

Our draft cost benefit analysis framework

February 2024

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1 Executive summary

- 1.1** In this document, we explain our cost benefit analysis (CBA) framework. We use this framework to help us develop policies we can expect to have a positive impact.
- 1.2** It is important that we base our policies on appropriate and informed economic evidence, which will often include CBAs. They help us examine whether regulatory action is likely to result in an overall positive impact. We think it is important to be transparent about how we use CBAs, which is why we are publishing our draft CBA framework at this stage.
- 1.3** In addition, the Financial Services and Markets Act 2023 (FSMA 2023) requires the Financial Conduct Authority (FCA) to establish an independent CBA Panel. It also amends the Financial Services (Banking Reform) Act 2013 (FSBRA) and requires us to publish a statement of policy in relation to CBA after consultation with the FCA CBA Panel. Once the FCA CBA Panel is operational, we will consult with it on our CBA framework. We will then publish a draft statement of policy for public consultation.

Why we use CBAs

- 1.4** CBAs can serve several internal and external purposes. Considering the potential impacts is part of the development of our regulatory interventions.¹ The CBA process is not simply about justifying a policy at the end of the process; it is an integral part of the analysis to develop policies. While there may be a final output (the published cost benefit analysis statement) at the end of the process, value may also be derived from the analysis carried out during the development stages, which assists in the wider decision-making process. Our CBA framework thus discusses both the CBA process and the output (which sets out a view of the costs and benefits to inform the final decision about the intervention and, if appropriate, may comprise a specific CBA document or chapter).
- 1.5** As an economic regulator, considering the economic evidence within a CBA framework is one of the tools that help us make effective and robust decisions, but such analysis is one input into decision-making that needs to be considered among other relevant factors.
- 1.6** CBAs can also help us communicate the economic reasoning behind our proposed interventions to stakeholders.

1 By 'regulatory intervention', we mean any action we take using our powers under sections 54 to 58 of FSBRA. The framework we present here applies directly to interventions under sections 54 and 55 of FSBRA. For any action we might take using powers set out in sections 56 to 58 of FSBRA, we will consider on a case-by-case basis whether the use of CBAs and thus the application of this framework would be meaningful and useful.

- 1.7** Our CBAs may compare a range of options for different regulatory actions and at the minimum compare a proposed intervention against the 'do nothing' option.² They allow us to test early assumptions and likely impacts (quantified as much as practicable and proportionate) with stakeholders. Testing our initial economic analysis in this way can help target our information gathering and ensures that final policy positions are supported by consistent, robust and relevant data.

When we carry out CBAs

- 1.8** We often carry out CBAs for our proposed regulatory interventions, whether or not there is a specific legal requirement to do so.
- 1.9** In some circumstances, we may rely on a higher-level appraisal of evidence, rather than developing a specific CBA. This depends on a number of factors, chiefly the proportionality of the resources needed to conduct detailed analysis for a CBA and the extent to which it would materially affect any ultimate conclusions, which may include considerations of the degree of uncertainty around the potential impacts of an intervention.

What we cover in CBAs

- 1.10** Our CBAs follow common principles and will take into account best practice. The precise methodology we apply in individual CBAs depends on case-specific factors, including the data available and the nature of the costs and benefits being assessed. We explain the specific methodologies we use within individual CBAs.
- 1.11** Our CBAs explore the likely overall balance of impacts, based on appropriate quantitative and qualitative evidence. In general, our primary focus is not to attempt to provide single point estimates for overall net impacts. Instead, we aim to identify the regulatory approaches that are likely to lead to better or more appropriate outcomes for people and businesses using payment systems. Taking account of inherent uncertainties, we look for a course of action whose positive effects are likely to outweigh or justify any negative effects.

How we develop CBAs

- 1.12** Our analysis of the evidence starts at the beginning of the policy cycle and evolves alongside policy development. Early analysis focuses on identifying and describing current market outcomes. Using frameworks such as causal chains, the analysis will also consider how regulatory intervention might materially change these market or other relevant outcomes, both positively and negatively. Later, analysis helps us narrow down the potential policy options. Finally, we assess the likely costs and benefits of a preferred policy option. In cases where we need to publish a formal CBA document, it will reflect these stages.
- 1.13** Engagement with external stakeholders is a key part of the CBA process. In addition to communicating our economic reasoning to stakeholders, CBAs can help us test our initial assessments and gather further evidence from stakeholders.

² We discuss the appropriate counterfactual, specifically the 'do nothing' option, in paragraph 5.19.

2 Introduction

Purpose and scope of this framework

- 2.1** The Payment Systems Regulator (PSR) is an independent, sector-specific regulator. Our mission is to ensure that payment systems are accessible, reliable and secure, and represent value for money. We promote competition and innovation and protect the interests of people and businesses that use payment systems.
- 2.2** Our regulatory tools include general and specific directions and requirements, and written guidance.³
- 2.3** Our regulation aims to be outcomes-focused and evidence-led. We act only where our intervention would be appropriate and proportionate. Economic appraisal – including, where appropriate, in the shape of formal CBAs – assists us in assessing the expected impact of a proposed intervention. Considered alongside other evidence-based analyses, a CBA process can help inform our decisions on whether and how to act.
- 2.4** The law requires us to prepare and publish CBA documents in certain areas of our work – namely, before imposing a generally applicable requirement.⁴ We do though also develop and publish CBAs where informative and proportionate even where we might not be required by statute to do so. This document sets out a basic framework for how, when and why might use CBAs in both scenarios.
- 2.5** The Financial Services and Market Act 2023 (FSMA 2023) amends the Financial Services (Banking Reform) Act 2013 (FSBRA) so as to require us to publish a ‘statement of policy’ on our approach to CBAs. Before publication we must share our proposed approach with the Financial Conduct Authority’s (FCA’s) expert CBA Panel for comment.⁵ We must also consult the CBA Panel on any CBAs we carry out that are required by statute.⁶
- 2.6** Publishing our CBA framework at this stage increases transparency and understanding around our approach to CBAs. This gives our stakeholders an opportunity to provide information that may materially assist our work.
- 2.7** When we conduct a CBA, we typically apply the principles set out in this document. However, we consider each case on its own facts, which means that we apply the framework flexibly and may adapt our approach where the facts indicate that it would be appropriate to do so. Should we do so, we will explain our reasons in the relevant CBA.

3 More information about our legal functions and powers is available at: www.psr.org.uk/how-we-regulate/regulatory-framework/

4 Section 104(3) of FSBRA.

5 Chapter 7 of this document sets out our next steps with regards to the publication of a statement of policy.

6 Except for CBAs that are listed in the statement of policy as excluded from the obligation to consult.

What we mean by 'CBA'

- 2.8** As we explain throughout this document, establishing current market outcomes and potential harms and/or market failures, considering the likely economic impacts of potential interventions and other aspects of economic appraisal are always part of our policy development, whether or not these are summarised and published in the form of a specific CBA document.
- 2.9** In principle, the term 'cost benefit analysis' could refer to any one of three related but somewhat distinct concepts:
1. The framework and process of how we consider and factor in the different elements that underpin an assessment of costs and benefits mentioned in paragraph 2.8, above.
 2. The act of applying that framework and process – that is, the act of analysing costs and benefits.
 3. The summary and evaluation of that analysis within a single (published) document.
- 2.10** Our CBA framework will discuss all three of these concepts. While distinguishing between these concepts is not always necessary, where it is necessary, we refer to 'CBA process' or 'CBA framework' (when referring to 1, above), 'CBA' (when referring to 2, above) and 'CBA document' or 'CBA statement' (when referring to 3, above).

