conduct (4.300-4.301). These proposals should make it easier for new PSPs to understand the Indirect Access market and to negotiate access arrangements, and the Code of Conduct should provide reassurance about certainty of supply and support in the event of termination by the Sponsor Bank. We note that the industry has already commenced work on producing an access Information Hub.

35. We think it better to implement these proposals in co-operation with the industry rather than by a prescriptive approach, to avoid the possible unintended consequence that Sponsor Banks become less interested in providing Indirect Access or even withdraw from providing sponsoring services, as Co-operative Bank has

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decided to do. We agree that, in the light of the requirements for Sponsor Banks identified in paragraph 4.201, new Sponsor Banks beyond the 'big four' are not likely to emerge.

36. With regard to question SP4-Q8, we strongly support the proposal to encourage the development of Technical Access solutions (4.314):

- Technical Access solutions could enable PSPs to gain access through a new form of access, with direct technical connectivity (4.263 C). This could solve our principal problem with Indirect Access - the lack of a level playing field in FPS (4.254).
- Technical Access solutions could support a 'common utility' (4.262), which would make it easier for new PSPs to get access to multiple payment systems, and could support Account Number Portability (2.114), which we think more likely than CASS to increase confidence in the PCA switching process and levels of switching in PCAs. The 'common utility' could also help with ensuring compliance with AML and sanctions requirements, which currently place burdens on Sponsor Banks (4.239) and which may lead to a reduction of the choice of Sponsor Bank available for some PSPs (4.244).
- Technical Access solutions may well be of greater interest to new banks and to alternative suppliers of payment processing services than to many existing banking industry participants.
- Technical Access solutions that provide direct access (or something close to it) at a reasonable price should enable smaller ring-fenced banks to comply with the expectation that they will be direct members of payments systems.

37. While we thought that the other proposals to enhance Indirect Access should be taken forward in co-operation with the industry, we believe that this very important initiative should not be left to the industry, because:

- existing participants, particularly the large incumbent banks, might not be sure about what Technical Access solutions would mean for them, or could even, quite rationally, see them as a threat; and
- whether intentionally or not, existing participants could delay the development and implementation of Technical Access solutions (as happened with Faster Payments and with mobile payments).

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38. On the other hand, we do not think that the PSR should take a prescriptive approach to Technical Access solutions (SP4-Q8). We consider it essential that the banking industry is properly engaged in this initiative.

39. We therefore suggest that consideration should be given to a PSR-led Technical Access solutions Task Force, along the lines of the OFT-led Faster Payments Task Force. Such a Task Force would have a single and clear focus, it could ensure that progress is being made on evaluating alternative Technical Access solutions (including those set out in 4.263) and could set realistic deadlines for implementing cross-industry Technical Access solutions that are agreed.

40. The Task Force which we suggest could also feed into the market review into the supply of Indirect Access, when it is reviewing the emergence of Technical Access solutions (4.323).

41. With regard to question SP4-Q9, we think that the costs and benefits identified for the proposed direction on Indirect Access seem reasonable, but we cannot provide additional data.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

42. We agree with the PSR on the approach of liaising with the CMA and Treasury on the implementation of European interchange regulations. We recognise that the PSR expects to investigate and take enforcement action on potential breaches of regulation in line with its aims of increasing competition and innovation in the marketplace. With regard to interchange more generally, we do not suggest any other specific actions, recognising that the market in cards appears competitive and that the costs of card transactions need to be fairly borne by the parties that use and benefit from them.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

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- SP6-Q1:** Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.
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- P6-Q2:** Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.
-
- SP6-Q3:** Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.
-
- SP6-Q4:** Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.
-
- SP6-Q5:** Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?
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- SP6-Q6:** Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.
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- SP6-Q7:** Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.
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- SP6-Q8:** Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.
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- SP6-Q9:** Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.
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SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

43. With respect to SP6-Q1, we support the proposed Principles that promote openness and transparency in all dealings with regulatory bodies and place the emphasis on individuals to conduct themselves in a responsible manner at all times. In addition, the financial prudence of those providing the payment services infrastructure is fundamental to the ongoing stability of the industry and therefore we also welcome Principle 3.

44. We agree with the PSR's proposed approach in SP6-Q2 that the PSR Principles on Relations with regulators and on Compliance should apply to all participants.

45. In relation to SP6-Q3, we note that Operators of card payment systems are already bound by CPSS-IOSCO guidelines relating to the prudent management of Business Risk. We believe that extending these obligations to Central Infrastructure Providers can only be beneficial in striving to ensure confidence amongst participants and safeguarding the reputation of the payment services industry in the wider economy.

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46. With respect to SP6-Q4, as all financial services companies regulated in the UK are bound by the Principles set out in the FCA Handbook (PRIN 2), it would be beneficial for any new regulatory principles to be aligned and consistent with other well-established industry guidance. We appreciate the differing nature and specific business relationships associated with participants in the payments services industry, but we see no reason for the exclusion of the principles on integrity, skill, care and diligence, management control, governance and the management of conflicts, that are fundamental to professional bodies throughout the UK.

47. In relation to SP6-Q5, we agree with the costs and benefits outlined in the paper associated with setting out clear expectations on individual behaviour and financial prudence.

48. We agree with the proposed approach for Objectives Guidance covered by SP6-Q6. The approach is consistent with that adopted by other financial services regulatory bodies.

49. In response to SP6-Q7, which refers to the Administrative Priority Framework, we agree with the proposed approach: the risk-based approach to regulatory oversight is in line with the current regulatory environment.

50. We agree with the proposed approach for the PSR's Powers and Procedures Guide (SP6-Q8), which is consistent with that adopted by other financial services regulatory bodies.

51. With reference to SP6-Q9, the proposals in this area relate to commercial disputes between Participants and/or Service Providers and make it clear that such disputes should be resolved by commercial negotiation between the firms as opposed to regulatory engagement with the PSR. We expect that in most circumstances disputes would tend to follow precedence due to the nature and volume of similar transactions taking place. In these circumstances the dispute resolution approach is similar to that taken by other regulators through to the use of Regulatory Decision Committees as currently adopted by the FCA.

52. We agree with the proposed approach for Super-complaints Guidance (SP6-Q10). The approach is consistent with that adopted by the other financial services regulatory bodies, for example that of the Competition and Markets Authority (CMA).

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53. We agree with the proposed approach to setting penalties (SP6-Q11), which is consistent with current regulatory practices.

54. With regard to SP6-Q12, we believe the penalty must be proportionate to the regulatory failing. Proportionality is attempted through the revenue method as this should differentiate between the sizes of entities. However, the circumstances of each individual case should not only determine the need for a financial penalty but also the level of the financial penalty. This should include the co-operation and the previous disciplinary record of the offending party. In addition, the proportionality of the fine should ensure that the integrity and security of any constituent member within the payment system is not compromised, thereby ensuring the ongoing resilience of the overall payment system.

55. In relation to SP6-Q13, we think upper limits are not appropriate. We believe proportionality of the penalty should be the objective rather than setting higher and lower limits. Indeed higher limits to fines, based on revenues or transaction volumes, could be seen as a deterrent to small or medium-sized participants and may therefore be seen as a barrier to entry, restricting the overall objective of competition that the Consultation Paper and Supporting Paper 6 aim to promote.

56. With regard to SP6-Q14, the guidance in this area differs from the current regulatory environment, primarily due to the absence of a direct link between the Payment Systems Regulator and individuals within financial services firms, as captured in the Approved Persons Regime. At present, certain individuals have a responsibility to escalate significant compliance failures to the FCA / PRA, and such individuals are key in identifying, reporting and remediating in the event of a compliance failure. They may also play a fundamental role in any dispute resolution and enforcement action procedures. The role of the individual and their responsibilities are not clearly set out in the Consultation Paper: for example, 19.4 states “a participant in a regulated payment system might also proactively approach us to disclose a compliance failure”. Under current FCA rules an approved person would be obliged to do so if the event was material or operationally significant.

57. The emphasis in the enforcement section is focussed on the corporate entity rather than the responsibility of the individual within that entity. This may reflect the nature of the payment services industry, but could lead to confusion for the individual decision-makers and material risk takers.

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58. The regulatory framework outlined in the Consultation Paper impacts firms that are regulated by the FCA but also some firms that lie outside the current regulatory framework. As such, it is unclear from the Consultation Paper how the new proposals link to the established framework on Senior Management Responsibilities. Until there is further clarity in this area we believe that some proposals put forward in the paper relating to behaviours, dispute resolution and enforcement could be undermined or misunderstood. For example, the role of the individual in raising awareness of regulatory failings or indeed the actions taken against individuals through enforcement are well established in the existing FCA framework. However, it is not clear how these will be undertaken under the new proposals. As a key objective is to introduce firms to the PSR regulatory environment that are not currently bound by the rules associated to senior management responsibilities, we believe further clarity is necessary to allow regulatory transparency across the payments Industry.

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Response to November 2014 Payment Systems Regulator's Consultation Paper CP14/1

12 January 2015

1 EXECUTIVE SUMMARY

- 1.1 Visa Europe¹ welcomes the continued stakeholder engagement by the Payment Systems Regulator ("PSR") in developing its regulatory approach.
- 1.2 Visa Europe strongly agrees with the PSR's Managing Director's opening remarks to the Consultation Paper PSR CP14/1 (the "**Consultation Paper**") that the "*way we spend, move and manage our money is changing radically driven by consumer demand, innovative business models and new technology*".² Visa Europe, as an internationally capable payment card system, has been at the forefront of these developments.³
- 1.3 UK consumers have today a wide choice of payment options. They can – and do – readily switch between card transactions (both face-to-face "card present" transactions and online "card not present" transactions), online payment schemes, bank transfers (which can be arranged in bank branches, or using "faster payments" online or via mobile apps) and cash. The sector is seeing new entry and significant growth by online players such as PayPal and mobile operators which are entering payment markets through contactless-enabled point-of-sale devices⁴.
- 1.4 Despite the significant growth in online and mobile transactions, cash continues to play a significant role in the UK. Visa Europe therefore operates in a highly competitive UK market which includes a wide and diverse range of traditional and new payment options, including among others MasterCard, American Express, PayPal, bank transfers and cash. This competition has and continues to drive investment and innovation for the benefit of both merchants and consumers.
- 1.5 Against this dynamic market context, Visa Europe welcomes the PSR's recognition that it fulfils the role of an economic regulator⁵ as opposed to a conduct regulator, such as the Financial Conduct Authority ("FCA"). Visa Europe also welcomes the PSR's acknowledgment that competition generally delivers better outcomes for service-users than collaboration (through regulation or otherwise).⁶ Visa Europe considers that these considerations are critically important in informing the PSR's development of its regulatory policy and approach. Further, the PSR together with HM Treasury must keep designation and regulatory measures under close review in light of market developments.
- 1.6 Overall the following overarching themes should be central to the PSR:
- Operate strictly within the legislative framework provided by Parliament;
 - The PSR is an economic regulator not a conduct regulator;

¹ Visa Europe is a dedicated European payment system. We assume that most of the PSR's activities will be directed at Visa Europe's business in the UK, including the activities of its national organisation, Visa UK Limited.

² Consultation Paper, page 3

³ Visa Europe refers the PSR to its submission of 15 April 2014 (attached again at **Annex 1**) in response to the Financial Conduct Authority's Payments Systems Regulation Call for Inputs and its response to the Treasury Consultation on "Opening up UK payments" (attached again at **Annex 2**). These submissions are not repeated in this response.

⁴ Supporting Paper 2, para 2.15

⁵ Draft Objectives Guidance, para 1.1

⁶ Draft Objectives Guidance, para 4.5

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- One size does not fit all, and regulation must expressly take account of this;
- A level playing field is key to supporting the PSR's objectives;
- Any intervention must be evidence based and proportionate; and
- Duplicative regulation should be avoided.

1.7 Judged against the above criteria, Visa Europe is concerned about a number of aspects of the PSR's proposals. In particular, it appears some proposals could serve to extend the PSR's regulatory remit to that of a general conduct regulator. A clear legal basis has not been articulated in relation to these proposals and there is a risk that they could displace or distort an effective competitive process with regulatory interventions that work against the interests of end-users. Visa Europe summarises its key issues and proposals below.

1. Visa Europe's concerns about the PSR's proposed regulatory approach

1.8 The PSR is an economic regulator by Parliamentary design. Everything it does must pursue the three statutory objectives of promoting competition, innovation and service-user interests (the "**Statutory Objectives**"). In doing so the PSR must have regard to 8 specific statutory regulatory principles (the "**Statutory Principles**"). The primary legal framework is clear and unambiguous.

1.9 The PSR recognises these legislative parameters in its Draft Objectives Guidelines. However, Visa Europe is concerned that this document and consequently many of its more detailed regulatory proposals do not properly take into account these Statutory Objectives and Principles. The PSR must go further in establishing the link between its policy proposals and the Statutory Objectives and Principles. To assist the PSR in this regard, Visa Europe has sought to extract a number of practical considerations which flow directly from the Statutory Objectives and Principles. These are:

- Protecting a level playing field while recognising objective differences;
- Promoting world-class UK payment systems, recognising the international dimension to aspects of the sector;
- Having due regard to prevailing market conditions, acknowledging that competition generally produces better outcomes for service-users than regulatory directions;
- Operating with a bias against regulation, ensuring that all regulatory interventions are based on robust evidence of market failures and are proportionate; and
- To keep any regulatory measures under review in light of market developments.

1.10 These considerations provide a framework for the PSR in assessing the consultation responses and developing further its regulatory approach and policies. Indeed, we would suggest that they are taken into account by the PSR whenever it considers introducing a new regulatory measure. Recognition of these considerations would also greatly increase transparency and legal certainty for all stakeholders in the UK payment systems sector.

2. The proposed PSR principles appear to go beyond the PSR's remit

1.11 The PSR proposes to adopt a number of Principles which would be legally binding on designated entities. Visa Europe has some concerns in relation to both their legal status and their substance.

1.12 The Consultation Paper does not specify the legal status of the PSR Principles. Indeed, Visa Europe considers that, as presently proposed, they appear to go beyond the PSR's powers. Further, they are contrary to the PSR's Statutory Principles, including the duty to act proportionally.

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In any event, Visa Europe considers that they should be unnecessary as they do not address any *actual* market failures.

- 1.13 The scope of the PSR Principles is broad and ambiguous. This is indicative of the PSR's wider approach to adopt "one size fits all" solutions. As a result, the PSR Principles would give rise to significant uncertainty and compliance costs for both the industry and the PSR.
- 1.14 Against that background, in Visa Europe's view the PSR must fundamentally review this proposal with an open mind in the light of the consultation responses it receives.

3. The case for a Payments Strategy Forum has not been made out

- 1.15 Visa Europe considers that the case for creating a permanent industry body has not been established; it is not clear that it is necessary or proportionate to drive collaborative innovation in the card payments sector. Such a forum would create significant costs. It would also require detailed governance and working rules to avoid being captured by individual commercial interests and to be capable of working effectively and efficiently. Instead, Visa Europe would suggest that the PSR should consider setting up framework arrangements to establish ad-hoc expert working groups with specific and time-limited objectives, to provide expert guidance to the PSR and the wider industry.
- 1.16 The PSR appears to have carried over some of the most criticized features of the Payments Council and has not taken into account best practices from other regulated sectors such as telecoms.
- 1.17 If the PSR nevertheless determines to set up a permanent industry-wide body, Visa Europe would favour Option 1⁷. Apart from the obvious need for robust governance and working rules, the status of the Forum's recommendations and decisions should be clarified.
- 1.18 Visa Europe considers that the Forum's remit should be strictly limited to an expert advisory role. Any power to impose binding outcomes on industry members would risk distorting both the competitive and the regulatory process in the UK.

4. The PSR's corporate governance proposal raises serious issues

- 1.19 Visa Europe supports the PSR's general observation that one should be cautious not to be too prescriptive in relation to the manner in which service-user views are communicated and taken into account. That said, Supporting Paper 3 appears to suggest that a new director, or an existing director, must have a specific obligation to representing service-user interests at board level (emphasis added). Visa Europe fundamentally disagrees with this proposal on the basis that it is unnecessary, unworkable and counter-productive:
- There is no evidence in the Consultation Paper which suggests that there are widely held or substantiated concerns in relation to Visa Europe's engagement with, and transparency vis-a-vis, service users;
 - Visa Europe is already subject to compelling market pressures to listen carefully to, and collaborate closely with, merchants and consumers to ensure the continued relevance of its scheme and products in a highly dynamic sector;
 - The Visa Europe and Visa UK Boards include independent directors with relevant expertise;
 - Visa Europe has a wide range of mechanisms to ensure it has continual feedback from end users including dialogue with individual retailers, retailer groups and consumer groups.

⁷

As set out in the Consultation Paper, i.e. the setting up of an industry-wide Payments Strategy Forum.

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- There are no precedents for any similar formal board representation of customers or other service-users in other regulated sectors; and
- Such a measure would give rise to potentially serious conflicts of interests which would fundamentally undermine effective governance and decision-making; the PSR will, for example, be aware of the current civil damages litigation by many merchants in relation to interchange fee issues.

5. The PSR's proposal on transparency requirements should be reconsidered

1.20 Visa Europe also has serious concerns in relation to the PSR's proposal to require Operators to publish their Board minutes. Such a proposal would in Visa Europe's view be unnecessary, disproportionate and counterproductive for the following reasons:

- The PSR has not referred to any evidence-based concerns in relation to a lack of public access to board minutes;
- Visa Europe already has extensive transparency and disclosure measures in place, which are continually evolving to meet market needs;
- It is not clear how the publication of board minutes could be reconciled with the strict requirements of EU and UK competition law regarding the treatment of competitively sensitive information;
- Such a measure would risk constraining frank and open discussions at board level, undermining the effective governance of Visa Europe to the likely detriment to service-users; and
- Visa Europe is not aware of any precedents for a similar general disclosure requirement by any other UK regulators. Indeed such regulators, as well as the PSR, already have the power to require the disclosure to them of all board minutes in unredacted form).

6. The PSR's proposals on access are unnecessary in relation to Visa Europe

1.21 Visa Europe considers that there are no material issues in relation to access to its scheme which require additional regulation to be imposed by the PSR.

1.22 Visa Europe does not object to a requirement to publish its access rules but it considers the requirement to provide the PSR with an annual compliance report is unnecessary and disproportionate, in the absence of any material concerns regarding access to its scheme. Such a compliance report would not address the very limited and narrow concerns identified in Supporting Paper 4 (observations regarding the interpretation of certain access rules).

7. The PSR's proposal on interchange fees is unnecessary considering upcoming EU legislation

1.23 As EU-wide IFR caps on interchange fees are expected to come into force in August 2015, Visa Europe considers that there is no basis for any further regulatory action by the PSR in this area.

8. The structure of Visa Europe's response

1.24 The remainder of Visa Europe's response provides further details in support of its submissions outlined above and is structured as follows:

- **Section 2** sets out Visa Europe's observations on the PSR's proposed regulatory approach and comments on the parameters set by the Act for the PSR's approach to

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regulation, including the PSR's statutory objectives and the regulatory principles specified in the Act.

- **Section 3** outlines the competitive dynamics of the market in which Visa Europe operates and explains the current economic and regulatory environments which drive Visa Europe's commercial policy and investment decisions.
- **Section 4** sets out Visa Europe's observations on the proposed Payment Strategy Forum.
- **Section 5** sets out Visa Europe's views on the PSR's corporate governance proposals.
- **Section 6** sets out Visa Europe's views on the PSR's proposals on interchange fees.
- **Section 7** sets out Visa Europe's views on the PSR's proposals on access to payment systems.
- **Section 8** sets out Visa Europe's observations on the proposed "PSR Principles".
- **Section 9** addresses Visa Europe's observations on the PSR's proposed powers and procedures.

1.25 For ease of reference, Visa Europe has also provided in **Annex 3** to this submission a high level summary of its position on each specific question raised by the PSR in this consultation exercise (including cross-references to Visa Europe's views in the main body of this submission).

2 OBSERVATIONS ON THE PSR'S REGULATORY APPROACH

- 2.1 The PSR's overall regulatory approach and each individual regulatory measure must be consistent with the spirit and the letter of the Act including, in particular, the regulatory objectives and principles set out in the Act. This section sets out certain overriding considerations ("**Framework Considerations**") which, in accordance with the Act, the PSR must have regard to when carrying out its functions and setting its policy. This section also explains how these Framework Considerations should be applied in relation to any regulatory intervention and oversight aimed at Visa Europe's activities, given the specific organisational, regulatory and competitive context within which Visa Europe operates.

Legislative parameters and overarching themes for the PSR's regulatory approach

- 2.2 Visa Europe notes that the PSR is under a statutory obligation under section 96 of the Act to provide "guidance about how it intends to advance its payment systems objectives in discharging its functions under this Part in relation to different categories of payment system or participants in payment systems." Visa Europe welcomes the draft Objectives Guidance provided in Supporting Paper 6, which aims to meet this requirement. Visa Europe in particular welcomes and agrees with the PSR's acknowledgment in that document that it is an "economic regulator" and that everything it does is (in accordance with the Act) guided by the statutory objectives under the Act (the "**Statutory Objectives**")⁸, having regard to the regulatory principles in section 53 of the Act (the "**Statutory Principles**")⁹.
- 2.3 Visa Europe considers that, as drafted, the Objectives Guidance does not take sufficient account of the Statutory Principles. In particular, Visa Europe would expect a more detailed discussion in the main body of the Guidance as to how the Statutory Principles inform its approach to regulatory policy and, where deemed appropriate, enforcement.
- 2.4 Visa Europe considers that this could effectively be done by setting out a number of practical framework considerations which necessarily flow from the Statutory Objectives and Statutory Principles. We refer to these as Framework Considerations.
- 2.5 On this basis, Visa Europe would propose that a limited number of Framework Considerations are included in the PSR's Objectives Guidance in order to provide precise and practical guidance to all stakeholders. In Visa Europe's view, these Framework Considerations should be helpful and uncontroversial, since they reflect the matters that the PSR would be required to have regard to in the proper exercise of its discretion in any event. Visa Europe would also note that the Framework Considerations set out below are not exhaustive, but rather reflect the most commonly occurring issues that could be expected to come before the PSR.
- 2.6 The PSR should then make clear in its discussion of its approach in relation to the individual Statutory Objectives how the Statutory Principles and Framework Considerations are reflected in its proposals:

⁸ As required under section 49(2) of the Act, together with sections 50-52, that is, (1) to promote effective competition in the markets for payment systems and for services provided by payment systems in the interests of service-users; (2) to promote the development of, and innovation in, payment systems and infrastructure to be used to operate payment systems in the interests of service-users; (3) to ensure that payment systems are developed in a way that considers and promotes the interests of service-users.

⁹ As required under section 49(3)(c) of the Act, together with section 53, that is to 1) utilize its resources efficiently; (2) exercise its functions proportionally; (3) encourage sustainable medium and long term growth in the UK economy; (4) acknowledge the general principle that service-users should take responsibility for their decisions; (5) have regard to the responsibilities of senior management of regulated entities; (6) where appropriate, recognize differences between different regulated entities; (7) where appropriate, publish information on, or require publication of information by, regulated entities; and (8) exercise its functions transparently.

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- Framework Consideration 1 - *Creating and/or protecting a **level playing field** for payment systems while recognising objective differences between different players.* This is necessary to advance the PSR's competition objective and flows from the Statutory Principle that the PSR should recognize differences between different payment systems.
- Framework Consideration 2 - *Promoting the creation of world-class payment systems in the UK while recognising that certain aspects of the **UK payment systems** are inseparable from their wider international regulatory and economic context.* This is necessary to advance the PSR's innovation objective and is also relevant to the other two Statutory Objectives, as intervention in the UK payment systems industry that cuts across global interoperability and the efficiency of cross-border transactions would be to the detriment of UK consumers and, contrary to the Statutory Principles, adversely affect the growth of the UK economy.
- Framework Consideration 3 - *Having due regard to prevailing **market conditions** and assessing the impact of regulatory intervention on these conditions, acknowledging that, in the absence of clear market failure, competition typically produces a more efficient allocation of resources and innovation strategies for the benefit of service-users than regulatory directions.* This advances each of the PSR's three Statutory Objectives, while respecting the Statutory Principle of proportionality.
- Framework Consideration 4 – *Operating with a **bias against intervention** and adopting **proportionate** regulatory decisions based on an **effects-based analysis** of real market failures and having regard to the extent to which such market failures are likely to be detrimental to service-users and ultimately consumers.* This advances the PSR's service-user objective and respects the Statutory Principle of proportionality as well as the Statutory Principle that the PSR should utilize its resources efficiently.
- Framework Consideration 5 - *Reviewing **regulatory interventions** over time to assess whether they remain necessary and appropriate in changed market circumstances.* Such an approach advances all of the PSR's Statutory Objectives and is consistent with the Statutory Principles of in particular proportionality and encouraging sustainable growth (by minimising compliance costs).

