THE FUTURE OF CASH

Protecting access to payments in the digital age

PositiveMoney

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Author: David Clarke

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EXECUTIVE SUMMARY

The ability to make payments is fundamental to any individual's participation in the economy. We believe that people should be able to use their money in the way they choose, and that fair and low-cost access to payments should be recognised as a universal need, like water or electricity.

Cash is still relied upon by 2.7 million people, including many who are on low incomes who may not have bank accounts and access to contactless debit cards, the elderly, or those struggling with ill health. Some find it useful for budgeting, while others are responding to a banking system that is failing to serve their interests. If we lose our access to cash, millions will struggle to manage their money and pay for the things they need.

The UK is on the verge of losing thousands of ATMs, as banks' determination to cut costs, spurred on by competition from VISA and Mastercard, is set to make many parts of our cash network unprofitable. Most ATMs operate via the Link network and are funded by transaction fees paid by banks and building societies. Link has recently confirmed plans to lower those fees, meaning that many ATMs may no longer be viable.

Action by the regulator is the only thing standing in the way of the decline of the UK's ATM network, but it's unclear that it will take the necessary steps to intervene. Government should assign the Payment Systems Regulator the explicit job of protecting people's access to cash and new enhanced powers to stop closures.

As is already the case in countries like Sweden, shops and restaurants will increasingly refuse to accept cash, putting products and services out of reach for potentially millions of people. Positive Money believes that Government should update the legal definition of legal tender, to require retailers to accept cash as a means of payment.

Conversely, if people want to store their money and make payments electronically, they should have the opportunity to do so without facing hidden costs or unnecessary risk. The Government should work with the Bank of England to introduce a digital version of cash, and set up a public payments provider with the specific job of reaching those who are currently excluded.

SUMMARY OF RECOMMENDATIONS

Protecting access to cash

- The Treasury Select Committee should consider whether the '1km rule' - determining the allocation of a financial inclusion subsidy for ATMs - remains fit for purpose. Alternative models could involve applying the increased fee to the remaining two or three machines in a 1km radius, or reducing the radius to 500m.
- Ensuring access to cash should be made a statutory duty of the Payment Systems Regulator. The PSR should clearly set out minimum expectations for what level of ATM access the public can expect, and engage proactively with Link and its competitors to ensure that this is upheld.
- The Payments Systems Regulator should ensure a level playing field between Link and other ATM schemes.
- The Department for Work and Pensions must investigate whether Universal Credit claimants have indeed faced difficulty because of their payments preferences. If so the DWP must move to reintroduce the option of receiving payments in cash.
- The Government should introduce legislation clarifying the definition of legal tender, to ensure that retailers accept payments in cash.

Expanding access to electronic payments

- Certain fintech firms are expanding access to electronic payments to groups which have so far been excluded. Regulators must remove unnecessary barriers to their growth.
- Government must work with the Bank of England to support and accelerate the introduction of a central bank digital currency.
- This should be combined with the establishment of a publicly owned payments platform.

INTRODUCTION

Technology is transforming the way we make payments. Just ten years ago, 22 million transactions were made in cash each day, and the use of cards a fraction of that[1]*. In ten years time, that number is expected to drop below twelve million. There are a myriad of different payment methods, with contactless cards, mobile payments and online shopping gaining popularity.*

The move towards digital payments has seismic implications. Over the coming decades, our economy will undergo a transformation, during which the banking system, the retail sector and our relationship with money will be irrevocably changed. Behind the move to digital payments lie powerful forces. Payments companies like VISA have spent millions on advertising in an effort to coax customers to switch to products like contactless cards[2].

The increasing popularity and convenience of digital payments is undeniable. But the future of cash is complex and uncertain. The total value of cash in circulation is actually rising. 2.7 million people in the UK rely on cash[3], and it's likely that a significant number of people will continue to use cash for decades into the future[4].

At this point of technological transformation, we must ask ourselves a crucial question. How can we ensure that the payments system serves our interests? We know that despite the wide availability of alternative forms of payments, millions of people prefer to use cash every day, for a variety of reasons. If cash becomes less accessible, and is less widely accepted, what disadvantage will these groups experience?

This paper explores three questions:

- What do we know about how the use of cash is likely to evolve?
- Who are the people who currently rely on, or have a preference for cash, and how will they be affected by the move to digital payments?
- How can we ensure that those people's interests are protected, and what is the role of policy, industry and innovation in doing so?

Positive Money comes from the starting point that of course there are opportunities created by technological innovation, but that the disappearance of cash is not inevitable, and that electronic payments are not inherently more desirable.

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[1] UK Finance (2017). UK Payments Markets Summary. https://www.paymentsuk.org.uk/file/2529/download?token=7ZkWTfjG

[2] See section 1.2

[3] UK Finance (August 2017). UK Cash & Cash Machines 2017 Summary. https://www.ukfinance.org.uk/wp-content/uploads/2017/08/Summary-UK-CASH-AND-CASH-MACHINES-3.pdf

[4] Ibid.

We use the term “financial health”, inspired by the work of Toynbee Hall and the Finance Innovation Lab. Financial health puts people first and asks: how can financial services be designed to work with a person’s life circumstances, wants and needs, rather than trying to fit the person into the existing financial system?

The ability to make payments is fundamental to any individual’s participation in the economy. It’s a utility to which everyone should be guaranteed easy access, and not face discrimination due to their payments preferences.

Universal access to payments

The ability to make payments is fundamental to any individual’s participation in the economy. People should be able to use their money in the way they choose, and that fair and low-cost access to payments should be regarded as a fundamental need, like water or electricity.

- People should not face unreasonable costs or discrimination due to their payments preferences
- Certain forms of payments should not be inaccessible due to income, geography, health or mobility
- People should have access to a risk-free form of money to make payments and manage their savings

PART 1:

THE OUTLOOK FOR CASH

To understand how the move to digital payments will affect different groups within the economy, it is first important to understand how cash use is likely to evolve. Predictions of "the death of cash" or of the whole economy "going cashless" are premature. Cash remains a crucial part of our payments system, and will do for decades into the future.

1.1: Current cash use

Cash still plays a hugely important role in the economy. It remains the most frequently-used payment method and in 2016 accounted for 44% of all payments made by consumers[5]. Cash payments continue to dominate key retail sectors, like newsagents, convenience stores, travel and pubs.

As well as being used as a payment method, cash remains popular as a way of storing wealth. The amount of cash in circulation is at record levels, and the Bank of England estimates that the total value of all notes and coins has now reached £80bn. The demand for cash grew sharply after the financial crisis, and again after the EU referendum.

ATM withdrawals, the main method of accessing cash, show the aggregate value of withdrawals have also stayed relatively stable with an average of £192 billion being withdrawn each year over the past decade. Consumers tend to visit ATMs less frequently, but to withdraw larger amounts. Although there was a slight drop in the number of adults using ATMs last year, the number has risen by 10 million in the last decade[6].