Structure of this document

- 2.11** The remainder of this document is structured as follows:
- **Chapter 3 – Why we use CBAs:** We set out the purposes of our CBAs and how we see them being applied in the most useful way.
 - **Chapter 4 – When we carry out CBAs:** We explain the typical circumstances in which we develop and publish CBAs.
 - **Chapter 5 – What we do in CBAs:** We present the scope and high-level methodology of our CBAs, including the questions we try to answer and how we go about answering them.
 - **Chapter 6 – How we develop CBAs:** We explain the processes involved in CBA development.
 - **Chapter 7 – Next steps:** We set out the steps following this consultation process.

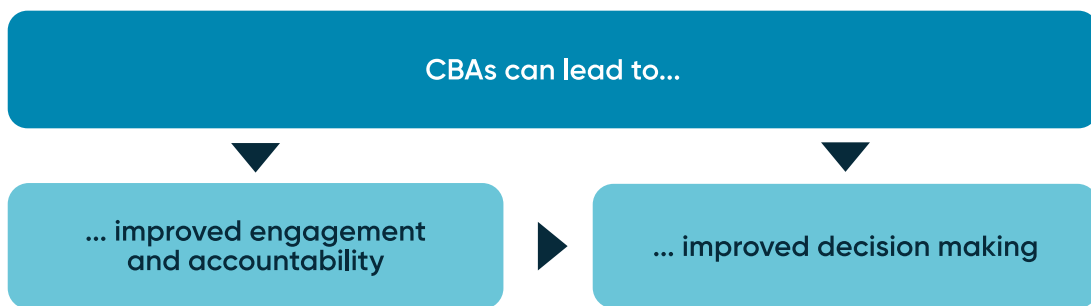
3 Why we use CBAs

Using a CBA framework provides a consistent and structured process for assessing the impacts of our proposed regulatory interventions. This helps ensure that we make effective, evidence-based regulatory decisions.

3.1 While applying a CBA framework may present some limitations and challenges, it can also offer significant benefits, which shape the core principles that we use when carrying out individual CBAs. Our rationale for applying a CBA framework drives when and how we carry out CBAs.

Benefits of CBAs

Figure 1: Purpose of CBAs



Improved engagement and accountability

3.2 We think that engaging transparently with stakeholders and presenting the evidence on which we base our regulatory interventions have an importance beyond fulfilling our legal requirements. This is why we sometimes publish CBA documents for regulatory interventions where there is no legal requirement for us to do so. Even where we decide not to publish a formal CBA document, we are still led in our decisions by evidence on the likely impacts of our actions. CBA goes beyond its application within published CBA documents.

3.3 CBA provides a well-understood and consistent framework for explaining the evidence and reasoning underlying our regulatory approach. For example, CBA documents published alongside policy consultations allow us to test different options, gathering evidence and sharing assessments of possible impacts with relevant stakeholders, whose responses can then help inform further policy development.

Improved decision-making

3.4 Improved engagement and accountability can, in themselves, ultimately result in improved decision-making by ensuring that stakeholders' views are considered appropriately. CBAs also help improve policy development and decision-making more directly. Early on, a CBA framework provides a structure within which to define both the

problem and the outcomes we are seeking to achieve. This can help frame the ultimate policy objectives.

- 3.5** Later in the process – for example, when consulting on a proposed regulatory intervention – a CBA framework can be used to test options and the associated estimated impacts. It can also help us gather further evidence, including from stakeholders. This strengthens the evidence base for final policy development.
- 3.6** In the final stages, a CBA framework can help highlight uncertainties as well as wider effects, such as equality and distributional impacts. It can also provide a structure to identify a preferred option among a set of possible alternatives.
- 3.7** Through the whole policy development cycle, this framework, and the individual CBA documents it generates, can help ensure that our decisions and policy development are based on solid and proportionate evidence. This approach allows us to assess and present the relevant economic arguments for why a particular regulatory intervention is needed and how it will lead to a better outcome than the ‘do nothing’ option.

Potential limitations of CBAs

- 3.8** Our CBA framework provides a structure within which to analyse potential policy interventions across the stages set out above. However, not all analysis we carry out and that might inform our decisions is done within a CBA framework. Furthermore, we have to take into account the practical limitations of CBAs and be aware that they are ultimately used to inform decisions. We do not see them as an exercise that seeks to provide a precise estimate or forecast for each specific impact or combined impacts over a specified timeframe.
- 3.9** The likely impacts of regulatory intervention can be uncertain, especially when an intervention applies to new or rapidly changing markets. Summarising costs and benefits within a single summary figure may not take appropriate account of this uncertainty or may not capture some of the nuances of these effects. This limitation applies mainly if CBAs focus overly on a single figure rather than on providing a sense of overall trade-offs and the likelihood of different outcomes occurring.⁷
- 3.10** Precisely estimating the benefits of regulatory intervention can be particularly challenging where we are considering intervening to prevent potential harm from materialising in the first place. CBAs can run the risk of systematically favouring interventions that aim to remove a harm that has already happened over those that aim to prevent an anticipated harm before it occurs.
- 3.11** Many impacts do not have clear prices associated with them, so monetisation of these might be infeasible and/or unduly onerous. Our CBA framework acknowledges that quantification or precise monetisation may not always be feasible or desirable. CBAs that rely solely on monetised figures fail to take account of ‘immeasurable’ or ‘hard to measure’ impacts that can still be significant and important. For this reason, our approach to monetising net benefits takes account of the purpose of the analysis and does not over-refine monetary estimates.

⁷ As discussed further in paragraphs 3.13 to 3.15, we think a CBA should take account of the degree of uncertainty. We discuss how we do this within our CBAs in more detail in paragraphs 5.38 to 5.40.

- 3.12** Some of our regulatory interventions are systemic in nature. That is, they can cause immediate compliance and implementation costs with the aim of creating long-term or diffuse but significant benefits. There is a risk that a CBA fails to express these long-term benefits adequately.
- 3.13** Some of these issues can partially be addressed by:
- applying an appropriately flexible methodology that can be tailored to specific cases⁸
 - an appropriate assessment of risks, uncertainties and limitations of the analysis⁹
 - factoring in qualitative estimates alongside quantitative estimates
- 3.14** Rather than the derivation of specific single numbers that may be uncertain or only spuriously accurate, our CBAs focus on plausible ranges and probabilities of impacts, supported by appropriate sensitivity analysis. We will also apply our regulatory judgment when balancing different effects, in particular where some impacts are easily quantified while others are uncertain and difficult to quantify (and/or occur in different timeframes). See Chapter 5 for more detail on our approach to uncertainty.
- 3.15** Our primary objective for CBAs is to present a clear logic for our proposed regulatory interventions as well as an assessment of the likelihood that costs will be outweighed by benefits. A CBA should present this logic clearly and help ensure that we make policies informed by this analysis.

