

Financial Conduct Authority



Payment Systems Regulation Call for Inputs

5 March 2014

Contents

1 OVERVIEW	3
Introduction	3
2 BACKGROUND	4
What is a payment system?.....	4
The Payment Systems Regulator	5
Who will the PSR affect?	7
3 THE PROPOSED APPROACH.....	9
Purpose of this Call for Inputs.....	9
What we are trying to understand	9
4 NEXT STEPS.....	17
What do you need to do next?	17
What will happen to your feedback?.....	17
ANNEX 1: COVER SHEET	19
ANNEX 2: RESPONDING TO THIS CALL FOR INPUT.....	20
When to send your response	20
How to submit your response	20
ANNEX 3: QUESTIONS	22
ANNEX 4: GLOSSARY OF TERMS	25

1 Overview

Introduction

The Financial Services (Banking Reform) Act 2013 requires the Financial Conduct Authority (FCA) to establish a new regulator for payment systems in the UK.¹ This new regulator, referred to in this paper as the 'Payments Systems Regulator' or 'PSR', will be incorporated as a subsidiary of the FCA by April 2014, and will be fully operational in April 2015.

Payment systems form a vital part of the financial infrastructure, enabling funds to be directly transferred between people and institutions, or other systems. Every year these payment systems process over 7 billion transactions, worth over £75 trillion.

Building on previous consultations by HM Treasury and the Office of Fair Trading, we are asking for views on the UK payments industry, in particular on issues of competition, access, governance, ownership and innovation.

We anticipate the findings of this exercise will inform the PSR's approach as it develops specific regulatory options for formal consultation later this year.

We invite all stakeholders and participants in UK payment systems to provide written views and comments on the issues raised in this document, **to the PSR by 5pm 15 April 2014.**² Details of how to respond to this Call for Inputs are set out in section 4 and Annex 2 to this Call for Inputs.

¹ We have published this paper as part of our duty under the Banking Reform Act to set up the PSR and ensure it is capable of exercising its functions. Publishing the paper now will also enable interested parties to submit information relevant to the PSR following its incorporation at the earliest possible opportunity.

² The PSR will provide the FCA with information relevant to its functions under a statutory gateway to be set out in secondary legislation under section 91 of the Banking Reform Act.

2 Background

The establishment of the PSR under the Banking Reform Act is the culmination of a series of reviews into UK payment systems.³

In March 2013, HM Treasury published a consultation *Opening up UK payments*⁴ on implementing regulation of UK payment systems. The consultation proposed the introduction of a competition-focused, utility-style regulation of payment systems.

In response to HM Treasury's consultation, the Office of Fair Trading (OFT) gathered evidence on competition and innovation in payment systems in the UK. In July 2013, the OFT published a report *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*⁵.

In December 2013, the Government introduced legislation through the Banking Reform Act to require the FCA to establish a new regulator for payment systems in the UK.

What is a payment system?

Under the Banking Reform Act, a payment system is defined as “a system which is operated by one or more persons in the course of business for the purpose of enabling persons to make transfers of funds, and includes a system which is designed to facilitate the transfer of funds using another payment system”.⁶

A payment system is effectively a set of rules designed to enable transfers of funds. The rules are determined collectively by the member organisations that own the payment system operators, set out how payments are processed and establish the

³ The reviews started with the *Cruikshank Report*, published in March 2000, which highlighted several competition concerns and inefficiencies associated with payment systems in the UK. Following this, the Office of Fair Trading (OFT) conducted several market reviews, including establishing the Task Force, which published four Working Group reports. The Independent Commission on Banking (ICB), the Treasury Select Committee (TSC), the OFT and HM Treasury published several reports and consultations between 2010 and 2013 highlighting ongoing concerns with the UK payments industry.

⁴ Available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/221903/consult_opening_up_uk_payments.pdf

⁵ Available at: http://www.offt.gov.uk/shared_offt/markets-work/OFT1498.pdf

⁶ Banking Reform Act, s.41(1).

criteria service providers need to meet in order to gain access to the system. Payment system operators contract with infrastructure providers to authenticate, process, and reconcile transactions amongst the service providers in the system.

The definition of a payment system does not include: (i) any arrangements for the physical movement of cash; (ii) a system that does not make any provision for the transfer of funds by payers, or to recipients, in the UK; (iii) a securities settlement system; (iv) a system operated by a recognised clearing house; or (v) any other system whose primary purpose is not that of enabling persons to transfer funds.⁷

Not all payment systems as defined by the Banking Reform Act will be regulated by the new PSR. HM Treasury is responsible for designating which payment systems are to be regulated through secondary legislation. It is expected that, following a consultation, HM Treasury will designate these payment systems by April 2015.

