

PSD2 review priorities

1. Assessing the impact of Payment Services Directive 2 (PSD2)

A public representative noted that the European financial industry has learned a number of lessons from the application of the PSD2 rules. The European Commission is expected to make a proposal on the review of PSD2 in the coming months, which means it is a timely moment to consider this question.

An official emphasised that it is difficult to make a precise and complete assessment of the impact of PSD2 without considering the huge changes that were taking place in the sector as a result Covid. It is hard to assess its impact without considering what would have happened if PSD2 had not been on track when the pandemic hit. Within that context, PSD2 has clearly had a very positive impact.

1.1 Despite its cost and complexity, strong customer authentication (SCA) has increased citizens' trust in electronic payments

An official highlighted the particular importance of user confidence in payment services. If users are able to make safe payments, it is to the benefit of all. Therefore, fraud prevention is the most important aim of the regulatory framework. In this context, PSD2's biggest achievement has been the introduction of SCA. This transition has not been friction free, but the rate of credit card fraud has dropped significantly since the new rules were introduced.

An official agreed that confidence is a particularly important issue. The reduction in fraud is a good starting point for consumer protection, which is one of the most important objectives. The second objective is about innovation and competition, which must happen alongside each other. The necessary improvements in transaction security usually come with a cost, but it is important to remember that customers who are satisfied and who feel protected will continue to use a payment service.

An industry representative emphasised that PSD2 has been one of Amazon's priorities for more than five years. This has been a positive journey for Amazon and e-commerce more broadly. Earning customer trust is central to Amazon's DNA. In that regard, PSD2 has given Amazon another reason to invest in earning customers' trust. Uniquely, PSD2 has also provided an opportunity to reduce fraud. Amazon's fraud rates are extremely low, and they have dropped as a result of its work on PSD2. PSD2 has been a success for businesses, customers, the payments industry and the broader financial services industry.

1.2 PSD2 has fostered innovation and enabled third party providers (TPPs) to compete

An official noted that the other important set of rules in PSD2 covers the regulation of third party providers of payment services. The practical impact of the

regulation on the Swedish market is difficult to quantify because many of these services were offered in Sweden before the directive came into force. There was an important change of mindset, though. The banks that controlled the payment market infrastructure had to allow other payment service providers (PSPs) to use this infrastructure to create new and innovative services, which contributed to achieving a level playing field for PSPs.

An official stated that there is clear data on innovation and competition. There has been an increase of at least 5% in the number of TPPs. New business models have emerged in areas such as payment initiation, aggregation and account information services. When the door to innovation is opened, it is hard to say where it will lead. At present, the interaction between TPPs and the traditional banking system is adding value for consumers and increasing competitive pressure. It is also leading to a reduction in the cost of service and an increase in customisation. This competitive pressure puts the industry on edge, however. With so many partnerships and synergies, it has become harder to see where traditional banking ends and where neo banks begin. It is important to ensure there is transparency on who is behind a service so clients and investors understand their rights and obligations.

An industry representative suggested that PSD2 has forced Amazon to innovate, which has been a real asset. As Amazon has so many e-commerce use cases that fall outside the typical flow of shopping on a browser or mobile device, it has had to innovate and develop new ways for customers to have these experiences. Indeed, the team at Amazon were able to file patents on the things they invented. The team became quite energised by something that could have easily become a 'not very fun' compliance project. Additionally, there has been excellent collaboration during this process. The dialogue between merchants, authorities and banks has been very open.

An industry representative noted that SCA has become best practice and has now expanded to other regions. American Express has developed new technology and new services such as Amex Express List, which can be used to avoid authenticating with every single merchant a consumer shops at. There are many other examples of this kind of innovation.

1.3 PSD2 enables citizens to access banks via a variety of channels and facilitates multi banking, but it has been difficult to define an efficient interface

A public representative noted that the banking sector played a key role in PSD2 implementation. In the past, open banking has been very closely linked with the review of PSD2. An industry representative emphasised that the banks are the institutions delivering the data.

The other players in the payments landscape simply receive data from the banks. Despite this, banks generally have a positive view of PSD2. The saving banks in Germany took an open approach to PSD2. They conducted workshops and questions and answer sessions with fintech companies and tried to forge connections with them. As a result, 56 of the TPPs in Germany now work with the saving banks' infrastructure and exchange data with them. There are now 73 million transactions per quarter. These are bank customers using banks via TPPs, which means that banks are serving their customers by having open architecture.

