



GLOBAL STANDARDS
PROPORTIONALITY (GSP)
WORKING GROUP



INCLUSIVE FINANCIAL INTEGRITY: A TOOLKIT FOR POLICYMAKERS



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ACKNOWLEDGMENTS

The Inclusive Financial Integrity Toolkit was developed in partnership between the AFI Global Standards Proportionality Working Group (GSPWG) and the Center for Financial Regulation and Inclusion (Cenfri).

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Ramizul Islam (Bangladesh Bank); Masehullah Farokh (Da Afghanistan Bank); Aram Kirakosyan (Central Bank of Armenia); Thinley Cheki (Royal Monetary Authority of Bhutan); Ban Lim (National Bank of Cambodia); Carlos Rodríguez Hernández (Superintendencia General de Entidades Financieras-Costa Rica); Erika Alexandra García Méndez (Banco Central de Reserva de El Salvador); Caroline Pickering (Reserve Bank of Fiji); Tumurkhuyag Batsuuri (Financial Regulatory Commission of Mongolia); Temitope Alabi (Central Bank of Nigeria); Ruth Stegens (Central Bank of Paraguay); Atty. Florabelle M. Santos-Madrid (Bangko Sentral ng Pilipinas); Moussa Dieng (Ministère de l'économie et des finances du Sénégal); Firdavs Tolibov (National Bank of Tajikistan); Peter Joseph Mmari (Bank of Tanzania); Joseph Munyoro (Bank of Zambia).

AFI is grateful for the peer-reviews received from the Financial Action Task Force (FATF) Secretariat; Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) Secretariat and Members; the Asia/Pacific Group on Money Laundering (APG) Secretariat, the Grupo de Acción Financiera de Latinoamérica (GAFILAT) Secretariat and Members; the Global NPO Coalition on FATF; GSMA; and technical expert Professor Louis de Koker (La Trobe University).

We would like to thank AFI member institutions, partners and donors for generously contributing to the development of this publication.

Cenfri's contribution to the toolkit was supported by FSD Africa, a specialist development agency funded by UK aid from the UK Government.

1. INTRODUCTION

Financial exclusion is a condition or state whereby individuals and communities lack access to formal financial services that could have a significantly positive impact on their livelihoods and wellbeing. Since financial exclusion disproportionately impacts those in low-income and developing countries, it compromises the achievement of the Sustainable Development Goals (SDGs) as well as specific national development objectives.

At the same time, widespread financial exclusion poses a serious risk to the integrity of the financial system since it forces individuals and communities to rely on informal financial services that are unregulated and unsupervised, thereby reducing the ability to detect, report, and investigate suspicious transactions. Effectively, this lessens the visibility of risk, which makes it challenging to identify, assess, understand, and mitigate money laundering and terrorist financing (ML-TF) risk.

Given the importance of both financial inclusion and Anti-Money Laundering and Countering the Financing of Terrorism (AML-CFT) to a country's sustainable development and to enhancing livelihoods at household and individual levels, there are opportunities to support the implementation of both processes in a mutually reinforcing manner. Complying with global AML-CFT standards brings many benefits but should not come at the expense of enabling the participation of low-income and vulnerable communities in the formal financial system.

It is against this background that the AFI Global Standards and Proportionality Working Group (GSPWG) has developed a toolkit in partnership with the Centre for Financial Regulation and Inclusion (Cenfri). Compliance and Risk Resources have also provided inputs into this toolkit. We are grateful for peer-reviews received from the FATF Secretariat, Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) Secretariat and Members, the Asia/Pacific Group on Money Laundering (APG) Secretariat, the Grupo de Acción Financiera de Latinoamérica (GAFILAT) Secretariat and Members, and experts.

“

Complying with global AML-CFT standards should not come at the expense of enabling the participation of low-income and vulnerable communities in the formal financial system.

