



**Association for Payment Clearing Services**  
Annual Review of 2003

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10	<b>Cheque and Credit Clearing Company</b> Oversees the clearing of cheques and paper credits.
12	<b>BACS</b> Operates the bulk clearings for direct debits, direct credits and standing orders.
14	<b>Card Payments Group</b> An industry association of organisations which participate in the UK card payments. It is responsible for formulating and implementing policy on non-competitive aspects of card payments.
22	<b>Cash Services Group</b> Acts as the focal point for the provision of strategic direction on co-operative issues for cash and is also the cash industry lobby group.
24	<b>Electronic Commerce Group</b> Responsible for formulating and implementing strategy on non-competitive aspects of e-commerce, focusing on the UK environment but within the global context.
26	<b>Liquidity Managers Group</b> Represents members on liquidity and collateral issues in the UK payments and securities settlement systems, particularly liquidity issues relating to real-time settlement.

APACS (the Association for Payment Clearing Services) is the UK trade association for payments. It provides the forum for the UK's financial institutions to come together on non-competitive issues, to develop banking systems for the future and to provide innovation and developments in payments. It is also the banking industry voice on payments issues such as plastic cards, card fraud, cheques, electronic payments and cash.

APACS supplies scheme and project management, business consultancy and secretariat services to the UK payments industry.

#### APACS members

Abbey  
ABN AMRO Bank N.V.  
Alliance & Leicester Commercial Bank Plc  
Bank of America, NA  
Bank of England  
Bank of Scotland (HBOS)  
The Bank of Tokyo-Mitsubishi, Ltd  
Barclays Bank PLC  
Capital One Bank (Europe) plc  
Citibank N.A.  
Clydesdale Bank PLC  
The Co-operative Bank p.l.c.  
Coutts & Co  
Deutsche Bank AG  
DnB NOR Bank ASA \*  
Dresdner Bank AG  
Egg Banking plc  
GE Capital Bank Limited  
HFC Bank plc  
HSBC Bank plc  
J P Morgan AG  
Lloyds TSB Bank plc  
Marks & Spencer Money  
MBNA Europe Bank Limited  
Morgan Stanley Dean Witter Bank Limited  
National Australia Bank Ltd  
National Westminster Bank PLC  
Nationwide Building Society  
Northern Rock plc  
The Royal Bank of Scotland plc  
Royal Mail Group plc  
Standard Chartered Bank  
Wachovia Bank, NA  
Woolwich plc

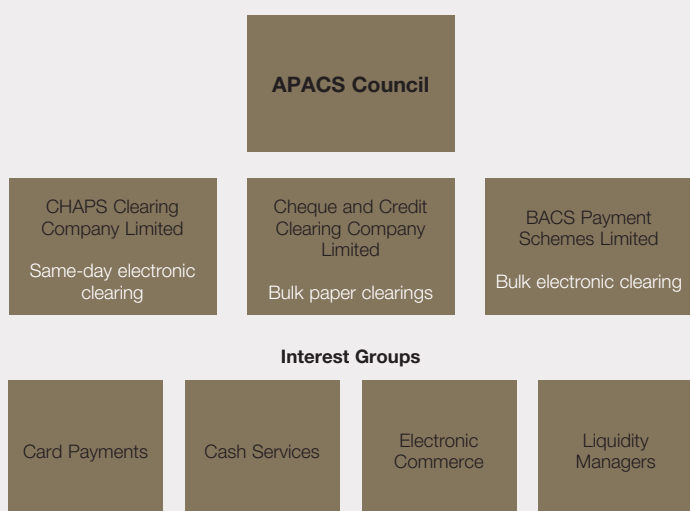
\* formerly Den norske Bank ASA

#### APACS affiliates

Accenture  
AIB Group (UK) plc  
Alphyra UK Limited  
Arab Bank plc  
Bank Machine Limited  
Bank of Ireland  
Britannia Building Society  
C Hoare & Co  
Cardpoint Services Ltd  
Chelsea Building Society  
Coventry Building Society  
Crédit Lyonnais SA  
Derbyshire Building Society  
Eiger Systems  
Fortis Bank S.A./N.V.  
GE Consumer Finance \*\*  
Goldfish Bank Limited  
IntraNet  
KAS Bank N.V.  
Liverpool Victoria Banking Services Limited  
Moneybox Corporation Ltd  
National Bank of Egypt International Limited  
Northern Bank Limited  
Securicor Cash Centres Limited  
Securitas Cash Management Ltd  
Sygma Bank UK  
TD Waterhouse Bank N.V.  
Vanquis Bank Ltd

\*\* the parent company became full members in September 2003

## 02 | APACS and Clearing Companies



On 1 December 2003 BACS was divided into two separate companies. BACS Limited, the infrastructure organisation, is now separate from APACS. The new company, BACS Payment Schemes Limited, will manage the scheme under which bulk electronic payments are made.

### Clearing Company and Group Chairmen

#### Chairman of the Council

Mr A Kane\*  
Lloyds TSB Bank plc  
Group Executive Director

#### Chairman of CHAPS Clearing Company Limited

Mr T N Turner  
The Royal Bank of Scotland plc, Director,  
Payment Trade & Banking Services

#### Chairman of Cheque and Credit Clearing Company Limited

Mr R A Parker  
Abbey, Director,  
Group Management Strategy

#### Chairman of BACS Payment Schemes Limited\*\*

Ms C Henry  
National Australia Group Limited,  
Head of Regulations & Industry Relations

#### Chairman of Card Payments Group

Mr S Brannan  
The Royal Bank of Scotland plc,  
Managing Director, Cards Business

#### Chairman of Cash Services Group

Mr W E Sutton  
Alliance and Leicester Commercial Bank Plc,  
Director, Customer Services

#### Chairman of Electronic Commerce Group

Mr C G Pearson  
APACS Chief Executive

#### Chairman of Liquidity Managers Group

Mr A R Gray  
Citibank N.A., Treasurer

### APACS Council

Mr A G Kane*	Chairman
Mr R A Parker	Abbey
Mr D MacLean	ABN AMRO Bank N.V.
Mr W E Sutton	Alliance & Leicester Commercial Bank Plc
	Bank of America, NA
	Bank of England
	The Bank of Tokyo- Mitsubishi, Ltd
	Barclays Bank PLC
	Capital One Bank (Europe) plc
	Citibank N.A.
	The Co-operative Bank p.l.c.
	DnB NOR Bank ASA***
	Deutsche Bank AG
	Dresdner Bank AG
	Egg Banking plc
	GE Capital Bank Limited
	HBOS Group
	HFC Bank plc
	HSBC Bank plc
	J P Morgan AG
	Lloyds TSB Bank plc
	Marks & Spencer Money
	MBNA Europe Bank Limited
	Morgan Stanley Dean Witter Bank Limited
	National Australia Group
	Nationwide Building Society
	Northern Rock plc
	The Royal Bank of Scotland plc
	Royal Mail Group plc
	Standard Chartered Bank
	Wachovia Bank, NA
Mr M Ward	
Ms M Lowther	
Mr J R Bunn	
Mr T Broome	
Mr P Nelson	
Mr E D Sepkes	
Mr K R Girling	
Mr F O Hansen	
Miss B A Crookes	
Mr H-J Schmidt-Gersbach	
Mr J Schratz	
Mr S Macphail	
Mr J N Turner	
Mr J Brian-Davis	
Ms M H Spearing	
Mr J Hazlewood	
Mr P Baker	
Mr M O'Neill	
Mr P Crowfoot	
Ms J Farhi	
Mr A Douglas	
Mr P Feldman	
Mr K R Barry	
Mr M Fisher*	
Mr G Halliday	
Mr K Hume	
Mr G M Doolittle	

\* Mark Fisher took over as Chairman on 1 January 2004

\*\* Chairman of BACS Limited (as the Clearing Company until 1 December 2003) Mr R J Whatford, Lloyds TSB Group

\*\*\* Formerly Den norske Bank ASA



Archie Kane

2003 was a year of unprecedented activity within the UK payments industry, which is evolving at an ever greater pace. Major developments are in hand and the industry continues to meet the challenges posed by both the regulatory environment and market demands.

I handed over the role of Chairman at the end of this eventful year to Mark Fisher of The Royal Bank of Scotland Group. I have stepped down from the post somewhat earlier than expected, due to a promotion of my role within Lloyds TSB. However, I believe that we are fortunate to have someone of the calibre of Mark, willing and able to step into the Chairman's role at this time. The hand-over has come at an exciting and challenging time for the industry, with national roll-out of chip and PIN under way and the issue of credit card transparency at the top of the agenda. Chip and PIN is set to deal a huge blow to the menace of card fraud, and the industry is proactively tackling the the consumer debt issues focused on by recent Government and media interest.

I am confident that APACS will continue to lead the industry in responding to new challenges and in ensuring that the UK's payment schemes continue to thrive.

In this vein, following a review of its governance arrangements, on 1 December 2003 BACS formally separated into two companies - BACS Limited and BACS Payment Schemes Limited. BACS Limited will continue to process payments as well as maintaining the operational network. BACS Payment Schemes Limited is a membership-based body whose role is to enhance and develop automated payments. The creation of the two companies meets the requirements outlined by both the Cruickshank Report and the more recent OFT investigation into payment systems.

I was encouraged to see the common sense outcome of the OFT's *UK Payment Systems* report in May. Their report came out at the end of an intensive period of briefing and close co-operation with both individual members and APACS. The report hit firmly on the head the accusation that there are any features of the schemes which hinder open access or prevent financial institutions from developing innovative services 'which would enable them to compete effectively for retail customers'.

The announcement in the Chancellor's pre-budget report that the OFT will be taking an enhanced role looking at payment systems over the next four years is an interesting development. We hope to build on our relationship with the OFT and enter into a constructive dialogue during that period.

Another significant achievement for the payments industry and APACS during 2003 was the execution of the settlement agreements for BACS and Cheque and Credit Clearing Company. These provide a legally robust framework for multilateral netting

to significantly reduce inter-member credit exposures. The industry is working together to put in further measures to reduce settlement risk. The next phase of the project will focus on loss-sharing agreements to ensure that sufficient funds are available to allow settlement to complete promptly and smoothly in the (albeit highly unlikely) event of a defaulting member.

On a personal note, I would like to express my thanks to my colleagues on the APACS Council who have supported me during my time as Chairman. I have found the experience hugely rewarding. Looking forward, it is vital that the industry continues to work together in those areas which require a co-operative stance. APACS will continue to take a lead in these initiatives, and in encouraging industry dialogue. The future for the UK's payments industry looks set to be a challenging one but I know that APACS, led by its new Chairman, is well up to the job.



## Objectives

- **To promote** the provision of secure, robust and competitive payment services.
- **To encourage**
  - high standards of integrity, efficiency, security and risk control, and compliance with competition regulation;
  - the development of new and existing payment services;
  - measures to control and reduce criminal activity on or through any payment service.
- **To assist**
  - in maintaining and promoting public confidence in payment services;
  - the public's understanding of payment schemes and payment services.
- **To liaise** with governments and regulators in the UK and elsewhere, representing and consulting members and evaluating the potential impact of any initiatives or regulations.
- **To provide** advice, assistance, information and services generally to or for members.

# 04 | Chief Executive's Foreword



Reliability, efficiency, innovation, resiliency - these are the watchwords for today's payments industry, and particularly for the UK's payment schemes. 2003 saw continued change, both to payment systems themselves, and also to the ways in which they are used by their customers. The dramatic change is the way in which we use our accounts and make payments. Over 11 million people use Internet banking services and more than half of those make payments online. Cheque volumes remain in decline, whilst automated payments continue to grow in popularity. Plastic cards, and particularly debit cards, are increasingly becoming what we use to pay for goods and services. Direct debits, on the other hand, are the success story for regular bill payments.

Trends in the CHAPS clearings continued those of recent years. Whilst volumes and values rose in CHAPS Euro, the sterling system experienced further growth in the lower-value payments bracket. CHAPS remains one of the largest real-time gross settlement (RTGS) systems in the world.

2003 saw the historic trial of chip and PIN in Northampton. This kicked off in late spring, the largest of its kind ever conducted, and was widely seen as a great success by all those involved. The encouraging factor was how well customers responded to chip and PIN with the overwhelming number preferring

PIN to signature and finding it easy to use. This bodes well for national roll-out, which is now under way.

The industry's fight against fraud does not, however, end with chip and PIN. A raft of anti-fraud measures are in place to help combat criminal activity on all fronts. It has become increasingly apparent in recent years that a high proportion of card fraud activity is linked to the menace of organised crime. The activities of the Dedicated Cheque and Plastic Crime Unit, funded jointly by the cards industry, represented by APACS, and the Home Office are going a long way to counteract this menace.

APACS is driving industry policy in several key areas, not least of which is the consumer credit arena. In 2003 APACS represented the industry at the Treasury Select Committee inquiry on the transparency of credit card charges and is taking forward the Committee's conclusions with members. Going forward into 2004, the Government and the media are expected to maintain their focus on consumer debt and transparency issues. The challenge for APACS and its members is to grab back the initiative and take the agenda for greater transparency forward on our customers' terms. As this latter issue generated ever greater levels of media attention in 2003, APACS responded by taking on a more public-facing

Chris Pearson

## Review of the Year

**14** March

**APACS, CHIS and the IWF join forces to beat child pornography**  
 APACS, the Children's Charities' Coalition for Internet Safety, and the Internet Watch Foundation are combining their efforts to crack down on online child abuse images.

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**11** April

**Banks, building societies and retailers join forces for radical fraud-busting programme**  
 The banking and retail industries confirmed their ground-breaking plans to combat the serious problem of card fraud in the UK by introducing a new, much more secure way for more than 40 million UK consumers to use their credit, debit and charge cards by 2005. Consumers will verify their purchases by keying in a four-digit PIN.

**22** May

**OFT publishes market study on payment systems**  
 Progress has been made with competition issues relating to payment systems says the OFT, although further work has also been identified on transparency on the length of clearing cycles.

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**8** July

**New research confirms worries over European Commission's draft Credit Directive**  
 A coalition of UK organisations, including APACS, representing major credit providers published an economic impact study on the draft Consumer Credit Directive which shows that an unchanged Directive could cause a fall in UK consumer spending of £4 billion, with loss in overall GDP of at least £2 billion.

**12** August

**New Guidelines to help organisations using Bank Giro Credits**  
 New revised Best Practice Guidelines for the Design and Use of Bank Giro Credit Vouchers have been published by the Cheque and Credit Clearing Company. The Guidelines provide companies with the means to avoid any frustrating and costly processing problems with their BGCs, whether a printer, part-printer or end user.

role. This was a first, prompted by the fact that competitive issues came under such scrutiny a response was required from the co-operative arena.