Application of the Framework Considerations to regulating Visa Europe

- 2.7 Visa Europe explains below (and in more detail in subsequent sections of this response) that there are specific organisational, regulatory and competitive factors that fundamentally condition its governance, investment strategies and market conduct. The PSR is under a statutory duty to justify any regulatory interventions and oversight in relation to Visa Europe by reference to these considerations.

A. Framework Consideration 1 – Level playing field and recognising objective differences between operators

- 2.8 It is a fundamental principle of EU and UK administrative law that similarly placed parties should be treated equally. This ensures the fair treatment of particular parties and avoids distorting competition between operators to the detriment of service-users, including consumers.
- 2.9 This means that it is critical that the PSR's regulatory oversight of Visa Europe does not result in providing its competitors with an undue competitive advantage. Instead, the PSR must ensure that parties offering comparable services are treated in a comparable way by its regulatory interventions. For example, Visa Europe should not be disadvantaged by regulatory constraints vis-à-vis undesignated four and three-party card systems (such as American Express and Diner's

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Club) or newer players (such as PayPal or mobile phone operators) that offer payment services which can act as effective substitutes to Visa Europe's payment services.

- 2.10 In particular, Visa Europe notes that HM Treasury's designation procedure may conclude that Visa Europe and MasterCard will be the **only two designated merchant payment schemes** for the purposes of the Act. In Visa Europe's view, any failure to designate payment schemes such as American Express and PayPal would risk giving rise to unjustified and inefficient market distortions (through regulation) which would not be in the interest of the UK economy and UK consumers. The concern of regulatory distortions is also shared by leading economists.¹⁰ Accordingly, Visa Europe has made it clear to HM Treasury that this view should be revisited and remains hopeful that it will revise its initial conclusions.¹¹
- 2.11 However, it may nonetheless be the case that other significant merchant payment schemes, such as American Express or PayPal, will not be designated. In these circumstances, any regulatory burden imposed on Visa Europe and MasterCard would clearly place these two schemes at a competitive disadvantage vis-à-vis other non-designated payment schemes with which Visa Europe and MasterCard compete.¹²
- 2.12 Visa Europe notes that in this situation, the PSR would have a particular responsibility to assess the proportionality of any regulatory burdens imposed on Visa Europe and would need to take great care to minimise any adverse impact on the ability of Visa Europe to compete effectively against non-designated competitors.
- 2.13 Further, the principle that similarly placed parties should be treated equally is reflected in the Statutory Principle that objective differences between parties must be taken into account in imposing regulation. In particular, Visa Europe's business and the competitive market it operates in as an internationally-capable card scheme are fundamentally different from the business model and competitive market context of interbank payment systems. Visa Europe is an international, open access payment scheme with a consumer brand proposition. Each of these aspects fundamentally conditions its conduct on the market. None of these aspects apply to UK interbank systems.
- 2.14 A clear recognition of this distinction between card schemes and interbank systems is required by Section 53(f) of the Act and ought to be expressly acknowledged by the PSR. It is critically important that this distinction is recognised by the PSR and that it ensures that any regulatory measures imposed on Visa Europe are appropriate and proportionate and therefore compliant with the Act.

¹⁰ See, for example, Professor Jean Tirole (2014 Nobel Laureate for Economics), "Payment card regulation and the use of economic analysis in antitrust", Toulouse School of Economics paper n° 4 - 03/2011: "A puzzle regarding the last two decades of antitrust enforcement in the payment industry is the sole focus on open systems. Such a focus tilts the industry's business model in favour of three-party systems for no clear reason. Whatever regulation (or lack thereof) one advocates, neutrality with respect to business organization should be the rule, so as to let the most efficient forms emerge."

¹¹ This approach is clearly supported by the intentions of Parliament. According to Sajid Javid, then Financial Secretary to the Treasury, "Under the new regulatory regime, HM Treasury will designate payment systems to bring them – and system participants – into the scope of the regulator's powers. Initially, the Treasury expects to designate the main inter-bank systems, the cheque clearing system and the international three and four party card systems. However, as set out in the legislation, all retail payment systems active in the UK will be in the potential scope of regulation, meaning "no-party" schemes may also be brought into the scope of regulation, if and when they meet the criteria for designation. These criteria require that the Treasury must be satisfied that any deficiencies in the design of the payment system, or any disruption in its operation, would be likely to have serious consequences for those who use, or are likely to use, the services provided by the system." (Hansard, HC Deb, 25 November 2013, c50W)

¹² It is also noted that the failure to designate operators which offer effective substitutes to the services offered by Visa Europe (such as American Express and PayPal) also distorts competition by increasing the funding burden which is borne by each designated operator in relation to the financing of the PSR's functions.

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- 2.15 In particular, given the significant competition faced by Visa Europe from Card Operators¹³ and non-card operators and the impact of EU and domestic regulation aimed at driving greater competition between Card Operators, Visa Europe needs to be able to react to changing customer preferences (including merchants and consumers). The sustained success of Visa Europe's scheme is driven by the widest possible acceptance of its scheme by all stakeholders in the supply chain, i.e. issuers, acquirers, merchants and consumers. These economic network effects (in themselves) create compelling incentives, independent of any further PSR led regulation, to protect the continued open and transparent access to its scheme and drive efficient investment in innovation. Visa Europe considers that the PSR should have the fullest regard to these fundamental features of the market in which Visa Europe operates when considering the exercise of its regulatory powers in relation to Visa Europe.

B. Framework Consideration 2 - Promoting the creation of world-class payment systems in the UK while recognising that certain aspects of the UK payment system are inseparable from their wider international regulatory and economic context

- 2.16 Visa Europe is a pan-European membership association, owned and operated by over 3,000 banks, financial institutions and payment service providers across Europe. While Visa Europe is a dedicated European payment system, responding to the needs of European service-users, it is also the sole licensee of Visa Inc. in Europe and works closely with Visa Inc. to enable the global interoperability of Visa payments anywhere in the world.
- 2.17 In order to achieve a harmonised approach to financial services regulation across the EU, the PSR needs to closely align its objectives, regulatory approach and regulatory measures, including its interventions within the market, with existing regulatory regimes in the UK and across the EU.
- 2.18 This is important for two key reasons.
- It ensures that there is regulatory consistency and legal certainty across different legislation and regulators, both in the UK and across the EU, which is a fundamental principle of EU administrative law.¹⁴ Given the PSR's concurrent competition law powers under the Act,¹⁵ and the Government's stated aim to avoid duplication of regulation, it is essential that consideration is given to how regulators interact with one another, as well as how they monitor and interpret developments at the European level. Close interaction and alignment by all concurrent regulators in the payment systems and services space is therefore crucial; and
 - It is of critical importance that the PSR avoids approaching its regulatory function in a manner which disadvantages international payment systems that operate in the UK. This would not only have a direct adverse impact on such players but also on the wider UK economy and on UK consumers. Further, it is essential that any exercise of the PSR's powers does not inadvertently undermine the operation of Visa Europe's business model in countries outside the UK as this would have an adverse effect on the overall resilience and effectiveness of Visa Europe's essential function as an internationally-capable payment scheme.

¹³ Visa Europe adopts the definition of Operators and Card Operators as set out in Annex 1 (Glossary) to the Consultation Paper. Given Visa Europe's role as a card payment scheme provider its comments in this submission are focussed on Operators and where appropriate more narrowly Card Operators, rather than Infrastructure Providers, unless otherwise specified.

¹⁴ See, *inter alia*: *R v Secretary of State for Transport, ex parte Factortame Ltd* [1991] 1 A.C. 603 (confirming the general supremacy of EU law over domestic law); *C-106/89 Marleasing SA v La Comercial Internacional de Alimentacion SA* [1991] ECR I-7321 (national law must be interpreted and applied, insofar as possible, so as to avoid a conflict with EU law); European Communities Act 1972, s. 2(1).

¹⁵ Particularly in relation to its powers under Part 4 of the Enterprise Act 2002 as provided under Section 59 of the Act.

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- 2.19 The case for a pan-European approach to regulation, particularly with regard to payment systems, is widely acknowledged; e.g. the former Commissioner for Internal Market and Services, Michel Barnier, stated in terms that *“we need a real single market in payment services, in particular online.”*¹⁶ Further, the Digital Agenda for Europe, produced by the Directorate General for Communications Networks, Content and Technology, states in relation to payment systems that *“the Commission will continue to forcefully address transformation and change of this current patchwork system to enable the development of a fully-fledged Digital Single Market”*.¹⁷ In other words, just in the same way Ofcom has to work within the common regulatory framework for electronic communications networks through the Framework Directive (2002/21/EC), the PSR must seek to harmonise its regulatory proposals with the workings of the European Commission, national competition authorities and other European regulatory bodies within the markets for payment systems.
- 2.20 In light of the above, the PSR should be mindful of both existing and forthcoming regulation that impacts (and will likely impact) designated operators, such as Visa Europe. In relation to Visa Europe, such regulation, both at the UK and EU level, includes:
- The Payment Services Directive¹⁸ (as implemented by the Payment Services Regulations 2009 in the UK); soon to be replaced by the Payment Services Directive II which contains similar provisions in relation to access;
 - The forthcoming EU Interchange Fees Regulation (the “IFR”);
 - The EU E-Money Directive;
 - The ECB Oversight Framework for Card Payment Schemes.
- 2.21 In particular, it is important that the PSR should have regard to the regulatory implications and likely market impact of the Payment Services Directive and the forthcoming IFR in designing regulatory policy that may affect Visa Europe. As the PSR is aware, Article 28 of the Payment Services Directive imposes on Member States the obligation to ensure that the rules on access to payment systems shall be objective, non-discriminatory and proportionate, and not unduly inhibit access. As explained in Section 6 below, these rules resulted in significant pan-European changes to Visa’s corporate governance structure.
- 2.22 The IFR, which has been agreed by the European Parliament and Council, and is likely to be adopted later this month (January 2015), will regulate the interchange fees payable by acquirers in the UK. The IFR also provides merchants with the flexibility to choose to accept only debit or credit cards of a scheme operator, without having to accept both (as also provided for under Visa Europe’s debit commitments agreed with the European Commission). Further, the IFR contains certain provisions which require a degree of functional separation between the operation of card and processing schemes. The IFR does not apply to specified activities of three-party payment schemes or to commercial cards.
- 2.23 The IFR caps on interchange fees are expected to come into force in August 2015 while the other rules set out in the IFR should be implemented by February 2016. These changes are expected to significantly impact the conditions of competition in the card payments sector. It is essential that the PSR takes careful account of the IFR and its market impact in the exercise of its regulatory powers,

¹⁶ Michel Barnier, Commissioner for Internal Market and Services, “Toward an integrated European market for card, mobile and internet payments”, Conference, 4 May 2012

¹⁷ DG Communications Networks, Content & Technology, The Digital Agenda for Europe – Driving European growth digitally, 18 December 2012, page 5

¹⁸ 2007/64/EC

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and avoids a situation in which regulatory intervention on a UK Member State-only basis undermines the implementation of a consistent pan-EU approach in this area.

- 2.24 The PSR will need to develop its regulatory policy in this already highly regulated international market place for merchant payment schemes in a prudent and careful manner to ensure it effectively discharges its statutory functions, in accordance with the Act's Statutory Objectives and Statutory Principles.

C. Framework Consideration 3 - Having due regard to prevailing market conditions and assessing the impact of regulatory intervention on these conditions, acknowledging that competition typically produces more efficient allocation of resources and innovation strategies for the benefit of service-users than regulatory directions

- 2.25 As the PSR is aware, Visa Europe operates a "four-party payment system" involving consumers, merchants, issuers and acquirers. Visa Europe has a direct relationship with issuers and acquirers through its membership structure. Whilst Visa Europe does not have a direct relationship with merchants or consumers, their interests are of critical importance to the development of Visa Europe's strategy. Accordingly, in order to remain relevant to them and competitive vis-à-vis other card and non-card payment systems, Visa Europe must listen to these stakeholders.
- 2.26 The dynamics of competition in the sector in which Visa Europe operates is set out in more detail in Section 4 below. However, to summarise briefly, in relation to card operators, Visa Europe's closest competitor is MasterCard Inc. Visa Europe and MasterCard compete vigorously for issuers and their respective propositions are substitutable by issuers and merchants. Indeed, there is significant evidence of issuers switching between MasterCard and Visa and, given that a single issuer can account for a significant proportion of all cards issued in a market, competition for each contract is intense. Such intense competition ensures that issuers have significant countervailing power over Visa Europe. MasterCard is therefore a significant competitive constraint on Visa Europe's commercial decision making, and Visa Europe must continually invest and innovate if it is to stay relevant.
- 2.27 In addition to MasterCard, Visa Europe also competes (among others) with three-party payment systems, such as American Express which competes directly with Visa Europe in the UK in relation to credit card payments, particularly at the higher end of the market. In addition, American Express has recently taken steps to expand its commercial offering, becoming more of a mass-market product. As noted in Visa Europe's response to the PSR's Call for Inputs of 5 March 2014, the inapplicability of the IFR to American Express's three-party scheme, coupled with HM Treasury's intention not to designate American Express under the Act, unfairly place Visa Europe at a competitive disadvantage. A distortion such as this harms competition in the long run as market success no longer depends upon which system is most beneficial to customers, but becomes dependent on which system has the least regulatory constraints.
- 2.28 Visa Europe also competes with newer non-card based entrants, such as PayPal, which operate in relation to e-commerce or face-to-face payments (or both) and has in recent years significantly expanded beyond its original ecosystem of eBay. As referred to in Visa Europe's response to the PSR's Call for Inputs, more than 90% of PayPal transactions are conducted with merchants unrelated to eBay.
- 2.29 Finally, Visa Europe competes with traditional modes of payment, such as cash and interbank transfers. In particular, the option for consumers to switch to cash payments remains a significant competitive constraint on Visa Europe, particularly given the practice of merchants to subsidise the fee for handling cash transactions. Recent developments in online and mobile banking also mean

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that interbank transfers can act as a substitute for a range of payments which can also be made using cards (e.g. payment of utility bills).

2.30 Visa Europe, therefore, operates in a competitive and dynamic market which (in contrast to interbank systems for example) is characterised by effective levels of switching by all stakeholders in its scheme, i.e. issuers, acquirers, merchants and consumers. This means that all players offering payment services solutions in this market must continually innovate to meet the evolving needs and options of service-users, including importantly consumers. As a result, the market itself creates compelling incentives for Visa Europe to act in the interests of service-users by innovating to compete more effectively in a dynamic market.

2.31 Any ex-ante regulation by the PSR may risk undermining these pro-consumer market incentives and may replace these with less efficient incentives or obligations, contrary to the PSR's Statutory Objectives and Statutory Principles. A careful factual assessment of the prevailing market conditions and clear evidence of market failure must therefore underpin any decision to impose additional regulatory measures on Visa Europe, to ensure that the PSR effectively discharges its statutory functions in a proportionate manner.

D. Framework Consideration 4 - Operating with a bias against intervention and regulation which is evidence-based and proportionate

2.32 Framework Consideration 4 can be re-cast as a practical three step process which should precede the adoption of any regulatory intervention by the PSR:

- First, the PSR must only consider intervention when markets alone do not deliver a specific Statutory Objective;
- Secondly, the PSR must collect and present evidence of market failure requiring regulatory intervention; and
- Thirdly, before imposing any specific regulation, the PSR must conclude, reflecting the relevant regulatory and market conditions, there is no less onerous measure which would adequately address the identified market failure.¹⁹

(i) Bias against intervention

2.33 The PSR has been set up as an economic regulator tasked with addressing market failures by evidence-based and proportionate regulatory measures. Visa Europe is concerned that the PSR has not consistently reflected this fundamental principle in its proposals in the Consultation Paper. This concern is further developed in Section 8 (The Proposed PSR Principles).

2.34 For current purposes it is noted that the regulatory policies and framework (including the levy of fees to cover the operational and start-up costs of the PSR) set out by the PSR and the decisions are likely to impose significant costs on designated operators and service-users (including consumers). It should therefore be a key principle of the PSR that it operates with a bias against intervention. This requires that a high hurdle must be overcome before it regulates, i.e. regulation is only seen as appropriate if the status quo fails to deliver outcomes consistent with the PSR's Statutory Objectives. It follows from this that Visa Europe considers that, before giving any direction or taking any other regulatory steps, the PSR should carry out appropriate impact assessments.

¹⁹ As Nobel Laureate J. Tirole states, "Basic economics by no means vindicates laissez-faire; market failures abound, that offer substantial scope for improvement through sensible policy intervention. But basic economics also teaches us that that policy interventions must be grounded in a rigorous treatment of several questions: what is the exact market failure and is it sizeable? Does the state have the information and the instruments to correct the failure? Will the remedy's costs be offset by sufficient benefits? Such questions should be satisfactorily investigated before enacting new regulations. The payment industry is no exception to the rule." J Tirole, (2011) op cit.

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- 2.35 As set out by the Better Regulation Task Force, "*the option of not intervening [...] should always be seriously considered. Sometimes the fact that a market is working imperfectly is used to justify taking action. But no market ever works perfectly, while the effects of [...] regulation and its unintended consequences, may be worse than the effects of the imperfect market.*"²⁰ Similarly, the Competition and Markets Authority ("**CMA**") notes in its prioritisation guidelines, "*Markets usually work well for consumers and the economy without any need for intervention, in a virtuous circle [...] The CMA only intervenes where necessary to protect competition or when it believes it can improve the way in which markets work.*"²¹ Moreover, the CMA always asks itself the question, "*Is the CMA best placed to act?*",²² before intervening, mindful as it is of alternatives such as private enforcement, action by other bodies, market developments, self-regulation or new UK or EU legislative developments.²³
- 2.36 The principle of operating with a bias against intervention has been accepted by utility regulators such as Ofcom²⁴ and has recently been reinforced by the Supreme Court decision in *BT v. Telefonica*,²⁵ where the Supreme Court held that Ofcom should avoid intervening in markets simply because particular activities "*might have adverse consequences for consumers, in the absence of any reason to think that they would*"²⁶ because this would risk "*applying an extreme form of the precautionary principle to a dynamic and competitive market*".²⁷ Visa Europe considers that an analogous common sense principle of regulatory constraint arises for the PSR under the Act.
- (ii) Evidence based regulation**
- 2.37 It necessarily follows from the above that if the PSR considers regulation necessary, it must justify such regulation on the basis of the evidence before it, consistent with the functions of an economic regulator. During the Act's passage through Parliament, the Government clearly expressed its intention to create an economic regulator and not a conduct regulator, such as the FCA. In its consultation documents, HM Treasury stated that "*the objectives of the Payment Systems Regulator will be set out in legislation separate from the FCA's existing functions, as a discrete set of objectives, duties and powers, reflecting the fact that utility regulation is a significantly different function from that which the FCA currently performs.*"²⁸ This position is expressly acknowledged by the PSR in the draft Objectives Guidance where the PSR confirms that it fulfils the function of an economic regulator, as opposed to a conduct regulator.²⁹
- 2.38 Furthermore, the PSR's Statutory Objectives of promoting effective competition in the market for payment systems,³⁰ promoting the development and innovation in payment systems for those who use such services,³¹ and ensuring payment systems are operated and developed in a way that

²⁰ Better Regulation Task Force (September 2003)
<http://collections.europarchive.org/tna/20050310232245/http://www.cabinetoffice.gov.uk/regulation/ria-guidance/content/alt-regulation/index.asp#Do>

²¹ CMA, Prioritisation principles for the CMA, CMA 16, April 2014, para 1.2

²² *Ibid.*, para 3.5

²³ *Ibid*

²⁴ See <http://www.ofcom.org.uk/about/what-is-ofcom/statutory-duties-and-regulatory-principles/>

²⁵ *British Telecommunications plc v Telefónica O2 UK Ltd and others* [2014] UKSC 42

²⁶ *Ibid.*, para 43

²⁷ *Ibid*

²⁸ HM Treasury, "Opening up UK payments: response to consultation", October 2013, para 2.54

²⁹ Draft Objectives Guidance, para 1.1

³⁰ Section 50(1)

³¹ Section 51(1)

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benefits service-users³² act as further evidence that its mandate is one of economic, not conduct, regulation.

- 2.39 The statutory scheme thus demands that the PSR carries out a careful factual, legal and economic analysis in respect of its proposed regulatory interventions. In practice, this means that the PSR must first seek to identify actual market failures, based on robust and compelling evidence. In this assessment, the PSR must not be guided by the commercial self-interest of individual market participants. Instead it must be led by the Statutory Objectives and Statutory Principles of the Act. This means that the PSR must demonstrate clearly that these market failures are likely to adversely affect the legitimate interests of service-users, including importantly consumers. Put simply, it is incumbent on the PSR to develop a robust evidence-based theory of harm before considering regulatory intervention.
- 2.40 Having identified an evidentially robust theory of harm in relation to a specified market failure, the PSR should seek to understand the causes and drivers of such market failures so as to act consistently with its statutory duties, including, in particular, promoting the legitimate interests of service-users, including consumers. Only based on a critically developed theory of harm, should the PSR contemplate regulatory interventions. Any resulting intervention ought to be designed to remedy the identified concerns in the most effective, proportionate and least distortive manner, having regard to the UK payment systems sector as a whole and in its international regulatory and commercial context.
- 2.41 By way of analogy, Visa Europe notes that the UK's principal competition regulator, the CMA, in carrying out its market reviews, typically spends 18 – 24 months gathering evidence, listening and responding to the views of interested parties and carrying out several rounds of consultation before it articulates a market failure (if any). Only then, if necessary, does it impose remedies on market participants (after clearly outlining why such market intervention is necessary and proportionate).
- 2.42 In light of Parliament's clear intention to give the PSR an economic regulation mandate, Visa Europe has concerns over the PSR's proposed regulatory approach, particularly with respect to its suggested PSR Principles contained in Supporting Paper 6 to the Consultation Paper.³³ Visa Europe has two key concerns in this regard:
- Visa Europe is concerned that the Consultation Paper (including the Supporting Papers) lacks specificity in its analysis of the market failures which the PSR seeks to address by the regulatory interventions it is consulting on. To the extent any market failures are identified, the Consultation Paper does not clearly articulate how the proposed regulatory interventions address this market failure. In addition, the Consultation Paper lacks any meaningful analysis of the likely effects of its proposed measures. Without an effects-based approach, it is impossible to determine whether an intervention is proportionate and, therefore, legally sound; and
 - Visa Europe notes the reference to over 170 meetings with 75 organisations which the PSR has held over the past six months. It is clearly welcome that the PSR is actively engaging with all stakeholders. However, it is equally important that the PSR critically evaluates the concerns raised with the PSR to test whether these concerns are supported by robust qualitative and quantitative evidence of market failures to the detriment of service-users and ultimately consumers. This should be supported by effective public consultation. The PSR should strongly resist requests for regulatory intervention in the absence of such robust and

³² Section 52(1)

³³ The nature and status of the Principles are discussed in greater detail in Section 4 of this submission.

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compelling supporting evidence of market failure, and without a proper assessment of the proportionality of any proposed regulatory measures designed to address these market failures.

- 2.43 Visa Europe is concerned that any conduct based approach to regulation by the PSR, which disregards the principles of an effects based approach, would exceed the PSR's statutory remit and would ultimately risk undermining effective and dynamic innovation in the payment systems sector, to the detriment of all stakeholders, including consumers.

