

The Payment Systems
Regulator Limited
Annual plan and
budget 2019/2020



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A note from Hannah Nixon





This annual plan is the last one I'll be involved with at the PSR, as I leave my post as Managing Director in April. It's been a privilege to be able to lead the organisation over the last five years, and I'm immensely proud of what we've achieved in that time.

We started life as a few people in a room in 2014, with an exciting but demanding challenge – to shake up the payments industry and make it work better for everybody. In my time we've successfully opened up access to payment systems, introducing greater competition and stimulating innovation. Our initiatives have led to the creation of a new payment systems operator, with a new payments architecture to follow. And we're starting to see a real difference in the fight against payment scams.

Although I'm moving on personally, this is really just the beginning for the PSR. It's grown from those few people to a thriving, diverse and dynamic organisation. I believe it's well equipped now to carry on the great work we've started, to face the new challenges ahead, and to help shape payments in the right way for the future.

Hannah Nixon

Outgoing Managing Director

Foreword

The payments industry is constantly evolving and innovating – and as its regulator, the PSR is no different. In the four years we've existed we've had to be bold and take the lead, using our powers to bring about change where it was needed. We've balanced that with a collaborative approach, working closely with the industry and letting it take things forward where that's been the best way of getting the right outcomes. We'll continue to evolve and innovate as we move forward – because the next year is set to bring more new challenges and new solutions to find.

In our initial phase of work, we concentrated on examining and fixing problems behind the scenes in the payments industry. Now we're increasingly involved in issues that more directly affect consumers, like payment scams and access to cash – work that also involves the Financial Conduct Authority and the Bank of England. People now have more protection from authorised push payment scams than ever before, and we're driving forward the implementation of important initiatives designed to increase that protection further. And our market review of acquiring services for card payments will look in detail at an aspect of payments that ultimately has an impact on all of us.

We'll also be increasing our work on ensuring that consumers, businesses and market participants benefit from the changes that are taking place in payments. This includes

continuing our work looking at how people can access cash in the future, including by exploring business and consumer needs in greater depth. And over the next year we'll explore some of the deeper issues in payments, so we can understand where the latest developments might lead and act where needed. As part of this, we'll examine the opportunities and issues raised by the use of payments data and by the move towards open banking.

Some of our early projects are now at the stage where we're monitoring progress – and enforcing compliance where we need to. Our work on access to payment systems has made a positive difference to the market, allowing new providers to connect to the systems and giving people more choice about how they use payments. As more players now want to enter the market, we will become increasingly involved in dealing with disputes about access – making sure that payment system operators and indirect access providers treat access seekers fairly.

Meanwhile, the industry's evolution continues apace. The consolidation of the operation of Bacs, Faster Payments and Cheque and Credit under one body, Pay.UK, was a major shake-up of how payments are run in the UK. Pay.UK will now oversee the development of a new payments architecture (NPA) for the UK, which will transform the way payment systems operate – bringing more opportunities for competition and innovation, which will have benefits for all the people and businesses that use payment systems.

Setting up Pay.UK and the NPA were recommendations of the Payments Strategy Forum, which we set up in 2015 to devise a strategy for collaborative innovation in payments. This is a great example of the flexibility of our approach: we led the industry to a place it wasn't going to get to by itself, but ultimately let it work out the best solutions where it was best placed to do so. We'll continue to watch the development of Pay.UK and the NPA closely, and will use the various tools we have to make sure they produce the right outcomes for everybody.

We're also following developments in the payments ecosystem that originated elsewhere. The second Payment Services Directive (PSD2) allows consumers to give permission to third parties to initiate payments from the consumer's bank account on their behalf. We will be keeping a close eye on how this changes the way banks, consumers, payment system operators and others work together.

So our work is expanding into new areas. We're making sure positive developments continue; we're using our powers to make sure there are fair conditions and a level playing field for participants in payment systems; and we're looking at new areas to make sure we're prepared for the next development in payments – whatever they may be. Of course, that includes keeping an eye on any issues that may be thrown up by the UK's withdrawal from the EU. And this year we'll appoint a new managing director, as Hannah Nixon leaves us in April.

Hannah has led the organisation through its 'start-up' phase and helped establish us as a dynamic regulator driving change in the payments industry. We'd like to take this opportunity to thank her for her contribution and wish her well for the future.

All this adds up to more ways for us to pursue our vision of payments that work well for all those that use them. We look forward to working with people in the payments industry and beyond to achieve that vision.

Louise Buckley and Chris Hemsley

Acting Managing Directors



Introduction

Our annual plan and budget sets out our key aims and activities for the year 2019/20 alongside our expected costs. We publish this document so anybody with an interest in payments and payment systems can have a clear overview of what their regulator is doing, why and how.

In the summer, we will publish our annual report on how we performed against our plans for 2018/19.

Our vision, role and powers

Our vision

Payment systems that are accessible, reliable and secure, and represent value for money.

Our role

As an economic regulator we're here to make payment systems work well for those that use them. We have three statutory objectives to help us achieve this:

- promote the interests of those that use or are likely to use payment systems
- promote competition in payment systems
- promote innovation in payment systems

These objectives are set by the Financial Services (Banking Reform) Act 2013 (FSBRA). We consider them in everything we do under our FSBRA functions, and we expect the same from those we regulate.

