



Innovation in Payment Services: The Role of EU Policies

The Hague, 18 January 2018

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Objectives of this presentation

Present the broader picture:

- **Policy objectives for payments**
- **The role of the EU in shaping payment services**

Focus on the 2nd Payment Services Directive

- **The ambition and how it is to be achieved**
- **What could go wrong**

Discuss the shape of things to come and the role of the EU

I. Policy objectives in relation to payments

- *Payments are an important sector of the economy*
90 000 jobs in France alone, producing services worth € 6-7bn
- *But payment services are not what people want to consume...* They are facilitators for the rest of the economy
- *Payments should be*
 - **Cheap** (thus keeping prices of goods and services low)
 - **Secure** (low fraud risks)
 - **Convenient** (which includes widest possible acceptance)
 - **Accessible** (means of payment should be accessible to any individual, but also to businesses)

Policy objectives: conflicting or complementary?

- *Security vs convenience?*
 - A question of technology
- *Low costs vs everything else?*
 - **Fraud increases the costs of various payment methods**
 - **But indirect costs not well taken into account: inconvenience, lack of trust in payment systems and online shopping**
 - **Digital innovation can lower the cost of security, convenience and accessibility**
- *Well-designed payment systems promote synergies among these objectives*

Who is responsible for delivering efficient payment systems?

- *What can markets achieve on their own?*
- *How much, and which, infrastructure should public authorities provide?*
- *How much regulation and supervision of market operators, including FinTechs, is required?*
- *Which public policy interventions at which level (national vs. EU)?* The subsidiarity question
 - **EU-level action required to allow payment services providers to operate across borders...**
 - **... and to avoid fragmentation: Single Market and free movement require payment services that work EU-wide**

II. EU regulatory interventions on payments

- *Three types of regulations directly addressed to payments:*
 - **Legislation to lower costs**
 - **Legislation to enhance accessibility**
 - **Legislation to support innovation**
- *But payments are also indirectly affected by EU legislation:*
 - **Anti-money laundering rules**
 - **Data protection rules**

Costs

- *Single Euro Payments Area (SEPA) significantly reduces costs for cross-border transactions in euro*
- *Interchange fee regulation (2015/751/EU) tackles competition issues in card payments market*
 - **Deals with incentives for issuing banks and card schemes to apply high interchange fees to the detriment of retailers and consumers**
 - **Caps fees for debit and credit card transactions**
 - **Prohibits surcharges for the use of such cards**
- *Still to be tackled under the new Action Plan on Consumer Financial services (March 2017)*
 - **Charges for non-euro cross-border transactions**
 - **Bad practices in dynamic currency conversion**

Single Euro Payments Area

- *Regulation 924/2009/EU: same charges for domestic and cross-border transactions in euro*
- *SEPA Regulation 260/2012: sets deadline for migration to SEPA credit and direct debit*
- *Vision: a single account should be sufficient for the entire SEPA area*
- *Mission almost accomplished*
 - **Payment services providers comply**
 - **But major payees** (tax authorities, utilities) **may still refuse direct debits from another country ('IBAN discrimination')**
- *National SEPA committees changing into Payments Councils/Committees tackling new challenges*

Cheaper non-euro transactions

- *Regulation 924/2009/EU allows non-euro countries to opt in, but only Sweden did so until now*
 - **Commission to propose to extend the scope of Regulation 924 to all Member States**
 - **Study in progress on costs and pricing of cross-border transactions involving non-euro currencies**
- *Dynamic Currency Conversion (pay in your home currency) to be investigated*
 - **Criticised by consumer organisations**
 - **But could lead to more competition on the currency conversion market**
 - **Commission to look at ways of increasing transparency and boosting competition**

Accessibility

- *Payment accounts Directive (2014/92/EU): Right to a basic bank account* allowing cash withdrawals, credit transfers, direct debits within the European Union
- *European Accessibility Act: proposal from the Commission* (COM/2015/0615, December 2015)
 - **Broad scope...**
 - **but specific requirements for banking services, including online and mobile banking and ATMs**
 - **Still under discussion in Council**
- New issue on the payments agenda - ERPB group
- What role for FinTechs?

Regulation with side-effects...

- *Anti-money laundering directive (2015/849/EU) - to be amended shortly*
 - **requires identification of customers**
 - **strengthens Financial Intelligence Units:** centralised registers linking accounts to persons
 - **will cover virtual currencies**
 - **Action Plan on Consumer Financial Services aims to facilitate electronic identification based on eIDAS**
- *General Data Protection Regulation (2016/679/EU)*
 - **Stricter rules to protect personal data, but also principle of data portability** relevant for AIS in particular
 - **Heavy fines in case of non-compliance.** Banks worried about liability in case of transmission of data to TPPs

Innovation

- *FinTech has been around for some time, particularly in the area of payments...*
- *First e-money directive adopted in September 2000 (revised by directive 2009/11/EC)*
- *Payment services directive followed in 2007, updated in 2015 to take account of new services (PIS, AIS)*
- *These directives*
 - **recognise new payment service providers and facilitate their access to the market**
 - **allow them to be licensed for EU-wide operation ('passporting')**

