4. PSD2 implementation

Transposition deadline draws closer as access debate continues

The deadline for transposition of PSD2 is now less than 6 months away. But with technical standards still under development and no pan-European consensus on how to meet the access to accounts requirements, many of the questions over how firms will comply and what the European payments market will look like in the future will continue well into 2018.

Building on the original PSD

The first Payment Services Directive (PSD) came into effect in 2009 and created a single market for payment services in the EU and the basis for the Single Euro Payments Area (SEPA). It harmonised, or in many cases introduced for the first time, the requirements for providing a payment service and set out clear rights for payers and payees.

However, finding there were gaps in this initial effort, European legislators set out to address the shortcomings with the revised Payment Services Directive, commonly known as PSD2. Agreed and published in 2015, it extends the scope of the payment rules - for example, transactions in non-EU currencies and those through online marketplaces will now be covered - and strengthens consumers' rights, with new maximum processing times for disputes and a ban on surcharging for the use of most types of retail debit and credit cards. But legislators have also tried to account for the changing nature of online payments, with two new sets of provisions that have been the cause of much debate throughout the EU:

- **higher security** for payments and internet banking, known as Strong Customer Authentication; and
- **access to accounts requirements** that will guarantee users are able to use third party services that function by accessing the information or payment operations in the user's online payment account.

The deadline for Member States to transpose PSD2 into national law - and therefore when it should come into effect - is January 2018. However, a number of details for how both Strong Customer Authentication and access to accounts (including "common and secure communication" between account providers and third parties) are to work will be set out in regulatory technical standards - often abbreviated to RTS on SCA and CSC. These won't come into effect until 18 months after they are adopted by the European Commission, which isn't expected until later this year.

The process of drawing up the standards has highlighted the range of views that remain as to what PSD2 is intended to do and how it should be implemented, as well as the gap that exists between what is explicitly in the directive and what falls to firms to interpret. Furthermore, the time lag between when PSD2 and the RTS on SCA and CSC come into effect, which will now be at least a year, creates a transition period where account providers are required to provide access to third parties but security requirements won't yet be in place.

Security and access to accounts

The higher security requirements will mean that for the majority of electronic payments two-factor authentication will now be required. That is, a user will have to provide two of three possible pieces of evidence to carry out a transaction: something they have (e.g. a debit card); something they know (e.g. a PIN); and something they are (e.g. a fingerprint). In addition, where it's a remote payment, the evidence will need to be linked to the payment amount in a process known as dynamic linking.

As explained in the July 2016 Digital Economy Outlook[10], the access to account rules will require banks to grant licensed third parties access to bank accounts when authorised by the clients. Those third parties will be able to offer two new types of regulated services:

- account information services (AIS) - the use of transactional and account information, for example the aggregation of multiple accounts together to offer better personal financial management; and
- payment initiation services (PIS) - the use of the payment functionality available through internet banking, for example to make a payment as part of an online purchase.

Regulatory Technical Standards

The directive itself does not specify the technical mechanism through which access to accounts will have to be granted. The European Banking Authority, in its first draft of the standards, therefore proposed that account providers (like banks) should provide at least one form of access: either through the user interface (essentially a form of screen scraping), or through a dedicated interface (for example, an Application Programming Interface - API).

The use of APIs is already widespread throughout internet based services and there is broad agreement that they can offer better security and control to users. However, some third party providers remain concerned that banks' APIs might not be fit for purpose, for example by falling short of the high levels of availability they need. Responding to these concerns, the Commission suggested in May a number of changes to the EBA's proposal, including a "fallback option" that wherever the API was not available for more than 30 seconds then third party providers would have access through the user interface.

In turn, the EBA expressed concern[11] that this change might reduce the likelihood of APIs being used, increase costs for account providers, and leave new third party entrants to the market at a competitive disadvantage, without any improvement to the reliability of access. The EBA proposed its own alternative amendments to meet the Commission's objectives and ensure that account providers using APIs developed them within the spirit of PSD2. These included the development and publication by account providers of key performance indicators of service levels

10: Pablo Urbiola. 2016. Open Banking: a regulatory perspective, BBVA Digital Economy Outlook
11: EBA opinion in response to the European Commission intention to amend the EBA Technical Standards for open and secure electronic payments under PSD2, June 2017

of their interface; making the interface available for testing 3 months before the RTS come into effect; and a review of how interfaces are functioning by the EBA.

Harmonisation and challenges

All eyes are now on the Commission as they produce a final version and look to adopt the RTS in the coming months. This will provide some welcome clarity to industry, but the debate on PSD2 implementation will be far from over.

While British regulators are forcing 9 of the largest banks in the UK to develop a common approach to PSD2 APIs for January next year[12], discussions on pan-European harmonisation are likely to continue well into 2018. A number of different parties have launched efforts to galvanize support for the development of common standards (such as the Berlin Group), a directory of third parties and account providers (Preta and Equens Wordline), and for shared infrastructure (CAPS). Harmonisation is also on the agenda of the ECB's stakeholder forum, the Euro Retail Payments Board, and the accompanying working group of the European Payments Council.

However, none of these efforts have yet received cross-industry backing or published detailed proposals, leaving it possible that in the short term country-level initiatives may instead emerge as ways to overcome fragmentation in a number of Member States.

In any event, as the RTS on SCA and CSC won't come into effect immediately, account providers can comply with the general access to accounts requirements in January 2018 by allowing the current standard practice - screen scraping - to continue. Many firms are therefore likely to wait until much closer to the entry into effect of the RTS on SCA and CSC (potentially around Q2 2019) to roll out their final PSD2 (and RTS) compliant solution. Whether they plan to use APIs or not, whether those APIs are harmonised, within or between Member States, and what this could mean for competition in the EU payments and banking market will become clearer over the course of the coming 18 months.

12: See https://www.openbanking.org.uk/

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