

Legal & Regulatory Working Group

Payments Innovation Forum (PIF) 2024



Competition Law Notice

Meeting participants are reminded that this meeting **must adhere to competition law rules** and as such no confidential or commercially sensitive information must be shared directly or indirectly between competitors.

Please do not share any confidential or commercially sensitive information and please do not ask questions that could lead to other participants to sharing confidential or commercially sensitive information about their organisation.

A written agenda has been circulated in advance and all discussion must keep to the agenda.

Please read our **Competition Law Guidelines** for further information:

[Competition Law Guidelines - Payments Innovation Forum](#)

Agenda – 9 December 2024

1. PIF response FCA proposed changes to the safeguarding regime – Summary of Key Concerns/Observations
2. FCA Finalised Guidance for firms that enable a risk-based approach to payments
3. FCA Financial Crime Guide Changes
4. Update on the US elections – implications for US fintech and payment sectors – Judith Rinearson, Partner, K&L Gates LLP
5. A.O.B.

1. PIF Response to FCA proposed changes to the Safeguarding regime

Key areas of concern:

1. Proposed rules and guidance on reconciliation of relevant funds and resolution packs
2. Statutory Trust
3. Safeguarding audits
4. Cost benefit analysis

Member Feedback Form:

<https://forms.gle/sZVKqGEC7WL41YXT7>

PIF response to safeguarding consultation

Rules and guidance on reconciliation of relevant funds

- We agree with some of the detailed guidance in principle, but the complexity involved in ensuring accurate reconciliation of relevant funds has been **underestimated** in terms of what is practically required of firms to meet the requirements:
- The challenge to address is the two-stage process where firms need to rely on their own records and those of third parties. Many firms access payment systems through third parties who are direct members of those systems. Because of this, **these firms lack direct access to detailed transaction information**. This contrasts with firms regulated under CASS who are typically direct exchange members and already have access to this level of detail. Payment systems operate differently. A payment firm's own information is therefore likely to be incomplete, leading to discrepancies.
- Given the very short time frame for firms to address any surplus or shortfalls in a safeguarding account, especially considering multiple currencies, this creates significant challenges. We recommend the FCA engages directly with the different types of Issuer/PSP to better understand the practical realities of reconciliation.
- **Question for members:** Can members provide any examples of the practical difficulties they could potentially face?

PIF response to safeguarding consultation

Rules and guidance on resolution packs

- The CBA underestimates the **substantial time and resources** required for compliance – the analysis seems to assume that firms can merely copy and paste the information they already have which overlooks the complexities involved.
- In reality, firms will likely need to undertake a comprehensive review and validation process to ensure their resolution packs comply with the new rules. The assumption that a senior compliance officer would need only **three hours** to review the pack seems arbitrary and disconnected from the reality.

PIF response to safeguarding consultation

Do we agree that a statutory trust is the best replacement for the safeguarding regime in the EMRs and PSRs?

- We believe this approach is fundamentally flawed:
 - **Lack of clear justification and impact assessment** – the FCA has not adequately articulated the rationale for implementing a statutory trust or provided a thorough analysis of the implications for firms. Specifically, the FCA has not addressed the **practical consequences related to fiduciary duties, treatment of profit** from assets, and **interest earned** on safeguarding accounts, which are key income sources for EMIs.
 - If interest can no longer contribute to firms' revenues, this will undermine a **crucial income stream**. EMIs may need to introduce service fees and charges, leading to higher costs for consumers, reducing the attractiveness of EMIs and potentially placing EMIs at a competitive disadvantage.
 - **A statutory trust does not inherently improve the accuracy of a firm's records** or their overall financial health. If a firm's records are poorly maintained, imposing a statutory trust does not resolve this. Enhanced supervision and enforcement of the existing regime would be more effective in ensuring the protection of customer funds.
 - Implementing a statutory trust weakens the UK's alignment with EU regulations, potentially jeopardising the UK's access to SEPA and making the UK a less attractive place to do business → this **goes against the grain of the National Payments Vision**, which is focused on making the UK “a world-leading payments ecosystem.”

