

# Recommendations for Regulating and Supervising Bank and Non-bank Payment Service Providers Offering Cross-border Payment Services: Consultation report

## Response to Consultation

### Bankers Association for Finance and Trade (BAFT)

#### *Introduction*

**1. Do the definitions contained in the report provide sufficient clarity and establish the common understanding necessary to facilitate the practical implementation of recommendations proposed in this report?**

The definitions contained in the report establish the common understanding of key objectives and the importance of improving the consistency and quality of regulatory and supervisory regimes for PSPs. It also reinforces the importance of promoting greater alignment between banks and non-banks operating in cross-border payment activities.

The spirit and overall aim of each recommendation are presented and aligned with industry discussions. However, to facilitate the implementation of the recommended proposals, more granularity is needed around the “future state” of the expected results for each recommendation.

A few considerations for each recommendation:

- Risk Assessment:
  - o Authorities should identify and assess risks across the PSP sector.
  - o Evaluate the effectiveness of existing laws and frameworks.
  - o Consideration: a common guideline or playbook defining minimum standards to identify and assess the risks associated with PSPs active in cross-border payments services would be very helpful.
- Regulatory and Supervisory Frameworks:
  - o Ensure frameworks address identified risks and are proportional to those risks.
  - o Promote consistency within and across jurisdictions.

- o Consideration: a common assurance guideline defining minimum standards to review if existing supervisory and oversight regimes address all key risks identified, are proportional to such risks, and are applied consistently would be very helpful.

- Consumer Protection:

- o Ensure transparency and protection for consumers using cross-border payment services.

- o Considerations: apply existing consumer protection rules to define minimum consumer protection expectations (e.g., the Dodd-Frank Wall Street Reform and Consumer Protection Act, section 1073, as well as rules effective in other jurisdictions, can be used to define best practices applicable globally for consumer protection related to cross border payments activities, such as Disclosure Requirements, Error Resolution and Cancellation, etc.).

- Supervisory Guidance:

- o Provide clear guidance on supervisory expectations to promote safe and efficient payment services.

- o Considerations: the FSB should provide a type of existing assurance processes that can be used to clarify expectations.

- Licensing and Registration:

- o Ensure licensing or registration requirements are risk proportionate.

- o Promote a level playing field from the time a PSP enters the sector.

- o Considerations: the FSB should provide licensing or registration processes and requirements that can be considered as recommended for cross-border payment activities. The banking community should agree on minimum standards based on lessons learned from existing programs. This should apply to direct and indirect participants of payment systems.

- Information Sharing:

- o Foster expanded information and data sharing within and across jurisdictions.

- o Critical for comprehensive risk assessments and regulatory actions.

- o Considerations: Data privacy and/or data localization requirements that could potentially be at risk in an environment where there is broader data sharing among players (banks and non-banks) should be flushed out. The FSB should recommend which bodies should monitor how consumer data is being shared and used. Information sharing in the context of cross-border payments is very a sensitive and complex theme. The global nature of financial transactions means that different countries have varying regulations, standards, and privacy laws, making it challenging to implement a common rule that applies universally. Along with data privacy, there are additional points to be considered, such as consumer

consent, fraud prevention, data validation, etc. In fact, information sharing can be even restricted at the local level. For that reason, local legislative bodies should provide a legal basis enabling the sharing of data at least in critical areas such as fraud, in line with the European Commission proposal for the review of PSD2.

o It is challenging to implement a common rule for information sharing in cross-border payments due to diverse regulatory frameworks, data privacy concerns, and security risks. To make progress in this front, support and collaboration from International Payments related organizations around standardization initiatives will be critical in addressing these challenges.

To facilitate the practical implementation of the proposed recommendations, additional work is needed to indicate in practical terms the minimum expectations for each recommendation. The overall recommendations should provide a view of what is expected from banks and non-banks operating in cross-border activities for each of the essential aspects of the regulatory and supervisory frameworks. This common understanding is crucial for achieving the goals of consistency, proportionality, and effective risk management in the regulation and supervision of cross-border payment services.

## **2. What adjustments are required to the draft definitions to improve clarity?**

BAFT recommends that the draft definitions of Payment Systems and Payment Service Providers (PSP) be further refined to explain that PSPs can be direct or indirect participants in a payment system.

