

**Featurespace response to PSR
consultation on Authorized
Push Payment (APP) scams
requiring reimbursement**

**F E A T U R E
S P A C E**

OUTSMART RISK

Featurespace recently welcomed the opportunity to respond to the Payment System Regulator (PSR) in its call for input on its proposed reforms to Authorized Push Payment (APP) scams, requiring reimbursement for victims.

This document contains both the Featurespace response to the specific questions posed by the PSR under **CP22/4: Authorized push payment (APP) scams: Requiring reimbursement**, as well as Featurespace's position on the wider aims of the proposed regulatory reform to UK financial services.

Featurespace on the State of Fraud in the UK

The PSR has long recognized the need for improvement in making the UK a safer place to transact. Fraud has grown to become the largest contributor to crime in the UK. Authorized Push Payments (APP) represent a significant proportion of UK fraud, more than 40% of total fraud values. In the first half of 2022 criminals stole a total of £609.8 million through authorized and unauthorized fraud, with £249.1 million lost to APP scams¹. Although the number of cases has decreased by about six percent, there remains much to be done when it comes to limiting the negative impact of fraud on the consumer. The number of fraud cases in which consumers were refunded is rising and the speed at which this is resolved is accelerating, which shows a strong commitment from the financial services industry to limit the impact on consumers. However, despite these improvements and acts of good faith, as the Contingent Reimbursement Model (CRM) is voluntary just 56 percent of consumers were

refunded in the first half of 2022. This clearly evidences the need to apply more regulatory pressure to ensure a fair and consistent approach to consumer protections in the face of fraud.

Regulating for collaboration

The proposed mandates are right and fair in that they ensure the swift refund to victims of fraud. It does appear that in the pursuit of consumer protection, there is a danger that additional operational complexity, technology overhead, and resource requirements are being created as a burden for financial institutions (FIs). The provision for adjustments to loss allocation through arbitration seems contrary to the overall aim: to fight back against fraud. Creating the provision for disputes between sending and receiving financial institutions could perhaps detract from the positive industry collaboration we have seen to date. And has the potential to divert attention and resource from innovations that could drive down fraud in its entirety, not just ensure refunds.

Consistently splitting the cost of consumer refunds equally between both sending and receiving parties is a blunt mechanism, but could ultimately create efficiencies in operations for all participants and drive an intensified focus on fraud reduction from both sending and receiving FIs. Creating a more active role for 'receiving only' FIs, often smaller Payments Service Providers (PSPs), brings their fraud prevention responsibilities in line with their access to financial services licensing and the payment systems under Open Banking and the New Access Model. To combat rising fraud operations by organized criminals there is a need to perform fraud

¹ 2022 Half Year Fraud Update, UK Finance

prevention on both outbound and inbound payments, and the inclusion of all PSPs in this proposal is a great step towards achieving this end-to-end fraud prevention approach in the UK ecosystem.

Achieving complete fraud prevention is not limited to FIs. Even in the proposed updates, there is not as yet any responsibility for those organizations on whose platforms' fraud is executed. With APP in particular, social engineering is often conducted through social and telecom networks yet there is no explicit provision for these organizations to participate in these anti-fraud measures.

Missing innovation

Regulated reimbursement treats the symptoms of fraud, but does not go far enough in tackling the disease itself. There are several clear gaps in the proposal.

Data collection and sharing

Early iterations of the consultation process indicated that centralized reporting, collection, and even publishing of fraud data would be a part of the framework. This version appears to discount this from the proposal. It is important to remember that fraud prevention is not a competitive differentiator for banks, and that the aim is to ensure that the ecosystem and economy is protected, however it is near impossible to effectively tackle fraud when there is no register of the true size and shape of the problem.

Card schemes have historically always collected fraud data in order to support members who are struggling with new trends and typologies. This would be an important role for the PSR to play in supporting its member to understand best practice.

