European Payment Institutions Federation aisbl

EPIF INPUT TO FATF PROJECT TO STUDY AND MITIGATE THE UNINTENDED CONSEQUENCES RESULTING FROM THE INCORRECT IMPLEMENTATION OF THE FATF STANDARDS

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ABOUT EPIF (EUROPEAN PAYMENT INSTITUTIONS FEDERATION)

EPIF, founded in 2011, represents the interests of the non-bank payment sector at the European level. We currently have over 190 authorised payment institutions and other non-bank payment providers as our members offering services in every part of Europe. **EPIF** thus represents roughly one third of all authorized Payment Institutions ("PI") in Europe. All of our members operate online. Our diverse membership includes a broad range of business models, including:

- Three-party Card Network Schemes
- E-Money Providers
- E-Payment Service Providers and Gateways
- Money Transfer Operators
- Acquirers
- Digital Wallets
- FX Payment Providers and Operators
- Payment Processing Services
- Card Issuers
- Independent Card Processors
- Third Party Providers
- Payment Collectors

EPIF seeks to represent the voice of the PI industry and the non-bank payment sector with EU institutions, policy-makers and stakeholders. We aim to play a constructive role in shaping and developing market conditions for payments in a modern and constantly evolving environment. It is our desire to promote a single EU payments market via the removal of excessive regulatory obstacles.

We wish to be seen as a provider for efficient payments in that single market and it is our aim to increase payment product diversification and innovation tailored to the needs of payment users (e.g. via mobile and internet).

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EPIF's contribution to the FATF project to study and mitigate the unintended consequences resulting from the incorrect implementation of the FATF Standards

General Comments:

EPIF fully supports the Financial Action Task Force (FATF) efforts to look into the unintended consequences resulting from incorrect implementation of the FATF standards.

In our response EPIF will focus on the issue of bank de-risking that many of our members are facing across Europe. While this is not only a European issue, as the representatives of the European Payment Institutions, we will focus our contribution and share our experiences in European markets.

EPIF agrees with the FATF that correspondent banking relationships are essential in the global payment system and vital to international trade and the global economy as a whole, including for emerging markets and developing economies.

The FATF approach to "de-risking" is based on the FATF Recommendations[1] which require financial institutions to identify, assess and understand their money laundering and terrorist financing risks, and implement AML/CFT measures that are commensurate with the risks identified.

When establishing correspondent banking relationships, banks are required to perform normal customer due diligence on the respondent bank. Additionally, banks are required to gather sufficient information about the respondent bank to understand the respondent bank's business, reputation and the quality of its supervision, including whether it has been subject to a money laundering or terrorist financing investigation or regulatory action, and to assess the respondent bank's AML/CFT controls.

However, we would like to point out that this is not always the case. From our experience, all the main money transfer operators (MTO) providing their services in Europe have experienced the unilateral closure of their bank accounts and the refusal to offer them banking services in breach of Article 36 of the revised Payment Services Directive[2] in different Member States. This poses an existential threat to their activities, employees and customers in that country and the continuation of this practice threatens to undermine the AML/CFT protections in place by driving MTOs out of the market and leading customers to use unlicensed illegal channels. Moreover, this process became even more accelerated in the past months with the COVI-19 crisis.

National and international policymakers including the FATF have labelled the concerted closure of bank accounts, or the refusal to provide banking services to certain industry sectors including the money transfer industry, as 'de-risking' or 'de-banking' and analysed it in order find ways to stop, prevent and reverse it. The FATF has subsequently issued specific Guidance to the banking sector in order to clarify applicable requirements and to stop further de-risking from taking place.

We share the concerns expressed in the FATF Guidance on correspondent banking[3], about the increase of situations where financial institutions terminate or restrict business relationships with entire countries

[1] https://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%202012.pdf
[2] https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32015L2366
[3] https://www.fatf-gafi.org/media/fatf/documents/reports/Guidance-Correspondent-Banking-Services.pdf

or classes of customers in order to avoid, rather than manage, risks in line with the FATF's risk-based approach (RBA). This issue may drive financial transactions into less/nonregulated channels, reducing transparency of financial flows and creating financial exclusion, thereby increasing exposure to money laundering and terrorist financing (ML/TF) risks.

Often the more marginalised or disenfranchised parts of society are deemed to be potentially more risky - as reflected in the most recent supranational risk assessment by the European Commission. This puts extra compliance burdens on the EPIF membership and in turn excludes them from conducting their business by being cut from bank and correspondent banking services.

Policy makers and supervisors have a role to play to in addressing this market failure and thereby helping to promote financial inclusion. Money transfer operators foster financial inclusion by enabling remittance flows from countries with highly banked and technologically equipped customers to communities overseas whose residents have limited access to formal banking services or technology. The International Monetary Fund (IMF) Working Paper published in May 2020 confirms the positive impact of remittances on financial inclusion especially in fragile states.

