

# DIRECT DEBIT CONSULTATION OUTCOMES

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May 2017



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\*The annexes are available as a **separate document**.

Direct Debit is our flagship product, used by over 90% of personal current account holders and around 40,000 organisations.



## 1 EXECUTIVE SUMMARY

The Bacs strategy, agreed in 2015, has four pillars; understanding value, enhancing our products, engaging our stakeholders and preserving the integrity of our payment products and services. Direct Debit (DD) is our flagship product, used by over 90% of personal current account holders and around 40,000 organisations. It was therefore natural for it to be the initial focus of our product enhancement activity. Despite Direct Debit's evident success our analysis suggested that there could be opportunities for improvement so that it might better serve the needs of niche markets not able to benefit fully from the advantages Direct Debit offers. Specifically, we wanted to understand how a wider range of organisations could access Direct Debit as a means of accepting payments and how the needs of consumers either unable or unwilling to use the product could be better met. A number of these opportunities aligned with detriments subsequently identified through the work of the Payments Strategy Forum (PSF).

Over the course of 2016, Bacs commissioned a series of targeted research projects designed to gain comprehensive and specific insight into stakeholder views of the Direct Debit product generally, and particularly to understand those niche markets we had identified. Through a mix of market research and direct stakeholder engagement we have found that:

- Direct Debit remains the most popular way for consumers to pay their regular bills
- Less frequent users require greater assurance over exactly when bills will be paid if their concerns over using the product are to be allayed
- The security provided by the Guarantee is important, but we are conscious that levels of understanding could always be higher. Consequently, there is a risk of further confusion if changes are made without adequate, careful and considered communication
- Small and Medium Enterprise (SME) payer usage lags behind that of consumers. Many of the smallest businesses do not see it as a suitable product for them, given concerns over their cash flow and uncertainty on exactly when payments would leave their accounts. Among larger SMEs direct credit is preferred, again for the added control over when payments are made
- SMEs are potentially open to a product with a shorter or restricted guarantee more appropriate to their needs but stressed the continued need for a way to be reimbursed in the event of any errors
- Confidence in the refund process is the most important feature of the Guarantee for consumers. In contrast, during our in-depth interviews the majority of Direct Debit originators and banks who sponsor service users stressed the need to cap the length of the Guarantee. However, they recognised the need to balance the commercial benefits of Direct Debit to their organisations with recognition of pressing consumer needs.

Our public consultation received around 600 responses, around half of which were from individuals. The remaining responses were from a wide mix of stakeholders include user organisations, consumer bodies, SME groups and Payment Service Providers (PSPs). The feedback we received echoed that in our quantitative research, confirming widespread support for Direct Debit as a simple, easy to use and manageable product that meets the needs of consumers and organisations for regular payments. There was also evidence that added flexibility for example around payment dates would be attractive but that some groups were not aware of the capabilities the product already offers in this respect.

## OPPORTUNITIES FOR PRODUCT ENHANCEMENT

We have identified a series of concepts that we will investigate over the course of 2017



**1** Payment Flexibility

**2** Pre-Authorised Direct Debit Collection

**3** New debit collection product with restricted Guarantee

**4** Facilities Management (FM)

**5** Account Verification

**6** Consumer Notification of Lodgement of DDI

## 1 EXECUTIVE SUMMARY

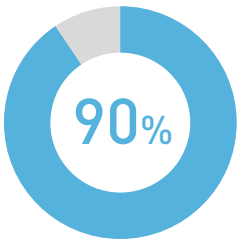
Our research findings reveal that opportunities for product enhancements exist. We have identified a series of concepts to test that we are planning to investigate over the course of 2017. These tests will be in conjunction with stakeholder volunteers from the service user and PSP communities and will be designed to generate data to support business case development. These concepts include:

- 1. Payment Flexibility:** to explore the benefits to collecting organisations and consumers of offering greater flexibility in terms of frequency and date of payment, meeting the needs of those who want more control
- 2. Pre-Authorised Direct Debit Collection:** to test the concept of giving customers greater control of individual Direct Debit collections
- 3. Restricted Guarantee:** a separate new debit collection product with a restricted guarantee that would be more attractive to SMEs and in the business to business payments market
- 4. Facilities Management (FM):** investigating ways to improve SME access to Direct Debit by continuing to work with the FM community to ensure that the market is competitive and open
- 5. Account Verification:** to test methods of account verification to provide improved security and further confidence that the two ends of the payment transaction are who they claim to be
- 6. Consumer Notification of Lodgement of DDI:** to test the impact of PSPs notifying their customers (payers) when a Direct Debit Instruction is lodged on their bank account, ensuring consumers have the information they need when they want it.

Although these concepts suggest scope for further development of the product our research and consultation also indicated that a wholesale change to Direct Debit currently could undermine its great value to the economy through a range of unintended consequences. We have identified a number of significant economic, legal and other implementation issues that will require detailed consideration before a robust business case for change can be presented. The concepts and analysis of them will help us to understand more about these potential unintended consequences.

We recognise that any change we identify must also align with other industry initiatives. To that end we are working with the Payments Strategy Forum (PSF) delivery workstreams looking at end user needs and the New Payments Architecture (NPA). Since Bacs will form part of the New Payment Systems Operator (NPSO) we expect that our work will provide a significant input as the new organisation's work plans are developed.

We want to ensure Direct Debit remains fit-for-purpose and relevant, so we looked at ways the product could be refreshed or improved.



