To: **HMT Payments Policy Team**

From: **Electronic Money Association**

Subject: **EMA response on HMT's questions on "risk-based approach to payments" proposals**

Date: **20. 9. 2023**

Background

HMT has continued to develop its policy on "risk-based approach to payments" proposals to allowPSPs to delay or refuse payments that could potentially result in fraud. It is expected this will involve a change to the provisions in Payment Services Regulations 2017 (PSR), to enable PSPsto delay or refuse payment beyond the currently prescribed backstop date under PSR (generally,within D+1). HMT consulted on these proposals earlier this year in the HMT's Payment ServicesRegulations Review and Call for Evidence (see Question 20).

EMA previous concerns about the proposals revolved around the impact on transactions that occur between a chain of PSPs, in particular but not only PISP-initiated transactions, and the need for appropriate safeguards to ensure to ensure that it will not disproportionately and adversely affect legitimate payments, as well as effectiveness of the payment system.

HMT has provided a brief update on the policy developments in this area and raised additional questions on which they are seeking feedback.

Please find below the EMA's response to these further questions.

Criteria for refusing a payment or delaying beyond D+1

As well as enabling delays, would it be helpful for legislation to also clarify that PSPs can refuse payments where they suspect fraud against the payment service user?

EMA response: Yes, we believe it would be helpful to explicitly confirm in the Payment ServicesRegulations 2017 (PSR) that PSPs can refuse payments in these circumstances.

This is an important aspect of the fraud prevention measures available to PSPs, and will be particularly important once the APP fraud mandatory reimbursement requirements come into force in 2023.

It should also be clear that this is an optional right for PSPs to exercise. In other words, the ability of a PSP to delay a payment should not be used as a reason to find against a PSP in cases where it does not delay a payment that then turns out to be fraudulent. Fraud monitoring measures cannot identify all frauds, particularly APP scams, and PSPs are in general obliged to execute payments on time. PSPs may be liable for charges/ lost interest etc. caused by payment delays, so should not at the same be held liable for not delaying a payment that turns out to be fraudulent.

What threshold should apply for a delay/ refusal to a payment? Are there any thresholds/ precedents which we should look to beyond "reasonable suspicion"? What evidence could be used to make such judgments and how could this be evidenced in case of challenge?

EMA response: We consider it is important to ensure that the sending PSP's ability to delay payments is balanced against the interests of the payer and payee in any transaction, as well asthat of any third-party payment service provider, such PISP. Considering the user expectations for immediate payments, as well as importance of immediate payments to commercial transactions and to efficient payment systems, any exceptions to the D+1 service level legal obligations should be narrowly defined and limited in scope.

It appears that the ability to delay payments in this way are intended to, but not limited to, investigating suspected APP scams - it may be helpful to provide further clarity for which types offraud the delays in payments are permitted. Creating a general allowance for investigations tobe carried out in order to mitigate the risk of loss to the PSP is in our view detrimental to the payment product itself, reducing fraud by reducing its overall utility for any payments.

We believe consideration should be given whether the APP scam must be one that is capableof being observed by the PSP through monitoring, or of coming to their attention through othermeans such as suspicious destination accounts etc. A general allowance for all APP scams would bring in many categories of APP fraud, many of which are largely invisible to the PSP, and could require extensive investigation to determine whether they have occurred. In other words, the more remote a fraud is from the PSP, the more time will be required to uncover its circumstances.

Accordingly, we consider any circumstances enabling the delay or refusal of payments beyondD+1 must go beyond "reasonable suspicion of fraud" or a similar standard, and must lay downadditional conditions that must be satisfied, in order to safeguard the effectiveness of paymentsystem and limit the disruption to the payments, including those that are legitimate.

In our view, the additional threshold and conditions could include the following:

- The value of the transaction must be such as to outweigh the impact of the disruption that will be caused by delaying the payment beyond D+1. There can be exceptions to avoid gaming of the thresholds by fraudsters, and these can be made subject to reviewby industry and regulators from time to time.
- There should be an absolute time limit following which the sending PSP could no longerdelay the execution of a payment and would therefore have to execute the payment or refuse the payment. The absolute time limit can be set out in legislation. Such a time limit should take into account that the customer would not have access to their funds, and be based on reasonableness. This should be confirmed in legislation or as a minimum in the revision of the Payment Services Regulation ("PSR"), and should apply even where the payment service user has failed to respond to the PSP's requests for information and warnings.

Ultimately, the rules should recognise that the funds subject to any delay are those of paymentservice users, and users must have the right to dispose of their funds by whatever means theywish. Once warnings are adequately given, PSP should be able to release funds to users, but simultaneously cannot be held responsible for any fraud that follows.

Should a delay beyond D+1 be justified on the basis of engaging a third party? Do you have any examples of third parties that a PSP may wish to engage in the course of investigating a payment? Are there any other reasons why a PSP would need to delay beyond D+1 to prevent a fraud?

EMA response: Where a payment is delayed, the PSP will need to contact their PSU to informthem of the delay and, likely, clarify the circumstances of the payment to assist their investigation. It would be reasonable to allow for a (reasonably short) delay beyond D+1 wherethe customer has been contacted, but their response is pending.

In addition to contacting the customer, the PSP may wish to contact the law enforcement authorities, and possibly other third parties that may provide useful information in regards tofraud (e.g. CIFAS, or other PSPs that may be involved).

The principle of the delay being justified on the need for engaging a third party seems reasonable.

Do you foresee any difficulties in practically implementing delays based on the above?

