SUMMARY REPORT OF THE DIGITAL PAYMENTS INITIATIVE

THE PSR PANEL

April 2022

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FOREWORD BY THE CHAIR OF THE PSR PANEL

I am pleased to present the report of the PSR Panel's Digital Payments Initiative (the Initiative).

This PSR Panel provides independent advice and input to the PSR on an ongoing basis but undertaking this dedicated piece of work has been a new way of working for us. I would like to thank the members of the Panel and others in the payments sector who have contributed to the Initiative.

The PSR and the Panel launched the Initiative last year against a backdrop of dwindling use of cash, a fast-growing and changing market in digital payments and a continued focus on ensuring trust in digital payments. But many consumers do not secure the benefits of using digital payments, because of digital exclusion, their lack of trust in digital payments or to reduce their risk of overspending particularly in light of sharply rising costs of living which could exacerbate their continued reliance on cash.

The Initiative brought together a broad range of expertise and considered emerging developments across the payments sector from changing infrastructures, including the New Payments Architecture, through the evolving market in new open banking payment services, to the potential for seamless transactions involving both secure digital identification and payment.

While recognising the emerging innovations across the payments sector, the Initiative identified open banking could be key to developing digital payment services that better meet the needs of users, including those who currently prefer to use cash. The PSR will have a key role in the next stage of the development of open banking. As co-chair of the recently announced joint regulatory committee overseeing the transition in open banking governance the PSR will be working on the development of a strategic roadmap for open banking including unlocking the potential of open banking payments. Recommendations in this report aim to help the PSR in taking forward this role.

This report is a first step to understanding the barriers and solutions to increased take-up of digital payments. It provides both strategic and more tangible recommendations for how the PSR together with the broader ecosystem could help the market to ensure that everyone has access to digital payment services that meet their needs.

Dr Ruth Wandhöfer

Chair of the PSR Panel

EXECUTIVE SUMMARY AND RECOMMENDATIONS

1. The Payment Systems Regulator (PSR) asked the independent PSR Panel (the Panel) to undertake the Digital Payments Initiative (the Initiative) to:

   - understand the potential barriers to the take-up of digital payments; and
   - identify potential solutions and appropriate regulatory actions that might be required to enable them focusing within the PSR's remit.

   The Panel views the Initiative as contributing to the PSR's strategic outcome for everyone to have access to payment services that meet their needs.[1]

2. The Initiative drew on the expertise and experience of members of the Panel in a Panel Sub-Group which included additional input from a number of external contributors. A wide range of payments industry and user expertise was brought to bear (though not all payments sector interests were comprehensively represented).

3. The Initiative's work was necessarily limited by time and resources. The Initiative also found the availability of data that could have informed its work was limited. The Initiative's scope did not include commissioning new research or data collection nor the undertaking of substantial stakeholder engagement or cost-benefit analysis.

4. The Initiative's conclusions and recommendations are therefore expert views on key steps that should be taken to encourage those who remain cash-reliant to use – and others to make greater use of – digital payments. We expect the PSR will take the Initiative's recommendations into account in its work programme and will undertake appropriate analysis and validation of the proposals.

Drivers of reliance on cash

5. Research[2] suggests that a main factor driving some consumers' continued reliance on cash is having a low income or other vulnerability and the associated importance of budgeting and avoiding overspending, which the physical nature of cash makes easier. The current cost of living crisis will make effective budgeting more important to a greater number of people and for some, this may result in an increased reliance on cash.

6. Other factors limiting use of digital payments include:

   - A distrust of digital payments as a result of concerns about fraud, personal error or privacy.
   - A lack of financial capability, for example confusion about the range of digital payment options.
   - A lack of access to digital and financial infrastructure, fo r example inadequate broadband or devices, affordability issues or being 'unbanked'.
   - A lack of the digital skills needed to undertake digital transactions.

7. Small businesses and other small organisations may also not have their needs adequately served by digital payments and some may rely on cash. They may:

   - not secure the funds from digital sales rapidly enough, causing cashflow management issues;
   - not readily be able to compare and switch digital payment services;
   - have insufficient data and labelling attached to digital payments, making reconciliation time-consuming; and
   - be unable to secure digital payment services at prices they are willing to pay for the value of services offered.

8. The Initiative took these drivers into account in considering potential solutions for increasing take-up of digital payments.

1 The PSR Strategy, January 2022.
2 FCA Financial Lives survey 2020; Understanding cash reliance – qualitative research, Savanta:ComRes & the FCA, 2021.

High-level recommendations

9. The Initiative concluded there are four high-level areas that need to be worked on to address the drivers of cash reliance and enable greater take-up of digital payments. These are:

- improving consumers', small businesses' and other small organisations' awareness and understanding of, and trust in, digital payment options;
- tackling barriers to new digital p ayment services and service features, including enabling new functionalities and improving trust by addressing fraud risks;
- reducing digital exclusion; and
- putting better data in place to monitor the transition to digital payments.

Improving consumers' and small businesses' and small organisations' awareness and understanding of, and trust in, digital payment options

10. The Initiative considered that a key barrier to take-up of digital payments is many consumers', small businesses' and small organisations' lack of awareness and understanding of digital payment options.

11. Some consumers find the range of digital payment options complex and therefore avoid using them. Consumers' confusion is likely to increase as new digital payment options including account-to-account retail payments emerge. The PSR has a role in ensuring that consumers can navigate the payments landscape and make good choices in order to access the payment services they need.

12. The use of more consistent terminology for account-to-account retail payments could help build consumers' familiarity and confidence in using this new type of digital payment.

13. The PSR should also explore the scope for activities to raise awareness and understanding of digital payment options. Chip and PIN is an example of a successful campaign to raise awareness about a new payment type led by the industry (APACS – the former Association for Payment Clearing Services). Another potentially relevant example is the campaign to raise consumer awareness of Pay.UK's Current Account Switching Service.

14. The PSR's card-acquiring market review (CAMR) found that it is hard for small merchants to compare card-acquiring services because prices are not typically published, and pricing structures and approaches to headline rates vary significantly. While the CAMR considered only the market for card-acquiring services these features of the market could also be a barrier to merchants comparing between card and alternative payment types – and therefore a barrier to take up of new digital payment services. The PSR has proposed as a potential remedy that sellers of card-acquiring services should provide both standard published and bespoke to each merchant 'key facts' information, setting out key price points and non-price service elements. The PSR has also proposed to encourage digital comparison tools in the card-acquiring market. While recognising their implementation may meet barriers, we broadly support the PSR's proposed remedies.

Recommendation 1: The PSR should engage with the industry to encourage the use of consistent terminology for account-to-account retail payments building on OBIE's work to help consumer and merchant familiarity and confidence. It should explore the scope for awareness-raising activities to build the trust of consumers, small businesses and other small organisations and help them navigate the payments landscape effectively to make good choices.

Recommendation 2: As the PSR undertakes detailed design of its proposed CAMR remedies to help merchants compare card-acquiring services' prices and service features, it should take into account that merchants may increasingly also want to make comparisons between cards and other payment options, including account-to-account payments.

Tackling barriers to new digital payment services and service features

15. In line with its mandate, the Initiative's main focus was on the barriers to new digital payment solutions. To encourage greater use of digital payments, new digital services and service features are needed that better address users' needs, particularly the needs of the cash-reliant for services that enable easy control of their spending, akin to the experience of using cash. Consumers also need to have trust in order to use digital services, including low levels of fraud and protections if they are a victim of fraud or make an error.

16. In considering its recommendations, the Initiative took account of the PSR's role in furthering competition in payment services and payment systems, helping to drive innovation in the new services needed, as well as its role in removing specific barriers to innovative new payment services and service features.

17. The Initiative focused on already emerging technologies with the aim of increasing take-up of digital payments in the short to medium-term. In the longer-term there will undoubtedly be new digital payment technologies, potentially including for example, Central Bank Digital Currencies, but we have not attempted to forecast services that could emerge in the uncertain longer-term future. From the Initiative's work emerged a focus on the potential of account-to-account retail payment services enabled by open banking. Open banking currently permits regulated third-party payment providers to securely access (with customers' consent) bank account data, via bank application programming interfaces (APIs), in order to provide services including payment initiation on behalf of customers. There is potential to further develop open banking so that it enables consumers to make all kinds of retail payments to merchants, directly from their account, as an alternative to card payments. This has the potential to increase competition between payment systems and to encourage development of new payment services and service features.

18. The Initiative identified specific technical recommendations for the PSR, summarised in the next section, under the following headings:

- Addressing barriers to new open banking retail payment functionalities.
- Improving the consumer experience of Direct Debit.
- Improving consumers' trust and confidence by addressing fraud risks.
- Incentivising performance of open banking interfaces adequate for retail payment use cases.
- Enabling the use of digital identity within digital payment services.

