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Payment Systems Regulator
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Dear Sirs

C&CCC RESPONSE TO FCA CONSULTATION “PAYMENT SYSTEMS REGULATION CALL FOR INPUTS”

The Cheque and Credit Clearing Company (C&CCC) is a membership-based industry body which manages the cheque clearing system in Great Britain. The Company was established in 1985 and from that time until the present day it is proud of its record in:

- providing consumers, via Financial Institutions, with the central payment system services for the exchange and settlement of cheques and credits. These services are underpinned by payments infrastructure including exchange centres, the network for the transfer of electronic cheque data, and an automated settlement system. It also includes a courier service for the return of unpaid cheques to the collecting bank;
- 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 and building societies that offer cheque clearing services, cheque processors, cheque printers and other suppliers, as well as regulators, trade associations and other payment schemes.



Objectives

The overall objectives of the Company are to:-

- maintain the integrity and sustainability of the clearings which have been operating in a declining market for some time,
- respond proactively to changes in the business and regulatory environments;
- facilitate innovation in the clearing process in order to deliver improvement in the customer proposition and, equally important, improvements in industry efficiency
- maintain a trusted centre of excellence, experience and expertise in the cheque and credit clearings.

In December 2013, the C&CCC Board reached an important milestone decision to adopt, as its strategy, a future clearing model which would deliver its overall objectives, as above, utilising an image based processing system, replacing the current, largely paper based, approach.

We see the new image based clearing model, which is a C&CCC Board initiative, providing sustainability for cheques, thereby enabling further innovation to take account of technological developments as they occur and addressing customer requirements so that the cheque will continue to be available for their use for as long as the demand is present.

Since 1985 C&CCC has provided a cheque and credit clearing service to customers who wish to continue to use cheques, whether as the recipient or issuer, and those customers can be confident that the service provided is both safe and efficient.

Payments Systems in the UK

We believe that all payment systems should be regarded as equal in terms of their importance to the full payments industry regardless of volumes or values handled in order to ensure the competitive market can continue to offer customer choice over payment type.

C&CCC is one of the major retail payments schemes in the UK and would expect to be regulated. Designating some, and not all, schemes has the effect of making the non-designated schemes seem less important in the eyes of the industry which introduces a risk that the customers using these non designated services will suffer because resource, such as that required for innovation or integrity, will be directed towards designated schemes which, banks may consider, hold the higher regulatory risk. The approach to designation should ensure a level playing field, avoiding unintended consequences and the opportunity for regulatory arbitrage.



Customers have made it very clear that they want to be able to use cheques as part of the range of payment choices they have. While cheque usage has declined steadily over the past 20 years, a sizeable number of cheque users remain, particularly amongst older consumers, charities and small businesses, and they want to be sure that they can carry on using cheques for as long as they want to. The Company fully understands and supports this requirement. We would like to see C&CCC designated and have its remit extended to the UK, thus including the NI banks and customers within the C&CCC remit. Our recent decision to adopt as our strategy the Future Clearing Model, enabling industrywide image based cheque and credit processing, will secure process efficiencies throughout the UK and enable us to sustain economically viable services and improve the cheque using customers' experience , whether demand continues to decrease, plateau or whether, for any reason, it should increase.

Competition in Payment Systems

There is a place within the payments architecture for collaboration between schemes but we believe primarily that schemes should use their expertise to deliver/ enable innovation which they should be free to research, develop and implement in a competitive manner in line with Member agreement.

Direct collaboration between payment schemes, without third party intervention, is necessary and relevant in areas such as:-

- risk reduction measures in all areas including fraud prevention and settlement
- payment reference data (sort code) control and management
- defining rules and standards to provide interoperability and reach.

Bank of England co-ordination of industry-wide settlement is also a vital strategic area where collaboration is essential.

Collaboration can bring significant benefit where the aim is to improve the integrity or innovation of the UK's payment systems and the resilience of payments infrastructure overall. This is likely to be necessary in only a limited number of instances to ensure there is not excessive concentration on one particular infrastructure without adequate mitigation. Where there is a case, the collaboration should be progressed directly between the relevant individual Scheme companies.

