

LLOYDS
BANKING
GROUP



LLOYDS BANKING GROUP PLC
Payments Strategy Forum

Blueprint for the Future of UK Payments
consultation paper.

22nd September 2017

LLOYDS BANKING GROUP PLC

Response to Payments Strategy Forum – Blueprint for the Future of UK Payments: a consultation paper.

INTRODUCTORY REMARKS

1. Lloyds Banking Group (LBG) is committed to Helping Britain Prosper through being the Best Bank for Customers. Having effective and efficient payment systems is critical in achieving these goals and for the wellbeing of the UK economy as a whole. LBG therefore has a strong interest in ensuring that the UK's payment systems are highly robust, reliable, and secure, while providing a platform to develop services for consumers and businesses. LBG believes that the UK payment systems are world-leading and strongly supports the PSF's work to deliver further improvements.
2. Delivering better outcomes for users of payment systems is rightly at the core of the PSF Blueprint, arising either directly from the initiatives proposed in the Blueprint or through laying the foundation and creating the environment to deliver enhanced competition and innovation through the end to end payments value chain. LBG therefore welcomes many aspects of the Blueprint and will continue to work with and support the PSF and New Payment Systems Operator (NPSO) as the Blueprint transitions through from design to delivery.
3. The PSF has done excellent work in the time available and has successfully brought together a wide range of stakeholders across the industry representing traditional banks, new entrants, fin-techs and representatives of end user groups to speak with one voice and to lay down an ambitious Blueprint for the development of UK payments.
4. In responding to the PSF consultation, we have structured our response into two sections: a separate response to the questions set out in the questionnaire; and a summary of our overarching comments which we have grouped into the following broad categories set out below.
5. **Aspects of the Blueprint that LBG strongly agrees with because they are so obviously right for customers and the UK**
 - The overall architectural approach of a single push payment layer built on ISO20022 and alignment with Open Banking and PSD2. Critical to achieving the overall architectural approach will be ensuring the adoption of ISO20022 is interoperable across different payment types. We also feel it is important to review the downstream impacts of migrating direct debits over to a push payment mechanism so that they are fully understood.
 - Simplification of the various infrastructure layers will enable access, competition and innovation better than the alternative of upgrading the current Bacs and FPS infrastructure.
 - The introduction of End User Need Solutions - Request to Pay, Assurance Data and Enhanced Data which will be designed and delivered in a way that offers accessibility

control and confidence in payments to all. Whilst LBG supports these developments, it is critical that the NPSO ensures that these solutions leverage the industry wide investment being made for Open Banking and PSD2 to avoid “throw away” investment. It is encouraging to note the intent to prevent any exclusion is at the forefront when considering overall design, marketing and risk levels. LBG strongly supports the intent to avoid exclusion because it will be critical to ensure that all customers can participate fully and enjoy the benefits of these new services. We also welcome the commitment to develop robust liability models for both Request to Pay and Enhanced Data which will be critical in building trust in these services and for the protection of customers.

- To engender user trust in safe payments through collaboration to prevent financial crime including consumer education measures to help prevent vulnerability and susceptibility to fraud, scams and other types of financial crime.

6. New Payments Architecture – a simpler and accessible infrastructure

- The New Payments Architecture is a radical change, the direction of which we support, however the PSF must ensure that there is strong emphasis on ensuring stability and customer experience so that customers benefit from a world class payment experience regardless of the access point they use to initiate their instruction and which payment journey their instructions follows.
- When all factors are taken into consideration, we support a centralised infrastructure model where the routing, settlement risk and settlement processing is managed centrally as a centralised approach is proven in reliability and efficiency whilst providing a clear and manageable risk model which supports the prevention and mitigation of systemic risk. It is also likely to be more cost effective and will potentially require less additional development to support the adoption of ISO20022 requirements.
- At the same time as the PSF will be finalising the Blueprint, the UK will be implementing cheque imaging based on a new central infrastructure that utilises modern international standards, is scalable and appears to have the capability to support all current UK payment services and the overlay services proposed in the PSF strategy. We would therefore encourage the NPSO to investigate whether or not the significant investment in this infrastructure can be leveraged to provide the core of the New Payments Architecture.
- However, if we want UK payments systems to make the step change from world-leading to world class, a leap would be required to move towards a more distributed system. Whilst there isn't currently a live distributed model of this scale in operation anywhere in the world., LBG believes a distributed model would drive competition in a completely different way and the end user would almost certainly benefit from a wider range of overlay services, many of which will not have been thought of yet. These potential benefits would need to be carefully assessed by the NPSO against the risk and cost concerns.
- With this in mind, LBG could therefore also support a distributed model provided this was built out from the foundations laid down for Open Banking and PSD2.