19. Open banking has hitherto been driven by the Competition and Markets Authority (CMA), via the CMA's Order following its retail banking investigation, and by the Open Banking Implementation Entity (OBIE). But these have no mandate beyond the terms of the Order. The recommendations in this report have been made on the assumption, agreed with the PSR, that the PSR has or will have appropriate powers in relation to open banking payments.

Recommendation 3: The PSR, alongside the FCA, will need to take a regulatory oversight role to ensure that open banking payments develop beyond the CMA Order to enable competitive new account-to-account retail payment services, while ensuring appropriate consumer protections.

Reducing digital exclusion

20. The Initiative recognised that focusing on enabling new digital payment services alone would fail to fully address cash reliance. Exclusion of some people from digital services per se is also clearly a key barrier to the use of digital payments.

21. The tools for addressing problems such as insufficient access to digital and financial infrastructure, inadequate digital skills and lack of financial capability largely lie beyond the direct remit of the PSR. But if the PSR's strategic outcome is to be achieved these problems will need to be adequately addressed.

22. The Initiative concluded therefore that the PSR needs to take a role in engaging with those able to represent the needs of the digitally excluded, such as consumer bodies and those in government and industry with the tools to address digital exclusion, challenging them to do so. The results of improved data gathering (discussed below) could be used to publicise progress towards the PSR's strategic outcome and to identify where additional actions by others are most needed to make further progress.

Recommendation 4: The PSR should challenge those with tools to address the causes of digital exclusion to do so, in order to remove these barriers to the take-up of digital payments. As part of this, the PSR should publicise progress towards its strategic outcome of everyone having access to payment services that meet their needs and identify where additional actions are most needed.

Putting better data in place to monitor the transition to digital payments

23. Good data would help inform the range of actions needed to improve take-up of digital payments. The Initiative welcomes the PSR's Sector Intelligence and Analysis workstream to improve identification and analysis of trends in the payments sector.

24. As part of this work, the Initiative would expect the PSR to build and maintain a sufficiently detailed understanding of:

- trends relating to the range of different digital payment services;
- the characteristics and needs of users and non-users of different digital payment services;
- progress towards the PSR's strategic outcome that everyone has access to payment services that meet their needs, using suitable metrics; and
- the effectiveness of the PSR's relevant actions and their contribution towards this strategic outcome.

Recommendation 5: The PSR should improve data gathering relevant to achieving its strategic outcome for everyone to have access to payment services that meet their needs.

Technical recommendations

25. The Initiative identified a number of technical recommendations for addressing barriers to new digital payment services and service features. The Initiative does not expect that its recommendations are comprehensive but considers that together they would make a difference.

26. The technical recommendations are summarised below, roughly in order from potential shorter term to longer term impact. Recommendations 6, 7 and 9 have most potential for shorter term impact, with 6 being a key recommendation. Recommendations 8, 10 and 11 have potential for medium term impact, with 10 being a key recommendation. The impact of recommendation 12 is likely longer term.

Addressing barriers to new open banking retail payment functionalities

27. Emerging open banking-based account-to-account retail payment services include features that give consumers greater control over their spending, which may therefore encourage greater take-up of digital payments. Examples include digital requests for payment from merchants that give consumers choice over whether and when they make the requested payment; visibility of a consumer's bank balance as

part of the open banking transaction process; and Variable Recurring Payments (VRP) services that provide greater control over recurring and frequent retail payments by allowing consumers to specify up front and edit payment consent parameters (provided consent dashboards are provided).

28. VRP functionality in particular, enabled beyond the 'sweeping' use case mandated by the CMA Order, has the potential to unlock significant account-to-account retail payment options, including potentially account-to-account payments at physical point of sale.

29. The Initiative identified a number of barriers to development of open banking account-to-account retail payment service functionalities, including the following:

- Account Servicing Payment Service Providers' (ASPSPs, i.e., banks and building societies) control the gateways for third party Payment Initiation Service Providers (PISPs) to access customer accounts and may not have the incentives to facilitate fair non-sweeping VRP access.
- Enabling VRP transactions beyond sweeping will bring some additional risks by involving payees who are not also the payer, and effective allocation of liability for losses will be needed.
- VRP consent dashboards that provide consumers with visibility and control over their VRP payments are not yet required for VRP non-sweeping use cases.
- Current approaches to open banking retail payments at physical point of sale do not meet the same standards of ease and speed as contactless card payments.
- There are some technical categories of open banking retail payment where the customer may not be able to see their bank account balance during the payment journey.

30. The Initiative has identified recommendations to the PSR for addressing these barriers.

Recommendation 6: The PSR should consider requirements on all banks to provide Variable Recurring Payment API access for all use cases (beyond the sweeping use case already mandated by the CMA on CMA9 banks) on a basis equivalent to the CMA's requirements for sweeping and single payment API access. Alongside this, the PSR should ensure:

- arrangements for operationalising the appropriate allocation of liability for unauthorised or defective payments; and
- availability of consent dashboards, or equivalents, to a standard that enables all consumers to easily identify, amend and revoke retail VRP consents.

Recommendation 7: The PSR should ask OBIE to consider updating the Customer Experience Guidelines to allow all banks to show the customer's balance in all payment journeys – including allowing banks to show the balance (either as an additional screen after authentication or as part of the authentication screen) when an open banking payment uses 'account selection at merchant'.

Recommendation 8: The PSR should investigate what actions may be needed to enable consumers to use their devices to make open banking retail payments at physical point of sale via contactless technology.

Improving the consumer experience of Direct Debit

31. It can take up to two weeks to set up a Direct Debit mandate and make the initial payment. An increasing number of billers are therefore seeking parallel sign-ups for both Direct Debit and for open banking VRP so that an immediate initial payment can be made via open banking. The digital sign-up process for Direct Debit is unfortunately not up to date nor consistent with the open banking sign up, simply mimicking the old paper instruction form.

32. A modernised Direct Debit sign-up process, made consistent with the open banking sign up, could reduce friction and encourage more people to sign-up to recurring digital payments using Direct Debits. However, any investment in Direct Debit would need to be proportionate to the likely benefits and consider the expected longevity of Direct Debits in the context of emerging new services for making recurring payments.

33. Many consumers do not receive an alert from their bank ahead of each Direct Debit (though a few banks do now provide this service). Consumers may therefore lack awareness of their recurring payments and feel less able to budget.

Recommendation 9: The PSR should the explore options to bring Direct Debit into the digital age.

- The PSR should explore whether there are proportionate steps the industry could take to update the Direct Debit sign-up process for improved compatibility with open banking payments sign up and to help future transition to new payment products.
- The PSR, along with the FCA, should consider encouraging all banks to provide digital alerts ahead of Direct Debits as this could improve digital adoption by making Direct Debit work better for those who struggle with it today.

Improving consumers' trust and confidence by addressing fraud risks

34. Open banking account-to-account retail payments have the potential to limit the risk of fraud. For example the risk of misdirected payments and scams is reduced where the PISP, rather than the consumer, populates the payee account details and the PISP may undertake effective due diligence on payees (in addition to that undertaken by the payee's bank).

35. However, there is more that can be done to ensure incentives on all the parties involved in open banking retail payments who can take measures to reduce fraud, including PISPs. Reducing the risk of fraud would help increase consumer confidence in – and therefore willingness to use –digital payment services using open banking.

Recommendation 10: The PSR should help ensure effective incentives on PISPs to prevent fraud and scams:

- Completion of the Lending Standards Board's work to enable PISPs to join the Contingent Reimbursement Model (CRM) Code would enable PISPs to become subject to standards for protecting consumers from Authorised Push Payment (APP) scams and where fault lies with them, to bear appropriate liability.
- The PSR's work on potential mandatory requirements that Faster Payments participants reimburse consumers for APP scam losses should ensure that where fault lies with PISPs, they bear appropriate liability for reimbursement.
- The PSR should ensure effective dispute resolution arrangements for operationalising the appropriate allocation of liability for fraud or scam losses in open banking payments.
- ASPSPs' policies on transaction limits and blocking should be responsive to the effectiveness of an individual PISP's processes for reducing fraud risk, for example populating payee fields or undertaking effective due diligence on payees.

Incentivising performance of open banking interfaces adequate for retail payment use cases

36. For open banking payment services to compete successfully in a retail context, they need to be highly reliable. Reliability depends in part on the performance and availability of ASPSPs' technical interfaces (APIs).

37. The current requirement under the PSRs 2017, is that API performance must at least match that of ASPSPs' direct customer interfaces (e.g., banking apps). This standard of performance may not always be sufficient for retail payment use cases. In addition, the performance of some ASPSPs has not met OBIE's benchmarks for well-performing open banking APIs.

Recommendation 11: The PSR, with the FCA, should consider how to ensure that the performance and reliability of technical infrastructure supporting open banking account-to-account payment services, including APIs, is maintained at the level needed for competitive retail use cases, including looking at standards and incentives.