PIF response to safeguarding consultation

Requirement for external safeguarding audits to be carried out in both the interim and end state:

▪ Concerns:

- **Lack of audit capacity** → not enough auditors to meet demand
- Frequent assignment of **junior-level staff lacking the necessary experience**/sector knowledge, often accompanied by disproportionately high fees
- Four-month timeline is aggressive. It will create a pinch point, placing immense pressure and costs on the industry
- **Accuracy of the cost benefit analysis** → substantially higher than current fees; appears to be based on pricing structure of the Big Four firms rather than auditors with a deep understanding of the safeguarding requirements
- Auditors overinterpreting their responsibility → **effective audits demand a thorough understanding of payment flows**, and not all deviations constitute non-compliance

▪ Recommendations:

- If the FCA has concerns about the quality of auditing firms, we would support the creation of an approved list provided the criteria are pragmatic and flexible enough to reflect the diverse expertise needed, e.g., similar to s166 of FSMA

PIF response to safeguarding consultation

Safeguarding returns and frequency of reporting

- **Monthly returns seem excessive** – we suggest quarterly submissions strike a more balanced and proportionate approach.
- **Practical implications** → how does the FCA plan to manage the influx of monthly data? Does the FCA have adequate resources to process and analyse the information effectively?
- **Questions for members:**
 - Do you have any views of the information required, and how easy it will be to provide this information on a monthly basis.
 - Will some of the data items to be included in the report be difficult (or disproportionately expensive) to obtain? What are your views on submitting some of the more static information every month?

PIF response to safeguarding consultation

Prescriptive rules on the segregation of relevant funds in both the interim and end state and proposal for relevant funds to be received directly into a designated safeguarding account

- We support the proposals in principle, as they provide clarity. However, requiring all funds to be deposited first into a safeguarding account and then extracting non-relevant funds introduces challenges and complexity.
- One major issue is the immediate mixing of non-relevant funds involving e.g., FX transactions across multiple days, different time zones/jurisdictions. Delays in receiving information from third parties further complicates the process.
- Under the new rules, firms would need to either deposit all incoming funds into safeguarding accounts and later withdraw non-relevant funds, or use their own funds upfront. **Both options are problematic** → they deplete a firms' liquidity, increase the complexity of reconciliation, and reduce capital available to the firm. Maintain liquidity will be challenging, especially if firms previously relied on the funds for payouts to customers before settlement.
- The **assumption that all funds flow into a single safeguarding account is unrealistic** → this issue is magnified for firms whose safeguarding accounts are held with banks outside the UK.
- **Question for members**
 - How will the proposed changes impact the way you manage and maintain your business. What (if any) changes will you need to make to deal with the practicalities of the new rules?

PIF response to safeguarding consultation

Funds received through agents and distributors either paid directly into the principal firm's safeguarding account OR protected through agent and distributor segregation

- Concerns:
 - The proposal does not address the core issue → transferring these funds does not inherently improve protection.
 - The challenge arises particularly when agents and distributors handle mixed remittances, which often include funds from non-regulated activities. Introducing more mixed remittances into these accounts – only to potentially remove them later – obscures the picture rather than clarifying it.
- Recommendation
 - A more effective solution might be drawn from the CASS 5 framework for insurance brokers whereby a risk transfer agreement ensures funds received by brokers are deemed to be held by the insurer. Applying a similar approach here – where agents and distributors have segregated accounts and hold funds as agents of the principal firm – could offer a more effective solution.

PIF response to safeguarding consultation

Ability of firms to invest in the same range of secure liquid assets as they can now in the interim state

- **Question for members**

- If you use this method, do you agree that firms should be able to invest in the same range of secure liquid assets as they can now in the interim state?

PIF response to safeguarding consultation

Ability of firms to continue to invest relevant funds in secure liquid assets in the end state

- There are some important considerations regarding the generation of surplus or excess funds. Under a statutory trust, firms have a statutory duty to account for these funds and cannot profit from the assets of the trust. Guidance is needed on **how firms should treat any surplus** – this is particularly relevant given firms are restricted from providing interest under the EMRs, but also prohibited from keeping any excess under a statutory trust structure. Firms need to know how to manage and allocate surplus funds.

PIF response to safeguarding consultation

Ability of firms to hold assets they invest in – or should they always be held by a custodian?

- Clarification would be beneficial, particularly to confirm that sending funds to a custodian does not fall under the FSMA-regulated activity of arranging custody, which could inadvertently bring firms within the scope of this regulation.
- Clear guidance is also needed on the types of assets firms can invest in – under the existing regime, firms must seek approval or ensure their investments meet specific criteria – will this continue?

