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MARKET REVIEW INTO THE OWNERSHIP AND COMPETITIVENESS OF INFRASTRUCTURE PROVISION PSR MR15/2.1

The Cheque and Credit Clearing Company welcome the opportunity to respond to the Payment Systems Regulator's market review on "Ownership and competitiveness of infrastructure provision - PSR MR15/2.1".

Background

The Cheque and Credit Clearing Company (C&CCC) was established in 1985 and from that time until the present day it is proud of its record in:

- Providing members with the central payment system services for the exchange and settlement of cheques and credits;
- Managing the operational processes of the central payment system services;
- Determining the rules, standards, and procedures required to maintain the integrity of the clearings, including the criteria for joining the clearings and ensuring compliance with those rules;
- Engaging with the full range of stakeholders which includes consumers and businesses that use cheques, banks that offer cheque clearing services, cheque processors, cheque printers and other suppliers, as well as regulators, trade associations and other payment schemes.



Our Objectives are to:

- ensure that cheques and credits remain a viable, secure and efficient choice of payment for all users, so we will:
- promote innovation and competition in payment choice by driving improvements in processing, service and efficiency
- provide a trusted centre of excellence for anyone with an interest in cheques or credits

Future Changes

As identified in your Market Review, C&CCC will be introducing the Future Clearing Model (FCM) of image based cheque clearing within two years. Therefore we agree that a detailed analysis of the current models used to support C&CCC would be of limited value.

The introduction of the FCM will fundamentally change the nature of C&CCC's supplier relationships. Currently, there are few contracts relating directly to the processing of cheques and credits (a full list has already been made available to the PSR on a confidential basis). Most processing is carried out by companies employed directly by C&CCC's Members. Under the FCM the infrastructure required by C&CCC will increase, and this will change the dynamics of the market and has the potential to change the nature of provisions procured by the FCM participants. It is therefore essential that C&CCC continues to have a robust, fair, defensible and open tender supplier policy at its core.

All current contracts (including that for the FCM infrastructure) have been let in accordance with our supplier policy.

Key Questions to be Explored

Your Market Review seeks to answer the following questions:

1. Is competition effective in the provision of infrastructure services in interbank payment systems, and if not, what are the reasons for this?

The experience of C&CCC is that there is effective competition in the provision of infrastructure that we have procured. Our recent tender for the FCM produced:

- 49 non disclosure agreements received in response to RFI
- 9 withdrawals after NDAs sent
- 13 Non respondents
- 21 RFI submissions
- 7 suppliers invited to ITT stage
- 4 compliant responses to ITT
- 2 non compliant responses to ITT

The award of the contract to a non incumbent payment systems infrastructure supplier reinforces our 'open resourcing' policy.



2. How do the current ownership arrangements of infrastructure providers affect competition in the provision of infrastructure services related to interbank payment systems?

The experience of C&CCC has been that some potential suppliers do not consider that all suppliers have the same opportunities in supply to payment schemes. This is reinforced from C&CCC's experience from a previous RFI for the 'Single Utility'. The ownership structure of some potential bidders and the holding of major contracts by others appeared to discouraged some potential suppliers from entering the market for provision of services.

Some PSPs also find that there is an inherent conflict between competing for market share, working collaboratively to deliver payment systems, whilst owning potential suppliers to that payment scheme. The move to cheque imaging in the FCM will be the culmination of work commenced in the mid 1990s and reinvigorated in 2009 by the announcement by Payments Council of its decision to close the cheque clearings. This has made the UK one of the last countries still using cheques to migrate to cheque clearing via image. Arguably, with a different industry structure this would have been implemented quicker.

C&CCC's experience is that innovation in cheques has been introduced by:

- Scheme company – for example the current unpaid process
- One Member – for example image fraud detection
- Regulators – for example T246

We do not have detailed insight into the level of innovation provided by the current infrastructure providers though it is clear that some banks are ahead of others in relation to innovation around cheques. It is believed that some innovation has been delayed due to innovation being seen as investment rather than gradual cost reduction in a declining market.