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1.1. ALIGNING FINANCIAL INCLUSION AND AML-CFT

This toolkit provides practical guidance on aligning financial inclusion and AML-CFT outcomes with respect to the formulation and implementation of related policy and regulation. It has been developed with reference to FATF Recommendations as well as risk-based approach guidance relating thereto.²

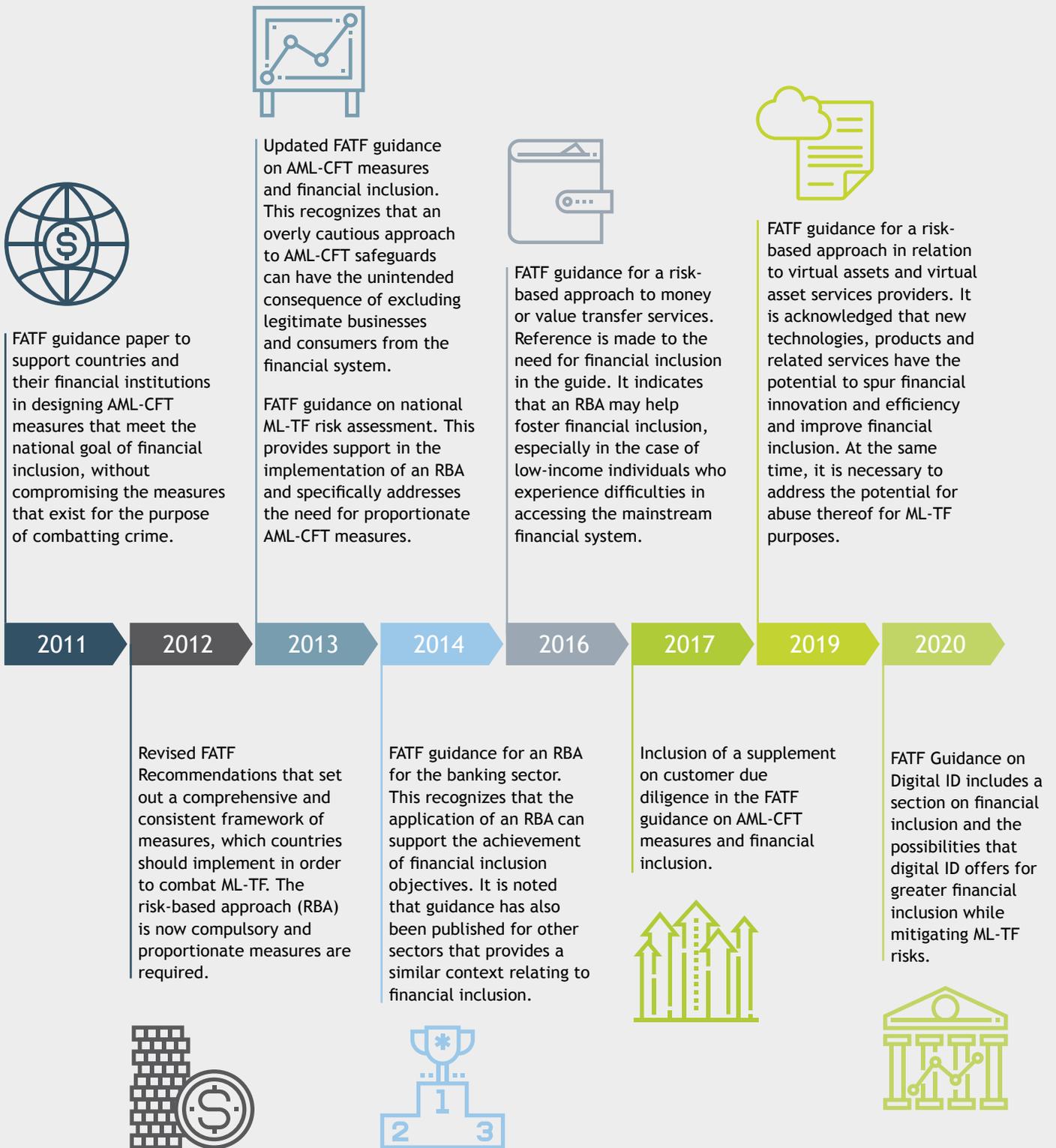
It is apparent that countries have made significant progress towards appreciating the need for financial inclusion within an AML-CFT context. Nevertheless, AFI members continue to face difficulty in developing and maintaining AML-CFT regimes that do not have unintended consequences on financial inclusion.³ Accordingly, aligning the dual policy objectives of financial inclusion and financial integrity remains a challenge. This toolkit seeks to complement existing AFI guidance based on the practical implementation experience of AFI members, and leverages on various studies that address the intersection between financial inclusion and AML-CFT.⁴