HM Treasury may only designate a payment system as being regulated if they are satisfied that any deficiencies in the design of the system or disruption of its operation would be likely to have serious consequences for users or likely users of the system.⁸ This is likely to be true for the major payment systems and payment card networks in the UK.

The Payment Systems Regulator

The PSR will be established as a subsidiary of the FCA, with its own Managing Director and Board. The FCA will incorporate the PSR in April 2014 and it will become fully operational in April 2015.

The PSR has a number of general duties relating to payment systems. These are: (i) giving general directions;⁹ (ii) giving general guidance; and (iii) determining the general policy and principles by reference to which it performs particular functions.¹⁰

The PSR has its own statutory objectives, distinct from those of the FCA:

- **The competition objective** is to promote effective competition in the market for payment systems and the markets for services provided by payment systems in the

⁷ Banking Reform Act, s.41(2).

⁸ Banking Reform Act, s.44(1).

⁹ 'General directions' are those that fall within section 54(3)(a) or (b) of the Banking Reform Act 2013, i.e. the directions apply generally (to all participants in payment systems) or they apply to: (i) all operators; (ii) all infrastructure providers; (iii) all payment service provider; or (iv) every operator, infrastructure provider or payment service provider of a specified description.

¹⁰ Banking Reform Act, s.49(4).

interests of service-users or likely users of payment services. This may include promoting competition between different operators of payment systems, different payment service providers and different infrastructure providers.

- **The innovation objective** is to promote the development of, and innovation in, payment systems in the interests of service-users and likely users of payment services, with a view to improving the quality, efficiency, and economy of payment systems. This includes promoting the development of and innovation in payment systems infrastructure.
- **The service-user objective** is to ensure that payment systems are operated and developed in a way that takes account of, and promotes, the interests of service-users and likely users of payment services.

In exercising its general functions¹¹, the PSR must also have regard to financial stability, the importance of payment systems in relation to the performance of monetary policy by the Bank of England, and general regulatory principles.¹²

The PSR will have concurrent competition powers with the Competition and Markets Authority (CMA) as well as five other specific regulatory powers. These are: (i) giving directions to payment system participants; (ii) imposing requirements on operators regarding system rules; (iii) the power to require the granting of access to payment systems; (iv) the power to vary agreements relating to payment systems; and (v) the power to require disposals of interests in payment systems.

The existing functions that relate to payments regulation, for example, the Bank of England's oversight responsibilities over recognised payment systems, will broadly remain unchanged. The PSR will work closely with other regulators in discharging its functions.¹³

¹¹ The PSR's general functions are: (i) giving general directions; (ii) giving general guidance; and (iii) determining the general policy and principles by reference to which it performs particular functions.

¹² Banking Reform Act, s.49(3).

¹³ Under the Banking Reform Act, the PSR needs to have a Memorandum of Understanding (MoU) with the BoE, the FCA and PRA. The BoE, the PRA and FCA may also give direction to the PSR to refrain from a specified action (i.e. these regulators have veto rights under the Banking Reform Act). For example, some payment services 'institutions' are currently covered by the Payment Services Directive (PSD). The FCA is the competent authority for most aspects of the PSD. The UK implemented the PSD through the Payment Services Regulations 2009, which came into effect on 1 November 2009. Some firms may be subject to both the Payment Services Regulations and the new regulator.

