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Consultation Response

The Payment Systems Regulator's consultation on *Our proposed PSR Strategy (CP21/7)*

Summary

- Which? welcomes the Payment Systems Regulator's proposed five-year strategy, which comes at a critical juncture for UK payments markets.

- We agree with the regulator's assessment that payments do not currently work well for everyone, and that more needs to be done to tackle the issues in payments markets.

- It is therefore crucial that the Payment Systems Regulator acts to urgently address key gaps in consumer protections and threats to access, whilst establishing a longer-term course of action for how it will ensure that payment systems work for all consumers.

- Which? broadly supports the four strategic outcomes that the Payment Systems Regulator has identified, and the four strategic priorities required to meet these aims (see Appendix 1 & 2 for outcomes and priorities).

- However, we raise the following concerns:

    - **Given the need for immediate action from the Payment Systems Regulator, we believe that the proposed measures would be better framed as specific, measurable objectives with clear timeframes for action.** There is an evident need for pace on pressing issues in the payments market, hence why the regulator's final strategy should detail how and when it plans to act.

    - To deliver on its strategy, **the Payment Systems Regulator must be willing, in practise, to intervene in areas of the payments market where competition between payment systems is insufficient in creating good outcomes for consumers (Priority 3).** This would require a significant shift in culture and approach taken by the regulator - changes which have not been clearly set out in the proposed strategy.

    - In particular, there are weak incentives for firms to compete on the basis of what consumer protections they offer, as many initiatives to strengthen protections require collaboration between firms. **Hence, it is vital that the Payment Systems Regulator acts to ensure that there are industry-wide levels of minimum protections for consumers (Priorities 2 & 4).** This is important given the recent challenges that have stemmed from voluntary initiatives for consumer protection, most notably in relation to authorised push payment (APP) fraud.

- **The Payment Systems Regulator should prioritise working with the Financial Conduct Authority (FCA) to protect access to existing payment systems that millions of UK consumers continue to rely on (Priority 1).** As well as supervising the uptake of new and alternative payment methods, consideration should be given to coordinating regulatory responsibilities and actions to maintain free access to cash, bank branches, and free-to-use ATMs in order to prevent further exclusion.

The proposed measures for action would be better framed as specific, measurable objectives with clear timeframes

The Payment Systems Regulator recognises issues in the payments market that require immediate attention. For example, the strategy underscores the need for action in mitigating the devastating harms of APP fraud; an area of concern where the shortfalls of existing consumer protections are apparent. But, despite the need for pace on many issues, there is an absence of time-bound objectives in the strategy, and detail on how the regulator plans to measure the success of its work. The inclusion of specific and high-level outcomes, targets, and timescales in regulatory initiatives is now a standard that is expected of regulators. The FCA is particularly effective at incorporating these measures into its strategies and consultations.[1]

The final strategy should outline clear timeframes for when the regulator plans to act, and specific deadlines for when it could expect such issues to be resolved. It should detail the areas of concern that will require urgent action in the short term, and those which may require sustained, long-term work, allowing for the better allocation of time and resources. Moreover, it should include ambitious yet achievable targets, such as what reduction in harm it aims to achieve in the next five years. By incorporating these details into its strategy, the Payment Systems Regulator could have greater impact and be more easily held to account in its role in mitigating risk and harms in the payments market.

The Payment Systems Regulator must be willing, in practise, to intervene in areas of the payments market where competition between payment systems is insufficient in creating good outcomes for consumers (Priority 3, see Appendix 2)

[1] For examples of this, see FCA (2021) Business Plan 2021/22, available at: https://www.fca.org.uk/publication/business-plans/business-plan-2021-22.pdf, and FCA (2021) Consumer Investments: Strategy and Feedback Statement, available at: https://www.fca.org.uk/publications/corporate-documents/consumer-investments-strategy.

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Competition is core to the Payment Systems Regulator's purpose: one of its three statutory objectives is to promote effective competition in the markets for payment systems and services.[2] The regulator's intent towards this translates into its strategy, where it proposes to focus on delivering improved outcomes for consumers through supporting competition between payment schemes and payment providers.[3]

Competition in the retail payments sector, in particular, has the potential to lead to better outcomes for consumers. Competition between firms in the uptake of interbank retail payments could increase affordability and access for consumers, whilst contending for the varied interests of consumer groups could promote innovation and inclusivity in the design of payment systems.