PIF response to safeguarding consultation

Proposal to maintain the use of insurance policies and comparable guarantee for safeguarding in interim and end state

- No concerns – for certain firms, this is particularly beneficial, e.g. firms dealing with significant fluctuations, such as FX transactions that are not their primary business but still constitute a portion of their operations, find it easier to safeguard customer funds and manage risks using these methods.

PIF response to safeguarding consultation

Proposals to clarify when the safeguarding requirement starts and ends

- The FCA should consider the complexities of different business models and payment flows, e.g., funds may pass through multiple PSPs before reaching the end customer. Requiring safeguarding at each stage, including when funds are transferred to another PSP with its own safeguarding obligations, results in **double safeguarding** which creates inefficiency and redundancy.

PIF response to safeguarding consultation

Requiring small EMIs to arrange an annual safeguarding audit:

- We believe that it would be prudent to treat EMIs similarly but need to ensure that audits are proportionate to the simpler business models and payment flows of smaller firms.
- Customers see no distinction between an EMI and a small EMI – they expect the same level of safety and security for their funds.

PIF response to safeguarding consultation

Cost Benefit Analysis

- We have significant reservations about the credibility of the assumptions underpinning the CBA.
 1. The FCA assumes “all firms will comply with the rules.” This is overly optimistic, given the FCA’s own insolvency analysis which identified a 65% shortfall. Moreover, the FCA acknowledges the improbability of the assumption, stating: “we are aware this assumption is unlikely to be achieved.” This contradiction raises doubts about the robustness of the projected compliance benefits.
 2. The FCA projects that the rules will reduce the average time to first distribution from 2.3 to 1.3 years. This assumption does not appear to be sufficiently evidenced and seems unrealistic. Importantly, when compared to the alternative of applying the FSCS which disburses payments within seven working days, the proposed one-year reduction is relatively insignificant, particularly for vulnerable customers.

2. FCA Finalised Guidance for firms that enables a risk-based approach to payments

[FG24/6: Guidance for firms that enables a risk-based approach to payments](#)

FCA Finalised Guidance for firms that enables a risk-based approach to payments

- The Payment Services (Amendment) Regulations 2024 enable PSPs to delay outbound payments by up to 4 business days where firms have reasonable grounds to suspect fraud. The aim of the revised regulations is to give PSPs the flexibility to prevent APP fraud more effectively, while minimising the impact on legitimate payments.
- The FCA's finalised guidance provides detail on:
 - **The requirements for delaying outbound payments** and determining whether the **threshold for “reasonable grounds to suspect”** has been met – the guidance explains PSPs require an objective ‘factual foundation’ for the threshold to be met and sets out what PSPs should consider when assessing whether the threshold has been met;
 - **How PSPs should use the payment delay window;**
 - **The obligations on PSPs if they delay an outbound transaction** – the FCA guidance explains the requirements for the PSP to notify certain parties if a transaction is delayed and highlights relevant **obligations under the Consumer Duty**. It also explains the potential for the PSP to incur liability to compensate a payer for any costs resulting from the payment delay, and
 - **Delaying suspicious inbound payments** – the FCA has set out its views on when the force majeure provisions in the PSRs apply to financial crime legislation. HMT did not amend these provisions. The force majeure provisions provide that where a PSP must breach the execution timescales in the PSRs 2017 (for example, by delaying making incoming funds available to a payee) to comply with other laws (including financial crime laws), the PSP will not be liable for the breach of the PSRs 2017.

3. FCA Financial Crime Guide Changes

[PS24/17: Financial Crime Guide changes](#)

FCA Financial Crime Guide Changes – Final Guidance

Summary of Key Changes

- **Sanctions** – the FCA has updated the sanctions chapter to reflect what the FCA and firms have learnt following Russia’s illegal invasion of Ukraine in 2022, and the FCA’s subsequent assessment of firms’ sanctions systems and controls. This includes changes to some of the terminology.
- **Proliferation Financing (PF)** – the FCA has updated the guidance to ensure that PF is explicitly referenced throughout the Financial Crime Guide, where appropriate, including the 2022 change to the MLRs which requires firms to conduct PF risk assessments.
- **Transaction Monitoring** – the FCA has set key guidance for firms on how to implement and monitor transaction monitoring systems. This includes “supporting responsible innovation and new technological approaches.”
- **Cryptoasset Businesses** – the FCA makes clear that cryptoasset businesses should refer to the guide, on the basis that cryptoasset businesses registered under the MLs have been subject to FCA supervision for AML/CTF/PF purposes since January 2020.
- **Consumer Duty** – The guide makes clear that firms should consider whether their systems and controls are consistent with their obligations under the Consumer Duty.

