

FB 001/15

Respondent's basic details

Consultation title:	Autumn 2014 PSR Consultation Paper – A new regulatory framework for payment systems in the UK (CP14/1)
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Confidentiality

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If you are claiming confidentiality over any part(s) of your response, please provide both a non-confidential Word version of your response and a confidential Word version in which specific information over which you are claiming confidentiality is **yellow-highlighted**. If you are not claiming confidentiality, please provide a Word version of your non-confidential response.

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Declaration

'I confirm that the correspondence supplied with this cover sheet is a formal consultation response that the PSR can publish. However, in supplying this response, I understand that the PSR may need to publish all responses, including those which are marked as confidential, in order to meet legal obligations, in particular if they are asked to disclose a confidential response under the Freedom of Information Act 2000.

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Craig Tillotson	
Name	Signed (original or scanned hard copy)

PSR Consultation Questions – Response template

This Word response template is intended to help stakeholders in responding to the questions set out in our Consultation Paper (PSR CP14/1) and in its Supporting Papers.

If you are claiming commercial confidentiality over specific information included in your response, please be sure to clearly mark this by **yellow highlighting** it. We will assume that all un-marked information is not confidential.

Responses should be emailed to us at PSRconsultations@psr.org.uk in Word and PDF formats by no later than **5pm on Monday 12 January 2015**. Any questions about our consultation can also be sent to PSRconsultations@psr.org.uk.

Thank you in advance for your feedback.

Question in relation to our proposed regulatory approach (see Part B of our *Consultation Paper* and *Supporting Paper 1: The PSR and UK payments industry* for more details)

SP1-Q1: Do you agree with our regulatory approach? If you disagree with our proposed approach, please give your reasons.

Yes.

Questions in relation to our proposed approach to payments industry strategy (see Part D of our *Consultation Paper* and *Supporting Paper 2: Payments industry strategy and areas for collaboration* for more details)

SP2-Q1: Do you agree with our proposed approach (Option 1) to set up a Payments Strategy Forum, as opposed to Option 2 (maintaining the Payments Council's or a successor body's role in setting industry strategy) or Option 3 (we develop high-level priorities for the industry ourselves), as described in *Supporting Paper 2: Payments industry strategy and areas for collaboration*? If you disagree with our proposed approach, please give your reasons.

Yes.

SP2-Q2: Do you have any comments on the design of the Payments Strategy Forum?

In particular, please comment on how the Forum could meet the need for broad stakeholder representation while still being effective.

Gaining timely agreement to the strategic direction, portfolio of change projects and allocation of change costs to a sector as diverse as payments is challenging. The PSR will have to play a particularly active role in ensuring an appropriate balance between broad, potentially conflicting, stakeholder views and timely and effective decision making. The PSR will also have to play a critical role in ensuring that there is a clear perception that views have been properly considered and appropriate decisions have been made – not everyone will be happy all the time. The PSR will also have to ensure that the Payments Strategy Forum is the only place such overall strategic and prioritisation decisions are being made, although some of the elements being considered may not be optional, given statutory requirements for change by particular deadlines. Good examples of these might include the provisions of retail bank ring-fencing and PSD-2 which will not be within the gift of the PSR to reprioritise. Requests from other stakeholders, no matter how influential, cannot be allowed to override these decisions if we are to move forward from the current situation. Given the unusual degree of cooperation and collaboration needed between stakeholders in many aspects of payments, we believe that The Payments Strategy Forum is a good place for the PSR to give guidance on which issues are in the competitive domain, and which require collaboration, and between whom. The PSR should quickly consider whether the existing Payments Council Government Coordination Committee (GCC) should be brought into the overall governance model by moving to becoming a reporting working group of the Payments Strategy Forum.

SP2-Q3: Do you have any comments on our indicative model for how the Payments Strategy Forum could operate in practice?

The model proposed is a good high-level view of how to approach this difficult task. The true complexities and challenges will only fully emerge once we start trying to operate the model. This should not stop us from proceeding in this direction, but will need to be considered as we move forward. In particular, thought will need to be given as to how prioritisation will occur. Some strategic options will impact on the ability to do other things and a clear mechanism for understanding and delivering on this will be required. The other core issue will be funding for initiatives. Coordination of potential funding of industry beneficial initiatives will be critical to successful delivery.

