HOUSE OF COMMONS

Treasury Committee

Oral evidence: The Payment Systems Regulator, HC 843

Wednesday 26 November 2014

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Watch the meeting

Members present: Mr Andrew Tyrie (Chair); Rushanara Ali, Steve Baker, Mark Garnier, Mike Kane, Teresa Pearce, Alok Sharma, John Thurso

Questions 1-70

Examination of Witness

Witness: **Hannah Nixon**, Managing Director, Payment Systems Regulator, gave evidence.

Q1 Chair: Thank you very much for coming to give evidence to us this afternoon. I think this is your first appearance before this Committee.

Hannah Nixon: It is.

Chair: And, I suspect, your first appearance before any Committee in your new capacity.

Hannah Nixon: Yes, it is.

Chair: You know the old quote from "The Wealth of Nations" that, "People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public"? That is pretty what much we discovered the Payments Council was engaged in: a conspiracy by a cartel to deprive the public of cheques, which the public then told us, noisily, that they wanted to keep. Furthermore we discovered that this would have damaged charities as well, considerably. Have you had any time at all in your new role to think about whether and, if so, how you might safeguard paper-based transactions?

Hannah Nixon: Yes, and it is a real focus for us. It is the consumer and the service users who are important here and we are committed to ensuring that while there is a demand for the cheques, they will continue.

Chair: So people should feel fully reassured about your commitment to paper-based transactions?

Hannah Nixon: Yes, absolutely. As I say, our focus is on making sure these payment systems work for the consumer and all service users—charities, small businesses and so on—and while there is a demand for that functionality of having a paper-based system, we are committed to ensuring it remains.

Chair: Good. I think that that is a very important initial reassurance for this Committee to have. It was that investigation that led us to look much more deeply into the way the Payments Council was operating and, in the end, decide that we could not carry on as a cartel. We are grateful to the Government for coming forward with legislation to do something about it.

Q2 Alok Sharma: Could I just start by asking this: you have been in place for four months, I think, in your role?

Hannah Nixon: Yes.

Alok Sharma: Could you tell us what you regard as your key achievement so far? At the end of your first year, what do you think you would regard as success in your role?

Hannah Nixon: The focus at the moment is very much on making sure we have the people, the processes and the policies so we are up and running on day one. We take up our powers on 1 April next year and the focus therefore is getting those three things in place so that we can be an effective regulator right from day one. As you are probably aware, 10 days ago we set out our proposals for how we intend to regulate so we have a firm and strong policy proposal that will be in force from day one. I would want, at the end of my first year, which will be towards the end of the summer next year, to have those things implemented and to start to see some real changes in behaviour of the payment systems so that access is easier to them and consumers start to feel those benefits.

Q3 Alok Sharma: Okay. You talked about recruiting people. How far along are you? Are you finding people with the right skills? Where are they coming from? Are you able to offer them the right level of compensation to get them from, I guess, the private sector?

Hannah Nixon: As you would expect, we are currently actively recruiting and we are building that team. We have a staff at the moment of 40, 23 of whom are permanent. The other 17 are on contracts. We have another nine offers that have been accepted so those people will be coming in shortly. I have to say, I have been really encouraged and pleased by the level of interest and the quality of people we have been able to attract and I think that just reflects that there is a—

Q4 Alok Sharma: Can I ask you where they are coming from?

Hannah Nixon: We are recruiting a mixed skill-set of people, so we are looking for economists, policy people, lawyers, payment specialists and so on and, as a result, people are coming from a range of backgrounds. We have people who have come in from the payments industry but we have a lot of people who have come in from other regulators, from law firms, consultancies and so on.

Alok Sharma: Basically what you are telling us is that recruitment is on track and you think you are going to have a really good team together over the next few months.

Hannah Nixon: Yes.

Q5 Alok Sharma: You talked about experience and getting people who have experience in the payment system. You obviously used to work for a bank but do you have any particular expertise yourself in payment systems?

Hannah Nixon: No, I do not come with a payments background. As you say, I did start my career in financial services but most of my background is in economic regulation. I have a strong background in economic regulation but not in payments.

Q6 Alok Sharma: What are you doing to get yourself up to scratch when it comes to payment systems, since that is the area that you are responsible for?

Hannah Nixon: Absolutely. One of the things that I have been really keen to do in my first few months, and indeed will continue doing on an ongoing basis, is to engage with the industry in a wider sense and all parties who are interested in this sector in the widest sense. We have been proactively reaching out, obviously to the industry but also to people who want to break into the industry, either as new financial institutions or as innovators in the space; also to consumers and their representatives, to charities and to businesses that use payment systems.

Q7 Alok Sharma: Can I just probe a little bit deeper on the payment systems expertise? How many people are you recruiting? You said you have 40 so far and you are taking on another nine so you are going to end up with around 50 people. If you just break down the level of expertise that each of these has, how many of those would you consider to be experts in payment systems, for instance?

Hannah Nixon: We have about five people who are payments experts and I think it is important that we balance that by getting external input where we need to. Payment systems themselves and the payment sector are very keen to engage with us, and that does help us to understand the issues and flesh those out, so it is important that we are an informed buyer of that information so we can respond to it appropriately and I think having that level of internal resource enables us to do that.

Q8 Alok Sharma: Just turning to your set-up within the FCA, are you satisfied with the level of independence you have from the FCA? Do you think you need to have further independence or are you too closely entwined with the FCA?