Technology for transparency

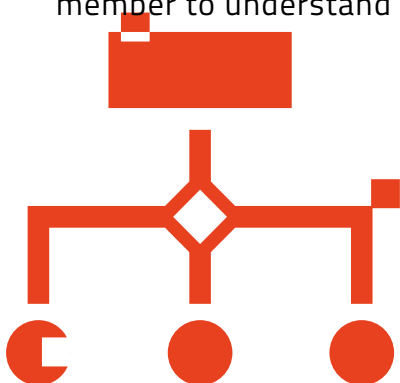
Under the current proposal there is no provision for the technical payment flow for cost sharing of the reimbursement from the receiving bank. There exists the opportunity to leverage both existing technical capability within the UK Faster Payments System (FPS) and future functionality planned under the New Payments Architecture (NPA).

The Request to Pay (R2P) messaging system could be leveraged by sending banks to facilitate the retrieval and reconciliation of 50 percent of refunds provided to victims of fraud, from receiving FIs. R2P was purpose built to improve the ease of reconciliation of inbound FPS, and many UK FIs have already completed the technical integration to the system. Additionally, Pay.UK would be able to easily count and report on this category of R2P on behalf of the PSR.

In the future when the migration to ISO 20022 has been completed under the NPA, this rich, structured data messaging-standard could be leveraged to create more transparency from receiving FIs in relation to transactions declined on suspicion of APP. Reason codes could be populated into the returned message that enable sending banks to augment their fraud strategies. With this enhanced transparency sending FIs would create efficiencies in fraud prevention strategies, as well as reduce the need for manual investigations, and ultimately improve the consumer experience.

Liability practicalities

There is some discussion within the financial services community as to whether the split of liability on fraud losses could in fact be removed from the proposal all together, in favor of beneficiary banks retaining 100 percent of recovered funds. This could reduce the complexity and overhead of refunds and loss-sharing, although perhaps does not meet the aims around equal participation in this anti-fraud initiative from all FIs. Receive-only PSPs who would be motivated to tackle their mule accounts under liability sharing, would in fact feel a significant benefit of retaining



those as long they were able to prevent the fraudulent funds leaving their institution toward their final destination. Obviously, all UK FIs want to tackle this national issue of fraud, but the proposal needs to be fair in its division of responsibility and cost to ensure that we move as one ecosystem.

Featurespace would not recommend repatriation of funds throughout an entire fraudulent transaction flow. The complexity of this and the diminishing returns of cost-sharing 50 percent of fraud losses throughout an entire disbursement tree would again create inefficiencies and detract from the higher purpose of preventing fraud. Instead, simplifying the scheme rules to provide an equal split on the fraud losses of each individual transaction between the sending and receiving bank would be more practical.

Future expansion

This nationwide initiative to focus the community on tackling fraud is critical. Featurespace sees this initiative on reimbursement as the first step in a much broader set of necessary reforms. Future phases would need to consider other types of users and customers, as well as other payment systems.

Business users

FPS is widely used by both consumers and businesses as a fast and efficient way to transact. Under the proposal there is no reimbursement protection for business users. For large corporations this may be simple to administer, but for small businesses often serviced by the retail arm of the bank it may prove challenging for FIs to enforce this from a customer service perspective. It is likely that independent traders and small business owners will expect the same Service Level Agreement (SLA) of protection for their personal and professional transactions.

If the reimbursement regulation is viewed primarily as a quick measure to protect consumers whilst the industry works to get fraud under control, then this may not prove to be a sticking issue in the long term. It is

possible that even business users would expect the same protections to be extended to their transactions on the same payment system eventually. This could present a very different risk profile for FIs in relation to potential reimbursement costs, as the transaction limit for FPS has been lifted to £1 million.

Payment types

Much of the proposal on fraud reimbursement could easily be applied to other UK payment schemes such as BACS and CHAPS, which prompts the question as to why these rails are not considered holistically within the PSR's proposal. Historically, fraud has migrated from payment type to payment type, avoiding each new effort to stamp out fraud on a payment rail. There is a possibility that current fraud conducted via APP will simply migrate to other rails if criminals deem it a more 'profitable' approach. If this should happen, those large banks that offer the full spectrum of payment services to their customers could once again be left bearing a disproportionate amount of the total cost of UK fraud.

