

Central Bank of Ireland response to the European Commission targeted consultation on the review of the revised Payment Services Directive (PSD2)

Introduction

The Central Bank of Ireland (Central Bank) welcomes the opportunity to provide views and insights from its experience with the implementation and impact of the revised Payment Services Directive (PSD2).

The European payments industry is a rapidly developing and dynamic space, which is constantly evolving through innovative technology and expanding markets. PSD2 has been an essential tool in both facilitating this development and allowing Competent Authorities (CAs) to put in place the regulatory measures to supervise payment services and protect consumers. In that sense, the Central Bank views the introduction of PSD2 as having had a very tangible and positive impact on the European payments industry.

Nevertheless, it cannot be said that the implementation of PSD2, and particularly some of the technical requirements around security and Open Banking, has been without its problems and it is crucial that lessons are learned from this. There is now an opportunity to bring the Directive forward with industry developments and to make it a better fit for all of the actors involved including payment service providers (PSPs), consumers and CAs.

In this regard, the Central Bank has some key high-level issues it would like to highlight in this letter. With the growth and expansion seen in the payments industry, the Central Bank sees some key measures that need to be both revised and introduced to facilitate the continued effective supervision of payment services, particularly from a prudential perspective.

From a technical requirements perspective, and in particular around security and Open Banking, our view is that the Directive needs to be as detailed and prescriptive as possible in setting out industry requirements in order to facilitate the effective and harmonised implementation of requirements across all jurisdictions. Further to this, and calling on the lessons observed from the implementation of previous technological requirements, it is imperative that a thorough analysis is carried out on the effort needed to implement new technological requirements across all of the payments industry ahead of the setting of implementation timelines. This is particularly important to consider, as the effective introduction of requirements can be reliant on actors outside of CAs regulatory remit taking action, such as was seen during the implementation of Strong Customer Authentication (SCA).

The Central Bank view is that the opportunity provided by the revision of PSD2 highlights not only the essential role the Directive has played in the development of the European payments industry but also the need to ensure that the framework both evolves with and develops a rapidly moving and changing industry. In order to do this the Central Bank view is that a legislative proposal for a PSD3 is necessary.

The feedback set out below is targeted at the key issues the Central Bank sees in both revising the current provisions of PSD2 and evolving the legislation to meet the needs of the payments industry.

Key Issues

Resolution Framework

The review should consider whether there is a need for the establishment of a framework for the resolution and recovery of payment institutions (PIs). The Central Bank view is that the introduction of such a framework is crucial to the safeguarding of the payments sector from both an economic and consumer protection point of view.

With many new players entering the market, and with the market rapidly evolving, there is a high possibility of overcrowding resulting in the failure of payment institutions. Whilst recognising that there will be firms who succeed and others that may fail, this can only be acceptable from a regulatory perspective on the basis that failures can be managed in an orderly fashion and inappropriate losses are not incurred by consumers. Therefore, the requirement for PIs to establish a risk framework to support orderly recovery and wind down in the event of insolvency or cessation of business, ensuring safeguarded funds have a clear pathway back to the underlying user, is an essential consideration.

A procedure as part of the EBA Authorisation Guidelines as well as in the Directive should be set out and it is important to ensure full alignment to the Deposit Guarantee Scheme Directive (DGSD). Additional consideration is also needed on how insurance policies pay out in the event of a failure, to ensure that underlying beneficiaries receive monies owed.

Corporate Governance

With the growth seen in the payments sector and so many different players of varying sizes entering, the Central Bank view is that a future Directive needs to be more prescriptive around governance expectations with, for example, minimum requirements set out around;

- Board Composition
- Executive Management requirements for PIs/EMIs
- Risk management capabilities and frameworks
- Key components of effective risk management and control functions
- Risk appetites
- Board sub-committee structure suitable for the PI/EMI sector
- Expectations regarding residential status of Executive Management team for applicant firms

Safeguarding

The Central Bank view is that further harmonisation of safeguarding requirements is needed and that further clarity is necessary on the consistency and standardisation of requirements around acceptable safeguarding processes to ensure the maximum protection of user's funds. Areas where we would like to see greater clarity and requirements that are more prescriptive include:

- Detail on the suitability of insurance policies;
- Acceptable comparable guarantees;
- Detail on what can be considered as a low risk asset or investment and full alignment with the EMD;

- Requirements that permit the identification of the underlying beneficiaries as well as aligning with the DGSD to ensure it is compatible with a pay-out under that legislation;
- Should safeguarding volumes be used as a method to determine if a firm is considered a Significant or Less Significant Payment /E-Money Institution?

