

The long(er) arm of regulation

Jacob Ghanty outlines the impact of the second Payments Services Directive, which will change the banking landscape in Europe

The text of the second Payment Services Directive (EU) 2015/2366 (PSD2) was published in the Official Journal of the EU on 23 December 2015. It entered into force on 12 January 2016 and must be transposed by member states into their national laws and regulations by 13 January 2018.

PSD2 replaces and repeals the original Payment Services Directive 2007/64/EC (the PSD) and builds on it in a number of respects. The general effects of PSD2 will be to broaden the scope of regulation in this market and to lower barriers to the provision of account-based services by non-bank payment service providers (PSPs).

This article provides a high level overview of some of the ways in which PSD2 extends the scope of regulation in the payments market and also of the removal of certain barriers to competition in the sector.

In Brief

- PSD2 broadens the geographical coverage of the PSD, meaning that firms will need to review their existing customer documentation and systems and processes
- PSD2 brings new categories of payment service providers within scope: payment initiation services providers, and account information service providers
- PSD2 removes a number of exemptions from regulation contained under the PSD. Firms that have relied upon an exemption will need to check that their model still works under PSD2
- PSD2 contains provisions intended to stimulate competition

Broadening geographical scope

PSD2 extends the scope of the PSD in a number of ways. Broadly speaking the PSD applies only to payment services provided in the EEA where both the PSP of the payer and the PSP of the payee are (or the sole PSP is) located in the EU. PSD2 extends this by applying certain disclosure and transparency requirements to so-called “one-leg transactions” where just one of the PSPs is located within the EU.

In contrast with the PSD, PSD2 also extends disclosure and transparency requirements to all currencies and not just EU currencies. Article 2 of PSD2 contains the relevant provisions concerning the application of the various requirements that depend upon the relevant currency used in a transaction and/or the location of the PSPs.

Given this broader territorial reach, firms will need to review their existing customer documentation and systems and processes and, if necessary, update them to ensure that the conduct of business rules are correctly applied to a broader range of transactions. Also, certain firms that have operated outside of the scope of the PSD (e.g. because they are engaged only in one-leg transactions and/or transact in non-EU currencies) will need to revisit whether their activities bring them within the coverage of regulation under PSD2.

New payment services

Two kinds of third party PSP (TPPs) will be brought within the scope of regulation under PSD2. This has been driven by technological advances in the way that banking, payment and other financial services are delivered by or through intermediary TPPs. Many such firms are not currently required to be regulated under the PSD, essentially because they do not execute the actual transfer of funds in a payment transaction.

The first are payment initiation services providers, which initiate payment orders at the request of the payment service user with respect to a payment account held at another PSP. This essentially will bring within the scope of regulation TPPs that provide means of paying for goods or services online without the need to use a credit or debit card. Often such firms are in effect providing a bridge to a payment service user’s bank account to initiate a payment in respect of an online purchase of good or services.

The second such type of TPP is account information service providers, which provide payment service users with “an online service to provide consolidated information on one or more payment accounts held by the payment service user with either another payment service provider or with more than one payment service provider.”

These changes potentially enlarge the constituency of regulated PSPs significantly, bringing into scope firms ►

that have been able to operate under the regulatory radar even though they provide quasi payment services of various types. Clearly there is a consumer protection element to this, although many smaller firms caught will complain of excessive red tape being applied where generally there will already be a regulated entity involved in a transaction (e.g. the bank which provides the payment account in relation to which a payment initiation service is provided).

Carving back on the carve outs

The PSD contains a number of exemptions from regulation, some of which will be narrowed or deleted entirely under PSD2, which again effectively broadens the scope of regulation. Firms that have relied upon an exemption will need to revisit their PSD assessment to check that their model still works under PSD2.

There are four exemptions amended under PSD2 that are particularly noteworthy.

The first is the so-called "commercial agents exemption". Under the PSD, this exempts payment transactions made from a payer to a payee through a commercial agent who has authority to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or payee. PSD2 amends this exemption so that it applies only where a PSP is acting for the payer or payee. PSPs acting as commercial agent for both payer and payee will not be able to rely on this exemption any longer under PSD2. The European Commission's apparent reasoning behind this was that various e-commerce platforms had been relying on this exemption when acting as agent for both parties without any real margin for negotiation for either party. Presumably this meant that the real value they are providing is the payment mechanism rather than acting as agent in relation to the purchase or sale of goods or services.

The second exemption that has been amended materially is the limited networks exemption. Under the PSD, services based on instruments used to acquire goods/services within a limited network of service providers (such as certain store and pre-paid cards) are exempt. PSD2 narrows this exemption in several ways. For instance, in order to rely on this the relevant services must be based on instruments that either:

- allow the holder to acquire goods or services only in the premises of the issuer or within a limited network of service providers under direct commercial agreement with a professional issuer; or
- can be used only to acquire a very limited range of goods or services.

PSD2 represents a recognition that the payments market is growing and changing at a pace that will rapidly render aspects of the PSD obsolete

The basic reasoning behind this change appears to be the sheer size of networks utilising this exemption and the volume of business undertaken through them.

The third such exemption concerns low value payments for digitally downloaded content or telecoms payments. This exemption applies to payments executed through mobile phones, the internet and other IT devices. Under PSD2 it is narrowed to apply only to ancillary payment services provided by providers of electronic communication networks or services (such as telecom operators). Some firms have used this exemption to effectively enable the transfer of money, whereas the Commission believed it should be utilised only for low value payments for digital content, including ringtones and so on that are provided as ancillary services to telecoms services. Under PSD2 this exemption will only be available for individual transactions not exceeding €50, with an overall cap of €300 in any billing month.

The fourth exemption relates to the provision of cash withdrawal services by independent operators of ATMs. This exemption remains under PSD2 although such operators will be required in future to disclose information concerning withdrawal fees.

Access to TPPs

PSD2 contains numerous provisions that are intended to stimulate competition by facilitating the use of payment initiation services. For example, PSD2 contains an obligation, in broad terms, on banks offering execution services from payment accounts to allow their customers to use the new payment initiation and account information services provided by TPPs. PSPs (e.g. a bank providing a payment account) will have to facilitate access and information provision to TPPs acting for payers. This represents a major change to how the market for banking services currently operates. For instance it means that a TPP could issue its own debit cards and essentially link them to an account provided by the third party bank used by its customer. It is unclear, however, precisely what efforts a bank in the scenario described above would need to use to facilitate its customer's use of a TPP's services and/or how the costs of enabling such activities should be apportioned.

Need to adapt

PSD2 represents a recognition that the payments market is growing and changing at a pace that will rapidly render aspects of the PSD obsolete.

One of the major effects of PSD2 will be to bring many more firms within the scope of payments regulation. Perhaps of even greater importance though will be the ability of TPPs to provide new types of payment service by linking to customers' accounts that are provided by third party PSPs.

Established participants and new entrants to the market will need to adapt quickly to the changing regulatory climate and should begin planning now to make sure their business model works under the incoming regulatory regime. ●



Jacob Ghanty is a Partner in K&L Gates LLP's Payment Systems practice.