

# Consultation on the draft legislation to implement the Payment Services Directive: a summary of responses

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February 2009



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# Executive summary

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This document summarises the responses to a consultation published in July 2008, in which the Government sought views on the UK's draft implementing legislation for the Payment Services Directive (PSD). This document also provides the Government's conclusions on the implementing legislation, taking into account some of the specific issues raised by respondents. The final implementing legislation, which has taken the form of Regulations made by HM Treasury under section 2(2) of the European Communities Act 1972, was laid before Parliament on 9 February 2009 and will come into force for different purposes on 2 March 2009, 1 May 2009 and 1 November 2009, in accordance with regulation 1(2)(b).

The July 2008 consultation document set out how the Government intended to implement the PSD's provisions into UK legislation. Further to a policy consultation in December 2007, the July 2008 consultation document also sought views on two policy options which were whether to:

- introduce a safeguarding threshold of £50, above which payment institutions must safeguard user funds; and
- apply the provisions of Titles III and IV to extra-EU payment transactions.

Stakeholders had 12 weeks to respond to the legislative consultation of July 2008, which closed on 3 October 2008. A total of 37 responses were received from a cross-section of interested stakeholders. These conclusions were further informed by around 10 stakeholder meetings with representatives from both industry and end-users. The conclusions reached in this document have been further informed by analysis undertaken as part of the European transposition process, led by the European Commission and involving all EU Member States. It should, however, be noted that the interpretation of specific provisions within the Directive will ultimately be for the courts to decide.

# 1

## Introduction and overview of the responses

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**1.1** In July 2008, the Government published a consultation on its legislative approach for implementing the Payment Services Directive (PSD) in the UK<sup>1</sup>. This consultation document included the draft Payment Services Regulations (referred to below as the Regulations or PSR) and set out how the Government intended to implement the Directive's provisions, in an effective, proportionate, and risk-based manner, into UK legislation. The purpose of the consultation was to seek views on the drafting of the Regulations and on two policy options:

- introducing a safeguarding threshold of £50; and
- applying the provisions of Titles III and IV to “one-leg” transactions.

**1.2** The legislative consultation formed part of a three staged consultation process:

- in July 2006, the Government consulted on the European Commission's proposal for the Directive<sup>2</sup>. The consultation responses informed the Government's approach to the European-level negotiations<sup>3</sup>;
- in December 2007, the Government published a consultation on the policy approach for implementing the PSD in the UK<sup>4</sup>. A summary of responses and Government conclusions on the policy options was published in June 2008<sup>5</sup>; and
- in July 2008, the Government launched a 12-week public consultation on the draft Regulations that would enact the PSD legislation in the UK.

### The aim of this document

**1.3** This document summarises the responses to the July 2008 legislative consultation and sets out the resultant Government conclusions, where appropriate. Following detailed analysis that has been undertaken as part of the European Commission-led transposition process and to address a number of specific issues raised in response to the consultation, a number of drafting changes have been made to the PSD implementing legislation and some new regulations have been added. The interpretation of specific provisions within the Directive will, however, ultimately be for the Courts to decide.

**1.4** This document:

- explores specific points made during the consultation in more detail and sets out the Government's conclusions on certain aspects of the Regulations (chapter 2);

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<sup>1</sup> Implementation of the Payment Services Directive: a consultation on the draft legislation, HMT, July 2008, [http://www.hm-treasury.gov.uk/payment\\_services.htm](http://www.hm-treasury.gov.uk/payment_services.htm)

<sup>2</sup> Payment Services Directive: a consultation document, HMT, July 2006, [http://www.hm-treasury.gov.uk/payment\\_services.htm](http://www.hm-treasury.gov.uk/payment_services.htm)

<sup>3</sup> A summary of responses to the consultation on the Payment Services Directive, HMT, December 2006, [http://www.hm-treasury.gov.uk/payment\\_services.htm](http://www.hm-treasury.gov.uk/payment_services.htm)

<sup>4</sup> Implementation of the Payment Services Directive: a consultation document, HMT, December 2007, [http://www.hm-treasury.gov.uk/payment\\_services.htm](http://www.hm-treasury.gov.uk/payment_services.htm)

<sup>5</sup> Implementation of the Payment Services Directive: a summary of consultation responses, HMT, June 2008, [http://www.hm-treasury.gov.uk/payment\\_services.htm](http://www.hm-treasury.gov.uk/payment_services.htm)

- sets out the next steps in the process (chapter 3); and
- lists the respondents to the consultation (annex A).

**1.5** This summary of responses document should be read together with the Payment Services Regulations 2009 (“the Regulations”) and will be especially relevant to businesses that will be affected by the Regulations, representative bodies acting on their behalf, the competent authorities responsible for supervising compliance with the Regulations, as well as payment service consumers and their representative groups.

## **Background to the Payment Services Directive**

**1.6** The European Commission adopted a legislative proposal for a Payment Services Directive (PSD) on 1 December 2005, aiming to achieve a Single Market in retail payment services. Political agreement between the Council and the European Parliament was reached in April 2007, the Directive was adopted on 13 November 2007 and was published in the Official Journal of the EU on 5 December 2007. The PSD must be implemented into national law by 1 November 2009.

**1.7** The aim of the PSD is to enhance competition and transparency across the EU, and to ensure that the level of consumer protection is sufficient and harmonised. The purpose of the consultation process has been to ensure that the payments industry, business and consumers:

- are informed of the objectives of the PSD;
- have had the opportunity to contribute to the negotiations of the Directive to benefit the UK; and
- have had the ability to seek clarity on the Government’s intended approach on the Directive’s implementation both in terms of policy and legislation.

## **Supervisory authorities of the Regulations**

**1.8** The competent authority for most aspects of the Regulations will be the Financial Service Authority (FSA) (with the Financial Services and Markets Tribunal as the judicial body, which hears references arising from its decision notices). However, other bodies will also have roles. Namely:

- HM Revenue and Customs will retain responsibility for the anti-money laundering supervision of money service businesses, and will additionally be responsible for the anti-money laundering supervision of any mobile phone operators or bill payment service providers that provide payment services which fall into the scope of the Third Money Laundering Directive due to the PSD;
- the Office of Fair Trading will be responsible for the implementation of article 28 (access to payment systems), which has a competition objective, while the Competition Appeal Tribunal will be the appellate body with respect to this article; and
- the Financial Ombudsman Service will provide the out-of-court redress mechanism envisaged in article 83 of the PSD.

## Analysis of the responses

**1.9** The legislative consultation on implementing the Payment Services Directive (PSD) closed on the 3 October 2008 and the Government received 37 responses from a cross-section of interested stakeholders, which included:

- industry trade bodies;
- credit institutions;
- e-money issuers;
- credit card issuers;
- mobile phone operators;
- money service businesses;
- independent ATM operators; and
- consumer groups.

Annex A provides a full list of respondents.

**1.10** In addition to the responses received, the conclusions reached in this document have been further informed by about 10 stakeholder meetings with a range of payment service providers and end-users. The meetings provided an opportunity to discuss the legislation in more detail, as well as providing an opportunity for Government to hear views and concerns on how to best implement the PSD in the UK.

**1.11** The Government is grateful to everyone who responded to the consultation in writing or participated in any of the meetings.

## Proposed legislative approach

**1.12** The responses received indicated broad support for the draft implementing legislation of the PSD, as set out in the consultation document. The majority of respondents believed that the Regulations were comprehensive and were generally supportive of the “intelligent copy out” approach that was adopted. All payment service providers and payment system operators seemed clear of their requirements under each regulation, and indicated that they adequately represented the Government’s policy intention. The proportionate enforcement approach of the Regulations, and the accompanying penalty regime, were also generally well received.

**1.13** In some cases, to address specific concerns that were raised in response to the consultation, and in view of the European transposition work that has been occurring in parallel to this consultation process, drafting changes have been made to the draft Regulations and some new regulations have been added. Chapter 2 highlights the changes the Government has made to the draft Regulations. The FSA will soon be publishing an “approach document” that will set out its views on the interpretation of the Regulations. Further to this, payment service providers and payment systems subject to the Regulations should seek to familiarise themselves with the full set of final Regulations.

# 2

## Consultation responses and Government conclusions

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**2.1** This chapter considers the responses to the 17 questions posed in the consultation document. It has been divided into sub-sections dealing with each question or set of questions posed, analysing in each case the responses to the issue described in the consultation document and, where appropriate, provides conclusions reached during EU-level discussions.

**2.2** For reasons of space, this chapter does not in all cases address points made by a single respondent or where the Government has not significantly altered its approach. The conclusions will also be subject to the ongoing transposition discussions at EU-level.

**2.3** The Government's conclusions on the consultation responses generally fall into one of the following categories:

- instances where there was explicit support for the proposed legislative approach;
- instances where points of clarification were requested;
- reactions with which the Government disagrees; and
- reactions with which the Government agrees, and has amended its approach (and the respective regulation(s)), as appropriate.

**2.4** The consultation requested responses to questions relating to the flexibility of the policy option concerning the safeguarding threshold (above which payment service providers must safeguard their users' funds). The Impact Assessment has been updated and can be found at [http://www.hm-treasury.gov.uk/fin\\_payment\\_index.htm](http://www.hm-treasury.gov.uk/fin_payment_index.htm).

**2.5** In early 2009, the FSA, as a regulator for most aspects of the PSD, will publish three documents:

- a policy statement in response to the consultation on FSA Handbook changes;
- a PSD Perimeter Guidance; and
- a PSD Approach Document.

These documents will detail, in particular:

- The complaints handling and ombudsman schemes; and
- The scope of the Regulations and the supervisory and enforcement approach of the regulators.

**2.6** The Office of Fair Trading will be contributing to these documents with respect to rules on fair and open access to payment systems in scope of the Regulations.

**2.7** The information that will be provided in these documents will take into account the conclusions reached during EU-level transposition discussions, Government published PSD-related documents, and conclusions drawn from stakeholder events and consultation responses. It is expected that these documents should provide a sufficient level of detail to support

payment service providers and payment systems in complying with the PSR. The documents, however, will only act as a guide and should not be taken to be definitive.

## QUESTION 1: SCOPE (SCHEDULE 1 AND DRAFT REGULATION 3(1))

Q1. Do you agree with the draft regulations proposed for the scope of the Payment Services Directive (PSD)? Is any further detail required, or are additional definitions needed?

**2.8** The PSD is divided into six Titles. Title I and the Annex to the Directive set out the subject-matter of the Directive, the types of providers and activities that fall within the scope of the Directive, and the definition of relevant terms. Part 1, “Introductory provisions”, and Schedule 1, “Payment Services”, of the Regulations transpose this Title and the Annex to the PSD.

**2.9** This section summarises the responses received and sets out the Government’s conclusions (as well as providing further clarity, where requested) on the intended scope, exempted institutions, negative scope and definitions used in the Regulations.

### Scope

#### Bill payment service providers

**2.10** The June 2008 summary of responses to the December 2007 policy consultation on implementing the PSD (paragraphs 3.9 to 3.11) concluded that some bill payment service providers were not considered to be providing money remittance services nor providing any other payment service within the meaning of the PSD. A few respondents to the July legislative consultation sought further clarity on which bill payment business models would fall into the scope of the PSD. Through further analytical work with the sector, it has been identified that at least two bill payment business models currently exist in the EU: one that would fall into the scope of the PSD and one that would fall out of its scope.

**2.11** In the first instance, the bill payment service offered to a customer wishing to pay a third party’s invoice would effectively be a simple money remittance service. In this model the receipt is issued to the customer and the payment to the invoice issuer’s bank account is generally guaranteed to the customer (together in some cases with notification to the invoice issuer). However, the issuance of the receipt and guarantee of payment does not result in the debt being extinguished. In the event of the bill payment service provider failing to complete the payment transaction, the liability would remain with the customer. This service would, and assuming no other negative scope provisions are available, generally be considered to be a payment service captured under points 1-3 or 6 of the Annex (paragraph 1(c) of Schedule 1 to the Regulations).

**2.12** The second business model operates on the basis that the invoice issuer is the principal and the bill payment service provider is its agent, providing a means by which the customer can settle a bill. In this model, the invoice issuer provides the customer with the option of settling the invoice by payment to the bill payment service provider. Such a payment extinguishes the debt by virtue of the agency relationship between the provider and the invoice issuer. This transaction is therefore equivalent to making a payment direct to the invoice issuer. In the event of the failure of the bill payment service provider to make the payment, the risk lies with the invoice issuer. As the receipt issued by the bill payment service provider is evidence of the debt having been extinguished, the bill payer would not have any risk exposure. As the invoice is settled as soon as the money is given to the bill payment service provider.

**2.13** The majority of bill payment service providers in the UK currently follow the latter model, which is captured by article 3(b) of the PSD (negative scope) and therefore falls outside the scope of the PSD. In the UK this model will fall outside the scope of the Regulations by virtue of

paragraph 2(b) of Schedule 1 to the Regulations. It is anticipated that the FSA Perimeter Guidance will also provide guidance on this issue.

## **Money remittance companies**

**2.14** Respondents broadly supported the draft Regulations in so far as they brought money remitters into the scope of the Regulations. Some, however, sought clarity regarding which firms within the business model of a large money remitter would need to become a payment institution.

