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PAYMENT SYSTEMS AND DIGITAL FINANCIAL SERVICES

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This Technical Note was prepared in the context of a joint IMF-World Bank Financial Sector Assessment Program (FSAP) mission in Panama during June 2023 led by Richard Stobo, IMF and Emile van der Does de Willebois, World Bank, and overseen by the Monetary and Capital Markets Department. IMF, and the Finance, Competitiveness, and Innovation Global Practice, World Bank Group. The note contains the technical analysis and detailed information underpinning the FSAP assessment's findings and recommendations. Further information on the FSAP program can be found at www.worldbank.org/fsap.

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ACRONYMS

ABP	Asociación Bancaria de Panama
ACH	Automated clearinghouse
AICPA	American Institute of Certified Public Accountants
AIG	Autoridad Nacional para la Innovación Gubernamental (National Government Innovation Authority)
ACODECO	Autoridad de Protección al Consumidor y Defensa de la Competencia
AML/CFT	Anti-money laundering/countering financing of terrorism
ANTAI	Autoridad Nacional de Transparencia y Acceso a la Información (National Authority for Transparency and Access to Information)
BNP	Banco Nacional de Panama (National Bank of Panama)
CCF	Consejo de Coordinación Financiera (Financial Coordination Council)
CDD	Customer due diligence
CSD	Central Securities Depository
COTEL	Correos y Telégrafos de Panamá
CPMI	Committee for Payments and Market Infrastructures
CSIRT	Computer Security and Incident Response Team
DvP	Delivery vs payment
ENEF	Estrategia Nacional de Educación Financiera de Panama (Panama National Financial Education Strategy)
FATF	Financial Action Task Force
FCP	Financial Consumer Protection
FSAP	Financial Sector Assessment Program
FMI	Financial Market Infrastructure
GPSS	Global Payment Systems Survey
IMF	International Monetary Fund
INAMU	Instituto Nacional de la Mujer (National Women's Institute)
IOSCO	International Organization of Securities Commissions
KFS	Key facts statement
KYC	Know your customer
MICI	Ministerio de Industria y Comercio (Ministry of Industry and Commerce)
MIDES	Ministerio de Desarrollo Social de Panamá (Ministry of Social Development)
MEF	Ministerio de Economía y Finanzas (Ministry of Economy and Finance)
NBFI	Non-Bank Financial Institution
PAFI	Payment Aspects of Financial Inclusion
PCI-DSS	Payment Card Industry Data Security Standard
PFMI	Principles of Financial Market Infrastructures
PIRPS	Prominently Important Retail Payment System
RPP	Registro Público de Panamá (Public Registry Office)
RTGS	Real-time gross settlement

SIACAP	Sistema de Ahorro y Capitalizacion de Pensiones de los Servidores Publicos (Public Employees' Pension Fund)
SSNF	Superintendencia de Sujetos No Financieros (Superintendency of Non-Financial Subjects)
SSRP	Superintendencia de Seguros y Reaseguros de Panama (Superintendency of Insurers and Reinsurers)
SSS	Securities Settlement System
SBP	Superintendencia de Bancos de Panamá (Superintendency of Banks)
TN	Technical Note
TR	Trade Repository
UAF	Unidad de Análisis Financiero (Financial Intelligence Unit)
UNPYME	Unión Nacional de Pequeñas y Medianas Empresas
UPU	Universal Postal Union
USD	United States Dollar
VA	Virtual Assets
VASP	Virtual Asset Service Providers
WB	World Bank

EXECUTIVE SUMMARY¹

This technical note presents a high-level assessment of Panamanian payment systems and financial inclusion policies. It is based on the Payment Aspects of Financial Inclusion (PAFI) framework published by the World Bank and the Committee on Payments and Market Infrastructures (CPMI). In accordance with the framework, the situation in Panama is assessed in each of the seven key areas: (1) public and private sector commitment; (2) legal and regulatory frameworks; and (3) financial and ICT infrastructures; (4) appropriate product design; (5) wide-reaching access networks; (6) digital and financial literacy; and (7) digitalizing large-volume, recurrent payment streams. Information was gathered during the Financial Sector Assessment Program (FSAP) mission to Panama that took place from May 24 to June 6, 2023, supplemented by materials provided by stakeholders and the World Bank.

Financial inclusion in Panama has been growing, however, the country lags its geographical peers. According to Global Findex 2021, around 45 percent of adults in the country have a transaction account, which increased from 25 percent in a decade.² While there is not a significant gender gap in terms of account ownership, the urban-rural divide seems to matter. Very few Panamanians use their accounts to make digital payments. For example, in 2021, around 18.5 percent of Panamanian adults reported making an in-store digital payment, and 12.5% reported making a utility payment using an account. Overall, around 32 percent of adults own a payment card, and 36.5 percent of adults made or received a digital payment during 2021. Savings at and borrowing from a formal financial institution are low, around 15 and 10 percent of adults, respectively. In terms of access to finance by micro, small, and medium enterprises (MSMEs), Panama has the largest MSME finance gap in the region, with an estimated 43 percent of GDP (compared to the regional average of 20 percent).³

While authorities are committed to increasing access to financial services, that commitment is yet to be formalized. The two strategic documents intended to codify that commitment—the national financial education strategy and the national financial inclusion strategy—are in various

¹ This Technical Note has been prepared by Oya Ardic and Karol Karpinski, WBG. Sambhav Maheshwari (WBG) provided research assistance.

² Please note that Global Findex measures financial inclusion from a demand-side perspective. During the FSAP mission, Panamanian authorities and financial institutions noted that financial inclusion measured from a supply-side perspective implies much higher figures for financial inclusion. However, the supply-side data provided to the mission was incomplete (sourced from one financial institution which had a significant share of the market) and the FSAP team decided instead to use the data from Global Findex in the narrative of this technical note.

³ IFC MSME Finance Gap Database, April 2023.

stages of preparation and drafting. Coordination between stakeholders is hampered by the absence of a central bank and the presence of a large number of financial sector regulators. Aside from the Superintendency of Banks of Panama (SBP), it includes the Superintendency of Insurers and Reinsurers (SSRP), the Superintendency of the Securities Market (SMV), the Ministry of Industry and Commerce (MICI), the Consumer Protection and Competition Safeguarding Authority (ACODECO) and other entities. While the Financial Coordination Council (FCC) was created as an umbrella body for information sharing and cooperation, it does not cover payment systems or fintech. Consequently, it is recommended that the authorities create a fintech subcommittee within the FCC and establish a national payments council.

The legal framework governing payment systems and fintech is complex, while certain key areas remain completely unregulated. Panama has not enacted a payment systems law. Consequently, there is no regulator charged with payment system oversight or licensing payment service providers. On the other hand, there are at least eight legal acts identified that contain isolated provisions relating to payment systems, each of them using different concepts and definitions. That can result in market confusion and legal uncertainty, for example when the AML/CFT law uses terms such as “electronic money issuer” without defining it. Ensuring financial consumer protection is made more difficult by the complex rules separating the remit of ACODECO from that of the SBP, which are not legible for many consumers. It is therefore recommended that Panama adopt a comprehensive payment systems and services law, followed by a payment systems oversight framework and additional regulations, for instance on electronic money issuance. As Panama has no central bank that could become payment systems overseer and regulator, that role should be assumed by the SBP. Once these are established, in the medium term, Panama is also recommended to develop and implement a comprehensive financial consumer protection framework for banks and non-bank payment service providers. These should cover the specific risks that may arise due to digital financial services and fintech, with SBP as the regulator and supervisor.

Panama has established the key financial market and IT infrastructures, but their risk management must be improved. Given that Panama is a dollarized country without a central bank, the Banco Nacional de Panama (BNP) plays the role of the main settlement bank and the operator of the most important settlement system (BNP clearinghouse). After its 2019 upgrade, the clearinghouse is capable of functioning as a real-time gross settlement system (RTGS). That functionality, however, is not utilized, and settlement occurs during five daily clearing sessions. Only banks can become members of that infrastructure. To guarantee settlement, the SBP requires members to maintain a

minimal balance on their “special clearing accounts”, calculated based on their average gross outflows—this method, however, has its disadvantages. Retail payment systems are operated by Telered, a consortium of six banks, and include a cheque processing system, an automated clearinghouse (ACH) for direct credits and debits, an instant low-value payment system (ACH Xpress), a local ATM network and debit card scheme, as well as an account-to-account bill payments system.

The management of credit and liquidity risks in both the BNP clearinghouse and retail payment systems is limited. The ability of participants in the local debit card scheme (Clave) and the instant low-value payment system (ACH Express) to run potentially unlimited and uncollateralized net debit positions is an issue of particular concern. While it is not likely to pose immediate risk due to the existence of plentiful reserves on the books of the BNP, it could create issues in times of market stress. Hence, it is recommended that both the BNP and Telered should institute settlement risk management frameworks and clear procedures to be followed in the event of participant default. Moreover, the organizational separation between the BNP’s clearinghouse and its commercial banking operation should be completed in the short terms, and authorities should undertake an analysis of liquidity flow in the system and review the clearing and settlement services’ fee structure.

Until recently, Panamanian banks did not offer products specifically addressing financial inclusion. That changed with the launch of digital account products benefiting from simplified KYC rules, which have dramatically boosted account ownership, at least in rural areas. On the other hand, access to credit is still constrained, and hardly any products address the needs of micro, small and medium enterprises (MSME). For that reason, the authorities are recommended to include MSME financing as one of the themes of their national financial inclusion strategy (NFIS). They are also advised to facilitate interoperability among new mobile wallets and focus on improving digital payment acceptance by small merchants.

Financial access points, such as ATMs and POS terminals, are widely available, but concentrated in urban areas. Few commercial banks have a presence in rural areas, where connectivity issues further constrain the possibility of making and receiving digital payments. A major exception is Caja de Ahorros (the state-owned savings bank), which has been running its trailblazing agency banking program. Even their agent locations, however, are absent from the most remote communities, such as those in the Darien Province. COTEL, the national post service, is the only financial services provider present where others are not. However, its potential is wasted because of underinvestment: branches prepare their accounts with pen and paper, lack mobile or satellite connectivity, and employ committed but untrained staff. If rural communities get satellite connectivity and COTEL’s operations

undergo digital transformation, the access gap between urban and rural areas can be greatly reduced or even eliminated.

There are several additional opportunities for Panamanian authorities to use digitalization of government payments to incentivize digital payments and further financial inclusion. While there has been great progress in digitalizing certain government-to-person (G2P) payments, financial inclusion is not at the center of these efforts as a goal. Social assistance payments are made into closed loop accounts, eliminating leakage and enabling tracing of spending to understand beneficiary needs. However, this does not empower beneficiaries with a transaction account, which can be a steppingstone for financial inclusion. Most local government payments are made via checks and some by cash. Enabling and enforcing digital government payments and collections, especially government-to-business and business-to-government, can foster the digital payments landscape and improve merchant acceptance of digital payments, furthering financial inclusion.

The following table contains the full list of recommendations.

Table 1. Key Recommendations		
Recommendation	To be adopted by	I/ST/MT⁴
PUBLIC AND PRIVATE SECTOR COMMITMENT		
Establish a sub-committee under the Financial Coordination Council to coordinate regulation and supervision of fintech	SBP, SMV, SSRP, MICI	ST
Consider establishing a national payments council to foster collaboration and cooperation in the payment system	SBP with PSPs	MT
LEGAL AND REGULATORY FRAMEWORK		
Facilitate the urgent adoption of a law on payment systems and services	MEF	I
Amend other legal acts to align with the provisions of the new payment systems law provision and issue relevant implementing regulations	MEF, SBP	ST
Develop an oversight policy framework for covering payment systems and payment services reflecting the new legal mandate	SBP	ST
Establish a comprehensive stand-alone financial consumer protection (FCP) regulatory framework with a specific focus on the new risks to consumers due to DFS and fintech.	SBP	MT

⁴ I – Immediate (within 1 year), ST – Short term (within 1-2 years), MT – Medium term (within 3-5 years)

Observe local developments in trading of crypto-assets and monitor evolving international guidance from SSBs in this area before starting to regulate this field	SBP, SMV, MEF	ST
FINANCIAL AND ICT INFRASTRUCTURES		
Conduct a self-assessment of the BNP clearinghouse according to the Principles for Financial Market Infrastructures, including an analysis of system liquidity flows	BNP	I
Continue the separation of the BNP's clearing and settlement functions from commercial banking operations.	BNP	ST
Review the fee structure for clearing and settlement services	BNP, Telered	MT
Put in place a settlement risk management framework for deferred net settlement systems, including participant default rules and revised minimal balance requirements	BNP, Telered	I
Ensure risk-based access to payment infrastructure by non-bank payment service providers.	SBP, BNP, Telered	MT
Provide a RTGS-type service for high-value time-critical payments with a collateralized intraday liquidity facility	BNP	MT
Develop regional links with other Central American payment infrastructures	BNP, Telered	MT
Implement an endpoint security strategy	BNP, Telered, Latinclear	ST
Enforce member banks' compliance with funds availability rules	Telered	ST
Consider following reforms in credit information systems to enable digital credit: (i) secure use of APIs for information retrieval from Tribunal Electoral and the Public Registry of Panama; (ii) amendment to Law 24 of 2002 to enable the credit bureau to access additional information on the consumers, within the scope of Law 81 of 2019 on data protection for improved credit scoring; and (iii) encourage providers of credit to offer differentiated interest rates based on credit scores.	SBP, Tribunal Electoral, RPP, APC Intelidad	MT
PRODUCT DESIGN		
Encourage interoperability among e-wallets to foster further adoption of digital payments	SBP with PSPs	ST
Improve acceptance of digital payments by micro and small merchants via encouraging (i) low-cost acceptance solutions, (ii) acceptance intermediaries, (iii) provision of value-added services.	SBP with PSPs	ST
Implement policies to improving availability of credit information	SBP with APC Intelidad	ST
ACCESS POINTS		
Consider ways to improve connectivity in remote areas and foster agent-based models	AIG, SBP	ST

Consider digitally transforming the Post Office as a way of building access points in remote areas	Ministry of Government, COTEL	MT
AWARENESS AND FINANCIAL LITERACY		
Mainstream digital skills and digital risks as part of ENEF activities	SBP with ENEF stakeholders	ST
LARGE-VOLUME RECURRENT PAYMENT STREAMS		
Exploit further opportunities for financial inclusion through digitalization of government payments that are currently done by cash and checks	Local governments, MoF	MT
Reconsider the payment method for social assistance programs from a financial inclusion perspective	MIDES, AIG, SBP	ST
Encourage digitalization of international remittances	SBP, MICI	MT

INTRODUCTION

1. Safe and efficient payment systems and services contribute to financial inclusion and are foundational to systemic financial stability. The absence of a central bank in Panama, and the lack of a legal framework governing payments have resulted in specific challenges for the Panamanian national payment system, with implications for financial inclusion and financial stability. This technical note provides an assessment of the *Payment Aspects of Financial Inclusion* (PAFI) in Panama. In doing so, the note assesses the enabling legal and regulatory framework and the enabling infrastructure from a financial inclusion perspective. The note also adds fintech aspects relevant for financial inclusion as appropriate for the Panamanian context.

2. The rest of the report is organized around the seven guiding principles of the PAFI framework (CPMI and World Bank, 2016).⁵ For each guiding principle, the report first provides the context within which the assessment is done based on the PAFI framework (CPMI and World Bank, 2016 and CPMI and World Bank, 2020), the PFMIIs (CPMI and IOSCO, 2012), or on the good practices in the area of financial consumer protection (World Bank, 2017; World Bank, 2021). The report then provides a detailed description of the current situation of the issues underlying each guiding principle, including achievements and gaps. Suggested steps for authorities and other stakeholders to close the identified gaps follow in the recommendations sub-section.

3. This Technical Note is drafted by the World Bank based on written responses to questionnaires and supporting materials provided by relevant authorities, meetings that took place during the onsite mission of May 24 to June 6, 2023, with relevant agencies, supervisors and private sector representatives.⁶

⁵ Box 1 provides a description of the PAFI framework used in this report.

⁶ The mission met with Superintendencia de Bancos de Panamá (SBP), Banco Nacional de Panamá (BNP), Autoridad de Protección al Consumidor y Defensa de la Competencia (ACODECO), Asociación Bancaria de Panamá (ABP), Ministerio de Economía y Finanzas (MEF), Ministerio de Desarrollo Social (MSD), Caja de Ahorros, Caja de Seguro Social, Autoridad Nacional para la Innovación Gubernamental (AIG), Treasury, Post Office, PC Mayor's Office, Tribunal Electoral, Comptroller, CONEP/UNPYME, LatinClear, APC Intelidat, ANIFI and several private sector institutions including banks and non-bank payment service providers and fintechs.

Box 1 – Payment Aspects of Financial Inclusion

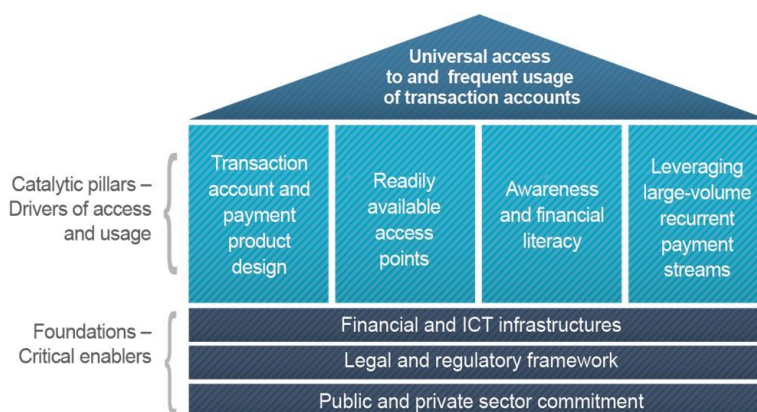
Based on the premise that financial inclusion starts with payments, the Committee for Payments and Market Infrastructures (CPMI) and the World Bank issued guidance on payment aspects of financial inclusion (PAFI) in 2016 (CPMI and World Bank, 2016). The PAFI report outlines seven guiding principles for public and private sector stakeholders and includes key actions for countries that wish to put these principles in practice. The PAFI framework has been used widely as the analytical underpinning for designing and implementing country-level actions and global efforts to improve access to and usage of transaction accounts with the ultimate goal of financial inclusion.

The PAFI report defines a transaction account as an account provided by regulated payment service providers (banks or non-banks) to make and receive payments, to safely store value, and to serve as a gateway to other financial services.

According to the PAFI framework, the three foundations of a sound enabling environment for financial inclusion include (1) public and private sector commitment; (2) legal and regulatory frameworks; and (3) financial and ICT infrastructures. Building on the enabling environment, four catalytic pillars drive access and usage: (4) appropriate product design; (5) wide-reaching access networks; (6) digital and financial literacy; and (7) digitalizing large-volume, recurrent payment streams. Figure 1 below illustrates the PAFI framework and the seven guiding principles.

In 2020, the CPMI and World Bank expanded the PAFI framework to include the fintech aspects, focusing on new technologies, new products and new access modes (CPMI and World Bank, 2020).

Figure 1. The PAFI Framework



Source: CPMI and World Bank, 2016.

I PUBLIC AND PRIVATE SECTOR COMMITMENT

A. Context

4. Financial inclusion requires a well-functioning retail payments ecosystem, which is characterized by a complicated balance between cooperation and competition, safety and efficiency issues, as well as specific regulations for innovative and inclusive payment schemes.

Fostering change in such an environment requires the ability to bring together diverse interests, launch policy research and development, change laws, mobilize funding to modernize financial infrastructures, and other similar requirements. Explicit, strong and sustained commitment from public and private sector organizations to broadening financial inclusion is indispensable if this agenda is to be effectively advanced.

5. A collaborative approach to payment system development is essential. Payment systems as core infrastructures are in constant evolution in terms of technology, regulatory frameworks and business processes as they adjust to the changing needs of the economy and the financial sector, especially in the context of digitalization. Successful implementation of strategies and industry-wide initiatives require support from a wide range of stakeholders.

6. Public sector authorities play a key role in creating an adequate enabling environment for financial inclusion in their respective jurisdictions. For example, many central banks are already working to better leverage the various roles they play in the retail payments space for this purpose.

7. Strong commitment from the private sector has also proved valuable in efforts to further the reach of transaction accounts that meet the needs of the unserved or underserved. In several cases, the industry has led the effort to provide basic accounts in their respective jurisdictions.

8. A collaborative approach to fintech is the key to achieving the full potential. First, fintech developments call for increased cross-sectoral coordination among regulatory authorities. Many fintech providers operate at the crossroads of various sectors (ICT, payments, etc.), which makes the interaction among different authorities necessary. Furthermore, to address challenges, customers might feel it is important that authorities understand and test fintech innovations to ensure that consumer protection and other legal and regulatory frameworks address potential risks. Regulators' initiatives such as sandboxes, innovation hubs, and innovation offices can foster the development of the fintech ecosystem. Lastly, collaboration among the private sector, specifically that between

traditional providers and fintech startups can enable further innovation and access to new markets and capital and can lead to a higher impact.

B. Status in the country

9. Panama does not have a central bank. It recognized the United States dollar as its legal tender shortly after its independence in 1903 and has been using it ever since. Banco Nacional de Panamá (BNP), a state-owned commercial bank founded on June 13, 1904, on the basis of its own Organic Law, has been performing some quasi-central banking functions—most importantly, acting as the government’s fiscal agent, managing the distribution of currency (in cooperation with the Federal Reserve System), and operating the payment clearinghouse and maintaining settlement accounts for all commercial banks operating in the country.

