

5-1-2009

Payment Transactions Under the EU Payment Services Directive: A U.S. Comparative Perspective

Benjamin Geva

Follow this and additional works at: <http://elibrary.law.psu.edu/psilr>



Part of the [International Law Commons](#)

Recommended Citation

Geva, Benjamin (2009) "Payment Transactions Under the EU Payment Services Directive: A U.S. Comparative Perspective," *Penn State International Law Review*: Vol. 27: No. 3, Article 9.

Available at: <http://elibrary.law.psu.edu/psilr/vol27/iss3/9>

This Article is brought to you for free and open access by Penn State Law eLibrary. It has been accepted for inclusion in Penn State International Law Review by an authorized administrator of Penn State Law eLibrary. For more information, please contact ram6023@psu.edu.

Payment Transactions under the EU Payment Services Directive: A U.S. Comparative Perspective

Benjamin Geva*

I. INTRODUCTION

Implementing a Proposal¹ of the Commission of the European Communities (“the Commission”), the Directive on payment services in the internal market, often colloquially referred to as “the payment services Directive” (“Directive”),² provides for “a harmonised legal framework” designed to create “a Single Payment Market where improved economies of scale and competition would help to reduce cost of the payment system.” Focusing on electronic payments, the Proposal purported to “only harmonise what is necessary to overcome legal barriers to a Single Market, avoiding regulating issues which would go beyond this matter.”³

* Professor of Law, Osgoode Hall Law School, York University. LL.B., Jerusalem; M, SJD, Harvard; member of the Ontario Bar. Research assistance by Osgoode student Joseph Juda is acknowledged with gratitude. Author takes responsibility for any error.

1. *Commission Proposal for a Directive of the European Parliament and of the Council on Payment Services in the Internal Market*, COM (2005) 603 final (Dec. 1, 2005), available at http://ec.europa.eu/internal_market/payments/framework/index_en.htm. Quotations in the text are from the Explanatory Memorandum, under “Context of the Proposal,” which further cites Articles 47(2) and 95(1) of the EC Treaty as the legal basis for the proposal. The proposal was discussed by this author in Benjamin Geva, *Recent International Developments in the Law of Negotiable Instruments and Payment and Settlement Systems*, 42 TEX. INT’L. L.J. 685, 712-25 (2007).

2. Council Directive 2007/64/EC, On Payment Services in the Internal Market, 2007 O.J. (L 319) 1 (EC) [hereinafter Directive]. This amended several previous Directives—Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC—and repealed Directive 97/5/EC of the European Parliament and of the Council of 27 January 1997 on cross-border credit transfers. [SHERRY: can you fix this extra, blank line?]

3. *Commission Proposal*, *supra* note 1, at 7 (under “Legal Elements of the Proposal”).

Title I of the Directive provides for subject matter, scope and definitions. It is followed by three substantive components. Title II covers payment service providers. Title III deals with transparency of conditions and information requirements for payment services. Title IV governs rights and obligations in relation to the provision and use of payment services. Under Directive Article 2, both Titles III and IV apply only where both the payer's and payee's payment service providers are located in the Community. In a major departure from the Proposal, Titles III and IV are not limited to payment transactions of up to EUR 50,000;⁴ there is no amount ceiling whatsoever for payment transactions governed by them. The three substantive components are followed by Title V, dealing with implementing measures and Payment Committee, and Title VI, consisting of final provisions. Particularly, implementing measures may be adopted by the Commission with the view of (i) amending "non-essential elements of [the] Directive, relating to" the adaptation of the list of activities that constitute "payment services" under the Annex, as well as (ii) updating amounts specified in a few provisions "in order to take account of inflation and significant market developments."⁵

This article endeavours to analyse the provisions of Title IV governing rights and obligations in relation to the provision and use of payment services. Analysis is particularly from a US comparative perspective.⁶ Attention will be given to Uniform Commercial Code ("UCC") Article 4A, which governs U.S. wire and other credit transfers as well as federal laws governing consumer retail payment systems. A broader but related objective of the article is the assessment of the contribution of Title IV to the harmonization of funds transfer and payment law, not only by comparison to the U.S., but also by reference to a few aspects of a national law of an EU Member State. Scope does not allow a comprehensive treatment to either aspect, particularly the latter; yet, salient issues will be addressed. The ultimate conclusion is

4. The applicable Proposal provision setting this ceiling for Titles III and IV is Article 2(1). Note that about 70% of all TARGET2 (for which *see* note 42 *infra*) payments are below 50,000 EURO. *See* EUROPEAN CENTRAL BANK-EUROSYSTEM, TARGET ANNUAL REPORT 2008 at 18 chart 9; BENJAMIN GEVA, LAW OF ELECTRONIC FUNDS TRANSFERS § 4.04[7] 4-139 n.180 (2008) (1992).

5. Directive art. 84. Another matter that can be so changed is "the definition of micro enterprise within the meaning of Article 4(26) . . .," *id.*, which may be important should a Member State move to apply to micro enterprises prohibitions against disclaimer clauses as set out in Title III and IV.

6. For a discussion of the entire Directive, albeit in a context of a significantly less extensive comparative analysis, *see* Benjamin Geva, *The EU Payment Services Directive: An Outsider's View*, in 28 YEARBOOK OF EUROPEAN LAW 2009 (Eeckhout & Tridimas eds., forthcoming).

that the Directive is a positive but inadequate step towards global and European harmonization.

II. SCOPE

The scope of the Directive is stated in Article 2(1) to “apply to payment services provided within the Community,” both national and cross-border.⁷ It governs the business activity of carrying out payment through the services of one or two payment services providers, each acting for a “payment service user”,⁸ the latter being either the payer (that is, “payor” in American English) or the payee, who may be either a natural or legal person.⁹ The payment service may be carried out for either a consumer or business transactions, and may be for any amount.

Payment services providers¹⁰ consist of: credit institutions (commercial banks and electronic money institutions), post office giro institutions, central banks, Member States or their regional or local authorities, as well as “payment institutions” established under the Directive—primarily, money transmitters.¹¹

Effectively, a payment service is performed in the form of carrying out a payment transaction: namely, a transfer of funds from a payor to a payee. The scope of the Directive, in comparison to legislation in the U.S. covering payment transactions, is thus to be assessed by reference to an overall framework explaining and classifying funds transfers.

Conceptually, a payment mechanism denotes a payment transaction; it can broadly be described as any machinery facilitating a non-cash payment in monetary value. While authorizing or conferring on the payee the right to claim the sum of payment from a third party, it enables the payor (i) to avoid the transportation of money and its physical delivery to the payee, and (ii) where applicable, to obtain in the process a discharge of a debt owed by the payor to the payee.¹² A payment mechanism carried out through the banking system may be described as

7. Directive art. 2(1). This is in departure from European Parliament and Council Directive 97/5/EC, On Cross-Border Credit Transfers, 1997 O.J. (L 43) 25 (EC) (known as “the Transparency Directive”), that was superseded by Title III and repealed by the Payment Service Directive.

8. Directive art. 4(10) (defining “payment service user” to mean “a natural or legal person making use of a payment service in the capacity of either payer or payee, or both”). “Payer” and “payor” are used in this article interchangeably.

9. See definitions of “payer” and “payee” in Directive Article 4(7) and (8), respectively.

10. Defined in Directive Article 4(9) by reference to Directive Article 1(1).

11. On the whole, they are mostly banks or deposit-taking institutions, so that hereafter, “payment service providers” and “banks” are used interchangeably.

12. This is designed to improve on, for example, Benjamin Geva, *International Funds Transfers: Mechanisms and Laws*, in *CROSS-BORDER ELECTRONIC BANKING: CHALLENGES AND OPPORTUNITIES 1-2* (C. Reed, I. Walden & L. Edgar eds., 2d ed. 2000).

a “funds transfer”;¹³ thereunder, funds “move” from one bank account to another, whether at the same or two different banks. It involves a process under which the debt owed to the payor by the payor’s bank is ultimately replaced by a new debt owed to the payee by the payee’s bank.

A funds transfer is initiated by payment instructions given by the payor or under the payor’s authority and issued directly or indirectly to the payor’s bank. It is the manner of communicating these instructions to the payor’s bank and the resulting sequence of the ensuing banking operations that determine the classification of each mechanism. Thus, depending on how these instructions are communicated to the payor’s bank, funds transfers are either debit or credit transfers. As a rule, the communication flow and the movement of funds are in opposite directions in a debit transfer but in the same direction in a credit transfer.

In a debit transfer, the payor’s instructions are communicated to the payor’s bank by the payee through the payee’s bank. Such instructions are issued by the payee under the payor’s authority, given in the form of either a specific check or general authority to initiate pre-authorized debits to the payor’s account (as, for example, in connection with recurring mortgage or insurance premium payments). When the instructions are communicated by the payee to the payee’s bank, the payee’s account may be credited. The payee’s bank passes these instructions onto the payor’s bank, either directly or through an intermediary bank or banks. When the instructions ultimately reach the payor’s bank, the payor’s account is debited. Funds are thus collected or “pulled” from the payor’s account to the payee’s account. By definition, in a debit transfer any credit to the payee’s account precedes the debit to the payor’s account; credit to the payee’s account is thus provisional; it may not necessarily be available for immediate use, and is subject to reversal if the payor’s bank dishonors the payor’s instructions (e.g., for lack of funds) and communicates its rejection to the payee’s bank. Such communication may be direct or through the same banking channels by which the instructions were communicated to the payor in the first place. Credit to the payor’s account becomes final only as of the time the payor’s bank becomes accountable, or makes a “final payment,” for the amount, irreversibly debited or to be debited to the payor’s account.

In contrast, in a credit transfer (such as a direct deposit of payroll, benefit, interest, pension, or dividend, as well as a wire payment) the payor’s instructions are communicated to the payor’s bank directly by

13. Unfortunately, however, the drafters of the Uniform Commercial Code reserved the term to denote exclusively a credit transfer. *See* U.C.C. art. 4A, Prefatory Note (2008).

the payor or the payor's agent without the meditation of a credit to the payee's account at the payee's bank. In terms of the banking operation, when the instructions are communicated to the payor's bank, the payor's account is debited. Thus, in a credit transfer, unlike in a debit transfer, the first impact of the payor's instructions on the banking system is a debit to the payor's account with the payor's bank. Having received the payor's instructions and debited the payor's account, the payor's bank forwards the instructions, directly or through intermediary bank(s), to the payee's bank, which ultimately credits the payee's account. Hence, in a credit transfer, the debit to the payor's bank precedes the credit to the payee's account and is not subject to reversal for lack of funds. Stated otherwise, in a credit transfer, funds debited to the payor's account are "pushed" and paid into the payee's account.

"Payment services" to which the Directive applies under Article 2(1) are defined in Article 4(3) to mean business activities listed in the Annex. "Payment services" listed in the Annex¹⁴ consist of: cash deposits in, and withdrawals from, payment accounts;¹⁵ execution of payment transactions¹⁶ in funds¹⁷ held on deposit in a payment account; execution of direct debits; execution of payment transactions through a payment card (or a similar device); execution of credit transfers (including standing orders); execution of payment transactions in funds covered by a credit line; execution of direct debits (including one-off direct debits);¹⁸ issuing of payment cards; execution of payment

14. The list is, however, quite disorganized and repetitive; for example, three items (card payments, direct debits and credit transfers) are enumerated separately according to whether they are used in connection with a "payment account" or credit line.

15. See Directive art. 4(14) (defining "payment account" to mean "an account held in the name of one or more payment service users which is used for the execution of payment transactions"). The Proposal required the account to be used "exclusively" for the execution of payment transactions, which was unnecessarily restrictive.

16. "Payment transaction" is defined in Directive Article 4(5) to mean "an act, initiated by the payer or by the payee, of placing, transferring or withdrawing funds, irrespective of any underlying obligations between the payer and payee."

17. "Funds" are defined in Directive Article 4(15) to mean "banknotes and coins, scriptural money and electronic money as defined in Article 1(3)(b) of Directive 2000/46/EC."

