Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Submitted by email: digitalpoundconsultation2023@bankofengland.co.uk and CBDC@HMTreasury.gov.uk

Dear Sir / Madam,

Financial Services Consumer Panel response to the Bank of England and HM Treasury's Consultation on the Digital Pound

The Financial Services Consumer Panel (the Panel) is an independent statutory body. We represent the interests of individual and small business consumers in the development of policy and regulation of financial services in the UK.

While the Panel's focus is predominately on the work of the FCA, we are responding to the Consultation on the Digital Pound because currency and payments are the cornerstones of the financial system and essential to consumers. Any decision on whether and how to introduce a Digital Pound, or whether and how to proceed without one, is a very consequential decision – most especially against the backdrop of growing digitisation. We therefore welcome this consultation as an important step in broadening the public conversation about the Digital Pound.

A Digital Pound, if introduced, would become part of the overall Payment System in the UK. The Payment System is crucial for all UK consumers: the ability to safely receive, store and spend a ubiquitously accepted unit of account and medium of exchange is of paramount importance to our society and economy. For this to be achieved, we believe the Payment System (whether including a Digital Pound or not) must be guided by the following principles:

- **Accessibility -** All UK consumers must be able to pay and be paid. The system must be accessible to all.
- **Fairness and affordability -** The cost of making payments should not exclude particular consumers, businesses of transaction types. It should not cost more for the poorest to pay.
- **Reliability & resilience -** The Payment System must be robust and reliable with appropriate redundancy measures in place to

ensure continuity of service in case of need. The failure of individual providers should not result in consumer losses.

- **Safety, security and consumer protection –** The Payment System must be safe and secure. It should offer protection to consumers, including against fraud and losses resulting from a firm's failure.
- **Transparency –** The costs, risks and protections associated with using different providers and services must be clear and easily understandable. Providers should also offer full transparency about how end users' data is used, by whom and to what end.

The remainder of this letter discusses the key issues we believe the Bank of England and HM Treasury must consider in order for the development of the Digital Pound to be in line with these principles.

Digitalisation and the risk of further fragmentation

The Payment System has been carefully built up over centuries through innovation and iteration, legislation and regulation, competition, interventions, technology, consumer need and custom. Thanks to this, central and commercial bank money are perceived 'as one', and the vast majority of UK society can benefit from the seamless, speedy exchange of value; a single unit of account being trusted, accessible and exchangeable throughout the economy, regardless of its form.

The rise of digitisation challenges this. While digitisation has brought immeasurable improvements in the way that we can access and use money, expanding economic opportunity and driving new forms of commerce, it also poses several risks. Most notably it presents the risk of fragmenting the Payment System.

Fragmentation of the Payments System could lead to a greater rate of financial exclusion, higher costs[1], new unwanted risks; a loss of competition, huge economic inefficiencies and, ultimately, economic and societal instability. The importance of preserving a System through which a single unit of account can be accessed, trusted and seamlessly exchanged and redeemed at par – irrespective of its form - cannot be underestimated. It is pivotal to the future functioning not just of our financial system, but of our economy and society.

To an extent fragmentation is already evident in payments – most notably between the cash and non-cash parts of the economy. Those consumers

[1] For example, Fair By Design has found the premium for using a prepaid card is £36 over a year and for cash, 1 in 3 low income households pay a premium of £20 over the course of a year.

that are dependent on cash increasingly find both access to and acceptance of cash being compromised – whether through cost of access or non-acceptance. This situation is likely to accelerate as habits continue to change and may even be worsened by the introduction of a Digital Pound.

Digital and financial inclusion

We recognise that in any transition – such as the digital transition currently underway – there are risks of some being left behind. Innovation theory evidences that such transitions are gradual. Innovators are typically followed by early adopters, the early majority, the late majority and eventually by 'laggards'. It is not exceptional for the later cohorts to suffer temporary disadvantage, marginalisation or exclusion as a result of their late adoption of new technologies.

Innovations in payments and domestic currencies are, however, different. Everybody depends on payments and currencies all the time, and ensuring everybody has fair and affordable access to them is in the public interest. Payments and currencies depend on trust and access being universal. Trust and access are mutually reinforcing – without access trust can evaporate and without trust, access loses its utility. Excluding some from payments and currencies – or prejudicing their access to the system – is not an option, even on a temporary basis.