Over 90% of consumers with bank accounts have at least one Direct Debit

## 2 BACKGROUND & CONTEXT

### 2.1 PURPOSE OF THE DIRECT DEBIT REVIEW

Direct Debit (DD) is an essential part of the UK economy. It touches the lives of almost every consumer with a current account and is the most popular way to pay for financial outgoings. It is the preferred way for organisations to collect regular payments. Given its huge importance, and the complex interplay between the multiple stakeholders involved, any potential changes need to be carefully considered. If they are not, the risk of undermining Direct Debit is very real and could result in significant unintended consequences.

Direct Debit is a highly effective product. Over 90% of consumers with bank accounts have at least one Direct Debit and it is the most common payment method across financial commitments among consumers. For consumers, Direct Debit gives peace of mind that their bills will be effortlessly paid on time, with the assurance that the Direct Debit Guarantee in the background allows any payments made in error to be reclaimed. For service users, the product provides certainty of incoming cash. With over 98% of payments collected successfully once submitted, the end-to-end processing costs are considerably less than other payment types.

We want to ensure Direct Debit remains fit-for-purpose and relevant, so we looked at ways the product could be refreshed or improved. Specifically, we have sought to understand how a wider range of businesses could access Direct Debit as a means of accepting payments and how the needs of consumers who are either unable or unwilling to use the product could be met. A number of these opportunities aligned with detriments identified through the work of the Payments Strategy Forum (PSF). These focused on simplicity, flexibility and control over payments and the implications of the unlimited Direct Debit Guarantee.

This broad review of Direct Debit provides us with the evidence base to evaluate potential change. It helps us understand behaviour, finesse possible product enhancement and provide the rigour necessary to justify any subsequent activity. Any proposed changes to the product must be based on genuine insight and statistical substantiation.

To fully understand the current views of Direct Debit, and the impact of any potential changes, we undertook five specific research streams:

1. Quantitative market research amongst consumers: In July we commissioned Ipsos MORI to investigate, through quantitative research, some of the key themes and issues around Direct Debit. This involved 2060 x 7-minute consumer surveys with individuals, undertaken via Ipsos' face-to-face omnibus, Capibus, and weighted to be nationally representative
2. Quantitative market research amongst SMEs: In parallel to our consumer research, we also commissioned Ipsos MORI to establish the view of SMEs. This involved 1000 x 10 minute online surveys with financial decision makers / influences across a range industry sectors and weighted to be representative by number of employees (0-250)
3. Market research amongst business leaders: To supplement the Ipsos MORI research we worked with the Institute of Directors (IoD) to understand their members' use of Direct Debit as a means of collecting payments. Using the IoD's Policy Voice online panel we collected the views of 1,071 business leaders across the full range of businesses

The consultation, which launched on 12 October 2016 and closed on 9 December 2016, elicited around 600 responses.



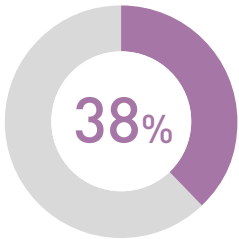
## 2 BACKGROUND & CONTEXT

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4. In-depth qualitative stakeholder interviews: Beginning in June 2016, we conducted two rounds of detailed interviews to establish the thoughts and observations of a representative cross section of stakeholders into Direct Debit. We conducted more than 25 interviews across consumer groups, banks and building societies, members of our affiliates group, charities, SMEs, trade associations, local government, non-ministerial departments and corporate entities. This cast was designed to provide a fully rounded view of Direct Debit
5. Public consultation: Feedback from all the research streams were used to design an online questionnaire (also available in print for those without computer access). The consultation, which launched on 12 October 2016 and closed on 9 December 2016, elicited around 600 responses.

The five research streams we undertook were designed to dovetail together to provide us with a firm evidence base for any future product development and/or promotional activity. The research built a solid body of evidence and identified consistent trends throughout.

Direct Debit remains the most popular way to pay for financial outgoings in the UK with over 90% of bank account holding consumers having at least one Direct Debit.



38% of households have more than six Direct Debit commitments

### 3 QUANTITATIVE MARKET RESEARCH

Direct Debit (DD) has long been established as the preferred payment mechanism among consumers for regular commitments. It enjoys almost universal brand recognition and represents the high water-mark amongst consumers when it comes to awareness and trust compared to similar financial brands. However, as Bacs is committed to ensuring Direct Debit continues to meet the needs of consumers and thousands of businesses alike, we recognised more could be done. This was the reason we launched a public consultation. It helped us understand the business challenges and customer needs of today, and the future. Ultimately, we wanted to establish where Direct Debit works well and where there may be potential to adopt changes to enhance it further.

#### 3.1 DIRECT DEBIT IS THE MOST POPULAR WAY FOR CONSUMERS TO PAY

Direct Debit remains the most popular way to pay for financial outgoings in the UK with over 90% of bank account holding consumers having at least one Direct Debit and Direct Debit being the most common payment method across financial commitments for this group. More than a third (38%) of households are “heavy” users of the Direct Debit service, with more than six Direct Debit commitments. Our research suggests those individuals who use Direct Debit more tend to have additional financial commitments, and as such, are generally more financially secure. This is reflected in both income, as well as stage of life. Many are earning more than the UK average (£27,600 p.a. in April 2016) and bringing up a family.