4. Update on the US elections: Implications for US fintech and payments sectors

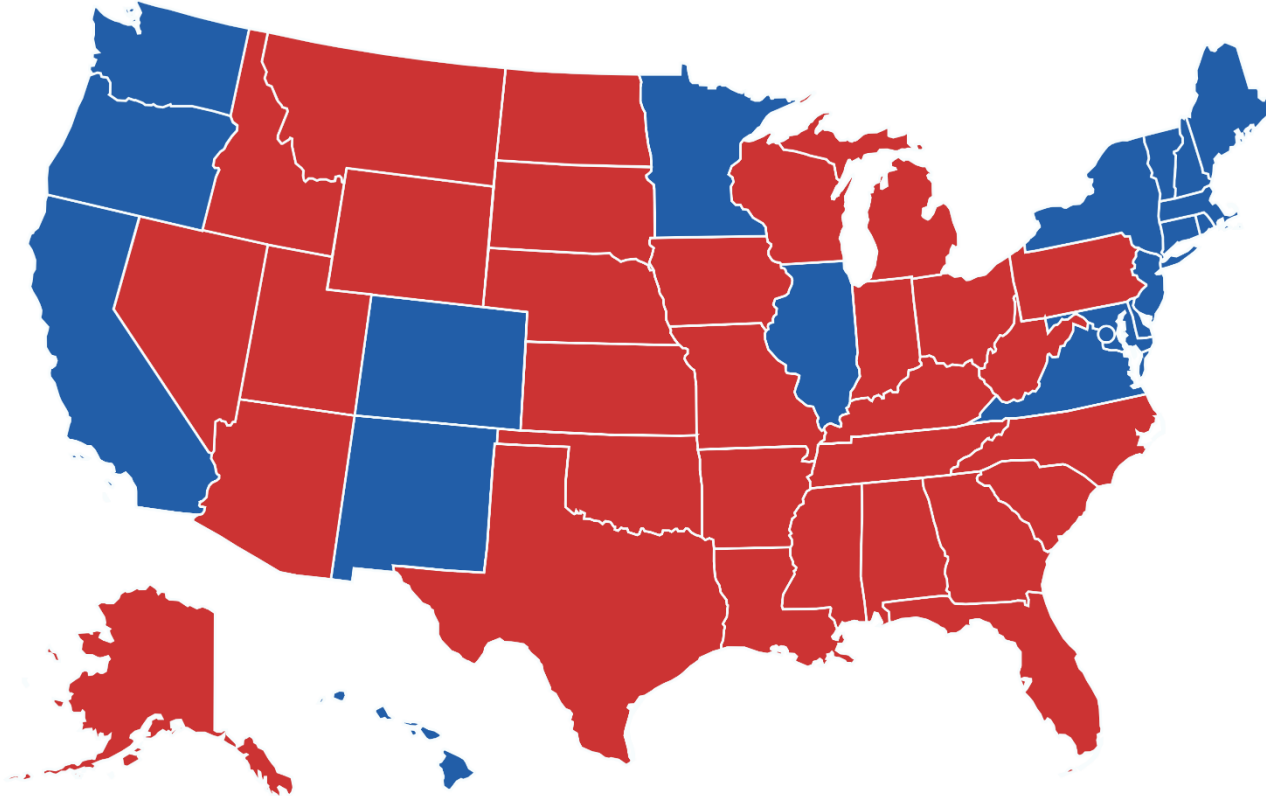
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US Post-Election Overview and Look Ahead to 2025

Judie Rinearson, Partner, New York & London

With thanks to the K&L Gates Public Policy Group in Washington DC

White House: President-elect Trump Wins a Very Close Race – with a majority of Electoral College Votes