Enabling the use of digital identity within digital payment services

38. There is potential for businesses to use the open banking framework for secure authentication and data sharing to build additional value-added services, for example allowing consumers to share additional digital identity attributes with merchants. This could enable seamless consumer transaction experiences such as a consumer being able to prove eligibility for a service by validating their age and address and make payment for that service all in a single digital step. This would benefit both consumers and merchants by providing greater convenience and by reducing opportunities for identity theft and payment fraud.

39. By enabling additional benefits from using digital payments such innovations could encourage more people to use them.

Recommendation 12: The PSR should engage with the Government on the development of digital identity standards to ensure that open banking capabilities can be used to implement digital IDs in transactions.

CHAPTER A. ABOUT THE INITIATIVE

Purpose and governance of the Digital Payments Initiative

40. The Payment Systems Regulator (PSR) asked the independent PSR Panel (the Panel) to undertake the Digital Payments Initiative (the Initiative) to:

- understand the potential barriers to the take-up of digital payments; and
- identify potential solutions and appropriate regulatory actions that might be required to enable them, focusing within the PSR's remit.

The Panel views the Initiative as contributing to the PSR's strategic outcome for everyone to have access to payment services that meet their needs.

41. This is the summary report of the Digital Payments Initiative, agreed by the PSR Panel.

42. The PSR Panel is established by statute and is independent of the PSR. The Panel's role is to contribute towards the effective development of the PSR's strategy and policy and offer advice and early input on the PSR's work. The Panel is made up of members drawn from payments system operators, payments service providers, infrastructure and technology providers and service users including consumer, government, large and small business representatives.

43. To undertake the work on the Initiative, a Sub-Group of the PSR Panel was established, chaired by the PSR Panel Chair. The Sub-Group included a number of additional contributors to broaden its relevant payments industry and user expertise. The Sub-Group members are listed in the Annex.

The Panel Sub-Group's approach to the Initiative

44. The Sub-Group agreed that the Initiative's scope was:

- digital payments involving consumers and/or small businesses and other small organisations[3] – not including digital assets / cryptocurrency;
- barriers to the use of digital payments (while recognising the barriers to digital inclusion per se were also important);
- the needs of users who do not currently use digital payments, and instead rely on cash transactions; and
- the needs of users who already make some use of digital payments but could make greater use if their choice of digital payments is broadened.

45. The Initiative's high-level approach was to identify:

- barriers to greater use of digital payments, including key user needs that are not currently being adequately met by digital payment options;
- potential solutions, including emerging digital services and service features that could better address user needs;
- obstacles to take-up of those solutions; and
- recommendations for addressing those obstacles.

46. The Initiative's work was necessarily limited by time and resources. While a wide range of payments industry and user expertise was brought to bear, the Panel recognises that not all relevant interests were represented on the Sub-Group or on the PSR Panel. The Initiative also found limited availability of data that could have informed its work. The Initiative's scope did not include commissioning new research or data collection, undertaking significant stakeholder engagement nor undertaking cost-benefit analysis.

3 Where the report refers to small businesses, this includes other small organisations.

47. The Initiative's conclusions and recommendations are therefore expert views on key steps that should be taken to encourage those who remain cash-reliant to use – and others to make greater use of – digital payments. We expect that the PSR will take the Initiative's recommendations into account in its work programme and will undertake appropriate analysis and validation of the proposals.

48. The Panel would not expect its recommendations on their own to be sufficient to encourage all those who remain cash-reliant to move into digital payments. But, taken together, the Initiative's proposals have potential to make a significant contribution, in the short and medium term, to greater take-up of digital payments.

CHAPTER B. BARRIERS TO GREATER USE OF DIGITAL PAYMENTS

49. The Initiative identified the following barriers to greater take-up of digital payments:

- Lack of awareness and understanding of digital payment options
- Digital exclusion
- Failure of digital payment options to meet consumer needs
- Failure of digital payment options to meet small business needs
- Lack of data on the barriers to take-up of digital payments

1 Lack of awareness and understanding of digital payment options

50. The Initiative considered that a key barrier to take-up of digital payments is many consumers' and small businesses' lack of awareness and understanding of, and therefore trust in, digital payment options.

51. Some consumers find the range of digital payment options complex, may lack confidence and trust in them and may therefore avoid using them. Consumers' confusion is likely to increase as new digital payment options, including open banking-based account-to-account retail payments, emerge. Consumers have limited awareness of open banking, and most are not yet familiar with the open banking retail payment experience.

52. Consumer awareness and familiarity is not helped by the variation in the experience of open banking retail payments between providers. The use of more consistent terminology for open banking retail payments could help build consumer familiarity and confidence in using this new type of digital payment, and OBIE has started addressing this, publishing guidelines on improved terminology.

53. There is potential for awareness-raising activities to help consumers gain a basic understanding of the different payment choices available to them. Chip and PIN is an example of a successful campaign to raise consumer awareness about a new payment type, led by the industry (APACS – the former Association for Payment Clearing Services). Another potentially relevant example is the campaign to raise consumer awareness of Pay.UK's Current Account Switching Service, which is underpinned by regulatory performance metrics.

54. The PSR has a role in ensuring that consumers are able to navigate the payments landscape and make good choices, in order to access the payment services they need.

Recommendation: The PSR should engage with the industry to encourage the use of consistent terminology for account-to-account retail payments, building on OBIE's work, to help build consumer and merchant familiarity and confidence; and it should explore the scope for awareness-raising activities to help build the trust of consumers, small businesses and other small organisations and help them navigate the payments landscape effectively to make good choices.

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55. Many small merchants are not readily be able to understand and compare relevant features of digital payment services.

56. The PSR's card acquiring market review (CAMR)[4] found that it is hard for small merchants to compare card acquiring services, including because prices are not typically published, and pricing structures and approaches to headline rates vary significantly. In addition, the indefinite duration of card acquirer and payment facilitator contracts do not provide a trigger for merchants to think about searching and switching; and the lack of portability of POS terminals and significant early termination fees for POS terminal contracts can discourage merchants from switching. As a result, most small merchants do not regularly consider switching or searching for other providers of card acquiring services. We note that these issues may also apply to many larger merchants.

4 Market review into card-acquiring services Final report, PSR, November 2021.

57. While the CAMR considered only the market for card acquiring services, these features of the market could also be a barrier to merchants comparing and switching between card and alternative payment types – and therefore a barrier to take up of new digital payment services. A small merchant should easily be able to understand what it can expect to pay each period for a given set of services.

58. The PSR has proposed, as one potential remedy, that those selling card acquiring services should provide both standard published, and bespoke to each merchant, 'key facts' information setting out key price points and non-price service elements. The PSR has also proposed to encourage digital comparison tools in the card-acquiring market. While recognising their implementation may meet barriers, we broadly support the PSR's proposed remedies.

Recommendation: As the PSR undertakes detailed design of its proposed CAMR remedies to help merchants compare card acquiring services' prices and service features, it should take into account that merchants may increasingly also want to make comparisons between cards and other payment options, including account-to-account payments.

2 Digital exclusion

59. Research[5] suggests that a main factor driving some people's continued reliance on cash is having a low income, or other vulnerability. This is associated with increased importance of being able to budget and avoid overspending, which the physical nature of cash makes easier (see the next section). Low income and vulnerability may also be associated with other drivers of cash reliance, including:

- lack of financial capability;
- lack of access to digital and financial infrastructure, for example inadequate broadband or devices, affordability issues or being 'unbanked'; and
- lack of the digital skills needed to undertake digital transactions.

60. 20-25% of adults lack the skills to undertake the digital transaction 'life tasks' as tested in Lloyds' *Essential Digital Skills Framework 2021*.[6] Older consumers and those with less formal education disproportionately lacked such skills. Digital interfaces used in payments may be a particular problem for many older people.[7] 2.3% of UK adults, and 5% of those where household income is less than £15,000 pa, have no current or e-money account.[8]

61. The Initiative recognised that focusing on enabling new digital payment services alone would fail to fully address cash reliance. Exclusion of some people from digital services per se is also a key barrier to the use of digital payments.

62. The tools for addressing problems such as insufficient access to digital and financial infrastructure, inadequate digital skills and lack of financial capability largely lie beyond the direct remit of the PSR. But if the PSR's strategic outcome – that everyone has access to payments that meet their needs – is to be achieved, these problems will need to be addressed.

63. The Initiative concluded that the PSR therefore needs to take a role in engaging with those able to represent the needs of the digitally excluded, such as consumer bodies, and those in government and industry with the tools to address digital exclusion, challenging them to do so. This could be supported by measuring and publicising progress towards the PSR's strategic outcome and identifying where additional actions are most needed to make further progress.

5 FCA Financial Lives survey 2020; Understanding cash reliance – qualitative research, Savanta:ComRes & the FCA, 2021.
6 Lloyds Consumer Digital Index 2021.
7 Response to Payments Strategy Forum: Being responsive to user needs – Draft strategy for consultation, Age UK, 2016.
8 FCA Financial Lives survey 2020.

