

Delivery and regulation of the New Payments Architecture

Payment Systems Regulator Consultation (CP21/2)

March 2021

Response from the Emerging Payments Association

Abstract

This paper sets out the Emerging Payment Association's (EPA) response to the first six questions Payment Systems Regulator's (PSR) consultation on the delivery and regulation of the New Payments Architecture (NPA). These six questions focus on the risks to the delivery of the NPA and the options for reducing these risks by changing the scope of and approach to the initial procurement. The EPA plan to submit a further response providing views on the PSR's proposals for mitigating competition risks including the pricing principles by the 5 May 2021 deadline.

March 2021

Introduction

The Emerging Payments Association (EPA) welcomes the opportunity to contribute to the Payment System Regulator's consultation on '*Delivery and regulation of the New Payments Architecture*'. The community's response contained in this paper reflects views expressed by our members and industry experts recommended by them. As the EPA's membership includes a wide range of companies from across the payments value chain, and diverse viewpoints across all job roles, this response cannot and does not claim to represent the views of all members fully.

We are grateful to the EPA's members and the experts they have recommended to us, who have contributed to this response which has been drafted by Mike Chambers, one of the EPA's long-serving ambassadors. We hope it advances our collective efforts to ensure the UK's payments industry continues to be progressive, world-leading and secure, and effective at serving the needs of everyone who pays and gets paid.

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Questions related to the risks to NPA delivery

1) Do you agree with our view of the risks to the successful delivery of the NPA?

The EPA broadly agrees with the PSR's view that option 1 presents unacceptably high risks. We also agree that the current delays are preventing the delivery of end user innovation and that the migration risk is a material concern.

Whilst it could be argued that the COVID pandemic has introduced an additional delivery risk, we are of the view that the validity of this risk as a determining factor in deciding the way forward for the NPA has passed.

The passage of time and the various programme resets have clearly had a profound impact on the delivery of the NPA and without clear, decisive and remedial action, the future delivery and success of the NPA cannot be assured.

The independent assurance review in Spring 2019 commissioned by Pay.UK noted the absence of strong foundations and recommended a programme reset. Whilst it is apparent that the programme reset adopted by Pay.UK and the intervention by the PSR is seeking to ameliorate the identified risks, we are principally concerned that the role of bulk submissions (especially Bacs Direct Debit) have not been thoroughly explored or validated with stakeholders. On this basis we believe that Option 1 has the additional risk of a vendor being selected and a solution being procured before the full scope of the NPA has been appropriately explored with stakeholders.

A clear tenet of the NPA programme is to deliver increased innovation and competition (both ‘in’ and ‘for’ the market’). The PSF was formed six years ago and the delivery timeline of the NPA has yet to be determined. The consequence of the passage of time is that the underlying services delivered by the Faster Payments and Bacs schemes have been preserved in aspic at exactly the time that a societal shift to digital payments, the payment opportunities afforded by Open Banking PISP and VRP and, perhaps even, the future of a Sterling CBDC are placing a greater dependency upon Faster Payments (and Bacs Direct Debit / Direct Credit to an extent). The net result is the delays and uncertainty of the NPA are presenting a material risk to effective competition and innovation.

Whether the NPA is delivered as originally envisaged or is delivered to a narrower scope, there is a material risk that continued delays, pausing and ongoing uncertainty will make it very difficult for Pay.UK to attract and retain the subject matter expert resources that are required to deliver such a complex and systemically important critical payment system.

Reviewing the scope of the proposed NPA to mitigate the identified risks is not without precedent. The current scope of the NPA focusses on replacing Faster Payments and Bacs Direct Debit / Direct Credit, whereas the original scope also included Image Cheque Clearing. Reviewing the scope as a mechanism to mitigate risk can be a pragmatic thing to do.

Questions related to procurement scope

2) Do you agree with our analysis of the suggested risks, pros and cons of the alternative options for the scope of the initial procurement?

The analysis conducted by the PSR explores how delivery risk might be mitigated and the extent to which an alternative approach might stimulate competition and innovation.

The findings of the Cruickshank Report (2000), events leading up to the creation of the Payment Systems Regulator, the Specific Directions set by the PSR and the recommendations reached by the Payments Strategy Forum (2017) all point to competitive procurement of the underlying services that support the UK’s retail payment schemes operated by Pay.UK.

