

MasterCard's Comments and Observations

on the European Commission's Communication concerning

a New Legal Framework for Payments in the Internal Market

MasterCard welcomes the opportunity to comment on the Consultative Document on the New Legal Framework for Payments in the Internal Market. Our comments are structured as follows: (I.) General Observations; (II.) Specific Observations; and (III.) Comments specifically relating to Electronic Money products.

I. General Observations

A. Scope of the proposed New Legal Framework - MasterCard seriously questions the appropriateness of covering all retail payment instruments (i.e. credit transfers, direct debits, debit and credit card payments, electronic purse, micro payments, etc.) under the same legal framework. As each of these payment instruments has specific features, it does not seem to us appropriate to include all of them under a "one size fits all" type of legal framework. Other than the fact that they are all means of payment, they have little in common to justify them falling under the same legal principles. By analogy to the transport sector, the Commission's approach would come down to making the different means of transportation (i.e. by road, air, sea, railway, etc.) subject to the same traffic rules.

The following Annexes of the Commission's Communication highlight this tension:

- On the right to provide payment service to the public (Annex 1), the Commission's proposal itself recognises that a different prudential regime must apply to the different types of payment activity;
- On information requirements (Annex 2), the need for information and the type of information to the consumer greatly varies according to the diversity of the payment products and services. A one size fits all approach does not seem to be appropriate; The Communication itself refers to the fact that *'some specific provisions applicable to certain payment services... may need to be considered'*;
- Value dates (Annex 4) take different forms according to the payment instrument involved;
- The same rules on revocability (Annex 10) cannot work across all payment instruments. The Commission's Communication itself recognises that revocability rules may have to distinguish between different means of payment;
- The aim of harmonising the rules on obligations and liabilities of the payment service provider in case of non-execution or defective execution of payment order (Annex 12) could result in taking away the incentive to enhance the service levels among competing payment instruments;

- The specific nature of the different payment instruments makes it inappropriate to introduce a general rule on the obligations and liabilities in case of unauthorised transactions (Annex 13).

At a minimum, the proposals contained in the Communication should identify in relation to each area proposed to be regulated which payment instruments are intended to be covered.

B. Regulation versus Self-Regulation

The Commission should be conscious not to introduce legislation in areas which so far have been left to market forces or self-regulation. As far as payment cards is concerned, this is the case for areas covered under Annexes 2, 4, 5, 7, 10, 11, 12, 13, 20 and 21. Introducing legislation in these areas could be counterproductive by stifling innovation, creating unnecessary complexity and compliance costs, which will inevitably be passed on to consumers. Furthermore, by the time of adoption, the legislation risks to be already outdated due to technological and market developments. For each of these Annexes, the Commission should therefore provide real justification as to why legislation is required.

C. New versus Existing Legislation

Quite a number of issues covered by the New Legal Framework are already regulated by way of existing Directives, Regulations and Recommendation. To the extent that the same issues would be legislated as a result of this new initiative, care should be taken to repeal provisions covering the same ground in previous legislation (inter alia the Distance Selling Directive, the Distance Selling of Financial Services Directive, the Cross-Border Credit Transfer Directive, the Regulation on cross-border payments in Euro, the Recommendation on the relationship between cardholders and card issuers, etc.).

D. Regulation versus Directive

On those issues where legislation is desired, MasterCard prefers the adoption of a Regulation over a Directive as it ensures a uniform legal environment across the EU.

II. Specific observations

The following are the Annexes we believe are particularly relevant to MasterCard and summarise our initial response. Annexes not referred to are considered to be not relevant to MasterCard's products and services.

Annex 01: Right to provide payment service to the public

- MasterCard agrees with the Commission's analysis, i.e. entities providing payment services and not having a banking license or electronic money institution license do not benefit from the single banking license and are subject to requirements imposed in each EU Member State;

