# AFEP newsletter

March 2016

## CHAIRMAN'S COMMENTS

Dear Members,

Here we are towards the end of Quarter 1 and as usual our industry has not stood still. GBP continues to be tested by the forthcoming 'Brexit' referendum and ongoing 'China Crisis'. There is the entertainment being provided by the US elections and accompanying impacts on markets. Closer to home the AFEP Executive is busy working in the background to keep members appraised of issues that impact and taking part in a plethora of regulatory consultation activities as we gear up for the anticipated changes.

In October 2015 Michael Southgate provided the digest on sanction screening tools as part of our 'best practice' guidance, which he then followed up with a presentation at the December member meet.

In November 2015 Millie Richardson co-ordinated the production of the Treating Customers Fairly Best Practice Guide and this was duly circulated to members. Also in November Ian Benson circulated the Safe Harbor Ruling by the European Court of Justice. All members are encouraged to keep this in mind when sharing data with US located persons. We also provided members with highlights of the PSD2 progress.

In December there was the member meet, which many of you attended. We heard from HMRC on the current state of the Common Reporting Standard and its relevance for Authorised Payment Institutions and E-Money Institutions.

Jude Bahnan provided an update on FX forwards and timings as envisaged under the MiFID2 proposals. We continue to focus on MiFID 2, which has now been formally delayed to 2017 for 2018 implementation. This newsletter contains an update.

AMLD4 continues to be a focus of our horizon monitoring, as does PSD2. Members of the executive are in consultation with HMT & FCA and in this newsletter we share an update on the comprehensive response on 'strong authentication' given to the FCA. In the background there are a number of PSD2 consultations focussing on different aspects of the proposed new regulations and the FCA / HMT liaison team are active participants.

We have highlighted an important Advertising Standards ruling on the use of rate comparisons using inter-bank rates in this newsletter and we encourage all firms to review their approach.

Forthcoming Events for your diary are:

- Member meet 9th March at MMS
- Fraud Round Table – first of our new initiatives and we will be asking for interest at the member meet so we can book space and dates.

Francesca Maritan

**Chairman**

# Consumer Rights Act 2015 (CRA) redefines consumers

The CRA came into force on 1 October 2015 and is the first significant piece of legislation addressing the fairness of terms in consumer contracts since the Unfair Terms in Consumer Contracts Regulations 1999 (UTCCR).

The new legislation applies to APIs/EMIs that deal with clients who are 'consumers' - which is widely defined, catching any 'individual acting for purposes which are predominantly outside their business, profession or trade', and extending to sophisticated and high-net-worth clients. Under the CRA, the burden of proving that a client is not a consumer falls on the bank.

A recent European Court of Justice (ECJ) case (Horatiu Ovidiu Costea v SC Volksbank România) - where a lawyer entered into credit agreement with a bank, who later challenged the fairness of a term of the agreement, highlights a key issue. The ECJ concluded that even a lawyer with sophisticated technical knowledge could still be a consumer, as he or she could still be the weaker party, compared to a (bank) supplier with their superior bargaining power.

The CRA also sees the introduction of important new measures, which have implications for all businesses, including APIs/EMIs, in their dealings with consumers. In particular, any oral or written statements made by a bank (or someone acting on behalf of a bank) about it or its services, which are taken into consideration by a consumer, will be regarded as a binding term of that contract, if the statement is relied upon by a consumer, before or after entry into the contract.

Consequently, a consumer who can point to such a statement will now have a ready-made relatively straightforward claim for contractual damages. APIs/EMIs will, therefore, need to be even more cautious with any statements made about themselves and the services they provide, as well as careful about their use of agents.

The CRA adopts the existing test for unfair terms: a term is unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations to the detriment of the consumer. Previous familiar FCA guidance on the UTCCR is no longer available and, therefore, reference will need to be made to new CRA guidance issued by the Competition and Markets Authority. APIs/EMIs will need to observe this guidance in their terms when entering into business with consumers.

In addition, under the CRA so-called 'consumer notices' will not be binding on a consumer should they be unfair. A consumer notice is widely defined as any oral or written announcement or communication which relates to rights or obligations between the bank and the consumer, or restricts the business' liability.

The UTCCR 'main subject matter' and 'price exclusion' from the 'fairness requirement' has also been tightened. Now, in addition to being in plain and intelligible language, such terms must also be sufficiently prominent, enough for an average, reasonably well-informed, observant and circumspect customer to be aware of the term.

Finally, the CRA expressly regulates contracts for the supply of digital content, or "data which are produced and supplied in digital form". This is a wide definition and includes both physical and non-tangible software and apps. The CRA requires such content to comply with standards similar to those relevant to the provision of goods. While 'free' digital content will not be subject to these standards (as long as it does not do damage to a consumer's equipment or device), the standards will apply if the free of charge digital content was part of a package of goods, services or other digital media that is paid for.

The CRA is a step-change in UK consumer legislation. Its impact on APIs/EMIs could be significant, who should to review their customer documentation and procedures in the light of this.

# PSD 2 – Strong Customer Authentication – brief introduction and update on committee's response to EBA discussion paper

One of the AFEP executive committee legal team's objectives is to make members aware of relevant upcoming legislation. One such piece of legislation is the requirement for strong customer authentication, as set out in the second payment services directive (**PSD2**), the specific details of which will be contained in regulatory technical standards which are yet to be published.

Article 97 of PSD2 states that member states shall ensure that a payment service provider (PSP) applies strong customer authentication where the payer:

(a) accesses its payment account online;
(b) initiates an electronic payment transaction;
(c) carries out any action through a remote channel which may imply a risk of payment fraud or other abuses.