**2.15** It is understood that certain money remitters, particularly those that tend to operate on a pan-European or global basis, use a 'super-agent' structure. At the top of this structure a company, 'TopCo', determines the nature of the money remittance service. It also provides key functionalities that give effect to those services, including a messaging service and a settlement system that provides net settlement between the TopCo's 'super-agents'. The money remittance services are branded primarily in the TopCo's name. The TopCo does not, however, necessarily provide services through direct contact with payment service users, and may only do so through its super agents.

**2.16** The super agents, appointed by the TopCo, provide the TopCo's money remittance services either directly to payment service users, or by appointing TopCo-approved sub-agents. The appointed sub-agents must comply with the terms set by the TopCo that relate, for example, to the terms by which the remittance service is to be provided, advertised and charged, and how remittances are to be made to the super-agent. Other commercial terms may be at the super-agent discretion.

**2.17** As the payment service users' perspective would be that they were using the remittance services of the TopCo, it is considered that the TopCo would need to become a payment institution. If the TopCo currently operates on a pan-European basis, it would need to seek authorisation in a Member State under that State's PSD implementing legislation. This would also enable it to continue to passport its services by means of its super-agents and sub-agents. It would be the responsibility of the TopCo to register its super-agents and sub-agents. If a TopCo super-agent wished to provide TopCo services on a cross-border basis through its agent structure, it would need to ensure that the TopCo had the appropriate passport in place. The FSA has consulted on draft guidance on when a service is provided on a cross-border basis<sup>1</sup>.

## **Mobile phone operators**

**2.18** The June summary of responses (paragraphs 3.29 to 3.32) concluded that, at present, the majority of UK mobile phone operators do not appear to require authorisation or registration as a payment institution under the PSD. It noted that currently operators are not pure intermediaries when facilitating the transfer of funds between a customer and a third party for the payment of digital goods or services. In this circumstance, the customer's payment obligation is towards the mobile operator and not the content provider or the provider of the goods and services. The third party, therefore, has no direct contractual relationship with the customer in respect of the payment, i.e. the mobile operator is not acting only as an intermediary. This service is not among the payment services caught by the scope of the PSD and has been reflected in paragraph 2(l) of Schedule 1 to the Regulations.

**2.19** The Government, in light of continuing innovations in mobile payments, will continue to engage with the sector and the payments industry to ensure that the Regulations remain appropriate to the commercial context. On 30 June 2008, for example, the GSMA (the global

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<sup>1</sup> See Question 41 in Appendix 8 of FSA's CP08/16 at [http://www.fsa.gov.uk/pages/Library/Policy/CP/2008/08\\_16.shtml](http://www.fsa.gov.uk/pages/Library/Policy/CP/2008/08_16.shtml)

trade association representing GSM mobile phone operators across the world) and the European Payments Council (the trade association representing the European banking industry on payment) jointly announced their plan to work together to accelerate the deployment of services that enable consumers to pay for goods and services in shops, restaurants and other locations using their mobile phones<sup>2</sup>. Separately, on 28 July 2008, the Payments Council in the UK (the organisation that sets strategy for UK payments) invited companies that could potentially develop a common infrastructure platform for mobile payments to respond to a formal 'Request for Information'<sup>3</sup>. Ongoing initiatives such as these, together with the European Commission's proposal to revise the Electronic Money Directive (see paragraph 3.6), could potentially lead to developments in mobile payment business models, such that the mobile operator serves to act as a pure intermediary in a payment transaction, and would thereby fall into the scope of the PSD.

## Treatment of third country firms

**2.20** As discussed in the June summary of responses (paragraphs 3.73 to 3.74) the scope of the PSD intends to capture all firms with a legal presence in the territory of the Community (as defined by Article 299 of the EC Treaty) together with their branches and agents providing payment services. The final text of the Directive, however, left the treatment of third country firms that have a legal presence outside the Community (i.e. non-European Economic Area (EEA) firms) ambiguous. During EU transposition discussions it has been concluded that the PSD, by reading the last sentence of article 10(1) in conjunction with article 29, introduces a regime whereby branches of third-country payment firms would have to become a payment service provider within the meaning of article 1(1) of the PSD to be entitled to provide payment services in the Community. This would mean that once the PSD comes into force, a branch of a non-EEA (a third country) firm would need to become incorporated within the Community and then seek authorisation as a credit institution or become a payment institution or e-money institution before being able to provide payment services within the Community.

**2.21** From a policy perspective, it is important that all businesses offering payment services in the EEA comply with the PSD conduct of business provisions. If third country firms did not fall within the scope of the PSD and were able to provide payment services through their branches within the Community, an unlevel playing field would be created, as third country firms would receive more favourable treatment than institutions located within the Community. This could inadvertently incentivise firms to locate outside the EU, compromising the prudential and consumer protection provisions introduced by the Directive.

**2.22** The Government does not, however, consider that the interpretation of the authorisation requirements extends to third country credit institutions. Currently, under the Banking Consolidation Directive (BCD)<sup>4</sup>, third country credit institutions, through registering their branch with a competent authority in a Member State, are able to accept deposits through their branch in that Member State. As the branches of third country credit institutions are operating lawfully in the EU in providing banking services, it would seem unnecessary to require them to become incorporated so that they are able to provide payment services. The Government will continue to engage at EU-level towards reaching agreement on this issue.

## Applicable law

**2.23** Some respondents questioned which law would apply if a firm were to passport its services into another Member State. If the firm provides its services through an established branch or an

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<sup>2</sup> <http://europa.eu/rapid/showInformation.do?pageName=recentPressReleases&guiLanguage=en>

<sup>3</sup> <http://www.paymentscouncil.org.uk/>

<sup>4</sup> <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2006:177:0001:0200:EN:PDF>

agent (i.e. an establishment) in the host Member State, then the host Member State's law would apply in relation to the information requirements and the rights and obligations relating to the business of the payment institution. (It should be noted that home laws will apply in relation to the prudential regulations of a payment institution.) The PSD does not expressly provide whether the home or host law relating to these matters will apply if the firm were to offer its services cross border from the home Member State. The Regulations have provided that, in this circumstance, the home Member State laws would apply and the FSA will be responsible for regulatory supervision of all the firm's payment activities.

**2.24** One respondent sought clarity on how 'a legally dependent part of the institution' under the definition of branch (regulation 2) would be interpreted in this context. Even though a branch would be legally dependent on its principal payment institution, if it were to operate in another Member State as an establishment, it would have to comply with the host Member State's laws (unless European law provided otherwise).

## **Gibraltar**

**2.25** The draft regulations that accompanied the July legislative consultation document made provisions to include Gibraltar within the scope of the Regulations. The Government is continuing to liaise with the territory regarding the application of the PSD. As these discussions are still progressing, references to Gibraltar have been deleted from the Regulations. Depending on the outcomes of the discussions, the Regulations might be amended in the future, as necessary.

## **Exempted institutions**

**2.26** Draft regulation 3 provided an exemption to credit unions, municipal banks and the National Savings Bank (NSB) from the scope of the Regulations.

**2.27** The majority of responses to the two previous consultations on the PSD strongly supported the view that credit unions should be exempt from the PSD, as they provide financial services to those at risk of financial exclusion. However, two respondents to the July legislative consultation argued that this exemption might create an unlevel playing field between credit unions and other non-bank providers that may wish to serve the same market. One of these respondents suggested that new players to enter this market should receive the same treatment as credit unions (i.e. to be exempt from the Regulations). The other stressed that all institutions that transact payments should be subject to prudential, capital and transparency requirements.

**2.28** Another respondent believed that NSB customers should receive the same level of information and service as they would from a commercial bank, which would be subject to the Regulations.

**2.29** The Government agrees that consumers should receive adequate consumer protection from institutions that provide payment services. Credit unions are currently regulated by the FSA. The credit union specialist sourcebook (commonly known as CRED<sup>5</sup>) sets out the prudential requirements, including solvency criteria and capital requirements that the sector is subject to. To extend the PSD exemption to firms that serve a similar market as credit unions would be disproportionate, particularly if they are not already subject to adequate prudential requirements.

**2.30** The June summary of responses (paragraphs 3.50 to 3.55) explained that the NSB could not be subject to the prudential requirement of the PSD. However, the Government agrees that an NSB customer should receive the same level of information and service it would receive from

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<sup>5</sup>Credit union specialist sourcebook: <http://fsahandbook.info/FSA/html/handbook/CRED>

a commercial bank that is subject to the Regulations. As explained in the June summary of responses, the NSB intends to provide this on a voluntary basis.

**2.31** It should be noted that credit unions and the NSB are subject to the Financial Ombudsman Service (FOS). Therefore, consumers of such providers' services would be able to seek redress through the FOS if necessary.

**2.32** The Government recently consulted on proposals to amend the Credit Union Act, including the qualifying criteria for membership (the "common bond"), as well as the range of activities credit unions in Great Britain are able to undertake. The Government will continue to engage with the credit union sector and the NSB to ensure that the regulatory approach towards them remains proportionate and risk-based.

## Negative scope

**2.33** Respondents broadly supported the draft provisions under Part 2 of Schedule 1 that set out the payment activities that are not captured by the Regulations (i.e. the negative scope). Some respondents, however, sought clarity on whether certain payment activities fell in or out of the scope of the Regulations:

- foreign exchange and forward contracts in relation to remittance services;
- limited networks;
- cash transactions;
- paper-based transactions;
- firms providing ancillary activities; and
- cash placed on accounts.

## Foreign exchange transactions

**2.34** A few respondents from the foreign exchange and the banking sectors questioned whether and how foreign exchange transactions would fall into the scope of the PSD. The PSD clearly identifies that cash-to-cash money exchange businesses operations, where funds are not held on a payment account, fall outside its scope. It is, however, less clear whether the electronic purchase of foreign exchange is in scope.

**2.35** Article 16(1)(a) provides that "payment institutions" shall be entitled to engage in "... the provision of operational and closely related ancillary services such as ... foreign exchange services ...". This indicates that a foreign exchange service is not itself a payment service. Therefore, firms providing foreign exchange services are only within the scope of the Regulations when and if they provide payment services (as defined by the PSD annex), by way of business, in the UK. In determining whether the services they offer are in scope of the Regulations, firms should refer, in the first instance, to the FSA's Perimeter Guidance (a consultation draft of which was appended to CP08/16: Quarterly Consultation Paper (October 2008), including Q9 and the relevant parts of 15.3 and 15.5). An example of the service that would be a payment service for the purposes of the Regulations is the money remittance element of a foreign exchange service (on behalf of clients to third parties).

## Forward foreign exchange contracts

**2.36** The Government believes that the conduct of business provisions of the PSD do not apply to commercial forward foreign exchange (fx) services. If they were to apply, then the policy intentions of the Distance Marketing Directive (DMD) in relation to the right of withdrawal could be undermined. For instance the DMD specifically provides that the right of withdrawal does not

apply to foreign exchange, whilst article 54 of the PSD specifically provides for withdrawal of consent.

**2.37** This does not, however, mean that certain aspects of commercial fx forwards would not be subject to the provisions of the PSD. For example, the electronic transmission of a payment by a payment service provider (e.g. by a bank via a bank account) to an fx services provider will be subject to the PSD, as this transfer of funds would be executed by the bank. More generally, it would be expected that in the case of a standard payment transaction involving the transfer of funds and currency conversion as part of that transfer the provisions of the PSD would apply, as appropriate. For example:

- the withdrawal of funds from an account in one currency and the deposit of funds into an account in another currency; and
- foreign exchange conversions that are provided as part of the provision of a payment service – for example where a card issuer allows the cardholder to make foreign currency purchases or where a customer makes a transfer in one currency to pay a bill in another.

**2.38** The FSA is considering giving guidance on this issue as part of its proposed Perimeter Guidance.

### Limited network

**2.39** The definition of limited network has been transposed using a copy out approach. For certainty purposes, a few respondents sought to include stricter boundaries in the Regulations to define a limited network. This level of detail is not provided in the PSD and it would not be appropriate to go beyond the Directive's wording. The FSA has consulted on guidance to help firms determine if they are operating a 'limited network'<sup>6</sup>. The final guidance will be contained in its Perimeter Guidance.

### Firms providing ancillary activities

**2.40** Regulation 2 defines the scope of "payment services" as the activities specified in Part 1 of Schedule 1 when they are carried out "as a regular occupation or business activity". One respondent sought clarity on the test that would be applied to establish whether a payment service is provided on an ancillary basis. As the Directive itself does not define this test, it would not be appropriate to include such a test in the Regulations. The FSA has consulted on guidance to help firms understand this test<sup>7</sup>. The final guidance will be contained in its Perimeter Guidance.

### Cash transactions

**2.41** The December 2007 policy consultation (paragraph 2.36 to 2.37) stated that the scope of the PSD primarily focuses on electronic payments. However, the Directive does capture cash deposits and withdrawals, such as a cash deposit made at a bank branch, where there is an electronic component to the transaction. Schedule 1, paragraph 2(a) copies out the negative scope article to delineate which cash transactions are out of scope of the Regulations. One example of an "intermediary intervention" that would bring cash back into scope would include the remittance of money.

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<sup>6</sup> See Q36 in Appendix 8 of FSA's CP08/16.