Customer communication standard

Is it reasonable to require a PSP to give reasons for refusal or delay to their payment service user based on the criteria in regulation 82 (1)(2) Payment Services Regulations? What evidence would be provided to a payment service user? Do you foresee any circumstances in which it would not be appropriate to communicate witha payment service user based on this standard?

EMA response: We believe it reasonable to require that a PSP informs their customer without delay if their payment is refused or delayed beyond reasonable user expectation, and certainly beyond D+1. However, any communication requirement should not put the sending PSP at risk of committing the offence of tipping off, or otherwise assisting the fraudster. In respect of tippingoff concerns, we note regulation 82(5) PSR allows a PSP to forego the notification requirement where such notification would be unlawful. In that respect, regulation 82 of PSR provides a good precedent.

We note the regulation 82 notification standard requires PSPs to notify their PSUs of the refusal(or delay) and, if possible, the reasons for such refusal (or delay). In our view, it does not also require the PSP to provide evidence for the reasons that led to the payment refusal. A requirement to accompany customer notifications with evidence needs to be considered carefully and in our view would not be appropriate. Any evidence could be passed on to the fraudster, hence in effect assisting the fraudster to adapt their fraud methods and/or evade detection controls accordingly.

Liability

Do you have any comment on whether the liability under regulation 94 Payment Services Regulations should continue to apply to payments which have been refusedor delayed beyond the normal timeframes?

EMA Comment: More clarity is needed on the PSP's liability in the event of delayed or refused payments, including in particular where a chain of PSPs and/or PISPs is involved. We would welcome further regulatory guidance, with practical examples. The liability framework and expectations under the new rules should apply a maximum timeframe within which a payment can be delayed, or must be refused – otherwise, it can be difficult to determine when the liability has crystallised, the liability rules that apply, and the consequences that follow (e.g. whether a payment is to be considered a late payment, or a non-executed payment, and which PSP is liable). The principle of a PSP's liability being limited to circumstances where a PSP has not met its obligations should be adopted. In other words, where a PSP has delayed or refused a payment beyond the normal timeframes but within the parameters set by the new rules, they should not beheld liable.

Payee's PSP liability for payments received late

With regards to payments which have been delayed by the sending PSP, but eventually executed (late payments), presumably it is intended that the provisions of regulation 91(7) PSR would apply.

This means that the receiving PSP would be required, on request of the sending PSP on behalf of the payer, to apply credit value date for the payee's payment account as if the transaction had been executed correctly, i.e. on time. However, Regulation 94 places liability on the receiving PSP towards the payee with respect to any charges incurred, or interest lost as a result of the late payment. In these cases it would be disproportionate for the payee's PSP to bear this liability where the payment delay is outside of its control (but is rather imposed by the sending PSP).

Whilst regulation 95 allows a PSP to seek recourse from the payer's PSP in these circumstances,the practicalities of doing so need to be addressed. For example, there should be a standardised process and clear regulatory guidance setting out the expectations on all parties. With the likelihood of delayed payments increasing (with the new rules), the need for such practical solutions is likely to become more important. This is particularly the case for smaller PSPs who have limited resources to absorb the additional liability and/or pursue recourse against individual sending PSPs on a payment-per-payment basis. We submit it would not be appropriate for the payee's PSP to be liable in the circumstances described above, unless there is an automatic and effective process in place to obtain reimbursement from the sender's PSP.

Where the payment is delayed with the parameters of the new rules, neither PSP should be liable for losses incurred by either PSU.

Guidance

Receiving PSPs and crediting of payments. Financial crime law already makes requirements in terms of how PSPs should treat the proceeds of crime, and there is an existing force majeure clause in the Payment Services Regulations which allows

firms to comply with these obligations (regulation 96). If FCA guidance clarified that receiving PSPs should consider regulation 96 before crediting a payment to a payee, would that be sufficient for your members to be more comfortable with delaying the crediting of funds to comply with EU/UK law including in circumstances where there are financial crime considerations?

EMA response: It would be helpful for the FCA to provide guidance to confirm that regulation 96 PSR permits PSPs to delay crediting a payment to a payee, or to make funds available to the payee, e.g. where the paymentis received as a result of fraud against the payer. To benefit clarity and commoninterpretation, such guidance could be supported by practical examples of when such delays would be permitted due to financial crime considerations.

Are there any other aspects of existing payments regulation that it would be helpful for the FCA to issue guidance on in relation to refusing/ delaying potentially fraudulent payments?

EMA response: We would welcome guidance that clearly sets out the alignment between the legislation and PSR rules, especially on liability.

Human Rights considerations

What consideration do you make for the applicability of Human Rights law, for example Article 1 of Protocol No. 1 to the European Convention on Human Rights (protection of property)?

EMA response: Article 1 provides that every natural or legal person to the peaceful enjoyment of his possessions, where peaceful enjoyment includes the right of access to the property. Any delays in executing payments or obstacles in accessing funds would impose a restriction on how people choose to deal with their money; the regulatory framework which allows for such delays must strike a “fair balance” between the individual’s rights and the public interest (the prevention/reduction of fraud). Article 1 considerations support our position that any rules permitting delays beyond the D+1 standard should be narrowly defined and limited in scope.

To strike the appropriate balance, Article 1 rights should be supported by a regulatory frameworkthat recognises (as per our comments above) that the funds subject to any delay are those of payment service users, and users must have the right to dispose of their funds by whatever meansthey wish. Once warnings are adequately given, PSP should be able to release funds to users, but simultaneously cannot be held responsible for any fraud that follows.