FDIC Supervisory Approach to Payment Processing Relationships With Merchant Customers That Engage in Higher-Risk Activities

Summary: The FDIC is clarifying its policy and supervisory approach related to facilitating payment processing services directly, or indirectly through a third party, for merchant customers engaged in higher-risk activities. Facilitating payment processing for merchant customers engaged in higher-risk activities can pose risks to financial institutions; however, those that properly manage these relationships and risks are neither prohibited nor discouraged from providing payment processing services to customers operating in compliance with applicable law.

Statement of Applicability to Institutions With Total Assets Under $1 Billion: This Financial Institution Letter applies to all FDIC-supervised banks and savings associations, including community institutions.

Distribution: FDIC-Supervised Banks (Commercial and Savings)

Suggested Routing:
Board of Directors, Senior Executive Officers, Chief Credit Officer, Chief Information Technology Officer, Bank Secrecy Act Officer

Related Topics:

Attachment:
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Highlights:
- Financial institutions that provide payment processing services directly or indirectly for merchant customers engaged in higher-risk activities are expected to perform proper risk assessments, conduct due diligence to determine merchant customers are operating in accordance with applicable law, and maintain systems to monitor relationships over time.

- Proper management of relationships with merchant customers engaged in higher-risk activities is essential. Financial institutions need to assure themselves that they are not facilitating fraudulent or other illegal activity. Institutions could be exposed to financial or legal risk should the legality of activities be challenged.

- FDIC’s examination focus is on assessing whether financial institutions are adequately overseeing activities and transactions they process and appropriately managing and mitigating risks. Financial institutions that have appropriate systems and controls will not be criticized for providing payment processing services to businesses operating in compliance with applicable law.

Note:
FDIC Supervisory Approach to Payment Processing Relationships With Merchant Customers That Engage in Higher-Risk Activities

The FDIC is issuing this letter to clarify its policy and supervisory approach related to facilitating payment processing services directly, or indirectly through a third party, for merchant customers engaged in higher-risk activities. Facilitating payment processing for merchant customers engaged in higher-risk activities can pose risks to financial institutions and requires due diligence and monitoring, as detailed in prior FDIC and interagency guidance and other information.

Financial institutions that properly manage these relationships and risks are neither prohibited nor discouraged from providing payment processing services to customers operating in compliance with applicable federal and state law.

The FDIC and other agency guidance indicate that financial institutions that provide payment processing services directly or indirectly for merchants engaged in higher-risk activities are expected to perform proper risk assessments, conduct due diligence sufficient to ascertain that the merchants are operating in accordance with applicable law, and maintain appropriate systems to monitor these relationships over time. The proper management of relationships with merchant customers engaged in higher-risk activities is essential. Financial institutions need to assure themselves that they are not facilitating fraudulent or other illegal activity. Institutions could be exposed to financial or legal risk should the legality of activities be challenged.

The FDIC is aware that some payment processors or merchants may target institutions that are unfamiliar with the related risks or that lack proper due diligence or controls to manage these risks. Thus financial institutions that engage or plan to engage in these activities should review this guidance. The focus of FDIC examinations is to assess whether financial institutions are adequately overseeing activities and transactions they process and appropriately managing and mitigating related risks. Those that are operating with the appropriate systems and controls will not be criticized for providing payment processing services to businesses operating in compliance with applicable law.

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1 Payments may be in the form of remotely created checks (also known as “Demand Drafts”), Automated Clearing House transactions, or similar methods.

2 Higher-risk activities are those that tend to display a higher incidence of consumer fraud or potentially illegal activities than some other businesses. Higher-risk activities are typically characterized by high rates of return, high rates of unauthorized transactions, consumer complaints, or evidence of state or federal regulatory or criminal actions against the business customer, which indicate that the activity needs to be reviewed to determine whether fraudulent or illegal activity is occurring. See FDIC, Financial Institution Letter, FIL-3-2012, Payment Processor Relationships, Revised Guidance issued January 2012.

3 FDIC guidance and other information on this topic includes:

FFIEC guidance on this topic includes:
   - The FFIEC Information Technology Handbook, “Retail Payments Systems Booklet.”