EPIF views on the Settlement Finality Directive (SFD)

Introduction

The Settlement Finality Directive (SFD), adopted in 1998, guarantees that transfer orders within the European Union which enter the intra-bank payment system of central banks or are used for clearing and settlement of securities are legally settled. The Directive ensures that when a transfer order has entered a system, it is "protected" from third-parties in the event of insolvency of one or more participants in the system.

The introduction of the SFD was an important development, right after the introduction of the Euro, to create legal certainty around settlement finality for Euro transfer orders. However, the scope of the SFD is limited to the circumstances of the Euro-introduction and does not reflect the emergent of new innovative business-models and services. The SFD precedes the introduction of the Payment Service Directive (PSD) and e-Money Directive (EMD). Meaning that e-money and payment institutions under the EMD2 and PSD2, respectively, are not currently eligible participants to the intra-bank payment systems as they are not necessarily deemed to offer settlement finality. EPIF would therefore welcome legal certainty in this regard by extending the SFD to bring our members into scope.

In the absence of a harmonised SFD solution at EU level, some Member States have introduced national solutions that allow e-money and payment institutions either direct or indirect participation in payment systems, provided they fulfil certain criteria. We agree with the European Commission that this situation has led to level playing field issues between Member States, fragmentation of the European retail payment market and legal uncertainty regarding the cross-border recognition of settlement finality on payment systems.

We would like to point out that under the current settlement arrangements for SCT Inst, EPIF members can only be indirect members of the TIPS ECB clearing arrangements. This puts the non-bank payment sector at a competitive disadvantage. Access to TIPS rests on our members having access to the system via their own banking relationships. Some of our members are facing the closure of bank accounts as banks reassess their AML/TF policies. The debate around de-risking demonstrates the dependence of the non-bank sector without direct access to TIPS via the intra-bank payment system. Indirect access also introduces supportability limitations, technical limitations and operational challenges, along with often opaque cost structures. The non-bank sector is dependent on the risk appetite and capabilities of a banking partner, limiting the level of functionality it can offer. This is particularly sensitive given that banks and non-banks are often in open competition. EPIF's membership will only really benefit from SCT Inst if the Settlement Finality Directive creates the legal framework for non-banks to have direct access to TIPS.

Evolution of the SFD importance

EPIF members have always supported an amendment to the SFD to extend direct access to the non-bank payment sector. With the evolution of the payments market and the objectives of the European Union, this is becoming increasingly urgent. The reason for the urgency is two-fold:

- In October 2022, the European Commission put forward its legislative proposal **mandating instant credit transfers** across the Euro Area. Due to the lack of direct access to intra-bank payment systems, which is reflected in an impossibility to have 'instant' settlements, payment institutions and e-money institutions were explicitly left outside of the scope of the proposal.
- The Eurosystem is also exploring the development of a **Digital Euro**¸ with a legislative proposal expected in May 2023. Without direct access to the underlying infrastructure needed to settle transactions in Digital Euros, non-bank PSPs will be dependent on their sponsor bank to carry out a competitive service (i.e., distribute digital euros), restricted in the services and functionality they can offer to merchants and consumers, and constrained in their capacity to help develop innovative cases for the Digital Euro.

Additionally to these forward-looking developments, non-bank PSPs still face significant challenges in the **application of the PSD2 rules**. Despite Articles 35 and 36 of the PSD2 establishing the legal right for non-bank providers to bank accounts, banks still have the commercial right to refuse access to said bank accounts on the basis of AML/CTF concerns *or* when it is incompatible with their business models. This has led to the so-called ***unwarranted de-risking*** practices, where banks refuse to open bank accounts or close bank accounts for non-bank payment providers.

These practices distort competition in the market, unbalancing the level playing field in favor of the banking sector.

Recommendations

In light of the above, EPIF strongly calls for payment and e-money institutions to be added to the list of eligible system participants under the SFD. This would ensure a level playing field and provide legal certainty in a cross-border context. The access to intra-bank payment systems should be conditional to the compliance with a number of pre-requirements to be established by the Eurosystem (e.g., capital requirements, liquidity requirements, etc.).

This amendment could take place either through a full dedicated revision of the SFD or through a targeted amendment taking place via another Regulation (i.e., the proposal for a Regulation on Instant Credit Transfers or revision of the PSD2). EPIF understands the concerns of the European Commission and co-legislators to re-open the SFD completely but we also highlight that an amendment through the PSD2 could not come into force until 2026 at the earliest. The non-bank payment industry therefore ideally calls for quicker action.

ABOUT EPIF (EUROPEAN PAYMENT INSTITUTIONS FEDERATION)

EPIF, founded in 2011, represents the interests of the non-bank payment sector at the European level. We currently have over 190 authorised payment institutions and other non-bank payment providers as our members offering services in every part of Europe. **EPIF** thus represents roughly one third of all authorized Payment Institutions ("PI") in Europe. All of our members operate online. Our diverse membership includes a broad range of business models, including:

- Three-party Card Network Schemes
- E-Money Providers
- E-Payment Service Providers and Gateways
- Money Transfer Operators
- Acquirers
- Digital Wallets
- FX Payment Providers and Operators
- Payment Processing Services
- Card Issuers
- Independent Card Processors
- Third Party Providers
- Payment Collectors

EPIF seeks to represent the voice of the PI industry and the non-bank payment sector with EU institutions, policy-makers and stakeholders. We aim to play a constructive role in shaping and developing market conditions for payments in a modern and constantly evolving environment. It is our desire to promote a single EU payments market via the removal of excessive regulatory obstacles.

We wish to be seen as a provider for efficient payments in that single market and it is our aim to increase payment product diversification and innovation tailored to the needs of payment users (e.g. via mobile and internet).