The digital transition makes this a very real prospect. It is in the public interest that this is addressed.

The Panel believes that, if designed appropriately, a Digital Pound could – alongside the Bank's commitment to continuing to make physical cash available for as long as there is demand for it – provide a means of addressing the transition problem. It could help to prevent further financial marginalisation and exclusion in what will undoubtedly be a more digital future.

Furthermore, a Digital Pound could even improve on the status quo. As a digital form of cash, a Digital Pound will arguably be superior to its physical alternative: cash risks theft and loss and relies on proximity for its utility, whereas a digital wallet stored on a lost or stolen smartphone or other device should be protected by security measures relating to the device and the wallet stored on it. If designed appropriately, a Digital Pound could also help encourage cash-users into the digital economy thereby both extending their access to a wider range of products and services and providing them with a means of safely storing and freely accessing and exchanging their funds.

As importantly, a Digital Pound could (and if rolled out *should*) be designed to maximise inclusion and to minimise costs for the poorest. It could be designed to ensure that those on lower incomes, or who are less digitally or financially literate, are properly served, and are not excluded or penalised in terms of the costs and risks they face in exchanging and storing value.

As mentioned above, there is already evidence that such consumers have been disadvantaged by the fall in the use of cash. They have also been adversely affected by the closure of bank branches which has complicated their awareness of and access to basic bank accounts. Many such consumers have been pulled into using newer non-cash forms of payment, such as prepaid cards and e-money accounts. These entail more risks, have weaker safeguards and cost more than basic bank accounts. Whilst we welcome many of such innovations, we do not believe that the poorest and most vulnerable should pay and risk the most to store and exchange value.

Payments are essential to participating in modern society and it is in the public interest that the ability to make and receive payments-whether in cash or via a Digital Pound-should be affordably accessible to all. We strongly support the ongoing provision of basic bank accounts. However, we also believe that a Digital Pound, together with an appropriately designed and rigorously upheld framework for participating Payment Interface Providers (PIPs), could present a much-needed opportunity to provide an updated universal offering – a manifestly available, digitally-designed, accessible and affordable alternative for all that need it.

Whilst we recognise that there might be other means to achieve these aims, we are not aware that any developed alternative has yet been put forward. We would strongly encourage the Bank and HM Treasury to keep these issues and these consumers front of mind as they continue in their exploration of whether to proceed with a Digital Pound.

Maintaining a consumer focus

The current discussion paper gives much emphasis to the economic and technological issues involved, but for a Digital Pound to be functional, trusted and useful these need to be considered in light of consumers' likely experiences. We therefore recommend that the Bank and HM Treasury, as part of the next phase of its work, conducts consumer research to:

- explore in detail the questions and concerns consumers (including small businesses and microbusinesses) have about the use (and usefulness) of a Digital Pound

- explore use cases specifically designed to identify potential user problems that will need to be designed out of the system.

We expect the findings of this research to demonstrably inform the eventual decision whether or not to proceed with the Digital Pound, as well as guide early and all subsequent stages of system architecture development.

We recognise that this consultation is only the beginning of the discussions on a Digital Pound. We would also like to see the Bank and HM Treasury actively seeking input from consumer groups and representatives throughout all future stages. This should include a dedicated engagement strategy and the broadening of membership of the CBDC Engagement Forum to include more consumer-focussed members.

Designing a Payment System fit for the future

In considering the development of the Digital Pound, the Bank should bear in mind that the context they should explore is not so much the present context – but a future, more digital one. And therefore, any decision *not* to proceed with the Digital Pound should be accompanied by a clearly developed proposal setting out how the aims discussed above will be ensured in that same digital future.

We set out our answers to the questions in the consultation in Annex A below.

Yours sincerely,

Helen Charlton

Chair, Financial Services Consumer Panel

Annex A – Responses to questions

1. Do you have comments on how trends in payments may evolve and the opportunities and risks that they may entail?

The Panel strongly concurs with the key concern set out in the Consultation Paper, namely that uniformity in money risks being undermined and fragmentation occurring, with all the attendant risks that would bring. We would encourage the Bank and HM Treasury to have particular regard in their deliberations on whether to introduce a Digital Pound as to how the more vulnerable and less remunerative customers will be served in a more digital future.