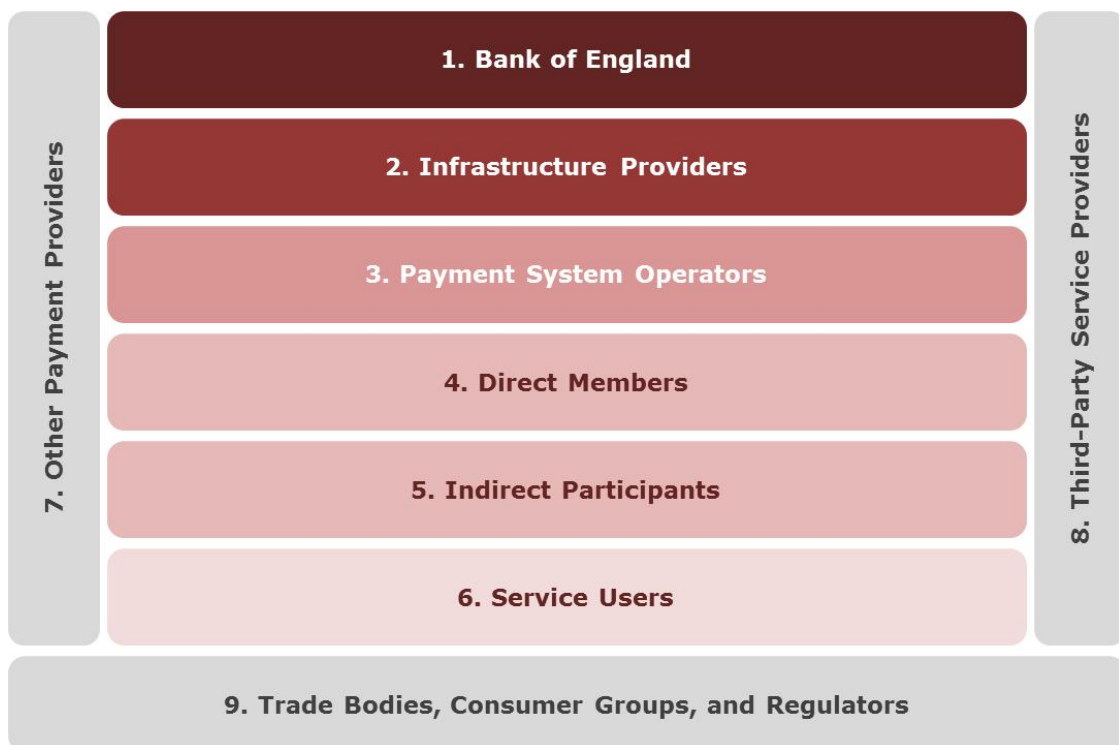
Who will the PSR affect?

The PSR's regulatory and competition functions will apply to 'participants' in regulated payment systems as defined in the Banking Reform Act¹⁴. These participants include:

- The payment system operators. This includes any entity with responsibility under the system for managing or operating it, such as the CHAPS Clearing Company.
- Infrastructure providers. This means any entity that provides or controls any part of the infrastructure used for operating the payment system. Vocalink is the main infrastructure provider for retail payment systems in the UK.
- Payment service providers. This is any entity which provides services to other stakeholders, who are not participants in payment systems, for enabling the transfer of funds using the payment system. For example, banks and building societies providing payment services to customers.

Including the abovementioned participants, the broader UK payments industry may include a number of other players.

Figure 1: UK payments Industry



¹⁴ Banking Reform Act, s.42.

1. The Bank of England facilitates settlement for the major UK payment systems.
2. Infrastructure providers (e.g. VocaLink, RTGS) control and operate the infrastructure over which the transfer of funds is executed for the purposes of operating the payment system.
3. Payment system operators are the schemes and networks (e.g. Bacs, Faster Payments (FPS), CHAPS, Link, the Cheque and Credit Clearing Company (C&CCC), and three and four party card schemes). For card schemes, the payment system operator and infrastructure provider may be same entity.
4. Direct members are payment service providers that have direct access to payment system operators, and can provide access to indirect participants. The major banks in the UK are direct members of most of the UK payment systems.
5. Indirect participants are payment service providers that access the payment system through agency agreements (i.e. via sponsorship) with a direct member. This may include, for example, smaller banks and new entrants.
6. Service-users are those who use, or are likely to use, services provided by payment systems to transmit funds. For example, businesses, consumers and government departments.
7. Other payment providers include non-banks and other service providers that use the payment systems to provide payment services to service-users. This could include overlay services, such as a mobile phone payment service that enables payments to be made with mobile phones over the Faster Payments Service.
8. Third-party service providers provide services across the value chain to facilitate the processing, acceptance, management and/or transmission of payments (e.g. technology providers, telecommunication providers, payment gateways/platforms, point of sale terminal providers, fraud management services).
9. Trade bodies, consumer groups and regulators represent the external stakeholders active within the payment industry (e.g. the Prudential Regulatory Authority, The European Commission, the Payments Council).

In referring to the payments industry in this document, we refer collectively to any, or all of, the stakeholders and participants within the UK payment systems.