Which? agrees with the Payment Systems Regulator's assessment that, as it stands, competition in the retail payments market - especially between card-based and interbank methods of payment - is insufficient in meeting the regulator's statutory objective of ensuring that payment systems "are operated and developed in a way that considers and promotes the interests of all the businesses and consumers that use them."[4] Despite significant developments in the payment methods offered to consumers in recent years, card-based transactions continue to prevail, albeit at a lower rate: UK Finance's 2021 Payments Market Summary shows that 52% of all payments last year were made using credit and debit cards.[5] Debit cards remained the most frequently used payment method in the UK, used in over 4 in 10 payments and held by 98% of the surveyed population.[6]

In contrast, the uptake of retail interbank payments in the UK remains low.[7] In 2020, over 12.8 billion more payments were made using debit cards than Faster Payments methods.[8] Future growth is expected however, with significant uptake already being seen in Faster Payments since the pandemic: Pay.UK's Quarterly Statistical report saw a 15% increase in the number, and total value, of payments made in Q1 2021 compared to Q1 2020.[9]

This highlights that competitive forces within the retail payments market are often insufficient to ensure good outcomes and robust protections for consumers. Where competition lacks, the regulator states that it will act to protect users when necessary, "setting expectations, and collaborating with the industry and users, or using our formal powers to secure change," but

[2] Payment Systems Regulator (2021) The PSR Purpose. Available at: https://www.psr.org.uk/about-us/the-psr-purpose/
[3] Payment Systems Regulator (2021) Our proposed strategy, p.21.
[4] Payment Systems Regulator (2021) The PSR Purpose. Available at: https://www.psr.org.uk/about-us/the-psr-purpose/
[5] UK Finance (2021) UK Payments Market Summary 2021, pp.1-2.
[6] Ibid, pp.1-2.
[7] Payment Systems Regulator (2021) Our proposed strategy, p,45
[8] 15.8 billion payments were made using debit cards, and just under 3 billion were made using Faster Payments methods, UK Finance (2021) UK Payments Market Summary 2021, pp.8.
[9] Pay.UK (2021) Quarterly Statistical Report, p.4. Available at: https://newseventsinsights.wearepay.uk/media/drafcd12/pay-uk-quarterly-payment-statistics-q1-2021.pdf.

fails to articulate in its strategy how it plans to deliver the shift in culture and approach required for such action.[10] So, it is crucial that the regulator demonstrates its willingness and commitment to intervene in the payments market to address the concerns it identifies in practise.

The extent to which the Payment Systems Regulator is able to intervene is dependent on the remit and scope of powers designated to it by HM Treasury. Therefore, the regulator needs to make clear in its final strategy that it is planning to do all it can in the next five years to ensure that it has sufficient regulatory powers to address current and emerging issues, and is willing to make efficient use of its existing and future powers. It should be publicly stating the powers it requires from HM Treasury to provide a strong framework of protections and mitigate harms for consumers, and should be making the case for the Government to remove any unnecessary barriers for appropriate intervention.

In this respect, the Payment Systems Regulator should follow the example of other regulators, particularly the Competition and Markets Authority (CMA), which explicitly and publicly sets out what powers it needs from the Government to tackle issues in the short and long term.[11] For instance, in response to the pandemic, the CMA publicly made the case for more emergency powers to take immediate enforcement action against exploitative 'price gouging' practises, as it believed it lacked the right set of tools to tackle the issue in this context.[12]

In sum, the regulator must clarify that it is willing and able to intervene in the payments market to deliver on its strategic objectives. It should show consideration towards what powers it would require from the Government, how it plans to gain them, and where its existing and future powers would be used in practise.

It is vital that the Payment Systems Regulator acts to ensure that there are industry-wide levels of minimum protections for consumers (Priorities 2 & 4, see Appendix 2)

Which? strongly supports the Payment Systems Regulator's proposed priority on consumer protections. Given the lack of incentives for payment providers and systems to compete on consumer protections, and the historical weaknesses of protections in the interbank system in managing risk and harm - as the regulator notes in its strategy - it is crucial that the Payment Systems Regulator takes immediate action to institute minimum levels of protections for consumers across the payments market, enabling users to confidently engage with payment methods. In particular, we continue to see the devastating effects of APP fraud; an area where the existing framework of protections has been limited in mitigating consumer harms.