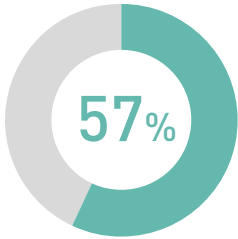
It follows that the more people use the Direct Debit product, the greater their level of understanding of its features and benefits. Indeed, the more regularly you commit to pay via Direct Debit, the more those surveyed value the ease and effortlessness of the service – with 88% of our most frequent users stating “the most important thing when selecting a payment method is that once payment is set up, I don’t need to think about it again”.

We suspect the numbers of frequent Direct Debit users might be larger than the figure projected by Ipsos. This is because people claiming to be non-users of the Direct Debit service were stating forms of payment (such as standing order and debit card); to pay for services like mobile phone bills that conventionally accepts Direct Debit as standard. If this is the case, this might indicate that more work needs to be done to communicate what Direct Debit is and the benefits it offers the consumer over alternative payment types.

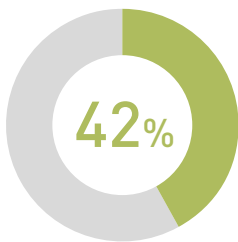
#### 3.2 LESS FREQUENT USERS REQUIRE GREATER REASSURANCE TO ALLAY CONCERNS

While the most frequent users of Direct Debit tended to be older and wealthier, less frequent and non-users were overwhelmingly younger and/or on less stable income streams. They tend to have fewer financial commitments and therefore consider themselves less financially confident. For example, around half said they manually manage bills to control what is in their account, with some were concerned they may not have the money to cover payments. While ease is considered an important factor when deciding whether or not to pay with Direct Debit, this is offset with a worry they cannot commit to having money in their bank account at a set time.

We also learned that the less an individual uses Direct Debit, the less aware they are of its different benefits and features. Moreover, they are more likely to think money can be taken out of their account at any time – or increased at any stage – with no prior notification from the service user. It is this audience who would like to be notified when DDs are set to leave their account. The fact this group does not realise that service users are already compelled to communicate this information to them in advance suggests communication from service users and further promotional activity might be required.



of consumers are either aware of or have heard of the Guarantee



of consumers wanted unlimited Guarantee duration

### 3 QUANTITATIVE MARKET RESEARCH

#### 3.3 AWARENESS OF THE GUARANTEE IS HIGH, BUT UNDERSTANDING IS LOW

More than half of consumers (57%) said they are either aware of or have heard of the Guarantee, with older and more financially secure individuals most likely to be aware of the Guarantee facility. Significantly, 2% of all consumers report to have previously claimed repayments through the Guarantee. However, operational metrics state last year 900,000 claims were processed, less than one in every 4,000 Direct Debit payments collected [less than 0.03% of Direct Debit payments collected], which is a far lower figure than the quantitative research reveals. This demonstrates the confidence the Guarantee provides consumers to reclaim funds directly from the organisation. This number also illustrates the huge success of the Direct Debit logo and supporting Direct Debit Guarantee claim on all Direct Debit Instruction forms and registration web pages. It also shows that concerns about excessive or false claims may have been overstated.

However, the research also suggested that Direct Debit is so ubiquitous people believe they know what the Guarantee is but many are not accurate in their understanding. More than a quarter of consumers do not know how long the Guarantee is valid for, with a third believing it is valid for a year or less. This does not mean to say that consumers are happy with what they believe to be the Guarantee period. When asked for an "ideal guarantee period", 42% want an unlimited duration. Interestingly, the biggest jump in perceived reality vs. expected ideal is amongst current non-users. This suggests the unlimited nature of the Guarantee is a compelling message to motivate non-users to consider adopting the service.

This is also significant because it means confidence in the Guarantee could be more brittle than might be perceived by the headline findings of the research data. Awareness is high but understanding low, which means there is a risk of confusion if the conditions are amended. Any changes must therefore be communicated carefully to consumers to ensure the overall reputation of the service is protected.

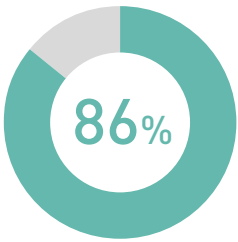
#### 3.4 SMALL AND MEDIUM ENTERPRISE USAGE LAGS BEHIND THAT OF THE GENERAL CONSUMER

While Direct Debit remains a popular payment method amongst SMEs, our research suggests the payment market is more fluid for this audience. Whereas 38% of consumers have six or more financial commitments paid for by Direct Debit, this falls to 3% for SME accounts. Indeed, our research suggests that this small group tends to be dominated by larger sized small businesses: 85% of single business employees and 81% with just one employee are non-business users of Direct Debit. This could reflect a lack of financial stability: non-users were significantly less likely to consider their business "financially strong" (40% for non-users v 74% frequent users) and therefore, like consumer non-users, are more concerned that lack of funds could impact the ability to pay on an arbitrary date.

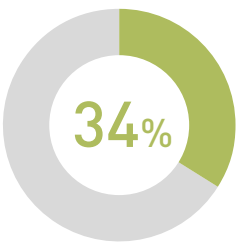
That said, unlike the consumer panel, where payment notifications were more likely to be used amongst less frequent and non-users, it is the more regular Direct Debit business customers that would appreciate this kind of facility. We believe this could reflect the time pressures faced by micro businesses and their lack of dedicated finance teams to manage prompt payments.