Our core principles

- **Our CBAs are part of our policy development process and may include comparison of regulatory options.** They are not about justifying a policy at the very end of the process. Their value lies not only in the final publication but also in the support they provide to our wider decision-making during the development stages.
- **Our CBAs help us make effective decisions, but they are not the only means of doing this.** CBA is one of several inputs into decision-making, and we consider it alongside other relevant factors and pieces of evidence. CBAs focus on economic impacts, but it is usually infeasible to summarise all impacts in a single number. Sometimes a CBA may identify costs that we judge are worth trading off against other objectives, such as the protection of vulnerable customers.
- **Our CBAs help us communicate the economic reasoning behind our proposed interventions to stakeholders.** We assess the economic case for intervention, establishing whether the benefits associated with a proposed intervention are likely to outweigh any costs.
- **Our CBAs provide an opportunity to consult effectively.** We can test our assumptions and consideration of likely impacts with stakeholders, including potentially seeking additional information to help improve our assessments.

8 For example, applying smaller discount rates for longer-term impacts.

9 For example, analysis that highlights that the costs and/or benefits of an intervention are extremely onerous to estimate and/or uncertain is useful information for decision-making.

4 When we carry out CBAs

Applying a CBA framework and processes in a proportionate manner always forms part of our policy development, and we may develop and publish CBA documents for our proposed regulatory interventions whether there is a specific legal requirement to do so or not.

Sometimes we may decide that the development of a CBA with meaningful impact estimation is not feasible or proportionate, or that we need to intervene urgently to protect service users from significant harm. We might not develop and publish specific CBA documents in such cases, but consideration of relative costs and benefits will still guide our thinking.

Legal framework and requirements

- 4.1** Section 53 of FSBRA sets out regulatory principles to which we have to have regard when discharging any of our general functions. These requirements include proportionality – that is, our regulatory intervention must be proportionate to the problem we aim to address. CBAs are one tool that can help us address part of this question of proportionality.¹⁰
- 4.2** Section 104 of FSBRA requires us to carry out CBAs in certain circumstances. We must publish a draft of any ‘generally applicable requirement’¹¹ we are proposing with a number of explanatory documents, unless we consider that publication would cause too much delay and potential prejudice to the interests of service users or potential service users. These documents include a CBA statement.
- 4.3** Section 104(6) of FSBRA also requires us to publish a new CBA document if a final requirement differs from the draft version in what is, in our opinion, a significant way.
- 4.4** There are other requirements that do not specifically refer to the use of CBAs but for which the use of CBAs might be relevant.¹²

10 CBAs are also different from any evaluation of a regulatory intervention once it is in force. This document does not address this different type of analysis.

11 Giving general directions under section 54 or general requirements under section 55.

12 Such as the Public Sector Equalities Duty within the Equality Act 2010.

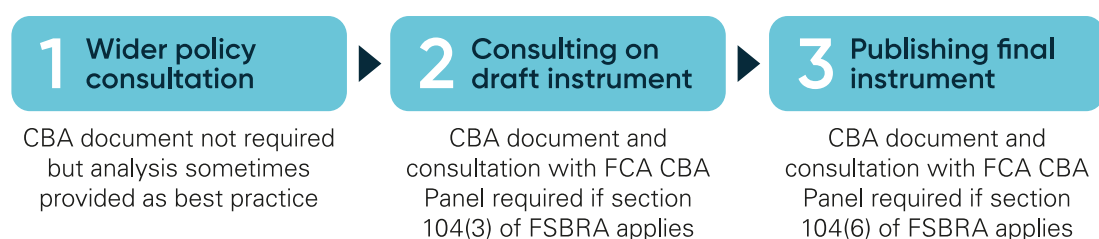
PSR best practice

Conducting CBAs when reasonable

4.5 We do not have an explicit statutory requirement to carry out and publish CBA documents for all our regulatory interventions. For example, they are not required for specific directions. However, in light of the benefits already discussed, and where it would not involve a disproportionate use of resources, our practice is to carry out specific CBAs for our regulatory interventions. See paragraphs 4.9 to 4.16 for circumstances in which we might decide the development of a specific CBA and the publication of a CBA document would be disproportionate. The degree of detail we provide in a CBA document will also reflect this proportionality criterion.

Conducting CBAs early

Figure 2: Stages of cost benefit analysis



4.6 Section 104(3) of FSBRA refers to the need to publish a CBA document alongside consultation on a legal instrument and the possible need for another CBA document if section 104(6) applies. It does not specify a requirement to publish a CBA document alongside possible earlier policy stages, such as a call for views or wider policy consultations.

4.7 At Stage 1 we develop our economic evidence alongside early policy development. This early analysis will aim to assess likely impacts, but there still may be uncertainties around some impacts and the finer details of the proposed policy. We aim to publish early analysis either in the form of a CBA or embedded within general policy consultations. This can help us test our initial assessments and methodologies with stakeholders, and to gather evidence for a more refined analysis in later stages.¹³

4.8 Where we need to refine an earlier CBA in response to evidence gathered during consultation, we will publish an updated CBA statement alongside a final policy. This also applies where we need to reflect a substantial change in policy following consultation.¹⁴ Our normal practice is to identify the relevant CBA analysis on which a final decision rests.

¹³ We do not typically publish CBAs alongside even earlier documents, such as calls for views, as we do not typically test any specific forms of regulatory intervention at this stage. We might though provide some analysis, such as an assessment of existing market outcomes and the potential scope for change, within such documents.

¹⁴ This is also a matter of compliance with section 104(6).

Exemptions

4.9 Sections 104(10) and 104(11) of FSBRA provide for exemptions from the CBA requirements established by sections 104(3) and 104(6).

Exemptions under 104(10) FSBRA

4.10 Section 104(10) states:

Subsections (2)(b) and (3) to (6)¹⁵ do not apply if the Payment Systems Regulator considers that the delay involved in complying with them would be prejudicial to the interests of those who use, or are likely to use, services provided by regulated payment systems.

4.11 A number of considerations may be relevant to our assessment of whether undertaking a CBA would result in a prejudicial delay, such as:

- the magnitude of harm to service users, whether in terms of the scale, likelihood and/or nature of the detriment
- the likelihood that the results of a CBA could meaningfully change decisions and/or the clarity of the available assessment
- the extent to which affected parties agree that the situation gives rise to a degree of urgency
- the degree of anticipated delay caused by undertaking a CBA

4.12 The above list is not exhaustive, and in each case we will balance all of the relevant considerations in the round to decide whether the exemption is met.

Exemption using section 104(11) of FSBRA

4.13 Section 104(11) of FSBRA states:

Subsections (3)(a) and (6) do not apply if the Payment Systems Regulator considers that, making the appropriate comparison—
(a) there will be no increase in costs, or
(b) there will be an increase in costs but the increase will be of minimal significance.