2 FATF Guidance for a Risk-Based Approach: The Banking Sector (2014). Available at: [https://www.fatf-gafi.org/publications/fatfrecommendations/documents/fatf-guidance-for-a-risk-based-approach-the-banking-sector.pdf](#); FATF Guidance on AML-CFT Measures and Financial Inclusion with a Supplement on Customer Due Diligence (2017); FATF Guidance for a Risk-Based Approach: Life Insurance Sector (2018); FATF Guidance for a Risk-Based Approach: Securities Sector (2018); FATF Guidance for a Risk-Based Approach: Virtual Assets and Virtual Asset Service Providers (2019); FATF Guidance for a Risk-Based Approach: Accounting Profession (2019). Please see Works Cited list for links.

3 Based on the experience of the AFI membership in practical implementation as shared during AFI-BNM Member Trainings on Aligning AML-CFT and Financial Inclusion in 2017 and 2018; stakeholder interviews with AFI members; and technical-level policy deliberations at various AFI forums.

4 AFI Guideline Note 20 on National Financial Inclusion Strategies: A Toolkit (2016) and 31 on Gender Considerations in Balancing Financial Inclusion and AML-CFT (2018); AFI and Bank Negara Malaysia Member Training on Aligning AML-CFT and Financial Inclusion (2017, 2018); AFI Global Standards Proportionality Working Group (GSPWG) Meetings (2017, 2018); AFI Survey on Aligning Financial Inclusion and AML-CFT (2018); AFI Digital Financial Services Working Group (DFSWG) KYC Innovations Study (2019); AFI targeted stakeholder interviews (2019); Cenfri Guidance Note on Inclusive Financial Integrity (2017); Cenfri Biometrics and Financial Inclusion Study (2018); Cenfri technical assistance and capacity-building work on inclusive integrity to date; and FATF Recommendations and various guidance, namely FATF Guidance for a Risk-Based Approach: The Banking Sector (2014), FATF Guidance on AML-CFT Measures and Financial Inclusion with a Supplement on Customer Due Diligence (2017) and FATF Guidance on Digital ID (2020). Please see Works Cited list for links.

BOX 1: FATF STANDARDS AND SELECTED GUIDANCE*



* The box does not represent a complete analysis of all FATF guidance that refers to financial inclusion. Selected references are included for illustration purposes.

Box 1 identifies FATF guidance that reflects on financial integrity in relation to financial inclusion. It provides context relating to the role that is being played by the FATF in addressing the need for financial inclusion.⁵

1.2. WHO IS THE TOOLKIT FOR?

This toolkit is intended for policymakers, regulators, supervisors and other stakeholders involved in the formulation and implementation of policy and regulation that advance both financial inclusion and financial integrity. It provides practical steps to engage with the country frameworks and processes that support financial inclusion and financial integrity.

1.3. HOW IS THE TOOLKIT STRUCTURED?

The toolkit begins by introducing the concept of inclusive financial integrity. The chapters that follow cover the interrelated components of AML-CFT structures and processes in this regard, specifically AML-CFT policy development and implementation, National Risk Assessments (NRAs), enabling regulatory obligations, National Financial Inclusion Strategies (NFIS), in on-going Customer Due Diligence (CDD) processes, risk-based supervision, as well as Mutual Evaluations (MEs). The challenges experienced by AFI members in aligning financial inclusion and financial integrity in the processes above are explored and experiential solutions are provided.

While the above topics are vast in their own right, the toolkit is not exhaustive on every topic. It selectively goes into greater detail on some topics more than others, largely based on key areas highlighted by AFI members during stakeholder interviews, trainings, and working group meetings conducted in 2017, 2018, and 2019.

The toolkit's chapters are structured as follows:

Chapter 1: Introduction

This chapter introduces the toolkit.

