

Market review into the supply of
Indirect Access to payment systems PSR MR15/1

Draft Terms of Reference

March 2015



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1 Introduction

Background

- 1.1 This draft Terms of Reference launches our market review into Indirect Access to payment systems in the UK. We are conducting this review using our general powers under the Financial Services (Banking Reform) Act 2013 (“FSBRA”).
- 1.2 Payment Service Providers (PSPs) can either have Direct Access or Indirect Access to payment systems. This review will focus on the Indirect Access services provided to PSPs which access payment systems through agreements with certain Direct PSPs known as Sponsor Banks. These arrangements enable Indirect PSPs to provide payment services to their own customers. For a large number of PSPs, or businesses that wish to become a PSP, Indirect Access provides an important, and in some instances the only, route to accessing payment systems.
- 1.3 Access to payment systems is an important driver of competition and innovation in the provision of payment services. This review is looking into the economic issues around Indirect Access, and whether current arrangements deliver a good outcome for all people and organisations that use payment systems.
- 1.4 This draft Terms of Reference sets out:
 - why we decided to look into the supply of Indirect Access to payment systems
 - the proposed scope of the review
 - what happens next, contact details and the information gathering process
 - what could happen as a result of the review.

Why are we conducting this review?

- 1.5 This review has been prompted by concerns raised during the Financial Conduct Authority’s (FCA) Call for Inputs¹ and the PSR’s evidence gathering process that led to our first Consultation Paper.² These concerns fell into nine broad categories:
 - lack of choice in Sponsor Banks
 - difficulties accessing and assessing information about different Indirect Access options
 - reliance on downstream competitors for the provision of access to payment systems
 - fees for Indirect Access

¹ FCA, *Payment Systems Regulation, Call for Inputs*, March 2014.

² PSR CP14/1, *A new regulatory framework for payment systems in the UK*, November 2014.

- communication of important information by Sponsor Banks
- the risk that Sponsor Banks may discontinue the supply of Indirect Access
- contractual arrangements that govern the supply of Indirect Access
- the quality and availability of Technical Access
- demand for alternative access mechanisms.

1.6 We consider that initiatives we have outlined in our Policy Statement will help to address a number of the concerns identified to us with regard to Indirect Access. Our direction requiring the four primary Sponsor Banks to publish access-related information will enhance transparency and improve Indirect PSPs' ability to make informed choices about their sponsor services. We also expect the Sponsor Bank Code of Conduct that we will approve to help address certain concerns regarding security of supply, contractual arrangements, reliance on downstream competitors, and the communication of information.

1.7 We are considering the quality and availability of Technical Access and the demand for alternative access mechanisms alongside these proposals.

1.8 However, there are a number of more fundamental, structural concerns that we would like to understand further. In our Consultation Paper, we said we would conduct a market review into the supply of Indirect Access, with a primary focus on:

- developing a deeper understanding of the economics of the supply of Indirect Access generally
- understanding what factors limit the degree of choice available to different types of Indirect PSPs.

1.9 We have taken into account responses to our Consultation Paper and we have held a number of meetings with stakeholders to help inform the proposed scope of the review.

1.10 Our review is aimed at gathering further detailed evidence about Indirect Access in order to better understand the market and consider whether current Indirect Access arrangements deliver a good outcome for service-users.

1.11 Our review will also inform our approach to monitoring and regulating Indirect Access to payment systems. The review is likely to inform administrative priority decisions if we receive applications for new access, or the variation of existing access agreements and fees, under section 56 or 57 FSBRA.

2 Scope of the review

What does this review cover?

Payment systems in scope

- 2.1 We propose to include Indirect Access to the following regulated payment systems within the scope of the review:
- Bacs
 - CHAPS
 - Faster Payments Scheme (FPS)
 - LINK
 - Cheque & Credit (C&C).
- 2.2 Although all PSPs participating in the LINK payment system are direct members, some members without access to a Bank of England settlement account still require a sponsor arrangement for the settlement of funds. Therefore, we propose to include LINK in the review even though the structure of the system means PSPs do not access this system indirectly.
- 2.3 We propose to exclude card payment systems from the review (e.g. MasterCard and Visa Europe (Visa)) as stakeholders did not identify significant concerns regarding Indirect Access to card payment systems. However, MasterCard and Visa are part of the competitive landscape for Indirect Access and we will take into account how access to those systems is relevant to the analysis of the structure of the market for access to interbank systems.
- 2.4 We expect to become the competent authority for various parts of the EU Interchange Fee Regulation and in our Policy Statement PSR PS15/1 we explain that we will start a programme of policy work on card payment systems. We will seek to understand if there are any further access-related concerns regarding card systems as part of that programme of work.

Services in scope

- 2.5 For the purposes of this review, a PSP has Indirect Access to a payment system if it has “a contractual arrangement with a PSP to enable it to provide services to individuals or businesses who are not Participants in the system, for the purposes of enabling the transfer of funds using that payment system.”
- 2.6 This definition distinguishes Indirect PSPs from corporate customers on the basis of their business activity. In other words, Indirect PSPs are the entities that transfer funds on behalf of other ‘persons’ (both individual and business customers). There are a number of different types of Indirect PSP, including both banks and non-banks such as Payment Institutions (PIs) and Electronic Money Institutions (EMIs).

