



# **Simplifying Access to Markets Working Group**

## **Liability in indirect access models sub-group**

### **Solution Description:**

**Accountability of Providers and Participants in  
Indirect Access Models**

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Approved [date]

***Working group objective is to examine whether and how payment systems can be developed in order to simplify access and participation in the markets for PSPs.***

## Solution Concept Assessment

### SOLUTION NAME: LIABILITY MODELS

#### PROBLEM STATEMENT:

PSPs seeking indirect access (IPSP) to the payment systems may be denied access because no indirect access provider (IAP) will provide services to them. This may be despite the IPSP having in place clear risk-based criteria for Know Your Customer, Anti-Money Laundering, Sanctions risk and other liability avoidance processes, as will the IAP. The small number of IAPs, and their similarity of type, has led to similar outcomes for various types of IPSP.

Although the IPSP is an authorised or regulated entity, IAPs remain concerned that they may be liable for an IPSP's shortcomings in meeting its AML/Sanctions checking responsibilities. IAPs with international activity, particularly in the USA, are concerned about the action by the US authorities. Money Remitters and small Payment Institutions are on record that they face particular barriers.

The core IAPs in the UK are Barclays, RBS, Lloyds and HSBC. The PSR Interim Access Review noted they have 80% of the SME market and 85% of IAP relationships. It also confirmed awareness of at least four further PSPs that are planning to become IAPs, and that it considers this entry and expansion to be likely, swift enough and sufficient in scale to address many of the concerns it has raised around indirect access.

PSR's review also states that it is aware that some non-agency IPSPs face a limited choice of IAPs, and that for many small IPSPs having a bank account is equivalent to having indirect access. A survey conducted by the Association of UK Payment Institutions (AUKPI), shared with PSR in connection with its review, showed that 35 out of 39 applications for bank accounts had been turned down, and 51 out of 71 respondents had had a bank account closed in the past 2½ years<sup>1</sup>.

Clarity is therefore needed so that when an infraction of rules/procedures is caused by an IPSP, the risk and liabilities are not excessive for IAPs, so that more are encouraged to offer this service and to a wider range of PSPs.

The new sub-group has comprised representatives from the SAM and Financial Crime WGs.

#### ***Detriments Addressed***

1. It remains difficult for Indirect PSPs to obtain bank accounts, and in some cases to retain their bank accounts as IAPs withdraw account services;
2. Larger IAPs are constrained by the threat of cross-jurisdictional AML/CTF/Sanctions breaches/Fines; and
3. IAP market remains small but is expected to grow, albeit growth may be slow.

There was a general acceptance of the principle that the 'polluter pays' for any infraction.

<sup>1</sup> PSR MR1512-indirect-access-market-review-interim-report.pdf Page 30

The PSR in its Indirect Access Market Review Interim report MR15/1.2 set out two relevant findings under its Finding 6:

**7.23 Financial crime regulation is a market characteristic that has an important influence on IAP behaviour.** *Some IAPs apply minimum revenue thresholds for new IPSP customers and have introduced de-risking policies for existing IPSPs – where they terminate access for customers perceived to be higher risk – in order to mitigate the perceived risks and costs associated with financial crime (chiefly money laundering and terrorist financing). This has particularly affected small non-agency IPSPs.*

**7.24** *IAPs also have different commercial appetites for attracting new (and retaining existing) IPSP business. Some want to expand their IPSP activities, while others are more selective about which IPSPs they serve. Generally speaking, large agency IPSPs and medium (agency or non-agency) IPSPs are seen as most attractive, while many IAPs have only limited interest in smaller non-agency IPSPs.*

## CURRENT STATUS OF INTERESTED PARTIES

Preliminary research was carried out by a sub group of the SAM WG called Liability in indirect access Models. The following observations were made:

- Most IAPs operate both within and outside the UK and are subject to global regulations which means that implementing uniform policy standards is difficult without global consensus among regulators;
- It was generally agreed that for any individual IAP, the potential benefit from servicing an IPSP was small in regards to the IAP's overall commercial operations, whereas the risk in servicing the IPSP (due to potential AML/KYC breaches) was virtually unlimited. Therefore, even though the possibility of damage from servicing any one IPSP might be tiny, the unbounded potential reputational risk incurred means that IAPs are less likely to provide services to IPSPs, and there is evidence that services continue to be withdrawn from some IPSPs; and
- A number of concerns around liability may be more immediately mitigated by the growth of IAPs that are domestic businesses, supported by the provision of simplified direct access and unified standards.

The PSR in its Indirect Access Market Review (Chapter 8/para. 8.5) also stated that it was '*aware of at least six reviews underway or recently concluded which may affect the way financial crime regulation applies in the UK and internationally. These reviews are aimed at improving the transparency, clarity and effectiveness of the UK's anti-money laundering and counter terrorist financing framework*'.

