THE ADVISORY GROUP ON APEC FINANCIAL SYSTEM CAPACITY-BUILDING

A Public-Private Sector Initiative

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Report of Training Program on Financial Inclusion 20-22 March 2013

Australian APEC Study Centre at RMIT University

PURPOSE	For information.
ISSUE	Report of the Training Program on Financial Inclusion
BACKGROUND	The purpose of the training program was to promote best practice proposals on policy and regulatory measures to promote financial inclusion in the region's banking and securities systems, including providing support for technology and innovation, compliance with Know Your Customer (KYC) and FATF requirements, consumer protection and the maintenance of financial system stability.
PROPOSAL	N.A.
DECISION POINT	Note the report of the training program and provide a description and reference in the 2013 Advisory Group Report.

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Executive Summary

The purpose of the training program was to promote best practice proposals on policy and regulatory measures to promote financial inclusion in the region's banking and securities systems, including providing support for technology and innovation, compliance with Know Your Customer (KYC) and FATF requirements, consumer protection and the maintenance of financial system stability.

The program built on earlier work organised by the Australian APEC Study Centre and focused on proportionate regulation as a means of enhancing the delivery of financial services to the underserved. Earlier work included a symposium in Manila in June 2011 which developed recommendations on best practice regulatory principles and proportionate regulation to support micro, small and medium sized enterprises access to finance and a regional policy forum held in Melbourne in October 2012 which focused on the use of technology in the delivery of financial services to the poor. The interface between financial regulation and the role of technology received particular attention, as it did in the training program.

The program was organised by the Australian APEC Study Centre at RMIT University and funded by AusAID through the Public Sector Linkages Program. The ADBI, ADFIAP and CGAP cooperated in the design of the program. 21 participants from the Asia Pacific region attended and the course involved presenters from international organisations, business groups, academics and senior representatives of financial policy and regulatory agencies from the region.

(A copy of the program is shown in Attachment 1 to this report)

Key Findings

- To broaden financial services, there should be more emphasis on women (and households) as account holders, particularly in Asian economies
- Remittance flows between urban and rural centres in countries in the region are extremely important drivers and more work is needed to provide secure remittance services
- Financial system regulators are generally taking a light touch to oversee electronic services and this is to be commended as it allows space for technology applications to develop and for innovation in service delivery
- Telecom regulators should provide fair and equitable access to financial service providers
- A collaborative framework is needed in economies to ensure technology platforms provide interconnectedness between different service providers
- Tensions between banks which wish to provide mobile network services and Mobile Network Operators who can and do, through pricing arrangements, keep banks out of the delivery system limits the reach of technology to the under-served. ***This tension presents a serious challenge to governments wishing to implement financial inclusion policies.***
- An increasingly important aspect of public policy should be to require finance system regulators and telecom regulators to cooperate to encourage the use of technology in the delivery of financial services – ***a whole of government approach is required***.
- Regulations to handle AML and FATF requirements are generally in place and the main focus now ought to be in relation to concerns on data privacy and competition practices; a key concern for consumers is data collection and the use of data by people who collect it.
- Security of customer data is vital to sustain consumer confidence in the industry
- Agent banking is a banking strategy beneficial for geographically isolated regions to help drive down delivery costs

Report of the Training Program

Introduction

The Training Program was organised by the Australian APEC Study Centre at RMIT University, funded by AusAID under the Public Sector Linkages Program and coordinated in collaboration with the Asian Development Bank Institute (ADBI), the Association of Development Finance Institutions in Asia and the Pacific (ADFIAP) and CGAP. It was the second part of a two part program designed to enhance the capacities of representatives from policy and regulatory agencies in the region to encourage financial inclusion in the region's economies, with particular reference to proportionate regulation. The program built on earlier work organised by the Centre in cooperation with ADBI and ADFIAP.

21 participants attended from APEC member economies, China, Indonesia, Malaysia, Mexico, Peru, Philippines, Papua New Guinea, Thailand and Vietnam and from other regional countries, Bangladesh, Bhutan, Cambodia, Fiji and Pakistan. The program was coordinated by the Director of the Australian APEC Study Centre and included as moderators/presenters, the Deputy Dean of the ADBI, the Principal Financial Sector Specialist of the IFC, a senior financial sector expert from the Asian Development Bank, the Deputy Head of the Financial Stability Department of the Reserve Bank of Australia and senior representatives of finance business groups from the region, academics and financial system consultants. Business, official and academic presentations provided for an interactive program and which involved case studies presented by regional regulators and working group activities on selected policy issues.

Background

Through two high level policy forums convened by the Australian APEC Study Centre in collaboration with ADFIAP and ADBI – held in Manila, June 2011 and Melbourne, October 2012 - useful guiding principles that policy makers and regulators could use to promote financial inclusion have been developed. The full reports from these forums are available on the Centre's web-site at: www.apec.org.au.

Some key principles include:

i) encouraging economies to pursue various initiatives to support regulatory approaches to promote financial inclusion;
ii) regional coordination and information sharing is important,
iii) the growth of new products like e-money mobile banking, smart cards combined with IT technologies are impacting sharply on the delivery of financial services to the poor, and
iv) telecoms and utility providers and branchless banking require new regulatory approaches.

Specifically, technology is an enabler for service delivery on a massive scale; it involves new risks as telecos, mobile network operators and financial service platforms challenge the traditional role of banks and existing payment systems. There is a need for creative and flexible responses by policy makers and regulators to enable the delivery of services on a massive scale to eradicate financial exclusion. Regulatory incentives should promote the use of technology, for example to prevent the monopolistic practise of technology innovators and the avoidance of price controls. Markets should be open to promote competition in the delivery of services and to reduce transaction costs. Holistic solutions should be considered since there is no one solution to the delivery of services. Governments should consider intervention policies where there are gaps in service delivery and where there is little or no prospect of profitability by private sector operators. Governments should clearly identify the agency/ies that mobile network operators should deal with in developing their operational strategies.