We regulate:

- the eight payment systems that have been designated by the Treasury (Bacs, CHAPS, Faster Payments, LINK, Cheque and Credit¹, Northern Ireland Cheque Clearing, Mastercard, and Visa)
- the participants in those payment systems (such as banks, building societies, merchant acquirers and other payment service providers (PSPs))
- the companies that provide the infrastructure for payment systems – the connections that make the systems work
- designated alternative switching schemes under the Payment Accounts Regulations 2015 (PARs) – this presently includes the Current Account Switch Service (CASS)

We are also the lead competent authority for the Interchange Fee Regulation (IFR) in the UK. The IFR mainly imposes requirements on payment card schemes, and issuing and acquiring PSPs.

And we are a competent authority in relation to the Payment Services Regulations 2017 (the PSRs 2017), implementing provisions of the second EU Payment Services Directive (PSD2) concerned with access to payment systems and information on ATM withdrawal charges.

Our powers

We have a range of powers under FSBRA, in particular in relation to:

- providing directions, both generally and in relation to particular participants
- changing or establishing rules regarding the operation of regulated payment systems
- granting access to regulated payment systems (subject to the changes made by PSD2)
- varying agreements between the operators of regulated payment systems and PSPs
- requiring the disposal of interests in an operator of a regulated payment system

In addition, we have enforcement powers relating to EU-derived legislation such as the IFR and certain provisions under PSD2, which we explain further in this document. We also have powers to monitor and enforce compliance under the PARs.

We have powers under the Competition Act 1998 in relation to participation in any payment system, including systems not designated under FSBRA. We can conduct market studies and make market investigation references under Part 4 of the Enterprise Act 2002.

In many cases, clear communication with the industry about what we want to achieve leads to the industry doing what's needed without us using our powers (for example, requirements or directions) – but we do use these powers when we think it is appropriate, and we monitor compliance. Our enforcement approach also plays an important role in the pursuit of our statutory objectives, whether involving enforcement of directions (specific or general) made under FSBRA, our concurrent competition powers, or our role as monitor and enforcer of the IFR, PSD2 or the PARs.

We will decide whether to pursue enforcement action on a case-by-case basis, having regard to our statutory objectives, functions and duties, and our Administrative Priority Framework. In determining whether enforcement action is appropriate we will consider all matters that appear to us to be relevant in each specific case.

Evolving for the future

The world we live in is constantly changing, and that includes financial services and payments. We're evolving as an organisation to make sure our decisions will remain effective and support improvements for consumers and businesses in the years to come.

This means carrying on with the work we've already done improving the way payment systems are run in the UK – and looking ahead to see where else we may be needed. This year we will continue our work on access to payment systems, making sure that conditions are fair and encourage competition and innovation. And we'll expand our work in other areas: exploring consumers' needs in greater depth than before; continuing our market review into card acquiring services; and monitoring and enforcing compliance with our regulations where we need to, to make sure that there's a level playing field for all participants in payment systems.

We'll continue to use our full range of regulatory tools, and to work in collaboration with our stakeholders where appropriate, to make sure payment systems continue to work well for all the people and businesses that use them.

Working for consumers

Over the last two years we've become more involved in directly consumer-facing issues. We've coordinated industry initiatives to improve financial crime detection and prevention, focusing on the issue of authorised push payment scams. This has led to the recent publication of a voluntary industry code for reimbursing scam victims, which will be active from 28 May 2019. From this date, consumers who fall victim to such scams, and did nothing wrong, will be reimbursed, even if the banks also did nothing wrong. We've also consulted on requiring banks to implement the Confirmation of Payee service, which will help make sure people send their money to the intended person, and are working through the responses. Both these initiatives should help reduce the number of successful scams and the impact they have. We'll watch them closely to make sure they have the intended effect.

We'll also continue working closely with LINK in relation to its ATM network. We issued a specific direction to LINK last year to ensure it was able to fulfil its commitments to maintain the broad geographic spread of free-to-use ATMs. LINK's programme includes protecting some of the more isolated ATMs and monitoring the impact of cuts made in the interchange fee. We're watching its progress and will respond to new developments as appropriate.

We'll examine the wider issue of access to cash in more depth this year, and carry out new research into consumers' behaviours and needs in relation to payments more generally. This exploratory work will be vital in helping us as we play a leading role in the discussion about access to cash in the longer term, and in helping us focus our resources where they're needed most – so we can continue making sure payments are serving consumers well.

Card payments

Card payments are a vital part of the UK's payments landscape, with more payments being made by card than any other method. Data collected by UK Finance showed that cards overtook cash as the most popular payment method in 2017, and we expect this trend to continue – so it's vital that we understand this market and make sure it works effectively for people and businesses alike.

A major part of our work in this area will be our market review of card acquiring services. We want to find out if the market is working well for merchants and, ultimately, consumers. If we find that it isn't, we'll consider what appropriate actions we should take.

We'll also continue our monitoring work as the competent authority for the Interchange Fee Regulation.

We'll examine the wider issue of access to cash in more depth this year.





Access to payment systems

Opening up access to payment systems has been at the heart of much of our work. By creating the conditions for fair access, we've given more PSPs the opportunity to connect to the UK's payment systems – meaning there's more competition, so people and organisations have more choice about how they pay for things.

We'll continue our work in this vital area this year. We'll make some changes to reporting requirements for payment system operators and access providers, and will issue updated directions covering access. The changes will make sure that we focus on the right things at the right time, and that our directions remain relevant in the years to come.

We'll also consider more access disputes, making sure that PSPs are given a fair opportunity to connect to the payment systems.

