



Response to CP24/11 – “Faster Payments APP scams: Changing the maximum level of reimbursement”

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Miss Tim Yi Jane Ngan: Response to CP24/11 – “Faster Payments APP scams: Changing the maximum level of reimbursement”

1. Background

- 1.1. I am a doctoral researcher affiliated with the Department of Criminology, School of Social Sciences (“SOSS”), University of Manchester. My research, funded by SOSS, focuses on regulatory responses to Authorised Push Payment Fraud (“APPF”), specifically in respect of the development of the Faster Payment Service (“FPS”), payments regulation, and how regulators and financial industry professionals influence and respond to change.
- 1.2. In addition to my academic interests, I have also worked extensively in the financial services and private banking industry, primarily in financial crime investigations and compliance leadership roles. Whilst I occasionally draw on my professional experience in my research, my response to the consultation exercise relates solely to my academic interests and affiliation; it does not represent the views of my current or previous employers.
- 1.3. CP24/11 outlines the Payment Systems Regulator’s (“PSR”) intention to lower the maximum reimbursement limit for APPF executed on the FPS from £415,000 to £85,000. I make no comments on where the reimbursement limit should be set; my response focuses solely on procedural fairness and reasoning underlying the proposal.
- 1.4. My response to CP24/11 is as structured follows:
 - a) The PSR’s reasoning in CP24/11 appears to place the interest of smaller Payment Service Providers (“PSPs”) ahead of the wider interests of other market participants. In seeking to address solvency and prudential risks said to be faced by smaller PSPs, the effect of the proposal may instead introduce market distortions, and ambiguity in the boundaries between the PSR’s mandate and the corporate duties of private firms;
 - b) The PSR’s general approach to CP24/11 does not, prima facie, adhere to two of the four Gunning Principles on public consultations;
 - c) It is recognised that the PSR’s other interventions to date have encouraged greater transparency and accountability by PSPs, and better protection for Payment System Users (“PSUs”). A proposed remedy to the issues highlighted in 1.4a. and 1.4b. is put forward.
- 1.5. This response to CP24/11 addresses the following questions raised in the consultation:
 - *Question 1: What are your views on the proposal to change the maximum level of reimbursement from the outset of the policy, to set it to the FSCS limit, which is currently £85,000?*

- *Question 2: What are your views on the impacts (including costs, benefits, and risks) of operationalising an initial maximum limit of £85,000 from 7 October 2024?*

2. Solvency and prudential risks of smaller PSPs

- 2.1. The PSR has stated that CP24/11 is borne out of concern of a potentially disproportionate impact on smaller PSPs, including prudential, solvency and fundraising concerns if the reimbursement limit was to be retained as originally proposed at £415,000.
- 2.2. Concerns raised in support of CP24/11 include views that £415,000 is close to some firms' typical capital holding, which could create the potential for loss making or market exits. It was also argued that a higher level of liability may see some PSPs struggle to attract investment and funding, or to limit funds available to be invested in anti-fraud measures.
- 2.3. The PSR, however, has failed to consider whether these concerns can already be addressed by smaller PSPs independent of a regulatory recalibration.
- 2.4. FPS can facilitate transactions up to the value of £1 million, however, PSPs retain the sole discretion to determine the transaction limit which applies to specific types of customers or services. Available data from Pay.UK for direct FPS participants show a significant variability in the transaction limits established by PSPs in line with their respective risk appetites and competitive positions¹.
- 2.5. **Smaller PSPs have sole discretion to establish FPS transaction limits appropriate to their capacity to absorb prudential and solvency risks.** By lowering the transaction limit to a level appropriate to the size, scale and operational maturity of its business, a PSP reduces its liability as a remitting firm of an APPF – that is, the service provider of a APPF victim. This business decision is central to well established risk management principles which apply to financial firms².
- 2.6. **Prudential and solvency risk management are directly related to, and inextricable from, a firm's internal systems and controls,** including its anti-fraud management systems. Improving fraud detection, including customer onboarding, due diligence and ongoing transaction monitoring systems together reduce a PSP's liability as a receiving firm of a APPF – that is, the service provider of a fraudster.

¹ Pay.UK. 'Transaction Limits'. Pay.UK. Accessed 16 September 2024. <https://www.wearepay.uk/what-we-do/payment-systems/faster-payment-system/transaction-limits/>.

² Financial Conduct Authority. 'PRU 1.4 Prudential Risk Management and Associated Systems and Controls'. The FCA Handbook. Accessed 16 September 2024. <https://www.handbook.fca.org.uk/handbook/PRU/1/4.html?date=2006-08-30>.

