EU payments: priorities for the incoming Commission

1. The EU retail payments market

1.1 Ambitious and challenging objectives for the European retail payment system

The Chair detailed that the panel concerned the broader perspective on the European payments market, what can be expected from the new Commission and what the priorities should be. One aspect is how to become independent of international players, and how to persevere with consumer protection, security, innovation and competitiveness. It is also about pushing concrete projects, such as the Payment Services Directive (PSD) 3 and Payment Services Regulation (PSR), the recent regulation on instant payment, the digital euro and financial data access. These are supposed to make Europe more competitive, better equipped against fraud, and provide stronger rights for consumers and increase transparency.

1.2 Innovation, competition and fraud prevention

A regulator highlighted that Europe is leading the way, much of which is due to PSD2, which was instrumental in striking the right balance between stability and efficiency for payment services. There are more than 4,500 banks providing payment services, and 1,500 non-banks and 400 entities that are also authorised to provide new open banking services. That is a significant change compared to 2018. An EBA database was created, which allows the market and general public to gather information on who the newcomers are, access to which facilitates entry into the payment services market. Fraud has been reduced. The EBA was working on the standards for Strong Customer Authentication (SCA). Having that in law was a key element in fostering market confidence.

1.3 Security in retail payments

A Central Bank official emphasised that there is an appetite for innovation, driven by market participants and the public sector. An important achievement has been the security of payments. Vital steps have been taken over the last 10 years, and PSD2 has been instrumental in that respect, through the development of strong authentication techniques. Nonetheless, the fight against fraud is an endless one.

1.4 Progress and leadership from Europe in the payments sector

An industry representative emphasised that Europe is a very competitive market for payments, and has created the environment for innovation. Much of that is due to the regulatory track over the last 10 years. The number of e-money firms, including new entrants, are a testament to the vision of creating regulation that can enable innovation, even when it is not known what the innovations will be.

Open banking has received some bad press, because it has not changed the world overnight, but it also creates an environment for innovation. An industry representative's firm has launched unsecured lending products in seven European countries, which is possible thanks to open banking.

Technology innovation has been very rapid in the past 15 years. Payments innovation is catching up somewhat with that, but the regulation needs to try to be ahead of some of the unintended consequences that can happen, such as the rise of digital fraud.

An industry representative remarked that Europe is leading the way in terms of modernising its payments infrastructure. It is also playing a key role in the global payments ecosystem. Europe represents about 40% of the flows on Swift, for example. Europe has embraced digital payment and its growth is expected to continue. Europe is also leading the way for having a harmonised payments ecosystem that is secure and open to innovation.

Instant payments were voted on by the European Parliament a few days previously and are part of the retail payment strategy. This regulation will raise the bar in terms of access to instant payments and upgrading fraud detection and prevention thanks to the IBAN and name checking services. There should also be a reduction in fragmentation, because many of the providers that exist today provide different IBAN and name check services.

An industry representative highlighted how innovative Europe has been with its legislation, such as with the Single Euro Payments Area (SEPA) and the General Data Protection Regulation (GDPR). GDPR was an excellent learning experience, because whenever there was the need to transpose across the globe, the experience of implementing in Europe is leveraged. Europe should continue to take such steps, and try to influence and work closely with the G20, because there is a roadmap for cross-border payments. Europe is ahead in terms of having legislative tools that allow the financial service industry to prosper, that protect consumers, that create jobs and that help in building a better world for everyone.

2. Issues with fragmentation and efficiency

A Central Bank official noted that the picture is more mixed in terms of efficiency. The digitalisation of payments brought many benefits from an end user perspective. The creation of a SEPA for credit transfers and direct debits is an important achievement, but important payment instruments, including card payments, were left out. Additionally, innovation is increasing fragmentation. There is also a rising sovereignty issue that needs to be addressed. For efficiency, there needs to be more integration. Sovereignty is a new issue that has to be addressed. There are a number of regulatory texts on the table. The issue is fine-tuning them and adapting a number of provisions.