Chapter 2: Inclusive financial integrity

The purpose of this chapter is to examine definitions of financial inclusion and financial integrity, address the concept of aligning financial inclusion and financial integrity and explain why it is important, as well as to highlight key aspects of “what success looks like” in relation to inclusive financial integrity.

Chapter 3: AML-CFT strategy, policy and accountability framework

The purpose of this chapter is to describe the context for AML-CFT policies and to discuss inclusive financial integrity considerations in relation to an AML-CFT policy and accountability framework.

Chapter 5: AML-CFT considerations in a national financial inclusion strategy (NFIS)

The purpose of this chapter is to briefly describe AML-CFT considerations in an NFIS and highlight key features relating to the synchronization of financial inclusion and financial integrity processes.

Chapter 5: Aligning financial inclusion and AML-CFT in NRAs

The purpose of this chapter is to identify and describe key considerations in aligning financial inclusion and AML-CFT in NRAs.

Chapter 6: Regulatory frameworks

The purpose of this chapter is to highlight key regulatory framework challenges, describe tools that can be used to inform the development of regulatory frameworks and identify RegTech opportunities.

Chapter 7: Aligning financial inclusion and AML-CFT in ongoing processes

The purpose of this chapter is to identify key challenges in aligning financial inclusion and AML-CFT in ongoing processes, to discuss how AFI member countries are addressing these to promote inclusive financial integrity and to discuss gender and forcibly displaced persons considerations in this regard.

Chapter 8: Risk-based supervision

The purpose of this chapter is to describe key aspects of the risk-based supervision approach and to highlight financial inclusion considerations relating thereto.

Chapter 9: Inter-agency coordination in NRAs and MEs

The purpose of this chapter is to identify inter-agency coordination challenges and to highlight possible solutions and considerations that are relevant in relation to NRAs and MEs.

Chapter 10: Aligning financial inclusion and AML-CFT in MEs

The purpose of this chapter is to identify and describe key ME considerations in relation to financial inclusion.

Chapter 11: Summary of key takeaways

This section concludes on key themes and takeaways across each of the sections.

It is envisaged that the toolkit will provide a platform for further engagement with AFI member countries. This will offer an opportunity to update the toolkit and progress the inclusive financial integrity conversation. The key takeaways that are included in Chapter 11 will serve as a point of departure in this regard.

⁵ <http://www.fatf-gafi.org/media/fatf/content/images/Updated-2017-FATF-2013-Guidance.pdf>

2. INCLUSIVE FINANCIAL INTEGRITY

The purpose of this chapter is to discuss definitions of financial inclusion and financial integrity, address the concept of aligning financial inclusion and financial integrity and explain why it is important, as well as to highlight key aspects of “what success looks like” in relation to inclusive financial integrity.

2.1. DEFINING FINANCIAL INCLUSION

There is no single definition of financial inclusion, and the established practice in the National Financial Inclusion Strategies (NFIS) of AFI members is for individual countries to adopt their own strategies based on specific country circumstances and priorities.⁶ However, in general terms, financial inclusion refers to the “access to, and usage of, a range of financial products and services provided by formal financial service providers to specific target groups or all segments of the population, as well as the quality of these products and services” (AFI, 2016).⁷ Defining financial inclusion is one of the most crucial steps in formulating a sound NFIS.⁸ This is an increasingly common policy approach adopted by financial regulatory authorities that are furthering financial inclusion objectives. Not only does a comprehensive financial inclusion definition clearly stipulate the mandate of the NFIS, it additionally guides the determination of the strategy’s financial inclusion goals, policy measures and actions, monitoring and evaluation framework, stakeholders, and target groups.

The definition of financial inclusion should be concise but comprehensive enough to enable specific actions by stakeholders, tracking, and impact measurement. Important dimensions that should be incorporated into a definition beyond the “number of bank accounts” include:

- > **Usage:** Regular usage indicates that financial products and services meet the needs of target groups and are effective in sustaining their financial inclusion.
- > **Convenience:** Ease of access demonstrates the ability to consider the proximity of target groups to formal access points.