Hannah Nixon: We are a subsidiary of the FCA and, in many ways, I think that gives us the best of both worlds because we are an independent regulator: we have our own board, we have our own objectives, on legal powers and so on, and that enables us to focus very clearly and get on and do our job. However, being a subsidiary of the FCA also enables us to work closely in those areas where our objectives are touching and that has to be in the best interests of consumers. We are able to leverage the resource of the FCA where that makes sense. So in many ways, I think we have the best of both worlds, but we have not even started regulating yet and I think the important thing is that, if we see that there are issues or tensions that that raises, we will obviously make sure that we raise them through the appropriate channels.

Q9 Alok Sharma: If you look at the make-up of the board, it is quite heavily stacked with people who are already doing something else for the FCA. Do you not think you need to have more independence on there?

Hannah Nixon: As you say, there are two non-executives who sit on both the FCA board and the PSR board, the Chair is the same, and Martin Wheatley is our Deputy Chair so they are people who are involved in the FCA. They do come at this, though, with the PSR hat on, if you like, and so there is that independence. I am satisfied it is working at the moment but I think this is one of those things we just need to keep under review to say, "Is this working?" and, if not, then clearly we need to change things.

Q10 Alok Sharma: But even your budget is coming through the FCA. Do you regard it as that of a body that is effectively independent?

Hannah Nixon: We are a subsidiary of the FCA and therefore the budget sign-off does go through that process. Now, that has worked so far but it is really early days and we obviously need to just keep monitoring that. However, that has worked and what is important for me is that we are able to operate in a way that means we can really focus on our duties and really make a difference for consumers and so far, as I say, I think we have the best of both worlds.

Q11 Alok Sharma: If you found that you were not getting the practical level of independence in your role, what would you do? Who would you then talk to?

Hannah Nixon: It would depend what the issue was but when I speak to our Chairman we discuss the make-up of the board, when we review that and whether we need to have different expertise on that. If it was a more fundamental issue then—

Alok Sharma: Your Chairman is the Chairman of the FCA.

Hannah Nixon: Indeed. If there are more fundamental issues, then I have the ability to raise that through the appropriate channels in Treasury.

Q12 Alok Sharma: The final question is that the FCA, the PRA and the Bank of England all have powers of veto over what you are doing. Does this not curtail significantly your powers and demonstrate that perhaps you are not quite as independent as you are telling us?

Hannah Nixon: I think the fact that those organisations have vetoes is really important, actually. It underlines for me what we are fundamentally trying to achieve. The PSR's role is about promoting competition and innovation in payment systems. We need to do that in the interests of consumers. Now, it is clearly not in the interest of consumers that we do anything to undermine the reliability or integrity of the system, responsibility for which sits with the Bank of England. It is also really important for consumers that we do not undermine the objectives of the FCA or the PRA either and so I think the fact that they have those vetoes just underlines that, when we are developing our policies, we need to speak to those organisations to make sure that we are not inadvertently jeopardising their objectives.

Q13 Chair: Why would you go to the Treasury if you are not happy?

Hannah Nixon: The Treasury set us up through the Bill and is our link department. Treasury is one route; bringing it back in through Parliament is the other route.

Chair: Treasury is not your link to Parliament; this Committee is your link to Parliament.

Hannah Nixon: Yes, indeed. Yes.

Q14 Chair: I just think there is some thinking that needs doing here because your independence is prettily heavily circumscribed. You have been given a set of objectives that are not the objectives of the FCA but are different.

Hannah Nixon: Yes.

Chair: There is an overlap but they are different and very distinct. Quite a bit of thought is going to be need to be done the first time that there is a difference of view about priorities between how you think the payment system should be run and any specific regulatory objective the FCA may have for the banking industry at the time. I would be grateful if you would give some thought to that and also make sure that, in a timely manner, this Committee is informed if you think there are difficulties; if necessary, initially in confidence.

Hannah Nixon: Yes. I can assure you that we will keep those issues under review and, if problems do arise, that we will raise them in a timely manner.

Q15 Mike Kane: I met Tony Lloyd yesterday, the Police and Crime Commissioner for Greater Manchester, and he was saying that the largest rise in crime is either in cyber-crime or payments through payment systems. Your vision states it has to be "reliable, secure, stable and predictable". He struggles to get officers who can be trained in this and to pay them an adequate wage to investigate this type of crime: they quickly move on from the force because they can get better offers, basically, in the private sector. I think it was Martin Arnold who said in *The Financial Times* a few weeks ago that JP Morgan are employing 1,000 people who they are training up and employing to help with this. You are going to have a staff of 50 people. Do you expect that you will be able to enhance the resistance of payment systems?

Hannah Nixon: It is crucial to the consumer that they have confidence in the security and reliability of their payment systems and this is where we work with the Bank to make sure we do not do anything to undermine that. We also work with the FCA, who are doing a lot of work at the moment on cyber-security and the functionality that banks and payment systems need to put in place. I think the question for the PSR is to understand what that functionality is and making sure that payment systems are building that in as they develop their systems.

Q16 Mike Kane: Yes. As Tony said, only the dumbest criminals now actually do bank heists; it is much better to do it electronically. The Bank of England obviously has oversight for BACS, CHAPS and the Faster Payment services. Will you have any responsibility for those areas as well?