- 2.7. The assertion by some PSPs that investment in anti-fraud systems and controls may be reduced in light of liabilities under APPF reimbursement signals potentially poor capital adequacy of these firms to absorb risks in general, and the risks they may introduce into the stability of the financial system at large. **It begs the question as to whether these firms ought to be offering payment services in the first place.**
- 2.8. **The limits to the PSR's pursuit of its competition objectives are not unbounded; encouraging higher numbers of PSP entrants into the UK market does not necessarily entail better outcomes for PSUs.** The PSR's own data has shown that smaller banks and payment firms received the highest value and volume of APPF relative to their size, compared with larger firms³.
- 2.9. The PSR's reasoning underlying CP24/11 to mitigate the prudential, solvency and fundraising risks purportedly faced by smaller PSPs appears to put the interests of smaller firms ahead of those market participants who seek to invest in robust fraud management systems and to maintain measured prudential risk management practices.
- 2.10. **The decision introduces a free-rider problem into the market.** Some smaller PSPs may be incentivised to focus on achieving scale (including aggressive customer onboarding) instead of investment into anti-fraud management systems. These firms can nevertheless benefit from anti-fraud controls established by larger and better capitalised PSPs without losing competitive advantage. In doing so, **the PSR has inadvertently endorsed suboptimal risk management practices as *the* competitive advantage for smaller PSPs.**
- 2.11. It bears reiterating that the responsibility for establishing and maintaining risk management systems, including prudential, solvency and anti-fraud management systems and controls, falls squarely within the corporate duties of private firms. A firm's risk-taking activities, including the types of products and services it offers to customers, must be proportionate to their capacity of absorb risk.
- 2.12. In light of the foregoing, I argue that the **PSR has exceeded its mandate in the reasoning applied in CP24/11. It has created ambiguity in the boundaries between its statutory objectives and those responsibilities which fall firmly within the corporate governance of private firms.**

³ Payment Systems Regulator. 'APP Fraud Performance Data', July 2024. <https://www.psr.org.uk/information-for-consumers/app-fraud-performance-data/>.

3. Adherence to the Gunning Principles

- 3.1. *R. v Brent LBC Ex p. Gunning* (1985) 84 LGR 168 set out the so-called Gunning Principles, which was later endorsed by the Supreme Court in *R (Moseley) v Haringey London Borough Council* [2014] UKHL 56.
- 3.2. The Gunning Principles, also known as the Sedley requirements, set out the expectations for public consultation exercises in four areas⁴:
 - I. Consultation must be made when proposals are at a formative stage;
 - II. Sufficient reasons for the proposal must be given to allow intelligent consideration and response;
 - III. Adequate time must be given for a response;
 - IV. The product of the consultation must be conscientiously taken into account in finalising proposals.
- 3.3. In assessing the approach adopted by the PSR in CP24/11, I focus on the first and third Gunning Principles, namely, whether CP24/11 had been put forward at a formative stage of the overall consultation exercise, and whether adequate time has been given for a response.
- 3.4. The PSR's website reflects the regulator's longstanding engagement with the issue of APPF reimbursement⁵. Detailed requirements for the reimbursement scheme were subject to consultation as early as September 2022; this was followed by successive consultations in 2023 and 2024.
- 3.5. The following table sets out the PSR consultations on APPF reimbursement and related information reporting requirements, from September 2022 to date, and the time allotted for each consultation:

⁴ Martin Smith. 'Decision-Making by Public Bodies: Avoiding Legal Challenge'. West Law - Practical Law Public Sector, 15 September 2024.

⁵ Payment Systems Regulator. 'A History of Our Work to Prevent APP Scams'. Accessed 15 September 2024. <https://www.psr.org.uk/our-work/app-scams/a-history-of-our-work-to-prevent-app-scams/>.

Ref.	Title of Consultation	Opened	Closed	Calendar days
CP22/4	Authorised push payment (APP) scams: Requiring reimbursement	29/09/2022	25/11/2022	57
CP23/1	APP scams data publishing guidance	09/02/2023	23/02/2023	14
CP23/4	APP fraud reimbursement requirement - draft legal instruments	07/07/2023	25/08/2023	49
CP23/5	APP fraud: APP scams measure 1 reporting guidance second cycle	11/08/2023	01/09/2023	21
CP23/6	APP fraud: Excess and maximum reimbursement level for FPS and CHAPS	15/08/2023	12/09/2023	28
CP23/7	APP fraud: The consumer standard of caution	15/08/2023	12/09/2023	28
CP23/10	Specific Direction on FPS participants - implementing the reimbursement requirement	28/09/2023	19/10/2023	21
CP23/8	APP fraud: APP scams measure 1 cycle 2 additional changes to timeline and reporting periods	14/09/2023	22/09/2023	8
CP24/3	The FPS APP scams reimbursement requirement: compliance and monitoring	17/04/2024	28/05/2024	41
CP24/8	CHAPS APP scam reimbursement requirement	08/05/2024	31/05/2024	23
CP24/7	APP scams data cycle 2 publication guidance	07/05/2024	30/05/2024	23
CP24/10	Consultation on draft guidance on supporting the identification of APP scams and civil disputes	18/07/2024	08/08/2024	21
CP24/11	Faster Payments APP scams: Changing the maximum level of reimbursement	04/09/2024	18/09/2024	14

3.6. The following analysis is restricted to a comparison of calendar days allocated between opening and closing dates of APPF-related consultations. It does not take into account pre-consultation announcements and publications which may offer potential respondents an early indication of areas subject to consultation, and hence greater time to prepare.

