

MOBILE MONEY AS AN ENGINE OF FINANCIAL INCLUSION  
AND LYNCHPIN OF FINANCIAL INTEGRITY

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ABSTRACT

*Few people would dispute that mobile money can be an engine of financial inclusion and has the potential to reach millions of customers, including those at the bottom of the socio-economic pyramid. Fewer though would characterize mobile money as the lynchpin of financial integrity. But financial inclusion and financial integrity have at least three tangential points to mobile money: (1) mobile money will help reduce dependency on cash, which is the common enemy of both financial inclusion and financial integrity, (2) mobile money generates data which is instrumental to the health and growth of both financial inclusion and financial integrity, and (3) mobile money accelerates the development of accounts, which are the backbone of financial inclusion and financial integrity. In any case, if mobile money is to deliver on its promises for both financial inclusion and financial integrity, three regulatory barriers need to be removed.*

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## INTRODUCTION

In its Monetary Policy Statement of February 2012, the Bank of Tanzania highlights how “mobile financial services have contributed significantly towards broadening access to financial services in Tanzania given the high level of mobile phone usage.”<sup>1</sup> Despite a high poverty rate, 78 percent of Tanzanian households and 63 percent of Tanzanians own a mobile phone. Simply walking through a market in Arusha shows ample evidence of the widespread availability of mobile devices and communication networks. By contrast, only 12 percent of the population in Tanzania was banked in 2009, leaving the remaining 88 percent to meet their financial needs through informal instruments and mechanisms outside the banking sector.

If people use mobile services to transmit voice and text messages, why should they not also use their mobile phones to transmit and store value? It may not be an obvious question for affluent customers who have several options with which to manage their financial needs, but for the 88 percent mentioned above, it is an important one. Leveraging existing infrastructure and services must be part of a solution that reduces costs low enough to reach down market and improve access to financial services in developing countries. In Tanzania, providers such as Tigo, Vodacom, Airtel, and Zantel are doing just that when they offer

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<sup>1</sup> BANK OF TANZANIA, MONETARY POLICY STATEMENT: THE MID-YEAR REVIEW 10 (2012), *available at* [http://www.bot-tz.org/Publications/MonetaryPolicyStatements/2012\\_Feb\\_MPS.pdf](http://www.bot-tz.org/Publications/MonetaryPolicyStatements/2012_Feb_MPS.pdf).

mobile money services. When customers sign up for one of these services, they get an account from which they can send, receive, and store money using their mobile phone. This is in large part what Bank of Tanzania refers to in its Policy Statement.

Mobile money is at the crossroads of mobile communications and financial services, its power in distribution and marketing disguised under a technology facade. It is without a doubt disruptive to the business of incumbent financial services providers and has the potential to foster broad transformation through improved efficiency and simplified access. It is still a very young “industry” however; the first services were only launched commercially in the Philippines less than ten years ago and mobile money is becoming a reality at scale so far only in East Africa. So the potential is there, but it still needs to be realized.

Among the stakeholders interested in mobile money, policymakers and regulators are in a good position to drive change. When it comes to financial inclusion, mobile money appears very promising as it addresses the problems of cost and proximity, both of which contribute to the staggering figures of financial exclusion. When it comes to financial integrity however, mobile money seems less appreciated. Some worry that mobile money can be damaging to financial integrity as it increases the velocity of transactions. Some even have the perception that mobile money, when issued by mobile operators in particular, might be unregulated. This creates the impression of greater risk and seems to reinforce views that financial inclusion and financial integrity are in opposition with each other.

Rather than being the apple of discord between financial inclusion and financial integrity, mobile money actually serves both objectives by (1) helping to reduce dependency on cash, which is the common enemy of both financial inclusion and financial integrity, (2) generating data which is instrumental to the health and growth of both financial inclusion and financial integrity, and (3) accelerating the development of accounts, which are the backbone of financial inclusion and financial integrity. If mobile money is to deliver on its promises for both financial inclusion and financial integrity, three regulatory barriers need to be removed.