Hannah Nixon: We are expecting Treasury to designate those three schemes, BACS, CHAPS and Faster Payments, among others, for us to regulate. They are out to consultation on that now. We are expecting those to fall within our remit and therefore promoting innovation and competition in those schemes and others will be a priority.

Q17 Mike Kane: What about the sort of international banking clubs, VISA, MasterCard and so on?

Hannah Nixon: VISA and MasterCard, again, we are expecting those to be designated and fall within our remit.

Q18 Mike Kane: Finally, the terrorism aspect and the cyber-security sides of this: the most vulnerable part of our financial system is obviously financial payment systems. There is a war going on out there; our systems are being continually tested. That is the quickest way you bring an economy to its knees; before you know it, we are living up trees again. In your opinion, how dangerous is the threat to those systems? Can you make them reliable, secure and predictable?

Hannah Nixon: For security of the system, the responsibility lies with the Bank. It is important we work with them so that nothing we do in terms of promoting innovation and competition inadvertently undermines that. Cyber-security is a paramount part of that, which is where our work with the FCA is important.

Q19 Chair: Are you a joint regulator with the Bank of England on resilience?

Hannah Nixon: I think the responsibilities are reasonably clear-cut in that the resilience responsibility lies with the Bank. Our role is to make sure that we promote innovation and competition in those systems in a way that benefits service users, which clearly means not undermining that resilience and integrity, but the responsibility for resilience and integrity has not changed. It has not moved from the Bank.

Q20 Chair: Your "vision", as it is called, states that the payments systems should be "reliable, stable, secure and predictable".

Hannah Nixon: Indeed.

Chair: That amounts to resilience, does it not?

Hannah Nixon: Yes, it does and I think that just underlines the point that when we go about promoting innovation and competition, we cannot do that at the expense of the reliability and integrity of the system. To do so would not be in the interests of consumers or users.

Q21 Chair: The point that I am trying to get to is that clearly the Bank has a particular interest in making sure that resolution is made as straightforward as possible, for example. Their objectives may not exactly coincide with your objectives. As I just set out, there may be a gap between those two and I am trying to probe what you are going to do to handle a situation like that.

Hannah Nixon: I am not sure I fully understand. Where do you see the gap?

Chair: Reliability, security, stability and predictability may lead you to want to do things that the Bank of England has decided are not appropriate because it wants to secure resolution of a bank above all else and it wants a payment system that is targeted at that. There is likely to be a similarity of objective there, but it will not be an identity.

Hannah Nixon: Yes, and I think that is just an area where we would need to work together to understand the pros and cons of the different positions.

Chair: I can see that when the first substantive issues come around, there are going to be some interesting conversations.

Q22 John Thurso: Competition is one of your key reasons for coming into existence. You have a statutory objective to promote competition in the payments industry. What will effective competition look like?

Hannah Nixon: I think that is a really good question. I look at this on three different levels. Well-functioning, open payment systems are a crucial part of the jigsaw in promoting retail banking competition and so we absolutely want to make sure that payment systems are facilitating that competition at the retail end.

There is then a second question: to what extent do we want to see competition between payment systems themselves, so between Faster Payments, CHAPS, BACS and between them and the card schemes, for example? I think that is an open question and work is ongoing at the moment to look at exactly how much competition we want between those. Do we want fewer schemes? Do we want more schemes?

Then there is the infrastructure, all the pipes and wires that sit behind that and allow the money to move, and again there is a question. Do we want competition in that space, either between competing infrastructures or for the market? There are different models out there. Some people have put forward a model of a really big central utility. That would take away the competition in the market but it is certainly a model that has some merits. There are other models, which also have merits, around opening this whole thing up and getting competing infrastructure. That is why we have said we are going to launch our market review, to look at this really carefully to make sure we have the right answer for the UK.

Q23 John Thurso: Can we disaggregate those two areas? You are right, they are both extremely important. You have the plumbing, as it were, and you have the more immediate systems. We can take those first: who does what, as it were. What will you set, as the regulator, as your prime objective—and possibly even your prime key performance indicators—in terms of achieving competition in that part of the payment system?

Hannah Nixon: We are developing a series of metrics and I expect them to be quantitative and qualitative, but this is a work in progress in terms of how we are going to measure success. It is really important we are able to measure and capture that. I expect it to be things like the ease of access to the payment systems: how many people who want direct access to the systems are able to achieve it. How long is it taking them? What is their experience on the journey of gaining access? We would also look at the indirect access to the schemes. Regarding people who choose to have indirect access rather that direct access or who cannot get direct access, what is their experience? How many people are willing to offer them a sponsor into that market? These are all things that we will do to measure success.

We put out a consultation a week or so ago and one of the key planks of that is really improving access, breaking open access so that it is much easier, there are more proportionate terms for direct access and a much better customer journey. Then on the indirect access there are some things we are doing immediately to improve transparency in that market. We have also said we are going to do a market review to really understand the dynamics there because out of 30 potential sponsor banks, only four, at the moment, choose to offer sponsor services.

Q24 John Thurso: The great complaint we always get from challengers, both on the Banking Commission and in this Committee, is that it is difficult and expensive to get into the system so, for me, one of the key indicators of how you are doing is whether the challengers are telling me it is easier to get in.

Hannah Nixon: Yes.