An industry representative stated that there is still the question of whether the EU is one market or 27. There are very dynamic and competitive national markets, with some diverging user habits resulting from how the banking industry and other financial institutions have matured over time. There is sufficient consistency of regulation driven by the EU rules and the EU has excellent payment sector infrastructure. Although there are many caveats and challenges, the EU single market is something to celebrate.

An industry representative noted that directives that leave too much interpretation to individual states do not create the harmonisation for the industry to grow or create a level playing field. Best practice from each country should be leveraged. It is also important to have continued growth in the payment industry, particularly in the remittance industry. Bank de-risking has been addressed in PSD2, but probably not with enough practical tools put in place. PSR is a major step in that direction, however, some improvements are to be made in order to reduce de-risking practices.

An industry representative added that PSD3 moving part of the directive into regulation, in the form of PSR, is a positive move, as it will drive consistency. Consistency is very important because differences in how the law is applied creates complexity for businesses.

A couple of items can be addressed in the new regulation. One concerns passporting. Currently, a payment institution cannot passport offer credit cards on a pan European basis because there is a 12-month limit for credit ancillary to a payment. This is an anomaly and should be removed. That would promote competition, because it will allow other payment institutions to compete with local banks and offer credit cards.

The way the surcharging is applied for cards not in scope of the Interchange Fee Regulation in Europe also varies across the countries, driving inconsistency and providing a very bad experience for the consumer. There are very few cards that are eligible for surcharging in Europe. They are not in a dominant position, so the merchants have a choice to accept or not. When a merchant chooses to accept, it can be extremely deceiving and deceptive for the card members to have to pay for paying at the end of the shopping experience. The regulator should make things simpler for consumers and ban surcharging on all cards across the EU.

3. Combining fraud control and the customer

An industry representative detailed that, for merchants, PSD2 equals SCA. SCA has led to a reduction in the level of fraud but also more technical complexity. It is, therefore, important to strike the right balance between fraud control and the customer experience.

The current regulation is not clear about whether behavioural biometrics can be an inherence factor or not. Regulator should clarify that behavioural biometrics can be recognised as an inherence factor as the technology exists today to allow for the authentication of the buyer with a very high level of certainty. Currently, for example, elderly people might struggle with entering the passcode and going to their bank application; by contrast, this alternative works completely in the background, is safe, and very user-friendly. It is also a good way of preventing spoofing fraud. With behavioural technology, it is very hard to steal identities or to replicate an identity since the authentication is based on hundreds of data points.

More clarity is also sought on exemptions. There is an opportunity in the PSR to allow the passporting of corporate exemptions on SCA between countries. The risk-based and result-oriented approach is positive. Transaction risk analysis (TRA) is a good example of this. If an issuer or acquirer has a low fraud level, then it is eligible for a higher threshold, below which it does not have to apply SCA. Although that logic is valid, the thresholds are arbitrary. A transaction of €1,000 is more likely to be fraudulent or suspicious than one that is at €500. A higher threshold should therefore be considered and should be conditioned to a certain level of fraud, which would allow for striking the right balance between fraud control and a frictionless experience.

A regulator remarked that more than 200 suggestions were submitted to the Commission for the initial proposal on how PSD2 could be improved, based on the experience gathered over the years. Most of those recommendations have been taken into account when writing PSD3, PSR and financial data access (FiDA). Guidelines on the authorisation of payment institutions, all prudential requirements, own funds, safeguarding of funds and notifications for banks will be developed. There are also many aspects related to fraud. There are about 35 mandates that the legislators have given to the EBA with this new package.

Market confidence is essential. The whole chain should be involved, including the merchants, the payment service providers and the public. Data protection aspects and inclusion aspects should be taken into account from the beginning. Customer experience is important, but issues around individual liberties must not be forgotten. Consumer protection in general should be taken to the highest possible level in order to obtain the trust sought for the products to be successful.

A public representative reported that there have been significant efforts to finish the European Parliament procedure as soon as possible. It is the end of the mandate of this Parliament, and the nature of the next Parliament is not known. The European Commission has proposed PSD3 and PSR so payments can be cheaper, safer and more user-friendly. Those objectives go in different directions, and a compromise had to be found to strike the right balance between them. The notion of authorisation has been better defined. The scope of who is responsible for tackling fraud has been enhanced to include digital platforms. Although digital platforms should not spy, they should react to information about fraudulent advertisements and accounts.