SP2-Q4: Are there any additional infrastructure-related themes you believe we, or the Payments Strategy Forum, should consider? If yes, please provide a description of why the additional themes are important to you.

We believe that the Payments Strategy Forum will additionally need to consider three areas: There is growing need for coordination of strategy around cyber risks and mitigations between payments systems and users as well as developing common approaches to AML and Fraud issues. Additionally, an industry approach to the provision of account access and/or payments initiation services to Third Party Payments providers (TPPs) is a growing service user issue and is likely to be brought to the fore by PSD 2.

Questions in relation to our proposed approach to the ownership, governance and control of payment systems (see Part E of our

Consultation Paper and Supporting Paper 3: Ownership, governance and control of payment systems for more details)

SP3-Q1: Do you agree with our proposed direction requiring all Interbank and Card Operators to ensure that there is appropriate representation of the interests of service-users in discussions and decision-making at board level? If you disagree with our proposed approach, please give your reasons.

Yes. FPSL agrees that there must be appropriate representation of the interests of service-users in discussions and decision-making at board level. We have been taking the first steps in this direction over the last few years using the Electronic Affiliates Group to gather a broad range of inputs from service users and recruiting independent directors to our board. In 2013, when we appointed our first independents, we ensured that they had available to them the power to veto any board decisions not in the public interest – you reflected this in your consultation document. In addition to this, also in 2013, we specified in their job descriptions that independent directors should

'ensure the Scheme strategy represents all the Scheme's members and other stakeholders such as indirect participants and end users (consumers, industry, regulators, and public policy)', and 'ensure that consumer, industry, regulators and public policy interests are represented at Scheme Board meetings and considered when developing the Board's strategy; and take a particular interest in any advisory panels or user forums which may be set up as part of any stakeholder consultation process.'

As part of this requirement, independent directors now attend the Electronic Affiliates Group and are also being aligned with potential new direct participants in the scheme during the joining process so that the new participants have an independent and direct link to the scheme board from an early stage in the process.

Synthesising the diverse interests of service-users in a way that is transparent, and efficient, will be challenging. The further development of the Electronics Affiliates Group is a good starting point, but there is much work to do. We intend to coordinate our efforts in this area with the other Interbank schemes to ensure efficiency for all parties, especially for the various consumer and other interest groups that will need to be engaged.

SP3-Q2: Do you agree with the costs and benefits identified for our proposed direction on Operators to ensure there is appropriate representation of the interests of service-users? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

While there may be some small incremental costs associated with the reporting requirements laid out in the consultation, we do not see any incremental costs associated with providing service user representation in board decision making beyond those steps we have already taken and planned to take anyway. We recognise the benefits you describe and we already have two independent directors and an independent chair that must ensure the interests of service users, and the public interest are properly considered in all board decision making. They will continue to engage in user fora like the Electronic Affiliates Group and directly engage with potential direct and indirect participants of the system to ensure proper and direct representation.

It is important to note that while each individual requirement from the PSR may not generate substantial incremental costs, the individual costs additionally associated with SP3-Q7, SP4-Q4, SP4-Q9, and of course the PSR setup costs and ongoing annual fees that

will be charged to Payment Systems Operators like FPSL, will place a significant additional cost on the scheme. A cost which, as a not-for-profit company, must be funded by participants.

SP3-Q3: Do you agree with our proposed direction on Interbank Operators requiring the Interbank Operator to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? If you disagree with our proposed approach, please give your reasons.

Yes.

SP3-Q4: Do you agree with our proposed approach not to issue directions at this time in relation to the other types of conflicts of interest identified by stakeholders? If you disagree with our proposed approach, please give your reasons.

Yes. We believe that we have a well-defined set of processes to identify and manage conflicts of interest within the governance of the scheme. These are processes that have been exercised with respect to the recent re-commissioning of our supply agreement with our infrastructure supplier and were high-lighted as a case study within the Accenture Governance report.

SP3-Q5: Do you agree with the costs and benefits identified for our proposed direction requiring the Interbank Operators to take all reasonable steps to ensure that any individual acting as a director of that Operator must not simultaneously act as a director of an actual or potential Central Infrastructure Provider to that payment system? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

Yes.

