RESPONSE TO CALL FOR INFORMATION

CCIA response to PSR and FCA call for information on digital wallets

CCIA is pleased to respond to the PSR and FCA call for information on "big tech" and digital wallets. CCIA members operate both as competing providers of digital wallets and in a range of adjacent markets and have diverse views and interests in this evolving sector.

Outside the immediate scope of the questions posed, our view is that "big tech" as a category upon which to focus investigations is an unhelpful aggregation which both: (a) elides a diverse set of companies that interact with financial services in very different ways; and (b) introduces artificial distinctions between companies operating in similar ways, in the same sectors based on their corporate origins.

That concern notwithstanding, we believe that there are interesting issues that the call for information raises about digital wallets and their interactions with financial services. We would be keen to discuss any of the issues raised in more detail if that would be helpful to your investigation.

Question 1: What are the benefits of digital wallets for consumers, businesses and other parties in the payments value chain?

Digital wallets provide a range of benefits for consumers, including:

- Enabling choice in payments - they can more easily choose from a wider range of means of payment, e.g. different cards.
- Improved convenience - they can make a payment using their smartphone, another option alongside their card, with easy biometric authentication.
- Improved integration with their wider digital lives - e.g. making payments online without having to manually enter card and address details. This will make it easier (and mitigate perceived risks) for consumers to engage with new e-commerce providers, with whom they have not yet shared those details, facilitating competition in that adjacent sector.
- Mitigating fraud. Consumers benefit from the wider expertise of digital wallet providers in security, trust and safety being available as an option for making digital payments. This requires ongoing investment and innovation on the part of digital wallet operators as fraud can otherwise rise.

Regulatory policy should focus on securing those benefits that consumers currently enjoy and avoiding any unintended risks to that experience.

Several factions indicate that consumers derive considerable benefits from the availability of digital wallets: most users have easy access to other means of payment (e.g. cards) and use digital wallets for some share of their overall spend. Those consumers could easily reduce that share if they did not find a digital wallet helpful. While the call for information document (Figure 3) argues that consumers' choices between digital wallets can be limited on some stores, in every case shown consumers have access to choices that match what would exist without digital wallets (i.e. a normal range of credit, debit and store cards) and includes multiple providers (at the issuer and scheme level).

At the same time, the variation in the digital wallets offered by retailers reported by the consultation document (Figure 3) speaks to those merchants having practical choice over which wallets they choose to accept. Regulators have expressed the concern in the past that the four party card schemes might be a de facto requirement for merchants. It seems inconsistent to argue that a situation in which merchants are choosing which wallets to accept is also evidence of a problem.

Policymakers should be comfortable with a situation in which there is a plurality of options and merchants and consumers can choose freely between accepting and using various payment instruments.

Question 4: Are there any features related to the supply of digital wallets that cause harm to (or mean that payments could otherwise work better for) service users?

There are some inherent challenges in building a payments product of any kind:

- Establishing a product useful to viable groups of users, appealing to both consumers and retailers.
- Establishing the necessary technical infrastructure.
- Meeting regulatory expectations, for example around security.
- Business relationships will often be required with other financial services institutions, e.g. banks.

Digital wallet providers have had to invest in order to meet those requirements.

In a market in which the goal is to connect those sending and receiving payments, the socially- and commercially-optimal number of payment services in any given segment may not be radically large. With customers only needing a limited number of payment products, in a relatively mature payments market such as the UK, any new product will need to be distinctive in order to establish itself. Digital wallets are relatively recent challengers in the context of retail payments and have had to establish that differentiation.

To the extent that policy either raises the challenges of creating new networks; imposes some degree of compulsory standardisation; or poses a risk to realising a commercial return it could exacerbate these challenges. This could then lead over time to a reduction in innovation and an increase in the quality-adjusted price of payment services.

Question 5: Please explain whether any harms identified in your response to Question 4 could be outweighed by benefits associated with those same features – for instance, in terms of greater convenience or security. Where available, please provide supporting evidence.

Even to the extent policymakers are concerned about barriers to entry in the payments market generally, there is apparent static and dynamic competition in the digital wallets segment specifically. Various kinds of businesses have been able to establish wallets including consumer-facing payments companies (PayPal), providers of mobile ecosystems (Apple, Google) and merchant-facing payments companies (Stripe). These services vary in ways that are important for wider regulatory policy, but in every case they fulfil a similar role for merchants and consumers, mitigating frictions in digital payments and e-commerce more generally.

This should not be seen as surprising given that the basic requirements are held by a broad range of businesses operating digital platforms: an active relationship with a threshold volume of merchants and/or consumers and technical infrastructure. In other markets, payments services of this sort have been established by companies from an even broader range of sectors. In Indonesia, for example, a prominent digital wallet (GoPay) was created by a platform with its origins in courier delivery and ride sharing (GoJek). To the extent digital platforms are commercially-attractive, more of these companies will have an incentive to enter the market, dynamic competition will be achieved with entry from adjacent sectors.

Outside of dynamic competitive constraints, the other major mitigating factor that should be considered in terms of potential harms resulting from digital wallets is that many of the companies operating them are doing so as a means to improve the functionality of devices and wider digital platforms. This naturally aligns the incentives of the providers of the digital wallets with the wider consumer and economic interest in high quality payment services.

Generally speaking, with a strong incentive and technical capabilities to deliver innovative services, companies with technology backgrounds outside the financial services sector are likely to raise the overall pace of improvement in payments, bringing distinctive innovations and mitigating rather than contributing to challenges establishing competitive markets in financial services.

