

Prepare for the Payments Directive



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EXAMINE HOW CORPORATES
NEED TO GEAR UP FOR THE
PAYMENT SERVICES DIRECTIVE BY 1 NOVEMBER 2009.

The Payment Services Directive (2007/64/EC) and the Single Euro Payments Area (SEPA) are likely to focus the attention of businesses on payment data storage and security, and lead them to reconsider their payments needs.

European member states must implement the directive by 1 November 2009. It aims for transparency of information and charges, certainty of transaction execution, clarity on rights and liabilities of payment service providers and users, customer protection and the opening up of national payment transaction markets to competition from licensed non-bank payment institutions. It also extends the reach of European legislation protecting customers in the payments world from purely cross-border to domestic (including non-euro) payments.

The Payment Services Directive forms the legal basis for SEPA, an integrated payment services market with uniform terms and standards for transactions in euros across the European Economic Area (the EU plus Iceland, Liechtenstein and Norway) and Switzerland that is being created on the initiative of the European banking industry, represented by the European Payments Council (EPC). The first SEPA products became available from January 2008 and the aim is to build up a critical mass of users by the end of 2010.

The SEPA project sets out interbank rules and standards for payments in euros using direct debit and credit transfer schemes, and provides a framework for the clearing and settlement infrastructures which provide operational processing services for euro payments.

Executive summary

- One of the objectives of the Payment Services Directive is to bring Europe-wide competition to national payments markets, enabling non-bank payment institutions in the UK to passport their services. Entities with a large part of their business in payments may consider setting up a payment institution, while larger corporates may set up, and even passport, their own payment institutions.

Businesses benefiting most from the changes brought in by the Payment Services Directive and SEPA will be those that make the greatest savings from reduced charges, uniform processing standards and the opportunity to rationalise multiple accounts and banking relationships in different countries. These are likely to be multinationals operating cross-border throughout Europe with high levels of payment transactions of different types from different countries and using different invoicing and reporting formats.

TERMS OF BUSINESS FOR PAYMENT SERVICES CUSTOMERS

Customer protection and choice are among the main objectives of the directive, which gives payment service customers stronger refund rights, more information and transparency of information,

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IN A PURE SEPA ENVIRONMENT, BUSINESSES MAY NO LONGER NEED TO MAINTAIN RELATIONSHIPS WITH DIFFERENT BANKS IN DIFFERENT MEMBER STATES AND MAY PREFER TO HAVE A SINGLE EURO ACCOUNT WITH ONE PAN-EUROPEAN BANK FOR ALL EUROPEAN COLLECTIONS.

higher levels of certainty for payment transactions, and clearer rights on security matters. The directive sets out information obligations on payment service providers relating to the contracts for, and the authorisation and execution of:

- single payment transactions;
- transactions covered by a framework contract;
- transactions involving currency conversion; and
- the imposition of surcharges or deductions for the use of certain personalised payment instruments.

The obligations cover content and communication of the main terms of the transaction, including fees, charges and currency exchange rates. For example, article 67 of the directive requires the payer's and the payee's payment service providers and any intermediaries to transfer the full amount of the payment transaction and refrain from deducting charges from the amount transferred.

Titles III (transparency of conditions and information requirements for payment services) and IV (rights and obligations in the provision and use of payment services) of the directive apply to payments effected by payers and recipients within the same country, in contrast to the focus of earlier European payments conduct of business legislation on cross-border payments. Payment services contract terms may need to be revised if business users do not opt out of the title III rules, which they are likely to do if their existing terms are better than those set out in the directive.

BUSINESS DAY The directive defines a business day as one on which the payment service provider of the payer or the payee involved in a payment transaction is open for business, as required for the

execution of a payment transaction. The term is used in various customer-facing provisions of the directive, including deadlines for the deemed receipt of payment orders, the new maximum payment execution deadline and value dating requirements.

Businesses will want to consider how the business day terminology used for these and the directive's other time limits and rules would tie in with that used in other agreements, transactions, market conventions and processes which need to overlap with or are part of a chain which includes directive-governed payment transactions. A business day for a transaction falling under the directive may not be a business day for the purposes of a non-directive transaction, even though both are meant to be effected on the same day.

