Payment Systems Regulator

Draft statement of policy on our cost benefit analysis framework

Stakeholder submissions

January 2025

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Names of individuals and information that may indirectly identify individuals have been redacted.

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NatWest welcomes the opportunity to input our views into the CBA framework. We broadly agree with the points made by UK Finance in their separate submission response to the PSR, however there are a few points we would like to make directly, as set out in this response.

The framework identifies several core principles guiding the approach to CBAs including proportionality, transparency, practicality, balance and an overall need for stakeholder engagement. In addition, the framework provides an overview of the analytical process covering problem definition, identifying remedies, estimating costs and benefits, and evaluating how changes in assumptions may affect outcomes.

Whilst CBA is a valuable tool for guiding regulatory decisions, the framework faces limitations related to data accuracy, uncertainty, complexity of assessing dynamic market impact and distributional effects as well as subjectivity in non-monetary evaluations. The PSR will need to remain mindful of these limitations to ensure that CBAs provide meaningful and balanced insights. In this response, we provide a few thoughts for consideration to guard against oversimplifying, overestimating or overstating the effects of regulatory interventions and policy formation.

Data limitations

CBAs often rely on assumptions about future behaviour, market trends or the estimated impact of regulatory interventions. The availability and quality of data can restrict the ability to accurately assess costs and benefits of regulatory actions. Incomplete or inaccurate data could lead to flawed conclusions. We accept that in such circumstances, the PSR must rely on the best available data at a point in time.

However, where such gaps exist and reduce the precision of analysis, for transparency the PSR should share their findings with the industry. This will help determine if industry can plug those gaps or help further analyse initial findings.

Complexity in distributional impacts

While CBAs aim to analyse the overall costs and benefits, distributional effects (i.e. how different stakeholders are impacted) are often more challenging to evaluate. Some groups may benefit, and others may incur unforeseen costs, because of regulatory interventions. Shortcomings in CBA assessments may result in unintended consequences for specific sectors or consumers if cost is passed through.

Subjectivity in assessing non-monetary impacts

Some regulatory interventions aim to achieve outcomes like increased consumer trust, enhanced competition, or better market access. Whilst important, these non-monetary impacts can be subjective and difficult to measure consistently. We would welcome further exploration of assessing non-monetary impacts, absent of which, CBAs may under (or over) represent the true value of regulatory interventions.

UK Finance

Payment Systems Regulator (PSR): Draft statement of policy on our cost benefit analysis framework (CP24/12)

UK Finance Response

11 November 2024

Response

This is UK Finance's response to the PSR's Consultation on its '*Draft statement of policy on our cost benefit analysis (CBA) framework*'[1]. This response was sent to econframeworks@psr.org.uk.

UK Finance welcomes the opportunity for industry to input its views into the PSR's CBA framework, particularly given that there is no statutory obligation to seek this input. We also value the PSR's engagement with the CBA Panel as part of this consultation.

Executive Summary

Our response focuses on:

- *Developing the methodology of the framework*.
- *Considering previous CBA assessments*.
- *Wider policymaking considerations*.

A consistent and robust approach to conducting CBAs is a crucial component of delivering evidence-based, outcomes-focused policy and ensuring the impacts of proposed strategic approaches and interventions are well understood, helping to strengthen confidence that regulatory measures will yield proportionate benefits relative to their costs, supporting sustainable growth and innovation in the payments ecosystem.

Developing the methodology of the framework:

- **Going beyond legal requirements**: We strongly welcome the PSR's decision to generally carry out CBAs for all regulatory interventions, whether or not there is a specific legal requirement to do so, and to engage with the CBA Panel on more cases than required under the FSBRA 2013. We encourage the PSR to always seek to display best practice in its approach to CBAs beyond what is the minimum legal requirement.
- **Enhancements to the CBA framework:** We consider there to be a number of elements that all CBAs should contain:
- i) a clear description of the specific market failure that the PSR's proposed intervention is seeking to address, and how that relates to its statutory objectives;
- ii) a quantitative baseline such as a point estimate, sensitivities or break-even analysis, in addition to qualitative considerations and indirect costs;

[1] PSR: CP24/12: Draft statement of policy on our cost benefit analysis framework.