MTOs and their agents depend on access to accounts held with credit institutions for the transfer, clearing and settlement of funds received from customers and for 'client funds safeguarding' purposes as required under applicable laws.

In Europe, in order to address 'de-risking', EU legislators adopted a specific provision in Article 36 of the PSD2. This article imposes an obligation on the Member States to ensure that payment institutions including MTOs have access to payment accounts held with credit institutions in order to allow for an unhindered and efficient provision of payment services. Still this issue remains a key challenge for MVTOs. Our members have experienced the closure of existent bank accounts and denial to access to bank accounts in countries where they intend to expand. This includes settlement accounts with agents, cash lodgement accounts (Agents deposits cash into accounts) as well as operational accounts. Consequently, this has led to the denial of access to financial products by customers.

This is particularly sensitive in smaller countries where there are fewer banks present.

EPIF has identified communication gaps in the context of correspondent banking relationships, both among banks and between banks and payment institutions. Dialogue between banks and money-service businesses is often limited. The lack of a safe space for banks and money-service businesses to exchange information on typologies can hinder an intelligence-led approach to financial crime risks.

In some countries, such as the United Kingdom (UK) and Lithuania, specific Guidelines have been produced to provide the banking sector with clear rules on how to provide access to the non-bank payment service providers. Of note, the dedicated Chapter 16 in the PSD2 Approach document of the UK specifies which criteria and procedures banks have to follow under Art. 36 PSD2. This has alleviated the impact of bank de-risking in the UK. The Lithuanian Central bank published similar Guidelines on 25th May 2020. The Finish FSA is also currently exploring similar possibilities, and the Polish FSA on 2nd June 2020 published a questionnaire for banks to use when entering into relationships with Payment Institutions. Unfortunately, this is not the case in all Member States.

EPIF has also called upon the European Banking Authority (EBA) to issue guidance to address this issue at a European level. We have also invite the EBA to explore any regulatory solutions to de-risking if banks no longer want to accept MTOs as clients, such as for example, an account held with the national Central Banks which would allow the MTOs to settle through the Central Bank's accounts.

Concerns about financial crime risks are seen as an important contributing cause of de-risking. EPIF would like to point out the negative impact that the Commission's SNRA assessment[4] of this sector had on our members. EPIF has provided feedback to the Commission to take into account when reviewing the Supra National Risk Assessment (SNRA) and expects that this will be taking into consideration when assessing the level of risk.

Detailed description of the situation:

Concrete impact of bank de-risking:

In some cases, we had to ask our agents to deposit the funds received from our clients in other banks, which caused a delay in the deposits as well as additional bank charges that we had to pay for.

In other cases, our clients were also clients of the bank that closed the account and they worked with us because it was convenient for them. Because of this, the closure of the account made one of our members lose 19% of their clients.

In another specific case, a payment institution has suffered the closure of different bank accounts in the last few years and at this moment, 95% of their transactions are managed through only one bank account, leaving them in a very vulnerable position. They have tried to open a bank account in 5 other banks but the access has been denied in every case.

De-risking drives up price. When we choose partners, we negotiate price. If we get de-banked and must find a new partner, this requires ongoing resources within the company and often means a more costly deal. De-risking also disrupts consumers' access to products. If a product in one Member State relies on a main banking partner and a back-up partner, if both of those banks decide to de-risk at one time, this is a risk to operational continuity. In some cases, we may no longer be able to offer our product for that Member State if both bank partnerships fall through.

De-risking also has implications for the entire market. It leads to ineffective mitigation of ML/TF. Transparency helps to build trust but strong communication is also essential in tackling the inherent risk of money laundering and fraud. If banks close their doors and are not willing to have an open dialogue about trends, controls and solutions, they are not contributing to the effective prevention of ML/TF.
De-risking also contributes to restricting access to the provision of business bank accounts. Restricted market access for a subset of consumers is, in effect, a market failure. This drives ineffective competition between PSPs and incumbents, and may also lead to the concentration of risk.

Examples in different EU countries:

Germany:

As regards the situation in Germany, one of our members had to terminate all its agency agreements except for one that is a company directly related to the payment institution. As they were just expanding

4 https://ec.europa.eu/info/sites/info/files/supranational_risk_assessment_of_the_money_laundering_and_terrorist_financing_risks_affecting_the_union.pdf

their activity through agents in Germany, they lost 22.000 Euros in annual revenues and have not been able to expand their business through agents in Germany in the last 6 years.