18. "Direct debit" is defined in Directive Article 4(28) to mean "a payment service for debiting a payer's payment account, where a payment transaction is initiated by the payee on the basis of the payer's consent given to the payee, to the payee's payment service provider or to the payer's own payment service provider." Unfortunately, "credit transfers" and "payment card" are not defined. Cf. Directive art. 4(23) (defining "payment instrument" to mean "any personalised device(s) and/or set of procedures agreed between the payment service user and the payment service provider and used by the payment service user in order to initiate a payment order"); see also *id.* art. 4(16) (defining "payment order" as "any instruction by a payer or payee to his payment service provider requesting the execution of a payment transaction").

transactions in e-money;¹⁹ money remittance services in funds accepted for the sole purpose of carrying out the payment transaction;²⁰ and execution of certain payment transactions by means of any telecommunication, digital or IT device.

Directive Article 3 deals with the outer limits of the Directive. Thereunder, cash payments, professional physical transport of banknotes and coins; payment transactions consisting of the non-professional cash collection and delivery within the framework of a non-profit or charitable activity; payment transactions through a commercial agent authorized to negotiate or conclude the sale or purchase of goods or services on behalf of the payer or the payee; as well as certain cash refunds are specifically excluded. Also excluded from the coverage of the Directive are currency exchange transactions in the form of cash-to-cash operations; paper checks, drafts (i.e., bills of exchange), vouchers, traveller's checks and postal money orders; payment transactions carried out within a payment or securities clearing and settlement system; payments transactions related to securities asset servicing; payment processing services; payment by instruments which are not redeemable within a limited network or affiliated service providers; certain payment transactions executed by means of a mobile telephone or any other digital or IT device;²¹ payment transactions carried out between payment service providers for their own account as well as between entities belonging to the same corporate group such as subsidiaries; and "services by providers to withdraw cash by means of automated teller machine acting on behalf of one or more card issuers, which are not a party to the framework contract with the customer withdrawing money from a payment account, on condition that these providers do not conduct other payment services as listed in the Annex."²²

19. See Council Directive 2000/46/EC, On the Taking Up, Pursuit of and Prudential Supervision of the Business of Electronic Money Institutions, art. 1(3)(b), 2000 O.J. (L 275) 39 (EC) (defining "electronic money" to mean "monetary value as represented by a claim on the issuer which is: (i) stored on an electronic device; (ii) issued on receipt of funds of an amount not less in value than the monetary value issued; (iii) accepted as means of payment by undertakings other than the issuer").

20. Directive Article 4(13) defines "money remittance" to mean "a payment service where funds are received from a payer, without any payment accounts being created in the name of the payer or the payee, for the sole purpose of transferring a corresponding amount to a payee or to another payment service provider acting on behalf of the payee, and/or where such funds are received on behalf of and made available to a payee."

21. Effectively excluded are "payment transactions executed by means of any telecommunication, digital, or IT device" made to "a telecommunication, digital or IT operator" acting as a supplier for "goods and services . . . delivered" and designed "to be used through a telecommunication, digital or IT device" and not "only as an intermediary between the [payer] and the supplier of the goods and services." See Directive art. 3(f).

22. See *id.* art. 3(o). This language is grammatically obscure and hence its meaning is not immediately discernable.

In the U.S., electronic funds transfers out of and into consumer asset accounts are governed by the federal Electronic Fund Transfer Act (“EFTA”)²³—subchapter VI of the Consumer Credit Protection Act (“CCPA”)²⁴—and Regulation E,²⁵ which implements the EFTA. Regulation E section 205.3(b) defines “electronic fund transfer” to mean “any transfer of funds that is initiated through an electronic terminal, telephone, computer or magnetic tape for the purpose of ordering, instructing or authorizing a financial institution²⁶ to debit or credit an account.”²⁷ The provision goes on to state that the term:

includes, but is not limited to, (i) Point-of-sale transfers; (ii) Automated teller machine transfers; (iii) Direct deposits or withdrawals of funds; (iv) Transfers initiated by telephone; and (v) Transfers resulting from debit card transactions, whether or not initiated through an electronic terminal.²⁸

Regulation E section 205.3(c) excludes checks, drafts or similar paper instruments, check guarantee or authorization service, transfers through Fedwire or similar wire transfer systems used primarily for business transactions, certain securities or commodities transfers, certain automatic transfers, certain telephone-initiated transfers, and pre-authorized transfers to small financial institutions.²⁹

At the same time, while EFTA and Regulation E govern access to a consumer asset account, the federal Consumer Credit Cost Disclosure Act (“CCDA”)³⁰—Subchapter 1 of the CCPA—implemented by section 226.12 of Regulation Z Truth in Lending³¹ governs a card accessing a credit plan, namely a credit card. “Credit card” is defined as “any card, plate, coupon book, or other single credit device that may be used from time to time to obtain credit.”³² This definition focuses on the credit facility provided by the card, and does not address the means of authenticating the payment by it. Nevertheless, the need for an

23. Electronic Fund Transfer Act, 15 U.S.C. §§ 1693-1700 (1978).

24. Consumer Credit Protection Act, 15 U.S.C. §§ 1601-1700 (1978).

25. Regulation E, 12 C.F.R. § 205 (amended 1981).

26. For our purposes, “financial institution” under EFTA is interchangeable with both “bank” under U.C.C. Article 4A and “payment service provider” under the Directive.

27. See Regulation E, 12 C.F.R. § 205, 205.2(b)(1) (defining “account” as a consumer asset account). Since 2006, the definition includes “payroll card account” as defined in Section 205.2(b)(2).

28. Regulation E, 12 C.F.R. § 205, 205.3(b)(1) (2006).

29. *Id.* §§ 205, 205.3(c).

30. 15 U.S.C. § 1631 (2006).

31. Regulation Z, 12 C.F.R. §226, as amended.

32. *Id.* § 226.2(a)(15), which goes on to define “charge card” to mean “a credit card on an account for which no periodic rate is used to compute a finance charge.”

authorized user's identification under the third condition for liability for unauthorized use, set out above, was interpreted to cover manual signature, photograph or fingerprint on the card, as well as magnetic stripe used in conjunction with a code.³³

Interestingly, under EFTA and Regulation E, neither "debit card" nor "debit card transaction" is defined; terminology must be in reference to a payment card facilitating the transfer of funds from or into a consumer asset account.³⁴ Thus, the dividing line between the credit card covered by Reg. Z and the debit card covered by Reg. E, is not the method of authentication, but rather the type of account to be accessed with the card; the former accesses a credit plan while the latter accesses an asset account.³⁵ Stated another way, both a debit card and credit card transaction, respectively covered by Reg. E and Reg. Z, could be authenticated either electronically or otherwise, including by means of a manual signature. What matters is the type of account accessed; it is an asset account for the debit card and a credit plan for the credit card.

The transaction covered in the U.S. by U.C.C. Article 4A is a credit transfer, called a "funds transfer."³⁶ It consists of a "series of transactions, beginning with the originator's payment order, made for the purpose of making payment to the beneficiary of the order . . . [which] is completed by acceptance by the beneficiary's bank of a payment order for the benefit of the beneficiary of the originator's payment order."³⁷ However, a funds transfer "any part of which is governed by [EFTA]" is specifically excluded.³⁸ Each of the "series of transactions" of which the "funds transfer" consists, involves a "payment order," meaning an instruction of a sender to a receiving bank, transmitted orally, in writing, or electronically (whether online or offline), to pay, or cause another

33. Regulation Z Official Staff Interpretations to § 226.12, 12 C.F.R. § 226, ¶ 12(b)(2)(iii)(1)-(2) (Supp. I 1999).

34. See Regulation E Official Staff Interpretations to § 205.3(b), 12 C.F.R. § 205, ¶ 3(b)(1)(1)(iv) (Supp. I 1999) (which covers "[a] transfer from the consumer's account resulting from a debit-card transaction at a merchant location, even if no electronic terminal is involved at the time of the transaction, if the consumer's asset account is subsequently debited for the amount of the transfer").

35. Obviously, delineation is not always straightforward. A card accessing an asset account tied to an overdraft line as well as a card that accesses both a credit and asset account could be a credit card governed by Reg. Z. See Regulation Z Official Staff Interpretations to § 226.2(a)(15), 12 C.F.R. § 226, 2(a)(2) ¶ 1(i)(A) and (B). Presumably, Reg. Z will apply to activities in the credit line and Reg. E to the asset account activity. Details are outside the scope of this study. See Reg. E § 205.12(a) and Official Staff Commentary on Reg. E 205.12(a); see also Reg. Z § 226.12(g).

36. U.C.C. § 4A-104 (2008). So far as terminology is concerned, no distinction is to be made between a "funds transfer" per U.C.C. Article 4A and "fund transfer" per EFTA and Reg. E.

37. *Id.* § 4A-104(a). Pertinent terms are defined in Sections 4A-103 to 105.

38. *Id.* § 4A-108.

bank to pay, a fixed or determinable amount of money to a beneficiary.³⁹ Accordingly, for each payment order, the parties are the sender and the receiving bank. In connection with an interbank transfer, other than solely between accounts in correspondent banks, the parties to a funds transfer are the originator, the originator's bank, one or more intermediary banks, the beneficiary's bank and the beneficiary.

In the terminology of the Directive, the originator under U.C.C. Article 4A is the payer; the beneficiary under U.C.C. Article 4A is the payee; the originator's bank under U.C.C. Article 4A is the Directive payer's payment service provider; and the beneficiary's bank under U.C.C. Article 4A is the Directive payee's payment service provider.

Unlike U.C.C. Article 4A, the Directive is not limited to credit transfers and does not exclude consumer transactions.⁴⁰ Its coverage extends to both credit and debit transfers as well as to consumer and business payment transactions. Unfortunately however, this achievement is mitigated by two factors. First, the Directive is not as comprehensive as U.C.C. Article 4A in terms of the range of issues covered. Second, the provisions outlining the scope of the Directive, set out above, are not entirely clear. They do not focus on the conceptual framework covering both credit and debit transfers but rather are saddled with unnecessarily long details, some of which are obscure. In the final analysis, in endeavoring to ascertain the underlying framework determining the scope of the Directive, one may get lost in a maze and not see the forest from the trees.

In turn, federal legislation in the U.S. governing consumer retail payment systems does not address the classification between debit and credit transfers; rather, scope of each relevant statute hinges on the type of consumer account accessed by consumers. In addition, federal legislation in the U.S. focuses on disclosures and misuse of payment devices; it does not purport to provide for a comprehensive scheme governing rights and obligations in connection with carrying out payment transactions. In short, consumer payment law in the U.S. is more of consumer protection law, with no parallel to U.C.C. Article 4A providing for a comprehensive scheme governing rights and obligations in connection with payment transactions governed by it.

39. *Id.* § 4A-103(a)(1).

40. See GEVA, *supra* note 4, § 2.02[3](c) (discussing the scope of U.C.C. Article 4A).

III. TITLE IV: RIGHTS AND OBLIGATIONS: OVERVIEW

Directive Title IV consists of:

- common provisions (Chapter 1 consisting of Articles 51-53);
- the authorization of payment transactions (Chapter 2 consisting of Articles 54-63);
- the execution of payment transactions (Chapter 3 consisting of Articles 64-78);
- data protection (Chapter 4 consisting of Article 79); and
- out-of-court complaint and redress procedures for the settlement disputes (Chapter 5 consisting of Articles 80-83).

The present article discusses the provisions of Chapters 1-3 by reference to parallel provisions in legislation in the U.S.

For the provisions of Title IV to apply, other than Directive Article 73 as discussed below, both the payer's and payee's payment service providers must be located in the Community.⁴¹ Stated otherwise, the Directive will not apply to payments coming from or going out of the Community, even when they are denominated in euro. As for the payment as it is carried out between two payment service providers located in the Community, transfer need not necessarily be over TARGET2,⁴² nor need it necessarily be in euro.

Other than in consumer⁴³ payment transactions, Directive Article 51 provides for the ability of parties to contract out of or vary some of the provisions of Title IV.⁴⁴ Directive Article 51 also allows Member States

41. Directive art. 2(1).

42. TARGET2 is the transfer system of the European Union for large-value and urgent payments. See e.g., *TARGET2- The New Payment System for Europe*, MONTHLY REP. OF DEUTSCHE BUNDESBANK, Oct. 2007, at 69; Nicolas de Sèze, *TARGET2: From Concept to Reality*, 149 BANQUE DE FRANCE BULLETIN DIGEST 1 (2006). For a comprehensive discussion on the legal framework, see Kestutis Laurinavičius, Klaus M. Löber & Hans Weenink, *Legal Aspects of Target2*, 23 J. INT'L BANKING L. & REG. 15 (2008). See numerous reports and informational brochures of the European Central Bank. See also Benjamin Geva, *TARGET2 Transfer of Funds and Harmonization of EU Payment Law*, 41 UCC L.J. 113 (2008).