- iii) a clear articulation of the outcomes and benefits the PSR expects, which allows for the review process to appropriately assess whether an approach or intervention had the desired effect;
- iv) a comparison of the PSR's proposed policy intervention(s) to a suitable range of alternative options, rather than just a "do nothing" option, and;
- v) a comprehensive analysis of a proposed intervention's impact on growth.
- **Enhancements to the interaction with the CBA Panel**: We welcome the PSR's proposal to publish summaries of the CBA Panel's key comments. We recommend some targeted enhancements to the PSR's proposed approach to engaging with the CBA Panel, to improve accountability. For example, we recognise that in certain cases, applying a full assessment or the higher standards may be disproportionate or impractical. In such situations, to increase accountability, we propose that the PSR seek agreement from the Panel before taking a final decision in these cases.
- **Taking a 'CBA approach' throughout the policy-cycle**: We support the proposal to embed CBAs throughout the policymaking cycle, ensuring they are seen as an important tool for evaluating the necessity and approach of a potential intervention, rather than as a means to justify decisions already made. The PSR should structure CBAs to facilitate future reviews of interventions, enabling ongoing assessment and adaptation. Our suggested enhancements would support this review capability and encourage a holistic view of the regulatory burden in policy development.

As UK Finance has highlighted to regulators across many areas of policy development, there have been examples of policy decisions in the past where a full and thorough understanding of the costs and impacts has not been undertaken (or, where insufficient weight has been given to the findings of that analysis). CBAs are a common internal mechanism for many, if not all regulators; both nationally and internationally. We encourage the teams responsible for this framework to consider established and evolving CBA methodologies across different regulatory bodies, which could provide valuable insights and best practices.

Considering previous CBA assessments:

In our response to the PSR's *Generally applicable requirements: draft review framework* consultation[2], we highlighted concerns specifically with the PSR's CBA processes in the past, including analysis being presented without consideration to other counter-policy interventions, including those proposed by industry. Examples include:

- **New Payments Architecture (NPA)**: The CBA case for NPA was not sufficiently robust and dynamic, it failed to adequately explore alternative options over time, leading to excessive sunk costs for industry as a result of Specific Directions 2(a) and 3(a).
- **Confirmation of Payee (COP)**: Three substantial change programmes were required to meet the regulator's intended objective, even while the benefits of COP were diminishing

[2] PSR: CP23/11: Generally applicable requirements - draft review framework.

as a scam prevention tool. A better approach would have been to assess firms' anticipated compliance costs before implementation. This could have prompted the PSR to adjust the level of regulatory intervention over time as the benefits decreased.

- **Authorised Push Payment Reimbursement (APPR)**: The industry has been clear from the outset that the CBA for APPR was not being properly considered, with the risks of the proposals significantly underplayed. These included clear counterfactuals from the industry on behavioural economics, user experience impacts and distortion of market competition. The PSR should also have considered the counter proposal of using the PSRs 2017 to deploy the requirements, rather than the resource-intensive change to Pay.UK scheme rules.
- **Card Acquirer Market Review:** CBA assessments used for the review were heavily quantitative, and did not consider wider relational benefits between acquirers and merchant customers.

We also wish to stress the importance of strong CBA assessments for future significant policy interventions, most notably the PSR's development of Account-to-Account payments.

Wider policymaking considerations:

We are encouraged to see the framework supporting the PSR's contribution to the government's economic growth mission. We believe that prioritising growth will be vital to all of the PSR's proposed interventions and recommend that the PSR fully commits to incorporating this focus consistently. The Financial Conduct Authority (FCA) is also exploring this topic in its recent paper, "**The Growth Gap: A Literature Review of Regulation and Growth**".

With the regulators growing interest in the intersection of technology and payments; such as the PSR's recent work on digital wallets, it's essential for the CBA framework to account for this increasing market complexity. The framework's processes and proposed strategic approaches should reflect the interconnected nature of new payment technologies.

Our members value CBAs that clearly link the PSR's proposed policies to its statutory objectives. Paragraph 5.19 specifies that a CBA will outline the PSR's intended policy outcomes and explain how the intervention will likely achieve them. We suggest that the policy statement explicitly commit the PSR to ensuring its analysis demonstrates how intended outcomes will support one or more of its statutory objectives and clarifies any trade-offs made between these objectives.

Questions

1. Do you agree with the general principles we set out in this draft statement of policy? If not, please explain what you disagree with and why, as well as what you think should replace them

The CBA framework's core principles are outlined below[3].