3 The proposed approach

Purpose of this Call for Inputs

We welcome input that will assist the PSR to understand the current concerns of the UK payments industry, develop its regulatory approach and design, and identify early priorities for action. The PSR will consider all the evidence and information from respondents to inform and scope a number of policy workstreams. These will lead to formal consultations on the regulatory framework and content later this year. The PSR will provide the FCA with information relevant to its functions under a statutory gateway to be set out in secondary legislation under section 91 of the Banking Reform Act.

Responses do not need to be limited to the questions posed below. Please include any other comments about payment systems and the regulator's new remit. We encourage stakeholders and participants to be clear in their responses and to substantiate any concerns or views raised with supporting material where possible.

There will be further opportunities to engage with the regulator via stakeholder events over the coming months to provide any additional supporting evidence or supplementary information (see section 4 for details).

What we are trying to understand

Payment systems in the UK

In its 2013 consultation, HM Treasury indicated the schemes that it is likely to designate for regulation by the PSR as: CHAPS, Bacs, FPS, LINK, Cheque and Credit, and the main three and four party card schemes.¹⁵ We are particularly interested in your views and any concerns that you might have regarding these systems.

Smaller and less systemic payment systems or services, such as mobile payment systems and other proprietary payment card systems, may not initially be designated for regulation. However, the responses to HM Treasury's consultation paper noted the importance of setting a framework that takes into account the full payments industry.

¹⁵ HMT, *Opening up UK payments*, March 2013, p15, paragraph 4.3.

As new payment systems develop and grow, they may at a later stage be considered for inclusion in the new regulatory regime. We therefore also welcome views and concerns about these systems and players.

Question 1: Do you have any views on which payment systems should be considered for designation? If this includes parties other than the UK payment systems listed above, please explain why.

Competition in payment systems

To inform how the PSR will advance its competition objective, it will need to understand how competition currently operates within the UK payments industry, and those areas where there is potential for competition to drive greater benefits to service-users. The PSR will also need to consider the question of how access to payment systems affects competition, resilience and the reliability of payments systems in retail banking (this is considered separately below).

Competition is or could in theory be present between:

- Payment services offered over existing schemes (e.g. mobile payments).
- The schemes themselves, including payment card networks.
- Infrastructure providers.

The PSR will need to understand where competition works well and where it doesn't, and where there is the potential to enhance competition to drive benefits to service-users.

Question 2: Where do you believe competition is effective or ineffective within UK payment systems?

Question 3: At which level(s) is there potential for competition to drive benefits for service-users, in terms of costs, quality or innovation?

Question 4: What are the main factors impeding more effective competition at each level?

There is an inherent tension between collaboration and competition, and it will be important to strike a balance. The need for coordination and cooperation is a major feature in UK payment systems. For example, direct members provide wholesale functionality to indirect participants with whom they also compete at the retail level.

Where interdependencies exist, some innovations increase the need for cooperation among the stakeholders within the value chain.¹⁶

As indicated in the OFT's report, it may be that the scope of collaboration should be strictly limited to circumstances where the regulator is clear that such collaboration, rather than competitive market forces, would be the most efficient manner in which to deliver changes in the sector.

We would welcome any views on the need for, and function of, a collaborative structure in UK payment systems and how to overcome any shortcomings in the current arrangements.

Question 5: What functions do you think need to be performed collaboratively in the industry? How best can this be achieved?

Ownership

The ownership structures of UK payment systems have been identified as a potentially significant barrier to competition. Widespread networks of overlapping vertical relationships and common ownership within the payment systems can affect the incentives for participants to innovate and compete vigorously.¹⁷

The HM Treasury consultation in 2013 identified a number of issues related to current ownership structures.¹⁸ These include the reliance of smaller players and new entrants having to seek access to systems jointly owned by their most significant competitors, and the limited incentives to develop new or more efficient services to which the ownership structures give rise.

The PSR has the power to require the disposal of interests in UK payment systems, if it deems it necessary and appropriate, and with the consent of HM Treasury. The Parliamentary Commission on Banking Standards recommended that the Government reports on the merits of requiring the large banks to divest ownership of the payments systems. In response, the Government committed to asking the new regulator to consider the case for and against taking action to force divestments shortly after it takes on its responsibilities.¹⁹

¹⁶ HMT, *Opening up UK payments: response to consultation*, October 2013, p13, paragraph 2.68.

¹⁷ OFT, *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*, July 2013, p7, paragraph 1.15-1.16.

¹⁸ HMT, *Opening up UK payments*, March 2013, p19, paragraph 4.24-4.26.

¹⁹ HMT, *The Government's response to the Parliamentary Commission on Banking Standards*, Page 6, paragraph 1.6 & p31, paragraph 4.9.