German savings banks are also using PSD2 to offer multi banking to customers. Almost 3% of customers use this functionality. There are problems with the PSD2 interface with other banks, which is a significant hassle. The German banks now understand both sides of the interaction. This difficulty is caused by PSD2's mixture of very defined and very open regulation. Sometimes, the industry needs the regulator to say, 'This is the right way to do it'. It would be helpful if the legislation were introduced in a different way.

A consumer representative observed that the payments sector is the nexus between consumers and the economy. It has a fundamental role in the wellbeing of citizens. With this in mind, the regulatory framework around PSD2 has been a success story. It has opened up markets and increased the security of payments. As a consumer organisation, BEUC's members look at how consumers are experiencing these systems. The data from Norway, which is usually considered to be a highly digitalised country, shows that up to 25% of consumers have faced problems making online payments. This can be due to a lack of skills, literacy or equipment.

2. Areas for progress in the payments industry

2.1 Fair access to data will ensure the emergence of new entrants and business models and provide new opportunities for incumbents

An industry representative emphasised that American Express wants to contribute to the Commission's objectives for PSD2: fostering innovation, enabling competition, customer protection, harmonisation, etc. Clearly, innovation is a key objective. In the digital new economy, data can be leveraged to create more value and protect customers more effectively, etc. There are new entrants and new business models associated with that. There have been some bumps along the way in terms of implementation, however. Open banking is definitely a good example of innovation. Ultimately, open banking needs to evolve to open finance and eventually to open data. It would be preferable to have something that operates in two directions and is not one way. The portability of data, with the right privacy measures, can be leveraged to enable consumer protection and better customer service.

An industry representative highlighted the fact that the banking industry has to pay, implement and provide all

of the data, while other firms simply consume the data. Firms such as Amazon can build business models using PSD2 interfaces, but the banks have to pay for it. If there is not a balanced approach, not everybody in the banking industry will be as supportive of open banking as the saving banks. If there were a more balanced approach, more banks would be fans of open banking. 3% of German savings banks' customers use multi banking. This is almost 300,000 customers, and it is possible because savings banks in Germany have a 50% market share. However, the level of usage is not as high as was expected. Consumers might not want multi banking integration because they only have one savings account or they want to see different kinds of information. If multi banking and open banking is the goal, the discussion should not only be about banks delivering data to everybody else for free. There must be more data from other sources, which would provide a better overview and help customers.

2.2 The regulatory framework has become increasingly complex

A consumer representative described how the regulatory framework for payments has become extremely complex in the last few decades. A multitude of factors intervene across the supply chain, all of which governed by different pieces of legislation, such as the E Money Directive, PSD2, Single Euro Payments Area (SEPA). Supervision can play a key role here, but the competent authorities have limited powers to supervise companies located in different countries. From the point of view of conduct and consumer protection, there is also confusion about the different SCA systems implemented by different players.

2.3 Inclusiveness and fraud remain important issues

A consumer representative highlighted the importance of inclusiveness. It is essential to ensure that everybody benefits from the protection granted by SCA. To take a banal example, access to a recent model of smartphone can be the difference between being able to pay and not. Payment fraud is also a key issue. Although SCA performs an important role, payment fraud is on the rise. The issue of authorised and unauthorised transactions continues to exist because different rules apply to this question across Europe. The key problem is the sophistication of payment fraud. Consumers simply do not understand it. This is a question of education, and BEUC is strongly in favour of financial education from a very early age. At the same time, it is also important to think about market design and the incentives for players to implement measures to reduce the risk of people falling victim to fraud. To provide one example, BEUC members have reported that firms are abusing the concept of consumer negligence in payment fraud. It is easier to say, 'This is your fault' than it is to implement measures to prevent fraud from happening.

A consumer representative noted that IBAN-Name Check has been successful. The data from the Netherlands suggests that it has reduced fraud and error in payments. This goes hand in hand with the question of how consumers can identify payments. In many cases, bank accounts only show a company's name, which might be

the name of the legal entity but not necessarily the name of the shop where the money was spent. This could be solved with a relatively simple solution.

2.4 The development of instant payments has huge potential

An official stated that the European payments market has not yet seen the full potential of open banking regulation. In particular, instant payments still need to be developed. Instant payments will dramatically change the infrastructure that is used for payments. When banks are able to send and receive instant credit transfers, there will be highways where previously there were only muddy country roads.

3. How to achieve the objectives of PSD2 and fight fraud: harmonisation, technology and creativity

An industry representative noted that there were several key opportunities to enhance PSD2. The size of Europe makes the practical execution of a framework like PSD2 difficult, but this could be solved by implementing outcome based targets. It is important to know what success looks like. This could be framed in terms of fraud rates, authentication success rates or availability. The regulatory and supervisory community should set a bar for what 'good' looks like and then allow banks and other TPPs to innovate. These businesses will hit or exceed the target, and they will probably invent interesting things along the way. One extension of this is harmonisation. Amazon has found it difficult to develop a consistent customer experience across Europe. Specifically, stronger guidance on the use of exemptions would be useful. There could be guidance on best practice, but firms should also be able to innovate.