## I. MOBILE MONEY REDUCES THE DEPENDENCY ON CASH

The role of cash, its costs, and its benefits are usually approached from a convenience point of view, and when cost is addressed, it is from the issuer perspective and how much it costs the State to mint. Canada is waving farewell to its one penny coins; they cost more to mint than they are worth.<sup>2</sup> The use of cash also has other indirect costs and policy ramifications.

Living on the equivalent of a couple of dollars a day does not only entail a more precarious life due to little means. It also implies spending a great amount of energy and resources to manage cash, keep it safe, and transport it. While wealthier people live their financial lives using electronic financial instruments, poorer customers often have no choice but getting by with cash and physical assets. From a regional perspective, the difference is staggering: any single individual performs on average one hundred or more cashless transactions per year in developed countries, but less than one in Africa.<sup>3</sup> Financial inclusion advocates could be tempted to limit their remittances to protect poor people using cash. A more ambitious goal to improve access to financial services, however, should actually start with finding ways to move away from a total dependence on cash and instead promote the use of electronic means to store value and transfer it. Make no mistake—this is not about going “cashless”; this is about providing consumers with an *option* to use electronic money or cash. As Mas and Porteous put it, “[i]t’s freedom from cash, not absence of cash.”<sup>4</sup> And this is where mobile money can help.

Simply put, mobile money is essentially electronic money. It contributes to the development of an electronic ecosystem of

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<sup>2</sup> *Canada Kills the Penny as Americans Advocate for Similar End*, HUFFINGTON POST (Mar. 30, 2012), [http://www.huffingtonpost.com/2012/03/30/canada-penny-currency-dead\\_n\\_1391050.html](http://www.huffingtonpost.com/2012/03/30/canada-penny-currency-dead_n_1391050.html).

<sup>3</sup> THE WORLD BANK, PAYMENT SYSTEMS WORLDWIDE: A SNAPSHOT – OUTCOMES OF THE GLOBAL PAYMENT SYSTEMS SURVEY 2010 vii (2010), available at [http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/282044-1323805522895/121534\\_text\\_corrections\\_3-15.pdf](http://siteresources.worldbank.org/FINANCIALSECTOR/Resources/282044-1323805522895/121534_text_corrections_3-15.pdf).

<sup>4</sup> Ignacio Mas & David Porteous, *A LiFi World*, CONSULTATIVE GRP. TO ASSIST THE POOR BLOG (Jan. 11, 2012), <http://technology.cgap.org/2012/01/11/a-lifi-world/>.

financial services due to three key attributes. First, it enables the conversion, both ways, between cash and electronic money through a network of retailers. This may sound benign but it is actually the part of the value chain that is most critically lacking and the most difficult to design and execute well.<sup>5</sup> Second, mobile money provides a storage facility for electronic value in the form of an account. For many customers, it will be their first account ever. Finally, mobile money offers a mechanism for transactions to take place electronically, which is particularly useful for non-proximity scenarios.

Of course, the ability to make mobile payments is not enough from a financial inclusion perspective. People need more than payment or storage functionalities to manage their financial lives—insurance, credit, and different types of saving options are also important, if not essential. However, repaying a loan when you only have cash is not always convenient. If you save a dollar a week, you might not feel like walking to the bank for that dollar every week. Paying someone close by is easy with cash, but still assumes you are going to carry cash with you, which is not always safe. Although mobile money is not a panacea, it can facilitate access to financial services in a manner that cash simply cannot.

The impact of mobile money on reducing the use of cash has less to do with the underlying technology and more with its convenience. Mobile money customers can use their own mobile devices to initiate transactions or check the status of their account wherever they have mobile coverage. If they need to deposit or withdraw cash, they know there is a store next door where they can make the conversion. If the experience is consistent over time and across different outlets, it will contribute to the creation of trust that is necessary to increase the use of electronic instruments and mobile money. Essentially, mobile money is more about distribution and accessibility than technology.