John Thurso: Is that the sort of thing you will be looking at?

Hannah Nixon: Absolutely. We have talked to a number of challenger banks and, as you would expect, we have heard exactly those concerns—it is hard to understand what you need to do; it is onerous and expensive to put the systems in place—and our proposals are very much focused at making that easier so the access terms are proportionate. It is not a case of one size fits all because big banks would put very different stresses and strains on the systems from a small challenger bank. The whole process just needs to be more transparent and the schemes need to be better at bringing new people on board. We are aware of 50-odd people who are trying to get direct access to schemes and we need to make sure that journey is easier for them.

Q25 John Thurso: Have you started an analysis of why they cannot get on to it, as a start point for working out how you can get them on?

Hannah Nixon: Yes, and I think it is around proportionality of the access requirements and the ease and transparency of information of the whole process.

Q26 John Thurso: Can I just ask, before I go onto the plumbing, as it were, do you think the CMA's work on personal accounts and SME accounts is going to impact on what you are doing at all, or is that just completely separate?

Hannah Nixon: No, there is a definite relationship there and we are obviously working with the CMA. In their statement, I think they highlighted three key concerns in retail banking in particular and one of those was access to payment systems. They recognise that the Payment Systems Regulator is here and we are working on that. I see that as a really important part of ensuring that there is effective retail competition.

Q27 John Thurso: If we turn to the competition in the plumbing bit, have you thought at all about how you might approach that? What would be the things that you would be looking for in deciding how best to deliver for the consumers at the various layers?

Hannah Nixon: We have said that we are going to do a market review of the infrastructure and we will launch that in the first quarter of next year. That is where all the investment sits and it is really important we get that right. We know there are a number of models out there and we know there is a debate about what the functionality of that payments infrastructure should be. How much of it sits in the middle? How much of it is sitting outside? What do we want in terms of cyber-security and additional functionality? There is work going on already in the industry to try to think about what functionality we need. We will be doing a review that continues that work and also looks at the options around delivery. Do we want a central infrastructure? Do we want something that is more disaggregated? Do we even want to have competing systems? There are some potentially interesting bypass models. All those things are on the table and we need to look at that over the next year.

Q28 John Thurso: Different countries have different systems: America, for example, has a number of different main plumbing systems, I think six or so, and the plus is you can pick whichever one you want. The minus is they have not got to chip and pin yet. Have you thought about what will be the advantages of competition versus what might be the disbenefits?

Hannah Nixon: That is exactly what the review will look at. The three models I outlined, there are clear pros and cons with each and we just need to weigh those up. We also need to look at the functionality we need and where that sits because it is really important that the model that we choose is the one that makes sure that the UK is at the forefront of payments.

Q29 John Thurso: The current set-up is basically you have got VocaLink—

Hannah Nixon: Yes.

John Thurso: —who sit in the middle bit and control a vast amount of it, and there are two issues there. One is that you could say, "Let us have a national grid of payments" and they are it—or you might not—but the other issue is: who then owns it.

Hannah Nixon: Yes.

John Thurso: The question is: is it right for the banking system to do that. Looking at that area—you have said you have proposed to look at the ownership of and competition in the provision of infrastructure—how will you shape your thinking on that? What will we be asking? What I am after is what you are looking at doing so we can ask you questions about it when you have done it. That is really the question that is in there.

Hannah Nixon: Okay. We are scoping out that study at the moment but it will look at those three things. What is the functionality? What is the structure? What is the appropriate ownership? The ownership of VocaLink is very much on the table.

Chair: Thank you. That is very helpful, a very helpful exchange.

Q30 Mark Garnier: Can I carry on with the ownership? The Parliamentary Banking Commission in its report in 2013 looked at the merits of getting the banks to relinquish ownership of the payment system and to look into it. You decided not to ask all major banks to relinquish ownership, though you did conclude that the concerns about this can be addressed through changes to governance and control of the systems. Why did you reach that conclusion?

Hannah Nixon: There are two layers here. The first is around the ownership of the rule book, the payment systems, where our proposals on governance are aimed. That is about making sure that it is not just incumbent banks that are controlling that rule book but that it is more open.

The second layer is the infrastructure layer, all the pipes and wires, the VocaLink layer, where we are doing the market review. We have not concluded that ownership should not change. That is still a question that we need to examine, and the reason that we want to take the time to do it is it is just such an important question for the UK. We have to get it right. We need to be evidence-based and robust in the way that we reach that conclusion. All options are on the table but we need to work through those options on an equal-merits basis.

Q31 Mark Garnier: Can you give us an idea of what an alternative to the current system would be in terms of the ownership?

Hannah Nixon: It could clearly be sold off to a completely different entity. It could be price-controlled as a sort of a national grid of payment systems, as was mentioned. There are a number of different options here. It could go to a for-profit company; it could go to a not-for-profit company. I think all that needs to be looked at in terms of the incentives for investment, innovation and access.

Q32 Mark Garnier: So it could be anything from a state-owned company all the way through to a PLC listed on the London Stock Exchange?

Hannah Nixon: Indeed.

Q33 Mark Garnier: Your proposed governance changes also require payment system operators to ensure appropriate representation of the interested services in their decision-making process. Can you unpick what you mean by appropriate representation?