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[10] Payment Systems Regulator (2021) Our proposed strategy, p.21.
[11] Which? (2020) UK lagging behind on laws to protect against price gouging. Available at: https://www.which.co.uk/news/2020/06/uk-lagging-behind-on-laws-to-protect-against-price-gouging/
[12] Osbourne Clark (2020) CMA seeks emergency powers to fight coronavirus 'price gouging.' Available at: https://www.osborneclarke.com/insights/cma-seeks-emergency-powers-fight-coronavirus-price-gouging/

It has been five years this month since Which? made its super-complaint to the Payment Systems Regulator, calling attention to the striking gap in fraud protections and redress for fraud via authorised push payments, compared to other forms of payment such as card-based methods. The regulator has since intervened by establishing the voluntary Contingency Reimbursement Model (CRM), designed to give victims of signatory firms fair and consistent redress, and mandating the 6 largest banking groups to sign up to the Confirmation of Payee Scheme, after banks and other payment providers failed to adopt the scheme on their own accord.

Yet, the partial and inconsistent implementation of these protections has meant that they have not been sufficient. We have seen the number of reported cases of APP fraud, and the level of financial loss, more than treble in the past five years.[13] Better reporting may have contributed to some extent to these increases, but there is no doubt that the threat of fraud is becoming part of our everyday lives. Our research shows that victims continue to be subjected to the devastating financial and emotional impacts of payment fraud, and although reimbursement rates have increased by signatory firms, levels remain shockingly low, to the extent that the Payment Systems Regulator itself has expressed that the CRM Code has not yet led to the significant reduction in APP scam losses incurred by victims that is needed.[14] It estimates that the overall level of reimbursement and repatriation is less than 50% of APP losses assessed under the CRM Code, meaning "customers are still bearing a high proportion of losses."[15]

Furthermore, the partial implementation of Confirmation of Payee by banks and other payment providers considerably undermines the scheme's potential benefits in helping to detect and prevent APP fraud. Which? has long called for the widespread adoption of the service by the payments industry, and whilst we have seen a small number of firms voluntarily introduce the service, the vast majority of firms using Faster Payments have not yet introduced Confirmation of Payee, and show little commitment in doing so. Consequently, the PSR's findings show starkly that fraudsters are exploiting this lack of coverage, harnessing accounts without the name-checking service in order to facilitate fraud, further undermining the potential benefits of the scheme.

In its Call for Views on APP scams, the Payment Systems Regulator proposed a measure to require Faster Payments to incorporate a reimbursement obligation into its scheme rules (Measure 3a), which Which? strongly supports instead of the regulator's alternative proposal for an updated Code that it would approve.[16] However, the regulator expressed that it faces restrictions on its ability to require payment providers to reimburse APP scam victims, and that

[13] Between 2017 and 2021, the number of reported cases and the level of losses both more than tripled: there were 143,259 cases involving customers with personal bank accounts in 2021, up from 38,596 in 2017. Fraudsters stole £388 million in 2021, compared to £108 million in 2017.
[14] See this for more detail on the emotional impacts of fraud: https://www.which.co.uk/news/2021/03/devastating-emotional-impact-of-online-scams-must-force-government-action/
[15] Payment Systems Regulator (2021) Authorised push payment (APP) scams Call for views, p.4.
[16] Ibid, p.29.

it was unable to act until the Government legislated to remove these barriers.[17] For this to happen, we emphasise our previous point on intervention. The Payment Systems Regulator must now be proactive in pushing the Government publicly for the necessary powers it requires to institute reimbursement obligations for Faster Payments. Further to this, it must push to ensure that there is a robust system of enforcement and supervision of firms.

Which? is pleased to see that the Payment Systems Regulator's proposed strategy prioritises consumer protections in the interbank payments sector for retail payments. The regulator should work to ensure that users are able to rely on a robust framework of consumer protections when using new and alternative payment methods, and have confidence in their ability to seek advice and redress if something goes wrong. This could, in turn, help foster trust in the use of payment methods such as Open Banking and Faster Payments, furthering the Payment Systems Regulator's competition objective.

The proposed strategy highlights the regulator's view to give Pay.UK a stronger role in the development of consumer protections. Whilst Which? welcomes the strengthening of protections in the interbank payments sector, we urge the regulator to consider whether delegating responsibility to Pay.UK would ultimately work in the interests of consumers.