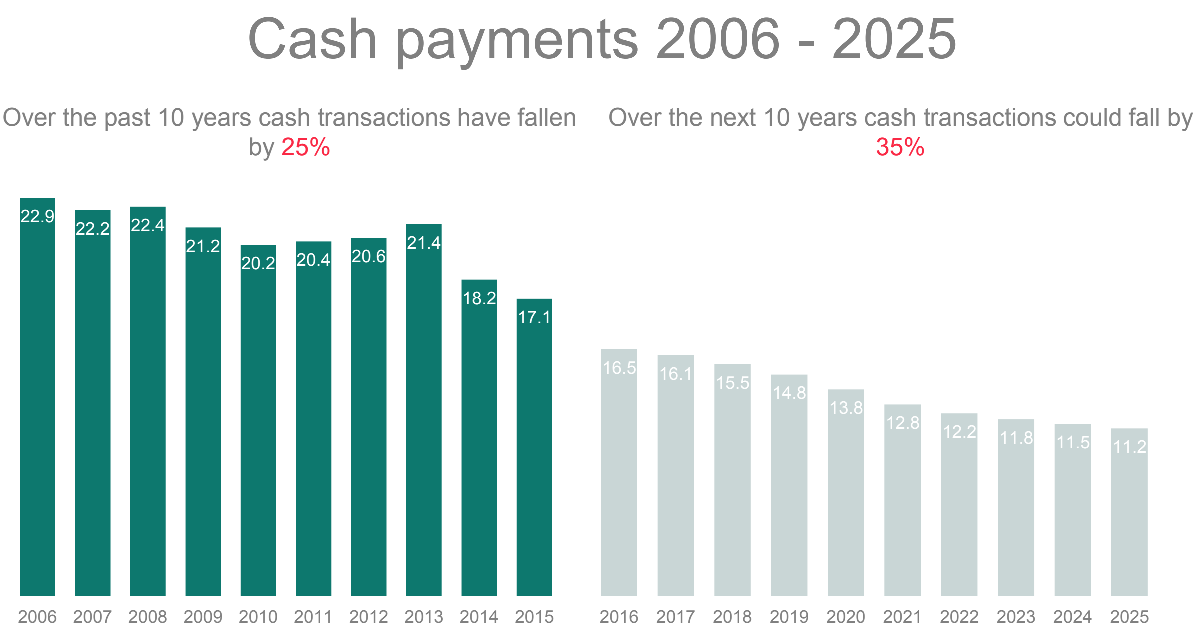
[5] UK Finance (August 2017). UK Cash & Cash Machines 2017 Summary. https://www.ukfinance.org.uk/wp-content/uploads/2017/08/Summary-UK-CASH-AND-CASH-MACHINES-3.pdf

[6] Ibid.

Over recent years, there have been signs that some consumers are increasingly reliant on cash to help them budget, and to manage low or irregular incomes. In 2016, 2.7 million people were reliant almost entirely on cash, up from 2.3 million the year before[7]. The makeup of this group is analysed in section 2.

1.2: The decline of cash

While in many ways cash still dominates, its long-term decline is undeniable. Consumers and businesses are spending cash less frequently, and the value of their spending is falling overall. Cash payment volumes have declined by a third in the past decade. The number of cash payments in the UK declined by 11 percentage points between 2015 and 2016. And the total value of consumer cash payments was £240 billion in 2016, a decline of five percent compared to the previous year. If current trends continue, we can expect the proportion of payments made in cash in the UK to drop to 26% by 2026.



UK Payments Markets 2016, UK Finance[8]

A significant section - six percent - of consumers now use cash only rarely. Young people, having come of age in the era of card payments, are more likely to be rare cash users than older generations. Businesses use cash far less extensively than consumers, with cash making up less than four percent of the volume of business payments.

[7] Ibid.

[8] UK Finance (2016). UK Payments Market 2016: https://www.paymentsuk.org.uk/sites/default/files/publication-free/UK%20Payment%20Markets%20Summary%202016%20-%20Free%20Download.pdf

The sharp decline in the volume of payments made in cash has been driven by the increasing popularity of alternatives, particularly the adoption of debit cards and contactless payments. This trend is likely to continue, as contactless payments are ever-more widely accepted. Contactless payments more than trebled in 2016 to £26bn. The popularity of online shopping, which grew at a rate of 19.5% in 2017, is a further driver[9].

For now, the uptake of mobile payments such as Apple and Android Pay has been relatively slow, with customers citing security concerns as reasons why they opt against using them regularly[10]. But as consumer behaviour continues to evolve, and mobile payment firms spend billions on advertising, it's likely that these innovations will continue to drive the move away from cash. New apps such as Monzo, that can monitor and even restrict spending for budgeting purposes, are also contributing factors.

There are powerful interests driving the move towards electronic payments. Visa, which boasts an annual media marketing budget of more than £5m, is running a "cash is awkward" campaign in an apparent effort to stigmatise cash use[11]. In the US, the company announced a programme to award small and medium–sized businesses up to $10k if they completely abandon cash in favour of credit and debit payments and suggested last year that a similar scheme could be implemented in the UK[12].

The decline in cash use is also driven by public policy. For example, the decision by Transport for London to allow contactless card payments across its network, and to stop accepting cash payments on buses, was followed by a significant uptick in card usage, not just in London but across the UK. In 2016, eighteen months after the announcement that contactless payments would be accepted on most TfL services, £25 billion was spent using contactless cards, more than double the spending in the previous eight years combined. Between January and June 2017 £23 billion was spent using contactless, nearly double the total for 2016. According to UK Finance there could be 11 billion contactless transactions by 2026, a four-fold increase on 2016[13].

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[9] Victoria Cleland, Chief Cashier and Director of Notes, Bank of England (13 June 2017). Insights into the future of cash - Speech given at ATM & Cash Innovation Europe, London. https://www.bankofengland.co.uk/-/media/boe/files/speech/2017/insights-into-the-future-of-cash.pdf?la=en&hash=F13A0D0BDADDF3F981DDC2A1B81C01E42BEF806D

[10] James Titcomb, Daily Telegraph (14 April 2017) Mobile Payment struggle to make impact on contactless card use. https://www.telegraph.co.uk/technology/2017/04/14/mobile-payments-struggle-make-impact-contactless-card-use/

[11] Matt Oliver, Daily Mail (14 July 2017). Credit card giant Visa plans to pay Britain's shops and restaurants to ditch coins and notes.
http://www.dailymail.co.uk/news/article-4694894/Credit-card-giant-Visa-wants-shops-ditch-cash.html

[12] Katie Morley, Daily Telegraph (13 July 2017). Visa declares war on cash with plan to pay British businesses to ban coins and notes.
http://www.telegraph.co.uk/news/2017/07/13/exclusive-visa-declares-war-cash-plan-pay-british-businesss

[13] David Fagleman, Head of Policy and Research at Cash Services (16 October 2017). Is cashless transit leading the payments revolution?
https://www.Linkedin.com/pulse/cashless-transit-leading-payments-revolution-david-fagleman/

Public policy is also encouraging the move away from cash through changes to the welfare system. Unlike existing benefits, Universal Credit claimants will only be able to receive payments via an account with a bank, building society or suitable alternative. The government has justified this by arguing that use of a bank account is “a key enabler to preparing people for the world of work and enabling them to budget effectively”[14].

