

# Delivery and Regulation of the New Payments Architecture

## LINK's response to the Payment Systems Regulator's consultation paper, February 2021

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### LINK's Experience of Competitive Infrastructure Tenders

1. On 5 February 2021 the PSR issued a [consultation paper](#) on the renewal of the UK's interbank payment infrastructure. This consultation covers the PSR's Specific Directions 2 and 3 (SDs). These require Pay.UK to run a competitive procurement for the central infrastructure for Bacs and Faster Payment Service (FPS) respectively. The PSR notes in its consultation paper that *"In the light of our conclusions, we will consider whether the directions should be varied, revoked or replaced"*.
2. LINK has recently conducted its own competitive tender for its central infrastructure service under a PSR SD (SD4), similar to those now being considered by Pay.UK for Bacs and FPS. LINK is therefore responding because its experience is directly relevant to the PSR's deliberations.
3. Although the consultation paper poses a number of detailed questions, LINK is providing this single overall response which it believes best summarises its experience.
4. LINK's recent competitive tender and the resulting Vocalink contract are subject to extensive commercial confidentiality constraints. Therefore, it is not possible to include commercial details in this public document. However, all the key points are set out. The PSR has already been provided with great detail relating to these events in its role as one of LINK's regulators and therefore has access to other evidence.

### **LINK recommends that the new contract should be negotiated with Vocalink directly and that the concept of a competitive tender not be pursued further**

5. Pay.UK and LINK together run all the systemically important interbank payment schemes in the UK. They are both regulated by the PSR and the Bank of England. Transitions of core infrastructure to new suppliers can be extremely risky due to the complexity of the networks involved, their high volume 24/7 nature, and the large number of participants connected to the central switches. Investment alone cannot always mitigate this risk. All of these systemically important interbank switches are currently provided by Vocalink or its precursor companies.
6. LINK is very similar to a system such as FPS, as FPS was developed by Vocalink and its members from the LINK infrastructure. The LINK experience is therefore directly

comparable to the FPS situation (albeit LINK has the additional issue of declining transaction volumes to manage).

7. The implementation of the New Payments Architecture (NPA) is now much delayed from the original plan. Opportunities to speed matters up are therefore likely to be valuable.
8. In light of this and the complexity of the task in hand, LINK recommends moving immediately to a detailed negotiation with Vocalink rather than spending another year assessing the competitive tender option. We have set out the main reasons for this recommendation below by reference to some of LINK's own experiences.
9. LINK found that the systemic risk management components of negotiations with bidders was greatly assisted by the regulatory approach followed by the Bank of England which uses a strong and established framework based on the BIS-IOSCO Principles for Financial Market Infrastructures (FMIs). This is identical to that used for other FMI including FPS and Bacs. This was a "regulatory requirement" of any new contract and this would have been the case whether or not a competitive procurement was undertaken. As such, from a risk management and operational resilience perspective, LINK does not consider that a competitive tender is needed to ensure a satisfactory contract.
10. LINK's view is that a similar approach could be adopted in respect of the PSR's competition and other requirements for the NPA such that any contract negotiated bilaterally with Vocalink must comply with any regulatory framework imposed by the PSR.
11. LINK notes that if these and other regulatory requirements and acceptable commercial terms were not achieved in direct negotiations with Vocalink then clearly Pay.UK and the PSR should reserve their right to revert to a tender/competitive process. The participants and process for that should be left as much as possible to the discretion of the board of Pay.UK to avoid further delay arising from a bureaucratic and lengthy competitive tender process.
12. In the case of LINK, a pressing strategic issue at the time of the competitive tender was (and remains) how to manage the reduction in cash usage by UK consumers and a smooth and inclusive move to digital alternatives. Declining cash volumes made a competitive tender a challenging proposition for participants (in seeking to recover "transition" costs) and LINK. The possible benefits from a competitive tender in respect of a lower price and improved terms were insignificant when compared to dealing with this enormous challenge (and taking account of the view of LINK that improved terms from a systemic risk perspective could be achieved through the regulatory framework required by the Bank of England). The LINK competitive tender therefore diverted scarce resources from a central challenge facing the UK in relation to cash. LINK also had to continue throughout as an effective systemic risk manager in line with its regulatory obligations. LINK's competitive tender took 18 months, cost millions of pounds in advisory fees, and was a top risk on the LINK risk register for that period. It absorbed some 25% of senior management and Board time to the detriment of managing other matters. LINK also estimates that the companies that elected to respond to the Request for Proposal would collectively have spent millions of pounds in participating in it.