Pay.UK and the new payments architecture

Last year saw three interbank payment systems – Bacs, Faster Payments, and Cheque and Credit – being brought together under a single new payment system operator, now called Pay.UK. The new body is overseeing the design and implementation of a new payments architecture for the UK, which should be in use by 2022. These developments mark a fundamental change in the way UK payment systems operate. They should make payments more efficient, increasing competition in the market and making sure the UK's payment infrastructure is fit for the future.

We will monitor Pay.UK's progress to make sure the NPA delivers its intended benefits for PSPs, businesses and consumers, and will take action if necessary.

Monitoring and enforcing compliance

In our annual report for 2017/18, we reported that we had opened one case under the Competition Act 1998. Work on this case is ongoing and will continue during 2019/20. We now have monitoring and enforcement responsibilities relating to our functions under the IFR and the Payment Services Regulations 2017 (access issues), and in respect of the directions we've issued under FSBRA and other legislation. We'll continue our monitoring and enforcement work throughout the year.

This work encompasses matters we've identified through stakeholder engagement and active monitoring, as well as issues and complaints that market participants and other stakeholders have raised with us. We decide what action, if any, to take, and whether to open investigations into possible non-compliance, after taking our Administrative Priority Framework into account. This helps us to use our resources in the most efficient and effective way to further our statutory objectives and fulfil our functions.

During the last year we've been reviewing our powers and procedures guidance, which we published before our launch in 2015. We now plan to update it to clarify and amend various aspects now we're four years into our operational role, and to align the wording with other guidance that we've published more recently. We'll consult on our proposed changes in the coming months.

Thinking about the future

It is important that our work is firmly rooted in evidence and robust economic analysis. To consolidate our work in this area we have introduced a Chief Economist role. The overarching aim of this role is to maintain and further our high standards of economic analysis and research. As with all the work that we do, we are eager to use the latest tools and relevant economic thinking when developing our policies. The Chief Economist will help to keep us at the forefront of economic thinking. The function will also focus on our market intelligence and analysis activity, and will identify relevant market developments that we may consider as we develop our future work programme.

Overall, we're covering more ground than before, and we've reached a point where we'll naturally be more involved in carrying out compliance and enforcement work. We'll meet these challenges with a small increase in staffing levels, reflecting our ambition to improve our overall effectiveness and efficiency.

By creating the conditions for fair access, we've given more PSPs the opportunity to connect to the UK's payment systems.

Our aims and activities for 2019/20





Promoting the interests of people using payment systems

The outcome we want to see from all our work is payment systems working well for all those that use them, from shopkeepers to charities to consumers. This year we'll look at consumers in more depth than before. We'll carry on our vital work protecting people from payment scams, but we'll also look at people's payment needs and behaviours in much greater depth – so we can continue to anticipate issues where we can make a positive difference.



Authorised push payment scams

Since 2016 we've been coordinating industry work to combat authorised push payment scams – where a scammer tricks you into making an online payment to an account that they control. The consumer group Which? submitted a super-complaint to us in September 2016, asking us to look into the growing problem of these scams.

We engaged with organisations across the industry to understand the issue, and published a report in November 2017 on the developments taking place to help fight these scams. We focused our efforts on initiatives to prevent scams happening in the first place. One key measure is the contingent reimbursement model, which has been developed into a new industry code. The code sets out what steps banks should take to help prevent scams and how consumers can protect themselves, as well as the circumstances under which a scam victim should be reimbursed. The code is designed to help victims to be reimbursed for their losses, provided they have taken due care when making the payment.

In February 2018 we set up a steering group of industry and consumer representatives to devise the code. It recently produced a final code, which will be active from 28 May 2019. From this date, consumers that fall victim to such scams, and did nothing wrong, will be reimbursed, even if the banks also did nothing wrong. We will monitor the code's implementation to make sure it's producing the intended outcomes, and will take action if necessary.

We've also encouraged PSPs and Pay.UK to develop and deliver the Mule Insights Tactical Solution, which helps banks identify and shut down 'mule' accounts – legitimate accounts taken over by criminals for money laundering, perpetrating scams and other financial crimes. We'll monitor this and look at its effectiveness, to help us understand more about how scams are set up and to inform our future work in this area.

Confirmation of Payee

Another major new initiative in helping to prevent scams, as well as accidentally misdirected payments, is the Confirmation of Payee service. For the first time, PSPs processing online payments will compare the name on the receiving account with the name entered by the payer – and tell the payer if they match. This will allow people to check that they are paying money to the person they intended. This will make it harder for scammers to trick people by substituting their bank details for those of the legitimate person the payer was expecting to pay. It will also reduce the number of accidentally misdirected payments caused by people typing in the wrong account details.

This initiative can only produce its full benefits if the vast majority of PSPs offer it, and if they introduce it at the same time. To make sure this happens, in November 2018 we consulted on a general direction requiring PSPs to implement Confirmation of Payee. We're working through the responses and issues raised, and will issue our own response in due course.

Access to cash

In the last two years, cards have overtaken cash as the most popular method of payment in the UK. For many people, their expectations of payment options are changing. And as the landscape shifts more towards card payments being the norm in many situations, the economics of cash are beginning to change. We're already seeing this with changes in the ATM market, and there will be other implications for the supply and distribution of cash in the future.

But cash isn't going to disappear any time soon. We all still rely on it to different degrees, depending on where we are and our different lifestyles – and we'll continue to do so for the foreseeable future. It's vital that everyone can choose payment methods that meet their needs. This means there needs to be a sustainable way for people to get hold of their money in cash, and this is one of our key areas of focus for the future.