Many school canteens have stopped accepting cash, requiring parents to transfer money onto a contactless card. This arrangement is thought to improve the speed of service, enable parents to keep track of what their child is eating and remove the stigma associated with free school meals.

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[14] Department of Work and Pensions (6 April 2016). Response to Freedom of Information request: Post Office Card Accounts for Universal Credit Digital Service.
https://www.whatdotheyknow.com/request/320876/response/792522/attach/html/2/FoI%20904%20reply.pdf.html

PART 2:

HOW WILL DIFFERENT GROUPS BE AFFECTED?

The vast majority of people use cash regularly, and millions of people rely on cash almost entirely. This group includes people of different ages and backgrounds, but there are some distinct patterns.

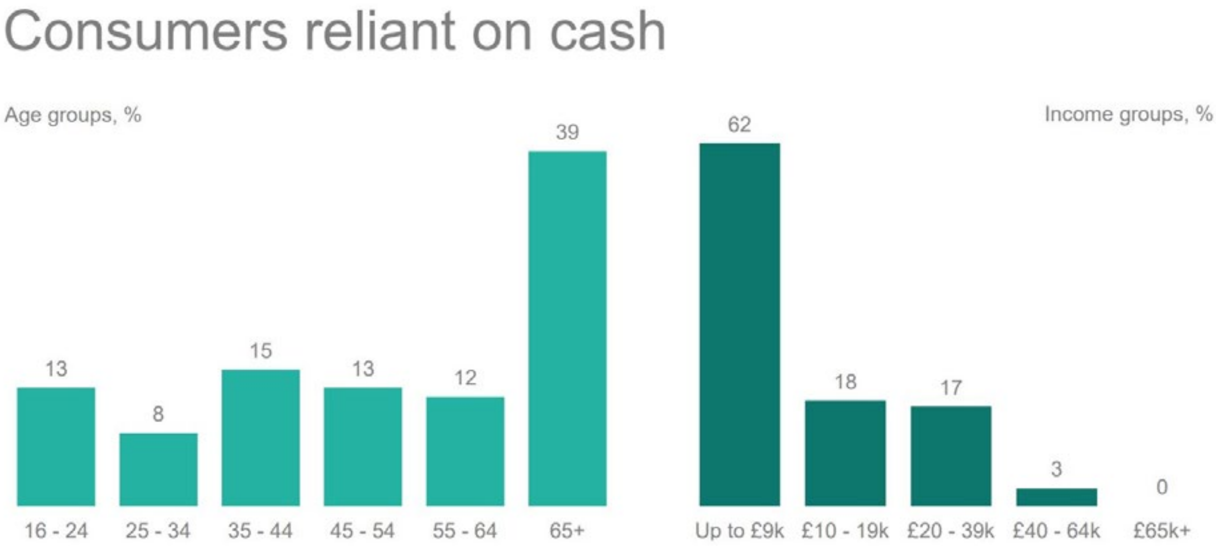
Forty seven million people, amounting to 89% of the UK's adult population, use a mixture of payment options. Only 5% of the adult population are rare cash users, while around 2.7 million people rely on cash for almost all of their day-to-day spending[15].

2.1: People on low incomes are more likely to rely on cash

Of the 2.7 million consumers who relied predominantly on cash during 2016, over half had household incomes of less than £15k per year. In 2015, 40% of consumers who rely on cash had a total household income of less than £10,000.

[15] UK Finance (August 2017). UK Cash & Cash Machines 2017 Summary. https://www.ukfinance.org.uk/wp-content/uploads/2017/08/Summary-UK-CASH-AND-CASH-MACHINES-3.pdf

Many of the people who rely on cash are 'unbanked', meaning that they have absolutely no access to a bank account. Toynbee Hall estimated that over one million of the people who use cash for their day to day payments are unbanked. And a 2015 survey of unbanked people carried out by Toynbee Hall found that 95 per cent earned £17,500 and below, with just three percent earning between £17,501 and £25,700, the UK's median household disposable income.



UK Payments Markets 2016, UK Finance[16]

2.2: Many people prefer to use cash, even when they have access to electronic payments

An agreement exists between the main banks to provide basic bank accounts to unbanked customers who are ineligible for a full-service account. This means that, in theory, all UK households should have access to a bank account should they choose to use it. Following the introduction of basic bank accounts in 2004, the number of adults living in unbanked households fell by over 50% and now represents less than 2% of the population.

But despite the availability of basic accounts, millions of people choose to be unbanked, and millions more use cash for almost all of their day-to-day payments. In fact, a significant majority of the people who only use cash also have a bank account. Around half of people with basic bank accounts choose to manage their money in cash[17].

Of those who are unbanked, the Financial Inclusion Taskforce found that only about half of people without a bank account actually wanted one[18]. A survey conducted by

[16] UK Finance (2016). UK Payments Market 2016: https://www.paymentsuk.org.uk/sites/default/files/publication-free/UK%20Payment%20Markets%20Summary%202016%20-%20Free%20Download.pdf

[17] Financial Inclusion Commission (March 2015). Improving the Financial Health of the Nation. http://www.financialinclusioncommission.org.uk/pdfs/fic_report_2015.pdf

[18] Financial Inclusion Taskforce (2010). Banking Services and Poorer Households, London: Financial Inclusion Taskforce. http://webarchive.nationalarchives.gov.uk/+/http:/www.hm-treasury.gov.uk/d/fit_access_to_banking.pdf

Toynbee Hall found that people had a variety of different reasons for not having an account. Many cited previous negative experiences with banks, while a large number reported that they lacked the correct identification to open an account, or were ineligible for other reasons.

Three quarters of the people Toynbee Hall interviewed had previously been a customer of a bank, and a significant proportion expressed a "preference" for being unbanked. The reasons given included people's fear of having an account, and their own behaviour with an account, with many citing an association with overdrafts and debt. Others found banks to be alien, too complicated or untrustworthy. This correlates with polling showing that a majority of UK adults don't trust banks to work in their customers' best interests[19].

Public distrust of banks grew considerably in the years after the financial crisis. The Financial Services Compensation Scheme means that customers will be fully compensated in the event that bank or building society is unable to repay deposits up to £85,000. But nevertheless, banks' involvement in risky lending activities and financial speculation is ever-present in the news. It's not widely known that unlike physical cash, bank deposits are technically the property of the bank.