Recommendation: The PSR should challenge those with tools to address the causes of digital exclusion to do so, in order to remove these barriers to the take-up of digital payments. As part of this, the PSR should publicise progress towards its strategic outcome of everyone having access to payment services that meet their needs and identify where additional actions are most needed.

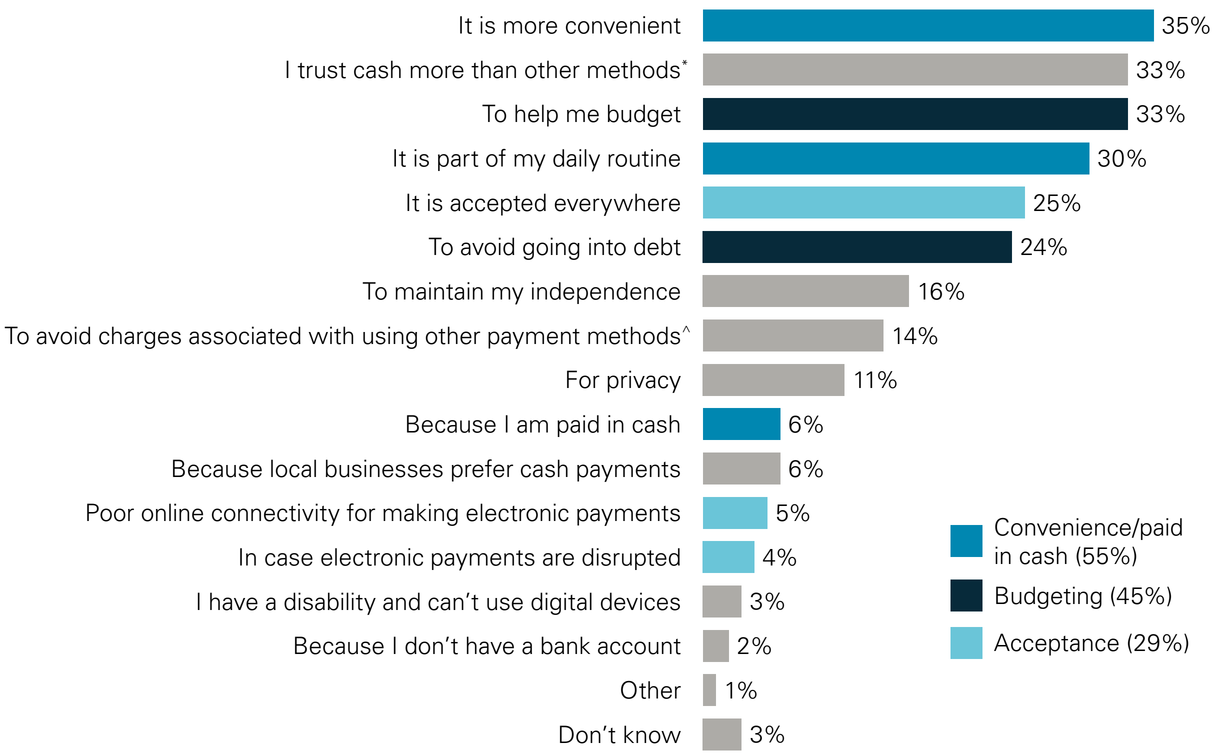
3 Failure of digital payment options to meet consumer needs

64. Consumers whose needs are not adequately met by digital payments are likely to make greater use of cash. Consumers who do not use of digital payments are increasingly likely to miss out on benefits of doing so, including reduced costs, new services and even the ability to pay some merchants. It is difficult to quantify the harms to consumers from not using digital payments. One key source of harm is the additional costs to consumers of paying utility bills by non-standard payment methods. The Personal Finance Research Centre estimated the premium, in 2019, for payment of electricity and gas bills on receipt rather than via Direct Debit was £108 pa.[9]

65. In 2020, 11% of consumers said they relied on cash to a great, or very great, extent, while a further 32% relied on cash to moderate extent.[10] Figure 1, from the FCA's *Financial Lives* survey, suggests that the most important drivers for those consumers who continue to rely on cash are perceived convenience, trust and to help them budget.

66. The Initiative took these drivers issues into account in considering solutions to increasing take-up of digital payments.

Figure 1: Reasons for relying on cash to a very great or great extent (Feb 2020), FCA 'Financial Lives' survey 2020



* E.g., a debit or credit card.
^ E.g., charges applied by some merchants when using a debit or cred it card

9 The poverty premium: a customer perspective, Personal Finance Research Centre, November 2020.
10 FCA Financial Lives survey 2020. Data was gathered pre-pandemic.

Budgeting and control of payments

67. Low-income consumers, and those with other characteristics of vulnerability, are most likely to rely on cash, and this is linked with the most important factor in driving a consumer's reliance on cash – a need to avoid overspending and live within their means. The current cost of living crisis will make effectively budgeting more important to a greater number of people, some of whom may therefore increase their reliance on cash.

68. According to qualitative research by the FCA[11], cash reliant consumers felt that using cash stopped them spending more than they had, helped them keep track of their spending and put enough friction into the payment process to enable them to evaluate whether or not they wanted to proceed with a purchase. Which? research[12] found that 7 in 10 people on the lowest incomes were concerned that technology made it too easy to spend. The FCA's *Financial Lives* survey[13] found that 33% of those who relied on cash did so to help them budget, and 24% to avoid going into debt.

69. People on irregular incomes may find it hard to budget for monthly lump sum digital recurring payments and may therefore, for example, incur penalties for missed Direct Debits. The Financial Inclusion Commission [14], found that many people chose to pay their bills through methods, such as pre-payment meters, which cost more but gave them more control. In addition, lack of visibility of, and control over, 'card on file' recurring payments makes it easier for consumers to be harmed by 'subscription traps.' The Payment Strategy Forum[15] found that customers wanted greater control over recurring payments so that they could choose when and how to pay. They also found that consumers wanted real-time balance information to help them manage cashflow better.

Safety and trust

70. Many consumers are concerned about their exposure to the risk of fraud when using digital payments, and they therefore lack trust in digital payments, including payments which involve sharing bank details or responding to digital messages (e.g., with requests to 'click'). Some consumers are also concerned about the privacy of their data when using digital payments and risk of making errors. These concerns reduce consumers' trust in using digital payments.

71. FCA's *Financial Lives* survey[16] found that 33% of those who relied on cash did so because they trusted cash more than alternatives and 11% for privacy. According to qualitative research for the FCA [17], one of the most important factors in driving a consumer's reliance on cash was distrust of alternatives, including concern about fraud, personal errors and privacy. This is in a context of rising fraud and scams, for example, there was a 71% increase in authorised fraud losses between the first halves of 2020 and 2021.[18]

4 Failure of digital payment options to meet small business needs

72. The Initiative identified a number of ways that digital payments may not currently meet the needs of small businesses.

73. Some small merchants need the funds from their sales earlier than existing digital payment methods provide for, and this may lead them to continue to make use of cash in some cases. For example, card scheme payments may take 1-3 days, and sometimes longer, to reach a merchant's account. Direct Debits may take up to 2 weeks to set up, delaying the merchant's receipt of the initial payment.

11 Understanding cash reliance – qualitative research, Savanta:ComRes & the FCA, July 2021.
12 Everyday Finances – What consumers need in a changing world of banking and payments, Which?, November 2019.
13 FCA Financial Lives survey 2020.
14 Improving the Financial Health of the Nation, Financial Inclusion Commission, 2015.
15 A Payments Strategy for the 21st Century Putting the needs of users first, Payments Strategy Forum, November 2016.
16 FCA Financial Lives survey 2020.
17 Understanding cash reliance – qualitative research, Savanta:ComRes & the FCA, July 2021.
18 Government-coordinated action needed as fraud losses rise by 30 per cent, UK Finance.

74. Existing payment methods may not provide small merchants with access to tools that could enable them to better manage their cashflow, such as real-time balances[19] and payment alerts [20].

75. Insufficient data and labelling attached to digital payments may make reconciliation difficult and time-consuming for merchants, particularly where multiple payment methods are involved. The Payment Strategy Forum identified that businesses wanted to be able to access data that allowed them to fully understand what a payment related to, for easy reconciliation.[21] Availability of more data on payments could help merchants better manage their businesses, including improving day-to-day management, enabling analysis of sales patterns and improving customer payment journeys.[22]

76. Some small merchants may be unable to secure digital payment options at prices they are willing or able to pay, for the value of services offered. For example:

- small merchants may not be able to access Direct Debit at an acceptable price point; and
- merchants face increasing costs of card payment services. The PSR found that fees paid by acquirers for card scheme services approximately doubled from 2014 to 2018, after adjusting for changes in the volume, value and mix of card transactions, and these fees were passed through to merchants in full.[23]

77. The Initiative took these issues into account in considering potential solutions to increasing take-up of digital payments.

5 Understanding of the barriers

78. Good data is needed to understand the barriers to take-up of digital payments and to inform what actions are required to improve take-up. In undertaking its work, the Initiative found limitations in the availability of relevant data.