4.14 When considering any regulatory intervention, our practice is to carry out some initial analysis of likely impacts. After that stage we might decide that initial analysis indicates that there are no costs – that is, that section 104(11)(a) of FSBRA applies. In these circumstances, so long as we had identified at least some potential benefits, we would not consider it necessary to undertake a formal CBA.

¹⁵ These subsections essentially establish that we need to consult and that our consultations on generally applicable requirements need to be accompanied by CBAs.

4.15 Should initial analysis identify only minor costs (that is, costs of ‘minimal significance’), we will consider a number of factors in determining whether section 104(11)(b) of FSBRA applies. These factors include:

- **The costs of developing and publishing a CBA alongside the consultation:** These include costs in time as well as in resources. If we consider that these costs are insignificant, we might publish a CBA that focuses on benefits and a qualitative assessment of costs that explains why we consider them to be immaterial.
- **Consensus on whether costs are negligible:** If, for example, we received consistent feedback from stakeholders during early engagement that regulatory intervention would be beneficial and would not impose any significant costs, we would consider there to be less need for a more detailed CBA.
- **The distribution of costs:** Even if costs are insignificant in aggregate – especially when compared to overall benefits – we will still consider how they affect individual parties or groups. If a regulatory intervention causes insignificant costs at the aggregate level but significant costs for specific parties, which in turn could affect competition or innovation, then we will be less likely to make use of this exemption.

CBA not required by section 104 of FSBRA

4.16 Whether or not section 104 of FSBRA applies, we aim to apply a CBA framework and consider publishing CBA documents for our regulatory interventions as long as their analysis can provide meaningful insight and any resource required for their development is proportionate.¹⁶ The exemptions discussed above only apply to statutory CBAs (as the general requirement in section 104 has to apply in the first place to be exempt from it). However, we would also consider these principles when deciding whether to develop a CBA for any intervention. In practice, we would usually expect to apply the principles behind sections 104(10) and 104(11) in all cases.

Our core principles

- **We will typically apply a CBA framework to our proposed regulatory interventions.** We will consider developing and publishing a CBA document in cases where there is no legal requirement to do so.
- **We may decide not to conduct a CBA using the exemptions listed in FSBRA subject to case-specific circumstances.** We consider whether the resources needed to carry out a CBA are proportionate to the problem under scrutiny, and whether a CBA is likely to change any ultimate conclusions.

¹⁶ This refers to both the resource required of us in developing the CBA and the resource that would be required of regulated parties – for example, in responding to necessary data requests.

5 What we do in CBAs

The precise methodology we use in our CBAs necessarily differs on a case-by-case basis. While our CBAs follow a common structure and set of principles, factors such as data availability determine the methods we use.

Our analysis is largely based on four implicit types of analysis:

- Identification of impacts
- Qualitative assessment of impacts
- Quantitative assessment of impacts
- Monetised assessment of impacts

In some cases, not all of these are feasible or proportionate. We do not consider quantified impacts to necessarily be of higher importance than impacts that are ‘only’ assessed qualitatively.

Our primary focus within CBAs is not to provide single point estimates for overall net impacts. Instead, we aim to provide an appropriate description of the likely overall balance of impacts, taking into account risks and uncertainty.

Legal framework

5.1 Section 104(7) of FSBRA provides the following definition of a CBA:

- (a) *“an analysis of the costs together with an analysis of the benefits that will arise*
 - (i) *If the proposed requirement is imposed, or*
 - (ii) *If subsection (6)¹⁷ applies, from the requirement imposed, and*
- (b) *subject to subsection (8) an estimate of those costs and those benefits.*

5.2 This is qualified by the exceptions set out in section 104(8) of FSBRA:

If, in the opinion of the Payment Systems Regulator—

- (a) the costs or benefits referred to in subsection (7) cannot reasonably be estimated, or
 - (b) *it is not reasonably practicable to produce an estimate,*
- the cost benefit analysis need not estimate them, but must include a statement of the Payment Systems Regulator’s opinion and an explanation of it.*

¹⁷ Section 104(6) of FSBRA states that if, in the view of the PSR, a final requirement substantially differs from the one initially consulted on, the PSR must publish details of the difference as well as a new CBA.

5.3 This means that a CBA need not include estimates if section 104(8) applies. This allows for a more qualitative assessment where quantification and monetisation might not be reasonable or practicable.

5.4 While sections 104(7)(a) and 104(7)(b) of FSBRA distinguish between analysis and estimation of costs and benefits, in practice this distinction is often blurred. We typically consider 'estimation' to be a type of analysis, particularly when conducting quantitative and monetised assessments. Similarly, it is arguable whether the provision of a 'rough' range of possible impacts or a relative classification – for example, into 'high', 'medium' and 'low' impacts – constitutes an estimation.

5.5 We start with the intention to quantify and monetise all significant impacts. Our judgement as to whether some effects 'cannot reasonably be estimated' or whether it is 'not reasonably practicable to produce an estimate' depends on a number of factors and criteria, such as:

- **The degree of uncertainty around an impact:** Where the degree of uncertainty around an impact is substantial, we will first consider the use of meaningful ranges and sensitivity analyses but might also rely on qualitative assessments. In instances where we can reasonably quantify only one element (for example, only the costs) we might also rely on the use of break-even analysis to provide an assessment of:
 - a. the scale of benefits that would have to materialise to offset these costs
 - b. the likelihood of that being the case
- **The information available and the cost of gathering further data:** As discussed further in paragraphs 5.11 to 5.13, the resources we allocate to our CBAs must be proportionate. This means that we are less likely to provide a specific value for an impact where creating an estimate would require the use of substantial resources – for example, due to limited data availability. This applies especially where initial analysis suggests that the impact in question is likely to be minor.
- **The balance of other costs and benefits:** If the balance of other estimated costs and benefits is such that one side clearly outweighs the other, we might judge that further estimation of other, smaller effects would not change the balance materially.

5.6 In instances where we deem section 104(8) to apply, and where estimation of costs and benefits is not required, our CBAs would typically focus solely on the identification of impacts and elements of qualitative assessments. They would not provide quantitative or monetised assessments.