SP3-Q6: Do you agree with our proposed direction to require all Operators to publish board minutes in a timely manner? In particular, do you agree with our proposal for the published minutes to include a record of votes and reasons for decisions made? If you disagree with our proposed approach, please give your reasons.

Yes. We assume that this direction will apply to all board meetings held from 1st April 2015. This should allow the scheme time to develop an appropriate redaction policy and for the PSR to ensure consistency in approach across all regulated parties. We have no objection to publishing records of votes and reasons for decisions. We would however note that final bullet of CP14/1.3 para 3.177 (requiring a statement from independent directors saying how, for each board decision, they have exercised their discretion related to public interest matters), will need to be implemented in a proportionate manner. Given the current frequency of board meetings, quarterly, and the need to gain sign-off from non-executive and independent non-executive directors, the publication timetable will need to be sensibly determined.

SP3-Q7: Do you agree with the costs and benefits identified for our proposed direction to require all Operators to publish board minutes in a timely manner? Can you provide any data that might further inform our analysis of the likely impact of our proposed direction?

We believe that production of publishable minutes, and application of an agreed redaction policy will increase the costs of scheme governance, but we do not believe this is significant overall.

SP3-Q8: Do you agree with our proposed approach not to issue a direction at this time in relation to Payments Council reserved matters? If you disagree with our proposed approach, please give your reasons.

Yes, FPSL and Payments Council formally terminated their relationship agreement and with it the reserved matters on 16th December 2014 and therefore no direction to FPSL will be required.

Questions in relation to our proposed approach to access to payment systems (see Part F of our *Consultation Paper and Supporting Paper 4: Access to payment systems for more details*)

SP4-Q1: Do you agree with our preferred option that an Access Rule, aligned with Principle 18 of the CPSS-IOSCO Principles, should be applied to those pan-GB Operators not subject to Regulation 97 of the PSRs 2009 (i.e. Bacs, C&CC, CHAPS and FPS)? If you disagree with our proposed approach, please give your reasons.

Yes. However, for efficiency and simplicity we strongly recommend that Principle 18 should be interpreted the same way by both the PSR and Bank of England. For similar reasons, while we would continue to expect the Bank of England to be the lead regulator, in general, for the application of the Principles for Financial Markets Infrastructure, it would be helpful if the PSR led the review of specific compliance with Principle 18 on behalf of both regulators. To the extent that the PSR wants to add more specific requirements, these should be articulated as additional requirements, rather than different interpretations of the existing principles.

SP4-Q2: Do you agree with our proposal to introduce a Reporting Rule (on compliance with the access obligations applicable to them) on all relevant pan-GB Operators (i.e. Bacs, C&CC, CHAPS, FPS, LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

Yes. The reporting timetable needs to be aligned with those of the Bank of England for the full CPMI IOSCO self-assessment and disclosure so that the annual process can be done efficiently.

SP4-Q3: Do you agree with our proposal to require public disclosure of Access Requirements for Operators subject to Regulation 97 of the PSRs 2009 (i.e. LINK, MasterCard and Visa)? If you disagree with our proposed approach, please give your reasons.

We have no comment to make.

SP4-Q4: Do you agree with the costs and benefits identified for our Access Package (i.e. our Access Rule and Reporting Rule)? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

We do not believe that the Access and Reporting Rule will generate substantially greater benefits or costs from those we are already incurring and planning for in executing our own strategy for enhancing access. We disagree with your estimates of the costs the Operators will incur in delivering an effective Access Package in CP14/1.4 para 4.180 and note 70. FPSL already has more than 5 FTEs working on Access today and has allocated further budget for this in the future.

SP4-Q5: Do you agree with our proposed direction requiring Sponsor Banks to publish certain information? If you disagree with our proposed approach, please give your reasons.

Yes. We welcome steps that will help the Indirect Access market function effectively.

SP4-Q6: Do you agree with our proposed approach in relation to the development (by industry) of an Information Hub? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

While we support the development of an Information Hub we believe the requirements for it, and the consequent benefits that can be delivered should not be overstated. There are a limited number of parties that seek access to this type of information, probably in the order of 150 – 300 in total. Sign-posting from this hub to www.fasterpayments.org.uk will be beneficial.

