Payment
Systems
Regulator

Consultation paper

Authorised push payment (APP) scams:

Requiring reimbursement

September 2022

CP22/4

We welcome your views on this consultation. If you would like to provide comments, please send these to us by **5pm on 25 November 2022**.

You can email your comments to **appscams@psr.org.uk** or write to us at:

APP scams
Payment Systems Regulator
12 Endeavour Square
London E20 1JN

We will consider your comments when preparing our response to this consultation.

We will make all non-confidential responses to this consultation available for public inspection.

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www.psr.org.uk/publications/consultations/cp22-4-app-scams-requiring-reimbursement/

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1 Executive summary

1.1 We are proposing new measures to fight payment scams, based on payment service providers (PSPs) reimbursing the victims. This reimbursement will be mandatory in most cases. The measures should protect people from fraud by giving PSPs good incentives to prevent scams, and making sure victims get their money back.

1.2 Authorised push payment (APP) scams happen when fraudsters trick someone into sending a payment to a bank account controlled by the fraudster. Once a victim realises they've been scammed it's often too late to stop it. Scam values vary, but in some cases they have a devastating effect on the victim's life or business.

1.3 There are more incidents of fraud than any other crime in the UK, and APP scams are rising quickly. They have now overtaken card fraud to become the largest type of payment fraud, both in the number of scams and the value of losses. In 2021, losses to APP scams totalled £583.2 million, a 39% increase on the previous year.[1] Many cases go unreported, so the real figures are likely to be higher. In reported cases, currently only 46% of total APP scam losses are reimbursed to the victim.[2]

1.4 Criminals are getting more creative and sophisticated each day. This affects how and where they target their victims, the methods they use to deceive them, and where the money ends up.

1.5 APP scam fraudsters need access to the UK banking system in order to receive payments into bank accounts they control. As the Payment Systems Regulator, our focus is on ensuring that the payments industry acts to:

- identify and address fraud in the Faster Payments system
- protect people who fall victim to APP scams

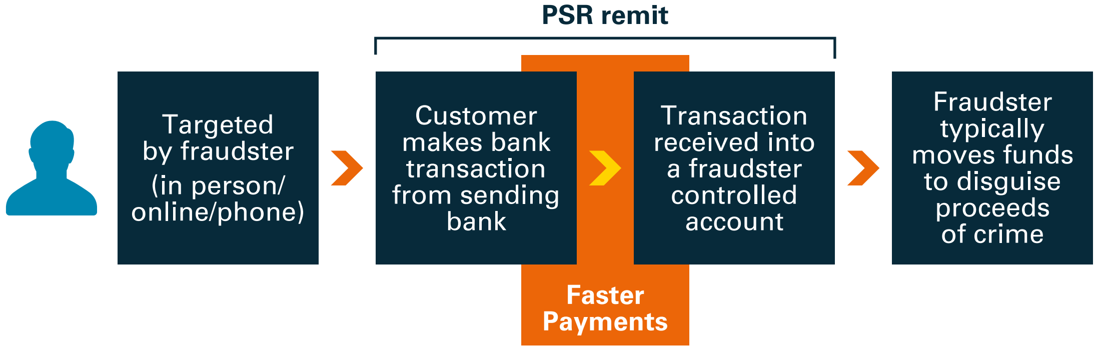
1.6 Remote banking payments processed through Faster Payments (or cleared in-house by banks) increased by 23% in 2021 compared to 2020, to reach 3.6 billion payments.[3] While fraudulent payments only represent 0.1% of overall volumes, Faster Payments was used for 97% of APP scam payments – so we want to severely limit fraudsters' ability to operate within this payment system.

1 UK Finance, *Annual fraud report – The definitive overview of payment industry fraud in 2021* (August 2022).

2 46% of losses in cases reported under the CRM Code.

3 UK Finance, *UK Payment Markets Summary* (August 2022).

Figure 1: A typical APP scam payment journey



1.7 A single scam typically involves multiple steps. These could include the fraudster recruiting their victim on social media, the victim making the payment, and any investigation, recovery of proceeds, reimbursement and prosecution. We are focusing on the parts of the APP scam 'ecosystem' that are within our remit. We are also engaging actively with government and regulatory bodies that are looking to address other parts of the fraud ecosystem (including Ofcom, the Home Office, the FCA and the National Economic Crime Centre).

The payments industry's current position

1.8 We began working on APP scams in 2016, after we received a super-complaint from the consumer organisation Which?. Which? was concerned about the lack of protection for consumers, and said payment service providers (PSPs) and payment system operators could have better incentives to manage the risks from these scams.

1.9 We set up a steering group to develop the industry's Contingent Reimbursement Model (CRM) Code, introduced in May 2019. This sets out standards for consumer protection relating to APP scams; it aims to reduce the number of APP scams and increase the proportion of victims receiving reimbursement.

1.10 PSPs have taken steps to tackle APP scams, including measures to increase customer awareness and new warning messages in the payment process. We see PSPs analysing data to identify unusual account behaviours and prevent fraudulent activity. We also know that in some cases PSPs are stopping payments to investigate further; and PSPs are reimbursing many victims (see Box 1).

Box 1: Examples of current reimbursement

- Ten PSPs have signed up to the CRM Code. Following the Code's introduction, the rate of victim reimbursement by value rose from an industry average of 19% in the first half of 2019 to 41% by Code signatories in 2020.[4]
- TSB has offered a fraud refund guarantee since 2019: the bank fully reimburses all APP scam losses unless the customer has been grossly negligent.[5] Refunds are capped at £1 million.
- Since 2021, Nationwide has provided a Scam Checker Service (SCS): members can talk to Nationwide when they're not sure about a payment they're about to make. If the SCS reviews a transaction that turns out to be a scam, Nationwide fully reimburses the customer unless the SCS advised them not to make the payment.

1.11 However, the overall level of reimbursement under the Code is still below 50% – and participation in the Code is voluntary. Some PSPs are not signatories and offer lower levels of protection, leaving many consumers exposed to significant risk.

1.12 We have recognised these issues and intervened in a number of other areas:

- We directed the six largest PSPs to implement Confirmation of Payee (CoP). This helps stop fraud by checking whether the name of a payee's account matches the name and account details the payer has entered.
- At the end of 2021 we directed Pay.UK, which operates Faster Payments, to move to the next phase of CoP, extending the service to up to 400 more PSPs – making the service available to even more payment system users.
- In November 2021, we proposed to require the largest PSPs to publish data on their performance on APP scams and reimbursement; this will begin in 2023.[6]
- We also set out our position that all consumers should benefit from reimbursement protections (noting that we could not require this under existing legislation).
- We have asked industry to improve intelligence sharing, to improve detection and prevention of APP scams.

1.13 The industry needs to do more to prevent APP scams. This includes identifying potentially fraudulent payments before they are sent, and preventing fraudsters receiving payments in UK bank accounts. We think that the Faster Payments ecosystem as a whole – Pay.UK and PSPs – needs to work together to prevent harm to consumers who use the payment system.

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4 Lending Standards Board, *Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams* (January 2021).

5 TSB exemplifies gross negligence as repeatedly ignoring safety advice.

6 CP21/10, *Authorised push payment (APP) scams* (November 2021)

1.14 In July 2022, the government published its Financial Services and Markets Bill. This would allow us to use our regulatory powers to require PSPs to reimburse APP scam victims. It would also place a duty on us to take regulatory action.

> ***'We need to make it harder for criminals to defraud people using the payment systems we regulate.'***
>
> *The PSR Strategy*

Our proposals: mandatory reimbursement and allocating costs

1.15 We want the payments industry to change the way it manages APP scams. We are proposing measures to:

- require reimbursement
- improve the level of protection for APP scam victims
- incentivise PSPs to prevent APP scams, whether as a sending PSP (which has the account the payment is made **from**) or a receiving PSP (which has the account the payment is made **to**)

These measures aim to protect people from scams and build their confidence in UK payment systems.

Mandatory reimbursement

1.16 We propose to require all PSPs sending payments over Faster Payments to fully reimburse APP scam victims, with only limited exceptions. This will apply to consumers, micro-enterprises and charities.[7]

1.17 The exceptions will include scams where the consumer is involved in the fraud themselves, or where they have acted with gross negligence. The exception for gross negligence is a high bar, which we expect will apply in only a small minority of cases. It would not apply where a consumer was vulnerable (we explain how we define this in Chapter 4).

1.18 The sending PSP will have to reimburse the victim as soon as possible, and no more than 48 hours from the fraud being reported. If the PSP has evidence or reasonable grounds for suspicion of either first party fraud or gross negligence, it will have more time to investigate and can delay the payment.

7 We refer to these from now on as consumers.

1.19 We propose to allow PSPs to:

- have a minimum threshold for a reimbursement claim (of no more than £100)
- withhold an 'excess' (of no more than £35)
- set a time limit for claims (of no less than 13 months)

These options may help PSPs ensure their customers take care in making small payments, minimise claims for civil disputes and maintain proportionate costs, while protecting consumers appropriately. We expect different PSPs to apply these options in different ways, reflecting factors such as competition and operational efficiency.

1.20 We propose to include all categories of APP scam in the rules on mandatory reimbursement. Every type of APP scam causes significant harm, and they all involve payments to PSP accounts controlled by fraudsters.

Allocating the costs of reimbursement

1.21 Both sending and receiving PSPs can take steps to detect potential frauds, and can stop payments or block accounts if they suspect fraud. Currently, sending PSPs pick up the vast majority of the costs of reimbursement under the CRM Code (over 95%). This means receiving banks do not have strong incentives to prevent fraud and stop fraudsters controlling their accounts.

1.22 We propose to allocate the costs of reimbursement equally between sending and receiving PSPs, with a default 50:50 split. PSPs can use a dispute management process to adjust the allocation, to better reflect the steps each PSP took to prevent the scam. We don't intend the 50:50 default to be a fine-tuned allocation, but to provide adequate incentives for both sending and receiving PSPs.

How we propose to implement these requirements

1.23 Our vision is for Pay.UK to make, maintain, monitor and enforce comprehensive payment system rules that protect consumers and prevent fraud from entering the system. However, we recognise that there are constraints on Pay.UK's ability to implement this from the outset.

1.24 We expect Pay.UK to consider how quickly it can implement our vision for Faster Payments scheme rules[8] and its role, and what interim arrangements it may need. Pay.UK is also developing the UK New Payments Architecture (NPA), which will replace Faster Payments in the next few years; we expect that the NPA's rules and standards will be fully consistent with our vision for Pay.UK's role.

8 'Scheme rules' are the rules for participation in the payment system.

1.25 In the short term, there may be a case for alternative options for implementing some elements of mandatory reimbursement. These include monitoring and enforcing compliance, and applying rules to indirect PSPs (which provide accounts through another PSP's connection to Faster Payments).

1.26 We would like to see our core requirements for mandatory reimbursement in place for consumers as soon as possible, and no later than during 2024. In the meantime, PSPs should continue to develop their fraud detection and prevention arrangements as quickly as possible.

Figure 2: Steps to implementing our proposals

Financial Services Bill introduced in Parliament	Consultation period	Industry engagement	Draft regulatory instruments	Final policy statement	Legislation in force	Implementation
20 July 2022	29 September – 8 weeks	Industry roundtable discussions				

1.27 Our goal is to significantly reduce the levels of APP scams. These measures will provide greater protection for consumers, ensuring that any victims get their money back (with limited exceptions). They will also incentivise PSPs to improve their fraud prevention capabilities, both for incoming and outgoing payments.

1.28 We understand there are wider implications of this proposal and expect that consumers will see a shift over time in how a current account operates. These measures are likely to lead to account providers intervening more to prevent fraud, much as is the case for card payments at the moment.

1.29 We believe that our proposals will help deliver a step change, making it harder for criminals to operate on the payment systems we regulate.

Your views

1.30 We would like your views on the issues set out in this consultation by 25 November 2022. We welcome feedback from all stakeholders and interested parties, not only entities that we regulate.

1.31 Please provide your feedback by emailing us at **appscams@psr.org.uk**. We would be grateful if you could provide your response in a Word document (rather than, or as well as, a PDF).

1.32 We will make all non-confidential responses available for public inspection. If your submission includes confidential information, please also provide a non-confidential version suitable for publication.

1.33 We will take all responses fully into account. We will set out our policy position and accompanying action in the first half of 2023.

2 Introduction

APP scams continue to grow. We identified concerns about outcomes under the current APP scams framework. We want to see more APP scams prevented and more victims reimbursed. In our November consultation we said we wanted a mandatory broadening of reimbursement. In May, the Treasury announced its intention to legislate to allow the PSR to require victim reimbursement for APP scams. We are consulting on the regulatory action we propose to take.

Background

2.1 A push payment is made when someone authorises their payment service provider (PSP) to send money to a payee's account. In an authorised push payment (APP) scam, someone is tricked into making a push payment to an account under a fraudster's control. APP scams cause significant harm. In 2021, there were around 189,000 reported APP scam cases on personal accounts (an increase of 30% on 2020), with a total value of £506 million (a 46% increase on 2020).[9] APP scams have increased year-on-year since UK Finance first published losses from APP scams in 2017. Many cases go unreported, so the real figures are likely to be higher.

2.2 **Examples of APP scams**

A customer sees a holiday advertisement on a social media platform. They click the link on the advert taking them to a website that appears completely legitimate. The customer decides to purchase the holiday, and does so via a bank transfer. A few days later, after not receiving much information and becoming increasingly concerned, they realise they have been a victim of a scam. The customer suffers a loss of £4,500.

Through a dating app, a customer is befriended by an individual who works overseas. Over months they build what appears to be a genuine relationship. In time the individual says they have fallen ill and, due to being overseas and the high cost of care, they are struggling to cover medical costs. Concerned, the customer sends multiple payments to help pay for the supposed medical care. Requests then follow for money to pay for flights, for the individual to visit the UK. After numerous payments being sent, the customer realises they are never going to see the individual, who is a fraudster, and they have fallen victim to a romance scam. The customer suffers a loss of over £15,000.

9 UK Finance, *Annual fraud report – The definitive overview of payment industry fraud in 2021* (August 2022).

2.3 Payment systems should be safe to use. We want PSPs to act to prevent APP scams, and to ensure that victims are reimbursed.

The Contingent Reimbursement Model (CRM) Code

2.4 So far, we have advocated industry-led approaches. This is mainly because of statutory restrictions on the actions we can take directly. In 2018, we set up a steering group of industry and consumer representatives, led by an independent chair, to develop a voluntary industry code of practice. This led to the Contingent Reimbursement Model (CRM) Code being introduced in May 2019.

2.5 The CRM Code aims to protect more consumers from APP scams, by reducing the number of scams and by increasing the number of victims reimbursed. The Code places responsibility on PSPs, where they are well placed to act and should meet standards for protecting consumers and reimbursing them, while allowing PSPs to take account of steps that consumers have taken to protect themselves.

2.6 Before the CRM Code came into force in May 2019, there was no systematic protection for victims, and the incentives for PSPs to prevent APP scams were weak. Reimbursement levels were significantly lower than they are now. In its review of the Code, the Lending Standards Board (LSB) reported[10] that the pre-Code industry average reimbursement rate by value was 19% in the first half of 2019; in 2020, for signatory PSPs following the introduction of the CRM Code, the rate was 41%. The CRM Code has begun to build momentum for improved protection of consumers and prevention of APP scams.

Issues with the current framework

2.7 APP scams continue to grow. This is true of Code and non-Code PSPs alike, which suggests the Code is not giving PSPs enough incentives to tackle fraud. More needs to be done to deliver consistent and better outcomes for victims. Everyone who plays a role in the problem – including PSPs, social media platforms and telecoms firms – has a responsibility to find the solutions.

2.8 We identified a number of concerns about outcomes under the current APP scams framework, including the following:

- Participation in the Code is voluntary. Ten PSP groups, including most of the big high street banks, are signatories to the Code. Many PSPs have not signed up to the Code, and there is considerable variation in reimbursement rates between Code signatories. Consumers get different levels of protection against potentially life-changing APP scam losses depending on where they bank, and banks face varying levels of incentive to prevent scams.

10 Lending Standards Board, *Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams* (January 2021).

- These differences create opportunities for scammers to switch to targeting non-Code signatory PSPs if they have less relevant warnings and support in place.
- The overall level of reimbursement under the CRM Code has been less than 50%.[11]
- There is very limited liability on receiving PSPs, so their incentives to address fraudster-controlled accounts are weak.

Our previous consultation and new legislation

2.9 In our consultation in November,[12] we consulted on a broad package of reforms to address the harms from APP scams. These included three specific measures:

- **Measure 1 – Publishing scam data:** We proposed to require the largest PSP groups to publish a balanced scorecard of data every six months. This would set out their performance in relation to APP scams, to provide greater transparency and give them incentives to improve their performance.
- **Measure 2 – Intelligence sharing:** We tasked the industry to improve intelligence sharing between PSPs about the riskiness of payments, to help prevent scams.
- **Measure 3 – Wider reimbursement:** We said we wanted all PSPs to give consumers reimbursement protections. We asked for views on the approach we could take to make this mandatory. We noted that we could not do this under the Payment Services Regulations 2017 (PSRs 2017), so legislation would have to change first.

2.10 In May, the Treasury announced[13] plans for legislation that would allow us to require PSPs to reimburse APP scam victims. In July, it published the Financial Services and Markets Bill. This has two key components related to APP scams:

- It clarifies Regulation 90 of the PSRs 2017, to make clear that we may use our regulatory powers to require reimbursement.
- It requires us to take regulatory action within prescribed timescales. Specifically, we must consult on a draft regulatory requirement within two months of the legislation coming into force, and impose a regulatory requirement within six months.