The research also suggested to us that we should consider, and then test in the field, various ways to refine the Direct Debit product to suit the needs of this community. This could be critical given that SMEs comprise of 99% of businesses in the UK economy, and around of 50% of private sector turnover [Source: Gov.UK].





of SMEs are either aware of or have heard of the Guarantee



of SMEs wanted unlimited Guarantee duration

### 3 QUANTITATIVE MARKET RESEARCH

#### 3.5 SMES ARE POTENTIALLY OPEN TO A PRODUCT WITH A SHORTER GUARANTEE PERIOD

Awareness of the Guarantee is substantially higher than with this group, compared with the general consumer audience. Some 86% of SMEs report to being aware or having heard of the Direct Debit Guarantee. This is surprising given the low take up of Direct Debit payments amongst this group. However, reiterating the precarious financial position of many of these SMEs, more than 80% of small companies stressed to us their need to be reimbursed for any error generated by the company being paid, although more than three quarters said they would contact their bank in the first instance. The SME community's knowledge of the Guarantee's validity period is also very low, with 63% not aware of what the current guarantee period is and 15% believing it is valid for two years or less.

Interestingly, expectations of an ideal guarantee period are lower amongst the SME community than consumers. Although 34% stated they wanted an "unlimited time period", half of SMEs stated a preference of less than two years. The different wants and needs of the SME community arose as a clear area of focus for us.

Throughout the interviews, stakeholders stressed the huge importance of Direct Debit to the UK and how well the service works for most people.



“DIRECT DEBIT IS A BEAUTIFULLY SIMPLE PRODUCT BUT JUST NEEDS TO EVOLVE SLIGHTLY TO KEEP IT RELEVANT.”

Consumer champion interview



## 4 QUALITATIVE STAKEHOLDER ENGAGEMENT

### 4.1 STAKEHOLDER INTERVIEWS

In the second half of 2016, we conducted two rounds of detailed interviews to establish the thoughts and observations of Direct Debit from a representative cross section of stakeholders. Interviewees included consumer groups, banks, members of our affiliates group, charities, SMEs, trade associations and corporate entities. This cast was specifically designed to provide a rounded view of Direct Debit and reflect the diverse make-up of its stakeholders. Their feedback was then used to design an online public consultation that launched on 12 October and ran until 9 December 2016. This section outlines the findings from the detailed interviews.

Each interview addressed five core areas, with stakeholders free to discuss any other points of note at the end:

1. How they use (or do not use) Direct Debit
2. The sign-up process
3. The Guarantee
4. The processing cycle
5. Issues of control and flexibility.

The interviews proved to be instructive and insightful, and in turn helped shape the structure of the public consultation. The feedback also provided vital context to supplement the quantitative research work stream.

#### 4.1.1 Use and importance of Direct Debit

Throughout the interviews, stakeholders stressed the huge importance of Direct Debit to the UK and how well the service works for most people, most of the time. While the stakeholder interviews provided extremely constructive feedback, they also highlighted areas of concern and others that might benefit from further attention.

#### 4.1.2 Flexibility of the Service

Consumer groups and charities emphasised the enduring importance of Direct Debit and how it helps to guarantee payment, seen as especially important for vulnerable customers such as those who may be prone to forgetting to make critical payments on time. However, interesting questions were also posed about the service's suitability for those on low or variable incomes where cash flow is inherently less stable, therefore sometimes making it difficult to meet an apparently fixed payment schedule. Here, a perceived lack of control was cited as limiting the take-up of Direct Debit. The relationship between control, flexibility and the certainty Direct Debit currently provides is being explored in detail through the entire consultation and research process.

However, even among the stakeholders who raised questions around certain elements of the service, there was a definite view that any potential change need to be thoroughly investigated and cautiously implemented, for fear of unintended negative consequences that might undermine a vital and fundamental payment mechanism. This view is perhaps best illustrated by the following feedback:

“Direct Debit is a success story – it’s an established system that’s trusted and widely used. We need to ensure that it’s maintained and enhanced. Don’t make any changes if they will threaten the good things about it as Direct Debit is a helpful day-to-day tool we all use to manage our lives.”

Regulatory stakeholder interview

“Fundamentally, Direct Debit is a really good service and the link to all the banks is vital. My starting point is that Direct Debit is a beautifully simple product but just needs to evolve slightly to keep it relevant.”

Consumer champion interview

## BUSINESS RESEARCH

Working with the Institute of Directors (IoD) we have identified three groups of users from a survey of over 1,000 businesses.



**1 KEEN USERS**  
See value in Direct Debits simplicity for the end customer and themselves

**2 FUNCTIONAL USERS**  
Use Direct Debit for regular payment options from consumers but prefer direct electronic payments from customers

**3 NON-USERS**  
Do not see Direct Debit as relevant to their business

## 4 QUALITATIVE STAKEHOLDER ENGAGEMENT

“ Direct Debit is really, really important – it’s the opportunity for banks and originators to take money in a controlled way, and a way for their customers to get a benefit – for example reduced fees.”

Challenger bank interview

### 4.1.3 Level of understanding

Interestingly, there was a noticeable disparity in the level of understanding about the service. This was instructive as Direct Debit is used by almost every adult in the UK. Areas of misunderstanding therefore need to be addressed to ensure the service is fulfilling its potential. It also raised an interesting point about bracketing potential changes into product design and operational enhancements vs. promotional and communication priorities.