Last year was the first full year of the European Payments Council (EPC) and I was able to represent a number of APACS members at

As ever, APACS' most vital resource - its staff - continues to evolve. 2003 saw a number of high-profile changes, notably the retirement of both Michael Lewis and John Wilkinson. Paul Rider was promoted to the role of Deputy Chief Executive and is well able to contribute an effective voice in our developing and dynamic management team. Our staff are passionate

## It is always **pleasing** to see the **high regard** in which **APACS** and its activities are **held by** European banking **colleagues**

the plenary meetings, complementing the individual UK members. It is always pleasing to see the high regard in which APACS and its activities are held by European banking colleagues and this was reflected in an invitation to me to participate in detailed discussion on developing the governance structure for EPC. As members will be well aware, that is an area in which APACS has considerable expertise.

and hard-working, and I make no hesitation in recognising the good work they do. Their efforts make a huge difference to the smooth-running of the industry, reaping benefits for the members and, ultimately, for their customers.



**2** October

### **Plans for chip and PIN roll-out announced**

The first chip and PIN cards outside of Northampton will hit the streets this month with 100,000 bank-owned tills upgraded by the end of 2003.

**8** October

### **Improved transparency on the cards**

The credit card industry outlined details of the new Summary Box that will appear on marketing literature by the end of March 2004. The Box will help customers better compare the features of the many credit card products they have to choose from in a simple and consistent format.

**22** October

### **The National Hi-Tech Crime Unit and UK banking industry join forces to help consumers stay safe online**

APACS, the BBA and the NHTCU issued a checklist for UK consumers to help protect themselves against the Internet fraudster. This follows scams involving e-mails being sent to consumers claiming to be from UK banks asking them to 're-register' or 'reactivate' their accounts at a replica bank website.

**10** November

### **New initiative to help protect shoppers and retailers from card-not-present fraud**

More than 81% of British shoppers who use debit or credit cards will buy goods over the Internet, by mail order, by phone or fax over Christmas. In doing so they risk falling prey to a £300,000-a-day fraud problem by not following simple steps to protect themselves.

**10** December

### **Chancellor gives enhanced role to OFT on payment systems**

The Government welcomes moves made by payment system participants to address some of the competition issues identified in the Cruickshank Report on banking services. It believes that the OFT could address remaining concerns in advance of any legislation.

## 06 | CHAPS Clearing Company Limited



*The primary objective of the CHAPS clearing is to process and settle systemically-important and time-dependent payments. Key drivers for the Company are the provision of a robust and resilient infrastructure, innovation through responding to members' and market needs and the ability to do so in an efficient and cost-effective manner.*

*CHAPS continues to be one of the largest real-time gross settlement (RTGS) systems in the world. It offers members and around 400 financial institutions utilising agency arrangements an efficient, risk-free and reliable same-day payments mechanism for both sterling and euro RTGS payment requirements. CHAPS Euro is an efficient means of accessing European RTGS services and is the second largest cross-border element of the European RTGS mechanism - TARGET.*

*CHAPS remains very clearly member-focused, with strategic direction, leadership and ownership vested in an active Board of Directors. The Company's strategy is to promote operational efficiency - internally by removing duplication and through outsourcing functions where appropriate, and externally by providing feedback to members on performance and by providing operational support in contingency situations.*

*The work undertaken in 2003 on strategic planning led to a road map being delivered which detailed the key milestones for investment in the future of the Company.*

David McFarlane

### **Key issues in 2003**

- Legal and operational robustness and resilience, specifically strengthening the robustness of the Company's level three contingency.
- The work undertaken by the Strategic Planning Working Group (SPWG) on the response to TARGET 2. Though it is currently in its early stages, this European Central Bank (ECB) project will have significant consequences in the future.
- It is vital that CHAPS is subject to vigorous scrutiny and that it can perform to the highest levels. In 2003 the Company secured a fully satisfactory SAS 70 report. Under criteria specified by the Bank for International Settlements, the CHAPS clearings have been judged to be of very high standard.

## Governance

### Legal

Following the 2002 APACS governance changes, a review and restructure was carried out of the constitutional documentation of the Company - namely the Memorandum and Articles of Association and the CHAPS Rules. The aim of this work was to support the greater level of autonomy provided to the Company. During 2003 an independent external review of the revised documentation was completed with the specific aim of procuring legal opinion on its robustness in light of the Competition and Enterprise Acts.

### Jurisdictional review

Work is in hand to complete a jurisdictional review of the constitutional documentation. The review's aim is to reconfirm that members whose primary business is based overseas are legally entitled and able to commit to the CHAPS Rules, and that their national legal systems cannot supersede their ability to fulfill their obligations.

## The **CHAPS** clearings are part of an increasingly inter-dependent and **complex** worldwide **matrix** of systems

### Tertiary contingency

In the unlikely event of the RTGS systems becoming unavailable, the Company can invoke RTGS bypass, which reverts to multilateral net settlement at close of business. A full review of the procedural arrangements for this contingency was undertaken during 2003. The changes recommended by the Steering Group were formally adopted by the Board and the CHAPS Rules and Procedural Documentation were changed to reflect the new arrangements.

In light of the work on settlement risk being carried out by both BACS Payment Schemes and the Cheque and Credit Clearing Company, CHAPS has undertaken to monitor this exercise and to consider enhancements to further strengthen contingency arrangements.

## Strategic Developments

### Strategic Planning Working Group (SPWG)

The Group was formed to review the purpose of the CHAPS Clearing Company and to provide the Board with a recommended strategic plan for the Company. This work is in line with the rationale announced at the Strategy Conference in June 2002. The Board agreed that these objectives would be achieved following a three-stage process: assessment, agreement and action. The SPWG has agreed a road map detailing the key milestones for investment in the future of the Company. This is a live document which will evolve to provide the Company with a tool to illustrate and aid understanding of the changing environments in which it operates. The document also includes a high-level vision for the Company and its primary objective.

### Resilience

Resilience is critical and was recently defined at SIBOS 2003 as 'the ability to recover from an unexpected change or disruption within a

timeframe that meets the business need.'

The CHAPS clearings are part of an increasingly inter-dependent and complex worldwide matrix of systems. The Company is directly involved in a number of initiatives to increase the operational resilience and robustness of these systems, both in the UK and globally. The Company has participated in a number of virtual contingency tests in the UK and, as a result, has further enhanced its communications and operational procedures. Globally, the Company is directly involved in a SWIFT initiative designed to strengthen SWIFT's own resilience and also that of the financial services community as a whole.

### Innovation

CHAPS is also participating in projects designed to improve efficiency and minimise costs for different types of operations. For example, through the SPWG and member representation on the TARGET Working Group, the Company was able to provide a UK industry response to the ECB's consultative document on the definition of user requirements for TARGET 2, scheduled to be introduced in 2007. Its goal is to provide a more harmonised, efficient and cost-effective means of providing RTGS services in euro.

### The euro

Preparing for potential UK entry to the euro presents a significant challenge. *The UK Banking Industry Outline Euro Blueprint* reflects current thinking on key issues arising from a changeover in the UK. It maps out how the banking industry would deliver its part of the entry process and documents conclusions reached about specific aspects of that delivery.

During the early part of 2003 the Company and its members assessed and validated the assumptions made in the *Blueprint* and, within these assumptions, agreed the requirements for euro migration.



## SWIFTNet Fin migration

The SWIFTNet FIN Steering Group was formed to oversee the migration to SWIFTNet, the secure IP-based communications solution built by SWIFT to replace their existing X25 network, from the perspective of the CHAPS clearings. It provides a forum comprising the Company and its members, SWIFT and the Bank of England to enable ongoing business co-ordination of this migration.

During 2003 both the Steering Group and SWIFT undertook to proactively identify issues and risks and to work towards their satisfactory resolution. By the end of 2003 two CHAPS members had migrated to SWIFTNet FIN. Full migration is expected by the end of September 2004.

The second phase of this project is to migrate to the new PKI (Public Key Infrastructure) security protocols. The Company and its members are actively engaged in the early stage of this phase of the project.

## Criteria for Membership

The Company's strategy for membership is to make the criteria open and transparent, with a fair pricing strategy. The Company welcomes membership requests. In order to be eligible for membership, a financial institution must:

- hold a sterling and/or euro settlement account at the Bank of England which the Bank has agreed may be used for the purpose of settling CHAPS payment obligations;
- have the ability to comply on a continuous basis with the technical and operational requirements of the CHAPS systems as set out in the Reference Documents from time to time;
- be a shareholder of the Company; and
- pay a single entrance fee when first becoming a member of any CHAPS system. Such an entrance fee is determined by the Board and is based on contributing to the cost of developing the CHAPS system(s) and the cost of technical implementation relating to membership.

Since the implementation of NewCHAPS, the single Company membership fee has been set at £100,000. This covers access to either one or both of CHAPS Sterling and CHAPS Euro RTGS clearings.

The membership criteria and fee structure are reviewed and revalidated on an annual basis.

## Audit and regulatory/oversight

### Audit

The Company is subject to a rigorous internal audit regime, supported by an external security audit undertaken by Deloitte & Touche. In addition, the clearings are overseen by the Market Infrastructure Division of the Bank of England.

The external audit on the security controls is based upon Statement on Auditing Standards No. 70 (SAS 70), an internationally recognised auditing standard developed by the American Institute of Certified Public Accountants. SAS 70 is the authoritative guidance that allows service organisations to disclose their control activities and processes to their customers and their customers' auditors in a uniform reporting format. An SAS 70 examination signifies that a service organisation has had its control objectives and control activities examined by an independent accounting and auditing firm.

The report for the period March 2002 to February 2003 was fully satisfactory. There were no issues arising relating to previous years and no findings to report for the period under review.

### Regulatory/oversight

Particular regard is paid to the Bank for International Settlements' *Core Principles for Systemically Important Payment Systems*, published in January 2001. In 2003 the CHAPS payment systems were judged by the International Monetary Fund to be of a 'very high standard internationally'<sup>1</sup> in light of compliance with the *Core Principles*.

The Bank of England, in its capacity as the designating authority for payment systems under the Financial Markets and Insolvency (Settlement Finality) Regulations 1999 continues to grant the CHAPS Sterling and Euro clearings designation for the purposes of these Regulations. The central objective of the Settlement Finality Directive is to reduce legal uncertainties regarding the status of payments in the event of insolvency. This can contribute to reducing systemic risk. The benefit to the clearings is that designation under the Regulations can mitigate the adverse effects caused by the failure of one participant on others, thereby safeguarding system stability.

Designation places a number of obligations on the Company and is recognised as a core component in protecting the integrity of the clearings and their members. The CHAPS clearings were the first UK payment systems to be designated in this way.

<sup>1</sup>International Monetary Fund, United Kingdom: Financial System Stability Assessment February 2003.

## CHAPS Sterling and CHAPS Euro volumes and values

### Volume and value input for 2002 and 2003

	Volume		Value	
	2002	2003	2002	2003
<b>CHAPS Sterling</b>	25,563,286	<b>27,214,642</b>	£51,896 bn	<b>£51,613 bn</b>
<b>CHAPS Euro</b> <small>(includes CHAPS Euro domestic transmitted and CHAPS Euro TARGET transmitted and received)</small>	5,281,304	<b>5,987,102</b>	€48,298 bn	<b>€53,411 bn</b>

### CHAPS Sterling

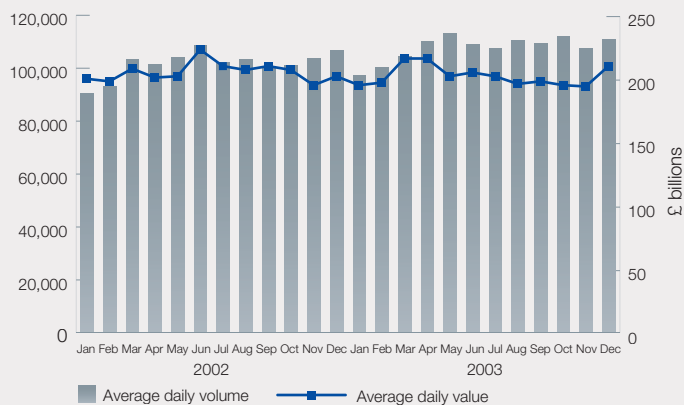
During 2003 the volume of transactions continued to increase at a rate of around 6%. However, the average value per payment has continued to fall - from £2.03 million to £1.90 million - indicating that the growth is mostly derived from lower-value non-financial customers.

### CHAPS Euro

A similar but more marked pattern emerged in CHAPS Euro. Growth in volumes for CHAPS Euro and TARGET payments was significantly higher than in CHAPS Sterling at around 13% against that reported for 2002. CHAPS Euro values rose by around 11% in contrast to the flat growth in aggregate value processed in CHAPS Sterling.

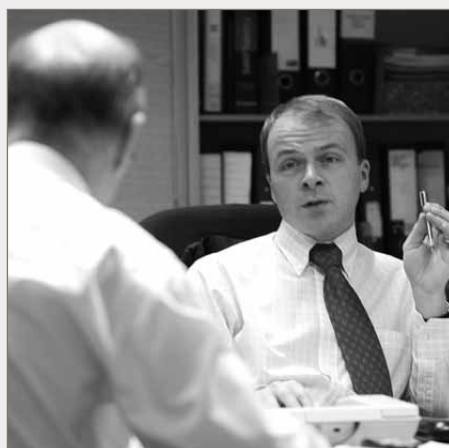
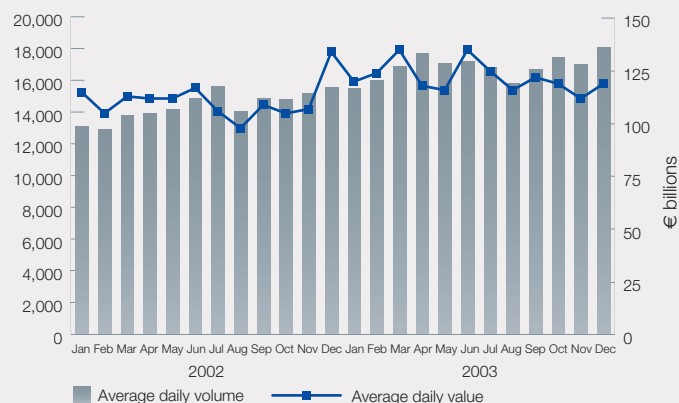
### CHAPS Sterling

Average daily volume and value throughput 2002/2003



### CHAPS Euro

Average daily volume and value transmitted 2002/2003



# 10 | Cheque and Credit Clearing Company Limited



*While customers increasingly choose debit and credit cards for making retail purchases, and direct debits for settlement of regular bills, the cheque is still a convenient alternative to cash. Although cheque use has declined each year since volumes peaked in 1990, 6 million items were still processed each business day in 2003. It is therefore vital that efficiency and quality are maintained.*

*The clearing cycle is the subject of frequent scrutiny, and is often perceived as the period between a cheque being paid into an account and the point at which the funds can be withdrawn. In actual fact the clearing cycle is the time taken for a cheque or credit to physically pass from the bank into which it is paid to the bank on which it is drawn - a short period of 48 hours.*

*In order to address some of the common misconceptions regarding the clearing cycle, in 2004 we will be publishing an information booklet which will describe the clearing process in detail and will also provide answers to the most frequently-asked questions. This booklet will be sent to interested parties such as journalists and opinion formers and will also be available on our website.*

Fred Galbraith

## Key issues in 2003

- The introduction of the new IBDE network, IBDE 2, which offers enhanced security for transmission of data between members.
- The move of the paper exchange centre to Tillbrook, Milton Keynes from London, where it has been in operation in one form or another for nearly 200 years. This was prompted by the fact that the majority of members' cheque and credit processing now takes place in the Midlands.
- The adoption by the Company of the settlement agreements, which address the issue of settlement risk.
- The enhancement of the Automated Settlement System, which has streamlined and improved the daily settlement operation.