Driving down the total cost of fraud

The cost of fraud reimbursement for consumers has to be funded from somewhere within the UK economy. There is a risk that inadvertently the consumer will end up paying this cost.

Larger banks who are members of the voluntary CRM code have already invested extensively, and the changes will still require further investment. There is a risk of some UK PSPs and fintechs being unable to bear this increased burden which may not be relative to the current size of their revenues. The UK has a thriving fintech scene, with more than 250 licensed PSPs (Electronic Money Institutions) (the highest number in Europe), which creates competition in financial services and choice for consumers. In theory these fintechs should be able to quickly adapt and create solutions to reduce fraud rates and therefore liability. If this does not happen in practice, the cost of fraud reimbursement

could collapse this fintech sector, and the choice of services will be restricted for consumers.

As FIs recalculate the total cost of fraud to include increased reimbursement, this may by default create an increase in the cost of financial services for consumers. This could be directly in the form of increased charges for services, or as indirectly as limited investment in innovation by FIs.

Changing customer behaviour

One factor that has been clearly evidenced since the launch of FPS, is the role of customer education in understanding the benefits and potential risks of a new payment system. Many larger FIs have moved to provide proactive and continuous education to their consumers. There should perhaps be a component of the proposal which includes a mandate to educate consumers. The burden of education is currently disproportionately born by banks.

There is rightfully some concern that we may see an increase in first-party fraud once the regulation is well publicized. More concerning is the increased possibility of collusion in a cost-of-living crisis, with criminal networks looking to recruit consumers into their schemes, likely as money mules. Financially vulnerable consumers may become targets for criminal recruitment.

Within the realm of consumer behavior, there is not a clearly defined framework for the gross negligence exception that the proposal allows for. Leaving this too open to interpretation risks placing the most vulnerable consumers at risk, in contradiction of UK financial inclusion policy aims. Any consumer can be vulnerable at any point in their financial services relationship.

There is some discussion of whether there will be a diminished sense of responsibilities from consumers once they no longer carry the risk of scams losses. However, the reality is that it is not the responsibility of the consumer to prevent scams. It is a broader policymaker, law enforcement, and private industry responsibility to safeguard the financial ecosystem and the economy at large.

Unreported scam volumes

What is likely is that with the change in reimbursement entitlement, that the industry will see a change in fraud rates. Romance scams in particular are likely vastly underreported, as victims feel embarrassed and unwilling to go through the turmoil of seeking reimbursement without a guarantee. With the legislation change, currently unreported scams will surface. As an industry we currently only see the tip of the iceberg, and it would be advisable for FIs to increase their fraud prevention budgets for 2023 onwards. Perhaps seeing the true extent of the problem in relation to the bottom line will support fraud teams in achieving sign off for their business case.

Inbound transaction monitoring

The extension of liability for fraud losses to receiving banks is an important step. But the question remains whether the proposal goes far enough in preventing criminals from accessing stolen funds.

Repatriation of APP scam losses occurs where the receiving PSP is able to detect, freeze and return funds stolen as part of an APP scam. Rapid and effective communication from the sending PSP may aid receiving PSPs in detecting and freezing fraudulent funds.

Transaction monitoring on inbound payments for the purposes of fraud prevention would be more effective in preventing criminal networks from profiting from scams, and simplify the repatriation and reimbursement process. There could be guidance from the PSR to include inbound transaction monitoring as a recommended line of defense against APP.

