SPOTLIGHT ON PAYMENT FACILITATION

Risk Mitigation for Payment Facilitators

A Spotlight on Payment Facilitators (PayFacs) and their Contractual Compliance Requirements

StratisAdvisory

RISK | STRATEGY | CYBER | COMPLIANCE MANAGEMENT

What is a Payment Facilitator?

A payment facilitator (PayFac) is a company that helps simplify electronic payments processing for smaller merchants or businesses. This allows merchants to accept payments quickly and with minimal paperwork. The origin of PayFac can be traced in the early 2000's when there was a demand to simplify payment processing among small businesses.

Key Features of a PayFac

Easy Merchant Onboarding

Merchant onboarding is quick and straightforward with reduced paperwork and automated approval process.

Aggregated Payment Processing

PayFac processes payments for multiple businesses under one account—removing the need to set up individual merchant accounts.

Compliance and Security

PayFac handles technical and administrative work such as payment processing and compliance, thus allowing businesses to focus on their daily operations.

Benefits of a PayFac

Quick Setup

Streamlined underwriting for approvals.

Simplified Management

Reduced administrative burden for businesses with compliance and security.

Reduced Costs

Lower processing fees with aggregated transactions.

With the increase in cashless payment operations, PayFacs maintain various upstream risk management requirements to ensure they are not susceptible to facilitating illicit crimes such as fraud, money laundering, human trafficking, etc.

Activities Related to Risk and Compliance

Financial Compliance Monitoring

PayFacs simplify the process in monitoring their clients' financial transactions and ensure adherence to AML regulations.

Account Activity Monitoring

PayFacs are expected to have controls to identify unusual transactions and be able to flag these activities for review.

Industry Standards

PayFacs typically contract with regulated financial institutions that pass on their regulatory requirements to the PayFac as part of their contractual processing agreement.

Risk and Compliance Overview for Payment Facilitator

The PayFac industry continues to evolve due to a heavy emphasis on card-based transaction activity. The rise of PayFac-as-a-Service (PFaaS) is vital in streamlining payment facilitation, which allows businesses to payment solutions. However, the regulated financial institution behind the PayFac typically passes down certain regulated requirements as part of the contractual relationship.

Data Privacy

PayFacs in the US are mandated to comply with several data privacy regulations to protect sensitive customer information. Mainly, these laws are meant to protect customer data, drive transparency and accountability, and ensure global compliance. Examples are the **California Consumer Privacy Act** and EU's **General Data Protection Regulation**. For the latter, although this is an EU regulation, it impacts US PayFacs when processing the data of EU residents.

Anti-Money Laundering

While PayFacs are not directly subject to compliance under the **Bank Secrecy Act ("BSA")**, acquiring banks enforce BSA/AML compliance and PayFacs must align their BSA/AML programs with the bank's risk management policies, customer due diligence, and enhanced due diligence activities. At scale, the rise of global digital payments requires PayFacs to comply with cross-border screening to ensure they do not involve sanctioned individuals, entities, or jurisdictions.

Bank Partnership Compliance

Maintaining compliance with bank partners is a complex and ongoing challenge for PayFacs as banks impose rigorous requirements related to AML, KYC, and transaction monitoring. These challenges extend as PayFacs must also manage their own compliance frameworks and proactively adapt to increased regulatory scrutiny and extensive verification processes of banks.

Cybersecurity

Cybersecurity laws impacting payment facilitators revolve around safeguarding data, ensuring resilience, preventing threat, and responding to incidents. Data privacy and cybersecurity are intertwined when it comes to compliance to ensure secure payment processing. The **Federal Trade Commission (FTC)** has been vital in overseeing PayFacs through enforcement of consumer protection laws, fraud prevention, and data security regulations which could shift focus with the US political landscape.

Payment Industry Standards

The **Payment Card Industry Data Security Standards (PCI DSS)**, although not a law, is a critical compliance standards for PayFacs handling cardholder data. They ensure the secure handling of payment card data, protecting the customers and businesses from fraud or data breaches. Non-compliance can lead to fines from payment networks like Visa and Mastercard so there is in essence, regulatory alignment with industry standards for payment facilitation.

Key Operational Challenges

Evolving technologies, changing regulatory landscapes, and increasingly sophisticated fraud schemes are the primary drivers of increasingly complex challenges for PayFacs. Moreover, PayFacs are powered by their transactional banking relationships, which require extensive ongoing compliance monitoring, annual reviews, and reporting. Maintaining compliance with banking partners is critical to success.

Discover what Stratis Advisory can do for you

Compliance Program Development

An enterprise AML and sanctions compliance program is founded on the five (5) pillars of internal controls, training, a compliance officer, independent review and customer due diligence. Stratis can help you develop, evaluate and implement a scale-appropriate AML and sanctions compliance program suitable for your business model and regulatory or partner-based environment, ensuring that you stay ahead of evolving regulations, guidance, and enforcement.

AML Independent Review

Whether operating as a regulated financial institution or through various bank, payment, or lending partnership models, typically an annual review of your AML and sanctions programs is a requirement. As Stratis serves a portfolio of global regulated and unregulated companies, Stratis can help you with performing your required AML and sanctions review on a scale and risk-appropriate basis to satisfy your statutory requirement, but also any requirement(s) from your banking partner.

TempCCO® Outsourced Compliance Function

Developing a compliance program is the just the initial step in operating as a Payfac, regulated financial institution, or as a partner of one. Operationalizing your compliance program is critical to maintain compliance, bank accounts, and for successful audits and examinations. Depending on the life cycle of your organization, Stratis can provide you with on-going risk, strategy, and compliance support under our TempCCO® outsourced compliance function to assist you while launching, scaling, or optimizing your compliant program.

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