10. There are three main financial sector regulators in Panama: (1) Superintendency of Banks of Panama (Superintendencia de Bancos de Panamá, SBP) overseeing the activities of banks, (2) Superintendency of the Securities Market (Superintendencia del Mercado de Valores, SMV) regulating pension funds, investment funds and fund managers, and (3) Superintendence of Insurers and Reinsurers (Superintendencia de Seguros y Reaseguros de Panamá, SSRP) regulating insurance companies. The Financial Coordination Council (Consejo de Coordinación Financiera, CCF) was created in 2011 as an umbrella body (Law No. 67 of 2011) to improve information sharing and co-operation among the entities to oversee financial stability. In addition to the three regulators, Instituto Panameño Autónomo Cooperativo, Public Employees’ Pension Fund (Sistema de Ahorro y Capitalización de Pensiones de los Servidores Públicos, SIACAP), and the Ministry of Industry and Commerce (MICI)—the latter being the licensing authority for non-bank lenders, pawnbrokers, remittance services providers, credit information bureaus and leasing or factoring companies—are members of CCF.

11. The Panamanian financial sector is bank-centric with 66 banks accounting for 91 percent of financial sector assets. Banks operate under various licensing regimes, with the most common being a “general license” allowing for banks to operate internationally as well. There are also 176 financial companies registered by MICI, 159 pawn shops, 17 money remitters, and 122 leasing companies. There is no legislation to license or regulate non-bank financial institutions, including non-bank payment service providers or fintechs in Panama.

12. The Government created Autoridad Nacional para la Innovación Gubernamental (AIG) in 2009 by Law 65 of 2009 to plan, coordinate, issue guidelines, supervise, collaborate, support

and promote the optimal use of information and communication technologies in the public sector for the modernization of public management, to recommend the adoption of policies, plans, and national strategic actions. In developing and promoting new technologies to support the digital transformation, AIG aims to also provide access to opportunities offered by connectivity to all Panamanian citizens. In this regard, AIG is an important stakeholder for digitalization of payments and financial inclusion, specifically in the context of digitalization of government payments and collections.

13. Panamanian authorities have been working on developing strategic frameworks to improve financial inclusion. More specifically, SBP has led the effort to develop a national financial education strategy, ENEF (Proyecto de Estrategia Nacional de Educación Financiera de Panamá) in coordination and collaboration with several stakeholders, including Ministerio de Economía y Finanzas (MEF), Ministerio de Educación, Ministerio de Desarrollo Social, SSRP, SMV, Instituto Panameño Autónomo Cooperativa, Contraloría General, Autoridad de la Micro, Pequeñas y Medianas empresas, Autoridad de Protección al Consumidor y Defensa de la Competencia (ACODECO), MICI, Instituto Nacional de la Mujer (National Women's Institute – INAMU), Banco Nacional de Panama (BNP), Caja de Ahorros, Asociación Bancaria de Panama (ABP), and APC Intelidat (the credit bureau). In addition, SBP has been leading the efforts to develop a national financial inclusion strategy in collaboration with relevant stakeholders, which is planned for finalization in 2023.

14. No specific collaboration mechanism covering a broad range of public and private sector stakeholders exists on payments or fintech. ABP has a sub-group on payments methods, however, this does not include non-bank providers. While fintech developments have been nascent so far, this lack of broad-based collaboration may hinder the development of the sector in the future. At the same time, discussions on legal and regulatory reforms may benefit from broad-based collaboration across various public and private sector authorities, including banks and non-bank providers. For example, in 2022 and 2023, two law bills on virtual assets were drafted and adopted by the National Assembly, but ended up being vetoed by the President, as insufficient coordination among stakeholders resulted in the laws not meeting Panama's AML/CFT obligations.

C. Recommendations

15. In order to coordinate new initiatives related to fintech, SBP, SMV, SSRP and MICI should establish a sub-committee, consultative in nature, under the Financial Coordination Council (CCF) for regulation and supervision of fintech. A collaborative approach to fintech is key

to enabling transformative business models, mitigating risks, and making an impact on financial inclusion. Such a collaborative body is also a key mechanism for implementation of a financial inclusion strategy. As many fintech providers operate across several sectors (e.g., ICT, payments, credit), interaction among different authorities is necessary. Furthermore, it is important for authorities to understand DFS and fintech innovations to ensure that consumer protection and other legal and regulatory frameworks are in place to mitigate potential risks. A collaborative approach to fintech development can enable further innovation, leading to a higher impact. As a coordination mechanism in the financial sector already exists (CCF), SRP, SMV, SSRP and MICI are recommended to utilize this mechanism to establish a sub-committee under the CCF for the purpose of information exchange, monitoring and enabling fintech. This sub-committee can later on become the coordination mechanism under the financial inclusion strategy upon its launch, and can be instrumental in its development.

16. Panamanian authorities should also consider establishing a national payments council (NPC) to foster collaboration and cooperation in the payment system. An NPC is a structured organization which focuses on the development of a safe and efficient national payment system that meets the evolving needs of a country. An NPC is usually led by the central bank and has relevant public and private sector stakeholders as participants to facilitate the dialogue. In the absence of a central bank in Panama, the establishment of the NPC can be led by the SBP, which is the public authority recommended in this note for the role of the regulator and supervisor of the national payment system. This would require the need to allocate resources and build capacity within SBP.

17. SBP is recommended to publicly launch the ENEF, and to develop and publicly launch the financial inclusion strategy in a timely manner. ENEF has been developed, but not publicly launched, and a financial inclusion strategy is planned. It is important to finalize these strategies publicly to ensure commitment, accountability and proper resource allocation for implementation.

II LEGAL AND REGULATORY FRAMEWORK

A. Context

18. As recognized in CPMI and World Bank (2016), the legal and regulatory framework of a country plays a critical role in creating an enabling environment for inclusive payment services.

Retail payment services involve a complicated mix of infrastructures, networks and services with both public and private sector investment, and benefit from varying degrees of competition and collaboration, as well as standardization and innovation. In addition, adequate risk management, mitigation of fraud, abuse and protection of consumer interests are key supervisory and oversight considerations.

19. The increasing array of new products, often offered by new entrants and/or without in-person end user support, might make it difficult for end users to establish the necessary trust to adopt financial services. Especially underserved and unserved groups might feel more confident if a sound framework is in place that protects consumers, their data and funds, and is able to cope with fintech developments. In this regard, competition is the key to innovation and fintech development.

20. Banks are no longer the only providers of payment services, a fact that had to be reflected in laws, regulations and licensing frameworks. While there is considerable heterogeneity in the way in which general payment system concepts are implemented in domestic legislation, nearly every law makes the distinction between the following two concepts:⁷

- **Payment systems**, understood as the rules, technical infrastructures and other arrangements allowing financial market participants, such as commercial banks and non-bank financial institutions (NBFI), to transfer funds, and clear and settle obligations between one another.
- **Payment services**, understood as services such as electronic money issuance, third-party card processing, bill payments or domestic and international remittances—the exact list of what constitutes a payment service depends on the country concerned.

⁷ In line with the terminology used by most global standard-setting bodies, this note will use the names "payment system" and "payment service" to refer to, respectively, the first and the second concept. However, that nomenclature is not universal. Please see Annex II for further details on regulating and supervising payment systems and services, including examples from other jurisdictions, and definitions of other relevant and frequently used concepts.

21. Just as laws and regulations applicable to payment systems have evolved in response to changing markets and emerging risks, so did authorization procedures for payment system operators and payment service providers. Authorizing such entities was considered redundant earlier—it was assumed that, since they provide services to commercial banks, indirect oversight through banking supervision departments would be sufficient. This is no longer the case, and payment systems and services are licensed, supervised, and overseen.⁸

22. Typically, central banks play the leading role in licensing, supervision and oversight of payment systems and payment services. Institutional arrangements for this purpose vary across jurisdictions. Latin America in particular is characterized by the institutional division between central banks and banking regulators (superintendencies); only very few jurisdictions have adopted the unified regulator model. As a consequence, banking regulators play a relatively more important role in the payments ecosystem, particularly with respect to licensing and supervision of payment service providers.⁹ On the other hand, the current division of those responsibilities still leaves a number of issues in a regulatory void, and may be unsustainable in the long run.

23. Fintech developments may challenge the applicability of traditional oversight concepts and standards. It is important to ensure that the existing legal and regulatory requirements do not discriminate against the use of a particular technology or disregard the use of technologies altogether. From the perspective of payment services oversight, it is critical to ensure the overall safety and integrity of a payment infrastructure. The involvement of a large number and type of providers (e.g., intermediaries, third-party service providers, etc.) may lead to new types of risks. Oversight frameworks need to be designed or updated to take these into account. In this regard, technologies can support authorities in fulfilling their supervisory and oversight tasks and market participants in meeting requirements more effectively and efficiently.

24. In the last few years, digital assets or crypto-assets¹⁰ have spurred intense policy and regulatory debate in the world due, in part to the significant risks, as well as the potential benefits. In a 2019 communiqué, the G20 acknowledged the benefits of technological innovations,

⁸ Annex II provides examples on licensing procedures from other jurisdictions.

⁹ Annex II includes further information on licensing authorities.

¹⁰ FSB (2020) defines digital assets as a digital representation of value which can be used for payment or investment purposes, which does not include digital representation of fiat currencies; and crypto-assets a type of private sector digital asset that depend primarily on cryptography and distributed ledger or similar technology. FATF (2021) defines a virtual asset as a digital representation of value that can be digitally traded or transferred and can be used for payment or investment purposes. Virtual assets do not include digital representations of fiat currencies, securities and other financial assets that are covered elsewhere in the FATF Recommendations (2012).

including those underlying crypto-assets, while warning against its risks particularly related to consumer and investor protection, anti-money laundering (AML) and countering the financing of terrorism (CFT) as well as financial stability risks albeit currently limited.¹¹ In response, international standard setting bodies (SSBs) have conducted analysis, revised standards and/or issued guidance as appropriate. Overall, SSBs call for taking an activity-based and functional approach by applying extant standards and regulations when crypto-assets perform an existing regulated function or activity – for example as securities or as means of payment. Meanwhile, at national level, authorities across the world have been taking different approaches and some have embarked on comprehensive regulatory efforts. Due to the nature of crypto-assets and markets, SSBs call for cross-border cooperation, coordination, and information sharing.¹²

25. The following seven key aspects of the legal and regulatory framework are analyzed in detail as key elements: (i) licensing and oversight of new non-bank providers and business models; (ii) regulatory proportionality, neutrality and predictability; (iii) risk management; (iv) protection of customer funds (including both deposits and e-money customer funds); (v) financial consumer protection and transparency, also including data frameworks to ensure data privacy and protection as well as consent; (vi) financial integrity; and (vii) competition in the sector.

B. Status in the country

26. Panamanian regulatory framework for payment systems is characterized by a patchwork of piecemeal laws and regulations leaving significant gaps in their coverage. This creates confusion among regulators and market participants, forcing both to rely on ad-hoc arrangements and procedures. While the Principles for Financial Market Infrastructures (PFMI) prescribe that “FMIs should be subject to appropriate and effective regulation, supervision, and oversight by a central bank, market regulator, or other relevant authority”, regulation, supervision and oversight of payment systems are present in a very rudimentary form, if at all. The absence of a comprehensive law regulating payment systems and financial infrastructures has been the main reason behind the

¹¹ [Communiqué](#), G20 Finance Ministers and Central bank Governors Meeting, Fukuoka. (Jun.8-9,2019)

¹² Caution is warranted before drawing conclusions about many aspects of crypto-assets as international policy making and experience is still fast evolving. FATF (2021) has issued guidance on the treatment of crypto-assets under AML/CFT policies and legal and regulatory framework. The FATF guidance reiterates existing standards and calls for their mandatory application for crypto-assets as well. The Basel Committee on Banking Supervision (BCBS) issued guidance on the prudential treatment of crypto-assets in December 2022 (BCBS 2022) for banks to monitor and manage their exposure to crypto-assets. FSB has just issued on guidance on regulation, supervision, and oversight of crypto-asset activities and markets (FSB, 2023a, 2023b and 2023c). IOSCO provides guidance on risks with respect to crypto-asset trading platforms and investor education (IOSCO 2020a and 2020b). Further work on this by SSBs is in progress.

situation. In that, Panama is becoming an outlier among Latin American jurisdictions, as several of them have already enacted the relevant legislation (see [Table](#)).

Table 2. Other Latin and Central American jurisdictions with laws (primary legislation) concerning payment and settlement systems.

Country	Details
Belize	National Payment System Act (2017)
Brazil	Brazilian Payment System Law (Law 10.214 of March 27, 2001)
Colombia	Decree 1692 of December 18, 2020 (concerning retail payments only)
Honduras	Law on Payment and Securities Settlement Systems (Decree 46-2015 of September 14, 2015)
Mexico	Law on Payment Systems of December 12, 2002
Paraguay	Law on Payment and Securities Settlement Systems (Law 4595)
Peru	Law on Payment and Securities Settlement Systems (Law 29440 of November 19, 2009)
Uruguay	Law on Payment and Securities Clearing and Settlement Systems (Law 18573 of September 13, 2009)

Source: World Bank staff compilation.

27. While there is no law specifically covering payment systems, some related provisions are present in other legislation. These include:

- **The Banking Law (consolidated text published by the Executive Degree 52 of April 30, 2008).**
The act creates the Superintendency of Banks and grants it the necessary powers for licensing, regulation and supervision of commercial banks. While it does not feature any sections specific to payment systems, it does allow the Superintendency’s Board of Directors to issue “technical standards” required for the compliance with the law—a power that has been used, for example, to standardize the format of cheques. In Article 54, it grants the Superintendency the powers to issue regulations pertaining to banks’ business continuity. Finally, it refers to “the Clearinghouse”

("la Cámara de Compensación") in two contexts: including the balances in the Clearinghouse in the calculation of banks' liquid assets and, in the event of insolvency, granting seniority to the unpaid obligations resulting from Clearinghouse netting (although of priority below that of secured debt). It is presumed that the term refers to the clearinghouse operated by the Banco Nacional, although it is not explicitly defined.

- **The Organic Statue of the Banco Nacional de Panamá (consolidated text published by the Executive Decree 4 of January 18, 2006).** Article 10 of the law specifies that "the Exchange¹³ and Clearinghouse of the national banking system" shall operate "under direction and responsibility of Banco Nacional de Panamá", and the Banco Nacional's Board of Directors "has the powers to regulate its operations and functioning". Furthermore, Article 5 prevents the bank from levying fees on most services provided to the government and its agencies, while Article 8 imposes the requirement on all public authorities, unless exempt by a separate law, to deposit all their funds with the Banco Nacional. Finally, Article 3 provides explicit state guarantee for all obligations and liabilities of the BNP.
- **Law on the Securities Market in the Republic of Panama and the Superintendency of Capital Markets (consolidated text published by the Executive Decree 1 of July 8, 1999).** Article 49 of the law contains the definition of "securities clearinghouse" ("central de valores"), entities performing the functions of both central securities depositories and securities settlement systems, which are to be licensed by the Superintendency of Capital Markets. According to Article 199, those clearinghouses can become members of the BNP-operated clearinghouse, subject to the rules laid down by the Board of Directors of the Banco Nacional de Panamá. The law also contains a clause providing qualified bankruptcy remoteness of pledged collateral, although its robustness is uncertain.
- **Law on the Protection of the Rights of Holders of Credit Cards and Other Payment Cards (Law 80 of December 31, 2009).** The law defines the concept of credit and debit cards and extends a number of consumer rights to their holders. It also forbids merchants to add markup on card purchases to cover the processing fee and mandates the Consumer Protection and Competition

¹³ In this context the word "exchange" ("el canje") refers to the exchange of cheques and other payment instruments.

Safeguarding Authority (ACODECO) to publish a comparison of interest rates and other fees charged by credit card issuers.

- **Law Regulating the Operations of Money Remittance Houses (Law 48 of June 23, 2003).** The law defines the concept of money transfer service, requiring providers of that service to obtain a license for the Directorate of Financial Companies at the Ministry of Commerce and Industries. It also contains a licensing exemption for already licensed banks, as well as the post office. Finally, it requires the licensing body to perform at least one inspection (examination) of each licensee over the course of the year.
- **Law Adopting Measures for the Prevention of Money Laundering, Terrorism Financing, and Financing of Proliferation of Weapons of Mass Destruction (Law 23 of April 27, 2015).** Article 4 of the law defines “electronic transfer”, while Article 22 of the law lists “issuers or processors or debit, credit and pre-paid cards” and “entities issuing payment instruments and electronic money” among “financial reporting entities”, supervised by the Superintendency of Banks for the purpose of AML/CFT prevention. The scope of the supervision is outlined in Article 20. On the other hand, remittance service providers—together with the post office, exchange houses, the Agricultural Development Bank and the National Bank of Mortgages—are listed in Article 23 as “non-financial reporting entities” and are subject to the AML/CFT supervision of another body—the Superintendency of Non-Financial Institutions.
- **Law Amending Articles of Law 76 of 1976 on Tax Measures (Law 256 of November 26, 2021).** The act requires businesses, other than those exempt by the law, to issue electronic invoices through the Electronic Invoicing System of Panama.
- **Law Outlining the Norms Regarding Consumer Protection and Safeguarding of Competition (Law 45 of October 31, 2007).** While the act covers consumer protection in all sectors of the economy, it contains provisions specific to financial services. For example, Article 73 refers to revolving credit accounts (mainly credit cards), specifying the minimal disclosure standards for such products.
- **Law on the Protection of Personal Data (Law 81 of 2019).** The act regulates the processing of personal data, outlining principles that entities making use of such data—companies, government

agencies and individuals—need to follow, as well as the rights of persons whose personal data are being processed.

- **Law Defining and Regulating Electronic Documents and Electronic Signatures (Law 51 of 2008).** This law introduced the concept of electronic signatures and electronic circulation of documents to the Panamanian legal system.

28. Furthermore, many pieces of secondary legislation—regulations, circulars and decisions (acuerdo)—issued by relevant regulators have impacted the payments services market. Among those, the rule 001-2013 of January 8, 2013 issued by the Superintendency of Banks, establishing the simplified Know-Your-Customer process for low-risk accounts, has had the greatest impact in creating enabling environment for financial inclusion.

29. The Panamanian authorities have recognized the need for payment-specific legislation. However, approaches to creating a regulatory framework for payment systems differed across stakeholders. Panamanian lawmakers adopted the “crypto law” (Bill 697 of 2021), which combined provisions relating to the inclusion of blockchain technology in Panama’s digital agenda (Title II) and the regulations on the use of crypto assets (Title III) with a comprehensive regulatory framework for the national payment system (Title IV), regulating the licensing of payment system operators and payment service providers, as well as granting the Superintendency of Banks the powers of supervision and oversight. The law, however, was vetoed by the President in June 2022 because of concerns about its provisions pertaining to digital assets with Panama’s AML/CFT obligations agreed upon with the Financial Action Task Force (FATF). After the bill was resubmitted, the President referred it in January 2023 to the country’s supreme court as potentially unconstitutional. In accordance with Panama’s constitutional norm, the law remains ineffective pending the court’s decision.

30. In parallel to the laws submitted to the National Assembly and vetoed by the President, there were other attempts at drafting comprehensive payment system acts. The Superintendency of Banks worked together with the Inter-American Development Bank (IDB) team on preparing a draft of a payment systems law that would not include the contentious cryptocurrency provisions. Other proposals have been developed by the Banco Nacional de Panamá. Nonetheless, none of them has been tabled in parliament.

Licensing and oversight

31. Because of that legal vacuum, payment systems and payment services in Panama are effectively unlicensed and unregulated. The only operator of a payment system with clearly defined legal standing is the Banco Nacional de Panamá, as its authority to operate the clearinghouse stems directly from its Organic Law. Operation of any other payment systems, such as direct credit, direct debit and local card schemes managed by Telered, is not a licensed activity. The same applies to payment services such as electronic money issuance or merchant acquisition.

32. Nonetheless, there are some provisions in various laws that are tangentially related to payment systems and payments services. While they do not provide for effective regulation, they still manage to confuse market participants and consumers. Such provisions are spread across multiple laws, outlined in the earlier part of this chapter. Many of those laws lack appropriate definitions of the concepts they use; in other cases, the interpretation of those definitions is a matter of contention.

33. The application of the AML/CFT law exemplifies the problem. The act (Law 23 of April 27, 2015) is the only piece of legislation in the country that uses terms such as “electronic money issuer”, “issuer of payment instruments” or “card processor”. However, those terms are not defined and as result, the market lacks clarity on which providers and services those provisions apply to. What is even more concerning, payment service providers’ registration with the Superintendency of Banks for the purpose of AML/CFT compliance may be confused—by market participants and the public alike—with a proper licensing and prudential supervision mechanism. As a result, users may mistakenly think that the risk involve in the use of such services is low, even though the SBP’s mandate for them is strictly limited to AML/CFT matter, leaving them unregulated and unsupervised with respect to credit, liquidity, operational and business risk management, or with regards to consumer protection.

34. Payment systems oversight is not performed. While the SBP, as the prudential supervisor of banks, occasionally performs supervision and issues regulations pertaining to the use or provision of payment services by commercial banks, it does not extend to performing oversight over payment systems as such. There are no legal or regulatory provisions granting any authority oversight powers, and the matter of responsibility for payment systems oversight is controversial: aside from the SBP, the BNP interprets its statutory authority to operate the clearinghouse, and the special role as the fiscal agent of the government operating with the latter’s full guarantee, as predestining it for the role of the lead payment systems overseer in the country.