11 Lending Standards Board, *Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams* (January 2021).

12 PSR CP21/10, *Authorised push payment (APP) scams* (November 2021).

13 HM Treasury, *Government approach to authorised push payment scam reimbursement* (May 2022).

Key outcomes we want to see

2.11 In January 2022, we published our five-year Strategy, setting out the outcomes we want to see in payments. One outcome is that people and businesses are adequately protected when they use payment systems and services, so they can use them with confidence. Key outcomes we want to see from our proposals in this consultation include:

- **Fewer APP scams:** The best result for consumers and for PSPs is a decrease in the number of APP scams. This avoids distress, disruption and financial loss for all involved. It also prevents money ending up in the hands of criminals.
- **Improved protection for payment system users:** We want more victims of APP scams consistently receiving higher levels of reimbursement of their losses. All consumers should enjoy protection, regardless of their PSP.
- **Effective incentives on PSPs:** We want PSPs to have financial incentives to further focus resources on preventing the scams that cause the highest harm.
- **Increased confidence in Faster Payments:** As a result of better prevention and protection, users maintain confidence in the payment system, helping it to be competitive.
- **Agile payment scheme rules:** We want the payment system operator to be able to manage evolving fraud threats effectively.

The scope of our remit on APP scams

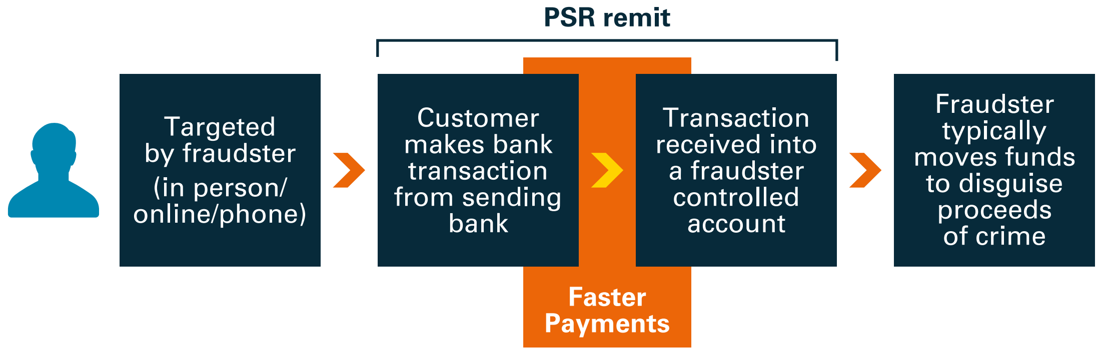
2.12 APP scams involve a range of tactics by fraudsters, including fake adverts on social media platforms, malware installation, and online, telephone and face-to-face 'recruitment' and 'social engineering'.

2.13 A single scam also typically involves multiple steps, including:

- the fraudster gaining control of a bank account
- victim recruitment
- social engineering of the victim into making a payment
- the victim instructing their bank to make the payment
- the bank sending the payment
- the payment being received into the account controlled by the fraudster

- the fraudster moving the money out (potentially via multiple accounts)
- the customer realising they have been scammed and reporting it
- any investigation, recovery of proceeds, reimbursement and prosecution.

Figure 3: A typical APP scam payment journey



2.14 We are focusing on the parts of the APP scam 'ecosystem' that are within our remit. We are also engaging actively with those government and regulatory bodies who are looking to address other parts of the fraud ecosystem including Ofcom, the Home Office, the FCA and the National Economic Crime Centre.

This consultation

2.15 In this consultation paper, we are asking for views on the regulatory actions we propose to take. These build on our November consultation on Measure 3 (reimbursement) options as well as on our extensive further thinking and stakeholder engagement, and they respond to the duty proposed in the Financial Services and Markets Bill. They aim to help achieve the key outcomes we want to see.

2.16 We said in our November consultation that, while we had not seen evidence that the balance of liability in the CRM Code was wrong, over time we might expect to consider the issue in light of experience. Since then, reimbursement of total APP scam losses has remained below 50%. Industry initiatives, including for improved data-sharing (Measure 2), continue to improve PSPs' ability to detect and prevent frauds. The proposed legislative changes in the Financial Services and Markets Bill also provide a new context for considering the balance of liability in relation to reimbursement. Our proposals in this consultation have therefore evolved significantly from November.

2.17 In parallel to this consultation, we are also taking forward work on Measures 1 (publication of performance data) and 2 (data sharing):

- **Measure 1:** Responses to the November consultation raised a number of important issues. We engaged with stakeholders to understand these better and find solutions. And we ran a voluntary trial of reporting on APP scams data, with seven PSPs participating. This took place during June 2022, with data reported on transactions from July to December 2021. During July and August, we further engaged with PSPs and trade bodies to discuss the lessons learned from the trial. This will inform development of our final guidance and data template. We plan to will publish these, along with a Policy Statement, before the end of 2022. We will ask directed PSPs to submit data to us during spring 2023, and we will publish the first set of data in summer 2023.

- **Measure 2:** Progress has been made on the industry proof of concept since November. A group of PSPs shared a set of historical data on account attributes to test how useful this data was in identifying scam payments. Provisional results were positive, and UK Finance and Pay.UK are now building rules and standards to allow PSPs to share data on a real-time basis. Some PSPs are moving to a second stage of the proof of concept by swapping real-time data, aiming to identify and iron out any issues with the proposed system. We want PSPs to implement the capability to send and receive the data – that will enable them to better identify and stop scam payments – in 2023.

- **Confirmation of Payee (CoP):** Following our consultation at the end of 2021 we directed Pay.UK to move to the next phase of CoP, extending the service to up to 400 more PSPs – making it available to even more payment systems users. In November 2021, we proposed to require the largest PSPs to publish data on their performance on APP scams and reimbursement, and this will begin in 2023.

2.18 The rest of this consultation paper is set out as follows:

- **Chapter 3** outlines our proposals at a high level and the impacts we expect.

PART A: The reimbursement requirements we propose

- **Chapter 4** sets out the rules for mandatory reimbursement of customers that we propose to require.

- **Chapter 5** sets out the rules for allocation of liability between firms that we propose to require.

PART B: How we propose to implement our requirements

- **Chapter 6** sets out our long-term vision for comprehensive scheme rules for implementing PSPs' obligations.

- **Chapter 7** sets out proposals and options for short-term implementation of our proposals for mandatory reimbursement.

- **Chapter 8** sets out the next steps, including how to respond to this consultation, our timetable and a list of the consultation questions.

ANNEXES

- **Annex 1** summarises the feedback we received to our November consultation on Measure 3 (reimbursement), and our responses to that feedback.
- **Annex 2** contains the initial cost benefit analysis of our proposals.
- **Annex 3** sets out our assessment of the likely equality impacts and rationale for our proposals, in line with our public sector equality duty under the Equality Act.

3 Outline and impact of our proposals

We are consulting on an initial package of requirements, covering:

- mandatory reimbursement for all types of APP scams by all PSPs sending payments over Faster Payments
- shared liability between sending and receiving PSPs

As a result we expect a much greater proportion of consumers' losses will be reimbursed than they are today. Our proposals will increase the cost of APP scams reimbursement for most PSPs, and are intended to incentivise both sending and receiving PSPs to do more to prevent APP scams. PSPs can mitigate their increased reimbursement costs by preventing more scams.

Introduction

3.1 This chapter outlines, at a high level, our proposals for mandatory reimbursement by PSPs and the potential impacts.

3.2 In Annex 1, we summarise the feedback we received on Measures 3A and 3B (on reimbursement) in our November consultation and our response. Having assessed the consultation feedback and engaged extensively across a broad range of stakeholders, our thinking has progressed significantly, and we have developed the proposals in this consultation.

3.3 In addition to the payments industry, others should take actions to reduce APP scams, including the digital platforms where many scams originate. This was highlighted in responses to our November consultation. We recognise the work being undertaken by other authorities in this area and we will continue to share information to help.

High-level outline of our proposals

3.4 We want Pay.UK to make, maintain and enforce comprehensive and effective scheme rules that address the risks to consumers using Faster Payments. These rules should provide appropriately high levels of protection for all consumers and allocate liability between PSPs in ways that best incentivise prevention. This may take time to achieve.

3.5 In this consultation we propose an initial package of requirements that will quickly increase protection for consumers and better allocate incentives for PSPs. Our proposals then allow for progression over time towards longer-term arrangements.

3.6 We propose mandatory reimbursement of consumers for all types of APP scams, and shared liability between sending and receiving PSPs. Specifically, we propose that:

- an APP scam victim's PSP (the sending PSP) must reimburse them, except in cases of first party fraud or gross negligence (unless the victim is a vulnerable consumer)
- the sending PSP must reimburse the victim within 48 hours of the fraud being reported, unless the sending PSP has evidence or reasonable grounds for suspicion of either first party fraud or gross negligence (it will then have more time to investigate)
- PSPs can set a fixed 'excess' of up to £35, and a minimum threshold claim for reimbursement of up to £100
- the costs of reimbursement (as well as any repatriated funds) are shared equally between sending and receiving PSPs by default; PSPs can use a dispute resolution process to refine the allocation of reimbursement costs to better reflect the steps each PSP took to prevent the scam
- PSPs can apply a time limit on claims of no less than 13 months from the date of the payment
- both direct Faster Payments participants and indirect PSPs will be covered by the requirements

3.7 Part A (Chapters 4 and 5) of this consultation describes in more detail the rules that we propose are put in place.

3.8 Our proposed high-level approach to implementing our proposals is as follows:

- Our vision is for Pay.UK to run the Faster Payments system so that consumers are protected, and fraud is prevented from entering the system. Pay.UK's role would include making, maintaining, refining, monitoring, and enforcing compliance with comprehensive scheme rules that address fraud risks in the system.
- However, we recognise that some elements of our vision for Pay.UK's role on APP scams represent a significant change from the current position on Faster Payments, and there are constraints on Pay.UK's ability to implement them right from the outset. We are discussing this proposed vision with Pay.UK and through this conversation, as well as our consultation process, we will explore the changes that would be necessary to support this expanded role. We expect that the NPA's new rules and standards will be fully consistent with our vision for Pay.UK's role.
- In the short term, there may be a case for considering alternative options for implementing some elements of our requirements for mandatory reimbursement – on monitoring, on enforcement of compliance and on applying rules to indirect participants.

3.9 Part B (Chapters 6 and 7) describes in more detail how we propose rules for reimbursement are implemented.

Potential impact of our proposals on consumers

Expected benefits for consumers

3.10 Following implementation of our proposals, a much greater proportion of consumers' losses will be reimbursed than they are today, because:

- all PSPs will be required to reimburse victims, compared to the voluntary commitments of just ten signatories to the CRM Code, which means coverage of all payments over Faster Payments[14]
- there will be a higher bar for PSPs not to reimburse than is currently the case under the CRM Code
- where consumers are reimbursed, except where PSPs choose to apply an excess of up to £35, consumers will receive full refunds, unlike under the CRM Code where many consumers receive only partial reimbursement (more than one third of the 46% of cases reimbursed under the Code in 2020 were only partially refunded[15])
- the 'excess' we propose would, at most, represent only 2% of APP scam losses by value (for example, if set at £35 by all PSPs)
- where PSPs chose to apply a minimum threshold of up to £100, only a small proportion of the total value of scam losses would be affected (since APP scams under £1,000 represented only 8% of APP scam losses by value in 2021[16])

3.11 Overall, we would expect reimbursement levels to increase very significantly from under 50% of cases being reimbursed under the CRM Code.[17]

3.12 We would expect increased efforts by PSPs to prevent APP scams, incentivised by the costs of more reimbursement. Preventing more APP scams in the first place will reduce the emotional distress caused to victims. A greater emphasis on preventing APP scams will be aided by more tools and processes for detecting APP scams, including industry initiatives for improved intelligence-sharing (under Measure 2) and the FCA's and PSR's tech sprint on fraud prevention.

Other potential consequences for consumers

3.1 Our proposals should mean that PSPs refuse more payment orders than now – those that they consider suspicious. This could mean that more genuine payments are also stopped

14 CHAPS currently accounts for only around 0.2% of the number of APP scams.

15 Lending Standards Board, *Review of the Contingent Reimbursement Model Code for Authorised Push Payment Scams* (January 2021).

16 UK Finance, *Annual Fraud Report* (August 2022).

17 We are also aware that some victims refer cases to the FOS which may then require reimbursement.

because they have specific elements that trigger PSPs' detection processes or are considered higher risk. Our view is that additional friction for a small proportion of payments is proportionate to preventing APP scams and achieving increased consumer protection.

3.2 Industry initiatives to improve data sharing between PSPs should help to minimise the number of payments stopped unnecessarily.

3.3 In response to requirements for mandatory reimbursement, some PSPs might consider restricting services to certain consumers, such as older consumers, because they may be perceived as more likely to fall victim to APP scams. We have considered this risk as part of our equality impact assessment (see Annex 3). PSPs should not refuse or deny banking or payment services to consumers more at risk of becoming victims of APP scams to reduce numbers of APP scams. PSPs should treat current and prospective customers according to their obligations in the Equality Act 2010.

3.4 If our proposals are successful in incentivising reduced APP scams, there is potential for fraudsters to migrate to other payment systems, including cards. Card systems have existing consumer protections in place, and we would monitor any trend for increased card fraud to inform any action that was needed.

Question 1: Do you have views on the impact of our proposals on consumers?

Potential impact of our proposals on PSPs

3.5 Our proposals will increase the cost of APP scams reimbursement for most PSPs. They will also redistribute the costs between sending and receiving PSPs, because under the CRM Code most of the cost of reimbursement falls on sending PSPs and many receiving PSPs are not signatories to the Code.

3.6 The increased cost is an intended effect of our proposals. Mandatory reimbursement, as well as protecting victims, is intended to incentivise further scam prevention by both sending and receiving PSPs. We would like to see as many APP scams as possible prevented so reimbursement is not required. PSPs have the ability to do more to prevent scams and thus mitigate their increased reimbursement costs:

- There is substantial variation between PSPs' current APP scam rates. Based on data for a number of large PSPs, the number of APP scams per million payments sent was seven times higher in the worst-performing than in the best-performing PSP. Some PSPs received more than ten times the rate of APP scam payments than others. This suggests significant scope for many PSPs to improve performance in reducing APP scams. We highlight initiatives by individual PSPs and by the industry, including in Chapter 4.

- The industry's work on increased intelligence sharing (Measure 2) will improve fraud detection and prevention efforts leading to a reduction in the ability of fraudsters to operate in Faster Payments.
- PSPs may refuse payment orders and block accounts that they consider suspicious. The FCA, as the competent authority for the PSRs 2017, has set out in guidance[18] its view that Regulation 82 of the PSRs enables PSPs, in exceptional circumstances, to refuse a payment order provided that its framework contract allows refusal on the relevant grounds.

3.7 Respondents to our November consultation highlighted the potential cost implications of our reimbursement proposals for small PSPs and for certain business models (see Annex 1). If such PSPs have a particularly high proportion of fraudster-controlled accounts, they could find that they have high costs of reimbursement under our proposals. They could also find that other PSPs, in response to suspicious payments, stop more payments to their accounts. Our view is that this would reflect the effective operation of the incentives we intend – and such PSPs should respond by putting in place more effective fraud controls.

3.8 If reimbursement costs were large enough for some small PSPs, this could, in principle, have prudential implications. We do not consider prudential risks would arise for larger PSPs, many of which are already CRM Code signatories. We continue to work with the FCA and the Prudential Regulation Authority (PRA) on how risks to individual small PSPs would be monitored and managed.

3.9 Fundamentally, we want all PSPs to take steps to reduce fraud in the system. Having robust fraud controls should effectively be a condition of operating in UK payment systems. If fraud is prevalent, it harms consumers, but also damages consumers' confidence in using the payment system, making it less attractive for PSPs.

Question 2: Do you have views on the impact of our proposals on PSPs?

18 FCA , *Payment Services and Electronic Money – Our Approach: The FCA's role under the Payment Services Regulations 2017 and the Electronic Money Regulations 2011* (November 2021).

PART A:
The reimbursement requirements we propose

4 Mandatory reimbursement for consumers

We propose rules should be put in place to provide for:

- mandatory reimbursement by the sending PSP of consumers, micro-enterprises and charities who fall victim to APP scams over Faster Payments, except in cases of first party fraud or gross negligence (unless the victim is a vulnerable consumer)
- an ability for PSPs to set a fixed 'excess' of up to £35 and a minimum threshold claim for reimbursement of up to £100
- an ability for PSPs to apply a time limit on claims of no less than 13 months from the date of the payment
- both direct Faster Payments participants and indirect PSPs to be covered by the requirements

Introduction

4.1 This chapter sets out our proposed requirements for reimbursing APP scam victims.

4.2 We propose mandatory reimbursement rules, requiring all PSPs sending payments over Faster Payments to fully reimburse all their consumers[19] who are victims of APP scams. There would be limited exceptions to ensure that consumers have appropriate incentives to exercise caution and that the requirements are proportionate.

19 Consumers, micro-enterprises and charities.

The scope of the reimbursement requirements

Payers in scope

4.3 We propose that our reimbursement requirements cover all payers who are consumers[20], micro-enterprises[21] or charities[22], as defined in regulation 2(1) of the PSRs 2017.[23] This is the same coverage of payers as in the CRM Code.

4.4 Larger business payers can be expected to have greater capability to protect themselves from APP scams, and it would not be proportionate to require PSPs to reimburse such businesses for their losses.

Payments and payment service providers in scope

4.5 Our aim is to protect all consumers who fall victim to APP scams, regardless of their PSP. This includes ensuring that a consumer banking with an indirect PSP is not excluded from reimbursement simply because their PSP uses an indirect access provider (IAP) to make and receive payments. A large proportion of respondents to our November consultation wanted more or all PSPs to be included in our reimbursement proposals (see Annex 1).

4.6 We propose that our requirements for mandatory reimbursement cover all APP scam payments over Faster Payments.[24] They would therefore apply to all directly connected PSP participants sending payments over Faster Payments, as well as PSPs indirectly connected via an IAP. (A significant proportion of Faster Payments transactions are sent from or to a PSP that is an indirect participant.)

4.7 The CRM Code applies to Faster Payments and CHAPS transactions, as well as 'on-us' payments (payments where the sending and receiving PSPs are part of the same group).

