SNAPSHOT

PSD2 Payments

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What is PSD2?

To define PSD2, we need to revisit the scope of the first European Payments Service Directive (PSD) implemented back in 2009. The driving force behind both directives is harmonisation of the payments landscape to level the playing field amongst EEA countries, including payment service providers, with the end goal of increasing competitiveness, creating better value for consumers and, at the same time, reducing barriers to entry and expansion.

The common themes are concerned with opening up the market to new types of regulated organisations and defining common standards for data sharing amongst players in the payments industry.

PSD created a single market for payments (i.e. credit transfers, direct debits and cards) in the EEA and introduced the concept of PSPs, or Payment Service Providers (e.g. PayPal, WorldPay). Firms in the payment industry are regulated, but to a lesser extent than banks. PSD2 relates to electronic payments and builds on concepts introduced in PSD, aiming to reflect new developments in the electronic payments market (e-Commerce and m-Commerce), making payments safer, increasing consumer protection and fostering innovation and competition.

The industry is facing tight timelines, as January 2018 marked the first regulatory milestone where national governments had to transpose PSD2 into local legislation. The second milestone is the implementation of Regulatory Technical Standards on Strong Customer Authentication and Secure Communication Organisations must comply by Q3 2019.

Why is it important to the financial services market?

The main implication of PSD2 is that it will significantly increase the number of entities that can access customer data and initiate payments on their behalf, creating more choice and flexibility, but also creating more risk, particularly in cybercrime.

The key development is the creation of the Access to Accounts (XS2A) functionality. Retailers and banks will be able to communicate with each other using an open Application Programme Interface (API) for which the European Banking Authority (EBA) was given responsibility for defining the Regulatory Technical Standards (RTS).

This new business environment will drive changes to how banks operate and serve their personal and business customers. The impact of PSD2 will span beyond technical interfaces and services; banks will have to rethink their entire operating model and build relationships with FinTech players through acquisitions, funding and joint ventures in order to address functional gaps or inefficiencies.

In order to help banks to articulate a clear implementation strategy and transform their business model, a deep understanding of banking operating models will be required, as well as mobilisation and programme management capabilities.

What's the BCS view on it?

There is no doubt that the PSD2 regulation is disruptive. It is forcing the payments industry to re-think its strategy and business model, moving into a landscape that's both new and exciting.

PSD2 is coming in the midst of a maelstrom of innovation, change and regulation. We believe that those industry players who are able to position themselves amidst the fast pace of change will prosper, whereas slow movers could see their position weaken and struggle to keep up.

Despite its objective of creating a level playing field for the payments industry, participants are impacted in a variety of ways:

- For larger, established banks, the burden is on providing open access to their data in a real-time, access-controlled solution. This is a technological and data-driven challenge, exacerbated in some cases by historic under-investment in technology infrastructure. These players must innovate and explore new commercial opportunities created by PSD2 and the onset of Open Banking to keep their current position in the payments market.

- For smaller, challenger banks or FinTechs there are significant opportunities to disrupt and take business from established banks. It will be crucial to develop solutions that can consume and mine the wealth of data from competing banks, in ways that both generate revenue and add value for their customers. For example, Starling Bank has developed a mobile banking app which customers can use as a portal for all their banking products (held with any bank). These players have to innovate to disrupt the established players and achieve the same customer trust levels, though not all of them will succeed.

- For Payment Service Providers, central industry participants and payment schemes, the anticipated shifts in payment and data flows provide both opportunities, like the provision of aggregation or centralised services such as analytics or KYC; and threats like disintermediation and new cyber or fraud risk trends. These players must innovate to keep up with market demands and trends.

- Finally, for customers, who are expected to benefit from the reinvigorated competition, it could pose a breakthrough moment for those that are tech-savvy, allowing their banking services to converge in a single place, such as an app or aggregator portal, driving innovative services and competitive pricing. However, on the flipside, less tech-reliant customers could see this as a confusing, perhaps alienating development, and one that they didn't ask for.

It's difficult to predict the outcome of these changes in the long term. This is a "once in a generation" shift that has not been seen before in payments. In other industries (such as telecoms or taxi services), an opening of the marketplace by regulators or technology has caused incumbents to lose market share to newer participants offering cheaper and more innovative services.

Banks and Payment Service Providers now have the opportunity, and a short time window, to adopt strategies that prepare them for the sea change that's coming.

Who should you speak to about it?

Our Payments and Open Banking SME

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