

Comments

on Article 5d (sanctions screening) of the
proposal for a regulation on instant credit
transfers COM (2022) 546 final

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The **German Banking Industry Committee** is the joint committee operated by the central associations of the German banking industry. These associations are the Bundesverband der Deutschen Volksbanken und Raiffeisenbanken (BVR), for the cooperative banks, the Bundesverband deutscher Banken (BdB), for the private commercial banks, the Bundesverband Öffentlicher Banken Deutschlands (VÖB), for the public banks, the Deutscher Sparkassen- und Giroverband (DSGV), for the savings banks finance group, and the Verband deutscher Pfandbriefbanken (vdp), for the Pfandbrief banks. Collectively, they represent approximately 1,700 banks.

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In addition to the comments by the German Banking Industry Committee (GBIC) of 25 November 2022 on a proposal by the European Commission “for a regulation on instant credit transfers (COM (2022) 546 final)”, we are sending you the GBIC’s assessment of the sanctions aspects of the proposed regulation.

6 Dispensing with mandatory transaction-related sanctions screening: take account of interaction with other rules and regulations

Proposed requirement: The Commission proposes adding a new Article 5d to the SEPA Regulation in order to regulate obligations arising from restrictive measures in accordance with Article 215 of the TFEU for instant credit transfers. Payment service providers (PSPs) are to continually check whether any of their customers (payment service users, PSUs) appear on the relevant sanctions lists. If a PSP fails to carry out this verification process, the introduction of administrative penalties and liability for damages caused to the other PSPs involved in a payment is proposed.

Assessment:

- This requirement addresses the particular challenges of sanctions screening that has to be carried out in a matter of seconds and the resulting false positive hits that would doubtless result. In principle, the European Commission’s proposed solution could help to mitigate these challenges.
- The banking industry and member states will nevertheless need to take a critical look at the proposal owing to interactions with other rules and regulations. This concerns, in particular, the high sensitivity of compliance with European sanctions and embargo regimes and the interplay with other external requirements as well as credit institutions’ own measures to prevent financial crime.
- In the opinion of the GBIC, the European Commission’s proposals aimed at reducing the number of false positive hits interfere too much with existing screening mechanisms. The ban on filtering transactions, a regularly significant component in screening for violations of Union restrictive measures, opens up a security loophole in sanctions screening.
- Simultaneously tightening the liability rules for credit institutions results in a security risk arising from the legislation being transferred exclusively to the credit institutions and is therefore neither appropriate nor proportional in this form.
- In addition, the proposal is at odds with proposals currently being tabled under proposed AML legislation which (though inappropriate there) provide for sanctions screening obligations to be included in AML (due diligence) obligations. European lawmakers must therefore ensure that contradictory rules are not enacted at the same time. Obligations to carry out sanctions screening should not be included in AML legislation.
- Before we comment on Article 5d in detail, we would like to make the following remarks on the importance of transaction screening:
 - The proposed regulation rightly assumes that credit institutions check both the individual transactions as well as their own customer data when carrying out sanctions screening. However, new listings are not automatically immediately available in the credit institutions’ systems after publication. Updates first need to be made available for download by the EU, and only then are they processed – usually by service providers – and then transformed into a machine-readable form, so they can then be imported into

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the credit institutions' systems. In addition, any transactions identified in the filtering or screening process (hits or alerts) must first be assessed manually in order to filter out the extremely large number of false hits; in some cases, the individual filtering process may take several days, especially if queries to third parties, e.g. banks, are required where names are very similar and there are no other unique identifying features, such as date of birth. Equally, when customer data is being screened, before an account is blocked the hit must first be verified manually because there are a high percentage of false positive hits here too. This takes up a certain amount of time and can only be done on bank working days due to the need for manual verification by members of staff. However, instant credit transfers need to be executed within just a few seconds, seven days a week. A sanctioned person would, in principle, have enough time to empty their account via instant credit transfer between the time they are listed and when they are blocked. With the current system, fraudulent transfers are no longer possible from the moment the new lists are imported into the systems and therefore payments are stopped for verification (or rejected in the case of instant credit transfers) much earlier. With the expectation that instant credit transfers must be able to be executed at any time, the Commission is creating a risk that would not occur were it not for the obligations arising from this regulation. This risk could be mitigated, however, if a (daily) maximum amount were introduced to prevent large sums of money being 'siphoned off'.

