

The Payments Revolution – *is your head on the block?*



6 March 2009

The implementation of the EU Payment Services Directive (the “PSD”) on 1 November 2009 will have a major impact upon businesses that provide “payment services”. You could commit a criminal offence if you provide a payment service in the UK without proper authorisation or registration as a “payment institution” under the Payment Services Regulations (the “PSRs”). You may also be subject to certain prudential and “conduct of business” (COB) requirements imposed by the PSRs.

Payment service providers

You will not fall within the scope of the PSRs unless you are a “payment service provider”. These are businesses that carry out one or more of the payment activities listed in Box 1 – and do so “as a regular occupation or business activity”. These payment services may be provided to a consumer, a charity or a business, whether as a payer or a payee.

It is clear that banks, building societies and e-money issuers fall within this definition when providing payment services, but could your business also do so?

“Regular occupation or business activity”

There are, of course, a broad range of businesses that may perform payment activities as part of their business. Investment firms can, for example, hold and transmit client money; and, to that extent, perform one or more payment activities. However, these payment activities generally enable or facilitate the investment firm to perform its main business– to provide investment services (and not payment services). The activities are a *necessary* or *integral* element of its investment services. Crucially, they are not activities performed as, or as part of, a regular business activity that is *separate* from the main business of the investment firm. Similar considerations apply to a law firm's operation of its client accounts.

Care must, however, be taken here. It is possible to carry on payment activities as a “regular occupation or business activity”, **even if your main business is not the provision of payment services**. For example, the main business of a chain store or petrol company is to sell its goods or services to customers. However, if that same chain store or petrol company issues a payment card to enable customers to purchase goods or services sold in its stores or petrol stations or elsewhere, then the issue of that payment card would (in the absence of a relevant exemption or exclusion) be a separate “payment service”. This is because the activity of *issuing* a payment card is *not* a necessary or integral element of its main business activity of selling goods or services. This contrasts with the activity of *accepting* a payment card by way of payment, which is clearly an integral part of selling your goods or services and does not, therefore, amount to the provision of a payment service.

In essence, a business may carry on more than one regular occupation or business activity. The further away that payment activities are on the spectrum from your main occupation or business activity, the more likely it is that those payment activities will be carried on as a separate occupation or business potentially falling within the scope of the PSRs.

Key client points:

- *Criminal offence to provide payment services in the UK without authorisation*
- *You may be providing payment services even if this is not your main business*
- *There may be exemptions or exclusions available to you*
- *You may not be providing your payment services "in the UK"*

Exemptions and exclusions

- Regulation 3 of the PSRs provides that the regulations do not apply to credit unions, municipal banks and the National Savings Bank (but the FSA will maintain a register of exempt institutions that do provide payment services).
- Part 2 of Schedule 1 to the PSRs contains a list of “negative scope” activities that do not constitute payment services – examples are given in Box 2.

Key negative scope exclusions include the “securities asset servicing” and “limited network” exclusions.

“Securities asset servicing” exclusion

In those limited cases where an investment firm is providing payment services by way of business - that is in addition to, rather than as part of, its main investment services - the PSRs will not apply to payment transactions related to securities assets servicing, including dividends, income or other distributions, or redemptions or sales.

The circumstances in which this specific exclusion is likely to be needed will be exceptional. As a general matter, we would expect any payment activities carried on by an investment firm to form part of its main investment services; and, therefore, such activities should not themselves be carried on “as a regular occupation or business activity” of the investment firm.

However, it may be a useful exclusion for such firms to the extent that their payment activities cannot be considered to be a necessary or integral element of the investment services provided to customers. In such cases, the PSRs will not apply to those payment transactions that are connected with securities asset servicing, while they will apply to payment transactions that fall outside the scope of the exclusion and are provided by the firm as part of a separate business activity.

“Limited network” exclusion

The “limited network” exclusion forms part of a broader exclusion which applies to services based on instruments that can be used to acquire goods or services only:

- in or on the instrument issuer’s premises;
- under a commercial agreement with the issuer, either within a limited network of service providers or for a limited range of goods or services.

In its draft Perimeter Guidance, the FSA has indicated that the question whether or not a “limited network” exists must be determined by reference to various factors (none of which is likely to be conclusive in itself). These include the number of service providers involved; the scale of the services provided; whether membership of the network is open-ended; the number of clients using the network; and the nature of the services being offered. Likely candidates for this exclusion include transport cards, membership cards, petrol cards and store cards. However, we would not expect “city cards” to benefit from the exclusion, as they provide users with access to a broad range of goods and services offered by a city’s shops and businesses.