Regulatory proportionality, neutrality and predictability

35. The large number of laws and regulatory agencies is not conducive to regulatory proportionality, neutrality and predictability. Regulation of financial service providers is, by large, conducted in the entity-based (rather than activity- and/or risk-based) manner. For example, there are fairly detailed laws regulating the issuance of credit and debit cards, but similar products that do not use the card technology remain unregulated. Because the market is regulated by multiple organizations, ensuring timely and relevant flow of information between them is challenging.

36. Access to payment systems and financial market infrastructures is generally limited to commercial banks. Only them, as well as operators of securities settlement systems, are currently able to directly participate in the BNP clearinghouse and systems operated by Telered. There are differing views on whether granting non-banks access to the former would require amendments to the BNP Organic Law, or whether regulatory measures would be sufficient. Because Panama does not issue its own currency, extending the access to payment systems to non-banks is less likely to create unforeseen consequences with respect to money creation and monetary policy.

Risk management

37. There are no regulatory standards pertaining to risk management by payment system operators and payment service providers. While the authorities are familiar with the Principles for Financial Market Infrastructures (CPMI and IOSCO, 2012), none of the key payment systems has been formally assessed. While the legal void resulted in the lack of formal regulatory standards, operators of the key payment systems—BNP and Telered—have been undertaking several initiatives aimed at improving their operational risk management practices, including business continuity planning and regular business continuity exercises. It should be underlined that while BNP is a supervised bank, and therefore subject to some rules pertaining to capital adequacy, operational risk and other aspects, as defined by the SBP, the regulatory void with respect to Telered is complete.

Protection of customer funds

38. Panama does not operate a deposit insurance scheme. On the other hand, state-owned commercial banks—BNP and Caja de Ahorros—benefit from an explicit government guarantee of all their liabilities, outlined in their respective organic statutes enacted by the National Assembly. Furthermore, funds deposited in either of those banks benefit from protection against garnishment, up to ten thousand dollars, with the exception of tax and social security liabilities and child support or alimony debt.

39. There is no mechanism for the protection of consumer funds with respect to electronic money issuers. Since provision of payment services is effectively unregulated, there are no limits on what non-bank electronic money issuers can do with their customers' money, as long as they do not engage in financial intermediation as defined in the banking law. Consequently, providers can co-mingle their customers' funds with their own cash accounts used for operational purposes. They are also not prohibited from investing those funds, even if such investments pose significant risks.

Financial consumer protection and transparency

40. Panama has made significant progress in enacting financial consumer protection measures, but the complex patchwork of laws and institutions may limit their efficiency. The SBP is responsible for financial consumer protection with respect to products and services offered by commercial banks (with "exclusive jurisdiction", according to Article 198 of the Banking Law, which simultaneously exempts banks from certain provision of the Law 45 of October 31, 2007), while ACODECO is the authority in charge of non-bank institutions. As far as commercial banks are concerned, consumer protection measures are applicable only to individuals purchasing one of the four financial products defined in the law: consumer loans (up to 50 thousand dollars), home loans (up to 125 thousand dollars), demand deposits (current or checking accounts; up to 20 thousand dollars) and savings accounts (up to 50 thousand dollars). They are also applicable to micro- and small enterprises with respect to commercial loans not exceeding 200 thousand dollars. On the other hand, there are no exclusions with respect to ACODECO's mandate regarding non-bank institutions, as Article 32 of the Law 45 of October 31, 2007, specifies that protection is extended "to all consumers of *final* goods and services"), and the definition of consumer in Article 33 encompasses both individuals and enterprises ("legal persons").

41. While the division of responsibilities between SBP and ACODECO may appear clear-cut—the former dealing with banks and the latter covering non-bank institutions—the situation is more complex. Based on the Banking Law and the Consumer Protection Law, it is the exclusive power of ACODECO to declare parts of contracts between consumers and banks null and void, based on the provider's use of a prohibited clause. At the same time, ACODECO must take into account the list of prohibited clauses listed in the Article 202 of the Banking Law, as well as other norms issued by the SBP. Furthermore, ACODECO maintains its exclusive jurisdiction over misleading advertising practices.

42. Applicable dispute resolution procedures differ between banks and non-banks. Only banks are required to develop an internal complaint handling procedure. If the complaint has not been resolved internally within thirty days, the consumer can appeal to the SBP through its out-of-court formal dispute resolution mechanism. However, the jurisdiction of the SBP is limited to disputes where the amount in question does not exceed 20 thousand dollars. By mutual consent of the consumer and the bank, the SBP can also act as an arbitrator in other disputes.

43. Non-banks are generally not required by law to have complaint handling procedures in place. Non-bank credit card issuers are an exception to this rule, as such a requirement is imposed on them by the Credit Card Law. Consumers of non-bank financial products can submit their complaints directly to ACODECO. The agency investigates the complaint and, as a first step, conducts mediation between the consumer and the provider. If that does not resolve the situation and the financial amount in dispute does not exceed 2,500 dollars, the agency resolves it through administrative procedure, which involves a hearing, at which parties can submit evidence, and concludes with a binding decision by the ACODECO director or a designated official. Consumer disputes concerning higher amounts are resolved in courts (“judicial procedure”), where ACODECO may represent the complainant.

44. The existence of multiple authorities and dispute resolution channels may be confusing to consumers. Based on the FSAP teams discussions with ACODECO, it seems that it is a common occurrence for consumers to complain to ACODECO with respect to matters that are within the scope of the SBP’s mandate. This is naturally reflecting ACODECO’s larger footprint: the organization has 12 branch offices around the country, not including its “mobile unit”—a truck travelling the country to deliver training on consumer rights in more remote locations. The agency is also active on social media and messaging apps: for example, it launched a WhatsApp complaints hotline. On the other hand, the awareness of the SBP out-of-court formal dispute resolution mechanism is more limited: banks rarely display information about it in a prominent manner, be it in their branches or within internet banking or mobile apps.

Figure 1: ACODECO's mobile training unit.



Photo by ACODECO.

45. The Banking Law, the Credit Cards Law, and the Consumer Protection Law contain the list of key terms and conditions that financial services contracts need to contain. They include , for instance, the statement of charges and fees, the annual percentage rate for credit products, payment deadlines, as well as the manner in which the financial institution will communicate changes to the contract. With respect to products offered by banks, the law requires the SBP to review “model contracts” for standard deposit and loan products and, if needed, order the bank to amend them to comply with laws and regulations. However, financial institutions are not required to provide standardized key fact statements (KFS) describing the main characteristics of their products. The absence of KFSs is partially compensated by the comparison of credit card products published annually by ACODECO; similar measures are, however, not undertaken with respect to any other products.

46. While there are no separate regulations pertaining to privacy and personal data protection in the financial sector, all institutions are bound by the Law on the Protection of Personal Data (Law 81 of 2019). Everybody whose personal data is processed has the right to: (1) be informed about data processing; (2) access any personal data processed by another party; (3) rectify incorrect information; (4) request erasure of that data, if there are well-founded and legitimate reasons; (5) receive a copy of the data in a format that ensures portability and (6) not be subjected to purely automated decision-making, if it could infringe upon one's legal rights.

Data protection and privacy

47. Panama has a data protection legislation in place, which is similar to the European Union's General Data Protection Regulation (GDPR). Law no 81 of 2019, supplemented by Executive Decree 285 of 2021, governs the principles, rights, obligations and procedures applicable to the protection of personal data, including provisions on privacy, consent, access, cancellation and portability. Autoridad Nacional de Transparencia y Acceso a la Información (ANTAI) is the regulator for data protection. The general data protection regime also applies to financial institutions. However, protection of credit history is governed by a "specialized law" (Law 24 of 2002, subsequently amended), which grants supervisory powers to MICI, ACODECO, and relevant tribunals.

Remittances

48. International remittances are regulated by the SBP, MICI and Unidad de Análisis Financiero (UAF, the Financial Intelligence Unit). Money remitters must obtain a license of operation from the MICI's Directorate of Financial Companies according to Law 48 of 2003. They also need to register with the SBP according to the *Prevention Agreement for Other Financial Obligators* No. 001-2018 for the purposes of prevention of money laundering, financing of terrorism and financing of the proliferation of weapons of mass destruction. Money remitters are responsible for suspicious transaction reporting to the UAF, and they report to SBP for AML/CFT purposes. There is some duplicity in these reporting requirements, which can possibly be streamlined for efficiency in reporting.

Financial integrity¹⁴

49. SBP Rule 1 of 2013 establishes the rules for the basic account regime in Panama, which has recently been instrumental in two Panamanian banks starting to offer specific digital

¹⁴ This topic is dealt with in detail as part of the Panama FSAP in the Technical Note on *Anti-Money Laundering and Combating the Financing of Terrorism (AML/CFT)*.

payment products. The rule defines “simplified process accounts” as those individual accounts opened by residents, expressed in national currency, with a B/. 1,000 as a limit on balance and a B/. 1,500 limit on cumulative monthly deposits and withdrawals. These limits were recently increased by SBP to B/. 5,000. Offering of these accounts by banks is not mandatory. In order to open a simplified process account, an ID card is needed as well as an up-to-date address provided by the client. The bank opening the account must verify the client’s ID within 30 days of opening the account. The process of account opening can take place online.

50. Measures of preventing money laundering and financing of terrorism are governed by Law 23 of 2015 in Panama. Article 22 of Law 23 lists the reporting entities subject to AML/CFT obligations. This list requires further clarification in the context of provision of payment services by non-banks. More specifically, Article 22.1.f limits the coverage of payment processors to card processors only, not acknowledging non-card payment instrument processors. Article 22.1.g is on institutions issuing payment means and e-money, which are currently not regulated or supervised in Panama for purposes other than AML/CFT.

Competition

51. Even though the Panamanian law contains anti-monopoly provisions (Law 45 of October 31, 2007), their application to the financial sector has been sparse. The confusion between the mandates of ACODECO and the SBP may have contributed to the problem: for instance, ACODECO’s predecessor—CLICAC—took the Superintendency to court in 2004 after its request for banking sector data was rejected; the case, after multiple appeals, ended in the Supreme Court, which sided with the competition agency. The fact that such a clash between regulators could have taken place suggests that banking and competition laws were sufficiently ambiguous.

52. Nonetheless, competition and market power issues may be present in the market. Non-bank fintechs reported difficulties with opening bank accounts and accessing financial infrastructures, while new closed-loop payment schemes may end up as de facto monopolies thanks to their network effects.

Digital assets

53. There were no crypto asset service providers, issuers, or trading platforms domiciled in Panama at the time of the drafting of this technical note, based on the discussions with several providers and regulators. Anecdotal evidence suggests that there are only a limited number of customers conducting crypto asset transactions through exchanges abroad.

54. There are no requirements imposed by SBP on banks acquiring exposures to crypto assets, engaging in crypto asset services and/or intermediating in crypto asset services. One Panamanian bank has been providing services to its customers in the past few months to safely access a US crypto asset service provider via its trust account, monitoring specifically for suspicious transactions. The bank has approximately 150 customers who conducted transactions totaling \$30m in the 10-month period. At the same time, two bills of law had been debated and approved by the Congress in 2022 and 2023, but both bills were vetoed by the President of the Republic of Panama mainly due to various concerns including operational, regulatory and supervisory aspects, risk management issues, and AML/CFT concerns. Following the last veto, the bill of law was sent to the Supreme Court for consideration.

Box 1. Banco Nacional de Panama

As the oldest financial institution in the country, the government's fiscal agent, and the operator of the main settlement system, Banco Nacional de Panama (BNP) is one of the most important national payment system stakeholders. It is imperative that it be given a significant role in shaping the national payment system development and contribute, on a regular basis, to strategic decisions. Does its central role also mean that it should play role in payment system oversight and supervision of payment system operators?

The answer, based on thorough research and expert consultations, is no.

The FSAP team has considered the special situation of Panama—in particular, the fact that it does not have a central bank. While it is indeed uncommon—even other dollarized economies such as El Salvador or East Timor have established their own central banks—Panama is not the only country in such a situation. Other jurisdictions without a central bank, such as Andorra or Liechtenstein, assign the powers to license and oversee payment systems to their banking or financial market regulators: the Andorran Financial Authority and the Financial Market Authority Liechtenstein. Furthermore, we examined institutions similar to the BNP in nature: state-owned banks with the full government guarantee, acting as fiscal agent of the government. Those include, for example, the National Bank of Liechtenstein (Liechtensteinische Landesbank) during its existence as a statutory organ of the government, or the newly founded Faroe Islands' National Bank (Landsbanki Føroya). In none of those cases did the government bank's authority extend to the oversight of payment systems. Further still, in countries where large-value or real-time gross settlement (RTGS) systems are operated outside the central bank, such as Canada (Payments Canada) or Hong Kong (Hong Kong Interbank Clearing Limited), those operators are not given any oversight powers. Finally, being responsible for printing or distribution of banknotes does not, by itself, grant any such powers, as exemplified by the Bank of Scotland, the Royal Bank of Scotland, and Clydesdale Bank (in Scotland); Bank of Ireland, Danske Bank and

Ulster Bank (in Northern Ireland); and HSBC, Bank of China and Standard Chartered (in Hong Kong SAR, China).

This is because the power to oversee does not come from operating a payment system. The prominent role that central banks play in payment system oversight had its roots elsewhere. The first consideration was that central banks, by executing monetary policy and therefore controlling the supply of money, control the supply of the settlement asset for payment systems. The second one was the financial stability mandate that most central banks had: as the experience of various crises has demonstrated, risks present in payment systems could cause, transmit or exacerbate financial instability. Finally, in more recent years, payment system regulation and oversight powers became explicitly granted to central banks by relevant legislation. While a number of central banks perform both operator and oversight duties, the situation may give rise to a conflict of interest, which is why international standards have been recommending administratively separating them, to the degree it is practicable.

Some of the conflicting opinions on oversight that the FSAP mission encountered might have stemmed from misunderstandings about the nature of oversight function. As Bossone (2001) or the European Central Bank (2016) demonstrate, payment systems oversight generally does not involve routinely interfering with the operator's decisions and policies or reviewing and overriding their decisions. Data collection and moral suasion are among the most important activities in the overseer's toolbox. More coercive measures are only used when the objectives of oversight, such as safety and efficiency of the national payment system, cannot be achieved in other ways. Overseers are not expected to interfere with operators' legitimate business or technological choices if there are no good public policy reasons to do so. Finally, overseers do not take away the basic responsibility for the safety and efficiency of a payment system or a market infrastructure, which lies with the operator.

C. Recommendations

55. MEF, together with the SBP, should facilitate the urgent adoption of a law on payment systems and services. Enacting such a law was already recommended by the previous FSAP and the rapid growth of the digital payments industry makes its adoption even more critical. The law should include (i) a clear mandate for the SBP to regulate, supervise and oversee the national payment system, guaranteeing its safety and efficiency; (ii) a clear mandate for the SBP to act as the licensing authority, supervisor and regulator for payment service providers, including remittance service providers and electronic money issuers; (iii) a well-founded, clear, transparent and enforceable legal basis for multilateral clearing and netting, settlement finality, bankruptcy remoteness of collateral, protection of e-money consumer funds and other key legal concepts pertaining to payment and settlement; (iv)

recognition of non-bank provision of payment services, which ensures a level-playing field backed by a risk-based approach; (v) inclusion of fostering competition and financial consumer protection among SBP's mandates (while, in line with the FSAP's recommendations, retaining financial stability as its primary objective); (vi) repealing or amending older laws that would conflict with the new provisions.

56. Once the relevant legislation is adopted, authorities should amend other legal acts (such as the AML/CFT law or the credit cards law, as well as the SBP statute) to ensure that the use the same definitions and follow the same principles as the payment systems law. For example, authorities should consider amending Law 23 of 2015 to introduce “payment service provider” as an umbrella term, which would encompass the entities in Article 22.1.f and 22.1.g. They may also consider folding some of the individual rules governing remittance service providers and credit card issuers into umbrella regulations governing payment service providers to ensure equal protection of consumers and reduce opportunities for regulatory arbitrage.

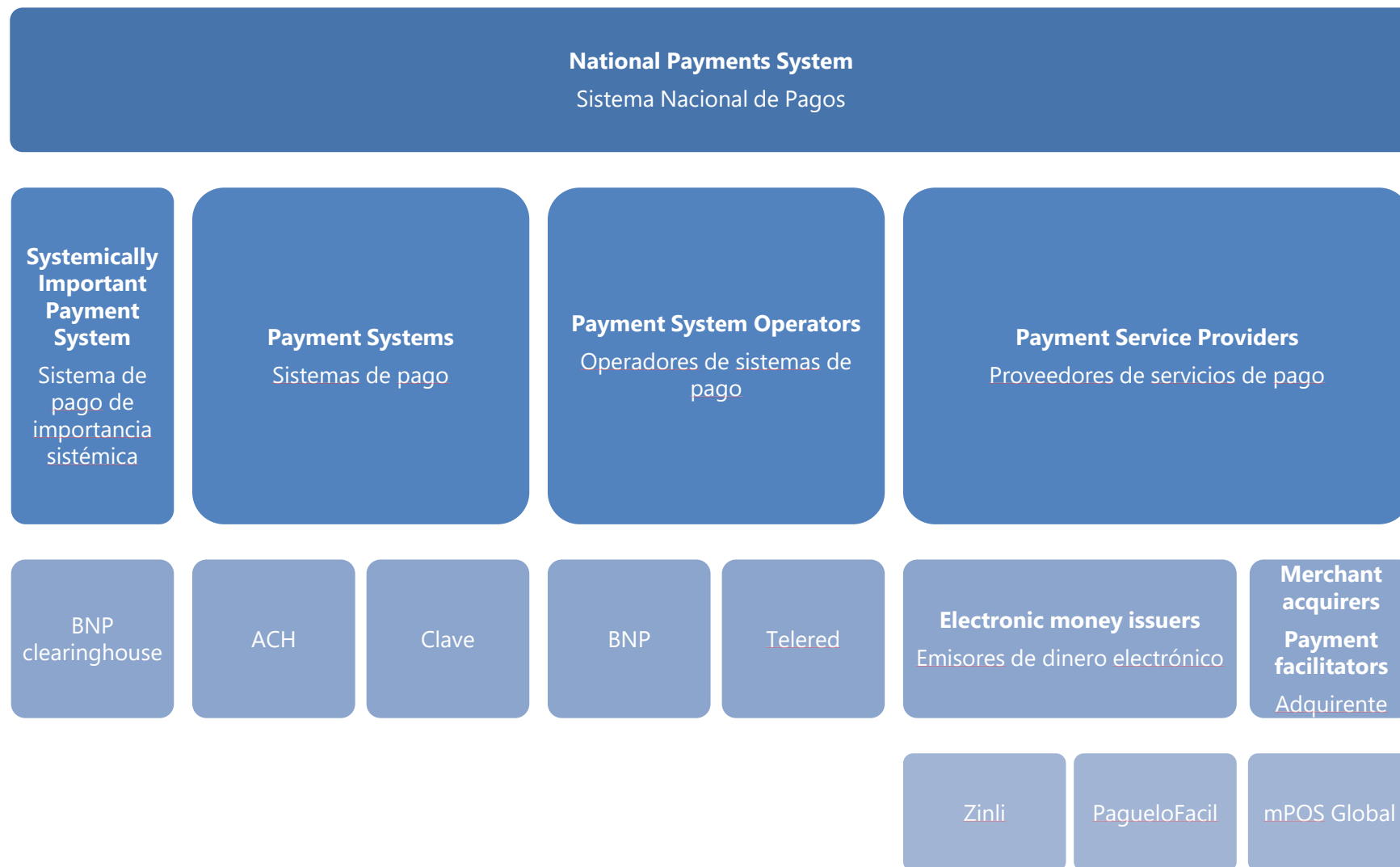
57. Upon the enactment of the new law on payment systems and services, SBP should develop an oversight policy framework reflecting the new mandate. The framework should cover payment systems and payment services, including innovative digital payment services, and it should be explicit about the objectives, scope, applicable standards and reporting requirements for payments oversight. SBP should also consider developing a capacity building plan for its staff on payments oversight to ensure effective implementation. It is important that the oversight policy be risk based and adopt realistic targets, as this function of the regulator will be built, effectively, from scratch.

58. It is important that the oversight policy framework focuses on safety and efficiency of the national payment system while minimizing undue burdens placed on system operators. For example, while some authorities do operate cost recovery frameworks and impose fees and levies on supervised entities, such charges should not be treated as a profit center by the supervising agency. Determining supervisory levies based on transaction volumes may create misaligned incentives and is to be discouraged.

59. Together with the oversight framework and in accordance with the enacted law, the SBP should also determine the licensing and registration procedures and timelines for new and existing payment system operators and issue necessary regulations to that effect. The priorities and timelines should be determined in a risk-based manner, in consultations with the industry. At the same time, it is crucial to provide the necessary protection to customer funds held with electronic

money issuers. For that reason, it may be necessary to prioritize licensing and regulation of that category of payment service providers.

Figure 2: Proposed regulatory framework and examples of entities belonging to each category



Note: To simplify the diagram, some categories have been omitted (e.g. critical service providers, correspondent banks, custodians).