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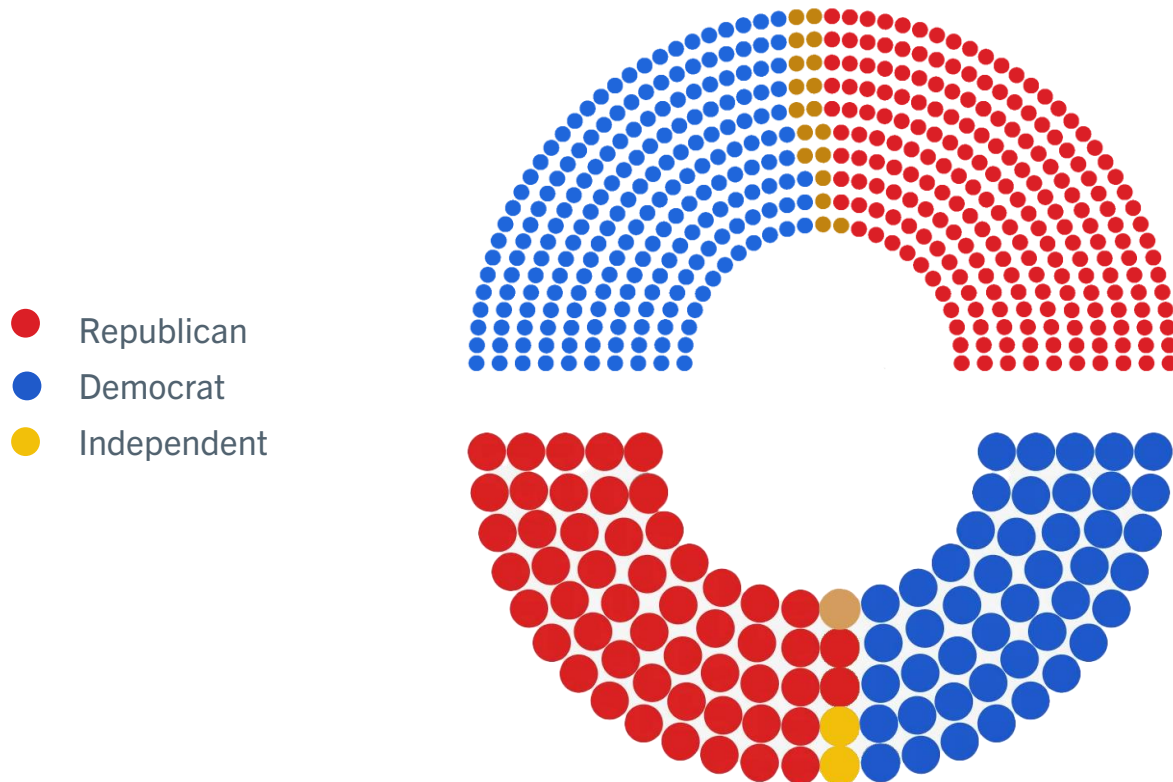
74,834,277
(50.4%)



226

71,239,855
(48.0%)

119th Congress – Republicans win a slim lead



HOUSE OF REPRESENTATIVES

Republican: **220**
Democrat: **215**

SENATE

Republican: **53**
Democrat: **47**
Independent: **2***
**Caucus with Democrats*

Source: AP News

The Red Wave? I don't think so...

- President Trump and Congressional Republicans have positioned their win as a “**mandate**”
 - BUT latest vote count shows one of the smallest margins since the 19th century.
 - Not a “landslide” – less than 50% of the popular vote
 - Still, the election will have **consequential policy impacts**
- **But also, a moment in time:** political pendulum swing continues to accelerate
- Control of House and Senate extremely slim
- US still highly divided and highly partisan

The Trump Agenda

- Trump won on two primary issues:
 - **Inflation** – appointees will be committed to a pro- economic growth agenda, including “DRILL BABY DRILL” to lower energy costs
 - **Immigration** – focus is on securing the border and deportation of undocumented criminals.
- Trade negotiations will revolve around:
 - **Tariffs** - goal is to address trade imbalances
 - **Energy** - goal is U.S. industry dominance
 - **China** – goal is economic and military isolation