### 4.1.4 The Guarantee

The Direct Debit Guarantee was the single biggest issue for almost every stakeholder interviewed. The majority of Direct Debit service users and banks who sponsor service users stressed their desire to cap the length of the Guarantee, while consumer groups and charities emphasised the importance of the unlimited Guarantee. However, even those who wanted the Guarantee period reduced also recognised the importance of the feature for consumer protection and to imbue confidence in the service. Corporate entities were especially illuminating as they provided a rounded viewpoint – balancing the commercial benefits of Direct Debit to their organisation with recognition of pressing consumer needs.

Overall, the detailed stakeholder interviews proved vital in shaping the direction of the public consultation. They highlighted why Direct Debit is such an integral part of the UK’s financial system, as well as providing important constructive criticism about areas which could be enhanced and modified. What was made clear throughout is that the success of the service is built on a complex interplay between the needs of multiple stakeholders. Any potential changes therefore need to be cautiously considered before they are implemented. If they are not, the risk of undermining Direct Debit is very real and might penalise the groups requiring the most protection.

## 4.2 BUSINESS RESEARCH

In order to understand the perspective of businesses as payees, using Direct Debit to collect payments from their customers, we worked with the Institute of Directors (IoD). Based on over 1,000 responses from a broad range of business types and sizes we identified three groups:

- Keen users: typically, the larger businesses who see the value in the simplicity of Direct Debit for the end customer and from their own perspective
- Functional users: concentrated amongst medium sized businesses, they tend to use Direct Debit to meet demand for regular payment options from consumers but prefer direct electronic payments from customers
- Non-users: concentrated amongst small businesses where the Direct Debit is not seen as relevant to their business or where it is not seen as an option offered by banks.

For both Keen and Functional Users, the key benefits of using Direct Debit are certainty of payment and low costs. The simplicity of processes were seen as important, contributing to cost efficiency. Interestingly, end-customer benefits and demands were seen as less relevant. For non-users the Direct Debit was not seen to meet their business needs. These non-users’ reasons were often associated with a focus on business to business commerce where Bacs Direct Credits were the preferred means of payment. Some concerns were also evident about the Guarantee and potential misuse in the B2B payment market. Some respondents were attracted to some form of B2B Direct Debit product with a restricted Guarantee which could feature some form of pre-authorisation. Allowing a two-day processing cycle also attracted interest.

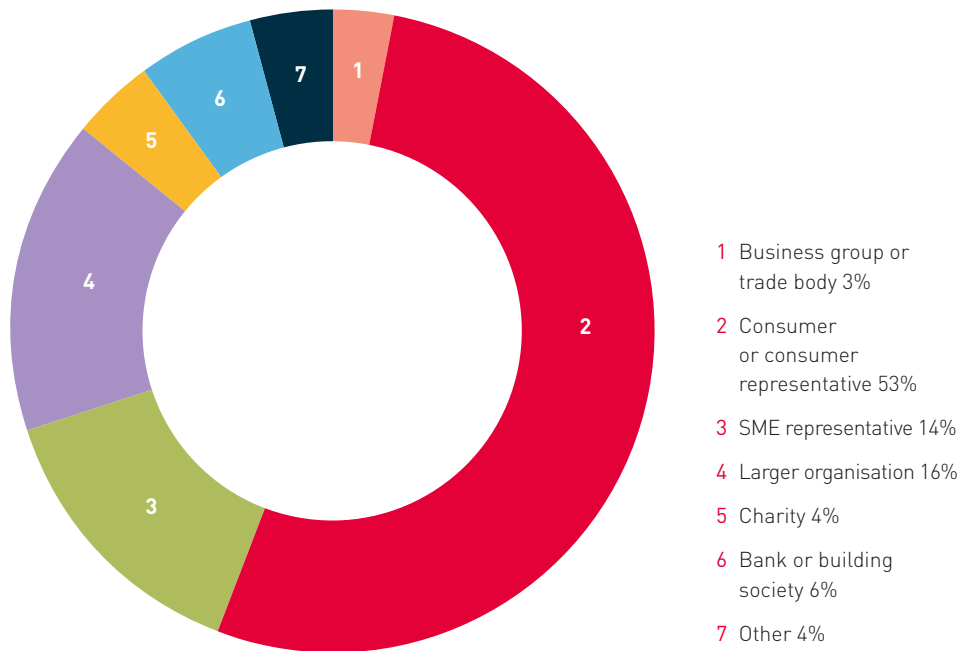
In the public consultation we approached nearly 400 representative groups and asked them to complete a short, tailored questionnaire.



## 5 PUBLIC CONSULTATION

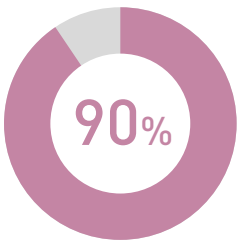
The public consultation was developed and designed to help us understand the business challenges and customer needs of today, and what these groups want in the future. Ostensibly, Direct Debit is a simple product but it taps into many different wants and needs; each audience has slightly different priorities and uses the service in different ways. In the public consultation we approached nearly 400 representative groups and asked them to complete a short, tailored questionnaire. In addition the questionnaire was available for the public to respond. In total around 600 responses were received, just over half from the public. The breakdown of respondents by type is illustrated below.

### BREAKDOWN OF RESPONDENTS BY TYPE



“THE DIRECT DEBIT GUARANTEE DOES MUCH MORE THAN PROTECT CUSTOMERS, IT PROVIDES REASSURANCE.”