Alongside our work monitoring the changes to the LINK network, we're looking in detail at how people get cash and at their changing attitudes towards it. We're analysing the economic characteristics of different ways of accessing cash, how easy it is for people to get cash and where alternative options to those available today are appropriate. Today the main way people access their cash is through ATMs, so we're also looking at different approaches used by ATM suppliers and considering their impact on cash availability.

This work will also take forward the issues raised by the Access To Cash Review group, chaired by Natalie Ceeney. The group published its final report in March 2019, emphasising the changes in the way pay people are making payments and the need to make sure cash remains viable for the foreseeable future.

The different elements of the cash system are all inter-related, and there are a number of other bodies with an interest in making sure cash is available for consumers when they need it. Therefore, we're engaging with other regulators and authorities as well as all other relevant stakeholders, including parliamentary groups and consumer bodies. We'll take all their input into account when we look at the key questions about how best to secure the access to cash that consumers and businesses will need in the future.

LINK and the ATM network

The most common way people access their cash is through ATMs. However, the number of cash withdrawals has been decreasing each year, and this trend looks set to continue. In turn, this has an effect on the economics of running cash machines.

The ATM network operator LINK is addressing the cost of ATM services by making changes to its interchange fees for cash withdrawals. These are the fees that banks and other card issuers pay to ATM operators every time one of the banks' customers uses an ATM. Reducing interchange fees helps reduce overall industry costs, but there were concerns that LINK's proposed cuts could lead to some areas losing their free ATM services – leaving people with no local free access to their cash.

We've been closely monitoring LINK's plans and changes over the last 18 months, and early last year we wrote to LINK setting out what we expected it to do to address these concerns. In response, LINK committed to:

- protect the current broad geographical spread of free-to-use ATMs, by introducing a new status of 'protected ATM' for any free ATMs that don't have another free ATM within 1km
- cut its interchange fees incrementally
- monitor the impact of each cut and take immediate positive action if there's a negative impact for consumers
- bolster its Financial Inclusion programme to continue to fill gaps in the free-to-use ATM network

LINK must also report to us each month on the impact of its interchange fee cuts. It published its first report in September 2018, which showed that a number of protected ATMs had closed despite LINK's commitments. In October, following consultation, we decided to give a specific direction to LINK, aimed at ensuring it meets its commitments. The direction requires LINK to fully develop its policies and processes for applying and implementing its public commitments and to report to us on a regular basis.

In January 2019, LINK announced that it will provide for additional payments to support the continued provision of protected ATMs with low transaction volumes, since these are seen to be under greater risk of closure.

We will continue to work closely with LINK and other stakeholders. We'll monitor the impact of its interchange fee cuts over time, and the effectiveness of its policies and measures in response to our specific direction.

We've been closely monitoring LINK's plans and changes over the last 18 months, and early last year we wrote to LINK setting out what we expected it to do to address these concerns.



Consumers and payments

The scope of our work has evolved over the last two years; we initially focused on access and competition within payment systems, but then began to deal with issues that affected consumers more directly – such as our work on authorised push payment scams, and on ATMs.

We now want to get a deeper understanding of consumer needs and behaviours with payments, so that we can improve how we identify the most important issues and make sure our work supports people where they need it most. Reflecting this, we will do further research to examine what consumers need and want when making payments. This will involve research and engagement with consumers and representative groups, including a programme of regional events across the UK. This will be an ongoing stream of work for us, and we'll feed our findings back into our policy work.

Data in payments

Since 2017 we've been conducting in-depth research into the use of digital data in payments. Data is integral to payment systems and is a fast-expanding area – and it's becoming increasingly important as new ways of using data become more and more widespread. These include initiatives to fight financial crime as well as new services and products for consumers.

We started a conversation with the industry about data, to examine where we might have a regulatory role to play. We published a discussion paper in June 2018, reporting on our work to date and highlighting three key issues that we wanted to explore further:

- Some people may have concerns about sharing the data attached to their payments with third-party companies.
- PSPs may have limited access to information about transactions across a whole payment system.
- There are potential barriers to consumers and businesses getting the benefits from what's known as 'enhanced' data in the new interbank payment system in the UK.

These issues could all potentially slow down the development of innovative new products and services, meaning consumers and businesses would not see the full benefits.

Alongside our discussion paper we held a roundtable event with a range of stakeholders, and had various other discussions as part of our regular engagement schedule. We received a good range of detailed responses which illustrated the breadth and complexity of the issues involved – and the number of different perspectives to consider in assessing these issues. We're working through the implications of all this material, and expect to publish an update later this year.

Direct debit

Direct Debit guarantee

Since 2016 we've been in regular dialogue with Bacs about improving Direct Debit for the people that use it. Bacs implemented a number of changes in the Direct Debit scheme rules to help ensure that refund requests claimed under the Direct Debit Guarantee are handled fairly, and that inappropriate or fraudulent refund claims are identified.

During the year we continued to monitor the effectiveness and operation of these changes, and continued to see encouraging progress.

Direct Debit facilities management – switching service provider

We've also been monitoring Bacs's implementation of rule changes on the provision of Direct Debit Facilities Management (FM) services. FM service providers collect Direct Debit payments on behalf of other organisations. In January 2018 we gave a specific direction to Bacs to ensure that FM service users could easily switch to an alternative FM service provider if they wanted to.

As a result of our direction, Bacs designed, and has now almost completed the implementation of, a new accreditation scheme for FM service providers, which requires them to assist service users who want to switch.

Bacs, and therefore Direct Debit, is now operated by Pay.UK. We'll liaise with Pay.UK and continue our monitoring of both these areas during 2019/20, and will consider appropriate action if the intended benefits aren't being realised.