A Payment System is defined as a “set of instruments, procedures, and rules for the transfer of funds between or among participants.” Payment systems can facilitate wholesale payments between participants who are typically financial institutions, sometimes including central banks, or retail payments between customers of those participants that would be high-volume, low-value transfers. The focus of this report is on retail payments and does not consider the services of intermediary banks. Participation can be direct, or indirect, defined as the use of the services of a correspondent bank that participates in a Payment System directly.

The term Payment Service Provider (PSP) as used in this report includes banks and non-banks that provide payment services. The latter covers:

- Remittance service providers (RSPs)
- Money services businesses (MSBs)
- Other providers of money or value transfer services (MVTs)
- Providers of prepaid transfers (e.g. prepaid cards or traveler’s checks) and pay-later transfers, such as credit card transfers
- Individuals that provide payment services, services enabling cash to be placed on or to be withdrawn from an account, the issuing of payment instruments and the acquiring of payment transactions, and payment initiation services and account information services.

This report focuses on PSPs that offer services directly to end users such as consumers and businesses. PSPs can be direct or indirect participants in the payment systems, depending on the rules of the particular system in question. Based on the possibility of direct or indirect participation, there is a need for clarification with respect to rules and control frameworks applicable to those offering payment services directly to end users as indirect participants of payment systems.

Moreover, the definition of PSPs includes account information services. Although this is aligned with the definition of PSPs in PSD2, account information services should be treated as data services and not as payment services and, therefore, be left out of the scope of this work.

### **3. What other terms should be defined in this section?**

One Leg Out (OLO) - OLO payments include support for payments to and from banks outside the direct participants in the domestic payment system, involving a cross-border element. This can include additional compliance/regulatory requirements and currency conversion, and is subject to the rules of the payment system on whether this activity is supported.

### **4. Does the explanation regarding the scope of the report provide sufficient clarity to promote the intended understanding of the recommendations?**

While in general, the scope is correct, what is missing or incorrect is the question of "who is providing the service to whom", and therefore, who is responsible/liable based on how to interpret the regulations and rules of the final PMI that is executing the final Clearing and Settlement. As such, there are two distinct models (which are evolving in some jurisdictions like Canada):

- PMIs where Banks are the only participants (e.g. Lynx), and
- PMIs where "others" can be participants (e.g. FPS).

The first is subject to the banks providing the service to "others" access to the PMIs and subject to their interpretation of the "rules." The second is when the PMI is directly responsible for enforcing the "rules," and therefore creates the disparity between banks and non-banks, and hence, the risk.

## *Section 1: The role of banks and non-banks in cross-border payments*

### **5. Do the descriptions of the roles of banks and non-banks in providing cross border payment services adequately reflect current practices?**

The definition of "retail payment" should be clarified, as there is no harmonized understanding of the definition. For some players in the field, it is in the same scope as "low-value transfer", and for others, it has an expanded meaning.

The definition of “correspondent banking” should be clarified as well, as there is no mention of the globally-secured setup that has been built to support it, based on accounts and RTGS connections.

Banks should support different positions within the payment chain, and roles and risks are consequently different among the bank of the payer versus the bank of the payee or intermediary bank. There are no clear distinctions for this in paragraphs 1, 1.1, and 1.3.

The systemic role of traditional commercial banks should be highlighted as geopolitical fragmentation and should be managed. This may disrupt progress towards quicker universal cross-border payment functionality across the globe.

Although there is a mention of "the lower levels of practices, characteristics, and supervision of non-bank PSPs compared to banks" in section "2.2, risks associated with cross border payments services" under "Money Laundering, Terrorist Financing, and Other Illicit Financial Crimes," the section "1.3, impacts of regulatory and supervisory inconsistencies" seems to be primarily written from the perspective of non-bank PSPs. We would appreciate it if the situation on the banking side could also be added to this section.

For example, "1.3. Impacts of regulatory and supervisory inconsistencies" states that "customers of non-bank PSPs may be subject to regulations and supervision unrelated to certain payment activities they conduct." However, from the perspective of enabling safe and secure customer transactions, banks are also required to manage third parties, among other regulatory and supervisory demands. When non-bank PSPs provide services using bank channels, appropriate measures are inevitably demanded from PSPs.

Furthermore, due to "the lower levels of practices, characteristics, and supervision of non-bank PSPs compared to banks," banks are indirectly paying more in compliance costs to manage the risks of these high-risk non-bank PSPs.