- As mentioned above, credit institutions do not solely rely on transaction filters but also screen their customer data – a screening measure only financial institutions are supposed to perform for instant credit transfers. As outlined above, it also takes time to perform the customer screening process. Even if credit institutions do it overnight when IT systems are less in demand, more time would still be needed for the additional processing steps. It is not an automated process that can be completed in a matter of seconds or even in a few hours. It would therefore be appropriate to also take account of the need for more detailed screening for instant credit transfers. To better understand the differences between these two screening measures, we have compared the features of transaction filtering (in Germany usually only used in cross-border payments) and customer screening under the proposed regulation on instant credit transfers in the following table:

Screening of individual payments (transaction filter)	Planned customer screening under the proposed regulation on instant credit transfers
In case of a hit (machine generated), payment is blocked until evaluation is concluded.	Account can be accessed until evaluation of a hit (machine generated) is concluded. Given the considerable restrictions and liability risks of incorrectly blocking an account, provisional blocking of an account based on an automatically generated hit is not a feasible option.
Filtering items are: <ul style="list-style-type: none"> ■ Payer ■ Payee ■ Relevant credit institutions ■ Reference 	Screening items are: <ul style="list-style-type: none"> ■ Account holder ■ Name(s) of authorised signatories for the account ■ Beneficial owner of the account

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Screening of individual payments (transaction filter)	Planned customer screening under the proposed regulation on instant credit transfers
All names are checked against the relevant sanctions lists (asset freeze, sectoral sanctions and key terms selected according to risk aspects), including national lists where applicable.	According to the proposed regulation, only screening against EU’s asset freeze lists. (Typically, the credit institutions’ customer screening measures do not only include these lists, they also include, for example, refinancing or sectoral transaction prohibitions.)
Possible to update lists during the day, but time required for editing, importing and processing of data. Once these steps have been taken, the lists can be accessed immediately.	Lists can only be updated and data verified overnight. Very time consuming due to need for comprehensive checking and process runs (requires considerable IT capacity).

- Payments are not only prohibited under asset-freezing sanctions but also under sectoral sanctions. These are not taken into account at all in the proposed regulation; the prohibition of transactions under Article 5aa of Council Regulation (EU) No 833/2014 (according to EU FAQ G. Sector Specific Questions 5.1.) also includes payments.
- The sanctions screening measures implemented by financial institutions have evolved over the years in response to the sharp rise in the number of listings for purely financial sanctions as well as sectoral sanctions, which have become considerably more complex, and have ultimately established themselves as an industry-wide standard. The Commission’s proposal to dispense with transaction filtering would mean omitting an important step in the screening process and not replacing it. Although dispensing with transaction filtering would relieve the credit institutions’ workload, we would like to point out that in its current form (i.e. with no daily maximum amount), a simplification of the process would inevitably lead to sanctions being less effectively enforced.
- We would like to address a specific issue in Article 5d of the proposed regulation:
 - Paragraph 1 of Article 5d requires payment service providers to immediately verify whether a person is listed (“PSPs shall carry out such verifications **immediately** [...]”). Credit institutions implement the adopted sanctions meticulously and without undue delay as soon as they are published in the Official Journal of the European Union. However, as outlined above, the earliest the sanctions lists can be accessed in the system is one day after publication. Furthermore, hits on the new lists have to be evaluated manually. This includes verifying the hits. The current legal situation in Germany provides for exclusion from personal penalties under Section 18(11) and/or Section 18(12) of the Foreign Trade and Payments Act (Außenwirtschaftsgesetz, AWG) if prohibited transactions are not detected within two working days. This deadline is appropriate. We therefore urge the Commission to change the word “immediately” to give credit institutions two bank working days to implement these lists. We believe the wording “**without undue delay**” would also be appropriate insofar as it is already in use in the current German legislation (“*unverzüglich*”). According to recital 15 of the proposed regulation, PSPs are to carry out verifications “as soon as possible” once the new asset freeze and/or prohibition has come