60. SBP should develop and implement a comprehensive, standalone financial consumer protection (FCP) framework for banks and non-bank payment service providers, with a specific focus on the new risks to consumers due to DFS and fintech in the medium term. SBP is in charge of financial consumer protection in the banking sector. After the enactment of the new payment systems and services law, with its new mandate on regulating and overseeing the national payment system and considering new developments in DFS and fintech in Panama, SBP should develop and implement a comprehensive standalone FCP regulatory framework for banks and non-bank payment service providers. The framework should cover dispute resolution, disclosure and transparency, fair treatment, and business conduct. Specific FCP considerations on DFS include fraud or other misconduct, platform unreliability, lack of transparency, riskier or complex product offerings unsuitable to consumers, algorithmic decision-making, and data privacy issues, among others.

61. While crypto asset trading does not seem to be developed in Panama at this stage, the Panamanian authorities are encouraged to monitor the local developments and observe/implement the international guidance from SSBs in this area. As the Panamanian market is quite nascent at this stage and the international guidance on regulation and supervision of crypto asset activities are still evolving, the authorities are recommended to closely monitor the developments and potential risks before taking further action. Any regulatory initiative should adopt the principle of “same risk, same regulation” to the extent that crypto assets fulfil equivalent economic functions, to avoid regulatory arbitrage and fragmentation in the payments ecosystem.

III FINANCIAL AND ICT INFRASTRUCTURES

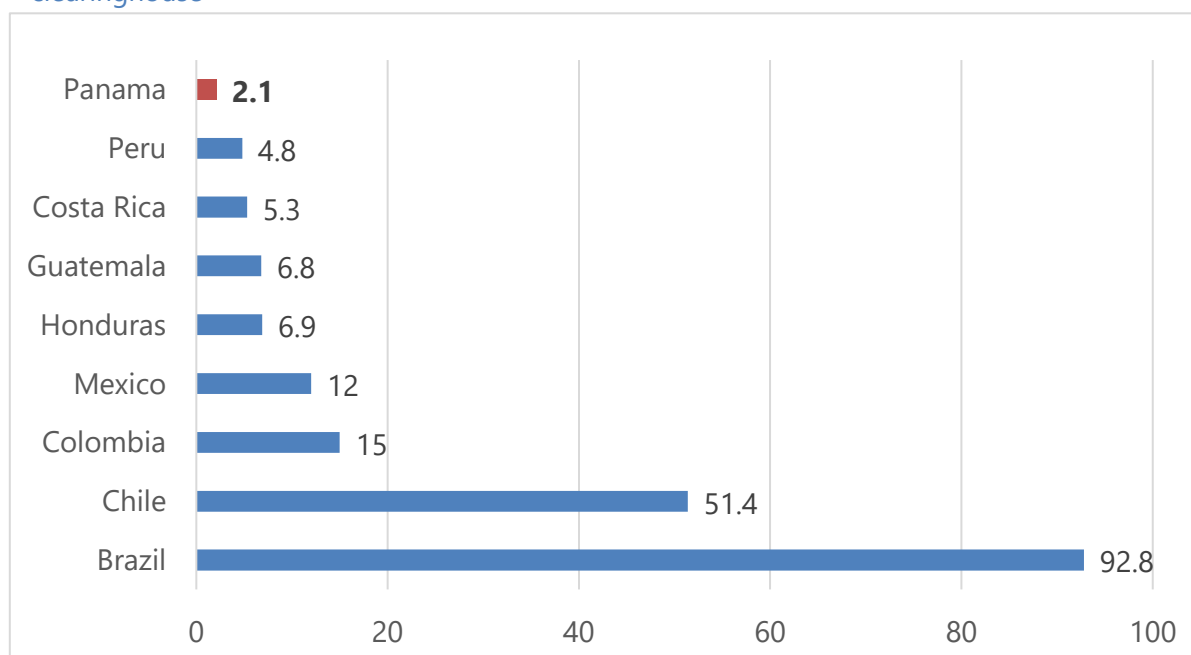
A. Context

62. Reliable financial, communications and other types of infrastructure are widely recognized as critical to the provision of efficient and cost-effective payment services, and, in this sense, are a fundamental foundation for financial access and inclusion. Analysis of guiding principle 3 begins with a discussion of the core payment systems in the country. Service point and access channel networks (e.g., branches, third-party agents and ATMs) are discussed separately under guiding principle 5. This is followed by a discussion of the other infrastructures that, while not being part of the national payment system, are also of major relevance for financial inclusion, as they provide critical information to payment service providers and other financial service providers. These include credit reporting and other data-sharing platforms, national ID systems and ICT more broadly.

B. Status in the country

Payment systems and other financial infrastructures

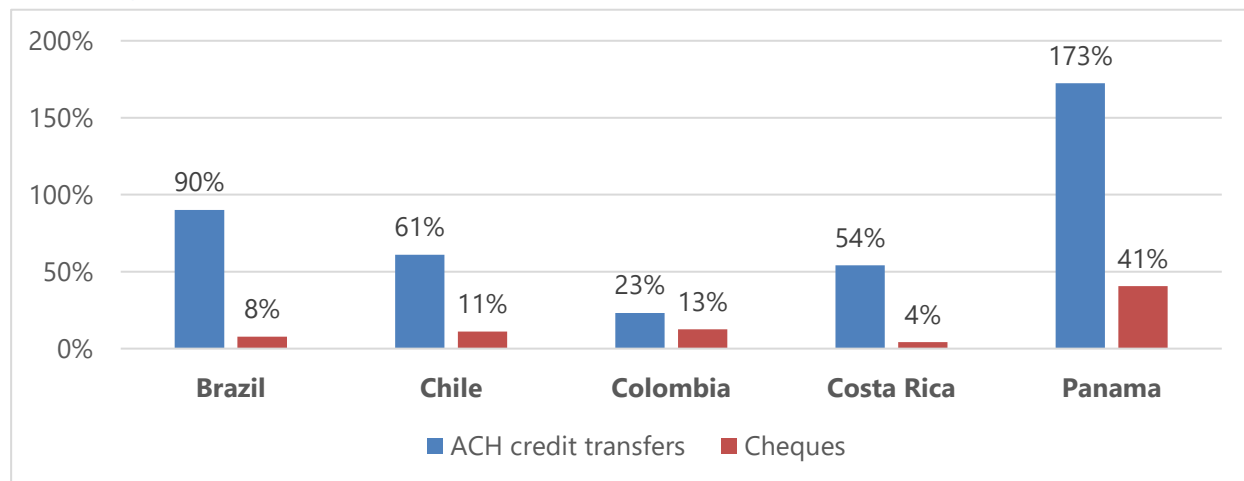
Figure 3: GDP turnover for RTGS systems in various countries (Panama's data refer to the BNP clearinghouse)



Source: SBP and the World Bank Global Payment Systems Survey (GPSS). Data for 2020 or the most recent year available.

63. While domestic clearing and settlement infrastructure is well-established in Panama, most of domestic interbank payments may actually be processed offshore. Panama is a relatively small, open, and dollarized economy, where nearly all banks have access to correspondent accounts in the United States, where they benefit from deeper and more liquid money markets. Given that Panama is a major regional financial center, there is no other plausible explanation of the fact that values of payments processed through domestic payment systems are dramatically lower than in other countries in the region. Adding up cheques and credit transfers processed through the automated clearinghouse, in 2022 domestic payment systems in Panama processed 214 percent of the country's gross domestic product (GDP). By comparison, Brazil's large-value real-time gross settlement system, STR, two years earlier processed payments equal to 9,280 percent, or almost a hundred times, of the GDP (see **Error! Reference source not found.**). Understanding the rationale behind the relatively low utilization of domestic payment systems will be important for assessing their systemic importance and developing a broader payment systems development strategy.

Figure 4: Total transaction values (2021) for interbank cheques and ACH credit transfers as percentage of the GDP.

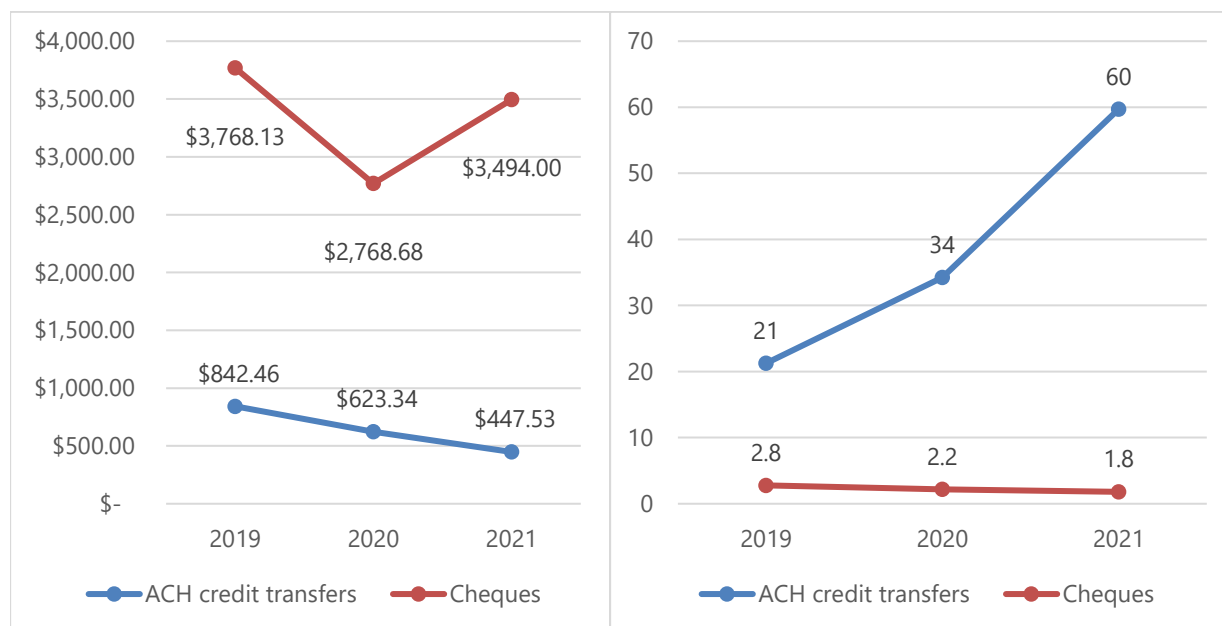


Source: World Bank staff calculations based on national central banks' data.

64. At the same time, the relative importance of cheques is higher than in neighboring economies. Even though the average Panamanian makes less than two cheque transactions a year, their cumulative value adds up to 41 percent of the GDP—approximately four times as much as in the case of Brazil and Colombia (see **Error! Reference source not found.**). Similarly, the average transaction size—3,494 dollars—is relatively high (**Error! Reference source not found.**). This suggests that cheques may be relatively popular as a payment instrument used for high-value time-sensitive

transactions, such as real-estate transactions or other business-to-business (B2B) payments—the use case that in other countries is most often handled by the RTGS system.

Figure 5: Average transaction size for cheques and ACH credit transfers in Panama (left) and average number of transactions per capita (right).



Source: SBP.

Banco Nacional de Panama clearinghouse

65. Panama operates a single settlement system—the clearinghouse of the Banco Nacional de Panama. In addition to that, there are several retail payment systems, most of them operated by Telered, a consortium of six commercial banks: a cheque clearinghouse, a deferred net settlement system for credit transfers and direct debits (ACH Directo), an instant low-value payment system (ACH Xpress) and a domestic debit card scheme (Clave). All of those systems settle in the BNP clearinghouse. Furthermore, a securities settlement system is operated by Latinclear, with the cash leg also settling in the BNP clearinghouse.

66. The “BNP Clearinghouse” is predominantly a settlement system for retail payment systems operated in the country. The role of the Banco Nacional de Panama in interbank settlements is legally mandated by the institution's Organic Statute and is connected to the other financial market functions it performs, such as the distribution of US dollar banknotes in coordination with the US Federal Reserve System and the issuance of balboa coins. Since November 2021, the BNP has been

working on separating its clearing and settlement functions from the commercial banking operations, beginning with the establishment of an independent Board Committee on Financial System Operations. Based on the committee's March 2023 decision, BNP management is proceeding to hire dedicated staff for the clearinghouse's risk management functions and other key roles and consolidate them in a single department independent from BNP-wide corporate functions.

67. Although the system, based on Montran software implemented in 2019, is capable of functioning as a real-time gross settlement system, the functionality is not used in practice.

Instead, settlement of clearing files received from Telered, as well as of cheques cleared by the BNP directly, occurs during five daily sessions, scheduled for 8am, 10am, 1pm, 3.30pm and 5pm. The settlement occurs on the books of BNP, where each participant of the system must open a "special clearing account".

68. It is the commercial banks' responsibility to maintain the minimal balance on the special clearing account.

The system rules determine the method for calculating the minimal balance, which is based on the arithmetic average of daily gross debit positions, measured over the course of the last three months. The BNP informs the participants if the balances fall below the minimal threshold and requires them to cover the shortage before the end of the business day; those failing to do so will be subject to monetary penalties. Balances can be topped up by: (1) transfers from banks' regular correspondent accounts maintained with the BNP; (2) CHIPS or Fedwire transfers to the BNP's nostro account in the United States; (3) interbank lending on the money markets. According to the BNP, a few banks had to be warned because their clearing account balances fell below the prescribed minimum; however, at no point in recent history there has been a failure to settle that has required unwinding.

69. There is no provision of intraday liquidity by the system operator.

Four commercial banks have arranged collateralized credit lines with the BNP, and disbursements from those could be used for the provision of additional liquidity throughout the day; the process is not, however, automated.

70. At this moment, every bank uses a single account for the purpose of settlement.

The BNP is planning, however, to introduce sub-accounts dedicated to the settlement of positions of individual ancillary systems. In this set-up, the account that a bank uses to effect settlement of cheque clearing will be separate from the account it uses for ACH Directo settlement. In a similar way, there will be separate accounts for the settlement of ACH Express, Clave, and Latinclear clearing files, as well as those of any new payment systems or clearing arrangements that could be launched in the future.

As a result, participants will have to proactively dedicate liquidity to the settlement of individual systems and proactively manage it throughout the business day.

71. There are system-level liquidity risks that the rules of the system may pose. While the fact that the RTGS functionality is not used means that a typical gridlock situation cannot arise, this may change after the introduction of separate settlement accounts for each system. This is because there it is theoretically possible that two banks, Bank A and B, have mutual obligations that net to zero when all the systems (cheque clearing, ACH Directo, ACH Express and so forth) are considered, but there is an asymmetry of their net positions across different systems. For example, Bank A expects that its large negative net position in ACH Directo would be covered by its large positive net position in ACH Expresses, while it is the opposite for Bank B. In the current framework, all those positions could be netted out, while in the “separate accounts” model, assuming that the settlement for both systems occurs at the same time, settlement for those two banks could fail because of the lack of funds.

72. Furthermore, the use of the gross debit position to calculate the required minimal balances to be held in the system can create some unintended consequences. While it results in the increase of aggregate liquidity available at the system level, it may result in misaligned incentives. Firstly, there is no incentive for “altruistic” behavior in the system. Let us assume that there are two banks: Bank A and Bank B. Over the given period, Bank A would receive no credits and accumulate one million dollars of debits to its special clearing account, resulting in a negative net position of one million dollars. On the other hand, Bank B would receive two million dollars of credits and accumulate one million dollars of debits, resulting in the positive net position of one million dollars. According to the current methodology, both banks would have to maintain the same compulsory balance on their special clearing account, even though the latter is providing a public good—ample liquidity facilitating the smooth flow of payments in the system—that the former does not. That effectively amounts to a penalty imposed on Bank B, which has to “pay” the opportunity cost of not being able to invest the funds in a more profitable manner. Secondly, the system is, by design, pro-cyclical: more gross debits during the period of market stress would result in higher minimal balance requirements. If the data is available, further analysis of banks’ payments behavior from the time of the 2008 global financial crisis, or the more recent period at the onset of the COVID-19 pandemic, could establish the extent to which this is a well-founded concern. Finally, the balance requirement, while substantively reducing the risk in the system, is not a substitute for the management of net debit positions in the netting systems

operated by Telered. Since net debit caps in those systems are not used, it is still possible that a bank's net debit position will exceed the minimal balance requirement.

73. Nonetheless, the liquidity and credit risk in the system remains limited for many reasons. While the FSAP team has not conducted a network analysis for payments between Panamanian banks, it is reasonable to assume that the BNP has a high level of centrality in the network, considering its role as the fiscal agent of the government. Accordingly, the requirements imposed on individual participants may effectively be less important than the fact that the BNP itself can access ample liquidity, and effectively backstop the system—however, it would require new legal and institutional arrangements, as the BNP currently does not provide intraday liquidity nor does it guarantee settlement. Furthermore, as previously mentioned, the system, although capable of working as an RTGS, is not used in that way—and thus its liquidity requirements are by definition lower. Finally, as noted at the beginning of the chapter, many of the high-value time-critical payments between banks, such as those related to money market transactions, may be processed through US payment systems. If transactions settled on BNP are of predominantly retail origin, they are much less likely to result in problems with liquidity.

74. There is no clear procedure to be followed in the event of a participant's default. The system rules do prescribe, however, the procedure to follow in the event of the SBP initiating resolution proceedings (intervención). Based on the Article 37 of the system rules (and Article 38 in the case of tiered participation arrangement), the participant's special clearing account is frozen upon the receipt of resolution notice from the SBP, at which point the manager of the BNP clearinghouse develops an action plan and continues with the settlement of net positions of the participant in resolution based on the following priority order of payment systems: (1) ATM (presumably referring to Clave), (2) ACH, (3) cheque clearing, (4) returned cheques, (5) Latinclear and (6) other systems. There is no clarity on the existence of any zero-hour rules, or the treatment of transactions that have entered a netting scheme prior to a declaration of default.

75. While it is not stated explicitly in the system rules, it seems that the "survivor pays" model has been adopted. Although it is not a problem in itself, it is concerning that the participant banks' knowledge of the rule is not universal. The FSAP mission has heard from a number of commercial banks' staff that they believe that the BNP will guarantee settlement in the event of a participant's default, and therefore other measures, such as guarantee funds or collateral pools, are not necessary. In other words, they may believe that the BNP will assume the liabilities of a defaulting participant. This may be caused by misinterpretation of the system rules, or by confusing the

government's guarantee extended by law to the BNP (which does exist) with a guarantee extending by the BNP to the clearinghouse participants (which does not). It is encouraging that the BNP has prepared new training curricula for system participants, which should result in a greater awareness of system rules and risk management principles throughout the banking system. Nonetheless, education by itself does not diminish the need for a formal mechanism to manage credit risk.

76. The BNP team has prioritized the management of operational risk in the system, with the view to ensuring business continuity and protecting participants from cybersecurity threats.

The clearinghouse has a business continuity plan, which is regularly tested (at least three times a year). Participants are included in business continuity testing and are, for example, expected to work from their alternate sites. A risk management team has been formed, with the bank aggressively hiring for new risk-related positions. The operator has attained the Systems and Organization Controls 1 (SOC) certification, created by the American Institute of Certified Public Accountants (AICPA), and is in the process of getting SOC 2-certified, which includes internal controls for security, confidentiality, and protection of personal data. Nonetheless, its management team recognizes that more needs to be done to align the clearinghouse's operational resilience—in particular, its cybersecurity posture—with the global best practices.

77. As mentioned in the previous chapter, currently only banks are entitled to join the clearinghouse as participants—either direct or indirect.

The BNP, however, is interested in opening up the participation to non-banks, such as electronic money issuers. Furthermore, it would potentially consider including the National Treasury as one of the participants to streamline the processing of government payments. This approach has been adopted by various jurisdictions worldwide—for example, the Bureau of the Fiscal Service at the US Department of the Treasury can directly participate in payment systems such as Fedwire and FedACH.

78. While most of the cheques are cleared through the systems operated by Telered, described later in this chapter, nine banks submit their cheques for clearing directly with the BNP.

The cheque clearing service is not seen by its operator to be a system separate from the "main" BNP clearinghouse. However, since its role (clearing) is distinct from the role that the BNP performs with respect to other payment streams (settlement of clearing files submitted from outside the bank), it could be considered a separate infrastructure. It is, by and large, a legacy system used by smaller banks that for various reasons were not onboarded onto the Telered-managed platform. The BNP is potentially open to discontinuing this service and transferring the entire cheque clearing operation to Telered, but no decisions on that have yet been taken. Given that cheques are considered to be a

payment instrument that is progressively phased out, the bank is not planning to modernize the system in any significant way: for example, cheque truncation has not been introduced and there are no plans to do so.

Retail payment systems

79. Telered is a private company, owned by a consortium of six commercial banks (Banco General, Banistmo, BAC, BNP, Capital Bank and Citibank), which operates the remaining retail payment systems in the country. These include a cheque clearinghouse, two ACH systems (a standard and a real-time one), an ATM network and a domestic card scheme, as well as an account-to-account bill payments system. Its members include 47 financial institutions (commercial banks and cooperatives).

80. The cheque processing system—PID (Procesamiento de Imagen y Documentos)—connects 36 banks and is responsible for most of cheque processing. Telered handles scanning the cheques, as well as the process of their archiving. Finally, it forwards the transaction file to the BNP clearinghouse for the final settlement.