4.8 Our powers do not extend to regulating on-us payments, as these payments are not transferred via a payment system designated under the Financial Services (Banking Reform) Act 2013 (FSBRA). But we have a clear expectation that PSPs should reimburse on-us APP scam payments in the same way as payments made via Faster Payments. Victims are impacted in the same way whether the scam payment is on-us or via Faster Payments. They should not have less right to reimbursement if the fraudster uses an account provided by the victim's own PSP. If necessary, the PSR and FCA may consider what further complementary guidance or rules may be required.

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20 A consumer is an individual who, in contracts for payment services to which the PSRs 2017 apply, is acting for purposes other than a trade, business or profession.

21 A micro-enterprise is an enterprise that employs fewer than ten persons and whose annual turnover and/or annual balance sheet total does not exceed €2 million.

22 A charity is body with annual income of less than £1 million and is a charity as defined in relevant legislation in the UK.

23 Payers covered by our proposed requirements are referred to as 'consumers' from now on.

24 Including PISP-initiated payments.

4.9 Around 0.2% of APP scam payments are made over CHAPS (4% by value).[25] We are working closely with the Bank of England on the proposals in this consultation. The Bank is considering the most appropriate approach to APP scam payments made over CHAPS.

4.10 We are working with the Bank – in its capacities as the operator of CHAPS and regulator of Pay.UK – and the FCA on aligning reimbursement requirements across Faster Payments, CHAPS and on-us payments.

APP scams in scope

4.11 The definition of an APP scam case in the Financial Services and Markets Bill s.62(2) is '(a) the case relates to a payment order executed over the Faster Payments Scheme, and (b) the payment order was executed subsequent to fraud or dishonesty'. We propose that the rules on mandatory reimbursement apply to authorised payments (that is, where the payer has given their consent) that meet this definition. Our proposed reimbursement rules would apply only to APP scams where the most recent payment was authorised after our regulatory requirements came into force.

4.12 We think this definition is broadly consistent with the definition in CRM Code, covering cases where the consumer was deceived into transferring the funds to a different person than they intended and where they transferred funds to a person for what they believed was a legitimate purpose, but which was in fact fraudulent.

4.13 Under the proposed definition, mandatory reimbursement would not apply to private civil disputes, such as where a consumer has paid a legitimate supplier for goods or services but has not received them, they are defective in some way, or the consumer is otherwise dissatisfied with the supplier.

4.14 We do not propose that any categories of APP scam are excluded from mandatory reimbursement. Significant harms arise from all types of APP scam and all types involve payments to PSP accounts controlled by fraudsters.

4.15 We recognise, however, that the lowest value scam payments – typically, though not exclusively, made as part of purchase scams – raise particular issues about PSPs' ability to detect and investigate them effectively, and the proportionality of mandatory reimbursement. Our approach to the lowest value scams is discussed in the sections below, where we discuss allowing an 'excess' and minimum claim threshold.

Question 3: **Do you have views on the scope we propose for our requirements on reimbursement?**

25 UK Finance, *Annual fraud report – The definitive overview of payment industry fraud in 2021* (August 2022).

Exceptions for first party fraud and gross negligence

4.16 We have considered the case for exceptions to mandatory reimbursement that a PSP could apply when considering a consumer's claim for reimbursement.

4.17 The first exception we propose to mandatory reimbursement is where the consumer themself has acted fraudulently ('first party fraud'). It is not the purpose of our proposed requirements to refund consumers who have been complicit in the fraud.

4.18 There is a potential risk that, if consumers are more confident of being reimbursed, they will take less care in ensuring that their payee is not a fraudster (see Box 2). We have therefore considered the case for a second exception to mandatory reimbursement where the consumer does not exercise adequate caution.

Box 2: Customer caution

We are not aware of conclusive evidence that, if consumers are more confident of being reimbursed, they will take less care in ensuring that their payee is not a fraudster. TSB told us it had not identified evidence for customers taking less care since introducing its refund guarantee.

The question of a consumer taking less care would not arise in many or most cases because the consumer is simply unaware there is any risk associated with the payment. In other cases, we consider there are clear incentives on consumers to be cautious even if they perceive that reimbursement was likely in the case of a fraud, particularly for transactions of significant value. People do not want to be scammed, and fraud is emotionally distressing.

Nevertheless, the evidence we have is limited. For example, we are not aware of relevant examples from other countries of the impact of any mandatory reimbursement for APP scams. We would welcome any concrete, including quantitative, evidence on the risks that consumers would take less care.

Since we cannot, at present, rule out this risk, we have considered an exception to mandatory reimbursement to incentivise consumers to continue to exercise caution.

4.19 We recognise that, when investigating an APP scam case, it can be hard to distinguish social engineering and sophisticated scam tactics from a lack of care by the consumer. A consumer caution exception could put inappropriate responsibility on consumers to spot sophisticated scams, risk PSPs blaming genuine victims for not taking sufficient care and limit the incentives on PSPs to take steps to detect and prevent fraud.

4.20 However, on balance, we propose that there should be a consumer caution exception – but one set at a high bar, higher than in the CRM Code. A high bar exception would signal to consumers that there remained a degree of risk that they may not be reimbursed – to provide incentives to continue to take care – while ensuring that victims are reimbursed in the vast majority of cases.

4.21 We will explore whether requirements for mandatory reimbursement, including the exception we propose, lead to any significantly reduced customer caution, as part of a post-implementation review, discussed in Chapter 7.

4.22 For a consumer caution exception to provide an effective incentive, consumers must expect that PSPs may investigate the circumstances of their claims. For the lowest value scams, PSPs may not be expected to fully investigate each claim. We therefore consider how PSPs could encourage consumers to take care when making low value payments in the sections below, where we discuss allowing an 'excess' and minimum claim threshold.

Gross negligence

4.23 We propose that the consumer caution exception to mandatory reimbursement should be triggered where the consumer acts with 'gross negligence'.[26] Gross negligence is already an exception to PSP liability for unauthorised frauds under section 77(3) of the PSRs 2017, and is one of the exceptions to reimbursement in the CRM Code.

4.24 Gross negligence is a high bar. The FCA has said in guidance: 'In line with the recitals to PSD2, we interpret "gross negligence" to be a higher standard than the standard of negligence under common law. The customer needs to have shown a very significant degree of carelessness.'[27]

Vulnerable consumers

4.25 We have considered the potential impacts of our proposals on vulnerable consumers, including as part of our equality impact assessment (see Annex 3). Vulnerable consumers may be more at risk from social engineering and less able to exercise caution and to protect themselves from APP scams. There is therefore a weaker case for applying exceptions designed to incentivise consumer caution to vulnerable consumers.

4.26 The CRM Code exempts consumers who are vulnerable to APP scams from its exceptions to reimbursement including its gross negligence exception. We propose also to exempt vulnerable consumers from our proposed gross negligence exception to mandatory reimbursement, that is, a PSP must reimburse a vulnerable consumer even if

26 It could still be appropriate, in some cases, for a PSP to reimburse, or partially reimburse, a consumer who had acted with gross negligence if the PSP should clearly have detected and stopped the payment. Ultimately, this would be for FOS to determine on the circumstances of the case.

27 FCA, *Payment Services and Electronic Money – Our Approach: The FCA's role under the Payment Services Regulations 2017 and the Electronic Money Regulations 2011* (November 2021).

they have acted with gross negligence. PSPs would need to investigate a consumer's vulnerability only in the small proportion of cases where they suspected gross negligence.

4.27 The CRM Code uses the following definition of a vulnerable customer: 'A customer is vulnerable to APP scams if it would not be reasonable to expect that customer to have protected themselves, at the time of becoming victim of an APP scam, against that particular APP scam, to the extent of the impact they suffered.'[28] The FCA uses the following definition of a vulnerable customer: 'A vulnerable customer is someone who, due to their personal circumstances, is especially susceptible to harm, particularly when a firm is not acting with appropriate levels of care'.[29]

4.28 We propose to use the FCA's definition to identify those consumers vulnerable to APP scams, so that, in relation to regulatory requirements, firms are working to a single definition of vulnerability.

Guidance on gross negligence

4.29 We have considered whether we should provide guidance on the application of gross negligence to APP scams, to help PSPs in assessing claims appropriately and consistently.

4.30 Gross negligence does not have a precise meaning in common law. Immediately following implementation of our proposals there may be a degree of uncertainty in precisely how PSPs should apply the concept of gross negligence to APP scams, and this could lead to disputes.

4.31 As noted earlier, the FCA has provided high-level guidance on the interpretation of gross negligence. We do not propose to provide additional guidance because:

- what qualifies as gross negligence is likely to depend on the precise circumstances of each case
- for APP scams, it is particularly difficult to specify particular consumer actions or inactions that would qualify as gross negligence – because it typically depends on what the customer believed when they authorised the payment, often in the context of social engineering
- there is a risk that giving guidance, such as examples of what a customer would be expected to do or not do, could encourage a 'tick-box' approach to PSPs' assessment, tending to lower the gross negligence bar
- fraudsters' tactics, including the sophistication of social engineering, technologies, customer behaviour and the approaches to fraud prevention available to PSPs are likely to continue to evolve, with implications for what constitute gross negligence, making it difficult or impossible to capture in static guidance

28 Lending Standards Board, *Contingent Reimbursement Model Code for Authorised Push Payment Scams* (April 2022).

29 FCA FG21/1, *Guidance for firms on the fair treatment of vulnerable customers* (February 2021).

4.32 We recognise that disputes are likely to be brought to FOS in the early days following implementation of our proposals. Our post-implementation review (see Chapter 7) would be able to consider the application of the gross negligence exception and whether any additional guidance would be appropriate.

Question 4: **Do you have comments on our proposals:**

- **that there should be a consumer caution exception to mandatory reimbursement**
- **to use gross negligence as the consumer caution exception**
- **not to provide additional guidance on gross negligence?**

Question 5: **Do you have comments on our proposal to require reimbursement of vulnerable consumers even if they acted with gross negligence?**

Question 6: **Do you have comments on our proposal to use the FCA's definition of a vulnerable customer?**

An allowed fixed 'excess'

4.33 As noted earlier, for our proposed gross negligence exception to be an effective incentive to exercise caution, consumers must expect that PSPs may investigate the circumstances of their claim. For the lowest value scams, PSPs may not be expected to fully investigate each claim. At the same time, though we do not have conclusive evidence, consumers may take less care where the smallest value payments are involved.

4.34 If PSPs do not fully investigate the lowest value claims, there is also a higher risk that civil disputes, such as disputes with legitimate retailers, are inappropriately reimbursed by PSPs rather than resolved between the parties or under platform rules.[30]

4.35 For these reasons, we propose to permit a third exception to mandatory reimbursement – to allow PSPs not to reimburse a modest, fixed amount of the consumer's claim (akin to an 'excess' in an insurance claim).

4.36 We note that section 77 of the PSRs 2017 allows PSPs to require that a payer is liable up to £35 for losses incurred in respect of unauthorised payment transactions arising from the use of a lost or stolen payment instrument, or from the misappropriation of a payment instrument.

30 Even though some PSPs already have a policy of automatically reimbursing small APP scam claims, there is a risk that greater awareness of mandatory reimbursement could increase the numbers of claims for PSP reimbursement of civil disputes.

4.37 Allowing PSPs to implement a similar fixed[31] 'excess' – of no more than £35 – could help provide incentives for consumers to take care when making smaller payments, such as when shopping online, and to use the proper processes for resolving civil disputes. We consider that no more than £35 would be needed to provide the intended incentives in relation to payments in the lowest value scams.

4.38 We have considered the impact of any 'excess' on vulnerable consumers, including as part of our equality impact assessment (see Annex 3). We propose that PSPs would be able to exempt vulnerable consumers from any 'excess' they chose to implement.

4.39 We are particularly keen to hear stakeholders', including consumer representatives', views on this proposal.

Question 7: Do you have comments on our proposals that:

- **sending PSPs should be allowed to apply a modest fixed 'excess' to reimbursement**
- **any 'excess' should be set at no more than £35**
- **PSPs should be able to exempt vulnerable consumers from any 'excess' they apply?**

Allowed minimum and maximum thresholds

An allowed minimum threshold

4.40 We propose to allow PSPs to set a minimum threshold claim value before our proposed mandatory reimbursement rules apply, up to a level of £100. If a PSP set a minimum threshold, mandatory reimbursement would apply only if an APP scam had a total value (including all payments made as part of the scam) greater than the level of the minimum threshold. For a scam exceeding the value of any minimum threshold, the consumer would be eligible for mandatory reimbursement for the whole loss (but minus any 'excess' that the PSP applied).

4.41 Reasons for allowing PSPs to set a minimum threshold include the following:

- A minimum threshold could help to ensure that the administrative costs to PSPs of our proposals are proportionate, by limiting the total caseload of APP scam claims that need to be processed, while ensuring that losses greater than any minimum threshold (at most £100) will be reimbursed in full.

31 That is, any excess would be fixed rather than a percentage. A percentage excess that was larger for large scams would not be appropriate because the purpose any excess relates only to the lowest value scams.

- The lowest value scam payments are typically the hardest for PSPs to detect and prevent, so PSPs may have the least scope to mitigate the costs of mandatory reimbursement.

- Like our proposal to allow PSPs to set a fixed 'excess', allowing a minimum threshold could help limit the costs to PSPs, and ultimately to their customers, of reimbursing small claims that are in fact civil disputes rather than purchase scams.

4.42 We consider that a threshold of no more than £100 (which, we note, is the minimum purchase amount for the protections of section 75 of the Consumer Credit Act) would be adequate to enable PSPs to ensure proportionate costs while providing for appropriate consumer protection for lower value scams.

4.43 We have considered the impact of any 'minimum threshold' on vulnerable consumers, including as part of our equality impact assessment (see Annex 3). We propose that PSPs would be able to exempt vulnerable consumers from any minimum threshold they chose to implement.

4.44 We would review the allowed minimum threshold in our post-implementation review (see Chapter 7). This would include considering whether, following bedding-in of our mandatory reimbursement requirements and further development of PSPs' ability to detect scams, the allowed minimum threshold should be reduced or eliminated.

4.45 We are particularly keen to hear stakeholders', including consumer representatives', views on this proposal.

An allowed maximum threshold

4.46 We have also considered the case for a maximum threshold, that is, a total scam value above which mandatory reimbursement rules would not apply. Capping PSPs' liability could have prudential and other benefits. We note that TSB caps refunds under its refund guarantee at £1 million, and section 75 of the Consumer Credit Act caps liability at £30,000.

4.47 We do not propose to have a maximum threshold, because of the following:

- We would expect PSPs typically to have the strongest safeguards in place for the largest payments. Given this, if a PSP allowed a very large payment to proceed, it should be liable if the payment is an APP scam (subject to exceptions for first party fraud and gross negligence).

- In practice most PSPs' Faster Payments transactions limits are very well below £1 million.

Question 8: **Do you have comments on our proposals that:**

- **sending PSPs should be allowed to set a minimum claim threshold**
- **any threshold should be set at no more than £100**
- **PSPs should be able to exempt vulnerable consumers from any threshold they set?**

Question 9: **Do you have comments on our proposal not to have a maximum threshold?**

A time limit for making claims for reimbursement

4.48 We propose that PSPs may set a time-limit for consumers to make a claim for mandatory reimbursement, with any time-limit set no less than 13 months from the final payment involved in the APP scam.

4.49 Allowing PSPs to set a time-limit would ensure that mandatory reimbursement did not lead to the build-up of open-ended liabilities on PSPs. We think the vast majority of consumers would become aware that they were the victim of a scam, and be able to make a claim, well within 13 months. This is the same as the time-limit for claims for refunds of unauthorised payments under the PSRs 2017.

4.50 We also note that consumers may appeal to the Financial Ombudsman up to six years from a problem happening, or longer, if still within three years of the consumer becoming aware (or of when the consumer should reasonably have become aware) of the problem.

Question 10: **Do you have comments on our proposals that:**

- **sending PSPs should be allowed to set a time-limit for claims for mandatory reimbursement**
- **any time-limit should be set at no less than 13 months?**

5 Allocation of reimbursement costs

We propose rules should be put in place to provide for:

- a requirement that reimbursement by the sending PSP will take place within 48 hours of the fraud being reported, unless the sending PSP has evidence or reasonable grounds for suspicion of either first party fraud or gross negligence (it will then have more time to investigate)
- the sharing of the costs of reimbursement (as well as any repatriated funds) equally between sending and receiving PSPs by default
- PSPs to use a dispute resolution process to refine the allocation of reimbursement costs to better reflect the steps each PSP took to prevent the scam

Introduction

5.1 This chapter describes how we propose that the costs of mandatory reimbursement are allocated.

5.2 Current arrangements in the CRM Code for apportioning fault between parties and costs between PSPs provide limited incentives to tackle APP fraud – particularly on receiving PSPs who contribute less than 5% on average to reimbursement costs.[32]

5.3 We propose that, as a default, the sending and receiving PSP should share the cost of reimbursement 50:50.

Responsibility for reimbursing the consumer

5.4 We propose that the sending PSP is responsible for reimbursing the victim of the APP scam. The sending PSP has a direct relationship with the consumer. It is best placed to assess the consumer's claim for reimbursement, including whether the proposed exceptions for first party fraud or gross negligence apply.

5.5 We propose that the reimbursement should be made as soon possible, and no later than 48 hours after a claim is made.

32 Data supplied by UK Finance for January to June 2021.

5.6 There will be exceptions. Where a PSP can evidence suspicions of first party fraud or gross negligence, the PSP may either refuse reimbursement or take more time to investigate whether those suspicions are founded. We expect this to be in a small minority of cases. We envisage that a PSP would need to notify Pay.UK in cases where it proposed to take longer to investigate, a standard of evidence would need to be reached and the further investigation should be time limited.

Question 11: Do you have comments on our proposals that:

- **the sending PSP is responsible for reimbursing the consumer**
- **reimbursement should be as soon possible, and no later than 48 hours after a claim is made, unless the PSP can evidence suspicions of first party fraud or gross negligence?**

Question 12: What standard of evidence for gross negligence or first party fraud would be sufficient to enable a PSP to take more time to investigate, and how long should the PSP have to investigate in those circumstances?