Thresholds clarity and relevance

The provision of thresholds in terms of both a minimum limit and excess complicates reimbursement understanding for consumers. If the excess is £35 and the minimum limit is £100, will a consumer claiming for £135 believe they will receive nothing? This could be simplified by expressing the excess as a percentage of the claim rather than applying both and would also make the limits fairer for consumers who may only lose £50, for whom it was their total account balance. A 5% excess in this case would be enough to illicit caution in future in the same way a 5% excess for a much larger claim would. The excess or lost cost for the consumer should be proportional to the total fraud if the aim is to both protect customers and encourage vigilance against scams.

There is a potential downside to defining thresholds, in that they could have the unanticipated consequences in driving fraudsters to adapt their tactics to target scams beneath these thresholds in order to avoid the investigative scrutiny of FIs, and their pursuit of funds for recovery. Or, if thresholds are applied across cases rather than individual transactions there is a possibility of creating first-party fraud, where customers may benefit from sending another scam payment so that their claim is over the threshold.

Making the UK a safer place to transact

As an industry it is necessary to address the current impact APP is having on consumers. It is neither right nor fair that consumers are bearing the costs of rampant fraud in the UK. The proposal in its current form appears a fairly blunt instrument. It may or may not eventually reduce the overall fraud levels in the UK. The missing element is the focus on making the UK a safer place to transact. Featurespace would welcome more specific mandates on driving down fraud rates, perhaps taking inspiration from the low-risk thresholds applied in Strong Customer Authentication (SCA) exemptions under

the Revised Payments Services Directive (PSD2), as this incentivizes low fraud rates. Complexities will of course arise as this consultation becomes policy in UK payments, and Featurespace is confident that the PSR will look to continually optimize APP fraud prevention measures as the practicalities play out and the market needs evolve.

All of this creates a massive incentive for UK FIs to invest in fraud controls, and particularly in technologies which can outsmart criminals. As an industry there is a lot of opportunity to apply machine learning, and in particular deep learning techniques to improve fraud prevention rates on both outbound and inbound payments.

Working with one large UK bank we have been able to deliver a huge reduction in false positives (over 90%) and massive improvement in the Value Detection Rate (~250%) for APP scam detection.

Learn more about Featurespace's approach to scam prevention.



Response to CP22/4: Authorized push payment (APP) scams: Requiring reimbursement

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Do you have views on the impact of our proposals on PSPs?

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- that there should be a consumer caution exception to mandatory reimbursement
- to use gross negligence as the consumer caution exception
- not to provide additional guidance on gross negligence?

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Do you have comments on our proposals that:

- sending PSPs should be allowed to apply a modest fixed 'excess' to reimbursement
- any 'excess' should be set at no more than £35
- PSPs should be able to exempt vulnerable consumers from any 'excess' they apply?

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Do you have comments on our proposals that:

- sending PSPs should be allowed to set a minimum claim threshold
- any threshold should be set at no more than £100
- PSPs should be able to exempt vulnerable consumers from any threshold they set?

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Do you have comments on our proposal not to have a maximum threshold?

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Do you have comments on our proposals that:

- sending PSPs should be allowed to set a time-limit for claims for mandatory reimbursement
- any time-limit should be set at no less than 13 months?

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Do you have comments on our proposals that:

- the sending PSP is responsible for reimbursing the consumer
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Question 1

Do you have views on the impact of our proposals on consumers?

At a high level, the proposals will incentivize increased focus on fraud prevention, and support fraud teams in securing investment for proven solutions to improve detection and increase protection for consumers.

Consumers not suffering fraud may experience increased friction, but assuming investment is sufficient, the friction will be significantly targeted, and processes will develop to ensure the net outcome is very positive for consumers. Increasing expectations of refunds will reduce stress and other detriment that consumers could suffer if they are victims of APP. However, those who are victims of lower-value APP fraud may suffer more than under the current voluntary CRM code. If their claims fall below the new thresholds, they may not receive any refund.

Question 2

Do you have views on the impact of our proposals on PSPs?