43. See Directive art. 4(11) (defining "consumer" to mean "a natural person who, in payment service contracts covered by this Directive, is acting for purposes other than his trade, business or profession").

44. See *id.* art. 51(1) ("Where the payment service user is not a consumer, the parties may agree . . . [that various provisions] shall not apply in whole or in part.").

to exempt consumers from Directive Article 83 requirements covering out-of-court redress.⁴⁵ It further allows Member States to provide that Title IV applies to micro-enterprises⁴⁶ “in the same way as to consumers.”

Specifically, Directive Article 51 provides for the power of parties to contract out of or vary some provisions other than in connection with a consumer payment service user.⁴⁷ Thus, in non-consumer payment transactions, parties may contract out of: provisions dealing with allocation of charges;⁴⁸ authorization by consent by means of an agreement;⁴⁹ time for notifying an unauthorized or incorrectly executed payment transaction;⁵⁰ onus of proof in connection with an alleged unauthorized payment transaction;⁵¹ allocation for losses for unauthorized payments;⁵² refund for debit transfers;⁵³ irrevocability of a payment order;⁵⁴ and loss allocation in connection with non-execution or defective execution.⁵⁵

By comparison, variation by agreement is recognized in principle by U.C.C. Section 4A-501.⁵⁶ Serious limitations nonetheless exist; for example, limitations exist in connection with unauthorized payment orders, receiving bank’s liability for improper or late execution, refund upon non-execution, and some beneficiary’s rights against beneficiary’s bank.⁵⁷ In line with the Directive, waiver of rights is precluded in the U.S. for consumer payment systems for both credit cards⁵⁸ and electronic fund transfers.⁵⁹

45. *Id.* art. 51(2).

46. Defined in Directive Article 4(26) to mean “an enterprise, which at the time of conclusion of the payment service contract, is an enterprise defined in Article 1 and Article 2(1) and (3) of the Annex to Recommendation 2003/361/EC [2003 O.J. (L 124) 36].” In principle, this is an enterprise (namely an entity engaged in economic activity irrespective of its legal form) which employs fewer than 10 persons and whose annual turnover and/or annual balance sheet total does not exceed EUR 2 million.

47. *See* Directive art. 51(1) (requiring that the specified provisions of the Directive “shall not apply in whole or in part”).

48. *Id.* art. 52(1).

49. *Id.* art. 54(2).

50. *Id.* art. 58.

51. *Id.* art. 59.

52. Directive art. 61.

53. *Id.* arts. 61, 62.

54. *Id.* art. 66.

55. *Id.* art. 75.

56. U.C.C. § 4A-501 (2008). Provisions of Article 4A may also be varied by Federal Reserve regulations and circulars and to some extent by funds-transfer system rules. *See id.* §§ 4A-107, 4A-501(b).

57. *See id.* §§ 4A-202 to 204, 4A-305(f), 4A-402(f), 4A-404(c). For a discussion, *see* GEVA, *supra* note 4, § 2.02[6].

58. CCCDA, 15 U.S.C. §§ 1631, 1643(c), (d) (2006).

59. EFTA, 15 U.S.C. § 1693l (2006).

In principle, the different treatment for consumer and business payments, which is common to both the Directive and U.S. legislation, is understandable. Moreover, policy grounds support the ability of business parties to contract out provisions that are suitable for consumer retail payments. However, unlike U.C.C. Article 4A in the U.S., the Directive does not contain a solid threshold—namely, a meaningful standard from which even non-consumers ought not to be released. The point will be demonstrated further below in the discussion on unauthorized payment orders.

Another common provision is Directive Article 53 dealing with derogation for low value payment instruments and electronic money. It applies to payment instruments that “solely concern individual payment transactions not exceeding EUR 30 or which either have a spending limit of EUR 150 or store funds which do not exceed EUR 150 at any time.”⁶⁰

Finally, a common provision, although not enumerated as such, is Directive Article 78, located at the end of Chapter 3. Directive Article 78 provides for a defense to liability under the liability provisions of Title IV. Thus, under Directive Article 78, “[l]iability under Chapter 2 and 3 [liability in connection with either the authentication or the execution of payment transactions] shall not apply in cases of abnormal and unforeseeable circumstances beyond the control of the party pleading for the application of those circumstances, the consequences of which would have been unavoidable despite all efforts to the contrary, or where a payment service provider is bound by other legal obligations covered by national or Community legislation.”⁶¹ Similarly, under EFTA § 1693h(b), a financial institution is exempted from liability where its action or failure to act resulted from “an act of God or other circumstances beyond its control”⁶² or technical malfunction known to the consumer.⁶³

IV. AUTHORIZATION OF PAYMENT TRANSACTIONS.

Authorization of payment transactions is governed by the Directive in Chapter 2 consisting of Directive Articles 54-63. The provisions cover authorization in general and electronic authorization in particular,

60. See Directive art. 53(1). However, under Directive Article 53(2), for national payment transactions, “Member States . . . may reduce or double [these] amounts. . . . They may increase them for prepaid payment instruments up to EUR 500.” “Prepaid payment instruments” are undefined.

61. *Id.* art. 78.

62. 15 U.S.C. §§ 1693, 1693h(b)(1).

63. *Id.*

onus of proof, liability for losses, as well as reversal of authorized debit transfers.⁶⁴

“Authorization” in the form of “consent” is to be given for the execution of a “payment transaction.”⁶⁵ Directive Article 54 treats authorization only in terms of the payer’s consent, which is obviously required also for “debit-pull” withdrawals by the payee from the payer’s account.⁶⁶ Directive Article 54 makes no reference to the payee’s authorization given to the payee’s service provider for carrying out a debit transfer from the payer’s account.⁶⁷

Authorization in the form of payer’s consent may be given under Directive Article 54 “prior to or, if agreed between the payer and the payment service provider, after the execution of the payment transaction” and “in the form” as well as under “[t]he procedure” agreed between them.⁶⁸ While in departure from the Proposal, consent is not necessarily required to be “explicit.”⁶⁹ The reference to an agreement, as well as a procedure, weakens the possibility of an implied authority and may be read to eliminate altogether the possibility of an apparent authority,⁷⁰ such as when a cardholder voluntarily delivered the card and shared the associated code with a friend or relative.⁷¹

Where it is required, authorization is not given for indefinite duration; nor is authorization irrevocable. Therefore, under Directive Article 54, consent “may be withdrawn by the payer at any time, but no later than the point in time of irrevocability” of the payment order under Directive Article 66.⁷² “Consent to execute a series of payment transactions” may also be withdrawn with the effect that “any future payment transaction is to be considered as unauthorised.”⁷³

The Directive contemplates authorization to be given either in an electronic form or some other form.⁷⁴ An electronic authorization is defined as authorization given by means of a payment instrument.

64. See Directive arts. 54-63.

65. See *id.* art. 54.

66. See *id.*

67. See *id.*

68. *Id.*

69. As in Article 41 of the Proposal.

70. As a matter of agency law, authority can be actual or apparent. Actual authority may be express or implied. See BLACK’S LAW DICTIONARY 142 (8th ed. 2004).

71. In which case, liability may nevertheless be fastened on the cardholder under Directive Article 61(2), discussed *infra*.

72. See Directive art. 54.

73. The withdrawal of consent to a single future payment transaction (rather than to a series of them) falls under the previous sentence.

74. Stated otherwise, a payment transaction falling under the Directive need not be electronic from end to end; rather, authorization can be given in writing. In fact, even an oral authorization is not precluded.

Important aspects of such authorization are governed by Directive Articles 55 - 57. "Payment instrument" is defined in Directive Article 4(23) as "any personalised device(s) and/or set of procedures agreed between the payment service user and the payment service provider and used by the payment service user in order to initiate a payment order."⁷⁵ A card, used with or without a personal code, will satisfy this definition. Moreover, any agreed upon security procedure will be a "payment instrument."

Limits on the ability to initiate a payment transaction by means of a payment instrument are provided for in Directive Article 55.⁷⁶ Under Article 55(1), where a "specific payment instrument is used for the purposes of giving consent, authorization may be given within agreed "spending limits for payment transactions executed through that payment instrument." According to Article 55(2), under the "framework contract," "the payment service provider may reserve the right to block the payment instrument for objectively justified reasons related to the security of the payment instrument, the suspicion of unauthorised or fraudulent use of the payment instrument" or for similar reasons.

Reciprocal obligations of payment service user and provider in relation to payment instruments are governed by Articles 56 and 57 of the Directive. Under Article 56, the payment service user is required "to use the payment instrument in accordance with the terms governing the issue and use of the payment instrument," and, in particular, to take all reasonable steps to keep safe the personalized security payment instrument. He⁷⁷ is further required to notify the payment service provider "without undue delay on becoming aware of loss, theft or misappropriation of the payment instrument or its unauthorised use."⁷⁸

In turn, the payment service provider issuing a payment instrument is required under Directive Article 57(1):

- (a) to make sure that the personalized security features of the payment instrument are not accessible to third parties;
- (b) to refrain from sending an unsolicited payment instrument other than as a replacement to an existing one;

75. Directive art. 4.

76. *See id.* art. 55.

77. I follow the language of the Directive which uses "he" and "him" to include "she" or "her" as well as "it." In contrast, American legislation is gender-neutral. Any inconsistency in this article reflects my objective to adhere to the language of provisions discussed.

78. Per Directive Article 53(1)(a), this requirement does not apply to a low-value payment instrument that "does not allow its blocking or prevention of its further use."

- (c) to ensure that appropriate means are available at all time to enable the payment service user to make required notifications such as upon the loss, theft, or misappropriation of the payment instrument;⁷⁹ and
- (d) to prevent the use of the payment instrument once such notification has been made.

Directive Article 57(2) allocates to the payment service provider “the risk of sending a payment instrument to the payer or of sending any personalised security features of it.” No reciprocal broad general duties of care to prevent and detect unauthorized use are fastened on the payment service user and provider.

Under Directive Article 59, where a purported payer denies authorization for a payment transaction as debited to his account, it is for his payment service provider “to prove that the payment transaction was authenticated, accurately recorded, entered in the accounts and not affected by a technical breakdown or some other deficiency.” “Authenticated” is however defined by reference to the verification of the authorization by means of a payment instrument.⁸⁰ Furthermore, Directive Article 59 states that “the use of a payment instrument recorded by the payment service provider shall in itself not necessarily be sufficient to prove either that the payment transaction was authorised by the payer or that the payer acted fraudulently or failed with intent or gross negligence to fulfil one or more of his obligations under Article 56.”⁸¹ Stated otherwise, evidence regarding the use of a payment instrument recorded by the service provider is an important element in meeting the required standard of proof for fastening civil liability for authorized use; yet, standing on its own, such evidence creates neither an un rebuttable presumption,⁸² nor even a rebuttable presumption that

79. *Id.*

80. Directive Article 4(19) defines “authentication” to mean “a procedure which allows the payment service provider to verify the use of a specific payment instrument, including its personalised security features.” There is no requirement, comparable to U.C.C. Section 4A-202(b), for a “security procedure,” which is “a commercially reasonable method of providing security against unauthorized payment orders.”

81. Per Directive Article 51(1), where the service user is not a consumer, the parties may agree that Directive Article 59 shall not apply “in whole or in part.” Also, under Directive Article 53(1)(b), which covers low-value payments, states that Directive Article 59 does not apply “if the payment instrument is used anonymously or the payment service provider is not in a position for other reasons which are intrinsic to the payment instrument to prove that a payment transaction was authorised.”

82. *Cf. Judd v. Citibank*, 435 N.Y.S.2d 210, 212 (N.Y.C. Civ. Ct. 1980), where the court stated that it was “not prepared to go so far as to rule that when a credible witness is faced with the adverse ‘testimony’ of a machine, he is as a matter of law faced also with an unmeetable burden of proof.”

reverses the onus of proof, as to whether use was authorized.⁸³ Rather, some corroboration is required.⁸⁴

Allocation of losses for unauthorized payments is governed in the Directive by Article 58, 60 and 61. First, under Directive Article 58, unless the payment service provider failed to make disclosures required under Title III, the payment service user is entitled to obtain rectification from his service provider, only if the user notifies the provider “without undue delay on becoming aware of any unauthorised or incorrectly executed payment transactions giving rise to a claim⁸⁵ . . . and no later than 13 months after the debit date.” Under Directive Article 60, refund by the payer’s payment service provider to the payer is to be made immediately, for the amount of the unauthorized payment transaction. “Further financial compensation may be determined in accordance with the law applicable to the contract concluded between the payer and his payment service provider.”⁸⁶ Presumably, such loss will also be for wrongful dishonour for items that lacked cover because of the debit for the unauthorized payment.