(iii) Proportionality

- 2.44 As noted above, the PSR has an express statutory obligation under the Act to ensure "*that a burden or restriction which is imposed on a person, or on the carrying on of an activity, should be proportionate to the benefits, considered in general terms, which are expected to result from the imposition of that burden or restriction*".³⁴ The principle of proportionality must therefore underpin everything the PSR does.
- 2.45 The Act's requirement to act proportionally reflects strict and long-established requirements under English and EU law. The principle of proportionality essentially requires that in imposing a regulatory burden, a regulator must conclude there is no less onerous measure which would adequately achieve the regulatory objective. The CMA has noted that "*a proportionate remedy is one that: (i) is effective in achieving its legitimate aim; (ii) is no more onerous than needed to achieve its aim; (iii) is the least onerous if there is a choice between several effective measures; and (iv) does not produce disadvantages which are disproportionate to the aim.*"³⁵ The CMA's guidance reflects the general legal principles which apply equally to the PSR by virtue of Section 53(b) of the Act.
- 2.46 As noted above and for the reasons set out above, Visa Europe is concerned that the Consultation Paper does not adequately explain the process followed by the PSR in assessing the proportionality of its proposals and fails to provide the evidence (if any) which underpin many of its regulatory proposals.

D. Framework Consideration 5 – The PSR must review regulatory interventions over time to check whether they remain necessary and appropriate in changed market circumstances.

- 2.47 Framework Consideration 5 flows from the PSR's statutory duty to act proportionally over time. The PSR must ensure that its regulatory policies and measures reflect the prevailing market conditions and other regulations conditioning the conduct of designated operators.
- 2.48 As such the PSR ought to be alive to the fact that the dynamic nature of the payments sector in the UK means the PSR's regulatory solutions can rapidly be rendered redundant by disruptive technology, the growth of new entrants and/or the imposition of pan-European regulation.
- 2.49 Visa Europe expects that, consistent with the practice of other UK regulators, the PSR will regularly review market conditions, the costs of regulation it imposes and whether regulation is still necessary and proportionate to achieve its stated objectives. Visa Europe notes in this regard that Ofcom has a specific statutory duty under the Communications Act to keep its functions under review with a view to securing that regulation does not involve: (a) the imposition of burdens which are unnecessary; or (b) the maintenance of burdens which have become unnecessary.³⁶

³⁴ Section 53(b)

³⁵ Competition Commission Guidelines for market investigations (as adopted by the CMA), para 344

³⁶ Section 6, Communications Act 2003

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- 2.50 In accordance with its statutory duties under Section 6 of the Communications Act, Ofcom regularly carries out market reviews and publishes simplification plans aimed at “*reducing regulation and minimising administrative burdens*.”³⁷ Visa Europe believes that the principles of proportionality and the general principles of good regulation require the PSR to adopt a similar approach aimed at reducing and simplifying regulation over time.
- 2.51 In conclusion, all of the PSR’s policies and measures must strictly be aimed at advancing the PSR’s Statutory Objectives, having regard to the Statutory Principles. The PSR has no margin of discretion in this regard. The Act is clear on this point.
- 2.52 Visa Europe considers that, as a result, the PSR must have regard to the Framework Considerations set out above which necessarily flow from, and are informed by, the Statutory Objectives and Principles. In Visa Europe’s view, it follows that the Framework Considerations should be incorporated in one form or another in its general policy documents to ensure legal certainty and transparency for the entire payments systems sector.

³⁷

See, for example, <http://stakeholders.ofcom.org.uk/binaries/consultations/draftap0910/annexes/simpl08.pdf>

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3 COMPETITIVE DYNAMICS OF THE PAYMENTS SECTOR

- 3.1 Visa Europe operates in a highly competitive market, which has changed significantly in recent years. In particular the market has seen strong growth of online transactions, contactless card transactions, mobile payments and person-to-person payment systems.³⁸ Visa Europe has been at the forefront of these changes to stay relevant in an innovative and dynamic marketplace.
- 3.2 Consumers today have a wide choice for their payment transaction requirements. They can – and do – readily switch between card transactions (both face-to-face “card present” transactions and online “card not present” transactions), cash, online payment schemes (such as PayPal) and traditional bank transfers (which can be arranged in bank branches, online or via mobile apps). Despite the significant growth in online transactions, it is important to recognise in particular the continued significance of cash as an alternative payment option in the UK. Visa Europe thus competes with a wide and diverse range of payment services options for payment transactions in the UK, including among others MasterCard, American Express, PayPal and cash.
- 3.3 This section presents a brief overview of the competitive landscape in which Visa Europe operates. It then explains how the competitive pressures in the market have driven service-user focussed investments and innovation by Visa Europe. Visa Europe considers that these market pressures ensure that Visa Europe has made and continues to make efficient investment choices to meet the changing demands of service-users, such as merchants and ultimately consumers. Visa Europe’s mission is to support payments on any device, on any network, with any issuer and with any payment product.

A. Competitive constraints faced by Visa Europe

(i) Competition with MasterCard and other card operators

- 3.4 In relation to card operators, Visa Europe’s primary competitor in the UK and across Europe is MasterCard Inc. Both Visa Europe and MasterCard operate four-party card schemes and offer a similar range of products and services. The brand recognition, reliability and credentials of MasterCard are similar to those of Visa Europe and card issuers can therefore readily replace Visa Europe’s products with MasterCard’s offering.
- 3.5 The substitutability between Visa Europe and MasterCard’s services has resulted in vigorous competition between Visa Europe and MasterCard in particular in relation to signing up issuers and market their products and services to merchants and consumers. As a single issuer can account for a significant percentage of the volume of debit or credit transactions in a relevant market, competition for each contract is intense.
- 3.6 Issuers therefore have significant countervailing power over Visa Europe and demand tough terms, threatening to switch to MasterCard if such demands are not met. These competitive pressures are reinforced by the very significant financial resources of MasterCard, allowing it to subsidise any switching costs incurred by issuers and acquirers.
- 3.7 Visa Europe understands that MasterCard is now actively investing in an enhanced MasterCard debit offer with the objective of securing debit business from Visa Europe in the UK (and elsewhere in Europe) in the near future.

³⁸

See for example the recent Nobel Laureate J. Tirole who states that the contours of the payments industry is “*rapidly changing. The competition between “four-party”, mainly open systems such as Visa and MasterCard and “three -party”, mainly closed systems such as American Express and Discover rages, with old-fashioned payment means (cash, checks) still commanding a respectable market share. It is hard to predict who, among incumbents or entrants will end up serving the various and interrelated business segments: debit and credit transactions, large, mid-size and micro payments, e- and mobile phone payments, P2P payments, and so forth.*” J Tirole, “Payment card regulation and the use of economic analysis in antitrust”, Toulouse School of Economics paper n° 4 - 03/2011.3.

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- 3.8 MasterCard therefore exercises a significant competitive constraint on Visa Europe's commercial decision making. As a result, Visa Europe must continually invest and innovate to remain relevant to issuers and acquirers. Ultimately this can only be achieved by continuing to offer compelling payment services solutions that the market (including merchants and consumers) wants.
- 3.9 It is however also important to recognise the competitive significance of other card operators, such as American Express and Diner's Club. In particular, American Express competes directly with Visa Europe in the UK in relation to credit card payments.
- 3.10 While historically, American Express has focussed on providing commercial credit cards and targeted so-called "affluent" consumers who make high value purchases, its business model has evolved in recent years. Today, American Express increasingly focuses on a wider range of consumers through a number of different approaches. For example, American Express' "Global Network Services" ("**GNS**") business operates its third party issuing and acquiring business and, in this context, operates a four-party model like Visa Europe and MasterCard. The GNS model provides more immediate access to larger numbers of consumers and merchants through American Express' three-party model. Visa Europe understands that in 2012, 78% of all non-US American Express cards were issued by GNS partners³⁹ including Lloyds, TSB, MBNA and Barclays in the UK.
- 3.11 In addition to its GNS programme, Visa Europe understands that American Express has signed more digital partners than any other payment system⁴⁰ including notable partnerships with merchants such as Amazon and Ticketmaster, online platforms such as Facebook and Twitter and others such as Microsoft and Samsung.
- 3.12 In relation to merchant engagement, American Express has implemented a number of initiatives to increase acceptance of its cards by smaller merchants. In the UK, American Express has relationships with at least 30 acquirers including WorldPay, Global Payments, Barclaycard and Lloyds Cardnet. It leverages these relationships to increase acceptance of its card in their respective merchant networks.
- 3.13 American Express therefore continues to be a major player in the commercial credit card and "affluent" consumer credit card segments, imposing significant competitive pressures on Visa Europe in these segments. In addition, American Express is actively expanding its commercial offering with the aim of developing into more of a mass-market payment services provider. Given American Express' knowledge of the market and its significant financial resources, Visa Europe can expect to face the same pressures from American Express in the wider consumer credit card segment in the near future that it already faces in the higher end credit card segments, particularly given that American Express' three-party business is outside the scope of the IFR and may not be subject to any regulatory constraints and costs under the Act (if not designated by HM Treasury).
- 3.14 In this context, Visa Europe also notes that market shares do not provide a meaningful proxy for the competitive position (or market power) of an operator. Given the lumpy nature of tenders for credit or debit books, competition is significant at the tender stage. What matters for any assessment of the competitive pressures which Visa Europe faces at the tender stage is whether there are *credible alternatives* for the tenderor (bank); one significant competitor may be sufficient to ensure that there is effective competition. Whether the tenderor ultimately decides to switch is not in itself significant in this regard.

³⁹ See Visa Europe response to HM Treasury's Consultation on "*Designation of payment systems for regulation by the Payment Systems Regulator*", page 9.

⁴⁰ *Ibid*

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(ii) Competition with cash and bank transfers

- 3.15 The ability of consumers to switch to cash as a substitute for card transactions also acts as a significant incentive for Visa Europe to continually invest in its scheme and expand its product offering. In developing its offer to act as a more attractive alternative to cash, Visa Europe has been engaging closely with merchants, such as Transport for London and McDonalds, to understand their needs and the evolving preferences of consumers. (Further details in this regard are set out below.)
- 3.16 Despite the increasing use of cards and electronic payments in commercial transactions, it is still the case that consumers choose to use cash more frequently than *all other* payment instruments combined, including debit or credit cards.⁴¹ In particular, cash plays a particularly dominant role for small-value transactions and cash is the leading payment instrument for many types of purchases.
- 3.17 For example, cash is the leading payment instrument in several types of merchants, including supermarkets, discount stores, cafes, off-licences, and pubs.⁴² Cash is also used for over 25% of payments in the retail, travel and entertainment categories.⁴³ Cash is also used for around 70% of person-to-person small business transactions, a proportion which has changed little in the last five years.⁴⁴
- 3.18 The continued use of cash is supported by the manner in which merchants recover their payment-service costs. Visa Europe understands that merchants' payment-service costs per transaction constitute a higher percentage of the transaction value for small transactions than for large ones. Thus customers with large transactions tend to subsidise customers with small transactions. As cards are used much more than cash for settling large transactions, and cash is used more than cards for settling small transactions, overall card users will tend to subsidise cash users.
- 3.19 The use of cash is also subsidised in other ways, even though it is generally understood that cash is a socially inefficient payment instrument. In most EU Member States, consumers pay no fees for cash withdrawals from the vast majority of ATMs. Consumers only bear the opportunity costs of making trips to an ATM and the risk of losing cash. They do not face any efficient pricing signal concerning many other costs of the cash system: the cost of counting and transporting cash to and from banks, the lost interest and cost of inflation on banks' cash holdings, the cost of printing new notes, and the cost of maintaining the ATM network.
- 3.20 It is clear that Visa Europe and other card operators compete with cash as a mode of payment. The subsidisation of cash transactions further intensifies the competitive constraint exercised by cash on other payment transaction providers.
- 3.21 In addition to cash, Visa Europe also competes with interbank transfer schemes in relation to certain types of payments. For example, UK consumers can, and many do, pay their utility bills and regular subscription-type payments through interbank transfers, such as standing orders or direct debit arrangements.
- 3.22 The continued attraction of cash and interbank transfers creates attractive opportunities and therefore economic incentives for Visa Europe to expand its product offer to persuade consumers to switch these payment modes to its card scheme. Product innovations in this regard cover new

⁴¹ In 2013 there were 20.8 billion cash payments in the UK, representing 54% of all payments. on "*UK Cash & Cash Machines*" (2013), UK Payments Council Report.

⁴² *Ibid*

⁴³ *Ibid*

⁴⁴ *Ibid*

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payment offers via contactless payments, e-wallets and mobile payments. Visa Europe sets out in sub-section B. below a number of practical examples to illustrate how these incentives translate into real transformational product development projects with individual merchants.

(iii) Competition for online and mobile payments

- 3.23 As e-commerce continues to thrive, an increasing proportion of transactions are completed online, with the card not present, rather than in traditional face-to-face point of sale transactions. For example, very recent press reports note online transactions in the UK on “Black Friday” (19 November 2014) were up 135% cent year-on-year, with an 80% increase in mobile payments.⁴⁵ As a result of the growth of providers such as PayPal and Zapp, these transactions can be completed without the involvement of Visa or MasterCard.
- 3.24 PayPal’s increasing presence in the UK, which accounts for 18 million of its 146 million accounts globally, emphasises the competitive pressures that Visa Europe faces from PayPal and other online and mobile payment systems. PayPal’s share of total global e-commerce was estimated at 18% in 2012 and total PayPal payments were estimated at \$27 billion in 2013. In addition to online payments, PayPal now also allows users to make peer-to-peer transfers directly from their bank account and are expanding into the physical point of sale space by offering merchants a card reader that connects to a mobile phone.
- 3.25 The continuing ambitious expansion plans by online retailers, global technology giants and general e-commerce platforms, such as Apple, Google, Facebook, Amazon and Alibaba, will continue to grow online transaction volumes and drive innovation in the market for payment systems.
- 3.26 Given the commercial significance of personal data (including transactional data), the competitive nature of the consumer payments sector will continue to intensify further over the foreseeable future. The experience of PayPal, which commenced operations as a “captive” payment service to facilitate eBay transactions, sets a clear precedent for the rapid growth opportunities for new entrants in this space; in particular for new entrants which can leverage off successful and growing online platforms.
- 3.27 The prevailing and anticipated market developments outlined above create compelling incentives for Visa Europe, as an internationally-capable payment scheme, to innovate to meet the demands of merchants and ultimately consumers.

B. Competitive dynamics drive infrastructure investment and service-user focused innovation

- 3.28 The competitive dynamics of the marketplace have driven Visa Europe’s significant investment and innovation strategies over the past decade. The focus of its investments has been on: (i) ensuring the resilience and reliability of its systems and scheme in a fast moving market, characterised by a constant flow of new payment options both in face-to-face transactions as well as online and mobile transactions; and (ii) developing innovative products for merchants and consumers. Clearly, both investment streams are closely inter-linked to ensure the effective and resilient operation of Visa Europe’s schemes and products in the UK as well as across Europe.

Core infrastructure investments

- 3.29 Visa Europe has invested heavily in building and maintaining a best in class processing system that delivers a highly reliable solution for cardholders and merchants. Visa Europe estimates that in recent years it has spent around **CONFIDENTIAL** on maintenance and capital investment in its

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Research based on data collected by Interactive Media in Retailer Group (IMRG) and Capgemini.

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core infrastructure systems. This figure has grown year on year and Visa Europe estimates that over the past decade it has invested around **CONFIDENTIAL** in its infrastructure systems.

- 3.30 Visa Europe's maintenance and investment spend has resulted in outstanding service performance for merchants and cardholders as indicated by the table below.

			Target	Achieved
Service Performance	Availability	Authorisation	99.999%	99.999%
		Clearing and settlement	99.86%	100.00%
	Quality	Authorisation	99.999%	99.999%
		Clearing and settlement	99.99%	99.99%

- 3.31 Put simply, Visa Europe's significant and targeted investments ensure that its card scheme is essentially "always on" and "always delivers" for cardholders and merchants.

Product innovation

- 3.32 In addition to investing in, and maintaining its core systems (described immediately above), Visa Europe has been a driving force for innovation in new payment technologies -- with over €1 billion invested across Europe into new technology and related supporting infrastructure over the last six years. Key areas of investment include contactless and mobile payments, digital wallets and personal payments.

- 3.33 With regard to contactless, Visa Europe has made a significant number of investments into acceptance and issuance of payments, providing a greater variety of ways to pay for consumers and allowing merchants greater flexibility and lower costs. Each of these investments has involved working closely and collaboratively with merchants to ensure that the developed solutions meet the needs of merchants and consumers in the most efficient way. By way of illustrative examples, Visa Europe refers the PSR to the following recent examples:

- The widespread introduction of contactless payment methods across the **Transport for London** network in September 2014 resulting in over 1.2 million journeys paid for with a contactless card in the first nine days of the scheme's introduction. At present, Transport for London is Visa Europe's largest contactless merchant and there are 22,000 new contactless cards being used to complete public transport journeys across London every day;
- An extensive introduction of contactless technology for **Tesco Bank** credit and debit cards has resulted in between 5,000 and 6,000 merchants being equipped to take contactless payments from Tesco Bank customers;
- Playing a fundamental role in taking **McDonalds** restaurants from being a cash-only business into one of its largest contactless merchants. Visa Europe assisted McDonalds in rolling out the infrastructure necessary to make it capable of accepting contactless payments, providing **CONFIDENTIAL** in financial support. Visa Europe's relationship with McDonalds has allowed McDonalds to redefine its "drive-thru" experience for consumers, as well as providing McDonalds with the means to access significant quantities of additional data about the tens of millions of transactions it processes on a daily basis; and

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- The introduction of contactless technology throughout **Marks & Spencer's** UK stores which has seen it become the leading contactless merchant in the UK, with 230,000 contactless transactions processed per week.

- 3.34 Visa Europe has invested significantly in mobile payments, such as a pioneering venture with **Vodafone** allowing up to 70,000 customers across Europe to make payments at the point of sale with their smart phones. Visa Europe's investment in this aspect of the payment systems market is driven by the competitive constraints created not only by other card operators but also by online and mobile payments operators, such as PayPal. The commercial launch of this project is due for March 2015 and the parties intend to grow the customer base ten-fold and bring mobile payments to millions of consumers across Europe.
- 3.35 Each of these projects involved intense interaction with merchants (in the wider sense) with a view to understanding better their specific needs as well as what drives consumer acceptance and behaviours when it comes to financial transactions. These projects play a significant role in Visa Europe's engagement with stakeholders and in turn drive its innovation and investment strategies to stay relevant in a fast-moving and competitive marketplace.
- 3.36 Visa Europe notes that the competition it faces also means that it continuously reviews how it engages with its stakeholders to ensure that it captures emerging market trends at the earliest opportunity. At the same time Visa Europe (like most organisations) is continuously reviewing the way it operates to ensure that it optimises the use of its resources.
- 3.37 One area Visa Europe is assessing in this regard is to further optimise the way it engages with the wide and diverse interests of service-users in general, and merchants in particular. In a world in which merchants have access to an increasing variety of different payment system options, it is critically important for Visa Europe to understand their evolving needs in order to remain competitive and relevant.
- 3.38 At the same time the multitude of different views held within the merchant community poses a challenge for Visa Europe in how best to absorb and address these views in an appropriate manner. Visa Europe is committed to operating in a transparent and responsive manner and continues to review how this is best achieved so as to strike a reasonable balance between the administrative burden of engagement and the need to listen to service-users, with their many different voices. Visa Europe discusses its views and proposals in this regard further in Section 5 (Governance).
- 3.39 In summary, the competitive dynamics of the UK payments sector mean that Visa Europe has clear commercial incentives to invest, innovate and continually engage with service-users in order to provide best in class payment services to service-users whenever, wherever and in whatever form they are required. Visa Europe considers that (as far as its activities are concerned) the market provides effective drivers to advance the competition, innovation and service-user objectives under the Act. Visa Europe would urge the PSR to approach any ex-ante regulation in this regard with extreme caution to avoid unintended consequences, such as a distortion of competition in favour of any particular payment systems (e.g. PayPal or American Express) or allocative inefficiencies (e.g. by requiring unproductive investments and avoidable costs).

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4 PAYMENTS STRATEGY FORUM

- 4.1 As set out in Section 3, Visa Europe faces significant competition in the UK and across Europe from a range of diverse players. These competitive pressures drive Visa Europe's market conduct and commitment to innovation.
- 4.2 Visa Europe agrees with the PSR's view that competition generally brings better outcomes for service-users than collaboration.⁴⁶ However, Visa Europe also agrees with the PSR that there is a role for collaborative initiatives to drive innovation and inter-operability across the payment systems sector in the UK. As such, there can be a role for expert industry bodies tasked with guiding and assisting in the development of collaborative strategies aimed at establishing world-class payment systems in the UK where competition does not deliver the right outcome for service-users.
- 4.3 However, in Visa Europe's view it is not necessary for a permanent body to be established to guide the PSR or develop collaborative solutions in the card payments sector (such a body may or may not be necessary for interbank operators; Visa Europe does not comment). Indeed in Visa Europe's view, such a body has the potential of stagnating innovation if there is a need to obtain consensus from multiple parties with conflicting incentives, a concern that the consultation Supporting Paper 2 also articulates.⁴⁷ It would be far more efficient, and consistent with regulatory best practice, to set up expert working groups, seminars or forums on ad-hoc basis to tackle particular issues which require collaboration or to guide the PSR with certain technical aspects of payment systems.
- 4.4 Visa Europe also notes in this regard that the Act requires the PSR to set up and maintain one or more industry stakeholder panels which it should consult with when developing its general policies and practices.⁴⁸ The Consultation Paper does not develop the PSR's views as to the nature and role of such statutory panels. Visa Europe considers that these panels could serve as a constructive forum for providing or supporting the development of expert commentary on specific regulatory policy proposals by the PSR.
- 4.5 To the extent that the PSR determines to set up a permanent industry-wide body, Visa Europe would favour Option 1 set out in the Consultation Paper, i.e. the setting up of an industry-wide Payments Strategy Forum (the "**Forum**"). However, Visa Europe notes that the PSR's proposals do not provide any justification for the regulatory reasons as to why such a Forum is necessary. Further, the PSR's proposals for the Forum do not provide sufficient clarity on the role of the Forum, its ability to affect the commercial decisions and strategy of independent operators or its working rules and an assessment of the legal implications of such an approach. As noted above, it is also unclear how the Forum would interact and co-exist with the statutory panels required by the Act. The lack of clarity on the purpose and functioning of the Forum means that at this stage Visa Europe is unable to respond in any detail to the PSR's proposals.
- 4.6 In the remainder of this section Visa Europe explains why it considers that it is unnecessary to establish a permanent industry-wide body such as the Forum in relation to card payment systems. Visa Europe then explains that, to the extent that the PSR still decides to create such a Forum, the role of the Forum and its working practices (including membership, governance, operational procedures, funding) should be carefully considered in collaboration with affected industry stakeholders to ensure that the Forum is effective in adding value by working efficiently.

⁴⁶ See, for example, the Draft Objectives Guidance, para 4.5

⁴⁷ See Supporting Paper 2 – Payments industry strategy and areas for consultation, Page 13 and 14.

⁴⁸ Section 103(3)

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A. A permanent body is not necessary to guide industry strategy in relation to Card Payments

- 4.7 Visa Europe considers that the Consultation Paper (including Supporting Paper 2) fails to provide sufficient justification that a permanent body is in fact required to "*agree and develop strategic priorities*" for the card payments sector in the UK.
- 4.8 Visa Europe notes that the proposed objectives of the Forum are broadly two-fold: first, to develop the sector through collaboration; and secondly to provide a voice to all stakeholders who have raised concerns that their views are not adequately taken into account in setting industry strategy.