### Outsourcing the processing operation

Ten members of the Cheque and Credit Clearing Company have now taken the decision to outsource some or all of their processing operations to external suppliers. Although the long-term advantages of this move will not be immediately realised, the benefits should begin to be felt by the end of 2004.

### Ongoing quality

Quality in the cheque and credit clearings is maintained by means of service level codes, which set targets designed to improve performance and minimise errors. Members' performance under these codes is closely monitored, particularly where failure to meet the prescribed standard would have an adverse impact on customers. The overall continued improvement in performance during 2003, in an environment of constant and significant change, is testament to members' commitment to quality.

### Cheque fraud

The Company is aware of the potential for increased cheque fraud as security on other payment methods is upgraded. The introduction of chip and PIN for credit and debit card payments may, for example, encourage fraudulent activity to migrate to a perceived easier target. Recent statistics show that incidents of counterfeit, as well as fraudulent alteration of amount and payee details, are increasing substantially, with fraudsters focusing on identity fraud and improved-quality counterfeiting. To counter this threat a review of the Cheque Printer

Accreditation Scheme commenced in November, due for completion in mid 2004, to ensure that the rules and standards remain robust in this environment.

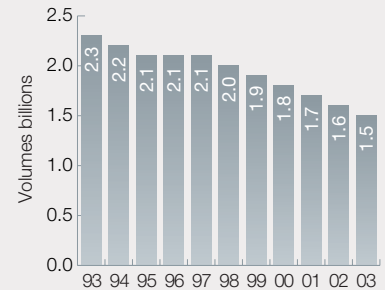
### Cheque Printer Accreditation Scheme

The number of cheque printers granted APACS accreditation increased from 74 in 2002 to 81 in 2003. The Scheme has been in existence since 1995 and APACS accreditation is now a well-respected mark of quality, recognised worldwide as playing an important part in increasing the security of cheque production.

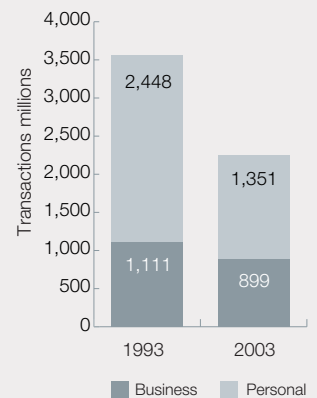
### Currency clearing

The currency clearing handles cheques, bankers' payments, bank drafts and mandated currency debits drawn in US dollars on UK accounts. In 2003 a total of 112,783 items were cleared with a sterling value of just over £2.1 billion. Since the introduction of the euro the clearing has only handled items drawn in US dollars, but it is still regarded as the most efficient way to process these items when compared to alternatives such as direct collection.

Cheque clearing volumes: 1993 - 2003



Business and personal cheque use





*A key achievement in 2003 was the successful completion of the corporate governance programme which culminated in the division of BACS into two separate companies on 1 December 2003. This programme was part of a corporate review to improve business processes and customer services, in response to regulatory advice to create more open payment markets. BACS Limited will continue to physically process payments, as well as maintain the payment network.*

*The new company, BACS Payment Schemes Limited, is membership-based and is dedicated to enhancing the integrity of the direct debit and direct credit payment schemes. A collaborative relationship providing secure, reliable and cost-effective funds transfer services is envisaged for the future as each company builds on its strengths.*

*Demand for BACS' services continued to grow throughout 2003 as consumers, businesses and Government increasingly used direct debits and credits. Volume growth in both direct debits and credits was driven by successful industry campaigns promoting the benefits and convenience of automated payments. Direct credits showed a record increase in items processed in 2003.*

*BACS' technology renewal programme continued in 2003 following the introduction of BACSTEL-IP, the new generation high-speed online payment and collection service. This service has been widely acclaimed for its state-of-the-art PKI (Public Key Infrastructure) security and won five major industry awards in 2003. BACS is now well-placed to meet the changing needs of existing customers and to develop new markets.*

Mike Chambers

### **Key issues in 2003**

- The governance programme involved the separation of BACS into two separate companies. A considerable undertaking, the separation was successfully completed on 1 December 2003.
- Of critical importance was the launch of the new live BACSTEL-IP service, including work with members to ensure that all went live.
- The NewBACS review was introduced to ensure that the design and scope of the NewBACS programme is fully aligned with market and customer needs. The successful completion resulted in enhancements to the programme.

#### Volumes and records

A total of 4,060 million items were processed in 2003 representing an increase of 326 million, or 8.7%, over 2002.

The total volume of items processed in one day exceeded all previous records when, on 28 November 2003, 64.0 million items were processed.

### Direct credit payments increased by 169 million items to 1,342 million - a record growth of 14.4%

#### Direct debits

In 2003 the number of direct debit payments reached 2,430 million - an increase of 141 million or 6.2%. Two of the fastest-growing areas were telephone billing, which increased by 25 million items to 192 million, and subscription payments, particularly in the charity, clubs and broadband Internet sectors.

#### Direct credits

Direct credit payments increased by 169 million items to 1,342 million - a record growth of 14.4%. This growth came as a result of the Government's programme to automate state benefit payments; Inland Revenue tax credits; and an increase in remote banking credits and business-to-business payments.

#### NewBACS

The NewBACS programme made significant progress in 2003 and all BACS members are now connected to the new BACSTEL-IP software. Customer migration is the next critical phase of the project, and the aim is for all customers to be using the new service by the end of 2005.

#### Relocation programme

Following the commissioning of a new data centre, BACS Limited initiated plans to move from Edgware to new, purpose-built headquarters in Rickmansworth. The new site is more suited to the Company's business requirements and the move is scheduled to take place early in 2004. An enhanced operations centre in the Home Counties is also planned, and development work began in 2003.

BACS Payment Schemes Limited relocated to offices in London at the beginning of December to coincide with the formal separation.



## 14 | Card Payments Group



2003 was a dynamic year for Card Payments Group (CPG), a notable highlight being the successful public trial of chip and PIN in Northampton - the largest trial of its kind in the world.

Credit cards attracted an unprecedented amount of interest from legislators, regulators and media during 2003. APACS represented the industry at the Treasury Select Committee during its investigations into transparency of credit card charges. This involved a number of written submissions, as well as appearances before the Committee. APACS was also heavily involved throughout the year in discussions with the DTI during preparation of the latter's Consumer Credit White Paper. Additionally, APACS commissioned an influential study into the detrimental economic impact of the European Commission's draft Consumer Credit Directive.

The Dedicated Cheque and Plastic Crime Unit (DCPCU), set up as a two-year pilot in April 2002 and which includes a number of APACS employees, continued its excellent work in combating organised plastic card and cheque crime. The Home Office commissioned an independent evaluation into the work of the DCPCU in 2003. This report showed the Unit, which is jointly funded by APACS and the Home Office, in a very positive light, arguing strongly for it to be set up as a permanent body after its trial period concludes in 2004.

APACS remains actively involved with the Home Office on a number of other fraud prevention initiatives covering such topics as identity fraud, Internet fraud and the use of payment cards to purchase child pornography over the Internet. APACS' tactical

work with key fraud-prone retailers continued throughout the year and two important aids to card fraud prevention were published: Identity Fraud - the UK Manual and the Spot & Stop Card-not-Present Fraud training pack. APACS also played an active part in the establishment of a European card fraud task force, working with the international card schemes and European banks to reduce cross-border card fraud losses.

The industry's multi-layered approach to fraud prevention continues to ensure that card fraud is tackled on all fronts resulting in a slight reduction of year-on-year fraud losses, before the UK experiences the longer-term benefits of chip and PIN.

Paul Marsh

### Key issues in 2003

- Agreement was achieved across the industry by members to implement the Summary Box and other significant initiatives to provide greater transparency to consumers in the credit card arena.
- The successful pilot of the Dedicated Cheque and Plastic Crime Unit (DCPCU) continued, resulting in Home Office consultants recommending that the Unit should become permanent once its trial ends in April 2004.
- A significant reduction in the growth of card-not-present (CNP) fraud was achieved following implementation of industry initiatives and greater awareness-raising of the problem amongst CNP merchants.
- APACS led the way in the UK's fight against identity fraud, publishing a Home Office-endorsed identity fraud prevention training pack.

## Card Payments Group

CPG is the leading industry association for UK card payments and is responsible for formulating and implementing policy on non-competitive matters. Its membership consists of the 16 largest card issuers and acquirers in the UK plus a representative from the community of smaller banks and building societies that issue cards. CPG welcomed two new members during 2003 - Morgan Stanley Dean Witter and Marks & Spencer Money.

Members have also agreed best practice guidelines regarding the issuance of credit card cheques, and continue to explore further ways of improving transparency of product information.

Two major legislative initiatives have occupied PAG - the DTI's review of the Consumer Credit Act 1974 and the European Commission's proposed Consumer Credit Directive, updating the 1987 Directive. Following extensive consultation with the industry the DTI

Additionally, consumers in the UK would be worse off by as much as £950 million, with up to 2 million people finding it difficult or impossible to obtain credit on the high street.

The industry's study was received with interest by a number of MEPs on the European Parliament's Legal Affairs Committee, which will debate the issue in 2004. The Parliament's report, drafted by Joachim Wuermeling MEP, is set to rewrite radically the draft Directive. It is expected to be approved in spring 2004.

## 2003 saw increasing interest in the cards industry from Government, regulators and the media

### Chip and PIN roll-out

See page 20.

### Public affairs

2003 saw increasing interest in the cards industry from Government, regulators and the media, including criticisms about transparency of charges and irresponsible lending. CPG, through its recently established Public Affairs Group (PAG), has taken a leading role in responding to this criticism, both by explaining the industry's existing practices and through the creation of new codes of practice.

APACS and its members provided input to the Treasury Select Committee inquiry into credit card charges. As part of this work, APACS members took the initiative by agreeing to include a standardised Summary Box in their marketing material, providing consumers with information on the key features of credit cards.

published a White Paper and draft regulations in December, to which the industry will respond further.

The industry has also lobbied extensively in Europe to ensure that the proposed Directive does not have an adverse impact upon either the industry or consumers. APACS, with other associations, commissioned an influential, independent report assessing the potential impact of the proposals on the UK economy.

The report found that the Directive, if implemented as proposed, would increase the risks of lending, limit consumer choice and impose unnecessary costs on credit providers. It concluded that, within two years of implementation, the knock-on effect on the UK economy would include a drop in consumer spending of at least £4 billion and a decrease in GDP of at least £2 billion.

In addition, PAG has:

- addressed external concerns over the increasing level of personal debt on credit cards;
- committed to support financially the work of the Internet Watch Foundation on Internet safety and child protection, seeking out illegal material on the web, until 2006. APACS co-sponsored a conference, involving Ministers and MPs, on this issue during the summer;
- shared knowledge with Government to assist in the development of proposals to introduce national entitlement cards;
- responded to Government consultations and generally liaised on issues as diverse as APRs; the Distance Marketing Directive; the Unfair Contract Terms Directive; consumer protection co-operation; debt collection; debt consolidation; money laundering; access to cash; and Section 75 of the Consumer Credit Act;
- represented the UK's interests at the European Payments Council card fora.





### Fraud prevention initiatives

During 2003 the Plastic Fraud Prevention Forum (PFPF) was extremely active in introducing counter-measures to deal with anticipated changes in criminal behaviour resulting from the implementation of chip and PIN. A major success was in significantly reducing the level of counterfeit fraud over the last 12 months, due in part to the work of the DCPCU and the comprehensive programme of tactical work being undertaken with key fraud-prone retailers.

### Dedicated Cheque and Plastic Crime Unit (DCPCU)

In 2003 the DCPCU completed the first year of its two-year pilot. The Unit is jointly funded by the Home Office and the banking industry, with APACS and its members also providing fraud investigators and administrative staff to work alongside police personnel.

The Unit has an impressive record of success in identifying, investigating, arresting and prosecuting organised criminal gangs that perpetrate cheque and plastic card fraud. Since its inception the DCPCU has recovered more than 35,103 counterfeit cards and compromised card numbers and 2,567 cheques earmarked for fraudulent use. It has also seized assets and recovered property valued in excess of £2.1 million from raids on suspected criminals. In the same period 88 people were charged, of whom 35 have been convicted and sentenced to terms of imprisonment. The Unit has enjoyed virtually a 100% success rate in cases taken to court. As a result of this work there has been a potential saving of £63.18 million to date.

### Fraud Intelligence Bureau (FIB)

APACS' FIB shares intelligence between the banking industry and police to combat skimming, the predominant form of card counterfeiting. In 2003 the FIB tracked over 15,000 compromised card numbers back to the retail outlet, petrol station or restaurant where the skimming occurred. Close liaison with the police resulted in the arrest of some 274 criminals involved in card fraud.



### Tactical work

APACS staff work closely with retailers to devise tailored fraud prevention programmes, of which training of retail staff is a key element. More than forty major retailers have used the APACS *Spot & Stop Card Fraud* training pack and in excess of 2,000 fraudulent cards have been captured as a direct result.

APACS' Management Information System contains a record of every fraudulent transaction carried out using UK-issued cards. The system is crucial in identifying retailers with high levels of card fraud and in assisting acquirers and retailers alike with their business cases for chip and PIN migration.

A training package for police was completed during the year. Aimed mainly at crime prevention officers and new recruits, this is already in high demand.

### Cross-border work

APACS has taken a leading role in the establishment of the European Payments Council's Card Fraud Task Force. Following a major conference held in Paris in October, a pan-European battle plan was agreed involving the banking industry, retailers and law enforcement agencies.

The main elements of this plan were developed by APACS based on its recent PFPF experience in tackling fraud, particularly in the areas of sharing data, best practice and establishing an anti-fraud toolkit. As a result, organisations from the UK, France and Spain are already exchanging fraud data. A further element of the plan involves the UK, represented by APACS, becoming part of an advisory group to co-ordinate banking industry input to the multi-sector EU Fraud Prevention Task Force, with particular emphasis on law enforcement issues in the first instance.

**Card Security Initiative**

APACS' Card Security Initiative, held in November, addressed the issue of card-not-present fraud - whereby fraudulent transactions are made via the telephone, fax, Internet or by mail order. With support from key retail organisations the initiative raised awareness amongst retail staff and consumers of the problem, and explained how to prevent this type of fraud from occurring. A media week raised its profile further, resulting in significant coverage on television news programmes, radio interviews and national and regional newspapers. Visits to [www.cardwatch.org.uk](http://www.cardwatch.org.uk), APACS' card fraud awareness website, also increased significantly during the week.