If mobile money helps the case of financial inclusion, it can also help another public good that is not available with cash:

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<sup>5</sup> Frederik Eijkman et al., *Bridges to Cash: The Retail End of M-PESA*, 34 *SAVINGS & DEV.* 219, 225 (2010), available at <http://ssrn.com/abstract=1655248>.

financial integrity. Criminal and fraudulent activities are often more difficult to spot and disrupt if their proceeds are in cash, which is anonymous, fungible, and largely invisible. In contrast, electronic transactions leave traces, which can be used to recognize patterns and identify who is party to them. This is true even in cases where the identity of the sender or receiver cannot be authenticated. Some have argued that when accumulated in large amounts, cash becomes effectively very visible and rather unpractical to handle discretely. While this argument is logical, a large amount of cash could be even more visible if everyone else was using electronic means.

Overall, financial exclusion and its cash corollary are increasingly recognized as an impediment to financial integrity. The recent guidance paper of the Financial Action Task Force (FATF) on Anti-Money Laundering and Terrorist Financing Measures and Financial Inclusion states that “informal, unregulated and undocumented financial services and a pervasive cash economy can generate significant money laundering and terrorist financing risks and negatively affect AML/CFT preventive, detection and investigation/prosecution efforts.”<sup>6</sup> As mobile money shifts a large portion of cash-based transactions to electronic-based transactions, it magnifies the sheer volume of financial movements that can be monitored.

Some may believe that mobile money has an impact on financial integrity risk. The velocity of mobile money transactions<sup>7</sup> could be considered by some as increasing financial integrity risks because they are faster than cash transactions in most cases since mobile money transactions are instant or near-instant. However, mobile money transactions are generally not more rapid than other electronic transactions. So as long as mobile money transactions

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<sup>6</sup> FIN. ACTION TASK FORCE [FATF], FATF GUIDANCE ON ANTI-MONEY LAUNDERING AND TERRORIST FINANCING MEASURES AND FINANCIAL INCLUSION 15-16 (2011), available at <http://www.fatf-gafi.org/media/fatf/content/images/AML%20CFT%20measures%20and%20financial%20inclusion.pdf> [hereinafter FATF GUIDANCE].

<sup>7</sup> Pierre-Laurent Chatain et al., *Integrity in Mobile Phone Financial Services: Measures for Mitigating Risks from Money Laundering and Terrorist Financing* 27 (The World Bank, Working Paper No. 146, 2008), available at [http://siteresources.worldbank.org/INTAML/Resources/WP146\\_Web.pdf](http://siteresources.worldbank.org/INTAML/Resources/WP146_Web.pdf).

are regulated as electronic transactions, there is little reason to be concerned by their velocity. Also, their speed can be met by real-time analysis, providing an opportunity for observation that cash cannot provide.

In fact, mobile money services have the potential to be lower-risk products with respect to financial integrity. Let us not forget that mobile money builds on a mobile operator's core business model of high volumes and low denominations. MTN Uganda allows its customers to send or receive as little as €1.5. Few electronic payment platforms would be able to match that. In its revised recommendations, FATF provides guidance on its risk-based approach and refers to lower-risk circumstances, which include "financial products or services that provide appropriately defined and limited services to certain types of customers, so as to increase access for financial inclusion purposes."<sup>8</sup> This does not mean that mobile money services *per se* are lower risk, but they could be designed in such a way. To qualify as lower risk, mobile money accounts are generally capped with limits in terms of transactions (number of transactions and amounts transacted) as well as balances. MTN Uganda for instance has set a maximum account balance equivalent to €300. Of course, fraudsters and criminals may very well try to use mobile money services if they have no better alternative, but such use would cause their reprehensible activities to become quite visible and traceable.

## II. MOBILE MONEY GENERATES DATA

While reducing the dependency on cash and contributing to the increase in the number of electronic transactions, mobile money also produces a very strong asset for both financial inclusion and financial integrity: data.

Key to the fight against money laundering or terrorism

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<sup>8</sup> FATF, INTERNATIONAL STANDARDS ON COMBATING MONEY LAUNDERING AND THE FINANCING OF TERRORISM & PROLIFERATION: THE FATF RECOMMENDATIONS 64 (2012), available at [http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%20\(approved%20February%202012\)%20reprint%20May%202012%20web%20version.pdf](http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF%20Recommendations%20(approved%20February%202012)%20reprint%20May%202012%20web%20version.pdf).