79. The PSR's Sector Intelligence and Analysis work stream has been set up to improve identification and analysis of trends in the payments sector. The PSR has also committed to measuring progress towards the strategic outcomes set out in the PSR Strategy.

80. The Initiative would expect the PSR to build and maintain a sufficiently detailed understanding of:

- trends relating to the range of different digital payment services;
- the characteristics, needs and concerns of users and non-users of different digital payment services;
- progress towards the PSR's strategic outcome that everyone has access to payment services that meet their needs, using suitable metrics; and
- the effectiveness of the PSR's relevant actions and their contribution towards this strategic outcome.

Recommendation: The PSR should improve data gathering relevant to achieving its strategic outcome for everyone to have access to payment services that meet their needs.

19 A Payments Strategy for the 21st Century Putting the needs of users first, Payments Strategy Forum, November 2016.
20 Research commissioned by Pay.UK from Revealing Reality, 2021. https://newseventsinsights.wearepay.uk/news-in-brief/smes-and-payments/
21 A Payments Strategy for the 21st Century Putting the needs of users first, Payments Strategy Forum, November 2016.
22 Research commissioned by Pay.UK from Revealing Reality, 2021.
23 Market review into the supply of card acquiring services Interim report, PSR, September 2020.

CHAPTER C. SOLUTIONS TO GREATER USE OF DIGITAL PAYMENTS

81. In line with its mandate, the Initiative's main focus was on enabling new digital services and service features with the potential to better address users' needs – particularly the needs of the cash-reliant for easy and safe control of their spending – and thus encourage greater use of digital payments.

82. The Initiative explored a range of digital payment services, focusing on already available or emerging technologies, with the aim of increasing take-up of digital payments in the short to medium-term. In the longer term there will undoubtedly be new digital payment technologies, potentially including, for example, Central Bank Digital Currencies, but we have not attempted to forecast services that could emerge in the uncertain longer-term future.

83. The initiative noted that there have been a range of recent innovations in card-based digital payment services enabling them to better address users' needs. These include:

- banking and card app functionality that enables consumers to stop their card themselves quickly and easily, helping them if they lose their card or feel nervous about spending on it;
- enabling carers to make purchases on behalf of people, with safeguards;
- gambling blocks on cards; and
- digital wallets with features focused on people on low incomes.

84. In considering its focus and recommendations, the Initiative took account of the PSR's role in furthering competition in payment services and payment systems – helping to drive innovation in the new services needed – as well as its role in removing specific barriers to innovative new payment services and service features. The Initiative gave due consideration to the appropriate allocation of roles between regulation and the market.

85. The Initiative's focus therefore turned significantly to open banking-based payments, where there is the potential for increasing competition between payment systems and services as well as for innovation in new service features.

86. The Initiative identified technical recommendations for the PSR set out in this section, which is structured under the following headings:

1) The potential of open banking retail payments
2) Addressing barriers to new retail payment functionalities
   i. Open banking Variable Recurring Payments
   ii. Balance visibility in open banking retail payment customer journey
   iii. Open banking payments at point of sale
   iv. Request for payment services
   v. Paym
3) Improving the consumer experience of existing recurring payment services
4) Improving consumers' trust by addressing fraud risks
5) Incentivising performance of open banking interfaces adequate for retail payment use cases
6) Enabling the use of digital identity within digital payment services

1 The potential of open banking retail payments

87. From the Initiative's work emerged a focus on the potential of account-to-account retail payment services enabled by open banking over the next few years.

88. Open banking enables regulated third parties to securely access (with the customer's consent) bank (or building society) account data, via the bank's application programming interfaces (APIs), in order to provide a range of services. Open banking account-to-account payment services are provided by third party Payment Initiation Service Providers (PISPs) who initiate a payment on behalf of a customer via the secure open banking connection to the customer's account. While the number of open banking payments is growing it is currently low compared to other payment types. Most open banking payments are currently online Single Immediate Payments.

89. There is potential to further develop open banking so that it enables consumers to make all kinds of retail payments to merchants, directly from their account, as an alternative to card payments. This has the potential to increase competition between payment systems and to enable development of new payment services and service features.

90. In an open banking retail payment, the consumer would typically select the open banking payment option at the merchant website's checkout (sometimes described as a bank transfer or similar) and is redirected to their own online banking or mobile banking app to authenticate the payment.

How open banking retail payments potentially address unmet user needs

91. Open banking retail payments have the potential to address user needs that are not adequately met by current digital payment options (as described in Chapter B). This could encourage greater use of digital payments.

92. Open banking payments can enable consumers to see their bank balance during a transaction and before confirming the payment. This gives consumers more visibility and control over their payments. It is analogous to a consumer checking the cash in their purse or wallet at the checkout before completing a physical retail transaction.

93. Open banking retail payments have the potential to reduce losses from fraud and error. Consumers do not need to trust a merchant website to store their card details [24], nor do they typically need to key in the bank details of the merchant (which are instead populated by the PISP).

94. Settlement of open banking payments is immediate, compared to a typical 1-3, and sometimes more, days for card payments, with benefits for small merchants' cashflow. (We note that some card acquirers offer merchants faster settlement service options.)

95. As each transaction is settled individually and without deduction, reconciliation is simpler for the merchant, compared to other payment types that provide a 'bulk credit' amount per day net of processing fees.

96. There is potential for value-added services to be offered on the back of open banking payment functionality, with benefits for consumers and for merchants. For example, open banking payment providers may make use of open banking data to help small merchants reconcile payments and make better business decisions. There is also the potential to combine digital identity data with open banking payments to create seamless consumer transaction experiences.

97. Open banking payments may also reduce payment costs borne by merchants. (We note that the effect on prices will depend on the overall costs of alternative payment methods, how costs are affected by the specific services delivered by each payment type, how the costs are passed on to merchants and the effect on prices of increased competition between payment methods – on which the Initiative has not done economic analysis).

24 Other solutions are available to avoid sharing card details, such as tokenisation.

Obstacles

98. The Initiative identified a number of potential obstacles to the successful development of open banking retail payments, and focused on the following:

- Lack of awareness and understanding of open banking retail payments (discussed in section B1)
- Barriers to new open banking retail payment functionalities (discussed in section C2)
- Consumer concerns about fraud risks leading to lack of trust in new payment options (discussed in section C4)
- Need for levels of technical reliability sufficient to support retail payment use cases (discussed in section C5)
- Need for effective regulatory oversight of the development of open banking retail payments (see below).

99. Open banking has hitherto been driven by the Competition and Markets Authority (CMA), via the CMA's Order following its retail banking investigation, and by the Open Banking Implementation Entity (OBIE). But these have no mandate beyond the terms of the Order.

100. The recommendations in this report have been made on the assumption, agreed with the PSR, that the PSR has or will have appropriate powers in relation to open banking payments. But the Initiative notes that the legislation establishing the PSR and its powers, the Financial Services (Banking Reform) Act 2013, as well the Treasury Orders designating payments systems under that legislation, pre-date implementation of open banking payments.

Recommendation: The PSR, alongside the FCA, will need to take a regulatory oversight role to ensure that open banking payments develop beyond the CMA Order to enable competitive new account-to-account retail payment services, while ensuring appropriate consumer protections.

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2 Addressing barriers to new retail payment functionalities

i. Open banking Variable Recurring Payments

101. Variable Recurring Payments (VRP) are a form of open banking payment where the consumer securely authorises a PISP to initiate payments from their bank account on an ongoing basis, rather than needing to authorise each single payment. VRP functionality, enabled for retail payments, therefore provides a potential alternative to Direct Debit and 'card on file' recurring payments, as well a means for low friction frequent payments at a trusted retailer.

102. VRP works by the consumer agreeing a VRP consent which has a set of parameters – including the period of the consent, the maximum single payment amount and the maximum total of payments in a given period – within which transactions may be executed without the need for further authorisation. VRP consents are cancellable and editable by the consumer, via either their bank or the PISP, where a consent dashboard is provided.

How Variable Recurring Payments potentially address unmet user needs

103. VRP has the potential to provide consumers with greater control over recurring and frequent digital payments, as a result of being able to specify payment parameters up front and easily edit the parameters, if circumstances change (where a consent dashboard is provided).

104. Enabling consumers to better manage their outgoing recurring payments against their income may encourage more consumers to use digital recurring payments rather than alternatives such as cash or prepayment meters. The improved visibility, editability and cancellability of VRP mandates – compared

to card on file payments in particular – could reduce the risk of 'subscription traps' and, more generally, build consumer trust in digital payments. (We note that a few mobile banking apps have begun to offer dashboards for managing card on file payments.)

105. VRP also allows for convenient, low friction retail payments with enhanced control. For example, a consumer could allow a frequently used retailer to execute payments without the need for specific authorisation, provided the payments complied with the VRP consent parameters. This would allow the equivalent of one-click payments on-line and 'contactless' at point of sale where a consumer had set up the facility with the retailer.