A public representative queried whether this remark was an invitation to the regulatory authorities to force more innovation on the industry. The industry representative agreed that regulators and supervisors should force the industry to innovate.

The public representative observed that savings banks are in the unique position of being on both sides of the data supply chain. An industry representative agreed with this. Fraud prevention is the savings banks' number one priority, but it must be done in the right way. Instead of implementing fixed requirements, the legislation should use targets. The industry needs to allocate greater financial means to fraud prevention, and it is important to increase the exchange of information about fraud between and among the industry. Until now, the legislation has focused on specific measures and excluded everything else. It must be more principles based. It is better for fraud prevention to be an aim or to use a particular success factor to measure it. Ultimately, these questions should be left to the industry. Alongside this, large scale pilots, such as DG Connect's digital identity pilot, can help to prove whether it is helpful, successful and practical to implement a proposal.

Experimenting through large scale pilots prior to legislation is preferable to the cost intensive hassle of organising everything afterwards.

An official suggested that technology is a transversal vector in this discussion. Firms must be properly incentivised to use and develop new technology. It is good to see technology this being used to tackle inclusion, for example. The industry needs to understand how to use technology to achieve a specific target and avoid excluding sections of the population, such as the elderly or the digitally illiterate. It is possible to use legislation to ensure that nobody is unable to use digital payments.

A consumer representative agreed on the need to design the legislation correctly, noting that there is a decision to make on whether it should be principles based. Certainly, the legislation should be technology neutral at level one. Principles can be difficult to enforce, however, and they leave room for interpretation. Therefore, it is important to strike the right balance between flexibility at level one and enforceability. The idea of targets has some merit and should be discussed with the European Banking Authority. It will be essential to ensure the targets correctly defined and effective, however.

An official observed that one industry representative is asking for the legislation to be more principles based and another is asking for it to include more guidelines. This is quite understandable, however. It is the job of the public authorities to strike the balance and create good regulation. In material terms, fraud prevention is the core of the regulatory framework. Another panellist raised the issue of data sharing. Fraud often involves a number of people with a number of bank accounts in different banks. Banks and PSPs need to be able to see the whole pattern to detect fraudulent behaviour.

An official agreed that targets be a solution to the question of whether to have principles based or detailed legislation. Targets are a good way to legislate, but they can be difficult to calibrate properly. One option would be to have very tough targets, particularly on some of the specific issues. However, the targets that are set must be enforceable.

4. Bespoke and harmonised regulations will create fair competition by addressing the specificities of different players and payment systems

An industry representative noted that PSD2 has led to new entrants and new models, but some of the important details have created additional barriers and prevented smaller players from competing with the dominant schemes. Sometimes, a one size fits all approach does not work. The regulation is designed to enable competition with big schemes, but sometimes applying the rules to smaller players has had the opposite effect. Trying to adapt is not only a challenge

for the firms themselves; it is also a challenge for supervisors. For example, some supervisors have fed back to American Express that they do not know how to apply particular rules.

As a specific example, open access in PSD2 assimilated three party schemes into four party schemes in certain circumstances where four party scheme rules had to be applied to a three party scheme, which is simply not feasible. This led to American Express closing down its operations in 18 different countries and shutting down millions of relationships with customers. The issue is easy to fix, however, and American Express would like it to be corrected. Another example would be payment institutions' ability to operate on credit cross border beyond 12 months. The obligations of payment or e money institutions are different to those of credit institutions, but this competition could be enabled through the use of the right rules and controls. This is also relevant for the upcoming regulation on instant payments and the digital euro. Payment institutions, e money players and other regulated entities need to have access to these schemes as well as credit institutions.

The industry representative highlighted the importance of harmonisation. For American Express, there is also a very specific question around surcharging. Not all

member states apply the same rules, which makes it hard for players, supervisors and customers to understand how to operate them. A consumer representative agreed on the need to move to a uniform approach to the interpretation of the payment framework, which will ensure that consumers are equally protected across the EU.

5. PSD2, open banking and data access

A consumer representative noted the important interplay of PSD2 with open finance. The two proposals will likely be published at the same time. Certainly, they share many synergies, especially regarding the important question of access to data and privacy.

An official emphasised that data belongs to the customer. When everything is structured around data usage and data sharing, it is important to remember who the rightful owner is, not only in terms of protecting particular pieces of data but also compensating for the use of data.