3. Are there are any barriers to effective competition?

The outsourced supply of cheque clearing in Great Britain is managed by two companies. One of which is partly Member owned¹. In a declining market it is therefore unlikely that there will be any new entrants in the market unless there is a fundamental change to that marketplace. That fundamental change could be the introduction of FCM, but new entrants will need convincing that they have the possibility of partaking and winning business in the changed market before committing their investment especially given the declining cheque volumes.

Whilst the existing suppliers have sought synergies between their customers, many of the processes that they operate are bespoke to a particular contract. This increases the cost and risk for PSP of switching between suppliers. The FCM seeks to put in place standard APIs and formats that will reduce some of the costs and risks, but for many PSPs the financial size of these contracts makes the possible savings of switching between suppliers insignificant.

¹ The three Members have in total a 49% share in the company with the remaining 51% being held by another entity.



4. What is the likelihood of entry or expansion in respect of the provision of infrastructure services?

As stated earlier, the contract let by C&CCC for provision of the FCM infrastructure has been awarded to a new (to the UK market) payment system infrastructure provider. This can only increase the confidence of other such suppliers that there is an open competitive market for supply to payment schemes.

C&CCC are very interested in the initiatives generated by the PSRs Forum. We see that the new infrastructure provider together with a state of the art payment mechanism will deliver competition to the payments market.

5. Are there any efficiencies resulting from the present ownership arrangements or from other factors, and how these could be affected if there were greater competition?

C&CCC believes that the current vertical industry structure has resulted in the development of efficient (through shared costs/overheads), robust and resilient cheque and credit systems. There is no evidence that if the industry were to be structured in another way that these similar efficiencies, robust and resilient systems would not have been delivered.

6. How does demand from interbank payment system operators as customers of infrastructure services providers, demand from PSPs as customers of interbank payment system operators, and demand from ultimate end-users of interbank payment systems, affect competition in the provision of infrastructure services related to interbank payment systems?

C&CCC believes that with a larger marketplace and increased demand for infrastructure services, more informed end customers, and the ability for customers and indirect PSPs to migrate easily between suppliers that the FCM would have been delivered earlier. It is hoped that in a properly functioning market such innovation would not have required the intervention of regulators for initiation.

The advent of mobile and other digital payment methods is bringing an unprecedented level of change and challenge to the industry and introducing new entrants for customers to engage with such as Apple Pay. This additional competition creating increased demand for payment services should bring further innovation in collaborative payment markets from the schemes, PSPs and infrastructure providers.

The introduction of a new (independently owned of the PSPs or schemes) service supplier into the UK payments market as part of FCM through an open tender process should help innovation and make the market more responsive to the needs of the customer.



7. What could be the benefits of greater levels of competition in the provision of infrastructure services in interbank payment systems?

Greater levels of competition could result in more world class payment systems being introduced into the UK earlier. However, there needs to be a balance between the robustness and resilience of payment systems and their competitiveness. The UK's payment systems rarely fail to deliver on a central infrastructure level, and this needs to be maintained for consumers to have confidence in the integrity of the systems. Failures that have occurred have been in individual PSPs and it would be expected that informed customers would choose their PSP accordingly.

Despite remaining important for many niche customers, the market for C&CCC services is diminishing and it is therefore unlikely that competing central infrastructure models could work. What we have shown, in FCM, is that competition for that infrastructure provision does work. Further, by the introduction of standard formats, APIs and enabling the portability of sort codes, we believe that competition for the provision of services to PSPs should increase thereby increasing the innovation and customer choice.

In opening up this market, through the implementation of the FCM, C&CCC is mindful that the central infrastructure provider should not have competitive advantage in the provision of other third party services to customers of PSPs by virtue of their central contract. Therefore C&CCC will be investigating different models of accreditation relating to the provision of third party services which are open, fair and transparent.

C&CCC believes that open tendering in a competitive marketplace is fundamental in payment systems. It is seeking through its implementation of the FCM to maintain best practice in this respect and to introduce competition between PSPs and other third party suppliers wherever possible. Through this open approach, it wishes to lead the development of payment systems without the need of regulatory intervention.

Confidentiality

C&CCC is content for this letter to be made available to the public. We will be making them available through our website.

We would, of course, be happy to meet with the PSR to discuss this response.

Yours faithfully

Angela Thomas
Chief Executive Officer of Cheque & Credit Clearing Company Ltd