(i) Driving collective action

- 4.9 The PSR acknowledges that the payment systems and services sector in the UK is characterised by dynamic innovation. A careful balance therefore needs to be struck between innovation by competition and innovation by collaboration. Visa Europe submits that EU and UK competition rules (in particular in relation to information exchanges and horizontal and vertical collaboration) serve as an important point of reference in this regard. On this basis, collaborative endeavours should be assessed on a case-by-case basis to ensure that they in fact lawfully drive competition rather than stifling it.
- 4.10 Visa Europe acknowledges that there may be genuine cases in which Card Operators and their service-users will be required to collaborate (for example, in relation to legitimate standard setting for interoperability purposes). However, the Consultation Paper does not refer to any instances in which Card Operators have failed to collaborate with one another or other third parties to the detriment of service-users. There is therefore no evidence of any market failure requiring further action to facilitate collaboration of card payment systems.
- 4.11 Further, in cases where collaboration is required, it may not be possible to achieve this without a permanent body being established in order to drive such projects. The UK's telecoms regulator, Ofcom, and energy regulator, Ofgem, both make extensive use of ad-hoc working groups, seminars and forums to drive industry strategies on particular issues which require or would materially benefit from collaboration. For example, Ofcom has, over the years, established working groups in relation to switching, non-geographic numbers and wholesale line rental. Similarly, Ofgem has established working groups in relation to electricity retail markets, transmission and sustainable development.
- 4.12 However, while facilitating ad-hoc collaboration, both regulators acknowledge that in the vast majority of cases, allowing competitors to take independent decisions produces the best market outcomes. In relation to telecoms in particular, this approach has resulted in the UK having one of the most innovative, competitive and robust telecoms markets in Europe.
- 4.13 In view of the above, Visa Europe is not persuaded of the merits of the PSR's proposal to depart from regulatory best practice which has proved successful by establishing a permanent body (with all its inherent overheads, costs and operational inflexibility). Visa Europe notes that the Consultation Paper does not specifically consider whether the PSR's objectives could be adequately met by ad-hoc working groups. The Statutory Principle of proportionality in Section 53(b) of the Act requires it to consider this less onerous (and less costly) proposal (also in the light of the establishment of statutory panels). If the PSR concludes to establish a permanent Forum, it needs to give reasons explaining why this is consistent with the Statutory Objectives and Principles. The reasoning in the Consultation Paper is in Visa Europe's view insufficient in this regard.

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(ii) Providing a voice to stakeholders

- 4.14 The PSR's second objective in establishing the Forum appears to be to provide a voice to stakeholders and service-users. It is not clear what weight the PSR has given in its assessment to the fact that the voice of stakeholders will already be strengthened through the statutory panels which the PSR is required to establish and maintain.
- 4.15 Also, the vast majority of concerns raised in this regard relate to interbank operators. Only very limited concerns have been raised in relation to Card Operators.
- 4.16 Supporting Paper 2 notes only the following concerns:
- One payment system provider complaining that it had not been given the opportunity to engage in discussions about payment strategy in its capacity as a major issuer of pre-paid cards;
 - Some merchants stating that they have no direct relationship with card operators; and
 - Certain acquirers complaining that they have struggled to have a voice in discussions.
- 4.17 On closer examination, particularly the evidence set out in the Accenture Report which the PSR included in the Consultation Paper,⁴⁹ it appears that the concerns can essentially be limited to those raised by a single acquirer and a single large merchant. Both of these parties are sophisticated users of payment systems and can be expected to lobby the PSR to further their individual commercial interests and their submissions should be assessed with care.
- 4.18 Visa Europe therefore submits that there is insufficient evidence to support the view that relevant service-users are unable to provide constructive comments on and influence Card Operators' strategy and rules in the best interests not of just themselves but the wider service-user group. As such, there is no evidence justifying that a permanent Forum is necessary to represent such stakeholder views. In any event, to the extent that such stakeholder views require, in the PSR's view, enhanced representation at an industry-wide level, this can be effectively achieved through ad-hoc expert working groups and the establishment of the required statutory panels.

B. Design considerations of a possible Forum

- 4.19 If, notwithstanding the strong objections to a permanent one-size fits all industry body set out above, the PSR still decides to establish a permanent Forum, it is vital that the role, powers and functions of the Forum are clearly defined. Given the lack of detail in the Consultation Paper, Visa Europe sets out its views below on how this could best be achieved.

(i) Areas requiring Forum consultation

- 4.20 Supporting Paper 2 indicates that the role of the Forum is to "*discuss, determine and agree strategic priorities*" for the industry. However, the practical implications of this proposition remain unclear. Visa Europe is concerned that as a result the Forum may be "captured" by partial commercial interests. Visa Europe is also concerned about the costs (in both human resources and money terms) of the operation of the Forum and its competition law compliance at all levels.
- 4.21 Visa Europe notes in this regard that the PSR "expect[s] Operators and other industry participants **to continue developing their own systems and services independently**, the Forum would focus particularly on areas where strategic development requires the collective action of

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stakeholders. It would maintain a high-level strategy to coordinate and drive this collective action to set priorities for the industry to deliver world class infrastructure for payment systems.⁵⁰

4.22 Visa Europe understands this to mean that the Forum would have no say over issues such as product development and commercial strategy of individual Operators but that it would play a role in driving collaboration amongst Operators where necessary, and within the confines of UK and EU competition law. For example, the Forum could be involved in standard setting in relation to existing products or systems, so long as this is consistent with the European Commission's guidance. However, this limited remit would provide further support for the use of flexible ad-hoc panels rather than an unwieldy permanent Forum structure.

4.23 In light of the considerable uncertainty, Visa Europe requests the PSR to clarify which areas the Forum would be involved in, in as much detail as possible, specifically in relation to card payment systems. Alternatively, if the PSR's view is that these issues are to be determined on an ad-hoc basis, Visa Europe notes that a permanent Forum structure would appear unnecessary.

(ii) Role of the Forum

4.24 Even if it is agreed that the Forum will only be involved in those areas requiring industry collaboration and a degree of coordination, it is unclear how the Forum will make decisions. Supporting Paper 2 appears to suggest that deliberations of the Forum may, at least in certain cases, have a binding effect on payment service providers. Visa Europe submits that such an approach (if that is indeed the proposal) has no basis in the Act and would amount to the PSR improperly delegating its functions to the Forum.

4.25 Moreover, Visa Europe considers that making the Forum's decisions binding would be contrary to the PSR's objective to advance innovation and competition. This is because it would create a significant risk that majority decisions (however the relevant majority is constituted) with binding effect on the industry would cut across the PSR's objectives or, alternatively, serve to disrupt innovation strategies by individual payment systems.

4.26 In Visa Europe's view it is important to clearly limit the powers of the Forum to an expert advisory role. Where necessary, efficient collaboration would be best advanced by an expert, consultative body designed to develop and critically test ideas and share best practice, rather than a formal organisation in which the pace of innovation falls to that of its slowest member. This is consistent with the role played by ad-hoc forums, seminars and working groups established from time to time by other economic regulators, such as Ofcom and Ofgem. Their role is to provide the regulator with a platform for industry engagement on specific issues. The regulator must then independently consider the merits of, and consult on, the recommendations of the Forum before any formal directions are adopted by the regulator to implement the recommendation.

4.27 For the avoidance of doubt, Visa Europe does not rule out that the Forum's recommendations may find universal support by its members (or at least affected members) and may lead to the coordinated *voluntary* implementation of a recommended strategy across the sector, subject always to full compliance with applicable competition rules. However, such joint implementation should always be the result of independent decisions by the relevant players.

(iii) Guiding principles and working rules

4.28 It is crucial that any Forum would be governed by a clear set of guiding principles and working rules to ensure that it is an objective expert body which pursues the general legitimate interests of all

⁵⁰ Supporting Paper 2, para. 2.87

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service-users and Operators by providing informed and balanced commentary on market developments and regulatory proposals.

4.29 Visa Europe has identified a number of uncertainties in respect of the operation of the Forum, including, but not limited to:

- Membership eligibility criteria, which must be clear, objective and regularly revised;
- Ensuring proportionate representation which, given the wide range of payment services providers that will be invited to contribute to the Forum, is crucial in ensuring that different parties are represented in a manner that reflects their relative interests and expertise in the matters that are being considered;
- Confirming a reasonable operational framework governing the organisation of the meetings of the Forum, which is critical in ensuring that the views of different payment service providers are adequately represented and that the platform is fair and well run; and
- Providing a framework that takes into account the international dimension of payment service providers, such as Visa Europe, which have significant international aspects to their businesses and infrastructure. The business of Visa Europe, together with certain of its competitors (e.g. MasterCard) are in their very nature highly international and the Forum therefore needs to ensure that this dimension is reflected in discussions.

4.30 Visa Europe suggests that the Forum should be governed by high-level guiding principles which should be referred to whenever the working rules (on which, see below) do not adequately cover the relevant situation. As a minimum, Visa Europe suggests that the key points discussed in (a) to (d) of paragraph 4.26 above should be addressed within the guiding principles. In this regard the PSR's own Objectives Guidance ought to be a key point of reference.

4.31 In order for the Forum to operate efficiently, Visa Europe proposes that detailed working rules are formally adopted by the Forum before it comes into operation. The rules should be reviewed at regular intervals, to reflect the practical experience of the Forum's working practices and output.

4.32 In order to assist the PSR, Visa Europe envisages that the working rules, should, as a minimum, cover the following points:

- Membership of the Forum:
 - (i) clear eligibility criteria regarding who can attend, as any new member may significantly impact the payment services industry;
 - (ii) clear rules regarding how new members can apply to attend the Forum;
 - (iii) clear rules regarding how the Forum as a whole will decide which members to admit – e.g. simple majority, unanimous;
- Scope of issues permitted to be considered:
 - (i) the Forum's working rules should maintain a specific list of issues which it is authorised to consider. As set out above, care should be taken to ensure that these discussions are consistent with competition law;
- Status and effect of decisions and recommendations:
 - (i) the PSR should ensure it does not improperly delegate its statutory decision-making powers to another body like the Forum. The Forum must have no more

than the power to make recommendations, which the PSR can implement only after proper consultation with the industry and the public;

- (ii) improper delegation of powers means the delegated authority has no proper jurisdiction: “action taken by a delegated authority when there was no power to delegate [goes] to the root of the jurisdiction” ;⁵¹

- There should be clear rules governing the frequency of meetings, notice of meetings, agenda for meetings, quorum, voting rights and publication of minutes;
- There need to be clear rules regarding voting rights, proportionate representation and whether the chairman of the Forum would have a casting vote; and
- Fair and non-discriminatory rules governing the funding of the Forum and its activities, mindful of the need for the Forum to have the resources to engage in expert discussions while ensuring that the Forum delivers “value for money”.

4.33 Visa Europe reiterates that, in its view, no permanent body is necessary to drive the limited industry collaboration and collective action that is required in the card payments sector. However, if notwithstanding this, the PSR chooses to establish a permanent Forum, great care should be taken to ensure that the Forum does not result in in fact slowing the pace of innovation or infringements of competition law. Further, for the reasons given above, the role of such a Forum should be purely consultative.

4.34 Visa Europe considers that the design of the Forum should be subject to a distinct consultation exercise to ensure that it is fit for purpose and delivers “value for money”, having regard to the PSR’s settled view on its own approach to regulation in the payment systems sector, following the conclusion of the present consultation exercise.

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Vine v National Dock Labour Board [1957] AC 488, per Lord Somervell at page 510

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5 VISA EUROPE'S CORPORATE GOVERNANCE

- 5.1 Visa Europe is committed to being at the forefront of technology to introduce new, easier, and more secure payment options, and in so doing, to serving the demands of merchants and consumers, as well as the acquirers and issuers that comprise its membership. Visa Europe's governance structure and its active involvement with stakeholders reflect these principles and provide a necessary balance between the representation of a multiplicity of views from a range of industry stakeholders and the ability to make efficient decisions in the long-term interests of Visa Europe.
- 5.2 Stakeholders views are adequately represented within Visa Europe's governance structure and any requirement to appoint a service-user representative to its Board would be unnecessary and therefore disproportionate. Further, Visa Europe has significant engagement with its members, service-users and other stakeholders, using a variety of methods. An onerous requirement to publish Board minutes to achieve even greater transparency is unnecessary, disproportionate and likely to be counterproductive.

A. The PSR's general direction on the representation of service-user interests

- 5.3 The PSR proposes to make a general direction requiring "*all Operators to ensure appropriate representation of the interests of service-users in their decision-making processes at board level by 30 September 2015.*"
- 5.4 Visa Europe notes that the PSR wishes to avoid being prescriptive about the manner in which the appropriate representation of stakeholders is being effected.⁵² However, the PSR's commentary in Supporting Paper 3 appears to suggest that a new director, or an existing director, must have the obligation of representing service-user interests at board level. Visa Europe fundamentally disagrees with this proposal.
- 5.5 Visa Europe accepts that any business needs to understand the needs and views of those using its products or services in order to remain competitive and relevant to its users. This is precisely why Visa Europe has, in recent years, made a number of changes to governance structure to obtain a better understanding of merchants', and acquirers' and others, needs. These changes, together with further steps Visa Europe is taking in this regard, ensure that all relevant stakeholders have a voice within Visa Europe. In any event, there are a number of factors, which make such a proposal unworkable and counterproductive.

(i) Representation of service-user views within Visa Europe's current corporate governance structure

- 5.6 As set out in Section 2, Visa Europe operates as a pan-European membership association, owned and operated by over 3,000 banks, financial institutions and payment service providers across Europe. In Visa Europe's response to the FCA's Call for Inputs, Visa Europe made a number of general comments concerning details of Visa Europe's governance structure which are not repeated in this submission. In summary, the remit of the Visa Europe Board relates to commercial and strategic decisions across the entire European business of Visa Europe, with representation from markets across Europe, whilst the Visa UK Board deals exclusively with commercial and strategic decisions concerning Visa Europe's UK business. Three members of senior management at Visa Europe serve as directors on the Visa UK Board.
- 5.7 It is clear that as a pan-European membership organisation, Visa Europe's governance structure is different to that of a UK private or public company and the PSR should be aware that different considerations apply when evaluating the impact of intrusive directions to change this structure.

⁵² Supporting Paper 3, Para. 3.69

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- 5.8 That said, as described below, given the increasing dynamism of the industry, Visa Europe has in recent years adapted its corporate governance procedures and continues to review these procedures to ensure that it can operate a business that is agile in providing a “best of class” card payment scheme and remains reliable, cost effective and innovative. In turn, this means it remains attractive to service-users, particularly merchants and consumers. In particular, Visa Europe’s Board represents the views of its diverse and growing members base and comprises a deep understanding of the market in which Visa Europe operates, including crucially the changing needs and preferences of merchants and consumers.

Amending Articles of Association

- 5.9 Visa Europe, including Visa UK, have taken a progressive approach to the appointment of independent non-executive directors to its Boards. The Visa UK Board unanimously voted to amend the Visa UK Limited Articles of Association to allow an independent director to serve on its Board.⁵³ Visa UK’s first non-executive director, Tony Surridge, was appointed as Chairman shortly after his appointment on the Board on 11 May 2006, a position he held until 1 November 2014. He has been replaced by the new Chairman of the Visa UK Board, Debbie Hewitt, also an independent director, who has an extensive retail background.

Visa UK Board

- 5.10 Given that it is plainly not the case that every shareholder in a public company (including regulated companies) has representation on that company’s Board, Visa Europe and Visa UK have far wider and diverse representation of interest at Board level than a significant number of the UK’s largest publically traded companies.

- 5.11 At the time of submission, Visa UK’s Board is comprised of seven issuers⁵⁴, three issuer-acquirers⁵⁵ and two acquirer only businesses⁵⁶ and is chaired by an independent director. Visa UK is currently in the process of appointing a second independent director. Visa Europe is hopeful that this process will be completed shortly after its “Directors’ Day” in February 2015. This is a forum for the Visa UK Board members to set the agenda for the market, strategic planning and commercial priorities for the coming year. The Visa UK Board therefore represents diverse relevant interests and backgrounds.

Visa Europe Board

- 5.12 Visa Europe’s Board (like the Visa UK Board) incorporates a wide range of voices with diverse relevant backgrounds. The Board is headed by an independent chairman, Gary Hoffman, and also includes two further independent directors, Yannick Chagnon and Eva Castillo Sanz (who has a retail background as a director of Telefónica Europe). Overall the executive Board comprises senior representatives of issuers, issuer-acquirers and acquirers only, with 17 members represented.⁵⁷

Payment Services Steering Committee

⁵³ Under the Articles of Association of Visa UK Limited, its board can have up to three independent directors.

⁵⁴ Santander UK plc, the Co-operative Bank plc, Citibank International plc, HSBC Bank plc, MBNA Ltd, Nationwide Building Society and the Royal Bank of Scotland plc

⁵⁵ AIB Group (UK) plc, Barclays Bank plc and Lloyds Bank plc

⁵⁶ WorldPay (UK) Limited and Elavon Financial Services Limited

⁵⁷ Cornèr Banca SA, Nationwide Building Society, Banca Carige, BPCE, ServiRed Sociedad Espanola de Medios de Pago, EnterCard Group, Landesbank Berlin, Israel Discount Bank, Royal Bank of Scotland Group plc, BNP Paribas, Yapi ve Kredi Bankasi A.S., Société Générale, PKO Bank Polski SA, WorldPay (UK) Ltd, Lloyds Banking Group plc, Visa Sweden Forening and Barclays Bank plc

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- 5.13 In addition to Board representation, Visa Europe interacts with its members through the Payment Services Steering Committee (the “**PSSC**”), which is a sub-committee of the Visa UK Board and acts as a forum for discussion of key developments in the payment systems industry affect Visa Europe in the UK. At present, there are 14 members of the PSSC, including members which represent acquirers and four members not currently on the Visa UK Board.⁵⁸ This interaction with its members is a further demonstration of Visa Europe's strong commitment to representing the interests of its members and having the benefit of a deep understanding of the views of service-users, for the purposes of its strategic decision-making process.

(ii) The PSR's proposals on service-user board representation

- 5.14 As set out in Section 2 above, Visa Europe strongly believes that, as an economic regulator, the PSR should only consider regulation when there is a clear evidence of market failure to the detriment of service-users, and that any such regulation must be proportionate. Visa Europe submits that any proposal to have service-users represented on the Visa UK Board does not satisfy this condition and must be reconsidered. This is for the reasons set out below.
- 5.15 **First**, as noted in this Section 5 above, the concern that the views of merchants and consumers are not sufficiently represented within Visa Europe is misconceived. It appears it is based on the evidence of a single issuer and one merchant. Visa Europe is concerned that the PSR may not have critically tested any concern raised by these two parties. (In Visa Europe's view these views do not genuinely reflect legitimate industry-wide concerns.) Accordingly, the PSR is not in a position to assess whether the remedy it proposes to address these concerns is necessary or proportional. Any mandated representation of any party which has commercial dealings with Visa Europe would be extremely intrusive and requires significant further analysis, investigation and consultation before it can be imposed.
- 5.16 As explained above, Visa Europe has taken significant steps to ensure that it is well informed of consumers' and merchants' views. Further, consumers' views are represented by issuers whose business model depends on delivering the best card payments technology to consumers. Issuers are therefore naturally close to and understand well consumer expectations and their changing preferences in a dynamic market and have regard to these views in Board discussions. Also, acquirer views are well represented on the Visa Europe board, which has two acquirer-only and three issuer-acquirer representatives. The presence of acquirers on the Board of Visa Europe and Visa UK further ensures that the interests of merchants are fully considered in Visa Europe's decisions.
- 5.17 **Secondly**, Visa Europe is not aware of a precedent for service-user board representation in any other regulated industry, including those which provide basic services to consumers (for example, transport, energy or telecoms) even where certain companies may be monopolies or hold positions of dominance in certain markets. It is unclear in what respects the PSR considers the UK card payments industry, which is competitive and dynamic, different from other regulated markets, which necessitates such an unprecedented and intrusive regulatory requirement.
- 5.18 **Thirdly**, Visa Europe is concerned that the PSR may not have fully (or at all) considered the potential unintended consequences of service-user Board representation. In particular, as the PSR may well be aware, Visa Europe, amongst other card payment systems providers, is currently subject to extensive litigation from merchants in relation to interchange fees.⁵⁹ To provide class-action type litigants with representation on Visa Europe and Visa UK's Boards would create a

⁵⁸ HBOS, Global Payment, Capital One and TSB.

⁵⁹ *Arcadia Group Brands Limited and ors v Visa Inc and ors* [2014] EWHC 3561

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fundamental conflict of interest at the highest levels of Visa Europe's governance. This would create a disproportionate burden on Visa Europe's decision-making process that would be likely to work to detriment of all stakeholders, including service-users, including consumers.

- 5.19 The practical issues of appointing parties with such diverse positions in respect to key strategic decisions, such as terms of pricing, ensures that an effective collaboration between such parties would be severely inhibited.⁶⁰ It is essential for the functioning of a dynamic and competitive market that companies positioned in all aspects of a particular market have the freedom to determine commercial strategy and Visa Europe submits that this position is reflected in the absence of any similar arrangements on the Boards of comparable regulated companies.

B. The PSR's general direction on the publication of Board minutes

- 5.20 The PSR proposes to make a general direction requiring "*all Operators to publish board minutes, including votes, in a timely manner from 1 April 2015*".
- 5.21 Visa Europe already has a number of measures in place to communicate with its members and service-users and strongly believes the PSR's proposed general direction regarding transparency is unnecessary, disproportionate and counterproductive. This is explained in more detail below.

(i) Visa Europe's existing disclosure channels

- 5.22 Visa Europe sets out below the principal key disclosure channels it presently uses to engage with its members and service-users:
- 5.23 **Annual Reports and Financial Statements:** The present disclosed contents in the annual reports and financial statements already provide stakeholders, including service-users, with detailed current information, including:
- Strategic reports with respect to Visa Europe's performance, strategy, business model, risk management, corporate responsibility and key management which are issues that are routinely discussed; and
 - Financial statements that address the directors' report, independent auditors' report, consolidated income statement, consolidated balance sheet and cash flows, amongst other things.
- 5.24 Visa Europe notes that its present annual report and financial statement regime extends significantly beyond what is required of a private limited company and adequately considers the need to regularly inform stakeholders, including service-users, of strategic decisions of the company.
- 5.25 **Visa Online:** Visa Online is a web portal for Visa Europe members providing all documents relevant to the Visa Europe scheme. These include member letters, product information, member newsletters, Visa Europe Operating Regulations and technical manuals. While Visa Online is primarily intended for a Visa Europe member audience, it contains a specific subsection for vendors (including third party processors).
- 5.26 **Member Letters:** Visa Europe makes extensive use of 'member letters' to communicate developments with its acquirer and issuer members and, where relevant, third party processors. In

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It is a well-known result in economics that when incentives differ amongst parties and each party is essential to an outcome there is a risk of 'hold-up' or 'double-marginalisation'. Each party may try to extract the most beneficial outcome to itself without taking account of the impact it has on other parties. Where there is asymmetric information or uncertainty between parties one of the outcomes of this 'hold-up' problem may be that beneficial projects are not able to be implemented. See for example Grout, P. 1984. Investment and wages in the absence of binding contracts: a Nash bargaining approach. *Econometrica* 52, 449–60. See also Tirole, J. 1986. Procurement and renegotiation. *Journal of Political Economy* 94, 235–59.

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2014, Visa Europe sent 103 member letters and 9 UK specific letters. Member letters are issued whenever a change is made to the rules, products, services and systems. Generally a member letter is shared with all members two weeks after the relevant Board decision has been taken.