For those not among the unbanked who still rely on cash for their day-to-day payments, it is often because they find cash to be a useful method of budgeting and managing low or irregular incomes. Using cash gives customers a greater sense of control over their money: it's obvious how much you have, and it's much more difficult to accidentally spend more than you intend to.

2.3 The impact of 'frictionless' electronic payments on financial health

A feature of most electronic payments is that they are more "frictionless" than cash. This means that the experience of paying takes less time and involves fewer conscious steps. With the advent of card payments and online shopping, it's possible to make purchases in seconds, at any time of the day. Payments firms and retailers are constantly pushing for new ways create a more seamless transaction experience[20], based on the evidence that with each fraction of a second that passes during the course of customers making a payment, the chance that they'll reconsider rises considerably.

The "frictionless" experience of electronic payments creates problems for people who worry about their own ability to make responsible decisions, or about others who have access to their money. A study of more than 5,000 people signed up to

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[19] Jake Palenicek, UK Head of Custom Research, YouGov (19 May 2017). Most Brits trust banks but don't think they work in customers' interests.
https://yougov.co.uk/news/2017/05/19/most-brits-trust-banks-dont-think-they-work-custom/

[20] Barclays (September 2016). Frictionless Payments.
https://www.barclayscorporate.com/content/dam/corppublic/corporate/Documents/tech_digital_innovation/frictionless-payments.pdf

the Money and Mental Health Policy Institute found that 93 percent of those self-describing as having mental health issues said they spent more when they were unwell[21]. Respondents to the survey also reported self-excluding from certain forms of payments because of mental health problems[22].

2.4: What does the move to electronic payments mean for those who rely on cash?

A lack of access to electronic payments is a key driver of the Poverty Premium, where people in poverty pay more for the same goods and services. Save the Children calculated that this amounted to nearly £1,700 for low income families. For example, a preference for cash may lead people to use a pre-payment meter for their energy, and a result, pay a higher rate per unit than customers on a direct debit. A typical annual household fuel bill could be around 21% more expensive, according to Save the Children's research[23].

Another example of potential increased costs is a reliance on pay-as-you-go mobile phones. Of the UK's main mobile networks, only Three accepts cash payments for pay-monthly contracts via banks' giro service, although this is £5 a month more expensive than paying via direct debit. Neither O2, Vodafone nor EE accept cash payments. Even for people who rarely use their phones PAYG costs £43.08 more a year than the top SIM only deals.

As ticket offices continue to close, advance-purchase train tickets are becoming increasingly inaccessible to people without access to electronic payments. Although many stations have ticket machines that accept cash, these usually offer only walk-up fares. Booking tickets in advance can be up to 80% cheaper[24].

Although some broadband providers accept cash, including Virgin Media and Talk Talk, only the Post Office does so without applying an additional charge[25]. Otherwise, paying with cash can cost up to £115 more per annum, and is impossible with many providers.

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[21] Rose Acton, Money and Mental Health Policy Institute. (March 2017). How fintech can help people with mental health problems.
http://www.moneyandmentalhealth.org/wp-content/uploads/2017/03/FCA-Briefing-paper-MMHPI.pdf

[22] Polly Mackenzie and Katie Evans, Money and Mental Health Policy Institute (14 September 2016). Submission to the Financial Exclusion Committee.
http://www.moneyandmentalhealth.org/wp-content/uploads/2016/09/LordsFinancialExclusionCommitteeresponseMMHPI.docx.pdf

[23] Priya Kothari, Graham Whitham and Thomas Quinn, Save the Children (2014): A fair start for every child https://www.savethechildren.org.uk/content/dam/global/reports/advocacy/a-fair-start-for-every-child.pdf

[24] Raileasy (August 2016). Book in advance & save money.
http://www.raileasy.co.uk/making-a-booking/book-in-advance-and-save-money

[25] Duncan Heaney, Broadband Choices (30 May 2017). Broadband without direct debit.
https://www.broadbandchoices.co.uk/guides/broadband/broadband-without-direct-debit

Paying in cash also stops consumers building a credit history, which they would otherwise be doing by making payments via direct debit. This prevents them taking advantage of certain credit facilities in the future, for example when they want to take out a car loan or apply for a mortgage.

2.5: Inaccessible products and services

A small number of shops and restaurants currently refuse to accept cash. When they do so, it has been unusual enough to be reported in the press[26]. But as consumer behaviour continues to evolve, this number is likely to increase. We spoke to business owners who have opted to refuse cash. They cited security concerns as the main reason for their decision. They also explained that with a majority of customers using card payments, the staff time involved with delivering cash to the bank was no longer economical. As cash payments decline as a proportion of transactions overall, and retail space continues to become more expensive in many UK towns and cities, we can expect more businesses to follow suit.

The outlook for cash

- Cash use is still strong, but is declining and will continue to do so
- However 2.7 million people rely on cash, many of them on low incomes
- Many people have a preference for cash, even when they have access to electronic payments
- Other groups have particular reasons to rely on cash, such as those with mental health conditions
- For those who rely on cash, the move to electronic payments could mean higher relative costs, particularly on subscription services like broadband and mobile phones
- Some products and services may not be accessible at all, as retailers begin to refuse cash payments

[26] Lucy Bannerman, The Times (24 April 2017). Rise of cafés where cash is off the menu. https://www.thetimes.co.uk/article/rise-of-cafes-where-cash-is-off-the-menu-w75007skj

PART 3:

SECURING UNIVERSAL ACCESS TO PAYMENTS

It is clear that the move to electronic payments poses risks for people who currently have a preference for cash. They are likely to face higher costs, while some products and services may be inaccessible to them. People have a legitimate desire to want to use cash for budgeting or health reasons, and instead of trying to change people's payment behaviour, policymakers should recognise their existing preferences and ensure that their interests are protected. There are two aspects to this. The first is ensuring people's ability to use cash where they want to, and the second expanding access to electronic payments.

PROTECTING ACCESS TO CASH

For the 2.7 million people who rely on cash, it is crucial that they are able to access it without facing undue costs or inconvenience.

3.1: Most people access cash via the Link ATM network

Cash is most often accessed via ATMs. They are the preferred method for the majority of consumers, regardless of income[27]. In 2016, customers withdrew £194bn from ATMs versus around £20bn using other methods. The ongoing closure of bank branches is increasing the proportion of cash accessed via ATMs still further. In ensuring that people continue to be able to access cash, ATMs are a key factor.

Currently, the UK has around 70,000 ATMs. Of those, 78% are free-to-use, while 22% charge a fee[28]. Ninety-eight percent of cash withdrawals are made at ATMs which are free to use. Almost every ATM is connected to the Link network, which is made up of banks, building societies and ATM operators. Most ATM transactions are between Link members.

3.2: Current ATM coverage

A minority of people currently experience difficulties accessing cash via an ATM. This can impact adversely on their lives and financial circumstances. Research by Toynbee Hall found that certain groups face "significant issues" getting access to the cash they need, and that those difficulties are most acute among those from low-income households in rural areas and on satellite housing estates[29].