The obvious impact to PSPs is increased costs due to increased refunds and implementing new processes to manage the arbitration requirements. The indirect impact will be the response of investing in processes to make them efficient and consumer friendly, whilst also investing to reduce the number of victims and mule accounts. Regulatory pressure and compliance requirements should support building the business case within PSPs, and may even help PSPs support changes that fraud teams had on roadmap to reduce fraud and improve

customer experience. This assumes any regulatory enforcement would outweigh the cost of development. Smaller PSPs may see impacts that are disproportionate to their relative revenues, but they are also likely to develop solutions more quickly and efficiently than larger PSPs.

Question 3

Do you have views on the scope we propose for our requirements on reimbursement?

Limiting scope to FPS may lead to fraudsters targeting other payment types (even if this will be harder for criminals to facilitate), and that fraud does not reduce as much as expected. If scope could be extended to cash withdrawals, CHAPS, and international payments, then consumer understanding and expectation would be better, and the fraud migration risk would be minimized.

Question 4

Do you have comments on our proposals:

- **that there should be a consumer caution exception to mandatory reimbursement**
 - **to use gross negligence as the consumer caution exception**
 - **not to provide additional guidance on gross negligence?**
-

It is reasonable that consumers should exercise some caution in initiating transactions, in line with information and guidance from their FI. Fraud prevention can

be strengthened with consumer awareness. In reality, a single consumer who is the target of a sophisticated scam from an organized criminal network cannot be reasonably expected to spot this. It is right that the burden of prevention and protection be placed on FIs who have the resources, expertise, and technology to outsmart this risk.

Gross negligence may seem a reasonable measure for liability, but defining that gross negligence is challenging. Proving whether a customer exercised any caution has been challenging in unauthorized fraud cases, and would be the same for APP.

Additional guidance should be provided by the PSR providing clear examples and scenarios, with a focus on what the customer believed to try and avoid Financial Ombudsman Service (FOS) disputes. For example, would previous APP claims be evidence of gross negligence? At this stage it seems this may be assumed by some PSPs.

Question 5

Do you have comments on our proposal to require reimbursement of vulnerable consumers even if they acted with gross negligence?

There is a duty of care that should be exhibited by FIs in relation to vulnerable customers who may become victims of these sophisticated manipulation and impersonation scams, even if a less vulnerable customer may have been able to avoid this. Vulnerability may be both permanent and transient depending on the customer and the moment in time.

Question 6

Do you have comments on our proposal to use the FCA's definition of a vulnerable customer?

Current FCA definitions of vulnerability appear to be working in other types of fraud cases.

Question 7

Do you have comments on our proposals that:

- **sending PSPs should be allowed to apply a modest fixed 'excess' to reimbursement**
 - **any 'excess' should be set at no more than £35**
 - **PSPs should be able to exempt vulnerable consumers from any 'excess' they apply?**
-

If customer is classified as vulnerable, then applying an excess amount should not be valid.

The provision for both an excess and a minimum threshold seems to disproportionately impact financially vulnerable customers, for whom £35 is a significant amount to lose in excess. Although the intent is likely to encourage customer caution, most consumers are not aware they are a victim of a scam until after the fact. This is the element that makes APP fraud so successful for criminals and so difficult to prevent. If the excess were a percentage of the total claim, it may have an increased impact and a fairer impact on customers with varying sizes of claim and varying balance

before the fraud. For example, 5% may work better so that customers with fewer funds and smaller claims are less impacted, but larger claims resultant from higher net-worth individuals would still have an impact and lead to increased caution.

PSPs may only apply the excess to cases with some level of negligence, or certain scam types such as investment and purchase, as well as potentially applying to repeat claimants. Negligence would be challenging to prove on an individual customer basis, as the customer would not be aware that other consumers had fallen for same scam.

The approach may provide a balance in relation to caution shown by consumers and whether the consumer was looking to make a financial gain when they became a victim. The key is that not all cases should be viewed as the same, even if the typology appears similar.