We are interested in views on the current ownership structure, as well as any proposals for alternate ownership structures.

Question 6: Do you think the current ownership structure creates problems? If so, please explain your concerns with the current structure.

Question 7: How might the regulator address any issues with the current ownership structure? Please explain how any remedy, including any alternate model, might address any or all of the issues you have identified and also highlight any potential concerns associated with such alternate ownership models.

Governance

Concerns have also been expressed regarding the governance arrangements of UK payment systems and infrastructure providers.²⁰ Smaller payment service providers may have minimal power or ability to influence the decisions of the governing boards of payment systems, including decisions in relation to access and setting strategy. For example, the OFT notes that payment systems need to adequately address the needs of minority stakeholders, smaller payment service providers and service-users, and that their concerns and views need to be taken into account in formulating the strategy and investment plans of UK payment systems.²¹

Question 8: Do you have any concerns about the current governance of UK payment systems?

Question 9: What do you believe is the appropriate governance structure for UK payment systems?

Access

A payment services provider can access a payment system either directly, i.e. by being a direct member of the payment system, or indirectly, through an agency agreement with a direct member of the payment system.

A participant that wants to become a direct member needs to meet certain criteria set by the payment system owners (i.e. the other direct members) to get access to the

²⁰ HMT, *Opening up UK payments*, March 2013, p7, paragraph 3.2.

²¹ OFT, *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*, July 2013, p17, paragraph 2.17.

system. This includes becoming a settlement bank with the Bank of England and meeting the technical and operational requirements set by the direct member banks and payment system operators. In practice, banks need to reach sufficient economies of scale and scope, invest substantial initial capital in their own infrastructure, and meet several requirements to become direct members.

A participant wanting indirect access to a payment system will need an agency agreement with a direct member bank or sponsoring bank. The access terms and conditions (including fees) are bilaterally negotiated between sponsoring banks and the indirect payment service providers. The OFT found that indirect participants have limited choice and bargaining power in negotiating the terms of access with direct members.²² There is also concern that lack of transparency and comparability in bilateral agency agreements may make it difficult for indirect participants to evaluate and change their arrangements.

We are interested in your views on the process of obtaining direct or indirect access to UK payment systems, and whether the current terms and conditions for gaining access are fair and reasonable.

Question 10: How do you access UK payment systems? Please provide details (e.g. direct or indirect, the conditions, fees and requirements for access etc.) for each payment system you have access to and any concerns you may have with your current arrangements. If you do not currently have access to UK payment systems, please provide details on how you participate within the UK payment industry, and detail any concerns or constraints you may have in this regard.

Question 11: For the access you described above (in question 10), are the access terms and conditions (including fees) fair and reasonable? If not, please provide details.

Question 12: Does the access arrangement you currently have limit your ability to compete or impact on the service-users' experience in any way?

Question 13: If you access payment systems indirectly through a sponsoring agreement with a direct member bank, do you have sufficient choice in sponsoring banks? Would you prefer to access payment systems directly? What do you see as the benefits and risks of doing so?

²² OFT, *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*, July 2013, p35, paragraph 5.11.

Question 14: Do you act as a sponsoring bank, providing indirect access to any payment system participant in the UK (please provide details for each payment system you provide access to)? If yes:

- To whom do you provide indirect access?
- What are the major risks and costs associated with providing such indirect access? On what basis do you choose whether to provide indirect access?
- Are there any barriers to becoming a sponsoring bank?

Question 15: What changes to access rules and conditions would you like to see? Are there any alternative routes to gain access to payment systems that you believe should be developed (e.g. a second tier membership to payment system operators)?

Question 16: Do you have any other comments regarding access?

Infrastructure

The technical requirements to gain access to payment systems in UK payment systems can be complex. The investments required to make (or 'effect') payment services through the central infrastructure and decentralised banking platforms at individual participants may act as a barrier to entry, innovation and change.

Question 17: What improvements or changes do you believe are required in the provision and use of infrastructure in the UK? We would also be interested in your views on the cost of such changes, for you or for the industry as a whole. What considerations, if any, need to be considered regarding the impact of any changes or improvements on the resilience and reliability of payments systems?

Question 18: What changes, if any, are needed regarding messaging standards in the UK? For example, would the adoption of ISO20022 standards alleviate any concerns or improve any constraints you experience? What timeframe and considerations would need to be taken into account in adopting new standards?

