



*Market review into the ownership and competitiveness of infrastructure provision. fYa YXJYg'XYVlg]cb*

.....Responses to  
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Dear Sirs

We welcome the opportunity to respond to the PSR consultation on its proposed Infrastructure Market Review Remedies. The opportunity for us to engage with the PSR Market Review team during the process has been gratefully received and we look forward to growing our close working relationship.

We are the longest established electronic interbank payment service operator (PSO) delivering batch-processed regular payments to UK citizens and corporates utilising two major payment services; Bacs Direct Credit (DC) and Direct Debit (DD). In 2016, we processed over 6.2 billion payments worth a total of £5 trillion and broke our record for single-day payments, processing 109 million transactions at the end of September.

We are approaching our 50<sup>th</sup> birthday and our flagship payment systems, DC and DD are integral to how money is moved in the UK. Virtually all government welfare and pension payments use DC and almost all employees receive salaries using this method. Virtually everyone in the UK uses DD to pay regular monthly bills without stress or hassle. Bacs is regulated by the FCA and PSR, is an FMI company and is supervised by the Bank of England.

We have responded to the two previous PSR consultation opportunities to comment on the PSR Infrastructure Market Review. In our responses we have consistently presented our view that in a competitive market, where the reasons to do so outweigh the reasons not to, PSOs should undertake competitive procurement exercises. We have also articulated our long-standing messaging strategy; to adopt ISO 20022 for all new 'greenfield' developments and we have, by way of example, demonstrated this in the building of the Current Account Switch Service and Cash ISA Transfer Service. We therefore recognise the intention behind the proposed final remedies.

The package of final remedies, as presented, brings into focus some implementation challenges relating to the timing of their delivery and their sequencing between competing priorities. The decision of the Payments Strategy Forum to recommend the consolidation of three retail PSOs in its final strategy is one such change that has added a new variable that must be considered alongside this decision.

The Forum conclusion that, to ensure the UK payments infrastructure meets future requirements, a New Payments Architecture (NPA or Simplified Payments Platform – SPP as it has been referred to) is built also affects the timing of PSO procurement strategies and the infrastructure market review remedies.

The adoption of international messaging standards for UK payments and the approach to installing competition into the supply of infrastructure for payment operators and systems will be delivered during a period of wide changes within the UK finance industry and these changes need to be prioritised and planned for appropriately and pragmatically. Otherwise the public and businesses will be subjected to a level of risk that could easily be avoided without altering the longer term goals. In this regard developing the proposed final remedies to reflect these challenges would not alter the long term outcome and perceived benefits for the UK as a whole.

Bacs is fully committed to playing a central role in maintaining the integrity of the payment systems we have today as well as tapping into our considerable experience to develop and deliver future payments systems for the benefit of the UK.

The attached annex provides our responses to the consultation questions.

Yours sincerely

A handwritten signature in dark ink, appearing to read 'MCh', with a long, sweeping horizontal stroke extending to the right.

Michael Chambers  
Chief Executive Officer

DD 020 3217 8361

Email [Michael.Chambers@bacs.co.uk](mailto:Michael.Chambers@bacs.co.uk)

## **Annex 1:**

### **Bacs answers to consultation questions**

#### **Competitive procurement remedy**

**1. *Do you agree with our assessment of effectiveness of the potential remedies identified?***

***If not, please explain why.***

Our main comment with the competitive procurement remedy is that it does not provide sufficient clarity. We believe that the procurement remedy would be enhanced if it were more effectively “joined up” with the proposed solutions of the Payments Strategy Forum (PSF), for example, in terms of consolidation of governance, and timings of the delivery of, and migration to, a Simplified Payments Platform (SPP).

The procurement of the SPP will be overseen by the consolidated Payment System Operator (PSO). We envisage that the SPP will include a Bulk Payment Processing component that will ultimately replace the Bacs architecture. A significant migration programme will be required to move existing Bacs service users to the SPP. The Bacs system will remain “as is” until the completion of this migration and there could therefore be a need to extend the current contract with VocaLink. This extension would not be subject to competitive re-procurement until it is clear how long any extension would need to be. In this scenario, we would expect to discuss specific timescales with the PSR when there is clearer evidence about how long a new platform will take to deliver.

In the event of long delay to the replacement of Bacs within the SPP, Bacs considers that message translations by users or their chosen agents to meet specific use cases would be the preferred interim measure. These can use the best practice mappings between ISO 20022 and the existing message standard that Bacs will publish in the near future. Whilst the option exists to procure conversion services at central infrastructure level (in a space between the users and central infrastructure), Bacs considers that this may be a costly procurement of a set of complex services for a limited user base built against a functionally rich legacy system that would be made redundant following migration to the SPP.

The user interfaces to the SPP will be ISO 20022 compliant. The access requirements for the SPP should incorporate the access requirements for the Bulk Payment Processing component. Separate, independent requirements exercises must be avoided.

We envisage that the Bulk Payment Processing component of the SPP will not be a like-for-like re-procurement of the existing Bacs system. It will not contain the functional richness of the existing system, which may be viewed as a reduction in service for corporate users of Bacs current payment products. Nor will it support the existing Standard 18 messaging standard.

**2. *Do you agree with our assessment of the costs of the remedies? If not, please explain why.***

We note that the costs of the remedies have a wide range and depend on calculations provided by a single source and these have not been examined or ratified. We would expect the methodology and application for the cost analysis to have been subject to its own external consultation to ensure a satisfactory level of wider independent scrutiny.

We envisage that the costs of the migration of Bacs service users to the new SPP are likely to be significant and should therefore be estimated before implementation plans are finalised. The next step to take is the development of a detailed investment case for which more work will need to be done to validate costs.

**3. Do you have any comments on the design of our proposed remedy, including but not limited to:**

**a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?**

***The Bacs ‘discovery phase’***

We note that the PSR has explained that a ‘discovery phase’ is not required for future procurement of Bacs system functionality because the services procured in the future will be significantly different to that currently provided. We assume that this is because the assumption is that the next planned procurement will be for a single payments platform, in which the provision of bulk-batch payments (eg Bacs system functionality) will be different.

We agree that in this scenario an additional discovery phase (for Bacs) would not be necessary. In other words if the next procurement for infrastructure services is for the SPP as described by the Payments Strategy Forum in their final strategy a discovery phase for Bacs is irrelevant. However, the requirement for a discovery phase for Bacs should not be completely discounted as it will depend on the likely build and transitional timescales for the SPP, and the future procurement strategy, as well as the time required to prepare the market for a competition. We believe that, to avoid any negative consequences caused by pre-empting how the future market for competitive tendering might look, due to the current closed nature of the market, the strategy and the procurement should be carried out by the new consolidated PSO.

***Exemptions***

We note the PSR’s addition of an exemption process that allows a PSO to obtain agreement to delay the implementation of a procurement strategy. This option makes sense given the plans well underway for a consolidating the PSOs. However the timing and requirement to lodge an exemption request before 31 December 2017 means the exemption would need to be made by the outgoing PSOs. We therefore suggest either postponing the requirement for strategy setting until a decision on the future structure of PSOs is known and the new PSO is in place, or extending the 31 December 2017 deadline to 31 March 2018 at the earliest. This would enable an exemption decision to be taken within the new consolidated PSO governance structure, as we believe this is how it should be.

We recognise the need to ensure there is certainty within the industry with regard to a transition between existing PSOs and the new consolidated PSO. Splitting the responsibilities for procurement policy between the current and proposed future governance structures may add a layer of unnecessary risk to the process when it can easily be avoided.

**b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?**

If the deadline for applying for an exemption cannot be changed we propose to apply for an exemption both to allow time for the consolidated PSO to determine their strategy and because we envisage continued usage of the existing Bacs system until the completion of the migration from Bacs to the SPP at some point in the future.

We agree that PSR's remedies for infrastructure supply must recognise the conclusions and recommendations reached by the Payments Strategy Forum and that close relationship with and recognition of the Forum's work is essential for effective delivery.

#### **Messaging Standards Remedy**

**4. *Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.***

As previously stated Bacs' messaging standards strategy is to deliver all new services ('greenfield' developments) using the ISO 20022 standard, where it is appropriate to do so. A good example of our approach is the Current Account Switch Service which adopted the ISO 20022 messaging standard.

On Thursday 12 January 2017, Bacs published a new guide to help organisations translate payment messaging between Bacs Standard 18 and ISO 20022 and back.

In 2017 we will be taking our work on messaging standards forward through the production of:

- Schemas, message implementation guides and sample messages for users of ISO 20022; and,
- Specifications for implementing the translation.

These documents will be complete and available by the end of March 2017, meeting the infrastructure market review remedy. In light of this we are unclear why the PSR still intends issuing a Direction in support of its remedy when this work is already well underway and will be complete before a Direction is issued by the PSR.

**5. *Do you agree with our assessment of the costs of the remedies? If not, please explain why.***

We have no comments on the PSRs assessment of the costs of this remedy.

**6. *Do you have any comments on the design of our proposed remedy, including, but not limited to:***

***a. Whether the use of XML standard should be required to make our remedy effective?***

We envisage that the ISO 20022 syntax requirements should be finalised as part of the SPP access requirements (and should not be subject to a remedy). There is a risk that the remedy is over prescriptive and acts as an unnecessary constraint by pointing to XML as being the only syntax for ISO 20022 messaging. This approach would act as a clear barrier to the opportunities that could be presented to the industry by other syntax structures that also fall within the ISO 20022 standard.

***b. Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?***

Whilst we do not believe that a remedy is required for continuity of messaging standards in procurements subsequent to that of the SPP, we have no objection to it remaining in place.

- c. ***Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?***

We consider that the PSO mapping information should be publically available.

#### **Ownership of VocaLink**

7. ***Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:***

- a. ***the financial incentive to protect VocaLink***
- b. ***alternative providers' belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements***

***If not, please explain why.***

Bacs does not believe that competitors of VocaLink would be disadvantaged should the four largest PSPs retain a 10% shareholding. We do believe that other protections are required to safeguard the UK payments infrastructure such as those envisaged by HM Treasury, designating the infrastructure company (e.g. VocaLink) as a Financial market Infrastructure (FMI). This coupled with the new rules for FMIs under the FMI Special Administration Regime will offer additional protection which should underpin and re-enforce governance arrangements based on the same with a view to subsume into contractual obligations towards PSPs for VocaLink

However notwithstanding the above, a 'bail-out' for an infrastructure company may fall to government (e.g. the taxpayer) in the short to medium term to ensure the continuity of the UK payment systems in future until such time as a new infrastructure company is selected to provide / run the operation.

#### **Remedies package**

8. ***Do you agree with our assessment of the effectiveness of the proposed remedies package? If not, please explain why.***

We believe that the ownership of infrastructure is not as important as providing the new consolidated PSO with a realistic and robust funding model that enables it to deliver services to the entire market, including the current PSP recipients and potential future recipients of PSO services.

There is a unique opportunity to establish a consolidated PSO that can independently deliver opportunities by enabling innovation, opportunity and new services. However, its strategy to enable this depends on maintaining clear segregation (e.g. independence) between infrastructure supply and the PSO that is responsible for the delivery of innovative payment products. By this we mean the complexity of maintaining the integrity of payment systems and compliance with the rules that ensures customers have confidence in the brand means the brand(s) must be provided by a trusted independent provider that is not influenced by profit.



9. ***Do you agree with our proportionality assessment of the proposed remedies package? If not, please explain why.***

Subject to our comments above we are content with this aspect of the proposed remedies package.

# Barclays response

PSR market review into the ownership and  
competitiveness of infrastructure provision:  
Remedies consultation

February 2017

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## 1. Remedy one: Competitive procurement remedy

- 1.1. Barclays supports payment system operators carrying out procurement exercises for central infrastructure.
- 1.2. Barclays remains of the view that a remedy that required the production of infrastructure strategies by Payment System Operators (PSOs) would have been a proportionate approach to delivering competition in the provision of payments infrastructure. Instead, the PSR has decided to mandate competitive procurement exercises take place in time for the end of existing contracts (or in the case of Bacs and LINK the earliest possible termination date of the contract). The PSR will require future competitive procurement exercises to happen at least every ten years after that. The PSR has also made it explicit that it is possible for Bacs and FPS to seek temporary exemptions from their respective directions in recognition of the Payment Strategy Forum's proposal regarding the development of a new payments architecture. The PSR proposes that such exemptions should be no longer than three to four years. Barclays considers that all three decisions are broadly acceptable. However, there are elements within the remedies that merit further consideration by the PSR.
- 1.3. We welcome that the PSR has carefully considered the implications of the Payment Strategy Forum's proposals for a new payments architecture. But we do not consider that the PSR has adequately examined the interaction between the work to create a new payments architecture and the consolidation of Bacs, Faster Payments and the Cheque and Credit Clearing Company. Consolidation is expected to complete by January 2018. Barclays' interpretation of the remedy is that both Faster Payments and Bacs will have to make significant progress on each of their procurement exercises during 2017. Barclays thinks this will reduce the ability of the new consolidated payment system operator to take a more strategic approach to the procurement of payments infrastructure services.

- 1.4. If the new consolidated payment system operator were able to take a more strategic approach, it would be free to take a range of approaches to the provision of payments infrastructure services. Such approaches could include seeking a temporary exemption from the remedy to pursue the creation of the new payments architecture; a consolidated procurement exercise for both Bacs and Faster Payments; two separate procurement exercises; or, variants on the above. As currently framed the remedies do not appear to give the new consolidated payment system operator the ability to consider such options.
- 1.5. Barclays have reached this conclusion because of the PSR's view that an application for temporary exemption for Faster Payments and Bacs must be submitted by 31 December 2017. The consolidated body will not be operational until 2018, and so it will have no opportunity to consider the output of the new payments architecture design authority before the PSR expects to receive such requests.
- 1.6. In Barclays view, the most appropriate time for operators of Bacs and Faster Payments to decide whether to seek a temporary exemption from the requirement to conduct a competitive procurement will be once the new payments architecture work has been handed over to the new consolidated payment system operator in early 2018. We think at this point the new payments architecture work will be sufficiently mature for the consolidated payment system operator to make such a decision.
- 1.7. In addition, if Bacs and Faster Payments do not seek a temporary exemption from the competitive procurement remedy to pursue the creation of the single payments platform during 2017 then they will be required to undertake procurement exercises. Faster Payments expects to run a competitive procurement exercise between autumn 2017 and June 2018. Bacs state in the remedies consultation that it would need a longer time to conduct a competitive procurement exercise than others and their exercise would need to be completed by December 2018. This timeline implies that there would be two significant

procurement exercises occurring at roughly the same time, and substantially overlapping the consolidation activity. This may not lead to the most competitive procurement exercise for one or both payment systems. It may be that running the procurement exercise jointly, as a larger contract, under the auspices of the consolidated payment system operator rather than concurrently may deliver a more competitive and efficient outcome. Alternatively a staggered approach could be preferable as it may enable potential providers to bid more effectively for both contracts.

- 1.8. Barclays invite the PSR to consider whether it is desirable to delay the competitive procurement deadlines for Bacs and Faster Payments to allow the consolidated operator to make a strategic decision on the future of the UK retail payments infrastructure services. If the PSR do not consider a delay possible, Barclays suggest that the PSR issue a clarification that the consolidated body could request a temporary exemption to the procurement remedy in early 2018. Furthermore, temporary exemptions will be considered not simply due to the creation of the new payments architecture, but, also for the delivery of a more competitive procurement exercise(s). The PSR would be in the position to appraise such exemption requests.
- 1.9. Finally, Barclays questions the necessity of six monthly reporting on progress by payment system operators. We recognise the need for the PSR to keep abreast of the planning and implementation of the different procurement exercises. However, we do not think that six monthly reports are a proportionate approach. Barclays suggests that the PSR should, in its ordinary supervisory activities, be able to track the progress of each of the operators. A combination of regular supervisory meetings and an annual report would be a more proportionate approach to achieving the same outcome.

## 2. Remedy two: messaging standards remedy

- 2.1. Barclays sees merit in moving the UK payment system onto a common international messaging standard as part of a longer-term vision, and during upgrades of legacy systems. In Barclays view, this will enhance the end user experience and link more data items to payments. It will also improve interoperability between the payment systems. However, the possible impact on UK businesses of moving to a new standard should not be underestimated.
- 2.2. Barclays welcomes the proposal that Bacs and FPS prepare and make available mapping and all necessary documentation to convert from existing standards into ISO 20022 based messages. We consider that this is the most proportionate approach to stimulate the creation of translation services in the medium term. We are pleased that both Faster Payments and Bacs, working with Payments UK, have completed mapping exercises and have made them available. In Barclays' view, as much information on the mapping as possible should be publicly available; although we do accept that some payment system related documents will remain sensitive for security reasons and access to them should be controlled by the operators.
- 2.3. Barclays supports the existing systems using procurement exercises to expand the services they offer. New services could include supporting ISO20022 compliant messages as well as current standards. However, our preference remains the adoption of new standards in any new infrastructure development. The development of the new payment architecture, using more modern messaging standards, as proposed by the Payment Strategy Forum is the most appropriate long term solution. Barclays supports this development.
- 2.4. Barclays believe payment systems should adopt the right standard for the job it is trying to do. We support an approach which is forward looking and takes into account the development of APIs using lighter-weight standards, particularly in the customer interface. The need to choose the right standard is why Barclays

does not think that the PSR should specify a specific syntax for the transmission of ISO 20022 messages. Being too specific could restrict the scope for innovation. In many circumstances, the use of XML would be appropriate. But in others it would not and the use of JSON may be more practical. In Barclays' view, payment systems, with appropriate input from end users, are best placed to take such decisions.

- 2.5. Barclays welcomes the PSR's consideration of each payment system on its own merits. Barclays does not consider that LINK needs to adopt ISO 20022 compliant messaging standards. We support the PSR's findings concerning LINK.



### 3. Ownership of VocaLink

- 3.1. Barclays agrees that, given the agreement by MasterCard to acquire 92.4% of VocaLink from shareholder PSPs (subject to regulatory approval), the PSR need not pursue a remedy in relation to this matter at this time. However, Barclays continues to disagree with the PSR's conclusion that Barclays, collectively with other shareholders, controls VocaLink or any payment system operator.
- 3.2. There is no evidence to support the PSR's view that simply because the shareholder PSPs have an interest in ensuring the security, stability and resilience of the UK's payment systems that they control VocaLink. There is no evidence to suggest any collective voting on the part of shareholder PSPs, including Barclays, in VocaLink that could give rise to control (on any measure). Nor is there sufficient "commonality" under the Enterprise Act 2002 (and the relevant case law) to make a collective finding of control. There is not sufficient evidence to support the conclusion that shareholder PSPs would act together in matters related to the exposure of VocaLink to competition. Nor is there any evidence in the final report to suggest that any director, individually or collectively, has acted in this way.

## 4. Package as a whole

4.1. We have no additional comments to make on the remedies package as a whole.

The Cheque and Credit Clearing Company (C&CCC) welcomes the opportunity to respond to the PSR's remedies consultation for their market review into the ownership and competitiveness of infrastructure provision.

## **Background**

The Cheque and Credit Clearing Company (C&CCC) was established in 1985 and from that time until the present day, is proud of its record in providing members with the central payment system services for the exchange and settlement of cheques and credits.

Our objective is to ensure that cheques and credits remain a viable, secure and efficient choice of payment for all users. To achieve this we promote innovation and competition choice by driving improvements in processing, service and efficiency; and provide a trusted centre of excellence for anyone with an interest in cheques or credits.

In the evolving payments landscape, cheques and credits remain a preferred and trusted payment option among certain groups and for certain types of payment. For example, cheques remain a convenient way for businesses to pay a trade supplier and manage cash flow, and amongst consumers, are a popular way to pay utility bills, tradespeople and clubs or societies. In the past year, nearly three-quarters of UK charities and two-thirds of UK businesses both received and made payments by cheque over a monthly period. In total, 558 million cheques were written in 2015 with a total value of £624 billion.

C&CCC is working to deliver the Image Clearing System (ICS), which will bring the cheque into the digital age via the implementation of an image-based cheque clearing process in the UK.

A full account of our background and objectives can be found on our [website](#), as can more information on the [Image Clearing System](#).

The consultation focuses upon Bacs, FPS and Link. As a PSO, C&CCC is not a stakeholder of these PSOs and it would therefore be wrong for C&CCC to respond in detail to your consultation. However, we do offer some general comments on the issues raised.

## **Competitive Procurement**

You asked the following questions:

1. Do you agree with the assessment of effectiveness of the potential remedies identified? If not, explain why.
2. Do you agree with the assessment of the costs of the remedies? If not, explain why.
3. Do you have any comments on the design of our proposed remedy, including but not limited to:
  - a. An additional requirement of a discovery phase is necessary to make Bacs competitive procurement effective?
  - b. Proposals for interaction with the Forum, possible temporary exemption periods, milestone timing and process for applications?