Allocation of reimbursement costs

5.7 Neither sending nor receiving PSPs can, at present, reliably detect 100% of APP scams, but both can take steps to detect potential frauds and can refuse payment orders or block accounts if they suspect fraud. Yet, under the CRM Code, sending PSPs pick up the vast majority (over 95%) of the costs of reimbursement, so there are weak financial incentives on receiving PSPs. Respondents to our November consultation highlighted the need to ensure receiving PSPs were appropriately included in our reimbursement proposals (see Annex 1). Receiving PSPs are providing the accounts that fraudsters control and that they use to implement APP scams. Receiving PSPs need adequate incentives to detect frauds and prevent fraud losses.

5.8 We propose that the cost of mandatory reimbursement of losses from an APP scam is, as a default, shared 50:50 between the sending and receiving PSP. The 50:50 default is not an attempt at a fine-tuned allocation. It is intended to provide for adequate incentives on both sending and receiving PSPs as part of our package of requirements to quickly increase protection for consumers and meet legislative deadlines.

5.9 We consider PSPs should be able to choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution based on a more tailored set of criteria for allocating reimbursement costs. We also propose that a more tailored criteria for allocation, and associated dispute resolution arrangements, are developed and designated in scheme rules. The CRM Code has identified a set of standards for assessing and allocating liabilities, and we would expect these criteria to build on the CRM Code. We discuss implementation of these proposed arrangements in Chapter 7.

'Multi-generational' scams

5.10 The 'end to end' journey of some APP scams involves more than one payment. In one example, the fraudster may 'socially engineer' the consumer to transfer money from their bank account to an account they hold at a different PSP (or perhaps persuade them to open a new account in their own name). The fraudster then persuades the consumer to transfer the money from that account into the account under the fraudster's control.

5.11 In some cases that second payment may be a transfer using Faster Payments to an account held at a PSP. In other cases, the second payment may be to a different type of account, such as a crypto wallet, which does not happen over Faster Payments, but uses another, for example, a card or a crypto-based, payment system.

5.12 Multi-generation scams may be harder for some of the PSPs in the chain to detect than others. For example, the first transaction is less likely to appear suspicious to the PSPs involved.

5.13 There are different ways that the costs of mandatory reimbursement could be allocated between the PSPs involved in such 'multi-generational' scams. We would welcome views on how scheme rules could implement our proposed 50:50 default allocation to multi-generational scams.

Question 13: Do you have comments on our proposal for a 50:50 default allocation of reimbursement costs between sending and receiving PSPs?

Question 14: Do you have views on our proposal that PSPs are able to choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution based on a designated set of more tailored allocation criteria?

Question 15: Do you have views on how scheme rules could implement our proposed 50:50 default allocation to multi-generational scams?

Allocation of repatriated funds

5.14 Repatriation of APP scam losses occurs where the receiving PSP is able to detect, freeze and return funds stolen as part of an APP scam. Rapid and effective communication from the sending PSP may aid receiving PSPs in detecting and freezing fraudulent funds.

5.15 UK Finance data suggests there are currently very low rates of repatriation. £12.4 million was returned to victims through repatriation in 2021, accounting for just 5% of the total reimbursed to victims by CRM Code signatories.[33] Fraudsters typically transfer

33 UK Finance, *Annual Fraud Report 2022* (August 2022).

stolen money quickly to other accounts and jurisdictions to make it hard for PSPs to trace and return. But there is also a lack of incentive for receiving PSPs to try to increase rates of repatriation. Receiving PSPs, even if they are signatories to the CRM Code, make very little contribution to the costs of reimbursement and so see little benefit from increased repatriation rates.

5.16 Where a receiving PSP recovers and is able to repatriate funds, we need to determine what will happen with that money when the consumer has already been reimbursed by the sending PSP under our proposed rules. We do not intend that the victim is double reimbursed. We propose that, as a default, repatriated funds should be shared 50:50 between the sending and receiving PSPs to defray their costs of liability for reimbursement. Any repatriated funds remaining after the PSPs have fully defrayed their reimbursement costs would go to the victim.

5.17 A 50:50 allocation is intended to provide for adequate incentives on both sending and receiving PSPs to take steps to increase levels of repatriation, as part of our package of requirements to quickly increase protection for consumers and meet legislative deadlines.

5.18 We propose that more tailored criteria for allocation of repatriation costs, and associated dispute arrangements, is also developed and put in place (alongside the criteria for allocation of reimbursement costs). PSPs may choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution based on these more tailored criteria.

5.19 Repatriation of funds can take time to process and resolve and our proposals ensure that any delay does not delay the reimbursement of victims by the sending PSP.

Question 16: Do you have comments on our proposal for a 50:50 default allocation of repatriated funds between sending and receiving PSPs?

Scope of rules for allocating reimbursement costs

5.20 We propose that the rules on allocating the costs of reimbursement apply to all directly connected PSP participants sending and receiving payments over Faster Payments as well as PSPs indirectly sending and receiving payments.

5.21 All PSPs should have incentives to detect and prevent APP scams.

5.22 We have seen a trend of fraudsters migrating to receiving PSPs who are not participating in existing safeguards including the CRM Code and Confirmation of Payee (CoP). For example, non-SD10 PSPs accounted for 20% of Faster Payments transactions in 2021 but received 50% of APP scam payments sent from SD10 PSPs.[34]

Question 17: Do you have views on the scope we propose for rules on allocating the costs of mandatory reimbursement?

34 Based on quarterly CoP data received from SD10 PSPs and industry Faster Payments data from Pay.UK in 2021, covering 2021 and Q1 2022.

PART B:
How we propose to implement our requirements

6 Our long-term vision for Pay.UK's role

Introduction

6.1 This chapter outlines our vision for Pay.UK's role on APP scams.

6.2 Our five-year Strategy, published in January 2022, explained that we wanted to see Pay.UK deliver against a broader role, actively improving the rules governing interbank payments. As part of this, we would like to see them taking responsibility for minimising APP scams in Faster Payments.

6.3 We would ultimately like to see scheme rules contain all the main requirements on PSPs relating to APP scams.

Our long-term vision

6.4 Our five-year Strategy set out that we want to give Pay.UK a stronger role to lead the development of protections for payment system users. Our vision is for Pay.UK, as payment system operator (PSO), to run Faster Payments so that consumers are protected, and fraud is prevented from entering the system. If account-to-account payments are to compete with cards for retail transactions, as part of securing our aim for greater competition between payment systems, consumers will need to have sufficient confidence in the safety of Faster Payments.

6.5 The PSO is the appropriate body, in the long-term, to undertake the role of making, maintaining, refining, monitoring, and enforcing compliance with, comprehensive scheme rules that address fraud risks in the system.

6.6 The alternative would be for the PSR to make directions on PSPs. But it is the PSO that has the operational oversight, the expertise on system rules and what works in practice, and the ability to coordinate across participants, which are needed. Scheme rules can be managed and refined more efficiently and quickly than regulatory instruments. Like other payment system operators and system operators in other sectors, who manage their system rules and the consequences for breaking them, Pay.UK's rulebook is the most practical tool for addressing the harms from fraud in the payment system.

6.7 Looking forward, we expect Pay.UK will need to establish, maintain and enforce cross-market arrangements on PSPs' conduct in a number of areas, including as part of its role in assessing and enabling use cases for the NPA, such as open banking account-to-account retail transactions. Prior to the NPA's implementation, APP scams provides an opportunity for Pay.UK to develop greater expertise in this territory.

6.8 In the long-term, we want Pay.UK to be a PSO that:

- is motivated to minimise fraudulent payments across its system
- specifies the circumstances when a PSP needs to reimburse the victim of a fraud
- is able to effectively monitor and enforce compliance with its rules on fraud protection
- reviews and amends the requirements on PSPs, to maintain their effectiveness in preventing fraud

6.9 For APP scams, this will include Pay.UK maintaining scheme rules on:

- mandatory reimbursement for consumers who become victims of APP scams by all PSPs whether directly or indirectly connected to the payment system
- criteria for allocating reimbursement costs, and dispute resolution arrangements, that provide for effective incentives for detection and prevention of APP scams

6.10 While our long-term vision is for comprehensive scheme rules, we recognise that there could continue to be a role for separate arrangements in support of scheme rules. For example, there could be a long-term role for a separate supporting document or code – designated in scheme rules – containing the criteria for allocation of reimbursement costs in support of dispute resolution arrangements (see Chapter 7). Our vision would nevertheless require that Pay.UK was responsible for ensuring any separate supporting arrangements were providing good consumer outcomes.

6.11 We consider that this vision aligns with our strategic priority of unlocking account-to-account payments because we also want Pay.UK to use its rules to ensure appropriate protections are available to consumers using such payments to make purchases. Pay.UK has also published its strategy, which sets out its ambition to be the platform leader and its vision of being the smartest way to move money. As part of this, they are working to develop a new rulebook for NPA and are considering the reach and scope of their rules that will be necessary to effectively discharge this role.

6.12 We will continue to work closely with Pay.UK (and other stakeholders) to develop this vision, including taking into account the feedback on this consultation.

Question 18: Do you have views on our long-term vision, and our rationale for the PSO being the rule-setter responsible for mitigating fraud?

Approach to achieving our long-term vision

6.13 Some elements of our vision for Pay.UK's role on APP scams represent a significant change from the current position on Faster Payments. We recognise that:

- Pay.UK has other significant projects to deliver in the coming years, not least the New Payments Architecture (NPA). The transition from Faster Payments to the NPA should help PSPs in preventing APP scams – for example, via enhanced ISO 20022 messaging data helping in identification of APP scams
- Pay.UK has governance arrangements that require consultation with, and seek the consensus of, its members before effecting rule changes
- it currently lacks visibility of, and data on, fraudulent transactions over Faster Payments, and the ability to monitor reimbursement for those transactions
- Pay.UK cannot currently apply Faster Payments scheme rules directly to indirect PSP participants in the payment system
- as highlighted by respondents to our November consultation (see Annex 1), Pay.UK currently has little ability to enforce Faster Payments scheme rules. The only significant enforcement sanction currently available to Pay.UK is to exclude participants from the payment system. Doing this would be so disruptive to consumers and businesses that it is unlikely to be a proportionate response to most breaches of payment system rule. This means the sanction is unlikely to be used

6.14 Through our continued conversations with Pay.UK, as well as our consultation process, we will explore the changes that would be necessary to support this expanded role. In addition, we will discuss with Pay.UK how initial arrangement could be delivered so that an effective APP reimbursement regime can be implemented by the end of 2023. Some of the considerations for those initial arrangements are discussed in the following chapters and we are keen to hear your views on these initial arrangements.

6.15 In the short term, there may be a case for considering alternative options for the implementation of some elements of our requirements for mandatory reimbursement. These are discussed in Chapter 7.

6.16 In the longer term, we expect that the NPA's new rules and standards will be fully consistent with our vision for Pay.UK's role. Pay.UK will need to develop the resources and arrangements it needs. We will support Pay.UK in this, including so it has greater ability to revise, monitor and enforce compliance with its rules to improve outcomes for users.

6.17 In the period before implementation of arrangements for mandatory reimbursement, we expect signatories to continue to adhere to the requirements in place under the CRM Code.

7 Short-term implementation of our requirements

We want as much as possible of our vision for comprehensive scheme rules on APP scams to be implemented at the outset.

However, we recognise potential challenges in achieving this. As a minimum, Faster Payments scheme rules should implement the requirements set out in Chapters 4 and 5 in the short term. We consider alternative short-term options for implementation of arrangements for the monitoring and enforcement of the rules on mandatory reimbursement, as well as for their application to PSPs that are indirect participants in Faster Payments.

In the long-term, we expect Pay.UK to keep the effectiveness of reimbursement requirements under review once all the requirements are in NPA rules. In the meantime, we will lead a post-implementation review of the initial Faster Payments rules on reimbursement ahead of the transition to the NPA.

Introduction

7.1 This chapter sets out proposals and options for short-term implementation of our requirements for mandatory reimbursement.

7.2 Chapter 6 outlined potential constraints on Pay.UK's ability quickly to implement some elements of our vision. We are therefore consulting on some alternative short-term implementation options.

A minimum initial set of Faster Payments scheme rules

7.3 We are looking to Pay.UK to consider how quickly it is able to implement our vision for Faster Payments scheme rules and for its role. We do not consider that the constraints that Pay.UK currently faces prevent the main elements of our proposed requirements for mandatory reimbursement from being implemented in scheme rules in the short term. If the Financial Services and Markets Bill comes into force in spring next year, we will be looking to make regulatory requirements to give effect to our proposals in Q2 2023. By then, we would want Pay.UK to be in a position to begin the process of implementation in scheme rules.

7.4 We expect as much as possible of our vision for comprehensive scheme rules on APP scams to be implemented at the outset. But, as a minimum, we expect Pay.UK to implement in Faster Payments scheme rules our proposals for:

- when a consumer must be reimbursed by its sending PSP
- a default 50:50 allocation of reimbursement costs (and of any repatriated funds) between the sending and receiving PSP, and any arrangements needed to enable sending and receiving PSPs to transfer funds between them
- designated arrangements to enable PSPs to choose to depart from default allocation by negotiation, mediation or dispute resolution based on more tailored allocation criteria (implementation of this is discussed further in the next section)

7.5 We consider that the most effective way for us to achieve the necessary changes to Faster Payments scheme rules will be to exercise our powers under section 55 of FSBRA to require the operator of a designated payment system to amend rules for the operation of the payment system so as to achieve a specified purpose. We will consider what arrangements for the monitoring and assurance of implementation of our requirements will be needed.

7.6 An alternative would be for the PSR to impose the requirements on all PSPs through directions, and for Pay.UK to operationalise the requirements. For the reasons set out in Chapter 6, we want Pay.UK to implement, develop and maintain scheme rules and we do not consider that the current constraints on Pay.UK prevent implementation of the minimum requirements in Faster Payments rules in the short term. Directing PSPs is therefore not our preferred option for implementing the minimum requirements. However, we consider this approach further, specifically in relation to indirect participants, later this chapter.

7.7 In addition to the minimum requirements, Faster Payments scheme rules should also, if possible, implement from the outset comprehensive arrangements for the monitoring and enforcement of the rules on mandatory reimbursement, as well as providing for their application to PSPs that are indirect participants. However, recognising the potential challenges in achieving this in the short term, we consider below alternative implementation options in these areas.

Question 19: Do you have comments on the minimum initial set of Faster Payments scheme rules needed to implement our mandatory reimbursement proposals?

Question 20: Do you have views on how we should exercise our powers under FSBRA to implement our requirements?

Dispute resolution arrangements

7.8 As set out in Chapter 5, we propose that the sending and receiving PSP should share the cost of reimbursement (and any subsequently repatriated funds) equally as a default. We also said PSPs should be able to choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution supported by a more tailored set of allocation criteria.

7.9 We consider that there needs to be a coordinated set of arrangements, so that all PSPs have the option to choose, and must cooperate with, dispute resolution arrangements based on an appropriate set of allocation criteria. Therefore we propose that such a set of arrangements must be designated in scheme rules, with Pay.UK responsible for ensuring they are in place and operating effectively. (We consider it is appropriate for Pay.UK rather than the PSR to take responsibility, for the reasons discussed in Chapter 6.)

7.10 Pay.UK would be free to decide how arrangements were put in place. They could, for example, ask the industry to develop and implement the arrangements. They could agree that another body or bodies maintained the allocation criteria and oversaw the operation of dispute resolution arrangements.

7.11 The allocation criteria themselves, once developed, could be brought into scheme rules – in the short or longer term. Alternatively, they could reside in a separate supporting document – a code – that was designated in scheme rules. We would expect the criteria, and associated standards for best practice, to evolve as technologies, detection and prevention measures and scammers' tactics changed over time. There could therefore be an advantage to maintaining a separate code if it could be more flexibly kept up to date.

7.12 The CRM Code – overseen, monitored and enforced by the Lending Standards Board – has already made significant progress in identifying a set of standards for preventing and detecting APP scams, and linking these to allocation of reimbursement liabilities. We would expect future arrangements to build on the achievements of the CRM Code.

7.13 We would expect the allocation criteria that are developed:

- to take account of the relative contribution of each PSP to the fraud loss
- to be applicable fairly to all relevant types of PSPs
- to provide for effective incentives on sending and receiving PSPs to prevent APP scams

7.14 We propose to monitor development of these arrangements. If we became concerned about progress or about the criteria being developed, we would consider whether we needed to intervene.

Question 21: Do you have views on how we propose that allocation criteria and dispute resolution arrangements are developed and implemented?

Monitoring compliance

7.15 Our vision is for Pay.UK, as PSO, to have full responsibility for monitoring compliance with its own scheme rules on reimbursement.

7.16 Effective monitoring will ensure that significant or sustained non-compliance by PSPs – with rules for reimbursement or for allocation of reimbursement costs (or repatriated funds) – is identified in a timely way, so that decisions on consequential actions, including enforcement, may be taken. However, Pay.UK may currently lack the necessary systems for effective monitoring of compliance.

7.17 We consider there are two main options for implementing compliance monitoring:

a. Pay.UK implements a system for real-time monitoring of reimbursement claims.

b. PSPs report regularly to Pay.UK on their performance on reimbursement.

7.18 Option a would be likely to produce the most timely, efficient and accurate information for compliance monitoring. Once up and running, it would also be the least resource-intensive for PSPs. But establishing the necessary system would take time and have a cost. We could require Pay.UK to put in place such a system. We would welcome views on the costs and benefits of such a system and when it could be introduced. If we did adopt this option, we would expect Pay.UK to develop a real-time monitoring system as soon as possible.

7.19 Alternatively, in the short term, we could simply require Pay.UK to create and implement an effective compliance monitoring regime, which Pay.UK could comply with via PSPs reporting regularly to it (option b).

7.20 For reporting-based compliance monitoring to be effective, Pay.UK would need to secure timely and accurate information from PSPs. Pay.UK would therefore need to include an appropriate reporting requirement in Faster Payments scheme rules. We could help expedite implementation of such a reporting requirement by requiring Pay.UK to include it in scheme rules.