The Netherlands:

Another example for the Dutch market is the case where a local Dutch PI – authorized to carry out the business of a payment service provider by the Dutch Central Bank (DNB) for the services as listed below – was denied access to open a bank account by different banks and therefore unable to start offering the services. As a result of this refusal to open a bank account, this company has decided to cease its activities even though it never really started.

A Correspondent bank who is not facilitating payment flows to and from our Agents could disrupt wire activity which supports our settlement process.

The closure of existent accounts produces the following negative consequences; 1) Service disruption affecting customers who need to send money to their families in need, 2) revenue decrease and cost of handling customer's funds increase, 3) employees' dismissal, 4) legal fees increase, 5) with challenges to cash lodgement, we have to move to armoured car and other more expensive cash collection processes causing higher cost to the consumer, 6) For smaller industry players, more expensive cash collection processes may not be as transparent to regulators.

The banks refusal to open new bank accounts produce the following negative consequences; 1) impossibility to gain access to new countries where other players are present impacting our business/expansion plans, 2) negative impact on revenues risking.

Sweden:

In Sweden, banks decided to de-risk the money transfer sector due to Money Laundering risk and the risk of handling cash. In Sweden the major 6 banks built a local mobile payment system (SWISH).

Swish is a mobile payments system launched in 2012 by six of the country's largest banks – Danske Bank, Handelsbanken, Länsförsäkringar, Nordea, SEB and Swedbank – emerging from a working group of the Swedish Bankers Association.

A number of other institutions are also now part of the network, including Skandia, Sparbanken Syd and ICA Banken.

Instant payments can be made between two parties via a mobile app connected to the user's bank account – and tied to the "BankID Säkerhetsapp" electronic identification system used by lenders across the country.

The payments network was initially developed for private transactions between individuals, but has evolved to cater for businesses and e-commerce platforms.

Since its launch, Swish has gathered around 6.9 million users throughout Sweden, which is more than two-thirds of the country's population.

In 2017, it launched a QR code facility to allow users to make faster and simpler payments.

More than one billion transactions have been made across the network, with about 22.5bn krona ($2.4bn) transferred on a monthly basis, according to the latest figures.

Small World have asked their bank in Sweden to grant access to SWISH for businesses in order to install the payment system in their agents and branch network, in this case they would totally mitigate the cash management risk that concerns most of banks in Sweden. SWISH refused to grant services to Small Word by saying “Swish Service is not opened or available for Money transfer operators”.

This is a clear example of the banks approach towards money transfer operators offering money remittance and how anti-competition features could be present behind the banks/Swish decisions.

Poland:

In addition to the above considerations, we would like to refer to the initiative of the Polish Financial Supervision Authority (“PFSA”), inspired by the practices of the Wolfsberg Group, regarding the obligation for banks to use a designated questionnaire when entering into relationships with payment institutions. The assumption of the PFSA is to increase the security of the transactions handled and to develop similar practices when banks establish relations with payment institutions. Banks will be entitled to use the questionnaire for payment institutions before establishing a relationship (opening a bank account) and during the course of that relationship (cyclical verification).

The analysis conducted by the Polish Organisation of Non-Banking Payment Institutions (PONIP), which is a member of EPIF, shows that the document in its current form may become a barrier to the use of a bank account by payment institutions. The most significant doubts are raised by the fact that the questionnaire contains inquiries that strike at the competitive balance in the financial market between banks and payment institutions. These questions concern, among others, the obligation to provide individual details about transactions and clients of a given institution (such as number, total value or an average of transactions), information on business plans and strategies, or information on the institution's current operations. As a result of using the questionnaire, payment institutions will also be required to provide banks with a number of documents, including internal procedures or descriptions of monitoring processes.

The idea of introducing the questionnaire by the PFSA is based upon a determination that relationship between banks and payment institutions are akin to a correspondent relationship within the meaning of the AML regulations. According to legal opinion, which has been commissioned by PONIP, the application of the ‘correspondent relationship’ definition to the relationship between domestic entities is very questionable, and this issue was indicated in the communication with the PFSA in this respect. The introduction of rigours reserved for the establishment of correspondent relationships with regards to the whole payment sector should be considered as a definite over-interpretation and constitutes a disproportionate approach.

In summary, we believe that the practices described above, pose a continuing risk of “de-risking” activities on the side of banks in the near future. The questionnaire in its current form creates a threat of being improperly used by banks to refuse or close accounts of payment institutions only on the basis of answers given by this institution in the questionnaire. Therefore, already at this stage of work, we would like to point out a problem in this area that appears in Polish practice.

How financial institution explain the decision not to have/withdraw a business relationship

In most cases faced by members, there was no formal process and a lack of communication regarding the closure of accounts and/or the end of the business relationship. Often, it is an internal decision by a banking partner in which money remitters have no way to challenge or change its decision to discontinue the banking services to the money remitter. Very little detail is provided by the banking partner.

