On 17 May 2017, we hosted our Fintech seminar, “Legal Challenges and Opportunities”, in our London office with guest speakers from the Financial Conduct Authority (FCA), Competition and Markets Authority (CMA) and Lloyds Banking Group, along with partners from our Fintech team, Intellectual Property & Technology Practice and International Dispute Resolution Practice.

Topics covered included:

- Competition Law – Risks and Opportunities
- PSD2 – Challenges and Opportunities
- Data Protection and Cybersecurity – Common Pitfalls and How to Avoid Them
- Litigation – Hot Topics for Fintech

There were two panel sessions, one on the new PSD2 and one on competition law aspects, followed by Q&A sessions with the audience.

In the session “Competition Law – Risks and Opportunities”, Fabio Falconi and Mark Bethell, from the FCA, gave a keynote presentation on the competition law mandate of the FCA. The session was then opened to a panel discussion moderated by Francesco Liberatore, partner, Russell Mascarenhas, lawyer at Lloyds Group, and Tom Smith, Legal Director at the CMA, who joined Fabio and Mark on the panel.

The panel concurred that competition law provides a flexible and effective tool for Fintech companies and that it can be used as a “shield” to disentangle the procompetitive effects of certain cooperation arrangements (such as information exchanges in blockchain technology) from its potentially anticompetitive effects; or can be used as a “sword” as leverage in commercial negotiations with larger players to reduce artificial market barriers.

The speakers commented on the concurrency of competition powers between the CMA and the FCA. Unlike in other jurisdictions, both organisations have powers to apply competition law in the Fintech sector. The speakers explained that, in practice, there have in fact been no complications in allocating cases. Firms have the option of approaching either or both organisations, without it mattering who is approached first.

The panel also broached the subject of the CMA’s use of its powers in a recent market investigation on retail banking when it adopted a wide-reaching package of reforms. These reforms have paved the way for the Open Banking revolution and the panel acknowledged that one of the barriers to small businesses in the UK is that core business banking services are still provided by the large banking groups with the industry seeing minor changes in structure over the past decades. The FCA highlighted they were keen to encourage innovation to capitalise on the opportunities presented by the reforms. They referred to the Nesta Fintech “Open Up Challenge”, which is offering a £5 million prize.

Finally, the panel discussed the potential tension between the regulatory/consumer protection obligations applying to financial institutions and the Open Banking remedies, in particular with reference to access to a bank’s transactions and customer accounts. They agreed that one way to reconcile this tension is to make sure that the technology used to provide such access seeks and obtains the appropriate customer’s consent.

In the session “Litigation – Hot Topics for Fintech”, Chris Webber, partner, discussed three key trends in Fintech litigation and regulatory enforcement activity. Firstly, drawing on case law from the US, the EU and the UK, the focus by regulators on the risks of financial crime and fraud from Fintech developments like cryptocurrency exchanges, crowdfunding and peer-to-peer lending was highlighted. That focus was mirrored in a surge in Fintech fraud litigation. Secondly, other cases in which courts had grappled with applying traditional legal principles to new products, particularly dematerialized, tradeable units of value that characterize many Fintech innovations, were outlined. Thirdly, it was noted that there is a trend of consumer protection interventions by US and UK regulators in Fintech areas like payday lending, crowdfunding, mobile payments and data protection breaches by payment apps and APIs. Overall, Chris predicted continuing growth in Fintech disputes and regulatory enforcement activity in the UK each of these areas as the UK Fintech market continues its rapid development.
In the section “PSD2 – Challenges and Opportunities”, Nilixa Devlukia from the FCA presented on her work at the FCA relating to the implementation and transposition of the revised Payment Services Directive (PSD2) and the various challenges related to this activity. Wolfgang Maschek and Paul Anderson, partners, joined Nilixa in a panel session facilitated by Wolfgang. The panel discussions were opened with an introduction on the evolution of the EU regulatory and supervisory framework for payments since the early 2000s. The importance of, and changes in, adjacent legislative areas, including anti-money laundering (AML), data privacy and consumer protection matters was underlined, together with a highlight of the underlying regulatory trends and related implications. These include a shift in supervisory powers from the Home to the Host member states, to the newly established “Level 2” implementation powers for European Supervisory Authorities, and to severely increased sanctions and regimes in AML and data privacy matters. The introduction concluded with an outlook on pending or proposed new EU regulatory initiatives of relevance to the Fintech and payments industry.

Some of the points emerging from the discussion – which was held under Chatham House Rule – are summarised below:

- Participants are encouraged by the FCA to respond to the PSD2 consultation that the FCA is running until mid-June 2017 and underlined the importance of dialogue between the supervisory authorities and industry.
- There are important changes that PSD2 will bring as of January 2018, including new payment services becoming subject to the PSD2 and the related licensing requirement. These new services are payment initiation services (PIS) and account information services (AIS), provided by so-called Third Party Providers (TPPs).
- The European Banking Authority is carrying out Level 2 work in the context of the PSD2: in particular the ongoing political debate regarding rules for “strong customer authentication and secure communication” for online payments. These new rules will, once adopted at EU level, only come into force 18 months after adoption and thus after the PSD2 application deadline – which leads to challenges for the industry.

Key changes in the new PSD2 regime vis-à-vis the existing regulatory framework were discussed and the changes in scope and the narrowing of exclusions from the PSD, for instance for limited networks, limited range and the application of the commercial agents exclusion so that those relying on it can only act for one side, payer or payee were explained.

Relevant legal aspects for Payment Account Initiation Service Providers (PISPs) and Account Informational Service Providers (AISPs) were discussed including communication between AISPs and PISPs and security and TPP access.

Further discussion on the ongoing political date at EU level around the new rules related to Strong Customer Authentication and Secure Communication followed and the session was closed with a discussion on the potential impact of Brexit on the UK-based Fintech and payments industry, which will likely be strong affected where reliant on the EU passport regime given the lack of equivalence rules for third countries in the applicable EU Payment Services and Electronic Money Directives.

In the final session of the morning on Data Protection and Cybersecurity, Stuart James discussed the impact of data protection and cybersecurity on the Fintech sector. He noted that data security is seen by the FCA and the UK Information Commissioner’s Office as being of critical importance, with cyber-attacks, such as the WanaCry incident that paralysed the NHS recently, becoming more and more frequent. The FCA has said that it will be turning its regulatory attention to smaller operators, so it is important that Fintech firms of all sizes have effective data security systems, policies and procedures in place. It was also noted that the FCA expects to see cybersecurity being addressed by companies at board level and that it intends to encourage investors to make the issue a priority when considering investments.

However, Stuart reminded delegates that the General Data Protection Regulation covers much more than just data security. He flagged up detailed requirements on data mapping, record keeping, service provider contracts, privacy notices and consents as all being matters that will require significant changes to business processes before the deadline for compliance on 25 May 2018.

For further information on any of the topics covered, please contact the presenters below or your usual contact at Squire Patton Boggs.

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