financing is data, which comprises the entire AML/CFT value chain. Financial institutions are charged, among other things, to generate information about their transactions, to store and monitor that generated data, and to report on the suspicious transactions they identify. This is the purpose of most of the so-called “preventive measures” contained in the FATF recommendations.<sup>9</sup> Public authorities are then responsible for following up on reported suspicious transactions. Recommendation 29 specifies the role of a Financial Intelligence Unit (FIU), which is to serve “as a national centre for the receipt and analysis of: (a) suspicious transaction reports; and (b) other [relevant] information.”<sup>10</sup> FIUs are dependent on the data produced by the financial services industry. The regulatory debate around new services such as mobile money often focuses on the ability of the industry to meet these demands and on whether or not non-bank issuers or providers have to comply with preventive measures. Clearly, if an entity provides a financial service such as mobile money, it should comply with those rules. The challenge is to ensure the rules are applied in a proportional manner.

The introduction of mobile money services also raises other questions: as it considerably increases the amount of electronic transactions and the overall quantity of data produced, what is the capacity of the overall value chain to handle that data? In countries where FIUs are formally in place and actually operational, they manage today, with different degrees of success, data representing the financial services operations of a minority of the population (12 percent in the case of Tanzania, for example). Can they handle the volume of data representing the transactions of 50 percent of the population? And later 75 percent?

If capacity can be an issue, the question of the efficiency of the AML/CFT controls becomes even more important. Mobile money services can be used for all types of transactions, but many of the schemes launched in developing countries are designed to capture low-value transactions. Should AML/CFT controls apply to small value transactions in the same way as they apply to larger value

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<sup>9</sup> *Id.* at 62-66 (Recs. 9-23).

<sup>10</sup> *Id.* at 24.

transactions? The answer is likely to revolve around the application of the risk-based approach.

New data and more data—thanks to the introduction of mobile money services—should prove very helpful on the financial inclusion front. Understanding how poor customers transact might start to shed some light on the behaviors and the needs of a segment of the market that has largely been ignored by many financial services providers. Although little has been done in that area, and a payment behavior does not necessarily reflect the same behavior for other services, there could be interesting applications in the areas of credit and insurance. Insurance services in particular are a great example of a highly data-dependent business that has had very little success in reaching down-market. Without consumer behavior data, the business case for providing insurance to the poor becomes very difficult to build. If insurance providers had access to payment data of poor customers, they could begin to build the business case to serve a new, diverse portfolio of customers. This concept of data's ability to better illustrate a segment of potential customers and allow providers to selectively market to them is of course not specific to the insurance industry; in general, one can imagine how a bank might utilize payment behavior data to develop opportunities to cross-sell additional products, such as credit or long-term savings accounts, that improve the business case for a low-value bank account.

The opportunities discussed above—while providing significant advantages to financial services institutions bold enough to innovate—also place the mobile operators that generate this data in a very sweet spot. This data creates potential new revenue streams that improve the business case for mobile operators. They can now selectively sell data to parties that can utilize it to market products and services that are not in direct competition with mobile money, but rather help to broaden the services that can keep customers loyal to their existing mobile money scheme.

### III. MOBILE MONEY ACCELERATES THE DEVELOPMENT OF ACCOUNTS

If financial inclusion and financial integrity have a common enemy in the form of cash, they may have a common ally in the form of an account, which is an important element of the backbone for financial services. The development of mobile money services increases the number of accounts and sheds a new light on their role for financial inclusion and financial integrity.

Mobile money is often seen through the prism of transactions and presented as a money transfer service and/or a payment platform. Airtel money services in India may “not [be] just about money”;<sup>11</sup> its use cases are centered on sending, transferring, and paying. The need to move money around in an efficient and convenient way is certainly a strong explanation behind the demand for mobile money, but it could not be met without an account. For wealthier users, a mobile money account will be an additional account that likely complements a primary bank account. Conversely, for poorer customers, a mobile money account is often the first one they have and has the potential to integrate them further into the formal financial services ecosystem by providing access to other accounts that cover the range of their financial services needs.