Question 19: What solutions can be developed to increase competition in the provision of infrastructure and/or managed services to support the technical and operational functions of agency banks participating in UK payment systems? How can this be achieved, and what will the impact and benefits of this be to your business?

Innovation

As discussed, changes to payment systems often require cooperation amongst the various stakeholders, which can slow the pace of innovation.

The OFT's recent report on competition and innovation suggests that the development of UK payment systems is slow, and that one of the primary reasons appears to be that banks do not have significant incentives to drive innovation.²³ As currently operated, many schemes (with the exception of the major card networks) appear to be cost centres rather than profit centres for the direct member banks.²⁴ With payments generating little or no revenue, it is unclear whether, or how, participants in payment systems will recoup the cost of investments.

Both HM Treasury's consultation and the OFT's report also suggest that, given the collective nature of innovation and common ownership of payment systems, the end result may be a general underinvestment in payments systems as banks may be less likely to invest in innovation that benefits their rivals, this would provide no competitive advantage.²⁵ The required collaboration can also impact on the pace of innovation, given that changes are affected at the pace of the slowest participant.

The PSR's innovation objective is to promote the development of, and innovation in, payment systems with a view to improving the quality, efficiency, and economy of systems in the interest of service-users. Given the breadth of stakeholders and the range of views on innovation in payment systems, we would welcome any views on the complexities, incentives and barriers to innovating in UK payment systems.

Question 20: Are incentives to innovate clear under current arrangements? Please also include any concerns you may have regarding fee arrangements and the impact of changing fee structures (such as changes to interchange fees).

Question 21: Do any factors limit your ability or incentives, either collectively or unilaterally, to innovate within UK payment systems?

Question 22: What changes, if any, are needed to facilitate a greater pace of innovation in UK banking and payments? Please refer to your previous answers where relevant.

²³ OFT, *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*, July 2013, p45, paragraph 6.26.

²⁴ OFT, May 2003, *An OFT market study of clearing systems and review of plastic card networks*.

²⁵ OFT, *UK Payment systems – How regulation of UK payments systems could enhance competition and innovation*, July 2013, p35, paragraph 5.11.

Question 23: What do you believe are the benefits and limitations of collectively driven innovation vs. unilateral innovation?

Closing questions

We would welcome any views from stakeholders and participants on the following questions:

Question 24: Do you have any other comments or concerns you would like to highlight?

Question 25: What, if any, are the significant benefits you see regulation bringing?

Question 26: What, if any, are the risks arising from regulation of payment systems?

Question 27: How do you think regulation might affect your business and your participation in UK payment systems?

4 Next steps

What do you need to do next?

We encourage stakeholders and participants to familiarise themselves with the deadlines and processes, as set out in Annex 2, in order to submit a response to this Call for Inputs. You also need to complete the Cover Sheet in Annex 1 to accompany your submission.

What will happen to your feedback?

The PSR will consider all the evidence and information from the respondents to inform formal consultations on the regulatory framework later this year. The PSR will also provide the FCA with information relevant to its functions under a statutory gateway to be set out in secondary legislation under section 91 of the Banking Reform Act.

An indicative timeline, setting out the key milestones and further opportunities to engage with the regulator, is presented below.

Table 1: Key Milestones

Date	Description
March 2014	<ul style="list-style-type: none"> FCA publishes <i>Call for Inputs</i> to gather views and information, start stakeholder engagement and set out timelines and milestones.
April 2014	<ul style="list-style-type: none"> Incorporation of the PSR. Appointment of the PSR Board. PSR receives responses from the Call for Inputs.
May 2014 – September 2014	<ul style="list-style-type: none"> The PSR works up proposals on the regulatory approach, fees, rulebook, priorities and other issues that are identified from the Call for Inputs

	<p>responses.</p> <ul style="list-style-type: none"> The PSR will finalise the outstanding legislative governance requirements (e.g. Memorandums of Understanding, establishing Panels, draft annual plan etc.).
September - October 2014	<ul style="list-style-type: none"> The PSR publishes formal consultations on the regulatory approach, fees, rulebook, etc.
December 2014 - February 2015	<ul style="list-style-type: none"> PSR statements published following formal consultations.
April 2015	<ul style="list-style-type: none"> Relevant payment systems are designated by HM Treasury. The PSR becomes fully operational and its concurrent competition powers commence.

We anticipate that the PSR will engage in a series of workshops, roundtables or presentations to collect further evidence and views from the key stakeholders and participants before setting out our formal views in consultation papers later this year. The PSR may also issue formal requests for information using its information gathering powers.