81. ACH Directo is the automated clearinghouse for direct credits and direct debits, which is a system that processes the majority of retail payments in the country. It is used by 47 banks and cooperatives and has an international link to the United States' ACH system, where settlement occurs between the BNP and the Federal Reserve Bank of Atlanta. The latter arrangement allows Panamanians to locally receive retirement pensions and other benefits accrued when the Panama Canal Zone remained under the US administration. There are three daily clearing sessions when the payment files are exchanged. However, there is only a single settlement session: the network operator transmits the day's clearing file, adjusted for declined transactions, to the BNP clearinghouse by 5.30pm. Incoming funds must be credited by 6.30pm on the same day.¹⁵ ACH Directo uses the NACHA file format; however, migration to ISO 20022 is planned in the near future.

¹⁵ While ACH Directo requires same-day availability of funds (by 6.30pm), the FSAP team has been presented with rare but concerning cases where it might have not been the case. One originator of a large payroll-type bulk transaction claimed that the intended recipients reported delays in the availability of funds. Without further investigation, it is impossible to determine where the issue was connected to a delayed submission of the file by the originating bank or a delayed crediting of the payment to the recipient's account by the receiving bank. Similarly, it is impossible to determine if the reported incident was caused by operational or financial issues on the side of either of the banks. Such occurrences—fortunately very unusual in Panama—do affect the public's confidence in the financial system.

82. ACH Express, on the other hand, is the real-time retail credit transfer system, belonging to a class that is most often called "fast payment systems" or "instant payment systems". Clients of its ten participating banks can send payments of up to 500 dollars (although participating banks could impose lower limits), which are instantly credited to the beneficiary account in the receiving bank. Settlement occurs, on the DNS basis, in the BNP clearinghouse during each of the five settlement sessions. One of the reasons behind choosing that threshold of 500 dollars was the fact that the value 90 percent of transactions processed through ACH Directo in 2022 was lower than 500 dollars. Launched in August 2022, it has been rapidly growing: since then, it processed more than 300 thousand transactions with the total value of over 130 million dollars. However, it is still rather small compared to ACH Directo's annual volume of 50 million transactions. This is primarily driven by the limited adoption of the service by commercial banks. Nonetheless, Telered estimates that by the end of 2023, ACH Express will be adopted by half of Panamanian banks, and that 90 percent of credit transfers below 500 dollars will be transferred in this way.

83. Aside from expanding its adoption, the operator is focusing on enabling more ancillary services for ACH Express participants and the end customers. These would include an aliasing service, an account validation service, as well as an improved dispute resolution system. In that way, ACH Express—together with an aliasing service—could become a merchant payments platform (utilizing QR codes as one presentment method). However, as discussed later in the document, it is not clear whether the banks are going to embrace those initiatives.

84. Clave is a domestic debit and prepaid card brand managed by Telered. The name is also sometimes used to refer to the Panamanian ATM network managed by the company: while only 27 thousand out of the estimated 3.2 million debit cards issued in Panama are formally co-badged (bearing Clave and Cirrus logos), the vast majority of internationally branded debit cards can access Clave's ATM network. That includes 778 thousand of debit cards for which Telered provides third-party processing services, as well as 60 thousand cards utilizing different issuer processors, but where an agreement to use the network has been signed. In that sense, the Clave network can be seen as the local equivalent of ATM networks such as Plus or Cirrus.

85. The Clave card has good brand recognition, built over decades; it has effectively become the ATM card for Panama. Cards with the Clave logo still account for the plurality of all cards issued in the country and the absolute majority as far as debit cards are concerned. However, remaining on the technological frontier with respect to technology and products has proven more challenging. Clave did adopt the EMV chip standard, but it still does not support contactless payments (work

on the implementation, based on white-label technology, is ongoing). Neither does it support tokenization services. Only recently has the functionality of Clave-branded cards been extended to point-of-sale purchases and e-commerce payments. Considering the fact that much of its growth in issuance is driven by the recipients of pensions and other social benefits (relevant authorities migrated their payments from cheques to Clave over the past three years), the long-term strategy for Clave remains unclear.

86. Telered's last brand, Mis Pagos Hoy, is an account-to-account bill payments service.

Using the same underlying infrastructure as ACH Directo, it provides customers of 25 participating commercial banks and cooperatives with a bill payments interface accessible from their electronic banking application, allowing instant payment confirmation integrated with the billers' system. At this moment, most billing providers offering Mis Pagos Hoy as a form of payment are utility companies and insurers.

87. Telered is not a regulated entity, and therefore it is not subject to supervision or oversight of any authority. This is not something the company itself is comfortable with: on the contrary, it has highlighted the fact that similar market utilities in other countries are regulated and supervised, which gives their owners and managers more regulatory certainty. Nonetheless, Telered voluntarily adopted certain industry standards. It has attained the PCI-DSS certification and imposed operational risk management standards on the clearinghouse participants, established a disaster recovery site and conducts regular business continuity exercises.

88. The most important risk that is *not* adequately managed is settlement risk. The issue has already been described in the part of the chapter that covers the BNP clearinghouse: the move from payments credited the next day, or at the end of the business day (cheques and ACH Directo) to those where funds are available immediately (cards and ACH Express) means that participants incur unsecured net debit positions, which creates a counterparty risk should such a participant default. Because payments are credited in real time (or, in the case of card payments, the cash is dispensed, or goods and services are sold in real time) it is possible for the final beneficiary to have already used the received funds by the time the sending institution is found to be in default. Because of that, real-time retail payment systems usually introduce net debit caps equivalent to the amount deposited by the institution on its prepaid settlement account. In other cases, settlement is insured by the means of a guarantee fund or non-cash collateral that can be liquidated in the event of default.

89. In the longer timeframe, the risks to Telered are of more strategic nature. Its shareholders do not seem to be in agreement on its broader direction. While all operators of financial infrastructures face the challenge of weighing the interests of various parties against each other (large institutions against small ones; big issuers against big acquirers), the situation in Panama adds other layers of complexity. For example, the priorities of banks that actively develop products based on the Clave network will differ from those that focus on international card networks and would like to see Clave limited to operating the ATM network. The lack of clarity also surrounds the relationship between Telered and the BNP clearinghouse: there is no agreement on the question of whether the BNP or both institutions should be primarily providers of public goods, or whether they should be seen as commercial entities that, for instance, would compete against each other or against third parties—for example in provision of clearing services, notwithstanding the BNP's exclusive role as the settlement agent.

Securities settlement systems

90. Latinclear, which runs the central securities depository and the securities settlement system, is the third and final operator of financial infrastructures in the country. Similarly to the systems operated by Telered, it uses the BNP clearinghouse for the final settlement of market participants' cash leg positions. Settlement procedures are described in Chapter XII of its operating procedures and follow the Delivery-versus-Payment (DvP) Model 2: the securities leg is settled on item-by-item (gross) basis, while the cash leg is netted. Cash positions are prefunded and settlement occurs on the second day after the trade date (t+2). Participants can preview the next-day settlement position on t+1.

Credit information

91. APC Intelidat, the credit bureau, has been operational for many decades, first founded in 1957 as Asociación Panameña de Crédito. The credit bureau has several data sources besides the financial service providers, including telcos and utility companies, with the exception of data from the water utility as the billing is to the address and not to the name. Both positive and negative data are reported, as well as data on companies in addition to consumers. The bureau has data on approximately 4 million persons in Panama, including foreigners residing in the country.

92. There are several barriers to a well-functioning credit information system in Panama:

- **Verification of identity via Tribunal Electoral is manual, costly and time consuming.** It costs \$1 per verification with no biometrics, and this can only be done via the website of Tribunal Electoral. API access is available only for the four vendors the Tribunal Electoral has been working with, and only for biometric verification. Thus, while APC Intelidat has API capabilities, it is unable to access Tribunal Electoral via APIs.
- **Verification of collateral is a challenge.** The Public Registry of Panama (RPP) has API capabilities; however, APC Intelidat cannot access the RPP via APIs to receive information and verify whether the lots owned are mortgaged or not, in order to validate them to be pledged as collateral.
- **Credit bureau law (Law 24 of 2002) is restrictive in the way in which it allows the credit bureau to access different types of information.** The credit bureau is only allowed to have the name and cedula of an individual in addition to their financial information, but no information on addresses, phone numbers or e-mail addresses, nor information on social security, salaries, or work history. While this is done with the intention of preventing fraud, this puts limits on credit scoring.
- **Banks and other providers of credit do not offer interest rates based on credit scores.** While APC Intelidat developed credit scoring in 2007, good credit score has not been used to offer a better interest rate to borrowers in Panama.

ICT infrastructure

93. Panama's ICT connectivity has been systematically improving, but the country still underperforms its peers. Even though it is the richest country in Latin America, as measured by the per-capita GDP, the internet penetration—at 68 percent of the population—barely exceeds that of much poorer Honduras and El Salvador and lags that of Argentina, the leader, by almost 20 points. With 14 fixed broadband connections per 100 residents, the country scores below its neighbors Colombia (16) and Costa Rica (21), while its distance to the regional leader, Uruguay (32) is increasing. At the same time, mobile internet may be too slow to be a good substitute for fixed broadband. 5G technology has not been implemented, and 4G signal reaches only 84 percent of the population. Consequently, Ookla's Speedtest Global Index from April 2023 scored Panama 115th in the world according to the speed of mobile internet (download speed of 17.39 Mbit/sec).

94. On the other hand, connectivity in Panama is relatively affordable. The International Telecommunication Union (ITU) calculated the average monthly cost for a mobile phone contract in Panama in 2021 to be around US\$ 21.80, which remained consistent with the previous year's value and better than the global average. Considering economic output per inhabitant, Panamanian users spend about 2.1% of their income on mobile telephony, a rate significantly lower than the global average of around 6.6%. In contrast, mobile phone users in the USA pay approximately \$38.10 per month.

95. With 138 mobile subscriptions per 100 persons, nearly all Panamanians have access to mobile phones. However, while an estimated 96 percent of the population is covered by mobile signal, it reaches only 38 percent of the country's territory. This means that sparsely populated areas of the country, such as the province of Darien (covering 15 percent of Panama's territory, but only 1 percent of its population) may be effectively excluded from digital services. A number of financial institutions, as well as the postal service, have informed the FSAP mission team about the challenges with digitizing services in those areas. As a result, many remote communities do not have access to digital financial services.

96. Panama is still developing its cybersecurity institutions. The Computer Security and Incident Response Team of Panama (CSIRT) has been established under the Government Innovation Authority (AIG).¹⁶ Its reports highlight key challenges related to cybersecurity in the country: professional criminals and state actors continue to be the most significant threat, inflicting the most damage; and digital attacks are being used to influence the democratic process. According to the National Strategy for Cybersecurity for 2021-2024, the government's priorities include: (i) preventing criminal behaviour in cyberspace; (ii) stopping the use of cyberspace for any illegal acts; (iii) innovation, training, and adoption of standards to develop a culture of cybersecurity; and (iv) preserving privacy of personal information. The authorities aim to move beyond simple threat awareness and into actively combating cyber threats and online services disruption.¹⁷

97. Currently, there is no CSIRT/CERT team specific to the financial sector. However, the SBP and AIG in 2021 signed a memorandum of understanding, providing a framework for the regulator to participate in the work of the national CSIRT. On the other hand, aside from the general Basel rules,

¹⁶ DataGuidance. "Panama," July 8, 2021. <https://www.dataguidance.com/jurisdiction/panama>.

¹⁷ International Trade Administration | Trade.gov. "Panama Country Commercial Guide," n.d. <https://www.trade.gov/panama-country-commercial-guide>.

no guidelines pertaining to the management of operational risk by financial institutions have been issued.

ID System

98. The coverage of Panama’s foundational ID system (cedula) is nearly universal. According to the Panamanian Constitution, its administration is the exclusive authority of the Electoral Tribunal. Each citizen receives an ID card (cedula) with a unique number (cedula number). In addition to the basic biographic data, the database managed by the Tribunal includes the proof of address and biometric information. The information can be shared with third parties such as banks or other financial institutions. The service is provided by four vendors contracted by the authority, who charge \$0.75 per each biometrically verified record. The data can also be shared with other government agencies, where it is used to provide, for example, social benefits. The Electoral Tribunal is presently focused on expanding its mobile app footprint: citizens can already renew their ID cards with assistance of face recognition software, while a future app will allow sharing selected ID information with third parties using QR codes.

C. Recommendations

99. The BNP should conduct a self-assessment of its clearinghouse according to the Principles for Financial Market Infrastructures (PFMI). The FSAP mission had the opportunity to examine some of the aspects relevant to PFMI compliance of the system and its operator, this technical note is in no way a substitute for a full-fledged PFMI assessment. For example, the analysis of the sources and flows of liquidity in the system, utilizing network analysis and simulation techniques, should be conducted to identify critical participants and test the system’s behavior in market stress scenarios. While the absence of a payment system law and the lack of regulatory clarity need to be addressed, they should not be an impediment for conducting the assessment, even though Principle 1 will likely assessed as “not observed”. It is also important to inform all relevant stakeholders of the assessment results, in accordance with the PFMI disclosure framework standards.

100. The BNP should continue the process of organizational separation between the clearinghouse and its commercial operations. The BNP’s explicit government guarantee positively affects its role as a settlement bank for payment systems and financial market infrastructures, as settling on the BNP’s balance sheet becomes, in terms of the risk profile, is the closest approximation of settling in central bank money that can be achieved in the Panamanian context. On the other hand, using the BNP books for settlement need not preclude making the clearinghouse operations more

independent from the bank, for example by spinning it off to a wholly-owned subsidiary. As a minimum, a "Chinese wall" should be maintained between the clearinghouse and other banking operations to allay any concerns about potential conflicts of interest, with reporting lines clearly separated. Governance of the clearinghouse should be designed to further strengthen its independence, for example by strengthening the role of the Board Committee on Financial System Operation and including independent directors in its composition. The rules pertaining to allowing new payment systems to settle within the clearinghouse should be equitable, transparent and publicly available. Finally, the separation should extend to cost accounting and cost recovery, in order to avoid conflicts of interest that could be associated with cross-subsidizing the clearinghouse by banking operations, or vice versa—also with respect to business losses or other non-default losses.

101. The BNP and Telered should review—and possibly revise—the structure of fees charged for clearing and settlement services. In the case of the BNP, it should be connected to developing a comprehensive cost recovery framework, including the in principle separation between the clearinghouse and the BNP's commercial banking operations,, and fair accounting for any BNP-wide cost centers, such as real estate or security. The possible principles applicable to fee-setting could include promotion of digital payments (and therefore imposing additional charges on some or all paper cheques), as well as facilitation of a smooth flow of liquidity in the system (and therefore incentivizing injection of liquidity or early submission of payment orders with lower fees). Telered should ensure that the fee structure is fair, fosters competition, and incentivizes the adoption of safest and most efficient digital payment instruments.

102. Telered and BNP should put in place a settlement risk management framework for their systems, as part of their system rules. This should include introducing clear and effective default management procedures, as well as tools for managing participants' credit risk. The latter may take the form of a net debit cap, tied to depositing an equivalent amount of cash collateral to a dedicated BNP account. Alternatively, a guarantee fund or other forms of collateral (pledged securities) could be considered. Each of those method will require additional integration of Telered systems (Montran and Smartvista) with the Montran system operated by the BNP. In connection with that, the BNP should evaluate and, if needed, revise the methodology for calculating its minimal balance requirements.

103. The BNP and Telered should develop a framework for the admission of non-banks, such as electronic money issuers, as clearing and settlement participants. Such a framework should only come into effect, however, once a proper licensing, supervision and oversight system for payment service providers is put in place.

104. The BNP should provide RTGS functionality for time-sensitive high-value payments and encourage the banks participating in the clearinghouse to use it for payments where instant settlement is required.

Implementing this recommendation will most likely require further study of payment behaviors of Panamanian businesses and assessing the impacts on system liquidity. However, it is likely that an RTGS facility could be a more appropriate channel for some of the payments that are currently made using high-value cheques. Introduction of collateralized intraday credit will likely be necessary to ensure a smooth flow of orders in the system, as well as the introduction of other liquidity management tools (priority setting, queuing, gridlock resolution).

105. The BNP and Telered should develop further international links with other systems in the region. While the existing ACH links with the United States are important, regional integration can yield further benefits, especially considering remittance flows and Latinclear's regional footprint.

106. The BNP should implement an endpoint security strategy, based on the CPMI toolkit on reducing the risk of wholesale payments fraud related to endpoint security. Similar measures can also be adopted by Telered and Latinclear.

107. Telered should strengthen enforcement of member banks' compliance with funds crediting rules, and ensure that a full-fledged compliance monitoring system is in place. This may require imposing reporting requirement on members if funds cannot be credited in a timely manner due to operational reasons. The operator should also coordinate with the SBP's financial consumer protection unit to sensitize the users to funds availability rules and gain access to any complaints related to delayed funds availability, so that appropriate investigations can be undertaken.

108. In order to improve the credit information system in Panama, the Panamanian authorities should consider:

- Enabling secure use of APIs for information retrieval from Tribunal Electoral and the Public Registry of Panama (RPP),
- Amending Law 24 of 2002 to enable the credit bureau to access additional information on the consumers, within the scope of Law 81 of 2019 on data protection for better credit scoring,
- Encouraging providers of credit to offer differentiated interest rates based on credit scores.

IV PRODUCT DESIGN

A. Context

109. The PAFI report defines a transaction account as an account held with banks or other authorized and/or regulated service providers which can be used to safely store some value and make and receive payments. Transaction accounts can be differentiated into deposit transaction accounts and e-money accounts. Both types of accounts are analyzed in detail as part of guiding principle 4 together with the associated payment product offering from the perspective of payers and of payees. Only if the transaction account and payment product offerings effectively meet a broad range of the transaction needs of the target population will end customers be willing to open a transaction account, adopt payment instruments and make use of their transaction account and associated payment instruments on an ongoing basis. To effectively design transaction account and payment products, the supply side needs to identify end customer needs and provide a mix of product features that offer the potential to meet those needs at a reasonable cost. These product-specific features, in combination with broader market practices (e.g., consumer protection), affect the attractiveness of the respective product for customers. Product-specific features also impact the cost for PSPs of providing the payment service.

110. Innovations in technology and business models have resulted in the rise of digital financial services (DFS) which can lower costs and increase speed, transparency, security, and availability of more tailored financial services that can serve the poor at scale.¹⁸ DFS in general and fintech in particular can be leveraged to improve the design of transaction accounts and payment products as well as other financial products, making them accessible to all, enhancing user experience and awareness, and achieving efficiency gains and lower market entry barriers. For example, instant payments, e-wallets in combination with contactless technologies, and super apps offer end-users with various features such as greater speed, end-user control, ability to manage several payment instruments via one app and facilitating a wide range of daily tasks. At the same time, these benefits come with certain risks in terms of operational and cyber resilience, the protection of customer funds, data protection and privacy, digital exclusion and market concentration. If not adequately managed,

¹⁸ Digital financial services (DFS) are financial services which rely on digital technologies for their delivery and use by consumers (World Bank, 2020). Fintech is defined as “advances in technology that have the potential to transform the provision of financial services, spurring the development of new business models, applications, processes and products.” (IMF and World Bank, 2018).

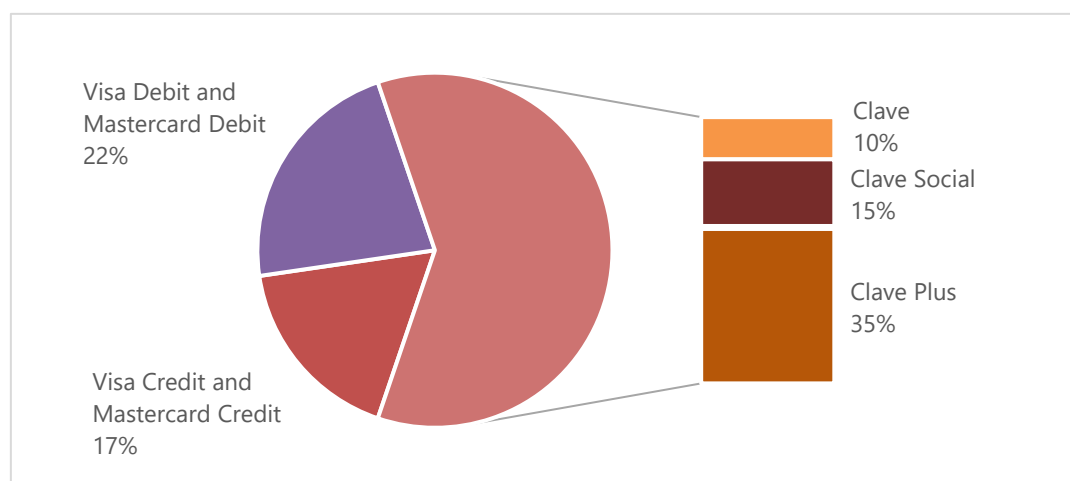
these risks could undermine financial inclusion outcomes. This underscores the importance of effective regulatory, oversight and supervision frameworks, which are discussed in section II.

B. Status in the country

111. Basic accounts have been regulated in Panama since 2013 by Rule 001-2013 of SBP. This Rule establishes “simplified process accounts.” Providers are not mandated to open simplified process accounts. According to this Rule, these accounts can be opened by Panamanian citizens and residents, must be expressed in national currency, with a maximum balance of \$1,000 and cumulative monthly deposits of \$1,500. These accounts can be opened remotely and using simplified KYC requirements – only the Panamanian cedula or a foreign resident ID card is to be provided to open the account. These accounts can use online and mobile banking.