Second, Directive Article 61 provides for the liability of the payer for unauthorized payment transactions. However, under Directive Article 51(1), parties can contract out of Article 61 “where the payment service user is not a consumer.” Purported payer’s exposure under Article 61 varies. The starting point, under Article 61(1), is that “the payer⁸⁷ shall bear the losses relating to any unauthorised payment transactions, up to a maximum of EUR 150, resulting from the use of a lost or stolen payment instrument or, if the payer has failed to keep the personalised security features safe, from misappropriation of a payment instrument.” It is noteworthy that this limited liability runs irrespective of fault and irrespective of lack of knowledge of the loss, theft or misappropriation. While under Directive Article 56(1)(b) the payment service user is to advise the payment service provider “without undue delay on becoming aware of loss, theft or misappropriation of the payment instrument or of its unauthorised use,” exposure to unauthorized

83. See GEVA, *supra* note 4, § 2.05[4] (discussing U.C.C. Section 4A-203).

84. Such as lack of credibility or some support to user’s version.

85. The notification requirement in Directive Article 58 applies also to a claim for an incorrectly executed payment transaction governed by Directive Article 75.

86. Directive Article 53(1)(b), regarding low-value payments, provides that Directive Article 60 does not apply “if the payment instrument is used anonymously or the payment service provider is not in a position for other reasons which are intrinsic to the payment instrument to prove that a payment transaction was authorised.”

87. The reference in Article 61(1) to the “payer” should have been to the “purported payer” because he did not “allow . . . a payment order from [the] payment account” nor gave a payment order, which is required to meet the definition for a “payer” under Directive Article 4(7).

payment transaction losses begins to run irrespective of whether the purported payer was in a position to give the required notice.

Under Directive Article 61(2), a payer's liability is unlimited when the payer incurred losses "by acting fraudulently or by failing to fulfil one or more of his obligations under Directive Article 56 with intent or gross negligence." For their part, obligations under Directive Article 56 refer to "the terms governing the issue and use of the payment instrument" as well as the duty to notify of a known incident of loss, theft or misappropriation. They also specifically cover the obligation to "take all reasonable steps to keep [the payment instrument's] personalised security features safe." However, not any breach of such term results in an unlimited liability; rather, per the language of Directive Article 61(2), the failure to fulfil an obligation under Directive Article 56 must have been made "with intent or gross negligence."⁸⁸ Arguably, unlimited liability for gross negligence may be fastened in cases that would have otherwise been treated as those of apparent authority as, for example, where the payment service user delivers the payment instrument to someone he considers to be a trusted agent who nevertheless betrays him.

And yet, the amount of exposure may vary where notice is given to the payment service provider. Thus, under Directive Article 61(4), having not acted fraudulently, the payer "shall not bear any financial consequences resulting from the use of the lost, stolen or misappropriated payment instrument after notification in accordance with Directive Article 56(1)(b)." The latter provision requires the payment service user to notify the payment service provider "without undue delay on becoming aware of loss, theft or misappropriation of the payment instrument or of its unauthorised use." Similarly, under Directive Article 61(5), the payer who has not acted fraudulently and who was not furnished with "appropriate means for the notification" by the payment service provider, is excused altogether from all financial consequences resulting from the unauthorized use of the payment instrument.⁸⁹

In the final analysis, in the absence of fraud, or intentional or grossly negligent failure to fulfil the obligations under Directive Article

88. Under Directive Article 53(1)(b), limitations to liability under Directive Article 61(1) and (2)—that is, limitations to both to the ceiling and the conditions of incurring liability (namely, fraud or gross negligence)—do not apply "if the payment instrument is used anonymously or the payment service provider is not in a position for other reasons which are intrinsic to the payment instrument to prove that a payment transaction was authorised." Purported payer's liability is then unlimited.

89. Per Directive Article 53(1)(a), these two exemptions do not apply in the case of a low-value payment instrument that "does not allow its blocking or prevention of its further use."

56, the purported payer incurs liability up to a ceiling of EUR 150. This liability exists even where he is faultless and unaware of the circumstances requiring him to give notice under Directive Article 56(1)(b). At the same time, except where he acted fraudulently, he incurs no further liability for losses occurring after notification. Moreover, regardless of lack of knowledge of the loss, theft or misappropriation, in the absence of notification and unless it is excused, liability is unlimited where the purported payer has either acted fraudulently or failed to fulfil an obligation under Directive Article 56 with either intent or gross negligence.

It seems that the proper interpretation of Directive Article 61(1) and (4) is that unlimited liability for losses occurring after notification hinges only on fraud by the purported payer and not on his intentional or gross negligent breach. In addition, arguably, undue delay in notifying the service provider of the loss, theft or misappropriation may constitute gross negligence on the part of the purported payer to fulfil the notification obligation under Directive Article 56(1)(b), which under Directive Article 61(2) exposes him to unlimited liability prior to the notification.⁹⁰ Finally as for the interpretation of Directive Article 61, the EUR 150 liability ceiling applies only in the absence of fraud or intentional or gross negligent breach; thus, for example, gross negligence in keeping of the personalised security feature safe, in breach of the specific obligation under Directive Article 56(2), arguably exposes the purported payer to unlimited liability under Directive Article 61(2), notwithstanding the fact that the mere failure to keep personalized security features safe, unaccompanied by gross negligence, is a case stated in Directive Article 61(1) to trigger the EUR 150 ceiling to liability.

Under Article 61(3), Member States may reduce both the EUR 150 ceiling and the unlimited liability by “taking into account, in particular, the nature of the personalised security features of the payment instrument and the circumstances under which it was lost, stolen or misappropriated.”

Directive Articles 62 and 63 deal with a limited right for refund in connection with authorized debit transfers.⁹¹ Specifically, Article 62 provides for a refund to which a payer is entitled from his payment service provider for an authorized completed debit transfer; that is, a

90. *Cf. Minskoff v. American Express Travel Related Services*, 98 F.3d 703 (2d Cir. 1996) (holding that receipt of a statement reasonably putting the customer on notice that one more fraudulent charges has been made precludes an argument based on lack of knowledge of these charges).

91. Per Directive Article 51(1), where the service user is not a consumer the parties may agree that Directive Articles 62 and 63 “shall not apply in whole or in part.”

“payment transaction initiated by or through the payee which has already been executed.” Such a right is available to the payer where the authorization did not specify an exact amount for the payment transaction and its amount “exceeded the amount the payer could reasonably have expected taking into account his previous spending pattern, the conditions in his framework contract and relevant circumstances of the case.”⁹² Such conditions may be waived in a framework contract⁹³ governing a direct debit. At the same time, a framework contract may provide that “the payer has no right to a refund where he has given his consent to execute the payment transaction directly to his payment service provider and, where applicable, information on the future payment transaction was provided or made available in an agreed manner to the payer for at least four weeks before the due date. . . .” Per Article 63, a request for a refund governed by Article 62 is to be made within eight weeks of the debit to the payer’s account. The payer’s service provider is to comply or respond within ten days.⁹⁴

In the U.S., under U.C.C. Article 4A, to bind a sender, the payment order must be an authorized payment order for which the sender is bound under the law of agency. Alternatively, unless it proves that the payment order was not caused directly or indirectly by a person under its control, a customer is bound by any payment order whose authenticity was verified by the bank according to a commercially reasonable security procedure agreed upon between the customer and the bank.⁹⁵ Under Section 4A-201, “[a] security procedure may require the use of algorithms or other codes, identifying words or numbers, encryption, callback procedures, or similar security devices. Comparison of a signature of a payment order with an authorized specimen signature of the customer is not by itself a security procedure.”

Under U.C.C. Section 4A-204, “a receiving bank accept[ing] a payment order issued in the name of its customer” which is neither authorized nor effectively verified is required to refund any payment

92. However, under Directive Article 62(2), “the payer may not rely on currency exchange reasons if the reference exchange rate agreed with his payment service provider . . . was applied.”

93. A “framework contract” is defined in Directive Article 4(12) to mean “a payment service contract which governs the future execution of individual and successive payment transactions and which may contain the obligation and conditions for setting up a payment account.”

94. According to Directive Article 63(2), a negative response must include a “justification for refusing the refund” accompanied by an indication of “the bodies to which the payer may refer the matter in accordance with Articles 80 to 83 if he does not accept the justification provided.”

95. See U.C.C. §§ 4A-201 to 203 (2008).

made by the customer for that payment order. The receiving bank is further liable to pay interest for the refundable amount. However, liability to pay interest is excused upon the customer's failure to exercise ordinary care to determine lack of authority and notify the bank with respect to it "within a reasonable time not exceeding 90 days after the date the customer received notification from the bank." Furthermore, under U.C.C. Section 4A-505, having failed to challenge a debit for an unauthorized or unverified payment order posted to the customer's account within one year of receipt of notification from the bank, the customer is precluded altogether from contesting it.

A different regime altogether applies in the U.S. for a consumer's liability in connection with unauthorized credit card payments and electronic funds transfers.⁹⁶ Thus, the liability of a credit card holder for the unauthorized use of the card is governed by § 1643 of the federal CCCDA⁹⁷ and § 226.12 of Regulation Z.⁹⁸ Consumer liability for unauthorized electronic fund transfers is governed by the § 909 of the federal EFTA⁹⁹ and Regulation E.¹⁰⁰ In both cases, that of the unauthorized credit card payment and the unauthorized electronic fund transfer, there is a ceiling for the consumer's exposure for unauthorized payments. In addition, the consumer's fault is irrelevant, other than in connection with the failure to promptly advise. The two schemes are however not identical.

Under Reg. Z § 226.12(b)(1), unless greater protection to the cardholder is afforded either by other applicable law or an agreement,¹⁰¹ "[t]he liability of a cardholder for unauthorized use of a credit card shall not exceed the lesser of \$50 or the amount of money, property, labor, or services obtained by the unauthorized use before notification to the card issuer." This limit was interpreted to be set in conjunction with a "series of unauthorized uses",¹⁰² such uses are not necessarily related.¹⁰³ No increased liability is provided for the failure to promptly advise the financial institution; in fact, the incentive for prompt notification is lost after \$50 unauthorized use loss has been incurred.¹⁰⁴ Notification to the

96. See Benjamin Geva, *Consumer Liability in Unauthorized Electronic Funds Transfers*, 38 CAN. BUS. L.J. 207 (2003).

97. See 15 U.S.C. § 1643 (2006).

98. See 12 C.F.R. § 226 (2008).

99. See 15 U.S.C. § 1693(g) (2006).

100. See 12 C.F.R. § 205 (2008).

101. *Id.* § 228.12(b)(4).

102. Regulation Z Official Staff Interpretations to § 226.12, *supra* note 33, ¶ 12(b)(2)(iii)(2).

103. Compare with the requirements of Reg. E, discussed below, under which the limit applies to a series of related unauthorized transfers.

104. Except that settling a balance on a periodic statement containing unauthorized transfers, can be viewed as the adoption of the unauthorized transfers, for which the

card issuer of the loss or theft may be given, at the option of the person giving it, “in person, by telephone, or in writing.”¹⁰⁵ For the purpose of this provision, “cardholder” means any person, not necessarily natural, to whom a credit card is issued, for any purpose, including business, commercial, or agricultural use, “or a person who has agreed with the card issuer to pay obligations . . . arising from the issuance of [such] a credit card to another . . . person.”¹⁰⁶ “Unauthorized use” is defined as “the use of a credit card by a person, other than the cardholder, who does not have actual, implied, or apparent authority for such use, and from which the cardholder receives no benefit.”¹⁰⁷

Three conditions are stated¹⁰⁸ to apply in order to fasten liability on a cardholder for the unauthorized use of the credit card. First, the card must be an accepted credit card, that is, either a “credit card that the cardholder has requested or applied for and received, or has signed, used, or authorized another person to use or obtain credit,” or a credit card “issued as a renewal or substitute in accordance with this paragraph.”¹⁰⁹ Second, “the card issuer has provided adequate notice¹¹⁰ of the cardholder’s maximum potential liability and of means by which the card issuer may be notified of loss or theft of the card.” Third, the card issuer must have provided “a means to identify the cardholder on the account or the authorized user of the card.” Where any of these conditions is not satisfied, the cardholder is not responsible for any unauthorized use of the card.

