

FUTURE PAYMENTS FORUM

19th September 2023 Meeting Review

The Forum met to consider the future of payments from the perspective of retailers and looked at those things that could be used as alternatives to the current payment services that we rely on today. Notably we considered the role of cash in society and its potential replacement with digital alternatives and the opportunity to use account-to-account payments at point-of-sale.

Dr Geoffrey Goodell, Lecturer, UCL, began the meeting by presenting his analysis of the payments market and its current challenges and then set out his alternative solution. It was interesting to have the distinction between the role and responsibility of a bank and that of a payment company set out so clearly and the debate in the forum recognised that this distinction may tell us why banks should not be the arbiters of the future of payments. A key point to note was that the current system of bank-based payment services creates a huge set of inefficiencies that could be eliminated by the correct design of digital cash. The conversion from one organisation's internal accounting token (casino chips was the term used by Geoff) to another's via the hands of third parties (central bank clearing structures) and various other intermediaries creates constraints on what is possible today and critically causes payments to be more expensive than they could be.

Geoff described his alternative to this model that essentially achieves the same outcome as physical cash in terms of the citizen's control over the token of exchange and privacy in its use, without reliance on a centrally controlled party, with ease of processing (compared to block chain processed cryptocurrencies) and at a potentially lower cost of cash. The forum debated this approach and recognised its value, but the discussion focused on the challenges of making this change happen given the tendency of all societies to favour incremental change. Evolution is preferred to revolution and in the absence of an external crisis such as covid or war, systems tend to be limited by the legacy drag of incumbent providers and their sunk cost investment in today's way of doing things. The forum considered that the current approach to the Central Bank Digital Currency is very much framed in this way. Given the potential for the solution proposed by Geoff to save money, deliver privacy and control to citizens and liberate economic activity, the forum will watch with interest how this exciting approach develops.

The next speaker was **Hannah Regan, Financial Policy Lead for the British Retail Consortium**. Hannah gave the meeting an insight into the state of payment in the part of the retail sector the BRC represents. It was surprising to note that resilience of cash usage despite government demonising cash as a transmitter of disease during the covid crisis. 15% of customers continued to use cash and the forum discussed the latest news from UK Finance that suggested a growth in cash usage in recent months. Hannah suggested that this was due to cash usage outside of retail and that her members reported a continued fall in use. For advocates of cash, she reassured the forum that her members remain committed to accepting it. Hannah shared the views of her members on the current costs of debit and credit cards and it is no surprise that her members state that they are too high. There was a debate in the room about the actual cost of card payment in the UK and it was interesting that the range expressed was from "3 to 4 percent" for smaller retailers to as low as 3 basis points (0.003%), of transaction value for major retailers with low-risk product sets.

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Given that this is a key economic point for anyone hoping to drive change in the PoS payments sector it would be useful to have a shared understanding of the market costs. Notably Hannah drew the forum's attention to the increasing costs of card scheme processing fees and the bewildering development of new fees that has occurred over recent years and especially since interchange was capped. The forum recognised that there was more regulatory interest in this area and that it would become the subject of investigation. Hannah then described what retailers want in an alternative payments system and the forum discussed the challenges of implementing any new service. The BRC are supportive of account-to-account payment services and welcomed innovation in that direction. However, it was agreed that while they can be cheaper than current methods for higher value transactions (above approximately £50) the lack of a unifying brand (e.g., Pay by Bank) and the challenges and cost of implementation at scale (i.e., to achieve meaningful uptake and acceptance) are considerable and require deep collaboration between competing providers of solutions. The forum discussed the likelihood of this happening and the role of the current regulatory, trade and other influential bodies in making this come about and it was agreed that it seems unlikely at present.

In our final session **Chris Moore, CEO** and **Phillip Godden, Director of Products of Kikapay** showed the forum what is possible using Open Banking to deliver payments at point-of-sale. They explained the benefits of A2A payment compared to card payments. They then demonstrated three use cases of A2A payments at the point-of-sale and showing A2A is clearly viable from a technology perspective. They demonstrated a charitable donation which can be initiated using a simple QR code and applied to any fundraising situation face to face. There was a QR code generator enabling staff of small shops to take an A2A payment. There was also an embedded payment in a high street retailer app which, in the case of the demonstration, combines with RFID tags and barcodes in the physical store to allow consumers to select items in store and pay for them without needing to go to a centralised check-out location.

The in-store environment is a place of conflicting challenges such as prevention of theft, payment efficiency, staff training and customer experience. It is for these reasons A2A solutions in general are taking off slowly. However, it is clear that such ideas will come to influence the design of stores in the future.

There are challenges of A2A payment at PoS. Speed of the customer journey is an issue as each payment needs to be authorised at the consumers bank meaning each payment takes up to 30 seconds. The cost saving of using A2A increases with higher value transactions so A2A becomes more attractive in certain retailers e.g. high value transactions where only a few transactions occur each hour e.g. those selling high value goods that need certainty of payment such as high-end watches, second hand cars professional services, there is clearly a market today. Many of the challenges for A2A at point-of-sale can be resolved in the next version of Open Banking payments which is Variable Recurring Payments which the group then discussed.

The forum agreed that the primary challenge remains the creation of a common approach (branding, usage etiquette, etc.) at PoS to encourage adoption and usage by consumers. Since most consumers receive their payment products as part of a free banking package and the products work well, everywhere, it's hard to see what incentive they can be given to drive market change.

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In summary, the current solutions for payment are powerful and dominate. The costs are rising and opaque. There are alternatives that could substantially address the needs of the market however they require something to force them into the market. In the past, crises have driven change (e.g., covid driving the adoption of contactless, fraud driving the creation and roll out of Chip and PIN), however there is no obvious crisis that will drive the change that is needed today. For consumers that care about privacy and control over their wealth and retailers that want to repatriate most of the current cost of payments, the primary challenge is to mobilise the citizenry to demand change.

Next Future Payments Forum Meeting: Tuesday, 14th November, London

If your organisation would like to present at a future meeting, please contact Annabel Cartwright at annabel@smartex.com

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