Key Focus of the Training Program

The program brought together expert presenters from financial system regulatory agencies from across the region, financial business representatives and experts from firms involved in mobile networks, the design and application of technology platforms for the delivery of financial services, representatives of major relevant international organisations, and academics and consultants with deep expertise in the development of financial inclusion policies in the region. A highly interactive program involved case studies (presented by regional regulators and business) and work in small working groups to consider policy responses on selected issues emanating from the program. In summary, the key focus on the program was to address the following questions:

- How should finance system regulators and regulators responsible for telecommunications provide compatible regulatory approaches to foster financial inclusion, including payment system arrangements?
- What approaches best manage the requirements of KYC and FATF in financial inclusion and the interests of consumers?
- How can regulators ensure an innovative and fair regulatory environment for all stakeholders?

The program was designed with the expectation that there would be great value in the sharing of experience between participants.

Contemporary developments and challenges in financial inclusion

Challenges in empowering underserved groups to access financial services are many. Some are context sensitive in nature and experiences are not easily transportable between countries. The challenges for financial regulators involve ensuring easy access for all customers to all financial services at affordable costs, ensuring consumer protection and the entry of players and providers to create a level playing field and to encourage completion among service providers. For teleco regulators their challenge is to provide fair and transparent policies which promote a level playing field and fair competition, meet the needs of consumers and ensure that Mobile Network Operators (MNOs) are able to make reasonable returns on their services.

Participants generally noted that regulators should seek to facilitate access to finance by underserved communities by ensuring low cost financial options with freedom of choice. Different initiatives operating across the world including branchless banking services originating in Kenya called M-PESA. Kenya's national identity cards which reflect KYC requirements contribute to the popularity of this mode of branchless banking. However, there is a robust discussion in Kenya around M-PESA relating to efficiency and to the speed of transactions.

Gender inequality is an important issue and the fact that women and households may not in some countries be permitted to open bank accounts. These limitations seriously impair the growth of financial inclusion. Resolution can be a sensitive cultural issue but one that government's need to address.

Another factor of global significance is that remittance flows from urban to rural areas in some major economies represent major financial flows and while attention is paid to international remittances, the provision of a secure environment to facilitate the flow of domestic remittances should be seen as an extremely important aspect of financial inclusion.

Due to their responsibilities bank regulators need to ensure systemic stability, deposit security and should be responsible for electronically deposited funds and transfers. As such, specific regulations relating to the safety and soundness of mobile money is considered to be in the domain of the banking sector.

From a teleco regulators view point, mobile money is seen as just another value added service like SMS. Most financial services are expected to have a mobile component – SMS through SIM card and MNOs are generally well placed to reach customers with affordable financial services. MNOs have the existing customer base, established infrastructure and experience with high volume low value transactions (sale of air time). Teleco regulators should allow MNOs to contest the market and allow proprietary control over SIM cards where mobile money can be incorporated directly and easily.

Governments are struggling to understand regulatory approaches that will balance the interest of customers with those of market players. This balance is needed to maintain market contestability and to encourage innovation. There is uncertainty over who should regulate when payment services are unbundled and separated from a bank's traditional service. Regulators ultimately want interoperable payment platforms and agents, but are often unclear on platform and agent exclusivity.

Robust agent networks provide the ability of a customer of one provider to use the agent of another provider for cash-in/cash-out services related to that customer's account. Agent interoperability is possible even when there is agent exclusivity, as long as platforms are interconnected (such as with interoperable ATM networks). Non Exclusive Agent networks typically expand financial access creating more access points.

For a major commercial bank, designing a mobile money initiative to enter a mass market is a challenge. It is not seen as a technology play but entry must be on an affordable commercial basis; it may involve cross-subsidisation and the capacity to cross-sell across mobile network channels. A driver will be the capacity to make more products available to customers at affordable prices. The key strategy is one that is transactions based however, a capacity to sell non-transaction based products is also important. A critical matter is ensuring liquidity and effective cash management. Products must be simple in design and must meet customer needs, this requires constant testing of market demands. A strong regulatory environment is necessary and should provide a level playing field for all providers. There should be free and open access to mobile network operators and negotiations with telecom regulators are important in ensuring access to networks.

An open access policy facilitating access to mobile financial service providers and innovative approaches to opening bank accounts would be particularly beneficial in promoting financial inclusion. Innovative approaches to opening bank accounts could be graded for example, from a level 1, anonymous account which could be opened at branches, agents and online with caps on minimum and maximum balances and no KYC details, through to level 5 which would be a full-fledged bank account opened only at branches where the bank would need to file copies of IDs, proof of address, tax ID and other details.

Collaboration between major stakeholders would also be greatly beneficial. From a customer perspective the benefit would be greater access to credit, a full range of secure low cost services and access to diversified products. Mobile operators would benefit from access to robust mobile platforms, agent networks and increased revenue per user by boosting mobile transactions. Commercial banks would gain by broadening their customer base and by an ability to channel loans to segments of the population at concessional interest rates. Regulators would benefit from policies which provide for fair and transparent treatment of financial service providers, increased competition and enhanced customer protection.

Technology is enhancing financial inclusion – the regulatory and industry implications

Financial inclusion policies are leading to the emergence of various technical concepts relating to the delivery of financial services. Mobile phones may not be the only answer to broadening financial inclusion. The platform industry is going through a process of change and while change is based on consolidation, the platform industry is moving toward mainstream payments, with the likely involvement of a number of market players, for example, MasterCard, Visa and of course, internet banking.