The Second Payment Services Directive

- *Adopted in 2015, applies from 13 January 2018*
- *Extends scope*
 - **“One-leg” transactions (involving a third country)**
 - **New service providers using existing bank accounts**
- *Better consumer protection*
 - **Ban on surcharges for card payments**
 - **Reduced maximum loss in case of fraud** (from €150 to €50)
 - **15-day deadline for responses to complaints and out-of-court redress**
 - **Strong customer authentication**
- *Important role for EBA: standards, guidelines, central register of payment institutions*

Key issues tackled in delegated act

- *Regulatory Technical Standard on two key issues:*
 - **Strong customer authentication (SCA)**
 - **Common and secure communication standards (CSC)**
- *Drafted by the European Banking Authority after extensive consultations*
- *Highly controversial – extensive lobbying*
 - **Retailers worried about loosing customers due to SCA**
 - **Banks and FinTechs arguing over access to bank account data**
- *Commission adopted final RTS on 27 November; EP and Council may reject it within 3 or 6 months*
- *Applies 18 months after publication in the OJ*

Strong Customer Authentication

- *High level of protection by using at least two independent elements from the categories below:*
 - **Knowledge** (of a password or PIN)
 - **Possession** (e.g. card, code generating device)
 - **Inherence** (personal characteristics, e.g. fingerprint, voice)
- *Numerous exemptions*
 - **Low value and contactless payments, transport & parking fees**
 - **Trusted beneficiaries and recurring transactions**
 - **Transaction risk analysis, if it keeps fraud levels low**
- *Monitoring obligation when exemptions are used*
- *Review clause for the fraud rate thresholds*

Secure communication (1)

- *Bank customers must not be prevented from using new services of '3rd Party Providers' (TPPs)*
 - **Payment initiation services:** Provider triggers a credit transfer from a customer's bank account to a payee; replaces card payments
 - **Account information services:** Providers get information from different accounts and offer personal finance monitoring and management services
- *TPPs often use 'screen scraping': accessing online banking interface with bank customer's credentials*
 - **Regarded as unsafe**
 - **Requires major investment in software by TPPs**

Secure communication (2)

- *PSD2 requires banks to provide account information to TPPs if they offer online banking*
- *Communication must allow identification of TPPs and exchange of security certificates*
- *Only information needed for a payment transaction to be obtained*
- *Two options for interfaces*
 - **Adapt the customer online banking interface**
 - **Create a dedicated interface which would then be mandatory for TPPs** – but lack of trust among TPPs
- *Dedicated interfaces best for rapid development of the market for new payment services*

Towards EU-wide open banking

- *PSD2 does not mandate a standard API, unlike UK CMA*
- *RTS empowers banks to mandate it:*
 - **If they offer an API, TPPs must use it, no more screen 'screen scraping'...**
 - **...provided the API is of good quality; adapted online banking interfaces as a fall-back for TPPs**
- *RTS provides incentives for standardization:*
 - **Banks want to avoid costs of fall-back...**
 - **...and can be exempted by NCA if they provide an API that is accepted by all market players**
 - **Use of standardized APIs increases chances of exemption**
- *EU evaluation group to be established by market players to review API standards*

A difficult transition to open banking

- *PSD2 applicable from 13/1/2018, but key requirements for secure communication only in force around September 2019*
- *Grandfathering: TPPs that existed before 12/1/2016 can offer the same activities in same markets as before*
- *New and existing TPPs licensed under PSD2 allowed to access accounts using screen scraping in all MS except those where it had been illegal before 12/1/2016*
- *But MS must ensure that banks do not abuse their own non-compliance with security standards to block or obstruct the use of payment initiation and account information services (Article 115(6), PSD2)*
- *EBA opinion on the transition: comply with RTS as soon as possible*

III. The shape of things to come

Drivers of change:

- *Regulation: what can third parties do with account access and information – PSD2 and RTS implementation, complying with data protection rules*
- *New infrastructure: instant payments, mobile payments*
- *Innovation and competition: how will market players respond?*

The impact of regulation

- *Right for consumers to use new services: payment initiation and account information*
- *Incentive to develop standardized APIs: lower barriers to market entry*
- *Strict data protection rules under PSD2 and GDPR may limit business models relying on exploiting personal data:*

Article 67(2)(f), PSD2: AISP shall not use, access or store any data for purposes other than for performing the account information service explicitly requested by the payment service user, in accordance with data protection rules

The impact of new infrastructure

- *Instant payments already available in a number of countries*
- *Eurozone catching up:*
 - **SEPA instant credit transfer scheme (SCT inst)**
 - **TARGET Instant Payment Settlement (TIPS)**
- *First application could be for mobile peer-to-peer payments*
- *Major impact when used by consumers for purchases*
- *Further enhances the possibilities of simple payment accounts; no need for credit cards, guarantees to merchants*

Who will be the dominant providers of payment services?

- *Banks competing with attractive apps and offering overdrafts to replace credit cards*
- *FinTechs providing the interface to banks which will 'mass-produce' account services with little direct contact to customers*
- *"Big Tech" players adding payment initiation and account information services to their mobile apps*
- *Mobile phone operators*
- *National card schemes developing payment solutions for a country's banks*
- *Global card or e-wallet schemes leveraging their brands and global acceptance with merchants*

Key question: how to make money with payments

- *Levying charges on merchants? Instant payments could offer cheap alternatives*
- *Account fees? Low acceptance by consumers*
- *Free payment accounts to attract customers for other services?*
- *Fees for payment instruments with premium features? (insurance, chargeback rights...)*
- *Personal data for free payment services?*