Consumer representative



Just under 90% of consumers find the set-up process easy and straightforward

## 5 PUBLIC CONSULTATION

### 5.1 UNDERSTANDING THE NEEDS OF BUSINESSES & CONSUMERS

A large proportion of respondents said they were aware of the Guarantee and what it entails. The public consultation reflected the trend identified by Ipsos MORI where more SME owners are aware of the Guarantee than consumers. This trend was echoed by larger organisations (those with over 250 employees), although interestingly trade bodies lagged behind in their understanding.

We would expect the numbers of respondents that know the Guarantee is an unlimited, lifetime indemnity to be lower than indicated and more in line with that reported by Ipsos MORI. This hypothesis is supported by the length of time payers thought the Guarantee should be valid for. And, although no consumers in the public consultation thought there should be no Guarantee whatsoever, two thirds thought it should be valid for two years or less and only a little over one third thought there should be no time limit. Support for the Guarantee among the business community was even more striking but almost all felt that the Guarantee should not remain limitless.

One consumer representative that we spoke to as part of the in-depth stakeholder interviews was especially passionate about the importance of the unlimited Guarantee:

“ The Guarantee shouldn’t have a time limit. Customers should have as much certainty and security as possible. Making a claim after three years is highly unlikely but it provides the reassurance for consumers that you’re really serious about their protection. To limit the period would fundamentally undermine the product.”

“ A lot of people don’t check their bank details and statements; even savvy consumers like myself aren’t as immersed in the detail as you arguably should be. The Direct Debit Guarantee does much more than protect customers, it provides reassurance.”

Given the potential effects of a substantial indemnity claim made against a business, it is understandable that the payee community is less supportive of an unlimited Guarantee than payers. However, a desire for a more limited Guarantee was noticeable even among SMEs – many of whom would not be recipients of payments via Direct Debit and so unaffected by any indemnity claims. On consideration, we feel that SMEs answers (like those from consumers) are based on current comprehension rather than desire. This is especially the case given that over two thirds of SMEs felt that the Guarantee should be valid for one year or less.

This finding suggests work needs to be done to ensure payers understand what the Guarantee is and how it can protect them.

### 5.2 ESTABLISHING WHERE DIRECT DEBIT IS DOING WELL

Consumers consider Direct Debit easy to set up. The public consultation revealed that just under 80% of them find the process either ‘easy and straightforward’ or ‘easy’. This increases to nearly 90% when you include those who find the process ‘fairly easy’. Only 5% of respondents said it is ‘difficult and complicated’ or ‘difficult’. We suspect the introduction of online and telephone payment authorities have helped to increase consumer satisfaction with the set-up procedure. This was also echoed in the stakeholder interviews:

“ I feel that it’s fairly simple already. You can do it over the phone and online. I can’t really see how else you would do it without compromising security. It all seems very straightforward now and doesn’t really require any further simplification.”

Government

The importance attached to simplicity is a key tenet of modern service provision. Consumers want and expect a frictionless and effortless experience. We know this first hand through the Current Account Switch Service where research conducted by Prescient highlighted that ‘simple’ and ‘stress-free’ were fundamental to imbuing consumers with confidence in the service. Concentrating on Direct Debit’s simplicity will therefore be key to promoting it to less frequent users. Ipsos MORI’s research has also indicated that ease is a powerful motivator for persuading lowest users of Direct Debit’s to consider adopting the service for other payments.

“THE THREE-DAY PROCESSING CYCLE IS NOT AN ISSUE. CUSTOMERS DON'T CARE OR DON'T KNOW.”

Originator – insurance firm



“HAVING THE ABILITY TO MOVE A PAYMENT DATE QUICKLY AND EASILY WOULD BE VERY USEFUL, BUT NOT THE ABILITY TO CHANGE THE PAYMENT AMOUNT.”

Consumer representative



## 5 PUBLIC CONSULTATION

While the overwhelming majority of consumers told us they find the set-up process easy and straightforward, the picture is less clear cut for business stakeholders. Less than half of SME respondents felt that it is either 'easy and straightforward' or 'easy', although only a small minority find it either 'difficult and complicated' or 'difficult'. This could possibly reflect the requirement for certain small businesses and charities to provide two paper signatories prior to any payment approval. This also reflects the findings from the Ipsos MORI research where ease was identified more by heavier users of the service than lower users (24% to 11%). Given this is not an issue which we are able to control directly, we will look to work with service users to identify ways they can advise their own customers how to handle Direct Debit instructions in a more flexible or efficient manner.

We also canvassed opinion over the current three-day processing cycle for Direct Debit and found little demand for changes to the existing arrangement. Tellingly, virtually no respondents said that reducing the processing cycle would prompt them to start using Direct Debit. This was a feature reinforced during the stakeholder interviews:

“The three-day processing cycle is not an issue. Customers don't care or don't know.”

Originator – insurance firm

“I don't see the benefit in shortening the cycle. From a customer perspective it's a same day service – they see the money come out on the date that they chose.”

Challenger Bank

“Maybe you could shave a day off it, but I'm not sure whether a) You can or b) if it would be worth it. Three days is fine really.”

Originator – utility firm

“I think all the customer cares about is knowing when the money is coming out.”

Consumer champion and charity

“Seems to work very well and we have no problems with it. The pause allows any corrections to be made. I've never come across anyone asking for it to be quicker.”

Originator – local government

While there was not an urgent call to increase the speed of the processing cycle, when respondents were presented with the option, almost a third said their organisations would be inclined to use Direct Debit more if it could be reduced to the next day. However, because payment leaves the account on a specified date, processing time should not (and does not) affect the payer.