Hannah Nixon: I think the point here is that we need to make sure that it is not just the incumbent banks that are controlling these rule books of how payment systems work. They need to hear the voices of a much wider constituency group, ranging from end consumers through to challenger banks, and they need to take that on board and respond to that, so it is not just, "I hear what you say" but "I am acting on it". They do need to have representation. They do have independent directors at the moment, which is a reasonably new feature. I think that proposal on governance needs to be seen with our proposals on opening up the minutes and transparency of these things because then that means that if we, as the regulator, can see that decisions on the rule book or the ownership of these payment systems are being made that compromise or undermine of the position of challenger banks, let us say, or a particular constituency group, we can step in and change that.

Q34 Mark Garnier: How do you envisage these minutes being scrutinised?

Hannah Nixon: Scrutinised?

Mark Garnier: Just publishing them allows *The Daily Mail*, great organ of the media that it is, to go through it and make some comments about it, but do you see those minutes being scrutinised by a committee like this or by the Treasury? How do you envisage proper scrutiny of the minutes? The problem is that inevitably you are going to get a situation where you have four or five banks that control the vast majority of the transactions in the payments system. There will always be an accusation that those four banks are dominating the governance of the rule book and all the rest of it. In order to be able to demonstrate that is not the case you do have to have proper representation from any number of challenger banks, and it is not just challenger banks. The idea of challenger banks challenging the big four or five is quite simply 47 or 50 other banks out there—from people like Kingdom Bank with a balance sheet of just £50 million, through various other sorts of banks—who are not trying to challenge the big four, they are trying to run perfectly good businesses.

The problem is inevitably going to be that even though the majority of individuals, if you like, if each one had a representation there, you would have a lot of people from smaller banks, who have quite disparate views on what is going on. But you do have the vast majority of the payment system and the use of the payment system being dominated by these big banks who are just four, but four very powerful people who can much more easily align their interests against those of the other banks. Just having sort of publicly produced minutes of these meetings is not necessarily going to get to the point where you have proper scrutiny of what is going on in these minutes, and how various people are held to account in order to make sure that those other, non-challenger but smaller banks are being listened to and are being heard and get a coherent message across for the benefit of not only them but their customers.

Hannah Nixon: Yes, there are a number of parts to this. One is making sure that those voices are heard and it is not just the four big banks who are controlling this stuff, which is absolutely the aim of the governance piece. On the publication of the minutes: it is about getting that transparency so people can really see not just what decisions are made but why, and there is a requirement there to set out why decisions were made. Also to record individual votes so people cannot hide behind the consensus, and that really forces individuals—particularly the independent directors on the boards, but others as well—to say why they have either supported or not supported a particular change. It also means that people out there can say, "I am concerned, PSR, we want you to look at this" and it means we have the ability to pick things up ourselves as well. That transparency ensures a lot more accountability.

Q35 Mark Garnier: I agree with you up to a point. Transparency is a great thing if the scrutiny that follows that transparency is clear and intelligent scrutiny. This is the problem. If it is just about publishing it and it going into the wider public domain you do not necessarily get proper scrutiny. For example, the Monetary Policy Committee publishes its minutes, we scrutinise that, as does everybody else, but you have a forum here where you have a formal type of scrutiny of what is going on. That brings it to a more—I use the words without trying to upset people—intelligent and thoughtful process of scrutiny through Parliament of what is going on. What worries me is that if you merely rely on transparency to provide that scrutiny of the minutes, you may not necessarily get as thoughtful and as rational answers as perhaps you would through a more cerebral approach. Discuss.

Hannah Nixon: I think we can take that away and think about. There is certainly an intention that the PSR is looking at the stuff, and I know from when we have been talking to challenger banks, and other service users as well, that a number of people are really keen to understand, if not be involved in, how these decisions were made so I would expect that they would also be interested in scrutiny. But perhaps we should take away that there is something additional that we need to put in place.

Q36 Mark Garnier: Absolutely. Coming on to other things we are interested in, you intend to ask that directors of payments system operators cannot at the same time be directors of infrastructure providers of the payment system. How do you see that tackling the problems associated with major banks' ownership of the payment system?

Hannah Nixon: It is not intended to tackle the problem of ownership of the infrastructure—

Mark Garnier: Or rather conflict of interest that their ownership is perceived to have.

Hannah Nixon: Yes, this is supposed to be something that we can put in very quickly that can make some early improvements in this. But the market review of infrastructure will be where we really look at the ownership of that infrastructure piece.

Q37 Steve Baker: I would like to ask you about access to payment systems specifically, but before we do can we just talk a little bit more about ownership?

Do you ever hear complaints from the banks that they built these payment systems and they own them and that, therefore, they belong to the people who built them?

Hannah Nixon: They have certainly put across the point that they have built them and invested in them, yes.

Q38 Steve Baker: How do you respond to that? How do you communicate to them the problem that you wish to solve?

Hannah Nixon: What we have seen is the payment systems develop over a number of decades and as a result we have a payment system that serves the interests of the incumbent bank with a degree of inertia in there and that creates a lack of competition and innovation, which is exactly what we are trying to break through.

It is interesting, having engaged with the big banks and others over the last six months to look at their response and the payment system's response because it could have been very defensive. But we have seen the opposite and I think the reason is that they have seen the writing on the wall here. There is a regulator coming in, powers become active on 1 April next year; we have some really strong powers and we have been clear that we will not hesitate to use those powers where we need to and I think they are seeing the writing on the starting to move in the right direction. There is a way to go but I think they understand clearly what we are trying to achieve.