Question 8

Do you have comments on our proposals that:

- **sending PSPs should be allowed to set a minimum claim threshold**
- **any threshold should be set at no more than £100**
- **PSPs should be able to exempt vulnerable consumers from any threshold they set?**

PSPs may quickly realize that they have a lot more vulnerable customers than anticipated. Once the regulation becomes public domain, advisors to victims will look to apply vulnerability every time it is relevant.

Similarly to applying an excess of £35, minimum claims could discriminate against customers with low account balances and low

claim values. It may be better not to have a minimum claim and just have an excess that is a percentage of claim. This would be simpler and remove the potential discrimination against the lower value claimants. The excess would cover the cost of processing the claims. Whether it was an excess or a limit, vulnerable customers should have claims refunded in full regardless.

Question 9

Do you have comments on our proposal not to have a maximum threshold?

No maximum threshold should not be needed as it is not relevant to the scam risk. PSPs and customers should be acting with increased caution with very high transaction values. The current proposal is focused only on consumers, however given the transaction value limit of FPS (up to £1 million) and the likelihood that similar regulation will be required for all transactions on the scheme, as well as other payment systems, beginning this regulatory reform without a maximum threshold seems prudent.



Question 10

Do you have comments on our proposals that:

- **sending PSPs should be allowed to set a time-limit for claims for mandatory reimbursement**
 - **any time-limit should be set at no less than 13 months?**
-

It seems reasonable to provide a guideline on length of time as it can become difficult to investigate a claim that is more than a year old, and for most APP, FIs could expect a customer to recognize and report a scam within these timescales. Thirteen months appears reasonable and aligns with unauthorized fraud regulations.

The challenge would be longer running scams, such as investment scams where customers think they are investing for the longer term. Or romance scams which usually happen over a long period of time, and only after larger payments do victims realize it's a scam. There is usually a long tail on romance scams and the customer is emotionally vulnerable. In these scenarios exemptions to the time limit could be offered.

Question 11

Do you have comments on our proposals that:

- **the sending PSP is responsible for reimbursing the consumer**
 - **reimbursement should be as soon possible, and no later than 48 hours after a claim is made, unless the PSP can evidence suspicions of first party fraud or gross negligence?**
-

This ensures the timely reimbursement of the consumer in cases of APP which is a positive improvement.

Question 12

What standard of evidence for gross negligence or first party fraud would be sufficient to enable a PSP to take more time to investigate, and how long should the PSP have to investigate in those circumstances?

Gross negligence is likely going to be very rare and challenging to prove. It would be better for the industry to focus preventing fraud rather than trying to shift liability back to the consumer. However, identifying whether a consumer received a targeted warning and/or data suggests a consumer is lying should be quick and could trigger several days more time to collect information and assess the case further.

Gross negligence would mean that the FI did everything within its power to identify potential fraud and advised their customer, who understood the warning and still

opted to complete the transaction anyway, believing or not caring whether they would be refunded if it turned out to be fraud. For this to work there would need to be a definition of 'everything within its power', this may include a requirement for a human interaction between the consumer and an experienced fraud analyst, something beyond an automated notification.

During scams the criminal is often on the phone with customer, instilling a sense of urgency and pressure. Criminals are aware of the FI systems and are talking victims through the process to make it happen quickly. Applying holds or cooling off periods to payments during the interaction between the fraud analyst and the consumer will be key to allowing consumers to come to terms with the reality of the scam.

In cases of first party fraud, the burden of proof would be the same as for authorized fraud cases. FIs would look to evidence that the customer has contradicted themselves in their account of the fraud and it does not align with the FI data, whilst also looking to identify links to other claims that therefore suggest organized and systematic exploitation of the claims process.

Question 13

Do you have comments on our proposal for a 50:50 default allocation of reimbursement costs between sending and receiving PSPs?

We would support a default allocation without the provision to contest between sending and receiving FIs. This shares the burden of APP more fairly across the entire financial services industry whilst providing an incentive to reduce fraud and the associated losses.