In general we believe that procurement by PSOs should be by competitive means. This would help in establishing effective competition in the payments market. However the length of contracts needs careful consideration, and we do not believe that there can be a 'one size fits all approach' for a number of reasons including:

- Systemically important payment systems are collaborative by their very nature, and there needs to be a critical mass prior to introduction for them to be effective.

Without this critical mass of PSPs and PSOs run the risk that investment, time and effort will be wasted.

- Payment markets are fast moving when a critical mass is reached, but can be slow and hard to predict when innovation is introduced. It would have been difficult to have predicted the rapid rise in FPS as well as the low take up of Paym.
- Payments once they become established have a long life, and it often takes regulatory change to initiate a move from another type of payment.

Therefore, we consider that ten years could be too long in an established payment scheme, and would suggest the ability to break any contract of that length after say five years. However, if companies are to invest in new markets, or for that matter support declining payments types, a ten year contract may be necessary if one off and migration costs are to be minimised.

C&CCC has recently managed a competitive tender. Due to the change from paper to image, the relatively small volumes of cheques and the declining market of cheques our costs are probably not typical of such procurement. However, the cost and complexity of managing such an exercise should not be underestimated for a relatively small PSO.

In general we would recommend the introduction of a 'discovery phase' in both new and existing payment systems to ensure that tenders meet and understand the PSOs requirements and incumbency advantage is minimised.

It is understandable that the PSR interact with the Forum's work, given that the PSOs may be consolidated by end of 2017. In the same way as the PSOs could be merged, it would also be possible to merge the infrastructure. However, this could result in resilience and robustness issues and a policy on this needs to be considered before competitive tendering results in such proposals especially with the introduction of ISO 20022..

## **Messaging Standards**

You asked the following questions:

4. Do you agree with the assessment of effectiveness of the potential remedies identified? If not, explain why.
5. Do you agree with the assessment of the costs of the remedies? If not, explain why.
6. Do you have any comments on the design of our proposed remedy, including, but not limited to:
  - a. Using XML standard should be required for the remedy to be effective?

- b. The remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?
- c. Should the operators of Bacs and FPS make mapping information publicly available or are there reasons why it should be made available subject to certain conditions?

C&CCC believes in general that having a common messaging standard between all payment schemes would improve interoperability, resilience and contingency. The C&CCC is working towards making ICS ISO20022 compliant with a view to gaining the ISO standard once ICS is live. We believe that conversion services should only be a short term, and a possible chargeable solution. Once the decision is made to move to a new standard new participants should be able to use the new standard without attracting overheads for other participants conversion.

### **Ownership of VocaLink**

You asked the following questions:

- 7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:
  - a. The financial incentive to protect VocaLink
  - b. Alternative providers belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements

Although the question raised concerns VocaLink, C&CCC considers that the response is true of any supplier to a PSO. Irrespective of the size of shareholding, so long as PSPs that own the PSOs have a share in any supplier to the PSOs there will always be a perception of unfair advantages. This perception could be to the advantage of the supplier (ie protect the supplier from retendering and competition), or to the advantage of the supplier's PSP minority owners (ie information, charging and preferential treatment).

### **Remedies Package**

You asked the following questions:

- 8. Do you agree with the assessment of the effectiveness of the proposed remedies package?
- 9. Do you agree with the proportionality assessment of the proposed remedies package? If not, explain why.

We have nothing further to comment on.

**Confidentiality**

C&CCC is content for this letter to be made available to the public. We will be making it available through our website.

**Conclusion**

C&CCC considers that this consultation raises many issues which will affect the payments market and will be critical the successful delivery of a new payments strategy. We would, of course, be happy to meet with the PSR to discuss this response.

Yours faithfully,

A handwritten signature in dark ink, appearing to read 'James', with a stylized, flowing script.

James Radford  
Chief Executive Officer

A decorative network diagram consisting of numerous red and orange dots of varying sizes connected by thin lines, forming a complex web that spans the upper and right portions of the page.

## **Response To Market review into the ownership and competitiveness of infrastructure provision**

**Remedies consultation  
December 2016  
MR15/2.4**





## Competitive Procurement Remedy

### 1. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

Yes we agree with the assessment of effectiveness mandating Operators to undertake competitive procurement for central infrastructure services. Option 1 (Issuing best practice procurement guidelines) and Option 2 (Requiring operators to set a procurement strategy) go some way but do not ensure a competitive procurement process.

We understand the main goals of the procurement remedy are to satisfy the service-user needs and promote competition. To achieve these goals we consider that the procurement strategy should be transparent with criteria that benefits UK society. Features of a competitive procurement process include:

- a) The factual and measurable definition “engagement with potential providers” to be evidenced. The collaborative nature of the interactions between the Operator and the potential providers can be captured via meeting minutes and communications.
- b) A definition of measurable Key Success Factors to assist comparison of potential providers.
- c) Each potential provider to be qualified according to the social benefit solution may provide.
- d) Taking the lessons learnt from the existing contract(s) with VocaLink<sup>1</sup>. We consider that current exit provisions require scrutiny.
- e) Commercial arrangements that apportion risk equitably between Operator and provider that support the optimal delivery of the infrastructure for all parties.

We welcome the initiative that the Payment Scheme Operator(s) will report at each stage of the procurement process to the PSR and that a non-confidential version of the final procurement contract will be published.

Allowing shortlisted providers on-site access to VocaLink staff Could pose a risk to current operations if VocaLink resources are diverted. Any invitation to tender (ITT) should contain all the information a new provider requires.

The procurement components below will support effectiveness:

- Strategy
- Consultation - With service users and providers prior to tender process commencement
- Transparent Shortlist
- Uniform Tender Award Criteria

We would expect and endorse the appointment of a competent third party to run and administer the procurement process.

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<sup>1</sup> 29 PSR MR15/2.3, Market review into the ownership and competitiveness of infrastructure provision 4.29

## 2. Do you agree with our assessment of the costs of the remedies? If not, please explain why

Yes we agree.

In our experience costs that are often underestimated include:

- Those incurred by all stakeholders for the migration to a new service provider, including; testing, parallel running, transition and warranty period after launch.
- Those for required network infrastructure and security changes.

## Do you have any comments on the design of our proposed remedy, including but not limited to:

### a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?

The introduction of a three month discovery phase is likely to impact procurement progress. The merits of analysing the 'As-Is' state are limited as changes are anticipated. The mature Bacs operation is well documented at both technical and business levels and potential providers will have considerable information from the current document set.

An option for consideration may be the provision of a Data Room – whereby VocaLink provide data on current operations, e.g. performance against SLAs, commercial terms, to prospective bidders through an “acquisition” style data room. Bidders to have registered an interest and been qualified. This assumes NDAs are in place.

## Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?

### Forum Interaction

The interaction of the procurement exercises with the Forum makes sense with regard to the three areas mentioned:

- Long term UK Payments Strategy
- Governance Consolidation
- New Payments Architecture Vision, including prioritisation and scheduling of change

Ideally design milestones and the procurement exercise will be aligned so as to identify optimum solution and costs.

### Temporary Exemption Periods

No comment.

### Milestones

#### Scenario 1 – New Payments Architecture Live End 2020

There are three dependencies in the scenario that require consideration:

#### 1. The conclusion of PSO governance consolidation by end 2017

This work is underway. Economies around rules and operation may not be as great as expected. This stakeholder group is predominantly PSO personnel and the impact on wider stakeholder community is manageable.

## 2. New Payments Architecture (NPA) designed by end 2017

The NPA design is material to the UK economy, PSPs and end-users. For this reason gaining consensus on NPA functionality may be protracted and redesign required. The initial stakeholders involved are likely to be technical in nature and disagreements are anticipated. A wider consultation exercise is expected with end-users. For these reasons the end of 2017 may be a challenging milestone but one to be aimed for in order to maintain momentum. It is anticipated that the NPA infrastructure will support incremental growth and the incorporation of new services.

Based on our experience in the Paym programme it is recommended that consideration is given to End of Life planning as part of the NPA design work stream.

NB: The ability to combine faster payments and batched payments in a single solution has not been attempted to date.

## 3. New Payments Architecture Challenges

A level of quality assurance will need to be applied to the NPA design. It may transpire that the combination of faster payments and batched payments may be challenging to implement in one tranche. It may also be challenging to deliver faster payments and batched payments on NPA with operational costs that are no higher than those for the current operations. It is recommended that this oversight remains independent of the combined PSO.

Timescales aiming for completion by 2020 are tight particularly considering protracted nature of legal, commercial and technical work packages.

Limiting the duration of translation services as with SEPA is recommended,

### Scenario 2 – New Payments Architecture Delayed

In this scenario a competitive procurement exercise for Cheque & Credit Clearing, Bacs and FPS infrastructures could take place. This is not ideal. It is recommended that no one supplier can ring all three procurements, (if there are three).

### Application Process

A clear case is required from the Operator detailing why benefits of procurement are outweighed by dis-benefits. In order to assess the application weightings should be applied to each benefit and dis-benefit to arrive at an overall outcome. The rationale for granting an exemption for contracts of less than five years duration is sound.

The duration of a temporary exemption at no longer than 3 to 4 years, should be defined as either 3 or 4 years for the avoidance of doubt.

## Messaging Standards Remedy

### 4. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

Yes we agree.

### 5. Do you agree with our assessment of the costs of the remedies? If not, please explain why.

Yes we agree that SMEs with low volumes will rely on conversion tools until their software supplier(s) can provide a straightforward method to convert historic formats into new ISO formats. The costs to SMEs to convert to ISO20022 are likely to be significant.

The advantages noted for large corporates (s4.36) will initially be offset by the significant effort required to implement new message formats in their organisations as seen with SEPA DDs. The remedy to facilitate use of conversion tools is welcomed.

**6. Do you have any comments on the design of our proposed remedy, including but not limited to:**

**a. Whether the use of XML standard should be required to make our remedy effective?**

There are significant benefits to be achieved by moving to a common messaging standard for UK payments and ISO 20022 has become the preferred standard for financial messaging.

**b. Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?**

Regardless of whether a competitive procurement exercise is undertaken a uniform format will assist processing cohesion between differing payment types.

**c. Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?**

The mapping of data in the message structures currently employed by Bacs and FPS to ISO 20022 has been made publicly available. This open information supports competition and transparency.

It is recommended that one owner of the mapping standard is appointed with the authority to create, modify and publish a series of documents to assist stakeholders in the migration incorporating new versions of the XML if they become available. Supporting documents to include:

- Character set supported
- Message Implementation Guides defining how the ISO 20022 messages are to be used
- Rulebooks defining rules and obligations of participants and CSMs (Clearing and Settlement Mechanisms)
- Implementation guidelines for PSPs
- Implementation guidelines for inter-bank payments
- Payment initiation characteristics e.g. contactless payments

## Ownership of VocaLink

**7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:**

**a. the financial incentive to protect VocaLink**

No. There may be a conflict of interest between the four largest PSPs and VocaLink depending on company board voting rights, power of veto, structure of VocaLink Board and company strategy. The merits of 'protecting' VocaLink are unclear.

**b. alternative providers belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements. If not, please explain why.**

No. Organisations without representation on the VocaLink Board are likely to influence company decisions thus remaining outside the 'circle of influence'.

## Remedies Package

**8. Do you agree with our assessment of the effectiveness of the proposed remedies package? If not, please explain why.**

Yes, partially. This is a good starting point but how will historic influence of large members be diluted.

**9. Do you agree with our proportionality assessment of the proposed remedies package? If not, please explain why.**

Yes. The quantification of the social costs can be derived from historical data.

**10. Will the messaging standards remedy the competitive procurement remedy or will the overall package result in the loss of any benefits to users?**

A loss of benefits to users is not envisaged. A standardised solution may be less able to accommodate bespoke services. Any loss in benefits to be weighed against overall cost and the user tariff model.

**Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.**

No response.



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# UK market review into the ownership and competitiveness of infrastructure provision

equensWorldline response to the PSR's Remedies Consultation

Final

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# 1 Management Summary

Please find below our responses to the Remedies Consultation questions on the proposed remedies to address the identified ownership and competitiveness issues.

Our responses are supportive of the stance being taken with regard to ensuring competitive procurements take place for the Bacs, FPS and LINK payment infrastructures. However, as the PSR and other stakeholders will appreciate from our responses, we are concerned that there are many potential diversions that could derail the PSR from achieving its competition objective.

We have, therefore, suggested enhancements to strengthen the remedies being put forward. We believe that, if the PSR includes these enhancements, competitive procurements will be able to deliver the competition and innovation that the UK payments market needs, for both consumers and businesses, within the shortest possible time period.

Our concern, if these enhancements are not taken forward, is that stakeholders in the payments industry will prevent true competition being achieved by adding complexity and delay to the process. This, we believe, will be inevitable if competitive procurements are, for instance, in any way linked to the output of the Payments Strategy Forum (PSF).

The work of the PSF and the needs of service users are extremely useful in informing the procurement requirements for Bacs, FPS and LINK and to ensure that the desired direction of travel along with the ability to fulfill future requirements is built in to the process. Critically, as the PSR has identified, this can be achieved in a timeframe that is consistent with the current contract end (or first termination) dates for Bacs, FPS and LINK.

We believe the best way to drive innovation and to achieve any future, agreed, target payments infrastructure is to ensure real competition is injected into the market at the earliest opportunity.

A key question for the PSR to consider is whether it will be able to maintain momentum around the implementation of its remedies. If the PSR does not get the strength of its remedies right then the competitive procurements will be severely delayed or, perhaps even worse, credible alternate providers will not believe the procurements are worth participating in either now or in the future.

With this potential negative outcome in mind we would ask the PSR to seriously consider the remedy enhancements we have detailed below.

Dave Allen  
Managing Director UK branch office  
equensWorldline

## 2 Competitive procurement remedy

We agree with the competition issues that the PSR has identified, namely that:

- operators and direct payment service providers (PSPs) do not have a strong incentive to run competitive procurements, which has resulted in limited competitive pressure on VocaLink
- the use of bespoke messaging standards by Bacs and FPS is a barrier to entry for alternative providers of central infrastructure services
- the current ownership and governance arrangements at VocaLink are likely to reduce the level of competition in the provision of central infrastructure services

However, we are not fully convinced that the remedies set out by the PSR will be able to fully solve the identified issues. Our reasoning for this assessment is set out below but, broadly, our concerns lie in the introduction of these remedies in a way that both supports alternative providers investing in the market and also prevents those currently involved in the UK payment ecosystem from maintaining the status quo through a reluctance to change.

### 2.1 Remedies consultation question 1

- Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

We agree with the assessment detailed in the Consultation that mandating, as opposed to setting best-practice guidelines or procurement strategies, offers the best route to establish effective competition for the market.

However, we do not feel that the consultation sets out strongly enough how this will be enforced and overseen. We believe that without strong enforcement and oversight the competitive procurements may not take place within a reasonable timeframe and that when they do take place they will still include incumbency advantage.

### 2.2 Remedies consultation question 2

- Do you agree with our assessment of the costs of the remedies? If not, please explain why.

We agree with the PSR's assessment that the cost of running a competitive procurement will be between £6 million and £10 million each for the Bacs and FPS schemes and less than £1m for the LINK scheme.

### 2.3 Remedies consultation question 3

- Do you have any comments on the design of our proposed remedy, including but not limited to:
  - a. Whether an additional requirement of a discovery phase is necessary to make a Bacs competitive procurement effective?
  - b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?

We believe that the PSR has correctly identified the key factors that could adversely impact a competitive procurement, but we are not comfortable with the PSR's assessment of what is needed to mitigate the impact of these factors.

For instance, with regards to the factor concerning 'the existence of credible alternative providers', although credible alternative suppliers do exist, their existence will be immaterial if they do not take part in the procurements because their respective organisations believe there is too much incumbency advantage and therefore the procurements do not offer a credible business opportunity. Therefore, unless the elements the PSR puts in place provide full transparency and clear and unambiguous procurement plans, that ensure no perceived incumbency advantage, all credible alternative providers will struggle to gain the internal sign-off that they will need to participate in one or more of the procurements.

In respect to the specific elements in section 3.59 that the PSR has considered, in deciding how to specify an effective competitive procurement, we would ask the PSR to fully consider the following points:

**Basic requirements** – we agree that the basic requirements that the PSR has listed for the procurement process must be included. However, we believe the PSR should additionally specify more detailed requirements with regard to how the procurements must be run, such as:

- Engagement with potential alternative providers, prior to the commencement of the procurement process, to understand their views on participating;
- An Expression of Interest (EoI) stage to shortlist a maximum of four or five alternative providers;
- A data room or discovery phase;
- A final Request for Proposal (RfP) stage that follows best practice with clear selection criteria.

This would ensure that the scheme(s) are proactively engaging with potential alternative providers and are fully aware of the capability that exists in the market, ahead of the EoI shortlisting of alternative providers to take part in the RfP selection stage.

**Independent audit or third-party run procurement** – to ensure potential alternative providers are confident that any UK payment scheme procurement is open and transparent it will be essential that the PSR mandates that the competitive procurements include independent audit. This will reassure potential alternative providers that the result will be the optimal choice for the wider market.

**Discovery phase for Bacs** – we believe that a data room or discovery phase will be essential as, even with ISO20022 being part of any Bacs procurement, the 40 plus years that the incumbent has operated the Bacs system means there is still technical and operational complexity and therefore incumbency advantage. This complexity will be even greater if requirements linked to peripheral Bacs services, e.g. CASS, DEPS, RTI, CashISA, etc., form part of what is being procured.

**Timing of the remedy** – the timing of the remedy is best, as the PSR has correctly described, aligned with the end (or earliest termination) dates of the current Bacs, FPS and LINK contracts (Scenario 2 in Figure 1 of the Consultation paper) and should therefore not be allowed to be held to ransom by having to wait for the PSF. The Bacs, FPS and LINK schemes can inform their requirements from the work being undertaken by the PSF and the Schemes can put in place contracts that provide flexibility. Linking the procurement to a dependency on the output of the PSF would likely delay the introduction of competition and we recognise that, as the consultation notes, the PSF dates are subject to change.

**Interaction with the Forum (including Work of the forum and service-users' needs)** – as above the work of the PSF and service-users' needs should inform the requirements for what Bacs, FPS and LINK wish to procure but the timings of the competitive procurements should not be linked to the timings for the PSF.

**Potential exceptions to our remedy** – whilst appreciating that nothing can be certain we feel that the opportunity for exceptions, that prevents one of more of the competitive procurements taking place, offers the potential for 'back-room' deals unless, when an exception is sought, it is

consulted on by the PSR as part of its assessment. Without this, alternative providers will feel that, even with the PSR providing regulatory oversight, decisions are happening behind closed doors. Transparency will be key in proving that payments is now working for the whole market and not just its members.

**The need for reporting requirements on the operators' progress** – we agree that regular formal reporting by Bacs, FPS and LINK is necessary to help ensure compliance. We think that this should start prior to July 2017, to ensure the PSR has full oversight of the progress being made by the Scheme(s). In addition, we believe that, in the first instance, the frequency of reporting needs to be greater than every six months – we suggest quarterly reporting – so the PSR is better able to react to any perceived delays in preparing for and running competitive procurement exercises.

**Implementation risks** – we agree with the PSR that the competitive procurement remedy should be straightforward to implement.

## 3 Messaging standards remedy

The messaging standards remedy will be very supportive in enabling alternative providers to participate in Bacs and FPS competitive procurements.

The consultation though is narrow in its conclusions on the Messaging Standards remedy. We believe the inclusion of ISO20022 as part of the competitive procurement of Bacs and FPS could include additional interventions that would widen its benefits beyond simply enhancing the competitive procurement of central infrastructures.

As such we ask the PSR to consider additional Messaging Standards interventions, including mandating that PSPs that are intrinsically linked to the payments infrastructure fully adopt ISO20022 in-line with the competitively procured Bacs and FPS services moving to this standard.

This type of additional intervention, along with an end date for the current messaging standard, would, we believe, enhance the messaging standards remedy beyond simply delivering enhanced competition benefits at the central infrastructure level.

### 3.1 Remedies consultation question 4

➤ Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

We believe that alignment with international messaging standards, as part of the wider package of remedies, will be supportive in enabling alternative providers to compete with the incumbent provider. We also believe, as the PSR has correctly identified, that the Messaging Standards remedy starts to lay the foundations for the end-to-end adoption of ISO20022 and as such is supportive of the PSF's thinking on ISO20022.

However, because it is supportive of the PSF's stated strategy around innovations such as Enhanced Data, we do not think the Consultation fully acknowledges that there is no reason why a PSF exception would be allowed to delay the competitive procurements of Bacs or FPS. There is clearly a need for the wider PSF thinking to inform requirements; this does not equate to a need for an exception or delays to the introduction of competition.