Our methodology

Types of analysis and estimation

- 5.7** Our analysis and estimation of impacts falls into four types:
- 1. Identification of relevant costs and benefits:** This is often best done within the context of causal chains and includes assessing which parties are likely to be affected and how, and in some cases, where relevant, which impacts are more 'direct' or 'indirect'. Direct impacts are first-order effects that are likely to occur as an immediate consequence of the intervention, while indirect effects are more general-equilibrium effects whose materialisation is typically less certain.
 - 2. Qualitative assessment of impacts:** For example, this might involve sorting effects into 'low', 'medium' and 'high' impact categories.
 - 3. Quantification of the scale of the likely impact:** For example, 'The measure will result in a x% reduction or prevention of fraud cases.'
 - 4. Monetisation of impacts:** That is, assigning pound values to impacts.
- 5.8** All analyses, but in particular 2, 3 and 4, are supported by initial information- and evidence-gathering exercises, followed by synthesis (that is, collating and summarising existing information contained, for example, in relevant academic research). Where we decide that existing analysis is unlikely to form a robust enough evidence base, we will aim to fill gaps in the evidence base identified by the synthesis of existing evidence with primary research, including by gathering necessary data.
- 5.9** Data and information to support any primary analysis may come from different sources. We may use stakeholder feedback gathered as part of consultations or within meetings and discussions. Where available, we may rely on publicly available data sources (for example, the Office for National Statistics), data published by other regulators, or data and information about the sector we gather routinely while carrying out our functions (for example, during our monitoring and enforcement efforts). We may utilise payments data gathered and published by stakeholders such as UK Finance or Pay.UK. Alternatively, where proportionate, we may gather bespoke data and evidence – for example, via commissioning surveys or use of our information-gathering powers under section 81 of FSBRA.
- 5.10** These types of analysis build on each other: for example, impacts must be identified before they can be quantified. However, we do not consider the list of analysis types in paragraph 5.7 to be necessarily in hierarchical order. For example, we do not consider a quantitative assessment of a particular impact to be of higher importance than a qualitative assessment. Feasibility or proportionality might dictate that some CBAs stop short of quantifying or monetising some impacts we identify, but in itself that does not mean those impacts are less important.

Table 1: Types of analysis and common techniques

Type of analysis	Purpose of analysis	Examples
Identification	Determining affected parties and the relevant types of impact	<ul style="list-style-type: none"> • Application of basic supply and demand theories • Analysis of economic incentives to identify likely responses to regulatory intervention • Use of logic chains to analyse likely effects of regulatory interventions • Consideration of behavioural science evidence to predict individuals’ likely behavioural responses
Qualitative	Providing a sense of likely scale of different impacts	<ul style="list-style-type: none"> • Case studies • Consultation responses and stakeholder feedback • Qualitative evidence contained in surveys or structured focus group interviews
Quantitative	Providing a more detailed estimation of the magnitude of impacts	<ul style="list-style-type: none"> • Estimated resource/time impacts on regulated companies • Data analysis to estimate reduction in or prevention of number of scams and misdirected payments as a result of additional authorised push payment (APP) scam protections • Econometric analysis
Monetisation	Applying monetary values to quantitative impacts	<ul style="list-style-type: none"> • Applying relevant wage and non-wage costs to quantified compliance impacts • Using value of time estimates to translate time savings into monetary values • Willingness-to-pay approaches where clear market prices do not exist

Proportionate analysis

- 5.11** Our analyses, and the resource and time they may require, should be proportionate to the likely impacts of a proposed intervention, the benefits of the CBA work required, the degree to which additional analysis could feasibly reduce uncertainty and the resources and time available to the PSR and stakeholders. We also have to be mindful of the degree of burden any data and information requests might impose on regulated firms.
- 5.12** The level of resources we devote to developing CBAs is case-dependent. In some cases, we may decide to rely predominantly on qualitative evidence gathered via stakeholder engagement. In others, we may be able to conduct quantitative and monetised assessments using detailed statistical, data science or econometric methods. The decision on which approach we take is typically based on proportionality considerations. When planning for the analytical needs of a specific case, we consider several criteria:
- **Likely magnitude of impacts:** If initial analysis shows that impacts in terms of costs and benefits are likely to be small, we may judge that it would not be proportionate to carry out more detailed quantitative analysis for the purpose of improved accuracy.
 - **The availability and reliability of existing data and evidence:** Where there is a reliable body of existing data and evidence, it can be more proportionate to use and expand on that evidence rather than to carry out new primary research. For example, this is more likely to be the case where an intervention builds on existing policy whose impacts are well established.
 - **The degree of uncertainty of impacts and ability to reduce it:** Where the initial assessment points to a very high level of uncertainty with a material effect on the likely balance of impacts, we might need to conduct more detailed analysis to reduce it. In contrast, the use of more resource-intensive analytical methods would likely not be proportionate if it was unlikely to reduce the degree of uncertainty.
 - **Distributional impacts and stakeholder views:** Our CBAs focus primarily on aggregate effects, but we also consider impacts on individuals and groups. If our initial analysis identifies considerable distributional effects, we may consider more detailed analysis to identify different impacts on vulnerable groups, including those with protected characteristics.
 - **The time-sensitivity of our proposed intervention:** Where we assess that quick intervention is required to reduce or avoid significant harm to the users of payment systems, we may consider the use of less resource- and time-intensive approaches as proportionate.
- 5.13** Proportionality also informs the form in which we present our economic evidence. In some cases, our analysis of costs and benefits might be presented in a separate, stand-alone CBA document. In other circumstances, we might present it as an annex to a policy consultation or policy statement. We have also explained that we always apply a CBA process even if we do not aim and are not required to develop and publish a CBA document. In such cases, the economic analysis that resulted from the CBA process might be presented within a 'formal' CBA document or embedded within the arguments set out in a policy consultation or statement of policy.

Structure

- 5.14** In our analysis of potential regulatory interventions, we typically consider standard best-practice principles of economic appraisal, such as those set out in the Treasury’s *Green Book*. Therefore, the general structure of our analyses will often look similar to CBAs developed by other regulators or impact assessments developed in central government. While structures and approaches can differ case by case, an archetypal CBA could contain some or all of the elements outlined in Table 2.

Table 2: Typical CBA elements and usual types of analysis

Chapter title	Contents
<ul style="list-style-type: none"> The case for intervention Policy objectives and desired outcomes Options 	<ul style="list-style-type: none"> Identifying the reason for intervention, options for intervention and outcomes via the use of causal chains. See paragraphs 5.15 to 5.19 for more detail.
<ul style="list-style-type: none"> Costs and benefits Summary assessment of net impacts 	<ul style="list-style-type: none"> Building on the previous analysis, providing a more detailed assessment and estimate of likely impacts using qualitative and quantitative techniques. See paragraphs 5.20 to 5.27 for more detail.
<ul style="list-style-type: none"> Wider considerations and impacts, such as distributional and equality considerations 	<ul style="list-style-type: none"> Identifying less immediate impacts, such as distributional or equality considerations. May use qualitative and quantitative techniques where proportionate. See paragraphs 5.28 to 5.35 for more detail.
<ul style="list-style-type: none"> Risks 	<ul style="list-style-type: none"> Identifying policy risks and possible unintended consequences, often as part of causal chain analysis. See paragraphs 5.36 to 5.37 for more detail.
<ul style="list-style-type: none"> Uncertainty 	<ul style="list-style-type: none"> Identifying uncertainty behind assumptions and quantified impacts, and possible quantification via tools such as sensitivity or scenario analysis. See paragraphs 5.38 to 5.42.

Case for intervention

- 5.15** Each of our CBAs contains an assessment of current market outcomes and an explanation of why an intervention could help improve outcomes for those making or receiving payments. Within this explanation we aim to assess the source of ‘sub-optimal’ market outcomes or market failures.

