



# **ECSAs Ad-Hoc Task Force on Sanctions Screening and Instant Payments**

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## Task Force Work

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- In its last meeting on 20 May 2021, AMI-Pay tasked the ECSAs to coordinate the work on possible developments concerning banks' own **internal operational processes** (e.g., decision reapplication modules, transformation of the internal operation into a 24/7 manner etc.), which may contribute to a more effective sanctions screening of Financial Institutions, hence to the **reduction of false positives**.
- The ECSAs put together a dedicated TF that started work in October
- TF quickly concluded that focusing on banks internal processes only would not really help to bring about an effective solution to the issues. Banks have consistently improved their screening tools and processes, thus optimising them even before the implementation of SCT Inst. However, SCT Inst **exposed issues surrounding the underlying sanctions screening framework that are not suited for a real-time world**.
- The TF is working on a comprehensive report evaluating different measures that should be finalised by year-end. It is important to note that this presentation reflects the **preliminary outcome of the work** that still needs to be approved within the ECSAs.



# Instant Payments and Sanctions Screening in the EU

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- There is an expectation that SCT Inst will be used much beyond the use cases of 'traditional' SCT, for instance **be deployed at PoI** as a possible alternative to card payments
- At the same time, **cross-border use of SCTInst** can also be expected to increase
- It has become increasingly evident that the **current sanctions screening framework needs to be amended before instant payments can be scaled to the level of 'new normal'**.
- The main issue related to cross-border instant payments (or domestic instant payments in some countries) in the SEPA area is the fact that they create a **high level of false positive alerts generated in transaction screening, causing rejects**.



# Instant Payments and Sanctions Screening in the EU

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- The high rate of false positive alerts is due to the **current legislative framework, which requires both the payer and the payee PSPs to perform ex-ante sanctions screening before respectively debiting or crediting the transaction**, in addition to screening the client databases.
- The process of reviewing a transaction screening alert and determining whether it is a true or a false hit require **human intervention** which does not comply with the requirements for processing SCT Inst (as this always takes longer than the maximum execution time of SCT Inst)
- Most banks now have an estimated alert rate for payments that often need to be manually reviewed and verified between 3% and 15%
- Banks are required to detect both sanctioned entities in case of a perfect match, as well as misspellings and other derivations -> screening tools alert on a lot of transactions that do not contain the sanctioned entity itself but only strings of data similar to the sanctioned entity. This implies that although screening may become more efficient with the deployment of new tools, by definition there will always be some level of friction.



## Best way forward: client database screening (1/2)

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- The best way to resolve the issues created by sanctions screening of instant payments would be to **rely solely on client database screening instead of transaction screening**: create a common EU sanctions framework where each PSP screens its customers both at the onboarding and is obliged to perform daily screening of its client database, instead of screening every individual transaction
- In terms of implementation effort for banks, all banks already apply customer screening when onboarding a client and most of the banks already conduct a daily screening of their client database, therefore very little additional implementation would be required. Both for client database screening and transaction screening the screening process is automated and the alert handling is largely a manual activity. Relying solely on client database screening would remove the need for manual checks on a transaction basis.



## Best way forward: client database screening (2/2)

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- However, transaction screening would still have to be applied in some cases:
  - In the absence of a **single EU-level sanctions list**, client database screening would not provide for a full solution as **PSPs would still have to maintain transaction screening for national lists**. Important frictions would still remain, even though false positive alerts causing rejects would be reduced. Therefore, **having a single, harmonised EU list would be the most optimal solution** since it would solve the problem at its root, thus improving the customer experience and making instant payments a reliable payment instrument for domestic and cross-border use and **allowing in the long term for the full development and deployment of instant payments across the EU**.
  - Furthermore, it seems unlikely that reliance solely on client database screening could be established for OFAC lists. Therefore, transaction screening will still have to be done by the banks subject to OFAC lists.



# Alternative measure: level playing field between cards and SCT Inst at Pol

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- Card payments currently largely rely on client database screening instead of transaction screening.
- Card transactions are also out of scope of the Funds Transfer Regulation (FTR) and FATF Recommendation 16 as cards are used for the purchase of goods and services and person-to-person transfers are not possible.
- If SCT Inst is to be extended to use at Pol, the EU framework for sanctions screening should recognize that when used in similar situations than card payments – at Point of Sale or online for the purchase of goods and services – **SCTInst transactions should be considered similarly than card transactions for sanctions screening purposes.**

## Other option considered

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- In order to provide a complete analysis of all the different aspects that could improve the current sanctions screening process, some other options have been analysed. However, after a thorough assessment the TF came to the conclusion that **none of them would resolve the issue** and would not allow for the required user experience and the scaling of SCT Inst, the main reason being that there will always remain a substantial amount of friction caused by transaction screening.
- More in detail, the TF analysed the following alternative options:
  - a) Single transaction filtering at the payer's side
  - b) Changes in the payment scheme (SCT Instant Payment Rulebook)
  - c) Improving data on sanctions list
  - d) Consider improving identifiers used in payment transactions in the long term
  - e) Move sanction screening to post-execution



## Other options considered:

### a) Single transaction Filtering at the Payer's Side

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- A possible measure to reduce frictions and to avoid duplicate screening would be to screen only at the payer's side, thus exempting the screening requirement at the payee's side and preventing double transaction screening.
- However, this measure would not remove the need to screen against EU national lists, which would still need to be done both at payer and payee PSP side. Other negative aspects of this potential option include:
  - Screening would remain transaction-based
  - The payer PSP does not necessarily receive correct information on the payee from the payer
  - The payee PSP would need to rely on the screening of another PSP
  - Problematic in a POI context



Other options considered:

## b) Changes in the Payment Scheme (SCT Instant Payment Rulebook)

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- Another possible option is the introduction in the SCT Inst Rulebook of a pending status for transactions that have generated an alert in transaction screening to investigate if they are true or false hits. After the review of the alert, the beneficiary bank would either confirm or rejects the transaction, depending on the outcome of the review. In this scenario, it could also be considered whether the originator should also get the possibility to cancel the transaction in case of an alert and revert to normal SCT.
- However, this option would alter the very nature of instant payments, creating uncertainty for end-users.
- This option would not provide a solution for SCT Inst transactions and would add a lot of complexity, especially at the POI.



Other options considered:

## c) Improving data on EU sanction list

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- EU authorities could help improve the screening process by improving the data on the EU and national lists, for instance by making a clear difference between strong and low-quality aliases, and authorisation not to filter low-quality aliases, as OFAC has done.



Other options considered:

## d) Improving identifiers used in payment transactions in the long term

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- Identifiers, such as the LEI (for companies) could offer an opportunity when used in the context of payment transactions and sanctions screening. The use of such an identifier would allow for the exact matching and would therefore facilitate the screening process.
- However, it seems unrealistic that the use of LEI or other such identifiers could be extended to individuals. Additionally, a broad implementation of the LEI across Europe has not been taken place so far, thus any strengthening of the LEI's role in sanctions screening could only be complimentary to the approaches discussed above.



Other options considered:

e) Move sanction screening to post-execution

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- In some jurisdictions, certain (instant) transactions can be screened post-execution and the funds can be reclaimed even once credited to the customer. If such a change in legislation would be considered, PSPs could move to a post transaction screening method.
- However, this option would remove the finality of SCT Inst transactions, which is a fundamental characteristic.



**Thank you for your attention!**