### 3.2 Remedies consultation question 5

➤ Do you agree with our assessment of the costs of the remedies? If not, please explain why.

We agree with the PSR's assessment that the costs for its ISO20022 remedy will be negligible, if conversion services are provided as part of the competitively procured central infrastructure provision.

However, we also believe that the PSR could make additional regulatory interventions as part of its ISO20022 remedy that would support movement towards the full adoption of ISO20022. This would enable the messaging standards remedy to deliver benefit beyond enhanced competition at the central infrastructure level.

These additional interventions are discussed below but they broadly acknowledge that ISO20022 is currently used across new payment services such as CASS, Cash ISA, etc. and as such the PSR could acknowledge the ability of PSPs, who are part of the payments infrastructure, to be fully

ISO20022 compliant compared to businesses, etc. who are users of payment services and current standards who would need the support of a central conversion service.

### 3.3 Remedies consultation question 6

- Do you have any comments on the design of our proposed remedy, including, but not limited to:
  - a. Whether the use of XML standard should be required to make our remedy effective?
  - b. Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?
  - c. Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?

We are supportive of the most widely used syntax for ISO20022 as this would ensure greater standardisation with the existing use of ISO20022, both in the UK and across existing alternative provider services.

Once introduced, the ISO20022 standard should then be further embedded with a plan for full adoption across both Bacs and FPS. As such, we believe the PSR should consider additional interventions to support full adoption, including mandating plans for Bacs and FPS to fully adopt ISO20022 during the term of the newly procured Bacs and FPS contracts, to enable the wider benefits of ISO20022 to be realised.

In addition, because PSPs, who are currently members of the Bacs and FPS schemes, already have ISO20022 based infrastructures in place, e.g. CASS, Cash ISA, etc., we believe the PSR could make an additional regulatory intervention to mandate those PSPs, that are part of the payments infrastructure, that they need to become fully ISO20022 compliant.

For alternative suppliers this would further support their involvement in competitive procurements for Bacs and FPS as well as enabling the wider benefits of ISO20022 to be realised.

We are supportive of mapping information being made available to ensure that how Bacs has interpreted ISO20022 is fully understood by all alternative providers ahead of any competitive procurements taking place.

## 4 Ownership of VocaLink

If the retention of a 10% ownership of VocaLink by the four largest PSPs does not provide the four PSPs with any additional voting rights or say over relevant reserved matters, then it is likely to be effective.

However, if there is a lack of transparency with regard to any additional strategic influence the four largest PSPs might have, then alternative providers may, because of their previous experience, assume that VocaLink has an advantage in the competitive procurements of Bacs, FPS and LINK.

### 4.1 Remedies consultation question 7

- Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:
  - a. the financial incentive to protect VocaLink
  - b. alternative providers' belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements
 If not, please explain why.

We agree with the PSR's assessment but are concerned that, if VocaLink's ownership or governance arrangements are not transparent, there could be a perception that the four largest PSPs may have a bias towards VocaLink. This perception may lead alternative providers to assume VocaLink will have an advantage in the competitive procurements of Bacs, FPS and LINK.

In addition, if a single supplier was able to win all three Bacs, FPS and LINK contracts this would create the view from alternative providers that the four largest PSP's want the outcome from any competitive procurements to be continuation of the current monopoly provision.

We believe that ensuring there are separate providers for BACS and FPS will guarantee competition and set up the necessary commercial tensions to drive innovation. This would only be possible if the major customers are significantly separated from ownership of one or other of the suppliers.

## 5 Remedies Package

In considering the full remedies package we believe the Consultation does not fully highlight the potential benefits that competitive procurements, in line with the current end (or earliest termination) dates of the Bacs, FPS and LINK contracts, could bring.

We were disappointed for instance that the Consultation does not highlight the potential for competitive procurements to deliver elements of the functionality that the PSF has set out as being required. Even if this was just the introduction of ISO20022 it would mean that this innovation would be introduced as part of the newly competitively procured Bacs and FPS services.

As such we believe the Consultation, in proposing its remedies package, has understated the benefits that running competitive procurements for Bacs, FPS and LINK, in-line with their current end (or earliest termination) dates, will bring to the market from both a functionality and a cost perspective.

As stated above, we believe the best way to drive innovation and to achieve any future, agreed, target payments infrastructure is to ensure real competition is injected into the market at the earliest opportunity. Commercial interests will then drive the necessary changes.

### 5.1 Remedies consultation question 8

➤ Do you agree with our assessment of the effectiveness of the proposed remedies package?  
If not, please explain why.

As above we believe the assessment of the effectiveness of the proposed remedies package both underplays the incumbency advantage and also the potential benefits (increased functionality and lower costs) for the market if truly competitive procurements can be run for Bacs, FPS and LINK.

### 5.2 Remedies consultation question 9

➤ Do you agree with our proportionality assessment of the proposed remedies package?  
If not, please explain why.

We agree with the proportionality assessment of the remedies package.

### 5.3 Remedies consultation question 10

➤ Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.

We believe the overall remedies package will only deliver benefit to users. The exception to this statement, however, is if the implementation of the remedies package is delayed and not delivered in-line with the end (or earliest termination) dates of the current Bacs, FPS and LINK contracts.

As the PSR has identified there is an estimated price benefit of £100m to £200m, in addition to the innovation benefit, that any delay would prevent being realised to the detriment of the users, including the biggest user the UK Government, of the payments systems.



FPSL welcomes this opportunity to respond to the Payment Systems Regulator (PSR)'s proposed remedies in the Market Review – Remedies Consultation (“consultation”) issued in December 2016.

Since the launch of the Market Review in early 2016, FPSL has been engaged with the PSR, and will continue to do so, to support the PSR in advancing their statutory objectives to promote effective competition, to promote innovation and to ensure payment systems are operated and developed in the interests of all service users. We continue to support the direction the PSR has taken to address the issues identified in its Market Review – Final Report and are pleased to see the PSR promoting an environment for effective infrastructure competition through its two proposed remedies in the current consultation.

In this letter we detail our views on the two proposed remedies: competitive procurement and messaging standards, which directly affect FPSL. We do not provide any comment on the PSR's assessment of costs of the two remedies and the effectiveness as we accept the business case as set out in the Final Report (July 2016).

### **Remedy one – Competitive Procurement**

FPSL has confirmed its intention to competitively procure by 2020 in our formal submissions to the PSR in April 2016 and September 2016 and through our ongoing dialogue with the Regulator. We are supportive of the specifics of this remedy that a competitive procurement tender must take place at least every ten years and that the tender must include the need to support modern messaging standards such as ISO 20022.

We will continue to be open and transparent with the PSR around our thinking and approaches to the various procurement stages we undertake between now and the point at which a contract would be signed.

FPSL is currently working on the early stages of its invitation to tender (ITT) where we are hoping to send these out to potential bidders in autumn 2017 and are currently on track to meet this timing. We make the following observations for the PSR to consider as part of this consultation process, which sets out the minimal amount of regulation in accordance with the Regulator's Proportionality and Efficiency Principles.

### **1. Reporting process**

FPSL believe the reporting requirement and process for this remedy is unnecessarily complex and places a disproportionate administration burden for FPSL **and** the PSR over and above our current working arrangements with the Regulator. We believe the costs and resources involved in the reporting process of every six months outweigh the benefits of fully focussing on the competitive procurement process effectively and efficiently in the interests of all service users and for us to work on the different stages required of a procurement exercise.

FPSL and the PSR have an existing, structured communication relationship that enables both organisations to receive regular progress updates against multiple work streams and to monitor and report any arising issues. For instance, since 2015, we have in place an ongoing, monthly meeting with the PSR's Access team to discuss FPSL's Access Programme and the dialogue we have with Fintechs, aggregators and other service users. This platform also enables the PSR to notify of us any developments and/or engagement they might have had with stakeholders that may be of interest to us. Such arrangement gives FPSL the flexibility to run its Access Programme effectively and for the PSR to monitor and receive updates without the need of regular published reporting, encouraging an open, transparent relationship where FPSL can voice early thoughts on issues and seek informal feedback from the PSR. We believe this approach has delivered optimal outcomes for new PSPs in our Access Programme which is agreed by all to be a very significant success for FPSL and the PSR.

Annex 3 of the consultation sets out a draft specific direction 3 on FPSL to report back to the regulator every six months its progress on the tender process and contract negotiation starting from July 2017. FPSL believes a formal specific direction is not required and sees no benefits to FPSL or the PSR in the long term. Given the specific direction applies to just two not-for-profit Payment System Operators (PSOs) and not multiple organisations; the reporting requirement is likely to increase our incremental costs. We therefore ask the PSR to consider the regulatory communication framework currently in place between us on an "open and no surprises culture" that accommodates progress of the work FPSL is actively undertaking on the different elements and/or stages described in Annex 3.

This approach will give the PSR the assurance it is seeking from us in ensuring a much richer, open and in-depth conversation as opposed to reporting, that will need to be formally reported on and published. As the PSR will be aware, significant administration burden is placed on both organisations to redact and publish reports and statements that, at times undermine the overall process it is trying to achieve. For sensitive matters such as procurement, it is likely that any publishable report would need to be so heavily redacted as to be of arguable benefit. The reporting requirement is likely to impact and/or reduce our flexibility on the commercial negotiations to get the best value for all service users that in turn will result in a poor value outcome for the next contract.

## **2. Derogation in the public interest - Exemption for unforeseen circumstances**

The consultation describes the potential exemptions (pages 22-26) to the PSR's remedy where circumstances may change and a temporary exemption is warranted requiring the PSOs to explain their reasons to the regulator by 31 December 2017. We strongly believe the exemptions are disproportionately prescriptive and could potentially be seen as a constraint on the overall procurement exercise. Further, it does not consider the unknown eventualities of the future. For example, one scenario is that, nine months prior to the go-live date of the new contract being signed with a preferred bidder, there could be another financial crisis; therefore the PSO should be in a position to approach the PSR to inform them that proceeding with a new contract would not be in the public interest, would not be good for the economy or would decrease financial stability.

FPSL proposes the PSR consider explicitly inserting a statement in the formal specific direction 3 that if the PSO wishes to apply for derogation in the public interest, it can approach the PSR at any time, rather than within a prescribed timeframe. The derogation capability will enable the PSO to approach the PSR and seek to make the case in the public interest or financial stability outside the prescribed exemptions and timeframe for whatever adjustment to the tender approach it believes is required.

Finally, we note on page 11, paragraph 3.16, the PSR explains a situation where a winning provider may walk away from delivering the contract. However, the consultation does not go far enough to articulate that the PSO may want to walk away from the contract. For example, should FPSL successfully select its preferred bidder and six months into the contract, the contractual terms are not being met by the provider or the transition to the new infrastructure has greatly impacted services users, the PSO should have a derogation in place to approach the PSR and inform them of their decision to end the new contract and extend the previous contract in the public interests or financial stability until a suitable solution has been found.

Our interests with the PSR are broadly aligned and, we want the best outcome for all services users. As noted earlier, with just two organisations to which these remedy applies to (who are expected to consolidate into a single entity by the end of 2017), there is a risk of unnecessary regulatory constraint on our negotiating and bargaining power in the interests of service users. We believe known and unknown eventualities are likely to occur between now and 2020, and beyond, such that setting deadlines is not the best regulatory approach.

We understand the desire of the PSR to provide regulatory certainty. However, given the complex environment, broad range of factors to be considered and multiple inherent uncertainties, we believe the approach proposed will not provide greater certainty, but will constrain decision making in the interests of service users and the UK economy.

### 3. Consulting Service Users

On page 18, paragraph 3.64, the consultation states “*operators will be required to consult service-users, including PSPs and end-users, about the services they wish to receive and in turn which the operators should procure.*” This statement is not accurate. We as a service provider and a commercial entity will be consulting with service-users to understand what our service users want and need. Based on our engagement, dialogue and research we are best placed to decide how best to prioritise and deliver to meet the requirements, whilst ensuring these wants and needs captures the current and future trends within the industry. Service users play an important role in informing us through a number of channels the services they want. However, it is up to the PSO to determine how best to provide those service users, including what should be outsourced. The PSO is **not a collective procurement agent**; it is a **service provider** responsible for the risk management and utility of the whole eco-system.

### 4. Ecosystem business case

When selecting a supplier PSOs need to consider the full ecosystem business case (including participant costs and benefits) to determine what is in the best interests of the economy. However, when factoring in participant costs and benefits it should be those for “an efficient PSP” to ensure that a decision in the interests of the UK economy is not derailed or prevented by the inefficiency of a particular PSP or PSPs.

## Remedy two – Messaging standards

As per our formal responses in April 2016 and September 2016 and our ongoing dialogue with the PSR of our intention to move to ISO 20022, FPSL is, we believe, already compliant with this remedy. In the last 12 months, FPSL has been working hard to drive forward the mapping documentation of messaging standard ISO 20022 to the bespoke iteration of ISO 8583 messaging standards used in FPSL's central infrastructure. This is designed to provide long term benefits to current and future providers. We have ensured this work is part of our corporate strategy, and the steps described in Annex 3 of the consultation, are included in FPSL's business plan.

On Tuesday 10 January 2017,<sup>1</sup> FPSL published the Faster Payments Standards Library, a new, free to use interactive model for developers working for FinTechs, challenger and established PSPs, aggregators, software vendors and others across the payments industry. The interactive model allows users after a simple registration step to use the tool and map the ISO 8583 messages used by the current Faster Payments infrastructure to and from the globally recognised ISO 20022 standard and vice versa. Our publication of the Library has been well received within the payments industry with the following registrations taking place since launch: 68 organisations (not including FPSL, Payments UK & UK Payments), 22 countries including Great Britain and 103 individual registrations.

We believe we are compliant with this remedy and meet the elements prescribed in the draft specific direction 5 including, where possible, given the constraints of mapping the information from one messaging standard to another. We therefore ask the PSR to confirm that, at the point at which the PSR issue specific direction 5, FPSL is already compliant and in accordance with the requirements of the final specific direction and consequently would not require us to submit a formal report, nor indeed set a deadline for FPSL to be compliant?

We note in paragraph 4.7, the consultation defines ISO 20022 as the appropriate international messaging standards based on the PSR's engagement with its stakeholders. FPSL does not agree it is appropriate to define ISO 20022 as **the** international messaging standard and consider that a degree of flexibility is required to amend the standard from time to time, to support the future needs, requirements and interests of services users at that point in time. We agree the provision for central infrastructure must be competitively procured at least every ten years and that the next procurement must support the use of ISO 20022. However, this messaging standard is appropriate to fulfil the requirements for today and may not necessarily be the case for the future. As such, the PSR should consider the likelihood of other future messaging standards that may develop over the coming years in its final decision document and not just mandate one particular messaging standard.

<sup>1</sup> Access to the Standards Library can be found [here](#).

Finally, in paragraph 4.49, the consultation discusses the widely used eXtensible Mark-up Language (XML). The use of XML provides an internationally recognised standard approach for message definition for interchange. The available tooling associated with XML, XML schema validation and XML data transformation make its usage compelling. However, newer structured data exchange formats exist such as JSON, which in certain contexts, such as APIs, may be more appropriate. ISO20022 does not necessarily mandate the method required to render particular business messages, although in most cases the preferred method is currently XML. As such FPS would support and recommend XML usage in future development, however we do not feel it is appropriate to mandate its **exclusive** use on all interfaces as other structured data exchange methods may be more appropriate in the context in which it is being used.

We look forward to continuing to work with the PSR on the proposed remedies and the outcome of their final decision.

**HSBC BANK PLC**

**PSR MARKET REVIEW INTO THE OWNERSHIP AND COMPETITIVENESS OF  
INFRASTRUCTURE PROVISION  
REMEDIES CONSULTATION MR 15/2.4**

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**RESPONSE TO CONSULTATION DATED DECEMBER 2016  
30 JANUARY 2017**

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## **Cover Submission**

HSBC is grateful for the opportunity to comment on the PSR's Remedies Consultation (the Consultation) in respect of the Market Review into the ownership and competitiveness of infrastructure provision.

You will be aware of HSBC's concerns highlighted in our response to the PSR's July 2016 Final Report (PSR MR15/2.3) into the ownership and competitiveness of infrastructure provision. These concerns have not changed but for the purposes of this response, we will concentrate on the package of potential remedies, leaving aside whether we agree with all the findings that have led to these remedies being proposed.

In broad terms we are supportive of the package of proposed remedies and are highly supportive of:

- The need for competition in the procurement of infrastructure, in order to promote innovation and meet the needs and expectations of end users, subject to our comments below;
- The PSR's preference for mandatory competitive procurement, option 3, noting the additional comments made in Section 1 below;
- The introduction of ISO20022, noting our additional comments below, and
- The decision to postpone any VocaLink divestment remedy, whilst the proposed MasterCard acquisition is being reviewed by the Competition and Markets Authority.

We do, however, have a number of significant ongoing concerns and comments about the approach to implementing these remedies which we have summarised below into the following three broad areas and addressed in more detail in the remaining sections of this response:

- Competitive procurement – we believe there is an alternative approach that would lead to enhanced competition.
- End user benefits – it is essential that we ensure that there are tangible benefits for end users from these remedies.
- Timing and sequencing – this section aims to provide some additional input and context to the complex implementation of the proposed remedies.

### **Competitive procurement**

As highlighted in HSBC's previous responses to various stages of the Market Review, HSBC remains convinced that the market should be moving to some form of direct contracting model, where PSPs are able to select the appropriate Payment System Operator-accredited infrastructure provider that meets their individual customers' needs. This would reduce the



need for and/or alter the nature of the mandatory competitive procurement exercise proposed by the PSR and open up the UK market to even greater competition and innovation.

Whilst we are encouraged that direct contracting is allowed for, assuming the Single Payments Platform is implemented, **HSBC would encourage the PSR to enable direct contracting as part of any mandated procurement exercise, in order that the market can achieve the competitive benefits which flow from this as early as possible** and move away from wholesale central procurement exercises in their current or proposed form.

### **End user benefits**

HSBC shares the PSR's view that it is essential that the proposed remedies realise significant benefits for end users, including HSBC's customers. The following comments are therefore made with this objective in mind.

The proposed consolidation of the three retail Payment System Operators (PSO), the conversion to ISO20022 messaging standards in BACS and Faster Payments, together with changes to VocaLink's ownership, will enable competitive procurement and support the achievement of the PSR's aims. However, it is less clear to us whether the package of remedies will really lead to benefits and service enhancements for end users.

Whilst the questions of cost/benefit raised in the Consultation are of course appropriate, we also believe that the question of risk needs to be addressed. Risk is a major factor which must be integrated into the overall cost and benefit equation. The proposed changes to critical national infrastructure must be achieved without dislocation to services at a time (the PSR envisages 2017-20) when the UK payments industry is already at full capacity implementing other major changes, most notably PSD2, Banking Reform, (i.e. ring-fencing) the introduction of cheque imaging, Open Banking, RTGS renewal and key elements of the Payments Strategy. Any infrastructure change carries the potential to disrupt the flow of payments on which our customers rely. We believe this should be carefully factored in to the timing and sequencing of the proposed changes – as further explained below.

### **Timing and sequencing**

The proposed timeline set out in the Consultation, together with the timetable linked to the Payments Strategy, create an ambitious landscape for the UK Payments Community. HSBC welcomes the challenge of moving forwards in the interests of our customers, but it is important that the final timetable that is set for the proposed changes takes into account existing in-flight change, the impact on end users and the risks highlighted in the previous section.

By way of example, we expect corporates in particular would wish to incorporate payment system change into their investment cycles and back office systems. Our past experience

would suggest that an absolute minimum of two years would be a likely timeframe for changes to core payment functionality and connectivity. Indeed some changes, such as the introduction of SEPA, have required an even longer period of adjustment.

This is especially important in connection with the ISO 20022 development. As we have referenced in HSBC's response to the Final Report, it is essential to recognise that there is far more to ISO 20022 implementation than just aligning payment standards. To gain the full benefits requires close co-operation with UK businesses to define re-usable business process ISO messages. If the industry fails to implement a migration to a new standard like ISO 20022 in the right way, then we will simply impose cost on corporates, without giving them much in the way of "Straight Through Processing" benefits. **In order not to miss an important opportunity, there needs to be room in the timetable for corporates to engage with the challenges and possibilities presented by the move to new messaging standards.**

HSBC does not accept the premise that the market cannot move to a direct contracting model in the near term. However if the PSR has decided that the only option is that proposed in the Consultation, then HSBC is highly supportive of the proposed competitive procurement exercises across the three in-scope PSOs. But the method, timing and sequencing of these activities is critical and HSBC is concerned that when it is not sufficiently clear today what the new payments architecture will entail, it will be very difficult for the PSOs to undertake an effective procurement process for that architecture. To put it differently, the PSOs have the capability to procure existing core and non-core services based on their existing platforms and architecture - but they do not have the ability to enter into a meaningful procurement exercise today for an unknown architecture. This places risk on the delivery of the competitive procurement remedy and highlights the need for very careful sequencing.