Question 6: If you think that there are features that result in harm, what measures would be effective and proportionate to improve outcomes?

Specific measures are not needed with respect to mobile wallets in the UK at this point, with the consumer experience positive; merchants choosing freely between services; and new services still being established relatively recently (e.g. Stripe Link in 2021).

In considering new measures, we would generally recommend as a priority avoiding the creation of a broad policy risk to companies expanding their digital wallet offerings, which diminishes the strategic case for new entrants from adjacent sectors or existing providers expanding their offerings. This could be avoided through a mix of restraint in regulatory intervention to the extent markets remain dynamic and clarity over the conditions under which regulatory intervention is less likely to be pursued.

Question 9: What role could digital wallets have in increasing the take up of account-to-account payments in the UK retail sector?

Customers have a “good enough” experience through existing card rails and so the tolerance for any inconvenience is relatively low. This has been a barrier to account-to-account payment solutions in the past, where they have required customers and/or merchants to pay in ways that they were not familiar with and were more challenging than conventional card payments. This is where digital wallets could help by integrating account-to-account payments alongside cards as an alternative. However other barriers remain that are not automatically or easily resolved by digital wallets.

Question 10: Are digital wallets likely to integrate existing and potential account-to-account payment types, including for spontaneous purchases? If not, what barriers exist and what do you think needs to happen for digital wallets to integrate account-to-account payment types in a manner that enables effective customer access to them?

There are several barriers to establishing account-to-account payments in UK retail that are only partially mitigated by digital wallets.

Any new service needs to establish merchant acceptance and this may be challenging to the extent they do not start with a large consumer base. While digital wallets could ease the path to merchant acceptance, acceptance for digital wallets does vary more than for card schemes

(Figure 3 in the call for information) and acceptance of a pass-through digital wallet does not entail acceptance of every payment rail offered (e.g. if a merchant does not accept American Express generally, that will not be an option to pay through Apple Pay).

This means a digital wallet provider or specialist business seeking to develop account-to-account payments through digital wallets would need to invest or provide a differentiated service to merchants. Regulators should bear this in mind in terms of establishing a regulatory framework for digital wallets that permits such differentiation. If they are interested in the role of account-to-account payments as a means to enhance competition in retail payments, it will also be important to bear this in mind in the signals sent to digital wallet providers by any regulatory actions following this call for information (providing some form of safe harbour guidance would be one way to mitigate the risk that regulatory risks discourage such services). If there is a sense that companies in adjacent technology sectors are generally assumed to be problematic, that will make it more difficult to justify investments in this and other expansions in services.

More broadly, any service would need to establish substitutes for practical functions carried out by card rails and not as part of conventional account-to-account payments at present. This is where partnerships with specialist financial services businesses are likely to be important (either new providers offering their services alongside cards through digital wallets, or as part of digital wallet providers themselves building such solutions). The regulator could consider whether there are gaps, or where it might be able to support increased provision in areas under-served by an existing market that assumes card payments. However it should do so with a realistic view that the principal barriers to account-to-account payments are not in the operations of digital wallets themselves.

Question 12: What harms are likely to arise in the event of a digital wallet provider's operational failure, either now or over the next five years?

It seems unlikely that a large number of consumers or a large number of merchants will no longer have access to card payments and other alternatives to digital wallets in the coming 5 years. This naturally limits the impact as those alternatives can be substituted in the event of a failure.

The more likely risk is in specialist business services supporting niche elements in the payments function, where the resource to mitigate potential failures might be more limited and there is less potential for those affected to quickly substitute alternative solutions. The recent Crowdstrike failure is a potential example. To the extent such a failure affected digital wallets, it would likely do so through and/or alongside its impact on banking and other financial institutions.

Question 14: What do you think are the likely impacts of digital wallets integrating with open banking – for example, in terms of users' access to financial services, security, or any privacy issues that may arise?

Additional consumer value might be created through the integration of digital wallets with other financial services. While at this stage our understanding is that CCIA members and similar businesses are not using Open Banking data,[1] integration could in principle allow consumers to use convenient digital wallets as a platform to access and integrate relevant financial services data and enable new services such as account-to-account payments.

Given the relative sensitivity of the data that digital wallet providers already process, and the capabilities associated with offering a digital wallet, they do not seem like the most likely to be a point of failure in terms of security, privacy and other consumer protection priorities. While these issues are obviously important they should be addressed in the same way as other Open Finance use cases.

As far as possible, regulators should aim to avoid picking winners in terms of use cases for Open Banking, or restricting the regulation based on less relevant characteristics (such as size or sector) of the firms receiving the data (again, see our earlier consultation response for more on this point). This will maximise the benefits of Open Finance data sharing.

Question 15: Are there any significant issues in relation to consumer rights and protections that could become relevant in the future? For instance, how significant is the risk that payment firms start to introduce new payment services through digital wallets that could disadvantage consumers without smartphones?

Given the broad reach of smartphones, over 90% of the population on recent estimates and rising, and the availability of most financial services outside of digital wallets, any risks will be speculative. New payment services introduced through digital wallets could play an important role in realising payments innovation (see the analysis around account-to-account payments

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[1] This is covered in more detail in an earlier CCIA submission to the FCA regarding potential data assymetries: https://ccianet.org/library/ccia-response-to-fca-call-for-input-about-competition-impacts-from-the-data-asymmetry-between-technology-companies-and-companies-in-financial-services/

above) and regulators should therefore proceed cautiously with any limitations on such benefits.