The approach for regulating unauthorized consumer electronic fund transfers under Reg. E is entirely different from that of UCC Article 4A for unauthorized business funds transfers. As well, the approach taken is not identical to that under Reg. Z for the unauthorized use of a credit card. The point of departure for both Regulations is quite similar; yet, the scheme of Reg. E appears to be an improvement on that of Reg. Z. Yet, no effort has been made to harmonize the two Regulations;

customer becomes liable under agency law, specifically when payment is made with knowledge of such unauthorized transfers.

105. Regulation Z, 12 C.F.R. § 226.12(b)(3) (2008).

106. *Id.* § 226.2(a)(8); *see also id.* § 226.12(a); *id.* § 226.12(b)(5) (explaining that an issuer can contract out of the limited liability rule only where at least 10 cards are issued for the use of employees of an organization, provided liability of the employees remains governed by the provision).

107. *Id.* § 226.12(b)(1) n.22. This definition effectively reproduces of “unauthorized use” found in the CCCDA, 15 U.S.C. § 1602(o) (2006).

108. 12 C.F.R. § 226.12(b)(2).

109. *Id.* § 226.12(a)(2) n. 21; *see also* CCCDA, 15 U.S.C. § 1602(l) (2006).

110. “Adequate notice” is defined as “a printed notice to a cardholder that sets forth clearly the pertinent facts so that the cardholder may reasonable be expected to have noticed it and understood its meaning. The notice may be given by any means reasonably assuring receipt by the cardholder.” § 226.12(b)(2)(ii) n.23.

particularly in connection with electronic authentication, the distinction does not appear to be justified.

The underlying principle of Reg. E is that a consumer is liable for authorized transfers, as well as, upon the failure to promptly advise the bank, for a limited amount of unauthorized transfers, up to the time of notification to the bank. Where such a notification is not given by a designated deadline, the customer is liable for the entire amount after the expiry of the notification period. The consumer's negligence contributing to an unauthorized transaction, other than in failing to give a timely notification, is not a factor in determining the consumer's exposure.

Reg. E §205.2(m) defines "[u]nauthorized electronic fund transfer" to mean:

an electronic fund transfer from a consumer's account initiated by a person other than the consumer¹¹¹ without actual authority to initiate the transfer and from which the consumer receives no benefit. The term does not include an electronic fund transfer initiated:

(1) by a person who was furnished the access device¹¹² to the consumer's account by the consumer,¹¹³ unless the consumer has notified the financial institution that transfers by that person are no longer authorized;

(2) with fraudulent intent by the consumer or any person acting in concert with the consumer; or

(3) by the financial institution or its employee.

111. This includes an erroneous or fraudulent transfer initiated by an employee of the financial institution as well as by the consumer himself or herself where "the consumer has been induced by force to initiate the transfer." See Regulation E Official Staff Interpretations on § 205.2(m), 12 C.F.R. § 205.17, 146 ¶¶ (1), (4) (2002).

112. Defined in Reg. E § 205.2(a)(1) to mean "a card, code, or other means of access to a consumer's account, or any combination thereof, that may be used by the consumer to initiate electronic fund transfer."

113. In furnishing the access device, the consumer must have acted voluntarily. Accordingly, where control of the access device is surrendered by the consumer as a result of robbery or fraud, the fund transfer initiated by the robber or the defrauding person is "unauthorized." In contrast, the exception applies so that the transfer is not "unauthorized" where "a consumer furnishes an access device and grants authority to make transfers to a person (such as a family member or co-worker) who exceeds the authority given." See 12 C.F.R. § 205.17, 146. Prior to this interpretation by the Federal Reserve Board, there was some judicial disagreement on the first point (that of *voluntarily* furnishing the access device). See *e.g.*, *Feldman v. Citibank*, 443 N.Y.S.2d 43 (N.Y. Civ. Ct. 1981); *Ognibene v. Citibank*, 446 N.Y.S.2d 845, 847 (N.Y. Civ. Ct. 1981); *State v. Citibank*, 537 F. Supp. 1192, 1194 (S.D.N.Y. 1982). In effect, the latter point may be regarded as dealing with apparent authority.

Transfers thus excluded are evidently deemed authorized to which the consumer is fully responsible.

In connection with debit card electronic authentication, it was held that “[i]n an action involving a consumer’s liability for an electronic fund transfer . . . the burden of going forward to show an ‘unauthorized’ transfer . . . is on the consumer.” However, “[t]o establish full liability on the part of the consumer, the bank must prove that the transfer was authorized.”¹¹⁴ These two statements can be reconciled as follows: to succeed in its action, the bank must initially make a prima facie case that the transfer was authorized. To that end, it is adequate for the bank to prove that the transfer was initiated by means of the access device it had issued to the consumer. At that point, the burden of proof shifts to the consumer alleging an unauthorized transfer. Proof of loss or theft of the access device, put forward by the consumer, is adequate to meet this burden. Obviously, notice of loss or theft given by the consumer to the bank is no more than prima facie evidence of loss or theft.

Ultimately, however, where loss or theft of the access device is not claimed, in determining the question of authorized or unauthorized transfer, the court may be forced to choose between the consumer’s testimony and the bank’s computer printout, often backed by some evidence as to the reliability of its security procedure. A review of case law reveals that a credible witness, usually where his or her testimony is corroborated, typically by some system malfunction, has consistently overcome the machine.¹¹⁵ Nevertheless, witness credibility may differ from one case to another. Furthermore, relevant case law is from the first half of the 1980s; it is quite possible that with time, confidence in the reliability of computer systems increases, so that greater weight may be given to evidence generated by them.

In the final analysis, an unauthorized transfer may be caused by computer fraud or even an internal fraud at the financial institution. Both causes do not necessarily manifest machine malfunction and are outside the ability of the consumer to prove. To that end, existing case law, as described above, is inadequate.

The extent of consumer liability for “an unauthorized electronic fund transfer or a series of related unauthorized transfers” is governed by Reg. E §205.6. To be entitled to the amounts specified in the provision, the bank must have provided the consumer with certain disclosures as to the extent of the consumer’s liability, the telephone number and address for providing notices to the bank, and the bank’s business days. As well,

114. *Ognibene*, 446 N.Y.S.2d at 847.

115. *See e.g.*, *Judd v. Citibank*, 435 N.Y.S.2d 210 (N.Y.C. Civ. Ct. 1980); *Feldman*, 443 N.Y.S.2d 43; *Porter v. Citibank*, 472 N.Y.S.2d 582 (N.Y. Civ. Ct. 1984).

“[i]f the unauthorized transfer involved an access device, it must be an accepted access device and the financial institution must have provided a means to identify the consumer to whom it was issued.”¹¹⁶

Thus, when these conditions are met, under the aforesaid Reg. E § 205.6, and subject to specified ceilings, liability is limited to unauthorized transfers occurring before the consumer advises the bank either of the loss or theft of the access device or of an unauthorized transfer that appears on a periodic statement. Where the consumer is not aware of the loss or theft of the access device, for unauthorized transactions occurring up to 60 days after the transmittal of a periodic statement containing an unauthorized transfer,¹¹⁷ the consumer is not liable. However, for such transfers, the consumer is liable up to a \$50 ceiling where he or she learns of the loss or theft of the access device and advises the bank of it within two business days. The \$50 ceiling does not apply where the consumer learns before the expiration of that 60-day period of the loss or theft of the access device but fails to advise the bank of the loss or theft within two business days. In such a case, the \$50 ceiling applies only until the close of two business days after learning of the loss or theft, and the overall liability for the period ending at the close of the 60-day period will not exceed \$500. Liability beyond the 60-day period is unlimited, until notice is given to the bank. To be entitled to the \$500 as well as the unlimited ceilings, the bank must establish that the consumer's timely notification would have prevented the loss.

Under Reg. E § 205.6(4), time periods for notification may be extended “to a reasonable period” where the consumer delayed notifying the bank “due to extenuating circumstances.” However, in *Kruser v. Bank of America NT&SA*,¹¹⁸ this provision did not assist a consumer who admitted that “she received . . . bank statements during her recuperation.”¹¹⁹ In one such a statement, she failed to notice and advise the bank of a \$20 unauthorized ATM withdrawal. Almost a year later, the consumer received statements containing close to \$10,000 in unauthorized ATM withdrawals. The consumer then promptly advised

116. See 12 C.F.R. § 205.6(a). An “accepted access device” is generally defined (in section 205.2(a)(2)) as an access device requested and received or used by the consumer. In order to be entitled to any amount of unauthorized transfers, the bank must establish the existence of these conditions. See *Ognibene*, 446 N.Y.S.2d at 847.

117. For an account to or from which electronic fund transfers can be made, a financial institution is required, under Reg. E § 205.9(b), to send a periodic statement for each monthly cycle in which an electronic fund transfer has occurred. Such requirement is not dispensed with for passbook accounts updated upon presentation, except where the accounts may be accessed “only by preauthorized transfers to the account.” See 12 C.F.R. § 205.9(c)(1)(i).

118. 281 Cal. Rptr. 463 (Cal. Ct. App. 1991).

119. *Id.* at 467.

the bank of all unauthorized withdrawals, including the one that was almost a year old. In the Court's view, the consumer failed to show the required "extenuating circumstances." Having delayed the notice for the first \$20 unauthorized transaction, the consumer was thus held liable for the entire amount of the unauthorized transfers.

V. EXECUTION OF PAYMENT TRANSACTIONS: OVERVIEW

Directive Articles 64-78 deal with the execution of payment transactions. "Execution" is not defined in the Directive. From the heading to the chapter containing these provisions, referring to the execution of the payment transaction, as well from the context elsewhere in the Directive,¹²⁰ the term denotes the performance of the entire payment transaction, rather than carrying out the instruction contained in the "payment order," as it is under U.C.C. Article 4A.¹²¹ However, elsewhere in the Directive, reference is made to the "execution" of a "payment order";¹²² hence, the use of the term is inconsistent.

Chapter 3 is divided into three Sections. Section 1, consisting of Articles 64-67, deals with payment orders and amount transferred. Section 2, consisting of Articles 68-73, deals with execution time and value date. Section 3, consisting of Articles 74-78, deals with liability.

VI. EXECUTION OF PAYMENT TRANSACTIONS: PAYMENT ORDERS AND AMOUNTS TRANSFERRED

Section 1, consisting of Articles 64-67, deals with payment orders and amount transferred. It deals with the receipt of payment orders, refusal of payment orders, the irrevocability of a payment order, and the relationship between amounts sent and received.

Directive Article 64(1) identifies "the point in time of receipt" with "the time when the payment order . . . is received by the payer's payment service provider." It goes on to state that if the point of time of receipt is not on a business day for the payer's payment service provider, receipt is deemed to occur on the following business day. As well, and on this point in the footsteps of U.C.C. Section 4A-106, the payer's service provider may establish a cut-off time, though only near the end of the business day, beyond which receipt will be deemed to occur the following business day.

Directive Article 64(1) applies to a payment order transmitted to the payer's payment service provider (i) directly by the payer, (ii) indirectly

120. For example, *see* the definition of "payment order" *infra*.

121. U.C.C. § 4A-301(a) (2008).

122. For example, Directive Article 65 deals with the refusal of payment orders and discussed further below. *See also* Directive art. 64(2).

by the payee through the payee's payment service provider, or (iii) indirectly through the payee, whether or not via the payee's payment service provider. The first two instances are respectively those of a credit and debit transfer. The third instance is that of a payment order issued by the payer to the payee who then transmits it either to his own service provider, in which case it results in a debit transfer, or to the payer's payment service provider, in which case it results in a credit transfer.