Q39 Steve Baker: The legitimacy for taking advantage of their private profit-making investment for public benefit is competition, is that right?

Hannah Nixon: This is about opening up the payment systems to other people. Part of it is about the rule book, where there is not much investment that they have made and there the Government's proposals are about opening up the ownership and control of the rule book. The investment is in the pipes and wires, which we need to think about carefully, hence the market review.

Q40 Steve Baker: When you say "pipes and wires" do you mean physically pipes and wires or do you mean metaphorically in terms of software systems?

Hannah Nixon: Probably both.

Q41 Steve Baker: Just thinking about software and rates of development and so on, I have Bitcoin Wallet on my phone; the wallet is not on the phone but access to it is. Bitcoin at the moment is quite a poor money: it is a bad unit of accounts, it fluctuates too widely and it is a poor store of value. But it does seem to me it is a very good payment system. To what extent have you considered the way that technology will surpass many of these arguments?

Hannah Nixon: A lot. We are very conscious of the fact that we do not want to do anything that entrenches a system of today at the expense of what we could have tomorrow. I think crypto currencies are a good example of that and hence I mentioned that in part of our market review we will look at the models for infrastructure and could include bypass of the existing infrastructure through crypto currencies or something else. We need to make sure the conditions for fostering those things are there and that we do not entrench the technology of today or even yesterday.

Q42 Steve Baker: I just observed that by downloading a Bitcoin Wallet and connecting my computer to the internet I am on the payment system. It is as simple as that and it is not regulated, and it seems to work. But that said, we are where we are.

How important is it for banking competition that banks have direct access to payment systems as opposed to indirect?

Hannah Nixon: The banks we have spoken to consider it very important to have direct access and we know a number of them are trying to get direct access at the moment. A key part of what we are proposing is to just make that much easier for those institutions to get direct access where they want to. There will probably always be some financial institutions that it just makes more commercial sense to go in directly because they have a low volume of payments. But where people want to go direct we need to make those access criteria proportionate for them.

Q43 Steve Baker: Does that proportionality include access to having an account at the Bank of England? If so, to what extent will you be able to influence those decisions?

Hannah Nixon: We have been talking to the Bank about that and they have been reviewing their requirements for getting a settlement account at the Bank of England. The schemes are also looking at their requirements and whether in all circumstances they need to have that direct settlement with the Bank of England or not. These things are under review.

Q44 Steve Baker: What does this mean for the customer, this issue of direct versus indirect access?

Hannah Nixon: For the end customer?

Steve Baker: Yes.

Hannah Nixon: The plumbing is largely unseen by the end customer, which is how it should be. As long as their money gets from A to B securely and safely then there is no particular reason why they should mind what the routing is. The important thing for the customer is that they pay for all of this indirectly and so they want a quality service at an efficient cost.

Q45 Steve Baker: What balance would you expect to see in future between direct and indirect access to payment systems?

Hannah Nixon: At the moment we have 30-odd institutions that are directly connected and a couple of thousand indirectly connected. We know we have about 50 who want to move from indirect to direct and you would hope that the majority of those would do so. There might be others who want to move as well when things become more proportionate, but the vast majority are those small financial-services providers who for volume and commercial reasons may well want to remain indirect. But the important thing is that people have the choice.

Q46 Steve Baker: Could you just say a little bit more about how those commercial reasons play out? Why would somebody want to be in one camp, not the other?

Hannah Nixon: If you are going to connect directly into the system there is a certain requirement in terms of your own IT capability to do that, which can cost at least a few million, depending on your size. So there is just a volume issue in terms of whether that makes sense to make that investment or whether you use a sponsor bank.

Q47 Steve Baker: We are talking about barriers to entry in competition: is the issue whether people are big enough to pay the cost of IT to get in as a direct accessor of the payment system? Or is there some other barrier to entry in that regard?

Hannah Nixon: The issue we are looking at is making sure that entry requirements are proportionate. There is going to be a cost of entry and setting yourself up, and in transacting over the system. We need to make sure that the requirements are proportionate, the cost is proportionate and that people have the choice to go direct or indirect, assuming they can meet the requirements of the system.

Q48 Steve Baker: On this business about making the requirements subjective, risk based, and publicly disclosed is it possible that the requirements could be all of those things and yet still be an insurmountable barrier to entry?

Hannah Nixon: There will be people who have low transaction volumes who will still see it as commercially unviable. That is quite possible. The important thing is by making the systems adhere to those criteria it makes them more accountable. It also means that we have the ability to intervene. The PSR does have the ability to mandate access to payment systems on specific terms and conditions, so people who are unhappy with the terms that they are being offered by the payment system do have the ability to come to us.

Q49 Steve Baker: Could you tell us a little bit about the scope of the market review that you are planning to launch by April 2015, please?

Hannah Nixon: On indirect access? Yes. We are planning to do a market review on indirect access. The timetable would be similar to the one on infrastructure and we would launch it in the first quarter of next year. It is being scoped at the moment. This is really about trying to understand that market better because there are 30 potential sponsored banks and only four choose to offer sponsor services. There were five. The Co-op is withdrawing from that sector. We really need to understand what the dynamics of that market are to understand if there are things that we might need to change or there are behaviours in the market that might need to change to make that work as effectively as possible. That, in combination with the things we are doing on improving transparency—for example at the moment we have heard that if you want indirect membership, you want to be sponsored by a bank into the system, you have to enter non-disclosure agreements before you can even find out what you need to do. This whole thing just needs to be much more transparent and much more customer friendly so that people can say, "I want this service, how do I engage with you, sponsor bank, to understand what you can offer me?"