Pay.UK would need to significantly develop its governance of interbank payments. Its Faster Payments scheme currently lacks rules or policies related to consumer protections against fraud or error, undermining consumer confidence. Other payment schemes, most notably card-based payment methods, have rules that protect consumers against fraudulent payments, such as Section 75 of the Consumer Credit Act, and the Direct Debit Guarantee. Hence, the Payment Systems Regulator must work with Pay.UK to introduce a new Faster Payments Guarantee into its scheme to protect consumers if issues arise in interbank retail payments. If implemented and enforced correctly, a Guarantee, which would include the institution of a mandatory reimbursement obligation for victims of APP fraud, as proposed in Measure 3a, has the potential to provide consumers with a reliable and robust framework of minimum protections in the retail payments market.

The Payment Systems Regulator should prioritise working with the Financial Conduct Authority (FCA) to protect access to existing payment systems that millions of UK consumers continue to rely on (Priority 1, see Appendix 2)

The Payment Systems Regulator's proposed strategy highlights that some groups of consumers do not have access to the payment methods that meet their needs. Cash, despite being in decline, continues to be an important payment method for people in day-to-day life: it was used for just under a fifth of all UK payments made last year, and was the second most frequently used payment method, behind debit cards.[18] Moreover, for many vulnerable people in the UK,

[17] Ibid, p.29.
[18] UK Finance (2021) UK Payments Market Summary 2021, pp.1-2.

cash remains a necessity. The Access to Cash Review found that over 8 million adults would struggle to cope in a cashless society, and Age UK recently reported that one in five older people rely on cash for everyday spending, highlighting the risks of reduced access in exacerbating social exclusion.[19] Which? strongly support the Payment Systems Regulator's view to protect the interests of these consumers in payments; our longstanding Freedom to Pay campaign has called for stronger protections in the provision of cash for consumers, communities, and small businesses.

A focal point of the proposed priority is monitoring the uptake of existing alternative payment options for groups who currently rely on cash. Whilst Which? agrees that encouraging the transition to alternative payments is important, especially given the recent transformations in the payments sector and potential benefits of digital inclusion, the Payment Systems Regulator should also prioritise the coordination of regulatory responsibilities and actions to maintain free access to cash, bank branches, and free-to-use ATMs. It must act alongside the FCA to make this a strategic concern to prevent further exclusion for groups reliant on cash payments.

Which? would like to see the regulator continue measures to support the transition to alternative payment methods. We welcome the Payment Systems Regulator's launch of a Digital Payments Initiative, which seeks to understand the potential barriers and challenges for users in the take-up of digital payments, and formulate potential solutions.[20] Such findings could be used by the regulator as a springboard for collaborative action with the Government and third-sector, encouraging the creation of digital skills initiatives to increase engagement and confidence in interbank retail payments.

[19] Access to Cash (2019) Access to Cash Review - Final Report, pp.6, Age.UK (2021) One in five older people rely on cash for everyday spending. Available at: https://www.ageuk.org.uk/latest-press/articles/2021/one-in-five-older-people-rely-on-cash-for-everyday-spending/

[20] PSR (2021) The PSR and the PSR Panel Launches Digital Payments Initiative: Realising the Benefits of Digital Payments. Available at: https://www.psr.org.uk/news-updates/latest-news/news/the-psr-and-the-psr-panel-launches-digital-payments-initiative-realising-the-benefits-of-digital-payments/

About Which?

Which? is the UK's consumer champion. As an organisation we're not for profit - a powerful force for good, here to make life simpler, fairer and safer for everyone. We're the independent consumer voice that provides impartial advice, investigates, holds businesses to account and works with policymakers to make change happen. We fund our work mainly through member subscriptions, we're not influenced by third parties and we buy all the products that we test.

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Appendix 1: The Payment Systems Regulator's four strategic outcomes, as proposed in its five-year strategy

Outcome 1: All users have access to payment services that meet their needs in terms of functions, quality, cost and other relevant factors.

Outcome 2: Users' interests are adequately protected when using payment services so that they can use systems and services with confidence.

Outcome 3: Payment systems are designed and operated to enable effective competition in the provision of payment services.

Outcome 4: Payment systems are efficient and commercially sustainable.

Appendix 2: The Payment Systems Regulator's four strategic priorities, as proposed in its five-year strategy

Priority 1: Ensure users have continued access to the payment services they rely upon, and support an effective choice of alternative payment options.

Priority 2: Ensure users are sufficiently protected when using the UK's payment systems, now and in the future.

Priority 3: Promote competition in markets and protect users where that competition is not sufficient, including a) between payment systems within the UK and b) in the markets supported by them.

Priority 4: Ensure the renewal and future governance of the UK's interbank payment systems supports innovation and competition in payments.