Article 98 of PSD2 requires the European Banking Authority (EBA) to draft regulatory technical standards on requirements of strong customer authentication and communication. The very earliest these regulatory technical standards will come into force will be October 2018.

"*Authentication*" means a procedure which allows the PSP to verify the identity of a payment service user or the validity of the use of a specific payment instrument, including the use of the user's personalised security credentials. "*Strong Customer Authentication*" means an authentication based on the use of two or more of the following elements:

(a) knowledge (something that the user knows);
(b) possession (something only the user possesses); and
(c) inherence (something the user is).

These elements need to be independent, in that the breach of one does not compromise the reliability of the others, and is designed in such a way as to protect the confidentiality of the authentication data.

Prior to the publication of a consultation paper which will contain the draft technical standards, which is currently expected in Q2 of 2016, the EBA and European Central Bank (ECB) decided to issue a discussion paper so that they can benefit from input by key market participants. The discussion paper did not suggest any specific regulatory solutions. Instead, it identified the problems or issues that the future regulatory approach is meant to mitigate, and asked respondents to express their views on the way the EBA has identified and characterised the problem. The executive committee has issued its response to the discussion paper on behalf of members.

# ASA industry ruling

Some members will no doubt be aware that ERIS FX, a non-member firm, has complained to the Advertising Standards Agency ("ASA") about the currency converters used by several member firms. The key complaint being that it is misleading to use a converter which shows the interbank rate as opposed to the client's actual rate.

Due to the thematic nature of the complaints received the ASA decided to use one such complaint as a test case and the firm in question was, unfortunately therefore, denied permission to come to an informal resolution. Given the industry impact, AFEP made representations to the ASA on behalf of the member firm and, while the ruling found in favour of the complainant, it is in line with what was requested both by AFEP and the firm. Key points to note are:

1. The ASA accepted that, while the interbank rate is not available to clients, it can be a useful tool. This is particularly true of clients wanting to understand what is happening in the market or monitoring their margin call positions.

2. The ASA ruled against the firm as, even though there was a clear explanation that the converter showed an interbank rate, it showed a potential saving. Using the interbank rate in the context of a savings claim gave the impression that the rate would be achievable.

The ruling therefore does not prohibit the use of interbank currency converters but does prohibit the use of such converters "in the context of claims about the rates that consumers could get…….,if the converter used rates and displayed amounts that were not achievable by consumers."

AFEP's Position and Future Action

AFEP continues to support advertising which is clear, fair and not misleading. We are pleased that the use of interbank converters is still permitted as, in the right context, these provide valuable information to consumers. We would now urge member firms to review their existing currency tools, in light of the ruling, and ensure that there is clear information for the customer and that, where interbank rates are displayed, these are not linked to savings claims or offered rates and cannot be construed as confusing for the consumer.

AFEP will work with the Committee of Advertising Practice ("CAP") as they work to achieve sector compliance and will advise members of any further requirements that arise from this work.

# Regulators and PSD II

There was a joint launch event on 29th January held by HMT and the FCA. They are looking to engage closely with industry for input into European negotiations during the first phase of transposition ahead of a formal consultation in the summer. It was also to provide an opportunity to meet with Edward Corcoran, who has taken over from Kate Appleby as head of the Payments Branch in HMT, and the wider HMT and FCA transposition team.

HMT and the FCA have sought input from industry groups to help them identify any areas requiring additional guidance or clarification during transposition. The following have been identified, but we urge members to let us know of any other areas you think we should consider:

| Article | Issue | Explanation/question |
|---|---|---|
| 36 – Access to accounts maintained with a credit institution | As MSBs our membership, particularly smaller members, have faced significant challenges both accessing and retaining access to banking which creates overreliance on individual banking counterparties and a significant barrier for new entrants in the market. We are not sure that the current wording will adequately ensure that there is greater access to banking for our members. | It would be very helpful to get greater clarity on the definition of "non-discriminatory and proportionate basis" and guidance on how banks would be expected to assess this. The current concern is that, while very well intended, it has little actual impact. |
| 18(2) | "where payment institutions engage in the provision of one or more payment service, they may hold only payment accounts which are used exclusively for payment transactions" | We are not entirely clear what this means or what the intention behind it is. We would like to better understand what impact it may have or issues it may raise for our members and to assess any potential unintended consequences. For example can a member firm still use DD to collect funds into a payment account? Can FX trades settle into a payment account for onward distribution to a beneficiary? |
| 18 (1)(a) | This covers related ancillary services but is unclear at what point they are ancillary and how this impacts the payment transaction. | In the FX market there is considerable debate about whether a customer is essentially requesting a payment in a foreign currency (i.e. FX is ancillary to the payment) OR whether these are two separate transactions i.e. they want to convert currency and enter into an FX transaction, once the currency is held they then initiate a payment. Most framework contracts operate to the latter model and legally separate the FX from the payment instruction. However there is a considerable potential knock on impact on the consumer as there is currently inconsistency in respect of segregation and safeguarding and whether or not payment account permissions are required. |

# MIFID II and FX forwards – update

The European Commission have now confirmed that the implementation date for MiFID II has been delayed by one year to Jan 2018. So while the rest of the UK financial services industry breathes a sigh of relief, what has not been clarified is the position of FX forwards under MiFID II. This will be determined by the Delegated Acts, which were due to be published last September, pushed out to December 2015, then January and are now anticipated in March 2016, but as before the timing may slip further.

Whilst the expectation is still that certain shorter-dated FX forwards connected to a payment obligation will remain out of scope, we do not know if this will come into force in Jan 2018 or an earlier date. We have been in touch with both HM Treasury and FCA who are equally in the dark and are not in a position to confirm the expected content of the delegated acts or the timing at this stage. In the meantime, we will continue to engage with HMT and FCA about this important issue on behalf of AFEP and its members.