While mobile money is the gateway to an account, accounts are a gateway<sup>12</sup> to using a variety of financial services. They can take different forms to allow more straightforward or sophisticated operations but in all cases, an account remains an essential tool. It provides its user with a financial identity through an account number, which may equate in some cases with a phone number or another legacy identifier. The mobile money account introduces an interesting dimension as it is effectively a transactional account,

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<sup>11</sup> Pia Heikkila, *Mobile Money on Slow Road in India*, THE NAT'L (Apr. 1, 2012), <http://www.thenational.ae/thenationalconversation/industry-insights/technology/mobile-money-on-slow-road-in-india>.

<sup>12</sup> Claire Alexandre, *Financial Regulators and the Gateway to Financial Inclusion*, E-FINANCE & PAYMENTS LAW & POLICY, Sept. 2011, at 11, available at [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=1968677](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1968677).

whereby the main function of the account is to enable transactions and not to solely hold float.

The change in emphasis and its focus on transactions enables an important shift in how to think about the economics of the account. It is no longer solely based on float but now also includes transactions. It is not surprising therefore that the concept was first devised by entities whose business model is primarily transactional: mobile operators. They are accustomed to handling a large number of transactions that are completed in very small denominations. There is no reason why banks could not also start thinking in the same terms and design transactional accounts as well. One of the reasons behind the high rate of financial exclusion lies in the design of accounts, which traditionally has required a minimum account balance at all times and fixed fees which are unrelated to the actual usage of the account. These attributes have placed standard financial accounts out of the reach of poor people.

Beyond their purpose of enabling transactions, mobile money accounts are also often low-value accounts. There are limits on how much one can transact or hold. These limits can be designed by the provider to meet the needs of a specific customer base but control its costs and exposure. They are often also set to reduce *ex ante* the money laundering and terrorism financing risks, and to benefit from lighter Know Your Customer (KYC) controls. In both cases, low-value accounts are attractive for poor customers, meeting some of their financial services needs while not presenting high barriers to entry.

From a financial inclusion perspective, a low-value account is much more interesting than a no-frills account because it is more likely to drive usage rather than simply access. The former is designed to be in some way or form profitable and does charge fees to customers using it; it is based on the analysis that poor customers can and will pay for services which meet their needs but need variable rather than fixed fees. The latter cannot earn revenue directly from the customers (there are usually “free” accounts, which by stipulation cannot incur any fees) as it is often mandated by governments upon service providers. To minimize their loss, these providers are likely to seek to limit the availability of such products and unlikely to market them actively. As expected, no-frills accounts have met limited success; once opened, they remain

dormant and are seldom used. This is the case in India and South Africa.

From a financial integrity perspective, the main benefit of accounts is to establish stable “business relationships” through which transactions can occur rather than witnessing stand-alone transfers on an occasional basis or the use of prepaid cards. This is an equally important point on the financial inclusion side: some services are mere money-transfer services, or over-the-counter solutions, for instance Easypaisa when it started in Pakistan or Tigo Cash in Paraguay. That way, it is relatively similar to Western Union, although for domestic remittances. It is also a popular method of paying bills. The account goes one step further. Overall it is a more recurrent proposition, which makes it easier to move towards a cash-light ecosystem. The account also helps correlate payments across the payment network and makes it easier to collect and analyze data.

#### IV. REMOVING REGULATORY BARRIERS

Mobile money *can* deliver on promises for financial inclusion and financial integrity provided it has the means to develop. While this may sound obvious, the basic supply-side regulatory conditions for mobile money to be issued and used—and therefore begin to develop—are not yet in place in most geographies. Debates are numerous and passionate about the complexity of the issue, the uncertainty, and the risks. Due to the novelty of mobile money businesses, it is not surprising that many are quick to raise issues around consumer protection; the emphasis on the data digitization component of mobile money especially contributes to concerns regarding consumers.

There is very little question regarding the importance of consumer protection, and there are a number of regulatory issues to address on the demand side. For example, ensuring that terms and conditions as well as retail tariffs are published and available seems very sensible. Requiring mechanisms for customers to complain and even a redress mechanism is common sense. Generating and processing and/or storing electronic data require some level of protection on behalf of the consumer. However, sequencing of these regulations is critical to the development of

mobile money. Focusing on these types of regulatory requirements before having even addressed the basic enabling regulatory framework is shortsighted and can impede the initial stages of development. If mobile money services cannot develop, there is no mobile money consumer or data subject to protect. So while not undermining the importance of having the right regulation on the demand side, the priority of any regulator today should be to create an enabling environment for mobile money and to address the supply-side barriers.