EPIF members noted that:

- Banks primarily offboard us with the reasoning that they no longer wanted to work with PSPs due to risk appetite. These strategic decisions are driven by senior management with the rhetoric from relationship managers that either fear of regulatory fines (AML) or change in senior management is the catalyst. In our experience, banks are terminating a relationship through fear of inherent risk with the sector, rather than conducting a review on an individual basis.
- There was no explanation from the financial institution. Most of the time the communication is done by a letter from the financial institutions in which they simply notify the closure of the account without explaining any reasons.
- In other cases we provided all the documents requested by the financial institution, and the bank decided to close the account without giving any explanation.
- In most instances, banks do not complete a detailed risk assessment or risk scoring of the MTO and have not asked MTOs for additional information in order to come to the account closure decision. For example, in Belgium the banks which decided to close the accounts failed to identify the risks that bring them to come to such decision
- In another case, the financial institution stated that unless we signed additional products (such as insurance policies, investment funds, payment of payrolls through their bank accounts, etc.) they would withdraw the business relationship. We also have evidence (emails) stating this situation.
- Sometimes financial institutions explain the decision by email, by letter or verbally. Sometimes financial institutions are just ignoring our requests and not responding our letters/emails.
- Usually financial institutions refer to commercial rights to justify the bank account closure ignoring art. 36 PSD2 rights.

It is important to note that the de-banking process can be very swift (one to two months) with little communication or formal notice, while securing an alternative banking relationship can take as long as one year. This puts PSPs at significant risk of being left with no banking partner at a given time, even with a back-up partner in place.

It appears that the banking industry is receiving unclear guidance from the regulator in managing MSBs relationships. A commitment from regulators to publish standards of diligence for maintaining MSB relationships would clarify requirements and reduce de-risking.

Process and possibility to have the decision reviewed

Our members were not given an opportunity to have their decision reviewed. In some cases EPIF members were notified by letter that the bank account would be closed on a certain date. They responded in writing but had no formal response, and when they then contacted the bank by phone were informed that this decision would not be reviewed.

Only in one case in Ireland, the bank granted an extension period of a few months. In the remainder of cases, the banks never reviewed or changed their unilateral decision. Neither were they open to sit down and discuss ways to mitigate risks e.g., to keep open the bank account only for non-cash transactions.

In the case in Ireland, the EPIF member passed successfully two AML inspection conducted by the Central Bank of Ireland and a very thorough Due Diligence performed by the Bank's Compliance Unit.

Our members are regularly examined by the same Supervisors as their banking partners. However, their banking partners do not believe MTOs are being held to the same compliance standards and are unable to rely on the fact that we are examined by the same Supervisors.

For example, last year the Belgian Central bank organised round table exchanges between the MTO's and Banks and Banking Federation representatives to find a solution to the outstanding issues related to de-risking. Unfortunately, during the meetings the banks' representatives clearly stated that the MTO's industry is considered high risk and therefore the banks choose to de-risk MTOs. EPIF and other MTO's offered to respond to all specific Compliance related questions and provide a presentation of how risks are mitigated by the MTOs, but the banks refused to engage in that discussion. Even the Belgian Central Bank's and the Treasury's arguments that the decision to de-risk must be made in analysing the situation on a case by case basis, did not make the banks to change their mind.

Another member notes that in their experience, the process of being de-banked varied between institutions but followed a similar pattern: first, the institution notified us that we would be de-banked. Our team would then ask the relationship manager for a reversal of the decision, and ask to go to an official committee to assess our case. In several instances, we were told there was no possibility to go to a committee. Alternatively, we were told our case was brought to an internal committee, but that our request was denied or it was impossible to reverse. It was difficult to know whether a formal process was actually carried out since the process was opaque. Each time we were confronted with being offboarded, we asked for the deadline of closing accounts to be extended. Ultimately, in most cases, the accounts are closed.

Alternative channels to access financial services

EPIF members attest that access to bank accounts has become harder and harder over the past years. While most institutions strive for back-up partners to mitigate the risk of being offboarded, securing a second partner is difficult and time-consuming, with some markets showing little to no appetite for serving PSPs altogether.

Our members have a diversified bank network because these banks follow the risk based approach and fully audit our compliance programs. However, there is an issue in jurisdictions where there are limited banking partners.

As previously mentioned, the business of one of our members depends (95% of it) on only one bank.

In other cases (for example in Germany), the only agent of one of our members sends the funds to the payment institution through a cash pickup service that sends the funds to the payment institution's bank account in Spain through Bundesbank.

In most of countries and due to de-risking trend, we have only access to one bank account. The alternative way to collect from the agent network and channel customers funds through the banking system is through cash courier companies (e.g. G4S).