106. VRP recurring payments could be more accessible to small merchants than Direct Debit. The precise nature of payments is agreed in the VRP consent so there is potentially less risk of the merchant being exposed to liabilities than under the Direct Debit Guarantee.

107. VRP services would also provide for the other benefits of open banking retail payments, as outlined in section C1, including immediate settlement for the merchant; potential for value-added services; and potential to reduce the costs borne by merchants.

Obstacles

108. To be able to offer VRP retail services, PISPs need access to customers' bank accounts via APIs with relevant VRP functionality. The CMA mandated the CMA9 major banks to provide VRP API access, free of charge[25], for the purposes of 'sweeping' funds between accounts held by the same customer. The CMA's sweeping requirement is focused on delivering remedies addressing adverse effects on competition identified in retail banking market investigation.[26] The CMA does not have the power to extend this mandate to VRP API access for non-sweeping, i.e., retail, purposes.

109. A PISP offering a VRP retail service needs access to most or all banks for the service to be ubiquitous and thus attractive to billers so that it can gain scale.[27] A PISP therefore has no choice but to secure access to each individual bank's API. Banks could exploit this position and create obstacles to VRP retail services, including:

- not enabling non-sweeping VRP API access;
- requiring conditions for accessing non-sweeping VRP APIs that have the effect of restricting access, such as unnecessarily onerous vetting requirements for PISPs or for VRP retail services; and
- levying excessive charges, above a level that would prevail in a competitive market, for PISPs' use of non-sweeping VRP APIs.

110. Such obstacles could limit development of VRP retail services and undermine competition. We note that VRP retail services would compete with existing services, such as card on file and other card payments, from which banks earn interchange fees.

111. VRP beyond sweeping will bring some additional risks because payments will (unlike sweeping) be going to payees who are not also the payer. This means that, depending on the protections offered by the PISP provider, some consumers could be less well protected than when they used a card for the same transactions.

112. The VRP benefits of control and visibility rely in significant part on the provision of consent dashboards by ASPSPs (banks and building societies) or by PISPs. Consent dashboards are only currently required of the CMA9 banks for sweeping functionality and are therefore not required for any banks for VRP retail use cases.

25 Banks may still charge the receiver and possibly the payer for the underlying Faster Payment in the normal way, as they do for customer-initiated payments and open banking single payments.

26 Retail banking market investigation – Final report, CMA, August 2016.

27 Experience supports the importance of ubiquity for new payment services to succeed – see discussion of Paym.

Potential solutions and recommendation

113. A potential solution to ensuring non-sweeping API access would be to require banks to provide such access on a basis equivalent to the CMA's requirements for sweeping and for single payment API access. Broadly, banks would be required to provide access to non-sweeping VRP APIs without discriminatory or unnecessarily onerous conditions and without extra charges to PISPs.

114. Any requirement not to levy charges on PISPs would not prevent banks charging, usually business, customers for the receipt or sending of the underlying Faster Payment, in the same way they currently do for open banking single and sweeping VRP payments. An advantage of this charging model would be that a bank's customer, if they objected to their bank's charges, could in principle switch bank – unlike a PISP, which has no choice but to deal with every bank.

115. To ensure VRP retail services are safe for consumers, potential solutions include:

- operational arrangements for ensuring that liability for unauthorised or defective payment losses is effectively allocated to the appropriate party, whether PISP or ASPSP;
- availability of consent dashboards for all consumers so they can easily identify, edit and revoke VRP consents; and
- standards for VRP consents that ensure consumers understand their agreement to a series of transactions within the consented parameters.

116. These issues should be addressed in ways that do not raise unnecessary barriers to development of VRP retail services.

Recommendation: The PSR should consider requirements on all banks to provide Variable Recurring Payment API access for all use cases (beyond the sweeping use case already mandated by the CMA on CMA9 banks) on a basis equivalent to the CMA's requirements for sweeping and single payment API access. Alongside this, the PSR should ensure:

- arrangements for operationalising the appropriate allocation of liability for unauthorised or defective payments; and
- of consent dashboards, or equivalents, to a standard that enables all consumers to easily identify, amend and revoke retail VRP consents.

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ii. Balance visibility in open banking retail payment customer journeys

117. Open banking enables consumers to see their bank balance as part of a payment journey, before confirming the payment.

How balance visibility potentially addresses unmet user needs

118. Balance visibility during the payment customer journey helps give consumers more control over their payments and enables them to budget.

Obstacle

119. In a minority of circumstances, open banking retail payment journeys do not currently allow consumers to see their bank balances before confirming a payment.

120. Specifically, the open banking Customer Experience Guidelines currently prohibit banks from showing the balance on an additional screen in the payment journey when account selection is in the 'merchant domain' (in order to minimise friction in the payment journey). This means that, where banks choose, or do not have the risk appetite, to show the balance on the authentication screen before the consumer has proved who they are, the consumer does not have an opportunity to see their balance.

Potential solutions and recommendation

121. There are workarounds to this issue, including account selection in the PISP domain or the PISP displaying the balance following a separate account information request to the bank.[28] Nevertheless, relaxing the Guidelines, to enable banks to show an additional screen, would allow all banks to show the balance to a consumer in all payment journeys, in a way that is proportionate to their risk appetite and technical capability.

122. As a result, all consumers would have visibility of their balance. This could encourage more use of digital payments by people currently reliant on cash for budgeting. We think, on balance, this benefit is likely to outweigh any friction from an additional screen in some banks' payment journeys.

Recommendation: The PSR should ask OBIE to consider updating the Customer Experience Guidelines to allow all banks to show the customer's balance in all payment journeys – including allowing banks to show the balance (either as an additional screen after authentication or as part of the authentication screen) when an open banking payment uses 'account selection at merchant'.

iii. Open banking payments at point of sale

123. In addition to their use in online payments, open banking retail payments could be enabled at physical retail point of sale (POS) in a way that is competitive with alternative payment methods.

How the open banking retail payments at POS potentially addresses unmet user needs

124. Competitive open banking payments at POS would extend the benefits of open banking retail payments, outlined in section C1, to physical payments, including balance visibility for the consumer; immediate settlement for the merchant; potential for value-added services; and potential to reduce prices borne by merchants.

Obstacles

125. Open banking single retail payments may currently be made at POS by the customer scanning a merchant QR code. After scanning the QR code, the consumer would be redirected to the banking app on their mobile device and would then need to authenticate the payment. This contrasts with the approach for contactless card payments, where the consumer's Near Field Communication (NFC) chip, in their phone or card, communicates instantaneously with the POS terminal. Authentication and transaction messaging are then carried through the POS terminal 'rails' associated with the card payment system, without further action by the consumer.

126. Issues with the current approach to open banking retail POS payments include the following:

- Consumers need to access their banking app online and then authorise payment. The risk of this resulting in even a short delay to completing the transaction significantly reduces the attractiveness of open banking payments in a physical retail environment, compared to the speed of contactless payments.
- QR codes are less secure than contactless communication between an NFC chip and a POS terminal.
- Contactless payments are very well-established and well-accepted by consumers.

127. Open banking retail payments are currently not able to use contactless payments. The POS ecosystem is not currently set up to deal with non-card payments, lacking necessary software and standards in POS terminals and messaging rails. In addition, on iPhones, Apple currently limits access to the NFC chip to the Apple Pay app.

28 An AIS call.

Potential solutions and recommendation

128. iPhone NFC chips should be made accessible to apps other than Apple Pay, in the way that Android NFC chips are accessible. We note that the European Commission is currently looking into Apple Pay.[29]

129. There are a number of possible avenues for achieving competitive open banking retail payment experience at POS. The way forward is not yet clear. VRP retail payment services could provide a partial solution. (At retailers where a consumer was a frequent shopper, they could set up a VRP consent for automatic payments up to a certain value, thus speeding-up the open banking checkout experience.) The existing POS ecosystem could be upgraded to enable contactless open banking payments at POS. Card Based Payment Instrument Issuers might also play a role in enabling contactless open banking payments at POS.

Recommendation: The PSR should investigate what actions may be needed to enable consumers to use their devices to make open banking retail payments at physical point of sale via contactless technology.

iv. Requests for payment

130. Based on research with users, the Payments Strategy Forum proposed a new digital service that would enable government, businesses, charities and consumers to create and send payment requests. Recipients of these requests would be able to decide if, how and when they wanted to respond. This would act as a complementary service to other forms of payment request such as Direct Debits.[30]

131. In May 2020, Pay.UK launched the 'Request to Pay' (RtP) messaging framework that works as an overlay with existing payments infrastructure. For each request from a biller, for example a consumer's utility company, there is a fixed set of options that the consumer may choose from: pay in full, pay in part, ask for more time, communicate with the biller, or decline to pay.

132. In addition, a range of alternative, competing open banking request for payment services are emerging, many of which support some or all of the features proposed in the RtP framework, and together offering a range of different payment option sets targeted on different users' needs.

