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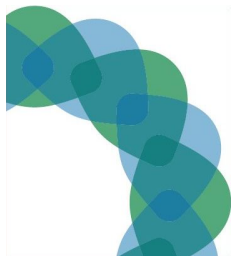
Global Partnership
for Financial Inclusion



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Basel, Switzerland

2nd GPI Conference on Standard-Setting Bodies and Financial Inclusion

Session 2: Digital Financial Inclusion and the work of the Standard-Setting Bodies



Hosted by

FINANCIAL STABILITY INSTITUTE



BANK FOR INTERNATIONAL SETTLEMENTS

Agenda

- Basel Committee on Banking Supervision (BCBS)
- Committee on Payments and Market Infrastructures (CPMI)
- Financial Action Task Force (FATF)
- International Association of Deposit Insurers (IADI)
- International Association of Insurance Supervisors (IAIS)
- International Organization of Securities Commissions (IOSCO)



Basel Committee on Banking Supervision (BCBS)

Basel Committee on Banking Supervision



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Why is digital financial inclusion relevant to BCBS and vice versa?

- Basic elements of digital financial inclusion models are relevant to BCBS:
 - Deposit-like stored-value products that combine features of payment instruments and current accounts, introducing new risks from banking angle; and
 - New market participants that alter roles and relationships among banks and non-banks, potentially changing nature and level of risks
- Such developments raise questions about expansion of supervisory perimeter for banks (and non-banks) and about interaction with other supervisors



Why is digital financial inclusion relevant to BCBS and vice versa?

- Revised 2012 Basel Core Principles (BCPs) reinforce concept of proportionality and allow banking regulators and supervisors to:
 - Accommodate diverse range of banking systems; and
 - Allow assessments of compliance that are commensurate with risk profile and systemic importance of broad spectrum of banks
- Supervisors now in better position to adapt their approaches to accommodate diverse digital financial inclusion models



Recent BCBS activities relevant to digital financial inclusion

- Basel Consultative Group (BCG) Workstream on Financial Inclusion focuses on:
 - Wide and rapidly evolving range of providers and provider ecosystems
 - Innovative deposit-like products for base-of-the-pyramid customers
- BCG Workstream's Range of Practice Survey includes:
 - Non-bank money issuers/distributors among provider categories
 - Questions regarding use of agents, permissible activities
 - Questions about operations permitted by regulation that are initiated and transmitted by mobile devices
 - Issues around licensing and supervisory cooperation
 - Issues around new data-driven approaches to credit risk management



Recent BCBS activities relevant to digital financial inclusion

(continued)

- As follow-up to Range of Practice Survey, BCBS BCG guidance paper planned for 2015 to include guidance on application of revised BCPs to digital financial inclusion
- BCBS 2014 guidance paper *Sound management of risks related to money laundering and financing of terrorism*:
 - Addresses bank's use of other banks, other types of financial institutions (including non-banks), or third parties such as retail agents to perform customer due diligence



Committee on Payments and Market Infrastructures



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Why is digital financial inclusion relevant to CPMI and vice versa?

- Innovations in retail payments have the potential to lower costs and to reduce entry barriers for customers
- Increasingly diverse products and suppliers will lead to more complex retail payments. Depending on the specific mandate of the central bank, this could require:
 - Broader focus of central banks to include legacy and new payment instruments, as well as relevant providers
 - Reconsideration of tools used by central banks to ensure consistent oversight of more complex retail payment systems
 - Balanced regulatory approach to prevent inconsistencies among already established regulatory requirements
 - Consideration of risk and level-playing-field issues with respect to banks and non-banks



Recent CPMI activities relevant to digital financial inclusion

- In 2011, CPMI and World Bank established Joint Forum on Retail Payments - objective is to advance dialogue around developments in retail payments. Recent topics: payments platforms to facilitate remittances and innovations in retail payments
- The 2012 report on *Innovations in retail payments*:
 - Catalogued innovative developments, identified drivers and barriers to innovation and potential issues and challenges for central banks
 - Innovations and financial inclusion: special limited-service bank accounts/prepaid accounts with non-banks; business correspondents/agents; and new means for transaction initiation and authentication
 - Need for central banks to cooperate with other authorities at national and international level as role of non-banks is increasing



Recent CPMI activities relevant to digital financial inclusion

- CPMI's 2014 *Non-banks in retail payments* report breaks new ground:
 - Categorises non-banks in retail payments
 - Reviews factors influencing the increasing presence of non-banks
 - Addresses the implications for efficiency and risk
 - Describes regulatory and oversight approaches
 - Addresses issues of competition and cooperation between banks and non-banks, of interest to financial inclusion
 - Sets out challenges posed for central banks and other authorities
 - States that central banks could act as catalysts complementing oversight role