Merging of PSD2 and EMD2 into one Directive

The Central Bank view is that PSD2 and EMD2 should be merged into one Directive. There is significant overlap between both Directives and references and interlinkages throughout both are not aligned resulting in significant ambiguity for firms and regulators. Using the example of safeguarding requirements to illustrate this point, a revision of both the PSD2 and EMD2 is required to ensure a robust and transparent legislative framework is established to ensure user funds are safeguarded in a consistent and appropriate manner.

Initial Capital Requirements/Own Funds

Considering the growth in the payments sector and the scale of some firms now operating within it, it is crucial that a review of the current requirements is undertaken to assess if they are still fit for purpose and meet the requirements of a rapidly growing market.

From an Irish perspective, and based on the growth that we have seen in the sector, we have concerns that the level of own funds held may not be sufficient to allow for an orderly wind down of firms, particularly given the number of customers, level of payment transactions and the pan European nature of firms in the sector.

In the present situation, calculations of firm's initial capital/own funds is often so low that they do not adequately reflect the inherent risks posed. It is imperative that calculation methods are reassessed in a way that allows them to take into consideration the nature, scale and complexity of each firm, i.e. allow for a more proportionate assessment of each firm.

Open Banking

The need for clear and detailed requirements that can be understood and implemented in a harmonised manner by Account Servicing Payment Service Providers (ASPSPs), Third Party Providers (TPPs) and CAs is crucial to achieving a fully functioning Open Banking industry that consumers can use in an accessible and protected manner. It is important that any future requirements be developed with consideration given to the work that has already been carried out by both TPPs and ASPSPs, as considerable resources have been invested in this area and feedback from all of industry is needed on what the impact of any potential changes will be. For example, if a proposal to apply a single Application Programme Interface (API) Standard across all jurisdictions were made, a thorough cost benefit analysis would be needed to factor in the work already done by the industry against the future work needed to establish a single API standard.

Strong Customer Authentication (SCA)

It is imperative that lessons from the implementation of SCA are learned and factored into how any future requirements are implemented. The implementation of SCA required a radical technological overhaul of security requirements and was heavily reliant on action being taken by players outside of

the regulatory perimeter for its successful implementation. It is vital that the undertaking required by all of the payments industry to implement such complex requirements is not underestimated and an essential condition going forward must be that detailed and clear requirements are available from the outset and that no timeline for implementation is set until this is the case.

The Central Bank sees merit in exploring how future SCA requirements can be developed to ensure an optimal user experience for both consumers that are technologically savvy/enabled and those that are less so. One group should not be catered for at the expense of the other. Future requirements should also be developed to meet evolving threats such as social engineering, which all consumers are vulnerable to.

Passporting of Services

The Central Bank is of the view that further clarity should be provided in relation to the provisions around the Right of Establishment and Freedom to Provide Services in other Member States, as there are significant differences of interpretation among PSPs and CAs across Member States.

In relation to triangular passporting specifically, differing interpretations in relation to the permissibility of triangular passporting amongst host NCAs has led to undue delays in the passporting notification process. Similar host NCA supervisory concerns are prevalent with regard to distributors located in third countries, particularly in a post Brexit context, and it is not sufficiently clear whether firms can operate using distributors/agents located in a third country jurisdiction. Therefore, further clarity and guidance on whether triangular passporting is permissible is needed to bring about increased convergence on this important issue. Transparency could be increased through examples of what is or what is not permissible. The use of third country agents/distributors, or the outlawing of same, should also be clearly addressed.

Article 15 of PSD2 requires the EBA to develop operate and maintain an electronic central register under PSD2. CAs, in turn, are required to provide the information to be contained on the central register, which should be mirroring the content of the information contained on their national registers. Greater harmonisation between the national registers and the EBA register is required.

Cash in Transit

Cash in Transit (CIT) companies play a critical role in the cash supply chain, not only with respect to the transport of banknotes and coin, but they also play a key role in cash processing and recirculation. With their evolution from cash in transit companies to cash management companies (CMCs) now providing additional cash management services, that role is becoming ever more significant. The exemption of CITs from PSD2, (Article 3 (c) “professional physical transport of banknotes and coins, including their collection, processing and delivery;”) creates a scenario where there is currently little or no financial regulation of the sector in many Member States.

The Central Bank considers that this review provides a valuable opportunity to reflect on the current exemption, and review its appropriateness for the CITs/CMCs that operate across the euro area. Their role requires the handling of significant volumes of cash. The absence of financial oversight for these companies creates a potential risk of loss or misappropriation of client funds. Furthermore, lack of regulation could potentially expose not only these CITs, but also their customers, to insolvency risk. By reducing that likelihood through regulation, CITs can continue to play a valuable role in the cash

supply chain, maintaining confidence in cash and supporting access to cash for those European citizens who wish to use it.