112. Credit transfer products, described in greater detail in the previous chapter, are a popular retail payment product. ACH Directo (same-day ACH) is provided by nearly all banks, while ACH Express (real-time credit transfer) is only offered by 11 institutions. Nearly all banks provide access to at least ACH Directo through their online and mobile banking apps. However, the cost of payment products is relatively high. Many commercial banks charge as much as \$5-10 for a single ACH transfer, which makes digital payments more expensive than cheques or ATM withdrawals. Interestingly, some banks do not vary charges between ACH Directo and ACH Express transfers. This is probably another consequence of the fact that ACH Express, not requiring prefunding or collateral, effectively does not impose any liquidity cost on participating banks, as described in Chapter III.

Figure 6: Credit and debit card issuance by brand



Source: Telered.

113. Payment cards are widely adopted in Panama. There are 2.4 million Clave debit cards in addition to another 883,000 debit cards by Visa and Mastercard. In addition, there are 56,000 Vale Panama pre-paid cards and 698,000 credit cards by Visa and Mastercard. These amount to around 1.33 payment cards per adult. Slightly more than half the card-based transactions are done in ATMs. This indicates a preference for cash by the Panamanians – withdrawing and spending in cash. Contactless payments by card, Apple Pay or Google Pay are becoming more and can, for example, be used to clear the gates on the Panama City’s transit network.

114. Credit and debit cards dominate the P2B payments market. Merchant acquisition has been dominated by large banks, which rent POS terminals to businesses in exchange for a monthly fee and a blended merchant discount rate. Because of that, digital payments acceptance among small merchants and informal businesses has been low—even though banks have recently started differentiating their merchant offerings and introducing low-cost payment acceptance products, such as m-POS terminals.

115. Several banks have recently launched digital banking products, offering e-wallets. The most prominent ones are Nequi by Banistmo, Yappy by Banco General and Wa by Caja de Ahorros. As of June 2023, there were around 1.5 million e-wallet account holders, used across the country.

116. These e-wallet products allow for instant, on-us credit transfers. In doing so, they have dramatically changed the landscape for P2P transfers. In addition, these have become the preferred method to pay small merchants, including informal street vendors. While these platforms have been working on acquiring registered merchants for P2M payments, most informal merchants accept P2P credit transfers. Those with merchant accounts, however, receive basic value-added services in the form of analysis and insights on sales.

117. At the same time, however, these e-wallet products are not yet interoperable. Banco General has plans to work with BNP to have settlement at the BNP-operated clearinghouse at the end of the day to enable other banks to offer Yappy to their clients.

118. The development of digital credit products in the Panamanian market is hindered by the impracticality of digital signatures and unavailability of e-contracts. The process of obtaining a digital signature is lengthy, requires in-person presence in only a handful locations which may require non-trivial travel, and is costly for many.

119. The Panamanian MSME sector has several barriers in accessing financial services. There is no overall strategy for MSME development in Panama and a large informal sector. UNPYME

estimates that for every registered business, there are 1.8 unregistered businesses in Panama. Business registration for small businesses has the same requirements as those for large firms. There are six different laws governing the process, so a simpler unified legislation can potentially help in formalization. In addition, even if there is simplified tax reporting for smaller businesses, this is not well known. As such, most small businesses are unbanked, are unable to receive loans or make/receive digital payments.

120. Acceptance of digital payments by small merchants is one step in facilitating further access to finance. Pilot programs (e.g., by UNPYME) show that the new e-wallets offered by the new digital banking platforms, which enable receiving payments digitally via merchant accounts or via personal accounts, can be quite instrumental in changing the way small businesses, especially those in rural areas, work. Until recently, such businesses operated mainly on cash. With the widespread use of these e-wallets, small businesses can accept digital payments and start paying their suppliers digitally. Value added services on top of digital payments can help develop sales strategies, manage inventory and accounting, and enabling productivity gains and growth.

C. Recommendations

121. Establishing interoperability among e-wallets can help foster further adoption of digital payments, both for P2P payments and for P2M payments. Currently, existing e-wallet products only allow for on-us transfers, limiting competition, resulting in network effects and potentially hindering more widespread use. Interoperability would further competition, allowing for development of better products tailored to the needs of individuals and merchants. This interoperability can be achieved by further developing Telered's ACH Express product. Thus, the authorities can explore building consensus among the market participants to proceed as such.

122. Focusing on improving acceptance of digital payments by micro and small merchants' can lead to an overall expansion of usage of digital payments in the country. The use of digital payments for day-to-day, small transactions from local shops can help build habit and further influence the use of digital payments and other digital financial products. However, micro and small merchants most often have a difficult time accessing financial services, including the ability to accept digital payments. Therefore, specific targeted interventions to enable digital payment acceptance by micro and small merchants can improve the usage of digital payments, financial inclusion and overall digitalization. In this regard, Panamanian authorities can consider encouraging (i) low-cost acceptance solutions (e.g., mobile POS/SoftPOS); (ii) acceptance intermediaries upon the enactment of the

recommended payment systems and services law which can help development of targeted acquiring models, fees and onboarding approaches for increasing digital payment acceptance among micro and small merchants; and (iii) providers to provide value added services to micro and small merchants as productivity solutions, which can act as an incentive for accepting digital payments. Such efforts could be connected to other activities facilitating MSME finance and included as one of the themes of the developed NFIS.

123. The Panamanian authorities are recommended to consider policies with which responsible provision of digital credit can be facilitated. These include enabling the credit bureau to use various sources of data based on customer consent including using information from the Public Registry of Panama (RPP) on validating collateral, encouraging provision of differentiated interest rates based on credit scoring, and working on improving the practicality of digital signatures and legality of e-contracts.

V READILY AVAILABLE ACCESS POINTS

A. Context

124. Access points include ATM networks, POS and other digital payment point networks, physical branches and agent locations as well as purely digital access channels such as internet or mobile banking. New products and access modes may result in fewer readily available access points such as bank branches or ATMs. As the network of physical access points becomes less dense, consumers are increasingly using remote access channels.

125. The success of retail payment services depends to a certain extent on the availability (including physical proximity), quality and reliability of these access points. Customer payment behavior is especially sensitive to the density of access points in close proximity to their home or workplace. Rapid digitalization of payments, growth in e-commerce (and s-commerce), and higher acceptance of electronic payments by physical retailers reduce the need for cash and the need for cash distribution. New technologies and business models enable new ways of accepting digital payments, offering a low-cost alternative to traditional POS terminals, such as contactless technologies, plug-in devices for mobile phones, and QR codes.

126. The success of fintech depends on connectivity, access to smartphones and mobile data. Smartphone penetration rates are increasing worldwide, but mobile data infrastructure is often not keeping pace and/or data packages are too expensive for underserved and unserved customers, especially in EMDEs and in rural areas.

B. Status in the country

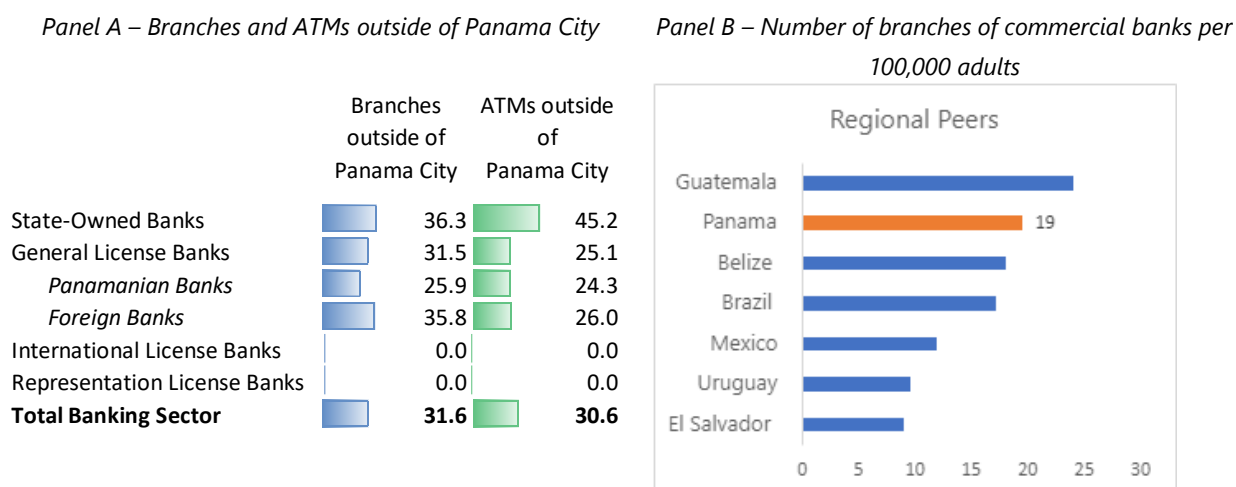
127. Panama has a large banking sector with 66 banks which collectively have 561 branches and offices, and 2,376 ATMs. While the number of banks operating in Panama is large, their branches and ATMs are predominantly in Panama City. Panama has significantly more bank branches than the average of its aspirational peers,¹⁹ with 19 branches per 100,000 adults (Figure 1- Panel B). However, almost 70 percent of banking branches and ATMs are in Panama City, which is at odds with its population share of 41.5 percent. International License Banks do not have a presence outside the capital city in the form of branches or ATMs. Among banking groups with operations outside Panama City, Panamanian private banks have the lowest availability of access points (Figure 1 – Panel A). In

¹⁹ We use the same country peers as in the recent Panama Systematic Country Diagnostic (2017). Available at <https://documents1.worldbank.org/curated/en/183431467986298985/pdf/97719-CAS-P151399-K8832-Box391451B-white-cover.pdf>

contrast, State-owned banks promote banking in rural areas by installing 45 percent of their cashpoints and 36 percent of their branches in other provinces. Additionally, while foreign banks with general licenses represent 45.9 percent of the total assets in the banking sector, they only have 38 and 29 percent of the existing branches and ATMs of the country.

128. Not many banks make use of agents to service the rural areas. The use of agent banking has been regulated by SBP since 2012 (Rule No. 002-2012). Caja de Ahorros has been working closely with pharmacies and convenience stores in rural areas as agents. There are 268 Caja de Ahorros agents, which are specifically located mostly in rural areas, including islands and indigenous reservations. Agents offer bill payments, deposits, and loan repayments. They also conduct weekly visits in their communities to open bank accounts, generate awareness and motivate savings.

Figure 7: Density of bank branches and ATMs



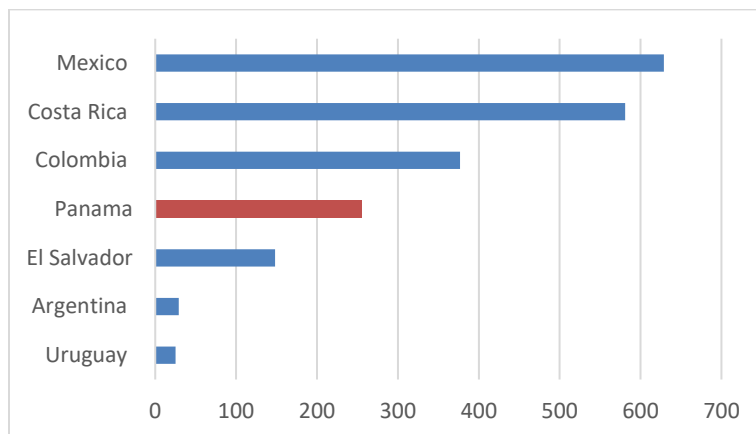
Source: IMF Financial Access Survey (2022), SBP and WB Finstats.

129. Many countries utilize the widespread postal networks to reach remote and hard to reach areas with financial services. The Panamanian national postal service, COTEL, provides domestic transfers and has been considering providing international remittance transfers to Cuba and Colombia, having conducted a market study with the assistance of the UPU. COTEL has 104 post offices nationwide. In small Panamanian towns and villages without banks, the post office is seen as a local bank branch. However, around half the post offices are not yet modernized or digitalized, and do not have POS terminals. While COTEL has plans for digitalization of the entire organization including post offices, the plan could not have been implemented due to funding constraints.

130. While digital and remote access channels also grew significantly, they compare poorly to some regional peers. According to the IMF Financial Access Survey (2022), the number of mobile and internet transactions per 1,000 adults grew from 12,065 in 2015 to 99,002 in 2021, with most of the growth coming from 2020 and 2021, likely a result of the pandemic. The value of mobile and internet banking as a percentage of GDP also grew significantly from 2015 by over 167 percentage points, and currently stands at 256% of Panama's GDP. However, it is still considerably lower than many of its comparable geographical peers (Figure 2). Additionally, banks can onboard customers remotely in Panama, which helps alleviating some constraints in terms of rural access.

131. Issues with connectivity in rural areas limit the possibilities for remotely accessing financial services. While internet penetration is high in cities, some rural areas still lack reliable and affordable internet. At the same time, the number of smartphone subscriptions in Panama is estimated to be around 4.7 million (Statista, 2023).

Figure 8: Mobile and Internet Banking as a % of GDP (2021).



Source: IMF Financial Access Survey (2022)

C. Recommendations

132. Panamanian authorities should consider ways to improve connectivity and promote agent-based models in remote areas. This could be done, for example, via satellite internet. Successful adoption of digital payments in remote areas can lead to efficiencies, especially for micro and small enterprises, in terms of supplier payments as well as for sales.

133. Panamanian authorities could consider the Post Office as one viable way of building access points in remote areas. However, for this purpose, digital transformation of the Post Office is

the key. This can be done via a phased approach where modernized post offices can start by offering more efficient domestic P2P transfers, and then potentially adding bill payments. In this regard, prioritization should be given to post offices in remote areas in the modernization process. Once the digital transformation process is complete, it will also be possible to use post offices as bank agents, providing much needed basic financial services in rural and hard-to-reach areas. For this purpose, a structured capacity building program for post office staff will be needed. Lastly, modernization of the Post Office could also enhance e-commerce in Panama, combining payment and delivery capabilities, especially in rural and remote areas.

VI AWARENESS AND FINANCIAL LITERACY

A. Context

134. Educational and outreach efforts are often needed to enable new and even existing users of financial products to effectively make use of their financial product with all its features.

In addition, the level to which end users are aware, or could become aware, of the financial product and service options available to them is important. End users, even knowledgeable ones, may not have easy access to, or be familiar with, certain tools that can assist them in obtaining useful, trustable and updated information on such options. Suboptimal choices are frequent under such circumstances. At the same time, technology enables new ways of delivering digital and financial capacity to users of financial services.

135. The growing digitalization of daily life and financial services is not necessarily matched with increasing digital and financial literacy levels (OECD, 2018). Digital capability may become a precondition to navigate the complex DFS ecosystem and for broader financial inclusion, making it more difficult for some disadvantaged groups (e.g., the elderly) less likely to be able to use the latest technologies, potentially leading to financial exclusion.

B. Status in the country

136. In 2019, the SBP started working on developing the National Financial Education Strategy (ENEF) and has been working on its implementation in collaboration with Panamanian stakeholders. ENEF is yet to be approved by the MEF. A working group was formed to design and implement the ENEF, and also to monitor progress. This working group included several public sector entities, including SBP, SMV, SSRP, MEF, Ministry of Education, MIDES, ACODECO, Comptroller's Office, and the MSME Authority, among others. In 2022, 14 banks joined the implementation of ENEF.

137. ENEF organizes the financial education efforts in Panama led by various stakeholders around a joint vision and objectives. Before the development of ENEF, various stakeholders in Panama had several financial education initiatives, however, these were not organized in a structured way. ENEF is also aligned with the National Strategic Plan as part of Panama's efforts to meet the UN SDGs.

138. Several activities as part of ENEF have been underway. A website was developed to promote financial education in Panama as part of the ENEF activities.²⁰ In March 2023, financial education was made compulsory in primary and secondary schools in Panama by law.²¹ Financial education curriculum at schools will focus on topics such as financial planning, savings, access to information, risks and benefits, financial decision making among others. The same law also established October 1 as the annual Financial Education Day in Panama.

139. ENEF prioritizes youth, entrepreneurs, workers and vulnerable populations as the target groups, and financial consumer protection and saving for retirement as the themes. However, while it includes references to DFS and fintech, it does not include a specific focus on digital skills needed for the use of DFS and the specific consumer risks arising from DFS such as fraud, data privacy, etc.

140. There is a gap in the financial and digital literacy levels of owners and managers of micro and small enterprises. According to a study commissioned by UNPYME, one important action item in the short term is to design and implement a program to build entrepreneurial skills, including digital and financial education.

C. Recommendations

141. As part of ENEF activities, digital skills and digital risks need to be mainstreamed. SBP, as the lead institution of ENEF, in collaboration with the ENEF stakeholders, should consider developing specific interventions on the digital skills needed for the use of DFS by individuals and by micro and small enterprises, including merchants. In addition, as part of the consumer protection focus of the ENEF, SBP, together with the ENEF stakeholders, should consider educating consumers on specific risks that can arise due to DFS. These include fraud, data privacy, technology unreliability, business failure or insolvency, disclosure format risks via digital channels, etc.

²⁰ <https://tubalboaconsentido.gob.pa/>

²¹ Law no. 374 of 2023.

VII LARGE-VOLUME, RECURRENT PAYMENT STREAMS

A. Context

142. Large-volume, recurrent payment streams can be leveraged to advance financial inclusion objectives through various channels. The most obvious one is by directly providing transaction accounts to unserved and underserved end users, mainly individuals. In addition, these payment streams can be leveraged to drive investment in core retail payments infrastructure as well as in distribution channels and in the development of new payment products and services.

143. Several government payment operations consist of large-volume recurrent payment streams, such as the payment of social benefits, wages, pensions, and other social security payments and contributions. Mass transport payment systems are another case of large-volume payments that are usually operated by the public sector. In the private sector, large-volume payment streams include employer payrolls and others.

144. Migrants and their families are among those less likely to be financially included. Given the volume of domestic and international remittances, there would appear to be space to leverage the periodic and ongoing use of remittances to foster financial inclusion, at least among these population groups.

B. Status in the country

Government payments

145. Government payments in Panama are largely digitalized, however, there is room for improvement from a financial inclusion perspective.

146. Most pensioners receive their pensions into their bank accounts via ACH transfers. Pensions paid via checks are an exception. During the pandemic, in discussion with the ABP, the Government mandated the pensioners to open accounts and gradually moved to using ACH transfers instead of checks. Across all pension programs, there are a total of 9,164 pensioners still receiving their funds via checks while over 300,000 pensioners receive pensions into accounts. The new payment disbursement method led to a cost savings of around \$2.5 million per year from printing and distributing checks.

147. Collection of social security contributions are collected via checks, cash and ACH transfers. Prior to COVID-19, all collections were made in cash. Caja de Seguro Social has been working with banks to enable payments of contributions via online banking.

148. Social protection payments during the pandemic were made digitally into a special e-wallet developed by AIG, which used the QR codes on the national ID cards. These e-wallets do not have transaction account functionalities in that they can only be used to receive social assistance payments and the funds can only be spent in merchants that are affiliated with the program. From the perspective of the Government, this allows for traceability of funds. In addition, spending habits of social assistance payments can help with a better understanding of the real needs of the population and can provide some form of measurement of impact. Solidarity fuel subsidy, provided by the Transit Authority, also uses the same disbursement method, where the funds can be spent at affiliated gas stations. Prior to the pandemic, most of these payments were disbursed into Clave Social cards, which are pre-paid cards specifically for social assistance payment beneficiaries that had transaction account properties: safe storage of funds, cash withdrawals at ATMs, and POS payments where Clave cards are accepted. The Ministry of Social Development needs to use helicopters to reach a few remote areas of the country to distribute social assistance payments in cash.

149. Most local government payments are not digitalized. Some of the local governments make payroll payments into bank accounts via ACH transfers. The Municipality of Panama has an online portal offering several local government services, for which payments can also be made online on the portal. However, most companies prefer to make payments in checks. The portal integrates with some other authorities' systems, including, for example, the Transit Authority for license plates or with Tribunal Electoral to verify the cedula numbers, but not with the Public Registry of Panama (RPP). At the same time, however, other municipalities do not have similar online services. Lastly, all vendor payments by all municipalities are done by checks as well as social assistance payments to the vulnerable groups.

Remittances

150. The Panamanian international remittances market has changed over time: at the start of the century, Panama was a net receiving country. From 2009 onward, Panama became a net sending country, following the inward migration patterns. According to the estimates by remittance service providers (RSPs) in the market, around 70 percent of remittance flows in the Panamanian market were outbound prior to the start of the COVID-19 pandemic. This trend has reversed since then, and at the

time of the writing of this report, around half the flows were inbound and the other half were outbound.

151. Remittances are mostly sent and received in cash and channelled mainly through money transfer operators (MTOs). Regulated money remitters that provide remittance services must have minimum capital requirements and are subject to auditing on a periodic basis by MICI. Money remitters must publicly disclose their prices for all their services.

C. Recommendations

152. Panamanian authorities are recommended to exploit further opportunities for financial inclusion through digitalization of government payments that are currently done by cash and checks. For example, most local government payments for social assistance and to vendors are done via checks as well as most local government collections.

153. Panamanian authorities are recommended to reconsider the payment method for social assistance programs from a financial inclusion perspective. While the payment method developed by AIG for use during the pandemic enabled quick and effective disbursements of social assistance, by moving away from the use of Clave Social cards, the new payment method eliminates the financial inclusion element as it is a closed loop instrument. Disbursing social assistance payments into transaction accounts can empower the beneficiaries with financial tools which can potentially be used for further risk mitigation through savings or small loans. Social assistance payments for emergencies can use different payment instruments for disbursements due to their special nature and the need to reach a large number of beneficiaries quickly. Such beneficiaries may not necessarily qualify for regular social assistance programs which have the main goal of reducing poverty over the long term, and therefore, financial inclusion considerations are of secondary importance. On the other hand, with regular social assistance programs with lifting beneficiaries out of poverty as the primary objective can empower beneficiaries over the long term with a transaction account, enabling them access the regulated financial system.