Banks are becoming more interested in mobile services but there is a need for them to look at how existing infrastructure and platforms can be leveraged and while banks need to be encouraged to support financial inclusion they need to understand the benefits that technology based platforms can bring. Banks are losing business to mobile network operators and this arises in part because of the cost of traditional branch services, ATMs and agent networks costs which are around 15% of operating costs. It is for this reason that banks have to defray costs by cross-selling and to meet market demands that branches can't meet. Ideally, banks need to make deals with mobile network operators but the latter price banks out of the market. For this reason banking and teleco regulators should seek to agree to fair access prices for banks to SMS systems.

From a governmental perspective, measures to promote financial inclusion need to embrace a number of policies in relation to technology, as follows:

- On-line access to personal authentication information
- Clear reporting requirements – for normal and abnormal transactions
- Regulations to promote a level playing field for the provision of new services
- Promote interoperability and interconnection between new financial service provider
- Privacy laws, and the protection of intellectual property

In addition, stakeholders need to discuss licenses to gain access to markets, data storing, privacy laws, reporting of suspicious transactions, fees and taxes. KYC requirements and the storing of this data is an important security concern for consumer protection including the need to maintain transaction audit trails. Additionally, communication with customers to notify them of changes and providing receipts are relevant. Regulations have a large effect on technological inclusion including access, encryption requirements, limits on transactions and remittances. Communication infrastructure is a necessary prerequisite to allow technology penetration and access to complimentary services by customers. Telecommunication companies require Government support regarding laws and guidelines.

Technology providers have sophisticated knowledge of what is needed to bring people out of financial exclusion. They can respond to the huge demand by people to make small scale payments or transfers; there is a capacity to leverage existing infrastructure without necessarily involving new approaches (for example Square in the US already deals with an aggregate merchant system) and there has been a shift that has absorbed mobile network operators into the payments system. Importantly, systems have been devised to safeguard against AML/anti terrorist funding.

A more relevant focus now ought to be toward data privacy and competition practices. Privacy is not just a developed country issue. Micro credit in Kenya led to the wide-spread use of mobile services and SIM cards. However, the requirements for registration of SIM cards and AML reporting requirements inhibit the poor from utilising mobile systems.

Governments should exercise caution to avoid over regulation of new service providers and platforms. They should avoid regulating on issues that occurred in the past and pay more attention to where the financial sector will be in the next two decades. Self-regulation by industry might be more relevant than formal government intervention. In this context, increased dialogue between stakeholders would be an imperative.

Technology applications are changing rapidly and policies requiring interoperability between platforms are not clearly identified. The profitability of mobile network operators is reducing yet MNOs now have an obligation to maintain platforms and this is occurring against changes in which communication applications can be commoditised. As an example of how quickly technology can impact on service delivery, a consulting group working in the Maldives had recommended an approach in which mobile phones would lead the thrust to the provision of financial services but people were already switching to internet banking.

The relationship between regulation, KYC, compliance with FATF and financial inclusion

CGAP noted in 2009 that inappropriate implementation of AML/CFT standards play a role in excluding low income people from formal financial services. The main issues relate to KYC and Customer Due Diligence (CDD) requirements and the lack of available identification. However, FATF allows for simplified customer due diligence where there is low risk of money laundering or terrorist funding and simplified CDD standards can be decided at the country or financial institution level.

The key principle remains that each financial institution must know its customers, what they do and assess whether or not they are likely to be involved in crime. KYC and CDD issues are included in the agenda of the Pacific Financial Inclusion Working Group the work of which is coordinated through the Alliance for Financial Inclusion (AFI). Emerging issues relate to the application of KYC and CDD standards to branchless banking, including by agents.

Innovative KYC practices in the region include that of Bangko Sentral ng Pilipinas' direction, allowing a choice of nearly 20 identity documents that clients may use to open a bank account or access mobile money. The Reserve Bank of Fiji approved the use of a reference letter from a village chief and a notarized photograph for KYC procedures related to mobile phone financial services. In Indonesia during a series of post-crisis restructuring and reforms, a flexible system was designed with AML policies tailored to high risk groups' such as migrant workers, remittance flows of female domestic workers and with responsive policies to promote capacity of financial institutions such as broad audit/controls for managed investment schemes and informal channels. A second round of reforms is currently underway.

Mexico has a tiered approach with 5 different levels of accounts relative to KYC standards. In India there are 12 digit individual identification numbers issued by the Unique Identification Authority of India to all residents of India on a voluntary basis. It is an e-KYC service that provides an instant, electronic, non-repudiable proof of identity and proof of address along with date of birth and gender. This identity infrastructure is for financial inclusion as well as for strengthening AML/FATF; it is paperless, inclusive, low cost and uses technology and biometrics including of the face, iris and hand. E-KYC may be performed at an agent location using biometric authentication, as well as remotely using an OTP on a website or mobile connection.

AML/FATF requirements in Mexico involve the regulatory authority (Ministry of Finance) which issues the legal framework; the Financial Intelligence Unit (which analysis suspicious activity reports and issues legal complaints; Supervisory Authorities which supervise compliance, impose fines, complete information requests from other authorities and investigate and prosecute. Supervisory powers in relation to AML/FAFT are now risk based, with planning around quantitative and qualitative factors, the identification of major vulnerabilities from AML/FAFT perspectives and which support targeted visits to institutions.