- 5.27 **Visa Europe Board Highlights:** Following every Visa Europe Board meeting, Visa Europe sends its members a bulletin called 'Visa Europe Board Highlights'. Visa Europe also publishes an e-bulletin, 'The Brief', which is sent to all members.
- 5.28 **Insights:** Visa Europe hosts a biennial meeting for members and non-members (including merchants, financial regulators and mobile networks) to update them on Visa Europe developments. Four similar events that are more tailored to regional markets Visa Futures, are planned for 2015.
- 5.29 **Regulatory updates:** In 2014 Visa Europe held regulatory workshops in London, Vienna, Stockholm, Paris, Milan, Sofia, Athens and Madrid with its members. Visa Europe also held three member conference calls on the IFR and Payment Services Directive II. Visa Europe has also launched a new flash bulletin called "Regulatory and Policy Update" for members.
- 5.30 **Press releases:** Visa Europe regularly updates all stakeholders on its key corporate developments as and when these occur. For example, during 2014, over 20 press releases were published on Visa Europe's website.
- 5.31 **Websites:** Visa Europe notes that it has a number of public websites which members and other stakeholders can visit to obtain information about Visa Europe. These include:
- Press releases <http://www.visaeurope.com/newsroom/>
 - Visa vision <http://vision.visaeurope.com/>
 - Governance <https://www.visaeurope.com/about-us/governance/>
 - Annual report <http://www.visaeurope.com/newsroom/annual-report>
 - Cardholder website <http://www.visa.co.uk/goldenspace/promotions/>
 - Twitter: @visaeuropenews
- 5.32 **Communication regarding European Commission Commitments:** A further example of effective stakeholder engagement by Visa Europe relates to the implementation of its Commitments given to the EU Commission in early 2014. In particular, Visa Europe informed members that, provided certain conditions relating to security and transparency set out in the Commitments were met, it would be offering a new programme to enable cross-border acquirers to choose between different interchange rates. In order to participate in this programme (officially called the "Cross-border Domestic Interchange Programme" or "CBDIP"), Visa Europe offered a substantial amount of assistance both to acquirers and to merchants.
- 5.33 In particular, Visa Europe used its official communication channels and held a number of member calls and meetings during which a number of points relevant to the practical implications of Visa Europe's Commitments were discussed. This included a discussion of the European financial passporting rules, the use of subsidiaries, and associate membership applications. These communications were also supported by a number of member letters.
- 5.34 Visa Europe, however, has gone further in this context recognising that acquirers' and merchants' individual circumstances all affect how best they can register for, and participate in, the CBDIP. Accordingly, Visa Europe has engaged directly with many individual acquirers (and in some cases their merchants) where they have asked for assistance. For example, in the fuel sector, the business models of certain fuel suppliers gave rise to a number of particular issues. Through a series of calls involving the merchant and Visa Europe, a practical solution was reached.

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- 5.35 Visa Europe has an all-day merchant meeting scheduled for March 2015. It will cover a wide range of topics relating to Visa Europe's interaction with merchants, including the impact of recent regulatory change and discussions around the opportunities for cards to displace cash.

(ii) PSR's proposal to publish confidential board minutes

- 5.36 It is clear from the above that Visa Europe has a significant number of measures in place to maintain transparency and clarity with stakeholders, including service-users. Indeed, the PSR has failed to identify any specific concerns in relation to Card Operators' transparency measures, which would justify intrusive regulation requiring Card Operators to publish board minutes.
- 5.37 Visa Europe reiterates that, as an economic regulator, the PSR should only act on the basis of a clearly identified theory of harm and any regulatory action should be proportionate to the harm identified. Visa Europe considers that the PSR's proposal to require disclosure of board minutes does not satisfy these criteria and will result in significant unintended consequences, to the detriment of Visa Europe and its service-users. Visa Europe's concerns are set out below.
- 5.38 **First**, it is plain that the matters deliberated in a Board meeting typically cover commercially sensitive information. While Supporting Paper 3 has highlighted that appropriate redaction will be permitted to minimise disclosure of such information, Visa Europe submits that this may lead to unforeseen results. Indeed, in any given Board meeting a significant proportion (and on occasions all) of the discussions would be commercially sensitive and would necessitate redaction. It is quite possible that this may leave little, if any, material information disclosed in Board minutes. This highlights the ineffectiveness and unnecessary compliance costs of such a proposal.
- 5.39 **Secondly**, the PSR's proposals could lead to a weakening of corporate governance. Boards of payment systems participants may be disincentivised to discuss and record matters thoroughly at Board level. This may result in the unintended, but entirely possible, consequence of weakened corporate governance across the payment services industry, resulting in lesser innovation and reduced competition.
- 5.40 **Thirdly**, Visa Europe has considered the disclosure regime of certain regulated sectors, including utilities and financial services sectors, both of which are highly regulated and is not aware of routine, public disclosure of Board minutes. Similarly, in respect of UK listed companies (that are required to adopt an enhanced disclosure regime compared to private companies), there is no mechanism to require the disclosure of Board minutes as a matter of routine.
- 5.41 More appropriately, listed companies are required to comply with a robust and stringent regime for disclosure through annual reports (with specific disclosure requirements), shareholder circulars and disclosure obligations under the UKLA's Disclosure and Transparency Rules. In summary therefore, Visa Europe submits that the routine disclosure of all Board minutes proposed by the PSR significantly extends beyond any present regime of which Visa Europe is aware and that its implementation is likely to be a disproportionate burden on all payment services participants or, in the alternative, largely ineffective in light of the extensive redactions that will be necessary due to the confidential nature of discussions at Board level.
- 5.42 **Fourthly**, Visa Europe notes that the Consultation Paper does not evaluate the possible impact of EU and UK competition law on the PSR's transparency proposals. As the PSR will be aware, the EU courts, as well as the CMA and the European Commission, have emphasised the need for economic operators to independently adopt their respective commercial approaches without reference to their competitors and that in this context competition law strictly prohibits economic operators from disclosing their intentions or decisions on the market to actual and potential

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competitors.⁶¹ Visa Europe notes that there appears to be a clear tension at present between this proposal and the established competition law enforcement regime on information exchanges.

- 5.43 In view of the above, Visa Europe submits that routine disclosure of all Board minutes would not be an appropriate method of achieving appropriate transparency within the payment systems industry and indeed would be likely to have perverse unintended consequences. In Visa Europe's view, these measures are disproportionate and contrary to the PSR's Statutory Obligations under the Act⁶²; in particular, given Visa Europe's existing transparency measures in conjunction with the PSR's extensive statutory powers to compel the production to it of confidential information under section 81 of the Act. Visa Europe therefore invites the PSR to reconsider its proposals in this regard insofar as they apply to Card Operators.

⁶¹ Case C-8/08 (June 2009) *T-Mobile B.V and others v Nederlandse Mededingingsautoriteit* (establishing that economic operators must act independently in the market and in particular that public disclosures concerning future market conduct that may influence actual or potential competitors are strictly prohibited); also see the Netherlands Authority for Consumers and Markets Case 13.0612.53 (establishing that public disclosures of planned commercial conduct could be a breach of competition law if such disclosure influenced the behaviour of competitors).

⁶² Section 53(b)

6 OBSERVATIONS ON THE PSR'S PROPOSALS ON ACCESS TO CARD PAYMENT SYSTEMS

- 6.1 As the PSR is aware, under Article 28 of the Payment Services Directive (as implemented by Regulation 97 of the Payment Services Regulations 2009) Visa Europe is required to have objective, proportionate and non-discriminatory rules for access to its system that do not prevent, restrict or inhibit access or participation more than is necessary.
- 6.2 The PSR acknowledges that since the introduction of the Payment Services Directive, the type of organisations eligible to join the card payment systems as license or members (i.e. Direct PSPs) has broadened to include a number of nonbank institutions (such as PIs). PSPs have not raised any concerns regarding the regulatory status criterion for gaining access to Visa's scheme.⁶³
- 6.3 The PSR also acknowledges that card payment systems have also recently on-boarded a number of new members or licensees and that Visa had **CONFIDENTIAL** new members in the UK in the year to April 2014, which included **CONFIDENTIAL** – no membership applications from UK entities were declined.
- 6.4 In view of the above, Visa Europe considers that there are no material issues in relation to access to its scheme which require additional regulation to be imposed by the PSR.

The PSR's proposed Reporting Rule

- 6.5 The PSR is proposing that Card Operators be subject to a reporting requirement which includes: (a) publishing their access rules; and (b) the provision of an annual compliance report to the PSR.
- 6.6 While Visa Europe does not object to the requirement to publish its access rules, it considers the requirement to provide the PSR with a compliance report unnecessary and disproportionate, in the absence of any material concerns regarding access to its scheme.
- 6.7 The PSR states in Supporting Paper 4 that the proposed Reporting Rule should apply to both the interbank and card payment systems, as concerns have been raised in relation to access to both. However, Supporting Paper 4 only sets out the following limited concerns raised in relation to access to card payment systems:
- *"While stakeholders raised no specific concerns over the technical and operating criteria for securing Direct Access to the card payment systems, some provided **general comments** that the MasterCard and Visa technical criteria and requirements are onerous and complex."*⁶⁴
 - *"Only a small number of PSPs raised concerns over the risk and liquidity management requirements (in particular the collateral requirements) of the card payment systems."*⁶⁵
 - *"Stakeholders noting that information from the card payment systems is not always clear or readily available. Transparency concerns were raised in particular in relation to access criteria and processes and procedures, as well as in relation to fees, which some stakeholders said could be difficult to assess."*⁶⁶
- 6.8 Visa Europe submits that the concerns expressed above are not sufficient to justify the imposition of a regulatory requirement to provide regular compliance reports. The comments above amount to some general observations regarding certain stakeholders finding some aspects of the access

⁶³ Supporting Paper 4, para. 4.51

⁶⁴ Supporting Paper 4, para. 4.64

⁶⁵ Supporting Paper 4, para. 4.75

⁶⁶ Supporting Paper 4, para 4.100

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criteria difficult to understand and very limited concerns over the risk and liquidity management requirements. The PSR has not carried out any analysis of whether these concerns are justified, require the imposition of a reporting requirement or whether the objectives of the PSR's reporting requirement can be met by less onerous means.

- 6.9 Moreover, Visa Europe does not understand how submitting a compliance report to the PSR will resolve concerns relating to the supposed complexity of Visa Europe's scheme rules. To the extent there is any such uncertainty, Visa Europe submits that the PSR's proposed requirement for Card Operators to publish their access rules is sufficient to resolve these limited concerns.
- 6.10 Visa Europe therefore requests the PSR to reconsider imposing a requirement that Card Operators be required to submit detailed compliance reports to the PSR on access to their schemes.

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7 OBSERVATIONS ON INTERCHANGE FEES

- 7.1 Visa Europe notes that the PSR is proposing to consider further action on interchange fees only in the event that the adoption of the IFR is delayed, or the implementation of its domestic fee caps is deferred to a later and separate date from the caps on cross-border interchange fees. Such action would be taken using the PSR's powers under the Act or using its concurrent competition powers.
- 7.2 As set out in Section 2 above, the IFR is likely to be agreed by the European Parliament and Council later this month (January 2015) and the IFR caps on interchange fee are expected to come into force in August 2015 while the other rules set out in the IFR should be implemented by February 2016.
- 7.3 In view of the above, Visa Europe submits that there remains no reason for the PSR to take further action on interchange fees.
- 7.4 However, Supporting Paper 5 states that even if the IFR is adopted, the PSR may still consider whether it is appropriate to take any further action using its powers under the Act or its or concurrent competition powers. As the PSR has not detailed what such action would entail, Visa Europe is unable to comment fully at this stage.
- 7.5 Visa Europe notes that prior to taking any action, either using its powers under the Act or its competition powers, the PSR must undertake a full consultation exercise detailing the reasons why it believes such action is necessary and must provide Visa Europe and other stakeholders an opportunity to respond to any proposal. Visa Europe's position is that there is no basis for any unilateral UK-centric regulatory intervention by the PSR, given recent EU developments.

8 THE PROPOSED PSR PRINCIPLES

8.1 Turning to the PSR's Proposed Principles (the "**Proposed PSR Principles**"), Visa Europe notes that these are intended to create "*legally-binding Principles to apply to all participants in designated payment systems*".⁶⁷

8.2 Visa Europe has serious concerns in relation to the Proposed PSR Principles. First, the legal status of the Proposed PSR Principles is unclear and, as presently proposed, may be *ultra vires*, in that they go beyond the PSR's jurisdiction as an economic regulator under the Act. Secondly, the substance of the Proposed PSR Principles is, as a result of their "one size fits all" approach, too broad and ambiguous to create clear-cut obligations for Operators. Visa Europe's concerns are reinforced by the PSR's proposal to sanction breaches of the Proposed PSR Principles with the imposition of fines.

A. Uncertain legal status

(i) The Proposed Principles are contrary to the intention of Parliament that the PSR act as an economic regulator

8.3 Visa Europe is concerned that imposing legally binding conduct obligations in a blanket manner on all Operators, outside a system of licences, approvals or other general condition scheme, is fundamentally inconsistent with the PSR's legislative remit. The intention of Parliament was clear when it passed the Act: the PSR was to act as an economic regulator, not as a broad conduct regulator. This is reflected in the final version of the Act and acknowledged by the PSR in its draft Objectives Guidance.

8.4 In Visa Europe's view, the PSR has not properly taken into account the fundamental distinction between "conduct regulation" and "economic regulation". Recognition of this distinction is vital when considering the PSR's statutory remit.

8.5 Conduct regulation is used to regulate the behaviour of participants in a relevant market. In the financial services context, the overarching purpose of conduct regulation is to ensure that regulated firms act honestly, fairly and professionally in accordance with the best interests of customers⁶⁸. In the worlds of the FSA (as it then was) the role of a conduct regulator concerns "*changing the culture and conduct of financial services firms and the markets they operate in – and as a result, to inject trust back into financial services*".⁶⁹ The emphasis of conduct regulation is therefore on how regulated firms are run on a day-to-day basis. In particular, it concerns the steps that are taken to ensure that customers are able to make well-informed decisions with regard to products or services that are suitable to their specific needs.

8.6 By contrast, economic regulation is typically focussed on markets where insufficient competition potentially results in market failure leading to consumer detriment. The aim of economic regulation is to remedy such market failure and prevent any associated consumer detriment. The focus of economic regulation is not typically geared towards the day-to-day conduct of market participants. This is addressed by conduct regulation.

⁶⁷ Supporting Paper 6, para 6.7

⁶⁸ See the FCA's Conduct of Business Sourcebook.

⁶⁹ Clive Adamson speaking as the Director of Supervision at the FSA to the Westminster Forum, 5 March 2013, (<http://www.fca.org.uk/news/speeches/journey-towards-a-conduct-regulator>). In addition, the FSA published an approach to regulation paper for the FCA in June 2011, which detailed how the new body would approach regulation. Paragraph 1.4 of the regulation paper states that "*The FCA will be responsible for regulating conduct in retail and wholesale markets*", with paragraph 1.9 stating that "*the creation of the FCA provides an opportunity to develop a new approach to conduct regulation*". Paragraph 4.9 states that "*a key task of the FCA will be continuing to ensure that the conduct of market participants is compatible with fair and safe markets*".

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8.7 Nowhere is this distinction so marked as in the present context. Parliament was clear in its intentions. It set up the FCA as a fully-fledged conduct regulator. In contrast, it established the PSR as an economic regulator with a set of narrowly defined Statutory Objectives and Principles. While the PSR itself appears to acknowledge this in the Consultation Paper⁷⁰, it is critical that this distinction is not blurred in the PSR's approach and guidance to regulation.

8.8 Visa Europe is therefore surprised that the Proposed PSR Principles seek to establish what appears to be a conduct-based regulatory approach. Indeed, the Proposed PSR Principles are to a large extent influenced by the FCA's Principles for Business. Further, the PSR itself admits that the Proposed PSR Principles are intended to establish "*behavioural standards*"⁷¹ to which all participants must adhere.⁷²

(ii) The Proposed PSR Principles do not qualify as "general directions"

8.9 Visa Europe notes that the Consultation Paper does not specify the legal basis of the Proposed PSR Principles. Visa Europe also notes that there is no express power in the Act for the PSR to adopt broad and uniform conduct standards for all Operators. It is therefore surprising that the PSR has not provided its views on the legal basis of the Proposed PSR Principles.

8.10 Visa Europe can only presume that the PSR has in mind that the Proposed PSR Principles should have the status of "general directions" under section 54(3)(a) of the Act. However, even then, Visa Europe does not consider that this can provide a proper legal basis for the Proposed PSR Principles.

8.11 Under section 54(2), any general direction, in order to be valid, must either be in relation to "specified actions" or clearly articulated "standards". Visa Europe considers that the PSR Principles do not satisfy either test, as currently drafted. In particular, they do not relate:

- to any "specified actions" which when given its ordinary and natural meaning⁷³ refers to precisely defined obligations in respect of specific identified issues; nor
- to any "standards" which similarly refers to precisely defined features of a system which can be accurately measured and verified.

8.12 Visa Europe also notes that the statutory test reflects the PSR's status as an economic regulator. In this sense it reflects the regulatory process set out in Framework Consideration 4 whereby specific regulatory remedies should be proportionate and should only be imposed where the PSR has sufficient evidence to support the remedy.

8.13 By contrast, the FCA's power to formulate legally binding principles derives from a much wider statutory provision, namely its "General rule-making power". This enables the FCA to "*make such rules applying to authorised persons [...] as appear to it to be necessary or expedient for the purpose of meeting any of its regulatory objectives.*"⁷⁴ No equivalent power is given to the PSR which reflects its narrower mandate as an economic regulator.

⁷⁰ Consultation Paper 14/1, page 7: "*The PSR is a subsidiary of the Financial Conduct Authority (FCA), but it is an independent economic regulator, with its own objectives and governance.*" Consultation Paper 14/1, page 9: "*As an economic regulator, our focus will be on making markets work well and our decisions will be underpinned by evidence.*" Supporting Paper 6, paragraph 6.45: "*We are an economic regulator and we share competition powers with other UK and EU competition authorities.*" Supporting Paper 6, Annex 1, paragraph 1.1: "*We are an economic regulator, and share powers with the competition authorities.*"

⁷¹ Supporting Paper 6, para. 6.2

⁷² The PSR's Proposed Principle 2 itself makes an express reference to "proper standards of conduct".

⁷³ The PSR will be aware that, unless expressly stated otherwise, statutory words should be given their ordinary and natural meaning: *R v Harris* [1836] 7 C & P 466, *Whitely v Chappel* [1868] LR 4 QB 147, *Fisher v Bell* [1961] 1 QB 394.

⁷⁴ Financial Services and Markets Act 2000, section 137A

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8.14 Visa Europe considers that the issues with the Proposed PSR Principles do not stop there. In particular, the scope of Proposed PSR Principles 1-3 ("**Proposed Principles 1- 3**") is too broad to allow designated systems to self-assess compliance with any reasonable degree of certainty. They therefore suffer from an inherent lack of legal certainty.

8.15 The remainder of Visa Europe's submissions on the Proposed PSR Principles in this Section 8 is without prejudice to its concerns to the lack of a sound legal basis for the Proposed PSR Principles.

(iii) The Proposed PSR Principles are contrary to the duty of the PSR to act proportionally in imposing burdens on Operators

8.16 Under Section 49(3)(c), the PSR is obliged to ensure that any regulatory measure it takes is consistent with the regulatory principles contained in Section 53. This includes the requirement that any measure must be "proportionate". The Consultation Paper provides no evidence of actual or likely service-user harm which the Proposed PSR Principles seek to address. Instead, the adoption of the Proposed PSR Principles appears to be driven by a desire to impose precautionary, ex-ante regulation on the entire sector.

8.17 In Visa Europe's view, in the absence of any evidentially sound theory of harm and any impact assessment, any adoption of the Proposed PSR Principles would be inconsistent with the PSR's general statutory remit and the principle of proportionality (section 53(b)).

(iv) The Proposed PSR Principles are contrary to the duty of the PSR to take account of objective differences between operators

8.18 Section 53(f) of the Act requires the PSR to recognize differences between different regulated entities. Accordingly, imposing a set of "one-size-fits-all" principles on all Operators is inconsistent with this statutory requirement. This is especially the case when those principles give rise to far-reaching, legally binding (positive and negative) conduct obligations as they do here. Indeed, there is no analysis in the Consultation Paper of why a single set of requirements or standards for both interbank systems and card schemes is required and proportionate. The fundamental difference between these two categories of market participants is discussed in Section 2 at paragraph 2.13.

8.19 Visa Europe considers that there is no objective justification (or indeed any practical need) for such uniform rules. Visa Europe is also concerned that the PSR is seeking to shift the burden of interpreting and applying these uniform rules to the Operators themselves.

8.20 Visa Europe considers that at this early stage and in the absence of any material legitimate industry concerns, the PSR should simply maintain a watching brief over the market conduct of designated operators for the time being. Over time it can then assess to what extent specific or industry-wide market failures need to be addressed by it (in a targeted and proportionate manner).

(v) The legal basis for imposing penalties for breach of the Proposed PSR Principles is unclear

8.21 The status of the Proposed PSR Principles is particularly relevant to penalties. Visa Europe notes that the PSR's Consultation Paper does not make any reference to a proposal to impose fines for a breach of a Proposed PSR Principle (despite their proposed legally-binding nature).

8.22 Under the Act⁷⁵ a financial penalty can only be imposed in respect of a "compliance failure", i.e. a breach of "direction" or a "requirement". The PSR's draft penalties guidance reflects this position.⁷⁶

⁷⁵ Sections 71 and 73

⁷⁶ Supporting Paper 6, Annex 5, section 1

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- 8.23 It is important that any penalty guidance of the PSR expressly acknowledges that a penalty cannot be imposed for a breach of the Proposed PSR Principles if these are retained in some form (irrespective of their legal status).
- 8.24 Given that the Proposed PSR Principles are by their very nature general and lack legal certainty, they are not an appropriate basis for enforcement action by the PSR.

B. The scope of the Proposed PSR Principles is too broad and ambiguous

- 8.25 In addition to its serious concerns set out above, Visa Europe has the following specific comments in relation to the Proposed Principles 1-3.

(i) Proposed Principle 1

- 8.26 Proposed Principle 1 states that *"A participant must deal with its regulators in an open and cooperative way and must disclose to the PSR appropriately anything relating to the participant of which the PSR would reasonably expect notice"*.
- 8.27 The standard set is so vague and cast so widely that it fails to provide Operators with any practical guidance as how to ensure full compliance with the obligations imposed on them.
- 8.28 The PSR attempts (unsuccessfully) to put some flesh on the bones of this Principles. It says that it does not expect participants to inform it of the minutiae of their business and expects participants to exercise sound judgment in determining the developments and changes that the PSR should be notified of. However, exactly what the PSR expects in practice remains unclear. It provides no practical guidance on how such judgment ought to be exercised or what the substance of this Principle entails. Operators are not (and cannot be expected to be) in a position to self-assess compliance against a standard which refers to the PSR's expectations from time to time.
- 8.29 The compliance burden that such an ambiguous and far-reaching obligation, possibly backed up by penal sanctions, imposes is considerable. In practice, the imposition of a legally binding Proposed Principle 1 would lead to over-notifications by Operators, wasting the resources of both Operators and the PSR.
- 8.30 Visa Europe understands that its concerns are supported by the FCA's experience with similar principles. Proposed Principle 1 is based on the FCA's Principle 11 of the Principles for Business (*"A firm must deal with its regulators in an open and cooperative way, and must disclose to the appropriate regulator appropriately anything relating to the firm of which that regulator would reasonably expect notice"*). As the PSR is likely aware, there is often considerable uncertainty and confusion surrounding the discharge of firms' obligations under the FCA's Principle 11. This has resulted in the FCA receiving many irrelevant and unnecessary notifications, while at the same time relevant disclosures may inadvertently not be made.
- 8.31 Visa Europe submits that to the extent necessary, and consistent with the PSR's duty under Section 53(f) of the Act to act proportionally and recognize differences between Operators, more specific transparency and disclosure rules ought to be developed for individual systems or classes of systems over time, following a careful analysis of the applicable theory of harm. Any such more specific measures must reflect the fact that the PSR has the general power to proactively demand the production of relevant internal documents, including board minutes, under its general powers of investigation.

(ii) Proposed Principle 2

- 8.32 The Proposed Principle 2 states that: *"A participant must observe proper standards of conduct, and must refrain from activity which that participant should reasonably have expected to restrict or*

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prevent another participant from complying with its regulatory obligations in relation to payment systems or services provided by payment systems.”

- 8.33 The Proposed Principle 2 expressly acknowledges that it imposes a conduct regulation measure as noted above in this Section 4, Visa Europe considers that this is inappropriate.
- 8.34 Further, as with the Proposed Principle 2 there is no analysis of the specific concerns which the PSR is seeking to address nor any practical guidance as to what the “proper standards” may be for different Operators or classes of Operators.
- 8.35 Visa Europe is also puzzled by the second part of the Proposed Principle 2 (to “... refrain from activity”). If this specific articulated concern is the rationale for the Proposed Principle 2 then the imposition of the general “proper standards” obligation is clearly excessive and disproportionate. Instead, the PSR ought to develop the concerns it has in this regard and address these through targeted regulatory measures. If the PSR does not have any specific concerns in this regard at present it would support the view that the proposed measure is unnecessary and disproportionate. Finally, the competition rules on dominance provide further tools to address inter-operability or related concerns. For these reasons the Proposed Principle 2 is in Visa Europe’s view unclear, disproportionate and duplicative and ought not to be adopted.