<sup>7</sup> See Q9 in Appendix 8 of FSA's CP 08/16.

## Paper-based transactions

**2.42** Some respondents requested the inclusion of credit card cheques, alongside travellers' cheques in paragraph 2 (g)(i) of Schedule 1 to provide a fuller illustration of the types of paper cheque that would not be caught by the PSD. Although the Government appreciates that providers would like certainty of the instruments that fall in or out of scope of the Regulations, the Government believes that the term "paper cheques of any kind" is sufficiently clear and that it is appropriate to follow the wording of the Directive (which explicitly refers to travellers' cheques but not to credit card cheques).

## Definitions

**2.43** Respondents generally seemed clear on the majority of definitions within the draft Regulations. Some respondents, however, sought clarity on instances where the definitions varied slightly from the Directive. Others requested the addition of further detail in certain definitions, to ensure certainty of application. This sub-section outlines instances where substantive changes to the definitions have been made and also where clarity has been requested.

### Branch

**2.44** The transposed definition of branch in the draft Regulations had been aligned with the definition of branch in the Companies Act 2006 and the Enterprise Act 2002. For the purpose of the Regulations the definition has been amended to include branches of EEA payment institutions.

**2.45** One respondent raised concerns that the transposition of the phrase "has no legal personality" in the PSD to "legally dependent part of the institution" in the Regulations might narrow the intended scope of the term "branch". The Government believes that the use of such wording effectively transposes the definition in the Directive and aligns it with English law.

### Charity

**2.46** The draft regulation has been revised to include all charities, with an annual income of less than £1 million, in the United Kingdom (the current threshold to make a compliant to FOS).

### Box 2.A: Definition of 'Charity' (regulation 2)

"...“charity” means a body whose annual income is less than £1 million and is—

- (a) in England and Wales, a charity as defined by section 1(1) of the Charities Act 2006<sup>(8)</sup>;
- (b) in Scotland, a charity as defined by section 106 of the Charities and Trustee Investment (Scotland) Act 2005<sup>(9)</sup>;
- (c) in Northern Ireland, a charity as defined by section 1(1) of the Charities Act (Northern Ireland) 2008<sup>(10)</sup> or, until that section comes into force, a body which is recognised as a charity for tax purposes by Her Majesty’s Revenue and Customs;...”

## Consumer

**2.47** One respondent requested assurances that the definition of consumer did not cover the individual’s acting on behalf of their employer’s trade, business, or profession. The definition for consumer in the Regulations has been revised accordingly to provide this assurance.

### Box 2.B: Definition of 'Consumer' (regulation 2)

"...“consumer” means an individual who, in contracts for payment services to which these Regulations apply, is acting for purposes other than [deleted: their] a trade, business or profession;...”

## Durable medium

**2.48** As set out in the June summary of responses (paragraph 3.45 to 3.46) the term durable medium could refer to emails and text messages, as well as paper. Some respondents suggested amending the definition of durable medium to reflect this. This approach was considered; however, as the definition under the draft regulation is medium-neutral (and so includes electronic documents that meet the definition), and to maintain consistency with other legislation, such the Distance Selling Regulations and Distance Marketing Regulations, the definition of durable medium under the Regulations remains unchanged.

## Payment account

**2.49** The June summary of responses (paragraphs 3.39 to 3.42) set out the high-level scope of the term payment account. Certain PSD provisions expressly apply to transactions involving a payment account. The Government is now working closely with industry to understand which types of accounts might be classified as payment accounts once the Regulations come into force, together with any subsequent impact. The FSA is considering what principles might be set out in its Perimeter Guidance to help payment services providers establish which types of accounts would be caught by the term ‘payment account’. The FSA Approach Document will finalise the approach to this and other issues.

## Loans

**2.50** It should be clarified that payments transacted by a financial institution where it is acting purely as a payer or payee in its own right (rather than facilitating or enabling payment transactions) do not fall into the Directive’s scope. For this reason the issuance and repayment of

<sup>(8)</sup> 2006 c.50.

<sup>(9)</sup> 2005 asp 10.

<sup>(10)</sup> 2008 c 12 (N.I.).

a pure loan or mortgage account would be out of scope of the Regulations. However, it should be noted that for current account mortgages, where payment transactions are made on the same account as the mortgage loan, the payment element would be classed as a payment account. Other accounts on which credit is provided, for example an overdraft on a current account, would also fall in scope of the PSD. It should be noted, however, that certain PSD provisions have been dis-applied to take account of consumer credit legislation.

## Payment service provider

**2.51** Sub-paragraph (g) of the definition of payment service provider in the Regulations has been modified to align it with that of the Directive, ensuring that central banks from other EEA states are also captured under the Regulations.

### Box 2.C: Definition of 'Payment Service Provider' (regulation 2)

" ...

"payment service provider" means any of the following persons when they carry out payment services—

- (a) authorised payment institutions;
- (b) small payment institutions;
- (c) EEA authorised payment institutions;

...

(g) the Bank of England, *[deleted: except]* **the European Central Bank and the national central banks of EEA States other than the United Kingdom, other than when acting in *[deleted: its]* their capacity as a monetary authority or carrying out other functions of a public nature; and ..."**

**2.52** It should be further noted that in order to distinguish between authorised payment institutions and payment institutions that meet the waiver criteria, the Regulations introduce the definitions "authorised payment institutions" and "small payment institutions". This means that only an "authorised payment institution" will need to comply with the prudential requirements and have the ability to passport its permission to other Member States.

## Money remittance

**2.53** Clarity was sought on whether the transposed definition of "money remittance" had been expanded to indicate that money or monetary value must be involved in the payment transaction. With regards to the PSD, only funds with monetary value can be caught by its provisions. The definition of money transmission in the Money Laundering Regulations 2007 remains unchanged.

## QUESTION 2: AUTHORISATION AND CANCELLATION PROCEDURES (DRAFT REGULATIONS 4 TO 12)

Q2. Do you agree with the draft regulations for authorisation of payment institutions and cancellation procedures?

**2.54** Title II of the Payment Services Directive establishes the supervisory requirements for the authorisation of (larger) payment institutions and the registration requirements for firms eligible to be waived from all or part of the prudential regime. Part 2 of the Regulations establishes the UK registration regime for payment institutions. Part 3 covers the prudential regime for authorised payment institutions. Part 4 covers general provisions applicable to both authorised and registered (i.e. small) payment institutions.

**2.55** The majority of respondents were content with the regulations under Part 2 that set out the registration process for payment institutions. Some respondents sought further clarity regarding the process and procedures firms would need to follow in order to become a registered payment institution. The FSA Approach Document will set out more detail in relation to the procedures for authorisation and registration. The FSA intends to further raise the awareness of the Regulations and their implications for various sectors by, for example, continuing with its PSD stakeholder user forum.

### Joint FSA / HMRC application process

**2.56** A few respondents sought clarity on the interplay of the payment services and money laundering application processes. Paragraph 3.18 of the July 2008 legislative consultation document stated that the FSA and HM Revenue and Customs (HMRC) would consider the scope to rationalise the application processes of the PSD and Money Laundering Regulations (MLR) for both authorised and small payment institutions to ensure, where practicable, processes are streamlined.

**2.57** At present the only sector to which such a joint application process could apply is money remittance (the great majority of which are already registered with HMRC for MLR). The FSA and HMRC have determined that a combined application process would have no advantage for these existing businesses and would only benefit an estimated maximum of 500 new businesses that might apply each year.

**2.58** Although there could be some scope for rationalisation, there are fundamental differences in the FSA and HMRC application and fees regime. Examples include the basis of charging structures, the timing of the ongoing fee renewals and the application process. In aligning these processes legislative and administrative difficulties would arise, and the costs in addressing these barriers would need to be passed onto business through fees.

**2.59** The FSA and HMRC have therefore concluded that a joint Payment Services Regulations – Money Laundering Regulations application process would not be practicable or cost effective for businesses. They are, however, continuing to work closely together to make the processes as clear and transparent as they can for jointly supervised businesses. The FSA and HMRC are developing a joined up communications plan to provide affected businesses with the necessary information in a clear and straightforward way to help these businesses to comply with both Third Money Laundering Directive and PSD requirements. The aim of both the FSA and HMRC is to make both application processes as simple as possible, consistent with their statutory responsibilities.

## Anti-Money Laundering supervisory responsibility

**2.60** Paragraph (6)(d) of Schedule 6 to the Regulations amends regulation 23(1)(d) of the Money Laundering Regulations such that HMRC will be the supervisory authority for the purpose of money laundering for money services businesses, bill payment service providers and telecommunication, digital and IT payment service providers which are not supervised by the Authority. It should be noted that, only those bill payment service providers and telecommunication operators that fall in the scope of the PSD would need to be supervised for anti-money laundering (AML) purposes.

**2.61** The MLR define a money services business as ‘an undertaking, which by way of business operates a currency exchange office, transmits money (or any representations of monetary value) by any means or cashes cheques which are made payable to customers’. It should be clarified that the only type of money service businesses that would be captured for the purpose of the PSD would be those that transmit money (or any representations of monetary value), i.e. money remitters. It should be noted that the scope of the MLR in terms of money service business remains unchanged.

**2.62** The FSA will be responsible for AML supervision of non-bank credit card issuers and merchant acquirers. There is no need to change the MLR to account for this new responsibility.

## The register

**2.63** Clarity was sought as to which legal bodies would be captured by the payment services register. The PSD obliges the FSA to publish a public register of both authorised and registered payment institutions. In the UK, this register will list all UK payment institutions together with their branches and agents that operate in the UK or (in the case of authorised payment institutions) within the EEA, as well as the payment service(s) they have been authorised or registered to provide. It will also be linked to the main FSA register, where details of credit institutions and e-money institutions, which are entitled to provide payment services as a result of their existing authorisation, can be found.

**2.64** Another respondent raised concerns that the Regulations would permit the FSA to commercially exploit the information contained in the register. The respondent believed that many registered institutions might prefer their details to be protected by the FSA as private information, in keeping with the Data Protection Act. Article 13 of the Directive provides that payment service providers, together with their agents and branches, must be entered onto a public register. The register must further identify the payment services for which the payment service provider is registered, and the natural and legal persons that have been registered. These provisions have therefore been included in the Regulations. The Financial Service and Markets Act 2000 (FSMA) currently enables the FSA to commercially exploit the information that is publicly available on its register. Regulation 4(4)(c) replicates this FSMA provision. The FSA does not propose to include information about individuals on the public part of the payment services register except where that individual is the payment institution or an agent (i.e. sole traders).

## Close links

**2.65** Regulation 6(8) (draft regulation 7(9)) provides that an applicant seeking to become a payment institution must inform the FSA of its close links (defined in regulation 6(9)) between itself and other natural or legal persons to ensure that the FSA can effectively exercise its supervisory function. In addition, authorised payment institutions will need to notify the FSA of material or significant changes to its close links in accordance with regulations 16 and 32.

**2.66** One respondent sought clarity as to how often the firm would need to submit this information. It was suggested that the guidance would need to be included in an authorised payment institution’s application pack and should be published by the FSA prior to it opening its

doors to applications. The FSA will be issuing information on notification requirements for firms in due course.

### **Right to bring early applications**

It should be noted that from 1 May 2009, under regulation 1, non-bank payment service providers will be able to submit applications to the FSA to become payment institutions. Regulation 124 further provides that applications received before 1 August 2009 must be determined before 1 November 2009. The payment services register can only be updated and come into effect on 1 November 2009.

### **Determination of applications**

**2.67** Regulation 9(1) (draft regulation 8(1)) requires the FSA to determine an application within 3 months of receipt of a completed application. Regulation 9(2) (draft regulation 8(2)) further provides for a backstop period of 12 months to determine an incomplete application. One respondent has noted that the Regulations do not set a timeframe for when the FSA should inform the applicant whether the application has been deemed complete or incomplete. The respondent has suggested that it would be prudent to apply a maximum of a 12-month period for this notification. The FSA will contact firms if it considers an application incomplete. In any event, the warning notice procedure for refusing authorisation mean that firms would have an opportunity for representations to be made before the 12-month backstop date is reached. The FSA Approach Document will provide further information on the FSA's approach to the application process.

## QUESTION 3: REGISTRATION FOR SMALL PAYMENT INSTITUTIONS (DRAFT REGULATION 13)

Q3. Do you agree with the draft regulations for registration as a small payment institution?

**2.68** Regulation 12 (draft regulation 13), which implements PSD article 26, establishes the waiver option open to Member States. It stipulates that applications to register as a small payment institution must contain such information as the FSA may reasonably require. There was broad support for the regulation implementing the waiver provision. It was believed that the regime was appropriate and clear.

**2.69** A few respondents argued that the implementation of the waiver might create an unlevel playing field between authorised and small payment institutions. They believed that the threshold level of executed payment transaction to be too high and could result in large firms being waived from the prudential requirements of the Regulations, promoting unfair competitive cost advantages.

**2.70** The Government takes note of respondents' concerns surrounding the creation of a two-tiered system. However, to impose regulatory burdens on smaller firms that transact a low volume of payments would be disproportionate and might result in these firms being priced out of the market or moving to the informal sector. This would be detrimental to consumer choice and could result in lower levels of consumer protection, in addition to compromising anti-money laundering and anti-terrorist financing policy objectives. The Government at this stage will retain the waiver thresholds provided in the Directive. However, the Government will continue to review the market to ensure that regulations remain proportionate.