- In addition, quite a number of new players are offering their services from outside of the EU to EU citizens without any form of supervisory or licensing regime. In order to create a level playing field, all operators active in the EU (irrespective of their place of establishment) should be subject to the same regime;
- MasterCard does not believe the first proposed option (i.e. applying mutual recognition) would work. Applying mutual recognition without harmonising minimum (licensing or registration) requirements for payment services would not create a level playing field. The third option (i.e. to transform the E-Money Directive into a general ‘Payment Institutions Directive’) is not materially different from the second option. MasterCard would first have to see the exact prudential regime before being in a position to comment;
- The (second) option to introduce a third licensing category, i.e. a so-called “payment institution license” *without the same level of prudential rules as required by the Credit Institution Directive or the E-money Directive, as there is no evidence that the simple payment transmission activity would require such extensive prudential regulation* gives rise for concern. It is unclear what level of prudential supervision these entities would be subject to. As a starting point, they should not contain a standard lower than the eligibility rules as applied by MasterCard. MasterCard’s eligibility rules require each applicant to be *a regulated and supervised financial institution that is authorised to engage in ‘financial transactions’ under the laws of the country or any entity that is directly or indirectly controlled* by such eligible financial institution. What constitutes ‘financial transactions’ for these purposes is widely defined;
- MasterCard requires members to be subject to a high degree of prudential supervision in view of its contractual obligation to ensure settlement of transactions originating from a failed member. Acquiring members can have significant liabilities in case a large merchant goes bankrupt;
- It is not clear from the Communication which type of payment services would be covered under this new licensing regime. We presume issuance of debit cards would be excluded as these are directly linked to the current account relationship involving deposit taking, an activity reserved to fully-fledged credit institutions;
- It is also not clear if the Commission’s proposal would result in a different licensing regime being applicable to card issuance versus card acquiring activities.

Annex 02: Information requirements

MasterCard does not believe there is a need to legislate in this area. Most of the information stipulated in the proposal is already provided by the issuer to the cardholder by way of the cardholder’s terms and conditions. The proposed text is too prescriptive and a large number of terms require definitions.

Whenever harmonisation at EU level of the information to be provided to the cardholder is chosen, it must consolidate the information requirements currently contained in other binding EU legal provisions (e.g. the Regulation on cross-border payments, the distance selling Directive, etc.).

Annex 04: Value Dates

The Communication refers to value dates as ‘*a complex pricing tool ...*’. The term ‘value date’ must be defined as it can refer to payment dates, posting dates or transaction dates. With regard to credit cards, the date from which interest runs varies from issuer to issuer and from product to product. As such, the use of value dates are competitive and should therefore be left to the market.

To the extent the proposal would not be limited to increasing transparency on value dates, but actually putting into question the very fact of value dates, it would go beyond the remit of the New Legal Framework.

Annex 05: Portability of Bank Account Numbers

It should be made clear that card accounts are not covered by this proposal. Not only is there no need for portable card account numbers, it would also not technically be possible under the current system’s architecture. For fraud prevention reasons, it is also important to be able to close down an account on its existing number and re-open under a new number.

Annex 07: The Evaluation of the Security of Payment Instruments and Components

Card industry security standards are agreed at a global level. Legislation supporting European standards could impede interoperability and increase the time and costs to market. Standardisation of security requirements should therefore be left to market participants.

This aspect is de facto also covered in the framework of the European Central Bank’s Oversight role.

Annex 08: Information on the Originator of a Payment (SRVII of FATF)

MasterCard is of the view that the obligation to carry with the transfer the name and address (or date/place of birth or customer/national ID number) of the originator is excessive and will jeopardise the Commission’s objective of promoting cost efficient means of transferring money. The goal in terms of enabling law enforcement agencies to track down terrorist activities can also be achieved by imposing on the remitting bank the obligation to maintain an appropriate record of the originator of the transaction. This database could then be made accessible by the receiving bank or public authority in case of an investigation.

Implementation of SRVII can best be done by EU legislation rather than national legislation. MasterCard agrees with the Commission’s approach that transfers within the EU should be considered domestic transfers and therefore fall under the minimum information regime of SRVII.

The question of the type of payment transactions to cover has been answered by the FATF Interpretation note to SRVII. With regard to payment cards, Section 10 of the note on exemptions stipulates that SRVII is not intended to be covered:

- a. *Any transfer that flows from a transaction carried out using a credit or debit card as long as the credit or debit card number accompanies all transfers flowing from the transaction. However, when credit or debit cards are used as payment system to effect a money transfer, they are covered by SRVII, and the necessary information should be included in the message.*

In order to avoid any doubt, the Commission should explicitly exclude the application of purse, debit and credit cards whenever they are not used as money transfer mechanisms.

As to the need for exemptions or thresholds, MasterCard supports the introduction of a Europe wide *de minimis* threshold of 3000\$ below which customer identification (name and address) should not be carried by the payment message. The absence of such a *de minimis* threshold could seriously impede the development of new products like person-to-person electronic purse solutions or other card-based money transfer products.

Annex 09: Alternative Dispute Resolution (ADR)

It should be clarified whether the proposed Article on ADR only covers cross-border disputes relating to ‘banking services’ (e.g. entering into a cardholder agreement) or would also include cardholder complaints resulting from the ordinary cross-border purchases paid with payment cards. If the Commission’s intention is the latter, the card schemes’ extensive chargeback procedures and rules on MasterCard cards effectively constitute an ADR mechanism.