Seven Pacific Island countries established a Pacific Financial Inclusion Working Group in 2009. On a national level, solutions have resulted. In Papua New Guinea a risk-based approach where a variety of documents can be presented to verify identification and in Fiji, since 2010, only one reference from a suitable referee is required where the customer is judged to be low risk and unable to provide formal ID. Mobile network operators in Fiji are exempted from CDD requirements for domestic e-money transactions up to a maximum cap. Guidelines have been issued to agents and a new initiative to issue Voter Identification Cards will enable use of the card to identify customers. The Solomon Islands Central Bank has recently issued new guidelines with three account tiers and progressively higher transaction caps with each level requiring more stringent KYC conditions. Lessons from the Pacific islands experiences point to the need for clarity in revised FAFT guidelines to confirm flexibility in application of standards, that national regulatory authorities may have stricter requirements that FAFT recommends and that financial institutions may have stricter requirements because of home country or group-compliance policies. Greater clarity in the use of agents to carry out AML/CDD functions is also needed.

From a banking group perspective, FAFT requirements pose complex managerial issues which are primarily jurisdiction centric. For a group operating in over 30 countries (ANZ Group) with operations in 11 countries in the Pacific, a major challenge is to develop uniformity in handling FATF requirements, in sourcing information about customers and in data collection and verification processes. In the CDD processes the nature of a legal entity posed complex matters. In Australia for example there are 15 types of entities and different jurisdictions may have different identification requirements.

Emerging challenges for major financial corporates include adopting increased levels of FATF recommendations, increasing levels of industry involvement and the resolution of privacy concerns. Mass small value transactions would involve a risk based approach but a bank would need to have an agreement from a regulator to non-documented business. Technology is vital to transaction monitoring; banks are required to hold data for several days and transparency, privacy and how data is stored and moved to a central storage point requires agreement by regulators. Importantly a bank must also have auditable trails.

As a general point, the promotion of financial inclusion is central to an effective and comprehensive AML/CDD regime. Financial inclusion brings more customers and transactions from the untraceable world of cash into the traceable world of formal financial services. There will be changing risk scenarios as financial inclusion expands coverage and supervising/regulating innovation or technology based services are utilised. Assessing risks and benefits and balancing them against the costs of regulation and supervision will be an ongoing process (particularly as experience is gained with new products, providers and delivery channels).

Consumer protection

Measures to encourage responsible financing in China involve social performance management and consumer protection; the latter involves policies to provide fair and respectful treatment of customers, responsible pricing, transparency, the privacy of client data and complaint resolution processes.

In Vietnam there is currently no legal requirement on consumer protection relating to the activities of micro finance institutions (MFIs). However, regulations relating to MFIs require that customers are provided with necessary information on pre-borrowing procedures, interest rates and repayment requirements. For general credit institutions the borrower is regarded more as a party requiring supervision rather than a party that can claim rights against a provider. The government has approved a strategy for building up the law on credit institutions relating to microfinance operations and for a revision of the legal framework to cover microfinance diversification and operations.

In regards to consumer protection the Bank of Thailand is focused on ensuring fair market practices and enhancing financial literacy to allow consumers to make informed judgements on financial services. Banks are required in their risk management processes to have regard to minimum income requirements of their customers, require minimum payment and ceilings on interest rates and other relevant expenses, take account of the need to adjust qualifications (income, age, types of assets as collateral), use of credit bureaus and set credit scoring systems. Banks must also apply information disclosure requirements, set rules for debt collection and for complaints handling. More emphasis on consumer protection would likely involve discussions with banks and non-bank associations and the promotion of financial education.

An aspect of concern to consumers, finance groups and regulators is that of system hacking. Hackers are techno savvy and are able to penetrate secured systems notwithstanding the considerable resources spent by firms to combat hacking and theft. When breaches occur regulators need to vigorously defend the system and ensure that the public is informed so as to maintain faith and confidence in the system and financial stability over the long term.

Agent banking and other non-traditional providers

Priority is being given to "unbanked" areas in China in setting up branches and products including unsecured micro loans and loans guaranteed by groups and agricultural insurance. Mobile services are bank led and with telecom companies seeking to cooperate with banks in providing financial services. This involves cooperation between financial and teleco regulators. However, mobile banking is not popular and banks provide internet banking services. Rural populations see banks as reliable and prefer to deal with banks. The use of pre-paid public transport cards is growing.

Peru's strategy to enhance financial inclusion has involved the development of a regulatory framework for agent banking. Regulations about AML and FATF that apply to agent banking are simplified and reduces some of the requirements on banks themselves. The operations and services that an agent can provide are restricted to the opening of basic savings accounts, the collection of payments for credit but not the granting of credits. The operator of the agent bank must comply with some requirements – for example a good credit rating and with qualified employees; the bank itself must ensure management of operational risks of agents, limits of operations and disclosure information. The bank is responsible for any claim about products and services offered by the agent banking on its behalf.

Agent banking has become an important tool to improve financial services; it provides convenience to a large diversity of clients, especially for those who don't have access to financial inclusion for geographic reasons and agent banking is helping drive down delivery costs. E-money is also a particularly good strategic choice for Peru which has geographically dispersed regions, highly disproportionate wealth distribution and with the mass proliferation of mobile phones it presents a new delivery channel that can be extremely beneficial for unbanked people.

E-money is not considered to be a deposit and is therefore not covered by any deposit insurance mechanism. In order to protect customers the funds received must be transferred to trust the issuers who may be multiple operational entities, such as banks, financial enterprises, microfinance institutions; and electronic money issuer enterprises (EEDE) whose main activity is the issuance of e-money and are not allowed to grant credit for funds receive. To prevent any inappropriate market conduct telecos must establish a separate entity to conduct e-money business and they are supervised. Likewise, telecos must provide services on equal basis to all e-money issuers. The Central Bank provides an opinion to the Superintendency of Banking, Insurance and Private Pension Funds Administrators on the authorization of EEDEs. Additionally, banks can have special offices of a temporary or permanent nature and can share office space with other banks or insurance companies, supervised by the Superintendency of Banking, Insurance and Private Pension Funds Administrators to promote and develop the support access to formal financial services.