How the request for payment services potentially address unmet user needs

133. Request for payment services directly address consumers', particularly low-income consumers', need for greater control and flexibility over their payments to help them budget. Also, at its most basic level, the payment request increases the transparency of payments by simply acting as a form of payment alert.

134. The additional control afforded by request for payment services may encourage more consumers to make use of digital recurring payments, such as Direct Debits, reducing the price premium they may currently face from using non-standard payment methods.

135. For billers, including small merchants, payment requests facilitate better data associated with payments, such as a reference label when requesting money, enabling easier reconciliation. Request for payment services may also facilitate better communication between billers and payers, reducing the costs to merchants of chasing payments.[31]

29 https://www.reuters.com/technology/exclusive-eu-antitrust-regulators-charge-apple-over-its-nfc-chip-tech-sources-2021-10-06/.

30 A Payments Strategy for the 21st Century Putting the needs of users first, Payments Strategy Forum, November 20.

31 Request to Pay, Pay.UK https://www.wearepay.uk/what-we-do/overlay-services/request-to-pay/.

Obstacles

136. Take-up of the RtP messaging framework has been slow, and no bank or merchant has yet brought live services to the market based on it. An obstacle to implementing RtP is the need for co-ordinated and widespread take-up by banks and merchants. Unless a critical mass of banks implements the RtP messaging service in their mobile banking apps, merchants are not motivated to adopt it. Yet banks are reluctant to implement the service without strong evidence of merchant interest. Many merchants remain unaware of RtP.

137. The RtP framework's prescribed set of five options for payers is seen by some merchants as complex and unsuited to their needs. For example, while the part-payment option may be helpful to utilities, typically it is not what many other payees, such as retailers and insurers, need. (For example, part-payment of insurance premiums could mislead consumers into believing they were covered.)

138. The RtP framework also requires a more complex adoption and sign-up process for consumers than has proved necessary in alternative open banking-based solutions. Consumers need to register with a provider, be given a Payer ID, share that Payer ID with the merchant and actively consent to receiving requests before they may receive a request from a merchant.

139. Lack of consumer trust could also act as an obstacle to take-up of request for payment services in general. For example, in order to avoid scams, consumers have typically been urged not to respond to requests to 'click to make a payment'.

Potential solutions and conclusions

140. One possible solution would be a regulatory requirement for banks to adopt the Pay.UK RtP framework. However, open banking has already enabled the introduction of functionally equivalent request for payment services that are being adopted and used by businesses and their customers. Given the emerging market in alternatives to RtP, which do not rely on banks to implement the RtP framework, it seems most important that obstacles to a competitive market in request for payment services are avoided. We expect take-up to be substantially driven by competing providers promoting their request for payment services. We do not therefore consider it would be appropriate to risk limiting market development by centrally mandating RtP.

141. Building consumers' trust in requests for payment is likely to be helped by trusted merchant brands adopting the services, by broadly consistent consumer experiences including consistent terminology across providers, and by addressing fraud risks (see sections B1 and C4). We are not persuaded that mandating the RtP standard, including its prescribed option set for payers, would be the right way to promote a consistent consumer experience.

142. We would like to see trusted brands, such as energy and water utilities, broadband, TV and mobile, begin to use request for payment services. This could help build trust in the payment type and have direct benefits for utility consumers who struggle with Direct Debits and for the utilities themselves by reducing the costs of failed payments. People on low or irregular incomes, who have hitherto avoided the inflexible monthly Direct Debits offered by utilities, may be encouraged to make more use of digital recurring payments.

143. The PSR could work with sectoral regulators, potentially through the UK Regulators Network, to raise awareness of request for payment services, in the context of sectoral regulators' responsibilities and objectives for protecting vulnerable consumers.

v. Paym

144. Paym is a service that enables person-to-person transfers using an individual's mobile phone number as their identifier. Paym requires access to mobile banking, and therefore a smartphone, to send money. It is available in many banks' apps.

How Paym potentially addresses unmet user needs

145. Paym allows individuals to pay money conveniently without having to use cash, while avoiding the inconvenience and risks of keying-in and sharing bank account details. There is scope in principle for Paym to be used in consumer-to-business payments, for example where a small merchant does not have a card reader (although businesses may prefer to instead make requests for payments using open banking services).

Obstacles

146. Paym was launched in 2014 but has failed to gain scale. We understand reasons for this may have included insufficient market-testing, lack of ubiquity of availability, limited promotion, inconsistent branding and operational features of the service, including friction in the user experience for new payment recipients.

Potential solutions and conclusions

147. Since 2014, new options for person-to-person digital payments have become available, including using open banking payment functionality. We think there is now potential for alternative person-to-person payment options to successfully gain scale.

148. Paym provides lessons for how to enable future new payment services to gain scale more successfully. The Payment Strategy Forum[32] examined lessons from Paym and from other cases.

149. We considered whether making Paym's routing table, which connects Paym customers' bank account details with their mobile numbers, more widely available (via API) could support development of other services using mobile numbers as identifiers. We concluded however that the costs of this would not be justified by the likely benefits. The routing table has limited coverage due to lack of take-up of Paym, and there are potential risks, for example misdirected payments where people have changed mobile number and their old phone number has been reallocated.

3 Improving the consumer experience of existing recurring payment services

150. Direct Debit is a long-standing and widely used service for billers, such as utilities, to pull fixed and variable amount regular payments from consumers, based on the Bacs payment system rails.

151. Continuous Payment Authority or 'card on file', enables a biller to pull variable amount payments on a recurring basis, based on card scheme rails.

Shortcomings in how these services address user needs

152. Direct Debit and card on file payments do not typically suit consumers with low or irregular incomes, who may struggle to budget for regular monthly lump sum payments. These consumers may incur penalties for failed payments – or they may use cash (or push payments) instead. Section C2 discussed the potential for requests for payment and for VRP retail payment services to give consumers greater control over digital recurring payments.

32 NPA Commercial Approach and Economic Models, Payments Strategy Forum, 2017.

153. At the same time, Direct Debit and card on file payments work reasonably well for many consumers who value the automatic, seamless management of regular payments. Many consumers recognise and place value on the Direct Debit Guarantee. Direct Debit also works well for many billers, with a high success rate compared to other payment types, and it is cheaper for them than alternatives.

154. Direct Debit and card on file therefore seem likely to continue to play a role in the digital payments landscape, potentially alongside newer, improved recurring payment services. We therefore think it is worth considering the case for proportionate enhancements to these services that could address some of their shortcomings and/or enable the transition to new recurring payment types.

155. It can take up to two weeks to set up a Direct Debit mandate and collect the initial payment. Billers are therefore increasingly seeking parallel digital sign-ups for both Direct Debit and for open banking VRP so that an immediate initial payment can be made via open banking. The digital sign-up process for Direct Debit is unfortunately not up to date nor consistent with the open banking sign up, increasing friction. It broadly mimics the old paper instruction form, including asking for a bank branch address.

156. Many smaller merchants face barriers to accessing Direct Debits, including because a limited number of banks sponsor Direct Debit services to smaller merchants. A reason for this is that the Direct Debit Guarantee is 'unlimited in time and value'. If a merchant is unable to honour a claim under the Guarantee, their sponsoring bank must pay out, limiting banks' appetite for sponsoring smaller businesses at a price acceptable to those businesses.

157. Many consumers do not receive an alert from their bank ahead of each Direct Debit (though a few banks do now provide this service). Few, if any, card issuers make card on file subscriptions visible to the consumer until a payment has been collected. Consumers may therefore lack awareness of their recurring payments, miss opportunities to budget better for them and risk 'subscription traps'.

Potential solutions and recommendation

158. There is a case for a modernised Direct Debit sign-up process, updated to good digital standards (including for mobile) and able to be offered in ways consistent with the open banking sign up. This could reduce friction, encourage more people to sign-up to recurring payments involving Direct Debit and help future transition to new recurring payment products. Better enabling parallel consumer consents for both Direct Debit and open banking payments could benefit billers and their customers, enabling the biller to switch between payment types according to the needs of the consumer. For example, if a consumer struggled with monthly lump sum payments, they could be offered an open banking request for payment service, while a consumer who preferred zero friction payments could remain on Direct Debit. Any investment in Direct Debit would need to be proportionate to the likely benefits and consider the likely longevity of Direct Debit in the context of emerging new services for making recurring payments.

159. There could be a case for limiting the Direct Debit Guarantee liability for smaller merchants, to reduce barriers to accessing Direct Debit. However, Bacs concluded[33] that imposing a time restriction on the Direct Debit Guarantee would involve a significant transfer of value from consumers to billers and their sponsor banks, and significant legal challenges would be likely to arise if such a change was attempted. We do not therefore recommend this and note that in future small merchants are likely to have an increasing choice of alternatives to Direct Debit for collecting recurring payments using VRP.