Monitoring the Current Account Switch Service

We will continue to fulfil our obligations as the competent authority for alternative switching schemes under the Payment Accounts Regulations 2015 (PARs). Switching schemes allow consumers to move their payment accounts from one PSP to another. Alternative switching schemes are services that are not operated by the PSPs themselves. We will consider applications from schemes to be designated as alternative switching services, and monitor and ensure their compliance with the designation criteria. In 2016 we designated the Current Account Switch Service (CASS) as an alternative switching scheme. We assess CASS each year to check that it continues to meet the designation criteria.

We will continue to monitor its performance against two key performance indicators set by the Treasury, and will report on this annually to the Treasury.

We want to get a deeper understanding of consumer needs and behaviours with payments.

Promoting competition

Competition in payments can bring benefits for the people and organisations that rely on them. One of our key early work areas was stimulating competition by opening up access to payment systems. Now we're looking in more depth at card payments, a vital part of the UK's economy.

Card-acquiring services: Our market review

This year we've begun our market review of the supply of card acquiring services – these are services to accept and process card payments on behalf of a merchant resulting in a transfer of funds to the merchant. We want to find out if the supply of these services is working well for merchants, and ultimately consumers.

Card payments are critical to the smooth running of the UK economy. They are now the most popular way for consumers to pay for goods and services, and their use continues to grow. Our market review has been prompted by concerns we've heard from stakeholders about the supply of card-acquiring services.

As part of our work, we will examine how competition in this market operates, and look at the outcomes of the competitive process. This includes looking at the fees merchants pay for card-acquiring services and the quality of service they receive.

We consulted on draft terms of reference for the market review in July 2018, and published the final terms in January 2019. We're now gathering evidence and information from a range of stakeholders, and expect to publish an interim report at the end of 2019.

The Interchange Fee Regulation

We are the lead competent authority in the UK for the Interchange Fee Regulation (IFR). This regulation caps interchange fees paid by merchants on certain card transactions and sets certain business rules. In 2019/20, we will continue our current approach to monitoring compliance as set out in our guidance.

Our work in the forthcoming year includes monitoring compliance with the requirements of Article 7 of the IFR and associated Regulatory Technical Standards Regulation (RTS Regulation). The Article requires the separation of payment card schemes and their processing entities. To enable effective and consistent compliance monitoring, we signed a Memorandum of Understanding (MoU) setting out how we will work together with other EU competent authorities to monitor Article 7(1)(a) of the IFR.

To date we have worked collaboratively with the European Commission and national competent authorities, recognising that the schemes subject to the IFR operate in countries across the European Union. We will

continue to seek to engage with those authorities with similar monitoring and enforcement functions.

As part of the preparations for the UK leaving the EU in a 'no deal' scenario, the Treasury has taken steps to onshore the IFR to make sure that it continues to function after exit day. This onshored legislation includes delegated powers for the PSR to onshore the RTS Regulation and maintain it in the future. We have amended the RTS Regulation to ensure that it functions effectively after the UK leaves the EU on exit day and is consistent with the statutory instrument onshoring the IFR. We published the EU Exit instrument onshoring the RTS Regulation in March 2019.

We will consider the implications, if any, of the conditions of the UK's withdrawal. We will explain how our monitoring and enforcement work and engagement with other EU authorities will be affected as soon as practicable.



Access to payment systems

A major focus for us since we launched has been access to payment systems. We broke new ground by removing some of the barriers to fair access, pushing forward our aim of creating the conditions for more effective competition within payment systems. This encourages innovations that benefit the people and organisations using the systems.

In the last three years, access has become much more open, with the numbers of new direct participants in the interbank payment systems growing year-on-year. New technology has presented more ways of connecting, such as aggregator services and direct technical access. The first non-bank PSPs have now connected directly to the interbank payment systems, and the first directly connected non-settling participant has joined Faster Payments – with more to follow. It also takes less time for PSPs to join a payment system than it used to.

We require payment system operators to report to us each year on their compliance with our directions on access and governance, which are

designed to make sure access is fair and transparent. We've seen continued improvement in these reports. We've now taken account of feedback we received in our consultation on our general directions to refine the structure of these reports. We worked with the operators to implement the new structure in mid-2018 ahead of the 2018 reporting deadline.

We'll continue to focus on indirect as well as direct access, and on making sure that operators' access requirements are proportionate, objective and non-discriminatory. We'll also examine the impact new providers are having on the market.

We also want to see greater consistency in the processes and information available for those seeking direct access, continuing the journey that we started in 2015. Now that Bacs, Faster Payments and Cheque and Credit are all operated by one body, Pay.UK, it is a good time to review direct access requirements and harmonise them where possible. We've already discussed these issues with Pay.UK, and it will consider the information it gives access seekers as part of its planned website development during 2019.



Our revised general directions

Last year we began work on reviewing and revising the directions we issued at our launch in 2015. Most of these were intended to improve access to payment systems in the UK, and their governance arrangements. Since then, there have been various market and legislative changes. By reviewing our directions we intended to ensure they continue to be fit for purpose in a changing payments landscape, so that payment systems continue to operate with users' interests in mind.

In March 2018 we published our consultation paper CP18/1, *Review of PSR Directions made in 2015*. We issued our final policy decisions in March 2019, including a consultation on the wording of the new directions.

We've made a number of changes to the original set of directions. As well as updates to reflect changes in legislation, we made changes designed to increase transparency and further improve the information available to PSPs applying for access to payment systems. The consultation on the text closes in April, and we expect to publish the final directions later in the year.