7.21 It is important that a monitoring regime is implemented immediately when the reimbursement requirements start. There is currently uncertainty around whether Pay.UK would be able to develop a real-time monitoring system in time. We therefore think that simply requiring Pay.UK to implement an effective compliance monitoring regime, including a reporting requirement on PSPs if necessary, is likely to be the most appropriate short-term implementation option.

Question 22: **Do you have comments on our preferred short-term implementation approach of requiring Pay.UK to implement an effective compliance monitoring regime, including a reporting requirement on PSPs?**

Question 23: **Do you have views on the costs and benefits of Pay.UK implementing a real-time compliance monitoring system and when it could be introduced?**

Enforcing compliance

7.22 Our vision is for Pay.UK, as PSO, to have responsibility for enforcement of its own scheme rules on reimbursement.

7.23 An effective enforcement regime would ensure that cases of non-compliance were effectively investigated, and proportionate sanctions applied, if appropriate, disincentivising future non-compliance. Pay.UK currently has constraints in its ability to take on this role effectively, including a lack of an effective penalty regime.

7.24 We will support Pay.UK in putting in place an ability to effectively enforce compliance with scheme rules on reimbursement.

7.25 If the PSR were to initially implement the reimbursement requirements on PSPs through a direction (as discussed earlier in this chapter), with Pay.UK operationalising those requirements, enforcement of those requirements would also fall to PSR. We would use our usual enforcement processes and principles in deciding when to act, and what action to take. As described above, this is not our preferred option.

7.26 If the initial reimbursement requirements are implemented in Faster Payments scheme rules (our preferred approach), we consider there are three main options for implementing enforcement arrangements in the short-term:

a. Pay.UK develops and improves its own enforcement regime in the short-term.

b. The PSR directs any PSP that has failed to comply with scheme rules on reimbursement to comply within a timescale, following which we would use our own enforcement regime for any further breaches.

c. Pay.UK applies its own enforcement regime, but with escalation to the PSR explicitly included as one of the steps in that regime. If escalated to us, we would follow the process in option b.

7.27 We want Pay.UK to fully explore what it can do to develop and improve its enforcement regime. While we want an effective enforcement regime in the short-term, we do not want to set a precedent by taking on a role that should properly fall to the PSO, nor to reduce the urgency for Pay.UK to develop an effective enforcement regime of its own. We note that escalation to the regulator is already a part of the Faster Payments enforcement procedure, though option c would make the PSR's role more explicit.

7.28 We would welcome views on how we ensure effective enforcement arrangements.

Question 24: **Do you have views on the best option for short-term enforcement arrangements?**

Applying reimbursement rules to indirect participants

7.29 As discussed in Chapter 4, it is important that our proposed requirements for reimbursement apply to all participants in Faster Payments, including indirect participants, so that all consumers are protected. In the longer term, we expect NPA rules on reimbursement to apply to all NPA participants – but Faster Payments rules currently only apply directly to direct participants.

7.30 If the PSR were to initially implement the reimbursement requirements on PSPs through a direction (as discussed earlier in this chapter), with Pay.UK operationalising those requirements, the PSR direction would apply to both direct and indirect participants. As described above, this is not our preferred option.

7.31 If the initial reimbursement requirements are implemented in Faster Payments scheme rules (our preferred approach), under current arrangements they would apply only to direct participants. We consider the following are the main options for implementing our requirements in relation to indirect participants:

a. The PSR gives a direction to all indirect PSPs to comply with the reimbursement rules in Faster Payments.

b. The PSR gives a direction to indirect access providers (IAPs) to ensure transactions by their indirect PSP customers comply with the reimbursement rules in Faster Payments.

c. The Faster Payments rules on reimbursement are applied to all transactions, making the IAP responsible for the transactions of its indirect PSP customers. We would expect IAPs may respond by updating indirect access contracts. We could require Pay.UK to make its rules apply to all Faster Payments transactions.

7.32 Our preferred option would be for Faster Payments rules to apply to all transactions. A single source of rules for participating in the payment system would be simpler to follow and administer. Having requirements in different places and under different organisations would create challenges – for example, for the consistent review and revision of those requirements.

7.33 There may be constraints on Pay.UK being able to change the way its rules apply in the short term. There may therefore be a necessary role for a PSR direction to ensure the reimbursement requirements apply to indirect participants as soon as they are in place.

7.34 Other considerations relevant to the choice of implementation option include the following:

- Indirect PSPs are reliant to some extent on their IAP for access to data on transactions. Placing a requirement on IAPs may therefore give them an incentive to share relevant data in a timely way.
- IAPs have limited ability to monitor their indirect PSPs' compliance, and do not have sanctions other than terminating their contract. Placing liability on IAPs could lead to them becoming more risk averse or exiting relationships.
- If, as a result of placing requirements on IAPs, indirect PSPs needed to share more data and information on their transactions with IAPs, this could raise competition issues. In many cases, IAPs and indirect PSPs are competitors or potential competitors.

Question 25: Do you have views on the best way to apply the rules on reimbursement to indirect participants?

Question 26: If it was necessary for us to give a direction, what are your views on whether we should direct indirect PSPs or IAPs?

Post-implementation review

7.35 Our proposals are a package of measures that we expect to quickly shift the dial on reimbursement levels, and they are capable of refinement over time. In the long term, we expect Pay.UK to keep the effectiveness of reimbursement requirements under review once all the requirements are in NPA rules.

7.36 In the meantime, we will lead a post-implementation review of the initial Faster Payments rules on reimbursement ahead of the transition to the NPA.

7.37 That review will also cover Measures 1 (performance data) and 2 (data sharing), to enable us to assess the overall impact of our measures for improving consumer outcomes on APP scams. We recognise that there may be some overlap between our proposals for mandatory reimbursement and publication of reimbursement data under Measure 1. We consider that Measure 1 will still deliver benefits, and we will review this as part of the post-implementation review.

Proportionality and cost benefit analysis

7.38 The proposals set out in this consultation are proportionate in relation to their expected contribution to our objectives of preventing scams and ensuring customers are appropriately reimbursed (as set out in Chapter 2). Our cost benefit analysis of the requirements we propose is in Annex 2. This sets out our assessment of a number of issues that are also relevant to proportionality.

7.39 As explained in Chapter 2, APP scams continue to grow rapidly, and there are problems with the current framework. APP scam victims are often not receiving reimbursement for their losses. There are large variations in the performance of PSPs both in terms of the rates of APP scams and in levels of reimbursement.

7.40 APP scams can have a devastating effect on victims. Measures to incentivise better prevention of scams, and reimbursement in appropriate cases, are therefore of great importance in protecting consumers and maintaining confidence in payments systems.

7.41 The Government has announced its intention to legislate to place a duty on the PSR to require victim reimbursement for APP scams. We have set out how we expect our proposals to require reimbursement will contribute to our objectives. We consider our proposals will lead to:

- higher overall levels of reimbursement of victims, with more victims of APP scams receiving higher levels of reimbursement of their losses, and all consumers enjoying protections, regardless of their PSP
- stronger financial incentives on both sending and receiving PSPs to prevent scams, given the increased costs to PSPs of reimbursing APP scam losses. PSPs have scope to respond to these incentives by taking further steps to detect potential scams, including by greater sharing of standardised risk data and use of data analytics, and to block accounts or stop suspicious payments while they are investigated

7.42 In developing our proposals, we have taken account of the need to ensure they are proportionate. Our judgements are discussed in this consultation and include the following:

- We have limited the scope of our proposed requirements for reimbursement to consumers, micro-enterprises and charities. Larger business payers can be expected to have greater capability to protect themselves from APP scams, and it would not be proportionate to require PSPs to reimburse such businesses for their losses.
- We have proposed an exception to mandatory reimbursement if a consumer is grossly negligent in order to incentivise customers to take care, and therefore limit any disproportionate costs to PSPs if customers were to exercise less caution following implementation of mandatory reimbursement.
- We have proposed to allow PSPs to set a minimum threshold for reimbursement claims, to apply an 'excess' to reimbursement payments, and to set a time-limit for claims. These are intended to ensure that the costs of mandatory reimbursement

are proportionate, including by limiting the risk of disproportionate administration costs, of reimbursing civil disputes, and of PSPs building-up open-ended liabilities.

- We have proposed, and are seeking views on, options for how our proposals could best be implemented in the short-term. Our aims include helping to ensure a proportionate implementation burden, including on Pay.UK, in the short-term.

7.43 We will continue to consider the proportionality of our proposals as we develop them further, including in light of responses to this consultation.

Question 27: Do you have comments on our cost benefit analysis at Annex 2 or any additional evidence relevant to the analysis?

8 Next steps

8.1 We are asking for feedback on the issues set out in this consultation by 25 November 2022. We will be holding discussion sessions with stakeholders during the consultation period, and will provide details in due course. We continue to welcome feedback from all stakeholders and interested parties, not only entities that we regulate.

8.2 You can provide feedback by emailing us at **appscams@psr.org.uk**. We would be grateful if you could provide your response in a Microsoft Word document (rather than, or as well as, a PDF).

8.3 We will make all non-confidential responses available for public inspection. If your submission includes confidential information, please also provide a non-confidential version suitable for publication.

8.4 In addition to the proposals set out in this consultation, we continue to progress other areas of work on preventing APP scams:

a. By the end of the year, we plan to publish a policy statement and a final direction on Measure 1 data collection and publication, as well as the final data template and reporting guidance. We will ask directed PSPs to submit data to us during spring 2023, and we will publish the first set of data in summer 2023.

b. We continue to monitor industry developments under Measure 2 (data sharing). After the final rules and standards are complete, we will consider whether we need to use formal powers to require any PSPs to build and deliver the capabilities to send and receive the relevant data. Irrespective of whether we use formal powers, we want PSPs to budget and implement the data-sharing system in 2023.

8.5 Following the deadline for this consultation, we will take account of feedback and will publish a policy statement on mandatory reimbursement early in the new year. We plan to publish draft regulatory requirements for consultation consistent with the expected statutory deadline of two months following the relevant legislative provisions coming into force. Our timetable assumes that the relevant provisions of the Finance and Markets Bill come into force around spring 2023.

Timetable

Q1 2023	• The PSR will consider the responses to this consultation in developing its policy decisions on regulatory requirements • The PSR will publish a policy statement on mandatory reimbursement • The PSR will publish draft regulatory requirements, consistent with statutory deadlines
Q2 2023	• The PSR will publish final regulatory requirements, consistent with statutory deadlines

List of questions

1. **Do you have views on the impact of our proposals on consumers?**

2. **Do you have views on the impact of our proposals on PSPs?**

3. **Do you have views on the scope we propose for our requirements on reimbursement?**

4. **Do you have comments on our proposals:**

   - **that there should be a consumer caution exception to mandatory reimbursement**
   - **to use gross negligence as the consumer caution exception**
   - **not to provide additional guidance on gross negligence?**

5. **Do you have comments on our proposal to require reimbursement of vulnerable consumers even if they acted with gross negligence?**

6. **Do you have comments on our proposal to use the FCA's definition of a vulnerable customer?**

7. **Do you have comments on our proposals that:**

   - **sending PSPs should be allowed to apply a modest fixed 'excess' to reimbursement**
   - **any 'excess' should be set at no more than £35**
   - **PSPs should be able to exempt vulnerable consumers from any 'excess' they apply?**

8. **Do you have comments on our proposals that:**

    - **sending PSPs should be allowed to set a minimum claim threshold**
    - **any threshold should be set at no more than £100**
    - **PSPs should be able to exempt vulnerable consumers from any threshold they set?**

9. **Do you have comments on our proposal not to have a maximum threshold?**

10. **Do you have comments on our proposals that:**

    - **sending PSPs should be allowed to set a time-limit for claims for mandatory reimbursement**
    - **any time-limit should be set at no less than 13 months?**

11. **Do you have comments on our proposals that:**

    - **the sending PSP is responsible for reimbursing the consumer**
    - **reimbursement should be as soon possible, and no later than 48 hours after a claim is made, unless the PSP can evidence suspicions of first party fraud or gross negligence?**

12. **What standard of evidence for gross negligence or first party fraud would be sufficient to enable a PSP to take more time to investigate, and how long should the PSP have to investigate in those circumstances?**

13. **Do you have comments on our proposal for a 50:50 default allocation of reimbursement costs between sending and receiving PSPs?**

14. **Do you have views on our proposal that PSPs are able to choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution based on a designated set of more tailored allocation criteria?**

15. **Do you have views on how scheme rules could implement our proposed 50:50 default allocation to multi-generational scams?**

16. **Do you have comments on our proposal for a 50:50 default allocation of repatriated funds between sending and receiving PSPs?**

17. **Do you have views on the scope we propose for rules on allocating the costs of mandatory reimbursement?**

18. **Do you have views on our long-term vision, and our rationale for the PSO being the rule-setter responsible for mitigating fraud?**

19. **Do you have comments on the minimum initial set of Faster Payments scheme rules needed to implement our mandatory reimbursement proposals?**

20. **Do you have views on how we should exercise our powers under FSBRA to implement our requirements?**

21. **Do you have views on how we propose that allocation criteria and dispute resolution arrangements are developed and implemented?**

22. **Do you have comments on our preferred short-term implementation approach of requiring Pay.UK to implement an effective compliance monitoring regime, including a reporting requirement on PSPs?**

23. **Do you have views on the costs and benefits of Pay.UK implementing a real-time compliance monitoring system and when it could be introduced?**

24. **Do you have views on the best option for short-term enforcement arrangements?**

25. **Do you have views on the best way to apply the rules on reimbursement to indirect participants?**

26. **If it was necessary for us to give a direction, what are your views on whether we should direct indirect PSPs or IAPs?**

27. **Do you have comments on our cost benefit analysis at Annex 2 or any additional evidence relevant to the analysis?**

28. **Do you have any other comments on the proposals in this consultation?**

Annex 1
Our November consultation

1.1 In November 2021, we published a consultation on our package of measures to combat APP scams. This chapter addresses the response to our proposal on Measure 3, where we consulted on our approach to mandating reimbursement.

1.2 In the consultation, we said we believed that reimbursement of scam victims should be made mandatory and set out two options for doing so:

- **Measure 3A:** Requiring Pay.UK to incorporate into scheme rules an obligation for members to reimburse APP scam victims who have exercised sufficient caution.
- **Measure 3B:** Formalising the CRM Code by requiring Pay.UK to incorporate into scheme rules a requirement for PSPs to sign up to a PSR-approved code.

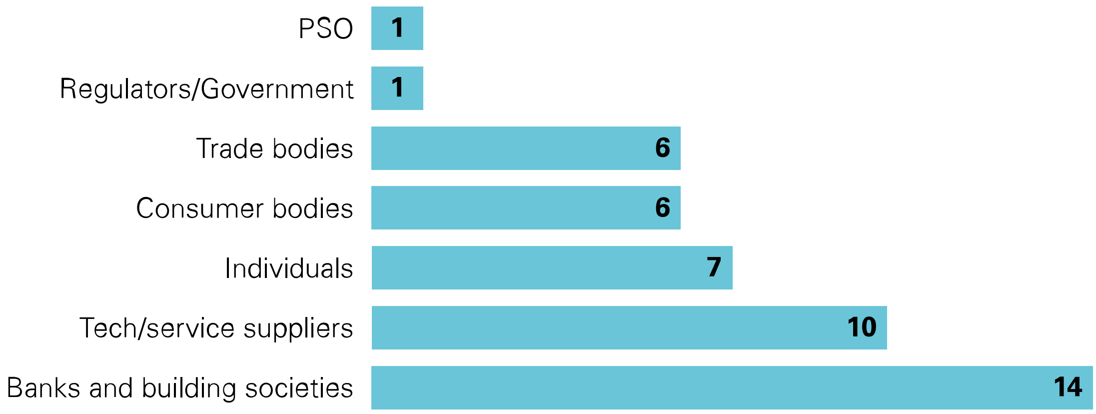
1.3 We looked at the pros and cons of the two options, and we asked for respondents' comments on these.

1.4 We also outlined our thinking on the roles of various bodies under the two options and implementation issues. We asked respondents for comments on our thinking on how the roles of the bodies currently involved in the CRM Code would differ between the two options.

Responses to our consultation

1.5 We received 45 responses to our consultation. Most were from PSPs, financial technology firms and third-party service providers. We also received responses from consumer bodies, industry trade bodies, private individuals, regulatory/governmental bodies and a payment system operator (see Figure 4).

Figure 4: Responses to our November 2021 consultation



Views on the Measure 3 options

Pros and cons of Measures 3A and 3B

1.6 The responses to our proposed options differed between PSP and non-PSP respondents. Many non-PSPs favoured Measure 3A, while PSPs tended to prefer 3B. Respondents also suggested some alternative options, which we set out below.

1.7 Most non-PSPs saw Measure 3A as offering better levels of reimbursement for victims. PSPs, on the other hand, did not support it as they felt it would reduce customer incentives to take sufficient care when making a payment, and could potentially encourage scammers through providing higher levels of reimbursement.

1.8 PSPs argued that Measure 3B would provide scope to reach more PSPs, and to recognise – in the provisions of the code – the customer's duty to exercise caution. Non-PSPs were however concerned that 3B might replicate the CRM Code's existing problems of low and variable reimbursement levels. Some respondents also noted that there would remain scope for less than universal coverage under this option, which could create a two-tiered approach to reimbursement of customers.

Our response

1.9 We considered the consultation feedback, including arguments for and against Measures 3A and 3B, and we have engaged extensively across a broad range of stakeholders. Our thinking has progressed significantly, and we have developed the proposals set out in this consultation.

1.10 In addition, since our November consultation, the Government announced its intention to legislate to allow, and place a duty on, the PSR to require victim reimbursement for APP scams, and has published the Financial Services and Markets Bill.

1.11 We propose to require all PSPs sending payments over Faster Payments to fully reimburse all consumers who are victims of APP scams, with limited exceptions to ensure consumers have incentives to exercise caution and proportionality. We also set out our proposals that reimbursement requirements should be implemented in Faster Payments rules, potentially supported by arrangements such as a code setting out the criteria for allocation of reimbursement costs between PSPs.

1.12 As set out in this consultation, we expect our proposals to result in higher levels of reimbursement for victims, consistent across all PSPs, while maintaining sufficient incentives on consumers to take appropriate care.