(iii) Proposed Principle 3

- 8.36 The Proposed Principle 3 states that “*an Operator or Infrastructure Provider must ensure it has, or has access to, adequate financial resources to ensure that it is able to carry out its functions and activities in relation to the regulated payment system it operates in the case of an Operator, or the regulated payment system or systems whose central infrastructure it provides or controls in the case of an Infrastructure Provider, including resources to: (a) cover potential general business losses and debts as they fall due; (b) continue operations and services as a going concern if those losses or debts materialise; and (c) comply with its regulatory obligations in relation to payment systems and services.*”
- 8.37 Visa Europe acknowledges the (self-evident) need to have adequate financial resources to operate. However, Visa Europe cannot identify any relevant market failure as regards its own operations and the operation of any other card scheme provider. As such, there is no evidential basis for the regulatory measure.
- 8.38 It is important to note that Visa Europe is also not under any obligation to provide its services. It is not subject to any “universal service” obligation and is not a provider of services of “last resort” (as they exist in certain other regulated industries). Visa Europe’s members are free, subject to complying with all applicable Visa rules, to discontinue using the Visa Europe scheme. However, such a scenario is of course wholly hypothetical in practice. Visa Europe is adequately financed and will continue to operate and innovate.
- 8.39 Further, Visa Europe does not envisage that the PSR should impose what are in effect akin to minimum standards of regulatory capital. Visa Europe considers that if the PSR does wish to implement such a requirement, the implementation should be subject to further consultation so that the economic and regulatory rationale for such a measure for individual designated parties (or classes of parties) can be articulated by the PSR and the industry can respond to the analysis in a meaningful manner.
- 8.40 At paragraph 6.43 of Supporting Paper 6, the PSR states that Card Operators are already subject to the ECB’s Oversight Framework for Card Payment Schemes and therefore the additional costs of complying with Principle 3 should be modest. The ECB’s Oversight Framework requires Visa Europe to “*manage and contain financial risks in relation to the clearing and settlement process*”.

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Visa Europe does not consider that this is equivalent to the financial resources requirements advanced by the Proposed Principle 3. Moreover, the ECB's Oversight Framework does not envisage penal sanctions for breach of this principle. Even to the extent that there is any overlap, this cannot provide a legal basis for the imposition of the Proposed Principle 3 and, in fact, is another instance of the PSR duplicating existing regulation.

(iv) The Additional Proposed Principles

- 8.41 In paragraph 6.30 of Supporting Paper 6, the PSR consults on a number of further proposed principles which relate to (i) integrity; (ii) skill, care & diligence; (iii) management & control; (iv) governance; (v) service-users' interests; (vi) conflicts of interest (the "**Additional Proposed Principles**").
- 8.42 As with the Proposed PSR Principles 1-3 the PSR has not provided any evidence, nor developed a theory of harm, to explain why these Additional Proposed Principles are necessary. Further, the PSR has not set out the market failure they are intended to address nor whether any identified market failure could be better addressed by other measures.
- 8.43 Given the serious compliance burdens that the Additional Proposed Principles are likely to impose, Visa Europe submits that it would be inappropriate and disproportionate to impose any of these principles without first clearly articulating the reasons why such principles are necessary and consulting stakeholders on its views in this regard.
- 8.44 Further, Visa Europe notes that a number of the Additional Proposed Principles seek to address issues which the PSR already seeks to address by specific regulatory proposals (see for example the Additional Proposed Principle 4 ("Governance") and Additional Proposed Principle 5 ("Service-user representation")).
- 8.45 In summary, Visa Europe is very concerned that the adoption of the Proposed PSR Principles (and any Additional Proposed Principles) would in practice amount to an attempt to implement a "short-cut" to the PSR's regulatory function which would give rise to bad rules, inefficient conduct by Operators, regulatory duplication and unnecessary regulatory compliance costs.

9 PSR POWERS AND PROCEDURES

- 9.1 In addition to submissions made above in relation to the general regulatory approach of the PSR (including in relation to the Proposed PSR Principles), Visa Europe has a number of additional comments regarding the specific powers and procedures proposed by the PSR in Supporting Paper 6, which are addressed in this section. Overall there are, however, a number of key open issues which limit Visa Europe's ability to provide a fuller response at this point in time.

Regulatory approach (including draft Objectives Guidance and Administrative Priorities)

- 9.2 Visa Europe is concerned as to the PSR's proposed exercise of its powers under the Powers and Procedures Guide. In Visa Europe's view, the PSR must determine, prior to exercising its powers, whether there are circumstances suggesting that the Statutory Objectives have been undermined. Every exercise that the PSR makes of its powers should strictly derive from the statutory framework set out in the Act.
- 9.3 In Visa Europe's view, in discharging its powers, the PSR must have regard to its duties as a public body. As a public body, the PSR must both be fair and be seen to be fair. A key aspect of this duty is that the PSR must have regard to the principles of natural justice in its decision-making. Visa Europe is of the view that, in order for the PSR to make absolutely clear that it is discharging its duties as a public body, it should allow oral representations. Visa Europe refers the PSR to DEPP 3.2.15G(2) of the FCA Handbook in this regard, which allows for the possibility of oral representations in similar instances.
- 9.4 With regard to the draft Objectives Guidance, as set out in Section 2, Visa Europe considers that a more detailed discussion is necessary in the main body of the Guidance as to how the Statutory Principles condition the PSR's approach to regulatory policy and enforcement. Visa Europe considers that this could effectively be done by reference to the practical Framework Considerations set out in Section 2.
- 9.5 Further, the current Objectives Guidance as it stands does not go far enough in articulating how the Statutory Objectives will be applied by the PSR. In Visa Europe's view, further explanation should be provided with respect to the approach the PSR will take when its objectives conflict. For example, whether any of the objectives can take precedence over the others and, if so, in what circumstances; and/or what other matters the PSR will have regard to in the case of conflict.
- 9.6 With respect to the PSR's proposed Administrative Priority Framework, Visa Europe notes that to foster a sense of market confidence, the PSR needs to approach its regulatory and policy decisions with a sense of longevity that shows that the PSR is willing to fully consider the consequences of any changes that it is contemplating in light of clearly articulated guiding principles.

Directions and Requirements

- 9.7 At paragraph 4.1 of Annex 3 to Supporting Paper 6, the PSR sets out criteria for the giving of directions or imposition of requirements. Visa Europe considers that additional criteria should be taken into account. As mentioned above, before giving a direction or imposing a requirement, the PSR must come to a view that there are circumstances suggesting that the Statutory Objectives have been, or are likely to be, undermined resulting in clear and measurable harm to consumers. Unless the PSR has come to such a view, which it can justify, it risks acting *ultra vires*. Visa Europe

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reminds the PSR that in discharging its function of giving directions, it must so far as is reasonably possible act in a way which advances one or more of the Statutory Objectives.⁷⁷

- 9.8 Paragraph 4.2 of Annex 3 to Supporting Paper 6 allows representations to be made in writing before the giving of a direction or imposition of a requirement. Visa Europe believes that oral representations should also be allowed (if requested).
- 9.9 Paragraph 5 of Annex 3 sets out the procedure for deciding whether to make a general direction or generally imposed requirement. In relation to directions and requirements relating to specific persons or a limited class of persons, any initial consultation should only take place with the persons or class of persons affected. The need for a second round of public consultation needs to be assessed on a case-by-case basis.
- 9.10 Visa Europe notes that under the Act decisions by the PSR to adopt general directions or generally imposed requirements are not capable of being appealed or referred to an independent body for a review on the merits. The only remedy available to a party aggrieved by such a decision is to apply for judicial review. This is different to the FCA and the PRA procedures, as all decisions by the FCA and PRA are capable of being referred to the Upper Tribunal for a full “on the merits” review. The lack of a similar appeal right means parties can only challenge general directions or generally imposed requirements by the PSR on judicial review grounds. This reinforces Visa Europe view that the PSR should exercise significant caution in giving general directions or imposing requirements and such regulatory measures must in each case be based on critically tested and robust evidence in relation to the purported market failure and the proportionality of the PSR’s proposed measure.

Skilled Persons Reports

- 9.11 Visa Europe has concerns with regard to the wide-ranging power of the PSR to appoint a Skilled Person to produce a report or require a participant to do so under paragraph 27 of Annex 3 to Supporting Paper 6. Visa Europe’s particular concern is that this power should not be overused by the PSR. In addition to the fact the power can only be exercised if the PSR has come to a view that there are circumstances suggesting that the statutory objectives have been undermined, the use of this power should in every case be proportionate. It is often the case that Skilled Persons reports are costly and disruptive and should not be undertaken lightly by the PSR. In the year from 1 April 2013 to 31 March 2014, the total estimated cost of FCA skilled persons reports to FCA-regulated firms was £145.7 million, with a median cost of £160,000.⁷⁸
- 9.12 As a public body, the PSR has a common law duty to retain the decision-making discretion that has been granted to it. It is essential that as part of this duty, the PSR does not improperly delegate any of its powers. In order to demonstrate the fact that there has not been, nor will be, an improper delegation of powers to Skilled Persons, the PSR should only use its Skilled Persons powers sparingly in cases where the expertise of the skilled person is absolutely necessary to the judicious exercise of the PSR’s other powers.
- 9.13 Visa Europe recalls that the financial industry as a whole has expressed concerns over the use of Skilled Persons reports by the FCA and PRA. These concerns were captured in two letters from the House of Commons Treasury Committee, both dated 23 June 2014 to the FCA and PRA respectively.

Investigative powers

⁷⁷ Section 49(1)

⁷⁸ FCA Annual Report 2013/2014, Appendix 1

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- 9.14 With regard to the PSR's investigative powers under the Act, paragraph 28 of Annex 3 to Supporting Paper 6 sets out the PSR's power to appoint investigators. Visa Europe is of the view that this power should only be exercised if the PSR has come to a view that there are circumstances suggesting that the statutory objectives have been undermined resulting in clear consumer detriment. This approach would be in line with the best practice of leading economic regulators such as the CMA. The CMA's prioritisation guidelines make it clear that it will "*focus [its] efforts and resources on deterring and influencing behaviour that poses the greatest threat to consumer welfare, and intervene in order to protect consumer welfare and, in the process, drive higher productivity growth.*"⁷⁹ There is therefore a need for a clearly articulated and appropriate evidential threshold to be met before investigators can be appointed.
- 9.15 Further, paragraph 32.2 of Annex 3 to Supporting Paper 6, states that if a notice of the appointment of investigators is issued, it should specify the reasons for their appointment. Given the serious impact of an investigation, the PSR must clearly articulate the objective reasons for the investigation and how it believes that there are circumstances suggesting that the statutory objectives have been undermined. Visa Europe is of the view that the proposals should at least set out the reasons why the PSR has come to the view that there are circumstances suggesting that the statutory objectives have been undermined.
- 9.16 Visa Europe is also of the view that, when changes are proposed to the scope of an investigation, further scoping discussions, as referenced in paragraph 33 of Annex 3 to Supporting Paper 6, must be undertaken with the parties concerned so that the PSR can discharge its duty as a public body to consult with those parties affected by its decisions. Any failure to consult in the event of changes of scope will undermine any efforts made in consultation at the initial stage of an investigation.
- 9.17 Where an investigation has been commenced, it will be more appropriate, in most cases, for the PSR to exercise its formal information powers (as set out in paragraph 37 of Annex 3 to Supporting Paper 6), as opposed to requesting information at a voluntary interview. While a participant may be happy to attend a voluntary interview, the context of the investigation means that the clearly defined lines of communication that the formal use of the PSR's information powers establishes are more appropriate.
- 9.18 In managing the investigation process, specifically responding to information requests from the PSR, as detailed in paragraph 37.4 of Annex 3 to Supporting Paper 6, Visa Europe would like to draw the PSR's attention to the fact that there may be circumstances in which a participant is unable to respond to an informal request for information. For example, the information requested by the PSR may be confidential. Therefore, an adverse inference should not be capable of being drawn from a reluctance to provide information at a voluntary interview.
- 9.19 Visa Europe is concerned that the proposed response period of 14 days to a preliminary findings letter issued by the PSR, as determined under paragraph 40.5 of Annex 3 to Supporting Paper 6, may be an insufficient timeframe for participants to provide adequate responses. Visa Europe considers that a timeframe of 28 days would be fair and proportionate in the circumstances, particularly given that the PSR may have had several months to consider the matter in question.
- 9.20 With regard to the PSR's powers to obtain information or documents, as proposed at paragraph 26 of Annex 3 to Supporting Paper 6, those powers should only be exercised if the PSR has come to a view that there are circumstances suggesting that the statutory objectives have been undermined. Visa Europe is concerned that a wide approach to the exercise of these powers would pose a serious burden on participants that is likely to be disproportionate.

⁷⁹ CMA, *Prioritisation principles for the CMA*, CMA 16, April 2014, para 1.3

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Enforcement actions

- 9.21 Visa Europe notes that the PSR's power to take enforcement action is set out at paragraph 19 of Annex 3 to Supporting Paper 6. Visa Europe considers that, before exercising this power, the PSR should conclude that:
- on the balance of probabilities, there is a 'compliance failure' for the purposes of section 71 of the Act (i.e. a direction under section 54 of the Act or a requirement under section 55 or 56 of the Act has not been complied with); and
 - it is appropriate to take enforcement action, as there may be circumstances where such enforcement action is not appropriate.
- 9.22 The PSR should, additionally, produce more detailed guidance setting out the exact criteria upon which an investigation may be commenced.
- 9.23 In relation to the financial penalties that the PSR may impose, Visa Europe would like to stress the fact that the PSR should be able to issue public censures or private warnings without at the same time imposing financial penalties. Visa Europe would like this to be made explicit in the PSR's guidance.
- 9.24 With regard to the Enforcement Decisions Committee ("**EDC**"), Visa Europe considers that the proposed separation of the EDC from the PSR investigators or other PSR case team members who may be involved in investigating compliance failures does not go far enough in affirming the independent nature of the EDC, which should not be comprised of any PSR staff. Visa Europe remains concerned that, if the EDC is not seen to be independent, the authority of its decisions is likely to be questioned, with judicial review applications an inevitable consequence.
- 9.25 In Visa Europe's view, the EDC should be an independent committee of industry practitioners, with relevant industry experience. PSR staff are likely to be unable to take a broad view of a matter after having been involved in the supervision of payment systems. By way of example, we refer the PSR to the composition of the FCA's Regulatory Decisions Committee.
- 9.26 Visa Europe also requests clarity on whether the decisions of the EDC are capable of being referred to another body for final determination in the event of errors of fact or law in a manner similar to the way tax and financial services matters are referred to the Upper Tribunal.
- 9.27 With respect to the PSR's power to seek injunctions as a means of enforcement, Visa Europe strongly considers that, given the burden imposed by such a measure, this power should only be exercised if the PSR has come to a view that there are circumstances suggesting that the statutory objectives have been undermined.
- 9.28 The PSR must take account of HM Treasury's review of enforcement decision-making at the financial services regulators, the final report on which was published on 18 December 2014. One of the conclusions of this review was that there should be greater transparency in the enforcement process as to what the case against a firm is, as well as greater consistency in the enforcement process. Visa Europe would urge the PSR to make clear in the Powers of Procedures Guide how it will ensure that, should enforcement action be commenced, firms are afforded a sufficient degree of clarity over what the case against them is.

Regulatory fines

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9.29 Visa Europe notes that the PSR's proposed penalties regime stipulates at paragraph 3.5 of Annex 5 to Supporting Paper 6 that the penalty resulting from steps 1 - 4 may not exceed 10% of the annual revenues or billings derived by the participant from the business activity in the United Kingdom to which the compliance failure relates. Visa Europe notes that this is broadly in line with the fining cap on other economic regulators.

9.30 However, Visa Europe strongly believes that a further consultation on the PSR's approach to fines is required once the PSR has determined the general regulatory approach it will take, having had the benefit of the responses to the present consultation exercise. At this stage, Visa Europe and other stakeholders are not in a position to provide any meaningful responses on the issue of fine setting, given the remaining uncertainties in relation to key aspects of the PSR's overall regulatory approach (see for example the status and scope of the Proposed PSR Principles).

Disposal of interests

9.31 At paragraph 16 of Annex 3 to Supporting Paper 6, the PSR sets out the procedure for the use of its power to require the disposal of an interest in a payment system operator. As has been mentioned above, before exercising this power, the PSR should come to a view that there are circumstances suggesting that the statutory objectives have been undermined. In any event, any exercise of this power must be based on robust and compelling evidence which supports the conclusion that the measure is indeed indispensable and proportionate to achieve the objectives of the Act. As such, it must be a measure of absolute last resort, given the serious interference with the fundamental structure of the market and, likely, private property rights.

Dispute resolution

9.32 Visa Europe has effective procedures to deal with different disputes.

- Payment transaction related disputes are dealt with under detailed formal procedures set up by Visa Europe, involving the relevant parties.
- Membership or merchant related disputes which are dealt with on a case-by-case basis, to ensure that there are dealt with in the most appropriate and effective manner.

9.33 Visa Europe considers that in order to protect the integrity and resilience of its card scheme and governance and to ensure a consistent and effective dispute resolution process, the PSR should protect Visa Europe's ability to seek to resolve disputes under its rules and processes. Visa Europe considers that these are fair, robust and effective.

9.34 This position is consistent with the position taken by other regulators in the financial services sector which do not typically get involved in the resolution of disputes. Visa Europe notes that should the PSR choose to get involved in dispute resolution it should do so mindful of existing alternative procedures. Absent any specific concerns with these existing procedures, these should (at least in the first instance) be relied on to resolve the dispute. Should the PSR get itself involved in the process it must, in accordance with the Act, undertake a balanced assessment, avoiding being "gamed" by any interested parties for their own private commercial benefit.

9.35 On a purely practical note, Visa Europe notes that Ofcom's dispute resolution mechanism has often been used by telecoms operators to delay payment, impose controls on non-SMP entities and gain an unfair leverage in negotiations. The PSR must ensure that its dispute resolution system does not invite similar tactics.

9.36 Visa Europe notes that the Supreme Court has recently imposed severe restrictions on Ofcom's dispute resolution powers, noting that Ofcom can only intervene where it is necessary to meet one of its statutory objectives (all of which are ultimately linked to consumer harm). Moreover, such

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intervention can only be justified when it is demonstrated that it is likely that its statutory objectives will not be met without such intervention (i.e. a mere risk of the statutory objective not being met is not sufficient to justify intervention).

- 9.37 Further, Visa Europe is concerned that the proposals do not provide any form of *de minimis* threshold within the PSR's proposed dispute resolution system. In the absence of reasonable thresholds to govern whether the dispute resolution mechanism applies, the PSR opens itself up to trivial and immaterial claims which only serve to act as an administrative burden on both the PSR's and participants' resources. By way of example, dispute resolution cases in telecommunications typically take between 2 -5 years to resolve (including appeals) and involve expenditure of millions of pounds in legal costs, including significant costs for the regulator (which is usually the primary respondent defending the decision).
- 9.38 Prior to accepting a dispute, the PSR should carefully evaluate whether all commercial negotiations have genuinely been exhausted and intervention should occur only when there is a clear likelihood of harm to consumers. Visa Europe sees no basis (or material benefit) of the PSR spending public money in becoming, in effect, an arbitral tribunal for private parties. Further, the current proposals appear to suggest that disputes can only be raised with the PSR against regulated entities. Visa Europe is concerned that the ability for disputes to be raised against non-regulated bodies only defeats the objectives of the proposed dispute resolution process and denies potential claimants' access to justice.
- 9.39 Finally, with respect to the procedural aspects of the proposed dispute resolution mechanism, the PSR should determine a timeframe within which it will resolve a dispute. By way of example, Ofcom currently has a four month time limit for the resolution of disputes.

VOCALINK

VOCALINK

Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper* and *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

We welcome the establishment of the PSR and support its objective of enabling an appropriate market environment for ensuring service-users and end-users can benefit from 'world class payment systems'. We look forward to working with the PSR to achieve its objectives.

There are two areas that require further consideration as a priority:

Strategy setting and implementation

The strategy setting and implementation process needs to be as simple and transparent as possible, with a clear communication mechanism for implementing the outcomes required by the Payment Strategy Forum (PSF). The PSF should not become another layer in an already complex ecosystem. It should define desired outcomes and timescales, but not define technical solutions nor take responsibility for delivery.

There needs to be a body (or bodies) responsible for defining, validating and implementing the collective innovation that the PSF recommends. This body should define the solution, agree how it should be funded and could also act as the contracting body for the parties delivering the solution.

Service-user representation

Service-users should be the driving force in strategy setting. Future development of payments systems should be demand-led and not tied to specific payment systems.

In this respect we are supportive of the PSR direction on representation of the interests of service-users at the Operator level and the proposed broad representation from industry, service-users and end-users on the PSF.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*?

If you disagree with our proposed approach, please give your reasons.

We agree with the proposed approach to set up a Payments Strategy Forum (Option 1) and welcome the PSR's intent to establish a body that can provide a platform for future collaborative innovation driven by the requirements of service-users and end-users. However, there are a number of areas that require further consideration.

We would welcome greater clarity on how the PSF intends to differentiate itself from the plethora of other forums that are already in existence and how it will avoid adding further complexity to an already complex payments ecosystem. We believe that one of the key opportunities for the PSR would be to simplify the structure of the payments system and by doing so creating a market model that provides incentives for innovation that can deliver benefits to service-users and end-users. We therefore believe it is important that the PSF does not become an additional consensus-seeking organisation with limited resource or ability to coordinate innovation.

To this end, the PSF's role and responsibilities should be clarified to ensure that the requirements of service-users and end-users are pre-eminent, but with a suitable support structure in place to validate and implement change.

It would be beneficial to clarify the governance of the PSF and in particular the relationship between the PSF and PSR, including the scope of the PSF's authority. We understand that the PSR does not want to set strategy for the payments industry and believe that that is a sensible view for a regulator to take. The PSR should create the market environment which motivates market players to innovate and develop world class payment systems for the benefit of service users and end users. There may be a case for the development of a process for the PSF to propose issues to the PSR to incorporate into its overarching regulatory approach. We appreciate that there will of course be informal channels for this to take place, but would ask the PSR to consider the merits of formalising a channel for the PSF to make proposals to the PSR.

We also believe that there should be greater clarity regarding which body / bodies will be responsible for defining, validating and implementing the collective innovation that the PSF recommends. Currently there is no organisation to translate service-user and end-user requirements into a specific solution; and no central organisation for infrastructure and other technology providers to contract with, in order to implement a specific requirement. We note the PSR's mention of 'working groups' to deal with the details of the strategy set by the PSF, but would request further consideration of how these will operate; to whom will they be accountable, how organisations will be represented on these groups; and what structure will be in place to encourage close collaboration between these groups. Crucially, we believe that there should be detailed consideration of what role these working groups will play in the implementation of projects, and in particular, collective innovation.

We do not see significant problems with the proposed approach where the requirements for change relate to a single Operator (e.g. a change to the current Bacs system). However for collective innovation, such as Richer Data, to succeed it is unlikely that one Operator would be able to implement change on its own; and there is currently limited clarity regarding how such projects would be implemented. I.e., which body or organisation would commission or procure collective innovation projects. There is also limited detail in the PSR's proposals regarding how such projects would be funded –an area where greater clarity is also required. In our experience at Vocalink over many years nice to have/need to have features do not always find a willingness to fund them. In line with good practice, we also consider that any recommendations should be subject to a rigorous cost benefit analysis.

However we would expect the PSR to provide a framework for collective innovation, in order to provide

the necessary guidance for industry on when collective decisions can be made, and when they cannot.

We believe that neither the PSR nor the PSF could or should be able to define, validate or implement a specific proposal as this would reduce the impartiality of decision making at each of these levels. I.e. if the PSF was given responsibility to implement its own recommendations, this may have a bearing on what recommendations it actually makes. We would recommend that the PSR and the PSF are 'technology-neutral' and delegate such considerations to the relevant working groups; or other industry bodies that are given the task of defining, validating and implementing the PSF's proposals.