**It remains HSBC's view that any procurement processes should be run in parallel across all payment schemes, preferably after common message standards (ISO 20022), a simplified rule-book and governance structure have been agreed.** This will be the most effective way in which to attract the highest number of quality potential providers.

The future full-scale infrastructure procurement exercises can also only be undertaken once the issues around common technical standards have been fully resolved. If the PSOs are to procure services using the new payments architecture, then it will likewise be essential for the PSOs to have a very clear and immediate picture on how their core and overlay services can be supplied using the new Simplified Payments Platform.

It will be critical to secure engagement to the plan across the UK payments industry. The PSR has considered effectiveness and proportionality in the Consultation but **the fit with the PSR's other policies and wider industry developments need to be fully explored.** We would welcome the PSR's engagement to consider the end-to-end sequencing of these remedies,

the Strategy Forum's initiatives and other key regulatory and legislative requirements into a holistic, end-user focused and risk-based plan.

## **Section 1: Competitive Procurement Remedy**

### **1. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

- 1.1 The Assessment of Effectiveness section (paragraphs 3.52 – 3.59 of the MR 15/2.4 Consultation) deals largely with the question of overcoming VocaLink's perceived incumbency advantage, particularly through the removal of bespoke messaging standards and mandating competitive procurement on a 'not like-for-like' basis, in line with the Simplified Payments Platform / New Payments Architecture (SPP/NPA) proposed in outline by the Payments Strategy Forum. Whilst we agree that these (and related) measures would largely be successful in their effectiveness in delivering the PSR's requirements, in our view the package of remedies will need to be very carefully sequenced and managed, in order to avoid the disproportionate introduction of risk and cost, without a parallel significant benefit for end users. Our thoughts on this were summarised in the preceding cover submission and are developed further below.
- 1.2 We agree with the PSR on the need for consultation with service users, including PSPs and end users. This is key to reviewing and validating the PSF Strategy to ensure that it meets the needs of those users for the next ten years or so. In our view, user consultation should be undertaken as widely as possible, so as to engage and receive the support and endorsement of all sections of users. We encourage the PSR to include this activity as part of the milestones outlined in paragraph 3.96.
- 1.3 Successful end user consultation is equally important at the more detailed, individual PSO level, particularly when fundamental change is proposed to a system such as BACS (paragraphs 3.69 – 3.73). The BACS clearing cycle, add-on BACS services, as well as the BACS Standard 18 messaging format, are deeply embedded within many UK corporate back-office systems. Whilst the central conversion of Standard 18 to ISO 200022 messages envisaged by the PSR in its Messaging Standards remedy may alleviate one aspect of the changes imposed on corporates, we note that the PSR is silent on all other complementary BACS services which would likely be changed in the switch to a fundamentally different service with a new infrastructure provider or providers and which would have attendant implications and costs for corporate service users.
- 1.4 The Timing of the Remedy section of the Consultation outlines very ambitious timescales for the completion of strategy work, user engagement, PSO consolidation, and competitive procurement. In our view, this is an aggressively tight timeframe for procuring services on a like-for-like basis. The procurement and implementation of new services along the lines of the SPP by 2020 appears to us near impossible without introducing significant risk and the possibility of unacceptable system outages and

customer detriment. Since that is highly undesirable, we consider that the PSR should re-think this timeframe.

- 1.5 As mentioned in our Timing of the Remedy comments in paragraph 1.4, implementation of the PSF Strategy by competitive procurement of new services by a new provider seems remarkably ambitious, not without risk and not consistent with direct contracting. We therefore agree with the PSR's recognition in 3.95 that 'the new payments architecture might take longer than anticipated in the Forum's Strategy'.
- 1.6 We support the PSR's proposal that the new competitive contract or contracts should be awarded for ten years, to allow the successful provider to invest in the services and achieve a reasonable profit. Following our direct contracting theme, a positive alternative would be for the PSO to set the strategy, standards, assurance and requirements for the next ten years, to allow multiple potential providers to enter the market.
- 1.7 HSBC is in agreement with the PSR on the need as outlined in paragraph 3.83, for the PSR to align implementation of its procurement remedies with the work of the PSF Strategy. PSO consolidation should be helpful in positioning the industry to achieve the necessary strategic change envisaged by the PSF. We are concerned however by the catch all element in paragraph 3.86, whereby the PSR is proposing to take further steps to ensure the new consolidated entity competitively procures 'any future central infrastructure that is required, including any infrastructure to support the new payments architecture', to the extent that any central infrastructure is required in future. This seems very open-ended and we would welcome clarification on what the further steps would be.
- 1.8 Given our concerns with the timetable and the impact of change on users, we welcome in broad terms the PSR's Potential Exceptions to the Remedy section 3.90 – 3.115. However, given the considerable investment required to effect the "not-like-for-like" change proposed by the PSF Strategy's SPP, we consider that the exemption regime should have a clear and more transparent governance process, along with transparent, objective tests. This makes sense, given the alignment of the remedies with the PSF, which includes cross-industry representation and user consultation.
- 1.9 Whilst we welcome the possibility of an exemption, in addition to having concerns about its governance, we feel that the framework outlined in paragraphs 3.100 – 3.102 (no exemption for contracts over 5 years; the possibility of an exemption for 3-5 years; a more likely exemption for 0-2 years), is too arbitrary a rule to be set. We encourage the PSR to consider linking the award or refusal of an exemption to the individual facts of the individual case, with a strong focus on end users' needs and potential risks.
- 1.10 The Implementation Risks section of the Consultation (paragraphs 3.113 – 3.115) acknowledges that there are other developments taking place in the industry, notably

PSD2 and ring-fencing, but considers that this will not impede implementation of the remedy. Whilst it may be true that competitive procurement could proceed successfully, although we fear this is unlikely, the PSR must also consider the wider impact of change on service and end users, having to integrate new services from a new provider into their banking and back-office platforms.

**Do you agree with our assessment of the costs of the remedies? If not, please explain why.**

2.1 We believe that it is for the PSOs to provide comment on this aspect of the Consultation.

2.2 As we have pointed out above, we are not as concerned with the costs of competitive procurement as we are with the costs to users of integrating the new payment services and any adverse impact on HSBC's customers. Ultimately these costs are likely to be passed on to end users. In this connection, the full costs to all parties – providers and users – of a switch from BACS and Faster Payments to a new provider cannot be estimated until the PSF's Strategy implementation plan has been fully articulated, a process that will take most of 2017 to achieve.

**3. Do you have any comments on the design of our proposed remedy, including but not limited to:**

**a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?**

3.1 On the basis that the PSR is supporting procurement for new payment services envisaged by the PSF's SPP, rather than on a like-for-like basis, there should be no need for a discovery phase for BACS.

3.2 However in the event that procurement using some or all of the existing BACS services is required then, given the immature development of the NPA, a discovery phase could be helpful to potential new infrastructure providers, given the significance, evolution and nature of the underlying BACS services.

**b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?**

3.3 Alignment of the PSR's remedy with the work of the Forum is essential, if the remedy is to provide any benefits for end users. Given the importance of this issue, we have provided our thoughts on exemptions, milestones and processes above, when commenting on the broader themes of Effectiveness and Costs (please see paragraphs 1.1 - 1.10).

## **Section 2: Messaging Standards Remedy**

### **4 Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

- 4.1 We agree with the adoption of ISO 20022 as the strategic messaging standard for the UK's payment systems. Messaging standards are of such fundamental importance to payments however, that we would prefer implementation to reap the benefits (in terms of richer data with payments) of ISO 20022, rather than the additional costs of conversion to/from legacy formats in pursuit of the singular goal of enabling competitive procurement.
- 4.2 Whilst centralised conversion services could isolate end users from the impact of ISO20022 implementation, we feel this issue should be examined more closely, particularly from a technical perspective:
- Would conversion significantly reduce Faster Payments transactions per second so as to compromise service level agreements and end user expectations regarding the time taken to receive payment confirmation?
  - There may be additional problems regarding batch conversion of BACS messages – would the failed conversion of a few payments in a BACS file lead to delays/rejection of the whole file? How would repair/recovery be effected?
  - The use of conversion services adds another layer in the processing and messaging flow that could potentially be compromised. There must be absolute clarity in terms of how data is converted, appropriate audit trails and robust security in place to prevent the payment messages being corrupted.
- 4.3 We agree that the exemption process set out by the PSR for the competitive procurement remedy should be equally applicable to the messaging standards remedy, and in particular should have regard to the needs of industry and users as set out in the PSF's Strategic plan. The caveats and concerns regarding exemptions set out above in our comments on competitive procurement exemption are also applicable here.
- 4.4 Finally, we agree that a messaging standards remedy for LINK is not required.

### **5 Do you agree with our assessment of the costs of the remedies? If not, please explain why.**

- 5.1 The costs of implementing the Messaging Standards remedy which the PSR has taken into account, as outlined in paragraphs 4.61 and 4.26 of the Consultation, seem to be just limited to the costs of the mapping exercise. The PSR seems to be taking the position that ISO 20022 central conversion is not a cost for the industry as it would be paid for by the central infrastructure provider. Whilst true in a limited sense, the linkage of the remedies to the PSF's Strategy, and the clear expectation from the PSR that competitive procurement will not be undertaken on a like-for-like basis, means that

providers and users will incur considerable additional costs to implement the SPP. Our key concern, as outlined a number of times above, is that in undertaking such a fundamental revision to the UK's payments infrastructure, we should take the opportunity to plan and consult properly, and reap the benefits of the new system, such as ISO 20022 richer data.

- 5.2 The introduction of the mapping exercises will involve a significant testing requirement, which will further drive HSBC's internal IT and external vendor costs. Any change to the UK national critical economic functions would have to be tested thoroughly on an end to end basis. This is not just a cost for HSBC, but for the industry as a whole. Significant investment would be required to ensure integrity of the payments infrastructure.

**6. Do you have any comments on the design of our proposed remedy, including, but not limited to:**

**a. Whether the use of XML standard should be required to make our remedy effective?**

- 6.1 The use of the common messaging standard ISO20022 is more important than a specific syntax. The use of XML, in and of itself, is not necessarily required to make the remedy effective, although we agree that this is the most common form of syntax associated with ISO20022.

**b. Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?**

- 6.2 We agree that once BACS and Faster Payments have moved to ISO20022, there is little likelihood of reversion to legacy formats. The remedy could therefore be limited to initial implementation only.

**c. Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?**

- 6.3 Unless there are security reasons for not disclosing the mapping information, we do not see why BACS and Faster Payments should not disclose mapping information publicly.



### **Section 3: Ownership of VocaLink**

- 7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:**
- a. the financial incentive to protect VocaLink**
  - b. alternative providers belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements.**

**If not, please explain why.**

- 7.1** As outlined above in our Cover Submission section, we are concerned that many of the issues raised in our response to the PSR's Final Report (MR 15/2.3) have not been addressed. Bullet point 3 from our response makes the following important point:

"Further, the two sections [framework for assessing control; protecting VocaLink from competition] do not build on anything that was contained in the interim report; we have not had any previous opportunity to comment on them. Given that the PSR appears to be (although it is difficult to discern) advancing findings that the largest four shareholders (or their appointed representatives on the payment schemes) may have sought to protect VocaLink from competition, and/or have the incentive and ability to do so, HSBC (as one of those shareholders) should have been given the opportunity to comment on what the PSR proposed to say, and should have had full access to the evidence which the PSR has sought to rely on."

- 7.2** The detailed points we made in HSBC's response to the Final Report (at paragraphs 4 – 42), questioned the PSR's approach, its arguments and its findings. We maintain our position on those points, which the Consultation does not appear to address.

- 7.3** That said, we are encouraged by the PSR's view that there is no present need for the PSR to pursue a remedy in respect of its perceived VocaLink concerns, in view of the MasterCard bid. This appears to be a pragmatic way forward at this time given the ongoing CMA merger control review and an approach that we very much support.

## **Section 4: Remedies Package**

### **8. Do you agree with our assessment of the effectiveness of the proposed remedies package? If not, please explain why.**

#### **8.1 We agree that the complete package of measures i.e. :**

- mandatory periodic competitive procurement,
- mandatory implementation of ISO 20022 messaging standards through central conversion of legacy formats by the new payments infrastructure provider,
- consolidation of PSOs (a PSF solution but integral to the PSR remedies), and
- the perceived 'ownership problem' of VocaLink

will introduce additional competition into infrastructure provision. Our concerns, already highlighted in the preceding sections above, but summarised again below, are based on our view that the costs and risks of the exercise (when considered in the broadest sense, including SPP implementation), may far exceed the potential benefits.

### **9. Do you agree with our proportionality assessment of the proposed remedies package? If not, please explain why.**

#### **9.1 The Benefits of the Package set out in paragraph 6.24 of the Consultation consists of an attempt by the PSR to quantify the negative effects of perceived lack of competition in the provision of infrastructure services.**

- The first bullet links competition in infrastructure with innovation in services based on that infrastructure. We would contend that the stability and integrity of the services provided by the incumbent, coupled with the longevity of the period over which (certainly BACS) services have been provided, provide a base from which the PSOs, PSPs and third party service providers and aggregators can provide additional, innovative services. The Current Account Switching Service, the Cash ISA service, PAYM, PayPal's use of BACS, and ZAPP are all based to some degree on the core services procured by BACS and Faster Payments from VocaLink. A new provider may well provide further or different innovation, but it is remarkably difficult to estimate and quantify the additional benefit to be accrued from the PSR's package of measures. In other words, the incremental benefits analysis is highly speculative.
- The second bullet cites an estimated figure, extrapolated from LINK's RFI 'experience'. The figure is highly questionable, as is the assertion that the PSR's estimate is probably understated.
- The third and fourth bullets – relating to competitive pressure and quality of service - are unquantified and we are unsure what underlying evidence exists to support these statements.

#### **9.2 Given the impact on providers and end users, not least the threat to the stability and integrity of the UK's payment systems, HSBC believes that risks and costs ought to be more fully understood and factored in to the proposals to achieve the desired aims of proportionality and securing end user benefits.**

9.3 Direct PSPs' costs are largely unknown and will remain so, until we enter the detailed business design and requirements phase. ....If we consider these projects as a potential benchmark for future direct PSPs' costs, then the costs will certainly be significant and indeed considerably higher than for previous programmes, given the scale of the proposed change.

9.5 Without more fully understanding the end-to-end cost and risk landscape, it is very difficult to see how the PSR can confidently support its apparent view that the benefits will exceed the costs, once risk and all other costs have been fully taken into account.

**10. Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims**

10.1 Provided the remedies package is appropriately and carefully introduced, taking account of the points we make in the Timing and Sequencing section of the Cover Submission, then we would be hopeful that there would be no direct loss of benefits to users.

10.2 We can foresee that the potential increased investment and payments costs associated with these remedies could be passed on to the end users downstream, making the underlying cost of payments more expensive. This may be appropriate provided of course the potential benefits are delivered in tandem as outlined in the End User benefits section in the Cover Submission. Please also see our comments in paragraph 2.2 above.

10.3 It is also important to consider the potential risks of the package, as outlined in the End User benefits section of the Cover Submission.

10.4 Finally, and accepting the premise that competitive central procurement is the best way to introduce competition into this market, the opportunity costs, brought about by the focus on competitive procurement, may forestall service improvements that would otherwise have been made.

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31 January 2017

Reference: PSR MR 15/2.4

## **IdenTrust Response**

### **PSR MR15/2.4 MARKET REVIEW INTO THE OWNERSHIP AND COMPETITIVENESS OF INFRASTRUCTURE PROVISION – REMEDIES CONSULTATION**

IdenTrust welcomes the opportunity to comment on the remedies that the Payment Systems Regulator has proposed in this consultation.

One of the critical aspects that we believe that needs to be given much greater weight and consideration is the operational risk being contemplated to the UK payment systems and the supporting systematically important Financial Market Infrastructures.

The PSR statutory objectives do not address risk, stability, reliability:

- a) to ensure that payment systems are operated and developed in a way that considers and promotes the interests of all the businesses and consumers that use them
- b) to promote effective competition in the markets for payment systems and services - between operators, PSPs and infrastructure providers
- c) to promote the development of and innovation in payment systems, in particular the infrastructure used to operate those systems

Given the rapid and daily change to the world order, is the 'generational' step towards wholesale change of the payments infrastructure the right thing to do at this point in time? "Steady as she goes" comes to mind keeping the ship heading steadily on the same course regardless of gusts of wind or cross-currents.

The velocity of change is unprecedented, with the PSR/PSF being only one element.

We do not agree with the statements that there is no requirement for the infrastructure data centres to be located in the UK. Both for reasons of national interest and for network traffic effectiveness, then we believe this is a requirement for a competitive procurement.

## Competitive procurement remedy

1. Do you agree with our assessment of effectiveness of the potential remedies identified?

If not, please explain why.

We agree with mandating competitive procurement exercises for Bacs, FPS and LINK when the operators of these systems purchase central infrastructure services for any new services that emerge from New Payments Architecture Design. We do not believe there that there has been an intentional closed contracting arrangement, but the integrated-by-design nature of the existing central infrastructures involved means that attracting other parties to compete has not been successful.

However, we believe that the Consolidated PSO entity should be allowed to extend the existing VocaLink contracts without a PSR exception being raised on the assumption that the New Payments Architecture will be delayed. This is not being negative, merely practical, as we would expect that VocaLink would also have the right to terminate. If they did exercise that, ahead of alternative provider/s being in place would be the worst of all worlds.

2. Do you agree with our assessment of the costs of the remedies? If not, please explain why.

No, we do not agree. The categories of costs are limited to the costs of running a competitive procurement. The scale of those estimates may or not be correct. No one will really know, until the requirements for what is being procured is determined. This in itself is a problem, as the timescales for the design of the new payments architecture under the PSF are extremely challenging. Whilst the New Payments Architecture Design Hub - Terms of Reference state that by July 2017, the Hub will design and document its draft NPA “blueprint” for public consultation – rather than a public consultation, it should really be an engaged impact assessment by all the actors who play a part in the extensive payments ecosystem within the UK. It is only at that point, will the scale of the changes become clear and can be costed – for providers and for end users alike. The BACS Solution Service Providers, as one special interest group, will already have product roadmaps for this period of time, and getting this level of change – of whatever it may be (as it is unknown) – in to scope cannot be assumed. IdenTrust and Gemalto are also critical providers that need to be engaged – currently providing many of the Public Key Infrastructure and digital signing components.

3. Do you have any comments on the design of our proposed remedy, including but not limited to:
  - a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?

- b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?

Clearly there have been many reports and assessments commissioned by the PSR, and the output runs to many hundreds of pages. However, at a practical level, until a security harness description and interface specifications can be provided to external parties for review/or for collaboration, will an impact assessment be able to be completed.

As to whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective, then this only becomes relevant if other parties are expected to bid on an “as-is” basis, but as indicated previously, we do not believe this makes any economic sense. The “as-is” should remain with VocaLink and the Consolidated PSO Entity free to make commercial decisions based on the need for the “as-is” platform without an exception – temporary or otherwise.

With regard to the PSR proposals for the interaction with the Forum, then we believe that the PSR/PSF – whilst hugely important – are not the only the drivers here. At a practical level, the Payment Community will need to participate in PSF II, and to be responsive to those outcomes, but not in isolation. Other legislations, other regulations, other governance, other security, other liability, other standards, other communications, other legal, other technologies are all on the agenda and all need to be addressed. The velocity of change is unprecedented, with the PSR/PSF being only one element.

A general observation is that the timescales are unrealistic, and the milestones must be at risk. PSF II is in start-up - *Members We will shortly be reaching out to the Payments Community to seek individuals with the required skills, expertise and capacity to support this work* and the milestones can only be seen as aspirational at this point.

### **Messaging standards remedy**

4. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

We believe that the reference to ISO 20022 mapping only considers a mapping between legacy standards and ISO 20022. However, greater consideration should be given to the agreement among the parties of the ISO 20022 definition itself ahead of mapping the legacy standards.

5. Do you agree with our assessment of the costs of the remedies? If not, please explain why.

As before, until the level of detail for the interface specifications, and the syntax of the ISO 20022 elements agreed, then the costs can only remain as a best guess, because all the

actors in the eco system will need the opportunity to assess the impact and costs for their application and services, for both initiation and receipt of output. Further costs will be incurred by end users. But will they see a benefit? A payment instruction is a payment instruction, and as long as the transfer of value takes place, we do not believe they would know or care about the format used.

6. Do you have any comments on the design of our proposed remedy, including, but not limited to:
- Whether the use of XML standard should be required to make our remedy effective?
  - Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?
  - Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?