In the remittance services sector, non-bank PSPs have become significantly important. From the viewpoint of competitive fairness, it is believed that there is a need to resolve regulatory and supervisory inconsistencies to ensure that non-bank PSPs bear an appropriate share of compliance costs, aiming for the realization of safe and transparent financial services within society.

## *Section 2: Cross Border Payment Frictions and Risks*

### **6. What additional risks or frictions, within the scope of this report, are created by potential inconsistencies in the legal, regulatory and supervisory frameworks applicable to banks and non-banks in their provision of cross-border payment services?**

In addition to the risks mentioned in the FSB consultation report (“Recommendation for Regulating and Supervising Bank and Non-bank Payment Service Providers Offering Cross-border Payment Services”), inconsistencies in the legal, regulatory, and supervisory frameworks applicable to banks and non-banks providing cross-border payments services

can lead to the risk of regulatory arbitrage, undermining the frameworks, potentially increasing systemic risk, and create a lack of market integrity. Non-bank entities might have an incentive to exploit differences in regulations, circumvent stricter regulations, or gain a competitive advantage. Non-bank PSPs might even choose specific jurisdictions according to the currently applicable regulations that might bring other competitive advantages compared to banks in other jurisdictions. Regulatory arbitrage can propel other risks related to cross-border payment activities, such as fraud, consumer protection, operational failure, money laundering, and terrorism financing. Potential inconsistencies increase the cost and complexity of compliance programs and operations for all participants as they navigate multiple, inconsistent requirements. This can cause delays in payment processing on a day-to-day basis and act as a barrier to innovation.

Despite that both banks and non-banks are subject to the FATF international standards for combatting money laundering and terrorist financing, FATF standards and local AML/KYC/onboarding requirements are not always included in a single activity-based regulation, but instead in entity-based regulations. This creates inconsistencies and gaps in their application.

Furthermore, we agree with the report statement that “non-bank PSPs are more likely to engage in ‘occasional transactions’ rather than transactions originating from established customer relationships.” This leads to situations in which non-bank PSPs do not perform their own KYC/AML/CTF checks, but rely on those done by ASPSPs (a bank, usually). This is especially concerning in the case where the PSP offers payment services that “connect” local payment systems or services from different jurisdictions. In these cases, the PSP offering the cross-border payment service should perform additional checks, ensuring that the payment complies with the applicable KYC/AML/CTF regulations in the “connected jurisdictions.”

### *Section 3: Principles for developing recommendations*

#### **7. Do the identified principles provide sufficient support and appropriately frame boundaries for the recommendations in the report?**

In addition to the principles mentioned in the report, a supplementary principle would be to practice non-discrimination towards any segment of any bank or non-bank provider, and also any participant, whether indirect or direct. In other words, there should be consistent regulations, across KYC/CDD, payments, and banking licensing requirements, regulatory oversight and supervision, etc. applied across all participants.

Another supplementary principle would be to emphasize the need to consider payment transparency, especially where the debate around unbundling of individual payments has been problematic across bank and non-bank requirements in the past. As such, it would be helpful for the following (page 19, first principle): “It is thus important that regulatory and supervisory requirements consider the entire payment chain, including consistency around what constitutes the “start of the payment chain”, and the role of all actors involved, and clarify the respective responsibilities and expectations transparently and consistently.” This is important given that the roles and responsibilities differ despite non-banks being involved

in an activity that historically has been outside of regulatory focus due to lack of consistency in when a payment chain begins.

In addition to cooperation, coordination, and information sharing within and across jurisdictions, we propose to add another guiding principle: the recommendations shall be made in a way that they take advantage of existing local practices and minimize the impact on local payment ecosystems.

Also, one of the ideas conveyed in section 4 could be included as another guiding principle: the recommendations should be made and implemented in ways that do not jeopardize jurisdiction-specific policy goals, such as the robust entity-level regulation and supervision to which internationally-active banks are subject.

#### *Section 4: Recommendations for improving alignment of PSP regulatory and supervisory regimes*

##### **8. Are the recommendations sufficiently granular, actionable, and flexible to mitigate and reduce frictions while accommodating differences in national legal and regulatory frameworks and supporting the application of proportionality?**

Overall, the recommendations are sufficiently granular, but not so detailed that they provide no flexibility for local authorities to cater to specific requirements around overarching principles. However, there is one area where we believe that concrete guidelines should be provided so that clarity is not in doubt – the use of activity-based regulatory frameworks rather than any form of entity-based criteria (see below response to question 9). Furthermore, the FSB might want to include another recommendation related to the responsibilities of indirect scheme participants. Indirect scheme participants' originating transactions via a direct member should be subjected to equivalent standards of regulation and oversight as direct members. In the absence of related consistent regulations and supervision, an undue burden is on the direct member to answer for any transactions originated by such indirect participants.