Annex 10: Revocability of a Payment Order

It should be made absolutely clear in the text of the proposed article that the principle of irrevocability shall not conflict with other legal or contractual rights like a cooling off period or chargeback rights. Indeed, although merchants benefit from a payment guarantee, under certain circumstances the acquirer is entitled to claim the money back from the merchant (e.g. repudiated MOTO transactions, absence of authorisation requested by the merchant on transactions above the floor limit, etc.). Equally, the issuer should be allowed to reimburse the cardholder in certain circumstances (goods not as described, processing errors, etc.) despite the principle of irrevocability of payments.

Annex 11: Role of the Payment Service Provider in the Case of a Customer/Merchant dispute

MasterCard is opposed to any form of connected lender liability as the issuer, not being a party to the relationship between the cardholder and the merchant, is only involved in the execution of the payment transaction initiated by the cardholder. Issuers should not by law be forced to get involved in the settlement of a commercial dispute between cardholders and merchant. Cardholders already benefit from the chargeback rules as operated by MasterCard and its member banks.

The proposal for specific revocability rules for payments in e-commerce conflicts with the recommended approach under Annex 10.

Annex 12: Non-Execution or Defective Execution

MasterCard has difficulties with the Communication's reasoning that '*harmonised rules covering the obligations and liabilities ... of non- or defective execution would facilitate the establishment of a level-playing field between the Payment Service Providers in the Internal Market*'. A level playing field cannot be understood to mean harmonising the service levels among the competing payment system providers towards consumers. It merely refers to creating the conditions enabling economic actors to provide competing services. Obligations and liabilities of the service provider towards the consumer in case of non-execution or defective execution is part of these competing services.

It is not clear what would have to be understood or what would be the actual consequence if card issuers would be liable for the non-execution or defective execution of card payment transaction. According to Article 3, it would mean that the issuer would be liable for the amount of the non-executed payment order, as well as charges and interest thereon. Such a liability provision is clearly disproportionate and would open the door to widespread abuses.

The existence of (and reliance on) third party contractual relationships are not a ground for proposing a strict liability approach. Quite on the contrary, the existence of a chain of parties involved in the transaction makes such approach impractical. For example, a consumer making a payment through an on-line banking product would have recourse to the Payment Service Provider even if the failure to execute was a result of the consumer Internet service provider failing to deliver the instructions to pay.

In some instances, it would be impossible to identify which party was responsible for the non- or defective execution of the payment order.

The introduction of a force majeure exemption will frustrate the Commission's objective as the application of such provision widely differs per country.

Imposing the mandatory nature of these provisions by legally barring the service provider from contractually excluding or limiting his liabilities totally runs counter the contractual freedom of the parties.

Annex 13: Obligations and Liabilities of the contractual parties related to unauthorised transactions

Article 1 (on liabilities between contractual parties) which stipulates '*the Payment Service Provider shall be liable for transactions executed without the Payment Service User's authorisation*' could be understood to conflict with Article 5 which provides for a cardholder's liability of 150€ for unauthorised transactions resulting from the loss/theft of payment card prior to notification. The wording in Article 5 '*if s/he has not fulfilled s.he obligation to notify the Payment Service Provider as required*' opens the door for interpretation issues. It could be understood as providing a zero liability to the cardholder so long as the cardholder complied with the provisions of notification. The wording of Recommendation 97/489/EC was much clearer, i.e. making the cardholder liable up to a maximum of 150€ for unauthorised transactions in case of loss/theft of the card in the period prior to notifying the issuer.

The meaning of *gross negligence* should be defined as it has a different meaning per country. The proposal not to impose liability on the card issuer only in the event the cardholder acted with *gross negligence* is disproportionate. Under the UK Banking Code Standard, the cardholder cannot benefit from the financial cap of 150€ if he acted *without reasonable care*.

There should also be a consideration of the liability of the merchant in relation to the transaction.

Annex 18: Data Protection Issues

MasterCard supports all initiatives outlined in the Communication in so far as they would help the industry to operate fraud prevention databases without the risk of infringing national data protection legislation. As data protection is not a payment specific issue, a solution for the problem of processing fraud related data does not naturally sit within the forthcoming Regulation or Directive on a new legal framework. MasterCard calls upon the Commission to convene a meeting of the Article 29 Working Party or sub-group with a view to resolving the outstanding problem.