Legislation is Not the Only Tool in the Box

- **Congressional Review Act**
 - Expect the Biden Administration to finalize as many regulations as possible before Jan. 20
 - CRA can be used to rescind regulations finalized by a prior administration; majority votes
 - CRA window is roughly August 1, 2024 through end of March, 2025
 - THE CATCH: Cannot issue “substantially similar” regulations once rescinded. Substantially similar is not defined. Republicans will need to use this tool strategically so they are not throwing the baby out with the bathwater.
- **Executive Branch**
 - Trump Administration can reopen regulatory projects
 - Can issue sub-regulatory guidance
 - Can pause open regulatory and guidance projects
 - Can issue executive orders
 - Agency appointees
 - Policy priorities, resource allocation
- **The Courts**
 - Challenges to regulations pursuant to *Loper Bright* and *Chevron* deference
 - Challenges pursuant to *Corner Post*
 - Courts may be how the SEC Climate Risk Disclosure rules get vacated

What's Next

- Lame Duck Session Priorities
 - Must pass legislation
 - FY2025 federal funding
 - Timing unclear
 - FY2025 NDAA (National Defense Auth Act)
 - Farm Bill
 - Debt ceiling
 - Senate judicial nominations
 - Leadership elections and conference rules

Committee Leadership Changes - HFSC



**Patrick McHenry (R-NC),
Financial Services**

- GOP contenders (clockwise from top left): Andy Barr (R-KY), French Hill (R-AR), Frank Lucas (R-OK), and Bill Huizenga (R-MI)
- Key Priorities for contenders: Capital formation, ESG, crypto



**Maxine Waters (D-CA), Ranking Member,
Financial Services**

- Key Priorities:
 - Racial equity and D&I-related efforts
 - Oversight of big banks and “bad actors”
 - Consumer protection
 - Housing affordability and access

Committee Leadership Changes - Banking



Tim Scott (R-SC), **Chair, Banking, Housing & Urban Affairs**

- Also likely NRSC Chair
- Key Priorities:
 - Capital formation
 - Reducing regulatory burdens
 - Housing
 - Digital assets



Sherrod Brown (D-OH), **Banking, Housing, & Urban Affairs**

- Defeated in reelection race
- Next most senior member without an existing role as top Democrat on another committee is Sen. Elizabeth Warren (D-MA)



Looking Ahead: Financial Services Policy

- Changes in committee leadership will lead to changes in policy priorities
- Republicans have signaled that a key aspect of their political platform is to undo certain “woke” financial policies implemented by the Biden administration and Democrats, as well as the Basel III Endgame proposal
- Top oversight priorities will likely include:
 - ESG (Environmental, Social, Governance)-related regulations, including countering the “Green New Scam,” proxy voting issues, corporate governance, etc.
 - DE&I (Diversity, Equity, Inclusion)-related regulations and agency initiatives, including human capital disclosures
 - International regulatory frameworks affecting U.S. companies (e.g., EU Corporate Sustainability Due Diligence Directive)
 - Regulations from the CFPB, SEC, and other financial regulators

However, Slim Margins Remain

- Despite Republicans having control of the White House and Congress, slim majority margins will continue to play a role in lawmaking and will necessitate bipartisanship
- Some areas of potential bipartisan agreement will likely include:
 - China investments
 - Digital assets
 - Regulation of AI in financial services
 - Need for substituted compliance with EU regulatory regime

Impact on ESG Policy

- Congress and Trump administration will work together to undo Biden-era regulations on climate, “equity,” etc.
 - CRA resolutions, EOs, and rulemaking
 - Primary GOP targets will likely be asset managers and proxy advisories
- EU Sustainability Reporting Regimes
 - Will push back on extraterritorial impact of CSRD and CSDDD on US companies
- State Laws
 - Will seek to preempt state laws (e.g., CA climate laws) if not vacated in court

Trump Administration – Financial Services Regulatory Impacts

- SEC
 - Former Commissioner Paul Atkins nominated to be SEC Chair.
 - Focus on rolling back Biden administration regs, particularly related to:
 - Climate risk disclosure
 - Digital assets
- CFPB
 - Unclear at this point who will be Director. Trump plans to remove current Director Chopra expeditiously
 - Focus on reducing regulatory framework
 - Suggested CFPB elimination? Not likely.
- BANKING
 - Expected relaxation on restrictions on banking “risky businesses”

BOTTOM LINE

- Good news for Crypto
- Good news for Fintechs looking to partner with banks
- Could be bad news for states rights - - over payments. Finally national charters or “passporting”...?
- Bad news for Consumer Protection, ESG and DEI.
- Still highly partisan and dysfunctional!
- Lobbyists in high demand!

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