Under U.C.C. Article 4A, each payment order is a request by the sender to the receiving bank which can be accepted or rejected. Notice of rejection is required to avoid liability for interest, and may preclude acceptance by a beneficiary's bank holding adequate funds as cover. Otherwise, there is no acceptance by inaction or mere passage of time; an unaccepted payment order expires after five days.¹²³ Suspension of payment by a receiving bank is tantamount to rejection by operation of law. In general, the occurrence of either acceptance or rejection is irreversible.¹²⁴

U.C.C. Article 4A is quite specific about the manner and contractual effect of acceptance, as well as the law applicable to an accepted contract. First, as its manner, acceptance of a payment order by the beneficiary's bank is accomplished either by paying (or advising) the beneficiary, or where the beneficiary has an account at the beneficiary's bank, also by obtaining cover for such a payment. Acceptance by a receiving bank other than the beneficiary's bank is by the *execution* of the payment order, that is, by issuing a corresponding payment order, intended to carry out the payment order received by the bank.¹²⁵ The executing bank must issue a payment order that strictly conforms to that received by the bank with respect to the amount, the ultimate destination of the funds, and the identity of any specifically designated intermediary bank. Otherwise, the executing bank's duties as to speed, the means of communication, the use of a funds-transfer system, and the selection of an intermediary bank where none is designated by the sender, are to be carried out with reasonable care and skill.¹²⁶ Nothing short of execution serves as acceptance by a receiving bank other than that of the beneficiary.

Second, as to its legal implications, acceptance of a payment order by a receiving bank obliges the sender to pay the amount of the order.¹²⁷

123. U.C.C. § 4A-211(d).

124. Rejection of payment order is governed by U.C.C. Section 4A-210.

125. *Id.* §§ 4A-209, 4A-301.

126. *Id.* § 4A-302.

127. *Id.* § 4A-402.

The sender's payment is carried out usually by means¹²⁸ of: (i) an interbank final settlement over a funds-transfer system; (ii) a credit by the sending bank to the receiving bank's account, in which case payment occurs at the midnight of the day on which the credit is withdrawable and the receiving bank learns of this fact, unless credit was withdrawn earlier, in which case payment occurred at the time of withdrawal, or (iii) a debit by the receiving bank to the sender's account, provided funds are actually available in the account. Where the receiving bank is that of the beneficiary, payment by means of a debit to the sender's account containing adequate cover, in fact, even by means of the availability of cover for a debit in such an account, will constitute acceptance only at the opening of the next funds-transfer system day, provided the payment order was not rejected until one hour thereafter.¹²⁹

As well, the acceptance by the beneficiary's bank of a payment order for the benefit of the originator's payment order denotes the completion of the funds transfer.¹³⁰ Acceptance by the beneficiary's bank further constitutes payment by the originator to the beneficiary, namely a discharge of the originator's obligation on the underlying transaction, that is, of the debt paid by means of the funds transfer.¹³¹ It fastens on the beneficiary's bank an obligation to pay the beneficiary,¹³² in principle, payment by the beneficiary's bank to the beneficiary is "final" and cannot be made provisional or conditional on the receipt of funds from the sender.¹³³

Finally as to contractual implications, acceptance by a receiving bank other than the beneficiary's bank inures to the benefit of the sender; acceptance by the beneficiary's bank inures to the benefit of the beneficiary.¹³⁴ Unless displaced by a bilateral agreement or a funds-transfer system rule,¹³⁵ the law applicable to each payment order is that of the jurisdiction in which the receiving bank is located. Similarly, the law of the jurisdiction in which the beneficiary's bank branch is located governs the relationship between the beneficiary's bank and the beneficiary, as well as the discharge of the originator's debt to the beneficiary.¹³⁶

128. *Id.* § 4A-403.

129. U.C.C. § 4A-209(b)(3).

130. *Id.* § 4A-104(a).

131. *Id.* § 4A-406.

132. *Id.* § 4A-404.

133. *Id.* § 4A-405(c).

134. *See generally* U.C.C. § 4A-212 (and Official Comment); *id.* § 4A-209 Official Comment 1.

135. As provided in U.C.C. Sections 4A-501 and 507.

136. Choice of law is governed by U.C.C. Section 4A-507.

No conflict of law rules are provided for in the Directive. This however is not an accident; as indicated, per Article 2(1), “with the exception of Article 73, Title . . . IV shall apply only where both the payer’s payment service provider and the payee’s payment service provider are . . . located in the Community.” Furthermore, under Article 3(2), Title IV “shall apply only to payment services made in euro or the currency of a Member State outside the euro area.” This unduly restricts the scope of the Directive; practically, this eliminates its application to both inbound and outbound Community payments and, unfortunately, renders academic the topic of conflicts of law in international (other than inter-Community) or foreign currency payments.

Nor does the Directive provide for acceptance. At the same time, refusal of payment orders is governed by Directive Article 65. Article 65(1) fastens on a payment service provider who refuses to execute a payment order a duty to advise the user of the refusal and if possible, the reason for it and the procedure for correction. Per the framework contract, the user may be charged for the notification of an objectively justified refusal.¹³⁷ On its part, the right to refuse is not entirely discretionary to the payment service provider. According to Article 65(2), and “irrespective of whether the payment order is initiated by a payer or through the payee,” namely, both in a credit and debit transfer,¹³⁸ “where all the conditions set out in the payer’s framework contract are met, the payer’s payment service provider shall not refuse to execute an authorized payment order.”

The position under U.C.C. Article 4A of an originator’s bank that rejects a payment order is more favorable. Thus, under U.C.C. Section 4A-212, “[i]f a receiving bank fails to accept a payment order that it is obliged by express agreement to accept, the bank is liable for breach of the agreement to the extent provided in the agreement or in this Article [4A].” Otherwise, and “except as provided in this Article or by express agreement,” a receiving bank “does not . . . have any duty to accept a payment order or, before acceptance, to take any action or refrain from taking action, with respect to a payment order. . . .” Thus, although

137. This is in fact enumerated in Directive Article 52(1) as one of the “information obligations” for which the payment service provider may charge the payment service user. Under Article 65(1), notification is to be made “in an agreed manner and at the earliest opportunity. . . .” In addition, the duty under Directive Article 65(1) is to be complied with “unless prohibited by other relevant Community or national legislation” *Id.*

138. As well, in the absence of a prohibition by Community or national legislation. *Id.*

under the Directive liability is based on contract,¹³⁹ the scope of liability is stated to be narrower under the U.C.C. Stated otherwise, unlike U.C.C. Section 4A-212, Directive Article 65 does not restrict liability by reference to its own provisions or the express agreement of the parties. In fact, liability provided under Article 4A is only for the failure to advise of rejection of a payment order which is only for lost interest.¹⁴⁰

Directive Article 66(1) precludes the revocation of a payment order “once it has been received by the payer’s payment service provider.” For credit transfers, this is a noteworthy departure from U.C.C. Article 4A under which revocation is permitted until acceptance by the originator’s bank.¹⁴¹ This will also reverse the current position under German law.¹⁴² Thereunder, as against the originator’s bank, revocation is available to the originator as long as the originator’s bank has not acted on the payment order. But even if the originator’s bank acted on the payment order, it is obliged to transmit the originator’s revocation order onward; unlike under the U.C.C.,¹⁴³ the bank has no discretion in the matter. Ultimately, the revocation is effective if it reaches the beneficiary’s bank prior to the latter crediting the beneficiary’s account.

In any event, under the Directive, the framework governing the ability of parties to provide for revocability is unclear. Thus, under Directive Article 51(1), irrevocability may be contracted out only “[w]here the payment service user is not a consumer.” At the same time, under Directive Article 66(5), and irrespective as to whether the payment transaction is a consumer or business transaction, revocability beyond points of time specified in Directive Article 66 may be a matter of an agreement between the payment service user and his payment service

139. Unlike U.C.C. Section 4A-212, the Directive lacks the emphasis on “express” agreement; so even on this point it is less favorable to the payor’s payment service provider (that is, the originator’s bank).

140. See U.C.C. § 4A-210(b) (which is specifically referred to (together with U.C.C. Section 4A-209(b)(3) that does not apply to the originator’s bank) in the Official Comment to U.C.C. Section 4A-212).

141. Until acceptance, injunction and creditor process by the originator’s creditors can also prevent the originator’s bank from initiating a funds transfer. Likewise, an injunction and creditor process by the beneficiary’s creditors can prevent the beneficiary from receiving the benefit of payment once the funds transfer has been completed. A funds transfer cannot, however, be intercepted by third parties between acceptance by the originator’s bank and by the beneficiary’s bank. See U.C.C. §§ 4A-502, 4A-503.

142. For the position under German law, see, for example, BENJAMIN GEVA, *BANK COLLECTIONS AND PAYMENT TRANSACTIONS: COMPARATIVE STUDY OF LEGAL ASPECTS* 222 (2001).

143. See U.C.C. § 4A-211.

provider, for which the payment service provider may charge the payment service user if so agreed in their framework contract.¹⁴⁴

Aside from an agreement as above, for a payment transaction initiated by or through the payee, revocability is denied even prior to receipt under Directive Article 66(1). Thus, according to Directive Article 66(2), a payment order issued by the payer through the payee is irrevocable as soon as it is transmitted. A payment transaction initiated by the payee becomes irrevocable as soon as the payer's consent is given; that is, as early as upon the authorization given by the payer to the payee to initiate the debit transfer.

However, under Directive Article 66(4), revocability is available for payment orders instructing payment in the future, though "at the latest by the end of the business day preceding the agreed day." For "a direct debit"¹⁴⁵ and without prejudice to refund rights" the same rule is specifically provided in Directive Article 66(3).

Directive Article 67 deals with the amount of a payment transaction. Similar to U.C.C. Article 4A-302 (d),¹⁴⁶ the basic principle of Directive Article 67(1), is that the full amount instructed is to be transferred, so that no charges are to be deducted by the payer's as well as the payee's service provider and by any intermediary. Fees are to be charged to the account as such and are not to be deducted from the amount transferred. Thus, under Directive Article 67(2), an agreed charge may be debited separately to the payee's account by his payment service provider, rather than made as a deduction to the amount credited. Per Directive Article 67(3), it is up to the service provider of the party initiating the payment transaction to ensure that the payee receives the full amount of the payment transaction.

VII. EXECUTION OF PAYMENT TRANSACTIONS: EXECUTION TIME AND VALUE DATE

Section 2, consisting of Directive Articles 68-73, deals with execution time and value date. It covers three distinct concepts: execution, value dating, and funds availability. Execution is used in the

144. This is in fact enumerated in Directive Article 52(1) as one of the "corrective and preventive measures" for which the payment service provider may charge the payment service user.

145. That is, per Directive Article 4(28), a debit transfer (i.e., "a payment transaction . . . initiated by the payee on the basis of the payer's consent") carried out as part of "a payment service," namely, a "business activity listed in the Annex" (Directive Article 4(3)). This is, presumably, as distinguished from an isolated debit transfer.

146. U.C.C. Section 4A-302(d) precludes the receiving bank, "[u]nless instructed by the sender," to obtain or instruct a subsequent receiving bank to obtain charges and expenses by deducting them from the sender's payment order. See also U.C.C. § 4A-404(c).

context of the completion of the payment transaction. Such completion is addressed by reference either to the receipt of funds by the payee's payment service provider in the form of credit to its account, or to crediting the payee's account by its payment service provider. In this context, it is not clear why receipt of funds by the payee's service provider is necessarily limited to the situation where funds are so received by means of credit posted to the account of the payee's payment service provider. Certainly funds can be received by other ways, for example, debit to the account of the payer's payment service provider.¹⁴⁷

"Value date" is defined in Directive Article 4(17) to be "a reference time used by a payment service provider for the calculation of interest on the funds debited or credited to a payment account." "Funds Availability" is undefined; it must be taken to refer to the unconditional availability to the payee's unrestricted use of the amount of the payment transaction. In theory, each of such events, namely, receipt by having the amount credited to an account, eligibility for earning interest on the amount,¹⁴⁸ and having the use of it as it is cash in the payee's pocket, are distinct and separate and hence they do not necessarily happen simultaneously.¹⁴⁹

Under Directive Article 69(1), the payer's payment service provider is required to ensure that after "receipt" of a payment order,¹⁵⁰ the amount of the payment transaction is credited "to the payee's payment service provider's account," namely to the account of the payment service provider, "at the latest by the end of the next business day." Such an account need not necessarily be held by the payer's payment service provider; rather, it could be held by a central counterparty such as a central bank. Until January 1, 2012 a payer and his service provider may agree "on a period no longer than three business days." All such periods "may be extended by a further business day for paper-initiated payment transactions." According to Directive Article 72, for national (domestic) payment transactions, Member States may shorten all execution periods under the Section.

Directive Article 69(1) appears to apply to both debit and credit transfers. It does not provide a remedy to the payee against a breach by

147. See e.g., *id.* § 4A-403 (enumerating several methods of interbank payment *viz.*, through a funds transfer system, by crediting the receiving bank's account, by having the receiving bank debiting the sending bank account as well as netting and any other means).