Roles of bodies involved in the Measure 3 options

1.13 Most PSPs expressed concerns with Pay.UK's current ability to enforce the rules envisaged under Measure 3A.

1.14 Some respondents argued that the Lending Standards Board's (LSB's) current approach to monitoring and enforcing the CRM Code was not working effectively. Measure 3B would place a significant oversight burden on the LSB if most PSPs signed up to a formalised code. There were also concerns that Measure 3B would curtail the LSB's independence or compromise its oversight role. One respondent said it was unclear what powers the PSR had to hold the LSB to account.

1.15 Many respondents said that our proposals did not address the role of organisations facilitating scams, such as large tech firms, social media platforms and telecommunications firms. It was argued that these should have liability for APP scam losses, to encourage greater accountability for the role they play in enabling APP scams. Some respondents suggested that the PSR, along with the Government and other regulators, should target fraud on a more holistic level, involving social media and other firms. A significant majority of PSPs suggested that a regulated code should be set out in legislation, with clear roles and liabilities and a viable funding model, with contributions from industries responsible for facilitating fraudsters.

Our response

1.16 We recognise that some elements of Measure 3A, and of the proposals we are now consulting on, represent a significant change from the current position on Faster Payments – and there are constraints on Pay.UK in being able to implement elements of our proposals in the short-term. However, we do not consider that the constraints that Pay.UK currently faces prevent the main elements of the requirements we are now consulting on, from being implemented in the short-term in Faster Payments rules.

1.17 Our long-term vision is for Pay.UK to run the Faster Payments system so that consumers are protected, and fraud is prevented from entering the system. In this consultation, we have outlined our approach to achieving this vision over time. We also recognise that there could continue to be a role for separate arrangements in support of scheme rules. For example, there could be a long-term role for a separate supporting document or code containing the criteria for allocation of reimbursement costs in support of dispute resolution arrangements. Any code would need to be designated in Pay.UK's scheme rules but could be developed by the industry and managed by Pay.UK or by another party on Pay.UK's behalf.

1.18 The Government has announced the legislative approach it is taking in relation to reimbursement. The Financial Services and Markets Bill would allow, and place a duty on, the PSR to require victim reimbursement for APP scams.

1.19 We recognise that there are other organisations that should also take actions to reduce APP scams, including the digital platforms where many scams originate. We recognise the work being undertaken by other authorities in this area, and we will continue to share information to help.

Measure 3 implementation issues

1.20 A large proportion of respondents said more (or all) PSPs should be included in Measure 3, to maximise coverage and protection for consumers. Respondents said it was not clear how Measures 3A or 3B would capture indirect participants. Some smaller PSPs felt that further work was needed to understand the implications of the mandatory reimbursement proposals on indirect participants. A couple of respondents expressed concerns that the Measure 3 would not be broad enough as to cover 'on-us' transactions and other payment systems (such as CHAPS and Bacs).

1.21 Many PSPs raised questions about how liability for the costs of reimbursement would be assessed. Many said that proposals did not address the role of receiving PSPs.

1.22 Some respondents raised questions about the need to recognise different PSP business models, and about the cost and effect on competition of increased reimbursement. Some smaller PSPs said Measure 3 would be costly to implement and could present a barrier to market entry, impeding competition. Some respondents said that moving to higher levels of reimbursement could deter some PSPs from using Faster Payments.

1.23 It was also suggested that the PSR should concentrate on education (building on the work of UK Finance and the Take Five initiative, a national campaign offering advice to prevent online, email and phone-based fraud), extending CoP, intelligence sharing and deploying the new Request to Pay framework.

Our response

1.24 In this consultation, we propose that our requirements for mandatory reimbursement cover all APP scams over Faster Payments and therefore apply both to directly connected PSP participants as well as PSPs indirectly connected via an IAP. In Chapter 7, we discuss options for short-term implementation of our requirements on indirect participants.

1.25 While our powers do not extend to regulating on-us payments, we have a clear expectation that PSPs should reimburse on-us APP scam payments in exactly the same way as payments via Faster Payments. Victims are impacted in the same way whether the scam payment is on-us or via Faster Payments – they should not have less right to reimbursement if the fraudster uses an account provided by the victim's own PSP.

1.26 We are working closely with the Bank of England on the proposals in this consultation, and the Bank is considering the most appropriate approach to APP scam payments made over CHAPS.

1.27 In Chapter 5 we set out how we propose the costs of reimbursement should be allocated between sending and receiving PSPs, with a default 50:50 allocation, to ensure adequate incentives on both sending and receiving PSPs. We are also consulting on enabling PSPs to choose to depart from the default allocation by negotiation, mediation or dispute resolution based on a set of more tailored allocation criteria.

1.28 Our proposals would increase the cost of APP scams reimbursement for most PSPs. The increased cost is an intended effect of our proposals. Mandatory reimbursement, as well as protecting victims, is intended to incentivise further prevention by both sending and receiving PSPs. We would like to see as many APP scams as possible prevented so reimbursement is not required.

1.29 We are aware that PSPs with certain business models may have a high proportion of fraudster-controlled accounts, and could therefore have high reimbursement costs under our proposals. Our view is that this would reflect the effective operation of the incentives we intend – and such PSPs should respond by putting in place more effective fraud controls. Having robust fraud controls should effectively be a condition of operating in UK payment systems.

1.30 Our proposals are focused on our remit. This includes our work with the industry on greater sharing of intelligence (our Measure 2) and the extension of CoP requirements across the industry, as discussed in Chapter 2. We continue to engage with the Government and other authorities on the broader approach to APP scams. We have also been engaging with consumer representatives throughout the policy development process, and will continue to do so during the consultation period. We are also looking at improved ways to inform the public of our proposals.

Annex 2
Cost benefit analysis

As set out in Chapter 3, our goal with this proposed policy is to reduce the levels of APP scams. The proposed measures will provide greater protection for consumers, ensuring that any victim has their money reimbursed (with very limited exceptions). They will also incentivise PSPs to improve their fraud prevention capabilities, both for incoming and outgoing payments.

We consider that requiring the mandatory reimbursement for the vast majority of APP scam losses and requiring receiving PSPs to share some of the costs of this will have very significant benefits overall. Our cost benefit analysis has not taken the approach of directly balancing the costs of increased reimbursement that PSPs will face against the benefits of increased reimbursement that victims will receive. That approach would simply find a large cost on one side cancelled out by the same scale of benefit on the other. Our approach has mainly focused on the benefits and costs that mandatory reimbursement, and a split of reimbursement costs, will generate due to the changed incentives to detect and prevent fraud that PSPs will face as a result, while also recognising that greater certainty in relation to reimbursement will also bring non-financial benefits to consumers.

Significant elements of these benefits are hard to quantify but we judge that they outweigh the costs incurred. The most important categories of benefits and costs are as follows:

- **Main benefit:** Strengthened financial incentives for PSPs to detect and prevent APP scams are likely to lead to improved fraud prevention and result in substantial decline in the overall amount of APP scam fraud that consumers suffer. Current levels of APP scam fraud, at over £500 million in 2021, could fall by between £100 and £150 million per annum, based on our assessment.

- **Main cost:** The increased costs of reimbursement will incentivise PSPs to invest more in fraud detection and prevention, and in pursuing and recovering funds lost to APP scam fraudsters. As such, the costs that PSPs will be incentivised to incur are likely to be significant. However, PSPs will be incentivised to incur costs that are proportionate to the scale of fraud involved – this is, a PSP that would face reimbursement costs of, say, £8 million per annum would be incentivised to invest in fraud prevention measures that are proportionate to that scale of fraud. This is in contrast to a policy where all PSPs are required to incur similar costs regardless of the scale of the problem they are facing.

In analysing the impacts of the proposal, our baseline scenario has assumed that, for the purposes of this assessment:

- the PSR's other proposed policies in relation to APP scams, Measure 1 (data publication) and Measure 2 (data sharing), would be implemented
- the PSR's policies in relation to the extension of Confirmation of Payee (CoP) checks would be implemented
- PSPs that currently reimburse their customers for APP scam losses on a voluntary basis would continue to do so
- current low rates of recovery and low shares of reimbursement coming from receiving PSPs would remain low

How will the proposal improve outcomes?

2.1 As set out in Chapter 3[35], in summary, we propose that rules are put in place covering mandatory reimbursement for all types of APP scams by all PSPs sending payments via Faster Payments, and shared costs of reimbursement between sending and receiving PSPs. Specifically, we propose:

- an APP scam victim's PSP (the sending PSP) must reimburse them, except in cases of first party fraud or gross negligence (unless the victim is a vulnerable consumer)
- the sending PSPs must reimburse the victim within 48 hours of the fraud being reported, unless the sending PSP has evidence or reasonable grounds for suspicion of either first party fraud or gross negligence (it will then have more time to investigate)
- PSPs can set a fixed 'excess' of up to £35 and a minimum threshold claim for reimbursement of up to £100
- the costs of reimbursement (as well as any repatriated funds) are shared equally between sending and receiving PSPs by default; PSPs can use a dispute resolution process to refine the allocation of reimbursement costs to better reflect the steps each PSP took to prevent the scam
- PSPs can apply a time limit on claims of no less than 13 months from the date of the payment
- both direct Faster Payments participants and indirect PSPs will be covered by the requirements

35 See Chapter 3.

Causal chain

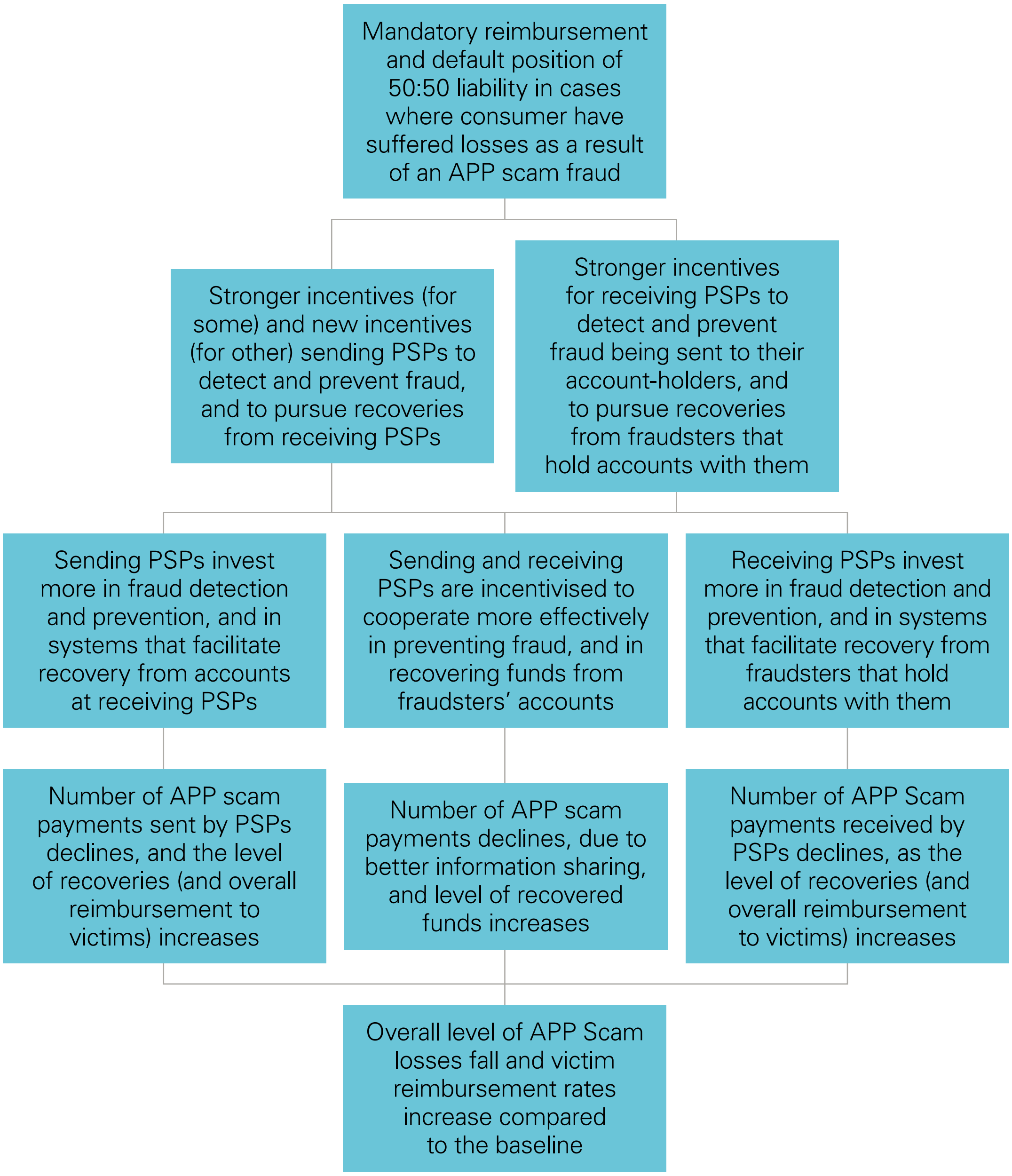
2.2 As set out in Chapter 3, our goal with this proposed policy is to significantly reduce the levels of APP scams. The proposed measures will provide greater protection for consumers, ensuring that any victim has their money reimbursed (with very limited exceptions). As set out in Chapter 3, we expect the proposed policy to benefit consumers by substantially increasing the proportion of consumers' APP scam losses that are reimbursed by PSPs, from the current level of just under 50% under the CRM Code. We would expect to see increased efforts by PSPs to prevent APP scams, incentivised by the costs of this greater reimbursement, with the potential to reduce the numbers of consumers who fall victim in the first place. They will also incentivise PSPs to improve their fraud prevention capabilities, both for incoming and outgoing payments.

2.3 The main mechanisms through which we expect our proposed policy to work is to provide incentives to both sending and receiving PSPs:

- to improve their detection and prevention of APP scams
- to cooperate more effectively in preventing scams
- to more effectively pursue funds that are lost, recovering these in order to reduce PSPs' own costs in reimbursing victims

2.4 Overall, we expect these changed incentives to lead to lower levels of APP scam fraud.

Figure 5: Causal chain for requiring reimbursement of APP scam losses



Baseline

2.5 We have analysed the impacts of the policy against a baseline, or counterfactual scenario, where the policy is not implemented. The starting point for our baseline is that PSPs will continue taking some action to prevent APP scams and reimburse some victims who have exercised sufficient caution. In coming to a view on the appropriate baseline, we have considered what assumptions to make in relation to:

- the PSR's other proposed policies in relation to APP scams (Measures 1 and 2), which are currently being considered, but have not yet been finalised or implemented[36]
- the PSR's policies in relation to the extension of Confirmation of Payee (CoP) checks, which has also not yet been finalised or implemented[37]
- PSPs that currently reimburse some of the losses incurred by their customers on a voluntary basis
- current rates of recovery of funds from fraudsters' accounts
- current shares of reimbursement costs coming from receiving PSPs, as opposed to sending PSPs

2.6 **Other PSR policy interventions:** In relation to the two other APP scams policy measures that the PSR is working on, we have assumed, for the purposes of this assessment, that these are likely to be in place in our baseline scenario.

- **Measure 1 – Publishing scam data:** Having consulted on the proposed approach to collecting and publishing data on APP scams and reimbursement rates[38], we undertook a voluntary trial of reporting on APP scams data in June. We continue to engage with PSPs and trade bodies in order to inform the development of our final guidance and data template. We plan to publish these, along with a policy statement, before the end of the year. We will ask directed PSPs to submit data to us during spring 2023, and we will publish the first set of data in summer 2023. As such, we have assumed, for the purposes of this assessment, that this measure is likely to be in place and having an impact on APP scam prevention in 2023.[39]
- **Measure 2 – intelligence sharing:** As set out in Chapter 2, progress has been made on developing this system and provisional results on the effectiveness of this in identifying scam payments are positive. UK Finance and Pay.UK are now building rules and standards to allow data to be shared on a real-time basis, and the PSR expects PSPs to implement the capability to send and receive the data that will enable them to better identify and stop scam payments in 2023.

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36 See Chapters 2 and 8.

37 See Chapter 2.

38 PSR CP21/10, *Authorised Push Payment (APP) scams* (November 2021)

39 We note that our November consultation included a draft cost benefit analysis of the impact of the information publication under Measure 1, including pointing to its likely impact on reimbursement and fraud prevention (page 49).

As such, we have assumed, for the purposes of this assessment, that this measure is likely to be in place and having an impact on APP scam prevention in the near future.

2.7 **PSR policy on the extension of CoP checks:** In May 2022, the PSR consulted on requiring a large number of PSPs to begin providing CoP checks from mid-2023 onwards.[40] Although a final decision has not yet been taken in relation to this policy nor a specific direction issued, for the purposes of this assessment, we have assumed that this expansion of the CoP system is likely to happen. As such, even absent our current policy proposal, we should expect some decrease in the level of APP scam fraud, at least those that are likely to be affected by the wider use of CoP checks, for example, impersonation scams. The broader scope of our proposed policy on mandatory reimbursement (in terms of covering all APP scam types) and the financial incentives that it provides to PSPs means that it is likely to have a greater effect on APP scams overall than our work on extending CoP checks.

2.8 **Voluntary reimbursement:** At present a number of PSPs offer reimbursement to their customers who are victims of APP scams. Under the CRM Code, just under half of consumer APP scam losses are reimbursed at present, a share which has been stable over a number of years. The number of PSPs that are members of the Code may increase in the future. In addition, as above, the incentives on PSPs to increase their reimbursement rates voluntarily, in response to the publication of Measure 1 data, may also lead to higher levels among sending PSPs absent our proposed mandatory reimbursement policy. However, as above, a system of mandatory reimbursement will, by definition, lead to a greater increase in overall reimbursement rates than the incentives that publication of reimbursement rates under Measure 1 would be likely to achieve.