Question 14

Do you have views on our proposal that PSPs are able to choose to depart from the 50:50 default allocation by negotiation, mediation or dispute resolution based on a designated set of more tailored allocation criteria?

There should not be a process for negotiation, mediation, or dispute as this will be time consuming and deliver unsatisfactory results. The time and cost should be saved by having one allocation that applies to all APP cases.

The option to deviate from the default allocation creates a lot of operational overhead for FIs, without any indication as to the capacity requirement for processing disputes. The split could be debated for a long time overall or on every case as they occur. The 50:50 split is a sensible starting point and should be applicable in all cases unless reassessed at a future point. Debating for individual cases would be time consuming and won't deliver clear and fair outcomes either.



It could be viewed that creating the dispute process creates an incentive for those PSPs who are 'receive only' for FPS to dispute every APP case in order to minimize their loss exposure. There may be a need to apply the 50:50 split to unauthorized as well as authorized fraud to avoid PSPs looking to share losses with receiving banks, by saying their customer authorized the payment.

Question 15

Do you have views on how scheme rules could implement our proposed 50:50 default allocation to multi-generational scams?

This is a very complicated concept and would need to be divided into logic that applies to each claim, and still can flow back to the original transaction and the originating claim. In this proposal each step or generation would need to be assessed independently and then funds repatriated back to the start in some kind of tree with transactional branches. It would be more practical to treat each transaction as an individual case for allocation and avoid multi-generational liability allocations, or even remove the repatriation and allow the final FI in the chain to keep any recovered funds

As an example of the complexity of multi-generational scam refunds: funding an account in the customer's own name would result in 50% of loss coming from the sender and 50% from the receiver. This may be the same PSP in some cases. If funds are then moved on by a fraudster from the new account, then the PSP would be liable for 100% of the fraud and could then return funds to the initial PSP to remediate the situation. If funds are moved on by the customer, then a second claim is started and treated individually. If payments aren't FPS and there is no refund, then no further action is taken. If a refund is paid from a card claim, then funds can be returned. If a refund is paid by FPS, then loss would be split again. This would then lead to the second and third PSPs sharing the loss and then passing the funds back, as shared liability and shared repatriation benefit to the first to fund the claim, and mean that the first PSP doesn't have a loss. The key element would be that the refund of the middle account means full funds are available to be repatriated.

Question 16

Do you have comments on our proposal for a 50:50 default allocation of repatriated funds between sending and receiving PSPs?

50:50 allocation for repatriated funds is common sense when the refund is 50:50, but this becomes very complicated and may even have to be completed in specific order to reverse a sequence of payments. It would seem to be possible for a system to utilize API calls to notify FIs about fraud claims and trigger automated payments to pay claims and split repatriation funds.

There is a potential for the repatriation of funds to be incredibly complex, there is no existing system to facilitate this, and it would be challenging and costly to build a central exchange system or require individual APIs as bilateral agreements between FIs. Sending FIs would not be aware that funds were recovered, so the onus would be on receiving banks to send the repatriated funds as refunds back through the transaction flow. This is mimicking the historical complexity of correspondent banking chains, which the transaction and cross-border payments teams are working to eradicate.

Question 17

Do you have views on the scope we propose for rules on allocating the costs of mandatory reimbursement?

Directly connected PSP participants and PSPs indirectly sending and receiving payments need to be allocated losses based on their customers sending and receiving fraudulent funds, regardless of whether they are direct or indirect participants.

Question 18

Do you have views on our long-term vision, and our rationale for the PSO being the rule-setter responsible for mitigating fraud?

The PSO has more ability than the PSR to be flexible and dynamic as these changes are rolled out. Scheme rules are more adaptable rather than regulation. As new niche cases emerge these rules can be added to the ruleset, and lessons learnt can be applied.

Question 19

Do you have comments on the minimum initial set of Faster Payments scheme rules needed to implement our mandatory reimbursement proposals?