**Identity fraud**

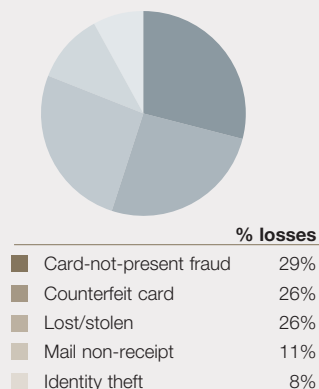
The introduction of chip and PIN will reduce the opportunity for fraudsters to use counterfeit and lost and stolen cards in a face-to-face environment. Identity fraud is one area which may see increased activity following full roll-out. A multi-sector working group, initiated by PFPF at the end of 2002, involving the UK banking industry, British Bankers' Association, CIFAS, key government departments and law enforcement bodies, continues to address the problem.

In June 2003 APACS published *Identity Fraud - the UK Manual* in conjunction with CIFAS and the FLA (Finance and Leasing Association) and endorsed by Home Office Minister Beverley Hughes. The *Manual* and its supporting material, including a training programme, explains the threat from identity fraud and how businesses can best protect themselves.

A Home Office Identity Fraud Steering Committee has been set up consisting of senior representatives from the public and private sector, including APACS, who have an interest in reducing identity fraud in the UK.

An Account Take-over Working Party has been set up under PFPF, with the key objectives of enhancing best practice and facilitating data sharing.

2003 fraud losses by category



# 18 | Card Payments Group - continued



## Card-not-present (CNP) fraud

CNP fraud is another likely area for fraud migration following national roll-out of chip and PIN. A five-pronged strategy has been implemented by PFPF:

- Promotion of the automated cardholder address and card security code checking system (AVS/CSC). Merchants are now benefiting from this fraud prevention tool, with some technology retailers experiencing reductions in CNP fraud of over 80%.
- The roll-out of Verified by Visa and MasterCard's SecureCode to combat Internet-based CNP fraud.
- A campaign of education centred on the new APACS publication *Spot and Stop Card-Not-Present Fraud*, a comprehensive training manual for merchants.
- Encouragement of retailers to make use of the various fraud prevention tools available from vendors.
- The development of a token-based approach to cardholder authentication, making use of pocket-sized card-accepting devices together with EMV credit/debit cards. A pilot of this new initiative will take place in 2004.

A series of retailer and banking fora have been set up for high-risk sectors, such as telecommunications, gaming, general/electrical retailing and travel. Sharing best practices and experiences has already proved useful to all participants.

## ATM issues

### Constitution and entry criteria to ATM Group

The ATM Group reviewed its membership and entry criteria and, with CPG approval, extended its remit to include independent ATM deployers (IADs). To date, four major IADs have become APACS affiliates and have joined the ATM Group.

### ATM availability

Data collected from ATM owners in 2003, covering both branch-based and convenience ATMs, indicated that they were working for 95.6% and 95.2% respectively of their available operational time.

### Chip and PIN

ATMs in the UK continue to be upgraded to read chip cards and more than 87% of bank-owned ATMs already have chip card readers installed.

### ATM Crime Group

This new Group was formed with the primary aim of developing and implementing co-ordinated industry action to combat the increasing number of attacks against ATMs. The Group comprises representatives from financial institutions, IADs, ATM suppliers, card schemes, cash-in-transit operators and law enforcement agencies. Notable achievements include:

- the development of a cross-industry ATM crime incident database;
- the development, in conjunction with LINK, of an early warning system to ATM deployers, card issuers and law enforcement agencies;
- fraud prevention education seminars for police forces across the UK as part of wider efforts to work with and educate police officers on plastic card crime.

### Euro planning

A Mobilisation Plan - to support a fast start to the full ATM Euro Migration Plan - was developed and approved by CPG. Both plans are being maintained on an ongoing basis.

## Other issues

### Cheque Card Scheme

The Cheque Card Management Committee (CCMC) oversees the governance of the UK Domestic Cheque Guarantee Card Scheme, which has 53 member banks and building societies. Activity in 2003 included the agreement of a set of best practice guidelines aimed at addressing retailers' concerns over inconsistencies in the acceptance of cheque guarantee cards.

### Authorisations

The second phase of a major strategic review of the role of authorisations in a mature chip and PIN environment was completed. The role of authorisations in controlling bad debt will potentially become as important as the historic emphasis on authorisations in preventing fraud. The bulk of future work in this area will be taken forward by the card schemes.

### Accreditation schemes

During 2003 a major review of the Card Protection Agencies Accreditation Scheme was completed ensuring that accreditation requirements in this area are up-to-date and fit for purpose.

### Communications

A number of topics attracted media coverage during the year including the annual plastic card fraud figures; a rise in the use of debit cards; identity fraud; and the collaboration between the UK banking industry and the Internet Watch Foundation to tackle the menace of child pornography on the web.

Newsletters, publications and card fraud prevention booklets were all produced during 2003 to ensure that members and other interested parties were kept up-to-date with current and future developments.

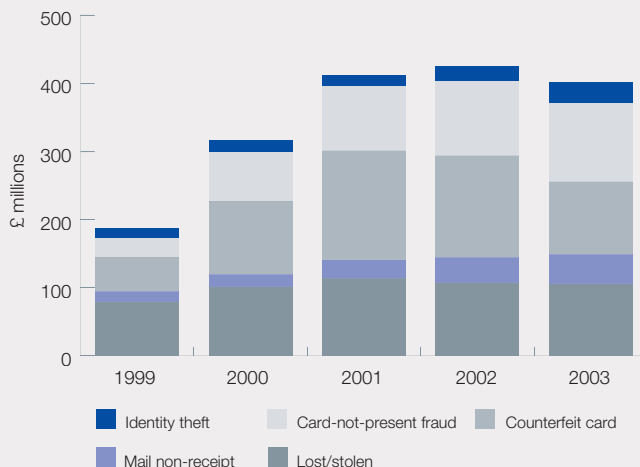
### Management information

APACS continued to provide the authoritative card industry statistics, producing both public documents and member-only confidential reports.

Two publicly available documents were published in the first half of 2003: the *ATM Survey*, which examines the deployment and usage of ATMs in the UK and the *Plastic Card Review*, which analyses trends in the use of plastic payment cards in the UK over the last ten years.

Throughout the year APACS continued to produce regular confidential reports, analyses and presentations of the latest industry trends and developments, that are used by the majority of CPG sub-committees. These included collation and report preparation relating to chip and PIN-enabled cards and terminals to brief the Chip and PIN Programme Management Organisation and members on progress towards key objectives.

Plastic card fraud figures over the past five years





*Excellent progress was made in 2003 to prepare for the UK's migration from signature to personal identification numbers (PINs). In future, cardholders will use PINs as the means by which they verify their plastic card transactions at the till.*

*In May banks, building societies and retailers began a three-month public trial of chip and PIN in Northampton. By the end of the trial more than 200,000 PIN-enabled credit and debit cards had been issued to Northampton residents and around 1,000 outlets including shops, restaurants, pubs, hotels and petrol stations had taken part.*

*The trial - the largest of its kind ever conducted anywhere in the world - was very successful. The technology had already been proven during extensive closed testing, so the main aim was to gauge cardholder reaction to the new system. This was overwhelmingly positive - nine out of ten cardholders preferred PIN to signature and they found chip and PIN easy to use. Retailers were equally happy, especially as PIN was proven to reduce queuing times.*

*National roll-out of chip and PIN began in October. Chip and PIN cards, and the PIN-enabled point-of-sale terminals that accept them, are now being introduced throughout the country. By the end of 2004 the majority of face-to-face plastic card transactions in the UK will be made using chip and PIN.*

Gary Hocking

### Key issues in 2003

- The key achievement of 2003 can be summed-up in just ten words: "World's biggest and most successful chip and PIN trial - ever!" 200,000 cards were used by 150,000 customers in 1,000 retail outlets, and both customers and retailers gave chip and PIN the highest imaginable favourability ratings. In addition, chip and PIN was not only technologically successful, but also resulted in faster transactions at the till.
- APACS' responsibility to ensure that the Chip and PIN Programme met its agreed performance targets and operated within tight budget control was successfully achieved.



### A more secure way to pay by plastic

The Chip and PIN Programme is backed by the UK's banks, building societies, card companies and retailers. A cross-industry multi-stakeholder senior Steering Committee governs the Programme, with delivery co-ordinated by a Programme team under the supervision of APACS.

Chip and PIN is a much more secure way for UK consumers to use their credit, debit and charge cards. It combines two effective security features: a chip (or microchip) embedded in the card that stores cardholder data more securely than the current magnetic stripe and is much harder to counterfeit; and a personal identification number (PIN), which is more secure than a signature and proves that the customer is the genuine cardholder.

The system is being introduced to combat fraud on plastic cards in the UK. About £1 million-worth of fraud is committed on cards every day in the UK - a crime every eight seconds. Chip and PIN will help tackle 60% of this fraud.

### Public trial in Northampton

Northampton was selected as the location for a three-month public trial of chip and PIN, as it is demographically representative of the UK as a whole. The trial aimed to gauge customer attitudes; confirm the optimum method of rolling out the new technology; and determine the communications programme required to inform consumers nationwide.

Customers involved in the trial were extremely positive about chip and PIN, its improved security and ease of use. Market research among Northampton consumers showed that nine out of every ten cardholders were in favour of the new system. The trial also successfully proved that the technology works. It was the first opportunity to test cardholder reactions to the use of PINs when paying by card, which led to shorter queues as PIN proved to be significantly faster than signature.

By the end of the trial the banking industry had installed more than 1,000 stand-alone chip and PIN terminals in smaller retailer outlets, and had worked with larger retailers to help them upgrade their own till points. Additionally, 180 cash machines were upgraded to offer PIN services, such as the ability for customers to change their PIN.

### Ministerial support

The Home Office has fully supported the introduction of chip and PIN. Following the trial Hazel Blears, Home Office Minister for Crime Reduction and Policing, said: "The public trial of chip and PIN in Northampton has been a great success and I am encouraged that the lessons learnt will be taken forward as the scheme is rolled out across the country. As well as fighting fraud, chip and PIN has proved to be an efficient, secure and customer-friendly system."

### National roll-out

The success of the trial paved the way for the national roll-out of chip and PIN, which began in October. This is happening on a country-wide basis, rather than focusing on any particular area, enabling cardholders to benefit from chip and PIN regardless of where they live. The roll-out plans announced so far by card companies and retailers mean that, by the end of 2004, nine out of ten cardholders will have at least one chip and PIN card and will be using them for the majority of their card transactions.

Banks, building societies and retailers are devising their own plans regarding the issuance of new chip and PIN cards and the provision of terminals. Cardholders will be contacted by their card issuers as the new cards are ready to be distributed.

### Disabled cardholders

APACS has always been careful to take into account the views and needs of disabled people, and will ensure that this continues throughout the national roll-out. Activities have included fora run with disability groups; a regular Disability Working Group for companies involved in chip and PIN and attended by the Disability Rights Commission (DRC); guidelines and advice issued to companies involved in chip and PIN (in conjunction with the DRC); and research commissioned among cardholders with a range of disabilities using chip and PIN during the Northampton trial.

Overall, chip and PIN will allow more disabled people to use cards than in the past as, in many cases, those who have difficulty signing will be able to use a PIN. It will not, however, suit everyone and those with difficulties will be able to discuss the option of continuing to use signature with their card issuers.

### Technical developments

APACS developed a robust set of security requirements for PIN entry devices to be deployed in the UK, at the heart of which was the need for independent evaluation to an agreed standard. The ISO common criteria process was chosen and a protection profile developed for manufacturers to follow. All UK devices will be subject to evaluation from 2004 onwards.

The Chip & PIN Operational Issues Group was created in response to a number of operational issues with legacy UKIS cards and terminals, and to address interoperability and operational incidents as they occur.

To ensure that APACS point-of-sale (POS) standards are compatible with the new chip and PIN POS environment, new merchant-to-acquirer interface standards were developed.

### A major change to the way we pay

The introduction of chip and PIN in the UK is a major project - the biggest change in the way we pay since decimalisation - and will take time to roll out fully.

There are more than 120 million cards, 850,000 tills and 40,000 cash machines to upgrade and it will affect some 42 million cardholders and 2.7 million retail staff. The target is for the majority of card transactions in the UK to be made using chip and PIN by the end of 2004.



## 22 | Cash Services Group



*In 2003 the main focus of the Cash Unit was the reduction of resource capacity coupled with continued support for members of the Cash Services Group (CSG). The Unit kept a watching brief on potential areas of future impact, in particular potential UK entry into the euro.*

Tina Dinnis

### **Key issues in 2003**

- Pay-in standards for unfit notes.
- The risks attached to wholesale cash provision in the UK.

### Note Circulation Scheme (NCS)

The transitional phase of NCS ended in June 2003. Member concern regarding proposals for pay-in standards for unfit notes continued, particularly in respect of proposed penalties for breaching standards, which were felt to be too severe.

demand for new coin was significantly understated. This was due to the fact that lower-than-expected levels of long-term-hoarded coin were released back into circulation. There have also been significant changes in business relationships between individual banks and retailers, in addition to

## 2003 was a particularly **challenging year** in that **forecast demand** for new coin was significantly **understated**

Revised proposals from the Bank of England have been welcomed and a 'shadow' implementation period for the quality standard with the penalty clause excluded has been extended to 31 March 2004, pending the outcome of an independent review by external consultants.

the usual anticipated volatility of retailer coin demand. Nevertheless, the industry is on course to meet demand without the need to take excess levels of coin on to balance sheets. APACS will continue to monitor demand against forecast levels on a month-by-month basis.

### £5 notes

The quality of £5 notes in circulation remains variable. As yet there is no obvious way forward in terms of increasing the number of notes made available to the general public and, through them, retailers. It is expected that the withdrawal of legal tender status for the Stephenson note and its replacement with the Elizabeth Fry note, printed on superior quality paper, will improve their general quality and lifespan in the short term.

### Cash risk assessment

During the year CSG led a cross-industry review of the risks attached to wholesale cash provision in the UK. This work resulted in the production of a comprehensive report that has been distributed to all key stakeholders. The report will enable these stakeholders to assess their contingency cover for potential major situations that could cause problems for the UK's cash market. The assessment will be subject to ongoing half-yearly reviews.

### The euro

CSG has continued to monitor this issue, working with the HM Treasury Notes and Coin Working Group as appropriate.

In addition, via APACS, CSG has input into discussions at the European Payments Council (EPC) Cash Working Group. The APACS Member Strategy Group commissioned a major report on the UK cash market and the well-received final paper was submitted to the EPC at the end of 2003.

