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CFPB finalizes rule defining the market for general-use digital payment applications

Initial perspectives related to the CFPB's latest rulemaking to supervise nonbanks that provide general-use digital consumer payment applications

On November 21, 2024, the Consumer Financial Protection Bureau (CFPB) finalized the sixth rulemaking under 12 CFR Part 1090 to define larger participants of markets for consumer financial products and services.[1] This final rule establishes the CFPB's supervisory authority over larger nonbank companies providing funds transfer and digital wallet functionalities through digital applications. This includes apps popular among consumers for peer-to-peer (P2P) and contactless payments. The final rule includes several changes from the proposed version that provide clarity to affected nonbanks on whether their business model is subject to the CFPB's risk-based supervision program. Overall, this rule represents a significant expansion of scope for the CFPB, which is now enabled to treat certain tech companies more like banks and potentially subjects such companies to "proactive examinations." Although this rule explicitly applies to companies handling more than 50 million transactions per year, it foreshadows the CFPBs increasing oversight over technology organizations offering consumer financial products and services through digital applications. The rule will be effective 30 days after publication in the *Federal Register*.

5 summary insights

Criteria of larger participant: The final rule has increased the threshold for companies to be considered a "larger participant" from 5 million (as under the proposed rule) to 50 million consumer payment transactions processed annually. The CFPB also excluded organizations considered small businesses by the Small Business Administration (SBA) guidelines and limited the rule's scope to US dollar denominated transactions, thus excluding crypto and digital asset volumes.

Definition of "general-use": The final rule clarifies the general-use digital consumer payment application market-specific activities, which includes providing funds transfer and digital wallet functionalities for consumer payment transactions. It is intended to cover a broad range of digital payment services, including digital wallets, payment apps, funds transfer apps, and P2P payment apps, which are used by consumers for various everyday transactions (e.g., contactless payments in store, social media payments, and payment buttons in ecommerce check-out flows).

Focus on embedded finance: The CFPB made it clear that their focus is on providers of digital wallets and P2P payment functionality across platforms, and not on single-purpose platforms or consumer payment experience. The rule excludes merchants and those originating credit (e.g., buy now pay later [BNPL] lenders and mortgage brokers), buying and selling securities (e.g., trading app providers), or offering currency exchange services.

Expansion of supervisory authority: Under the final rule, CFPB expands its regulatory remit over nonbanks, which allows examinations of an organization's existing compliance and risk management related policies and procedures as well as broader records and business operations. This includes requesting relevant transaction-level data from supervised entities to assess their compliance with applicable Federal consumer financial laws.

Risk-based supervision: Now that the market has been defined, the CFPB has the authority to begin their supervision of larger participants to detect, assess, and address risks to consumers and markets. The CFPB's risk-based supervision program may include supervisory monitoring activities (e.g., inquiries regarding new products or compliance matters) or examinations. Supervisory monitoring may focus on complaints management, consumer payment disputes, fraud risk management, and third-party oversight programs.

5 considerations to evaluate

1. **Re-evaluate applicability:** It is important for organizations to understand if their current products or services meet the applicability of the final rule's revised definitions and gain visibility into their volume of in-scope transactions. Any prior analysis completed to understand the scope of transaction volume included in the larger participant test should be reassessed.

2. **Adapt compliance strategies and prepare for potential growth:** Organizations should continuously adapt their compliance infrastructure, strategies, and product features to ensure ongoing compliance with evolving regulations. In the era of open banking, an organization can experience rapid increases in payment transaction volume. Establishing a roadmap for potential CFPB supervision should be a part of any organization's long-term business planning.

3. **Maintain product roadmap visibility and assess compliance in product development:** Given the evolving nature of embedded finance, organizations should maintain visibility into their product and feature development roadmaps. The final rule emphasizes that merchants and marketplaces facilitating payments for their own goods or services, or for those on their platform, are not in scope. However, a peer payment feature within the app could meet the definition and trigger CFPB supervision as a larger participant.

4. **Assess compliance with consumer financial laws:** While nonbanks covered under this larger participant rule are already responsible for complying with consumer financial laws, the heightened scrutiny of CFPB supervision increases the importance of understanding applicable compliance obligations. Market participants should assess how consumer financial laws such as the Electronic Fund Transfer Act (EFTA); Gramm-Leach-Bliley Act (GLBA); and the statute prohibiting unfair, deceptive, and abusive acts and practices (UDAAP) apply to their products and services.

5. **Formalize compliance and risk programs:** To prepare for the CFPB's risk-based supervision program, a covered nonbank should consider enhancing its Compliance Management System (CMS) and governance related to compliance with federal consumer financial laws and consumer protection. Preparing for forthcoming supervisory monitoring activities by documenting risk management activities and developing processes for regulatory request management will be critical to help lessen the burden of supervision.