148. Presumably, the actual earning of interest, as opposed to the eligibility to earn interest, may well depend on the type of account into which the amount in question is credited.

149. *But see* A/S Awilco v. Fulvia S.p.A. Di Navigazione (the "Chikuma"), [1981] Lloyd's Rep. 371 (H.L.) (effectively identifying all three points).

150. As defined in Directive Article 64.

the payer's payment service provider. Presumably, the theory is that in case of delay the payee is to sue the payer who can turn around and seek reimbursement from his payment service provider.

Indeed, the payee is accorded a right against his own payment service provider. However, this right is for the failure to value date the credit to the account and make it available once funds have been received by the payee's payment service provider. Receipt of funds is in the form of credit *actually made* to the account of the payee's payment service provider. The payee's right is by reference to the time credit is made, rather than the time credit *should have been made*, to the account of the payee's payment service provider. Thus under Directive Article 69(2), in conjunction with Directive Article 73(1), towards the payee, the payee's payment service provider is obligated to value date the credit to the payee's account "no later than the business day on which the amount . . . is credited to the payee's payment service provider's account." Directive Article 73(1) goes on to require the payee's payment service provider to ensure "that the amount of the payment transaction is at the payee's disposal immediately after that amount is credited to the payee's payment service provider's account." Under Directive Article 70, this time frame for funds availability by reference to the credit to the account of the payee's payment service provider equally applies where the payee does not have an account with the payment service provider. All this however, does not permit the payee any remedy for a delay in posting credit to the account of his payment service provider in contravention of Directive Article 69(1).

Being more general in its nature so as to accommodate an infinite number of banking linkages, U.C.C. Article 4A is in no position to time payment to the beneficiary by reference to the acceptance of the originator's payment order by the originator's bank. Rather, U.C.C. Article 4A times the obligation of the beneficiary's bank to pay the beneficiary to coincide with the day of acceptance by the beneficiary's bank.¹⁵¹ However, on this point, Article 4A is preempted by US federal law. The latter effectively provides that the beneficiary's bank must make funds available to the beneficiary no later than at the start of the next business day after the banking day of acceptance by means of receiving a sender's payment.¹⁵²

Directive Article 73, dealing with value date and funds availability, is not limited to an intra-Community payment. Rather, it is the sole provision in Title IV, which applies also when only one of the parties'

151. U.C.C. § 4A-404(a) (2008).

152. Availability of Funds and Collection of Checks (Regulation CC), 12 C.F.R. § 229.10(b)(1) (1988).

payment service provider, that is, either of the payer or that of the payee, is located in the Community.¹⁵³

VIII. EXECUTION OF PAYMENT TRANSACTIONS: LIABILITY

Section 3, consisting of Articles 74-78, addresses liability. The central provision as to liability is Directive Article 75, which contains rules allocating responsibility in cases of non-execution or defective execution.¹⁵⁴ Under Directive Article 51(1), “[w]here the payment service user is not a consumer, the parties may agree that Article . . . 75 shall not apply in whole or in part.”

Each of the rules set out in Directive Article 75 is stated to be “without prejudice to Directive Article 58, Directive Article 74(2) and (3), and Directive Article 78.”¹⁵⁵ Directive Article 58 provides for the payment service user’s right to obtain rectification from the payment service provider upon notifying to him “without undue delay on becoming aware of any unauthorised or incorrectly executed payment transactions.” Directive Article 78 exempts from liability a party successfully pleading “abnormal and unforeseeable circumstances beyond [his] control.”

Directive Article 74 protects a payment service provider that acted in reliance on an incorrect unique identifier. Under Directive Article 4(21), “unique identifier” is defined to mean “a combination of letters, numbers or symbols specified to the payment service user by the payment service provider and to be provided by the payment service user to identify unambiguously the other payment service user and/or his payment account for a payment transaction.” The simplest example is an account number. Directive Article 74(1) deals with a payment order executed in accordance with a unique identifier. It authorizes a payment service provider to rely on the unique identifier so that “the payment order shall be deemed to have been executed correctly with regard to the payee specified by the unique identifier.” It follows, and it is so provided in Directive Article 74(2), that the payment service provider that acted on the basis of the incorrect unique identifier provided by the user “shall not be liable . . . for non-execution or defective execution of the payment transaction.” Moreover, under Directive Article 74(3), where the user furnishes the payment service provider with information in addition to the unique identifier, “the payment service provider shall

153. Directive art. 2(1).

154. See generally R. Steenot, *Erroneous Execution of Payment Transactions According to the New Payment Services Directive*, 6 INT’L. J. TECH. TRANSFER AND COMMERCIALISATION 145 (2007).

155. Both in Directive Article 75(1) and (2).

be liable only for the execution of the payment transaction in accordance with the unique identifier provided by the payment service user.” Under Directive Article 74(2), having acted on the basis of the incorrect unique identifier, the payment service provider bears liability limited only to the making of “reasonable efforts to recover the funds involved in the payment transaction,” an effort for which the payment service provider may charge the payment service user if so agreed in the framework contract.¹⁵⁶

One effect of Directive Article 74, therefore, is that a payment service provider, which receives a payment order identifying a user by name and number, is free to act on the number alone. This goes, unnecessarily, further than U.C.C. Article 4A, that does not protect a payment service provider acting on the basis of the incorrect unique identifier with knowledge of the error or discrepancy.¹⁵⁷ In addition, under U.C.C. Section 4A-207(a), a payment order for a nonexistent or unidentifiable beneficiary cannot be accepted by the beneficiary’s bank.¹⁵⁸ There is no parallel to that provision in the Directive.

Thus, and as indicated, “without prejudice to Article 58, Article 74(2) and (3) and Article 78,” Directive Article 75(1) allocates liability for the non-execution or defective execution of a payment order initiated by the payer, as follows:

1. To begin with, the payer’s “payment service provider shall . . . be liable to the payer for correct execution of the payment transaction.” Effectively, this means that the payer’s payment service provider is discharged at the point of time in which “the payee’s payment service provider [timely] receive[s] the amount of the payment transaction. . . .”¹⁵⁹
2. At the point in which the payer’s payment service provider discharged its liability to the payer, “the payee’s payment service provider shall be liable to the payee for the correct execution of the payment transaction.”
3. The liability of the payee’s payment service provider to the payee is discharged by immediately placing the amount of

156. This is in fact enumerated in Directive Article 52(1) as one of the “corrective and preventive measures” for which the payment service provider may charge the payment service user.

157. See U.C.C. § 4A-207(b) (2008).

158. *Id.* § 4A-207(a).

159. As specified in Directive Article 69(1).

the payment transaction at the payee's disposal and, where applicable, crediting the corresponding amount to the payee's payment account.

4. A payer's payment service provider in breach with its obligation as in #1 above "shall without undue delay refund to the payer the amount of the non-executed or defective payment transaction and, where applicable, restore the debited payment amount to the state in which it would have been had the defective payment transaction not taken place."
5. Regardless of breach or defense to liability, in the case of non-execution of defective execution, and on request, the payer's payment service provider shall "make immediate efforts to trace the payment transaction and notify the payee of the outcome."

This overall scheme for credit transfers is in the footsteps of U.C.C. Article 4A in two major respects. First, the Directive fastens responsibility on the payee's payment service provider as of the time of receiving funds.¹⁶⁰ Second, it entitles the payer to a "money-back guarantee" from the payer's payment service provider in case funds do not reach the payee's payment service provider.¹⁶¹ At the same time, the Directive does not follow UCC Article 4A¹⁶² and does not specify that the arrival of funds to the payee's payment service provider marks the occurrence of payment by the payer to the payee. Rather, it leaves this to national laws.

Furthermore, the Directive does not take a position on who bears the responsibility for an erroneous payment order transmitted by the payer. By way of comparison, in principle, under U.C.C. Article 4A, the sender is responsible for the contents of its own payment order. The sender is also responsible for any discrepancy arising in the course of the transmittal of a payment order through a third party communication system (e.g. SWIFT). This means that such an intermediary system is

160. Thus under U.C.C. Section 4A-104(a), a credit transfer is completed by the "acceptance" of a payment order by the beneficiary's bank, which under Section 4A-209(b)(2) could be in the form of receipt of funds. Upon "acceptance" under Section 4A-404, the beneficiary's bank becomes obligated to pay to the beneficiary (as provided for in Section 4A-405).

161. See U.C.C. § 4A-402(c); *id.* § 4A-402 Official Comment 2. Nonetheless, under U.C.C. Article 4A an originator that selected a failed intermediary bank is responsible for the amount prepaid by the sender to that bank.

162. *Id.* § 4A-406 (in conjunction with Section 4A-209(b)(2)).

deemed to be an agent of the sender who is bound by the contents of the payment order as sent to the receiving bank by that communication system.¹⁶³ A sender can nevertheless shift the loss arising from the transmittal of an erroneous payment order (whether by itself or by a communication system acting as its agent) where the receiving bank has failed to comply with an *agreed-upon* security procedure which would have detected the error. Such a procedure may require a unique code for each payment order (so as to alert the receiving bank in the case of a duplicate payment), different codes for different levels of amounts, or identification of regular beneficiaries.¹⁶⁴ In order to benefit the sender, the security procedure, with which the receiving bank failed to comply, must have been agreed upon in advance.

Also troublesome on the coverage of the Directive is the lack of definition of defective execution and lack of adjustment of remedies, or the provision of a comprehensive scheme, in cases such as underpayment, overpayment, and payment to the wrong payee. In contrast, the provisions of U.C.C. Article 4A are more detailed. Thereunder, the sender is not responsible for the erroneous execution of its payment order by the issue of a nonconforming payment order by the receiving bank. A receiving bank executing the sender's order is required to issue a conforming payment order of its own.¹⁶⁵ Effectively, this means that the risk of an erroneous execution is placed on the erring receiving bank.¹⁶⁶ For example, in case of overpayment resulting from the issue by the erring bank of a payment order in a larger amount than indicated in the payment order it received, the erring bank is required to pay the (larger) amount of its own payment order but is entitled to be paid only the (smaller) amount of the payment order it received. Recovery of an erroneous payment, resulting either from an erroneous payment order¹⁶⁷ or from erroneous execution,¹⁶⁸ can be made, but only to the extent allowed under the law of mistake and restitution. Such recovery is available to the erring bank only directly from the actual beneficiary, irrespective whether the two are in privity.

163. *Id.* § 4A-206.

164. *Id.* § 4A-205.

165. *Id.* § 4A-302.

166. U.C.C. § 4A-303 (dealing with erroneous execution leading to overpayment, underpayment or payment to a wrong beneficiary). The receiving bank is effectively exonerated where its nonconformance is in the selection of an intermediary bank other than that selected by the sender but the funds transfer is nevertheless completed without exception (so that in fact no loss occurred).

167. *Id.* § 4A-205(a).

168. *Id.* § 4A-303.

Certainly, the money-back guarantee under Directive Article 75(1) provides for only one aspect in such cases. And yet, this is the only remedy specifically provided for in all cases of defective execution.

Indeed, the Directive deals with the amount of liability, though not in a comprehensive manner. Thus, according to Directive Article 75(3), “payment service providers shall be liable to their respective payment service users for any charges for which [the payment service providers] are responsible, and for any interest to which the payment service user is subject as a consequence of non-execution or defective execution of the payment transaction.” Under Directive Article 76, any additional financial compensation “may be determined in accordance with the law applicable to the contract concluded between the payment service user and his payment service provider.” As well, under Directive Article 77(1), where a liability of a payment service provider under Directive Article 75 is attributed to another payment service provider or to an intermediary, “that payment service provider or intermediary shall compensate the . . . payment service provider [liable under Directive Article 75] for any losses incurred or paid under Article 75.” Along the same lines as Directive Article 76, Directive Article 77(2) goes on to provide that “[f]urther financial compensation may be determined in accordance with agreements between payment service providers and/or intermediaries and the law applicable to the agreements concluded between them.”