- We note that the Blueprint is does not mention the use of the NPA for payments that originate overseas. Overseas and international payments represent an important service for many UK consumers and business and these payments also involve specific risks that the NPA must consider and look to mitigate. Accordingly the final design of the NPA must ensure 1) that such payments can be flagged for sanctions checking, etc. and 2) that under ISO20022 message standards there is sufficient carriage data so that full remitter and intermediary bank details are carried for sanctions checking purposes.

7. Implementation Plan and approach

- We are supportive of the transition approach which defines clear phasing of activities and subsequent closure of existing scheme infrastructure and responsibilities. Whilst it is a given that each transition state should clearly demonstrate the successful launch and migration to NPA, it would be beneficial to ensure that the benefits of scheme closure are clearly visible at each transition state. The transitional arrangements and sunset period for the existing infrastructure need to strike a careful balance between big bang, moving at the pace of the slowest and creating customer detriment.
- Transition state 2 in the paper covers migration of all bulk payments (FPS & Bacs) which we believe is high risk given the likely significant complexities of Bacs migration. We would therefore recommend that the NPSO gives further consideration to changing the sequence of transition states so that the migration of Bacs should not commence until all FPS transactions have migrated. This would create a new additional transition state which would follow after the Image Clearing System in Transition State 3. Bacs migration should also ensure that Bacs credits are transitioned ahead of and separately to Direct Debits. We would see **the lowest risk order of migration as follows:**

Transition State 1	FPS – in our opinion given volumes involved we would recommend commencing with SIPs.
Transition State 2	Bacs Credits
Transition State 3	Image Clearing System
Transition State 4	Bacs Direct Debits
Transition State 5	Close down of legacy services completed

- We recommend that the PSF should also look at and not rule out a co-existence where Direct Debits remain as a pull payment. Direct Debits work really well for the vast majority of users today and care needs to be taken to ensure that the changes made by the introduction of the NPA do not undermine confidence in the existing mechanisms. A further and more detailed understanding would be useful of the potential implications and costs for businesses and Direct Debit originators of a move to a push only model for the payments infrastructure.
- The final implementation approach should also consider the impact of major regulatory and market driven changes as well as identifying other projects and initiatives that may need to be delayed or cancelled to free up resources and capacity to implement the Blueprint safely. It is critical to identify any mandatory changes that underpin the

successful delivery of the blueprint. In finalising the approach it would also be useful to understand the initiatives that are prioritised as providing an enhanced user experience for customers.

8. Cost Benefit Analysis for the NPA

We have a number of recommendations for the NPSO to consider in finalising the business case that will be required to deliver the NPA.

- We should ensure that there is a full understanding on the cost of change for all end users. Larger corporates, specifically those collecting or sending payments on a large scale may incur significant cost in making changes to their systems and notifying clients and these costs, once known should be factored into any benefits case. By way of example, we are aware that the migration to SEPA Direct Debits in Europe was costly to corporates not only in system changes, but also in terms of notifying clients and setting up the new mandates with them.
- More clarity is required to show how the benefits and costs of the NPA align and will be distributed to ensure that the impacts for each component are clearly understood. Overall, whilst it is useful to demonstrate that total benefits outweigh the costs, it is equally important to show if the total position results in an imbalance with costs being incurred in a different area to where the benefits will be realised when this is broken down further.

9. NPA Commercial Approach and Economic Model

- We acknowledge that more work needs to be undertaken to land an appropriate economic model to provide funding for the implementation of the Blueprint for what will be a significant change programme for the industry costing billions of pounds to implement and affecting all stakeholders in the system.
- We hope that the PSR will provide support to the PSF and the NPSO to finalise economically sound principles on how to allocate costs (build costs and running costs) of the system. The competition framework set out in the Blueprint provides a good foundation for consideration; we would suggest that further analysis and or market testing may be helpful in order to determine which type of competition each service falls into, before determining the future procurement model. For example, NPSO could consider seeking input from vendors on whether switching and settlement could be carried out efficiently and securely by multiple vendors, rather than a single vendor as today.

10. Improving Trust in payments

- We acknowledge and are supportive of the work that has been undertaken to date to improve industry collaboration to develop the Payments Transaction Data Sharing and KYC Data Sharing solutions and believe that these can produce good customer outcomes by keeping payments safe and secure.

- As the PSF hands over to other industry bodies we hope that all stakeholders, including cards companies, regulators and government agencies, continue to engage and build upon the work to date in order to develop a comprehensive and holistic approach to implementation in order to gain maximum value from the data sharing and data analytics solutions. The PSR's support will be helpful in navigating the regulatory requirements to ensure that payments transaction data can be shared, pooled and interrogated in order to protect customers. We recommend that work be undertaken in parallel by industry to develop a cohesive and clearly articulated data sharing strategy that will overlay the blueprint.
- The owners of the post-PSF solution delivery activity (we understand and are supportive of the approach made to UK Finance/FFA UK) should continue to collaborate and build on the positive work to date in order to ensure that the design, development and testing of their deliverables are mutually consistent and supportive of the overall objective to reduce customer detriment and provide an environment for a more effective and innovative payment services market place.
- The PSF and NPSO must ensure that all the proposed PSF solutions are aligned to ensure they are supporting the wider customer serving environment. This alignment must be satisfied across solutions that equally promote the development and delivery of commercial products and services (e.g. cross industry provision of frameworks, standards, and infrastructure), as well as across the end to end fulfilment journey (e.g. customer facing services, payment execution services, and financial crime prevention controls).