"***Our CBAs are part of our policy-development process and may include comparison of regulatory options.*** *They are not about justifying a policy at the very end of the process. Their value lies not only in the final publication but also in how they aid our wider decision-making during the development stages.*

Our CBAs help us make effective decisions, but they are not the only means of doing this. *A CBA is one of several inputs into our decision-making that helps us establish the likely balance of impacts of a proposed intervention. We consider such evidence developed within a CBA alongside other relevant factors and pieces of evidence. CBAs focus on economic impacts, but it is usually not feasible to summarise all impacts in a single number. Sometimes a CBA may identify costs that we consider worth trading off against other objectives, such as the protection of vulnerable customers.*

Our CBAs help us communicate the economic reasoning behind our proposed interventions to stakeholders. *We assess the economic case for intervention, establishing whether the benefits associated with a proposed intervention are likely to outweigh any costs.*

Our CBAs help us to consult effectively. *We can test our assumptions and consideration of likely impacts with stakeholders, including potentially seeking additional information to help improve our assessments.*"

In general, our members are supportive of the framework's principles. See below commentary on how the framework can build on these further.

Taking a CBA approach throughout the policy lifecycle:

- We fully support the principle of using CBAs throughout the entirety of the policymaking cycle, including comparing different regulatory options at early stages of development. We would recommend the use of CBAs within the initial strategic thinking stage of policy development, before developing a list of possible interventions; to clarify the thinking behind the broad market and consumer challenge regulators are trying to solve. CBAs should be seen as a valuable tool for determining if and how to move forward with an intervention, rather than a mechanism to justify a decision that has already been made.

Considering wider evidence than pure quantitative/qualitative data:

- UK Finance agrees with the wider positioning of the principles, which includes "*Our primary focus within CBAs is not to provide single point estimates for overall net impacts. Instead, we aim to provide an appropriate description of the likely overall balance of impacts, taking into account risks and uncertainty*". We welcome the principle of considering evidence outside of the often-restricted picture which a limited set of qualitative and quantitative data provides. Sometimes 'direct' and 'indirect' costs and benefits will exist within newly emerging markets, including open banking payments

[3] Paragraph 3.15, page 12.

(VRPs) and digital wallets. While we agree that limited data will sometimes challenge the aims of building a clear and accurate assessment of the potential impact of proposed interventions, some members question the purpose of an intervention with uncertain benefits from the outset.

- We encourage the PSR to make use of available cost data wherever possible or to consult with the industry for this information. As with all information seeking requests[4], these should be targeted, timed appropriately to give industry enough notice to provide evidence, and designed to minimise any additional burden on firms. Responding to statutory information requests can be resource-intensive for firms and other stakeholders, so it's essential for the PSR to use these powers carefully and proportionately.
- The framework should seek to use the most robust approach depending on the policy proposal in question, the market it relates to, and the available data. The PSR should seek to always present either a point estimate, or where that is impossible, a range with sensitivities or break-even analysis. Where the PSR considers these estimates do not paint a comprehensive picture, it should argue why other factors matter, although always having a rigorous quantified analysis would be helpful for transparency. The PSR should always be able to demonstrate a break-even analysis, setting out precisely under which scenarios/assumptions there is a net benefit, linking to the proposal above to routinely and clearly articulate the outcomes a proposed intervention is seeking to achieve.

Using clear definitions of costs to all parties:

- We note the importance of utilising clear and well-defined terms, especially highlighting where a set of proposed 'costs' will occur as a result of an intervention. For example, an intervention may result in additional costs for financial institutions, however; these costs will likely to be passed onto other market participants and even end users. As such, the regulator must consider the full impact of where additional charges will be made, and how that will affect the commercial viability of all economic actors involved within the service.
- We would suggest the framework's monetisation assessment includes further consideration on how resources and costs incurred by regulated firms are transferred to consumers (known as 'distributional transfer models')[5]. Within the framework's review process, we would encourage the PSR to work closely with the FCA to unpack existing distributional transfer models, including the FCA's assessment of distributed costs across different consumer groups[6], and HM Treasury's Social Time Preference Rate (STPR)[7] within its Green Book (2022) publication[8].

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[4] Set out within the Financial Services (Banking Reform) Act (FSBRA) 2013, Section 81.
[5] Table 2: Types of analysis and common techniques.
[6] FCA: [How we analyse the costs and benefits of our policies](), Appendix 5: Distributional weightings.
[7] 14.1 Role of discounting.
[8] HM Treasury/Government Finance Function: [The Green Book (2022)]().

- The framework must ensure all forms of participants, providers and Third-Party Providers (TPPs) are accounted for within assessments.
- The principles must consider ongoing operational and development costs of compliance, for example in APP scams, COP and commercial variable recurring payments (cVRPs). While industry acknowledges the importance of recognising the long-term benefits of projects like open banking payments, it's important to recognise that 'ongoing costs' are more than 'reporting costs'[9]. Assessments must account for this regulatory challenge.