A way forward is to move away from a one-size-fits-all regulatory model tailored around one product—credit—and one set of financial service providers—credit-issuing institutions. This way forward implies creating more classes of licenses, allowing tiered controls for account opening, and enabling distribution beyond bank branches through agents and retailers. Ironically by doing so, regulators—although they may disturb the established operating and business models of incumbent banks—may actually contribute to helping them become more efficient and better positioned to serve more customers.

In fact, mobile money is much simpler than it seems at first sight, even from a regulatory perspective. Take the “mobile” element first. It essentially refers to the distribution method the electronic money issuer has decided to use. So the regulatory risks associated with the “mobile” part in mobile money should be dealt with as part of the management of any technology and of the operational risks inherent to any financial service. Presently all financial services have important technology components; technology is not specific to mobile money. There are singularities around mobile technologies, whether at the level of the communication protocols or on the device side, but again they are not unique to mobile money and should be considered within the context of all technology and operational risks. They are present in mobile banking<sup>13</sup> for instance, when a bank allows its customers to access their bank account using a mobile device. Regulatory frameworks are generally more useful and efficient when they

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<sup>13</sup> In this case, the bank is offering a mobile-based service, but does not issue electronic money, so it is not mobile money.

remain neutral from a technology perspective. So there is no need for specific “mobile money” regulation *per se* but instead for rules on electronic money that also apply to mobile money services. Unsurprisingly the “money” element is the most important. From a regulatory perspective, mobile money is not an alternative currency, it is essentially the same currency in electronic form: mobile money is already included as a monetary aggregate through the pooled accounts at the banks. It can be offered by a mobile operator but not exclusively: a bank can also offer a mobile money service, or even a retailer or a technology provider.

The confusion around mobile money usually stems from the question on the licensing of the issuing entity, in particular when it is not a bank. There should be no doubt that any issuer of electronic money must be regulated and therefore licensed to offer the service. This principle is also valid for mobile operators or any third-party technology provider or retailer. The issuing entity should, however, be regulated as an e-money issuer and not as a credit issuer (i.e., a bank). Financial services regulators are mostly accustomed to dealing with banks and tend to associate any funds received from the public as deposit-taking, an activity over which credit-issuing entities have a monopoly. However, electronic money is not a deposit, so electronic money transactions cannot be intermediated by the issuer if it is not a bank. Both the European legislation<sup>14</sup> and the Philippines’ circular on electronic money<sup>15</sup>—which were precursors in mobile money regulation—are very clear on that point. An e-money issuer that is not a bank is usually required by legislation to safeguard those funds and place them within a commercial bank, which is the regulated entity from a prudential perspective. So electronic money should be regulated, but there is no need to regulate the same funds twice.

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<sup>14</sup> Council Directive 2009/110, E-Money Directive, 2009 O.J. (L 267) 7 (EC), available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:267:0007:0017:EN:PDF>.

<sup>15</sup> Amando M. Tetangco, Jr., *Guidelines Governing the Issuance of Electronic Money (E-Money) and the Operations of Electronic Money Issuers (EMI) in the Philippines*, Bangko Sentral ng Polipinas, CIRCULAR NO. 649 (Mar. 9, 2009), available at <http://www.bsp.gov.ph/downloads/Regulations/attachments/2009/c649.pdf>.

In many countries today, there is still no option to issue electronic money without being a bank, buying a bank, or applying for a banking license. There must be more efficient ways to increase the amounts of electronic sources of funds and contribute to improving the efficiency of the payment systems and thereby of the overall financial services sector. Creating new classes of licenses for electronic money issuers is an important step to progress mobile money.

Another regulatory hurdle that mobile money faces relates to account opening. Mobile money issuers are unlikely to invest in mobile money if opening a mobile money account, which is the first step toward using the service, is made impossible or difficult. In many cases today, the same requirements are imposed for customer due diligence (also referred to as Know Your Customer) for any type of account, no matter what amounts they hold or are enabled to transfer. This is unfortunate for two reasons: (1) it defeats the purpose of the controls; and (2) it makes the overall system inefficient.