We believe that a move to a standard that supports the ability to carry transactional data – if customer consent has been provided – supports the wider industry goals for CMA9, PSD 2 and so on. Yet this could be in conflict with provisions of GDPR. However, the only reason it would fall within a remedy would be if the industry was not meeting the need to provide transactional data. If the thoughts are that the central infrastructure role is purely to process the payment settlement, then the transactional data should be an overlay service. In which case, it is not completely clear why introducing the ISO 20022 messaging standard in future procurements for Bacs and FPS would be part of the remedy.

### **Ownership of VocaLink**

7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:
- the financial incentive to protect VocaLink
  - alternative providers belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements

If not, please explain why.

We do not believe that the PSR have demonstrated that the four largest PSPs have an interest in protecting VocaLink from competition. Given the MasterCard acquisition of 92.4% of VocaLink, we believe the question should be asked the other way around, that is, what % holding should the UK PSPs have of the infrastructure provider to retain sufficient stakeholder representation and protection of services in a 10 year contract.

**Remedies package**

8. Do you agree with our assessment of the effectiveness of the proposed remedies package?

If not, please explain why?

No, we do not agree. It all seems too premature and over prescriptive. The commercial entities have to be given the opportunity to determine the way forward. The existing PSPs have a strong track record of collaboration for the definition of solutions. With the wider work of the PSF and the establishment of the Payment Community, we believe that the opportunity for new entrants engage and to collaborate is addressed. With regard to costs, much is made that the parties would need to update anyway – but that has little to do with a regulator surely?

9. Do you agree with our proportionality assessment of the proposed remedies package?

If not, please explain why?

We do not believe that enough consideration has been given to the existing software solutions and payment products and the costs that they will incur. We believe that the “least-costly effective option” is still costly. We believe the funding of the new Consolidated PSO Entity, the funding of the competitive procurement and the payment of the New Payment Architecture has not been addressed. One reference point could be the ICAO PKD <http://www.icao.int/Security/FAL/PKD/Pages/How-to-Participate.aspx>

10. Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.

We do not believe that the consultation has demonstrated customer detriment or described the benefits of stability, security and resilience provided by the eco-system today. There is customer choice in the system today – customers are free to choose software from alternative suppliers, free to choose PSPs, free to choose bureaux. Interoperability is provided for within the payment infrastructures today, underpinned by a Public Key Infrastructure using digital signatures. Digital signatures meet the knowledge and possession requirements; proves and establishes identity; delivers non-repudiation; combats frauds; provides audit and compliance tracking; guarantees privacy; ensures data integrity; eliminates man-in-the-middle attacks; provides legally binding user-level signatures and can be used in multiple applications. The signatures can be validated in real time by the relying party. With the number of parties involved at any one time, the relying party will change through the transaction flow and identification, and authentication, between account servicing payment service providers, payment initiation service



providers, account information service providers, payers, payees and other payment service providers then real time validation at the point of reliance is critical. The inter-party liability provisions do not seem to have been addressed. An end-to-end secure payment system underpinned by using digital signatures with a risk management and liability framework could help provide this.

## About IdenTrust

IdenTrust enables organizations to: a) effectively manage the risks associated with identity authentication; b) work interoperably with countries around the world; and c) minimize investment in creating their own policies and legal frameworks. As a bank-developed identity authentication system, IdenTrust provides a unique legally and technologically interoperable environment for authenticating and using identities worldwide. To support this, IdenTrust has developed a Public Key Infrastructure (PKI) identity scheme, called the IdenTrust Trust Network, and a hosting and delivery framework, called the IdenTrust Trust Infrastructure to deliver a framework that combines policies, legal framework, trusted operations and technology (P.L.O.T.) to create a comprehensive environment for issuing trusted identities. IdenTrust is the only company to provide a solution incorporating all four of these elements. IdenTrust solutions help organizations define and implement their identity strategies by providing a spectrum of products that ensure trust in the most efficient, intelligent, and cost effective manner available today.

**LLOYDS  
BANKING  
GROUP**



**LLOYDS BANKING GROUP PLC**  
**Payment Systems Regulator**  
**Infrastructure Market Review:**  
**Response to Remedies Consultation**

## LLOYDS BANKING GROUP PLC

### Response to Payment Systems Regulator Infrastructure Market Review: Remedies Consultation

#### EXECUTIVE SUMMARY

1. With the PSR's support, the UK payments industry has recently developed its future payments strategy. The strategy will deliver generational change in payments. It will resolve the PSR's concerns relating to competition in payments infrastructure by building competition into the system design from the outset. It will also deliver more fundamental and wide-ranging improvements to payments for the benefit of consumers, businesses and Government, while enabling increased downstream competition between payment service providers (**PSPs**). Given the central importance of payment systems to customers and the economy their resilience, security and integrity are paramount. Lloyds Banking Group (**LBG**) has been a core supporter of the work of the Payment Strategy Forum from the outset, and will remain so.
2. The potential costs and benefits of the PSR's remedies are driven in large part by whether, and when, the new simplified payments platform (**SPP**) proposed in the strategy will be implemented and the existing infrastructure "switched off".
3. In that context, we have assessed the proposals against three scenarios:
  - **Fast SPP Migration:** SPP is built and migration completed from existing schemes by c. 2020.
  - **Base Case:** SPP proceeds within or close to projected timelines, and existing schemes operate for up to 4 more years to allow for a phased migration (i.e. until c. 2024). LBG believes this to be the most likely scenario.
  - **Slow/ No SPP Migration:** SPP does not proceed, or existing schemes continue to operate for a longer transition period in full or in part.
4. As the PSR recognises in its consultation document, in the Fast SPP Migration scenario, the PSR's competition concerns would be resolved without the need for remedies, since the implementation of SPP will include a competitive procurement on ISO20022.
5. LBG believes that in the Slow/ No SPP Migration scenario, a full competitive procurement on ISO20022 may be cost-effective. We estimate that an 8-10 year infrastructure contract would be likely to justify this approach, because it would enable full end-to-end adoption of ISO20022, while a 4-8 year contract would require a case by case analysis.
6. However, LBG considers that unless the remedy package is amended, it is likely to be ineffective and disproportionate under the Base Case scenario, which we consider to be the most likely scenario, because:
  - The payment scheme operators (**PSOs**) will not be able to run an effective competitive procurement until they know whether and when the SPP will be

implemented. **The remedy requires the operators to start the procurement process too early.**

- A competitive procurement is unlikely to be cost effective unless the contract length is at least 4 years (noting that this scenario implies that a competitive procurement has taken or will take place for the SPP that will replace Bacs and FPS). **The remedy should not apply to contract extensions of less than 4 years.**
  - Requiring Bacs/ FPS infrastructure to operate on ISO20022 appears unnecessary to achieve the PSR's objectives. **There are lower cost and risk alternatives that could meet those objectives.**
  - The cost-benefit analysis of competitive procurement and of requiring the use of ISO20022 for Bacs/ FPS is not robust and does not include significant cost drivers. **The evidence base does not support the remedy package as proposed.**
7. We recognise that the PSR has proposed a derogations system which is intended to address some of these concerns. However, we do not believe that introducing remedies in the expectation that derogations will be required under the most likely future scenario is proportionate or necessary. We have identified alternative options which we believe would provide better solutions to these concerns. These include:
- In relation to competitive procurement:
    - i. Allowing the PSOs to launch the formal stage of any competitive procurement when they know whether and when the SPP will be implemented, and the Bank of England has completed its plans for a new Real Time Gross Settlement system (**RTGS**) – likely to be in early 2018. This may require a very short (c. 6 month) extension to Bacs' and FPS' existing contracts with VocaLink to allow time for the procurement and any necessary transition to be completed;
    - ii. Using the PSR's procedural flexibility to implement any remedies, if required, at a later stage when the path to SPP is clearer and the remedies can be more precisely scoped; and/or
    - iii. Making clear that there is no obligation to use a full competitive procurement for any contract of less than 4 years.
  - In relation to ISO20022: testing the real costs and benefits of procuring on ISO20022 by allowing the operators, in addition to inviting tenders for infrastructure on ISO20022, to invite tenders on the existing standards and then reach a commercial decision on which offer provides the best overall value for customers.
8. In relation to the ownership of VocaLink, as set out in our response to the Final Report, we support the PSR's view that the proposed sale of VocaLink to MasterCard would address the PSR's concerns. We note that in light of the transaction, the PSR is not proposing or consulting on any remedy in relation to ownership. Should the transaction not proceed, we would expect that the PSR will consult on any potential remedy and will respond at that time. In that respect, we were disappointed that the PSR's press release and other public comments suggest that the PSR's mind may already be closed on whether a divestment would be implemented and urge

the PSR to fully engage with affected parties at the relevant time – we provide initial comments below.

9. We would be happy to discuss our alternative proposals, or any other aspect of this response, in more detail with the PSR.

## **COMPETITIVE TENDERING**

10. LBG understands that the PSR considers there to be a range of credible competitors for future Bacs, FPS and LINK infrastructure contracts. On that basis, LBG agrees that competitive tendering could be appropriate for future contracts, provided that the benefits of doing so outweigh the costs.
11. The key questions for any such procurement are:
  - How to ensure the most effective tender, which delivers the best combination of price, service and resilience to customers?
  - In what circumstances are the benefits of a competitive tender process likely to outweigh the costs?

## **Ensuring the most effective tender**

12. LBG agrees with the PSR's view that designing an effective tender requires that PSOs develop a clear understanding of user needs and a procurement strategy. However, we do not believe that the PSR has given sufficient consideration to the "supply side" – how to ensure that the tender is attractive to potential providers in order to drive competition. Key issues for providers will include:
  - certainty that the contract will be awarded (to reduce the risk of wasted bid costs);
  - contract length and break periods;
  - clarity on the technical requirements; and
  - committed volumes/ revenue.
13. At this stage, the biggest uncertainty for any future contract is whether and when SPP will be implemented. This impacts all of the above criteria, for example:
  - Will the PSOs proceed with awarding new contracts or will they migrate directly to SPP when the existing contracts with VocaLink terminate?
  - If the existing schemes continue, when will transition complete and the existing schemes "switch off"? What notice would they give a new provider?
  - What will the technical requirements be, e.g. a like-for-like extension of the existing service (although we believe the PSR does not expect this to be the case), or a full end-to-end implementation of ISO20022? Given the importance of interoperability across UK payment systems, how will the schemes interact with the Bank of England's new RTGS system? What support will be required for any transition to SPP? How will the infrastructure provider be required to support interoperability with SPP during the transition phase?

- Will the operators provide minimum volume commitments and what are the expected timelines for migration of volume if there is a period of parallel running with SPP?
14. Until there is greater clarity on these issues, any tender is unlikely to be effective because providers will either be disincentivised from competing or will have to build in significant risk factors to their bid. In a worst case, a winning bidder may have to pull out if the requirements change substantially. The practical implication is that the PSOs should not launch the formal stage of a tender until they know the implementation plan for SPP. They may also have to factor in additional time for consultation with regulators, Government and other stakeholders on proposed “switch off” dates for the existing schemes.
15. If the PSF reports at the end of 2017, this means a formal tender – if required - could launch in early 2018. This does not preclude operators from making preparations for a tender, such as engaging with customers and the PSF to understand users’ needs. But it does suggest that the PSR’s projected timelines for seeking derogations will not be workable. LBG believes the following would be more appropriate:
- Bacs: launch formal tender H1 2018; award the contract in H2 2018 and, if necessary, trigger the notice period under the existing VocaLink contract. This means that Bacs would not trigger notice at the first available period, but would instead roll for approximately 6 additional months under its “evergreen” contract.
  - FPS: launch formal tender H1 2018; award the contract in H2 2018. If migrating to a new supplier, FPS would need to review with its members whether a c. 18 month migration period would be sufficient, or if it would be necessary to negotiate a short contract extension (of c. 6 months) with VocaLink.
  - LINK: launch formal tender H2 2018, award by April 2019, allowing triggering of 24 month notice period if necessary.
16. LBG recognises that, in a scenario where a full competitive procurement occurs, these timelines may delay the benefit of such procurement by approximately 6 months. However, we believe that the costs and risks of rushing in to a poorly specified tender would very significantly outweigh the potential benefits of terminating existing contracts at the earliest opportunity (and would encourage the PSR to consider the marginal cost versus the marginal benefit of introducing the remedy now rather than waiting until SPP plans are clearer). In addition, our proposed timelines would reduce the risk of wasted cost if the SPP implementation timing would not justify a full competitive procurement – the scenario we consider to be most likely.

#### **In what circumstances are benefits likely to outweigh costs?**

17. Given the importance of the cost benefit analysis in considering the proportionality of the remedies package and the PSR’s obligations in this regard, we would urge the PSR to find a way to make more of this information available to the industry. Without this, LBG notes that heavy redactions make it difficult to comment on the PSR’s cost-benefit analysis. However, we understand that the analysis finds that a longer term contract of 8-10 years is likely to justify a competitive procurement; we share that view.

18. It is not clear that the PSR has conducted any cost-benefit analysis of applying the remedy to a contract of less than 5 years.<sup>1</sup> As a starting point, LBG does not consider that it can be appropriate to apply the remedy to a shorter term contract without having conducted a cost-benefit analysis of doing so. Moreover, LBG notes that third party evidence provided to the PSR suggests that a contract would have to have a minimum term of 5 years to make it attractive to potential bidders (and this does not address potential volume risk if the existing schemes were migrating to SPP during the contract term).
19. Accordingly, the PSR should not impose a remedy which may not satisfy a cost-benefit analysis, and then require operators to seek exemptions from that remedy. This could lead to costs being incurred unnecessarily in preparing for a tender which does not proceed, and/or in going through an exemptions process, when it is clear that such a short term contract would not justify a competitive tender. This would also be an unnecessary diversion of resources from implementing the PSF's strategy. LBG believes that it is unlikely that a contract length of less than 4 years could justify a competitive procurement and that the PSR should make this clear now, rather than requiring a case by case analysis at a later stage.
20. LBG believes a case by case analysis would be required for a contract of between 4 to 8 years. We note that the PSR's cost-benefit analysis suggests a positive net present value to competitively procuring a contract with duration of at least 5 years. However, we do not consider that this provides a sufficient basis for mandating competitive procurement for such contracts at this stage, because it understates likely costs, and is heavily dependent on assumptions which should be tested with further evidence. We provide more detailed comments on the cost-benefit analysis below.
21. LBG has therefore considered alternative options that would address the PSR's concerns while avoiding disproportionate costs to users – see paragraphs [6] and [15] above.

## MESSAGING STANDARDS

22. LBG understands that the PSR's objective for this remedy is to increase competition in future infrastructure tenders for FPS and Bacs by requiring that they procure central infrastructure that operates on ISO20022. The PSR believes this would be effective because more suppliers would be interested in the tenders given their existing ISO20022 operations, which would mitigate VocaLink's incumbency advantage.
23. However, the PSR does not intend to mandate end-to-end adoption of ISO20022 to drive the potential end-user benefits associated with adoption of this standard. Accordingly, the remedy would involve the use of translation services, allowing users to continue operating with legacy messaging standards. The PSR considers that this approach would be straightforward and would not involve any cost to end-users.<sup>2</sup>
24. LBG notes that the cost-benefit analysis and proportionality assessment of this remedy contains significant uncertainties, including the extent of competitive benefit derived from procuring on ISO20022, and the potential costs and risk of

<sup>1</sup> We note that in Table 1, paragraph 6.50 of the consultation, the PSR calculates the costs and benefits in three scenarios - a "short term", "medium term" and "long term" contract. Reading this in combination with paragraph 6.43, we understand that the "short term" scenario equates to a 5 year contract.

<sup>2</sup> Paragraph 4.64, Market review into the ownership and competitiveness of infrastructure provision. Remedies consultation.

doing so. In particular, the benefit case is based on an extrapolation from the last LINK renegotiation – it is highly uncertain whether this is an appropriate benchmark for FPS/ Bacs and whether the assumed savings of between [9-23%] and [13-29%] would be achievable. In addition, the cost-benefit analysis does not take account of potentially significant costs and risks associated with this proposal. We provide further detail below.

25. LBG does not believe that it is necessary to take the risk of implementing a potentially disproportionate messaging standards remedy based on these assumptions. The PSR can test the real costs and benefits of its proposals in practice by mandating that PSOs invite bids on ISO20022 but allowing them also to invite alternative bids on legacy messaging standards should they wish. The tender process will provide robust evidence of potential benefits from competition, and help to explore potential costs and technical risks.
26. Once informed with evidence from the tender, PSOs can form a robust cost-benefit analysis on whether to switch to an ISO20022 solution or remain with legacy standards.
27. We note that, according to the PSR's evidence, this approach should not preclude ISO20022 infrastructure operators from submitting bids using legacy standards, if the PSR is correct that central infrastructure providers can "translate between existing standards and ISO20022 and that this would not put them at a competitive disadvantage. It is our understanding that – considering the total volume of Bacs and FPS – the average cost that they would incur to provide centralised conversion services would not be significant."<sup>3</sup> FPS and Bacs are already undertaking work to support this approach, having recently published their mapping from legacy standards to ISO20022.
28. For completeness, if the PSR intends to resolve its concern by simply adding cost to VocaLink as the incumbent provider, LBG does not believe that would be an appropriate or economically sound way to deliver benefits for end-users.

LBG would also propose that the PSR review whether its proposals are compatible with Article 58 of the Payment Services Directive 2, in particular to the extent that they assume that richer data transmitted on ISO20022 messages can be truncated or withheld on translation into legacy messaging formats.<sup>4</sup>

## PROPORTIONALITY

29. LBG does not consider that the proportionality assessment is robust. It relies on some very significant and questionable assumptions, and does not include all relevant costs.

## Assumed benefits

<sup>3</sup> Paragraph 4.28, Market review into the ownership and competitiveness of infrastructure provision. Remedies consultation.

<sup>4</sup> Article 58 provides that *"after the execution of an individual payment transaction, the payee's payment service provider shall provide the payee without undue delay in the same way as laid down in Article 51(1) with all of the following information: (a) a reference enabling the payee to identify the payment transaction and the payer, and any information transferred with the payment transaction..."*



30. LBG notes that the benefits case is based on an assumption that the savings produced in the last LINK contract renegotiation would apply to future infrastructure tenders. LBG considers that this analysis is questionable for the following reasons:

- There are important differences between the schemes which mean that they may not be comparable with LINK. For example, Bacs has richer functionality, and volumes passing through the schemes are significantly different.
- It appears to assume that LINK will generate further equivalent savings in a future tender, despite having already achieved the benefits of competition in its last contract renegotiation. This appears to amount to “double counting” these benefits.
- It assumes that all of the price reduction in the LINK retender was driven by competition. LBG does not believe that there is any reason to make this assumption given the other factors that could have driven a price reduction, such as VocaLink’s existing investments, reductions in technology costs over time, or other changes in the commercial structure or term of the contract. (In its Final Report, the PSR recognises the “special circumstances in which the LINK contract negotiations were held”).<sup>5</sup>
- The LINK renegotiation commenced in 2015; and can terminate in 2021. A shorter term contract would be expected to generate lower savings because providers would have less time to recover any investments (conversely, savings may be higher for a longer term contract).
- It assumes that volumes will be constant over the life of the contract. This is very unlikely if SPP proceeds; it is more likely that volumes will migrate over time to SPP.
- For Bacs and FPS, the benefits are benchmarked against average 2011-2015 revenues. This does not adequately reflect the contract renegotiations that were completed in 2014 which have provided Bacs, FPS and LINK with a **[redacted]** In addition, the analysis does not appear to net off VocaLink’s committed investment budgets during the contract terms.
- In relation to the assumed benefits associated with the use of translation services, whilst a like for like conversion should be relatively technically simple, there is more complexity in the scheme rules, business rules, messaging protocol, payment state management and orchestration. It is not certain that introducing an ISO20022 veneer on top of existing payment schemes, with the many years of business rules built into them, will result in greater competition.

### **Assumed costs**

31. The analysis does not adequately reflect the following costs:

- Tender costs for participant PSPs: LBG notes that members will incur their own costs, in addition to PSOs’ costs, in supporting any tender and considering the merits of alternative providers. For example, these might include costs to examine the technical impacts to members’ internal systems and connectivity to switch to an alternative provider. In addition, in LBG’s opinion the estimated

<sup>5</sup> Paragraph 4.65. Market review into the ownership and competitiveness of infrastructure provision. Remedies consultation.

costs for the PSOs to run a competitive procurement exercise as outlined in section 3.127 and 3.128 of the remedies consultation are potentially understated.