That is, additional compensation to charges is not rejected altogether, but its determination is to be made by reference to the law applicable to the relevant contract. This is in departure from both EFTA and U.C.C. Article 4A. Thus, under EFTA §169h(a), in principle, a financial institution is liable to a consumer “for all damages proximately caused by . . . the financial institution’s failure to make an electronic fund transfer” as instructed and per the terms of the agreement with the consumer. Conversely, under U.C.C. Section 4A-305, the liability of a receiving bank for late or improper execution, as well as for nonexecution in breach of contract, is limited to interest losses, expenses,¹⁶⁹ and in some circumstances, reasonable attorney fees. There is no liability under U.C.C. Section 4A-305 for consequential loss, even foreseeable, including exchange losses, or loss of a profitable contract due to the failure to meet a contractual payment deadline,¹⁷⁰ except by

169. Expenses may not be recovered in the case of mere delay. *See id.* § 4A-305(a).

170. This is an obvious departure from the common law rule of *Evra v. Swiss Bank*, 673 F.2d 951 (7th Cir. 1982).

express written contract. In the view of the drafters,¹⁷¹ this rule is rationalized on the need “to effect payment at low cost and great speed.”

Excluding altogether liability for consequential loss under U.C.C. Section 4A-305 is not beyond criticism; and yet, the distinction between business and consumer transactions, as between U.C.C. Article 4A and EFTA in the U.S., can simply be rationalized on the extent of damages, as well as on the greater tightness of retail payment systems compared to the some looser interbank links in wholesale payments. Conversely, avoiding the issue altogether, as was done in the Directive, is certain not to contribute to harmonization.

Moreover, the combination between “money-back guarantee” under the Directive and additional damages that may be recovered under national law may not always be harmonious. Similar disharmony with national laws can be produced by the lack of a comprehensive treatment in the Directive with regard to the completion of the payment transaction and the discharge of the debt paid by it. Two examples taken from German law may be noted.¹⁷²

First, by way of background, historically, the “money-back guarantee” rule was introduced in the U.S. under U.C.C. Section 4A-402(c) to “compensate” the originator for the loss of the right to recover consequential losses from a bank for a bank’s default in carrying out its part in the credit transfer.¹⁷³ That is, instead of a right to recover unlimited amount of foreseeable losses caused by the fault of a bank,¹⁷⁴ the originator was accorded an automatic right to recover from the originator’s bank, loss caused at the originator’s or intermediary bank, regardless of any fault, though in principle,¹⁷⁵ only in the amount to be paid to the beneficiary.¹⁷⁶ Later, in the footsteps of this development, the German Credit Transfer Law purported to strike a balance. The law did not affect the originator’s right to obtain damages for consequential

171. U.C.C. § 4A-305 Official Comment 2.

172. Fundamentals of German law are set out in GEVA, *supra* note 142, at 218-26.

173. See U.C.C. § 4A- 212 (strict privity requirements and hence no vicarious liability); *id.* § 4A- 305 (in principle, no bank liability for consequential losses).

174. Prior to U.C.C. Article 4A, such a right was recognized in principle in *Evra*, *supra* note 171.

175. Exceptions cover incidental losses such as for interest and expenses; additional damages are recoverable only if so provided in an express written agreement. See U.C.C. § 4A-305.

176. See *id.* § 4A-305 Official Comment 2. Damages for the loss of a profitable contract such as in *Evra* are not recoverable then under the “money-back guarantee” rule. In *Evra* consequential damages were for \$2.1 million while the amount of the transfer, recoverable under a “money-back guarantee” rule, would have been a mere \$27,000.

losses,¹⁷⁷ but further provided for the vicarious liability of the originator's bank for consequential losses caused by the fault of an intermediary bank not selected by the originator.¹⁷⁸ At the same time, it provided the originator with only a limited "money-back guarantee" from the originator's bank,¹⁷⁹ which was an innovation under German law.¹⁸⁰

This balance, that is, entitlement to *unlimited* damages for consequential losses caused by fault, and yet only to a *limited* amount under a "non-fault" "money back-guarantee" rule, is to be upset by the Directive, which provides for a "money-back guarantee" for the entire amount and yet does not affect remedies for consequential losses. Certainly, an entitlement to both a "money-back guarantee" and damages for consequential losses are not logically mutually exclusive; however, the exposure of banks to losses incurred in the course of carrying out credit transfers are to be dealt with comprehensively and not be the result of patching together different pieces of legislation which are not necessarily harmonious.

Second, under the German civil code, while a monetary debt is discharged upon the arrival of the money to the debtor, in the absence of special circumstances, a debtor performs a monetary obligation by *sending* the money and not *delivering* it or *bringing* it to the creditor.¹⁸¹ Stated otherwise, while the debtor bears the risk of loss in transit, it is the creditor who bears the risk of delay. In connection with payment into a bank account by means of a credit transfer, the prevailing view is that money is sent when the debtor-originator issues to the originator's bank the payment order directing payment to the creditor-beneficiary; from then on, unless the underlying contract on which the debt is paid specifically requires arrival of funds by a designated date, risk of delay is borne by the creditor-beneficiary. This means the debtor-originator does not incur interest charges for late payment as long as the debtor-originator sends payment, namely, instructed the originator's bank, no later than the due date. At the same time, the risk of loss is borne by the

177. Pursuant to section 611 of the German Civil Code ("BGB"), the contract underlying the credit transfer is a contract for service, also governed by most provisions relating to the mandate (BGB § 675). See GEVA, *supra* note 142, at 218-19.

178. BGB § 676c (under the Credit Transfer Law 1999, Überwiesungsgesetz vom 21.7.1999, BGBI. I 1999, s. 1624 ff) (using an unofficial translation of the statute).

179. BGB § 676b.

180. The German Credit Transfer Law implemented Directive 97/5/EC on cross-border credit transfers, see *supra* notes 2 and 7, and expanded its scope to cover domestic credit transfers.

181. BGB §§ 269-270. See THE GERMAN CIVIL CODE (as am. to 1 Jan. 1975) (I.S. Forrester, S.L. Goren & H.M. Ilgen trans., 1975) (supp. trans. by S.L. Goren, 1981). A more recent, updated English translation is available online at http://www.gesetze-im-internet.de/englisch_bgb/index.html.

debtor-originator; no discharge occurs until funds are credited to the account of the creditor-beneficiary by the beneficiary's bank.¹⁸²

However, under Article 3(1)(c) of the EU Directive on combating late payment in commercial transactions¹⁸³ (hereafter "late payment Directive"), a creditor is entitled to interest for late payment "to the extent that (i) he has fulfilled his contractual and legal obligations; and (ii) he has not received the amount due on time." This is so unless "the debtor is not responsible for the delay." According to Article 3(1)(a) of that late payment Directive, "interest . . . shall become payable from the day following the date or the end of the period for payment fixed in the contract." Dealing with an obligation to make payment to be credited into an designated bank account by due date, the European Court of Justice interpreted this provision to entitle the creditor, whose account has not been credited by due date, to receive interest payment as of due date.¹⁸⁴

Prima facie, the case appears to have dealt with a contract that specifically required arrival of funds to the designated account by due date. Nevertheless, the case is regarded in Germany as upsetting altogether the traditional distinction between the risks of loss (borne by the debtor-originator) and delay (borne by the creditor-beneficiary), and fastening them both on the debtor-originator. But even so, a question arises as to whether, in light of the payment services Directive, the cutoff point both for the discharge of the underlying debt and avoidance of interest is the liability of the beneficiary's bank (payee's payment service provider) to the beneficiary (payee), rather than the actual crediting of the funds to the payee's account. Certainly, the beneficiary's bank becomes liable to the beneficiary already upon receiving funds for the payment order directing payment to the beneficiary. As indicated, Article 75(1) of the payment service Directive fastens responsibility on the payee's payment service provider as of the time it receives funds. As under U.C.C. Article 4A, this would have been a logical point for discharging the originator altogether, as if the originator delivered funds to an agent appointed by the beneficiary-creditor. Lack of a comprehensive treatment in the Directive as to the completion of the payment transaction and the discharge of the debt paid by it thus leads to an unfortunate uncertainty.

As for non-execution or defective execution of a payment order initiated by or through the payee, and as indicated, "without prejudice to

182. See GEVA, *supra* note 142, at 218-26.

183. Council Directive 2000/35/EC, 2000 O.J. (L 200) 35 (EC).

184. Case C-306/06, *Telecom v. Deutsche Telekom*, 2008 E.C.R. I-01051, available at <http://curia.europa.eu/content/juris/index.htm>.

Article 58, Article 74(2) and (3) and Article 78,” payment services Directive Article 75(2) allocates liability, as follows:

1. To begin with, the payee’s payment service provider “shall . . . be liable to the payee for correct transmission of the payment order to the payment service provider of the payer in accordance with Article 69(3),” that is, “within the time limits agreed between the payee and his payment service provider, enabling settlement, as far as direct debit is concerned, on the agreed due date.”
2. Upon becoming liable under #1, the payee’s payment service provider “shall immediately re-transmit the payment order in question to the payment service provider of the payer.” In addition it “shall . . . be liable to the payee for handling the payment transaction in accordance with its obligations under Article 73” and “ensure that the amount of the payment transaction is at the payee’s disposal immediately after that amount is credited to the payee’s payment service provider’s account.” Directive Article 73 requires that credit to the payee’s payment service provider be value-dated “no later than the business day on which the amount of the payment transaction is credited to the payee’s payment service provider’s account” and that the payee’s payment service provider ensure that funds become available to the payee immediately. As in connection with Directive Article 73, the assumption is that payment to the payee’s payment service account is necessarily by posting credit to its account.
3. Where the payee’s payment service provider is not liable as above, “the payer’s payment service provider shall become liable to the payer.” The implicit but unstated assumption is of course that the non-execution is not attributed to insufficient funds or any other breach by the payer.
4. Where the payer’s payment service provider is liable under #3, it shall “as appropriate and without undue delay, refund to the payer the amount of the non-executed or defective payment transaction and restore the debited

payment account to the state in which it would have been had the defective payment transaction not taken place.”

5. Regardless of breach or defense to liability, in the case of non-execution of defective execution, and on request, the payee payment service provider shall “make immediate efforts to trace the payment transaction and notify the payee of the outcome.”

In principle, Directive Article 75(1) covers credit transfers while Directive Article 75(2) covers debit transfers. And yet, Directive Article 75(2) is stated to also cover credit transfers initiated by the payer through the payee. Indeed, depending on the architecture of a system, payment transactions initiated through the payee could be either debit or credit transfers. Thus, when they are routed through the payee’s payment service providers they are debit transfers. At the same time, when they are routed from the payee to the payer’s payment service provider, whether directly, through a switch, or even through the payee’s payment service provider acting merely as a communication channel, they are credit transfers. As credit transfers, such payment transactions initiated through the payee ought however to be covered by Directive Article 75(1) and not 75(2).

IX. CONCLUSION

The Directive provides for a harmonized legal framework, focusing on electronic payments. It is designed to create conditions for integration and rationalization of national payment systems, and thereby, the establishment of a common framework for the Community payments market. Intended to leave maximum room for self-regulation of industry, the Directive purports to harmonize only what is necessary to overcome legal barriers to a Single Euro Payment Area, or “SEPA.”

Thus, the Directive is not a comprehensive payment law. A narrow range of selected topics, primarily focusing on the payer-bank and payee-bank relationships, resulted in a scheme whose scope and contents, at least so far as credit transfers are concerned, cannot be compared to, for example, those of U.C.C. Article 4A.

Moreover, as the few examples from Germany demonstrate, for gaining what may be called *horizontal harmonization* among the various legal systems in the area of payments, cost has been incurred in the form of loss of *vertical harmonization*, between the provisions of the Directive, and provisions of general laws.

As well, in a globalized environment, it is regrettable that the terminology of U.C.C. Article 4A was not followed. Indeed, in adopting its Model Law on International Credit Transfers,¹⁸⁵ the United Nations Commission for International Trade Law (known as “UNCITRAL”) followed both the terminology and conceptual framework of U.C.C. Article 4A. Thus a measure of international consensus had been achieved that regrettably was not adhered to in the Directive.

Nevertheless, as a follow-up to the Euro/single currency project, in bridging differences among established legal systems of sovereign nations, some of which of major financial centres, the payment services Directive made a giant leap forward, towards harmonization and even uniformity of payment laws. Moreover, in providing for one statutory framework to apply to both debit and credit transfers, as well as for business and consumer payments, the Directive may have done better than the more compartmentalized and incomplete statutory scheme in the U.S.; the latter deals with consumer and business payments in various pieces of legislation and has no comprehensive statute for a debit transfer. In the final analysis, and notwithstanding valid criticism and room for significant improvements, the Directive is a noteworthy milestone in the march to a comprehensive payment law.

185. G.A. Res. 47/34, art. 6(b), U.N. Doc. A/RES/47/34 (Feb. 9, 1993).