C&CCC believe that there should be competition:

- between the schemes;
- within the schemes between Financial Institutions in the way that they offer services to the customer; and,
- within the schemes between the outsourced scheme infrastructure providers.



Ownership

The company would welcome a review of the different ownership models currently employed by the payment schemes in order to understand if there are benefits to be gained by moving to a different model.

The Company is owned by the System Members. The company has no assets so there is no intrinsic value in the single share that all Members of the System are required to acquire upon joining but all benefit from the option to appoint a non-executive 'Member' Board Director.

A list of our current Members is available on our website. www.chequeandcredit.co.uk

As part of the Future Clearing Model, a review of the membership criteria will take place, as a move to an image based model has the opportunity to enable new providers of infrastructure to enter the market (provided that they do not adversely impact stability, integrity, security and compliance with scheme rules and standards) with lower investment, and thereby increasing choice for financial institutions. It is anticipated that this will enable more banks and building societies to become Members and, therefore, under the current ownership model, owners of the scheme.

Governance

The C&CCC Board is the decision making body for the Company and is made up predominantly of non executive Directors who are directly employed and appointed by the Scheme Members, i.e the shareholding owners. These Member Directors have very clear and frequent conflicts of interest (which they declare) as they balance what they believe to be a correct course of action to meet their fiduciary duties to the Company, with the legitimate concerns, of their own Member organisation and employer. Under our corporate governance model the Member Directors currently declare a number of additional conflicts of interest including where they undertake multiple directorships across payment schemes and where they are shareholders in infrastructure providers.

The Company appointed an independent Chairman, in 2004, before there was a regulatory drive to do so, to assist with mitigating Member Director conflict of interest issues and we have recently added two new independent non-executive Directors whose role is to represent public interest. The Member Directors can provide valuable experience and industry knowledge to the C&CCC Board.

Major decisions have been made by unanimity, or near unanimous consensus, which means change proceeds at the pace of the slowest Member or not at all. Historically, the Board has had difficulty in driving innovation where it has not been seen to be in the interests of all the owning Member organisations represented by Member Directors. The appointment of independent directors will help to ensure that the customer focus is maintained whilst formulating and driving innovative developments, avoiding Members' internal concerns which may have hindered progress in the past.



Access

The C&CCC has 11 settlement Members and participation by other financial institutions in the cheque clearing is achieved via these settlement Members. The C&CCC enables Members to have direct access to its central processing infrastructure and the scheme. It allows Members to provide the services to other financial institutions, such as agency banks, on a commercial basis. The provision of agency bank access is a matter for individual Members and is not mandated by the scheme, i.e. a settlement member can choose whether or not to offer such a service. The Future Clearing Model will make it easier for challenger and agency banks to switch between settlement member providers if they wish to remain as agency banks or, alternatively, to join as a settlement Member in the same way as they can in the electronic schemes because the model removes the total reliance the paper clearing has on sort code lead pairs to sort paper.

There is currently only one C&CCC membership category, i.e. a full settlement member. Access to the clearings is a key element of the Future Clearing Model which is likely to be achieved by introducing a wider range of distinct membership categories enabling challenger and agency banks to participate in the clearing at their preferred level. Proportionate criteria for such membership will be set at a different level to that required for settlement membership to protect the integrity of the clearing system.

The proposed introduction of a prefunded, capped settlement model, within the Future Clearing Model, means the provision of settlement services will become easier for banks to manage by moving from a 'survivor pays' to a 'defaulter pays' model in line with the changes the electronic schemes are implementing. There is, therefore, the possibility that more settlement members will enter the market or that some agency banks will choose to become settlement members.

Infrastructure

Within our current model, we have two types of infrastructure, Member Processing and Central Processing, further information on each is available on our website at www.chequeandcredit.co.uk.

In terms of Member Processing, since the first outsourcing of a cheque clearing operation in 1992 the infrastructure model has evolved in response to member requirements which have, wherever possible, been acknowledged and accommodated. Even if a Member uses a common outsourcer as their infrastructure provider their actual solutions are likely to be very different. This can also cause further conflicts of interest for Member Directors, whereby a particular change can impact disproportionately on different Members, which can result in difficulties agreeing a solution for any new innovation.