154. Digitalization of remittances can help improve financial inclusion in Panama. In addition, digital remittances are shown to have lower cost, enabling savings in terms of fees and commissions.²² Sending and receiving remittances is usually the one time when migrants and their families have to

²² See World Bank (2022), Remittance Prices Worldwide Quarterly Report, December 2022.

interact with the regulated financial sector. This can be used as an opportunity to promote account-to-account remittance transfers.

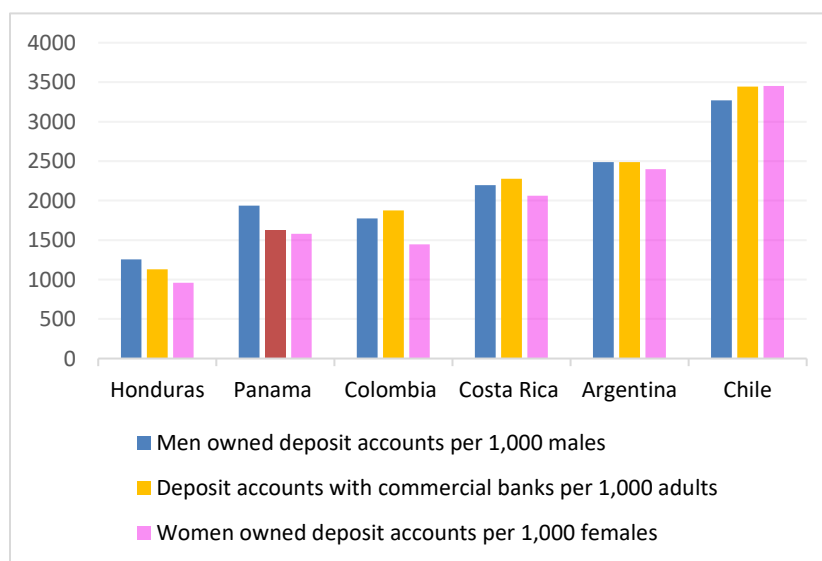
ANNEX I – OVERVIEW OF FINANCIAL INCLUSION IN PANAMA

Access to Transaction Accounts

1. **As of 2021, Panama ranked relatively poorly among its geographical peers in access to deposit accounts.**²³ The number of deposit accounts per 1,000 adults grew by over 40 percent between 2012 and 2021, but the country still lags its peer economies in the number of accounts per person. While access to account has been growing, the gender gap has become wider: the number of accounts per person grew by 33 percent among men and only by 13 percent among women from 2015. On average, men have 22 percent more deposit accounts than women, which makes it the third most unequal country in the Latin American region.

2. **At the same time, the 2021 data does not yet fully capture the rapid growth in account ownership during the COVID-19 pandemic.** It could not have yet accounted for the popularity of Yappy and other app-based simplified accounts, which grew the fastest throughout 2022 and the first half of 2023. It is possible thus that Panama is on its way to reducing or closing the gap.

Figure 1: Deposit Accounts with Commercial Banks (2021).



Source: IMF Financial Access Survey (2022)

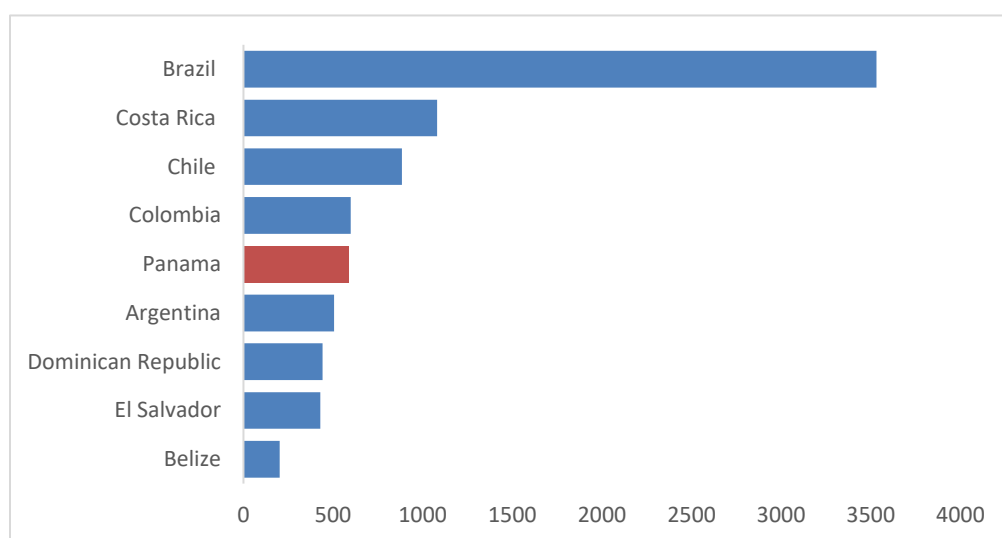
²³ See International Monetary Fund (2022), Financial Access Survey, October 2022.

Access to Credit

Households

3. Despite the large size of Panama's financial sector, access to credit compares poorly with neighbor countries. As per the IMF Financial Access Survey (2022), access to credit in Panama is about 36% lower than the LATAM average (Figure 2). Even though Panama has one of the largest and most developed financial sectors in Latin America, it has failed to improve access to credit since the last FSAP in 2012. The compounded annual growth rate for the number of loan accounts per 1,000 adults in Panama is 1 percentage point lower than the average of its geographical peers in the 10-year-period from 2011, and the number of loan accounts has also declined by over 12% in the last two years.

Figure 2: Number of Loan Accounts with Commercial Banks Per 1,000 Adults (2021).



Source: IMF Financial Access Survey (2022)

4. Alternative data sources confirm that households with lower income have relatively lower access to credit; especially in the case of women.²⁴ Panama's Multiple Purpose Survey (EPM2017) provides insights into households with debt. The survey shows that 16.5 and 23.3 percent of households in the two lowest income brackets have been capable of taking on debt, whereas this

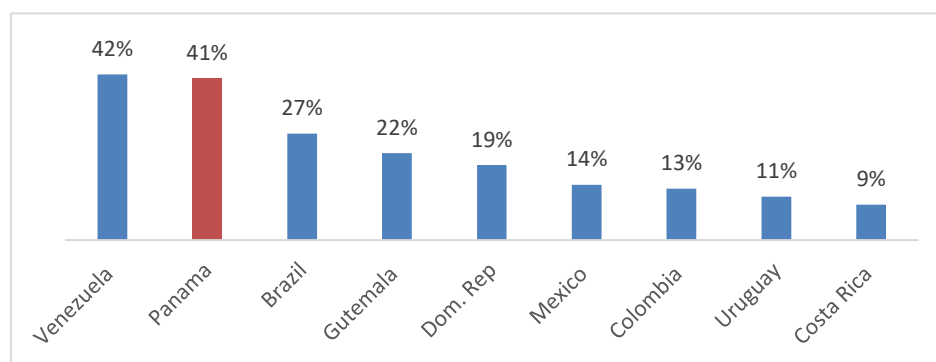
²⁴ For additional details, see IDB (2022) *Inclusión financiera en Panamá. La importancia de la calidad institucional y las brechas territoriales, de ingreso y de género*. Available at: <https://publications.iadb.org/es/inclusion-financiera-en-panama-la-importancia-de-la-calidad-institucional-y-las-brechas>

percentage is around 77 percent for the wealthiest bracket. There is a steep spread between the second and third deciles of 13.3 percent, implying that credit to low-income segments is disproportionately underserved. The same survey includes a gender component showing that, on average, 52 percent of households with a male head had borrowed money, compared to only 46.6 percent of those female-headed. This gap widens among lower-level income households and disappears at higher income levels.

MSMEs

5. MSME financing gaps in Panama are significant. According to the SME Finance Forum, a considerable finance gap exists for SMEs in Panama.²⁵ It shows that Panama had almost 202,000 MSMEs in 2018, of which 26 percent are estimated to be fully financially credit constrained and 5 percent partially constrained.²⁶ Overall, the finance gap is close to US\$ 21.3 billion or 41 percent of the GDP, the largest among regional peers (only surpassed by Venezuela). This finance gap is primarily attributed to the limited availability of financing options, particularly for those SMEs that are in the early stages of development or lack collateral. The lack of access to formal financing also hinders the ability of SMEs to invest in new technology, equipment, and training, limiting their ability to compete in the global marketplace.

Figure 3: Finance Gap for MSMEs Number of Loan Accounts with Commercial Banks Per 1,000 Adults (2021)



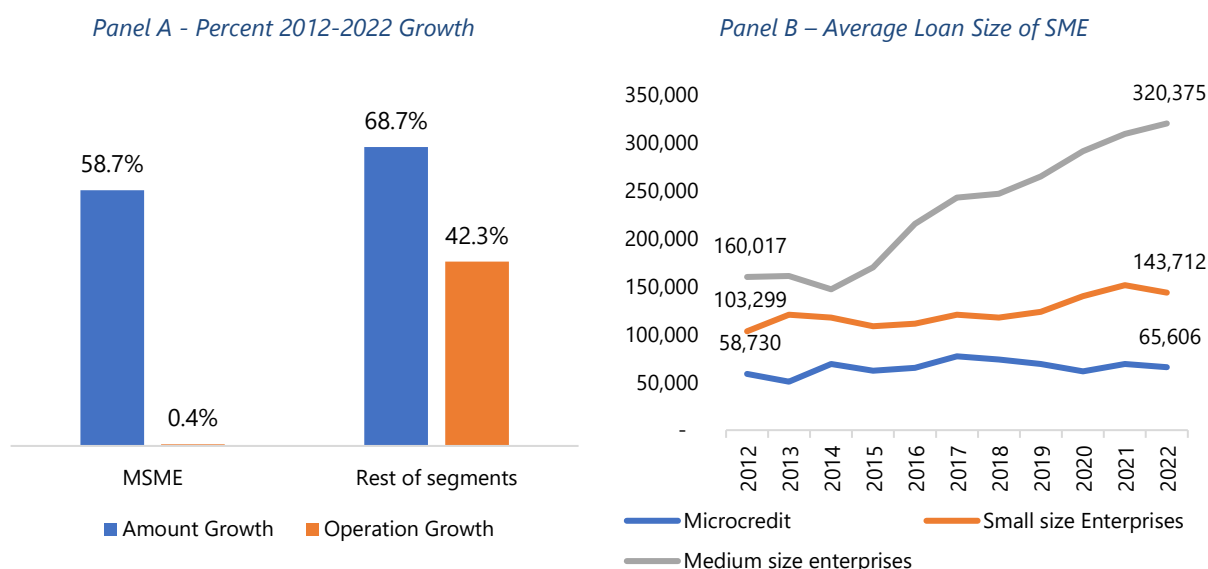
Source: *SME Finance Forum*.

²⁵ Finance Gap is calculated as Potential Demand for MSME finance – Existing Supply. Further explanations in <https://www.smefinanceforum.org/data-sites/msme-finance-gap>

²⁶ Fully financially credit constrained firms are defined as those that find it challenging to obtain credit. Partially constrained firms are defined as those that have been somewhat successful in obtaining external financing.

6. In recent years, the average loan size for MSMEs in Panama has experienced a notable increase, outpacing the inflation rate. Throughout the last decade, credit growth has increased significantly. The total credit outstanding increased by 68.7 percent, and the number of operations by 42.3 percent. In contrast, in the case of MSMEs, the credit amount increased by 59 percent, and the number of operations remained mostly flat, translating into a significant increase in the average size of loans. Panel B of Figure 9 shows the average loan size for medium size enterprises, which doubled in this period; and increased by 39.1 percent for small and 11.7 for micro firms. Inflation from 2013 to 2022 grew by 7.9 percent. The real increase in loan size in the SME sector is a sign of financial exclusion, as larger loan sizes may be a barrier for some smaller businesses to access financing.

Figure 4: Credit Growth and Average Loan



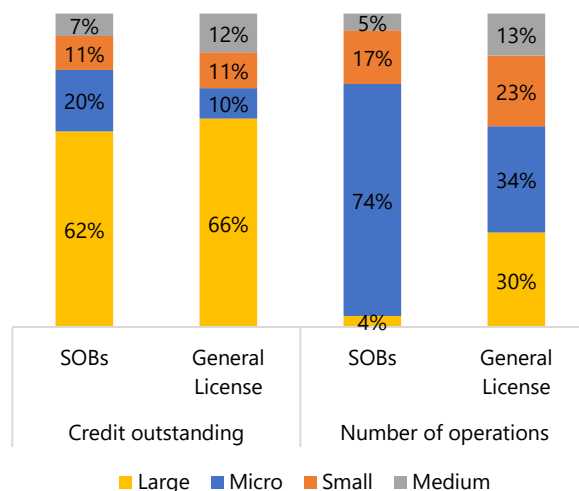
Source: SBP.

Note: MSME operations grew by 17 percent from 2012 to 2017 but then started decreasing back to 2012 levels.

7. Total credit provided to MSMEs has been stable in recent years, close to 15 percent. Since 2013, the share of the total credit received by MSMEs has been close to 15 percent (or 34 percent of the credit to NFCs), with microenterprises representing four percentage points. Across bank types, SOBs show a more significant focus on this market segment as they tilt 38 percent of their credit portfolio and 96 of the number of operations to MSMEs, compared to 34 percent and 70 percent in the case of General License banks, respectively. As shown in Figure 4, Panel A. This market focus is more evident in the case of microcredits. However, at the individual level, the largest providers of

MSME credit are the large Panamanian general license banks, *Banco General* and *Global Bank*. Most MSME borrowers are active in the agriculture, livestock, commerce, industry, and construction sectors.

Figure 5: Distribution of Credit Outstanding and Number of Operations Across Firm Size (Dec-22).



Source: SBP

Regional disparities

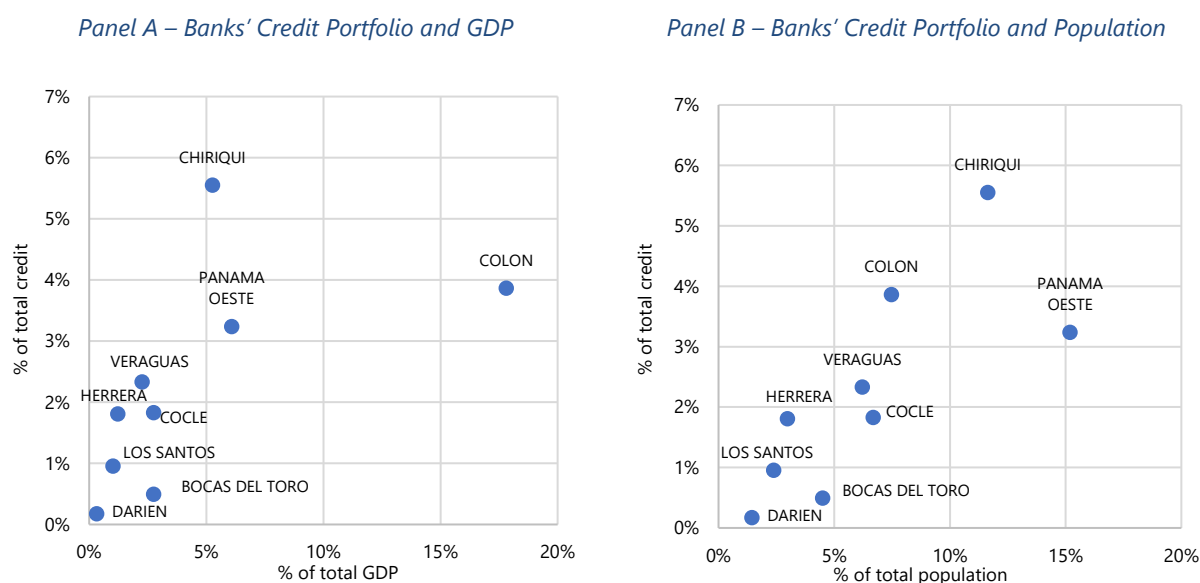
8. Panama City concentrates a higher provision of credit than its contribution to the country's GDP suggests. As the core of business activity in the country, Panama City concentrates 79 percent of the total local credit of the nation. However, its share of GDP is lower, at 62 percent (and 41 of the population). In absence of measurement issues, it is reasonable to expect a similar distribution of banks' credit lending shares and other economic variables, such as GDP.^{27,28} Therefore, provinces with lending shares significantly lower than their contribution to the national production could indicate financial exclusion. This relationship is particularly at odds in Colon, as it represents 17.5 percent of the total GDP and only receives 3.9 percent of total credit. This province's GDP is

²⁷ Usually, the regional distribution of banks' credit portfolio is registered based on the location of bank branch originating the loan. Therefore, as a caveat, there could be a statistical bias on the distribution of banks' credit portfolio across provinces, as loans registered in Panama City could be capturing a share of (i) loan originations to firms that, while residing in Panama City, allocate the loan proceeds to different geographies across the country, (ii) firms not residing in Panama City but traveling there to borrow.

²⁸ While the GDP distribution across provinces can provide a general understanding of the economic potential and credit demand, it is important to consider a wide range of factors to accurately predict or determine the credit portfolio distribution of banks across provinces.

heavily influenced by the construction sector (38.9 percent of total GDP in 2021), which may signal that loans in this segment are underserved or that firms in the construction sector raise funding in other provinces (likely Panama City). Overall, after Panama City, Chiquiri, Colon, and Panama Oeste provinces are the most relevant credit recipients (see Figure 6 for additional details).

Figure 6: Regional Distribution of Banks' Credit Portfolio, GDP, and Population.



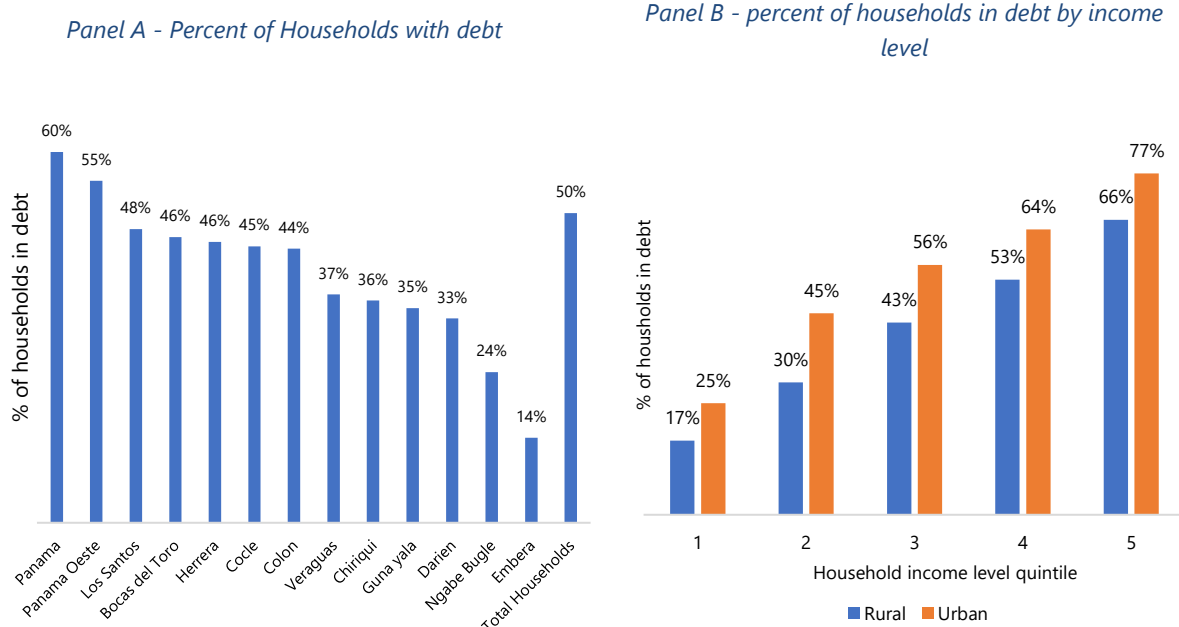
Source: SBP

Note: The Province of Panama gathers 79.8 percent of total credit, 62.1 percent of the total GDP, and 41.5 percent of the total population. For presentation purposes, it is excluded from the graph.

9. Lower access to credit in rural areas persist across households' income distribution, but the gap increases in lower-income families and poorer provinces. The Panama EPM survey reveals significant economic disparities across provinces in Panama, with a notable positive correlation between household and provincial income levels and accessibility to financial borrowing. In 2017, approximately 60 percent of households in the province of Panama had the capacity to take on debt, whereas this figure was merely 14 percent in the province of Emberá. This disparity can be attributed to pronounced income inequality between the provinces, as measured by per capita income. Furthermore, at the household level, credit access tends to be lower for families residing in rural areas compared to those in larger urban centers. Irrespective of household income, urban residents generally have greater opportunities for securing loans, with the disparity becoming more pronounced among lower and middle-income households. For instance, within the lowest income quintile, approximately 25 percent of urban clients and 17 percent of rural clients are indebted,

reflecting a regional gap of approximately 32 percent. In the highest income quintile, 77 percent of urban households and 66 percent of rural households have borrowed money, highlighting a narrower but still prevalent gap of around 15 percent.

Figure 7: Access to Credit by Province and Income Level.