Industry engagement and gathering of further evidence:

- The industry would like to understand the full evidence and strategic thinking behind proposed interventions at an early stage. We are therefore pleased to see the PSR's plan to share CBA findings to strengthen engagement with stakeholders. Our members appreciate the commitment to gathering additional evidence from stakeholders, and as seen with the recent APPR implementation, there is strong industry support for the PSR to consider evidence provided by the sector.
- In our response to the PSR's Authorised Push Payment (APP) Scams Call for Views[10], we requested the PSR to conduct a more complete economic assessment of the proposals, potentially including quantitative analysis of similar reimbursement schemes, and the experience of the health and motor insurance markets, before moving forward with a reimbursement framework, if it is to be based on a gross negligence exception alone. We also noted the CBA assessment, utilised alongside the proposed intervention, made no reference to significant market risks, which includes the potential impact on competition and innovation and ultimately consumer choice. While the PSR noted the potential migration of fraud risk to other payment methods and prudential implications for some Payment Service Providers, it did not quantify the potential costs.

Panel engagement:

We have the following observations in relation to the PSR's proposed engagement with its CBA Panel:

- We note that there are some cases where the PSR would propose not to conduct a CBA, because doing so would be disproportionate, or would impede urgent intervention. In these cases, we believe the PSR should commit to seeking agreement from the CBA Panel before taking a final decision. This will increase the degree of accountability surrounding the PSR's approach to CBAs and will ensure the Panel's experience is brought to bear on decisions about whether to conduct a CBA.
- We welcome the PSR's decision, in some cases, to consult the CBA Panel even where this is not required by law. The draft statement of policy advises that the PSR will do so "*from time to time and depending on the specific context*"[11]. We would welcome more

[9] Paragraph 5.23, page 24.
[10] UK Finance: Response to Payment Systems Regulator Call for Views on Authorised Push Payment (APP) Scams.
[11] Paragraph 6.8, page 31.

clarity on the circumstances in which it will seek input from the Panel when not legally required to do so. We would welcome confirmation of our understanding that in contrast to the FCA, the PSR is not relying on a quantitative *de minimis* threshold for consulting the Panel (i.e. a level of expected costs, such as implementation costs, below which it would not consult the Panel on a proposed policy intervention). We agree with this decision given the economic impact of policies may not always relate to implementation costs.

- Passing 'Specific Direction'[12] cost benefit analysis models, including those for cVRPs, to the FCA CBA Panel for review would add an extra layer of oversight to ensure that interventions are justified and proportionate. We welcome the PSR's commitment to ongoing engagement with the Panel.
- In addition to the points raised regarding Section 53 of the FSBRA 2013 below, our members feel 'proportionately' should be added into the second principle.

We welcome the PSR's approach of summarising the Panel's views and the PSR's response in each consultation. We note that the draft statement of policy states the PSR will "*usually*" take this approach[13], so we would welcome clarity on the circumstances in which the PSR envisages not doing so.

2. Are there any areas you consider that a more specific methodological approach would be better than our current principles-based framework? If so, which areas, and what approaches do you think we should consider adopting?

- It is important the framework supports the PSR's thinking regarding both strategic approaches and interventions, which means key forms of analysis, including monetary estimates, cannot be the *only* consideration to when decisions are made.
- The framework must fully recognise and consider the subjectivity within a limited set of qualitative and quantitative data. This includes utilising statistics obtained predominantly from one side of the value chain, or survey results from market participants, and not end users. It's also worth highlighting that non-monetary impacts can be subjective; including within the regulator's aims of meeting its high-level outcomes including increased consumer protection, enhanced competition, or better market access. Additionally, the framework must consider possible contradictory results across different forms of analysis. For example, quantitative data evidencing strong *interest* from consumers, whilst qualitative data indicates significant *disinterest* from firms regarding the market's commercial model (for example). Within this context, it is critical the framework includes

[12] As set out within Paragraph 2.2, page 6.
[13] Paragraph 6.7, page 31.

the necessary workings to outline how a strategic approach or intervention considers this evidence.