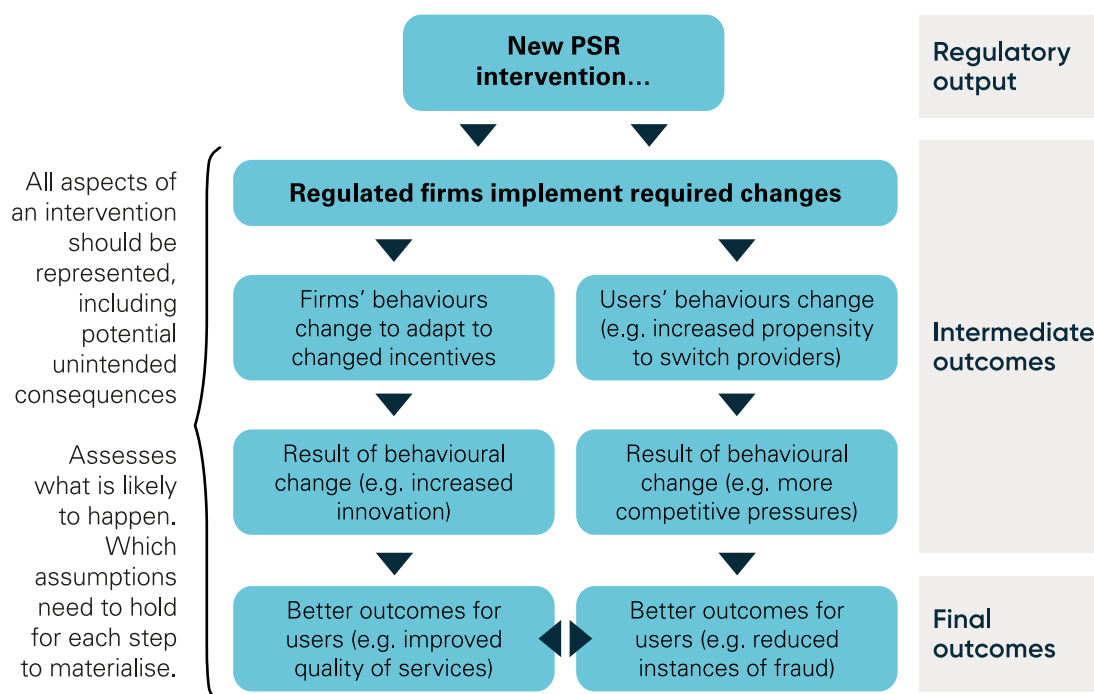
5.16 A high-level assessment of the potential scale for improvement in outcomes is a further focus in the early stages of a CBA to help inform policy before a more detailed impact estimation on options for intervention can be carried out.

Policy objectives and desired outcomes

5.17 Our analysis sets out the intended policy outcomes and the economic reasoning of how the proposed policy is likely to achieve them. In future, we would typically aim to use causal chain logic.

5.18 Causal chains allow us to analyse the likely consequences of a potential intervention, assess the probability of possible impacts and consider what needs to happen for positive outcomes to occur. This helps us isolate which assumptions have to be valid and which intermediary steps need to materialise for an intervention to achieve its intended effect on outcomes. Causal chains can also help highlight possible unintended consequences.

Figure 3: Causal chains



Options

5.19 When developing potential policy interventions, we may consider different options for how we could achieve intended outcomes. Our CBAs assess a proposed intervention at the minimum against the appropriate counterfactual and its outcomes. This is usually a ‘do nothing’ scenario, but in special circumstances we might apply other counterfactuals.¹⁸ The ‘do nothing’ counterfactual is not a ‘no change’ assessment. Rather, it includes impacts that we expect to occur regardless of our proposed

18 In line with a common best-practice approach taken, for example, by the FCA and central government, one such exception is regulatory change relating to revoked EU law. In this scenario, the common ‘status-quo’ counterfactual includes the pre-existing EU law before it was revoked. For example, where we move previous EU regulation into UK regulation/statute without change, this would be considered to cause no impact overall.

intervention – for example, other planned interventions and likely changes in the markets or macroeconomic environment.

Costs and benefits

5.20 Our CBAs highlight which impacts are most likely and which are less certain. Where useful, we categorise impacts as either **direct** or **indirect**. This is not always a clear binary distinction; however, direct impacts occur as a direct consequence of an intervention, whereas indirect impacts rely on intermediate steps.

5.21 We also may consider categorising impacts as **one-off** or **ongoing** – for example, initial familiarisation costs¹⁹ and implementation costs, such as updating required systems, are typical one-off costs. Ongoing costs might include relatively direct ongoing compliance costs (such as annual reporting costs) or more indirect ongoing impacts that result from adjustments in the market over time (increase or decrease in business and thus revenue for regulated parties).

5.22 The immediate costs to regulated parties of regulatory interventions are often easier to quantify and monetise than benefits. Assessing these benefits often, almost by definition, involves less tangible and direct factors and relies to a greater degree on assumptions about intermediary steps.

Table 3: Illustrative common benefits

Benefit type	Relevant issues	Illustrative measures
Improved choice and service	<ul style="list-style-type: none"> • Availability of a choice of payment systems (e.g. access to cash) • Reliability of payment systems 	<ul style="list-style-type: none"> • Number of means of making and receiving payments available to consumers and merchants • Number of consumers experiencing avoidable adverse impacts • User satisfaction
Increased consumer protection/ reduced fraud	<ul style="list-style-type: none"> • Payment systems embed advanced fraud protection • Consumers have adequate protection if they become victims • Consumers trust payment systems 	<ul style="list-style-type: none"> • Reduced financial loss • Reduced probability of financial loss • Perceived reduction in psychological stress • User satisfaction

¹⁹ These are costs associated with regulated entities familiarising themselves with the changes and the possible need to share this information across the organisation. In some cases, where appropriate, we might assume these are absorbed by business-as-usual activities of regulated entities.

Benefit type	Relevant issues	Illustrative measures
Faster transactions	<ul style="list-style-type: none"> Time to settle transactions is adequate for users' needs 	<ul style="list-style-type: none"> Time per transaction × number affected × value of time
Fair and effective competition	<ul style="list-style-type: none"> Promotion of dynamic competition and future innovation 	<ul style="list-style-type: none"> Assessment of barriers to entry Ability and ease of users switching providers (e.g. merchants' ability to compare prices and switch providers of card-acquiring services)
Externalities	<ul style="list-style-type: none"> Positive spillover benefits to others in the wider ecosystem are considered 	<ul style="list-style-type: none"> Assessment of positive externalities (e.g. psychological benefit of reduced instances of fraud to consumers as a result of increased fraud protection investment by banks) Additional economic value provided by innovative services as a result of better access to existing infrastructure

5.23 Any general assessment of the proposed intervention will take into account all impacts, whether they are assessed qualitatively or quantitatively, or monetised.²⁰

5.24 Sometimes we have to protect or maintain anonymity of sensitive data. This can constrain the techniques we use and how we present published CBA documents. For example, we might need to present results at a more aggregated level to ensure information and data are not attributable to specific data subjects.