SP4-Q7: Do you agree with our proposed approach in relation to the development (by industry) of a Sponsor Bank Code of Conduct, to be approved by the PSR? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We agree that a common/generic Sponsor Bank Code of Conduct should be developed, specifically by the sponsor banks engaging with their Agency customers, and that approval by the PSR will be beneficial.

SP4-Q8: Do you agree with our proposed approach in relation to the development (by industry) of Technical Access solutions? Or do you consider that we should take a more prescriptive approach at this time? If you disagree with our proposed approach, please give your reasons.

We welcome the PSR's support for encouraging the development of a variety of competitive Technical Access Solutions to Faster Payments, and where relevant, to other systems and services. We believe that our own plans are consistent with this approach - see our White Paper, '*Faster Payments – A Vision for a New Access Model, Opportunities for Payment Service Providers and Solutions Vendors*' published on the 8th December 2014, and downloadable from our website. This consistency eliminates one of the most significant risks posed to our strategy, namely that third parties fail to engage with us as they hold out for some form of other regulatory intervention. We believe the time is right for the development of these competitive solutions, and that further specification from the PSR is not required at this stage, although we continue to welcome the PSR's strong interest in their development.

SP4-Q9: Do you agree with the costs and benefits identified for our proposed direction on Indirect Access? Can you provide any data that might further inform our analysis of the likely impact of our directions?

We do not see substantial incremental benefit or costs arising from these Indirect Access proposals over and above our own plans and the significant investments we are making in this area. FPSL wishes to see its real time payments capability made available to all the service users that require it, independent of their access mode. These proposals support that aim.

Question in relation to our proposed approach in relation to interchange fees (see Part G of our *Consultation Paper Supporting Paper 5: Interchange fees* for more details)

SP5-Q1: Are there other matters regarding interchange fees that you think we should consider at this stage?

We have no comment to make.

Questions in relation to our proposed approach to our regulatory tools (including our high-level Principles, and our enforcement and dispute resolution processes) (see Parts H and I of our *Consultation Paper Supporting Paper 6: Regulatory tools* for more details)

SP6-Q1: Do you agree with our three proposed high-level PSR Principles on Relations with regulators, Compliance and Financial Prudence? If you disagree with our

proposed approach, please give your reasons.

Yes, although we note that Principle 3 already applies to FPSL via the CPMI IOSCO PFMIs and our supervision by the Bank of England.

SP6-Q2: Do you agree with our proposed approach that our PSR Principles on Relations with regulators and on Compliance should apply to all participants? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider they should apply to and why.

Yes.

SP6-Q3: Do you agree with our proposed approach that our PSR Principle on Financial prudence should apply to Operators and Central Infrastructure Providers? If you disagree with our proposed approach, please give your reasons for disagreeing, and explain which categories of participants you consider it should apply to and why.

Yes. We believe that FPSL is already subject to these requirements via the CPMI IOSCO PFMIs, but support the extension to Central Infrastructure Providers. The locus of responsibility on these matters between the PSR, and the Bank of England as supervisor of the designated FMIs will need careful management

SP6-Q4: Do you think that we should also adopt some or all of the additional proposed Principles relating to Integrity, Skill care & diligence, Management & control, Governance, Service-users' interests, and/or Conflicts of interest? If you think we should adopt some or all of the additional proposed Principles, do you agree with the proposed participants to which each Principle would apply? Please give reasons for your response. If you disagree with the proposal to adopt some or all of the additional Principles, please give reasons for your response.

As an FMI, we are already subject to the CPMI IOSCO PFMIs. The board directors have Companies Act responsibilities. Given this, and because the PSR is being established as an Economic Regulator, not a Conduct Regulator, we do not believe that it is either necessary, nor appropriate for the PSR to take on additional conduct principles from the FCA – a Conduct Regulator.

Related to this point, while we understand the cost advantages of the PSR being operated as a subsidiary of the Financial Conduct Authority, we are very surprised that the PSR Board has been established wholly from within the FCA Board. While some overlap is clearly beneficial, we believe that not only must the PSR executive include a strong economic regulatory skill set and capability, but this must also be reflected in the composition of the PSR Board which oversees the executive.