### Coin procurement

CSG members participating in the Coin Distribution Working Party have completed a third year working under an arrangement stipulated by the Royal Mint, whereby a certain percentage of the total forecast requirement for new coin be taken, irrespective of the fact that it may not ultimately be required. 2003 was a particularly challenging year in that forecast

## 24 | Electronic Commerce Group



*The major focus in 2003 has been on maintaining the integrity of online banking. Other initiatives have included work on mobile payments and authentication, e-Government issues, market analyses, monitoring and responding to legal and regulatory issues, and developing messaging and other standards. Within APACS, ECG collaborates closely with the Card Payments Group and the Security Advisory Group. Much of the detailed analysis is undertaken by Working Groups focusing on specific areas of interest.*

*Over the year, links have been developed and strengthened with other UK organisations concerned with online fraud, such as the National Hi-Tech Crime Unit, and with a growing number of banks and associations abroad.*

Peter Finlayson

### Key issues in 2003

- Co-ordinating the industry response to attempts to dupe customers of online banks in the UK and abroad into divulging their security details at replica bank websites.
- Working closely with MasterCard, Visa and a number of associations overseas, to encourage the development of a common global specification for token-based authentication.
- Working with a wide range of external organisations to reach agreement on payment and authentication standards for mobile commerce as well as the regulatory framework.
- Exploring with APACS members and the Office of the e-Envoy the potential to make use of the registration and authentication mechanisms developed for online banking to enable customers to access e-Government services.

### **Electronic Commerce Group (ECG)**

ECG is the senior UK payments industry body with responsibility for agreeing and implementing strategy on non-competitive aspects of electronic banking and related activity.

### **E-banking fraud**

In the latter months of 2003 a number of high-profile attacks aimed at customers of online banks in the UK and abroad took place, commonly known as phishing scams. The scams attempted to dupe customers into divulging their security details at replica bank websites. Although thankfully few customers became victims of these scams, and the underlying security of bank systems was not

## **APACS** has played an active **role** in the MPF's work on third-party **authentication**

affected, there was concern that confidence in the integrity of online banking might be shaken. A multi-pronged approach was taken to address the problem, including the creation of a new working group comprising representatives from APACS members, the British Bankers' Association and the National Hi-Tech Crime Unit; information gathering and intelligence sharing; publication of best practice guidelines for customers; and dissemination of information on technical measures to help combat fraud.

### **Token-based authentication**

An initial UK specification for the use of chip and PIN cards in handheld readers was issued at the end of 2002, giving members the option of using dynamic, two-factor authentication for customers when banking or paying online. Token-based authentication would provide customers with a similar experience to that at cash machines and in retail outlets. Whilst benefiting from the investment being made in chip and PIN, it would be significantly stronger than authentication based on password and user identity.

In 2003 interest in token-based authentication increased significantly within the UK and abroad. APACS has been working closely with MasterCard, Visa and a number of associations overseas to encourage the development of a common global specification.

### **Mobile commerce**

Mobile commerce remains at a formative stage with different business and operating models being developed with mixed success. The Mobile Payment Forum (MPF) has been attempting to broker agreement between key stakeholders in the banking and telecommunication sectors on operational and business models for mobile payments and authentication. APACS has played an active role in the MPF's work on third-party authentication. Other activity has included discussions with Simpay and individual mobile network operators on areas of mutual interest, and liaison with the European Commission and FSA on regulatory issues.

### **E-Government**

Activity on e-Government issues increased towards the end of the year. Together with the Office of the e-Envoy, APACS members are exploring the potential for exploiting the registration and authentication mechanisms developed by banks for online banking to help their customers access e-Government services. A number of challenging commercial and operational issues will need to be resolved if progress is to be made and discussions are in their early stages.

### **tScheme**

tScheme operates an approvals regime for Trust Service Providers (TSPs). ECG provides and funds Board-level representation for tScheme and also sits on the Profiles Committee that develops the criteria against which electronic TSPs are assessed for tScheme approval.

### **Legal and regulatory issues**

ECG provides guidance to members on key issues affecting the regulation of e-commerce. During 2003 it provided input for responses to consultations on the entitlement card and the regulation of e-money. ECG also maintains a database of legal material relating to e-commerce on APACS Online.

### **Standards and Security**

The Standards and Security Unit provides support to ECG in the area of e-commerce standards and security. This includes representing APACS members in relevant international standards arenas, such as the European Committee for Banking Standards' initiatives on mobile commerce, e-payments and bank trust services.

### **European Payments Council (EPC)**

ECG is represented on two task forces: the Straight-Through Processing Customer-to-Customer Task Force and the Business and Customer Requirements E&M Payments Task Force. This latter Task Force has been one of the most active groups within the EPC, initially focusing on the development of a common vision for electronic and mobile payments. APACS has played a central role in this activity, supported and directed by ECG.

## 26 | Liquidity Managers Group



*Liquidity Managers Group (LMG) has shown that the rationale behind its formation (that liquidity management is now central to real-time high-value settlement systems) was sound. The main high-value settlement systems in London with which LMG is concerned - CHAPS, CREST and CLS - are working well and LMG, as a result of its regular dialogue with specialists in liquidity management, was able to deal with occasional disruptions relatively easily.*

*Now that the major settlement system construction projects of the last few years have been completed - TARGET, CLS, and DVP in CREST - attention has turned to improving their efficiency and designing the next generation. LMG provided input to the European Central Bank's review of the collateral it takes against providing liquidity for TARGET. Also in 2003 LMG participated in work to design the next generation of this system. Efforts continued in the UK to ensure that settlement risk is reduced in the remaining systems. APACS is working hard in that respect along with BACS and Cheque and Credit Clearing Company, and liquidity considerations form part of that debate. Similarly the FSA is considering how sufficient liquidity can be guaranteed for the real-time systems and LMG is providing input in this area.*

*Business continuity is an important ongoing issue, and arrangements for transferring liquidity between systems in an emergency have been kept under review. During 2003 the New York Federal Bank published a plan for a global collateral pool which could be used in emergencies; this continues to be the subject of debate amongst the world's central banks.*

Antony Littleton

### Key issues in 2003

- The migration of money market instruments into CREST enables all financial securities traded in London in sterling and euro to be dematerialised and settled in CREST with full Delivery versus Payment (DVP) in real time.
- LMG has concentrated on examining the potential consequences of the failure of a real-time settlement system, particularly from the point of view of liquidity management.
- APACS is working on the consolidation of securities settlement in Europe from a variety of perspectives: with the European Central Bank; with the European Banking Federation; and with EuroClear and CRESTCo.
- As pressure grows for quicker, more harmonised securities messaging between players, especially cross-border, APACS is becoming increasingly involved in the work to meet this demand.

### Money market instruments switch to CREST settlement

In September 1998 the Bank of England published the results of its review of the arrangements for settling securities traded in London - *Securities Settlement Priorities Review*. The future they envisaged was one in which London-traded securities are dematerialised and settled on a single settlement system in which ownership rights are well-founded in law, with simultaneous transfer of title against cash with finality - continuously, cheaply and, if possible, with links to overseas settlement systems.

The merger of CRESTCo into Euroclear is proceeding and Euroclear have recently announced changes to their planned governance structure in response to the reservations expressed by some of their customers. At the same time they are consulting with the industry on the design of the Single Settlement Engine and APACS is responding to this consultation.

Securities settlement harmonisation is a complex issue and is sometimes perceived to be proceeding with frustrating slowness. Nevertheless, it is making gradual progress as

technical work. Over the next few years, as systems become more automated and are required to interact with each other increasingly quickly, this work will assume even greater importance.

The LMG Legal Issues Sub-Group played a key role in preparing for the migration of CMO. It has also been involved in work to consider the implications of harmonising European and global securities legal frameworks. The production of a standard European legal framework for securities is well under way and is expected to make further progress in 2004.

## APACS continues to contribute to the European securities settlement arena

In October 2003 this was realised, with the successful dematerialisation of money market instruments, enabling them to be settled in CREST alongside bonds and equities, and the closure of the Central Moneymarkets Office (CMO). APACS played an important part in co-ordinating the settlement banks' preparations for this and liaising with the activities of the Bank of England and CRESTCo.

### Europe

APACS continues to contribute to the European securities settlement arena. The Financial Services Action Plan programme is making progress and the resultant legal consultations emanating from Brussels are designed to ensure that securities can be traded and settled across European borders within a consistent legal framework.

the various inter-dependencies are achieved. The situation in Europe is also reflected in the global arena, with similar legal debates being held. This will result in the world's securities markets becoming gradually linked and harmonised, leading to widespread economic benefits.

### Operational and legal

The Securities Industry Operational Group (SIOG) was heavily involved with the migration of the settlement of money market instruments from CMO onto CREST. This required attention to detail with regard to technical issues, such as the running off of securities on the old system and reissuing replacements on the new. Attempts are being made to harmonise securities messaging across Europe and SIOG's role is becoming increasingly focused on the resulting



## 28 | Member Strategy Group



*Member Strategy Group (MSG) has operated as a sub-group of APACS Council since November 2000, with membership open to all APACS members. MSG takes an overview of domestic and international co-operative developments, focusing on strategic, pan-scheme issues that are not addressed within other fora. Its aims are to provide useful insight and guidance to Clearing Companies and Interest Groups, although it has no direct authority to influence their decisions.*

*The Group is the primary co-ordinator for the UK payments industry's participation in European Payments Council activities, and interest in these developments has led to an increase in MSG membership, which currently stands at 16 financial institutions.*

Tina Dinnis

### **Key issues in 2003**

- Working with the European Payments Council (EPC) to develop the Single European Payments Area (SEPA), including agreement on conventions for cross-border credit transfers; establishing the UK entry point for the EBA STEP2 scheme; and development of a model for a Pan-European Direct Debit (P€DD) scheme.
- The OFT market investigation into payment systems resulted in the publication of their favourable report in May 2003. APACS and its members had been heavily involved in briefing the OFT on how payments in the UK operate.

### European Payments Council

During 2003 MSG's work has been dominated by activities related to the EPC, which is co-ordinating the construction of SEPA. The aim of SEPA is to enable customers to make intra-EU payments in euro as easily as they make domestic payments, without price discrimination. Regular meetings provide a forum for members to debate EPC developments and to receive briefings from some of the UK representatives on the various working groups. The aim, wherever possible, has been to reach a UK view on the direction being taken at European level. As EPC matures, there is

- Supporting the EPC's strategic aims to reduce the volume of cash handled by banks and to improve the profitability of cash handling. Cash processing in the UK costs around £2 billion per annum, and a strategy for increasing the rate of migration to non-cash instruments in the UK has been developed.

**OFT investigation into payment systems**  
The OFT Member Contact Group, a subset of MSG, acted as the main information exchange and member communication channel during the OFT market investigation into payment

## The aim has been to reach a UK view on the direction being taken at European level

an increasing focus on the implementation practicalities, and a dedicated UK EPC group has been established by MSG to undertake this role.

Key EPC activities during 2003 include:

- Agreement on the basic standards, rules and conventions for cross-border credit transfers.
- Ensuring that all financial institutions will be reachable by PE-ACH, the Pan-European ACH, for which the EBA STEP2 scheme has become the first accredited provider. HSBC has agreed to be the UK entry point for STEP2; transactions will be forwarded to beneficiary banks via BACS Remit.
- Designing a P€DD scheme, with the establishment of a new scheme rather than to try and harmonise the legal frameworks and practices of national schemes. By the end of 2003 the EPC was nearing agreement on a model that bears a close resemblance to that favoured by the UK banks.
- Increasing the level of cross-border co-operation on card fraud prevention by creating a European equivalent of the APACS Plastic Fraud Prevention Forum.

systems. The OFT's report, published in May, was generally balanced and favourable, reflecting the constructive and detailed input by members and scheme companies during the consultation period. One of the drivers for changing APACS' governance arrangements in September 2002 was to improve regulatory compliance and counter issues highlighted by the Cruickshank report. The OFT report made favourable comments on the current governance arrangements, except for criticism of the exclusion of non-financial institutions from the BACS schemes. This issue will be actively addressed by BACS Payment Schemes Limited in 2004.

### APACS governance

At the time of introducing APACS' new governance arrangements, it was agreed that there should be a post-implementation review after 12 months to determine whether the new arrangements were operating satisfactorily. The early findings were reported to APACS Council in November, and it was agreed that a radical review of APACS governance and organisation would take place in 2004. The relationship between APACS and the Clearing Companies, the co-ordination mechanisms and the relationship with the regulators will all be within its scope.





*APACS provides the authoritative voice on co-operative issues for the UK payments industry and 2003 was an extremely exciting and busy year as a prodigious number of issues hit the headlines. APACS is experiencing a higher level of media interest than ever before, resulting in increased recognition of APACS members' role. The major communications issue for the industry was without doubt the trial of chip and PIN in Northampton followed by national roll-out. This is the greatest change to the way we pay since decimalisation and affects every single cardholder - over 90% of the adult population.*

*Other issues hitting the headlines in the past 12 months include the growing menace of identity theft and the Treasury Select Committee inquiry into transparency of credit card charges. APACS members scored a notable success in agreeing a Summary Box enabling customers to compare credit card key features and getting that out to customers in very short order. Several issues quickly became hot spots of media attention during 2003, notably cash machines and the move from low-tech to hi-tech fraud, and phishing e-mail scams. Our objective is to ensure consistency of message across the payments industry, working closely with members' press offices in developing key briefing material. Within Europe the progress of the Consumer Credit Directive continued, and we undertook concerted lobbying to get our views across and influence the debate.*

*On 9 June 2003 the Chancellor of the Exchequer announced that the five economic tests for UK entry to the euro had yet to be met, but a series of reforms would be put in place in order to facilitate UK entry. At the same time HM Government published its third Outline National Changeover Plan and in November the draft Single European Currency (Referendum Bill) was released.*

Sandra Quinn

### **Key issues in 2003**

- APACS provided key spokesmen for the launch of the chip and PIN trial and national roll-out. Considerable broadcast and print media interest was generated, providing an excellent PR platform in advance of the national advertising campaign.
- The heightened awareness of credit card issues led to APACS being the first port of call on a myriad of related media and governmental issues, reflecting the increased view that these have a massive impact on the industry's reputation.
- Close working relationships with HM Treasury ensured a timeline for euro entry being proposed which, for the first time, met key industry objectives.

## Communications

### An increasingly proactive role

In 2003 APACS produced an unprecedented number of press releases and statements to ensure that the industry's point of view was recognised. Corporate Communications was able to play its rightful part in developing key industry policy. Our aim is to meet issues head-on and provide the best possible response.

National and regional press briefings were held for chip and PIN. Northampton became something of a second home and we were delighted to witness chip and PIN working so well on the ground and share this with a number of different organisations including the Home Office, OFT and Consumers' Association.