2. Do you have comments on our proposition for the roles and responsibilities of private sector digital wallets as set out in the platform model? Do you agree that private sector digital wallet providers should not hold end users' funds directly on their balance sheets?

The Panel supports the proposition as set out in the Consultation Paper and agree that private sector digital wallet providers should not hold end users' funds directly on their balance sheets.

3. Do you agree that the Bank should not have access to users' personal data, but instead see anonymised transaction data and aggregated system-wide data for the running of the core ledger? What views do you have on a privacy-enhancing Digital Pound?

The Panel agrees that the Bank should not have access to users' personal data and strongly support the privacy-enhancing proposal set out in the Paper.

4. What are your views on the provision and utility of tiered access to the Digital Pound that is linked to user identity information?

The Panel supports the tiered access model.

5. What views do you have on the embedding of privacy-enhancing techniques to give users more control of the level of privacy that they can ascribe to their personal transactions data?

The Panel strongly supports privacy-enhancing techniques being embedded in the Digital Pound.

6. Do you have comments on our proposal that in-store, online and person-to-person payments should be highest priority

payments in scope? Are any other payments in scope which need further work?

The Panel agrees that in-store, online and person-to-person payments should be the highest priority payments.

7. What do you consider to be the appropriate level of limits on individual's holdings in transition? Do you agree with our proposed limits within the £10,000–£20,000 range? Do you have views on the benefits and risks of a lower limit, such as £5,000?

The Panel was surprised how high the proposed limit was set in the Consultation Paper. While acknowledging that the lower limit of £5,000 would accommodate only a third of people to receive (all) their pay in Digital Pounds, in doing so it would accommodate those most likely to need to rely on a Digital Pound. A lower limit like this would also be much more effective at curbing large bank deposit outflows as acknowledged in the Consultation and, we would presume, have less impact on bank lending. Combined with sweeping technologies, it would also enable middle and higher earners to receive part of their salaries in Digital Pounds. The Panel would also note that the assumption made in the Chart D.9 is that consumers would hold surplus balances over from month to month as 'digital cash' rather than sweeping these unremunerated balances into interest-paying accounts which would seem a more likely outcome (at least for as long as the Digital Pound remains unremunerated).

8. Considering our proposal for limits on individual holdings, what views do you have on how corporates' use of Digital Pounds should be managed in transition? Should all corporates be able to hold Digital Pounds, or should some corporates be restricted?

SMEs, which typically face disproportionately high charges for making and receiving payments as well as long settlement delays, could potentially strongly benefit from a Digital Pound and should be able to hold and use it. Recognising the challenges in calibrating the size of balances that corporates should be able to hold and the potential impacts on monetary and financial stability, we would encourage the Bank and HM Treasury to explore carefully how sweeping and instantaneous automated transfers might work in practice – not only with the financial industry, but with microbusinesses and small and medium-sized corporates that might eventually depend on them.

9. Do you have comments on our proposal that non-UK residents should have access to the Digital Pound, on the same basis as UK residents?

The Panel understands and supports the practical motivation for allowing non-UK residents access to the Digital Pound. Recognising that the Bank is actively engaged in international fora and is sensitive to the risks of currency substitution occurring in more vulnerable currency zones, we presume it would actively monitor this to avoid inadvertent upset.

10.Given our primary motivations, does our proposed design for the Digital Pound meet its objectives?

The proposed design for the Digital Pound *does* meet its objectives, however the design alone will not lead to the Digital Pound's success. Its success will also depend on integration with the commercial banking system and the consumer roll-out, including consumer education and awareness. It's initial and ongoing success will also require strict ongoing enforcement of the principles for PIPs, particularly where it comes to inclusive design, universal access and comprehensive marketing reach.

11.Which design choices should we consider in order to support financial inclusion?

To have true utility the Digital Pound must be universally accessible to the UK population. This does not just depend on its design, including the potential for offline payments; or the principles set for PIPs and the strict monitoring of PIP's adherence to them, but also on comprehensive awareness and understanding of the Digital Pound. Ensuring the initial and ongoing awareness amongst the public will not be a trivial endeavour and will require a carefully considered initial and ongoing engagement, education and marketing programme that we presume would depend on public, third and private sectors combined. Given that the financial incentives for serving those on low incomes will be low, it will be essential that the principles for PIPs govern not only inclusive product design and service features, but also initial and ongoing marketing and promotion requirements.