Recent CPMI activities relevant to digital financial inclusion

(continued)

- CPMI and the World Bank convened Task Force on Payments Aspects of Financial Inclusion (PAFI) has goal of providing guidance on:
 - Ways to increase inclusion in payment services, examining demand and supply side factors
 - Actions public authorities could take to promote broader access to payment services
- PAFI report, expected in 2015, will inform on:
 - The potential role of payment services as gateway to other financial services targeting financially excluded/underserved customers
 - Role of legal and regulatory frameworks in facilitating effective access to payment services and impact that design and governance of payment systems could have on accessibility and inclusiveness
 - Leverage social benefit transfers to expand access to financial services



Financial Action Task Force (FATF)



Why is digital financial inclusion relevant to FATF and vice versa?

- Safeguards against money laundering and terrorist financing and financial inclusion are mutually reinforcing goals and objectives
 - Customer identification and transaction recordkeeping are essential to inform private sector marketing decisions, fraud prevention, and consumer protection—to achieve scalability and sustainability
 - Financial inclusion supports law enforcement goals
- Key to ensuring AML/CFT safeguards are compatible with financial inclusion and DFS is the FATF risk-based approach to AML/CFT



Recent FATF activities relevant to digital financial inclusion

- Risk-based approach allows countries to adopt more flexible set of measures in order to target resources more effectively and apply preventive measures commensurate to risks
 - For higher risk situations, countries should strengthen AML/CFT requirements
 - BUT...Countries have considerable flexibility where money laundering or terrorist financing risk may be lower
 - *Provided country or financial institution conducts an adequate risk assessment that fully justifies its action*, simplified customer due diligence (CDD) measures could be appropriate



Key Issues and Recent FATF activities relevant to digital financial inclusion

- When and where simplified CDD is appropriate for financial inclusion purposes, and whether new digital technologies can be leveraged to satisfy CDD requirements are the AML/CFT issues of greatest relevance for digital financial inclusion
- Recent FATF Policy Work on Financial Inclusion
 - February 2013--Methodology for Assessing Technical Compliance and Effectiveness
 - February 2013--Guidance, Anti-Money Laundering and Terrorist Financing Measures and Financial Inclusion
 - June 2013--Guidance, Applying Risk Based Approach to Prepaid Access, Mobile Payments, and Internet banking
 - June 2014—Virtual Currency Key Terms and Potential Risks



International Association of Deposit Insurers (IADI)



Why is digital financial inclusion relevant to IADI and vice versa?

- Stored-value aspect of digital transactional platforms raises question of whether customers' balances fall within the definition of an "insured deposit" under law
- The offering of digital deposit-like products by new players raises the question of whether they should be brought into deposit insurance schemes
- Expanding coverage raises issues of technical difficulties of insuring entities not regulated and supervised in the same way as banks



Recent IADI activities relevant to digital financial inclusion

- IADI's 2013 *Financial Inclusion and Deposit Insurance: Research Paper* incorporates consideration of relevance to digital financial inclusion:
 - Some jurisdictions cover or are considering coverage for digital stored-value products under their deposit insurance systems
 - Most formal definitions of insured deposits appear broad enough to include innovations in delivery, as long as they are provided by eligible members of the deposit insurance system
 - There is broad recognition of the many practical issues regarding extending deposit insurance to digital deposit-like products, which are yet to be explored by IADI



Recent IADI activities relevant to digital financial inclusion

(continued)

IADI's updated *Core Principles for Effective Deposit Insurance Systems* - to be finalized by end of 2014 – indicate that:

- Deposit insurers should keep abreast of financial inclusion initiatives and technological innovations, particularly those affecting unsophisticated small-scale depositors
- Extension of coverage to digital stored-value products should be undertaken with strong engagement of, and coordination with, supervisory authorities
- Public awareness campaigns should address which products are covered by deposit insurance and which are not, in order to minimize confusion among depositors and providers



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International Association of Insurance Supervisors (IAIS)



Why is digital financial inclusion relevant to IAIS and vice versa?