It is positive that anti-fraud innovations are to be integrated into the payment rules directly. Approaches need to be standardized where possible to help embed with consumers and ensure fairness regardless of who they bank with. The standardization needs to still allow for innovation towards a best in industry solution. Rules around the standard of evidence must not be open to interpretation. Additionally, designated arrangements to depart from default allocation are not needed initially and may not be needed at all.

Question 20

Do you have views on how we should exercise our powers under FSBRA to implement our requirements?

N/A



Question 21

Do you have views on how we propose that allocation criteria and dispute resolution arrangements are developed and implemented?

If the allocation is introduced as 50:50 and not open to individual debate or dispute, then the process will be much simpler and work better in practice. The application of the CRM code shows what happens when inconsistency is created in the system: not all FIs are members, those who are members are refunding at different levels, and there is no clarity from the consumer point of view.

This approach will raise the bar terms of fraud controls. The logic behind avoiding disputes is to encourage collaboration and consistency as much as possible.

Question 22

Do you have comments on our preferred short-term implementation approach of requiring Pay.UK to implement an effective compliance monitoring regime, including a reporting requirement on PSPs?

A reporting requirement is a crucial aspect of enabling the industry to get a better control of APP fraud. Industry data is confidentially shared between FIs, because fraud prevention is a non-competitive aspect of their operations. Centralizing this reporting and creating consistency in reporting requirements will help combat historical challenges around individual banks becoming the target for APP scams, with better visibility on how fraud trends shift in the ecosystem.

Accurate and useful fraud data requires honesty from reporting members and a requirement to publish these numbers. FPS could be used to split claims and return funds, thus giving Pay.UK visibility of some of the process to help with monitoring and compliance.

Question 23

Do you have views on the costs and benefits of Pay.UK implementing a real-time compliance monitoring system and when it could be introduced?

Centralized reporting and compliance monitoring could be very beneficial for PSPs who will need to agree on claims and return funds. It is very difficult to assess the costs and benefits of a real-time compliance monitoring system, and the current proposal requires many assumptions. It is unlikely that anything would be designed and built in less than twelve months and therefore would not be ready for use in 2023.

Question 24

Do you have views on the best option for short-term enforcement arrangements?

Initially encouragement rather than enforcement might be the best approach. Publishing performance ratings privately to members has been shown to encourage participants in FPS to meet SLAs around uptime and clearing windows. Perhaps a similar leader board could encourage compliance rather than needing to threaten fines or exclusion from FPS. But in the longer-term enforcement via fines or

increased fees seems reasonable, and echo the fraud performance metrics managed card networks.

Question 25

Do you have views on the best way to apply the rules on reimbursement to indirect participants?

Indirect participants are still licensed financial entities under the FCA. If they have agency access, transactions associated with their own sort codes can be subjected to the same reimbursement rules as any direct participant. For non-agency participants who share a sort code with other indirect PSPs, the sponsor entity would need a mechanism to pass the liability through to the PSP. In this scenario the indirect access providers (IAPs) would need to factor this into their business model. In this way all participants can be held to the same standards through their sponsoring banks.

Question 26

If it was necessary for us to give a direction, what are your views on whether we should direct indirect PSPs or IAPs?

There should be direction to ensure consistency. The aim is to reduce fraud. Without direction indirect participants and IAPs risk becoming the weak link in the anti-fraud defenses.

Question 27

Do you have comments on our cost benefit analysis at Annex 2 or any additional evidence relevant to the analysis?

The analysis is very general in its approach at this stage. There are no built-in growth projections neither for FPS transactions nor levels of scams, and there is no underlying baseline from which to forecast these accurately. There is currently a large volume of unreported APP fraud which will become evident as reimbursements become mandatory. Those FIs who currently do not leverage some APP-prevention capabilities and could take a significant time to develop them, could see their rates increase by an order of magnitude. Particularly for new players in the ecosystem and indirect PSPs who have not previously borne any liability these costs could be unbearable.

Learn about scam typologies and how to stop them, in Scams: The Complete Guide from Featurespace.



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