Since then the FCA has in its 2016 Business Plan identified Financial Crime and Anti-Money Laundering as one of its seven priorities and signalled its continued intention to work closely with Government and other regulators on regulation e.g. the EU's Fourth Money Laundering Directive (4MLD), which requires UK implementation by mid-2017, and its participation in the Financial Action Task Force (FATF), as the standard setting body to combat such crime and threats.

On 24<sup>th</sup> May 2016, FCA published its research on the issue of 'de-risking,' a term it uses to describe its observations that 'banks are withdrawing or failing to offer banking facilities to customers in greater volumes than before'. There is a perception that this is driven by banks' concerns about the money laundering and terrorist financing (ML/TF) risks posed by certain types of customer.

In April 2016 the Government released its action plan for anti-money laundering and counter-terrorist finance.

For further information follow this link:

[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/517993/6-2118-Action\\_Plan\\_for\\_Anti-Money\\_Laundering\\_print\\_.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/517993/6-2118-Action_Plan_for_Anti-Money_Laundering_print_.pdf)

The WG is particularly interested in proposals which improve the current state of affairs, where both the IAP and the IPSP have to duplicate and perform AML/CTF work for the same payment (by providing some kind of Safe Harbour for the IAP, given the AML/CTF work carried out by the IPSP). The WG proposes to liaise with the Home Office and FCA and industry contacts to understand current developments more clearly before proposing any formal activity, since this priority area for legislators and regulators also covers the WG's area of concern.

Engagement is underway with BBA on its work through the Joint Money Laundering forum, and with the FCA. Both of these will be progressed to support this paper ahead of 27<sup>th</sup> June.

## **SOLUTION DESCRIPTION**

Both the SAM and Financial Crime, Data and Security WGs agree the need to ensure a healthy end-to-end payments infrastructure, with clear guidance to all participants and users. This becomes increasingly important as more new type participants enter the market.

The early solution proposed a mapping exercise and analysis, with the objective of seeking clarity on which party holds the responsibility for such obligations and in doing so identify where a solution needs to be found. We think this may still form a useful part of next stage activity and who undertakes this will need to be agreed. It will be important to ensure that any agreed Solution actions (1-4 below) covering obligations/responsibilities' mapping are made available to all that require it.

To this we have added a number of other actions arising from our subsequent discussions and the inputs attached in the appendices.

## ***Solution Objectives***

- a. To ensure greater transparency at a transactional level for an IAP and an IPSP handling the same payment, such that KYC and AML requirements, responsibilities and liabilities are clear and can be carried out sufficiently and reasonably.
- b. To ensure clearer defined rules describing what criteria a PSP needs to meet to qualify for a bank account.
- c. To simplify and standardise the accreditation process of direct and indirect access to markets.
- d. To standardise reporting requirements.
- e. To understand the end to end AML etc., accountabilities as they apply to payments flows in the UK.
- f. To agree a common level of required industry practice that relates to KYC and AML.
- g. To determine if safe harbours is a relevant concept to the solution, and provide assurance to IAPs that they can service IPSPs without undue liability.
- h. To examine the de-risking of banking and how it has impacted commercial business.
- i. To consider how other players with different risk outlook might be encouraged to become IAPs.

## ***Solution Actions***

1. Produce a clear mapping of parties in the payment chain and articulate regulatory and legal responsibilities for each player and where, if a party accesses a payment system via another party, where responsibility is considered to arise and when this applies;

2. The definition of the liabilities remains broad and may have different meanings to different people – sanctions, AML, US OFAC requirements etc. These will be split out and worked on to provide clarity. Expertise will be sought from Financial Crime WG representatives;
3. Liaise and work with the Home Office in clarifying Safe Harbour and liability issues arising from an IAP and a IPSP handling the same payment, and look to promote early publication of such findings;
4. Based on the mapping, look at flows, the checks performed and what changes to liabilities etc. need to be made, depending on the services used or provided. There may also be a need to clarify, depending on the regulated party is, who can take action against it;
5. From this analysis, syndicate to interested organisations, including relevant regulators;
6. Engage with possible new participants in the Bacs, Faster Payments and CHAPS schemes to determine what actions can be taken by industry and/or regulators to assist them in entering the market;
7. Determine what the FCA, Prudential Authority, Home Office and Bank of England are doing with regard to liabilities particularly to open markets to attract more IAPs, and liaise with them; and
8. Clarify the industry position in relation to the PSOs and regulators with a view to opening access to markets, encouraging new IAPs, increasing competition and determining clear transparent accreditation rules.