### Evaluating our impact

In March 2003 a poll of personal finance journalists was undertaken on our behalf by MORI. Journalists writing for major national and regional publications were interviewed, including those who are major freelance names. Journalists' familiarity with APACS was measured, as were their reactions towards us. In addition, comparisons were made against other major organisations to put the results into context. Unsurprisingly, at the early stage of the year recognition of APACS was relatively low. However, the results were largely encouraging. Quotes from the journalists were included in the survey results; these were generally very positive as these two examples show:

- *"They're always there shouting about ... one of those bog standard basic parts of banking. But APACS do a good job of making sure people understand what goes on in that industry."*
- *"I always find them very, very helpful, very professional."*

It will be interesting to see whether our increased profile is reflected in 2004 results, even if this means more bruising comments.

### The industry voice

The number of both media and public queries dealt with in a year has rocketed. The growth of media interest in APACS issues resulted in more than a doubling of the calls received from

print and online journalists. Broadcast activity increased exponentially, even on those days where we were not leading the agenda.

A case of mistaken identity in South Africa was a clear example of APACS being seen as experts in an increasingly busy field - identity fraud and how to avoid it.

Members' confidence in APACS resulted in a growth in the number of calls being referred

## The growth of **media interest** in APACS issues **resulted in** more than a **doubling** of the **calls** received **from print and online journalists**

to us on a welter of different issues - e-mail scams, cash machine fraud, transparency, as well as the old chestnut - the length of clearing cycles for cheques and automated payments. An interesting development in 2003 was the blurring of competitive issues with industry-wide reputational matters.

In addition the level of public queries and requests for advice streamed in by e-mail, phone and post. Many of these are referred by a mix of other organisations, particularly the Financial Services Authority, Financial Ombudsman Service, British Bankers' Association, Bank of England and Banking Code Standards Board. Improved briefings and monitoring of these queries may lead to a stemming of this flow which takes considerable time and tact.

Many calls are fielded by the Reception team, who work very closely with the rest of Corporate Communications.

## Government and EU relations

APACS' role as a trade association has always ensured close relationship with government in all its different guises. The increasing raft of legislation impacting payments has led to stepped-up activity in this area. The extensive list of issues has provided an ideal platform to extend the breadth and depth of our

relationship. Contacts have been successfully extended amongst Ministers, key MPs and civil servants in the UK. On the EU side, there have been regular meetings with MEPs as well as the European Commission to increase their understanding of members' concerns.

To assist members, the remit of the EU Regulatory Consultative Group has been widened to include UK as well as EU regulatory initiatives, reflecting the frequent overlap of issues. APACS has played a lead role in co-ordinating a UK financial services response to the proposed Consumer Credit Directive through the newly-formed UK cross-industry group involving a number of financial services trade associations. This co-ordination has gone down well in Europe and offers a template for improving the focus of any UK response to European legislative proposals.





### Consumer Credit Directive

APACS has continued to work closely with members, Whitehall and other trade associations on this issue, through the Consumer Credit Directive Working Group, the DTI's consultation group and the UK cross-industry group. Throughout 2003 there has been heated debate in the European Parliament and also the European Council. Support for the UK perspective has been achieved from a number of influential MEPs, including the rapporteur, Joachim Wuermeling.

### Treasury Select Committee inquiry into transparency of credit card charges

The Treasury Select Committee report was published on 17 December. APACS gave evidence to the Committee in July 2003 and supported members prior to further evidence sessions in the autumn.

### New legislative framework for payments in the internal market

The European Commission published its long-awaited Communication on 2 December 2003. APACS responded to the Commission via the Regulatory Consultative Group and is taking an active role in working groups set up by the European Payments Council and HM Treasury. The current timetable for the Commission's publication of draft legislative proposals is late spring 2004.

### Banking Code

APACS works closely with the BBA and the BSA as industry sponsors of the Code. A review of the 2003 Banking Code will begin in January 2004 and continue until the autumn. Together with other co-sponsors of the Code, APACS is taking an active role in the review.

### Euro preparations

#### Banking industry position

Extensive lobbying by the industry continued on the practical implications of a euro changeover, specifically lead-time requirements for the development and testing of the payments infrastructure. These requirements are recognised by the *Managed Transition Plan* (previously referred to as the *Phased Approach*) contained in the third *Outline National Changeover Plan* (ONCP3).

The joint APACS and BBA UK Banks' Technical Group continues to meet on a monthly basis. The Group's primary focus has been to ensure that aspects of banking industry policy on euro entry are being widely communicated via the different workstreams set in place by HM Treasury's Euro Preparations Unit.

#### HM Treasury activities

The Treasury's major activity was obviously publishing its assessment and 18 studies on criteria for UK entry to the euro and ONCP3 on 9 June. It published its seventh *Report on Preparations for Euro* in November, which further details the work programme noted in ONCP3. The Treasury's Managed Transition Advisory Group has put in place a series of workshops, with very active participation from the industry, with the objective of further detailing how the managed transition would work in the UK. Specific attention is being paid to how different interfaces within each sector would be managed. HM Treasury intends to publish a revised *Managed Transition Plan* and an *Integrated Communications Plan* for the UK by the summer of 2004.

The banking industry will continue to maintain a key role in providing consultative advice to those sectors with which it has close relationships.

A commitment to review the progress of these reforms is expected in the 2004 Budget. This will be seen by many as a crucial point in the overarching political debate as to whether HM Government will decide to ask the question: "Should the United Kingdom adopt the euro as its currency?" Such a commitment from HM Government would signal a massive step change and impact on the banking industry's preparations for euro entry.

*All participants in payment systems - customers, regulators, and members - share a strong common interest in ensuring that risks are identified and controlled; that regulations and laws are framed to be cost-effective and have no unintended adverse effects; and that rules and laws, once instituted, are adhered to. Achieving these aims is central to APACS' role.*

*With increasing globalisation the UK is impacted more quickly and directly than ever by European, US and other worldwide regulation. Concerns about potential major operational disruptions as a result of terrorist action, and the exposure of financial and financial control weaknesses, are raising the stakes. A further key challenge for the UK payments industry is to manage effectively the rising tide of new controls from both inside and outside the banking industry, and each Clearing Company and Interest Group is taking action.*

Paul Rider

### Key issues in 2003

- The execution of settlement agreements for BACS and the Cheque and Credit Clearing Company which provide a legally robust framework for multilateral netting, significantly reducing inter-member credit exposures.
- The various legal, regulatory, governance and audit best practice requirements have been summarised in a single set of guidelines for the use of the Clearing Companies.
- To strengthen industry awareness of, and resilience to, potential major operational disruptions, APACS is participating in the HM Treasury Task Force on legal measures, in scenario-based virtual tests of industry contingency arrangements, and is sharing experience with the US financial industry and others.
- Tracking the increasing volume of proposed regulations which will have significant implications for the UK financial industry, from their inception through to enactment and compliance.



## Risk control

To remain world-class in their control of risk the UK payment systems need to satisfy a wide range of principles and guidelines set out by bodies such as the Bank of England, the Financial Services Authority (FSA), the Bank for International Settlements (BIS), accounting institutes, and also those laid down in UK laws or European Regulations. APACS has summarised these requirements in *APACS Best Practice Guidelines for Risk Control for Payment Schemes & Interest Groups*, a single source which Clearing Companies and Interest Groups can use to plan, monitor and audit their compliance. The *Guidelines* are being updated as regulations and best practice evolve.

APACS needs to ensure that the Clearing Companies and Interest Groups which use the APACS brand and resources conform to best practice on risk control. In line with this requirement, these entities are supplied with risk control, audit and legal expertise where necessary. APACS Council has formed a Risk Committee to monitor, advise and provide recommendations on industry-wide risk issues for UK payments.

## Settlement risk

Under normal operations CHAPS members exchange funds for each individual transaction as it takes place - that is, they settle in real time. However, for retail payment systems such as BACS, cheques and cards the sheer volume of transactions makes this impractical, so members settle with each other once a day for the net total value of transactions exchanged.

This gives rise to settlement risk - the risk that when the time comes to settle up at close of business, one member may not be able to meet its obligations. The members of BACS and the Cheque and Credit Clearing Company have set up a project to mitigate this risk, in accordance with the principles outlined by the BIS:

- *Phase one reduced member exposure very substantially by limiting the settlement exposure to the net, rather than the gross, amounts owed by each member. New settlement agreements, framed using specialist legal advice, were signed by all members of the two Clearing Companies in 2003.*
- *Phase two apportions the residual settlement losses in the event of a member failure. This loss-sharing agreement will require each member to put up collateral in advance, and also to commit to sharing losses above the amount of this collateral. The precise terms of this agreement are still being negotiated, and are expected to be finalised in 2004.*

## Risk of major operational disruption

The New York terrorist attack in September 2001, and more recent large-scale disruptions such as power failures on the Eastern seaboard of the US and in Italy, have focused attention on the vulnerabilities of key payment systems.

- HM Treasury consulted on the question of whether the UK needed additional legislation to enable it to cope in the event of major operational disruption in the

financial sector. Following the responses a Task Force was created, in which APACS participated, to investigate the question in depth. In December 2003 the Task Force reported that the potential drawbacks of new legislation outweighed the potential value, and the Government therefore decided not to legislate further.

The Task Force did, however, frame recommendations on good practice which the financial industry should follow, and APACS is looking at these.

- APACS conducted a scenario-based virtual contingency test with members, Clearing Companies and LINK, and is responding to the lessons learned from its outcome. It also participated in similar tests run by a standing committee comprising HM Treasury, Bank of England, and the FSA, and by the London investment banking community.
- APACS shares information with the US financial industry, and with global payment systems through membership of BITS - the US financial services round table - and its close relationship with SWIFT. Issues included in these arrangements are business continuity, telecoms resilience and crisis management. This enables APACS to progressively develop and adopt good practice in these areas.



### New regulations and laws

There are numerous laws, regulations and regulatory investigations which have significant implications for the UK banking and payments industries. Roughly half of these were introduced or significantly modified in the past two to three years, and the rate of this evolution is accelerating. APACS has mapped the general process - from inception of a regulation through research, investigation, consultation, recommendation, proposed regulation/law, enactment, interpretation and compliance - and is targeting its resources to contribute to and influence industry thinking and action in a way that matches this process. Two key APACS member groups, the Regulatory Consultative Group and the Legal Advisory Group, steer and provide input to this work.

Payment systems necessitate that members, who otherwise compete keenly in the marketplace, work together on co-operative issues. The Office of Fair Trading (OFT) needs to be satisfied that, where members co-operate, the rationale is objective, justifiable and transparent, and in the overall interest of customers. An OFT investigation into UK payment systems published in 2003 concluded that this was generally the case, and in December the Government decided that primary legislation strengthening the OFT's payment systems powers could safely be deferred for some years, with the OFT taking on an enhanced role within its existing powers. The payments industry and the OFT continue to liaise closely on outstanding issues such as the length of the payment process, the existence of 'float', and transparency to the end customer.

### Audit services

Clearing Company Boards and Interest Groups need to ensure that their rules and decisions on risk controls and member and supplier performance are being soundly implemented by:

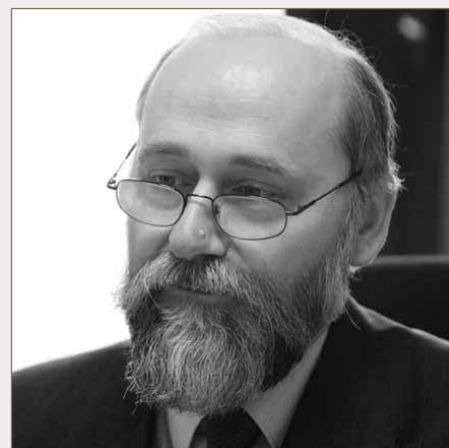
- Gathering and regularly reviewing performance statistics and investigating any incidences of poor performance.
- Performing risk-based operational audits of the Companies' processes and those of their members.

- Commissioning external auditors to provide an independent review of risk controls, using internationally accepted audit standards.
- Accrediting third parties which fulfil key parts of the payments processes, to ensure that their own risk controls meet the standards set by members to protect the security and integrity of the payment systems. Accreditation is performed for BACS bureaux, Industry Hot Card File providers, card protection agencies, cheque guarantee card manufacturers and for cheque printers.

The Clearing Companies and Card Payments Group use APACS' audit and security expertise and resources to provide, manage or assist in these activities. APACS also audits the management processes for its major projects to ensure that these meet high professional standards.

### Sorting codes

Sorting codes are the 6-digit UK payments industry 'postcodes' that ensure that payment transactions are delivered to the correct bank branch. APACS manages this issue, maintaining and disseminating sorting codes on behalf of the Clearing Company members. The electronic update process is subcontracted to the BACS infrastructure company, which is introducing a more streamlined process with web-based facilities in 2004 as part of its NewBACS development programme.



## 36 | Payment Markets



*APACS provides an in-depth analysis of the current and future structure of the UK payment markets. This analysis is based upon detailed market research, extensive discussions with banks and other payment providers and modelling of future trends and developments. It provides input into much of the market planning undertaken at industry level and by individual members.*

*The Payment Markets and Electronic Commerce Unit undertakes a broad range of consultancy projects for APACS Clearing Companies and Interest Groups. In 2003 this included the annual survey of CHAPS traffic, detailed analysis of settlement risk in BACS and the Cheque and Credit Clearing, ongoing economic risk analysis of credit card arrears and support for the development of a UK cash strategy.*

Peter Finlayson

### Key issues in 2003

- For the first time more than half of all adults in the UK now use debit cards on a regular basis to make purchases.
- The fastest-growing payment method was direct credit - the shift to Direct Payment of state benefits was the leading factor behind a 14% increase.
- Around 12 million adults use Internet banking and over 18 million have purchased goods or services online, predominantly paying by plastic card.
- The cashless society remains a long way off; there are very few people who do not make significant use of cash.

## Overview

Plastic card use became increasingly dominant in the high street, although there was a slow-down in growth caused in part by the economic environment. Direct Payment of state benefits boosted direct credit volumes, and the other bulk payment methods saw similar rates of growth to the previous year. Overall, non-cash transaction volumes rose by 4% to 14 billion.

In future years consumer choice will expand as access to existing payment methods becomes more widespread, and as new products enter the market. E-commerce is having a major impact on both the personal and business sectors and chip and PIN will introduce a new dynamic to the card payment environment. The implementation of Direct Payment will increase account holding and change the payment and cash acquisition behaviour of many benefit recipients.

In terms of future trends, total payment volumes are set to continue to rise. The proportion of automated and, in particular, plastic card payments is expected to rise considerably, whilst cheque volumes will continue to shrink. Specifically, plastic cards will account for 60% of the total projected transactions of 19.2 billion in 2012. Although the death of cheques is much-trumpeted, they will still account for one in 14 of all non-cash transactions in ten years' time, compared to one in six now.

## Cash

Cash remains a vital payment method for the UK economy. In 2003 cash accounted for around 70% of all payments in the UK, an estimated 25 billion transactions. Cash spending still accounts for around one-quarter of GDP. Nearly £270 billion was spent by individuals using notes and coin during the year, which equates to an average weekly spend by each adult of around £110 in cash. One person in four still prefers cash for all of their day-to-day purchases and there are only a very small number of adults who do not make significant use of cash.

