

10 April 2008

Dear Sir / Madam,

BACS' RESPONSE TO THE TRIPARTITE CONSULTATION

This is the initial response of Bacs Payment Schemes Ltd to the tripartite consultation on financial stability and depositor protection published by HM Treasury, the FSA and the Bank of England.

The UK Payments Council is also responding, on behalf of its members, and Bacs has had input to their document.

Bacs supports, in principle, the five overall objectives of the consultation proposals and believes they could bring benefits to customers and the payments industry if effectively implemented:

- Strengthening the stability and resilience of the financial system;
- Reducing the likelihood of individual banks facing difficulties;
- Reducing the impact if, nevertheless, a bank gets into difficulties;
- Providing effective compensation arrangements in which consumers have confidence; and
- Strengthening the Bank of England, and ensuring effective coordinated actions by authorities.

Looking at those with a potential impact on the Bacs Scheme:

Reducing the likelihood of individual banks facing difficulties - Oversight of payments systems

- Bacs considers that the current Bank of England oversight regime for payment systems already provides effective control using its ten Core Principles. Against these Bacs scores well. In the 2007 Payment Systems Oversight Report Bacs is assessed as fully observing four of the Core Principles, broadly observing a further five and being partly observant on only one (concerning the length of the clearing cycle). Work is ongoing to move further towards full observance.
- The Bank of England is close to the Bacs payment and settlement issues. It is not clear what additional benefits would be obtained by putting the oversight onto a statutory basis, but Bacs would support a review of the Memorandum of Understanding to strengthen the current framework.

- Oversight of all payment systems should be the responsibility of one body rather than a split resulting from CHAPS, as a “systemic system”, being under the Bank of England, and the other payment systems moving to the FSA.
- Even if the FSA takes over this role the Bank of England will need continued dealings with each payment scheme to maintain its understanding of the system and support its role as settlement service provider.
- Any new regime for payments systems oversight should be flexible and of “light touch” and there should be no duplication. (Question 3.6)
- Elements facilitated through statutory powers should be the minimum necessary to ensure there is no failure of a payment system. (Question 3.7)
- The European model for oversight of payment systems used in every other country in the EU has the central bank as the overseer on the basis that central banks are central to payment systems. This is also the case in many other countries.
- Bacs understands that further consultation will take place on the oversight proposals and would like to be involved in this process.

Reducing the impact if, nevertheless, a bank gets into difficulties

- In principle Bacs supports a special resolution regime to protect banks, the payment systems, and customers and believes that Building Societies should be subject to the same regime. (Question 4.26)
- There needs to be no uncertainty in respect of action to be taken by payment schemes when a bank gets into difficulty and is subject to coming under the provisions of the Special Resolution Regime (SRR). Schemes need to know if action required is different from that laid down in its legal documentation, especially with regard to settlement and exclusion from a scheme. Provision for this may need to be made in advance in schemes’ legal documentation.
- A bank that is under the provisions/responsibility of the SRR must meet all the same settlement obligations as any other member and as it had prior to the SRR being invoked.
- Effective realisation of collateral provided to the BoE in connection with carrying out its responsibilities in relation to financial stability (1.35) should provide certainty of settlement at the point of insolvency of a Bacs member.
- Any moves or changes of ownership must preserve the authority of the signatories to the legal agreements of the scheme, and the solvency of the failing bank. Any insolvency, however temporary, will render the scheme agreements null and void, and result in the exclusion of the failed bank.
- Bacs would need to understand the effects of any adjustments to the “...contractual relationships between the bank and other parties” and the “...temporary suspension of the ability of counterparties to treat the Authorities’ action as an event of default” discussed in paragraph 4.23. Any change in the status of the contractual arrangements may cause problems for the Bacs Settlement Agreement, the Payment System Rules and the LFCA.

- Any such arrangement must provide an ongoing ability for customers to make and receive payments in the short term and transfer their business to another bank in the longer term. This will require the preservation the bank sort code allocation for routing purposes. (Question 4.6)
- Payment systems need to consider their ability to respond to increases in payments traffic caused by the moving large numbers of retail deposits from a failing bank to another provider.
- Bacs supports the move by the FSA to work with indirect members of the payment systems, agency banks, to ensure that they have contingency arrangements with another Bacs Member which can be put in place quickly in the event that their sponsor bank fails.

Providing effective compensation arrangements in which consumers have confidence

- If the customer's new bank is known (by some pre-arranged agreement between a bank and the FSA) Bacs Direct Credits can be used to transfer customers' money to another bank as an interim arrangement prior to the customer deciding on his final choice of new bank. If the funds are deposits rather than current account funds immediate withdrawal may not be required in all cases. (Question 5.9)
- Bacs does not support the portability of account numbers. This issue has been discussed previously with a number of regulatory bodies including the Payments Systems Task Force which concluded that account portability is too costly and difficult to implement for little real value. In a recent response to the EC Consultation from the Expert Group on Customer Mobility in relation to Bank Accounts the Payments Council noted that the proposal was contrary to the use of BIC and IBAN only recently implemented for EU payment systems.
- If banks can open a new account in one week and the FSCS can provide prompt payment of funds via Bacs Direct Credit or the new Faster Payments Scheme (rather than by issuing cheques) then the remainder of the switching activities can take place using the Transfer of Direct Debits and Standing Order process (ToDDaSO). The Bacs Direct Credit service can transfer funds between accounts in three working days. The Bacs "Account Switching Working Group", with its delegated authority to coordinate action on account switching matters on behalf of the wider banking industry, is addressing ways to improve the end-to-end account switching process. (Question 5.30)
- It is not necessary for the full switching process to complete in order for funds to be transferred either into or out of new accounts. This core facility can operate for both debits and credits within three days to give the customer confidence that deposits are safe. Other elements of the new account such as chequebooks and plastic cards can be made available subsequently.
- A sudden massive increase in the numbers of accounts being switched could cause capacity problems for banks and originators. This in turn could be expected to cause delays and a deterioration of service with regard to the switching process.

Yours sincerely