Summary assessment of net impacts

5.25 One simple interpretation of a CBA is as an exhaustive estimation of all costs and benefits caused by a proposed regulatory intervention, assessed over a specific appraisal period, discounted appropriately and finally summarised in a single 'net present value' (NPV) figure. We will provide such estimates where this can be done in a meaningful way, taking account of relevant uncertainties in line with general best practice.²¹ However, this is not our usual approach towards CBAs.

20 We acknowledge that monetisation is a form of quantification, but for the purpose of this document it makes sense to treat general quantification and monetisation as separate concepts.

21 That is, applying best-practice principles on issues such as appropriate discounting or appraisal periods as set out, for example, in the Treasury's *Green Book*. We might though deviate from commonly applied approaches or parameters; where we do, we will explain the logic behind our approach within the specific CBA.

5.26 We aim to assess and estimate impacts to a sufficient degree of specificity, but in most cases we do not consider the ‘netting off’ of identified costs and benefits within a single NPV estimate as the core purpose of our CBAs.²² Our main aim is rather to provide a holistic assessment of whether a proposed intervention can reasonably be expected materially to improve outcomes.

5.27 In some cases, we might also use analytical tools such as sensitivity analysis or scenario analysis to take account of risks and uncertainties, or break-even analysis to show how much of a positive change an intervention has to cause to offset identified costs. This depends on factors such as the extent to which it is possible to quantify or monetise impacts, or whether a qualified assessment is more appropriate. We explain the specific approach used in each CBA.

Distributional issues and transfers

5.28 We will consider how a regulatory intervention will affect different groups, such as regulated companies, merchants or consumers. We will consider whether first-order transfers (whose immediate impacts cancel each other out in aggregate) should be assessed as impact neutral in terms of welfare on a case-by-case basis. We may instead consider the application of welfare weights either within the CBA or in how we take the evidence presented by a CBA into account. Where we do apply weights, we will explain and justify our approach in the individual CBA and/or the relevant policy statements.

Equality

5.29 Section 149 of the Equality Act 2010 requires public authorities to have due regard to several equality considerations when exercising their functions. Public authorities such as the PSR must consider impacts on groups or individuals with ‘protected characteristics’. The Act does not specifically require that we publish Equality Impact Assessments (EIAs), but these are a common means of demonstrating compliance with the Public Sector Equality Duty (PSED).

5.30 We analyse equality impacts as part of our general policy development and appraisal. Unless we consider there is a significant equalities issue that warrants a specific, separate EIA, we usually aim to provide it as part of the CBA. In most cases, we think it makes sense to consider equality impacts as part of a breakdown of general impacts, in particular where specific equality impacts are assessed as part of distributional analysis.

The Better Regulation Framework

5.31 On 29 June 2023, the Retained EU Law (Revocation and Reform) Act 2023 came into effect. This abolished the Business Impact Target (BIT), the statutory basis for the previous Better Regulation Framework, and with it our statutory obligation to report against the BIT. The new Better Regulation Framework was introduced in September 2023.

5.32 As an independent regulator, we are not in scope of the new Better Regulation Framework. However, our economic analysis process will incorporate the principles of the Better Regulation Framework where appropriate.

²² For example, the Treasury’s *Green Book* uses a default ten-year appraisal period and an annual 3.5% discount factor but allows for deviation from that default – for example, for interventions that have very systemic, long-term impacts.

Other factors

5.33 Section 49 of FSBRA establishes our three core statutory objectives:

- **Our service user objective:** Ensure that payment systems are operated and developed in a way that takes account of, and promotes, the interests of those who use or are likely to use them.
- **Our competition objective:** Promote effective competition in the interests of those who use or are likely to use services provided by payment systems.
- **Our innovation objective:** Promote the development of, and innovation in, payment systems in the interests of those who use or are likely to use their services.

5.34 Section 53 of FSBRA sets out additional matters we must incorporate into our regulatory principles. These include a requirement to have regard to sustainability and impacts on environmental targets, such as net zero.

5.35 Our future CBAs will aim to capture all relevant economic effects, including impacts on competition, innovation and the environment. We will explain in each individual CBA which wider impacts we see as particularly relevant and might thus be worth expanding on in more detail.

Risks

5.36 The early stages of the CBA process are designed to highlight possible policy risks and unintended consequences.

5.37 Our analysis of the economic reasoning will set out the immediate impacts a regulatory intervention might cause and how those immediate impacts might in turn affect identified outcomes. The assessment will not set out what we want to achieve; instead, it will provide an assessment of what immediate (first-order) and less immediate (second-order) impacts an intervention might cause. In doing so, our analysis will highlight possible policy risks as well as the assumptions on which the causal chain of impacts depends. This will help highlight potential risks and the possible degree of likelihood of these risks materialising (that is, it will identify the degree of certainty that a policy will achieve its outcomes).

Uncertainty²³

5.38 Any form of ex ante appraisal that assesses a potential policy's consequences involves a degree of uncertainty. The degree of uncertainty typically depends on a variety of factors, such as how novel a policy intervention is.

5.39 This inherent uncertainty in economic appraisal is one of the reasons why we will usually not rely a singular NPV figure. Such a figure, which is typically the result of aggregating multiple individual impact estimates with their own degrees of uncertainty, is often not a robust basis on which to make decisions. Instead, we typically prefer to provide and consider likely ranges of impacts.

²³ This section refers to the degree of uncertainty of the analysis itself rather than to policy risks and uncertainty. For a discussion of that related but separate matter, please refer to paragraphs 5.36 to 5.37.

5.40 We might also use sensitivity and scenario analyses to show how robust or sensitive our assessment is to any underlying analytical assumptions and inputs, and how our estimates may vary under a different set of inputs or in different scenarios. In more complex modelling scenarios, we also consider the appropriateness of techniques such as Monte Carlo analysis²⁴ to present a full probabilistic representation of possible outcomes. We also use break-even analysis in cases where quantification or monetisation of impacts is challenging. Such analysis helps us assess what level of change an intervention would need to achieve to be net beneficial, and how realistic that appears to be.

Optimism bias

5.41 The Treasury's *Green Book* describes optimism bias as 'the proven tendency for appraisers to be optimistically biased about key project parameters, including capital costs and operating costs, project duration, and resulting benefits delivery'.

5.42 We acknowledge the principle of optimism bias, but we do not prescribe specific optimism bias adjustments like those set out in the Treasury's *Green Book*. As also shown in the *Green Book* guidance, most optimism bias relates to big spending projects such as improvements to infrastructure that involve significant capital expenditure, contracting with third parties, complex project management over many years and so on. These are not the types of regulatory interventions we typically make. However, we will consider using optimism bias adjustments for specific cases and we will often expect to use cautious estimates (see also our approach towards general uncertainty in paragraphs 5.38 to 5.40). In cases where we rely, at least partially, on cost estimates provided by regulated parties, there are also effects that tend to counteract optimism bias. Regulated parties can have a tendency – and may have an incentive – to overstate potential regulatory burdens; or, at the very least, they are unlikely to be subject to optimism bias on the potential success of regulation where that would mean understating costs to themselves.