- The IAIS has broad membership, with considerable number of members from emerging markets and developing economies
- Developments in technology bring greater access to insurance but pose challenges from perspective of policyholder protection
- Proportionate application of IAIS Standards and capacity are significant challenges for insurance supervisors



Recent IAIS activities relevant to digital financial inclusion

- The IAIS' *Application paper on regulation and supervision supporting inclusive insurance markets* recognizes importance of technology-based distribution to expand access to insurance, suggests criteria for fostering technical innovations, including:
 - Formalization requirements
 - Facilitation of innovations
 - Enabling pilots
 - Adoption of proportionate approach to supervision and regulation
- The application paper recommends that people should know they have insurance coverage and when it ends, and notes that insurance offered via digital platform can be more challenging (layering of insurance)



Why is digital financial inclusion relevant to IAIS and vice versa?

- Expansion of insurance sold through or with mobile network operator (MNO) triggers new issues, in particular in area of conduct of business:
 - Power imbalance between MNOs and insurers
 - Existence of multiple regulatory and supervisory authorities, resulting in overlaps, gaps, or ambiguity in regulatory oversight
 - Possible confusion among customers as to who is insurer
 - Questions regarding who pays premiums and who settles claims and related reinsurance issues



Why is digital financial inclusion relevant to IAIS and vice versa?

(continued)

- Agents of typical digital platforms will often not meet definition of “agent” qualified to sell insurance under country’s laws
- However, digital platforms may make possible delivery of insurance products that are affordable to customer and profitable to insurer
- The proportionate approach endorsed in IAIS Insurance Core Principles (ICPs) allows for:
 - Recognition of diversity of potential insurance intermediaries
 - Space in application of ICPs to permit delivery and servicing of insurance products via digital platform
- However, technical aspects and non face-to-face relationship may call for focus on specific risks



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Recent IAIS activities relevant to digital financial inclusion

- The IAIS is developing issues paper on market conduct and distribution that include MNOs - or other “client aggregators” outside of traditional broker space, including entities whose core business is not insurance
- In support of IAIS’ work in financial inclusion, Access to Insurance Initiative (A2ii) has:
 - Provided input to paper on innovative insurance business models and their associated consumer protection risks, as well as on potential regulatory responses
 - Held consultation calls on (digital) technology in insurance for supervisors
 - Developed training module on financial inclusion, which includes digital issues



International Organization of Securities Commissions (IOSCO)



Why is digital financial inclusion relevant to IOSCO and vice versa?

- Rapidly changing nature of financial markets and products, mainly due to technological changes and financial innovation, triggers regulatory concerns related to retail investor protection. Investment protection is pre-requisite of financial inclusion
- Investment products are already reaching poor retail customers via digital transactional platforms in multiple countries. Such customers, particularly in emerging markets (EMs), are most vulnerable and need protection
- Regulation of sales and distribution of financial products relies heavily on disclosure, but challenges exist in approaching this issue with digitally marketed securities and BoP customers
- Financial education is important, as well as sound regulatory and supervisory frameworks to ensure that digitally marketed securities are safe to invest in – especially for youth, given their large representation among early adopters of digital financial inclusion



IOSCO mandate and activities relevant to digital financial inclusion

- IOSCO's Objectives and Principles of Securities Regulation (38 Principles) are based upon three objectives of importance to digital financial inclusion:
 - Protecting investors
 - Ensuring that markets are fair, efficient, and transparent
 - Reducing systemic risk
- IOSCO's Growth and Emerging Markets Committee is dedicated to emerging market matters, where financial inclusion is major issue
- IOSCO has comprehensive capacity building program for EMs, where digital financial services are booming



IOSCO mandate and activities relevant to digital financial inclusion

- IOSCO Committee 8 on Retail Investors conducts policy work on retail investor education and financial literacy and advises to IOSCO Board on emerging retail investor protection matters
- IOSCO members benefit from behavioral economics in their efforts to improve informed decision-making by retail investors and to strengthen consumer protection
- IOSCO is doing work on SME financing, where digital financial inclusion may help alleviate the financing constraints of SMEs and channel financial resources for growth and employment



Recent IOSCO activities relevant to digital financial inclusion

- Some of IOSCO's investor protection related work includes:
 - Use of social media and automation of advice tools
 - Cyber-crime and cyber resilience
 - Regulatory issues on market efficiency and integrity raised by impact of technological changes
 - Emerging issues of potential future relevance to digital financial inclusion, such as crowd-funding over internet-enabled mobile devices
 - Sales of retail structured products to retail investors
 - Suitability requirements for retail customers
 - Point of sale disclosure to retail customers
 - Credible deterrence – to ensure markets are safe for retail investors





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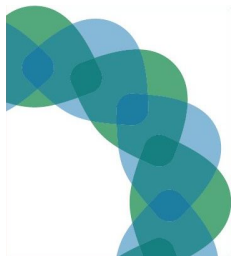
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Standard Setting in the Changing Landscape of Digital Financial Inclusion



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