A uniform KYC<sup>16</sup> means that some customers will not be able to open accounts: they simply do not have the necessary identification documents. As a result, they will continue to manage their financial lives using informal instruments on which no AML/CFT controls are imposed. By placing too high a threshold, the controls are only applied to a very small proportion of the overall transactions and accounts. The total amount of transactions conducted by a given population remains the same; there is simply a greater proportion which happens informally and is therefore not controlled.

A one-size-fits-all approach is not proportionate to the risks of the different accounts. A low-value account ought to have less scrutiny than an account that can be used to transfer or hold more. The type of customer (poor or not) matters relatively little here: a customer is not low risk because he is poor; rather he is low risk when he uses a low-value product.<sup>17</sup> Applying a disproportionately

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<sup>16</sup> The FATF has allowed some flexibility on KYC since 2003, but country-level regulation has often not implemented that option.

<sup>17</sup> As also noted in FATF GUIDANCE, *supra* note 5.

high level of KYC to some accounts and/or transactions does not make them safer in any way but simply more expensive. Putting on a helmet, gloves, and a padded jacket before heading out for a stroll on a walkway similarly does not add much to one's security. It mostly adds cost and inconvenience. Finding the right level of KYC is a matter of efficiency for the service providers and for the whole system.

The solution is to apply a tiered approach whereby different KYC treatments apply to different types of accounts. Mexico has recently adopted legislation along those lines, starting with a very low level anonymous account with limited functionality and then progressively increasing financial and usage limits as the level of KYC increases. This principle of a gradual approach can also be found in the new FATF Recommendation 10 on Customer Due Diligence. The revised sets of international standards are most notable though for including this risk-based approach in the very first Recommendation. It reflects the significant shift exhibited by the intergovernmental organization in the last decade.

The restriction on distribution is the third regulatory hurdle and often an underestimated obstacle. Having mobile money issuers is one good thing, and being able to open an account is another. Having the option to open that account close to home or to work is even better. It excludes the use of bank branches that are relatively few compared to the size of the population.<sup>18</sup> It requires instead the adoption of a broad distribution network, which can be composed of agents and third-party retailers or merchants. This model is not usual in the banking industry, where vertical integration has been the dominant approach. Such a model is expensive to deploy and operate. The solution is once more a tiered one, whereby different locations are available to manage different types of operations. If you only need to open a low-value account or to exchange cash against electronic money, you can go to the “mom and pop shop around the corner” (a small-scale, owner-operated nearby business), reasoning that they sell rice, soap, and pens, why not

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<sup>18</sup> In 2010, there were less than 11 commercial bank branches per 100,000 adults in India and Serbia for instance. There were 35 in the U.S., 33 in Japan and 23 in the Netherlands. *Financial Access Survey*, INT'L MONETARY FUND, <http://fas.imf.org> (last visited Aug. 28, 2012).

also electronic money? If you need to complete paperwork to apply for a loan, you might find it convenient to hand your forms over to an agent. If however you needed to actually discuss a loan with a credit officer or buy a more complex financial product, at that point it might make sense to visit a bank branch.

In most industries, this tiered approach is very common. It is adapted to customers' needs and streamlines the costs of operations. To date, it has not permeated the banking industry, potentially in part due to frequent regulatory restrictions on the overall use of agents or third parties, the type of entities which can play that role, the type of services they can render or also the conditions they must meet to do so. In that case too, agents and merchants should be regulated but in a way that makes sense for the type of service they are providing and for the actual risks generated.

#### CONCLUSION

When not portrayed as contradictory policy objectives, financial integrity and financial inclusion have often been presented as incompatible. Financial inclusion was said to put financial integrity efforts at risk by promoting the use of financial services by the majority if not the entirety of the population. For some expanding access in such a way remains a scary thought. Financial inclusion advocates were blaming financial integrity guardians for undermining their efforts by erecting strict KYC controls. In truth, there is no tradeoff between financial inclusion and financial integrity—on the contrary, they reinforce each other. And mobile money is strengthening that relationship.

