PaymentsCompliance

The Great Balancing Act: Payments Regulation Today

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The challenge of regulating payments in an age of terrorism has been brought into focus by this week's EU announcement that fresh money laundering laws are to be altered before any national authority has a chance to implement them. PaymentsCompliance spoke with several experts in the field to discuss business ramifications, and how future events may again cause a rewriting of rules.

Virtual currency exchanges and prepaid cards are the main target of the European Commission's Action Plan to combat terrorism funding.

However, a week earlier, Europol, Brussels' increasingly powerful and influential enforcement unit, said "despite third-party reporting suggesting the use of anonymous currencies like Bitcoin by terrorists to finance their activities, this has not been confirmed by law enforcement".

France has been the major driver of change, pushing for last minute amendments to the revised Payment Services Directive (PSD2) following the Charlie Hebdo massacre.

Unsuccessful in its lobbying, it again attempted to force the EU's hand after a second wave of terror attacks in November.

Now, amendments will be made to the 4th Anti-Money Laundering Directive (4th AMLD).

Financial crime specialist Jessica Parker, a partner at Corker Binning's London practice, pointed to how the the enhanced due diligence required with regard to prepaid cards was prompted by the initial Paris attacks.

"Such a high profile incident is bound to galvanise legislators into action; reviewing whether they have provided law enforcement agencies sufficient powers to trace and respond," she said.

"The fact that the directive is already subject to amendment so soon after being passed should come as no surprise.

"The challenge faced by legislators at domestic and European level is that they tend to react to rather than predict changing methodologies in financial crime."

The 4th AMLD was adopted in May 2015, and despite initially giving a two-year window to implement, the EU is pushing for states to adopt it "by the end of 2016".

It will widen to accommodate the changes highlighted in the action plan, forcing virtual currency exchanges to hand over more data on users, and call for a heightened verification process for prepaid card retailing.

Despite the concern in Europe, two territories not mentioned anywhere in the EU texts regarding terrorism activity are the beating heart of Bitcoin, boasting the largest exchanges, wallets and transaction volume — the US and China.

The EU believes licensing is the way forward, where it can look to the US for a first example.

AML and virtual currency experts at Washington D.C., law firm BuckleySandler told PaymentsCompliance an industry well versed in volatility would have to brace further for regulatory disruption.

Dana Syracuse, who worked on the BitLicense for the New York State Department of Financial Services prior to joining the firm, and Amy Davine Kim, counsel and e-money specialist, pointed to a brighter future using existing technology.

"Regulators need to educate themselves on the technologies available to analyse the blockchain," they said.

"Just as there are protections within our traditional financial markets, appropriate guard rails need to be built around Bitcoin and virtual currency."

Companies providing financial services, such as exchanges, should expect to be regulated in the same way as any other similar financial institution transferring fiat currency on behalf of others, the pair note.

"And yes, this includes calling for a robust AML/BSA compliance programme," they said.

"The danger is always regulating in the face of a crisis when there is a temptation to overcorrect."

Financial services expert and partner at the firm, Margo Tank, added: "Regulation in this space must be the result of a continuing dialog between state, federal, and international regulators and not reactive policymaking."

A view shared by Coinbase, the pair note that regulatory silos bubbling up in an industry where cross-border payments is unlikely to succeed, and that the EU and New York, for example, must attempt a consistent approach.

"Depending on how formulated, the regulation would be consistent with US principles of knowing your customer and screening customers for potential matches to terrorist lists, including New York's BitLicense regime," they said

For Parker, the dangers inherent of a hasty response are clear.

"The speed of their reaction is as slow as their legislative process while criminals and terrorists are adept at adapting to new threats to their funding infrastructure," she said.

"On the other hand, legislators should not be too hasty to respond.

"The directive requires the commission to provide a report identifying key AML/CTF risks across Europe by June 26, 2017 (Art 6).

"It would be preferable to bring the date of this report forward to present a balanced case for amendment."

The European Commission denied when approached by PaymentsCompliance it was indulging in regulation "on the hoof" or that it had allowed a mission creep of AML laws to occur.

Siân Jones, founder of COINsult and the European Digital Currency and Blockchain Technology Forum, recently spoke at a commission treasury roundtable on the subject of virtual currencies.

She understands the quandary regulators are in, but advises the sector to not assume too much as the commission itself acknowledges virtual currencies are "considered a useful tool for rapid international payment transfers and low cost money remittances".

The commission indicated it resisted an outright ban on the grounds they represent a "small market".

"EU policymakers and legislators, the European Commission and supporting institutions, and EU regulators all have virtual currencies on their current agenda," Jones said.

"They will likely have to table specific legislative amendments which will, in turn, be subject to parliamentary scrutiny and enactment processes."

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