- Testing: in addition to the costs of testing connections to a new provider in the event of a switch, there would be material costs associated with testing infrastructure based on ISO20022, whether operated by VocaLink or another party. Even if PSPs continued to operate on legacy standards, they would be required to test the effectiveness of message translation tools. This would be an incremental cost of the messaging standards remedy.
  - Translation: the PSR assumes that the remedy would not impose any additional costs to users, because translation tools could be used. However, this does not reflect the costs of translation services, which would be borne by any successful bidder. Even if seen as a “cost of doing business”, in a competitive market such costs are passed on to end-users.
  - In addition, the PSR does not appear to have undertaken any detailed analysis of the potential technical effects or risks of using translation services, such as any impact on processing time, or any resilience risk associated with introducing additional processes and parties into the payments architecture. (The PSR notes, in paragraph 4.42 of the consultation, that some parties had mentioned “drawbacks” associated with conversion services, but do not appear to have given this detailed consideration in its cost-benefit analysis.)
  - The PSR does not attempt to quantify member switching costs. However, it suggests that switching costs are likely to be lower than £75 million, which would equate to a cost of more than £1 million per PSP.<sup>6</sup> In LBG’s view, if all of the schemes were to switch provider and to a new messaging standard, **[redacted]** In LBG’s view, it would be appropriate for PSOs to take all switching costs into account, because these are ultimately passed on to end-users. It is, therefore, very plausible that switching costs could exceed £75 million in some scenarios (LBG also notes that the net present value for a number of the PSR’s cost-benefit analysis scenarios is significantly lower than £75 million, which would imply costs that exceed benefits under the PSR’s analysis).
  - If MasterCard’s acquisition of VocaLink did not proceed and the PSR were to mandate a divestment, the lost benefits of the current ownership structure and the costs of the divestment remedy would also need to be included in the cost-benefit analysis for the overall package.
32. These concerns mean that there is a significant risk that the PSR could introduce disproportionate remedies, which could lead to higher costs for customers and distract from the wider work currently underway to improve payments in the UK. The cost-benefit analysis cannot support the remedies package as proposed; LBG therefore proposes that the PSR consider the alternative options set out in paragraphs [25-28] above in order to make any remedies more effective and less costly.

## Service User Implications

<sup>6</sup> Paragraph 6.56, Market review into the ownership and competitiveness of infrastructure provision. Remedies consultation.

33. LBG notes that the PSR's primary aim is to improve the outcomes for the end user of the payment systems which is consistent with LBG's primary focus on putting customers and clients first. We believe that the long term indirect benefits for customers from the introduction of SPP will be a lower cost of services and greater flexibility through common industry standards.
34. Any regulatory or technical developments that require a mandatory change for service users will have a disruptive and costly impact on them to adapt their systems and interfaces for each payment system. Therefore, wherever possible, we support an approach that minimises impacts to end user interfaces and/or avoids repeated changes to such interfaces.
35. An early migration to SPP provides one approach to minimising service user costs as it involves the least change and will deliver the long term benefits earlier. We would not support introducing changes to the Bacs or FPS services, pending the introduction of SPP, if they would increase the cost or disruption for service users.

## **OWNERSHIP OF VOCALINK**

36. As explained in more detail in LBG's response to the Final Report, while we do not agree with the PSR's concerns in relation to the current ownership of VocaLink, we agree that the proposed acquisition by MasterCard would address such concerns.
37. We note that in light of the transaction, the PSR is not proposing or consulting on any remedy in relation to ownership. Should the transaction not proceed, we would expect that the PSR will consult on any potential remedy and will respond at that time.
38. Given the very significant nature of any potential intervention in this respect, it is vital that the PSR consult with a genuinely open mind on the full range of options that may address its concerns (short of divestment), and, if a divestment is in contemplation, whether it would be proportionate in the context of the overall remedies package, how to ensure non-discriminatory treatment of VocaLink's current shareholders, and on what basis a divestment should take place.
39. LBG is very disappointed that the press release of 7<sup>th</sup> December 2016 accompanying the consultation suggests that the PSR has already taken its decision on whether a divestment is required: "In the event that the proposed MasterCard acquisition of VocaLink does not receive regulatory approval, the PSR will pursue the divestment remedy."<sup>7</sup> In addition, in evidence to the Treasury Committee on 18<sup>th</sup> January 2017, the PSR stated that "We have been absolutely clear that if that [MasterCard] merger does not go through, for whatever reason, we will pursue the divestment remedy, so we will require the banks to divest their ownership of VocaLink".<sup>8</sup> Therefore, we again urge that the PSR genuinely engage with affected parties if required.
40. At this stage, we do not believe that it is necessary for the PSR to reach any view other than whether the MasterCard acquisition would meet its concerns. Accordingly, we do not believe that the PSR should express a view on the maximum permitted shareholding (which we believe should be significantly higher than 10%), or on any other requirements of a possible divestment remedy.

<sup>7</sup> <https://www.psr.org.uk/psr-publications/news-announcements/Generational-step-towards-wholesale-change>

<sup>8</sup> <http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/work-of-the-payment-systems-regulator/oral/45939.html>

## **LBG RESPONSE TO PSR CONSULTATION QUESTIONS**

### **Competitive procurement remedy**

- 1. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

LBG does not agree with the PSRs assessment of the effective remedies as set out in paragraph 6 of our Executive Summary.

**2. Do you agree with our assessment of the costs of the remedies? If not, please explain why.**

LBG does not agree with the assessment of the costs of the remedies and feels that they are inadequate in a number of areas

- Tender Costs for Participant PSPs
- Testing
- Translation
- Potential Member Switching Costs

These are explored in more detail in paragraph 34 of our assumed costs comments.

**3. Do you have any comments on the design of our proposed remedy, including but not limited to:**

**a) Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?**

LBG agrees with the conclusion that a discovery phase is not necessary for the reasons highlighted in the PSR findings as detailed in section 3.72 of the remedies consultation.

LBG also agrees that an independent external audit of the procurement process is unnecessary.

**b) Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?**

LBG believes that close interaction with the Forum is vital to ensure that the payment scheme operators can run an effective competitive procurement. In our opinion, this will not be possible until they know whether and when the SPP will be implemented.

Furthermore, LBG does not believe that introducing remedies in the expectation that derogations will be required under the most likely future scenario is proportionate or necessary.

We have provided further detail in our Executive Summary paragraphs 6 & 7 as well as within our competitive tendering comments paragraphs 10-21.

## **Messaging standards remedy**

**4. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

LBG welcomes the PSRs conclusion that the Messaging Standards remedy is not appropriate for LINK. However, LBG does not agree with the PSRs assessment of the

effectiveness of the potential remedies identified for Bacs & FPS. Requiring the Bacs & FPS infrastructures to operate on ISO20022 appears unnecessary to achieve the PSR's objectives. We believe there are lower cost and risk alternatives that could meet those objectives and these are set out in more detail in paragraphs 26, 27 & 28 of our messaging standards comments.

**5. Do you agree with our assessment of the costs of the remedies? If not, please explain why.**

The cost-benefit analysis of competitive procurement and of requiring the use of ISO20022 for Bacs/ FPS is not robust and does not include significant cost drivers. The evidence base put forward by the PSR does not support the remedy package as proposed.

**6. Do you have any comments on the design of our proposed remedy, including, but not limited to:**

**a) Whether the use of XML standard should be required to make our remedy effective?**

LBG supports the use of XML syntax to encode ISO20022 messages. This is the predominant format today for fields and messages. However, for API architectures, JSON is emerging as the industry standard syntax. Determining the syntax is an implementation decision, and should take into account emerging industry standards at the time. There are a number of other technical decisions that would need to be agreed in a standard and consistent way such as protocol, character set, ISO20022 Message Implementation Rules etc.

**b) Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?**

LBG agrees that future competitive procurement exercises should consider other messaging standards that may become preferable in the future and therefore it should not be a requirement for the remedy to be in place following completion of the next competitive procurement exercise for Bacs & FPS.

**c) Should the operators of Bacs and FPS make mapping information publicly available or are there are reasons why it should be made available subject to certain conditions?**

LBG understands that both Bacs & FPS have already made mapping information publically available at the request of the PSR. It would be useful for the PSR to confirm in due course that this meets its requirements.

Furthermore, in our experience of deploying ISO20022 the supporting business rules are equally important as the standards mapping, if not more so. This is a key consideration and one which LBG would encourage the PSR to work closely with Bacs & FPS to ensure it is accommodated in the implementation approach.

LBG also notes that a like-for-like ISO20022 message set will require a new set of ISO20022 messages that align to the existing scheme models.

**Ownership of VocaLink**

**7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:**

**a) the financial incentive to protect VocaLink**

- b) alternative providers belief that they are at a disadvantage to VocaLink because of ownership**  
**c) and governance arrangements**  
**If not, please explain why.**

At this stage, we do not believe that it is necessary for the PSR to reach any view other than whether the MasterCard acquisition would meet its concerns. Accordingly, we do not believe that the PSR should express a view on the maximum permitted shareholding (which we believe should be significantly higher than 10%), or on any other requirements of a possible divestment remedy.

#### **Remedies package**

- 8. Do you agree with our assessment of the effectiveness of the proposed remedies package?**  
**If not, please explain why.**

LBG does not agree with the PSRs assessment of the proposed remedies package, the rationale to support this view is set out in the response to Questions 1 and 4 and within our more detailed commentary in paragraph 6 of our Executive summary

- 9. Do you agree with our proportionality assessment of the proposed remedies package?**  
**If not, please explain why.**

LBG does not consider that the proportionality assessment is robust. It relies on some very significant and questionable assumptions, and does not include all relevant costs as outlined in our more detailed comments in paragraphs 29 – 32 of our response.

- 10. Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.**

LBG believes that there is a significant risk that the PSR could introduce disproportionate remedies, which could lead to in the round or over time higher costs for customers and distract from the wider work currently underway to enhance payments in the UK.

The cost-benefit analysis does not support the remedies package as proposed as outlined in more detail in paragraphs 17 to 21 within our competitive tendering comments and paragraphs 31 – 32 within our messaging standards comments. See also the final point in paragraph 31 in relation to the potential for lost benefits should the PSR mandate a divestment remedy at a later stage.

Payment Systems Regulator  
Infrastructure Market Review Team  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

30<sup>th</sup> January 2017

Dear Sirs,

I write in response to the PSR's Proposed Remedies consultation on its Market review into the ownership and competitiveness of infrastructure provision.

LINK does not request any confidentiality regarding its response, other than the two sentences highlighted. This is to maintain confidentiality of our intention from potential suppliers and not undermine our commercial negotiating position.

**Competitive procurement remedy**

1. Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.

**LINK Response: LINK agrees with the PSR's assessment of the effectiveness of the potential remedies in relation to LINK.**

2. Do you agree with our assessment of the costs of the remedies? If not, please explain why.

**LINK Response: LINK believes that the cost of the mandated competitive procurement remedy in relation to LINK may exceed its benefits, as set out below. However, LINK broadly agrees with the procurement cost estimates in relation to LINK.**

3. Do you have any comments on the design of our proposed remedy, including but not limited to:

a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?

**LINK Response: LINK has no comment on whether an additional requirement of discovery phase is necessary to make a BACS' competitive procurement effective.**



b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?

**LINK Response:** In relation to LINK, LINK supports the principle of a required competitive procurement, but not necessarily at the next break point. This is because the cost of the competitive procurement exercise may exceed its benefits at that point. To mitigate this, the decision should be left to the Board of the Operator company for a further two years. LINK therefore requests that this remedy pre-approves a temporary exemption for an initial two years.

**Cost may exceed benefits because:**

- The recent competitive exercise with LINK/VocaLink only ended last April and has already delivered a significant cost saving for service users. Further meaningful benefits may or may not be possible through requiring a tender at the next break. The decision to tender or extend should therefore be left to the Board of the Operator company for a further two years.
- Value for money is already ensured by the removal of indexation as part of that competitive exercise.
- Interchange presents a severe risk and must be resolved, otherwise no tender is possible as the Scheme could be in wind down for year 5. This may take 1-2 years depending on the nature of the solution agreed. A mandated tender at this point may competitively destabilise LINK and risk its failure, as Members may choose to leave rather than participate.
- LINK's recent separation means that the Operator company is well incentivised to seek competitive infrastructure provision.

- [X].

- [X].

### **Messaging standards remedy**

**LINK Response:** LINK has no views as it falls outside the scope of this proposed remedy.

### **Ownership of VocaLink**

7. Do you agree with our assessment that the four largest PSPs retaining a shareholding of around 10% is likely to be effective at addressing:

- a. the financial incentive to protect VocaLink

- b. alternative provider's belief that they are at a disadvantage to VocaLink because of ownership and governance arrangements. If not, please explain why.

**LINK Response: LINK is content that its existing contractual position offers sufficient protection and therefore has no comment.**

**Remedies package**

8. Do you agree with our assessment of the effectiveness of the proposed remedies package? If not, please explain why.

**LINK Response: LINK is supportive in relation to LINK, subject to the two-year extension request.**

9. Do you agree with our proportionality assessment of the proposed remedies package? If not, please explain why.

**LINK Response: LINK is supportive in relation to LINK, subject to the two-year extension request.**

10. Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.

**LINK Response: LINK is supportive in relation to LINK, subject to the two-year extension request.**

I hope that this information is helpful and I am happy to discuss further as necessary.

Yours faithfully,



**John Howells**

**CEO LINK Scheme**

## **1 INTRODUCTION**

Payments UK welcomes the opportunity to respond to the Payment Systems Regulator's (PSR) Final Report on the Market Review into the Ownership and Competitiveness of Infrastructure Provision: Remedies Consultation.

Payments UK is the trade association launched in June 2015 to support the rapidly evolving payments industry. Payments UK brings its members and wider stakeholders together to make the UK's payments services better for customers and to ensure UK payment services remain world-class.

In line with our response to the Market Review's Interim and Final Reports, our comments relate in particular to remedies numbered 1 and 2 and the underlying analysis. We note the current status of remedy 3 and will continue to work alongside the industry to assist the PSR in the next steps of the Market Review.

## **2 OUR RESPONSE**

### **2.1 General comments**

Payments UK is supportive of the PSR's ambitions to make the ownership of payments infrastructure work even more effectively for the benefit of the end user. Moreover, we support a market that operates in a way that is conducive to competition and innovation, so long as it does not compromise the integrity, resilience and security of the payments industry. It is on this basis that we broadly support the overall aims of the review.

As we have stated in our previous submissions, we agree in principle that the objectives of the review could be achieved by the provision of cheaper, more efficient and innovative service offerings. In light of this, Payments UK believes we need to be clear that the steps taken and

outcomes are in line with the PSR's assessment and will produce significant benefit, will not incur overly burdensome cost to industry and end-users, and will not compromise the industry's stability or resilience. We believe that the timing and design of its execution are paramount to the success of the remedies.

## **2.2 Remedy 1: Competitive Procurement of Future Central Infrastructure Contracts**

The timing of the procurement and implementation of the remedy is important. Since the PSR launched this review, the Payments Strategy Forum (PSF) has set a Strategy for UK payments that includes infrastructure provision for a new payments architecture. There is also a process in place to do the more detailed work through the PSF Design Authority. This work will pass to a new entity – the new Payment System Operator (NPSO) – and will complete during 2017. Alongside this work, there is the investigation by the CMA in relation to Remedy 3 into Mastercard's acquisition of VocaLink.

As the report recognises, multiple developments complicate the competitive procurement of FPS, Bacs and LINK. Challenges will arise in the immediate short term for the PSOs to meet the 31 July 2017 target date (4.78) for technical work to be completed to the standard necessary; and in a way that is cognisant of and aligned to the PSF Design Authority work. We note that, as the report states, doing so will unlock wider and more far reaching benefits. Further, we note that the report includes provisions for the PSOs to request a full or temporary exemption; placing the decision on aligning these processes, which include a wider range of entities, with the PSOs. Therefore, there is merit to introduce coordination through the PSF Design Authority and the Delivery Group.

### **Question 3a: Whether an additional requirement of discovery phase is necessary to make Bacs competitive procurement effective?**

Given the complex technical and operational architecture of Bacs, we are unclear of the investment appetite to implement significantly different system requirements in the timescales set out in the remedy. The extent to which the system requirements are different enough not be a like-for-like procurement could be usefully considered by the PSF Design Authority. Depending on the outcome the use of discovery phase for Bacs may still be required.

Finally in noting section 3.112, it should be noted that the design of standards for PSD2 and Open Banking may also impose new requirements that the PSOs would need to integrate within their technical design work. This could include, for example, payment initiation standards (ISO 20022) proposed to be used by Payment Initiation Service Providers (PISPs) or additional data to be conveyed within a payment instruction. This type of cross cutting requirement can be effectively managed and coordinated by the establishment of a common standards capability. This capability, which we refer to as a central standards body, is consistent with the vision and objectives of the Delivery Group working on payment system governance consolidation.

### **Question 3b: Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and process for applications?**

Accepting the need for the PSOs to begin the detailed work as soon as possible, there should be no delay. Granting a temporary exception may also further hamper the opportunity to seek alignment and lessen the opportunity to fulfil some of their obligations jointly prior to the consolidation. Specifically, the work necessary to design and document the adoption of ISO 20022 and formation of translation documentation should be synchronised to ensure, as far as possible, a common approach. Payments UK standards expertise, already deployed in support of FPS, can be further leveraged to assist with these processes to cement the establishment of a common standards capability which is consistent with the vision and objectives of the Delivery Group working on payment system governance consolidation.

It would be advisable to require that the PSOs formally coordinate with the PSF Design Authority during 2017 to ensure the direction of the work is harmonised and to provide a coordination function. This will help to reduce the risk of fragmentation.

We support the PSR's recommended 5 step approach to procurement (3.63). We note however that point 2 ought to be refined to make it explicit that the PSF Design Authority must be consulted. We also would like to propose, the Delivery Group working on payment system governance consolidation should become involved. It is important to note that while the design of the procurement should proceed at pace under existing governance, ultimately the body that will conduct the market engagement, review and selection process will be under the new retail PSO. There ought to be a method to ensure the two activities of design dovetail together. This will also help to ensure a consistent and joined up approach towards engagement with the supplier market and maximise the opportunity for alignment to ensure as far as possible that suppliers are fully incentivised to offer competitive bids looking beyond the immediate next contract period for Bacs and FPS.

## **2.3 Remedy 2: Messaging Standards**

Payments UK supports the decision to define ISO 20022 as the appropriate international messaging standard. Our knowledge and experience of this standard - and the fact that Payments UK provides the leadership of the international ISO 20022 group responsible for the standard - has provided us with unique insights into: the development of the standard internationally; and the design and implementation of the standard for services such as CASS, where Payments UK led the standards design effort. Based on this knowledge we would like to highlight the following issues set out in the message standards remedy.

Mapping from legacy formats to ISO 20022 is only a prerequisite because of the decision to make adoption of ISO 20022 only mandatory on the central infrastructure provider. While appreciating that this may reduce the cost of implementation, especially on end-users, it creates the risk that the design and implementation of ISO 20022 will be unnecessarily and artificially constrained to be backward compatible with the data, process flows and functionality of Bacs and FPS. We note this tension in section 4.34 where it states that "...with conversion, many of the efficiency and competitive benefits that may be available from ISO 20022 do not occur, due to the ongoing constraints on the amount of information that can be included within the messages". In order to counteract this limitation it is recommended that a central standards body, consistent with the vision and objectives of the Delivery Group working on payment system governance consolidation,

be made responsible for the mapping exercise as set out in section 4.13. This activity must be considered as one of the tasks that the PSOs fulfil jointly. We would also advocate a sensitive approach to the development of new ISO 20022 messages that might be necessary only to replicate UK specific data, process flows or functionality. Were this necessary rather than new messages, we would advocate the use of alternative ISO 20022 compliant methods to address these requirements, such as Extensions, Variants or market practice. We would also strongly recommend that the ISO 20022 implementation compliance checklist<sup>1</sup> should be universally followed to maximise alignment with existing implementations of ISO 20022.

**Question 4c Should the operators of Bacs and FPS make mapping information publically available or are there any reasons why it should be made available subject to certain conditions?**

Payments UK believes that all documentation related to the adoption of ISO 20022 for Bacs and FPS should be made publically available, including mapping and translation documentation. All these documents should be readily available and should conform to a common industry agreed format so that they are presented consistently, maintained accurately and kept up to date. Our recommendation is to develop specific U.K. implementation guides (IGs) to foster greater interoperability when implementing ISO 20022. These should have clear business rules. Further, there would need to be a central standard authority to facilitate the development of a harmonised and consistent set of publically available UK ISO aligned IGs to ensure consistency and avoid divergence of implementation across the different Payment System Operators. All transactions to and from UK electronic payments would need to be technically compliant with these IGs.

Payments UK has developed a Standards Collaboration Framework (SCF) to act as an authoritative source of documentation related to technical standards in the UK payments market. The Framework is a library of standards that enables technical mappings between formats as well as message standard development. The SCF utilises commercially available software<sup>2</sup>, however Payments UK believes the use of this tool alone does not unlock the necessary value the industry requires from a central standards approach. There is need for a 'Standards Authority' that will execute an automated approach to define, maintain and manage UK payment standards. The SCF approach is one option to consider as part of any implementation strategy. It has facilitated both FPS and Bacs in their mapping to ISO 20022 and is endorsed as an approach by the PSF.