Access to cash is determined largely by location. People in affluent and urban areas usually live within walking distance of an ATM. Difficulty is more often faced by those living on out-of-town housing estates or in isolated rural areas[30]. Sixteen percent of the general population in England and Wales live further than 1km of a free-to-use to access ATM.

This means that a small but significant section of the population is poorly served by ATMs, and that some people suffer detriment, for example those with care requirements, limited mobility, or face other issues which limit their ability to travel. People in these circumstances are also often on the lowest incomes, often reliant on benefits, and are often careful cash budgeters so require greater than average access to cash. Toynbee Hall identified a large number of areas where many benefit-dependent people live more than 1km from an ATM[31].

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[27] Toynbee Hall (2016). Response to Payments Strategy Forum User Needs Consultation. https://consultation.paymentsforum.uk/sites/default/files/documents/Toynbee%20Hall%20Webready.pdf

[28] The UK's ATM network - Financial Conduct Authority: Payment Systems Regulator (March 2018). https://www.psr.org.uk/psr-focus/the-UK-ATM-network

[29] Ibid.

[30] Ibid.

[31] Toynbee Hall (accessed 2018) Is there Low income Consumer Detriment from Gaps in Free-to-Use ATM Provision? https://www.link.co.uk/media/1184/toynbee_hall_executive_summary.pdf

The Link network has taken steps to address these barriers. It says that its Financial Inclusion Programme has delivered cash access to over 1,700 communities by subsidising machines which may otherwise be unsustainable. It recently announced that it plans to triple the maximum subsidy for such ATMs[32].

3.3: The threat to free-to-use ATMs

Although the number of ATMs has remained steady, there is a risk that their numbers will decline considerably in the coming years. Currently, the UK has around 70,000 ATMs, and over 97% of withdrawals are from free to use machines[33]. The cost of free-to-use ATMs is covered by an 'interchange fee' being charged to the card issuer by the ATM operator, each time a transaction is made. The total cost of the UK's free to use ATM network is around £1bn, and transactions between Link members, account for £750m of this total. Link has confirmed plans to reduce the fee from around 25p to 20p over four years, which has prompted reports that the move will result in a significant reduction of free-to-use ATMs in the UK. The ATM industry association, which represents independent ATM operators, projects that this could lead to the closure of up to 10,000 machines[34].

Link CEO John Howells says that the organisation is "committed to maintaining an extensive network of free-to-use cash machines. Free access to cash is vital for UK consumers and Link intends to maintain this for many years to come." The network has also announced that any free-to-use ATM that is more than 1km from the next nearest one will receive an increased subsidy of up to 30p on each transaction, three times the current maximum rate.

Link is governed by an independent board, although given that the majority of its members are banks, and funding for the scheme comes from banks and building societies, questions have been raised about whether the organisation is truly independent[35]. In reality, John Howell's commitment to protect financial inclusion is only good for as long as Link's members continue to support it. Link has recently completed a consultation on the future of free-to-use ATM provision, but elected not to make the responses public. It acknowledged that certain large banks in its network have been pushing for a larger and faster reduction in the interchange fee. If certain banks are pushing for this, the public has a right to know. We agree with the former Treasury Select Committee chair Lord McFall, who argued in his own submission that the consultation responses should be published on Link's website[36].

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[32] Link Interchange Consultation Announcement (31 January 2018). https://www.link.co.uk/media/1355/h-documents-uploads-Link-interchange-consultation-announcement-31-january-2018.pdf

[33] Link (2018). Charges at ATMs: https://www.link.co.uk/consumers/charges/

[34] Jill Treanor, The Guardian (1 November 2017). Plan to shut free-to-use cash machines could lead to 'ATM deserts' in UK: https://www.theguardian.com/money/2017/nov/01/free-to-use-link-cash-machines-atm-deserts-uk

[35] Treasury Committee (January 2018). Oral evidence: Work of the Payment Systems Regulator, HC 711. http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/treasury-committee/work-of-the-payment-systems-regulator/oral/77521.pdf

[36] New City Agenda (4 December 2017) Lord McFall: Proposals for free cash machine network are a leap in the dark https://newcityagenda.co.uk/cashmachines/

The availability of free-to-use ATMs is also threatened by the ongoing closure of bank branches. Monitoring RBS branch closures in Nottinghamshire, the campaign group Move Your Money found that of 51 RBS closures announced in the first part of 2016, only 10 were leaving behind an ATM[37]. The UK has lost 53% of its bank branches since 1989, leaving 1,500 communities with no bank, and another 840 with only one bank remaining. More than 600 branch closures have occurred in the last year alone, and UBS has predicted that the UK is set to lose another 50% of its total branch network in the next ten years.

3.4: Link must be held to its commitment to ensure widespread coverage

Link accepts that there will be a decline in the number of ATMs, as machines become less profitable. CEO John Howells says "it will eventually become too expensive for cash machines to operate in some parts of the UK, but as long as there is still one person in a village that still uses cash, we need to make sure they still have access." Starting in 2018, the network is trialling free in-store cash services at tens of thousands of newsagents. But it is clear that these offer an inferior alternative to ATMs, as cash would only be accessible during the opening hours of the shop, and dependent on the shop staying in business. The priority must be to ensure that ATMs stay open.

Even if the increased interchange fee on the last ATMs in a 1km radius were successful in protecting isolated machines, this could mean that town centres will be left with just one ATM. Such ATMs would likely face significant demand, and may therefore be more likely to run out of cash, or face other technical issues due to heavy use. One kilometre is still a long way to travel for people with limited mobility, or for those in areas with difficult terrain or poor transport infrastructure.

Since Link's existing financial inclusion arrangements were developed in partnership with the Treasury Select Committee, the committee should take the lead on considering whether the 1km rule remains fit for purpose. Alternative models could involve applying the increased fee to the remaining two or three machines in a 1km radius, or reducing the radius to 500m. Either option would not be inconsistent with the justification that Link uses for reducing the standard interchange fee, which is that the intention is to reduce the density of ATMs in areas which are already well-served.

Recommendation:

The Treasury Select Committee should consider whether the '1km rule' determining the allocation of a financial inclusion subsidy - remains fit for purpose. Alternative models could involve applying the increased fee to the remaining two or three machines in a 1km radius, or reducing the radius to 500m.

[37] Fionn Travers-Smith, Move Your Money (July 2016). Abandoned Communities: The Crisis of UK Bank Branch Closures and their Impact on Local Economies.
https://gallery.mailchimp.com/c9b157c9d89ca0bdb156c5128/files/Abandoned_Communities_V2.1.pdf

3.5: The role of VISA and Mastercard

Link run one of three ATM schemes in the UK. These are shared arrangements developed by banks, building societies and ATM operators to ensure that every customer is able to use their card at almost any ATM. The other schemes are operated by Visa and Mastercard. ATM operators can belong to multiple schemes, but card issuers such as Lloyds, Barclays and RBS can only belong to one. Link accounts for the vast majority of ATM transactions, and the Visa and Mastercard schemes only a very small proportion.