It is worth noting that the “limited network of service providers” and “limited range of goods” elements of the broader exclusion are disjunctive (“either ... or”). It follows that the exclusion would still be available if a broad range of goods or services is provided within a limited network of service providers; or, conversely, if a limited range of goods or services is provided within a broad network of service providers.

Territorial scope

If you conclude that you are carrying on payment activities as a regular occupation or business, and no relevant exclusion or exemption is available to you, you will need to consider whether you are providing those services “in the United Kingdom” - as the PSRs only potentially apply to businesses that do so.

You will only provide a payment service *in the UK* if you have a “legal presence” here. This requires you to provide your payment services from “an establishment” located here. This includes your head office or a branch. It also includes those cases where you use an agent located in the UK to provide payment services and the agent:

- has a permanent mandate from you to transact payment services;
- is subject to your management and control; and
- is able to commit you to provide payment services to clients.

It follows that merely because you provide payment services to UK-based customers will not in itself mean that you are providing such services “in the UK”. If you do not have a legal presence here or in another EEA state and, for example, contract to provide payment services to your customers through the internet or other means of distance communication, you are unlikely to fall within the scope of the new regime.

EEA authorised payment institutions

If your head office is in another EEA state (your “home state”) and you are authorised by your home state as a payment institution, you will be able to provide your services in the UK without any further requirement to be authorised or registered under the PSRs. Such “EEA authorised payment institutions” can provide their payment services from an establishment or otherwise cross-border by exercise of “passport rights” under the PSD and PSRs. The prudential requirements of your home state will alone apply to you in such cases.

Where an EEA authorised payment institution provides its payment services in the UK from an establishment here, it will however need to comply with the COB requirements of Part 5 (information requirements for payment services) and Part 6 (rights and obligations in relation to the provision of payment services) of the PSRs.

Box 1: Payment activities

- (a) Services enabling cash to be placed on a payment account and all of the operations required for operating a payment account;
- (b) Services enabling cash withdrawals from a payment account and all of the operations required for operating a payment account;
- (c) The execution of the following types of payment transactions –
 - (i) direct debits, including one-off direct debits;
 - (ii) payment transactions executed through a payment card or a similar device;
 - (iii) credit transfers, including standing orders;
- (d) The execution of the following types of payment transaction where the funds are covered by a credit line for the payment service user-
 - (i) direct debits, including one-off direct debits;
 - (ii) payment transactions executed through a payment card or a similar device;
 - (iii) credit transfers, including standing orders;
- (e) Issuing payment instruments or acquiring payment transactions;
- (f) Money remittance;
- (g) The execution of payment transactions where the consent of the payer to execute the payment transaction is given by means of any telecommunication, digital or IT device and the payment is made to the telecommunication, IT system or network operator acting only as an intermediary between the payment service user and the supplier of the goods or services.

Box 2: Payment services

The following are examples of payment services:	The following are <u>not</u> payment services (“negative scope” activities):
<ul style="list-style-type: none"> • cash account deposits and withdrawals • credit transfers (including standing orders) • direct debits • payment card transactions (e.g. credit card/debit card transactions) • issuing payment instruments (including e-money, password or PIN-initiated payments) or acquiring payment transactions (e.g. merchant acquiring) • money remittance (including certain forms of bill payment services where provider does not merely act as agent of the payee) • IT/digital device-initiated payments (e.g. mobile phone network operations where provider acts as mere payment intermediary and does not add value to the goods or services purchased) 	<ul style="list-style-type: none"> • pure cash/banknote transactions • “cash back” services • physical transportation of banknotes and coins • bureaux de change providing cash only forex services • paper cheques and other paper instruments • settlement system transactions and other payment transactions between payment service providers acting as principals • payment transactions linked to securities asset servicing (e.g. dividend payments, share sales or unit redemptions) • technical services (e.g. the processing and storage of data as outsourcee for a payment service provider) • limited network instruments (e.g. staff catering cards, store cards, club cards) • intra-group payment transactions • independent ATM operators

Disclaimer

Please note that the contents of this note provide an overview only. This note is guidance only and should not be relied upon as legal advice. Clients’ circumstances will differ in each case. If you would like to receive specific advice on the new regime for payment services, please contact:

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