- 3.7. It is also acknowledged that the PSR retains discretion in determining and differentiating the consultation periods required for a range of different issues. Heterogenous consultation periods are expected to be the norm.
- 3.8. Excluding CP24/11, 12 other consultations published during the period averaged 28 calendar days between the opening and closing dates. The 14 days allotted for CP24/11 is substantially below average.
- 3.9. When comparing CP24/11 with CP23/1 and CP23/8, which have consultation periods of 14 calendar days and 8 calendar days respectively, the substance of these consultations is found to be qualitatively different:
- a) CP23/1 relates to the PSR's draft guidance on PSP's reporting of data on their handling of APPF. The guidance was intended to support data publication requirements which came into force until 23 March 2023⁶.
 - b) CP23/8 sought to condense the frequency for data reporting by PSPs, and to reduce the resource burden for impacted firms⁷.
- 3.10. CP24/11, in contrast, relates to a substantial reduction in the maximum reimbursement limit for APPF, an issue with significant divergence between stakeholders. The controversial nature of the reimbursement limit was acknowledged by the PSR's policy statement in December 2023: some consumer groups had argued that reimbursements should be uncapped, some PSPs were in favour of the £415,000 limit, whilst smaller PSPs had argued for a lower limit, such as £30,000 or £85,000⁸.
- 3.11. The threshold for reimbursement had been subject to consultation as early as September 2022. In CP22/4, the PSR first consulted on its proposal to **not** establish a maximum threshold, reasoning that PSPs would typically have the strongest safeguards in place for the largest payments, and most FPS transaction limits are well below £1 million⁹.
- 3.12. Between 2023 and 2024, prior to the publication of CP24/11, PSR had consistently maintained its position to establish a maximum reimbursement limit at £415,000, which in

⁶ Payment Systems Regulator. 'PS23/1 APP Scams: Measure 1 - Collection and Publication of Performance Data', 23 March 2023. <https://www.psr.org.uk/publications/policy-statements/ps231-app-scams-measure-1-collection-and-publication-of-performance-data/>.

⁷ Payment Systems Regulator. 'CP23/8: APP Fraud: APP Scams Measure 1 Cycle 2 Additional Changes to Timeline and Reporting Periods', 14 September 2023. <https://www.psr.org.uk/publications/consultations/cp238-app-fraud-app-scams-measure-1-cycle-2-additional-changes-to-timeline-and-reporting-periods/>.

⁸ Payment Systems Regulator. 'PS23/4 Fighting Authorised Push Payment Scams: Final Decision', 19 December 2023.

⁹ Payment Systems Regulator. 'CP22/4: Authorised Push Payment (APP) Scams: Requiring Reimbursement', 29 September 2022. <https://www.psr.org.uk/publications/consultations/cp22-4-app-scams-requiring-reimbursement/>.

its view struck a balance between consumer protection objectives and the financial viability of PSPs, despite necessary trade-offs, including the prudential and solvency concerns of PSPs¹⁰.

3.13. As evidenced in the foregoing, the reimbursement limit had been subject to a period of extensive consultation: the PSR had devoted some 15 months of stakeholder feedback to arrive at the decision to establish the reimbursement limit at £415,000 (between the publication of CP22/4 in September 2022 and PS23/4 in December 2023).

3.14. **I argue that, prima facie, the PSR's general approach to CP24/11 does not adhere to two Gunning Principles:**

- a) *The principle that a consultation must be made when proposals are at a formative stage.* CP24/11 was not put forward in the formative stage of the APPF reimbursement consultation. Indeed, the PSR had rejected previous consultation responses to reduce the reimbursement limit to £85,000 (or lower). The reopening of the consultation, on a matter already concluded in previous consultation stages, which were arguably “formative” and reflected the PSR’s position for a period of 15 months, is not well explained.
- b) *The principle that adequate time must be given for a response.* As explicated in paras 3.5-3.9, the time allotted for CP24/11 is substantially below the average of 12 other PSR consultation exercises for APPF, and is qualitatively different to two consultation exercises with equal or lower allotted times. It should also be noted that the decision to reopen the consultation on 4 September 2024 falls only one month before the effective date of the reimbursement scheme on 7 October 2024.