IMPLICATIONS OF D+1 Payment service users will benefit from the certainty introduced by full implementation of the directive's new maximum execution deadline in 2012, when transfers must be credited to the payee's account by the end of the next business day (D+1). Businesses will want to consider carefully the impact of D+1 on treasury products that settle under different market conventions and timelines and which are in the same processing chain as payments transactions within the scope of the directive, especially foreign exchange transactions settling two days after the trade date (T+2). Mismatches will need to be anticipated and dealt with up front so as not to trigger penalty clauses or indemnities.

PRICING The recitals to the directive make it clear that it is essential that payment service users know the real costs and charges of payment services so they can make a proper choice. Recipients should receive the full amount transferred by the sender of the remittance. Value dating, which can restrict the availability for use by a recipient of funds credited to their account, may no longer be used. Instead, same-day value payments will facilitate pricing transparency and reconciliation by users and recipients.

The aim of EC Regulation 2560/2001 on cross-border payments in euros was to reduce fees for cross-border payments to the level of those charged for domestic euro payments. Fees for cross-border payments made using SEPA instruments should also be the same as those charged for domestic transactions. The SEPA rulebook requires banks to inform payment beneficiaries of their service charges and greater competition between payment service providers is expected to reduce the cost of most transactions in Europe.

BANKING RELATIONSHIPS In a pure SEPA environment, businesses may no longer need to maintain relationships with different banks in different member states and may prefer to have a single euro account with one pan-European bank for all European collections. During the transition period, however, when both SEPA and non-SEPA products are in use, businesses may prefer to continue operating decentralised accounts in each member state in which they trade. Local regulatory and tax restrictions, a preference for maintaining existing bank relationships, or their own customers' preference for paying into local accounts or using non-SEPA paper-based domestic instruments such as cheques, may also lead to businesses maintaining decentralised accounts. The cost of changing accounts and banking relationships may also have a deterrent effect.

SWITCH TO SEPA-COMPLIANT INTERFACE Businesses will need to review their IT systems and internal processes to identify any changes required for them to become fully compliant with the Payment Services Directive and SEPA. The standardised formats for SEPA direct debits and credit transfers require uniform content

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A PAYMENT ORDER FOR A SEPA CREDIT TRANSFER WILL BE REJECTED BY SEPA-COMPLIANT SYSTEMS IF THE PAYER DOES NOT KNOW THE RECIPIENT'S IBAN. BUSINESSES ANTICIPATING SEPA-COMPLIANT PAYMENTS SHOULD PRINT THEIR OWN IBANS ON THEIR INVOICES AND MAKE SURE THEY HAVE THEIR CUSTOMERS' AND SUPPLIERS' IBANS.

(IBANs and BICs) and software (ISO 20022 XML standards) so that businesses can connect to their banks' systems and accept SEPA transactions. Corporates are not obliged to move to the ISO 20022 XML format, but legacy payment formats may no longer be supported by banks and software suppliers in the medium term, and a move to the uniform format may save technology support costs.

A payment order for a SEPA credit transfer will be rejected by SEPA-compliant systems if the payer does not know the recipient's IBAN. Businesses anticipating SEPA-compliant payments should print their own IBANs on their invoices and make sure they have their customers' and suppliers' IBANs. They will also need to update their databases and accounting systems to incorporate and store these new payment details, which begs the question as to how that data is securely stored and updated.

PAYMENT INSTITUTIONS One of the objectives of the Payment Services Directive is to introduce Europe-wide competition into national payments markets, enabling licensed UK non-bank payment institutions to passport their services. Entities which have a large segment of their business involved in payments, such as supermarkets or utilities, may consider setting up a payment institution. Larger corporates may decide to set up and even passport their own directive-licensed payment institutions.

But perhaps the hidden question is whether entities in financial sector groups need to become licensed as payment institutions. Challenging questions of interpretation arise on the scope of the directive in relation to providers of investment and other financial services that involve making payments. Entities providing payment services (including credit arrangements, cards and vouchers, refunds and online accounts: the definition in the directive's annex is wide) must become regulated as payment institutions from 1 November 2009. While there are carve-outs for banks and electronic money institutions, businesses in other areas such as telecoms, retail, transport and energy could be affected by the licensing and conduct of business requirements for payment institutions.

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