2.9 **Recovery of funds from fraudsters:** At present, funds recovered from fraudsters' accounts at receiving PSPs account for less than 5% of funds reimbursed to victims of APP scams.[41] This low level of recoveries prevails despite the incentives that already exist for sending PSPs to pursue receiving PSPs in attempting to recover these lost funds. As above, the publication of comparative data on PSPs' reimbursement rates is likely to strengthen the incentives on sending PSPs to increase their rates of reimbursement. This, in turn, may strengthen sending PSPs' incentives to pursue recoveries from fraudsters' accounts in order to offset their greater costs in reimbursing more APP scam losses. However, it is not clear to what extent Measure 1 alone will increase recovery rates, especially given that many sending PSPs already incur significant costs in voluntarily reimbursing their customers, yet this has not led to material rates of recovery from fraudsters' accounts at receiving PSPs.

40 PSR CP22/2, *Confirmation of Payee: Requirements for further participation in CoP* (May 2022)

41 UK Finance, *Annual Fraud Report* (August 2022), page 49: Repatriation from beneficiaries' accounts to victims accounted for £12.4 million out of total reimbursement of £467.5 million under the CRM Code in 2021. That is around 2.7% of the value reimbursed came from funds recovered from fraudsters' accounts at receiving PSPs.

2.10 **Reimbursement from receiving PSPs:** At present, reimbursement from receiving PSPs accounts for under 5% of all funds reimbursed to victims of APP scams.[42] In the absence of any material change in receiving PSPs' incentives to provide greater reimbursement to victims, we do not expect this low rate to increase, absent this policy proposal.

What is our assessment of the impacts?

2.11 We have analysed the impacts of the proposal against a baseline scenario, as set out above, where a number of other PSR policies are likely to impact the level of APP scams and the level of voluntary reimbursement. While it is outside the scope of this cost benefit analysis to assess the relative likely impacts of the PSR's various APP scams policies, we note the following:

- As set out in, for example, Chapter 2, above, the various measures that we are taking forward, or have consulted on in recent months, form part of a package, with different elements working in different ways. For example, CoP checks are likely to have an impact on some types of APP scam fraud (for example, impersonation scams) but not on others (for example, purchase scams).
- There is a degree of complementarity between the different measures, for example, while requiring reimbursement will provide financial incentives to PSPs to reduce APP scams (under Measure 3), the publication of data on current (voluntary) reimbursement rates and on the rate of APP scams sent and received by PSPs (under Measure 1) will provide reputational incentives to PSPs to improve their (relative) performance.
- Having said this, the scale of the change in financial incentives on PSPs that our mandatory reimbursement policy proposal will cause is such that we expect it to have the greatest impact on how PSPs tackle APP scams among the various policies that are being put in place.

2.12 The following sections set out our assessment of the likely costs and benefits of the proposal relative to the baseline. Our assessment is based on a combination of qualitative, as well as quantitative, evidence. It has not been possible to estimate the likely impacts of all the relevant benefits and costs with precision, but we have given some indicative numbers where possible. We would welcome additional evidence in relation to the quantification of any of the benefits and costs set out below.

2.13 As set out in Table 1, there are four main areas where we expect the policy to lead to relevant benefits and seven areas where we expect it to potentially generate relevant costs.

42 PSR analysis of UK Finance data on CRM Code outcomes, 2021.

Table 1: Summary of main benefits and costs

Benefits	Relative Magnitude	Costs	Relative Magnitude
Reduced incidence of APP scams	High – indicative estimate £100-150 million per annum	Increased investment in fraud prevention by PSPs	Proportionate to the scale of fraud being tackled
More consistent reimbursement for victims	High	Administrative costs of pursuing completed payments and resolving disputes	Medium
Increased recovery of APP scam funds at receiving PSPs	Medium	Costs of investigating, delaying and stopping suspicious payments	Medium
Level playing field across different PSPs	Medium	Increase in reported APP scams	Low
		Customer caution and moral hazard	Low
		Potential exclusion of customers in opening new accounts or accessing certain services	Low
		Migration to other payment methods	Low

2.14 As set out below, overall, we consider that the benefits of our proposed policy on mandatory reimbursement and the allocation of those costs between PSPs are likely to outweigh the costs of the proposed policy.

Benefits

Better prevention of APP scams

2.15 As set out in Chapter 3, the main intention of the policy is to incentivise PSPs, on both the sending and receiving sides, to take more effective steps to prevent APP scams. We have considered the changed incentives for PSPs from three perspectives:

- from the sending side, where the PSP offers little or no reimbursement to its customers now
- from the sending side, where the PSP currently voluntarily reimburses a material share of its customers' losses (for example, CRM Code members)
- from the receiving side, where currently receiving PSPs account for a very low share of reimbursement costs to victims

2.16 Broadly speaking, all relevant PSPs are both sending and receiving PSPs, although different customer bases and business models will mean that different PSPs have different ratios of transactions sent to transactions received.

Sending PSPs that currently offer little or no reimbursement

2.17 First, our proposed policy will lead to PSPs on the sending side of transactions that currently offer little or no reimbursement to their customers becoming liable for mandatory reimbursement. At present, ten PSPs (accounting for more than 90% of Faster Payments transactions) are members of the CRM Code and, as such, they reimburse some of their customers who fall victim to scams[43], although the rates at which different signatory PSPs reimburse their customers vary widely. While there are also non-Code members that offer reimbursement to their customers[44], we would expect the greatest impact (in terms of increased rates of reimbursement) to be among non-Code PSPs. These PSPs currently account for c.13% of Faster Payments transactions, and these are likely to be the PSPs that have the most marked change in their incentives to tackle APP scams due to the increased burden of reimbursement. As such, they should have the greatest incentives to increase their investment in fraud detection and prevention.

Sending PSPs that already reimburse consumers

2.18 Second, we have considered the effects on those PSPs on the sending side of transactions that already refund a material share of their customers' APP scam losses. For CRM Code members, reimbursement rates are currently under 50% – the vast majority of this (over 95%) coming from the sending PSPs. Given the proposed default to a 50:50 split of reimbursement costs between sending and receiving PSPs, we may expect to see an increase in the overall rate of reimbursement, but the change for (some of) these PSPs may not be substantial. Indeed, for some sending PSPs, the

43 See Chapter 2.

44 TSB and Nationwide, as set out in Chapter 1.

expectation of a 50% liability for reimbursement costs could mean that their costs of reimbursement (as a sending PSP) may be lower than at present (that is, a number of PSPs currently reimburse in excess of 50% of their own customers' APP scam losses).

2.19 However, this is only looking at those PSPs on the sending side. They would still have increased liability for reimbursement costs from APP scams due to the APP scam transactions that they would be liable for as **receiving** PSPs. Currently, receiving PSPs reimburse a negligible amount (less than 5%) of overall APP scams losses at present, so these PSPs would see a substantial increase in their liability for reimbursement costs on the receiving side. As such, even a PSP that currently reimburses, for example, 80% of its customers' losses on the sending side is likely to see an increase in its overall reimbursement costs if it faces the cost of reimbursing only 50% on the sending side but now also 50% on the receiving side.

2.20 As such, the incentives to invest in fraud prevention, detection and recovery are still likely to be strengthened for the majority of PSPs due to increased receiving-side share of reimbursement costs under the proposed policy.

Receiving PSPs

2.21 Third, under our proposed policy, PSPs on the receiving side of transactions will have a much stronger incentive to detect and prevent APP scams than they do at present. As set out above, receiving PSPs account for a very low share of total reimbursements at present (less than 5%) and recovered funds from fraudsters' accounts at receiving PSPs also account for a very low share (c.5%) of funds reimbursed to victims.

2.22 In addition, there are very substantial differences in the rates at which different PSPs receive APP scam payments, with some of the PSPs with the highest rates being more than ten times the rate of those PSPs that receive proportionately lower levels of APP scams. While there may be a number of reasons why different PSPs experience different rates of fraud, this high level of variation does suggest there is significant scope for many PSPs to improve performance in reducing APP scams, as set out in Chapter 3. Requiring receiving PSPs to share 50% of the costs of reimbursement, as a default, will provide a strong incentive on them to increase their investment in fraud prevention and detection, and to increase their cooperation with sending PSPs in detecting and prevention APP scams.

Quantification of reduction in APP scams

2.23 We have analysed data collected from a number of PSPs and have found a wide variation in the rate at which different PSPs report their levels of APP scam payments sent by their customers and the levels of these APP scam payments received by accounts at other PSPs. Using this data, in combination with data on the total volume and value of Faster Payments transactions at the relevant PSPs, we have calculated rates of APP scam payments sent and received by different PSPs.

2.24 These rates varied widely on both the sending and, especially, on the receiving side. Although these rates are not perfect indicators of different PSPs' effectiveness in fraud prevention, they are likely to reflect real differences, and are indicative of the scope for some PSPs – those that display high rates of APP scams being sent and/or received by their accounts – to improve their performance.

2.25 Taking this as a starting point, we took the average (median and mean) rates of APP scams sent and received by the PSPs for which we had data. We then looked at those PSPs that displayed rates of APP scams sent and received that were higher than these averages, and calculated how much the value of APP scam fraud would fall if these poorer performing PSPs managed to cut their APP scam rates to the average levels. We found:

- for sending PSPs, if those PSPs with above average rates of APP scams reduced their rates in line with the median rate, then APP scam losses would fall by almost £150 million per annum
- for receiving PSPs, if those PSPs with above average rates of APP scams reduced their rates in line with the median rate, then APP scam losses would fall by almost £100 million per annum

2.26 As these are two ways of looking at the effect on the same set of fraudulent transactions – from the sending and receiving sides, respectively – these estimates should not be thought of as separate impacts that can be aggregated. Rather, they each give an imprecise estimate of the broad scale of the potential impact of stronger incentives on sending and receiving PSPs, and of stronger incentives for PSPs on both sides to cooperate, based on two measures of how PSPs perform now.

2.27 While these estimates of the likely benefits are substantial, they could well underestimate the scope for improved APP scam prevention:

- They are based on PSPs improving to the level of current median rates of fraud sent and received. Our proposed policy would strengthen the incentives on all PSPs – those that perform well, average and poorly at present – to take further steps to prevent fraud. As such, those median rates would be expected to fall in the future, pointing to greater scope for poor performing PSPs to improve further.
- As above, even PSPs with low rates of APP scam payments sent and received at present would face stronger incentives to prevent fraud, so we could expect reduced APP scams among those PSPs too. This reduction is not taken into account in our simple analysis.
- This analysis is based on data covering the majority of Faster Payments transactions (73%) and a similar proportion of reported APP scams over Faster Payments (75%).[45] We have not made any assumption about the transactions and the PSPs that fall outside the analysis. As such, the estimated impact, in terms of reduced APP scams losses, only relates to those PSPs covered in

45 UK Finance, *Annual Fraud Report 2022* (June 2022), page 68.

our data set. Any reduction in APP scams sent or received by other PSPs as result of the proposed policy is, therefore, not reflected here.

- We have also not made any assumption about future changes in APP scam numbers (which rose by 39% in value terms between 2020 and 2021)[46] nor about future changes in Faster Payments transaction numbers (which rose by 24% in value terms between 2020 and 2021).[47] It would be reasonable to assume that, absent our intervention, the scale of APP scam fraud would continue to grow, so the benefits to increasing detection, prevention and reimbursement could also be expected to grow over time.

2.28 There are also a number of reasons why these estimates may overstate the likely impact on APP scam fraud:

- First, fraudsters may target the PSPs with the weakest controls, so even where they improve their systems for detecting and preventing APP scams, these PSPs may not reduce fraud to the level of the average-performing PSP.
- Second, as set out below, we have considered the risk that mandatory reimbursement could lead to some customers exercising less caution when making payments. Such a potential increase in APP scam losses could offset some of the potential gains from enhanced detection and prevention by PSPs.
- Third, the proposal to allow PSPs to apply a minimum claim, of up to £100, and 'excess', up to £35, may reduce the costs of reimbursement to PSPs and so reduce PSPs' incentives to invest in improved APP scam prevention. As set above, we would not expect these to have a material impact on PSPs' incentives, as APP scams with values under £1,000 accounted for only 8% of losses (by value) in 2021, while, even if all PSPs adopted a £35 'excess' it would account for around 2% of APP scam losses by value.[48] In both cases, these thresholds are options that PSPs could choose to adopt or not, and many PSPs may decide not to impose a minimum threshold nor to deduct an 'excess' from their reimbursement payments.

2.29 Overall, we consider that our estimates are far from precise, but do provide a useful indication of the likely scale of the impact of our proposed policy. We also note that the reduction in fraud is a benefit that persists – with consumers and PSPs avoiding the costs of prevented fraud over time – while, as set out below, some of the relevant costs are more short-lived.

Increased recovery of APP scam funds at receiving PSPs

2.30 At present, less than 5% of APP scam losses that are reimbursed come from recovered funds. Given that reimbursement (under the CRM Code) accounts for under 50% of relevant APP scam losses, the overall level of recoveries is likely to be lower than 5%

46 UK Finance, *Annual Fraud Report 2022* (August 2022), page 47. APP scam fraud increased by 27% in terms of case numbers between 2020 and 2021.

47 Pay.UK website (accessed on 5 September 2022): www.wearepay.uk/what-we-do/payment-systems/faster-payment-system/. Faster Payments transactions rose by 20% in volume terms between 2020 and 2021.

48 See Chapter 3.

overall. At present, those sending PSPs that voluntarily reimburse their customers when they fall victim to an APP scam have an incentive to pursue the receiving PSP and seek recovery from the fraudster's account. With a broader requirement on all sending PSPs to reimburse their customers and, more importantly, a new requirement on receiving PSPs to reimburse victims, the incentives for PSPs to pursue successful recovery of funds is significantly increased. An increase in successfully recovered funds should act as a disincentive to fraudsters, compared to the current situation where successful APP scams fraud very rarely result in the funds being recovered back from the fraudster.

2.31 We have not been able to quantify a likely effect from these strengthened incentives, as we do not have data on different PSPs' level of recoveries. In any case, the low level across the sector suggests that most PSPs are achieving a very low rate of recovery of funds from fraudsters' accounts at present. This low level suggests that there is room for substantial improvement, but we have not been able to quantify the scale of any likely increase in response to our proposed policy.

More consistent reimbursement for victims

2.32 We have previously pointed to the wide variation in reimbursement rates across individual PSPs.[49] This continues to be the case. At present, even among CRM members, reimbursement rates vary substantially – from less than 20% to over 70% in terms of the value of losses reimbursed, based on annual data for 2021.[50]

2.33 A more consistent approach would benefit victims – and consumers more broadly – as there would be more certainty about how APP scams losses are treated by PSPs. This will increase trust in the payment system for consumers more generally, through an increase in their confidence that they will be able to recover any money lost where they have exercised sufficient caution.

2.34 We have not been able to quantify the scale of the benefits that this increased consistency and certainty for customer would bring. However, given the current wide variation in reimbursement rates, even within the same PSP across different time periods, moving towards a consistent level of reimbursement, based on a set of criteria that apply to all Faster Payments transactions, will lead to a substantial improvement in the welfare of victims and all consumers.

Level playing field across PSPs

2.35 In principle, we might expect competition between PSPs to lead to higher and more consistent levels of reimbursement for customers that fall victim to APP scams. This might particularly be the case if customers expected this to be provided as a standard feature of their current account service. However, many consumers are unlikely to make the decision of which PSP to open an account based on their expected level of

49 PSR CP21/3, *Authorised push payment (APP) scams – Call for views* (February 2021), page 16, Figure 4.

50 PSR analysis of UK Finance data collected from CRM Code members, 2021.

fraud reimbursement. The wide variation in reimbursement rates across different PSPs is evidence that competition on that parameter is not effective at present.

2.36 At present, ten PSPs are members of the CRM Code, and, as such, voluntarily provide reimbursement, in certain cases, to their customers. In addition, some PSPs outside the Code also provide material levels of reimbursement to their customers.[51] However, that leaves a large number of PSPs, accounting for a material share of Faster Payments transactions, providing little or no reimbursement to their customers. In addition, even among those PSPs that provide material levels of reimbursement at present, the rates of reimbursement vary widely.[52] A system of mandatory reimbursement with a consistent set of criteria will provide a level playing field between PSPs, which will benefit both customers and those PSPs that currently focus on protecting their customers from APP scam fraud.

Improved reimbursement rates for APP scam victims

2.37 As outlined above, APP scam volumes have been increasing over time, with victims often losing life-changing sums of money. This means that any improvement in reimbursement rate would likely have a significant impact to victims. As set out above, to the extent that reimbursed funds represent a cost to PSPs and a benefit to consumers, in the context of this cost benefit analysis they could be thought of as cancelling each other out. However, there are benefits to consumers in addition to the purely financial benefit of being reimbursed for an APP scam loss.

2.38 For victims, there are non-financial benefits to higher levels of reimbursement and greater certainty in relation to reimbursement. In addition to money lost to the fraud itself, customers may face psychological and other costs associated with these crimes. Even if they are fully reimbursed (weeks or months later), they will still suffer a cost for losing the money in the first place and will face the stress and anxiety of not knowing if and when, they will be reimbursed. Making scams less likely to happen in the first place will mitigate these issues. Our proposed policy will also increase trust in the payment system for consumers more generally through an increase in their confidence that they will be able to recover any money lost where they have exercised sufficient caution.

Costs

Increased investment in fraud prevention by PSPs

2.39 Mandatory reimbursement and a default 50:50 split of reimbursement costs between sending and receiving PSPs will lead to a substantial increase in the costs of reimbursing APP scams for almost all PSPs.

51 See Chapter 2.

52 PSR CP21/3, *Authorised push payment (APP) scams – Call for views* (February 2021), page 16, Figure 4.

2.40 As set out above, we have not considered the direct costs of PSPs increasing their rates of reimbursement as being a relevant cost for this cost benefit analysis. We have not taken the approach of directly balancing the costs of increased reimbursement that PSPs will face against the benefits of increased reimbursement that victims will receive. That approach would simply find a large cost on one side cancelled out by the same scale of benefit on the other. Rather, we have focused on the change in incentives and their effect that will be caused by our proposed policy.