Assuming that the regulatory desire for the competitive procurement of clearing and settlement services by a Payment System Operator remains, the analysis of the alternative options outlined in the consultation to mitigate the risks considered to be unacceptably high has the potential to address some, but by no means all, of the identified risks.

On balance, and reflecting on the risks covered in question 1, the EPA broadly agrees with the analysis presented in the consultation paper.

3) Do you prefer scope option 1 or 2, or another alternative? How do the cost implications differ for you? What are the other reasons for your preference?

Given the challenges that the NPA programme has experienced since it was inception in early 2018, it is difficult to see how option 1 can be considered to be viable in its current form. Even with a significant reset it is hard to envisage how some of the views held by the PSR on the material risks could be satisfactorily mitigated.

Based on the arguments made in the consultation paper, a binary decision between option 1 or option 2 would point to selecting option 2. An initial competitive procurement of a core clearing and settlement service layer along with the common services needed to successfully migrate Faster Payments to a new NPA platform, followed by a second procurement approach (if required) for Bacs Direct Debit and Direct Credit, would be an obvious solution to a binary choice.

However, for a number of reasons (including para 1.30 of the consultation which states that *...limiting the initial scope will allow time for Pay.UK to do further work to assess how Bacs services should be delivered in the future*), the EPA would like to propose an alternative option for the NPA programme.

An alternative approach to the binary choice between option 1 and 2 would be to further develop option 2 and progress a reconfigured NPA programme in four distinct tranches:

Option 3:

- *Tranche 1: Settlement Services*

This tranche would focus on the settlement aspects of the NPA and seek to align with the services to be offered by the Bank of England as settlement agent and within the scope of the RTGS Renewal Programme. This would include but not be limited to: settlement cycles to support Faster

Payments moving from NRT to RT settlement, on-boarding access for new participants and efficient use of liquidity across payment schemes.

The historic delays, current pause and any subsequent reinstating of the NPA programme means that the settlement services aspects of the NPA need to be defined, agreed and delivered within the timeframe of the Bank of England's RTGS Renewal Programme or the opportunity to maximise the benefits noted above might be lost.

- *Tranche 2: Faster Payments 2.0*

The consultation paper states a preference (option 2) for a narrower scope initial NPA which might reduce complexity, accelerate Faster Payments migration and support the faster realisation of any benefits.

In addition, this tranche should also consider the end user proposition aspects of Faster Payments including moving the current Near Real Time proposition to Real Time. Such an approach will also benefit developments within Open Banking where a real time payment leg is required and the market adoption of innovations such as Request to Pay.

When launched over a decade ago Faster Payments led the world – Faster Payments needs more than an ISO 20022 based NPA transition, it needs a holistic reset to create Faster Payments 2.0 as an upgraded real time system.

- *Tranche 3: Direct Debit 3.0*

Processing over 4.5 billion transactions a year and a strong 50 year heritage, it is clear that Bacs Direct Debit is a much valued payment instrument.

The EPA believes that the future role, function and delivery of Direct Debit within the NPA has not been fully determined or validated with stakeholders. Para 1.30 of the consultation states that *...limiting the initial scope will allow time for Pay.UK to do further work to assess how Bacs services should be delivered in the future* and the independent assurance review conducted in Spring 2019 noted the absence of strong foundations.

Narrowing the scope of the NPA procurement to exclude Bacs Direct Debit as suggested in the PSR proposals will provide the opportunity to consider the merits of both push (Direct Request) vs pull (Direct Debit) collections, bulk vs 1x1 payments and whether the infrastructure required to serve end user needs is better delivered inside or outside a primarily Faster Payments based NPA.

An additional benefit of this approach is that other facets of the Direct Debit proposition such as processing cycle, consumer guarantee, service user inclusion and alignment with 'overlay' services

(e.g. Request to Pay and Open Banking offerings (Variable Recurring Payments and sweeping)) could be explored at the same time.

The EPA believes that time and opportunity drivers point to the creation of Direct Debit 3.0 with assessment of the infrastructure fit within NPA taking place in tandem and not sequentially to the other tranches.

Such an approach would also facilitate, if required, a competitive procurement process within or outside of a NPA procurement process.