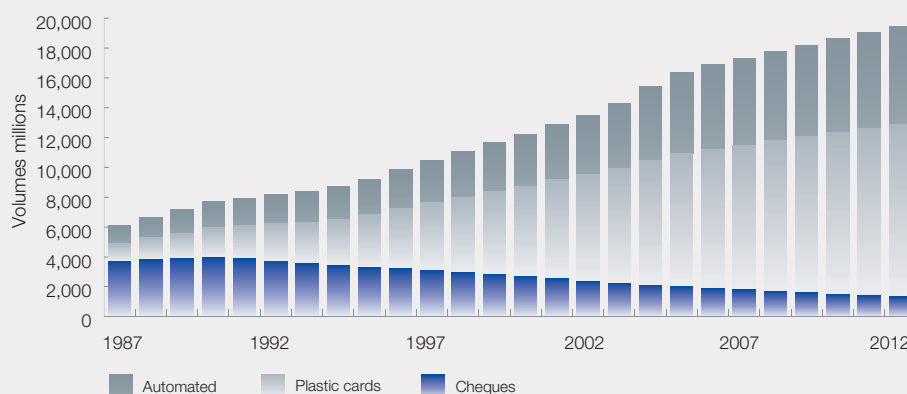
Direct Payment of state benefits and pensions will be the major influence on cash use over the next two years. It is expected to reduce the demand for and use of cash, as some recipients are likely to make more non-cash payments once their benefits are paid into a bank account.

Other than the impact of Direct Payment, only a modest decline is expected in the volume and real value of cash transactions, continuing the trend of recent years. Migration to debit cards for retail payments and direct debits for bill payment will erode cash use; however, much of this will be counter-balanced by the impact of economic growth and population increase.

C1 is near saturation and a major development here is multiple card holding. Six out of ten cardholders in these groups have at least two cards, and 15% have four or more.

Credit card volumes are sensitive to the economic cycle and over the next few years levels of use will be influenced by the extent to which consumers tighten their belts and the

APACS forecast for non-cash transaction volumes: 1987-2012



The overall forecast is that there will be 24 billion cash payments in 2012 to a total value of £260 billion in today's money. In ten years' time cash will still account for around 60% of all payments. The cashless society remains a distant vision.

## Plastic cards

In a milestone for plastic card use, over half of adults in the UK made regular use of their debit cards in 2003. Debit card volume growth has been slowing as a result of the maturity of the product, and was further depressed this year by the sluggish nature of the economy. There were an estimated 3.2 billion debit card payments in 2003, 7% more than in 2002.

There remains considerable potential for ongoing solid growth in debit card volumes. Many cardholders are not yet regular users and there are still opportunities for wider card acceptance, in particular arising from the introduction of chip and PIN. Debit card volumes are forecast to grow to 5.3 billion in 2012.

Despite continued vigorous competition between issuers, credit card payment volumes were also affected by the economic situation. Volumes only rose by an estimated 2% to 1.7 billion in 2003 - the slowest rate of growth for a decade. Card holding in groups AB and

rate of growth in borrowing slows. In the longer term, volumes are forecast to grow to 2.7 billion in 2012.

## Cheques

2002 saw the largest ever fall in cheque volumes in the UK, both in absolute and percentage terms. Similar rates of decline continued in 2003, with volumes of 2.3 billion, 6% lower than in 2002. A major driver is the move away from cheques by businesses as their preferred method to pay their suppliers and other trading partners. Increasingly companies are using electronic banking and accounting systems to make their business-to-business payments by automated means. This trend is expected to accelerate.

In the personal sector, migration to debit cards and direct debits continues to erode guaranteed cheque volumes and cheque use for the payment of regular household bills. Key questions for future cheque volumes are when, and to what extent, established and emerging electronic alternatives will reduce cheque use in those areas where volumes have not been declining. These include the payment of credit card and mail order bills, and person-to-person and person-to-small business payments.

The main APACS forecast is that cheque volumes will decline to 1.3 billion in 2012.



### Automated Payments

The introduction of Direct Payment, coupled with the new child tax credit, has already had a significant impact upon direct credit volumes. State benefits accounted for one in four of all BACS direct credits in 2003, compared to fewer than one in five in 2002. Other areas of strong growth during the year were telephone and Internet banking payments, with 12 million adults now using such remote banking services. Overall, there were 1.3 billion BACS direct credits, 14% more than in 2002. Looking forward, Direct Payment will substantially boost direct credit volumes in 2004 and 2005. Business use of direct credits to pay other businesses, and personal use of remote banking credits for bill payments are both projected to grow strongly over the next ten years. It is forecast that there will be 2.7 billion direct credits in 2012.

Standing orders remain popular for applications such as donations to charities and subscriptions to clubs and societies. It is estimated that in 2003 there were around 420 million standing order payments. Steady volume growth is expected to continue.

Direct debits were used to pay more than half of all personal regular commitments in 2003, including over 60% of utility bills. The major billers are expected to continue to promote and incentivise payment by this method. In 2012 it is forecast that nearly two-thirds of all regular bills will be paid by direct debit, with 3.4 billion payments in that year.

### Cash machine withdrawals

Over half of all cash acquired by individuals is obtained from cash machines. In 2003 an estimated £144 billion was paid out in 2.4 billion transactions, 5% more than in 2002. The rate of growth rose during the year and may reflect benefit recipients shifting to the use of cash machines once their benefits are paid by Direct Payment rather than obtaining cash at the post office. Direct Payment will give a further boost to this trend in 2004 and 2005 and, in the longer term, the demographic pattern of preferences will be a steady driver of growth - younger customers are more likely to use a cash machine than older customers. In 2012 it is projected that cash machines will pay out over £190 billion in today's money in 3.1 billion transactions.

The other major development in the cash machine arena is the continued growth in the

independent (i.e. non-bank) deployer sector. At the end of the year 14,436 of the 46,461 cash machines in the UK were owned by independent deployers. As these machines typically charge customers to withdraw cash, the levels of use are much lower than for non-charging bank-owned machines.

### CHAPS

CHAPS Sterling processed 27 million payments in 2003, 6% more than in 2002. The total value processed was stable at around £52,000 billion. The continued decline in the average value of a CHAPS payment indicates that the volume growth derives largely from non-financial customers such as businesses and solicitors. This will have been driven by the high levels of activity in both house purchase and re-mortgaging during the year.

By contrast, both volumes and values saw strong growth in CHAPS Euro. There were 6 million CHAPS Euro payments in 2003, 13% more than in 2002, and volume growth has returned to trend after the step increase in 2002 caused by the phasing out of legacy currencies in the eurozone. CHAPS Euro values rose by 11% to €53,000 billion. These increases are due to a number of factors, which include banks switching payments between euro systems, continuing expansion in retail payments and the growth in the euro as a world currency alongside the US dollar.

In addition to the two CHAPS systems, the total market for same-day payments, including correspondent banking and payments processed by other systems, has been estimated at around 60 million transactions in 2003 to a total value of £160,000 billion. In the retail area steady growth in demand is likely to continue: from businesses for trade and salary payments, from solicitors for housing payments, and from individuals for cross-border remittances. Value trends are more uncertain and will depend crucially upon settlement and trading patterns in the foreign exchange and other financial markets. Volumes and values will also depend upon banks' choices of payment system for transactions which are not inherently same-day. The forecast is that in 2012 the same-day market will account for 95 million payments to a value, in 2003 money, of over £250,000 billion.



## Market research

In addition to providing market research in support of specific projects undertaken by APACS Clearing Companies and Interest Groups, APACS also provides members with market information from a variety of surveys.

### The Consumer Payments Survey

The Consumer Payments Survey has been run on a continuous basis since 1988. It provides a basic monitor of the personal sector's financial holdings, payments and cash acquisition behaviour. The wealth of information it provides, together with its long unbroken sequence of operation, enables an invaluable understanding of the factors causing change in the payments market to be obtained. Data from the Survey is used in APACS' payment volume forecasts, and for a wide variety of other purposes in support of members. A *Digest of Statistics* from the Survey is produced each year for APACS members.

### Consumer Attitudes to Plastic Cards, their Finances and the Internet

In 2003 APACS undertook a research exercise examining how the attitudes of credit and debit cardholders influence their financial behaviour. It also specifically looked at how individuals interact with their banks and their attitudes towards making purchases over the Internet. This research complemented the information obtained from the Consumer Payments Survey to help provide a more complete picture of the payments market.

Some of the key findings from the research are:

- Non-users or light users of credit cards (39% of all debit and credit cardholders) want to avoid the temptation of getting into debt and incurring interest. If they do have a card they reserve its use for specific one-off purchases, such as holidays, or for unexpected emergencies, such as the breakdown of domestic equipment.
- Nearly half of all debit and credit cardholders have never had a store card. Only 10% use a store card for borrowing. Even among those who have a low awareness of credit card interest rates and who do not shop around for the best deal

on a credit card, there is a general understanding that store cards are an expensive means of borrowing.

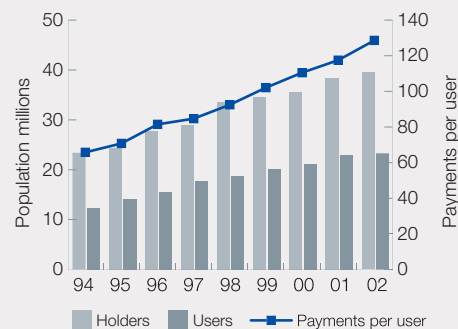
- There is high awareness of particular benefits of credit card use, such as protection against fraudulent use of the card and reward schemes. However, the protection provided by Section 75 of the Consumer Credit Act is less well-known.
- Over one-third of those with access to the Internet have used it for online banking. However, at present, not all users are comfortable using it for all financial activities. Nearly all users of online banking use it to check balances or make transfers, but only 14% would try to sort out a problem online, the majority preferring to go to a branch or speak on the phone.
- Convenience and value-for-money are the factors that have encouraged users to purchase a range of products and services over the Internet. Most had some initial fears when first purchasing online but, having successfully done so, their inhibitions largely disappeared and they became advocates for sites they found particularly good.

### Internet Monitor

APACS continues to publish a regular *Internet Monitor* every six months, providing information on personal consumers' use of Internet banking and e-commerce. Key findings from the third *Internet Monitor* published in September 2003 include:

- Nearly four in ten Internet users bank online.
- 48% of Internet bankers use it at least once per week.
- Over half of all Internet banking users initiate payments online.
- Over half of Internet bankers also use telephone banking.

Trends in debit card holding and use - obtained from the Consumer Payments Survey



## 40 | Standards and Security



*Whilst APACS continued to monitor a wide range of issues across the international arena, the development and future direction of payment standards within Europe has been dominated by the creation of the European Payments Council (EPC). The European Committee for Banking Standards (ECBS) has accordingly been restructured to take its strategic direction on payment standards for Europe from the EPC.*

*In addition to focusing on European payments, APACS will continue to monitor developments in the wider international arena, particularly cards-related activity, messaging issues and developments in information security.*

Dick Mabbott

### Key issues in 2003

- A global patent monitoring service was successfully established during the year to actively monitor all new patent applications from around the world.
- The ebXML Core Component Technical Specification (CCTS), a technology-neutral method of specifying the business information content of transaction messages, developed under the auspices of the UN, was completed during the year. CCTS provides the backbone for standards convergence in this area.
- The industry-developed protection profile for PIN entry devices achieved its final certification under the common criteria during the year.
- A European Regulation aimed at reducing the cost of cross-border payments within the EU stipulates that banks take the necessary steps - by clearly communicating this information to their customers - to ensure customers quote both the IBAN of the beneficiary and the BIC of its bank on their payment instruction.

## Standards

### Plastic cards

APACS continues to provide leadership and administrative support (chairman and secretariat) to the International Organization for Standardization (ISO) committee responsible for plastic card standards, which addresses all aspects of generic identification associated with plastic cards. The work of this committee has assumed far greater global importance since the terrorist attacks of September 2001. 2004 sees the introduction of machine-readable passports incorporating similar chip technology to smart cards, enabling biometric identification of the document holder at border crossings. The UK Government is pursuing the same technology for its proposed national identification card and APACS is closely monitoring long-term trends and the potential ramifications on personal identification for e-banking and banking technology generally.

Work to enhance the ISO PIN Management Standard continued throughout the year and revision of the basic management standard is now complete. Aspects relating to cryptography are still undergoing revision.

### IBAN - International Bank Account Number

Originating financial institutions are required by European Regulation 2560/2001 to provide clear IBAN and BIC information to their customers. This should lead to lower costs for cross-border payments. As a result, political and consumer pressure to implement IBANs has intensified over the year, with APACS supporting members' IBAN implementation.

Input and guidance has been provided to relevant EPC groups on the use of IBANs as a means to facilitate straight-through processing rates across the Single European Payments Area.

More information on IBANs can be obtained from the APACS website and also the ECBS website ([www.ecbs.org](http://www.ecbs.org)).

### Messaging standards

The ebXML Core Component Technical Specification (CCTS) is a technology-neutral method of specifying the business information content of transaction messages, documents or interactive dialogue by which business is carried out. It is equally applicable to paper

(such as UN Layout Keys), traditional EDI, XML or, indeed, future formats.

CCTS is a major deliverable of UN/CEFACT (United Nations Centre for Trade Facilitation and Electronic Business). It forms the backbone for standards convergence and is recognised by organisations such as SWIFT and Open Applications Group as the means by which this can best be achieved. In 2003 CCTS successfully completed two trials to become a global standard. Continued work in the coming year will centre on the maintenance and promotion of the standard as a viable technical solution.

APACS has played a major role in the UN/CEFACT work on cross-industry and intra-standards harmonisation between ISO15022 second edition and UN/CEFACT XML solutions. It is also involved in the UN/CEFACT Finance Group which is central to the development and harmonisation of finance industry standards via ebXML, and ISO15022 second edition where SWIFT is currently the registration authority.

APACS continued to participate in the meetings of the Corporate Reference Group as part of the UN/CEFACT Finance Group. It is significant to note that the large multinational corporates that make up this group are now engaging with their smaller counterparts, with a view to representing their collective requirements to banks for adoption.

### SWIFT

SWIFT has also made considerable contributions to CCTS and the UN/CEFACT work as a whole. As well as finance-specific

activities, SWIFT has been working to facilitate standards convergence under the auspices of ISO and UN/CEFACT. In doing so they have helped position the UN/CEFACT Finance Group as a key stakeholder in achieving standards convergence. The SWIFT Standards XML documentation, currently being reviewed, is due for release in 2004.

### European Committee for Banking Standards (ECBS)

ECBS continues to act as an important European reference point for the development of and guidance on finance and banking standards. During 2003 APACS has been actively involved in developing the meta standards and guidance relating to the refinement of the PE-ACH technical architecture. This included a detailed knowledge-gathering and comparison exercise between existing European domestic ACHs, together with technical recommendations on improved functionality of the PE-ACH architecture.