Actions already taken in Mexico include increasing availability through creating access points to financial services by banking agents, decreasing transactional costs, developing saving and payment vehicles for mobile payments that adequately suit the needs of the underserved with appropriate limits.

Indonesia's comprehensive strategy for financial inclusion involves education, public financial facilities, mapping of financial information, supporting regulation/policy, intermediary/distribution facilities and customer protection. The approach involves subsidies by Government, fiscal incentives and social welfare programs to deliver a productive and high purchasing power society with easy access to the financial system. A number of teleco e-money operators offer transfer and payment services. Indonesia is rated as having a relatively high level market and institutional environment for the delivery of financial services through technology or based on agent banking. Challenges currently being examined include the appropriate level of access between rural, commercial banks and telecos, the degree of regulation, the implementation of branchless banking, complaint and dispute resolution mechanisms and how to evaluate developments.

In PNG non-bank e-money issuers such as telecos must have a separate entity and must meet a minimum capital requirement. Transactions are capped on a daily limit and e-money issuers must maintain a trust account for a pool of funds in deposit. Due to geographical and infrastructure difficulties, mobile banking making use of the wide mobile network coverage is seen as the major means of widening financial inclusion.

Payments systems

The Reserve Bank of Australia's (RBAs) financial stability mandate includes ensuring the stability, efficiency and competitiveness of the payments system. The RBA has strong ties with other regulatory agencies and through its semi-annual Financial Stability Review where it raises awareness of systemic risks and vulnerabilities. If problems arise the RBA will contribute to crisis management arrangements, including the role of lender of last resort. Cash is the predominant retail payment method, followed by cards; cheques and BPay/online payments are a very small fraction of total retail payments. Newer payment methods include contactless card payments but despite the high penetration of mobile phones, mobile payments are relatively very small and mobile are predominantly used in the Australian market to purchase apps linked to bank.

Value is dominated by 'wholesale payments'; 'retail' payments give rise to much smaller flows so wholesale payments, such as those arising from financial market transactions, account for around 75% of daily payment volumes, and they are therefore the priority in terms of stability analysis and safeguards. The RBA owns, supports and operates a high value payment system the Reserve Bank Information and Transfer System (RITS). Settlements are made across Exchange Settlement Accounts and eligible account members include banks and authorised deposit taking institutions, third party payment service providers, centralised counterparties and securities settlement facilities; small accounts can settle through an agent. Financial stability standards for key clearing and settlement infrastructure involve two classes based on international standards, Central Counterparties (CCPs) and securities settlement facilities. Stability in the system reflects the quality of regulatory agencies, cooperation between them, good information on exposures, linkages and risks – data and liaison, and judgement making on the materiality of risks (involves balancing stability with efficiency and allocating limited regulatory resources).

Working group discussions

Group 1 **considered the primary policy, regulatory approaches and institutional structures required to support financial inclusion.**

Group views: Approaches should be principles based and contextually based; non-restrictive; collaboratively sound and inclusive of dispute resolution mechanisms; agreements should have legal force; proactive engagement involving all stakeholders, regulators and financial institutions should involve in direct discussions with technology firms in the development of independent platforms.

Group 2 **considered the tensions that policy makers and regulators must take account of in managing tensions between prudential supervisors and ministries that are responsible for managing/authorising IT communications systems when used in the delivery of services to deepen financial inclusion.**

Group views: There are different objectives of different groups – KYC, ownership of payments system, risk management, state versus private interests; monopoly interests versus competition. There are a number of players – parliament, central banks and regulators including teleco regulators; ministries of trade and commerce, national development, consumer affairs, justice, tax and industry associations.

The group concluded that central banks should take responsibility of promoting financial inclusion. It is responsible for system stability and the central bank may well have to take an assertive position with the teleco regulators in regard to accessing the financial system. There needs to be a collaborative approach via a steering committee involving financial regulators, business and telecommunication regulators. Work should be directed to develop a plan within two years with measureable milestones

Group 3 **considered, against a background of scale what can be provided by mobile network operators, telecos and utility companies in the delivery of financial services, the managerial challenges that financial system supervisors need to manage in promoting financial inclusion through IT and communications systems.**

Group views: Firstly assume that there is no regulation. Benefits could include the ease of companies to do business which could increase competition, enhance quality of current market players, drive competitive prices and leading to self-correction and market punishment of failures. However, this scenario comes with the risks of unregulated pricing, the prospect of monopoly power arising, systemic risk and low consumer protection. Assume over-regulation, benefits will include lower systemic risk, stability, reduce reputational risk and loss of jobs, better consumer protection and a reduction in KYC risk. The risks in excessive regulation include a curbing of innovation, high regulatory costs and adverse impacts on economic growth and with complex regulatory processes. It concluded that a first principle should be the design of a national financial inclusion strategy that does involve leadership with the objective of developing a risk management approach and one based on sound business models with a minimum of regulation.

> *Group 4* **was based on compliance with KYC and FATF requirements and discussed where the responsibility lies in governments to handle these processes and what key policies should be followed to meet the objectives of proportionate regulation to reflect the interests of consumers of micro financial services.**

Group views: There should be flexibility in terms of identification which could include village certificates, references by other consumers and national identify cards. Low risk financial services should be accompanied by proportionate regulation, for example, e-money could be based on no-frills accounts and limitations on minimum balances/transactions. Outsourcing of KYC and FATF should be considered, including with trained agents; the burden of proof should be with the issuer, and standards and guidelines developed in respect of outsourcing. Supporting infrastructure for the exchange of information and credit reporting bureaus and guidelines developed to ensure the security and safety relating to the sending and storing of documents. It was concluded that this work should be overseen by a specialist group in a central department of state or the central bank. The work should be resourced and provide independent advice.