To summarise, we look forward to clarification of the following issues:

- How would the PSF differ from the plethora of forums that are already in existence; and how will the PSR ensure that the PSF does not add to the current complexity of the payments system?
- What is the governance of the PSF in terms of its specific responsibilities and powers, in relation to the PSR?
- What organisation validates, implements and funds collective innovation projects, recommended by the PSF?

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

We believe that there should be further clarity around how the PSR intends to guard against "areas where strategic development requires the collective action of stakeholders" (p17; 2.87; '*Supporting Paper 2: Payments industry strategy and supporting area for collaboration*'; PSR) being contradicted by the individual strategies of participants.

The PSR should ensure that the PSF and the PSR Panel are not undertaking the same roles – currently there is the potential for the two to overlap and potentially to contradict each other, given that the PSR Panel also has very broad representation, including end-users. As set out in our response to SP2-Q1, we believe that the PSR should seek to use its powers to simplify the current complexity of the payments ecosystem where possible.

We would also like to see clarification of how the PSR envisages infrastructure providers, and other technology innovators, being represented on the PSF. There is a strong case for the PSF to be able – through the representation of stakeholders with relevant expertise – to take on board the 'technological art of the possible' in its deliberations.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

We believe that there needs to be greater detail set out by the PSR on what the specific responsibilities of the PSF will be, in comparison to those of the PSR.

The role of the PSF should be highlighting issues that need to be addressed and then tasking the 'payments industry' to develop and deliver solutions to address these issues. One approach could be akin to the Bank of England's priorities where the recognised Payment Systems Operator is tasked with either addressing an issue by a specific date or presenting a plan to do so, again by a specific date. This would avoid the PSF being responsible for determining a (technical) solution which they would lack the technical expertise to develop; and which would also prejudice their 'neutral' role (see answer to SP2-Q1).

This concern could be addressed through the establishment of a 'payments industry' body to act as a delivery / implementation / technical validation vehicle for the PSR's strategy and the PSF's recommendations. Such a vehicle would need to be defined and established in parallel to the PSF and could take the form of a standing committee or an ad hoc working group, created on an 'as needed' basis. However, a 'payments industry body' would be in danger of adding to the plethora of existing bodies (see response to SP2-Q1 above). It would therefore be important to know what industry bodies could be retired in order to avoid further complicating an already complex ecosystem.

We would also suggest that all recommendations made by the PSF are evidence-based and are bound by a timeframe by which the 'payments industry' has to implement them. One of the biggest challenges to collaborative innovation in the past has been the competing priorities of stakeholders leading to 'drag' on implementation timeframes. The other 'drag' is funding availability, which as previously noted, can be a rock on which good ideas quickly or slowly perish.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

There are a number of infrastructure related themes that the PSF and the PSR should consider as part of its remit in order to agree the strategic priorities for the long-term development of payment systems in the UK.

- Opening up much wider and easier access to payment systems and payment services.
 - The infrastructure-related themes within the 'World Class Payment Systems' plan. VocaLink agrees with the PSR's proposal to avoid disrupting existing industry initiatives such as this.
 - Richer Data initiatives.
 - How the broader payment system can be made more resilient.
 - How the LINK network can be leveraged to provide a broader range of banking / payment services to a wide range of participants.
 - How payment systems platforms could be consolidated to deliver more innovative, resilient, secure and cost-effective services.
 - Identity and authentication initiatives to reduce fraud and error; and improve the delivery of public services.
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Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our *Consultation Paper* and *Supporting Paper 3: Ownership, governance and control of payment systems* for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

We agree that there should be appropriate representation of service-user and end-user interests in discussions and at board level within the Interbank and Card Operators. However, we do not believe it would be appropriate for end-user groups (e.g. consumer groups) to be directly represented on an Operator board although, there are clear benefits for such groups to be directly represented at the PSF level. We believe that guidance is required from the PSR on the role it expects the Interbank and Card Operators to perform, before making any changes to their governance.

Whilst we are generally supportive of the PSR's proposals in this area, the issue of Operator representation needs to be approached in a way that will ensure decisions are made in the best interests of service-users and end-users whilst seeking to balance the interests of all participants.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We agree with the costs and benefits identified by the PSR; and especially with the overarching benefit of appropriate representation of the interests of service-users in the decision-making processes at the Operator board level.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposed direction on Interbank Operators.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposals in this regard.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We agree with the PSR's proposals in this regard.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposals in this regard.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We are not in a position to express an opinion on this question.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

We agree with this approach, but would highlight that some level of co-ordination is required at an industry-wide level in order to achieve collaborative innovation such as Richer Data or 'World Class Payment Systems'. Detailed thought needs to be given to how this can be achieved in this new ecosystem; how the 'working groups' that the PSR has alluded to in its presentations at the industry day (9 December 2014) will operate in practice; and how they will draw in the appropriate expertise and representation. It is important that the PSR provides for an adequate level of co-ordination at this industry-wide level, to ensure that progress being made on industry initiatives (e.g. the 'World Class

Payment Systems' plan) is not wasted.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's preferred option.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposal to introduce a Reporting Rule on all relevant pan-GB Operators; and on a wider level welcome the PSR's intentions to introduce greater transparency into access arrangements.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposal and on a wider level welcome the PSR's intentions to introduce greater transparency into access arrangements.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

We are not in a position to express an opinion on this question.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposed direction and on a broader level welcome the PSR's intentions to introduce greater transparency into access arrangements.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposed approach and on a broader level welcome the PSR's intentions to introduce greater transparency into access arrangements.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We are not in a position to express an opinion on this question.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's proposed approach in relation to the development of Technical Access solutions by industry. However, in overseeing industry initiatives in this area, the PSR (and the PSF) should have the resiliency and security of the payment system as its fundamental concern. Increasing the availability of Technical Access platforms should not jeopardise this and we would welcome further information from the PSR detailing how it intends to maintain the balance between competition and resiliency / security.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

The PSR needs to be mindful of the potential for conflict between the PSR's access to payment systems agenda and the access to payment services agenda contained in the Second EU Payment Services Directive (PSD2) – see inter alia draft article 58. For example, for a challenger bank or PSP it might be more appropriate to help them gain access to payments services (as a payment initiation service provider) than to become a direct (or indirect) participant of a payment system.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

We believe that introducing UK-only regulations pending implementation of the EU regulations on interchange fees for card-based payment transactions, may lead to only minor temporary benefits and may require affected parties to make two sets of changes in quick succession. It may also run the risk of confusing service-users and end-users.

However in the longer term it is important that the PSR ensures that interchange fees are set in a transparent manner, and in doing so ensuring a level playing field for all stakeholders.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

We generally agree with Principle 1 (Relations with regulators) and Principle 2 (Compliance).

Regarding the practical operation of Principle 1, it will be important that there is speed and clarity where responses are required from the PSR (see reference to 'no surprises culture' at paragraph 6.16 of Supporting Paper PSR CP14/1.6) as it is possible that any delay in receiving a 'non-objection' from the PSR to proposed new projects and services may create a planning blight and act to slow down innovation. Furthermore, it appears that Principle 1 envisages participants having to communicate separately with each regulator. To the extent that the regulators have overlapping mandates it would be helpful for the PSR to provide further guidance regarding its participant reporting expectations.

We believe that the rationale for Principle 3 (Financial prudence) is adequately covered by existing regulatory / oversight regimes in that there is overlap with the oversight regime which applies to those

systems that are recognised under Part 5 of the Banking Act 2009.

Additional protection is provided in Part 6 of the Financial Services (Banking Reform) Act 2013 which introduced a Special Administration Regime for infrastructure companies (including operators of, and services providers to, interbank payment systems). These existing Part 5 BA 2009 and Part 6 FSBRA 2013 powers can be applied not only to the Operators of payment systems but also to infrastructure providers, at HM Treasury's discretion.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

We agree with the proposed approach.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

We believe that this may duplicate existing regimes; see our response to SP6-Q1 above.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

We do not believe that the additional proposed Principles relating to 'Integrity', 'Skill care and diligence', 'Management and control', 'Governance', 'Service-users interests', and / or 'Conflicts of interest', are necessary to deliver the PSR's objectives.

Several of the proposed additional Principles are directed solely at the Operators and Central Infrastructure Providers. For the reasons outlined in our response to question SP6-Q1 above, we believe that the concerns that these additional proposed Principles are designed to address are already covered by the existing regimes; and by introducing the additional proposed Principles the PSR could unnecessarily increase the regulatory burden on the affected organisations.

Two of the additional proposed Principles apply additionally to Direct PSP's. We believe that the manner

in which a Direct PSP conducts its business is also already adequately covered by existing regimes. Typically, a Direct PSP's (as defined by the PSR) business activities will already be subject to conduct regulation arising under one of the following regimes:

- Payment Service Regulations 2009 – the scope of which will be further increased following adoption of the second EU Payment Services Directive;
- Electronic Money Regulations 2011;
- Banking Conduct Regime.

Each of these regimes is already regulated by the FCA and include detailed rules concerning the conduct of the particular regulated business. The two additional proposed Principles ('Integrity'; and 'Skill, care and diligence'), which the PSR proposes should apply to Direct PSP's, will overlap with the purpose and intention of the existing regimes and the work of the regulator responsible for those regimes; and may impose an additional unnecessary regulatory burden on the affected participants.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

We generally agree with the anticipated benefits statements identified although, as noted above, we consider that the issue that Principle 3 is designed to address is already adequately covered by existing regimes. We also agree with the costs statements and that, as currently envisaged, the incremental costs of complying with the Principles should not be too significant.

We are concerned that there is a risk of a 'blurring of the boundaries' between the three principal regulators for payment services – FCA, Bank of England, and PSR. The proposed Principles (especially the additional proposed Principles) will cover areas of business conduct which are already subject to comprehensive regimes designed to protect service-users and end-users; and ensure the continued stability and integrity of the UK payment systems. In order for Participants to be able to operate their businesses with certainty it is important that there is a clear demarcation between the roles, scope, and authority of each regulator. In this respect, we note the intention to put in place a tri-partite memorandum of understanding between the regulatory bodies and would respectfully emphasise the importance that the MoU is clear and unambiguous and is implemented as soon as practicable following 1 April 2015.

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

We support the proposed approach that "[The PSR].. will only seek to promote innovation that is in the interest of service-users." However, it should be recognised that some innovation may be disruptive to existing business models leading to the withdrawal of services that some service-users and end-users might have relied on. We would welcome more clarity on how these conflicting considerations would be resolved.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

We agree with the proposed approach set out in the draft Administrative Priority Framework (APF). However, whilst the APF refers to consideration of whether other agencies may be better placed to undertake the work (para 4(c) APF), we believe that it would be helpful for the APF to explicitly reference out to the proposed Memorandum of Understanding that the PSR will enter into with each of the FCA, Bank of England, PRA, and CMA, (referred to at paras 9.5 and 9.8 of Annex 1 to Supporting Paper PSR CP14/1.6) which should stipulate the circumstances in which a specific agency will have prime authority to determine whether it is appropriate to take any action in respect of any potential regulatory breach.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Subject to our comments below (responses to SP6-Q9 and SP6-Q11), we agree with the general approach taken in the Powers and Procedures Guide (PPG).

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

At Paragraph 14 of the PPG (Other commercial disputes) the PSR states that commercial disputes between participants over matters other than those covered by sections 56 and 57 of FSBRA, may be escalated to be determined by the PSR; and that the PSR may give a specific direction or impose a specifically imposed requirement in respect of such matters. Whilst we agree that the PSR should have authority to investigate and enforce regulatory breaches, commercial disputes which do not involve a regulatory breach should not be within the scope of the PSR's powers and should be left to the parties concerned to resolve – usually in accordance with the contracted terms which the parties have agreed. The PSR should not become involved in resolving disputes over contractual matters which have been agreed in the ordinary course of business. The PSR should only become involved in commercial disputes where the dispute relates to a regulatory breach.

In this context, we believe that it is extremely important that the PSR provides further clarity in respect of paragraph 14 of the PPG in order that all participants can properly assess the level of certainty that any existing or future dispute may be determined in accordance with the contractual terms (including dispute resolution procedure) agreed between the parties.

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

We agree with the proposed approach.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

We agree with the PSR's general approach to setting penalties. We agree that there should be no floor for the level of penalties and also that an upper limit on penalties should be applied.

We do not believe that setting the level of a penalty by reference to the value of funds transferred through the relevant system would be a fair or proportionate approach. The values transferred through a payment system are not a good metric for assessing the size of penalty to be imposed for a regulatory breach relating to that system. For example, the effect of a regulatory breach relating to the Bacs system may be no less impactful to the service-user than a similar regulatory breach relating to the Visa system, irrespective of the significant difference in values processed by each system annually.

We agree that the revenue based approach for calculating the level of penalty is the most appropriate and likely to result in fair and proportionate penalties, taking into account the size of the business of the infringing party.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

For the reasons given in our response to SP6-Q11 above, we do not consider that value of funds transferred through the relevant system should be used as a basis for calculating penalties, irrespective of the nature of the business of the offending participant. In the case of the not-for-profit entities (such as Operators) which are owned / controlled by other participants, it may be possible for enforcement actions to be taken against both the Operator entity and owning / controlling participants, to the extent that the latter have also committed a regulatory breach which has resulted in, or contributed to, the Operator regulatory breach. In such circumstance the penalties applied could fairly reflect the difference in size of business (revenue) of the offending Operator and offending participant.

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

We believe that an upper limit on penalties of 10% of annual revenues derived or billings made by the

participant from the business activity in the UK to which the compliance failure relates, is appropriate. We do not consider that there is any need to apply different upper limits according to the category of participant, as a percentage of revenue approach should reasonably ensure that the hardship suffered by an offending participant as a result of the penalty is equally proportionate.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

We agree with the proposed approach.

WHICH?

WHICH?



Which?, 2 Marylebone Road, London, NW1 4DF

Date: 14 January 2015

Response by: Louise Vergara

Consultation Response

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Which? response to 'A new regulatory framework for payment systems in the UK' (PSR CP14/1)

About Which?

Which? exists to make individuals as powerful as the organisations they deal with in their daily lives. We are now the largest consumer body in the UK with over 800,000 members: we understand consumers and what makes them tick. We operate as an independent, a-political, group social enterprise working for all consumers and funded solely by our commercial ventures. We receive no government money, public donations, or other fundraising income. We plough the money from our commercial ventures back into our campaigns and free advice for all.

Introduction

Which? welcomes the opportunity to respond to the Payment Systems Regulator's (PSR) consultation on their proposed regulatory framework for UK payment systems. As the PSR's consultation outlines, payment systems form a vital part of the UK's financial system. For consumers, who are the end 'service-users' of payment systems, these services are critical. Not only do consumers rely daily on a stable, continuous and secure service, but they are also increasingly looking for greater innovation at a product and service level to make transactions easier, more convenient and cheaper.

Payment systems also play an integral role in the level of effective competition within the retail banking market. Any potential new payment provider will need to have an effective level of access to payment systems to be able to provide a competitive offering to consumers. This makes the role of the PSR vital in ensuring that consumer needs are met.

We recommend that the PSR focusses on three areas in particular to enhance its approach to payment systems regulation to ensure effective outcomes for consumers:

1. Ensuring effective and pro-active consumer representation in payment systems strategy;
2. Improving access to payment systems to encourage greater competition and innovation in the Personal Current Account Market; and

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3. Investigating and taking action against barriers to competitive provision of payment services with regard to ownership, governance and control.

Given the clear importance of payment systems regulation to retail banking, it is imperative that it is not viewed in isolation. There is immediately a clear overlap of the important role of the PSR with the Competition and Market Authority's (CMA) ongoing market investigation of the competitiveness of retail banking market. Therefore, we encourage the PSR to ensure that it works effectively with the CMA to identify and resolve barriers within the payment system that prevent new and existing providers from driving consumer focussed innovation and competitive pressure in the market. The two market reviews that the PSR are due to launch in 2015 should play a key role in driving joint action between the PSR and CMA.

On a longer-term basis, together with the CMA, FCA and PRA, the PSR must play an important role in ensuring that the financial services sector is focussed on meeting the needs of consumers.

1. Regulatory approach

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

We broadly agree with the regulatory approach proposed by the PSR. However, we recommend that the new regulator should go further in order to ensure that: proactive consumer representation is enhanced; access to payment systems improved; and barriers related to the provision of payment services removed. Doing so would encourage greater competition and innovation and play a part in creating a banking system that is centred on meeting consumer needs. Further action should include:

1. Ensuring effective and pro-active consumer representation in payment systems strategy

- The PSR should clarify their definition of 'service-users' to emphasise the importance of consumer voice (i.e. the 'end-user') in the strategy development and operation of payment systems.
- The PSR must ensure effective representation of consumers' interests in payment systems strategy development and within payment scheme governance. The regulator must be prepared to use its powers to actively hold industry to account and report on its progress in this area.

2. Improve access to payment systems to encourage greater competition and innovation in the Personal Current Account Market

- We want to see improvements to direct access of payment systems (including splitting technical access and settlement services from banks to third party providers to encourage greater access for challenger banks on a more level playing field).
- Some of these improvements may require intervention outside of the PSR's remit. As such, the CMA should also explore and assess these regulatory interventions as part of encouraging greater competition and innovation in the PCA market.



- The PSR must be transparent and report on the success of their strategy to improve access. It should identify and articulate areas outside of its remit that inhibit such improvements and work with the FCA and PRA to ensure these barriers are tackled.
- 3. Investigate and take action against barriers to competitive provision of payment services with regard to ownership, governance and control**
- The PSR must ensure that any consumer detriment coming as a result of conflicts of interest in ownership, governance and control of payment systems is addressed. This includes exploring the potential impact of collective ownership by the larger banks of both central infrastructure and payment schemes.
 - Alongside their proposed measures to improve transparency and consumer representation, the PSR should also ensure that member directors of payment scheme operators appointed by banks that have a significant ownership stake in Vocalink (or any Central Infrastructure provider) are mandated to step back from both procurement decisions and wider strategic decisions that could impact upon the choice of infrastructure provider.

We elaborate on these recommendations below.

PSR's consumer engagement:

While the PSR has stated that 'service-user' does include consumers, its proposals for engagement appear to focus on firms that use payment systems to deliver services to end-users (i.e. consumers and business customers), rather than consumers themselves. As such the proposals, while helpful, do not necessarily do enough to improve the influence of the consumer voice in either the long-term strategy or the ongoing operation of payment systems. In this regard, we also recommend that the PSR make clear that the needs of consumers, who are the ultimate end-users of payment systems and whose views have been systemically underrepresented, should be placed at the centre of the new regulatory regime. This should be explicitly embedded in the PSR's principles, guidance and overall approach.

The PSR should make clear how it will directly and proactively engage with service-users, and specifically end-users, to ensure that they are fulfilling their statutory obligations. The PSR has stated within its draft objectives guidance that it will:

*'...assess how well payment systems and services provided by payment systems are working for service-users by seeking their views and expect industry participants to raise issues and concerns with us. In addition, we are setting up a panel which will have representation from service-users.'*¹

Along with focussing specifically on consumers as ultimate end-users, we offer the following recommendations to enhance consumer engagement as well as our briefing 'Eight strategies to guide effective consumer representation' (Annex A):

- Given the diversity of consumers within the market, the PSR should employ segmentation modelling, similar to the FCA's 'consumer spotlight' segmentation, to assess the different needs of varying consumers groups - including the needs of more

¹ Payment Systems Regulator, Regulatory tools, supporting paper 6, PSR CP 14/1.6, pg, 5, para. 6.3

vulnerable consumers - who rely on payment services. We note that the FCA is currently engaging on a work stream focussing on vulnerable consumers in financial services.

- As the PSR have indicated during roundtable discussions with consumer groups, they must be conscious of the resourcing capacity of consumer representative organisations. Given this, consideration should be made to how the PSR could take advantage of existing engagement opportunities and avoid duplication. For example, the existing consumer engagement frameworks set up by the FCA (such as the quarterly Consumer Network meetings, as well as the Financial Services Consumer Panel).
- We also recommend that the new regulator supplement their engagement with consumer organisations through undertaking research directly with different consumer segments. They should assess whether or not their needs are currently being addressed within the current payment system and how future needs will be met through the proposed strategy. This should involve primary research including surveys, focus groups, panels and consumer listening events.
- To assist in coordinating information exchanges between consumer groups and the regulator, the PSR should designate a central point of contact for these groups to liaise with. A similar model already works well within the FCA.

Lastly, in keeping with the PSR's commitment to transparency, it must ensure that it reports publicly with regard to its progress in this area in line with its statutory objectives.

2. Approach to payments industry strategy

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in Supporting Paper 2: Payments industry strategy and areas for collaboration? If you disagree with our proposed approach, please give your reasons.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

We agree with the proposed approach (Option 1) to set up the Payment Strategy Forum which will be responsible for the long-term development of payment systems strategy. We support

the PSR's vision for the Forum to 'drive innovation, enable new and improve services and help realise our vision of world class payment systems'.²

Given that consumers are the ultimate end service users of payment systems, Which? argues that the needs and views of consumers must be embedded within the strategy development process. A lack of effective proactive consumer engagement can lead to a number of detrimental and unintended consequences. A recent example acknowledged by the PSR was the cheque withdrawal decision by the Payments Council.³

Ensuring consumer representation within payment systems decisions and strategy development can be perceived as a challenging task. This is due to the apparent arms-length relationship between these systems and consumers despite their daily use of these services, as well as the resourcing constraints on consumer representatives as mentioned previously. However, effective consumer representation is crucial, and Which?'s experience has been that, in order to work well, representation and engagement needs to be both effectively integrated and a two-way process.

In addition, the PSR must ensure that there is appropriate accountability and responsibility for ensuring consumer engagement in development a payment systems strategy, and must be prepared to hold the industry to account for demonstrating how consumers' views are heard and reflected accordingly. We strongly recommend that as part of this process, the PSR oversight of the strategy development includes assessing whether the needs of all consumers across different segments, including vulnerable consumers, have been addressed within the strategy. As part of this, the PSR could play a role in collecting and reporting relevant data. Part of the PSRs early work should be to set out a strategy for doing so.

As part of the Payment Strategy Forum's agenda, alongside the infrastructure themes identified by the PSR listed in their consultation document, we also recommend that the new regulator and/or Strategy Forum consider potential efficiencies which can be made in the payment system to improve the end-user's experience and use of payment services. This may include for example an assessment of potential consolidation of interbank payment schemes. In doing so, the PSR must ensure that the needs of all consumers, including those who are most vulnerable, are at the centre of any assessment process and proposed strategy.

3. Approach to ownership, governance and control of payment systems

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

We are encouraged by the PSR's approach to improving representation of the interests of service users in discussions and decision-making at the board level of interbank schemes operators. However, to address the systemic under-representation of the views of end-users

² PSR, Payments industry strategy and areas for collaboration (PSR CP14/1.2), para 2.2, page 5

³ PSR, Payments industry strategy and areas for collaboration (PSR CP14/1.2), para 2.73-2.74, page 16

in strategy and decision making will require a significant cultural change within payment scheme operators. We recognise that this step change in approach may take time and, as part of this, there is a strong onus on scheme operators to commit to genuine reform to imbed consumers' needs and views within their decision making processes.

To ensure that this happens, we believe the more must be done, in particular with reference to 'appropriate representation' of 'service-users'. Here, the PSR should require operators to demonstrate that end-user consumer views have been properly considered, and reflected within strategy development and implementation. To do this, the PSR should place a specific requirement on the schemes to:

- Engage directly with consumers to seek their input into both operational issues and strategic developments in payment systems; and
- Put in place independent scrutiny of their consumer engagement processes with reports to the PSR on the efficacy of arrangements, including how consumers' views feed into scheme decision making.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service- users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

No additional comment.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

While we agree with the PSR's proposed direction, we believe that the regulator could go further to mitigate potential conflict of interests within scheme operators during both the procurement of, and strategy for, central infrastructure.

While it is right that no single individual should serve as a director of both a scheme operator and central infrastructure provider, the potential for a conflict of interest could still exist. For example, scheme member directors appointed by banks that also have a significant shareholding interest in any central infrastructure operator. Such institutions could exert informal influence over infrastructure procurement decisions. This primarily results from the fact that a bank nominated scheme member director will typically be directly employed by that bank, and could share a reporting line with the bank's nominated director of Vocalink.