- > **Affordability:** Affordable financial products and services means ensuring that target groups are not discouraged from accessing formal finance and do not resort to informal products and services due to expensive charges.
- > **Consumer protection:** Protecting the target group is essential and ensures that formal financial providers offer products and services that are fair, treat consumers with dignity, protect their data, and build consumer trust.
- > **Target group:** An inclusive definition would state “all segments of the population,” “financially excluded,” or “underserved customers.” Typically, the target groups of NFIS are the low-income, particularly vulnerable and marginalized segments of the population.

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The mandate of advancing financial inclusion is not a task of a single institution, but a cooperative and supportive effort among different stakeholders.

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6 Alliance for Financial Inclusion. 2018. National Financial Inclusion Strategies: Current State of Practice. Available at: <https://www.afi-global.org/sites/default/files/publications/2018-06/National%20Financial%20Inclusion%20Strategies.pdf>

7 Alliance for Financial Inclusion. 2016. National Financial Inclusion Strategies Toolkit. Available at: <https://www.afi-global.org/sites/default/files/publications/2016-08/Guideline%20Note-20%20FIS-Toolkit.pdf>

8 According to AFI (2017), an NFIS will specifically: (a) Inform the setting of financial inclusion goals, objectives, strategic measures and targets; (b) Guide the development of an action plan and monitoring and evaluation (M&E) framework to ensure the targets are achieved; (c) Enhance the linkage with wider national development objectives; (d) Facilitate the communication of the NFIS to a wide range of stakeholders who are instrumental in its formulation and implementation, including AML-CFT stakeholders, the private sector and civil society; and (e) Shape expectations around the market dimensions that will be emphasized and how each target group will benefit. Alliance for Financial Inclusion. 2017. Defining Financial Inclusion. Available at https://www.afi-global.org/sites/default/files/publications/2017-07/FIS_GN_28_AW_digital.pdf

Figure 1 highlights the dimensions that member countries have incorporated in their definitions of financial inclusion.⁹

The dimensions referenced below do not need to be viewed as static when the NFIS is being implemented. They should evolve as financial technology, financial exclusion, and financial integrity issues evolve. However, the definition of financial inclusion should be properly contextualized to address the unique financial exclusion challenges of a country from the outset. This will support the appropriate interpretation thereof by stakeholders when the NFIS is implemented.

Stakeholder interviews (2019) and engagement during AFI training (2017, 2018) confirmed that country definitions of financial inclusion have been a valuable source of reference in the formulation of country strategies.

2.2. DEFINING FINANCIAL INTEGRITY

Financial integrity generally refers to the soundness of a financial system in dealing with risks and threats to its safety. A financial system is considered to have integrity if it is effectively safeguarded against efforts to use it for ML-TF purposes, financing of proliferation and other financial crimes, such as illicit financial flows. It should have adequate and effective measures in place to

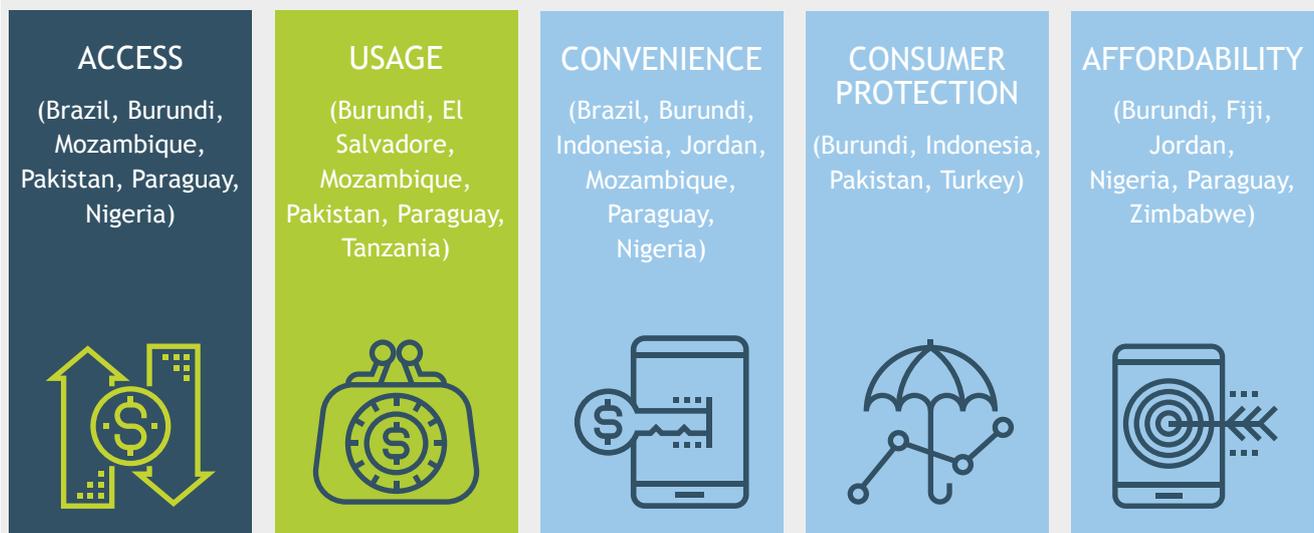
identify, assess, understand and mitigate the risks. It should also provide for the means to act as soon as the risks have been detected.