Further consideration of the ideas emanating from the working groups highlighted the following views. Money transacted through e-money is relatively very small and so banks which are excluded by a dominant teleco player in a particular market should be in a position to require access to the e-money market through for example using their influence with other agencies in terms of telecos access to the broader payments system. At this juncture, telecos have positioned themselves based on USSD system technology but other technologies are likely to come into play. Central banks could consider establishing a "challenger fund" where they offer a prize of say $5million for technology vendors who submit "neutral" open technology platforms.

ATTACHMENT 1 - TRAINING PROGRAM

DAY ONE: Wednesday 20 March 2013 **Issue 1: Technology to enhance financial inclusion**
8.20am – 9.00: Breakfast in Pre-Function Area
9.00am-9.30am, Session 1: Welcome and Introduction **Review of outcomes of the 2012 Financial Inclusion Forum that will expand the facilitation of financial inclusion in the region** - Dr Jae-Ha Park, Deputy Dean of ADBI, Japan - Mr Ken Waller, Director of the Australian APEC Study Centre
9.30am-11.00am, Session 2: How technology is being used in the region: e-money, mobile money, e-wallet. Are regulators coping and responding to this? **Chair:** Dr Jae-Ha Park, Deputy Dean of ADBI, Japan - Mr Sanjay Saxena, Managing Director of Total Synergy Consulting Private Limited, India - Ms Supriya Singh, Professor, Sociology of Communications, Graduate School of Business & Law, RMIT University - Mr Yushi Endo, Economist, Payment and Settlement System Department of the Bank of Japan
11.00am-11.30am: Morning Tea
11.30am-12.00am: Group Photo
12.00am-1.00pm, Session 3: Regulatory and technology interface – how do regulators utilise and encourage financial inclusion. Case Study presentations from regulators addressing technology to enhance financial inclusion. **Chair:** Dr Jae-Ha Park, Deputy Dean of ADBI, Japan - *Philippines:* Miss Marlene Tiquia, Deputy Director of Bangko Sentral ng Pilipinas - *Cambodia*: Mr Samrith Chhuon, Deputy Director of Ministry of Economy and Finance
1.00pm-2.30pm: Lunch
2.30pm-4.00pm, Session 4: Essentials of a conducive regulatory environment utilising technologies. **A technology perspective.** **Facilitated by:** Mr Tony Lythgoe, Principal Financial Specialist of International Finance of the IFC - Mr Brad Jones, Managing Director of Mobile Accelerate, Singapore - Mr Peter Cook, CEO of Novatti Discussant - Prof. Bill Maurer, Director of the Institute of Money, Technology and Financial Inclusion and the Co-Director of the Intel Science & Technology Center for Social Computing at the University of California, Irvine
4.00pm-4.30pm: Afternoon Tea
4.30pm-5.30pm, Session 5: What are the best practice principles to support adaptation & the use of technology? Panel Discussion **Facilitated by:** Mr Ken Waller, Director of the Australian APEC Study Centre - Mr Sanjay Saxena, Managing Director of Total Synergy Consulting Private Limited, India - Mr Brad Jones, Managing Director of Mobile Accelerate, Singapore - Mr Tony Lythgoe, Principal Financial Specialist of International Finance of the IFC

DAY TWO: Thursday 21 March 2013
Issue 2: The relationship between regulation, know your customer (KYC), compliance of the Financial Action Task Force (FATF) and financial inclusion

8.20am – 9.00: Breakfast in Pre-Function Area

9.00am-10.30am, Session 6: What are the regional practices to accommodate regulation requirements for KYC and FATF and how are they implemented?

- Mr Erik Aelbers, Senior Financial Sector Expert of PLCO/PSDI's, Asian Development Bank
- Ms Raniya Sobir, Senior Consultant/Vice President of Total Synergy Consulting Private Limited
- Mr Dinesh Anand, Anti-Money Laundering, Counter-Terrorism Financing and Sanctions of ANZ

10.30am-11.00am: Morning Tea

11.00am-12.30pm, Session 7: Case Study presentations from regulators on the relationship between regulation, know your customer (KYC), compliance of the Financial Action Task Force (FATF) and financial inclusion

Facilitated by: Mr Ken Waller, Director of the Australian APEC Study Centre

- *Fiji*: Mr Joseph Vakatekua Masitabua, Chief Manager of Financial Institutions of Reserve Bank of Fiji
- *Mexico*: Mrs Nora Garcia Medina, Director General of National Banking and Securities Commission

12.30pm-2.00pm: Lunch

Issue 3: Consumers in financial inclusion

2.00pm-3.30pm, Session 8: Measures to encourage consumer involvement in financial services, confidence in product design and delivery, protection and flexibility of services

- Ms Wang Dan, Managing Deputy Secretary General of the China Association of Microfinance
- Mr Gary Collins, Head of Mobile and In-Store Banking at Westpac Pacific

Dispute resolution mechanisms and consumer protection issues as they relate to financial infrastructure.

- Mr Tony Lythgoe, Principal Financial Specialist of International Finance of the International Finance Corporation

3.30pm-4.00pm: Afternoon Tea

4.00pm-4.45pm, Session 9: Case Studies – A business and regulatory perspective on how MFI's and Banks accommodate regulatory requirements on matters of consumer protection.