Annex 20: Security of the networks

The concern of ensuring that controllers and processors of personal data take appropriate measures to protect networks against unauthorised access is specifically covered under the EU Data Protection Directive. The reference to '*the limited enforcement of the data protection legislation in this area*' does not provide a rationale ground for introducing separate and supplementary legislation in this area. The focus should in the first place be on ensuring consistent implementation of and compliance with the existing legal provisions.

This aspect is de facto also covered in the framework of the European Central Bank's oversight role.

Annex 21: Breakdown of Payment Network

In so far as the breakdown of the payment network results in the non-execution or defective execution of a payment order, we refer to the comments made under Annex 12. Provisions on liabilities of the payment provider towards cardholders and merchants in case of breakdown of the network should in the first place be left to the contractual arrangements concluded between the parties.

It should also not be overlooked that there is a strong self-interest to ensure that networks do not fail in the first place. For example, scheme authorisation procedures provide for stand in or off line authorisation services to enable transactions to be completed even if the member bank's authorisation procedure failed.

This aspect is de facto also covered in the framework of the European Central Bank's oversight role.

III. Comments specifically relating to Electronic Money products

A. General observations

MasterCard is pleased to see that the Commission is determined to see a regulatory regime in place that ensures a “level-playing field: same activity, same risks, same requirements.” This is a paramount requirement of the proposed new legislation and failure to achieve will undermine the efforts of the Commission.

The intention not to regulate specific purpose payment instruments is supported as long as this dispensation is withdrawn as soon as such payment instruments involve third-parties. Regulating such products should not be delayed until they have evolved into a fully blown general-purpose payment instrument.

B. Specific observations

Annex 01: Right to provide payment service to the public

MasterCard is concerned that this section of the document does not accurately reflect the present situation with regard to e-money in that:

- The interpretation of e-money is at odds to that in the E-Money Directive and moreover the definition as understood by most Member State regulators, the e-money industry and the ECB;
- The alternative definition is not technologically neutral which will result in a position where different e-money products will not be dealt with in a consistent manner. On the basis that all e-money products seek to target the same need, and their underlying business propositions are the same, it would be inequitable for an inconsistent approach to be adopted;
- The reference to the majority of e-money schemes that are more or less close to “real e-money schemes” being operated by undertakings which hold a credit institution license is inaccurate;
- The suggestion that some e-money products are closer to deposit-taking (the phrase “are closer to credit transfers in a centralized account system” is used) is misleading. The issue has been discussed at length by a number of regulators including the ECB and it has been agreed that deposit-taking does not arise in any of these products;

In view of the above comments, MasterCard believes that using this interpretation of the E-Money Directive as a basis upon which to regulate other payment service providers and providers of money remittance services is flawed.

MasterCard is opposed to the exemption of any payment services from the legislation unless transactions only take place between the consumer and the service provider. The introduction of third parties into such schemes must result in that scheme being liable to regulation even if it is an integral part of another service. To allow such services to be unregulated would not result in a level playing field.

MasterCard questions the reason to regulate post-pay services as the products are already dealt with through consumer credit legislation and in any case are completely different in nature to e-money services or money remittance services.

Annex 10: Revocability of a Payment Order

MasterCard is concerned about the “one size fits all” approach. E-money products have differing attributes, some of which are effectively “bearer” in nature and which would therefore offer no opportunity for payments to be revoked.

Annex 11: Role of the Payment Service Provider in the Case of a Customer/Merchant dispute

For payment service providers to have to become involved in disputes between consumers and merchants would be costly and would either lead to increased charges to the consumer, or to withdrawal of the product from the market. This general concern is especially valid for e-money operators where the average value of transactions tends to be relatively small and thus the cost of dealing with disputes would be out of proportion to the transaction size. Bearing in mind that some e-money products such as Mondex seek to replicate notes and coins and in many respects have the attributes of physical currency, it is inequitable that such payment methods should be liable to resolve disputes.

Annex 12: Non-Execution or Defective Execution

The proposal is especially unworkable for e-money products. Many of those products operate in an electronic/virtual environment where devices and networks under the control of others, including those owned by consumers, are involved in executing the transaction.

Annex 13: Obligations and Liabilities of the contractual parties related to unauthorised transactions

Many e-money products are negotiable and would therefore require a separate regulatory regime to that set out in Annex 13.

Annex 20: Security of the networks

The Communication approaches this aspect from the perspective of consumer protection and the security of personal data, but the issue is far wider than that. The ECB and BIS have published a number of documents in connection with this subject which approach the subject in a much wider context and MasterCard contends that these bodies together with National Central Banks should remain responsible for this issue.