Europe is in a race against its global competitors and technological progress. It will always be somewhat behind in that respect, and has to close the gap between state-of-the-art technology and state-of-the-art solutions from China and the US. The European payment system is still quite fragmented. The non-bank champions are mainly local. However, Europe has a relative advantage in the fintech industry. As free as is reasonable access to the banking infrastructure should be offered to fintechs.

An industry representative remarked that the strength of the EU regulatory framework is that there is collective willingness to revisit it and optimise it. Other parts of the world are taking inspiration from PSD2, the Digital Operational Resilience Act (DORA) and GDPR. PSD3 and PSR could take greater account of other business models, especially in large tech companies where there might be anxiety about the provision of certain services in this space. Likewise, SCA measures could better embrace innovative approaches alongside the focus on safety to make sure users get the best outcomes, while being protected and having as frictionless and trustworthy an experience as possible. With these issues, together with some of the other competition issues that the Directorate-General (DG) for Competition and the DG for Communications Networks, Content and Technology are looking at, there are important steps forward that need to be taken.

An industry representative noted that there is an opportunity to help European champion firms become global players. Aspects of the single market are not working well. Three blockers to business are IBAN discrimination, the proliferation of alternative payment methods (APMs) in various countries and fraud.

Regarding IBAN discrimination, the SEPA scheme has not worked in terms of adoption and enforcement. Regarding APMs, although SEPA wiped out many of the existing legacy schemes, new ones have arisen due to technological innovation, and it is quite difficult for organisations to join those if they are not local. That does not help the situation. For an industry representative's firm, 75% of the fraud it encounters originates from one social media platform. There is a need to keep pushing big tech to become part of the solution.

The Chair agreed that considering competitiveness outside of Europe is important to consider. One area that needs to improve is co-operation, because there are many diverging views and concrete ideas. The question is how to bring all of that together efficiently. An interplay between the public and the private players is needed to succeed.

4. Co-operation between market participants, and the public and private sectors in a global context

4.1 Adopting the payment standard and fostering interoperability and interconnectivity

An industry representative noted that the retail payment strategy and its four pillars should be implemented. The first pillar is the rollout of the instant payment regulation, which includes mandatory IBAN and name-checking services. Banks need to be compliant with this regulation. It will ensure connectivity and interoperability with the existing solution. Providers that exist today will provide IBAN and name-checking solutions, and it should be ensured that banks can connect easily and do not have to connect to each individual solution. Banks can then also pre-validate at the cross-border level.

The second pillar of the Commission's payment strategy is to offer the best services for citizens with a high level of protection. An industry representative's firm is working on increasing the cross-border payment experience, not only for wholesale but also for retail and small and medium-sized enterprises (SMEs). It is working with the banking community to make sure that it can offer instant (or quasi-instant) payments that are transparent, and traceable. Banks are being encouraged to upgrade the front-end od retail SME applications with these capabilities.

The third pillar is interoperability with instant payment systems. An industry representative's firm offers connectivity to TARGET Instant Payment Settlement (TIPS) and Real Time 1 (RT1). It is also a key component of the One-Leg Out Instant Credit Transfer (OCT-Inst) of the European Payment Council (EPC). The firm is innovating with central bank digital currencies (CBDCs), with a focus on ensuring interoperability with existing networks. The fourth pillar of the retail payment strategy in Europe is supporting the cross-border agenda from the G20.

4.2 Developing integration and sovereignty

A Central Bank official highlighted, regarding integration and sovereignty, that there is more of a role for market players, both private and public, and including central banks. It is something that market players and market forces should address. That is where partnership comes into the picture. A number of initiatives need to be undertaken. For example, there is the European Payments Initiative (EPI), which can contribute to the integration agenda and the sovereignty issue. For the sovereignty issue, there is also the digital euro, which is the central bank contribution. That project requires a strong partnership between the central banks and payment service providers.