Facilitated by: Mr Sanjay Saxena, Managing Director of Total Synergy Consulting Private Limited, India

- *Vietnam*: Mr Nguyen Dang Khoa, Deputy Director, International Cooperation, Ministry of Finance
- *Thailand*: Miss Chulaluk Pubulchol, Senior Analyst at the Financial Consumer Protection Center, Bank of Thailand

6.30pm-8.00pm: Group Dinner
The Merchant Osteria Veneta – Rialto, 495 Collins Street Melbourne

DAY THREE: Friday 22 March 2013
Issue 4: Agent banking and other non-traditional providers of financial services

8.20am – 9.00: Breakfast in Pre-Function Area

9.00am-10.00am, Session 10: What are the implications for regulators to ensure finance and payment system stability?
Facilitated by: Mr Ken Waller, Director of the Australian APEC Study Centre

- Mr Carl Schwartz, Deputy Head of the Financial Stability Department of the Reserve Bank of Australia
- Ms Zhu Xiujie, Division Director, Financial Cooperatives Supervision Department, China Banking Regulatory Commission (CBRC)

10.00am-10.30am: Morning Tea

10.30am-11.30pm, Session 11: Case Study presentations on involvement of agent banking and other non-traditional providers of financial services and managing regulatory implications.
Facilitated by: Dr Muhammad Cholifihani, Capacity Building and Training Consultant, Asian Development Bank Institute (ADBI)

- *Peru*: Mr Jimmy Izu, Head of the Regulation Department of the Superintendency of Banking Insurance and Private Pension Funds Administrators
- *Indonesia*: Mr Ricky Satria, Assistant Director of Financial System Stability, Bank Indonesia
- *PNG*: Mr Nickson Kunjil, Unit Manager of the Banking Supervision Department, Bank of Papua New Guinea

11.30am-12.00am, Session 12a: Group Preparation for Workshop
Policy issues to be discussed in subsequent workshop will be defined

Presented by: Mr Ken Waller, Director of the Australian APEC Study Centre

12.00am-1.30pm: Lunch

1.30pm-3.00pm, Session 12b: Workshop
Break into 4 groups to analyse a major policy issue from a major issue in the program

Facilitated by: Mr Sanjay Saxena, Mr Tony Lythgoe, Ms Raniya Sobir and Mr Brad Jones

3.00pm-3.30pm: Afternoon Tea

3.30pm-5.30pm, Session 13: Reporting from Working Groups
Analytical discussions by all participants

Facilitated by: Dr Jae-Ha Park, Deputy Dean of ADBI, Japan and Mr Ken Waller, Director of the Australian APEC Study Centre

5:30pm-6.00pm Graduation Ceremony: Presentation of certificates to participants

ATTACHMENT 2 - ECONOMY CASE STUDIES

China - **The Chinese government has developed a wide range of strategies to improve access to finance in rural communities, these involve among other institutions the Postal Savings Bank of China, the Agricultural Bank, Agricultural Development Bank and small and medium sized rural financial institutions. Strategies include multi-level development systems, strengthening supervision, meeting financial product demand, encouraging innovation of new rural products and services, easing the entry regulations of new types of rural financial institutions which has led to the expansion of village and township banks, lending companies and rural mutual credit cooperatives.**

Various groups provide micro finance services in China, including members of the China Association of Microfinance which comprises 100 NGOs, commercial banks providing micro credit services to the poor, low income farmers and laid off workers; 6,000 micro finance companies, the Postal Savings Bank of China with over 4,500 branches of its 39,000 providing micro loans, Rural Credit Cooperatives with over 2,900 branches in rural areas and the China Banking Association comprising 200 village, township banks and commercial banks. Notwithstanding this institutional presence in China there is a bottleneck in the supply of micro finance and this arises in part from the fact that NGOs do not have a legal status by which they can attract funding other than from private donors.

Fiji - A national financial inclusion taskforce incorporating financial literacy, microfinance and statistics working groups has been established. Strategies include education, mapping and expanding payment instruments, the latter includes mobile money, micro-insurance, branchless banking, consumer protection through complaints management policies, disclosure processes and negotiation on fees and charges. There is recognition that technology and innovation are the key to driving financial inclusion. Cognisant of the fast pace of development in financial inclusion the Reserve Bank of Fiji is prepared to take bold steps to pursue financial inclusion. The Reserve Bank is drafting legislation to cover payment systems. The banking sector and telecos have yet to resolve issues on the pricing of access to communications services by banks although the banks resolve to enhance the delivery of services via telecos. Telecos require authorisation to become e-money issuers and there is a regulation regarding the distinction between e-money and airtime values.

Mexico - A framework has been designed to promote financial inclusion that includes targeting awareness, access and usage. Further public policies are needed to target high transaction costs, ID requirements, lack of financial service penetration, product design and needs that can be addressed by public policies on financial inclusion. In 2011, a National Council of Financial Inclusion was established as a coordination mechanism among all financial authorities and relevant stakeholders; this mechanism established both medium and long-term goals, to formulate policies and issue official opinions.

Papua New Guinea - 85% of the population do not have access to financial services. Geographical and infrastructure problems limit the delivery of these essential services. There is a low literacy rate and as a consequence, financial inclusion is limited but this is a priority policy of the government and Central Bank. Initiatives include a micro finance expansion project, financial education, legislative reviews relating to a national payments system, savings and loan societies, personal property security and mobile banking regulation. Three models of mobile banking are being promoted; a bank led, a teleco led and one led by the Post Office on a money transfer service. Licensed financial institutions are authorised to offer financial services as part of banking business but there are some concerns about non-banks being involved in issuing e-money. The Central Bank considers that mobile banking is banking business and regulates it under the Banks and Financial Institutions Act 2000; a specific regulation and prudential standards have been issued to bank and non-bank e-money issuers.

The Philippines - A number of laws and circulars issued by Bangko Sentral Ng Pilipinas has set out the legal framework governing the banks financial inclusion strategy, consumer protection for e-banking, the issuance of e-money, the operations of electronic money issuers (EMIs), microfinance lending, savings and insurance, the outsourcing of e-money related services and anti-money laundering and regulations. The Central Bank approach to market based products has been to proceed with flexibility yet with caution, based on an understanding of operating/business models, risk identification and management. Developments are closely monitored and there is resort to existing regulations but with a capacity to adopt regulatory approaches based on lessons learnt.