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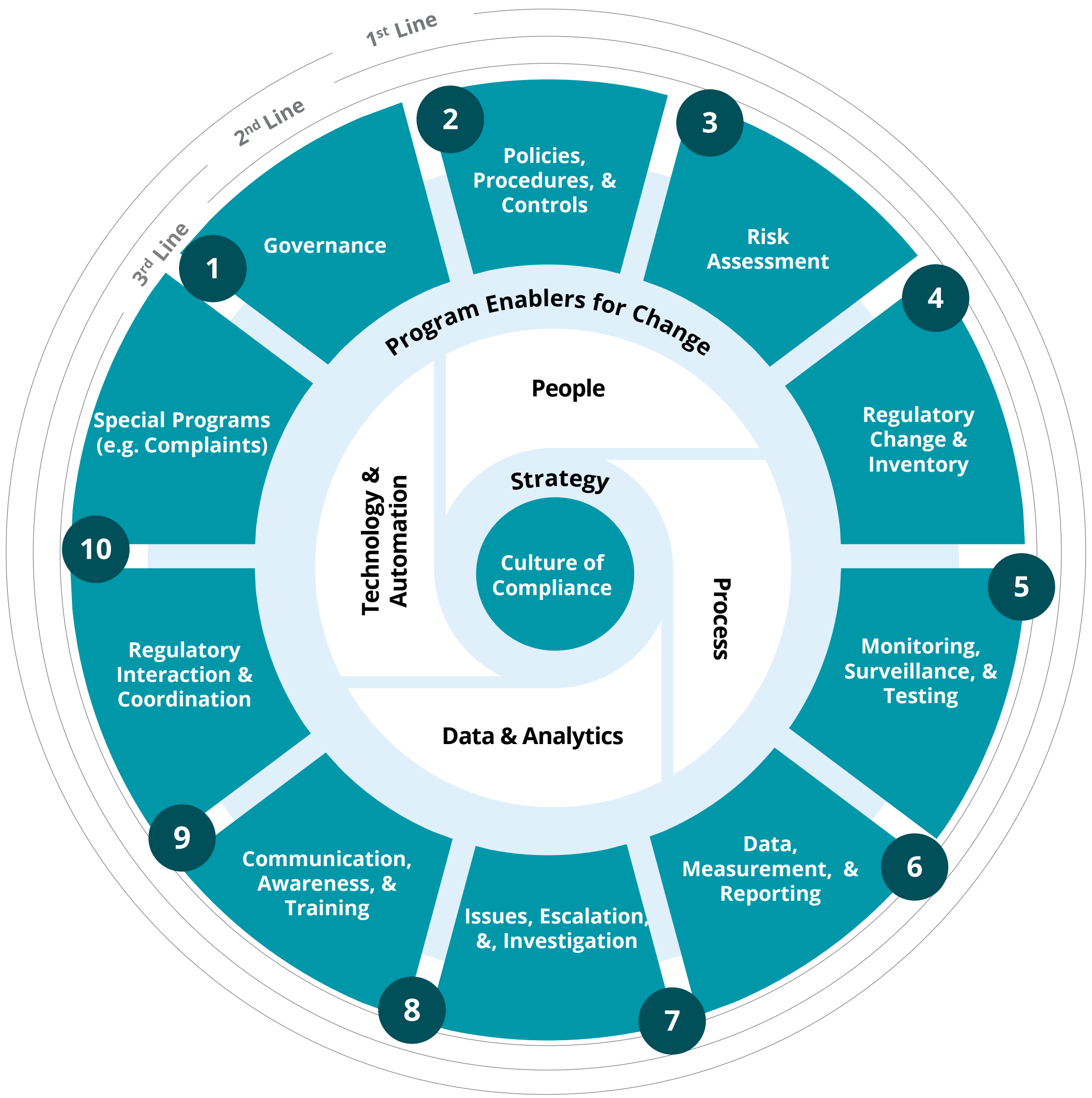

COMPLIANCE RISK MANAGEMENT FRAMEWORK

Organizations should incorporate the CFPB's latest rulemaking into their *compliance risk management framework*, with appropriate involvement from cross-functional stakeholders (e.g., legal, compliance subject matters experts, business function aligned compliance officers, and regulatory relations.)

KEY COMPONENTS

- **People**: Provide ongoing training programs, clearly define and communicate compliance roles and responsibilities, and provide for adequate staffing and resources.
- **Process**: Develop and maintain operating procedures to streamline compliance processes and provide for consistent workflow management. Establish clear process for identifying, reporting, and addressing compliance incidents.
- **Data & Analytics**: Develop key risk indicators (KRIs) to monitor potential compliance risks in real-time and utilize advanced analytics tools to provide insights into compliance performance and risks.
- **Technology & Automation**: Identify areas of automation to complete repetitive compliance tasks, reducing manual effort and error rates and leverage technology solutions to identify and respond to compliance-related incidents.

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Endnotes

[1] Consumer Financial Protection Bureau (CFPB), "CFPB finalizes Rule Defining Larger Participants of a Market for General-Use Digital Payment Applications", November 21, 2024.

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