- 2.7 The scope of this review includes services provided to all types of PSP. For the avoidance of doubt, we do not propose to include the provision of access to corporate customers such as utilities and retailers in the scope of the review. This is because they do not use payment systems to provide services to persons who are not participants in the system, for the purposes of enabling the transfer of funds using that payment system.
- 2.8 Sponsor Banks make and receive payments using regulated payment systems as part of international correspondent banking relationships. Stakeholders have not raised concerns about these relationships. We do not view it as necessary or appropriate to include such relationships within the Indirect Access definition. We therefore consider that for this market review, Indirect Access does not include international correspondent banking relationships.
- 2.9 We will consider the provision of Indirect Access services by all Sponsor Banks as part of this market review. This includes services provided by the four primary Sponsor Banks (Barclays, HSBC, Lloyds and RBS), but is also likely to include other banks. We understand that there are a number of other Direct PSPs, and some Indirect PSPs, that provide Indirect Access.
- 2.10 We have decided to apply the Direction to publish access-related information³ to the four primary providers of Indirect Access (Barclays, HSBC, Lloyds and RBS), and will expect compliance from them with the Sponsor Bank Code of Conduct, as set out as part of our Policy Statement. However, subject to its findings, the market review could result in broadening the coverage of the Direction and/or Code of Conduct.

Issues to be explored

- 2.11 The three key questions we propose to address in the review are as follows.

I. What are the implications for competition arising from the structure of the market?

We will look at the characteristics of Indirect Access to develop an economic framework for assessing the nature of competition and any access-related concerns this may raise for service users. This will inform the basis for our approach to regulating and intervening in the provision of Indirect Access. It will also provide further context for the other two key issues below.

II. What factors may limit the number of Sponsor Banks offering Indirect Access to payment systems?

We would like to understand the barriers to providing Indirect Access to payment systems, which may be preventing more PSPs from becoming Sponsor Banks. This will include considering the initial and ongoing elements involved in providing indirect access, as well as risks associated with providing services across different types of Indirect PSPs.

III. What might a competitive Indirect Access offering look like?

We intend to assess the outcomes experienced by service users, e.g. are the quality of services and prices consistent with a competitive market? During the review we will also develop a deeper understanding of the limited degree of choice some Indirect PSPs face when trying to secure Indirect Access.

- 2.12 The PSR has not reached any conclusions about whether the concerns raised mean that the current arrangements are, or are not, delivering a good outcome for service-users.

³ Specific Direction 1 (Access: sponsor banks)

3 Next steps

Feedback

- 3.1 We welcome feedback on the proposed scope of the review, as set out in this draft Terms of Reference. We are particularly interested in answers to the following questions.
- Do you agree with the key questions and issues on which we propose to focus the review?
 - Do you agree that the review should focus on the main interbank payment systems: Bacs, CHAPS, FPS, LINK, and C&C?
 - Do you agree that the review should focus on the services provided by Sponsor Banks to Indirect PSPs?
- 3.2 Following publication of this draft Terms of Reference, we will be continuing to work on the issues highlighted in it. After reviewing feedback to this draft Terms of Reference we will publish final Terms of Reference for the review, which we expect to do by the end of May 2015. This will also set out the timetable for the review.
- 3.3 As well as examining existing research and analysing information that we already hold, we plan to collect additional information from market participants. We will engage with Operators, Infrastructure Providers, PSPs and service-users over the coming months. We will use a variety of methods for this engagement, including but not limited to: interviews, roundtables and site visits. We expect to gather evidence through the use of specific surveys and requests for detailed information from some participants.

How to submit views

- 3.4 Please send your comments to iamr@psr.org.uk by **Friday 24 April 2015**. Or in writing to:
- Indirect Access Review Team
Payment Systems Regulator (15th floor)
25 The North Colonnade
Canary Wharf
London E14 5HS
- 3.5 We may make all responses to this draft Terms of Reference available for public inspection; in full or in part, unless the respondent specifically identifies commercially sensitive information for which confidentiality is requested. We will not regard a standard confidentiality statement in an email message as a request for non-disclosure. We will also not accept blanket claims of confidentiality, and will require respondents to identify specific information over which confidentiality is claimed, and to explain the basis on which confidentiality is sought.
- 3.6 Despite this, we may be asked to disclose a confidential response under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Rights Tribunal.

Possible outcomes of the review

3.7 Possible outcomes of our review include:

- making new directions or modifying existing directions
- continued monitoring of the directions we are putting in place on access to regulated payment systems
- considering making participant-specific directions
- requiring Direct or Indirect Access to be granted to a payment system
- making recommendations for further industry initiatives or enhanced industry self-regulation
- making proposals to the Bank of England, FCA or Prudential Regulation Authority as appropriate
- publishing guidance
- asking the Competition and Markets Authority to consider investigating the market(s)
- taking no further action at this time.