- Whilst the framework's proportionate analysis[14] mechanism gives policymakers a useful starting assessment criterion to determine which data to select for analysis, we suggest identifying sources it uses the most, and their level of success in supporting approaches and interventions.
- The quality and validity of data is critical. This includes secondary quantitative sources accurately reflecting the existing market players across the value chain. Incomplete or inaccurate data could lead to flawed conclusions. This also applies to approaches and interventions relating to future markets, or value chains which are yet to the matured. Whilst utilising qualitative data, including hosting industry engagement forums, is a welcome form of analysis, we would encourage further creative thinking when it comes to finding the most optimal forms of primary and secondary sources.
- We welcome the framework's consideration towards HM Treasury's reference to 'optimism bias' within its Green Book. We suggest the PSR monitors the degree to which its CBAs exhibit bias within the framework's review process. Regulators can often remain blinkered when far into the development of a proposed intervention, which can lead to some risk aversion to additional evidence which may support alternative actions. Our members also question comparing a proposed intervention to other options "in special circumstances" (set out within paragraph 5.21), which sets too high a bar for such a comparison. We believe the framework should routinely compare its favoured policy intervention to alternative options. Arguably, the PSR's support for NPA is an example of this.
- CBAs should clearly state the specific market failure that the PSR's proposed intervention is seeking to address, as well as the intended outcomes and benefits. This should be outlined in a way that enables the PSR to assess, in any post-implementation review, whether the intervention has successfully achieved its stated goals.
- It is important to avoid considering the expected costs of a policy intervention in isolation. The PSR should, where possible, take a holistic view of the regulatory burden, considering the marginal impact of its intervention on firms' abilities to support the wider economy, considering existing regulatory (or at least, PSR-driven) investment and compliance cost. The marginal adverse impact on firms, and the associated opportunity cost, of any given policy proposal is likely to increase as the regulatory burden on firms increases.
- Our members would welcome further consideration from the PSR regarding the proportionality obligation set-out within Section 53's 'Regulatory principles' of the FSBRA 2013. When considering whether the exemption in Section 104(11) of the FSBRA 2013

[14] Paragraphs 5.12-5.15, pages 21-22.

applies, the PSR should ensure it considers *indirect* costs as well as *direct* costs. We would welcome this being explicitly stated in paragraph 4.14 of the statement of policy. Additionally, we would welcome the PSR consulting industry on its assessment of 'no identified costs'; determining a CBA assessment to not be used.

- We also encourage the PSR to refine the list of illustrative benefits set out in Table 4 to ensure it is appropriately nuanced. For example, it could usefully recognise that "*choice for choice's sake*" may not necessarily always be a good outcome.

3. Is there anything missing in this statement of policy that you think this document should address? If so, which are areas that you think we should expand on further?

- **Transparency and review mechanisms**: We recognise the PSR has already started to think about a review mechanism, which will evaluate the effectiveness of data used in relation to whether an intervention matches the expectations within the original assessment. This is outlined within paragraph 6.3. "*[past CBAs] can provide valuable insight as to whether impacts matched the expectations our CBA outlined, and, if not, how we might need to adjust analysis and assumptions for future CBAs".*

- **Publication of assessments**: We would welcome a commitment to publish all conducted CBAs. For example, those which were used ahead of the APPR go-live date. This should also include a publicly accessible log of proposed outcomes following CBA assessments, and when they have/haven't been used. It would also be useful for the review process to include assessments of when the 'do nothing' approach (or another non-regulatory option) was selected after a CBA. We would also welcome the PSR providing examples of when CBAs have been used to choose 'no regulatory intervention required'.

- **Regulatory coordination**: While we support the framework's focus upon individual interventions[15], the PSR needs to increase efforts to build regulatory coordination across the now complex mix of financial services regulators. For example, the recent '*Big tech and digital wallets call for information'* highlights the importance of using data from a broad range of sectoral data to inform all relevant financial regulators' strategic approaches to regulating digital wallets within specific payment rails. We welcome the framework's mechanism to consult the FCA's CBA review panel[16], and we recommend building further means of cross-regulatory review, for example with HM Treasury's regulatory regime for fiat-backed stablecoin payments. This should also include measures to consider potential divergent regulatory priorities, and how supporting analysis might favour different regulators' analysis.

[15] Outlined within Figure 3, page 22.
[16] Paragraph 1.12, page 4 (in reference to the FSMA 2023).

- **National Payments Vision (NPV)**: We encourage the PSR to consider how this framework will connect to macro approaches to payments, particularly HM Treasury's NPV. This alignment could also reflect the distinct objectives regulators have, such as prudential and economic responsibilities, particularly as they increasingly collaborate on regulatory and supervisory developments. With the interconnected growth of innovation areas like smart data, tokenisation, Artificial Intelligence (AI), and digital wallets; a cohesive approach will support efficient oversight and foster progress across these emerging fields.

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