**Question 4: Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

The design of the ISO 20022 messages to replicate the complete technical architecture for Bacs will be a complex and extensive exercise. Our estimates suggest that there may be in excess of 40 ISO20022 messages that would need to be developed to replicate the current Bacs architecture. We do have concerns about the expectation that this can be completed to the high quality required by 31 July 2017.

**Question 5: Do you agree with our assessment of the costs of the remedies? If not, please explain why.**

<sup>1</sup> <https://www.iso20022.org/news/iso-20022-implementation-compliance-checklist-available>

<sup>2</sup> GEFEG MBH

We note that the proposal for the cost of conversion is to be recovered by the central infrastructure provider; therefore we would recommend that for transparency, this cost component be specifically broken down as part of the procurement. We also note that central infrastructure providers confirmed their acceptance of this approach in terms of enabling competition.

**Question 6b: Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs FPS?**

Our recommendation is that the use of centrally procured conversion should only be part of the next procurement. This is because ISO 20022 will be unnecessarily and artificially constrained to be backward compatible with the data, process flows and functionality of Bacs and FPS, which significantly limits the benefits (4.34). Additionally as noted in section 4.19 the expectation is that over the next 5 years users will upgrade their internal systems generate, send, receive and process ISO 20022 messages, so the justification to continue with central conversion as a way to minimise cost impact on users would no longer be valid.

**Question 6a: Whether the use of XML standard should be required to make our remedy effective?**

To clarify, compliance with ISO 20022 requires the adoption of a syntax that respects the rules and structures of the standard. ISO 20022 defines the normative rules for two compliant syntaxes<sup>3</sup> (ISO 20022 XML and ASN.1). Any submission to ISO must define the syntax that is to be registered. ISO 20022 XML is the default. Where an alternative syntax is requested it must be defined in an ISO 20022 compliant manner and formally submitted, approved and registered by the ISO 20022 Registration Management Group in compliance with ISO 20022-5:2013 Financial Services -- universal financial industry message scheme -- Part 5: Reverse engineering.

The choice of which syntax to implement should not be mandated by the PSR. However, it does require coordination to ensure that ISO 20022 is adopted in a consistent manner avoiding the risks of unintended consequences that may undermine the objectives of this review. Given the 31 July 2017 deadline, the PSR should strongly recommend the adoption of ISO 20022 XML, and give consideration of how the decision, definition and approval at ISO of alternative syntaxes would be managed. Payments UK advocates that this activity would be undertaken by a common standards capability which is consistent with the vision and objectives of the Delivery Group working on payment system governance consolidation.

<sup>3</sup> ISO 20022-4:2013 Financial services -- Universal financial industry message scheme -- Part 4: XML Schema generation, ISO 20022-8:2013 Financial services -- Universal financial industry message scheme -- Part 8: ASN.1 generation



**Santander UK plc: Response to MR15/2.4 –  
Market review into the ownership and competitiveness of infrastructure provision:  
Remedies consultation  
February 2017**

**Introduction**

1. Santander UK plc (Santander) welcomes the PSR's remedies consultation following the publication of the Final Report into its market review into the provision of UK payments infrastructure. In general, Santander supports the two remedies set out in the MR15/2.4 remedies consultation.
2. We consider that the proposals fit together well, and, if executed effectively, will continue the good progress made to date in simplifying and enhancing the access model for users and creating a level playing field where competition can thrive. Santander believes it is important that a clear and objective strategy is defined for the tasks set out to ensure that the expected benefits are delivered in a timely manner to meet the objectives of the PSR and the payments community.
3. In summary, we note:
  - a. While we agree with the PSR's assessment of the effectiveness of the competitive procurement remedy, we would encourage a greater proportion of time be devoted to shaping the earlier stages of the process. Although this may have cost implications, it will produce a more efficient end result in the long run;
  - b. We agree with the PSR's assessment of the effectiveness of the messaging standards remedy and would encourage the industry to define timescales for end delivery which underpin cost assumptions.
4. Given the PSR's remit as an economic regulator, we look forward to continuing work with you as you develop a robust review of the economic benefits of the remedies, to ensure that the implementation of the proposed remedies package is clear, proportionate and delivered in a timely way to ensure effectiveness.
5. Please note that Santander considers the contents of this response to be confidential and in some places commercially sensitive. Therefore we do not consent to this response being published in whole or in part without prior notice and our written consent.
6. If you have any questions about this response, or you would like to discuss this in more detail, please email us at [santanderregulatoryliaison@santander.co.uk](mailto:santanderregulatoryliaison@santander.co.uk).



## Santander Response

### **Competitive Procurement Remedy**

*Q 1. Do you agree with our assessment of effectiveness of the potential remedies identified?*

5. We agree the competitive procurement remedy will result in greater competition within the UK payments' sector and address the previously limited competitive pressure on VocaLink.

*Q 2. Do you agree with our assessment of the costs of the remedies?*

6. Santander considers the cost assumptions to be sensible, and appear to be in order of magnitude expected for Bacs and FPSL. However we are of the view that the Link estimate may be too low. It is important to reflect on other recent industry collaborative projects which evidence that the more time spent planning in the early stages of the deliberation, the greater the benefits derived as supplier engagement starts. Notwithstanding taking the time to create robust and detailed specifications and aspiration will drive higher costs, we believe this approach is necessary.
7. Assuming that Bacs and FPSL are merged entities by the time the remedy implementation process commences, we would encourage some collaboration with Link to ensure that a consistent model is followed to drive alignment across PSOs. We consider that such collaboration would assist in negating the risk of diverging message standards or technology, which is an important objective driven from the Payment Strategy Forum (the "Forum").

*Q 3. Do you have any comments on the design of our proposed remedy, including but not limited to:*

- a. Whether an additional requirement of discovery phase is necessary to make a Bacs competitive procurement effective?*
8. We believe it would be sensible to assess this in the context of the new Payment Systems Operator (the consolidated Schemes) to determine if there would be benefit to future suppliers. The scale of change is likely to be significant, particularly if the visions of the Payment Strategy Forum are to be enabled, or delivered within this procurement exercise. As such, the need for some form of detailed "discovery phase" would be essential to ensure a clear set of requirements are provided in the supplier selection process.
- b. Our proposals for the interaction with the Forum, possible temporary exemption periods, the timings of our milestones, and the process for applications?*

We consider the proposals to be appropriate. However, we believe that sufficient time and concentrated effort between the PSOs and Forum strategy is required to ensure clear alignment and benefit is delivered. As such, the timeline suggested is appropriate, but – given the significance of the task and scale of change planned - it should be reviewed at relevant milestone points to ensure it remains appropriate.

### **Messaging Standards Remedy**

*Q 4. Do you agree with our assessment of effectiveness of the potential remedies identified? If not please explain why.*

9. We agree with the PSR's assessment of effectiveness of the messaging standards remedy to tackle the barrier to entry for alternative providers of central infrastructure services.

*Q 5. Do you agree with our assessment of the costs of the remedies? If not, please explain why.*

10. Santander agrees that the assessment is sensible but considers the detail of design and delivery will have an impact on the true cost. For example, it could be interpreted from the summary that the conversion process could continue indefinitely, and so this in itself would damage the business case for wanting to adopt sending ISO20022 – i.e. there is less incentive to invest in sending more content if it is only to be truncated back into Bacs Standard 18 format. A firm approach to the timescales of messaging standards will drive the more detailed cost assumptions. *Q 6. Do you have any comments on the design of our proposed remedy, including but not limited to:*

- a. *Whether the use of XML standard should be required to make our remedy effective?*

11. We consider the XML standard, as noted in the remedies consultation as the most widely used syntax for ISO 20022 and also an international open standard, to be the most appropriate approach in today's industry.

- b. *Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?*

12. As suggested in the report, the competitive procurement and features around this should become a "business as usual" feature of the PSOs; therefore the remedy itself should not be necessary.

- c. *Should the operators of Bacs and FPS make mapping information publicly available or are there reasons why it should be made available subject to certain conditions?*

13. Mapping information ensures that payment messages and their functional attributes developed under existing standards are mapped into ISO 20022 and tested once mapping is completed. In our opinion, mapping information should be treated as publicly available information.

**Remedies Package**

*Q 8. Do you agree with our assessment of the effectiveness of the proposed remedies package? If not please explain why.*

14. We agree with the PSR's assessment that the proposed remedies package as a whole will have the effect of remedying the competition issues as identified in the final report.

*Q 9. Do you agree with the proportionality assessment of the proposed remedies package? If not please explain why.*

15. We agree with the PSR's proportionality assessment of the proposed remedies package.

*Q 10. Will the messaging standards remedy, the competitive procurement remedy or the overall package result in the loss of any benefits to users? Please explain how these benefits to users currently arise and why they are unlikely to arise following the implementation of the remedies. Please provide evidence to back your claims.*

16. In general we do not envisage the overall package will bring a loss of benefits to users. However, to ensure this, assessment of remedy delivery should be an integral feature of the remedy. During the assessment process it may be identified that features exist that are used by some users, but that these features actually bring complexity to the process - be it in the core back-office, the end users or the legal/compliance regime around the transaction. In this scenario, were these features changed, there may be impact on certain users. As such, decisions should be focused on whether the feature is relevant and should be carried forward to the new designs.

**Santander UK plc**

**1 February 2017**

**[ENDS]**



## SWIFT Response to the Payment Systems Regulator on the Remedies Consultation MR 15/2.4:

“Market review into the ownership  
and competitiveness of  
infrastructure provision”

01 February 2017

SWIFT thanks the Payment Systems Regulator for the opportunity to provide comments on the Remedies Consultation 'Market review into the ownership and competitiveness of infrastructure provision'.

SWIFT is a member-owned, cooperative society headquartered in Belgium. SWIFT is organised under Belgian law and is owned and controlled by its shareholding Users, comprising over 3,000 financial institutions. We connect more than 11,000 connected firms, in more than 200 countries and territories. A fundamental tenet of SWIFT's governance is to continually reduce costs and eliminate risks and frictions from industry processes.

SWIFT provides banking, securities, and other regulated financial organisations, as well as corporates, with a comprehensive suite of messaging products and services. We support a range of financial functions, including payments, securities settlement, reporting, and treasury operations. SWIFT also has a proven track record of bringing the financial community together to work collaboratively, to shape market practice, define formal standards and debate issues of mutual interest.

If you wish to discuss any aspect of our response please do not hesitate to let us know.



**Natasha de Terán**

SWIFT | Head of Corporate Affairs

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**Question 4: Do you agree with our assessment of effectiveness of the potential remedies identified? If not, please explain why.**

SWIFT recognises that the motivation for this remedy is to address barriers to entry for alternative infrastructure providers. Given this goal, the like-for-like approach outlined in the remedy, where ISO 20022 is mapped to the existing legacy standards, makes sense.

However, a like-for-like approach does risk negating some of the key benefits of ISO 20022, specifically:

- a. By limiting the ISO 20022 implementation to cover only the existing capabilities of Standard 18 (BACS) and ISO 8583 (FPS), implementers are effectively still presented with two specifications, rather than one, adding to their costs.
- b. Two distinct 'flavours' of ISO 20022 will make it difficult to move payments between schemes, limiting operational agility and the resilience benefits of convergence to a single standard.
- c. Without very rigorous specifications, like-for-like mapping can lead to data truncation when data is moved from rich/structured ISO 20022 to a less rich/more loosely structured legacy format. This problem can make it difficult to 'round-trip' data. For example, if data is presented in ISO 20022, mapped to Standard 18 then *back* to ISO 20022, for example to return to the originator, it may lose some of its structure and precision in the process.
- d. Finally, when the new architecture envisaged by the PSF materialises, users of the 'cut-down' ISO 20022 versions that are a consequence of like-for-like will be confronted with a significant upgrade cost if they are to benefit from any of the value-added features of the new platform.

SWIFT further understands the provision of a centralised mapping utility will greatly ease implementation for new entrants, supporting the principal goal of the proposal. Nevertheless, experience in other countries has shown that like-for-like mapping provided by a central utility can lead to an extended period of coexistence of standards and entrench a dependency on legacy data structures, even if the syntax used to exchange data is more modern. The lack of a 'clean break' can complicate the later introduction of a more advanced system.

It may be possible to mitigate some of these risks and concerns by careful design and implementation of the approach described in the remedy.

**Question 6: Do you have any comments on the design of our proposed remedy, including, but not limited to:**

- a. **Whether the use of XML standard should be required to make our remedy effective?**
- b. **Whether the remedy should remain in place following completion of the next competitive procurement exercises for Bacs and FPS?**
- c. **Should the operators of Bacs and FPS make mapping information publicly available or are there reasons why it should be made available subject to certain conditions?**

- a. XML is the default and most widely used syntax for ISO 20022. However, for some technological approaches, other syntaxes, such as JSON, may be more suitable. Although ISO 20022 does not support JSON as a native syntax today, work is going on in the ISO 20022 technical community to add this capability. In principle it will be possible to mix JSON and XML syntaxes and still maintain interoperability at the level of the data payload. The key is to ensure that the same specifications for the data content are shared, regardless of the syntax. As noted above, the greater the harmonisation of these data content specifications, between BACS and FPS, and between these

two systems and the new payments architecture, the easier it will be for scheme participants to implement and upgrade.

- b. Where the remedy means implementation of ISO 20022, indeed the next procurement exercise should cement this decision. For the central translation part of the remedy, we would urge more caution. Here, a commitment to continue to offer a basic service based on legacy formats might undermine the uptake of new and beneficial services offered by the new system. A clear plan to phase out this backward compatibility over time might mitigate this risk.
- c. Mapping information should be made publically available as this will help institutions to migrate more easily from the legacy formats to the new standard. Also, this would help allow mapping rules to be consistent across the industry and ensure all providers of conversion solutions (such as aggregators and gateway services providers) map in the same way.

----- END -----

Dear PSR,

Question 6: Do you have any comments on the design of our proposed remedy, including, but not limited to:

a. Whether the use of XML standard should be required to make our remedy effective?

In regard to the above question in the Infrastructure Market Review Remedies Consultation, our comments are as follows:

From an IT viewpoint, the format (such as XML, JSON) of a messaging standard affects very significantly the costing of that standard.

If the ISO20022 standard is imposed without specifying XML as a standard, then there will be no easy IT standard, and very large and significant cost will be imposed on industry in operating APIs using different formats (such as JSON, XML, etc.).

It is important that XML is adopted as a standard, as then IT programming can be made with certainty that the other party in a message chain (sending or receiving) will also be using XML, and not some proprietary format that will involve great expense to programme for. Without mandating XML use, the very benefits of the ISO20022 implementation will be lost, and great industry loss will be incurred.

Best Regards,

Andrew Kaye  
CEO – Transpact.com

[By email]



Infrastructure Review Team  
Payment Systems Regulator  
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1 February 2017

Dear Sir/Madam

**Virgin Money response to MR 15/2.4 Market review into the ownership and competitiveness of infrastructure provision: remedies consultation**

Virgin Money welcomes the opportunity to respond to the Payment Systems Regulator's consultation on proposed remedies flowing from its Market Review into the ownership and competitiveness of infrastructure provision.

In previous submissions to the PSR as part of this Market Review, we have expressed our support for the two specific remedies on which the consultation is focused – namely, requiring competitive procurement exercises for the provision of infrastructure services, and a common international messaging standard for Bacs and FPS.

This response focuses on the second of the two remedies, which we think has the potential to deliver significant benefits to UK consumers. Our key points are as follows:

- We believe strongly that moving to a single, interoperable international payment standard will be pivotal in supporting the development of innovative new banking services for consumers and enabling further competition in UK retail banking.
- We therefore think a clear direction from the PSR is required to ensure that the industry adopts the ISO 20022 messaging standard. Without this, UK banks are likely to remain wedded to a range of incompatible messaging standards, which could undermine efforts to modernise the UK payments system along the lines proposed by the Payments Strategy Forum (PSF) in its *Payments Strategy for the 21<sup>st</sup> Century*.

We make a number of specific observations about this remedy below, regarding the provision of ISO 20022 capabilities by payment system aggregators and sponsors, the importance of mandating the adoption of the standard, and the costs of adoption.

## **Messaging Standards Remedy**

Virgin Money supports the PSR's assertion (in paragraph 4.7 of the consultation paper) that ISO 20022 should be the international messaging standard of choice. As the PSR notes in the remedy, adopting ISO20022 would support the work of the PSF, which has recommended that new and existing payment systems align to this standard.

### *Implications for central infrastructure*

As noted in paragraph 4.17 and 4.33 of the consultation paper, we recognise that conversion from a constrained standard to a more data-rich standard such as ISO20022 (either by the central infrastructure or between the user and the central infrastructure) may result in truncation of additional data. Truncation has implications for the richer data initiatives proposed by the PSF, because if the central infrastructure truncates additional data, users will not be able to make use of new richer data capabilities. We would therefore concur with the remedy of section 4.48 that the central infrastructures be mandated to provide ISO20022 capabilities as part of the core infrastructure as part of their next procurement exercise.

### *Implications for aggregators and sponsors*

The payment schemes have set up aggregators and sponsors to support growth banks with connection to payment schemes. Under the proposed remedy, it is possible that aggregators and sponsor banks may not provide ISO20022 capabilities to the growth banks that connect through their services. If these capabilities are not provided, smaller growth banks will be denied the opportunity to use the new formats or make use of extended data capabilities, and risk being excluded from access. We would therefore propose that aggregators and sponsor banks be mandated to provide native, un-truncated ISO20022 capabilities.

### *Mandating the ISO 20022 standard*

Mandating the ISO 20022 standard to be native in scheme communication will reduce the complexity of implementing the standard. It will allow for richer data to be used, and will increase competition in both the connectivity market and infrastructure provision.

Mandatory adoption by users in the short term may be difficult given the related cost implications. We believe that the option of staged upgrades of internal systems, as suggested in paragraph 4.20 of the consultation paper, would provide a good alternative for users by allowing their existing systems to reach the end of their financial lifecycle.

However, we also agree with the PSR's view, set out in paragraph 4.24 of the consultation paper, that the absence of a mandatory end date for transition to ISO

20022 could result in the benefits of the standard not being realised in terms of enhanced data (as suggested by the PSF) for the whole industry.

We therefore believe that a mandatory end date should (as with SEPA) be agreed so that the Government, businesses and consumers can realise the significant benefits of enhanced data that are outlined in the PSF's strategy, such as the ability to easily identify what a payment relates to and to reconcile payments with internal systems accurately and more efficiently.

#### *Costs associated with adoption of ISO 20022*

Given the short-term cost issues associated with adopting ISO 20022, we suggest that the PSR should consider other interim mechanisms to encourage the industry to adopt ISO20022 such as mandating aggregators and sponsor banks to provide ISO20022 message formats, as we suggest above.

With respect the central infrastructure provision, we recognise the costs associated with transition to ISO 20022 on the existing infrastructure may be significant. We therefore support the recommendation proposed in paragraph 4.48 of the consultation paper that any new infrastructure procurement should require the inclusion of native ISO 20022 functionality.

Virgin Money is keen to continue to work closely with the PSR as it finalised its proposed remedies and we would be pleased to discuss any of the above points in more detail if that would be helpful. Please do not hesitate to contact us if we can be of further assistance.

Yours faithfully

Mark Parker  
Chief Operating Officer  
Virgin Money

## VISA EUROPE

### PSR CONSULTATION: Market Review into the ownership and competitiveness of infrastructure provision

#### 1. EXECUTIVE SUMMARY

- 1.1. Visa Europe (**Visa**) welcomes the opportunity to provide comments in response to the Payment System Regulator's (**PSR**) Remedies consultation, part of its *Market review into the ownership and competitiveness of infrastructure provision* (MR 15/2.4) (**Remedies consultation**).<sup>1</sup>
- 1.2. We welcome the stakeholder engagement that the PSR has conducted since the Final report consultation<sup>2</sup>, and we look forward to continuing to engage with you. We recognise that the PSR has taken some of the stakeholder feedback into consideration and adopted a more robust analytical approach in its market review and carried out quantitative analysis to assess the costs and benefits of its proposed remedies. It has also commissioned external expert reports to support its review. However, Visa considers that this analysis has been completed at a very late stage in the process, after remedies had already been announced, and only serves to support rather than to inform the PSR's proposals. Moreover, the PSR still provides insufficient detail on the remedies and their expected impact.
- 1.3. Visa also considers that the PSR has failed to consider the impact of concurrent market developments on its conclusions and proposed remedies. *First*, the PSR has not considered the impact on competition of MasterCard's proposed acquisition of VocaLink. *Second*, the PSR should consider how the recommendations arising from the Payment Strategy Forum's (**Forum**) Final Strategy,<sup>3</sup> are going to impact competition and interact with the remedies proposed in this review.
- 1.4. The remainder of this response is structured as follows: In Section 2 we set out our comments on the PSR's overarching approach and process over the course of this market review. In Section 3 we provide our views on the specific remedies that have been proposed.