3.15. It has been widely reported that the PSR has been subject to intensive pressure and lobbying by government ministers and fintech firms in advance of the publication of CP24/11¹¹. These reports, along with the problems discussed in the foregoing, **raise doubts on the procedural fairness and propriety of the exercise.**

¹⁰ Payment Systems Regulator. ‘PS23/3: Fighting Authorised Push Payment Fraud: A New Reimbursement Requirement’, 7 June 2023. <https://www.psr.org.uk/publications/policy-statements/ps233-fighting-authorised-push-payment-fraud-a-new-reimbursement-requirement/>; Payment Systems Regulator. ‘CP 23/6: APP Fraud: Excess and Maximum Reimbursement Level for FPS and CHAPS’, 15 August 2023. <https://www.psr.org.uk/publications/consultations/cp-236-app-fraud-excess-and-maximum-reimbursement-level-for-fps-and-chaps/>.

¹¹ Quinio, Akila, and Lucy Fisher. ‘Head of UK’s PSR Steps down as Regulator Faces Fraud Rules Backlash’. *Financial Times*, 31 May 2024, sec. UK financial regulation. <https://www.ft.com/content/f369205f-1ed1-48fb-a04e-ca88f2b279bf>; Quinio, Akila, Martin Arnold, George Parker, and Michael O’Dwyer. ‘UK Regulator to Slash Maximum Fraud Losses Banks Are Forced to Cover’. *Financial Times*, 3 September 2024, sec. UK banks. <https://www.ft.com/content/69611fac-03a2-4731-b12e-bf1583219270>.; Quinio, Akila, Martin Arnold, George Parker, and Michael O’Dwyer. ‘U-Turn on Fraud Refunds Prompts UK Payment Companies to Call for More

- 3.16. The imbalance of power and available resources between PSPs and PSUs in influencing PSR decision-making cannot be overstated. The PSR must have regard to the needs and circumstances of PSUs, and their ability to mobilise a credible response within the available timeframe. As it stands, **it is unclear how the PSR has sought to address this imbalance of power in its approach to CP24/11.**

4. Potential remedy

- 4.1. To summarise, Section 2 highlighted that the PSR has overstepped its mandate by concerning itself with the prudential and solvency risk management practices of private firms, primarily smaller PSPs. In doing so, the PSP has potentially disadvantaged other market participants.
- 4.2. Section 3 argued that the PSR's approach to CP24/11 does not adhere to two of the four Gunning Principles, and the manner through which the consultation exercise has been conducted brings into question its procedural fairness and propriety.
- 4.3. In addressing the concerns raised in Sections 2 and 3, the PSR may wish to reconsider its approach to CP24/11. One potential remedy is to reformulate the provisions within CP24/11, which seek to re-evaluate the maximum level of reimbursement after the policy has been in place for 12 months.
- 4.4. Instead, the PSR should consider retaining the maximum reimbursement level of £415,000, which had long represented its position following a substantive consultation period. A re-evaluation of the claim limit should then be conducted within 12 months of the implementation date of 7 October 2024.
- 4.5. This remedy has the advantage of overcoming the procedural propriety and fairness concerns associated with CP24/11 and allows time for the PSR to undertake an evidenced-based market impact assessment post-implementation.

5. Conclusion

- 5.1. Despite the foregoing concerns on the PSR's approach to CP24/11, the regulator's work in improving the outcomes for APPF victims, and increasing transparency in APPF performance by PSPs should be applauded. In particular, the publication of APPF performance data, including detailed comparison between firms, has facilitated scrutiny on the highly uneven fraud management systems and controls within the payments market.

- 5.2. This improvement in transparency has helped identify industry outliers. In November 2023, the Financial Conduct Authority imposed restrictions on one small PSP, following the PSR's publication of APPF data which showed the firm received more APPF payments per transaction than any other PSP¹².
- 5.3. The PSR's positive contribution in developing a balanced and proportionate solution to the devastating consequences of APPF should be recognised. Eight years have passed since the Consumer Association highlighted the serious detriment faced by members of the public, and the poor conduct of some PSPs in responding to their plight¹³. The PSR is accountable for addressing this imbalance of power between users and operators of payment systems, and its response to the handling of CP24/11 is a unique opportunity to demonstrate this leadership.

¹² Donal Griffin. 'UK Payments Firm With Russian Ties Had 1-in-5 Shady Transactions'. *Bloomberg.Com*, 2 November 2023. <https://www.bloomberg.com/news/articles/2023-11-02/uk-payments-firm-with-russian-ties-had-1-in-5-shady-transactions>.

¹³ Which? 'Which? Super-Complaint: Consumer Safeguards in the Market for Push Payment', 23 September 2016. <https://www.psr.org.uk/media/t0sln5vn/which-super-complaint-sep-2016.pdf>.