**2.71** Another concern raised by one respondent was the reputational risk to an authorised payment institution resulting from the failure of a small payment institution. The public might not be aware of which service providers were operating under the waiver regime and which were not. The FSA has consulted on whether only authorised payment institutions would be able to use its logo under certain circumstances. It is also considering developing wording that small payment institutions could choose to use, whereby the consumer would be aware that an institution was registered with the FSA and able to offer payment services under the Regulations. The FSA would also expect both authorised and small payment institutions to disclose their status to the payment service user. Further details will be made available in the FSA Approach Document.

### Safeguarding

**2.72** Representatives of the remittance service sector requested an option for small payment institutions to be able to voluntarily safeguard their payment service user funds as provided by safeguarding requirements under draft regulation 22. The Government believes that this approach would provide consumers with additional protection. Draft regulation 22 (now regulation 19) has been amended accordingly, enabling, but not obliging, small payment institutions to do this as they see fit. If they do voluntarily safeguard funds, the provisions of regulation 19 will apply to them if they become insolvent in the same way as they apply to authorised payment institutions.

### Fees

**2.73** Some respondents felt that the indicative FSA fees for registered payment institutions of £500, together with the conduct of business provisions would be overburdensome for small payment institutions. It should be noted that the £500 per year registration fee in the impact

assessment, accompanying the consultation document, was a high-level estimate. The FSA has based this estimation on an initial analysis of the expenses it could incur while carrying out its regulatory functions to enforce the Regulations. The FSA is currently analysing the PSR fee structure. It intends to consult on the PSD related fees in its February 2009 Regulatory Fees and Levies consultation, giving stakeholders an opportunity to comment.

## Waiver conditions

**2.74** As small payment institutions will be unable to passport their services to another Member State, draft regulation 15(5) stipulated where firms, subject to the waiver conditions, must be located while conducting their payment services. This regulation (now regulation 13(5)) has been amended to clearly stipulate that the head office or the place of residence of the small payment institution, in which it actually carries out its business, must be located in the UK.

### **Box 2.D: Regulation 13 (previously draft Regulation 15): Conditions for registration as a small payment institution**

“...13.—(1) The Authority may refuse to register an applicant as a small payment institution only if any of the conditions set out in paragraphs (2) to (6) is not met.

...

(5) The applicant’s head office, registered office or place of residence, as the case may be, must be in the United Kingdom. ...”

## Varying the registration of a small payment institution

**2.75** The draft Regulations have been changed to enable the Authority to vary a small payment institution’s registration on its own initiative (regulation 14, which applies regulation 11 on variation of authorisation on FSA’s own initiative to registration as a small payment institution). This is intended to cover situations such as where a small payment institution breaches provisions within the Regulations on a systematic basis where under the draft Regulations the FSA’s only option would be to cancel the small payment institution’s registration entirely. This amendment should result in a more proportionate outcome for businesses where action is necessary to protect consumers.

## QUESTION 4 AND 5: PRUDENTIAL REQUIREMENTS FOR AUTHORISED PAYMENT INSTITUTIONS (DRAFT REGULATIONS 21 TO 25)

Q4. Do you agree with the approach to the implementation of the ongoing prudential requirements for authorised payment institutions, concerning the capital requirements, safeguarding provisions, accounting and audit, outsourcing, record keeping and the duty to cooperate with the competent authority?

Q5. On safeguarding in particular do you agree with the proposed £50 threshold above which providers must safeguard user funds?

### Capital requirements: initial and ongoing

**2.76** Regulations 6(3) and 18 (draft regulations 7(4) and 21, respectively) transpose articles 6, 7 and 8 of the Payment Services Directive (PSD) and set out the initial and ongoing capital requirements for authorised payment institutions in the UK. Schedule 3 defines the capital that can be used to meet these requirements.

**2.77** The majority of respondents believed that the draft regulations for initial and ongoing capital requirements were appropriate. It was felt that the policy intention of allowing firms to choose the applicable method for calculating their ongoing regulatory capital, subject to FSA agreement, was adequately transposed. Respondents further believed that the prudential requirements for authorised payment institutions were comprehensively outlined in the regulations and the associated Schedule 3.

**2.78** A few respondents continued to stress the importance of homogeneously implementing the Directive across the EU. These stakeholders tended not to be supportive of the flexible approach of allowing firms to propose their method of calculating ongoing capital. They believed that it could lead to adverse risks in payments market. It should be noted that the FSA would have the ability to impose a different method of calculation if it was felt that the one chosen by the payment institution was inappropriate in relation to its circumstances.

**2.79** One respondent questioned whether the draft regulations actually prevented firms from choosing their own method of calculating funds. It believed that the wording in Schedule 3, Part 2, paragraph 11 (“An authorised payment Institution must hold own funds in accordance with such Method A, B or C as the Authority may direct.”) may allow the Authority to determine the method of calculation.

**2.80** The PSD requires the calculation method to be determined by the competent authority. However, the FSA, as part of the authorisation process intends to ask payment service providers which calculation method they wish to initially adopt within the application pack. The FSA anticipates that it would generally follow this choice unless the information available to it indicated that it would be inappropriate.

**2.81** Another respondent was concerned that a consistent method of applying a 20 per cent variation to the own funds calculation could be difficult to achieve, as payment institutions may pursue a number of diverse business models. The Government believes that the application of the provision, which will be at the discretion of the Authority, would be applied to mitigate risks and to ensure that there is a proportionate regulatory outcome.

### Safeguarding

**2.82** Draft regulation 22 addressed the PSD safeguarding requirements (PSD article 9) and established the legal requirements underpinning the policy options that were adopted by the Government during the policy consultation phase.

**2.83** Several respondents provided suggested modifications to the draft Regulations in order to fully achieve the policy intentions that were set out in the June summary of responses and the July legislative consultation documents. After further work with the Insolvency Service and the Accountant in Bankruptcy the safeguarding requirements have been amended to ensure that they not only implement the policy intentions but are also in line with current insolvency procedures.

**2.84** Respondents sought clarity on which type of account the safeguarded funds could be kept in. The Government believes that firms forming part of a larger group would have to safeguard their users' funds in an account separate from the group's other activities (where they are not covered by an insurance policy in accordance with regulation 19(9)). In particular, the Regulations provide that any users' funds held at the end of the business day must be safeguarded in a separate account. This is so that, in the event that the payment institution within the group becomes insolvent, the users' funds would be clearly distinct from other activities of the firm or the group and easily available to meet the claims of payment service users. Payment institutions would be able to place funds in authorised credit institutions, as defined in the Banking Consolidation Directive (i.e. with EEA authorised credit institutions or branches of third country credit institutions), provided that this would be in line with the protection given to safeguarded funds. Payment institutions would not, however, be able to place funds in a third country credit institution without an EEA-authorised branch.

### **Safeguarding threshold**

**2.85** As part of the legislative consultation views were requested on whether to lower the threshold above which user funds must be safeguarded from €600 to £50. The majority of respondents supported the Government's intended approach of reducing the threshold from €600 to £50. They believed that the harmonisation of thresholds (i.e. with the Consumer Credit Act and the user liability provision) should make the liabilities and rights for payment service users easier to understand. The Government concludes that it will implement a safeguarding threshold of £50, whereby authorised payment institutions would have to safeguard user funds above £50. Industry could, however, choose to simply safeguard all user funds regardless of the threshold.

## Box 2.E: Regulation 19 (previously Regulation 22): Safeguarding requirements

### Safeguarding requirements

19.—(1) For the purposes of this regulation “relevant funds” comprise the following—

- (a) sums received from, or for the benefit of, a payment service user for the execution of a payment transaction; and
- (b) sums received from a payment service provider for the execution of a payment transaction on behalf of a payment service user.

(2) Where—

- (a) only a portion of the sums referred to in paragraph (1)(a) or (b) is to be used for the execution of a payment transaction (with the remainder being used for non-payment services); and
- (b) the precise portion attributable to the execution of the payment transaction is variable or unknown in advance,

the relevant funds are such amount as may be reasonably estimated, on the basis of historical data and to the satisfaction of the Authority, to be representative of the portion attributable to the execution of the payment transaction.

(3) Where the relevant funds in respect of a payment transaction exceed £50, an authorised payment institution must safeguard such funds in accordance with either—

- (a) paragraphs (4) to (8); or
- (b) paragraphs (9) and (10).

(4) An authorised payment institution must keep relevant funds segregated from any other funds that it holds.

(5) Where the authorised payment institution continues to hold the relevant funds at the end of the business day following the day on which they were received it must—

- (a) place them in a separate account that it holds with an authorised credit institution; or
- (b) invest the relevant funds in such secure, liquid assets as the Authority may approve (“relevant assets”) and place those assets in a separate account with an authorised custodian.

(6) An account in which relevant funds or relevant assets are placed under paragraph (5) must—

- (a) be designated in such a way as to show that it is an account which is held for the purpose of safeguarding relevant funds or relevant assets in accordance with this regulation; and
- (b) be used only for holding those funds or assets.

(7) No person other than the authorised payment institution may have any interest in or right over the relevant funds or relevant assets placed in an account in accordance with paragraph (5)(a) or (b) except as provided by this regulation.

(8) The authorised payment institution must keep a record of—

- (a) any relevant funds segregated in accordance with paragraph (4);
- (b) any relevant funds placed in an account in accordance with paragraph (5)(a); and
- (c) any relevant assets placed in an account in accordance with paragraph (5)(b).

(9) The authorised payment institution must ensure that—

- (a) any relevant funds are covered by—

- i. an insurance policy with an authorised insurer;
  - ii. guarantee from an authorised insurer; or
  - iii. a guarantee from an authorised credit institution; and
- (b) the proceeds of any such insurance policy or guarantee are payable upon an insolvency event into a separate account held by the authorised payment institution which must—
- i. be designated in such a way as to show that it is an account which is held for the purpose of safeguarding relevant funds in accordance with this regulation; and
  - ii. be used only for holding such proceeds.

(10) No person other than the authorised payment institution may have any interest in or right over the proceeds placed in an account in accordance with paragraph (9)(b) except as provided by this regulation.

(11) Subject to paragraph (12), where there is an insolvency event—

- (a) the claims of payment service users are to be paid from the asset pool in priority to all other creditors; and
- (b) until all the claims of payment service users have been paid, no right of set-off or security right may be exercised in respect of the asset pool except to the extent that the right of set-off relates to fees and expenses in relation to operating an account held in accordance with paragraph (5)(a) or (b) or (9)(b).

(12) The claims referred to in paragraph (11)(a) shall not be subject to the priority of expenses of an insolvency proceeding except in respect of the costs of distributing the asset pool.

(13) Paragraphs (11) and (12) shall apply to any relevant funds which a small payment institution (or an authorised payment institution in relation to relevant funds of £50 or less) voluntarily safeguards in accordance with either paragraphs (4) to (8) or paragraphs (9) and (10).

(14) An authorised payment institution (and any small payment institution which voluntarily safeguards relevant funds) must maintain organisational arrangements sufficient to minimise the risk of the loss or diminution of relevant funds or relevant assets through fraud, misuse, negligence or poor administration.

(15) In this regulation—

“asset pool” means—

- (a) any relevant funds segregated in accordance with paragraph (4);
- (b) any relevant funds held in an account in accordance with paragraph (5)(a);
- (c) any relevant assets held in an account in accordance with paragraph (5)(b); and
- (d) any proceeds of an insurance policy or guarantee held in an account in accordance with paragraph (9)(b);

“authorised insurer” means a person authorised for the purposes of the 2000 Act to effect and carry out a contract of general insurance as principal or otherwise authorised in accordance with Article 6 of the First Council Directive 73/239/EEC of 24th July 1973 on the business of direct insurance other than life insurance<sup>(11)</sup>, other than a person in the same group as the authorised payment institution;

“authorised credit institution” means a person authorised for the purposes of the 2000 Act to accept deposits or otherwise authorised as a credit institution in accordance with Article 6 of the banking consolidation directive other than a person in the same group as the authorised payment institution;

“authorised custodian” means a person authorised for the purposes of the 2000 Act to safeguard and administer investments or authorised as an investment firm under Article 5 of Directive 2004/39/EC of 12th April 2004 on markets in financial instruments<sup>(12)</sup> which holds those investments under regulatory standards at least equivalent to those set out under Article 13 of that directive;

“insolvency event” means any of the following procedures in relation to an authorised payment institution or small payment institution—

- (a) the making of a winding-up order;
- (b) the passing of a resolution for voluntary winding-up;
- (c) the entry of the institution into administration;
- (d) the appointment of a receiver or manager of the institution’s property;
- (e) the approval of a proposed voluntary arrangement (being a composition in satisfaction of debts or a scheme of arrangement);
- (f) the making of a bankruptcy order;
- (g) in Scotland, the award of sequestration;
- (h) the making of any deed of arrangement for the benefit of creditors or, in Scotland, the execution of a trust deed for creditors;
- (i) the conclusion of any composition contract with creditors; or
- (j) the making of an insolvency administration order or, in Scotland, sequestration, in respect of the estate of a deceased person;

“insolvency proceeding” means—

- (a) winding-up, administration, receivership, bankruptcy or, in Scotland, sequestration;
- (b) a voluntary arrangement, deed of arrangement or trust deed for the benefit of creditors; or
- (c) the administration of the insolvent estate of a deceased person;

“security right” means—

- (a) security for a debt owed by an authorised payment institution or a small payment institution and includes any charge, lien, mortgage or other security over the asset pool or any part of the asset pool; and
- (b)** any charge arising in respect of the expenses of a voluntary arrangement.