At the broadest level, the recommendation is that regardless of entity-based standards set out by the applicable regulator, the underlying activity of the "entity" should be the driving factor around risk assessments, requirements, and oversight. It is not particularly explicit enough that for this to be a feasible solution, there would need to be a shift away from the license-led way of regulatory oversight, to the activity-led way of regulatory oversight (even if the license held is not that of 'full' authorization, such as a bank).

Another area that could be more prominent is the impact differences in licensing have on the activity permitted. For example, the MAS Digital Payment Token license does not restrict entities (Coinbase SG, for example) from servicing clients outside of Singapore (i.e. non-resident accounts for crypto-exchanges where the Bank partner would facilitate fiat pay-ins and pay-outs in USD through a "hubbed" location). In this scenario, the risks associated with dealing with non-resident accounts and the roles and responsibilities of entities involved in the chain related to AML controls and FIU reporting should be consistent.



**9. To what extent would the recommendations improve the quality and consistency of regulation and supervision of non-bank payment service providers (PSPs) active in cross-border payments services?**

The recommendations do not emphasize the “same activity, same risk, same rule” principle. On page 22, it is stated that “General issues that should be considered include the appropriate use of activity- or entity-based regulation;...considerations of whether to introduce more rigorous or comprehensive regulatory, supervisory and oversight approaches...for non-banks with significant financial activities.” This refers back to possible entity-based regulations, and suggests different segments of providers, be it banks or non-banks (or further, different segments within banks or non-banks, such as digital banks, small-cap banks, PSPs, MSBs, etc.) can have different regulatory requirements or criteria depending on their risk profile. This might introduce more complexity and less consistency in rule implementation and oversight, and encourage providers to represent themselves as belonging to a segment with less stringent criteria.

We believe that a purely activity-based regulatory framework should be applied. We agree that risk assessments should ideally be performed in the cross-border payments sector and on providers who will eventually be seeking to obtain the requisite license. However, this is only to understand the overall risk profile of the participants. The design of the framework that spells out the regulatory requirements, supervisory processes, and oversight criteria (and penalties) should only address the key risks that pertain to the cross-border payment activity, and not be dependent on the type of provider offering the service. This offers clarity to participants and keeps participants’ focus on adherence to activity-based risk reduction and mitigation, as opposed to regulatory arbitrage by diverting resources to downplay segment-specific risks.

**10. For the purpose of identifying material areas to be addressed from a priority and effectiveness perspective, should the report categorise the identified frictions created by inconsistencies in the legal, regulatory and supervisory frameworks applicable to banks and non-banks in their provision of cross-border payments services in terms of focus or order in which they should be addressed?**

We assume the “frictions created by inconsistencies in the legal, regulatory, and supervisory frameworks”, refer to those cross-border payment frictions identified by CPMI and FSB in footnote 27, as well as to the additional one the report introduces, which is “the complexities of meeting compliance requirements, including those designed to counter illicit finance, fraud and operational risks, such as cybersecurity, and strengthen resilience.” We believe listing them out in the current order is fine, all are of equal importance.

**11. Recommendation 5 focuses on domestic licensing. How and to what extent would licensing recognition regimes between jurisdictions support the goal of strengthening consistency in the regulation and supervision of banks and non-banks in their provision of cross-border payment services? What risks need to be considered?**

Some clarity on what is meant by “licensing recognition regimes between jurisdictions” is requested. If it is just a generic term, then there should be consistency among licensing



requirements across countries, and a key goal to prevent some form of regulatory arbitrage and to increase the ease of providers participating in various markets.

Licensing requirements across jurisdictions should be as consistent as possible. However, realistically speaking, the approach to the question and supervision of non-bank PSPs is very heterogeneous across jurisdictions, and, therefore, it will be unlikely to have full alignment globally or even regionally unless a regional authoritative body is involved, e.g., European Central Bank. Still, different currency regimes and geopolitical and economic objectives will contribute to misalignment of licensing requirements across countries. The best FSB and other international bodies can provide is a framework, in the form of a Model Code that establishes a set of global principles applicable and enforceable to all participants active in the payments and clearing space, based on simplicity and consistency. As such, the framework aligned with activity-based regulatory oversight should be provided.