- *Tranche 4: Faster Payments DCA / FIM and Bacs Direct Credit.*

When considering option 2, the consultation correctly identifies that Faster Payments DCA / FIM and Bacs Direct Credit are intrinsically linked. It is also clear that choosing an option other than option 1 retains a level of complexity for bulk file submissions for both Faster Payments and Bacs.

Although the market adoption of Faster Payments DCA and FIM is limited it is difficult to envisage these services being withdrawn and, conversely, with the wide market adoption of Bacs Direct Credit it is impossible to contemplate the withdrawal of bulk push payment submissions.

As a precursor to commencing phases 2 and 3, a decision will need to be made about bulk submission. There are four options: (a) withdraw bulk file submission, (b) include DCA / FIM in the Faster Payment / NPA scope, (c) include all push payment submissions into phase 3 or (d) dictate that NPA will only process 1x1 transactions and bulk submission can only be provided as an 'overlay' service.

Mindful of the need to meet customer needs and the 2009 'end of the cheque that never was' decision, careful consideration of these four potential options is required. At a first glance it seems that only options 'b' and 'c' are viable, but both have significant pros and cons.

However, option 'd' might provide a neat solution for Faster Payments DCA / FIM and potentially provide a solution to enable Bacs Direct Credit migration to NPA be a fast follower to Faster Payments. Were this to occur, then a solution for Bacs Direct Debits outside of NPA but within the settlement layer might present itself.

4) Under scope option 2:

a: What do you think would be a suitable time frame to allow the emergence of market-led propositions that could assist with the migration of Bacs transactions (including Direct Debits) to the NPA? What actions could be taken, and by whom, to help assist or stimulate the creation of such solutions?

It is possible that the elapsed time frame to transition Bacs Direct Credit and Direct Debit to a NPA environment may not differ significantly between options 1 and 2.

The alternative approach (option 3) outlined in the answer to question 3 above will cause the 'bulk submission' question to be resolved and, subsequently, delivered within a Faster Payments (Phase 2) or Bacs (Phase 3) NPA delivery stream.

Crucially, option 3 provides opportunity for the complex Bacs transition challenges to be addressed without any further detrimental impact on the settlement and Faster Payments aspects of the NPA development.

As the consultation suggests, there is a need for any decisions regarding the future of bulk file submission and (pull) Direct Debits to be built on solid foundations. Also, to avoid a repeat of the 'end of the cheque that never was' decision, a programme of strong end user engagement is required.

These activities should be progressed by Pay.UK, utilise subject matter experts and include independent challenge / thought leadership. The EPA would be willing to provide access to practical expert input to support this process.

b: Do you think file-based common services to enable the migration of Faster Payments DCA/FIM transactions should be excluded from the initial procurement and considered further, in conjunction with common services to support the migration of Bacs transactions?

This question has been covered in the answers to questions 3 and 4a.

c: To what extent would an initial, narrower, CIS procurement (focusing on Faster Payments) still need to consider how the procured solution could support Bacs-related features in the future? Which Bacs-related features in particular might require such focused attention prior to the initial procurement?

This question has been covered in the answers to questions 3 and 4a.

Although there are many proposition, operational and infrastructure synergies between Bacs Direct Debit and Bacs Direct Credit, they are two very different payment instruments that perform different functions.

If both Bacs Direct Debit and Bacs Direct Credit are delivered outside of NPA, then ensuring central bank settlement synergies would be important (see question 3 above).

If it is decided that Faster Payment DCA / FIM are delivered via a NPA enabled Faster Payment solution, then it is possible that Bacs Direct Credits could be a 'fast follower' and be migrated from the existing Bacs engine. Faster Payments DCA is, in effect, a white label version of Bacs DCA so the process here would reverse the arrangements Bacs originally provided Faster Payments. Obviously other aspects of Bacs Direct Credit will require changing (e.g. clearing cycle).

This would potentially leave Bacs Direct Debit outside of a NPA solution which has pros and cons.

Finally, if bulk submissions were to be delivered as a NPA 'overlay' service then any future Direct Debit (pull) or Direct Request (push) may be less complex to deliver inside or outside the NPA.

Questions related to procurement approach

5) Which of the procurement options do you consider is the best way forward and why? Please explain if your view differs depending on the scope of the initial procurement.