### 5.3 INVESTIGATING THE IMPORTANCE OF FLEXIBILITY

In the same way views on the sign-up process were clearly split between consumers and business, so were views regarding the flexibility of the Direct Debit product.

We asked respondents to tell us whether they would be more or less likely to use Direct Debit if they could choose when and how payments could be taken. For example, if they could move the date a Direct Debit came out of their account at short notice. This echoed questioning during stakeholder interviews, where we discussed flexibility and control in detail:

“I'm not sure that flexibility matters – we want certainty of cash flow and customers don't want to think about it.”

Originator – insurance firm

“A more flexible process might benefit consumers but perhaps would not be welcomed by originators.”

Trade body

“Paying a set amount each month increasingly doesn't match the ways consumers are managing their money.”

Charity

“PAYING A SET AMOUNT EACH MONTH INCREASINGLY DOESN'T MATCH THE WAYS CONSUMERS ARE MANAGING THEIR MONEY.”

Charity



## 5 PUBLIC CONSULTATION

“ Having the ability to move a payment date quickly and easily would be very useful, but not the ability to change the payment amount.”

Consumer representative

Perhaps unsurprisingly when considering the likely issues faced by a small business, three quarters of SME respondents said they would be more inclined to make DD payments if the product was more flexible. In fact, most respondents who identified as something other than a consumer said a more flexible Direct Debit offer would make them more likely to use it. However, SMEs also incorrectly assumed that this trend would apply to consumers and again most of them assumed consumers would be more likely to use Direct Debit if the model was more flexible.

Larger organisations attached even more sway to the potential impact of increased Direct Debit flexibility, with nearly three quarters of respondents assuming consumer usage would increase. In reality, almost half of consumer respondents said they would be more likely to use a more flexible Direct Debit product. What is more, nearly half of consumers admitted adding such flexibility to Direct Debit would not have any impact – positive or negative – on how much they use Direct Debit.

The small business respondents identified cash flow as a determiner in whether to use Direct Debit or not, and given the results of the consultation, we suspect that a bespoke business product with greater levels of control and/or flexibility would increase uptake and usage.

We have defined a set of product development concepts that could enhance Direct Debit's ability to meet stakeholder needs more effectively.



## 6 CONCEPT DEVELOPMENT

Based on our research findings and earlier analysis we have defined a set of product development concepts that could enhance Direct Debit's ability to meet stakeholder needs more effectively. Bacs will be partnering with organisations to evaluate these concepts, generating real metrics to enable assessment of a range of potential changes. These concepts will then be taken forward in a structured product development plan delivering benefit to all stakeholders.

During Q2 2017, Bacs are working with partners from across the payments industry, including collecting organisations, facilities management organisations and PSPs to scope how best to validate these concepts and establish usable metrics from real-world data.

The concepts that are being validated relate to particular findings from the research. The tests are:

- 1. Payment Flexibility:** This will explore the benefits to collecting organisations and consumers of offering greater flexibility in terms of frequency and date of payment. These are capabilities that already exist within the Direct Debit product and offer benefits to payers and are one of the reasons for individuals deciding not to use Direct Debit for their bill payments
- 2. Pre-Authorised DD Collection:** This test will give customers (payers) control of individual Direct Debit collections by adding an interaction between the collecting organisation and the payer to give permission to make a Direct Debit collection. We will also seek to understand which scenarios of payment, customer combination that this is most suited to, e.g. b2b, or annual cheque payers
- 3. Restricted Guarantee:** Working with collecting organisations, we will define a debit collection product with a restricted guarantee which will enable collecting organisations to collect and demonstrate evidence of collection which will be sufficient to refute a claim on a revised guarantee, while providing clarity to customers about how and in which circumstances they would be eligible to make a claim. The aim will be to understand the extent to which claims which are an abuse of the guarantee could be prevented
- 4. Facilities Management (FM):** We will be continuing to work with the FM community who provide a range of payment services, typically to smaller organisations, providing access to Bacs services. Our focus will be on ensuring that the market is competitive and open and that the Bacs ruleset does not hinder the operation of this market. In addition, we are keen to encourage this market as it provides a promising way for smaller organisations to access Direct Debit
- 5. Account Verification:** We will be working work with selected collecting organisations to test methods of account verification so as to provide greater certainty that the two ends of the payment transaction are who they claim to be. This is a key area of focus for the Payments Strategy Forum. It will help us assess different methods for achieving this recognising that there are already tools available in the market. Working with these collecting organisations, we will then be able to determine how such approaches can contribute to the management of the claim process either within the Direct Debit product or as part of a Restricted Guarantee product
- 6. Consumer Notification of Lodgement of DDI:** Working with PSPs we will be testing the impact of banks notifying their customers (payers) when a Direct Debit Instruction is lodged on their bank account.



We have seen strong positive support for the Direct Debit product, with its highly efficient 'exception' only processing and the added value supporting services, from businesses, government and non-business organisations.



## 6 CONCEPT DEVELOPMENT

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We will approach the testing of these concepts in a variety of ways, with some being field trials to assess consumer behaviour, while others will be 'desk-based' analysis where it would be impractical to create the required test environment for a practical field trial. We expect to collect the outputs from the testing of these concepts during H2 2017 and to feed proposals for future product development into the NPSO design and planning process.