The Central Bank makes a clear delineation between deposit-taking, transactions and the receipt of funds for funds transfer purposes and consequently regulates proportionately. Banks providing micro finance services are required to comply with the same standards and capital adequacy and licensing standards and the regulator requires that they (the banks) have a clear underwriting standards and practices for cash-flow lending and high frequency monitoring of portfolio risk and corresponding risk provisioning reflecting the peculiar risks associated with micro finance.

Where a bank is the e-money issuer, (SMART Card is an example), the bank has the primary relationship with the account holders; telecos operate and maintain the technology and teleco agents serve as cash in-cash out centres; users are required to have an account with the bank that is not treated as a deposit but as electronic money. GCASH is a non-bank-led model/teleco centric model, where the teleco has a subsidiary (the e-money issuer) which operates e-money business and has the primary relationship with the account holder.

Proportionality principles require that e-money is clearly distinct from deposits, transactions limits are in place as is technology risk management and the electronic money issuer (EMI) is responsible for the behaviour of agents and must meet capital, liquidity management and effective audit requirements. The Philippines Development Plan 2011-2016 includes the provision of access to financial services for all. An inclusive financial system should provide a wide range of financial services that serve different market segments, products are appropriately designed, priced and tailor-fitted to meet market needs, that there is a wide variety of strong, sound and duly authorised financial institutions utilising innovative delivery channels, and effective inter-face of bank and non-bank products, delivery channels, technology and innovation to reach the financially excluded.

The case for expanding banks' virtual reach using mobile phones reflects the potential of technology to a large number of bankable but un-banked groups, particularly in rural and hard to reach areas at lower cost and higher efficiency. The mobile phone industry serves all income groups especially low income groups and there is almost 90% mobile phone penetration. SMART Communications is a leading wireless services provider in the Philippines with around 51 million people on its GSM network; Globe Telcom offers wireless voice and data services to consumers and business, currently serving nearly 31 million subscribers.

Currently there are 24 e-money bank issuers and e-money non-bank money issuers; together these issuers have an agent network of 12,000 which is continuously expanding. In 2011 there were over 150 million e-money transactions amounting to Php. 535 billion. There are also over 56 rural banks offering mostly mobile e-money facilities. The costs of transactions using e-money facilities are 0.7% compared to 8%, 5.3% and 10% respectively for remittance agents, pawnshops and banks. E-money is being used to deliver conditional cash transfers in government to people (G2P) with savings to the government in reaching 400 municipalities and 500,000 beneficiaries. There is potential for similar opportunities for wage and pension payments.

From a broader economic perspective, the authorities in Thailand are concerned to maintain a stable level of household debt and a sustainable economy through disclosure and transparency in the operations of financial institutions and increased market discipline.

Cambodia - Banking penetration is around 5% and mobile phone penetration around 94% with 6 mobile operators. Prakas (Rules and Implementing Regulations) on third-party processors to regulate the operation of mobile phone payment systems was introduced in 2010. Prakas defines the duties and responsibilities of service providers, reporting requirements and including their efforts to combat money laundering and the financing of terrorism. The National Bank of Cambodia (NBC) has to approve outsourcing of payments transactions through all third-party processors. Approved processors can provide communications facilities, inter-bank clearing, management of bank customer accounts, send or receive point of payment orders remittances by mobile phone or other means, settlement of debit and credit card payments and manage and operate on behalf of one or more banks a payments system.

By the end of 2011, the NBC had authorised 3 establishments to offer mobile phone banking, WING, ACLEDA Unity and Cell Card operated by Union Commercial Bank. WING, the first bank-led mobile money model in Cambodia enables customers who are typically "un-banked" to access financial services from mobile phones. Bank-led WING incorporates consumer protection based regulation, processes more than 500,000 revenue generating transactions per month, has universally acceptable handsets, networks, dual currency and operates on a stand-alone basis and is expandable into other markets.

WING is connected with all active GSM mobile network operators in the Khmer market, representing more than 70% of mobile phone users and with 100% geographic coverage. There are now 260,000 customers and over 850 WING Cash Xpress agents (in all 24 provinces). The majority of its customers had no financial access before WING and were in the poorer segments of Khmer society. WING is used predominantly for small money transfers with the costs of the service significantly lower than informal money transfer services.

Japan - There is no legal definition of e-money. E-money is classified as either prepaid (IC chip-based - plastic cards and mobile phone/smart phone) and server based, or as post paid. IC chip-based prepaid e-money is popular and the use of IC chip-based post-paid e-money is spreading as it is installed in mobile phones. (Recent developments in e-money in Japan are published by the Bank of Japan). The number of instruments and terminals has increased although there is some slowing in the growth of terminals operating at outlets at railway stations for cards issued for public transport. That said, the volume and value of transactions settled using e-money has continued to increase, particularly as payment for public transport, and the number of mobile phones that record and store electronic money (mobile phones with electronic money functionality) has continued to increase. E-money is being increasingly used as a settlement for relatively small value payments; use of e-money is relatively limited among the elderly.

Pakistan - A major barrier in transaction risk was removed by agreement by the authorities to allow agents to provide transaction services. Pricing by regulators was seen as something of a two-edged sword; it could remove an incentive to platform providers and a preferred approach could be to let the market set fees in the early stages. Perhaps the only role for governments is to require providers to provide government to people payments services and to avoid regulatory risks, governments could require performance standards in regard to speed of transactions and accurate reporting. If governments require data storage on shore to reduce risk that may inhibit innovation as would prohibitions on the use of cloud computing.