Access disputes

We can intervene in access disputes using our powers under sections 56 and 57 of FSBRA and under the PSRs 2017. Payment system operators and indirect access providers must have access terms that are proportionate, objective and non-discriminatory. If we find that they don't, we can issue fines, order them to grant access to a payment system, or vary the conditions of access.

We have opened three cases under section 56 or 57 of FSBRA. In one case, the parties came to a commercial agreement before we had issued a final decision. In two cases, the applicants withdrew their applications before we issued a final decision. We gained our powers under the PSRs 2017 in January 2018. Under these powers, credit institutions are required to tell us when they refuse or withdraw bank accounts for other PSPs. We received 197 notifications in 2018. We have also received a number of complaints from PSPs who have had bank account access refused or withdrawn. We have not opened any cases to date, but are still considering several of the complaints.

We're reviewing our guidance on how we deal with complaints under the PSRs 2017 and access disputes under FSBRA. We'll consult on changes in the coming year.

We intend to ensure our directions continue to be fit for purpose in a changing payments landscape.



Promoting innovation

Payments technology is fast-moving, and the way people pay for things is also evolving rapidly. We want to make sure payments in the UK keep up with changes and are able to adapt as new innovations come along – while making sure people have a choice of ways to pay that are right for them.

Pay.UK and the new payments architecture

One of the biggest changes happening in UK payments is the creation of Pay.UK – the new payment system operator that has taken over the running of Bacs, Faster Payments and Cheque and Credit. This will support further significant change, with the creation of a new payments architecture (NPA) for the UK, which is being led by Pay.UK.

These two developments were initiated by the Payments Strategy Forum, which we set up in 2015 to create a strategy for collaborative innovation in UK payments. In January 2018 we set out our expectations for Pay.UK as an organisation and its development of the NPA. We continue to monitor its progress to make sure it and the NPA produce good outcomes for payment system users in the UK.

Competitive procurement and message standards

In 2015/16 we carried out a market review of the supply of infrastructure to interbank payment systems. We found that there was not effective competition in this market, and in 2017 published our remedies: the use of common message standards (specifically, ISO 20022), and a requirement that the infrastructure of Bacs, Faster Payments and LINK should be procured by a competitive tender process.

In March 2019 we granted an extension to the deadline for LINK's infrastructure procurement, to allow it to resolve certain contractual issues. It will now have competitively procured central infrastructure services by 2 October 2021. In 2018 we granted extensions for the Faster Payments and Bacs infrastructure procurements. The deadlines are now 30 June 2023 and 1 December 2023 respectively. At that point the previous infrastructure will be switched off and both systems will be replaced by a single, competitively procured infrastructure as part of the NPA. There will be a transition period of parallel running before that, and Pay.UK will begin the process to procure an infrastructure provider for the NPA in 2019. We will monitor the procurement to make sure it achieves the benefits that we and the Payments Strategy Forum intended.

The future of retail payments

The Second Payment Services Directive (PSD2) is aimed at widening access to payment services. Traditionally, consumers could only initiate payments from their bank accounts by contacting their bank and requesting that a payment be made. After PSD2, consumers may allow authorised third parties (such as payment initiation service providers (PISPs)) to tell the bank to initiate a payment on their behalf. In the UK, the Open Banking initiative has been working to establish common open standards for how banks and third parties should communicate with each other to support these new types of payment.

We're interested in how these new permissions and standards are likely to change how consumers pay for goods and services in the future. We hope that these initiatives will bring innovative payment services to the market. Opening up access to consumer bank accounts in this way could bring benefits to many people, but it will be important that all participants understand their rights and obligations in the new environment. We will carry out research this year on the impact these new services could have on participants in payment systems, from consumers to PSPs, and on competition between PSPs.

Market knowledge, data analysis and assessment

We are a forward-looking regulator, and this is all the more important given the fast-moving nature of payments and the changing needs of businesses and consumers. In previous years our horizon scanning has informed our work and we have run projects to improve our understanding of emerging issues. Our recent work on payments data and contactless mobile payments, where close working with industry and other stakeholders supports our work, are good examples of this.

This year we will develop this approach so that we have a more systematic approach to gathering and analysing data. The overarching aim of this work will be to improve our understanding of the markets that we regulate, structure our analysis and identify relevant trends. This will allow us to take better decisions on how we regulate and what to prioritise.

In addition to the data and information gathering work, we will coordinate with other regulators and work together with the industry to prioritise the areas that we should be looking into in more depth. This work will all be overseen by our Chief Economist. An example of the type of work we'll do under this stream is looking into the potential effects of PSD2 and Open Banking on retail payments.



Working with our stakeholders

Working with other authorities

We have a legal duty to coordinate with the Bank of England (the Bank), the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA). This coordination improves our knowledge and approach to financial regulatory issues.

We continue to work closely with the FCA in our work to combat authorised push payment scams, and in preparation for the UK's withdrawal from the EU (including its potential effects on our powers and responsibilities). We will continue to work with them, and other relevant stakeholders, to help ensure payment systems work well for those who use them.

We have a joint Memorandum of Understanding with the Bank, the FCA and the PRA. This sets out the high-level framework we use to cooperate with one another in relation to payment systems in the UK, which each body has a different mandate for.

We are also part of the Authorities Response Framework alongside the FCA, the Bank and the Treasury. We will continue to work closely with these stakeholders and other

regulators and competition authorities in 2019/20, and in particular in relation to our shared competency with the FCA in monitoring and enforcing compliance with Regulation 105 of the Payment Services Regulations 2017.