In its response to the consultation about *Opening Up Payments*, published in October 2013, HM Treasury stated in para 2.11 that

'While the Government wants the Regulator to benefit from synergies with existing FCA resource, it is also important that it has the freedom to develop its own strategy for meeting its payments objectives.'

and in para 2.14 that

'the Payments Systems Regulator will adopt a utility-style approach, distinctive from the FCA's existing remit. The PSR will have a distinctive role to that of the FCA and will require a different set of skills in order to fulfil that role'.

A PSR Board made up entirely of a subset of the FCA Board does not seem to promote the possibility of the PSR having a distinctive role to that of the FCA, and may blunt its effectiveness as a true economic regulator.

SP6-Q5: Do you agree with the anticipated costs and benefits identified for our three proposed high-level Principles? Can you provide any data that might further inform our analysis of the likely impact of our proposed directions?

For FPSL we see no incremental benefits or costs associated with compliance with the three proposed high-level principles.

SP6-Q6: Do you agree with our proposed approach for our Objectives Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q7: Do you agree with our proposed approach for our Administrative Priority Framework, or are there any additional points that you think we ought to cover? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q8: Do you agree with our proposed approach for our Powers & Procedures Guide? If you disagree with our proposed approach, please give your reasons.

Yes, in general. However, we would like to see a more symmetrical set of deadlines for formal interaction between the scheme and the PSR. For example, paras 4.2 and 11.1 in Annex 3 to CP14/1.6 require the scheme to respond to a request from the PSR within 14 days, while para 1.0 in Annex 4 of CP14/1.6 allows the PSR up to 90 days to respond to a request to it. Given the size of many Payment Systems Operators, at least 28 days to respond, to allow for critical staff being on annual leave, for example, would seem more appropriate.

In paras 5.1 and 5.2 in Annex 3 to CP14/1.6 the PSR is not currently required to formally communicate to PSOs when consulting on the provision of a general direction or imposition of a generally-imposed requirement. Given that there are less than ten designated PSOs, it does not seem unreasonable for the PSR to be required to communicate formally to each

PSO that such directions are being considered.

In para 6.2 we do not understand why the appeal route to the Competition Appeals Tribunal (CAT) available for specific directions or requirements is not also the appropriate appeal route for general directions or requirements. The restriction to Judicial review seems a disproportionately high hurdle versus the CAT.

SP6-Q9: Do you agree with our proposed approach for our dispute resolution and applications procedures? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q10: Do you agree with our proposed approach for our Super-Complaints Guidance? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q11: Do you agree with our proposed approach to setting penalties? If you disagree with our proposed approach, please give your reasons.

Yes.

SP6-Q12: Do you think that we should also take into account metrics other than revenues when setting penalties, in particular when considering participants organised as not-for-profit entities (e.g. should we take into account the value of funds transferred through the relevant system and relating to that participant in such a case)?

No. The use of value of funds transferred could be highly distortive as any detriment being addressed is unlikely to be aligned to the value of funds involved and could expose the scheme to an unmanageable regulatory financial risk. Ten per cent of funds transferred for FPSL would amount to a fine of over £100 billion!

SP6-Q13: What should be the upper limit (if any) on penalties (e.g. 10% of annual revenues derived or billings made by the participant from the business activity in the United Kingdom to which the compliance failure relates), and should this upper limit differ according to the category of participant?

An extreme upper limit of 10 per cent of scheme costs/revenue would seem proportionate. However FPSL operates on a not-for-profit/cost recovery basis and the incremental cost of any fine would have to be recovered from all system participants. There is no profit margin/shareholder return or dividend that can be used to fund such a fine.

SP6-Q14: Do you agree with our proposed approach with respect to the enforcement and enforceability of penalties? If you disagree with our proposed approach, please give your reasons.

Yes. However, we are concerned that the interplay between fines and the Financial prudence principle, expressed in 6.101 and 6.102 in CP14/1.6 would be unworkable unless the upper limit on penalties is set proportionately and pragmatically. If FPSL were required to have in place funding arrangements to deal with a fine of 10 per cent of value transferred, then even a very small system participant, perhaps with 0.1 per cent of system volume would be potentially exposed to a liability of £100 million as their share. This would represent a very significant regulation induced barrier to participation.