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into force in accordance with Article 215 of the TFEU. This would then be the case with the above wording.

- Paragraph 1 of the new Article 5d also requires that verifications are carried out “...**at least once every calendar day**”. This approach is understandable to ensure a seamless implementation of the current listings. However, the EU only publishes in its Official Journal on working days. In addition, this rule would force credit institutions to make fundamental changes to the way they organise their processes. As things currently stand, customer screening is not generally carried out at weekends or on national holidays, particularly because working on Sundays or on national holidays is subject to tight restrictions in Germany. We would therefore recommend changing the wording to “**at least once every bank working day**”. It would also be helpful if the text were to state that PSPs only need to check changes to the sanctions lists and to customer data against the entire lists (double delta approach).
- Paragraph 2 states that where PSPs reliably carry out verifications that their PSUs are not listed persons or entities, they do not need to verify whether the payer or the payee of instant credit transfers are listed persons or entities. In addition to the considerations outlined above, we would also like to comment on the proposed ban on further checks (“**shall not verify**”) when executing the transaction. The complete waiver of such checks could put credit institutions in a difficult situation when dealing with other jurisdictions (e.g. national lists and other legislative prohibitions that can also only be implemented with this kind of transaction filter). We therefore propose deleting this complete prohibition on transaction filters.
- Paragraph 3 requires a PSP to **compensate** another PSP **for damages** incurred where there is a violation of an asset freeze or prohibition of making funds available. “Damages” in this case are penalties imposed for executing a prohibited transaction. EU sanctions law does not recognise strict liability; this means that businesses can only be held liable for a sanctions violation if they intentionally or at least negligibly violate sanctions regulations or meet the liability requirements outlined in the individual EU sanctions regulations. Since the originator’s verification obligations (i.e. customer screening) lie solely with the PSP of the originator of a payment, the PSP of the payee of an instant credit transfer cannot be held liable for failures by the originator institution. It is therefore difficult to imagine a situation where this regulation would come into play. However, if the payee’s PSP is (itself) at fault there is no legal reason why the originator institution should indemnify the other PSP against “damages” incurred due to its error. We therefore see no reason for including this stipulation and it should therefore be deleted from the proposed regulation.
- In addition, the new paragraph 1b to be added to Article 11 sets out minimum penalties for violations. EU sanctions regulations regularly contain a passage according to which member states must set penalties that are “effective, proportionate and dissuasive” (see, for example, Regulation 269/2014, Article 15). No further requirements are made in this regard because the enforcement of sanctions is a matter for the member states. The new wording in Article 11 departs from this practice and sets minimum penalties which seem unreasonably high and only apply to instant credit transfers. This is quite a considerable departure from the usual practice. Furthermore, it is completely unjustified and disproportionate to provide for such high penalties for compliance officers in cases of

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personal liability, for example when careless mistakes are made. Against the background of the EU Commission's recently published proposal for a directive "on the definition of criminal offences and penalties for the violation of Union restrictive measures", we therefore recommend deleting the passage on minimum penalties in the current proposal and leaving the issue of criminal offences to the new directive.

- With this in mind, we recommend a thorough analysis of the Commission's proposal and more intensive dialogue with the banking industry regarding such interactions. The associations of the German Banking Industry Committee and their members would be happy to attend a meeting of experts to discuss this topic.