Our core principles

- **The precise CBA methodology we apply will necessarily differ on a case-by-case basis.** While our CBAs follow a common structure and set of principles, factors such as data availability, the scale of likely impacts and proportionality considerations determine the methods we use. We explain our choices in each individual CBA.
- **In general, providing single-point estimates for overall net impacts within our CBAs is not a primary focus.** Instead, we aim to provide a description of the likely overall balance of impacts, taking into account risks and uncertainties, and using both quantitative and qualitative evidence.
- **The focus of our CBA process changes through the policy development cycle.** Early CBA development tends to focus more on a clear explanation of the economic reasoning behind our proposed intervention, while later analysis tends to focus more on a refined assessment of likely impacts.

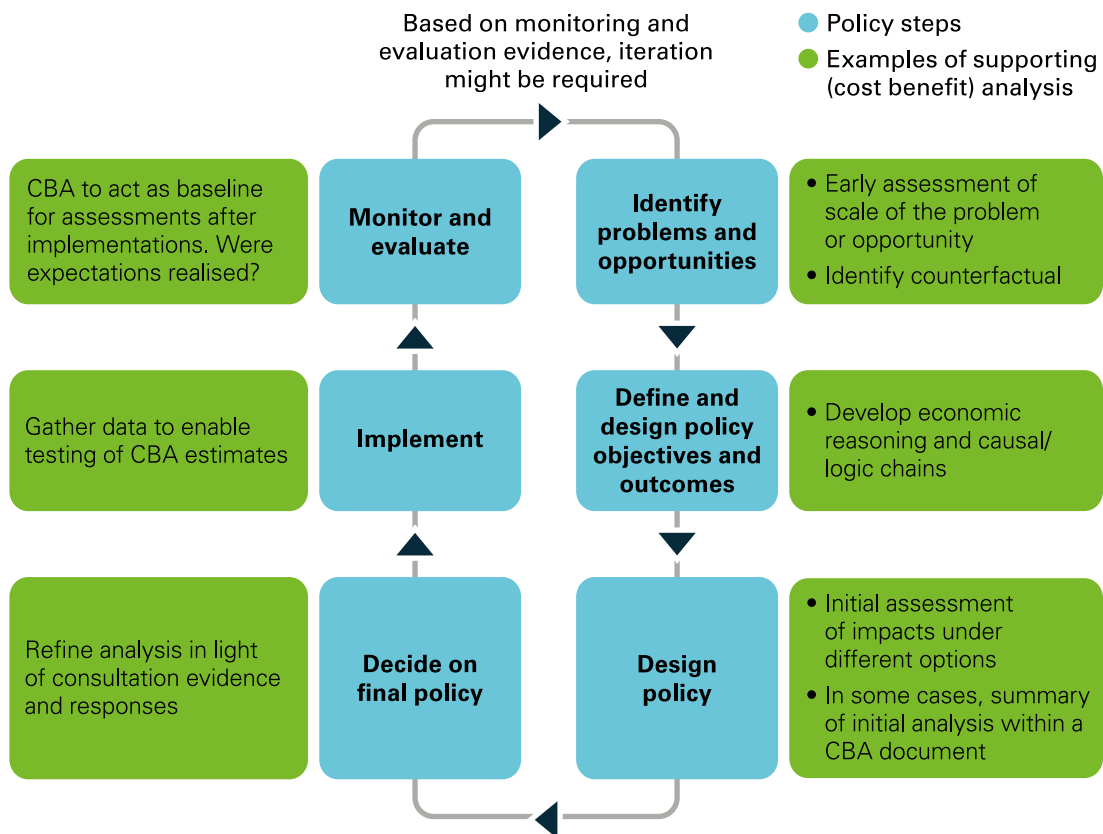
²⁴ Monte Carlo analysis is a form of simulation-based modelling in which inputs are not assumed as particular fixed values but are instead drawn repeatedly and randomly from probability distributions. As a result, it generates an entire probability distribution of results.

6 How we develop CBAs – our processes

6.1 Developing a CBA needs to be integrated into the policy cycle in order to act as an effective tool to improve decision-making. This chapter sets out how we typically ensure that we factor our CBA into policy development at the appropriate times. It also sets out the processes we typically use to ensure that our CBAs are quality assured and reflective of relevant stakeholder views.

CBA process within the policy cycle

Figure 4: Analysis within the policy cycle



6.2 As shown in Figure 4, we consider CBA development to be a process across our whole policy cycle. The focus of the analysis changes in response to the different stages of policy development, moving from early, high-level assessments to a more detailed CBA at the end. Our analysts are typically embedded within our policy teams, helping to ensure that the economic evidence developed as part of the CBA process responds to and influences the policy development process.

- 6.3** Monitoring and evaluating the impacts of our interventions after implementation can provide extremely useful feedback, not only for the effectiveness of an intervention itself but also on the type of analysis we conducted. It can provide valuable insight as to whether impacts matched the expectations our CBA outlined, and, if not, how we might need to adjust analysis and assumptions for future CBAs.
- 6.4** There can be instances – particularly when a potential regulatory intervention is market sensitive – in which we have to consider publishing a more detailed analysis at an early stage. As part of early analysis, we identify whether a CBA could contain market-sensitive information and take the appropriate steps in response.
- 6.5** We also learn from CBA processes that have been undertaken so as to inform our approach to this framework in light of its ongoing application.

Ensuring robustness and consistency

- 6.6** When we publish CBAs alongside consultation documents, we treat views expressed by stakeholders as a useful source of scrutiny that we can factor into any revisions and future relevant CBAs.
- 6.7** All our CBAs are subject to the process of internal quality assurance (QA). Our internal QA process is largely based on three principles:
- ensuring we are using appropriate analysis
 - ensuring we execute the analysis correctly
 - ensuring we document and store our analysis appropriately
- 6.8** The degree of QA activity we carry out needs to be proportionate to the analysis and the underlying intervention itself and may at times also involve bringing in external resource and expert advice. What degree of QA is proportionate is generally independent of the specific legal instrument we are considering. That is, our internal QA does not differentiate between CBAs that refer to measures implemented via general or specific directions. The relevant factors are rather the potential impact of a measure and the complexity of the analysis.

Our core principles

- **Our CBA process starts at the beginning of the policy cycle and evolves alongside policy.** Early analysis focuses on identifying the scale of existing problems and analysing causal chains for possible interventions. Later, the analysis narrows down potential policy options. Final analysis assesses the likely impacts of a preferred policy option.
- **CBA development is supported by a quality assurance framework that focuses on ensuring that our analysis asks the relevant questions using robust and proportionate methods.** We consider views expressed by stakeholders when revising existing CBAs or developing new CBAs.

7 Next steps

- 7.1** We are publishing this document as a matter of transparency, so that stakeholders can have a better understanding of how we approach CBAs. This document will also form the basis of our initial engagement with the FCA CBA Panel once it is in place.
- 7.2** Following any advice and comments we receive from the FCA CBA Panel, we will publish a revised version of this document – a draft statement of policy on our use of CBAs – for public consultation.

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