In addition, we are actively engaged with the Payments Strategy Forum's (PSF's) work addressing consumer needs and the potential New Payments Architecture (NPA). We believe that there is significant potential for elements of the Direct Debit product and supporting processes to contribute to the Request to Pay concept. We have seen strong positive support for the Direct Debit product, with its highly efficient 'exception' only processing and the added value supporting services, from businesses, government and non-business organisations. They use it to meet the needs of around 90% current account customers who value it as a simple and reliable way to ensure household bills get paid. It is critical that their needs continue to be met effectively. We are working to ensure that these needs are reflected in the development of the NPA and future infrastructure supply arrangements. The PSF is continuing its work during 2017 prior to handing it over to the new Payment System Operator when it becomes operational. We will continue to develop our concepts in parallel with the PSF workstreams in the second half of 2017.

At this stage, the analysis has considered a broad range of possible outcomes.



## 7 IMPLEMENTATION CONSIDERATIONS

Alongside the wide-ranging market research and consultation Bacs has developed an economic model to assess potential changes to the Direct Debit product. The model has been created using a structured technique called Value Management. This is a proven approach that starts from the perspective of a stakeholder, e.g. consumer, billing organisation, bureau or bank. It analyses the benefits and costs associated with potential change. The model allows us to explore the links between changes and business outcomes and to identify the key sensitivities that have greatest impact on outcomes. We have used this tool to perform a balanced, high level assessment of the economic merits of potential change for each stakeholder group. At this stage, the analysis has considered a broad range of possible outcomes but does not represent a fully developed business case for change at this stage.

Through this analysis Bacs identified and quantified over three hundred elements that could contribute to benefits across the stakeholder groups. The analysis has highlighted the key sensitivities underpinning the economic model. These are:

1. DD transaction volume, either as growth or retention of transactions due to the continued attractiveness of DD to both payers and billing organisations
2. The number of billing organisations offering Direct Debit as a payment method to their customers, particularly thinking of increasing SME access to the Direct Debit product
3. The impact on the number of claims under the Direct Debit Guarantee.

Our concept testing work will be used to explore these sensitivities and generate further inputs to allow robust quantification of benefits as part of a structured business case.

In 2016, 4.2 billion Direct Debit payments were made. There are some 20,000 organisations who submit Direct Debit payment requests directly with a similar number using the product via bureaux and other services. The product is supported by a full suite of supporting processes that allow effective straight through process of payments, maintenance of instructions, and other services such as redirection of payments when customers switch their accounts as part of the Current Account Switch Service. Most of the user organisations have invested heavily in internal processing and infrastructure to exploit these services, leading to a highly cost effective customer management and payments infrastructure. Any changes to the core product must be considered against that backdrop.

We have sought legal advice on potential changes to the Guarantee and indemnity. Our initial understanding is that implementing any change to existing contracts between customers and suppliers using Direct Debit would not be practicable, and that any attempt to phase in a new contract with a more limited guarantee would be open to challenge. Migration to a new Direct Debit contract through natural turnover would also likely be a long and protracted process since Direct Debit instructions are in place on average for around seven years. That approach would be open to customer confusion and necessitate more complex customer facing processes for both the organisation using Direct Debit to collect payments, their sponsoring bank and their consumers' banks.

The consultation process confirmed the central role that Direct Debit plays in the economic life of the UK.



## 8 SUMMARY

The consultation process confirmed the central role that Direct Debit plays in the economic life of the UK. It is seen by consumers as the preferred way to pay regular commitments and by organisations as the most cost effective product to collect payments. However, some SMEs do not consider it a relevant payment mechanism and are often not able to achieve the benefits they might from it. For some organisations fears about the unlimited nature of the Guarantee may restrict its use and while consumers value this feature of the Direct Debit they do not necessarily fully comprehend it.

A major aspect of the market consultation was whether the unlimited nature of the Direct Debit Guarantee should be changed and whether this constituted a barrier to entry for SMEs. Through our research, we found the following:

- Imposing a time restriction on the Direct Debit Guarantee would involve a significant transfer of value from consumers to organisations using Direct Debit as a collection mechanism, and to their sponsor banks
- Significant stakeholder and legal challenges would arise if such a change was attempted
- Although some SMEs do not see Direct Debit as an appropriate product for them opportunities do exist for extending its reach into this market
- Those opportunities could best be addressed through new product development rather than by restricting the Guarantee period
- In the meantime changes to the indemnity claim process are addressing concerns from some service users and banks over potential misuse of the Guarantee.

As a result of these conclusions, Bacs has identified no substantive case for restricting the Direct Debit Guarantee period at this time. It would be appropriate to review this position following implementation of product changes and new product developments which we believe will on balance address the requirements of the market protecting both payers and collecting organisations.

Any development of the Direct Debit product also needs to be seen in the context of wider industry change. Specifically, following from the PSF's strategy we are actively engaged in the development of the Request to Pay product that has the potential to meet the needs of consumers for whom Direct Debit is not ideal while reusing underlying components and processes that are used to deliver the Direct Debit. Similarly, we are working to ensure that the needs of the extensive business, government and other organisation Direct Debit user base are reflected in developments such as the NPA and future infrastructure supply arrangements.

### ANNEXES

- **Annex 1 – quantitative market research**  
The ipsos mori 70 page slide deck which covers both consumer and sme surveys.
- **Annex 2 – qualitative market research**
- **Annex 3 – public consultation**

The annexes are available as a **separate document**.

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