Just like Link, the Visa and Mastercard schemes charge an interchange fee to the card issuer every time a customer uses an ATM. Link's interchange fee is set at a rate that is supposed to reflect the true cost of a transaction. But it has been reported to the Payment Systems Regulator that Visa and Mastercard have been setting their service fee at a level below the true cost, in an apparent effort to attract card issuers to switch from Link[38]. Alternative schemes are reportedly offering interchange rates 30% below those of Link[39].

This is significant because if Link members choose to leave and join these alternative schemes, the service fee may not be enough to compensate the ATM operator for the true cost of the transaction, leading ATMs to become unprofitable. The commercial viability of some ATM operators may be put at risk.

Link's interchange arrangements incorporate an effective subsidy for ATMs in remote locations, paid for by banks and building societies. The network has clearly-defined financial inclusion and social policy objectives[40]. But the Payment Systems Regulator has acknowledged that there is no explicit mechanism that would help to ensure that widespread access to free-to-use ATMs continues to be delivered through competing schemes[41]. It warns that setting financial inclusion and social policy objectives is principally a matter for the Government. Link is the subject of close scrutiny by the regulator because it is the dominant player in the provision of ATMs, but VISA and Mastercard are able to set low fees knowing that they have no responsibility for ensuring that isolated locations continue to be served.

Link cited the competition of alternative schemes as a reason for its recent changes to the interchange arrangements. So even if no card issuers choose to make the switch, VISA and Mastercard's low fees have already had the effect of reducing the amount of revenue received by ATM operators, with many ATMs likely to close as a result.

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[38] Correspondence to the Treasury Select Committee from the Managing Director of the Payment Systems Regulator, relating to the Link Scheme (20 February 2017). https://www.parliament.uk/documents/commons-committees/treasury/Correspondence/Letter-from-Managing%20Director-Payment-Systems-Regulator-Link-Scheme-20-02-17.pdf

[39] Link Interchange Consultation Announcement (31 January 2018). https://www.Link.co.uk/media/1355/h-documents-uploads-Link-interchange-consultation-announcement-31-january-2018.pdf

[40] Introduction to the Link Scheme (2018). https://www.link.co.uk/media/1374/introduction_to_link.pdf

[41] As 25

These developments must be viewed in the context of Visa and Mastercard's efforts to discourage cash use. With Mastercard's merger with VocaLink last year, the company already provides Link's processing technology. As leading providers of electronic payments, there is a clear conflict of interest if they are also able to control this essential part of our cash infrastructure.

3.6: Effective regulation

As ATMs are increasingly operated by independent companies, and banks therefore receive very little income from interchange fees, Link members have a clear incentive to see the fee reduced. With VISA and Mastercard offering a lower-cost alternative, the Link board is faced with the ongoing threat of banks taking their business elsewhere.

Once Link has completed its reduction in the interchange fee by 20% over the next four years, it seems likely that its members will push for further cuts, given their incentive to discourage cash withdrawals, and the ongoing competition from alternative schemes. There may also be pressure to reconsider Link's financial inclusion arrangements.

The only thing that stands in the way of widespread ATM closures is whether there is a regulator with the necessary powers, mandate and will to intervene. Link is regulated by the Payment Systems Regulator, which has the goal of ensuring that payment systems are operated in a way that promotes the interests of the consumers that use them. Currently the PSR appears to be taking a reactive approach towards Link's changes, promising to "monitor the situation" until such a time as "service user needs are threatened". But it is not clear at what point the PSR would deem Link's changes unacceptable.

Although the PSR has promised to intervene if it believes the current broad geographical spread of free-to-use ATMs is threatened, it is unclear where this sits within its statutory objectives. It has no specific responsibility for financial inclusion, or access to cash, and in fact told the Treasury Select Committee that setting financial inclusion and social policy objectives is principally a matter for the Government. The PSR was set up as an economic regulator, not to uphold consumer protection. Its responsibility for ensuring cash access should be made an explicit objective.

The regulator should clearly set out its minimum expectations for what level of ATM access the public can expect, and engage proactively with Link to ensure that this is upheld. If the PSR deems this beyond its scope, then the Government should step in to implement a robust regulatory strategy that upholds consumers' right to access cash.

Link is one of several 'designated' payments systems. Once a system is designated, the PSR has a range of powers over its participants. Both Mastercard and Visa Europe are also designated for regulation by the PSR, and this includes in any activities facilitating ATM services. But while the PSR takes an active interest in the interchange arrangements of Link, committing itself to intervening if it feels service users' needs are threatened, it is not obvious that it intends to do the same for Link's rivals. In fact, PSR CEO Hannah Nixon seemed to welcome reports that VISA and Mastercard have set their interchange fees at lower levels than Link, on the basis that "it could prompt Link and its members to consider whether they are offering value for money for members." It is unsustainable for the regulator to take such divergent approaches towards these different ATM schemes. We propose that instead, the regulator should apply the same requirements for both Link and its rivals.

Recommendations:

Ensuring access to cash should be made a statutory duty of the Payment Systems Regulator. The PSR should clearly set out minimum expectations for what level of ATM access the public can expect, and engage proactively with Link and its competitors to ensure that this is upheld.

The Payments Systems Regulator should ensure a level playing field between Link and other ATM schemes.

3.7: Changes in welfare payments

The introduction of Universal Credit began in 2017, replacing state benefits such as Job Seekers Allowance, tax credits and housing benefit. Unlike existing payments, such as tax credits, Universal Credit can only be received as a transfer to an account with a bank, building society or a 'suitable alternative'[42].

Tax credit and child benefit claimants who have not provided account details were previously receive payment via a cash cheque, which could be redeemed at Post Office. With Universal Credit, this is no longer an option. Universal Credit also sees a shift to an online system for managing claims. The DWP is also phasing out the option of claimants receiving payments via a Post Office card account, which provided the option of withdrawing cash over a post office counter, paypoint outlets, as well as via Bank of Ireland ATMs.

The DWP sees the use of a transactional bank account as "a key enabler to preparing people for the world of work and enabling them to budget effectively"[43]. But, as has been documented in numerous studies, many people prefer to budget

[42] Money Advice Service (2018). https://www.moneyadviceservice.org.uk/en/articles/choosing-a-bank-account-for-your-universal-credit-payment

[43] Department of Work and Pensions (6 April 2016). Response to Freedom of Information request: Post Office Card Accounts for Universal Credit Digital Service. https://www.whatdotheyknow.com/request/320876/response/792522/attach/html/2/FoI%20904%20reply.pdf.html

in cash, even if the option of a bank account is available to them[44]. There is nothing wrong with government seeking to expand access to bank accounts and economic payments. But these changes to welfare payments are forcing people to adopt behaviour that may actually undermine their ability to manage their money effectively.