In terms of Central Processing, some elements of C&CCC infrastructure, such as the IBDE network, settlement system, unpaid cheques courier service and exchange centres, are managed by the Company but have been outsourced, within the rules of the Company's supplier policy, through a process of competitive tendering. There is no single infrastructure supplier to the Company.

Since 1990 cheque volumes have declined steadily and this has had an impact on the appetite for reviewing the current infrastructure model. It has become complex with multiple interested parties which has caused difficulties for the Company. For example, a recent tender exercise for improvements in processing efficiency did not attract potential credible bidders, perhaps due to existing or potential relationships with Scheme Members and outsourced contractors. The conflicting interests of the various parties within the current infrastructure model, therefore, had a direct impact on the Company's ability to innovate.

The main cheque processing infrastructure is managed on behalf of Scheme Members by two outsourced suppliers:-

- HPES – which holds the processing contract for RBS Group; and,
- iPSL and UPSL – which hold all other Members processing contracts.

In addition the Company sources a number of services from UK Payments Administration Limited.

The Future Clearing Model offers an opportunity for C&CCC to review the extent of the infrastructure that it manages and work is underway to consider:

- comparative scheme infrastructure models;
- the advantages and disadvantages of each;
- recommendations for the preferred model for the C&CCC; and
- proposals for how we could transition to the preferred model through the implementation of the new Future Clearing Model.

The UK payments system and the economy it serves could benefit from increased numbers of infrastructure suppliers. This offers increased competition and potentially innovation whilst providing contingency and resilience. It would be necessary for there to be some commonality on interface requirements. Increased commonality of standards could improve access for challenger and agency banks and their ability to switch between suppliers and schemes at minimal cost. For example, the Future Clearing Model is considering utilising a common messaging format (ISO20022) which will bring many of these benefits.



Innovation

Cheque clearing demands collectively driven innovation for the base clearing service to ensure customers can benefit from a common core service. Banks, however, are free to offer additional services for the benefit of their customers, in the competitive space over and above the core Scheme clearing service.

The schemes need to move forward by consensus to ensure a common customer experience and, to a large extent, unanimity which takes time to build. There has also been a multiplicity of, at times, conflicting regulatory pressures over the past 15 years which have both absorbed change management and investment capacity and resulted in the industry becoming risk averse in taking the initiative itself. More effective dialogue is needed between regulators and the schemes to ensure that innovatory scheme proposals do not conflict with potential regulatory issues.

Within these constraints, the C&CCC has a good record of delivering innovation albeit more recently only with a direct regulatory driver to mandate that change, e.g. the T+2-4-6 customer promise and the Cheque Redirection Service within Account Switching, but this is always set against a declining market and competing Member priorities in other payment schemes, e.g. mobile payments and FPS. To this extent the Company views regulatory intervention as positive where it helps Members resolve competing priorities. However, we believe regulation should define the required outcomes, leaving Schemes and competing Financial Institutions to determine how best to achieve that outcome.

Innovation may be iterative or result in a step change. Transformational change is only achievable if constraints such as the C&CCC's current heavy reliance on sort code lead pairs for sorting cheque paper, reliance on paper and potential barriers caused by, what may be seen as, prohibitive set up costs are removed. We believe the Future Clearing Model will address these issues, not only achieving significant savings now, but opening the way to further innovation and increased competition at all levels.

Summary

The Company would welcome a competitive and regulatory environment where consumers and businesses continue to benefit from an efficient cheque clearing system, providing the option to continue using cheques for as long as they wish. Our current experience during discussion on the Future Clearing Model suggests that some Members have a preference for projects to be mandated by a regulator to avoid internal budgetary and prioritisation issues. We need a robust and effective payments architecture and governance structure underpinned by the highest quality expertise. We believe that the expertise on cheque and credit clearings is found mainly within the C&CCC.



Any new payments architecture, scheme ownership and governance arrangements must support the Company in its efforts to improve cheque processing through its commitment to an industry wide image based cheque clearing in order to sustain cheques for as long as customers want to use them.

We would be happy to meet to discuss this response as we seek to deliver an excellent cheque clearing service for as long as it is required by customers.

Yours faithfully

Angela Thomas,
Managing Director
Cheque & Credit Clearing Company Ltd