We support this coordination with secondments between us and other regulators. This helps us share and develop skills and knowledge. We currently have three outward and two inward secondees, and expect others to follow during the year.

Our concurrent competition powers and our role as lead regulator under the IFR lead to regular engagement with the Directorate-General for Competition and other EU national competent authorities. We will continue to participate in networks such as the UK Competition Network and the UK Regulators Network so that we can share experience and best practice on regulatory and competition matters. We will incorporate this into our regulatory approach.

Where possible we will cooperate to advance our objectives, and coordinate to reduce costs to our regulated communities.

The PSR Panel

The PSR Panel is an independent group of experts, from the payments industry and beyond, that contributes towards the effective development of our strategy and policy. Establishing and maintaining the Panel is one of our statutory requirements. The members are drawn from payment system operators, PSPs and other stakeholder groups, and offer advice and early input on our general policies and practices.

The Panel remains a key channel for us to be able to understand how our wide range of stakeholders may respond to our policies and approach, and we will continue to consult it regularly.

In November 2018 the Panel held an annual discussion session with PSR staff, providing an opportunity to share the Panel's insights more widely among the organisation. The event was very successful and we plan to repeat the exercise this year.

UK withdrawal from the European Union

Our work to prepare for the UK's withdrawal from the EU has primarily involved working with the Treasury and the FCA to make sure relevant EU legislative instruments continue to function at the point of leaving – the process known as 'onshoring' (to the extent that it falls within our remit). These include:

- the Payment Account Regulations 2015
- the Payment Services Regulations 2017
- the Interchange Fee Regulation.

We have worked with the Treasury to fix deficiencies arising from the UK's withdrawal in domestic legislation that falls within our remit:

- the Financial Services Banking Reform Act (FSBRA) 2013
- FSBRA (Disclosure of Confidential Information) Regulations 2014 (FSBRA DCI)

Given the cross-cutting nature of the regulatory and supervisory landscape in the payments sector, we have also been working with the FCA, the Bank of England and the Treasury to prepare for the potential impact of the UK's withdrawal from the EU. We will continue monitoring developments and working with the sector to ensure that risks remain well managed.

The Panel remains a key channel for us to be able to understand how our wide range of stakeholders may respond to our policies and approach.

Our organisation

Our people

As we evolve as an organisation, our aim is to continue to provide a collaborative, engaging and progressive environment that encourages our people to be at their best.

Looking forward, our People Strategy for 2019/20 continues to focus on:

- our programme of leadership and management development
- staff development – by increasing awareness of and access to our learning and career development resources, and by using the PSR Capability Framework
- carrying out our work in line with the PSR Values

Our headcount for 2019/20 is likely to be around 100. Our growth has been spread evenly across all areas of the organisation, with resource planning being driven by the anticipated direction of our work programme.

We continue to build flexibility into our organisation by having a mix of permanent, fixed term and temporary staff. As a small organisation, this enables us to act nimbly to meet the changing demands of our work programme. The external environment

presents some challenges, particularly regarding the quality and volume of the candidate pool for legal expertise. We are also conscious that succession planning and building resilience into the organisation is a challenge given the size of our team.

Our Diversity and Inclusion policies are designed to help us build an organisation which reflects the society that we serve, so we can bring diverse views and experiences to both to our work and our workplace. We are a signatory to the Women in Finance Charter, and our commitment to diversity and inclusion includes disability, ethnicity, lesbian, gay, bisexual and transgender (LGBT) and gender identity, as well as mental health and social mobility issues. Our employee-led networks help to raise awareness of diversity and build an open and inclusive workplace. We also have an active Diversity and Inclusion working group which is committed to broadening awareness, creating an inclusive culture and providing corporate responsibility opportunities that enable our people to contribute and give something back to the community.



Our budget for 2019/20

Our annual budget for 2019/20 reflects our operating costs from 1 April 2019 to 31 March 2020. We estimate these costs to be around £15.6 million. During 2018/19 we were continuing to grow towards our planned staffing level. The 2019/20 budget reflects the staff costs of this operating model throughout the year, allowing for a 2.0% Consumer Price Index (CPI) increase. The 2019/20 budget is approximately £700,000 higher than the 2018/19 budget.

As in previous years, staff costs are our largest operating expense. We continue to run a lean staffing model, using flexible resources and agile working across different projects to achieve our objectives.

Staff costs and professional fees

This year we anticipate staff costs increasing to £11.4 million. This is a result of a small increase in staffing for 2019/20, and a change in our mix of resources – with an increased focus on seniority to reflect the complexity and breadth of our work programme. This will give us the flexibility we need to cope with unpredictable work streams and react to new developments at the right time. We anticipate our 2019/20 headcount to be around 100 during the year. To help ensure we provide the best value for money and grow our corporate knowledge and memory, we continue to recruit permanent and fixed-term employees, with a small number of temporary staff who we use on a short-term basis to provide particular specialist services or short-term resourcing.

Each year, we re-baseline our professional fees (for specialist services to support our work). In 2019/20 we expect these costs to be around £1.8 million, down from £2.0 million in 2018/19.

Other operational costs

As an independently accountable subsidiary of the FCA, we continue to use its operational support for services such as finance, human resources and information services where it is viable, effective and efficient to do so. We will continue to reimburse the FCA on an annual basis for costs incurred on our behalf.