The National Housing Federation commissioned a survey of social housing tenants receiving housing benefit. Of those interviewed, 40% did not have internet access[45]. Even half of those with access felt that they would not be confident applying for benefits online. While this survey was specifically concerned with tenants accessing benefits online, the results suggest that many claimants may have difficulty accessing electronic payments, without the option of receiving Universal Credit in cash. Given the evidence that many people, particularly on low incomes, have a preference for managing their money in cash, the Department for Work and Pensions must investigate whether Universal Credit claimants have indeed faced difficulty. If so the DWP must move to reintroduce the option of receiving payments in cash.

The government has also been trialling GovCoin, a blockchain solution to welfare payments, which allows claimants to receive payments via a mobile app, and to create virtual "jam jars" into which they apportion money for different expenditure, such as housing, food or travel. The app's creator argues that this technology could give claimants faster access to their money than relying on the banking system. Under the model being trailed, DWP does not have access to customers' payments data, but a former member of the Government's Digital Service warned the BBC that the platform offers "a potentially efficient way for DWP to restrict, audit and control exactly what each benefits payment is actually spent on"[46]. There are also fears that the design of blockchain involves putting highly-sensitive personal data on a shared ledger, which can never be altered or deleted. It is unclear whether the DWP plans to move beyond small-scale trials.

Recommendation:

The Department for Work and Pensions must investigate whether Universal Credit claimants have indeed faced difficulty because of their payment preferences. If so the DWP must move to reintroduce the option of receiving payments in cash.

[44] Ibid.

[45] National Housing Federation (December 2014).Submission: Financial Inclusion Commission. http://www.financialinclusioncommission.org.uk/uploads/written/National_Housing_Federation_-_response_to_UKFIC.pdf

[46] Rory Cellan-Jones, BBC News Technology correspondent (14 July 2016). Blockchain and benefits - a dangerous mix? http://www.bbc.co.uk/news/technology-36785872

ENSURING OUR ABILITY TO PAY IN CASH

3.8: Retailers and cash

Although a small number of shops and restaurants currently refuse to accept cash, this number is likely to increase as consumer behaviour continues to evolve. We spoke to business owners who cited security concerns as the main reason for their decision. They also explained that with a majority of customers using card payments, the staff time involved with delivering cash to the bank was no longer economical. As cash payments decline as a proportion of transactions overall, we can expect more businesses to follow suit. Such moves will cause obvious difficulty to those who rely on cash.

No requirement currently exists for retailers to accept cash. Although the concept of legal tender is commonly understood to dictate what form of payments retailers must accept, in reality its definition applies only to the repayment of debts[47]. Despite this, there is precedent for regulation determining retailers' payment arrangements, with the recent move to ban credit and debit card charges[48].

Massachusetts has a law stipulating that retailers should not "discriminate against a cash buyer by requiring the use of credit by a buyer in order to purchase such goods and services," and that "all such retail establishments must accept legal tender when offered as payment by the buyer." Canadian law requires that retailers should evaluate the impact of rejecting certain forms of payments.

There is no reason why such a law could not extend to online retailers. There are options available to online retailers wishing to offer customers the option of paying in cash. Many of the most popular e-commerce websites already provide this option. Amazon operates its own service called Amazon Top Up, which lets customers deposit cash into their Amazon account by scanning a barcode at retailers with a PayPoint facility. These can be found in at many supermarkets, newsagents and petrol stations.

Other retailers accept cash via PayPoint's PayCash service. This allows customers to order items from an online retail website and go through checkout. After checkout, they print out a voucher to pay for the order via a PayPoint outlet. Although apps such as Uber and Deliveroo do not currently accept cash, they should investigate whether these innovations can be integrated into their service.

Recommendation:

The Government should introduce legislation clarifying the definition of legal tender, to ensure that retailers accept payments in cash.

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[47] Bank of England (2018). What is legal tender? http://edu.bankofengland.co.uk/knowledgebank/what-is-legal-tender/

[48] HM Treasury and John Glen MP (13 January 2018). Card surcharge ban means no more nasty surprises for shoppers. https://www.gov.uk/government/news/card-surcharge-ban-means-no-more-nasty-surprises-for-shoppers

EXPANDING ACCESS TO ELECTRONIC PAYMENTS

3.9: The role of fintech

Several studies have sought the views of people who currently rely on cash, to identify what an ideal current account would look like. As researchers at the University of Bristol found, the conclusions are remarkably consistent. People want their account to have the following facilities:

- Deposits;
- Withdrawal cash at ATMs and also at local Post Offices and PayPoint outlets;
- A payment card for purchases and use at ATMs;
- A small buffer zone to permit balances of under £10 to be accessed at an ATM;
- An ability to check exactly how much is in the account at will, and mobile phone text alerts when the balance is getting low or a when major payment is due and there are insufficient funds to meet it;
- An automated payment facility that puts more control in the hands of the account holder than direct debits.

Some of these facilities are already being offered by firms like Pockit and Monzo. But the evolution of payments in the UK has been limited by regulation. In particular, anti-laundering regulations have placed more onerous requirements on payment service providers in terms of what forms of identification they can accept when signing up customers. Regulators must ensure that measures to prevent fraud and criminality do not come at the expense of including vulnerable and currently-excluded groups.

Recommendation:

Certain fintech firms are expanding access to electronic payments to groups which have so far been excluded. Regulators must remove unnecessary barriers to their growth.

3.10: Cryptocurrencies won't do much to enhance financial inclusion, for now

In recent years, there has been a proliferation of cryptocurrencies, which offer the opportunity to store money and make payments digitally, without the need for a bank account. Cryptocurrencies are a form of digital currency which use cryptographic technology to secure transactions, and are usually denominated in a currency not backed by a central bank. The most famous cryptocurrency is Bitcoin, which has gained notoriety for sharp fluctuations in its value. Over the last several years, many fintech companies have touted the idea that Bitcoin can help expand financial access by allowing people to bypass the costs and delays associated with traditional financial intermediaries.

But these claims should be treated with some scepticism. Looking at the reasons why people choose to manage their money in physical cash, Bitcoin addresses few of them. Bitcoin relies on internet access and a significant degree of digital capability, meaning that it is not a solution for the digitally excluded. Its price has fluctuated wildly in value, meaning that is likely to be rejected by those who are concerned by the riskiness of the traditional banking sector. It offers no added advantage to those who prefer the "physicality" of cash. Although the option of making electronic payments without a bank account is attractive for some, there is no reason to believe that cryptocurrencies would be preferable to other non-bank payments firms which denominate payments in a sovereign currency.