<sup>(11)</sup> OJ No L 228, 16.8.1973, p.3.

<sup>(12)</sup> OJ No L 145, 30.4.2004, p.1.

## Small payment institutions

**2.86** As stated in paragraph 2.71 regulation 19 has been changed in order to permit a small payment institution to have the option of voluntarily safeguarding users' funds under the same terms that apply to authorised payment institutions.

## Accountant and audit, and record keeping

**2.87** Draft regulation 23 (PSD article 15) required authorised payment institutions, if undertaking other non-payment service activities, to provide separate accounting information to the FSA with respect to its payment service activities. Draft regulation 25 (PSD article 19) specified that authorised payment institutions must keep relevant records for at least five years.

**2.88** One respondent was concerned that the draft regulations did not clearly state the type of information that firms need to retain. Depending on the information requirements some sectors might not be able provide all the information required, as certain products operate on an anonymous basis.

**2.89** The type of records that would need to be kept should demonstrate the payment institution's compliance with the prudential parts of the Regulations. These would include the capital requirements, safeguarding requirements, accounting and statutory audit, and outsourcing. The anonymous operation of products is unlikely to impact on the record keeping requirements relating to these areas. It should be noted that payment institutions will need to make a judgement as to what information they need to retain to demonstrate that they have complied with the relevant requirements. The FSA Approach Document will further outline the information that would need to be provided to the Authority.

**2.90** The respondent raised further concerns relating to the requirement to keep records for 5 years. Currently under card scheme rules transaction information is retained for around 2 years and in line with accounting standards other information, depending on type, up to 7 years. If records need to be kept for 5 years, the respondent believed that additional costs and contractual burdens (if this activity has been outsourced) might be placed on payment service providers.

**2.91** Article 19 of the PSD, states that the record keeping provision should not prejudice national law, which would mean that records should be kept for a minimum of 5 years, subject to national requirements to maintain records for a longer (but not shorter) period. The regulation (now regulation 22) has been amended accordingly.

## Outsourcing

**2.92** Draft regulation 24 stipulated that authorised payment institutions must notify the FSA of their intention to outsource any operational functions of their payment service business. The majority of respondents found the regulations concerning this provision to be appropriate.

## QUESTION 6: PASSPORTING (DRAFT REGULATIONS 26 TO 31)

Q6. Do you agree with the draft regulations for the implementation of the passporting rights and obligations?

**2.93** Draft regulations 26 and 27 set out the procedures for a payment institution to exercise its passport right to provide services including through the establishment of a branch in another Member State. The majority of respondents believed that the transposition of this provision was appropriate. The effect of the draft provisions has been reproduced in the final Regulations with some changes that are only formal.

### Granting of credit

**2.94** In relation to the granting of credit, payment institutions will be subject to the provisions of UK consumer credit legislation when granting credit within the UK. UK authorised payment institutions should be able to passport their credit granting in relation to payment services which are provided into another Member State without having to adhere to further licensing requirements of the host Member State, but would, as at present, be required to have an OFT consumer credit licence. They are also likely to have to comply with consumer credit rules in that state. Payment service users in the host Member State must repay the credit granted by such payment institutions within 12 months, when such credit is passported.

**2.95** Firms passporting into the UK would not be required to have an OFT licence, on the basis that such firms are already authorised in accordance with the PSD in their home Member State. However, they would be required to comply with consumer credit legislation in the UK. It should be noted that the PSD does not provide for the passporting of any other additional non-payment service activity.

**2.96** At a European level, Member State PSD authorities are due to meet early in 2009 to discuss their approach to passporting. Any conclusions reached from these discussions, where appropriate, will feed into the FSA Approach Document.

## QUESTION 7: GENERAL PROVISIONS FOR PAYMENT INSTITUTIONS (DRAFT REGULATIONS 32 TO 36)

Q7. Do you agree with the draft regulations for the general provisions for payment institutions, which concern the activities that may be undertaken, the provision of payment accounts, and the use of agents?

### Payment Account

**2.97** Draft regulations 32 and 33 reflected article 16 of the Payment Services Directive (PSD) and concerned the activities and ancillary services payment institutions (authorised and small) may undertake. They also stipulated that payment institutions may only hold payment accounts used exclusively for payment transactions. The majority of respondents believed that the regulations clearly described and transposed article 16.

### Merchant acquirer

**2.98** One respondent stated that merchant acquirers are beginning to have business models that do not involve an account for making payments. Although this may be the case, point 5 of the PSD annex clearly states that acquiring is a payment service caught by the PSD. All merchant acquirers, regardless of whether or not they hold payment accounts, are therefore in scope of the PSD. As noted previously, the FSA will be responsible for the anti-money laundering (AML) supervision of non-bank merchant acquirers. Furthermore, it should be noted that merchant acquirers will be subject to FOS jurisdiction and FSA complaint handling rules in relation to the services they provide.

### Agents

**2.99** Draft regulation 34 (PSD article 17) set out the UK procedures for dealing with the agents of payment institutions. Respondents generally agreed that the regulation would adequately implement PSD article 17. The provision about the use of agents is at regulation 29 of the Regulations.

**2.100** One respondent requested clarity on the scope of the regulation governing the registration of agents. Under the Regulations, UK payment institutions would have to inform the FSA of all of their agents throughout the European Economic Area (EEA), and these would appear on the FSA's register together with the payment service(s) the payment institution has been authorised to provide. An EEA (which is a non-UK authorised) payment institution would have to inform its own competent authority about its agents that operate in the UK and their AML compliance. Their home competent authority would then inform the FSA of the EEA firm's agent network in the UK.

**2.101** If a UK payment institution were to have agents in a third country (i.e. a non EEA country), then there would be no requirement under the Regulations to inform the FSA of these agents for the purpose of registering them. However, the fact a firm operates in third countries may be relevant to a firm's authorisation application. Also, a franchise, depending on its legal identity, would be treated as either a branch or an agent. If the franchise has a separate legal status to its principal, then it would be treated as an agent of the principal.

**2.102** One respondent questioned whether agents of an EEA payment institution would be subject to AML controls of the FSA (regulation 34(2)(b)(ii)(bb)) rather than HMRC. It should be emphasised that regulation 29 of the PSR does not alter the supervision arrangements under the MLR.

**2.103** Clarity was sought on the timeframe the FSA would have under regulation 35(b) (now regulation 29) to assess whether it intended to include the agent in the register. Further information on processing of agent applications will be provided in the FSA Approach Document.

### **Power to de-register agents**

**2.104** In the draft Regulations, if agents were not compliant with the registration provisions on a continuing basis, for instance the directors and persons responsible for the management of the agent were not fit and proper, the Authority was limited in the action it could take in relation to the agent. To make the regime more effective, the Regulations have been changed so that the FSA would be able to remove a non-compliant agent from the register in accordance with regulation 30.

### **Duty to notify of change in circumstance**

**2.105** The PSD establishes a duty to inform the Authority of changes in circumstance “without undue delay”. Respondents sought clarity on the timeframe relating to “without undue delay” (at regulation 13 and 32; draft regulation 15 and 36 respectively). The FSA Approach Document will outline the meaning of “without undue delay”.

## QUESTION 8: ACCESS TO PAYMENT SYSTEMS (DRAFT REGULATIONS 96 TO 109)

Q8. Do you agree with the draft regulations in relation to article 28 of the PSD on access to payment systems including the investigation powers to be assigned to the Office of Fair Trading (OFT) and the associated enforcement provisions?

**2.106** Part 8 of the Regulations transposes article 28 of Title II of the Payment Services Directive (PSD), which concern access to payment systems. The majority of respondents generally considered the intentions of the Directive, in relation to access criteria for payment systems, were transposed adequately by the draft regulations. They further believed that the powers assigned to the Office of Fair Trading (OFT) for investigation and enforcement were in line with standard provisions of a similar nature and that the assigned powers would enable the OFT to apply a consistent approach within the UK.

**2.107** One respondent, however, raised concerns about provisions under draft regulation 100 which provided that if a person refused or failed to comply with an information request under draft regulation 99, the OFT could refer the matter to the High Court which could treat the refusal or failure as contempt of court, for which the penalty could potentially be a term of imprisonment.

**2.108** The regulation has been reviewed (regulation 104) and a more proportionate regime implemented. In particular, the contempt of court provision has been replaced with a provision whereby, on an application by the OFT under regulation 100, the court may make an order requiring the defaulter to provide the information or otherwise take steps to remedy the consequences of the failure to provide the information.

### OFT enforcement

**2.109** One respondent requested further clarity on the determining procedures that the OFT would use to assess whether the rules governing access to payment systems were fair. The respondent further requested information on the right to appeal and the structure of the fining regime.

**2.110** Under regulation 105 the OFT may impose such penalty as it considers appropriate. This is in line with similar powers under the Competition Act 1998. There is a right of appeal to the Competition Appeal Tribunal from either a decision by the OFT to give a direction or the imposition of a penalty. The OFT's approach to regulating the provisions on access to payment systems and the right to an appeal will be outlined on its website, as well as within the FSA Approach Document.

### Role of the Bank of England

**2.111** In the June 2008 summary of responses, it was concluded that the OFT in investigating a complaint against a payment system's access rules would liaise with the Bank of England to check whether the relevant access conditions were justified (and if necessary, have been applied) on the grounds of protecting the financial and operational stability of the payment system. To effect this intention draft regulation 102 (now regulation 98) has been amended to include a duty on the OFT to consult the Bank of England when investigating a possible breach of regulation 97(1)(b)(ii) – that rules governing access to a payment system must not prevent or restrict access more than is necessary to protect the financial and operational stability of the payment system. This regulation follows a similar legislative model provided in Financial Markets and Insolvency (Settlement Finality) Regulations 1999.

**2.112** It should be noted, however, that the Bank of England does not have any regulatory responsibility with regard to the PSD.

### **Faster payments**

**2.113** It should also be noted that the Faster Payments Scheme is seeking to be designated in accordance with the Settlement Finality Directive by November 2009. Once it receives its designation it will no longer fall under Part 8 of the regulations.

## QUESTION 9 AND 10: APPLICATION (DRAFT REGULATIONS 37 TO 39)

Q9. Do you agree with applying the stated scope of the PSD to the Payment Services Regulations? What do you think would be the likely regulatory impact of extending the scope?

Q10. Do you agree with the draft regulations to implement the PSD derogation for low value payments from some of the information requirements?

**2.114** Part 5 of the Regulations transposes the information and transparency provisions provided by Title III of the Directive. Under these regulations payment service providers are obliged to provide certain information to their customers about the payment service being provided.

### Scope

#### One leg out transactions

**2.115** PSD article 2 provides that Title II will apply to all establishments in the European Economic Area (EEA) whether operating only in the EEA or sending money out of the EEA. Titles III and IV will apply to payment services and associated transactions within the Community, with the exception of Article 73 which concerns value dating, and which should be applied to all transactions.

**2.116** The UK Remittance Task Force (UK RTF), a private sector-led, DFID funded body, responded in continued support of the Commission Service's proposal of extending the scope of the conduct of the business requirements to payment transactions to or from a non-EEA country (i.e. one leg out transactions). The Task Force believed that this extension of scope would provide customers, in particular migrants who remit to destinations outside the EEA, with increased transparency of information on, for example, charges and exchange rates; as well as greater certainty on the execution of their payment transactions.

**2.117** The Task Force further believed that jurisdictional issues could be resolved by payment service providers conducting due diligence before signing any agreements with third country agents. Through this agreement, the payment service provider would then be responsible for ensuring that their agents were compliant with the Directive.

**2.118** One other respondent also supported the Commission Service's proposal. It argued that an increasing number of EEA citizens used online providers (some of which were located outside the EEA) to conduct payment transactions. These transactions should be protected as if they were executed within the EEA borders.

**2.119** A significant number of other respondents were strongly opposed to extending the scope of the conduct of business provisions to one-leg out transactions, primarily for workability reasons. The trade associations that represent the majority of UK money remitter service providers felt that their members could reasonably satisfy the Directive's information requirements that were in line with the Remittance Charter, developed by the UK RTF, so that consumers making payment transactions from the UK to non-EEA country would similar receive transaction information to those making payments within the EEA. They noted that a significant number of their members have adopted the Charter. In contrast, they did not believe it would be feasible for their members to comply with the Title IV rights and obligation provisions, such as the guaranteeing of execution times.

**2.120** Other respondents believed that if equivalent protection and information had to be given to all payment transactions, regardless of where the payment was being sent or originated from,

then substantial payment infrastructure changes would be required. Respondents also raised concerns that UK payment service providers, for compliance purposes, would become dependent on payment service providers outside the EEA.