Separately, it is expected that the HM Treasury will consult on the designation of payment systems before the PSR becomes fully operational in April 2015.

Annex 1: Cover sheet

Basic information	
Consultation title:	
Name of respondent:	
Contact at respondent:	Name:
	Email:
	Address:

Nature of organisation (select as appropriate)	
Infrastructure provider (e.g. Vocalink)	
Payment system operator	
Direct member of payment system(s)	
Indirect participant in payment system(s)	
Service-user	
Other payment provider (e.g. ZAPP)	
Third-party service provider (e.g. ATM distribution)	
Trade / Government / Regulatory body	
Other Please specify:	

Confidentiality	Yes	No
Do you wish any part of your response to remain confidential?		
If 'Yes', please submit both confidential and non-confidential responses.		

Annex 2: Responding to this Call for Input

When to send your response

We are requesting that responses to this paper should be sent to the PSR. The FCA is publishing the paper now to enable interested parties to submit relevant information to the PSR following its incorporation at the earliest possible opportunity.

We invite all stakeholders and participants in UK payment systems to provide written views and comments on the issues raised in this document, **to the PSR by 5pm on 15 April 2014**.

Together with your response, please also complete the Cover Sheet (see Annex 1).

How to submit your response

Please email the cover sheet (Annex 1) and your **response** to **paymentsystems@fca.org.uk**, by attaching your response document and any supporting material you would like the new regulator to consider. Additional hard copies are not required if you send a response by email.

Alternatively responses can be posted to:

25 The North Colonnade
Canary Wharf
London
E14 5HS

The PSR will make all responses to formal consultation available for public inspection unless the respondent requests otherwise (please complete Annex 1). A standard confidentiality statement in an email message will not be regarded as a request for non-disclosure.

Despite this, the PSR may be asked to disclose a confidential response under the Freedom of Information Act 2000 (FOIA). You may be consulted if such a request is received. The PSR will be subject to a statutory confidentiality regime (under section 91 of the Banking Reform Act) from the date it is incorporated²⁶ and will therefore be entitled to rely on the exemption in section 44 of FOIA where the information provided is confidential information for the purposes of that section **from that date**. Any

²⁶ It is expected that the PSR will be incorporated early April 2014.

decision not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

It is anticipated that the PSR will pass confidential information to the FCA under a statutory gateway to be set out in secondary legislation under BRA section 91.

Annex 3: Questions

Question 1: Do you have any views on which payment systems should be considered for designation? If this includes parties other than the UK payment systems listed above, please explain why.

Question 2: Where do you believe competition is effective or ineffective within UK payment systems?

Question 3: At which level(s) is there potential for competition to drive benefits for service-users, in terms of costs, quality or innovation?

Question 4: What are the main factors impeding more effective competition at each level?

Question 5: What functions do you think need to be performed collaboratively in the industry? How best can this be achieved?

Question 6: Do you think the current ownership structure creates problems? If so, please explain your concerns with the current structure.

Question 7: How might the regulator address any issues with the current ownership structure? Please explain how any remedy, including any alternate model, might address any or all of the issues you have identified and also highlight any potential concerns associated with such alternate ownership

Question 8: Do you have any concerns about the current governance of UK payment systems?

Question 9: What do you believe is the appropriate governance structure for UK payment systems?

Question 10: How do you access UK payment systems? Please provide details (e.g. direct or indirect, the conditions, fees and requirements for access etc.) for each payment system you have access to and any concerns you may have with your current arrangements. If you do not currently have access to UK payment systems, please provide details on how you participate within the UK payment industry, and detail any concerns or constraints you may have in this regard.

Question 11: For the access you described above (in question 10), are the access terms and conditions (including fees) fair and reasonable? If not, please provide details.

Question 12: Does the access arrangement you currently have limit your ability to compete or impact on the service-users' experience in any way?

Question 13: If you access payment systems indirectly through a sponsoring agreement with a direct member bank, do you have sufficient choice in sponsoring banks? Would you prefer to access payment systems directly? What do you see as the benefits and risks of doing so?

Question 14: Do you act as a sponsoring bank, providing indirect access to any payment system participant in the UK (please provide details for each payment system you provide access to)? If yes:

- To whom do you provide indirect access?
- What are the major risks and costs associated with providing such indirect access? On what basis do you choose whether to provide indirect access?
- Are there any barriers to becoming a sponsoring bank?