**12. There are no comprehensive international standards for the regulation, supervision and oversight of non-bank PSPs and the cross-border payment services that they offer. Is there a need for such international standards?**

As cross-border payments by nature have different jurisdictions for sending and receiving parties, and often different intermediary jurisdictions, it is logical to enforce international standards allowing the application of controls by all parties.

In the case of PSPs, banks, and non-banks, the following international standards are critical for the sustainability of the services so that all participants in the payment chain can duly identify, control, and monitor the flows in a consistent and automated manner. For example:

- As the common ISO2022 standard is adopted for cross-border payments, the data should be provided to identify the ultimate debtor party, the debtor, and in some cases, the debtor agent. All PSPs providing a cross-border service for a third-party PSP will need to apply the same standards in order to permit the AML models along the payment chain to interpret the information and meet the transparency expectations. Only a global standard enforced by a recognized standards body will allow such a norm to be applied across jurisdictions.
- Another basic international standard is the identification of all intermediaries to the payment flow. Cross-border transactions up until the final credit to the beneficiary will have to respect the need for FATF transparency, and while this is now possible with ISO20022 standards, the international guidelines can ensure that no short-cuts are made across the world and that local payment systems are implemented in a way that this information is protected and carried along the payment process.

The key question is how to ensure the enforcement of these standards is applied consistently across jurisdictions and to reduce interpretations in terms of currency, messaging system, or use cases.

In principle, a Model Code on cross-border payment regulation and supervision would be beneficial. This rulebook would include best practices and rules established in countries that have already an approach to this matter. BAFT released a white paper in May 2024, entitled,

“Uneven Regulations in the Payments Industry” that acts as a Model Code for even regulations across banks and non-banks, and across various jurisdictions.

## *General*

### **13. What, if any, additional issues relevant to consistency in the regulation and supervision of banks and non-banks in their provision of cross-border payment services should be considered in the report?**

In addition to the points already covered in the report, some additional issues could be considered to enhance the consistency in the regulation and supervision of banks and non-banks in their provision of cross-border payment services.

First, effective regulation and supervision of cross-border payments require collaboration among multiple international stakeholders. Organizations such as the Financial Action Task Force (FATF), the Committee on Payments and Market Infrastructures (CPMI), and the Financial Stability Board (FSB), among others, play crucial roles. Harmonizing guidelines and standards across these organizations can help create a unified approach to managing cross-border payment risks.

Moreover, the involvement of regional and country-level organizations, trade associations, and industry bodies is essential. These entities can provide region-specific and industry-specific insights, ensuring that global standards are adapted to local contexts without losing their effectiveness.

Given the complexity of the cross-border payment ecosystem, effective governance is another crucial element that must be addressed. Governance structures should include clear responsibilities and dependencies, executive oversight built upon solid management practices, metrics and controls, a well-adopted risk culture, and independent control functions. Such governance will ensure that regulation is evenly applied across all participants, effectively executed, and disseminated within each market participant, thereby supporting both banks and non-banks in providing secure and efficient cross-border payment services.

In addition to effective governance, the following are some of the areas where guidelines can steer harmonization and prepare for standardization:

- **Connectivity and communication:** with diverse connectivity and open banking standards including trust frameworks, it would be important to evaluate how data providers/recipients and service owners/recipients within open banking and finance need to be regulated, controlled, and monitored to support the domestic and cross border payment system. While countries and regulators are framing their API standards and models, these standards might, in the future, influence the creation of a common, domestic, and international operating standard.
- **Harmonization of business processes:** Processing systems across jurisdictions should be able to reduce asymmetries and agree on common benchmarks around payment finality, exception management, fund return, and recall including response times and transaction reporting. Inconsistent user experience arises out of such situations often due to jurisdiction

or entity-specific rules. Standardization of service rules and the creation of a minimum set of standards for uniform adoption is recommended, if not explicitly included.

Finally, regulatory frameworks should avoid ambiguity by clearly defining in-scope activities and establishing explicit guidelines. As previously mentioned in our responses, regulatory oversight should be based on the activity rather than the entity providing the service.

We look forward to further dialogue on these important issues.