Other considerations:

- Whether there may be commercial solutions, which might link with other solutions e.g. technical aggregators. There is precedent with CLS which performs OFAC scanning centrally for its participants. Could there be a collaborative/competitive solution developed for the payment systems? Further consideration and discussion to take place;
- On liability issues, a sponsor is responsible for its Direct Debit indirect participants and thus this may need to remain in scope although the outputs of the proposed Bacs DD indemnity review will need to be evaluated; and
- Clarity is needed on:
  - o How the FCA supervises PSPs, and similarly how HMRC supervises Money Services Businesses; and
  - o With the development of the PSD 2 AISP model to access account data – if a payment is made in error based on that data, which party will be liable.

## PEOPLE INVOLVEMENT AND ACTION

WHO	WHAT
FPS	AML report has already been shared with Working Group.
SAM Working Group	<ul style="list-style-type: none"><li>Mapping of flows, liabilities, regulatory status and other requirements.</li></ul>
PSR / Bank of England / FCA	<ul style="list-style-type: none"><li>Support discussions and ultimately support changes to legal/regulatory frameworks to clarify liabilities for payments infractions.</li></ul>
Liabilities Sub Group	<ul style="list-style-type: none"><li>Produce topography of payments participants and how they are affected.</li></ul>
Home Office	<ul style="list-style-type: none"><li>Taking forward Government April 2016 Action Plan to examine Safe Harbour service for IPSPs where both parties are handling the same payment.</li></ul>

### LEADERSHIP

The SAM Working Group will provide initial leadership in developing the mappings. However it will need to engage actively with expert stakeholders to bring clarity and to make any change required possible.

### COMMUNICATION

A communications programme will need to be developed as part of any agreed changes to the legal and regulatory framework affecting liabilities, and it will need to be agreed where this is led from for the payments industry. There will be a need to ensure, from the AML, FinCrime and indirect access perspectives, that communications and related activities are aligned to deliver expected outcomes.

### SYSTEMS AND PROCESSES

Little direct impact on systems and processes within participants – this is mainly around legal and regulatory compliance /change. However once liabilities have been clarified, changes would result from the likely different operating models that would emerge for IAPs and IPSPs.

### DEPENDENCIES

- Potential regulatory willingness to engage /take action to take this subject forward and deal with the associated legal and regulatory framework changes that may be needed; and
- Clarification of regulatory requirements not only in the US but other international jurisdictions may be required and there may be dependency on UK regulators as to how this should be addressed.

### COST BENEFIT ANALYSIS

The initial phase of any activity i.e. mapping, analysis and engagement is low cost, and would create the platform to determine what further activity might be needed.

Any technical developments, such as potential central OFAC screening, would need formal cost: benefit analysis if a proposal were agreed. This would be considered as a medium-sized industry development.

Cost	Benefit
- Cost of making legal and regulatory framework changes to clarify liabilities	- IAPs and IPSPs would have clarity over their respective responsibilities and liabilities.
- Additional cost of regulatory fines and reputational damages for participants when AML / KYC procedures are incorrectly followed	- More IAPs are likely to consider offering services if liabilities and risks are clearly understood.
	- Financial models are clearer for challenger banks and new entrants using indirect access to payment systems via an IAP which will assist business planning and risk management.

## SECURITY / RESILIENCE

No direct impact expected on security and resilience. This change could encourage more indirect participants, with potential impact on these topics.

## EXISTING OR IN-DEVELOPMENT SOLUTIONS

Current regulator publications now issued which may lead to industry engagement but no known solutions are currently in-development and any this would be a new initiative.

## INTERNATIONAL INSIGHTS / BENCHMARKS / HORIZON SCANNING

As part of the proposed analysis, it will be important to look at international comparisons and how other countries manage the same/similar risk/liability issues for access to payment systems. This could give alternative approaches.

## COLLABORATIVE OR COMPETITIVE

This solution is very much about collaboration to determine the true extent of the issues still and what is currently being considered to mitigate these. The issues are long-standing and known, with regulatory and industry engagement and discussion. However the access concerns remain and the 'solution' is to ensure that a clear understanding is developed of issues to be resolved.

## QUICK WIN VS SUBSTANTIAL PROJECTS

The mapping and initial analysis ought to be capable of being completed within months – after which time planning will be required for longer term changes, e.g. changes to regulatory guidance / legislation.

## IMPLEMENTATION APPROACH AND TIMEFRAME (OVERALL)

As noted above, the initial analysis could be completed within months. Changes to legislation and regulation are likely to take multiple years.

## IMPACT: SUCCESS METRICS

Success would mean that IAPs and IPSPs would have full clarity of the liabilities they are taking on, what being regulated (e.g. as an Authorised Payment Institution) actually means in liability terms, and ideally a clear understanding that the principle of 'polluter pays' applies when it comes to regulatory infractions.