Q50 Steve Baker: How concerned are you that sponsor banks are being required to provide services to their competition?

Hannah Nixon: For the people who are wanting directly to engage in the banking space it is important that if they want to they should be able to access the system directly, hence our proposals on direct access. That is the important thing—that people have that choice to be able to enter directly.

Q51 Steve Baker: I suppose what I was really driving at is do you see that there is as problem with incentives when a bank is required to provide services to those customers of it who might turn out to be its competitors in due course?

Hannah Nixon: Yes, potentially, I think that has to be a concern.

Q52 Rushanara Ali: You will take responsibility for regulating Link, which provides the payment system for ATMs, and there remain continued concerns about making sure that there are free ATM facilities, particularly in deprived areas. According to even recent news reports some 300,000 do not have close proximity to free ATM machines. Is this of concern to you? If so, what will you do about it?

Hannah Nixon: There are two parts to ATM provision and one is ensuring that consumers have access to cash when they want it. It is important that consumers do have that access because I am well aware that not everybody has the iPhone that they can use to pay for things. So where people want cash will remain an important part of the economy and transactions and making sure that those ATMs are available and people have access is an important part and something the PSR is committed to.

The second part of that is the balance between the free and the charging ATMs. The majority are free but I am aware that many of them are also charging. That takes us into a sort of wider picture or issue of the free and credit current-account banking. We know that the

CMA is looking at that at the moment and so I would expect those sorts of issues to be teased out there. There is a role here for the CMA, for us, and for the FCA in looking at charging for ATMs.

Q53 Rushanara Ali: But you do not have a target of reducing the number of ATMs that do the charging?

Hannah Nixon: No, we do not. We are committed to making sure that ATM network is widespread and people continue to have access to the cash.

Q54 Rushanara Ali: How do you propose to do that when the industry, again according to another report, says that cash machines will not be a priority because there is no consumer issue?

Hannah Nixon: This is a really important reason why we need to have an economic regulator here because it is the consumer need and user need that needs to be the focus. While there continues to be a need to have cash and ready access to cash there will need to be an ATM network or something equivalent, which is why the PSR is committed to making sure that remains in place.

Q55 Rushanara Ali: Can I just give you an example of the disparities between geographies, which has been a long-running concern for MPs and members of this Committee? There are rural/urban divides but also if you just take an example in London, I did my own analysis and according to that, looking at the Link website, if you live in Sloane Square in West London, about 14%—fewer than one in seven—of the closest 50 ATMs charge. If you go to Whitechapel—which is in my constituency—it is 34%. That is one in three. It is also an area with half the population with child poverty. These disparities are very significant and I am not really convinced that this is being given the urgency it deserves. How can you reassure us that that is going to change?

Hannah Nixon: There are a number of people here that need to be involved in this. The PSR itself does not have that remit but it is part of the picture so this access to cash, as I say, is really important for the PSR. We are committed to making sure that user need is met. But I think it does come into this wider debate about the current account and free and cash model that is being looked at. There are also issues of engagement in terms of payment systems understanding the needs of specific user groups. That is another area where the PSR can help to make sure Link—and indeed all systems—really understand their user groups. We have been doing a lot of engagement with charities, for example, and end-consumer representatives, to really understand the needs of those user groups and to make sure the payment systems can respond to them.

Q56 Rushanara Ali: But no one at this stage is prepared to set any kind of target, any kind of objective to reduce the number of cash machines in these sorts of areas where they are charging sometimes close to £2 per transaction to withdraw?

Hannah Nixon: What the PSR is very active in doing is making sure that all these voices are heard. We held a consumer round table recently where we had Toynbee Hall, we had Citizens Advice, Age UK, Scope and so on, all around the table to understand exactly some of these concerns. Payment systems need to understand to support and I understand Link does have an outreach programme there. These constituencies will be part of our wider industry and consumer panels so we can make sure that the things that we are bringing forward are stress tested in that arena. This is an important voice we need to respond to, but I think the answer in terms of the charging point is slightly wider than payment systems. It does go to banking more widely.

Q57 Rushanara Ali: Are there points that this Committee could pick up on to help facilitate a change for the better? Do you have any suggestions on things we could do to help push things along in the right direction?

Hannah Nixon: I will take that away but it is a good question and I will give it some thought.

Rushanara Ali: Thank you.

Chair: Very helpful.

Q58 Teresa Pearce: Could I just first declare an interest? I am an independent member of the Consumer Council for Link. Just to pick up on what Rushanara's questions, she was asking about people who have to pay to access cash and you were talking about basic bank account holders and current account holders. Obviously, if you bank with certain banks you might have to pay to access an ATM of another bank. What we are talking about here are the non-bank cash machines that are in Costcutter and places like that. Link have done an enormous amount of work in reducing the number of those and on free-to-use ATMs, and I am glad to know that you are working with them on that, and Toynbee Hall who have done a fantastic piece of work on that. But, with the closure of so many bank branches, it is becoming more common now not to have an ATM and have to go somewhere and pay to use it. I would be interested in the future to hear how you have got on with that discussion.