In fact, there is concern that many of the people who have bought cryptocurrencies like Bitcoin are exposing themselves to considerable risk. As well as seeing sharp price rises, Bitcoin has also seen its value plummet. Because it is unregulated, consumers have no guarantee that they will avoid being left with nothing if the price collapses. Ultimately, Bitcoin is unlikely to function as a widespread means of payment because of its high volatility, the limited scope for it to scale, and the energy intensity involved in its operation.

3.11: The case for digital cash

The disappearance of cash is not inevitable, and Positive Money believes that moves to hasten its demise should be resisted. Government should commit itself to protect access to cash, and ensure our ability to make payments in cash. Giving households the opportunity to save and pay in risk-free central bank money is one of the most important responsibilities of our public financial institutions. But as well as honouring this responsibility by protecting cash, Government and the Bank of England must also consider the need to adapt to changes in technology and payments preferences.

The decline of cash and move towards electronic payments has led to growing calls for central banks to give people access to risk-free central bank money in a digital form. This can be done through the introduction of a central bank digital currency, or "digital cash". This would retain many of the characteristics of physical cash; a widely-accepted means of payment and store of value, which is available to everyone and can be used at any time of day. And just like physical cash, it could be stored and used without relying on a high street bank[49].

Giving people the ability to make electronic payments without reliance on traditional financial intermediaries could open up new opportunities to people who currently rely on cash, or who are poorly served by the current market. As set out in section 2, a key reason why many people rely on cash is that they are dissatisfied with the

[49] See Dyson (2016) Digital Cash: http://positivemoney.org/publications/digital-cash/

service offered by high street banks. For most people, making digital payments, such as via contactless card, mobile wallet or online transaction, can only be done using a bank account at one of a small number of institutions, given that Barclays, HSBC, Lloyds, RBS and Santander UK account for 80 percent of the UK retail banking market. As Toynbee Hall's research showed, some people associate banks with overdrafts and debt and find banks to be alien, too complicated or untrustworthy. Polling has shown that a majority of UK adults don't trust banks to work in their customers' best interests.

A crucial difference between physical cash and the electronic money held in bank accounts is that technically, the latter is legally the property of a bank, and exists as an promise that the bank will deliver on at the point where a customer wants to withdraw cash or make a payment. The Bank of England confirmed this in a 2014 paper 'Money Creation in the Modern Economy'. With the vast majority of our money existing as bank deposits, the payments system is increasingly in the hands of a small number of risk-taking institutions. The fact that a major bank defaulting could mean millions of people losing access to their money is a key reason why large financial institutions are regarded as "too big to fail". The government guarantees deposits up to £85,000 through the Financial Services Compensation Scheme, but has previously judged that it is preferable to bailout institutions with taxpayer funds than to let them fail and compensate depositors.

The Bank of England already issues a digital currency, in the form of deposits held by commercial banks in accounts at the Bank of England. But this facility is not accessible to the public, and these deposits circulate separately from the money that the public can use. The Bank can provide digital currency simply by making these accounts available to non-bank companies and individuals.

Although the idea is already being researched by the Bank of England, the Governor has expressed reservations about its introduction, and recently said that given the risks associated with offering central bank accounts for all, "a true, widely available reliable central bank digital currency does not appear to be a near-term prospect." But the benefits of digital cash may not be fully recognised by a central bank whose job it is to pursue a narrow focus on monetary and financial stability. Government must also take the lead.

Recommendation:

Government must work with the Bank of England to support and accelerate the introduction of a central bank digital currency.

3.12: Establishing a publicly owned payments system

The introduction of a central bank digital currency would, in principle, mean universal access to risk-free savings and payments. For the millions of people who feel poorly-served by the existing banking sector, this would present an attractive opportunity. But in practice, its success depends on whether digital cash accounts would have different characteristics, and support facilities that are not offered by existing bank accounts. Positive Money believes that digital cash could help to reduce the entry barriers on the payment market and stimulate innovation. But we cannot rely entirely on the private sector to meet people's payment preferences. Fair and universal access to digital payments can only be safeguarded through the introduction of a publicly owned provider of digital cash accounts.

Positive Money proposes that digital cash accounts would be opened up via an "indirect access" approach, whereby the Bank of England would create and hold the currency, but the payments and customer services would be operated separately. Operating digital cash accounts would be a considerable administrative burden for the central bank, and could distract from its other responsibilities of regulating the financial sector and managing monetary policy. This is a function that is best performed independently of the Bank of England.

The providers of digital cash accounts would have responsibility for providing payment services, debit cards, account information, internet and mobile banking, and customer support. Any funds paid into the digital currency account would be electronically held in full at the Bank of England, so that each provider could repay all its customers the full balance of their account at all times. They would also be responsible for allowing account holders to make payments via the normal payment networks, such as BACS, FasterPayments, Visa and Mastercard. This would enable people to spend digital cash in the same way that they can spend bank deposits. But the digital currency account provider would be prohibited from lending or taking any risk with their customers' funds.

Digital currency accounts could be provided by private firms such as technology startups, established mobile phone companies and/or existing banks. Payment services are ultimately a technology service. They require a database that stores the balance of customer accounts, a protocol for allowing payments to be validated, and a network that allows different payment systems, payment terminals and banks to communicate with each other. In Positive Money's 2016 paper on Digital Cash, Ben Dyson argued that it seems obvious that tech firms – whether 'Shoreditch startups' or firms like Google or Apple – would want to enter this space and launch innovative payment services that could compete with the incumbent banks[50]. Unlike traditional banks, which combine the distinct services of providing payments with savings and loans, non-bank payment providers would be focused simply on providing payments, and therefore could be expected to provide a better service to consumers.

Furthermore, because digital cash account providers would never put their customers' funds at risk, they would require much less intensive regulation. For example, there would be no need for digital cash account providers to be subject to Basel capital requirements, because they would hold no risk-bearing assets. This would make it easier to allow new entrants from the technology industry to provide some competition to the incumbent banks, and would ensure that there would be incentives for these firms to innovate.

[50] Dyson (2016) Digital Cash http://positivemoney.org/publications/digital-cash/

But while innovation could go some way towards meeting the preferences of certain groups who currently rely on cash, the market cannot be relied upon to provide universal access to digital cash accounts in a way which meets the needs of every single group. As we have seen, many of those who rely on cash are on low incomes, older people, or those experiencing ill health. The reasons why these people have not been well-served by the traditional banking sector may also apply to the private firms providing digital cash accounts. In order to provide universal, risk-free savings and payments to everyone, including these groups of consumers and companies, the public sector must step in.

We propose the establishment of a public company with the job of providing universally accessible digital cash accounts, and a specific remit to develop payment services to serve those whose preferences are currently unmet.

Positive Money

303 Davina House
137-149 Goswell Road
London
EC1V 7ET

Tel: +44 (0)207 253 3235

info@positivemoney.org

www.positivemoney.org

Positive Money is a not-for-profit company limited by guarantee, registered in England and Wales.

Company number 07253015