APACS continues to represent the interests of the UK industry at the ECBS, tempered with a strategic overview of international standards development.

### Cross-Border Standards Group (CBSG)

During 2004 APACS will continue to influence key standards initiatives to secure the interests of the UK banking industry. It is anticipated that CBSG will be central to the UK taking an active and informed role in standards developments, under the auspices of EPC, SWIFT, ISO and UN/CEFACT. CBSG continues to be an important reference point for this work in the UK.



## Security

### Security Advisory Group (SAG)

As the senior industry group on information security, SAG holds an overview of security issues.

### Chip and PIN

Continued support has been given to the roll-out of chip and PIN and, together with member card security experts, we are exploring what steps should be taken to ensure that the underlying technology remains secure and effective. This has included reviewing the implementation of chip and PIN in other countries as well as card architectures.

Work to promote terminal security has included the final certification of the industry's protection profile for PIN entry devices. Awareness has been raised amongst vendors and developers of how to prepare their products for evaluation, including evaluation processes and the use the industry will make of these results.

### E-banking

Work on tackling the threats against e-banking services has included the co-operative development and continual review of the industry's principles and practices for secure remote banking, which set out the essential design principles and risks that institutions should address. Information has been shared on threats to e-banking services, together with co-operative procedures developed within the industry to respond to incidents, between APACS members and with law enforcement agencies and other interested parties.

Support of the Electronic Commerce Group continued, examining strategies for delivering enhanced security for e-banking services that will be economical, effective, easily scalable and easy for end users to deploy and use.

### E-crime and security industry liaisons

A contribution has been made to the debate within the wider UK information security community on the challenges from e-crime, and the need for all sectors of UK business to implement and deploy security measures more effectively. Discussion papers on the particular challenges and difficulties faced by the UK SMEs have also been incorporated in the formative responses to the Home Office's evolving e-crime strategy.

### Third-party processors

A re-assessment was carried out of the security of third-party service providers that use and store bank customers' information. Alternative assurance and audit methodologies were examined, resulting in the formulation of the industry's view of the most appropriate and relevant way forward for its purposes, which include both BS7799 certification and tScheme approval.

APACS is supporting the development of new industry accreditation schemes that will use these evaluation methodologies as measures of a provider's ability to protect customer information.

### tScheme

HM Government, in its plans to modernise access to government, actively encouraged the adoption of digital signatures by both citizens and corporates and thus the use of digital

certificates issued by Trust Service Providers. However, take-up of such services has been slower than expected.

One new approach is for Government to use intermediaries, such as banks with their online banking identification processes, to identify customers on their behalf and then convey the pre-authorised user to the Government gateway to access its services. The Government has asked tScheme to develop a suitable profile against which organisations offering such an introductory service can be accredited.

### Patents

At the start of the year APACS was asked to monitor all new and old patent applications and grants for any patent that would potentially be either disadvantageous or of interest to members' business. These would be brought to the attention of the appropriate business group within APACS or to the Patent Monitoring Group specially set up for the purpose.

This patent-monitoring service has been established and all new global applications, published under the Patent Co-operation Treaty, are now actively monitored. Monitoring applications and grants prior to the beginning of 2003 is considerably more difficult. The priority, however, is to intercept potentially troublesome patents and applications as early as possible as, generally speaking, the earlier the intervention the cheaper the cost of that intervention.





*The Statistical Unit continues to provide support across a range of Clearing Company and cash-related projects. It publishes a monthly report showing clearing volumes and values for the APACS Clearing Companies and an annual publication, the Yearbook of Payment Statistics, which contains historical data in respect of UK payment systems. More detailed information is provided to individual members on a monthly and quarterly basis, supplemented by comprehensive annual reports.*

Steve Hammant

## Key issues in 2003

- Detailed, individual member reports and data are available on APACS Online or direct from the Statistical Unit.
- A new system has been implemented to dynamically link all the weekly coin data to ensure fair and accurate allocation of coin sales.
- The transaction level CHAPS data provided by the Bank of England enabled us to analyse the spread of values and the country of origin (where appropriate) of CHAPS payments each day. This information is circulated to members each month and for the first time will be published in the *Yearbook of Payment Statistics* in 2004.

### Yearbook of Payment Statistics

The *Yearbook of Payment Statistics* provides annual clearing statistics dating back to 1990, with a management summary to highlight key

points. It also describes the development and history of the cheque clearing process and provides summary information relating to the UK payment markets.

### Data in electronic format

Annual, monthly and an historic monthly series of clearing statistics are published on the APACS website. Earlier series, in some instances dating back to 1868, are available on request from the Statistical Unit.

All regular reports, together with individual member reports, can be accessed via APACS Online. Where appropriate, data is stored in secure member-specific areas. Reports are also available in paper format if required.

### CHAPS clearings

The data for the CHAPS clearings is obtained directly from the Bank of England, and allows the regular monthly reports (which now include details of message types and a breakdown by value band) to be produced at the beginning of the week following the month end. Detailed analysis was undertaken during the migration from SWIFT Message Type 100 to 103 and the relevant information was passed to members to enable them to monitor their performance at set intervals. Daily forecasting to predict CHAPS Euro and Sterling peak days is also carried out.

Liquidity in Crest continued to be reported on a quarterly basis, and additional data supplied by SWIFT was processed for use in the CHAPS Traffic Survey.

### Cheque and credit clearings

Cheque and Credit Service Level Reports are produced each month to help members improve their operational performance.

The underlying codes are reviewed annually to ensure that they remain relevant and sufficient for members' needs. The English paper exchange centre moved from London to Milton Keynes at the end of 2003; the Statistical Unit helped to facilitate a smooth transition by constructing delivery matrices and forecasting volumes in advance to assist members with their planning. Information has been received from members each working day since the move and is collated to ensure that clearing items are still delivered for processing in a timely manner.

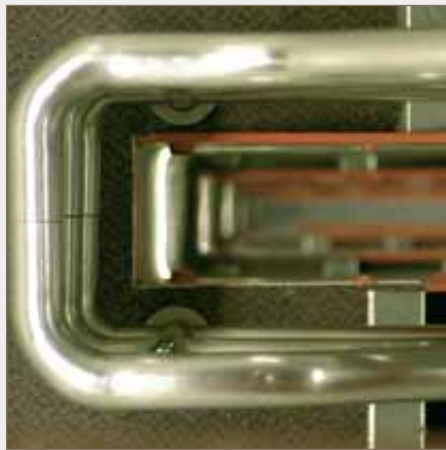
The ongoing collection of data relating to the bulk euro-denominated cheque clearing continues, with volumes remaining steady at approximately 3,000 items per day.

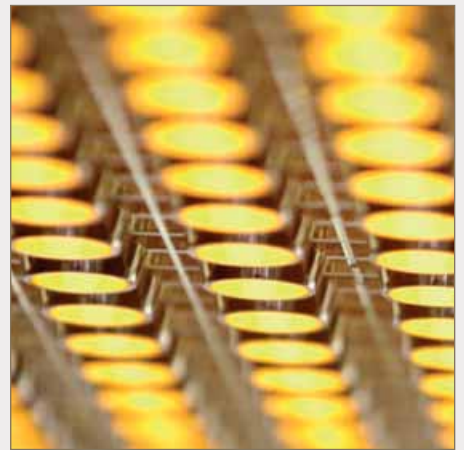
Work is ongoing to monitor the number and type of paper credits that pass through the clearing, the quality of cheque and paper credit printing, and the numbers of travellers' cheques exchanged. Statistics for the US dollar clearing, the only remaining currency clearing, continue to be collated. The clearing currently averages about 450 items per day.

### Cash

The analysis of wholesale movements of notes and coin continued throughout the year, as did support for the Coin Distribution Working Party (CDWP). A new system has been implemented to record inter-bank coin movements. The system has improved the allocation of coin to members and has made it easier to track actual coin demand against forecasts. In 2004 it will be used to assist in a review of CDWP operating procedures.

44 | Behind the scenes





## APACS structure and membership

*APACS is a non-statutory, unincorporated association, set up in 1985 as the forum for discussion of non-competitive issues relating to money transmission in the UK.*

*Membership of APACS is open to any institution which is a principal member of a payment scheme widely used or otherwise significant in the UK (i.e. a payment scheme which handles more than 1% of the UK's payment volumes and/or more than 0.1% of the UK's payment values).*

*Organisations (or individuals) with a strong interest in the UK payments industry, but which are either not eligible, or do not wish, to join APACS may opt to become APACS affiliates. Affiliates receive regular updates on payment matters, including invitations for their staff to attend seminars, and copies of APACS publications.*

*At the end of December 2003 there were 34 APACS members and 27 affiliates (see page 1). APACS is keen to attract new members and affiliates. For more information please contact **corpcomms@apacs.org.uk**.*

The major UK payment clearing systems are managed by three autonomous Clearing Companies operating within APACS who are responsible for maintaining the financial integrity and operational efficiency of the clearings:

- CHAPS (page 6)
- Cheque and Credit (page 10)
- BACS Payment Schemes (page 12)

The APACS constitution enables various payment schemes and interests to pool information, resources and skills for mutual benefit. These are formally recognised as APACS Interest Groups:

- Card Payments Group (page 14)
- Cash Services Group (page 22)
- Electronic Commerce Group (page 24)
- Liquidity Managers Group (page 26)

In addition the currency clearing operates as a clearing group for US dollar paper items.

APACS (Administration) Limited, a non-profit company owned by the APACS members, acts as the service company for the Association, and also provides services, staff and resources for the three Clearing Companies.

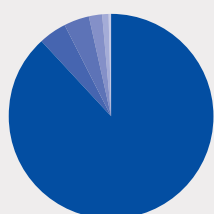
APACS maintains close links with other payment and banking organisations, including the British Bankers' Association, CRESTCo, Euro Banking Association, European Banking Federation, European Payments Council, LINK, MasterCard, SWIFT and Visa.

## Clearing peak values and volumes in 2003

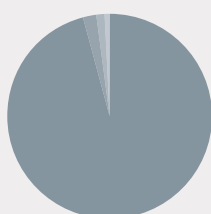
	Peak daily value of items	
	Million	Date
BACS	£21,153	27 Nov 2003
CHAPS Sterling	£297,884	22 Apr 2003
CHAPS Euro	€327,357	30 Jun 2003
Cheque clearing	£8,109	1 Apr 2003
Credit clearing	£835	22 Apr 2003

	Peak daily volume of items	
		Date
BACS	63,985,405	28 Nov 2003
CHAPS Sterling	220,254	28 Nov 2003
CHAPS Euro	37,755	30 May 2003
Cheque clearing	8,703,189	7 May 2003
Credit clearing	919,123	4 Mar 2003

### The clearings - values



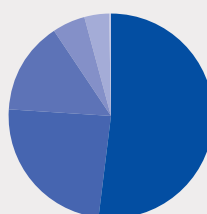
	1993
CHAPS	88.1%
Cheque clearing	4.4%
Town clearing*	4.0%
Direct credits and standing orders	2.1%
Direct debits	1.0%
Credit clearing	0.4%



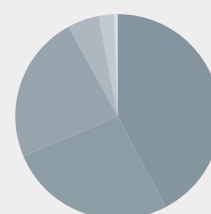
	2003
CHAPS	95.8%
Direct credits and standing orders	2.1%
Cheque clearing	1.3%
Direct debits	0.7%
Credit clearing	0.1%

	1993	2003
Electronic	91.2%	98.6%
Paper	8.8%	1.4%
<b>Total annual value (billions)</b>	<b>£26,719</b>	<b>£92,470</b>

### The clearings - volumes



	1993
Cheque clearing	52.0%
Direct debits	24.1%
Direct credits	14.6%
Standing orders	5.2%
Credit clearing	3.9%
CHAPS	0.3%

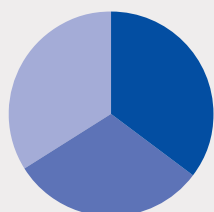


	2003
Direct debits	42.2%
Cheque clearing	26.4%
Direct credits	23.3%
Standing orders	5.0%
Credit clearing	2.4%
CHAPS	0.6%

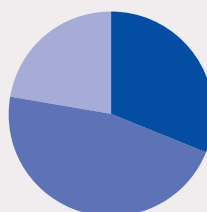
	1993	2003
Electronic	44.0%	71.1%
Paper	56.0%	28.9%
<b>Total annual volume (billions)</b>	<b>4.3</b>	<b>5.8</b>

\* The Town clearing ceased operation on 24 February 1995

### Plastic cards



Number of cards in issue (thousands)		
1993	2003*	
Credit and charge	27,588	71,256
Debit	24,118	62,854
Cash machine stand-alone	26,580	24,874



Transaction volumes (millions)		
1993	2003*	
Credit and charge	812	2,026
Debit	1,215	5,208
Cash machine stand-alone	582	438

\* best estimate at time of publication

## Management staff

### Association for Payment Clearing Services

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[www.apacs.org.uk](http://www.apacs.org.uk)

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Chris Pearson

#### Deputy Chief Executive

Paul Rider

#### Finance Director

Ewen Stamp

#### BACS Scheme Managing Director

Mike Chambers

#### CHAPS Clearing Company Manager

David McFarlane

#### Cheque and Credit Clearing

##### Company Manager

Fred Galbraith

#### Director, Card Services

Paul Marsh

#### Director, Chip and PIN Implementation

Gary Hocking

#### Director, Corporate Communications

Sandra Quinn

#### Director, IT and Office Services

Sue Yoe

#### Director, Payment Markets and Electronic Commerce

Peter Finlayson

#### Director, Special Duties

Roger Jones

#### Director, Special Duties

Michael Lewis

#### Director, Standards and Security

Dick Mabbott

#### Director, Strategy

Tina Dinnis

#### Head of City Markets

Antony Littleton

#### Head of Security

Colin Whittaker

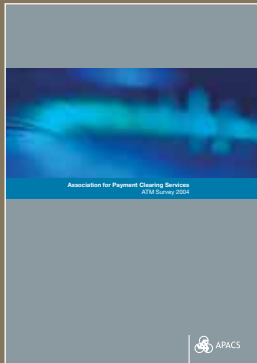
#### Personnel Manager

Chris Bailey

#### Senior Statistician

Steve Hamant





#### **ATM Survey 2004**

Examines the deployment and usage of automated teller machines in the UK.

**£50**

Available April 2004

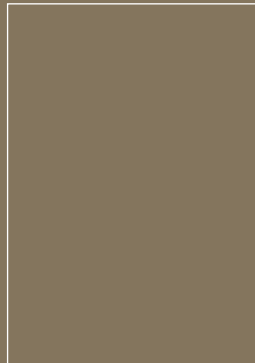


#### **Yearbook of Payment Statistics 2004**

A comprehensive source of UK payment clearing statistics over the last ten years.

**£130**

Available May 2004



#### **Plastic Card Review 2004**

A new-style publication looking at plastic cards and their use.

**£150**

Available May 2004

## **APACS**

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