Question 15: What changes to access rules and conditions would you like to see? Are there any alternative routes to gain access to payment systems that you believe should be developed (e.g. a second tier membership to payment system operators)?

Question 16: Do you have any other comments regarding access?

Question 17: What improvements or changes do you believe are required in the provision and use of infrastructure in the UK? We would also be interested in your views on the cost of such changes, for you or for the industry as a whole. What considerations, if any, need to be considered regarding the impact of any changes or improvements on the resilience and reliability of payments systems?

Question 18: What changes, if any, are needed regarding messaging standards in the UK? For example, would the adoption of ISO20022 standards alleviate any concerns or improve any constraints you experience? What timeframe and considerations would need to be taken into account in adopting new standards?

Question 19: What solutions can be developed to increase competition in the provision of infrastructure and/or managed services to support the technical and operational functions of agency banks participating in UK payment systems? How can this be achieved, and what will the impact and benefits of this be to your business?

Question 20: Are incentives to innovate clear under current arrangements? Please also include any concerns you may have regarding fee arrangements and the impact of changing fee structures (such as changes to interchange fees).

Question 21: Do any factors limit your ability or incentives, either collectively or unilaterally, to innovate within UK payment systems?

Question 22: What changes, if any, are needed to facilitate a greater pace of innovation in UK banking and payments? Please refer to your previous answers where relevant.

Question 23: What do you believe are the benefits and limitations of collectively driven innovation vs. unilateral innovation?

Question 24: Do you have any other comments or concerns you would like to highlight?

Question 25: What, if any, are the significant benefits you see regulation bringing?

Question 26: What, if any, are the risks arising from regulation of payment systems?

Question 27: How do you think regulation might affect your business and your participation in UK payment systems?

Annex 4: Glossary of terms

Term	Description
Agency agreement	An agreement whereby 'indirect payment service providers' obtain access to payment systems through a 'sponsoring bank'.
Agency bank	A credit institution that is an indirect payment service provider (see definition of 'Indirect payment service provider').
Collective innovation	Innovation delivered collectively through more than one payment system participant or stakeholder. This delivers benefits to all participants in a particular payment system or the payments industry as a whole.
Direct member bank	A payment services provider that accesses the payment systems directly through membership of a Payment System Operator (without sponsorship or agency agreement with other bank / payment services provider).
Indirect payment service provider	A payment services provider that accesses the payment system through an agency agreement (i.e., sponsorship) with a direct member.
Infrastructure provider	Any entity that provides or controls any part of the infrastructure used for operating the payment system.
Interchange fees	A transaction fee payable in the context of a payment card network by one participating financial institution to another, ²⁷ for example fees charged by a cardholder's bank (the 'issuing bank') to a merchant's bank (the 'acquiring bank') for each sales transaction made at a merchant outlet with a payment card. ²⁸
Other payment service providers	Includes non-banks and other service providers that use the payment systems to provide payment services to consumers or service-users. This could include overlay services, such as a mobile phone payment service that enables payments to be made with mobile phones over the Faster Payments Service.

²⁷ Bank of International Settlements, *A glossary of terms used in payments and settlement systems*, March 2003, available at: <https://www.bis.org/publ/cpss00b.pdf>

²⁸ European Commission, http://ec.europa.eu/competition/sectors/financial_services/enforcement_en.html

Participants in UK payment systems	Participants within designated payment systems will include all payment system operators, payment service providers and infrastructure providers.
Payment processing	The transmission of information to affect the transfer of funds within a payment system.
Payment service provider	A entity that provides payment services to other entities in a payment system to enable the transfer of funds (e.g., bank providing payment services for customer).
Payment services	Any service provided by any stakeholder within the UK payments industry that enables the transfer of funds.
Payment system	A system operated by one or more entities to enable the transfer of funds.
Payment system operator	An entity responsible for managing and operating a payment system (e.g. payment scheme).
Payments industry	A representation of all the broad range of relevant stakeholders that participate in the UK payments systems.
Service-user	Those who use, or are likely to use, services provided by payment systems.
Sponsoring bank	A credit institution that is a 'direct payment service provider' that provides access to other payment service providers within payment systems.
Third-party service providers	Third-party service providers provide services across the value chain to facilitate the processing, acceptance, management and/or transmission of payments (e.g. technology providers, telecommunication providers, payment gateways/platforms, point of sale terminal providers, fraud management services).
Unilateral innovation	Innovation by a single payment service provider or stakeholder that differentiates their payment service offering to service-users.