2.41 We looked at the likely increase in PSPs' reimbursement costs from three perspectives in turn:

- For those PSPs that already reimburse a material share of their customers' losses on the sending side (for example, those CRM Code members that reimburse, on average, just under 50% of their customers' losses), their average reimbursement costs, as sending PSPs, are likely to increase, but may not change substantially. However, they will face substantially increased costs on the receiving side.
- For those PSPs that do not reimburse a material share of their customers' APP scam losses at present (as the sending PSP in the transaction), these PSPs will become liable for significant new costs.
- PSPs on the receiving side of transactions now account for a negligible share of reimbursement (less than 5%), and so will face substantially increased reimbursement costs under our proposals.

2.42 From all three perspectives, these increased reimbursed costs will mean that PSPs will now have much stronger incentive to invest in their fraud detection and prevention systems. The proposed policy will also lead to much stronger incentives for sending and receiving PSPs to cooperate effectively in fraud detection and prevention. It is these additional costs – from increased spending by PSPs on their fraud detection and prevention systems – that represents the relevant cost for the purposes of our cost benefit analysis, and is likely to be the most significant relevant cost that arises due to the proposed policy.

2.43 While we have not been able to quantify the likely costs with any degree of precision, we note a number of relevant points in assessing the broad scale of these costs.

2.44 First, as set out above, the rates at which individual PSPs send and receive APP scams vary widely. Given this, some PSPs will face much higher potential reimbursement costs than others. As a result, the incentives to invest in fraud detection and prevention will vary widely across individual PSPs. This will lead to the costs that different PSPs are incentivised to incur also varying widely, depending on the scale of the APP scam fraud that each PSP is sending and/or receiving.

2.45 Second, and related to this, the costs that individual PSPs are incentivised to incur will be proportionate to the scale of their fraud issue. For example, a PSP that currently sends £8 million worth of fraud and receives £12 million worth of fraud per annum would be incentivised to invest in fraud prevention measures that are proportionate to the costs of reimbursing victims in relation to that scale of fraud. This is in contrast to some other policies, where PSPs may be required to incur a fixed level of additional costs regardless of the scale of the problem being addressed at that individual PSP. For example, PSPs that are required to provide CoP checks will face the cost of introducing and maintaining the system regardless of the level of relevant APP scams or of misdirected payments that they face. Here, PSPs are incentivised to incur costs in proportion to the scale of the problem to be tackled.

2.46 Third, PSPs already expend resources in fraud detection and prevention, and many already incur the costs of reimbursing victims, at least partially. Given this, our proposed policy will provide incentives to invest in additional measures, over and above what PSPs are already doing. It is these incremental costs that are relevant to our assessment, not PSPs' current or total spending on APP scam detection and prevention. To take the example above, a PSP that currently sends £8 million worth of fraud and receives £12 million worth of fraud per annum: this PSP may already voluntarily reimburse £5 million of the losses that its customers incur as victims on the sending side. Our proposed policy would increase the PSP's reimbursement costs by £15 million. It is this additional reimbursement cost that incentivises incremental spending on fraud prevention, rather than necessarily the full £20 million of annual APP scam losses.

2.47 Fourth, the costs are likely to be higher in the early years of the proposed policy, as PSPs invest in their fraud detection and prevention systems, and set up processes to cooperate with other PSPs in detecting and preventing fraud and in pursuing funds and successfully recovering lost funds from fraudsters' accounts.

2.48 Fifth, our proposed policy allows PSPs to put in place a minimum threshold for a reimbursement claim (of no more than £100), to withhold an 'excess' (of no more than £35) and to set a time limit for claims (of no less than 13 months). These implementation options may help PSPs ensure that consumers take care in making small payments, minimise claims for civil disputes and maintain proportionate costs, while ensuring their consumers are appropriately protected.

2.49 Overall, while we cannot quantify the likely scale of the costs to PSPs, we consider that:

- these costs are likely to be proportionate to the problem being tackled (as reimbursement costs and so incentives to prevent fraud are directly linked to fraud sent and received at each PSP)
- only those additional costs that PSPs are incentivised to incur are relevant, not all spending on anti-fraud measures that PSPs incur
- much of the cost will arise in the early years, whereas the benefits of reduced fraud will continue to accrue, relative to a baseline of APP scam levels remaining high or even increasing further

Administrative costs of pursuing completed payments and resolving disputes

2.50 At present, in many cases of APP scams fraud, there is little or no contact between the sending and receiving PSPs. Increased reimbursement costs on the sending side and the introduction of significant reimbursement costs on the receiving side will mean that PSPs will have much stronger incentives to pursue recoveries, possibly following the trail of funds through multiple accounts and PSPs after the initial transaction which triggers the report of an APP scam.

2.51 In addition, there are likely to be cases where the sending and receiving PSPs dispute the appropriate split of reimbursement costs – an issue which rarely arises at present, outside the context of cases that are decided by the Financial Ombudsman Service.

2.52 In both cases, our proposed policy is likely to lead to PSPs incurring additional costs that they do not face at present, although we have not been able to quantify these.

Costs of investigating, delaying and stopping suspicious payments

2.53 In addition to the costs on PSPs of increased fraud detection, prevention and cooperation with other PSPs, there may also be costs to customers and business if PSPs introducing stronger controls also leads to a higher number of payments being queried, delayed or even declined, as set out in Chapter 3, above. Any increase in friction in the system, even if effective in reducing APP scam numbers, could also impose costs on other customers and business due to delayed or missed payments.

2.54 We have not been able to quantify the likely costs of any delayed or declined payments but note that the current industry initiatives to improve data sharing between PSPs (APP scams Measure 2) and increased incentives to improve fraud detection and prevention should help to minimise the number of payments delayed unnecessarily.

Other potential consequences of the proposed policy

2.55 As set out above, and in Chapter 3, increasing PSPs' liabilities to reimburse victims and, hence, incentivising them to invest more in fraud detection and prevention is the intended consequence of the proposed policy. There are also a number of other potential consequences that could lead to higher costs, on both PSPs and on customers.

2.56 **Increase in reported APP scam numbers:** Moving to a system of mandatory reimbursement could lead to an increase in the number of reported APP scams. At present, where reimbursement levels vary widely across PSPs and with many customers not being aware of the likelihood of their being reimbursed, it is likely that there are material numbers of APP scams that go unreported. Greater clarity and consistency for customers is likely to lead to an increase in the level of reported APP scams. On one level, this represents additional costs to PSPs, but it also represents a benefit to those customers that were previously left completely out of pocket having decided not to report their loss. As such, the net costs, if any (for example, increased administrative costs to PSPs), are likely to be modest.

2.57 **Customer caution and moral hazard:** Moving to a system of mandatory reimbursement could lead to an increase in payments where customers have not exercised sufficient caution, in the knowledge that any losses will be fully reimbursed. As set out in Chapter 4, we are not aware of conclusive evidence that, if consumers are more confident of being reimbursed, they will take less care in ensuring that their payee is not a fraudster.

2.58 While the evidence we have is limited:

- on one hand, the introduction of a reimbursement guarantee that is (almost) universal, mandatory, rather than voluntary, and well-publicised (unlike the CRM Code) could lead to increased moral hazard issues
- on the other hand, there are psychological costs to victims when they fall victim to a scam and, even where full reimbursement is expected, there may be financial costs (while the victim waits for a refund) and costs in terms of time and effort to pursue a claim

2.59 As above, we note that allowing PSPs to put in place a minimum threshold for a reimbursement claim (of no more than £100) and to withhold an 'excess' (of no more than £35), as well as the proposed exception for customer 'gross negligence', should provide incentives to customers to take sufficient care in making small payments, and should help to minimise claims for civil disputes and maintain proportionate costs for PSPs.

2.60 We would welcome any concrete, including quantitative, evidence on the risk that consumers would take less care.

2.61 **Potential exclusion of some customers:** As set out in Chapter 3, in response to requirements for mandatory reimbursement, some PSPs might consider restricting services to certain consumers, such as older consumers, because they may be perceived as being more likely to fall victim to APP scams. We have considered this risk as part of our equality impact assessment (see Annex 3).

2.62 An important aim of the proposed policy is to incentivise receiving PSPs to maintain robust policies around new accounts (for example, 'know your customer' checks) in order to prevent fraudsters setting up accounts. There is a risk that enhanced scrutiny could lead to certain consumers finding it more difficult to access some services as a result. While we might expect the overall cost to be small, this could have a material impact on some consumers. As above, we also expect PSPs to continue to treat all prospective customers equally. PSPs should treat current and prospective customers according to their obligations in the Equality Act 2010.

2.63 **Migration to other payment methods:** There are a number of ways in which our proposals could, in principle, lead to some switching away from Faster Payments for some payments:

- First, as set out in Chapter 3, if our proposals are successful in incentivising reduced APP scams, there is the potential for fraudsters to migrate to other payment schemes, including credit or debit cards, and CHAPS.
- Second, the potential for payments to be delayed or stopped as PSPs exercise greater caution in processing suspicious payments (as set out above), could also lead to customers switching to other payment methods.
- Third, the potential for PSPs to nudge payers away from Faster Payments and towards, for example, card payments, could lead, for example, to increased costs for payees.

2.64 While we have not sought to quantify the potential costs, if any, of any such migration, we note that:

- these alternative channels have existing consumer protections in place, for example, the consumer protection in card schemes, and the greater level of engagement with the PSP that typically takes place when making a CHAPS payment
- as set out in Chapter 4, the PSR is working closely with the Bank of England and the FCA on aligning reimbursement requirements across Faster Payments, CHAPS and on-us payments
- we would monitor any trend for increased fraud on other payment channels to inform any action that was needed

2.65 **Potential prudential implication for some PSPs:** As set out in chapter 3, respondents to our November consultation highlighted the potential cost implications of our reimbursement proposals for small PSPs and for certain business models. If reimbursement costs were large enough for some small PSPs, this could, in principle, have prudential implications – for instance, where firms face the cost of reimbursement and may not have the capacity to invest in fraud detection and prevention to combat the problem effectively. As set out in chapter 3, we continue to work with the FCA and the Prudential Regulation Authority (PRA) on how risks to individual small PSPs would be monitored and managed.

Conclusion

2.66 Considering these impacts in the round, we consider that the benefits of our proposed policy on mandatory reimbursement and the allocation of those costs between PSPs are likely to outweigh the costs of the proposed policy. In undertaking this assessment, we have sought to account for the likely timeframe in which these impacts will be realised. We recognise that some of these impacts may occur immediately and materialise mostly in the beginning of the policy, in particular, the costs to PSPs of increased investment in fraud prevention and in enhanced cooperation with other PSPs in tacking fraud and pursuing defrauded funds. On the other hand, most benefits may take time to fully materialise, but we envisage that they will continue throughout the period – for example, reduced incidence of APP scams, due to better prevention, is an impact that will continue to generate substantial benefits for providers and customers.

Annex 3
Public Sector Equality Assessment

In line with our Public Sector Equality Duty (PSED) under the Equality Act 2010[53], which includes having regard to the need to advance equality of opportunity, we must assess the likely equality impacts and rationale for any measures we propose and consult on. In this Annex we explore the impacts that we believe the measures we are considering (and their implementation) will have, including on those with relevant protected characteristics.

We ask for comments and evidence to support us in carrying out our assessment on our policy decisions following this consultation.

Approach to our PSED assessment

3.1 In developing the proposals discussed in this consultation, we have considered the matters set out in section 149 of the Equality Act 2010 (the Public Sector Equality Duty), particularly the impact of our proposed requirements for mandatory reimbursement on people with protected characteristics, which include:

- age
- disability
- gender reassignment
- pregnancy and maternity
- race
- religion or belief
- sex
- sexual orientation

53 The Equality Act 2010 (Specific Duties and Public Authorities) Regulations 2017, which have replaced the Equality Act 2010 (Specific Duties) Regulations 2011.

3.2 Our proposed requirements aim to protect consumers who fall victim to APP scams, by providing for mandatory reimbursement. As a result of our proposals we would expect increased efforts by PSPs to prevent APP scams, incentivised by the costs of reimbursement.

3.3 In developing our proposals, we have taken particular account of the interests of vulnerable consumers, who are more at risk of falling victim to APP scams. The FCA's definition of a 'vulnerable customer' is 'someone who, due to their personal circumstances, is especially susceptible to harm – particularly when a firm is not acting with appropriate levels of care', and, as set out in Chapter 4 of this consultation, we consider this definition is appropriate for our work on APP scams.

3.4 There is likely to be a significant overlap between vulnerable consumers and those with certain protected characteristics. There is evidence[54], for example, that shows that older consumers are more likely to be victims of APP scams. Those who have disabilities, such as those who are visually impaired or deaf, may also be more vulnerable to being victims of APP scams.

3.5 Overall, we believe that our proposals would have a positive impact on consumers who use the Faster Payments system, including those with protected characteristics – because the measures should reduce the risk of consumers becoming victims of APP scams and increase the likelihood of reimbursement if they do. Since vulnerable consumers are more at risk of falling victim of APP scams, and the significant overlap between vulnerable consumers and those with certain protected characteristics, we consider that our proposals would contribute to advancing equality of opportunity.

3.6 We have identified where some of our proposals could potentially risk poorer outcomes for some consumers with certain protected characteristics than for consumers as a whole. Our view is that these risks arise because the consumers with the relevant protected characteristics are, or are perceived to be, more vulnerable to APP scams. Therefore in the discussion below, where we consider the risks for vulnerable consumers, this also addresses the risks for consumers with relevant protected characteristics.

Risks associated with our proposals

Proposals to allow exceptions to mandatory reimbursement

3.7 We propose to allow a number of exceptions to mandatory reimbursement. We consider below how each of these exceptions could impact vulnerable consumers and how we propose identified risks are addressed.

54 https://www.ageuk.org.uk/surrey/about-us/news/articles/2022/scams-awareness/

Gross negligence exception

3.8 We propose, in Chapter 4, to allow PSPs not to reimburse a consumer if that consumer has acted with gross negligence. This is in order to maintain an incentive for consumers to exercise caution in making payments.

3.9 Vulnerable consumers may be more at risk from social engineering and less able to exercise caution and to protect themselves from APP scams. There is therefore a risk that vulnerable consumers could be disproportionately affected by the proposed exception to mandatory reimbursement in cases of gross negligence.

3.10 We therefore propose to exempt vulnerable consumers from our proposed gross negligence exception – that is, a PSP must reimburse a vulnerable consumer even if they have acted with gross negligence.

Minimum threshold and 'excess'

3.11 We propose to allow PSPs to apply:

a. a minimum scam value threshold before our mandatory reimbursement requirements would apply, up to a level of £100

b. a fixed 'excess' to the amount reimbursed, of no more than £35

3.12 The purpose of these proposed exceptions is to enable PSPs to ensure proportionate costs of mandatory reimbursement while providing for appropriate consumer protection for lower value scams. For example, the exceptions may incentivise consumers to exercise caution, and to use the proper dispute resolution processes for civil disputes, in relation to small payments.

3.13 Any minimum threshold or 'excess' applied by their PSP would, by limiting mandatory reimbursement, have a greater impact on APP scam victims who are in financial distress. We recognise that financial distress may be a factor in vulnerability, and that vulnerable consumers may be more likely to be suffer financial distress. We also recognise the current acute economic pressures on consumers.

3.14 The new Consumer Duty on firms[55], which the FCA is implementing, will require PSPs to focus on the real and diverse needs of their customers, including those in vulnerable circumstances, at every stage and in each interaction. In its guidance on vulnerable customers[56], the FCA says PSPs should consider both the potential positive and negative impacts of their products or services on vulnerable consumers. We would expect PSPs to carefully consider their obligations under the Consumer Duty and FCA guidance when deciding whether and how to apply a minimum threshold or 'excess'. To help PSPs, we propose to allow PSPs to exempt vulnerable consumers from any minimum threshold or 'excess' they implement.

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55 FCA FG22/5, *Final non-Handbook guidance for firms on the Consumer Duty* (July 2022).

56 FCA FG21/1, *Guidance for firms on the fair treatment of vulnerable customers* (February 2021).

Denial of payment services

3.15 Under our proposals set out in this consultation, PSPs will be incentivised to reduce the incidence of APP scams among their customers. There is therefore a risk that some PSPs reduce or deny banking or payment services to vulnerable consumers, including consumers with certain protected characteristics who they perceive as being more at risk of falling victim to APP scams.

3.16 To mitigate this risk, we will make it clear to PSPs in any decision to implement our proposed measures that they must ensure that the needs of people with disabilities, the elderly and other groups who may be vulnerable are met. For example, we will make it clear that consumers more at risk of becoming victims should not be refused or denied payment services to reduce numbers of APP scams. We expect PSPs to continue to treat all current and prospective customers, including vulnerable consumers, fairly and according to their obligations in the Equality Act 2010.

Increased reluctance to use payment services

3.17 There is a risk that vulnerable consumers reduce or cease their use of payment services because of greater awareness and fear of the risks of fraud arising from increased warnings and other scam prevention activity by their PSPs, which has been incentivised by our proposals.

3.18 We would expect that this risk would be mitigated to the extent that consumers would also acquire greater awareness of their rights to mandatory reimbursement if they did fall victim to an APP scam. We also consider that, to the extent that our proposals led to fewer APP scams, this would have a mitigating impact on fear of fraud. We therefore do not consider that we would need to take any further mitigating action. We would expect PSPs to make their customers, including vulnerable consumers, aware of the measures that they are taking to reduce APP scams as well as their customers' rights to reimbursement if they fall victim.

Slowing of payment services

3.19 Under our proposals, PSPs will be incentivised to reduce the incidence of APP scams. PSPs are likely therefore to refuse more payment orders – those that they consider suspicious. This could mean that more genuine payments are also stopped because they trigger PSPs' detection processes or are considered higher risk. There is the possibility that this might affect people with certain protected characteristics more than other customers, as they may be perceived as more vulnerable to becoming victims of APP scams.

3.20 Our view is that additional friction for a small proportion of payments is proportionate to preventing APP scams and achieving increased consumer protection, including additional protection for those most vulnerable to becoming victims.

3.21 We also note that current industry initiatives to improve data sharing between PSPs and increased incentives to improve fraud detection and prevention should help to minimise the number of payments stopped unnecessarily.

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