**2.121** Although the Government recognises the need to provide sufficient levels of protection to all customers that use payment services, it believes that there should be a balance between consumer protection and workability. The Government encourages all payment service providers to adopt and adhere to the Remittance Customer Charter so that customers receive transparent payment transaction information. Additionally, from a customer protection perspective, the Financial Ombudsmen Service (FOS) currently handles complaints for one-leg payment transactions executed by a credit institution. The FSA and FOS have proposed extending FOS's jurisdiction to include one-leg transactions that have been executed by non-bank payment service providers. In determining a complaint, the FOS would refer to what is fair and reasonable in all the circumstances of the case. It would take into account the relevant law and regulations, regulators' rules, guidance and standards, codes of practice, and (where appropriate) good industry practice, such as the Remittance Customer Charter, at the relevant time.

**2.122** The Government concludes, for the present, that the scope of the conduct of business provisions, with the exception of value dating, should only cover payments transacted within the EEA (i.e. two-leg transactions).

### **Micro-enterprise**

**2.123** Respondents believed that the draft regulations transposed the Government's approach to the treatment of the micro-enterprises adequately.

**2.124** Draft regulation 37(5) permitted payment service providers to contractually agree that their users would have a duty to inform them at the outset whether they are a micro-enterprise and of any subsequent change in status. Following further analysis, this provision has been deleted from the Regulations. It has been considered that a duty to inform of any subsequent change in status may be contained within the contract between the payment service provider and user, without a need to specify this duty in the Regulations.

**2.125** Payment service providers could also require charities to inform the provider of its change in status, within their contracts, whether it be due to passing the turnover threshold or its charitable status.

**2.126** A few respondents suggested that it would be helpful for the Authority to provide guidance detailing the definition of a micro-enterprise in terms of, for example, headcount and turnover, so that both parties - the firm and the payment service provider - could determine a firm's status. This is being considered by the FSA.

**2.127** Some other respondents questioned how fluctuations in the exchange rate between Sterling and the Euro would impact on the financial threshold applicable in determining whether an entity is a micro-enterprise. Since the test for being a micro-enterprise is applied at the time of entering into the contract, there is no need for an ongoing assessment. However, it is anticipated that, in practice, most payment service providers will operate using higher thresholds to ensure that the test they apply to determine status does not fluctuate frequently.

**2.128** Some respondents raised concerns that by treating micro-enterprises as consumers, some payment service providers would face a complex legislative environment impacting on current relationships between providers and commercial consumers, and specific product offerings to micro-enterprises. Other respondents believed that while consumers should receive the benefit of a higher level of protection, micro-enterprises enjoyed sufficient negotiating power, thereby allowing for the prevalence of contractual freedom with respect to the application of Titles III and IV.

**2.129** The Government has not altered its policy decision on micro-enterprises that was agreed as part of the December 2007 policy consultation.

### **Low value instruments**

**2.130** In the June 2008 summary of responses it was concluded that the low value instruments, determined by value thresholds for individual transactions, would not be subject to certain PSD information provisions. The majority of respondents supported transposition of the low value instrument provisions and believed the draft legislation met the policy intentions.

**2.131** There was general support for the value thresholds detailed in draft regulation 55 as the provisions were in line with similar thresholds placed on current pre-paid products. One respondent, however, questioned how fluctuations in the exchange rate between Sterling and the Euro would impact on the value threshold applicable in determining whether the instrument can be categorised as low value. The FSA recognises that this is a problem for payment service providers and would expect them to take a reasonable and consistent approach to dealing with fluctuations in exchange rates in relation to low value payment instruments.

### **PSD overlap with consumer credit legislation**

**2.132** In January 2008, the Consumer Credit Directive (CCD) was adopted by the European Parliament and the Council. This Directive will be implemented by June 2010. In the PSD there are number of provisions that overlap with the current consumer credit legislation and the recently adopted CCD. The Government has taken the approach that where there is a conflict between the PSD and consumer credit provisions, consumer credit legislation, either provided by the Consumer Credit Act 1974 (CCA) or the Directive, will take precedence. To effect this approach, regulation 34 (draft regulation 38) dis-applies certain information provisions in cases of consumer credit agreements:

- Prior general information for framework contracts (regulation 46(4))
- Changes to contractual information (regulation 47)
- Termination of framework contracts (regulation 48)

**2.133** When the CCD is implemented the Regulations may need to be amended in due course to bring them into line with the CCD. For example, there will need to be consideration of article 13(2) of CCD, which concerns the provision of information in relation to open-ended credit agreements.

**2.134** The majority of respondents were supportive of this approach. They believed that it would minimise the risk to payment service providers of having to make two sets of system changes within a short period of time and would provide legislative simplicity.

**2.135** A few respondents queried how the regulation would apply to 'partly regulated' and 'unregulated' credit agreements. The respondents noted that the CCA exempts low risk agreements from its provisions. They argued that if the regulation were to dis-apply only certain provisions for regulated agreements, then stricter standards would be imposed on low risk agreements (partly or un- regulated agreement). As one of the PSD objectives is to improve consumer protection, the regulation will only dis-apply the provisions for regulated contracts. Consumers with partly regulated or unregulated credit agreements would therefore receive the level of protection afforded to them under the Regulations.

**2.136** Other respondents raised concerns about the treatment of micro-enterprises under the overlapping provisions. Under the consumer credit legislation, certain micro-enterprises will enter into 'regulated agreements' as they will be 'individuals' under the meaning of the CCA;

others will not. Those micro enterprises not covered by the CCA regulated agreements will receive the protection offered to them under the Regulations.

## Framework contracts

**2.137** A few respondents raised concerns about the requirement under draft regulation 45 for payment service providers to give 2 months notice if they were to vary the payment services within the agreed framework contract. Regulation 42(2) provides that on agreement of the terms of the framework contract a payment service provider could unilaterally make a change to the framework contract provided the payment service user does not, before the proposed change, notify the provider to the contrary.

**2.138** In circumstances where a user does not notify its provider that it does not accept the change within the two-month period, the provider can effect the change two months from the date the provider notified the user of the change. If a user does not agree with the proposed change, it could either cancel its contract with the provider or accept the change.

**2.139** A few respondents questioned the implication of the two-month notice requirement on certain instruments, such as credit limits, overdraft limits and interest rates, that are linked to a payment account. Respondents from the banking sector raised concerns that if the two months notice requirement applied to credit and overdraft limits, the management of a bank's credit exposure and ability to lend responsibly could be compromised.

**2.140** PSD article 55 permits payment service providers to block instruments in certain circumstances including where the payment instrument has a credit line and where there is a significantly increased risk that the payer may be unable to fulfil its liability to pay. This has been implemented in regulation 56(2)(c). If a bi-lateral agreement could not be reached between the user and the provider to reduce credit and overdraft limits, a provider would therefore be able to block any payment instruments associated with the account, provided the condition at regulation 56(2)(c) is met.

**2.141** It has been confirmed by the Commission that changes in interest rates on an account should be considered as being changes to the underlying account. Variations in interest rates and exchange rates can be applied immediately and without notice on condition that such a right is agreed within the framework contract between the user and provider, and the changes are based on a reference interest or exchange rate provided to the payment service user; or the changes are more favourable to the payment service user. If, however, the spread of the interest rate (i.e. the proportion by which the rate is calculated based on a reference rate) were to change, then providers would be subject to the two-month notice requirement.

## Termination

**2.142** Respondents broadly supported the transposition of the termination provision. It should be clarified that although the providers would normally have to give two months notice prior to terminating a contract, this is without prejudice to any right of a party to treat the contract as unenforceable or void (for example if there has been a fundamental breach of the contract)(regulation 43(7)).

## Dynamic currency conversion

**2.143** Dynamic currency conversion (DCC) is a service by which a payment transaction in a currency other than the currency of the payment account (e.g. a transaction denominated in Euro on an account in Sterling) is converted so that the debit received by the user will be in the currency of the account. This service is typically offered on card based payment transactions and by a person other than card issuer (i.e. third party); examples would include a retailer or the withdrawal of cash from an ATM.

**2.144** PSD article 49 (regulation 49) details the information that a person offering such a service should provide. During the EU-level transposition discussions it has been clarified that DCC provided at ATMs, other than those of the card issuer, would not fall within the wording of article 49. Despite this conclusion, it should be noted that under UK LINK scheme rules all ATM operators within the scheme are required to comply with the DCC provisions of article 49. Therefore, UK ATM users are able to see the exchange rate and charges, and are able to confirm their acceptance before authorising a transaction.

## **Charges**

**2.145** Draft regulations 47 to 49 (now regulations 44 to 46) established the information provisions in relation to the execution of payment transactions. They required the provider to provide a breakdown of charges for a transaction. As the charging structure follows the SHARE principle (unless there is a currency conversion involved), whereby the charge is borne by both payer and payee providers, the payer's provider would only need to provide the payer with the breakdown charges it will place on the transaction.

## **Information for the payer after receipt of a payment order**

**2.146** One respondent sought clarity as to whether the PSD obliges payment service providers to provide the payer with information about the recipient (payee) of a payment transaction, in particular regarding remittance transactions. The respondent noted certain instances where the payer has been a victim of fraud, when a fraudulent person has acted as the payee.

**2.147** Under the PSD, payment service providers are required to provide the payer (and payee) with certain information before and after a transaction, including the date of receipt of a payment order. The Directive, however, does not specify that the provider must inform the payer of the payee's identity details. As the PSD is a maximum harmonising Directive, it is not possible to require payment service providers to inform the payer of additional payee details under this legislation.

## QUESTION 11 AND 12: APPLICATION (DRAFT REGULATIONS 53 TO 55)

Q11. Do you agree with applying the stated scope of the PSD to the Payment Services Regulations, or do you think that the UK should go further and require providers to also comply with some or all of the PSD conduct of business requirements in Title III for one-leg out transactions?

Q12. Do you agree with the draft regulations to implement the PSD derogation for low value payments from certain rights and duty requirements?

**2.148** Part 6 of the Regulations transposes Title IV of the Payment Services Directive (PSD), and relates to the rights and obligation of payment service providers and of payment service users.

### Scope

#### One-leg out transactions

**2.149** As per paragraph 2.114, the Government concludes that it will not extend the scope of the Part 6 to one-leg out transactions, with the exception of the value dating provision. The Financial Ombudsman Service (FOS) and the Financial Services Authority (FSA) have proposed to include one-leg transactions under FOS's jurisdiction. In March 2009, the FSA and FOS are expected to publish their finalised policy.

#### Micro-enterprises and charities

**2.150** The provisions of Part 6 will apply to all consumers, micro-enterprises and charities alike. A provider would be able to include within the terms of their contract with their users that micro-enterprises and charities would have to inform it if their status were to change.

#### Low value payment instruments

**2.151** Respondents generally supported the transposition of the low value instrument provision (PSD article 54) and believed that the draft regulations reflected the policy intentions well.

**2.152** One respondent sought clarity on how the value thresholds could be protected from the fluctuating exchange rates between Sterling and the Euro. The FSA recognises that this is a problem for payment service providers and would expect them to take a reasonable and consistent approach to dealing with fluctuations in exchange rates in relation to low value payment instruments.

### PSD overlaps with the Consumer Credit Directive and current consumer legislation

**2.153** The Government has taken the approach that where the PSD and current consumer credit legislation or the recently adopted Consumer Credit Directive overlaps, consumer credit would take precedent, unless consumer protection is compromised. In accordance with that approach, draft regulation 54 dis-applied various provisions, where a regulated consumer credit agreement is in place. Draft regulation 54 has been amended (now regulation 52) to apply various provisions of the Consumer Credit Act 1974 in place of the following regulations:

- the prohibition on the sending of unsolicited payment instruments (regulation 58(1)(b));
- notification of unauthorised or incorrectly executed payment transactions (regulation 59);

- payment service provider's liability for unauthorised payment transactions (regulation 61); and;
- payer's liability for unauthorised payment transactions (regulation 62);
- Information requirements where a payment instrument is blocked (regulation 56(3) to (6)).

## QUESTION 13: AUTHORISATION OF PAYMENT TRANSACTIONS (DRAFT REGULATIONS 56 TO 81)

Q13. Do you agree with the proposed regulations for implementing the PSD Title IV rights and obligations in relation to authorisation of payment transactions? Is any further detail needed?

### Transaction times

**2.154** A few respondents sought clarity on the application of the transaction times of D+1. The D+1 time frame requires a payer's payment service provider to credit the funds to the payee's payment service provider's account by the close of business the next business day after the transaction was initiated. There are further obligations on the payee's payment service provider to value date by the end of the business day, and immediately put the funds at the payee's disposal, after the funds are received by the payee's payment service provider.

**2.155** Before 1 January 2012 the payment service user, as a payer, can agree with its payment service provider to extend the transaction period by which funds are credited to the payee's payment service provider's account from one business day to three. It should be noted that the user and its provider must bi-laterally agree this extended time period. In the absence of such agreement, the D+1 requirement will apply.

### Merchant acquirers

**2.156** Some respondents sought clarity on how the transaction time requirements could be applied to the merchant acquiring model. In order for a merchant to receive funds from card transactions two payment transactions typically take place: one from the card issuer to the acquirer, and a further one from the acquirer to the merchant. Each of these two transactions will need to comply with the transactions times of D+1. When a merchant acquirer requests the transaction from an issuer, the payment must be transacted in D+1. The merchant acquirer can then hold these funds in a payment account on behalf of the merchant. However, contractual freedom between the merchant acquirer and merchant would then determine when the acquirer makes the payment to the merchant. On the agreed date the payment needs to be transacted with the transaction times provided in the PSD. Further details of this will be provided in the FSA's Approach Document.