The findings of the Cruickshank Report (2000), events leading up to the creation of the Payment Systems Regulator, Specific Directions set by the PSR and the recommendations reached by the Payments Strategy Forum (2017) all point to competitive procurement of the underlying services that support the UK's retail payment schemes operated by Pay.UK.

Noting the implication of such a decision, there is an argument that the provision of systemically important payment systems could be delivered by the Payment System Operator and not outsourced.

Also, there is precedent that demonstrates that it is possible for a renewed contract to be negotiated with an incumbent supplier.

However, assuming that the regulatory desire for the competitive procurement of clearing and settlement services by a Payment System Operator remains, then:

- For option 1 (original NPA scope) the current procurement process ought to continue.

Much time has been invested in progressing PQQ and RFI and getting ready for RFP. To start the process again will cause further delay and, given the complexities and vendor experiences, is unlikely to result in additional vendors entering the fray.

- For option 2 and option 3 (narrower scope), then a new competitive procurement process should be commenced.

Both options 2 and 3 represent a new and far less complex scope and starting a new process (perhaps combining PQQ and RFI into one stage) would provide opportunity for current, excluded and new vendors to enter the procurement process, which would support a truly competitive process.

Although elapsed time is an issue, there are a number of examples around the world of Faster Payment equivalents being implemented within 12 to 18 month timeframes.

6) Do you consider that there are other realistic options available that we have not identified? What do you see as the risks and benefits of any additional option(s)?

Answers to previous questions consider the pros and cons of bulk vs 1x1 submissions and the merits, or otherwise, of transitioning a 'pull' payment (Direct Debit) to a 'push' payment (Direct Request).

Permanently excluding Bacs Direct Debit and Bacs Direct Credit from the scope of the NPA is a realistic option. That said, such an option cannot be regarded as a 'do nothing' option as the infrastructure will still need procuring, ongoing hardware / software investment will be required, settlement synergy will be required and the proposition will need developing (Direct Debit 3.0). All decisions would need to be based on a clear strategy for bulk push / pull payments set in the context of a holistic payments strategy.

The scope and role of the proposed overlay services component of the NPA remains undefined. The role of overlay services in driving competition and openness in the eco-system should not be underestimated.

It is worth questioning the extent to which a central infrastructure is required, and we invite the regulator to consider deploying a distributed architecture model, such as that deployed in the EU with the introduction of SEPA and SEPA Instant, where the role of the EPC is quite different to that of Pay.UK. This would perhaps relieve Pay.UK of the procurement pressure and lead to increased focus on scope, design and the rulebook, as well as greater supply side competition and more competitive pricing.

Although beyond the scope of this consultation, it is important to note that the NPA offers a ‘once in a generation’ migration path to a feature-rich ISO 20022 utilising enhanced data building blocks. It is important that, in all the adjustments made to enable the delivery of NPA, the message standard opportunity is not lost.

Finally, it is important not to lose sight of the Financial Stability Board’s cross border payments roadmap as a joined up approach that cascades down to domestic application is important.

About the Emerging Payments Association (EPA)

The Emerging Payments Association (EPA), established in 2008, sets out to make payments work for everyone. To achieve this, it runs a comprehensive programme of activities for members with guidance from an independent Advisory Board of 16 payments CEOs.

These activities include a programme of digital and (when possible) face-to-face events including an online annual conference and broadcast awards dinner, numerous briefings and webinars, CEO Round Tables, and networking and training activities. The EPA also runs six stakeholder working groups. More than 100 volunteers collaborate on the important challenges facing our industry today, such as financial inclusion, recovering from COVID-19, financial crime, regulation, access to banking and promoting the UK globally. The EPA also produces research papers and reports to shed light on the big issues of the day and works closely with industry stakeholders such as the Bank of England, the FCA, HM Treasury, the Payment Systems Regulator, Pay.UK, UK Finance and Innovate Finance.

The EPA has over 130 members that employ over 300,000 staff and process more than £7tn annually. Its members come from across the payments value chain including payments schemes, banks and issuers, merchant acquirers, PSPs, retailers, TPPs and more. These companies have come together to join our community, collaborate, and speak with a unified voice.

The EPA collaborates with its licensees at EPA EU and EPA Asia to create an interconnected global network of people passionate about making payments work for all.

See www.emergingpayments.org for more information. Contact malik.smith@emergingpayments.org for assistance.