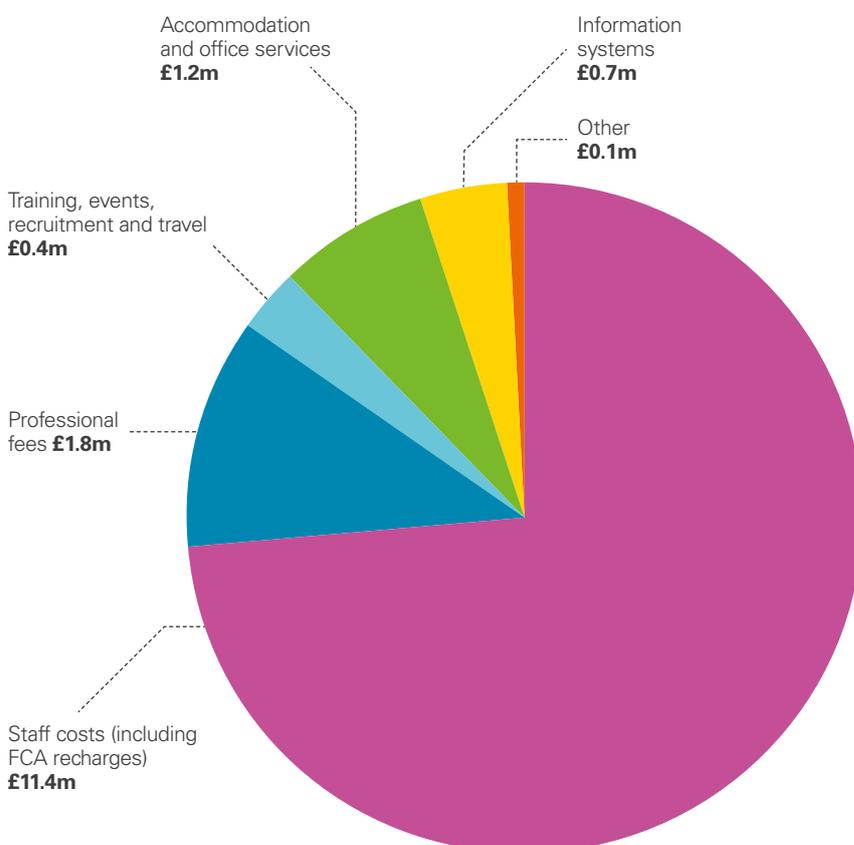
Annual funding requirement and impact on fee payers

We will continue to recover our costs through the annual fees paid by the organisations that we regulate. These include fees paid by the PSPs that directly participate in any of the payment systems we regulate, and the operators of alternative arrangements designated under the Payment Accounts Directive.

Value for Money

Our overarching Value for Money (VFM) strategy is to have as much impact as possible in delivering our statutory objectives, while minimising costs. Our efforts to further improve our effectiveness, efficiency and economy are ongoing, and we include VFM criteria in our decision-making processes at all levels. This, together with reviews of our internal processes, benchmarking, and ensuring flexibility in our workforce, will allow us to make more savings. We also work closely with other regulators to share expertise, best practice and resources where possible.

Budget costs (£15.6m)



Risk

Identifying and assessing risks to delivering our statutory objectives forms a key part of our planning process. Our continued aim is to identify and respond promptly and effectively to emerging issues, so we can best promote the achievement of our statutory objectives.

We look beyond our immediate remit by horizon-scanning across the industry to anticipate user needs and market

requirements, while working closely with other regulators to get the right outcomes and minimise harm to consumers. This helps us assess whether our existing regulations will continue to achieve their goals as designed, and if not helps us assess how we need to change them.

The following are the most material external risks and trends that could pose a risk to our objectives in the coming years.



Demographic trends and longevity

The payment needs of future generations of consumers are likely to evolve from the needs of previous generations. We need to continue to consider how we ensure consumer choice across different age groups and regions, and different types of business.

Technology and innovation

Technology has the potential to increase competitiveness, support innovation and efficiency, transform business activities and shape access to payment systems and services. However, this can also lead to incumbent businesses trying to protect their markets with barriers which could block innovation and competition.

Smart data, digitisation and data analytics

The expected increase in the availability and commercial use of payments data within the industry in the future could affect the rate of innovation in the industry, influencing the ability of the sector to deliver new and improved services. It could also influence how competitive advantage is derived, ultimately affecting market structure and the nature of competition in the sector. Finally, it could also create risks for end-users with respect to data privacy and security.

Cyber security and resilience

Consumers are looking for greater trust and assurance that payments are protected and secure, including protections from cyber-crime and other systemic incidents. Consumers also expect that incidents will be dealt with appropriately and recourse provided where required. We, along with the Bank of England, the Prudential Regulation Authority and the FCA, have an interest in payment systems resilience issues, and certain relevant responsibilities. In view of the functions of the Bank and the FCA, together with their specific objectives regarding stability and resilience, we would not usually expect to lead on issues of cyber security and resilience. However, we continue to work closely and coordinate with both the Bank and the FCA on these issues, and we continue to have regard to our objective to ensure that payment systems are operated and developed in a way that promotes the interests of service users.

Operational risk

To properly focus our efforts, we identify and assess the potential impact associated with each part of the work programme, including any harm to consumers that may be caused by inadequate action or resources.

In turn, this helps us to assess and manage our operational risks. This includes prioritising our resources and making sure we have the right skill sets to ensure that we have the expertise we need, when we need it, as well as the business processes and systems support our vision while delivering value for money.

We continue to have regard to our objective to ensure that payment systems are operated and developed in a way that promotes the interests of service users.