11. Finally, LBG has identified some key critical success factors, risks and dependencies that the NPSO will need to address as part of the design and delivery phases of the Blueprint

Critical Success Factors

It will be important for the NPSO to agree on a number of assumptions during the mobilisation of the PSF Blueprint programme to ensure the full range of industry stakeholders have as much clarity on key issues from the outset as follows:

- Legacy infrastructure will have an agreed end date for closure set to ensure and encourage migration to NPA. Some proposals may need to be mandated to drive implementation and universal acceptance: the PSF and NPSO may need to engage with the PSR and other relevant regulators if they identify undue delay in delivering benefits to consumers and businesses.
- Customer protections that are in place today should continue or be replaced with alternatives that deliver better outcomes for consumers and businesses.
- Existing industry initiatives must continue to enhance the availability of sort codes for PSP's, better access to settlement account options by the Bank of England, enabling and developing aggregator models to broaden the range of connectivity options available to PSP's and clarifying liability models for indirect access.

- Access for agency banks and non-bank financial Institutions will be maintained or enhanced under the NPA.
- Maintaining resilience and security of UK payment systems at all times will take precedence over other design and transition considerations.
- Some of the end user need Solutions, for example Confirmation of Payee, would benefit from 100% ubiquity to ensure that real tangible benefits to all customers are achieved. In an ideal world we would want to completely remove all misdirected payments.

12. Risks

The key risks that the NPSO will need to mitigate and manage through the transition phases of the PSF Blueprint are inevitable given the extent of the change proposed to move UK payments systems from world-leading to deliver truly world class services for consumers, business and the UK as a whole.

- £8.2 trillion payments are processed each year through the existing infrastructure and by 2025 all will be processed on new infrastructure. The UK economy is dependent on a resilient and secure payments infrastructure, which must continue on the NPA.
- The need for security is critical as the payment landscape evolves – we must ensure users are protected and continue to hold trust in UK payment systems and the UK banking market.
- Speed of payment processing: the UK is a leader in the development of payment products such as Faster Payments. Image Clearing System (ICS) will deliver greater speed cheque clearing removing ‘firebreaks’ available during multi-day clearing. Expectations on all forms of payments to be quicker leads to increased operational risks with impacts on fraud and competition.
- PSD2 & Open Banking are the enablers of choice, opening up the options available to consumers and businesses by creating competitive pressure. With the PSR driving scheme consolidation and easing the access channels (and reducing costs) for organisations to join, a new range of providers will become available to the consumer. An influx of new entrants can increase risk.
- The industry has finite capacity to change and therefore effective sequencing and prioritisation with other regulatory initiatives will be critical.

13. Dependencies

The Key dependencies that the NPSO will have to manage during the implementation of the PSF Blueprint will include.

- It will be important for the NPSO to manage the dependencies between transitioning to the PSF Blueprint and the implementation of Open Banking, PSD2, structural reform and the Bank of England new RTGS system.

- In order to ensure the successful delivery of the Blueprint for the Future of UK Payments, it is especially important for the NPSO to receive robust support (in terms of expertise, capability and authority to act) and ongoing engagement that it will inevitably require by continuing to work closely with the industry, the PSR, other regulators and the Government.
- Although the Blueprint is silent on card initiatives it will be important that the NPSO considers dependencies with card based products and services, especially when considering the payments landscape through the eyes of consumers and businesses.

14. Conclusion

- In conclusion, the PSF Blueprint sets out an ambitious programme of work designed to transform the UK's world-leading payment systems into a world class service that will benefit UK consumers, businesses and the UK economy as a whole. The outcome envisaged by the Blueprint is therefore closely aligned to the LBG strategy to Help Britain Prosper by being the Best Bank for Customers, and therefore LBG strongly supports the PSF completing the design phase of the Blueprint so that it can be passed to the NPSO to begin implementation.
- It will be important for the NPSO to manage carefully the sequencing and prioritisation of the PSF Blueprint with other regulatory initiatives, to secure the necessary resources and funding to ensure delivery and to manage and mitigate the risks associated with a change of the magnitude proposed in the PSF Blueprint to ensure continuity of the £8.2 trillion payments processed each year through the existing infrastructure. The UK economy is dependent on a resilient and secure payments infrastructure and this must remain paramount.

PAYMENT STRATEGY FORUM CONSULTATION QUESTIONS

Contained within LBG Question Response Template