Source: IDB, *Inclusión Financiera en Panamá* (2018).

ANNEX II – GLOBAL AND REGIONAL EXPERIENCES IN REGULATING PAYMENT SYSTEMS

A. Evolution of Payment Systems Regulations

1. Legal and regulatory frameworks governing payment systems have been evolving over time. Most of the early regulations were instrument-specific: for example, the growth in global trade in the 19th century was accompanied by enactment of laws on bills of exchange and negotiable instruments. However, proliferation of new technologies and the growing realization that risks related to payments can affect the broader financial system led to the conclusion that payment systems need to be regulated in a comprehensive, risk-based and technology-neutral manner. For the majority of countries, it meant enacting a separate payment systems law, although in some cases relevant provisions would be included in the central bank law or the banking law. Its key provisions would include legal definitions of key concepts in payment, clearing and settlement (e.g., netting, settlement finality, bankruptcy remoteness of collateral), powers of the relevant authority—usually a central bank—to license and oversee payment systems and payment services, procedures to be followed in the event of insolvency and resolution of payment system operators, as well as consumer protection safeguards for users of payment services. According to the World Bank’s 2021 Global Payment Systems Survey (GPSS), a payment system law—or a similar piece of legislation—has been adopted by 81 percent of world’s jurisdictions.²⁹

2. Banks are no longer the only providers of payment services, a fact that had to be reflected in laws, regulations and licensing frameworks. While there is considerable heterogeneity in the way in which general payment system concepts are implemented in domestic legislation, nearly every law follows the same broad contours. Among those, one of the most important ones is the distinction between the following two concepts:

- **Payment systems**, understood as the rules, technical infrastructures and other arrangement allowing financial market participants, such as commercial banks and non-bank financial institutions (NBFIs), to transfer funds, and clear and settle obligations between one another. Examples of such systems include Fedwire or CHAPS in the United States, ACH Directo in Panama,

²⁹ In addition, 97 percent of respondents to the GPSS have a central bank law and 85 percent have a banking law which includes direct references to payments and financial market infrastructures, including defining the powers and obligations of the payment system regulator and laying out main public policies in the area of payments.

or card networks such as Visa or Mastercard. Operating such systems does not involve providing direct services to individual consumers or non-financial businesses (e.g., an individual cardholder does not directly interact with Visa or Mastercard). Accordingly, the phrase "system participants" or "members" refers in this context to commercial banks and NBFIs.

- **Payment services**, understood as services such as electronic money issuance, third-party card processing, bill payments or domestic and international remittances. They generally do not perform clearing and settlement functions; on the other hand, they do provide services to non-financial businesses and general public.

3. While this note, in line with the terminology used by most global standard-setting bodies, will use the names "payment system" and "payment service" to refer to, respectively, the first and the second concept, that nomenclature is not universal. The following table presents equivalencies between legal terms used in selected major jurisdictions. What is important is not the exact terminology used, but rather the clear differences between risk profiles of those entities. Payment systems may pose credit and liquidity risk, and the important goal of regulating them is ensuring that obligations between participants are settled, even in extreme but plausible market conditions. Because high-value payment systems play an important role in interbank lending and execution of monetary policy, mismanagement of their risks may result in contagion and create crises for the entire financial system. On the other hand, supervision of payment services is more focused on the protection of their customers' funds, operational risk management and financial integrity (AML/CFT). While the failure of large payment service providers can certainly affect market confidence and have systemic consequences, those risk normally do not stem from network effects.

Table 1: Naming conventions used to refer to payment systems and services in selected G20 countries.

Jurisdiction	Payment system (for example, an automated clearinghouse)	Payment system operator	Payment service (for example, electronic money issuance)	Payment service provider
Australia	<i>Payment system</i>	-	<i>Purchased payment facility*</i>	<i>Provider</i>
Brazil	<i>Settlement system</i>	<i>Clearinghouse</i>	<i>Payment scheme</i>	<i>Payment institution</i>

		<i>Clearing and settlement service provider</i>		<i>Payment scheme owner</i>
Canada	<i>Clearing and settlement system³⁰</i>	<i>Clearing house</i>	<i>Payment function and/or retail payment activity</i>	<i>Payment service provider</i>
European Union	<i>Payment system</i>	<i>payment system operator</i>	<i>Payment service</i>	<i>Payment service provider</i>
Hong Kong SAR, China	<i>Payment system</i>	<i>System operator</i>	<i>Stored value facility*</i>	<i>Issuer*</i> <i>Facilitator*</i>
India	<i>Payment system</i>	<i>System provider</i>	<i>Payment system</i>	<i>System provider</i>
Indonesia	<i>Payment system infrastructure</i>	<i>Payment system infrastructure provider (PIP)</i>	<i>Payment system</i>	<i>Payment service provider (PJP)</i>
Mexico	<i>Payment system</i>	<i>System administrator</i>	-	<i>Electronic Payment Fund Institution (Institucion de Fondos de Pago Electrónico)*</i>
Turkey	<i>Payment system</i>	<i>System operator</i>	<i>Payment service</i>	<i>Payment service provider</i>

Terms marked with an asterisk () refer specifically to the issuance of electronic money.*

4. Several other concepts entered the field of payment regulation in the recent years.

Payment schemes are defined, somewhat ambiguously, as "set[s] of formal, standardized and common rules enabling ... electronic payment instruments". The concept was popularized by the European Union's 2015 Interchange Fee Regulation (IFR), which aimed at separating the "rules layer"

³⁰ Payment Clearing and Settlement Act 1996

from the "processing layer" of international card networks, such as Visa or Mastercard. The former—the payment scheme—is to be managed by the international network and includes aspects such as branding, user experience, technical requirements for cards or mobile apps, cost- and revenue-sharing, as well as dispute resolution frameworks. On the other hand, the processing entity, which could be separate from the scheme manager, would be responsible for conducting the actual exchange of authorization and clearing messages.

5. The distinction between schemes, processors and underlying clearing and settlement infrastructures is still ambiguous, and relatively few countries outside the EU introduced similar regulations. However, it is worth noting that this distinction is also applied in Brazil with respect to Pix: Pix itself is legally defined as a payment scheme (*arranjo de pagamento*), distinct from the underlying settlement infrastructure (*Sistema de Pagamentos Instantâneos—SPI*).

6. In addition to that, some jurisdictions recognize the concept of critical service providers: entities that are neither payment system operators nor payment service providers, but that perform activities essential to the functioning of both, such as provision of connectivity and messaging services. As an example, Group of Ten (G10) central banks recognize SWIFT as a critical service provider and perform cooperative oversight of the institution, led by the National Bank of Belgium (NBB). Finally, most authorities and standard-setting bodies also use a broader umbrella term—financial market infrastructures (FMI), which, in addition to large-value payment systems also encompasses central securities depositories (CDS), security settlement systems (SSS), central counterparties (CCP) and trade repositories (TR).

B. Approaches to Defining Payment Services

7. While legally defining payment, clearing and settlement systems is relatively simple, developing a coherent definition of payment services is more challenging. The landscape of payment services and their providers is diverse and heterogeneous: it includes activities ranging from third-party merchant acquiring to electronic money issuance. Because of that, most jurisdictions ended up adopting an enumerative approach: relevant laws and regulations simply contain the list of activities that are considered to be payment services. Sometimes a second list is also included: this is the list of exceptions—types of services that, even though they seem to be included on the first list, are not to be considered payment services. That latter list is generally used to provide exemptions from relevant regulations to limited acceptance instruments, such as store gift cards, or to services

regulated by other legal instruments, such as securities settlement systems. Selected examples of that approach are presented in Table 2.

Table 2: Definitions of "payment service" in selected jurisdictions.

	Activities that are payment services	Activities that are not payment services
European Union	<p>Account cash-in and cash-out</p> <p>Execution of direct debits, card transactions and credit transfers</p> <p>Issuance of cards (or other payment instruments) and merchant acquisition</p> <p>Remittance services</p> <p>Payment initiation and account information services</p>	<p>Payments between banks or PSPs executed within a payment, clearing or settlement system</p> <p>Physical transport of banknotes</p> <p>Cash-to-cash currency exchange</p> <p>Point-of-sale cashback</p> <p>Transactions based on cheques or paper-based drafts and money orders</p> <p>Third-party technical infrastructure provision (e.g., data storage or network connectivity)</p>
Canada	<p>"Payment function that is performed in relation to an electronic funds transfer that is made in the currency of Canada or another country"</p>	<p>Limited-purpose electronic money</p> <p>ATM withdrawal</p> <p>Internal transfers between affiliated entities</p> <p>Transactions within a designated payment, clearing or settlement system</p> <p>Activities performed by commercial banks, credit societies, insurance companies, loan companies, the central bank or the designated payment system operator</p>

Singapore	Account issuance Domestic and cross-border money transfer Merchant acquisition Electronic money issuance Digital payment token issuance Currency exchange	Payments with cheques, money orders, drafts and postal orders Payments between two or more participants in a payment system Physical transport of currency Provision of ancillary technical infrastructure (data processing and storage, authentication and IT security, communication networks, point-of-sale terminal maintenance) Transactions with limited-purpose e-money (e.g., store gift cards)
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C. Licensing Authorities and Procedures

8. Just as laws and regulations applicable to payment systems have evolved in response to changing markets and emerging risks, so did licensing procedures for payment system operators and payment service providers. In the early days of digital payments, authorities considered licensing such entities redundant—it was assumed that, since they provide services to commercial banks, indirect oversight through banking supervision departments would be sufficient. This is no longer the case, and payment systems and services are licensed, supervised and overseen. Details, however, differ across jurisdictions.

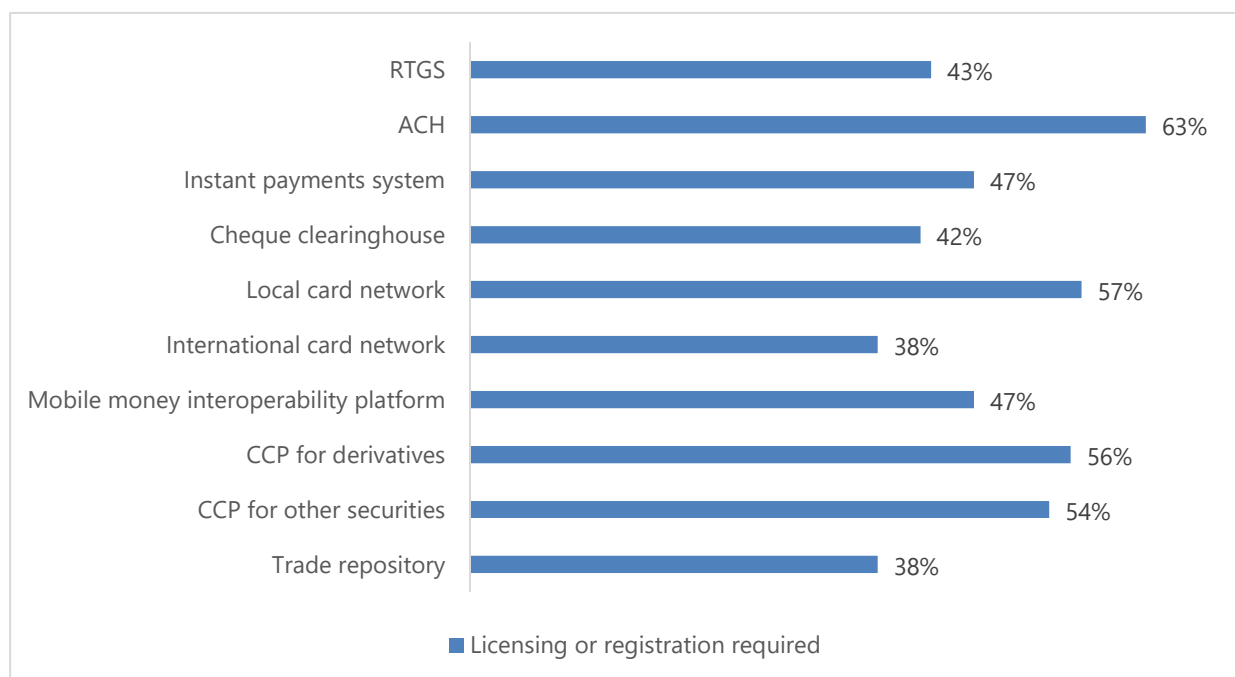
9. With respect to payment system operation authorities around the world have generally adopted either of the following approaches:

- **Operating payment systems is not subject to licensing, but there is a special designation procedure which, if applied, results in the system and its operator being subject to oversight by the regulator.** This approach is adopted, for example, by the United States and Canada. In this model, the operation of a payment system such as an ACH or an RTGS is not a subject to license and, in theory, any institution can perform such an activity without asking for permission. However, the law defines a procedure by which the regulator may designate a payment system as

“systematically important”. Such a designation automatically empowers the authorities to perform oversight activities, including but not limited to performing on-site and off-site inspections, issuing instructions to the operator and imposing certain risk management standards. There may be certain criteria used in evaluating whether the system is systemically important, such as the market share, the type of payments cleared and settled by the system, or transaction volumes and values. Furthermore, certain jurisdictions apply various level of designation with concomitant designation criteria and oversight standards. For example, the European Central Bank beyond designating systems as “systemically important” may also declare them to be “prominently important retail payment systems” (PIRPS).

- **Full-fledged licensing, registration or authorization procedure for all payment systems and financial market infrastructures.** This approach, adopted by approximately half of the jurisdictions (see Figure X), requires every operator of a payment system to obtain license or authorization from the relevant authority before commencing operations. On top of that, systems designated as systematically important may be subject to additional rules and requirements. Systems operated by central banks are typically exempt for such licensing requirements.

Figure 1: Share of jurisdictions requiring license or registration for operators of payment systems and financial market infrastructures.



10. Typically, central banks play the leading role in licensing, supervision and oversight of payment systems and payment services, but institutional arrangements vary across jurisdictions. Latin America in particular is characterized by the institutional division between central banks and banking regulators (superintendencies); only very few jurisdictions have adopted the unified regulator model. As a consequence, banking regulators play a relatively more important role in the payments ecosystem, particularly with respect to licensing and supervision of payment service providers. Based on the World Bank's analysis of 11 jurisdictions, presented in Table 3, seven of them (64 percent) designated the banking supervisor as the lead licensing authority for payment service providers. Licensing or registration of payment system operators is typically the responsibility of the central bank, but Colombia and El Salvador bestowed that power upon their banking superintendencies (in Colombia only with respect to low-value payment systems).

Table 1: Licensing authorities for payment systems and payment services in selected Latin American jurisdictions.

Country	Authority responsible for licensing payment, clearing and settlement systems operators	Authority responsible for licensing payment service providers, including electronic money issuers	Notes
Argentina	Central Bank of the Argentine Republic	Central Bank of the Argentine Republic	<p>Payment system operators (other than those operated by the central bank) are licensed as clearinghouses (cámaras de compensación) in accordance with the Communication "A" 2557 of the Central Bank of the Argentine Republic.³¹ Clearinghouses must be limited liability companies whose shareholders (directly or indirectly) must be licensed financial institutions.</p> <p>PSP licensing procedure is outlined by the Communication "A" 7712.³²</p>
Brazil	Central Bank of Brazil	Central Bank of Brazil	Non-bank payment service providers can be licensed as "payment institutions" according to the Law 12,865 of October 9, 2013.
Chile	Central Bank of Chile	Financial Market Commission	There is no single "payment service provider" license, but most non-bank payment service providers have been licensed as card issuers or operators of card systems ("Empresa Operadora de Tarjetas"). While the Financial Market Commission is responsible for issuing licenses, the Central Bank of Chile is responsible for prescribing all technical standards pertaining to payment services.

³¹ <https://www.bcra.gob.ar/Pdfs/comytexord/A2557.pdf>

³² <https://www.bcra.gob.ar/Pdfs/Textord/t-snp-bsp.pdf>

Colombia	Bank of the Republic (as the operator of high-value payment systems) Financial Superintendent of Colombia (for low-value payment systems)	Financial Superintendency of Colombia	<p>Most payment systems (CEDEC-CCSD, CENIT, CUD, SEN), including all systemically important systems, are operated in-house by the Bank of the Republic.</p> <p>According to the Decree 1692 of 2020, the Superintendency is the authority responsible for licensing and oversight of low-value payment systems ("sistemas de pago de bajo valor").</p> <p>are licensed and regulated as "companies specializing in deposits and electronic payments" ("sociedades especializadas en depósitos y pagos electrónicos"—SEDPE). Licensing is the responsibility of the Financial Superintendency of Colombia in accordance with the Law 1735 of 2014.</p>
Costa Rica	-	General Superintendency of Financial Institutions	<p>All relevant payment systems are operated in-house by the central bank. While the General Superintendency of Financial Institutions managed the process of payment service providers registration, it is the central bank that determines the technical standards applicable to them.</p>
El Salvador	Superintendency of the Financial System	Superintendency of the Financial System	<p>The Superintendency of the Financial System issues licensed to clearinghouse operators based on the Article 24 of the Banking Law. However, the operating rules of the clearinghouse must be approved by the central bank before the license is issued.</p> <p>On the basis of the Law on Fostering Financial Inclusion (Ley Para Facilitar La Inclusion Financiera), the Superintendency also issues licenses for electronic money providers (Sociedades Proveedoras de Dinero Electrónico—SPDE). However, also in this case the Central Reserve Bank of El Salvador is responsible for the issuance of technical standards concerning the operation of electronic money issuers.</p>

Guatemala	Bank of Guatemala	-	<p>While the majority of payment systems are operated in-house by the central bank, it has issued an authorization for a company owned by the consortium of commercial banks (Imágenes Computarizadas de Guatemala) to operate an automated clearinghouse.</p> <p>There is no licensing framework for payment service providers, including electronic money issuers.</p>
Honduras	Central Bank of Honduras	Central Bank of Honduras	<p>The Central Bank of Honduras authorizes entities operating payment systems based on the Law on Payment and Securities Settlement Systems of 2008.</p> <p>Licensing of payment service providers is performed by the central bank in accordance with the Regulation on the Services Offered by Entities Providing Electronic Payment Services (13/2022).</p>
Mexico	Bank of Mexico	National Banking and Securities Commission	<p>With respect to payment systems, the Bank of Mexico follows the “designation” model. According to the Law on Payment Systems of December 12, 2002, only systems that reach a certain threshold of transaction volumes are considered “payment systems” for the purpose of the law. Such a designation is announced by the central bank in the official gazette (Diario Oficial de la Federación). Within ten days of the designation date, the operator must submit system rules for the central bank’s approval. Systems that have not met the designation threshold are not subject to licensing and formal supervision.</p> <p>The National Banking and Securities Commission is the licensing authority for electronic money issuers, known as Electronic Fund Transfer Institutions (Instituciones de Fondos de Pago Electrónico—IFPE), as prescribed by the Law on the Regulation of Financial Technology Institutions of March 9, 2018. However, the</p>

			<p>decision to authorize the new provider must also be approved by the Interinstitutional Committee, consisting of two representatives of each of the three institutions: the Bank of Mexico, the National Banking and Securities Commission, and the Secretariat of the Treasury and Public Credit. While decisions are adopted by simple majority, approval of license applications requires a “yes” vote for at least one representative of each authority.</p>
Nicaragua	-	Superintendency of Banks and Financial Institutions	<p>All relevant payment systems are operated by the central bank. The Superintendency of Banks and Financial Institutions licenses electronic money issuers, known as Electronic Money Entities (Entidades de Dinero Electrónico) according to the procedure prescribed by the Resolution CD-SIBOIF-671-1-MAR30-2011 of March 30, 2011.</p>
Peru	Central Reserve Bank of Peru	<p>Central Reserve Bank of Peru</p> <p>Superintendency of Banking, Insurance, and Private Pension Fund Administrators</p>	<p>According to the Law 29440 on Payment and Securities Settlement Systems and the concomitant regulations (Circular 012-2010-BCRP of May 3, 2010), Peru applies the designation model, similar to the one followed by Mexico. Based on the volume and value of processed payments, as well as the interconnectedness with other financial infrastructures, the central bank can issue a designation (reconocimiento), subjecting a payment system to its supervision. The designation can be issued <i>ex officio</i> or based on the request from the system operator.</p> <p>Regulation of payment services is more complex. According to the Law 29985 on Basic Characteristics of Electronic Money as an Instrument of Financial Inclusion, electronic money issuers, known as Enterprises Issuing Electronic Money (Empresas Emisoras de Dinero Electrónico—EED), are licensed by the Superintendency of Banking, Insurance, and Private Pension Fund Administrators. Before issuing the license, however, the Superintendency has to</p>

receive approval from the Central Reserve Bank of Peru. Furthermore, if the electronic money issuer offers mobile wallet services or QR code-based payments, it must register with the central banks in accordance with the Circular 0003-2020-BCRP of January 31, 2020.

11. The payment services market is rapidly evolving. New fintech products may challenge the applicability of traditional concepts and require regulators to adopt a more agile posture. It is important to ensure that the existing legal and regulatory requirements do not discriminate against the use of a particular technology or disregard the use of technologies altogether. From the perspective of payment services oversight, it is critical to ensure the overall safety and integrity of a payment infrastructure. The involvement of a large number and type of providers (e.g., intermediaries, third-party service providers, etc.) may lead to new types of risks. Oversight frameworks need to be designed or updated to take these into account. In this regard, technologies can support authorities in fulfilling their supervisory and oversight tasks and market participants in meeting requirements more effectively and efficiently.

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