Something else that consumers are quite bothered about is bank account switching. To what extent do you consider switching to be part of your remit?

Hannah Nixon: Payment systems are definitely a part of that promotion and competition in the retail banking space. The FCA, as you are probably aware, is doing a review of the current account switch service at the moment—

Q59 Teresa Pearce: Are you involved in that review?

Hannah Nixon: We are not directly involved in the review but we are really keen to see what comes out of it because I think there is a question then for what that means for the payment systems. Part of that work, as I understand it, will be to look at what additional features or things could be put in place to make that whole switching process faster, easier, more secure, or give consumers more confidence. Anything that could do that clearly has to be a good thing for the consumer. So there might be things coming out of that review that have implications for the payment systems and so we are following that very carefully to see what the implications are.

Q60 Teresa Pearce: Would you not agree that direct debits are a barrier to people switching often and that is clearly part of the payment system? Do you believe you should be integral to these discussions on account switching?

Hannah Nixon: We need to see what comes out of the review and they are doing some survey work to tease out exactly those issues. We have been discussing, through our consumer groups, concerns on direct debits and so these things are feeding into our thinking.

Q61 Teresa Pearce: This current review, do you have any preliminary conclusions you would like to share with us as to what might come out of that review?

Hannah Nixon: The FCA is doing it now. I have not seen what has come out of it.

Q62 Teresa Pearce: It was worth a try. Do you have any initial views on account-number portability?

Hannah Nixon: Again, this is a really important part of the piece of looking at how switching is working and the FCA will be looking at some of the benefits of account-number portability. From a payment systems point of view it is very much an option on the table. We want to see what comes out of that FCA work. We will feed it into our thinking of what we need from the world-class payments infrastructure, which comes back to the earlier discussion about what we want from the payments infrastructure in the first place and then what are the options for delivering it and ownership. That work that the FCA is doing on the benefits of account-number portability will feed directly into our thinking there.

Q63 Teresa Pearce: Do you think the current-account switch service, the seven-day service, has been a success?

Hannah Nixon: The FCA are reviewing it, let us see. But, I mean, the high level numbers—you have 1 million or more additional people who have switched—I think anything we can do to make that switching service easier and more effective has to be a good thing.

Q64 Teresa Pearce: Would you support a move to make it a five-day switching service?

Hannah Nixon: I am not close enough to the detail. As I say, anything that makes this easier for the consumers and more secure has to be a good thing, but I have not looked at the pros and cons of that.

Q65 Teresa Pearce: One last question. Going back to what you said earlier about innovation and how you do not want to stick with old systems, you want to embrace anything new. The Link system, ATMs, are quite well trusted by people. They understand them. Is there not more that those ATMs could do? Would you be supportive of ideas of being able to maybe pay your gas bill at an ATM? Would you think that is something that could be looked at?

Hannah Nixon: Yes, and I think there are some really interesting ideas out there on innovation, particularly when there is a big question about branch facilities versus ATM facilities, and really making sure that payment systems can do what they can for financial inclusion. There are lots of interesting models out there and we are certainly interested in promoting that sort of innovation and thinking.

Q66 Teresa Pearce: It seems to me that for some people the ATM is the only banking facility they have now that there is no branch left in town. So the banks previously—it is my understanding—did not want the ATMs to do more because they want people to come in the branches, but if the branches do not exist surely it is time to look at that. What you can do on your smart phone you must be able to do on an ATM, surely.

Hannah Nixon: Yes, I think there are some real opportunities there.

Q67 Chair: Is the EU getting involved in this area?

Hannah Nixon: There is a lot of activity in the payments space broadly at European level. We are engaged in the discussions around PSD2, for example, and we do that with our FCA colleagues to influence and engage in Europe.

Q68 Chair: The European system of central banks, they have a payments regulation responsibility, have they not?

Hannah Nixon: My understanding is that largely mirrors the Bank of England responsibility in the UK in that sense in that it is primarily focused on the reliability and integrity of the system, so the Bank is very engaged with the European Central Bank on those issues. Again, because we work closely with the Bank we are able to feed things in to that route if we need to.

Q69 Chair: Have you had any conversations with counterparts in other countries to see how they are running their systems?

Hannah Nixon: We have done some survey work to understand what happens in other countries. In fact we have published a short report on some of the comparators. Increasingly we are engaging with other countries to understand their thinking, yes.

Q70 Chair: You have heard some of the concerns around the table, probably only a sample, not all colleagues are here today anyway. We put quite a bit of effort into trying to sort out this area once we realised it was frankly a cartel operating, at least in part for the benefit of the banks rather than consumers. We are very glad you exist and we think that you have roughly the right remit since it is quite close to what we recommended in the beginning.

We wish you well in your work. We are very keen that you should be empowered to do it without let or hindrance. You are part of quite a complex framework that perhaps only the British could have invented for a new organisation right at the start. I hope that this hidden wiring that lies behind the way you are operating works for the good and does not end up stymieing your activities, but if it does, we would be very grateful if you come to us sooner rather than later so that we can sort it out. We wish you well, thank you very much.

Hannah Nixon: Thank you, and I assure you we will come back and we are determined that we do make a difference in this area, so thank you.