13. It seems to LINK that the timely and safe rebuilding of the UK's digital infrastructure is the priority issue when it comes to the NPA. LINK itself is dependent in part on a successful and rapid outcome, as this is needed by cash users to enable a smooth and inclusive move to digital payment methods. LINK assumes that these relevant lessons from the LINK experience will be useful when considering the situation facing the NPA.
14. In the case of the LINK service, great emphasis was put by SD4 on the pricing improvements available through a competitive tender. Whilst an improved price was achieved, the cost of the service compared to the overall cost of running the ATM network and the LINK Scheme is insignificant. The actual reduction achieved is a fraction of this. LINK would have expected to have achieved a cost reduction in a bilaterally negotiated contract with Vocalink. While the extent of this can't easily be assessed, what is certain is that the cost of achieving this would have been significantly less than by running a competitive tender. Therefore, the focus on infrastructure pricing was not in line with the overall pricing of the payment system. LINK also notes that there are alternative mechanisms to a competitive tender to manage pricing with a supplier, including with an incumbent, such as benchmarking and open book approaches.
15. The Payments Strategy Forum originally set out its Vision for payments in November 2016. It proposed:
  1. The development and implementation of the NPA.
  2. The consolidation of the main UK retail Payment System Operators including Bacs and FPS.
  3. A set of solutions to help prevent or reduce the impact of financial crime on users.
16. Almost five years on, matters are now pressing, especially in relation to point three.
17. The first and last of these Vision components can be delivered through direct engagement with Vocalink. The second has been delivered already in the case of the scheme (this is Pay.UK) and in the case of the infrastructure is irrelevant given that all proposed options plan to progress just with FPS.
18. As noted above, if direct engagement with Vocalink were not to result in a suitable outcome then it would be up to Pay.UK to return to a process with some element of competition to resolve any impasse. This should be a last resort.

**Pay.UK should be trusted to develop the technical and commercial capabilities it needs to manage the negotiation with Vocalink**

19. LINK's experience was that significant commercial and technical skill was required within its team to manage the contract negotiations with potential suppliers, and the final detailed negotiations with Vocalink.
20. Given the temporary nature of a tender (whether competitive or a direct negotiation with an incumbent) these skills will inevitably involve procurement of temporary external expertise.
21. This sourcing of such external expertise takes skill and effort. It was a key responsibility for the LINK Board, and this will presumably be the case for the Board of Pay.UK. LINK notes that both Boards are leading not-for-profit companies limited by guarantee and with a public interest focus.

22. It is LINK's experience that it should be up to the Board of Pay.UK to seek the best advice and have broad discretion to operate the procurement process within a clear regulatory framework and that when regulators trust the Boards of the companies that they regulate, and focus on regulating, this leads to good outcomes. LINK's Board is aware that, should regulators not be satisfied with the competence of the Board to execute its role effectively, then a number of remedies are available within the existing regulatory framework.

**The industry, informed by extensive consumer insight, has developed already a good blueprint for the future and the need now is to get on with delivery urgently**

23. LINK's competitive procurement was informed by a clear requirement largely based on duplicating the existing service. This was because there was no need to change what was being delivered.

24. LINK notes that, whilst the NPA is a new service, robust work has already been done by industry and informed by extensive consumer insight on what is required. LINK notes in particular the excellent summary of requirements set out in the UK Finance document "*Future Ready Payments 2030 - Working with a dynamic, purposeful and united agenda for the UK*" published in February 2021".

25. LINK's experience of working with Vocalink is that it has extremely good capability in translating such requirements into live services. The issue is managing the negotiation to achieve a satisfactory commercial outcome.

26. Given the already lengthy delays with the NPA, LINK recommends moving immediately to a negotiation with Vocalink, utilising an appropriate commercial and technical capability within Pay.UK to deliver the negotiation, and not pursuing a competitive tender except as a last resort.

27. A final point relates to the whole of payments infrastructure. Whether for good or bad, Vocalink currently runs all the regulated interbank infrastructure and the Post Office Counter Service network infrastructure. It is beyond question that it does so efficiently with a very high level of resilience. If Vocalink loses responsibility for one service, this could well have implications for other parts of the industry. Vocalink is itself regulated as a systemically important infrastructure provider. The PSR should move away from the need for a competitive tender process for the provision of infrastructure which at best could provide only limited benefits and certainly involves substantial costs and risks.

**About LINK**

28. Link Scheme Holdings Ltd (LINK) manages the UK's main cash dispenser (ATM) network and is central to the operation of the UK's cash infrastructure.

29. LINK's network connects the vast majority of ATMs (both free and charging) in the country and allows customers of banks and building societies (card issuers) who are LINK Members to make cash withdrawals and balance enquiries with their payment card at almost all ATMs. All major card issuers and ATM operators currently choose to become Members of LINK. This helps to ensure that consumers in the UK have the choice of using cash should they wish to.

30. Cash is in long term decline in the UK and, whilst the Government committed in March 2020 to introduce legislation to protect access to cash, this has yet to be implemented,

meaning there are no obligations that give consumers the right to access cash (free or otherwise). In the absence of legislation, LINK is continuing to ensure that communities throughout the UK have satisfactory free access to cash.

31. LINK is regulated by the PSR and by the Bank of England as a systemically important payment system and values a collaborative and strategic relationship with both.
32. The LINK network is based on a highly resilient real-time high-volume infrastructure, currently supplied by Vocalink. The contract with Vocalink resulted from a competitive tender mandated by the PSR through its SD4 which is similar to the SDs in force for Bacs and FPS. LINK has already fed back its views and lessons learned to the PSR.

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