In order to more robustly enforce a level playing field for infrastructure procurement and minimise potential conflict of interest, the PSR should require all member directors appointed by member banks that have a significant ownership stake in Vocalink (or any other potential central infrastructure provider) to step back from decisions on procurement. They should also step back from decisions that significantly impact on wider strategy around the schemes use

of infrastructure (which, in turn, will impact on procurement decisions). We believe that this could be implemented whilst ensuring that quorum can be achieved at board meetings. This will go some way to ensure that the governance of infrastructure procurement is free from potential conflict of interest at both an individual and institutional level, and may also improve competition *for the market* in central infrastructure.

We understand that the PSR intends to explore this area in greater detail during its market review into the competitiveness of infrastructure provision to commence in April 2015. We agree that this is an area that requires more in-depth consideration, alongside the work of the CMA's inquiry.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

See above. Furthermore, while the PSR may choose not to issue additional directions at this stage, the regulator must continue to monitor potential conflicts of interest in ownership, governance and control of payment system and its detrimental impacts on end-users. As such, the PSR should ensure that it provides regular and public reports to identify such instances and progress in this area.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

No additional comment.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

We agree with the proposed approach to improve transparency in decision making by the boards of payment service operators. However, as detailed previously, we believe that the PSR can go further in enhancing reporting to make it clearer and more transparent.

P3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

No additional comment.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

No additional comment.

4. Access to payment systems

Which? supports the PSR's focus on improving access to payments systems. As previously mentioned, access to payments systems is vitally important to the overall competitiveness of the retail banking system - in particular to the personal current account market. We are particularly in favour of encouraging greater direct access to new payment service providers as this affords members full use of current and future functionality of payment systems, as well as the ability to innovate in product and service delivery due to access to richer data available within payment systems. It can also allow for new members to play a role in directly shaping future technical developments to meet consumer demand.

This will help new entrants to compete effectively with incumbent banks in their product and service provision (including providing tailored or innovative offerings to customers), thereby stimulating effective competition in the market. This can also have an impact on driving up the quality of indirect access service provision by sponsor banks if direct access is seen as a viable alternative for newer providers.

However, we recognise that a number of policy solutions related to access, particularly direct access, can extend beyond the regulatory scope of the PSR. For example, we note a number of submissions to the PSR's Call for Inputs which make reference to settlement and prudential regulation, and Anti-Money Laundering (AML) legislation, that are perceived as being an onerous barrier to payment system access. In its proposals, the PSR is largely silent on the barriers to non-banks that parts of prudential regulation might create.

We encourage the PSR to be more open and explicit about such barriers. It should guard against any reluctance to comment on relevant matters outside of its remit. In this respect, the PSR should play its part in the wider regulation of financial services and ensure that it is actively engaging with the FCA, PRA and CMA wherever it sees areas outside of its remit, that are detrimental to PSR achieving its goals.

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

We agree with the approach

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed

approach, please give your reasons.

No additional comment.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

No additional comment.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

We agree with this approach.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree with this approach.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

No additional comment.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

As previously mentioned, Which? encourages the development of solutions which improve direct access for new payment service providers. This may include 'technical gateway services' which allow for direct access through third party providers instead of acquiring access indirectly through sponsor banks. While we do not oppose the approach of relying upon industry to design and develop technical access solutions, the PSR also has a strong role to

play in monitoring and publicly reporting on the progress of these solutions. In doing so, the PSR should make it clear that, should insufficient progress be made in this area, it is prepared to use its powers to take action accordingly.

As part of this, once again we recommend that the PSR outline areas outside of its remit that may impinge on the ability for challenger payment service providers to obtain direct technical and settlement service access to payment systems.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

No additional comment.

5. Regulatory Tools

Measuring progress and outcomes related to payment system regulation

As part of its commitment to transparency, we encourage the PSR to look at how it measures, assesses and reports its progress with regard to its statutory objectives and its overall vision. We recognise the challenges of this task and the difficulties in, for example, predicting future innovations or the changing nature of competition and consumer needs. However, we encourage the PSR to specify what indicators it will use in measuring progress with specific reference to consumer outcomes.

We recommend that the PSR include the following:

- Numbers of new direct and indirect members of payment schemes (including applications pre and post the introduction of the new regulator);
- Proportion of access requests agreed to and timescales within which agreements are concluded;
- The degree to which certain key barriers to innovation (including lack of direct access, sponsor service levels, data richness, etc) are cited less by PSPs over time - the data might be collected by regular survey, building on the PSR's Call for Inputs baseline;
- Reporting on new innovation within, or stemming from, payment systems. Careful attention should be paid to the impact (both positive and negative) of this on the various segments of end-users (including vulnerable consumers); and
- Progress on service-user, in particular end-user, representation in decision-making within payment service operators and within the strategy forum.

Working with other regulators

As already highlighted, there is a close relationship between payments systems regulation and financial conduct, prudential stability and competition regulation. This means that the PSR must work closely with other regulators to undertake its work successfully.



For competition, there is a clear role for the PSR in ensuring that payment systems are structured to allow access for new providers to drive genuine innovation, and competitive pressure, in the market - rather than replicating existing product and business models. This could result in flow on effects for not just the PCA market, but also other retail banking products including cash savings. Given this, we strongly encourage the PSR to work closely with the CMA in exploring ways that reform of payment systems can enhance consumer focussed competition and innovation within the PCA market. This includes the PSR's market reviews on infrastructure provision and indirect access.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial Prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service- users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

No further comment.

SP6-Q10: Do you agree with our proposed approach for our Super-complaints Guidance? If you disagree with our proposed approach, please give your reasons.

We agree in principle with the PSR's approach. However, the PSR should provide clarity over the criteria that will be used to determine designation, and the process to apply for super-complaint powers. We encourage the PSR to co-ordinate with HMT to confirm this process as



soon as possible and, if possible, to minimise administrative burdens by taking on the approach of the FCA.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

No further comment.

Which?

14 January 2015

YORKSHIRE BUILDING SOCIETY

YORKSHIRE BUILDING SOCIETY

YORKSHIRE BUILDING SOCIETY

Response from Yorkshire Building Society to Payment Systems Regulator

Consultation

Yorkshire Building Society (YBS) is owned and governed by its members and is the UK's second biggest building society with over 3.4 million customers. The primary business areas are deposit-taking activities, mortgage sales and administration and mortgage related insurances. YBS operates through a number of distribution channels including telephone, post and the internet. The primary distribution channel is, however, its network of 230 branches which, in addition to the YBS brand, incorporates the other brands YBS trades under – Barnsley Building Society, Chelsea Building Society and Norwich & Peterborough Building Society. YBS also has a wholly owned subsidiary, Accord Mortgages Limited, which handles intermediary mortgage business.

YBS welcomes the opportunity to respond to this consultation. YBS believes the costs for direct access to payment systems are disproportionately high and act as a fundamental barrier to entry to the current account and payments markets, which has benefited the incumbent plc banks. Furthermore, payment system providers relying on agency banking arrangements are left often in a position which is at a significant disadvantage, impacting on downstream markets, most notably for current accounts.

Question in relation to our proposed regulatory approach (see Supporting Paper 1: The PSR and UK payments industry for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

YBS supports the approach laid out by the PSR, and agrees that it will give the new regulator both the market knowledge and necessary powers to achieve its objectives. In particular, in addressing the significant barrier to entry to the current account market which is the requirement for direct access to payments systems, the approach to use the available competition powers concurrently will be vital. The powers are extensive, yet exercising these will only be effective with appropriate collaboration. Due regard will need to be taken by the CMA, FCA and the PSR itself of key barriers to effective competition in the retail banking sector, which is built on the payments infrastructure. YBS also support the 'innovation' objective and would add that the associated benefits should also be made available to providers reliant on sponsor banks so that they are not placed at a competitive disadvantage from the introduction of new developments. In short, payments need to operate on a 'level playing field' basis given the inter-connected (and inter-dependent) nature of financial services.

Questions in relation to our proposed approach to payments industry strategy (see Supporting Paper 2: Payments industry strategy and areas for collaboration for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves),

YORKSHIRE BUILDING SOCIETY

as described in Supporting Paper 2 If you disagree with our proposed approach, please give your reasons.

YBS supports the establishment and operation of the Payments Strategy Forum in the manner proposed under option 1. YBS agrees that should facilitate the development of more cohesive and inclusive payments strategies. YBS also believes that strong consideration is also needed into how strategy is implemented once it has decided by the Payments Strategy Forum. Previously this would have been coordinated by a third party such as the Payments Council however their function going forward is still unclear. YBS believes that the PSR will need to ensure that all PSPs have sufficient support and communication throughout the design and implementation of any industry projects.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

YBS agrees that the type of broad based stakeholder engagement model, which the PSR is proposing, will be a significant improvement on the status quo.

In terms of our own specific sectoral group of building societies, and the other smaller Payment Service Providers, we would be keen that we are given an 'equal voice' in deliberations. Any bias towards the large clearing banks (with the vast resources at their disposal) could lead to outcomes that are weighted in their favour. We would argue that the PSR should have processes in place, in establishing both the initial working group to establish the forum and the forum itself to avoid such bias. This could be done by ensuring that when constituting the working group and the forum itself other service users and stakeholders including those relying on agency banking arrangements and challenger institutions are always included in at least the same number as incumbents.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

YBS would suggest that the forum meetings should move around the United Kingdom to help facilitate in person attendance and its visibility, by having a presumption where at all possible the discussions will be public and any items with confidential elements kept to a minimum.

In terms of the secretariat, it is reasonable to suggest that consumer groups and challenger providers and institutions in all of their forms may wish to meet separately in advance of full forum meetings to discuss issues of common concern. A formal sub-forum panel would allow them to mirror other existing industry structures where incumbents could have such discussions. In an analogous way to the FCA practitioner and consumer panels, the secretariat should include dedicated post holders to support these newly constituted PSR sub-forum panels. The panels could include a wider membership than the forum itself, ensuring that those representing participants and interest groups without formally constituted representative arrangements act in line with the views and interests of all those that they represent, ensuring that they can deliver what they commit to.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

YBS strongly supports Account Number Portability (ANP), and as we have previously made clear to the Competition and Markets Authority in the context of their investigation into the current account market, ANP would reduce the risk to customers of switching (which often acts as a significant behavioural barrier to switching) and would reduce the dead cost to the industry of moving

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customers' payment instructions from one bank to another. YBS notes that the market has not seen a material uplift in switching since the introduction of the Current Account Switch Service (CASS), and a proportion of the uplift that was evident in the early days is likely to be due to customers switching between Lloyds and TSB as a result of the sort-code based approach of the TSB separation which led to a number of customers being separated from their local branch. CASS was proposed and implemented after the plc banks, which dominate the current account market made the case that it would give a more predictable switch, but there are outstanding problems. Forwarding of payments, even after its recently announced extension, will still be time limited, after which time they are bounced. The obstacles to customers are substantial, and it is why the half-way house of a switching service is clearly sub-optimal when compared to the introduction of ANP. Portability reduced barriers to switch considerably in the mobile phone industry and there is every reason to think that it could do the same for banking, quickening the pace of changes in the pricing models which will underlie a more competitive market. YBS strongly holds the view that a world class payments system will need to have ANP at its core.

YBS would suggest that a high level working group including those within the industry who support it to pursue ANP is established at the same time as the full forum. This would begin feasibility work on portability interest to ensure that the PSR has the opportunity to evaluate a coherent case. This would give the counter arguments to many of the industry myths about the possible costs for instance, which do not reflect all of the possible options or necessary an unbiased reading of the evidence.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Supporting Paper 3):

Ownership, governance and control of payment systems for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

YBS agrees with the analysis of the situation affecting smaller and challenger institutions interests. YBS believes that there are significant weaknesses in the manner in which service user engagement mechanisms currently work. YBS would argue that the level of influence they are given, particularly at an early stage, will need to be improved substantially going forward. In addition, the way boards operate will need reform, which should place a number of directors to represent the needs of smaller players and challengers, rather than one as suggested in the consultation, who should be accountable and if possible be directly selected by service user groups and fora. A suggested litmus test for the PSR in assessing the real progress made on board composition would be that both independent directors and those with knowledge and expertise of providers other than from a direct PSP should always make up the majority, ensuring that those nominated by direct PSPs could not make decisions without at least the support of one or more of the independent directors.

There is of course the possibility that these changes may not be forthcoming and evidenced in annual reports published by operators in 2015, which YBS would hold to be a reasonable timescale for implementation of reforms. In this circumstance, we will expect the PSR to bring forward swiftly prescriptive proposals to achieve the requirements set out in the consultation by those means instead.

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SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

YBS agrees with benefits cited, and in addition would argue that the cost of more than one additional director on boards would be justified in order to avoid those directors with any knowledge of the needs of smaller players and challengers being vastly outnumbered, and potentially marginalised.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

YBS agrees fully with the PSR proposed approach in this area.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

No specific comment from YBS.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

YBS agrees with the benefits of mitigating the risks of higher prices or the lower quality service as suggested.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Yes, YBS supports this on grounds of transparency and agrees that it will have a positive impact in terms of increasing competition, innovation and service users' opinions.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

YBS agrees with the benefits cited. YBS agrees that the costs will be minimal and far outweighed by the benefits.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

YBS supports the PSR position, and welcomes the fact that it is planned by the Payments Council and the Interbank Operators involved that the Payment Council's reserved powers will be terminated.

Questions in relation to our proposed approach to access to payment systems (see Supporting Paper 4: Access to payment systems for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

YBS supports the draft principle that 'An Operator should have objective, risk-based, and publicly disclosed Access Requirements, which permit fair and open access'.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

YBS supports this approach, and takes the view that it will help ensure that there is the necessary substantial reform by payment systems to allow a greater number of institutions to have direct access at a proportionate initial financial cost, as well as on an ongoing basis. This will help address the wider barriers to entry to the UK current account market.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

YBS supports this proposal.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

YBS agrees that the significant benefits of this proposal more than outweigh the modest costs.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

YBS agrees that the publication of basic information will be helpful. However, this will only be an initial step in addressing the fundamental weaknesses in how the market for indirect access to the payment system currently works in practice for those institutions and their customers who depend on it.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

YBS supports the development of the information Hub. [REDCATED - CONFIDENTIAL]

YBS believes that sponsor banks should be required to disclose publicly on the Hub that the payment facilities provided differ significantly from each of their institutions, as this further limits the available choices to agencies who will be using the facility. For example, the BACS credits file provided by HSBC do not contain as many characters as the file provided by RBS; the outward faster

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payment facilities provided by Barclays are in a format which doesn't suit 'bank grade' agencies [REDCATED - CONFIDENTIAL] . The lack of standardisation of services is in itself a significant barrier to effective competition, but making potential customers aware of these problems in identifying a sponsor bank would be a valuable first step. YBS would suggest that if sponsor banks will not voluntarily publicly disclose the key relevant differences between their systems and service up front, the PSR should compel them to do so prior to the information Hub first going live. This will avoid it not including all of the most relevant information needed for it to be a useful research tool to market entrants and those seeking to change supplier.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

YBS supports the proposal for the development of a Sponsor Bank Code of Conduct, and welcome the proposal that sponsor banks engage with agency banks throughout its development. It should be highlighted that a standardisation and increased levels of fairness are critical to institutions like YBS. There are some specific comments on what the Code should include, and currently the opportunities for it to be shaped by the experience of institutions like YBS is not as extensive as it could be. However, YBS will of course engage fully if and when requested to do so by our sponsor bank before the deadline for the Code to be approved this year. YBS will put to its Sponsor Bank that the Code should also require the banks to carry out contract negotiations in a timely manner (currently negotiations can take several years) and to put in place common industry wide minimum Service Level Agreements, a minimum base level of services offered and key terms relating to the performance of their scheme's access gateway systems (i.e. to include targets/measurement of system availability/performance, incident resolution and root cause reporting and also formal incident escalation procedures). [REDCATED - CONFIDENTIAL]

As part of the sign off process of the Sponsor Bank Code of Conduct, YBS would suggest that those institutions and bodies which represent agency banks on the Payments Forum, and a suitable panel or other representative group for challengers in all respective forms (such as building societies), be given the right to negotiate and agree the final wording of the Code (as it will be between sponsors and agencies) before the PSR approves it. YBS would suggest that the forum secretariat should facilitate this process.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

YBS supports the PSR's proposal to require the scheme operators to consider and promote alternative technical access solutions (and membership criteria) which make it economically and technically feasible for PSPs with smaller volumes, to become direct scheme members. YBS would also encourage the development of Technical Access solutions by FinTech vendors in order to remove the reliance on technology supplied by sponsor banks. YBS believes that many of the restrictions imposed on agency banks by sponsor banks could be mitigated by removing the technical reliance on sponsor banks.

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SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

YBS supports the PSR's proposals to carry out a market review of indirect scheme access next April. We support the cost and benefits outlined by the PSR. [REDCATED - CONFIDENTIAL]

Question in relation to our proposed approach in relation to interchange fees (see Supporting Paper 5: Interchange fees for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

YBS believes that there are no other matters that the PSR should consider at this time.

Questions in relation to our proposed approach to our regulatory tools

(including our high-level Principles, and our enforcement and dispute resolution processes) (see Supporting Paper 6: Regulatory tools for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

YBS agrees with the three proposed high-level PSR principles.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Yes, YBS considers that they should apply to all participants.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial Prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

YBS agrees with proposed approach.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

YBS supports the principles and the proposed groups they should be applied to.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

YBS agrees with benefits cited here.

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SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

YBS supports the proposed approach.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

YBS agrees with approach for the Administrative Priority Framework.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

YBS supports the proposed approach.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

YBS agrees with the dispute resolution procedures as laid out.

SP6-Q10: Do you agree with our proposed approach for our Super-complaints Guidance? If you disagree with our proposed approach, please give your reasons.

YBS supports the super complaint guidance as set out.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

Regarding the proposals for imposition of penalties for scheme operators and participants that breach the prescriptive PSR directions, YBS supports measures that are a deterrent for non-compliant organisations because non-compliance could result in a detrimental effect on levels of service that YBS provides to its customers.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

YBS would view it as reasonable to apply a percentage levy to the value of funds transferred through a relevant scheme by an offending participant as an alternative metric. The upper limit which is higher on either, so revenue or value of funds transferred, should apply as the upper limit in a particular case.

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

YBS would agree an upper limit of 10% of annual revenues from the business activity directly associated with the compliance breach would appear to be reasonable, but in light of significant damage to consumers who rely on wider retail banking system, we believe that this level could potentially need to be set higher to allow for the most serious issues.

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SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

YBS supports the proposed approach as set out.

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Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper* and *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

Yes. Your regulatory approach is sound. Your expectation of a 'no surprises' culture as stated in paragraph 1.96 is appropriate. Operators, Infrastructure Providers and PSPs would also desire a similar cultural approach from the PSR relating to anticipated developments in a change in powers, regulations and so on as well as any information requests we issue.

Further questions:

- Regarding the sixth bullet point in paragraph 1.53, how will the PSR accurately and consistently recognise the differing nature and objectives of PSPs when exercising PSR functions?
- In adopting in full the principle stated in the sixth bullet point in paragraph 1.53, in what ways will the PSR ensure that their requirement and frequency of information from PSPs to be published is not onerous on daily PSP activity – stated in the seventh bullet point?
- The fourth bullet point in paragraph 1.64 – will the Operators and PSPs bear the cost of an investigator being appointed or is this cost of this compliance activity part of the annual cost that Operators and PSPs bear?
- Regarding paragraphs 1.83 and 1.84, how will the PSR communicate to Operators, Infrastructure Providers and PSPs the result of any meetings with the Bank, the FCA and the PRA? If working with authorities in the financial sector, competition authorities and other authorities is not as effective as first envisaged, does the Treasury have the ultimate authority to ensure future co-operation is more effective and transparent?

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

Option 1 from the three options is our preferred choice as it is the most proportionate and appropriate one. Creating a Forum will generate a greater appreciation by industry and other participants; will ensure that proposed innovations in and improvements of payment systems will be given the appropriate consideration; and will ensure that industry will be more adaptive to changes in demand and end-user preferences.

Our disagreement with Option 2 is based on the paper titled 'Independent Review of Governance and Performance of the Payments Council'. With a number of groups perceiving a lack of transparency in the Council's work; the composition of the Council Board not adequately representing consumers or business; a lack of power to mandate members to implement Council policies; and the overturned decision relating to cheque-clearing, it looks like the Council currently is not the best candidate to set industry strategy. In the Review, the Council proposed a light-touch intervention approach rather than 'detailed changes'. If the PSR wants to improve the effectiveness of payments industry strategy and collaboration within the financial sector, the Payments Council will not provide the required heft for the job – see the 'Roadmap' strategy issue paragraph 2.56.

Our disagreement with Option 3 is that the imposition of directions on participants to achieve PSR-created priorities for the financial sector will be an impediment to progress as the participants will not readily adopt priorities that have not resulted from wide participation as well as service-users' interests may not get sufficient prominence.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum? In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

It would be beneficial to have the following:

- a mechanism that rotates working group representatives from across the payments industry and service-user groups every two years
- discussion between PSR and the representatives on PSR's timescale expectations of when decisions need to be implemented (depending on the complexity of the decision)

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

It would be useful to have a parallel indicative model for how the PSR will act if the Payments Strategy Forum does not advance the PSR objectives on a timely basis.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

No.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our

Consultation Paper and Supporting Paper 3: Ownership, governance and control of payment systems for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

Yes.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

Yes. As mentioned in paragraph 3.106 Directors with conflicts of interest may be involved in taking decisions which impact on competition in the provision of payment services and/or infrastructure; development of new payment services and the speed at which they can be brought to the market; development of, and innovation in, payment systems; and, whether the operation and development of payment system is in the interests of service users. A relevant example would be VocaLink and LINK partially mentioned in paragraph 3.114.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

Yes.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Yes. To dispel the charge of 'lack of transparency' and to work towards diminishing the impact on competition, innovation and service-users, the direction is needed.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

Yes, as the PSR expect that the contractual modifications between the Payments Council and the relevant Interbank Operators will mean that the Payments Council will no longer have a right of approval over reserved matters as set out in those generic contracts.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper* and *Supporting Paper 4: Access to payment systems* for more details)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

Yes. This will provide fair and open access to these payment systems – access requirements will be publicly disclosed, risk-based and bespoke.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes. The publically disclosed annual compliance report will be very useful in finding out how compliant Operators have been in maintaining fair and open Direct Access to potential customers.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes. This will be very useful indeed from a Direct Access information point-of-view.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

Yes. As indicated in paragraphs 4.188 and 4.189 most Operators already have Access Requirements in place for Direct Access as well as a cost-effective planned annual reporting cycle.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

Yes. For transparency reasons this is suitable for Indirect PSPs.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree with your proposed approach. It would be useful if the PSR would pursue clarification on the exact content of the Hub as well as when the Hub will be designed.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

Yes, as the PSR have already stated what they are going to do if the Code of Conduct is not in place by 30 June 2015 and being complied with from 30 September 2015.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by

industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree with your proposed approach. It would be useful if the PSR would pursue clarification on the exact content of the Technical Access solutions as well as when the solutions will be created and of use.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

Yes.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

Paragraph 5.8 states that ATM interchange is not in scope and we agree with this.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our proposed approach, please give your reasons.

Yes. The three principles based on Relations with regulators, Compliance and Financial prudence and sound and succinct.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Yes.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

Yes.

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

The PSR should adopt all of the additional proposed Principles. Direct PSPs, Operators and Central Infrastructure Providers will have already adopted these Principles, albeit worded slightly differently.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

YourCash Europe agrees with all the costs and benefits related to the Principles.

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

Yes. Can the PSR clarify if there would be any costs associated with the dispute resolution and applications procedures?

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

Yes, with a caveat. Can the PSR clarify the aggravating /mitigating factors that will impact the penalty?

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

No. YourCash Europe believes that the percentage of revenues derived from the activity or system to which the compliance failure relates is appropriate for all potential cases.

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

The upper limit should differ according to the category of participant.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

Yes.