### Surcharging

**2.157** One respondent sought clarity on whether the issuers of e-money products, such as pre-paid cards, could continue to charge for the use of an e-money instrument to, for example, withdraw cash from ATMs, under the PSD. In the UK, the Regulations will continue to permit surcharging.

**2.158** Another respondent questioned whether the Regulations should refer to the Price Discrimination Order 1990. Having reviewed the wording of the Order, it is not considered that the Regulations are in conflict with this legislation and therefore there would be no need to refer to this Order.

**2.159** As independent ATMs are exempt from the PSD they do not need to provide information on charges as detailed in the Directive. LINK scheme rules, however, require all UK ATM operators to adhere to equivalent provisions, and therefore UK independent ATM operators will continue to provide transparent charging information. Under the Regulations, issuers of payment instruments will be able to continue to charge for the use of their instrument at certain third parties, including ATMs.

## Direct Debit Guarantee and refunds

**2.160** Under the PSD a payment service user has 8 weeks from the date on which the funds were debited to request a refund for an authorised payment transaction and 13 months for an unauthorised transaction. As this provision must be implemented in the Regulations, certain instruments, such as the Direct Debit Guarantee Scheme, could be legally limited.

**2.161** The Government continues to request industry to go further than the PSD and retain the unlimited Direct Debit Guarantee, which is currently administered on a voluntary basis. This is possible, as the PSD enables providers to always do better than the Directive with respect to consumer protection. The Payments Council, (the organisation that sets strategy for UK payments), as part of its National Payments Plan is currently reviewing whether the Direct Debit Guarantee should be limited and is due to report its decision shortly.

**2.162** PSD Article 60 provides that a payment service user would be able to receive an immediate refund for unauthorised transactions as soon as it had informed its provider. It has been clarified during EU-level discussions that, if the payment service provider suspects first-party fraud, then the provider would be able to investigate the claim. If the provider's investigation concluded that no first-party fraud had taken place, then the provider will have to refund the funds immediately together with any interest.

## Payer's liability

**2.163** In the June summary of responses the Government concluded that the payer liability threshold for unauthorised payment transactions would be set at £50, to maintain existing UK standards of consumer protection, while guarding against the risk of moral hazard. To further align this threshold with previous and existing provisions, the Government has reduced this threshold to zero (i.e. zero liability) for purchases bought through the means of distance selling e.g. over the internet (regulation 62(3)). This will align the Regulations with the distance-selling regime in respect of consumer credit and will otherwise make the Regulations the sole source of liability in this area following the revocation by the Regulations of equivalent provisions in the Consumer Protection (Distance Selling) Regulations 2000. This is for the sake of legislative clarity.

## Value dating and availability of funds

**2.164** A few respondents queried the application of the value dating provision, in particular how funds could be given value and made available during a non-business day. During EU-level transposition meetings it has been concluded that if funds were transacted to the payee's provider on a non-business day, then this provider would have until the next business day to complete the transaction. This would take into account, for example, varying bank holidays across the EU and cash placed in night safes.

## QUESTION 14: COMPETENT AUTHORITY (DRAFT REGULATIONS 82 TO 95)

Q14. Do you agree with the proposed duties and powers assigned to the competent authority for the effective supervision and enforcement of the draft regulations?

**2.165** The majority of respondents believed that duties and powers placed on the Financial Services Authority (FSA), as the Authority responsible for most aspects of the Payment Services Directive (PSD), within the draft Regulations were in line with the existing provisions within the Financial Services and Markets Act 2000 (FSMA). The approach taken regarding the duties and powers has been regarded as sensible. Respondents felt that a move away from current practices would seem contrary to the overarching objectives of the PSD.

### Powers assigned to the Authority

#### Entry without a warrant

**2.166** Draft regulation 85 provided the FSA with the power to enter and inspect a premise without a warrant. Some respondents viewed this power to be disproportionate. Respondents believed that the draft regulations considerably extend the current powers of the FSA, particularly as FSMA requires the FSA to have a warrant before gaining access to a premises.

**2.167** Although FSMA does not contain a power to enter and inspect premises without a warrant, the FSA's rules in its Supplementary Manual oblige firms authorised under FSMA to give access to the FSA for the purpose of supervisory visits (and to take steps to ensure their outsourced service providers give similar access). These FSA rules, however, do not extend to payment institutions. Article 21(1)(b) provides that competent authorities shall have the power to carry-out on-site inspections at payment institutions or any agent or branch providing payment services or at any entity to which activities are outsourced. Similar provisions in the Money Laundering Directive and MiFID have been implemented in the UK via the Money Laundering Regulations 2007 and the FSA rules referred to above. The Regulations therefore continue to grant the FSA with the power to enter a premises without a warrant. It should be noted, however, that the Home Office is currently undertaking a review of all bodies that have the power to enter without a warrant. Depending on the outcome of this review, the Regulations might be amended.

#### Restitution

**2.168** Draft regulation 89 provided the Authority with the power to require restitution. This power enables the Authority to oblige a payment service provider that has contravened any requirement of the Regulations to provide restitution to the appropriate person(s) with an amount that has accrued as profit or an amount equivalent to the person(s)'s loss as a result of the contravention.

#### Reporting powers

**2.169** The draft Regulations gave the FSA responsibility for making arrangements to ensure the compliance of persons subject to requirements under Parts 2, 3 and 4 of the Regulations and to determine whether there had been any contravention of draft regulations 114 to 118. The draft Regulations also provided the Authority with the ability to maintain arrangements to determine the compliance of those subject to requirements by or under Parts 5 and 6 of the Regulations. The draft Regulations, however, did not contain measures to facilitate the Authority in its

obligations (apart from a right of entry to premises, and a power backed by criminal sanctions) to request firms to provide their compliance documents or information.

**2.170** For the FSA to meet its obligations in an effective and efficient manner the preferred option would be to regularly receive and review compliance information provided by the firms concerned. An alternative option would be for the officers of the regulator to visit the firm and review the necessary information. Although the submission of a return could impose a cost on each firm, a firm in scope of the Regulations would need to prepare the necessary compliance information in any event. The additional burden would therefore only be attributed in the submission of the return. In comparison to onsite inspections, this approach is likely to be less disruptive and burdensome to the day-to-day operation of a business.

**2.171** The Government accepts that the FSA needs information in order to fulfil its obligations. The final Regulations have provided the Authority with the power to require information returns from payment service providers.

## **Insolvency**

**2.172** In order to provide further protection to payment service users, in addition to the FSA's ability to cancel the authorisation of a payment institution, the final Regulations have provided the FSA with the power to initiate insolvency proceedings against authorised payment institutions and EEA authorised payment institutions (via the application with modifications of the appropriate provisions in FSMA – Schedule 5, paragraph 6). In particular, the FSA will be able to ask the court to wind up such payment institutions or make an administration order. The court will be able to do so on the usual insolvency grounds or, in the case of winding-up, on just and equitable grounds. It should be noted that the FSA may only initiate winding-up proceedings in relation to an EEA authorised payment institution upon request from its home state competent authority.

**2.173** These powers enable an insolvency practitioner to be appointed in cases, where appropriate, to wind down a firm's business and distribute any payment service user funds.

## **Right of a private person to bring action in relation to certain contraventions**

**2.174** In order to ensure adequate consumer protections, regulation 120 of the final Regulations provides that in the event of a payment service provider contravening regulation 17, 19 or the conduct of business requirements a private person who suffers as a result of that contravention would be able to bring an action for the breach of statutory duty.

## **Complaints**

**2.175** Regulation 91(1) (draft regulation 84(1)) states that the FSA must allow interested parties to submit complaints to it when a payment service provider (including a transitional firm under regulation 121 or 122) has breached a provision in the Regulations. The FSA will consider such complaints as part of its supervision of payment service providers. It will also notify relevant complainants that they may have a right to take their complaint to the Financial Ombudsman Service (FOS). Further information regarding complaints handling, including in relation to transitional firms, will be detailed in the FSA Approach Document.

## **The jurisdiction of the Financial Ombudsman Service**

**2.176** One respondent raised concerns that the draft Regulations did not address the implementation of PSD article 83, which provides that MS should ensure that out-of-court complaint and redress procedures for the settlement of disputes between payment service users and their payment service providers concerning rights and obligations arising under the PSD are put in place. The FSA's Consultation Paper 08/14 proposed that the FOS could provide the out-

of-court redress mechanism for the UK with respects to the PSD and that FOS' existing "fair and reasonable" jurisdiction under the Financial Services and Markets Act 2000 (FSMA) should apply. The respondent questioned whether it would be appropriate to apply the "fair and reasonable" jurisdiction to the PSD out-of-court redress mechanism as article 83 does not provide a reference as to which basis the disputes should to be determined.

**2.177** Article 83 provides that the PSD out-court-redress mechanism should be adequate and effective, and to use existing bodies where appropriate. The approach to apply the existing FSMA fair and reasonable jurisdiction meets the Directive's requirement of an adequate and effective mechanism, as each case is assessed in the round, taking into account the relevant law and regulations, regulators' rules, guidance and standards, codes of practice, and (where appropriate) good industry practice, such the Remittance Customer Charter, at the relevant time.

**2.178** Article 83 should also be read alongside Commission Recommendation 98/257 on the principles applicable to the bodies responsible for out-of-court settlement of consumer disputes. The 19th recital of the Recommendation is particularly relevant: "the out-of-court bodies may decide not only on the basis of legal rules but also in equity and on the basis of codes of conduct...".

**2.179** The Government concludes that the application of the "fair and reasonable" principle to payment services would be appropriate.

## **Resourcing**

**2.180** A few respondents questioned how the Authorities plan to provide sufficient resources to supervise and enforce the PSD regime. Regulation 92 (draft regulation 91) provides the Authorities with fee-raising powers. The FSA will be able to set its fees in order to carry out its functions under or as a result of the Regulations, or for any incidental purpose. Through this fee structure the Authorities will ensure that they have sufficient resources to enforce and supervise the regime.

## QUESTION 15, 16, AND 17: COMPETENT AUTHORITY (DRAFT REGULATIONS 110 TO 120)

Q15. Do you agree with basing the penalty regime on the precedent in Financial Services and Markets Act (FSMA)?

Q16. Do you consider that the implementing regulations ought to make provision for the unenforceability of agreements entered into in contravention of the prohibition in regulation 110(1)?

Q17. Do you agree with the proposed implementing regulations in Parts 9 to 11, concerning general provisions, transitional provisions and amendments to other legislation? Are there other pieces of legislation in need of amendment?

### Penalty regime

**2.181** Respondents broadly supported the approach to base the penalty regime in the Regulations on that used in the Financial Services and Markets Act 2000 (FSMA). Respondents believed that this seemed to be a sensible approach. To move away from current practices would seem contrary to the overarching objectives of the Payment Services Directive.

### Unenforceability of agreements

**2.182** Respondents believed the inclusion of the unenforceability of agreements provision to be appropriate, as this would be in line with existing UK process.

**2.183** One respondent, however, believed that such unenforceability need not be absolute, but would best be judged by the FSA (subject to the usual appeal mechanisms), or on application to the courts. The Government, however, believes that decisions relating to the unenforceability should be left to the courts and therefore the regulation has not been amended.

### Transitional provisions

**2.184** One respondent sought clarity on the legal status of non-bank payment providers taking advantage of the transitional process and where the liability of the funds and activities would lie during the transitional period. As these providers would be transitional firms, despite needing to comply with conduct of business provisions from 1 November 2009, they would not be considered as being fully operational payment institutions.

**2.185** As the conduct of business regime will be in force from 1 November 2009, customers will need to have access to an out-of court redress scheme from this date. The Regulations therefore amend FSMA to enable the FSA to extend FOS's jurisdiction to firms using the transitional provisions. In spring 2009, the FSA intends to consult on the complaints-handling and ombudsman regime that will apply to these firms.

**2.186** Another respondent was concerned that if other Member States implemented regulation 110 (draft regulation 110 - prohibition on provision of payment services by persons other than payment service providers) prior to the UK's effective date of 1 May 2011 (as detailed within transitional provision (regulation 122 (draft regulation 118))), payment institutions authorised in another Member State could exercise their passport right earlier than UK payment service providers. This could result in a competitive disadvantage for UK firms.

**2.187** It should be noted that it is optional for firms to take advantage of the transitional provisions. For those firms wishing to be authorised on from 1 November 2009, the FSA will be taking applications for authorisation from 1 May 2009. Once the application is successfully

completed, firms would be able to passport their services into other EU Member States from 1 November 2009. Under the PSD, no business will be able to passport its services into another Member State until 1 November 2009, the implementation deadline for all EU Member States.

**2.188** During the EU-level transposition discussions it has been concluded that national transitional provisions are only available to firms incorporated in that particular Member State. Therefore, non-bank payment service providers that currently operate on a pan-European basis will need to seek authorisation on 1 November 2009 if they wished to continue with their operations under their current business models.