#### 2. OUR GENERAL COMMENTS TO THE PSR'S PROPOSED REMEDIES

##### Market context

- 2.1. We agree with the PSR (and have stressed throughout this review) that payment systems form a vital part of the UK's financial system and are fundamental to the UK economy more broadly. Furthermore, the payments industry is a dynamic and evolving market directly influenced by the development of information and communication technology. This has led to the emergence of new payment channels, new payment instruments, new market participants and an increasingly global payment market over the past decade. The industry will remain

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<sup>1</sup> <https://www.psr.org.uk/psr-publications/market-reviews/IMR-consultation-remedies>

<sup>2</sup> <https://www.psr.org.uk/psr-publications/market-reviews/MR1523-final-report-infrastructure-provision>

<sup>3</sup> <http://consultation.paymentsforum.uk/history/forum-launches-payments-strategy-21st-century>

dynamic given continued innovation, new propositions and increasing customer engagement throughout the sector.

- 2.2. The scale and pace of change distinguishes payment systems from other 'traditional' regulated industries. It is therefore vital that any market intervention considered by regulatory authorities is thoroughly evidenced and justified, and that the proposed regulation does not stifle innovation. The PSR must also bear in mind the global nature of the market for payment systems when considering imposing regulation in the UK market.

**The PSR has now conducted quantitative economic analysis, but this has taken place too late in the process**

- 2.3. Visa notes that since the publication of its Final consultation, the PSR carried out additional cost-benefit analysis to assess whether the benefits of the proposed remedies outweigh their expected costs. The PSR also commissioned a study to assess the costs and benefits of the migration of Euro-denominated transactions from legacy payment schemes to the new SEPA<sup>4</sup> payment scheme, which has also adopted ISO20022.<sup>5</sup> These exercises demonstrate that the PSR considered Visa's comments regarding the need to analyse the impact of potential remedies on the payments industry before any remedy is finalised and imposed.
- 2.4. However, while we recognise that the PSR has attempted to follow due process in assessing the costs and benefits of the proposed remedies, Visa believes that the PSR's analysis falls short of the standard that should be expected from an economic regulator. *First*, we believe that research and analysis was carried out too late in the process, *i.e.* after remedies had been announced. *Second*, we believe that the PSR has not provided sufficient evidence to link the introduction of the remedies to the benefits to competition that it would like to see.
- 2.5. While we note that the PSR has attempted to carry out a cost-benefit analysis for the package of remedies it introduced, we do not believe that the PSR's analysis is sufficiently robust or based on sufficient evidence. Visa believes that the cost of introducing the proposed remedies may exceed their benefit and result in higher rather than lower costs to users. The quality of the PSR's analysis is not sufficient to exclude this possibility.

### **3. SPECIFIC COMMENTS ON THE PROPOSED REMEDIES**

#### **Competitive procurement remedy**

- 3.1. Visa broadly agrees with the introduction of competitive tendering for the provision of infrastructure services to Bacs, FPS and LINK. Visa recognises that competitive tendering can deliver benefits to payment system providers (**PSPs**) by ensuring that credible providers have the opportunity to bid for the provision of payment infrastructure and are incentivised to offer enhanced services at a competitive price.
- 3.2. Visa also believes that initiatives that contribute to reducing incumbency advantages are likely to benefit the competitiveness of the procurement process so long as they are not overly prescriptive. Visa therefore welcomes the PSR's decision not to pursue an overly prescriptive

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<sup>4</sup> Single Euro Payments Area.

<sup>5</sup> <https://www.psr.org.uk/sites/default/files/media/PDF/ISO-20022-in-SEPA-FINAL-report.pdf>

remedy. As expressed in our previous consultation responses, we believe that a third party audit would go far beyond what is generally imposed by regulators in markets which see substantially less competition than payment infrastructure (for example markets for utilities facing natural monopolies). Similarly, the imposition of any particular syntax requirement as part of the messaging procurement remedy would be overly prescriptive.

- 3.3. We also welcome the PSR's conclusion that a discovery phase for the next Bacs procurement is not required to reduce the incumbent's knowledge advantage. The PSR appropriately considers that the expected output of Bacs's consultation of its customers' future needs will reduce this incumbency advantage by introducing a number of changes to current procurement requirements. This, in turn, would reduce any benefits which may be gained by mandating a scoping phase as part of the remedy.
- 3.4. However, Visa strongly disagrees with the PSR's conclusion that competitive procurement will, on its own, be sufficient to enable effective competition for the provision of infrastructure services. [X] The Competition and Markets Authority (**CMA**) has expressed explicit concern regarding the effectiveness of competition for the provision of infrastructure services to LINK under the transaction and is considering undertakings to address the identified reduction in competition.<sup>6</sup> Visa believes that the PSR has not fully considered and has thus underestimated the impact of the proposed transaction on reducing competition and the effectiveness of the PSR's proposed remedies, including the competitive procurement remedy. In its most recent decision, the CMA specifically recognises the PSR's responsibility as sector regulator to observe how competition develops in its sector and intervene should it observe or identify a reduction in competition.
- 3.5. Similarly, and as explained in previous submissions to the PSR, Visa considers there is continued uncertainty about the implementation and implications of the Forum's proposal to consolidate Bacs, FPS and C&CCC and its longer term vision to develop a new, simplified layered architecture for the UK interbank payment system. For example, it is unclear whether the proposed consolidation would entail a single tender for services covering the entire interbank infrastructure. A single tender could limit the number of potential providers able to tender for the provision of the services and reduce competition. In the long term, it could also reduce competition between interbank payment systems and the innovation resulting from this competition. Consequently, this would impact the effectiveness of the remedies proposed by the PSR in this market review. Visa believes that the PSR has not reviewed the potential consequences of the Forum's proposals in sufficient detail and that implementation of the proposals as they stand could lead to an unintended reduction in competition resulting from the merger of the interbank payment systems. Visa also expresses concern about whether the Forum's conclusions and recommendations are supported by evidence and represent an appropriate solution for the payments sector as a whole.
- 3.6. As set out in our response to the Forum's draft strategy, we believe that as the sector regulator for payment systems the PSR must undertake a full, independent analysis of the Forum's proposals to ensure that any initiatives are fully aligned with the PSR's work in this market review, other key areas of the PSR's work, and the PSR's overarching statutory objectives. We strongly believe that the PSR must undertake this analysis before it finalises the remedies for this market review and that any of the Forum's recommendations that would

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<sup>6</sup> <https://www.gov.uk/government/news/cma-to-consider-mastercardvocalink-remedies>

be implemented should be considered and incorporated into remedies considered by the PSR.

- 3.7. Regarding the implementation of any competitive procurement remedy, Visa notes that where the PSR considers that competitive procurement is appropriate or required, it should seek to impose competitive procurement as early as is practicable. The PSR should review whether current contracts should remain in place until their expected expiry in 2020 and 2021 even under the remedy. In this context, Visa is concerned that the implementation of the Forum's proposals may lead to significant delays in the introduction of the remedy. It is paramount for the PSR to consider the full impact of any delays in implementing the remedy whether arising from existing agreements or market developments.
- 3.8. As regards the relative costs and benefits of the competitive procurement remedy, Visa welcomes the step the PSR has taken to review historic evidence and consider stakeholder responses to develop estimated costs and benefits for the proposed remedies. However, while Visa broadly agrees that the benefits of competitive procurement are likely to outweigh its costs (to the extent that there will be sufficient credible providers to yield effective competition) Visa considers that there are significant limitations to the data and evidence that the PSR has used to conduct its analysis.

#### **Messaging standard remedy**

- 3.9. Visa notes that since the publication of its Final consultation, the PSR has carried out further analysis to assess whether the benefits of the messaging standard remedy would likely outweigh its costs. In particular, the PSR commissioned a study to assess the costs and benefits of the migration of Euro-denominated transactions from legacy payment schemes to the new SEPA payment scheme, which has also adopted the ISO20022 messaging standard.
- 3.10. However, Visa notes that there is still very limited evidence on the actual costs of the messaging standard remedy and expresses concern that the PSR may underestimate the actual costs of the remedy. The PSR states that the costs that a central infrastructure provider would incur for introducing ISO20022 for Bacs and FPS would be insignificant and that users would not incur these costs given the availability of conversion services. However, Visa considers this assumption to be overly simplistic. While the remedy minimises the implementation costs for PSPs by retaining optionality of standards, the ongoing cost to infrastructure providers of servicing multiple standards concurrently and indefinitely may be significant. The PSR has also failed to consider the governance costs associated with maintaining the standard for the selected interbank payment systems.
- 3.11. Visa also believes that the PSR likely overestimates the benefit of adopting the ISO20022 standard.<sup>7</sup> Permitting PSPs to use either of two standards implies that it is unlikely that all PSPs will move to the ISO20022 standard. This in turn will result in a low impact of the proposed remedy, while creating complexity and additional costs to infrastructure providers who would be required to maintain a legacy standard for a small number of PSPs. In addition, the remedy as it stands introduces no requirement to keep the standard current. This would stop some of the benefits from switching to the new standard from being realised.

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<sup>7</sup>

Visa notes that the PSR has not explicitly stated which ISO20022 standard its remedy proposes to introduce.

- 3.12. Visa broadly agrees with the suggestion that if the remedy is introduced it should only apply to the first set of tenders, and it should not automatically apply to subsequent tenders. As we have explained above, the PSR needs to ensure that the remedy addresses a specific restriction or barrier to competition. We would expect that if this remedy is introduced, PSPs are likely to signal their preferences in terms of messaging standards, and this may in itself reduce the barriers to entry identified by the PSR, and reduce the rationale for the remedy. A full impact assessment should therefore be carried out to decide whether to extend the requirement in the future.
- 3.13. Overall, the PSR appears to have done insufficient due diligence on the remedy prior to consultation. Nevertheless, Visa considers that interbank payment system operators should make any conversion/mapping information available to third parties to help reduce barriers to entry.

#### **Ownership of VocaLink**

- 3.14. We believe that in this area the PSR has concluded on a divestment remedy without having clearly demonstrated a link between the ownership structure of VocaLink and consumer harm. Moreover, we believe that the PSR has failed to consider the full impact of the remedy ahead of making it public and underestimated the unintended consequences of the remedy.
- 3.15. Furthermore, the PSR has not undertaken sufficient analysis of the extent to which the MasterCard acquisition of VocaLink may raise competition concerns and reduce the level of competition in the market. The preliminary merger assessment by the CMA identified concerns that the transaction is likely to significantly reduce competition for the provision of payment infrastructure services to LINK. In this respect, the lack of alignment between the PSR and the CMA is particularly concerning. [X] It has therefore also underestimated the impact of the transaction on competition in the market.
- 3.16. In addition, while Visa broadly agrees that a reduction in the shareholding of the largest PSPs in VocaLink is likely to reduce the financial incentive to protect VocaLink, we do not believe that the PSR has provided sufficient evidence to demonstrate that a divestment remedy is either effective or proportionate to address this concern.



Paul Smith  
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1 February 2017

Dear Paul

### **Infrastructure Market Review**

We welcome the opportunity to respond to the PSR's remedies consultation for its Market review into the ownership and competitiveness of infrastructure provision ('Remedies Consultation')<sup>1</sup>.

We share the PSR's view that the proposed acquisition of VocaLink by Mastercard would be effective in addressing the competition problems that the PSR identified in relation to VocaLink's ownership structure. Therefore, we agree with the PSR that, subject to the approval of the acquisition by the CMA, it is not necessary for the PSR to continue to develop the previously proposed divestment remedy. The interests of VocaLink and the PSR are aligned because, as explained further in the Annex, the Mastercard transaction delivers benefits that the PSR could not achieve through the exercise of its legal powers alone.

We also concur with the PSR's conclusions that its *'package of actions, taken together, will address the competition issues that we have found. In particular, they will enable new infrastructure providers with different technology to enter the market and drive new and innovative products and services. This can benefit all users of payment systems, from large PSPs to consumers'*<sup>2</sup>.

We welcome the PSR's view that its common standards proposed remedy is best delivered through the use of message translation services at the core of the network. This will significantly reduce the costs of the remedy and enable PSPs to move to the new standard, if they so wish, in a cost efficient manner.

We welcome full and competitive procurement exercises. Such processes will enable purchasers to fully assess the options available to them. This should ensure

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<sup>1</sup> December 2016 MR15/2.4.

<sup>2</sup> Paragraph 1.6, Remedies Consultation, December 2016.

that future contracts continue to deliver the iteratively better outcomes already achieved by previous contracting exercises<sup>3</sup>.

We also agree with the PSR's competition assessment that, as a result of the remedies, any competitive concerns in the market will be resolved and that VocaLink will not have any material incumbency advantage.

We believe the PSR continues to have a key role to play in ensuring the PSF's collaborative activities are limited to the minimum level necessary, in order to leave the maximum opportunity for future competition and commercial innovation

Our principal area of disagreement is with the PSR's reluctance to intervene more actively in encouraging direct contracting between PSPs and infrastructure providers. VocaLink is of the view that even greater innovation and customer benefit could be achieved if the PSR more actively encouraged direct contracting, and we look forward to working with the PSR on this issue in the future.

Yours sincerely



**Andrew Williams-Fry**  
Chief Regulatory Officer

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<sup>3</sup> VocaLink, 'Market Reform: VocaLink's Response to the PSR's Infrastructure market review', April 2016, paragraphs 2.27 to 2.38.

**ANNEX**

- 1) We agree with the PSR that the acquisition of VocaLink by Mastercard will resolve the competition concerns arising from the banks' ownership and control of VocaLink.
- 2) This transaction will enable the PSR to meet its change of ownership objective in a more expedient timeframe than it could have achieved through the formal exercise of its legal powers. Further, the transaction has many elements that the PSR may find desirable, but which its legal powers do not enable it to mandate when seeking to require the disposal of an interest in an infrastructure provider<sup>4</sup>. (For example mandating a sale to a purchaser with significant experience in running important infrastructure, or mandating the sale of share capital to the extent of this transaction.) This demonstrates that VocaLink's and the PSR's objectives are very much aligned on this issue.

**Divestment remedy**

- 3) In our response to the PSR's Final report, we noted that that there was a significant risk to the industry and to VocaLink from the regulatory uncertainty that could be created if the PSR continued to detail its proposed divestment remedy at the same time as the CMA was conducting its merger review. We agree with the PSR's decision to pause its work on the proposed divestment remedy and, as a consequence, avoid any conflicts between the two processes.
- 4) On 4 January 2017 the CMA stated that the merger may be expected to result in a substantial lessening of competition in relation to the provision of central infrastructure services for the LINK Scheme. In response Mastercard offered undertakings to address the CMA's competition concerns. On 18 January 2017 the CMA stated that it considers that there are reasonable grounds for believing that the undertakings offered, or a modified version of them, might be accepted by the CMA. It remains appropriate for the PSR to pause its proposed remedy until the CMA has reached a decision on whether to approve the acquisition. In the event that the CMA approves the acquisition, the PSR will no longer need to pursue this proposed remedy.

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<sup>4</sup> We set out our views on the limitations of the PSR's powers under s.58 FSBRA in paragraphs 5.47 to 5.53 of our response to the PSR's interim report.

### Competition assessment

- 5) We welcome and agree with the PSR's assessment that we will have no material incumbency advantage in future procurements<sup>5</sup>. While the PSR's assessment is contingent on its remedies, our view is that market developments mean inevitably that we will have no incumbency advantage at the next contract procurement processes. For example:
- the divestment by the banks of their holdings in VocaLink will remove the PSR's concern that the current incentives on the scheme companies prevent the undertaking of full procurement processes;
  - FPSL and LSL have already confirmed that they intend to undertake full procurement processes<sup>6</sup>;
  - the Payment Strategy Forum's strategy<sup>7</sup> and work plan<sup>8</sup> strongly suggest that there will be substantial changes (for example, the New Payments Architecture<sup>9</sup>) that will result in VocaLink not having any incumbency advantage; and, as the PSR has acknowledged,
  - *'a competitive procurement, even with a limited number of participants, can produce a competitive outcome, as participants that are efficient and provide interchangeable services will constrain each others' offers in the procurement process'*<sup>10</sup>.
- We conclude that the next procurement processes, regardless of the PSR's remedies, will be the most competitive yet.
- 6) In addition to these market developments, competition will further benefit from the PSR's proposed remedies. We agree with the PSR that its *'package of actions, taken together, will address the competition issues that we have found. In particular, they will enable new infrastructure providers with different technology to enter the market and drive new and innovative products and services. This can benefit all users of payment systems, from large PSPs to consumers'*<sup>11</sup>. In our participation in tendering processes in the UK and overseas markets we routinely encounter alternative suppliers with competitive products. Therefore, our experience is consistent with the further evidence that the PSR has collected since its Final Report from its engagement with a number of alternative providers that are all active in

<sup>5</sup> Paragraph 3.49, Remedies Consultation, December 2016.

<sup>6</sup> Paragraph 3.55, Remedies Consultation, December 2016 .

<sup>7</sup> A Payments Strategy for the 21st Century Putting the needs of users first, November 2016.

<sup>8</sup> <http://implementation.paymentsforum.uk/sites/default/files/pictures/timeline%20alt%202.jpg>

<sup>9</sup> <http://implementation.paymentsforum.uk/working-groups/npa-design-hub>

<sup>10</sup> Paragraph 3.15, Remedies Consultation, December 2016.

<sup>11</sup> Paragraph 1.6, Remedies Consultation, December 2016.

similar markets. The PSR found these to be credible competitors to VocaLink once the barriers to competition (message standards and ownership) the PSR identified in its final report have been removed.

**Procurement remedy**

- 7) We welcome full and competitive procurement exercises and note that FPSL and LSL have told the PSR that they will run competitive procurement for the next contract regardless of the remedy. Such processes will enable the purchasers to fully assess the options available to them and Mastercard's proposed undertakings, by facilitating access for potential new processors to VocaLink's existing communications infrastructure, should help ensure that such options are available.
- 8) We consider that the incentives to run such full and competitive procurement processes (whether undertaken by the banks in a direct contracting market structure, or the scheme companies in the current market structure ('the procurement agent')) could be significantly strengthened by the change in ownership of VocaLink. Therefore, we would be supportive of a procurement remedy that places the fewest mandated requirements on the procurement agent, and gives it the freedom to run a procurement process that best meets its needs. If the PSR seeks to be prescriptive as to the procurement process to be followed, not only could that be disproportionate, but it could also prevent the procurement agent from running innovative procurement processes that fully meet its requirements and interests.

**Messaging standards**

- 9) The PSR proposes that at the next procurement exercise the operators of Bacs and FPS procure central infrastructure capable of receiving and sending messages under the ISO 20022 messaging standard, as well as, where required, existing standards (i.e. translation/conversion to the existing standards should be provided centrally). We welcome the PSR's pragmatic approach of proposing the use of translation services. In particular, the use of a central conversion facility would ensure that users do not need to upgrade their systems or implement conversion services, unless they prefer to do so.
- 10) We continue to be supportive of a move towards ISO 20022 message standard and agree that translation services (including payment aggregator services such as our PayPort products) offer a faster, more cost effective and, therefore, more proportionate way of delivering the vast majority of the benefits of adopting a common international standard.
- 11) The PSR's proposed approach removes the barrier to competition but, as the PSR itself recognises, many of the wider benefits of ISO 20022 beyond enhanced competition at central infrastructure level (the vast majority of the

benefits of adopting a common international standard)<sup>12</sup> are not likely to arise. However, the PSR's proposal is an important first step on the journey to a common standard used by all.

**PSF**

- 12) Noting the various references in the Remedies Consultation to the ongoing work of the PSF, we believe the PSR continues to have a key role to play in ensuring the PSF's collaborative activities are limited to the minimum level necessary, in order to leave the maximum opportunity for future competition and commercial innovation.

**Direct contracting**

- 13) We note the PSR's view that its remedies do not dictate the market structure nor preclude direct contracting. However, the PSR's passive approach misses the opportunity to put in place remedies that actively enable and encourage competition in the market. We maintain that, in the future, direct contracting between infrastructure providers and PSPs can deliver significant improvements, in particular for innovation. We are disappointed that the PSR has not considered our suggestion that it should assess the appropriate functions of the scheme companies and in particular whether scheme companies should have procurement functions or whether PSPs would be better placed to select their own suppliers (i.e. direct contracting between PSPs and infrastructure providers).

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<sup>12</sup> Paragraph 8.65, PSR, Market review into the ownership and competitiveness of infrastructure provision: Final Report, July 2016.