160. There could be a case for requiring alerts ahead of individual Direct Debit and card on file recurring payments. Banks are already required, following the CMA's retail banking investigation, to provide alerts before a customer enters overdraft, and some banks are already providing alerts ahead of individual recurring payments.

33 Direct Debit Consultation outcomes, Bacs, 2017.

Recommendation: The PSR should the explore options to bring Direct Debit into the digital age.

- The PSR should explore whether there are proportionate steps the industry could take to update the Direct Debit sign-up process for improved compatibility with open banking payments sign up and to help future transition to new payment products.
- The PSR should consider, with the FCA, encouraging all banks to provide digital alerts ahead of Direct Debits, as this could improve digital adoption by making Direct Debit work better for those for whom it is a struggle today.

4 Increasing consumer trust by addressing fraud risks

161. Consumers could be wary of the risk of fraud in new digital payment types, particularly, for example, when these involve messages with requests to make a payment. Reducing the risk of fraud would help increase consumer trust in – and therefore willingness to use – new digital payment services.

162. Open banking retail payments have the potential to limit the risk of fraud. The risk of misdirected payments and scams is reduced where the PISP, rather than the consumer, populates the payee's account details; information on banking credentials or card details is not shared with merchants; and the PISP may undertake due diligence on payees (in addition to that undertaken by the payee's bank). Open banking may engender trust by embedding a customer's own bank into the payment process, i.e., customers are redirected to their bank to authenticate payments.

163. There nevertheless remain risks, including that consumers make errors with the payment details (where a consumer populates them) or are tricked into paying a scammer via open banking payments. PISPs have yet to be fully integrated into arrangements for addressing fraud including dispute resolution mechanisms for allocating liability in open banking payments and the CRM Code for Authorised Push Payment scams (APP) scams.

Potential solutions and recommendations

164. One way to further promote trust could be to implement and promote a centralised open banking payments 'Trustmark' standard. However, a Trustmark would need to gain familiarity with, and earn the trust of, users. It could also in principle be fraudulently copied by scammers. Existing trusted merchant brands and promotion of payments brands are likely to play key roles in building consumer trust in open banking retail payments. Competition between payment providers may lead to innovation in effective approaches to building consumer trust and a centralised Trustmark standard could stifle this. The market ought to be given time to develop ways to build the trust of consumers in open banking payments.

165. There need to be effective incentives on all the parties able to address the risks of fraud and scams including, where appropriate, on PISPs. Pay.UK and OBIE are progressing work on enabling Confirmation of Payee (CoP) to be brought into relevant PISP payment journeys, which we support. The Lending Standards Board has been exploring how to enable PISPs to join the voluntary Contingent Reimbursement Model Code for protecting consumers from Authorised Push Payment (APP) scams and reimbursing them for losses. The PSR has consulted on potential mandatory requirements on Faster Payments participants to reimburse consumer for APP scams.

Recommendation: The PSR should help ensure effective incentives on PISPs to prevent fraud and scams:

- Completion of the Lending Standards Board's work to enable PISPs to join the Contingent Reimbursement Model (CRM) Code would enable PISPs to become subject to standards for protecting consumers from Authorised Push Payment (APP) scams and, where fault lies with them, to bear appropriate liability.
- The PSR's work on potential mandatory requirements that Faster Payments participants reimburse consumers for APP scam losses should ensure that, where fault lies with PISPs, they bear appropriate liability for reimbursement.
- The PSR should ensure effective dispute resolution arrangements for operationalising the appropriate allocation of liability for fraud or scam losses in open banking payments.
- ASPSPs' policies on transaction limits and blocking should be responsive to the effectiveness of an individual PISP's processes for reducing fraud risk, e.g., populating payee fields or undertaking effective due diligence on payees.

5 Incentivising performance of open banking interfaces adequate for retail payment use cases

166. For open banking payment services to compete successfully in a retail context, they need to be highly reliable. Reliability depends in part on the performance and availability of ASPSPs' APIs, on which open banking services rely.

167. The principle of parity, under the PSRs 2017, requires ASPSPs to ensure that their APIs offer at all times the same level of availability and performance to PISPs as their best-performing direct customer interfaces, e.g., banking apps. OBIE, noting that parity with a poorly performing direct customer interface could still lead to a poor open banking experience, went further, and established the 'OBIE Recommended Benchmark' for well-performing open banking APIs.[34]

168. The performance of some banks has not always met benchmarks for well-performing open banking APIs, in terms of availability and successful consents [35], making it harder for open banking payment services in turn to provide well-performing services. OBIE collates data[36] on reliability and performance and has been undertaking work on the root causes of unreliability. Most recently we note that overall performance levels have improved.

169. The standards for reliability required for the success of new retail payment use cases for open banking is likely to be higher than for some other use cases.

Potential solutions and recommendation

170. Effective application of sanctions for poor reliability of APIs would incentivise performance. The FCA has relevant powers of supervision and enforcement over all banks. The CMA could also penalise CMA9 banks if they were deemed not to have complied with the CMA Order. However, enforcement action by regulators is a somewhat nuclear option, that would likely be applied only in the most sustained and egregious cases of poor performance. Lesser instances of inadequate reliability and performance could undermine the competitiveness of open banking retail payments.

34 The Operational Guidelines, Open Banking Ltd, v. 3.1.9 https://standards.openbanking.org.uk/operational-guidelines/availability-and-performance/key-indicators-for-availability-and-performance/latest/.

35 PISPs may also sometimes be responsible for unsuccessful consents.

36 https://www.openbanking.org.uk/api-performance/.

171. In other regulated sectors, there are examples of virtually automatic financial and reputational incentives for instances of poor service performance. For example, rail operators and Network Rail are liable to compensate other rail operators affected by their performance shortcomings.[37] Utility regulators also typically put in place financial and/or reputational incentives related to utilities' performance.

172. Financial and reputational disincentives could be considered for inadequate performance open banking APIs.[38] It would be important that they did not enable banks simply to pay to deliver poor performance as a cost of business. So, any disincentive mechanism should not have the effect of reducing the likelihood of regulatory enforcement action for a given level of performance.

Recommendation: The PSR, with the FCA, should consider how to ensure that the performance and reliability of technical infrastructure supporting open banking account-to-account payment services, including APIs, is maintained at the level needed for competitive retail use cases, including looking at standards and incentives.

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6 Enabling the use of digital identity within digital payment services

173. Open banking provides a secure framework, based on APIs, which allows consumers to digitally authenticate themselves to share banking data or make a payment. There is potential for businesses to use the open banking framework to build additional value-added services, for example allowing consumers to share wider digital identity attributes with merchants. This could enable seamless transaction experiences such as a consumer being able to prove eligibility for a service, by validating their age or address, and making payment for the service, in a single digital step. There are successful international examples, such as BankID in Sweden and NemID in Denmark, of common digital authentication for accessing both banking and public services.[39]

174. This would benefit both consumers and merchants, by providing greater convenience and by reducing opportunities for identity theft and fraud.[40] Combining open banking payments with wider identity authentication services would enhance the consumer experience, potentially encouraging take-up of digital payments and helping open banking payments compete with cards.

Potential solutions and recommendation

175. The Government has recently consulted on proposals to support the market in developing digital identity services, including proposals for a Trustmark framework with standards for privacy, security, inclusivity and interoperability. The Government has said there need to be agreed technical and operating standards to define what good quality digital identity products look like.[41]

176. The Government's framework for digital identity needs to be compatible with open banking. Inappropriate standards could limit the ability of open banking-based digital identity services to provide the sort of ubiquitous experience that consumers and merchants value.

Recommendation: The PSR should engage with the Government on the development of digital identity standards to ensure that open banking capabilities can be used to implement digital IDs in transactions.

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37 Under the 'Schedules 8' train performance regime.

38 https://www.openbanking.org.uk/wp-content/uploads/2021/04/Consumer-Priorities-for-Open-Banking-report-June-2019.pdf (page 40).

39 Digital identity in the post-COVID era – how Open Banking can help, Accenture, Dec 2020.

40 As with any digital ID data, the consumer would be consenting for their data to be shared and potentially passed on, and appropriate safeguards would need to be in place.

41 Digital identity and attributes consultation, DCMS, July 2021.

ANNEX: MEMBERS OF THE DIGITAL PAYMENTS INITIATIVE PANEL SUB-GROUP

Dr Ruth Wandhöfer (Chair)	Chair of the PSR Panel
Flora Hamilton	Member of the PSR Panel
Andrew Hewitt	Member of the PSR Panel
Matthew Hunt	Member of the PSR Panel
Conor Langford	Member of the PSR Panel
Mark O’Keefe	Member of the PSR Panel
Anne Pieckeleon	Member of the PSR Panel
Natasha de Teran	Member of the PSR Panel
Mike Banyard	Director at Ordo
Neira Jones	Independent payments advisor
Faith Reynolds	Non-executive Director, PSR Board
Jack Wilson	Head of Public Policy (Global) at TrueLayer