**2.189** With respect to the transitional provisions themselves, article 88 states that firms seeking to take advantage of the transitional provisions must inform the competent authority of their intent by 25 December 2007. During EU-level discussions, as many Member States had not appointed their competent authority by 25 December 2007, it was determined that this would have been unfeasible. It is therefore expected that the deadline for notification will be amended to that of 25 December 2009.

**2.190** It should be noted that the transitional provisions only apply to the application process for non-bank payment service providers to become payment institutions. They do not apply to the access to payment systems provisions or the conduct to business rules. All payment service providers will have to comply with the conduct of business provisions within Titles III and IV from 1 November 2009, and payment systems will have to ensure that their access rules meet the access criteria.

**2.191** Some respondents noted that both the banking and non-banking sectors would have to adjust their systems to meet the conduct of business requirements from 1 November 2009. These respondents requested FSA guidance of its enforcement approach from the effective date. Details of the FSA's supervisory and enforcement strategy will be contained in the Approach Document.

## Overlap with other legislation

**2.192** Respondents believed that the amendments to the primary and secondary legislation were comprehensively detailed in Schedule 7 of the draft Regulations and did not perceive a need to amend any other pieces of legislation.

## Overlap between CCD and PSD

**2.193** Respondents supported the Government's interpretation of article 30(3) of the PSD whereby the PSD should be without prejudice to national measures implementing the current CCD, and should also be without prejudice to any other European Community, or national measures regarding conditions for granting credit to consumers. Based on this interpretation, the approach that has been taken forward is that in areas of potential conflict between the PSD and the CCD provisions, the CCD measures would take precedence, unless consumer protection has been compromised. Respondents acknowledged the strong overlap between the PSD and consumer credit legislation and welcomed the Government's approach to providing carve-outs to related Consumer Credit Act provisions, as they believed this approach would provide legislative simplicity. It should be noted, that the Regulations will continue to govern the transactional elements of consumer credit.

**2.194** The Government aims to continue to engage with the industry while implementing the CCD to ensure the implications of this overlap are fully understood.

# 3

## Next Steps

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**3.1** The final Regulations were laid on 9 February 2009 and can be found at [http://www.hm-treasury.gov.uk/fin\\_payment\\_index.htm](http://www.hm-treasury.gov.uk/fin_payment_index.htm). Subject to Parliamentary approval, the Regulations will come into force on 1 November 2009 (with some provisions coming into force before then), meeting the implementation deadline set within the Directive.

### Related consultations

**3.2** In addition to the Government's consultation process on the PSD, the FSA consulted in autumn 2008 on the following proposed changes to its Handbook as a result of the PSD:

- changes to the 'Dispute Resolution' section of its Handbook so that the FSA's complaints handling rules apply to payment institutions;
- changes to the jurisdiction of the Financial Ombudsman Service so that it can perform the out of court redress function as required under article 83;
- changes to the Decision Procedure and Penalties Manual and the Enforcement Guide (EG) to explain the FSA's approach to enforcement of the PSD implementation legislation; and
- necessary consequential changes.

**3.3** The FSA is due to issue a Policy Statement in March 2009. Additionally, in February 2009, the FSA plans to consult on its approach to Payment Services Regulations fees and intends to publish an Approach Document in the second half of March 2009 outlining its approach on matters such as authorisation and supervision under the Regulations. The Office of Fair Trading will be developing its own approach to ensuring fair and open access to payment systems, which will feed into the FSA approach document.

**3.4** The PSD transposition work at EU-level, which has been running in parallel to the UK implementation timeline, will continue into autumn 2009. This transposition work aims to ensure that EU Member States interpret the Directive and its provisions in a consistent manner. The European Commission convened several meetings in 2008, including a meeting with industry and consumer groups representatives in November 2008. Further meetings will be scheduled in the first half of 2009.

### Other related regulatory changes

**3.5** Although this document concerns the implementation of the PSD, stakeholders should also be aware of wider European legislative and domestic developments in that might effect the payments environment either directly or indirectly. Other such pieces of regulation include:

- the Electronic Money Directive;
- Regulation 2560/2001 on Cross Border Payments in Euro;
- the Consumer Credit Directive;

- the Capital Requirements Directive;
- Regulation 1781/2006 on Wire transfer;
- the Directive on Consumer Rights; and
- Retail banking conduct of business.

### **Electronic Money Directive**

**3.6** E-money institutions are currently prudentially regulated through the Electronic Money Directive (EMD), which was adopted at EU-level in 2000, and implemented in the UK in 2002. The Commission has recently published a proposal to revise the EMD with the longer term possibility of amalgamating the EMD with the PSD. The main aim of the Commission proposal is to create a more business-friendly and streamlined regulatory framework for the issuance of e-money, in line with the stated objectives of the original Directive. However, until the EMD has been revised and implemented into national law, e-money institutions will need to continue to pay heed to both the existing EMD and its prudential requirements, and to the PSD conduct of business requirements which apply to all payment service providers. The Government is broadly supportive of the Commission proposal and is currently engaging in negotiations with a view to agreeing a compromise text within Council.

### **Regulation 2560/2001 on cross border payments**

**3.7** Regulation (EC) No. 2560/2001 on cross border payments is intended to ensure the price of cross-border euro payments is no higher than the price of identical euro payments within a Member State. The Regulation came into effect in the UK in 2002. The Regulation applies to euro payments between two Member States of up to €50,000 made with credit transfers, card payments and cash machine withdrawals. The Regulation allows non-eurozone Member States to apply the provisions of the Regulation to cross-border payments made in their national currency. The main objectives of the Regulation are to:

- reduce the level of charges levied on cross-border electronic euro payments, as these were perceived to be unduly high; and
- encourage the payments industry to make significant improvements to the existing cross-border payment infrastructure, in terms of cost, speed and quality, so as to facilitate an internal market.

**3.8** In February 2008 the Commission reported on its review of the Regulation's application. The review found that the overall impact of the Regulation was broadly positive, as it had achieved its intended objectives. However, to address gaps resulting from recent market developments, and to align the Regulation with changes that will be introduced, from 1 November 2009, by the PSD, the Commission concluded the Regulation would need to be amended.

**3.9** This Commission proposed Regulation would, as foreshadowed, repeal Regulation (EC) No. 2560/2001 and create a new Regulation while retaining the objectives of Regulation 2560, namely: to achieve a single market for euro payment services, subject to effective competition and where there is no difference of regime between cross-border and national payments, thereby providing significant savings and benefits to the Community's wider economy.

**3.10** The main proposed amendments to Regulation include:

- modifying Regulation (EC) No. 2560/2001 so as to facilitate the Single Euro Payments Area (SEPA), in particular the SEPA Direct Debit and to align it with the PSD;
- phasing out balance of payment reporting; and

- introducing a requirement to appoint a competent authority and out-of-court redress body.

**3.11** The Government welcomes the Commission proposal to revise Regulation (EC) No. 2560/2001, as it is in line with the Government's better regulation commitment to improve the quality of legal provisions and to keep administrative burdens to a minimum. It agrees with the Commission view that the Regulation should take into account the final text of the PSD and the emerging outcomes of the SEPA. It is envisaged that since the proposal maintains the same currency scope as the present Regulation, the impact of the amended Regulation on UK business would be negligible.

**3.12** In assessing the proposed Regulation the Government's priorities are to ensure that the UK and European payments market should be open, transparent, competitive, innovative and efficient — balanced with ensuring appropriate consumer protection. The Government is currently engaging in negotiations to ensure that the final outcome meets its objectives and is seeking technical changes where they are deemed to be necessary.

### **Consumer Credit Directive**

**3.13** The 1987 Directive on consumer credit established the Community framework for consumer credit with a view to promoting the setting-up of a common market for credit and establishing minimum Community rules to protect consumers. Following a review of the legislation, the Commission concluded that the Directive was in need of revision.

**3.14** In January 2008, the European Parliament and Council adopted the Consumer Credit Directive following a political agreement, which was reached in May 2007.

**3.15** The December 2007 policy consultation on implementing the PSD noted that non-credit institution credit card issuers and some money transfer operators currently extend credit lines to their consumers, and that, broadly speaking, all businesses that lend money to consumers are licensed by the OFT under its consumer credit regime. The July 2008 legislative consultation outlined the transposition hierarchy of PSD in relation to the provisions that overlap and conflict with existing European and national consumer credit legislation, taking into account the adopted Consumer Credit Directive, as credit card issuance and payment services involving the granting of a credit line fall within the scope of the PSD, as set out in Annex 4 and 5.

**3.16** Where the PSD does not contain a related harmonisation provision (i.e. in all other cases) UK consumer credit legislation should, however, prevail. The Payment Services Regulations aim to make this hierarchy clear in the dis-application provisions in Parts 5 and 6 of the Regulations where there is a potential overlap with CCA provisions. One remaining issue concerns the provisions of the new Consumer Credit Directive (CCD), which repeals and replaces the previous Consumer Credit Directive, and is to be implemented by June 2010. There might be further potential overlaps or inconsistencies between the new CCD and PSD provisions, as certain CCD requirements might not be covered in the CCA. This might in turn necessitate an amendment of the PSR.

### **Capital Requirements Directive**

**3.17** The Capital Requirement Directive (Directives 2006/48/EC and 2006/49/EC), which took effect in the UK on 1 January 2008, updates European legislation in line with international recommendations by implementing in the EU the new Basel Accord, Basel 2. Basel 2 is intended to reduce the possibility of consumer loss or market disruption as a result of prudential failure by seeking to ensure that the financial resources held by a firm are commensurate with the risks associated with the business profile and the control environment within the firm. The Directive applies to all credit institutions and certain investment firms. The European Parliament and Council are currently negotiating the Commission proposal to amend the Directive to:

- strengthen prudential requirements;
- improve supervisory coordination and efficiency of supervision; and
- increase convergence across the Community.

**3.18** The specific changes relate to the large exposures regime, hybrid capital instruments, supervision and supervisory colleges, requirements for securitisation and risk transfer activities and liquidity and is scheduled to be implemented by 31 December 2010. The changes may ultimately lead to some amendments to the Regulations.

### **Regulation 1781/2006 on wire transfers**

**3.19** The Wire Transfer Regulation aims to update European legislation on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing so that it reflects Special Recommendation VII on Wire Transfers made by the Financial Action Task Force<sup>1</sup>.

**3.20** The principal objective behind the Wire Transfers Regulation is to update and enhance European legislation to bring it in line with Special Recommendation VII of the international standards on combating money laundering and terrorist financing set out by the Financial Action Task Force (FATF).

**3.21** This regulation came into effect in the UK on 15 December 2007.

### **Proposal for a Directive on Consumer Rights**

**3.22** On 8 October 2008, the European Commission adopted the proposal for a Directive on Consumer Rights. The proposal intends to maintain a high level of consumer protection and aims to establish a real retail internal market by: making it easier and less costly for traders to sell cross border, and providing consumers with a larger choice and competitive prices. The Consumer Rights Directive would merge four existing EU consumer directives (Sale of consumer goods and guarantees (99/44/EC), Unfair contract terms (93/13/EC), Distance selling (97/7/EC), and Doorstep selling (85/577/EC)) into one set of rules. At the same time it would update and modernise existing consumer rights, bringing them in line with technological change (m-commerce, online auctions) and strengthening provisions in the key areas where consumers have experienced problems in recent years – particularly in sales negotiated away from business premises (e.g. door to door selling).

### **The FSA's proposals on regulating retail banking conduct of business**

**3.23** Retail banking conduct of business (COB) is currently largely self-regulated. The Banking Code Standards Board currently monitors and enforces compliance with the voluntary Banking Codes for dealing with personal and business customers, to which virtually all retail banks and building societies subscribe.

**3.24** The FSA has proposed changes to the current arrangements in consultation paper 08/19 'Regulating retail banking conduct of business' under which the FSA would monitor and enforce a high-level COB regime which includes full application of the FSA's Principles for Businesses. This is in part because of the FSA's new responsibilities for supervising payment services under PSD, which replaces around 40% of the Banking Codes. The FSA's proposals will impact payment accounts operated by retail banks as well as all other retail bank accounts and payment services that are out of scope of PSD. It has proposed that these new arrangements should come into effect at the same time as the PSD.



# A

## List of consultation respondents

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ABCUL

American Express

Bank of England

Barclays

British Bankers Association

British Retail Consortium

Cards Payment Group, APACS

Citi Bank

Community Development Finance Association

Corporate FX Ltd

Currencies Direct Ltd

Custom House Financial Services (UK) Ltd

Department of Enterprise, Trade and Investment (Northern Ireland Insolvency Office)

Edgar Dunn

Electronic Money Association

Halo Financial Ltd

Halifax and Bank of Scotland Plc

HiFX Plc

International Association of Money Transfer Networks

Insolvency Service

The Internet Fraud Advisory Group

Lloyds TSB

Lovells

MasterCard

Nationwide

Payments Council

PayPal

Royal Bank of Scotland

Royal Mail

Sidley Austin

Standard Life

Trading Standards Institution

Travelex

UK Remittance Taskforce

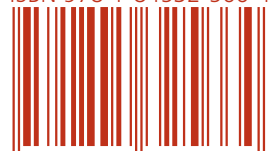
UK Money Transfer Association

VISA

Western Union



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