There appears to be some ground to cover in understanding the full extent of financial integrity. For example, during interviews held with stakeholders from AFI member countries (2019), the indications were that the role and impact of the informal financial system is not fully appreciated in the context of financial integrity. One of the outcomes of this position is that, in general, countries do not appear to have a structured approach to addressing the overall financial system both formal and informal. Illicit financial flows that move through the informal financial systems may not be properly appreciated or accounted for. Accordingly, there is an opportunity to address the definition of financial integrity at country level to ensure that all aspects are incorporated into a country’s AML-CFT strategy and regime.

⁹ Only includes AFI member countries that responded to the survey conducted for Guideline Note 28: Defining Financial Inclusion. AFI. 2017. Available at https://www.afi-global.org/sites/default/files/publications/2017-07/FIS_GN_28_AW_digital.pdf

¹⁰ Alliance for Financial Inclusion. 2018. National Financial Inclusion Strategy: Current State of Practice 2018. Available at: <https://www.afi-global.org/sites/default/files/publications/2018-06/National%20Financial%20Inclusion%20Strategies.pdf>

FIGURE 1: EXAMPLES OF DIMENSIONS INCLUDED IN THE DEFINITION OF “FINANCIAL INCLUSION” IN SELECTED NFIS



2.3. RISK AND THE RISK-BASED APPROACH (RBA) TO ACHIEVE FINANCIAL INTEGRITY

Achieving financial integrity outcomes requires a robust understanding of risk and the implementation of a Risk-Based Approach (RBA) that is in line with FATF Recommendations and related guidance.

FATF guidance (2013) indicates that ML-TF risk is a function of three factors - threat, vulnerability, and consequences. Threat refers to the factors that could potentially cause harm to a country. In the ML-TF context, a threat is a person, group of people, object or activity which could conduct ML-TF and/or exploit the financial system for criminal activities. Understanding the threats that a country faces with regards to ML-TF is an essential first step in developing a framework for combatting ML-TF. Vulnerability refers to the weaknesses in the AML-CFT systems or controls for a sector, financial product or service that enable the threats to materialize. Consequences refer to the impact or harm that ML or TF may cause. When viewed together, these concepts represent the ML-TF risk of a country.

Addressing risk in an RBA entails a proportionate approach whereby “countries, competent authorities and financial institutions are expected to identify, assess and understand ML-TF risks to which they are exposed and take AML-CFT measures commensurate to those risks in order to mitigate them effectively” (FATF, 2014).¹¹ This means more resources should be allocated towards addressing higher-risk areas and fewer resources allocated to lower-risk areas.

Each jurisdiction may face different risks and the context of its threats and vulnerabilities will influence the AML-CFT strategies pursued by the public authorities and private sector. The key risks with impact on financial integrity are described in Box 2.

The risks are experienced differently and differ in degree at institutional level depending on the customer, product, delivery channel, client and geographic factors. Country-level consideration of all the risks contained in Box 2 has the potential to steer country-level policy towards addressing the broad challenges that are often experienced in relation to inclusive financial integrity, including financial exclusion risk and illicit financial flows risk.

BOX 2: KEY FINANCIAL SECTOR RISKS

ML RISK

The risk that a country, financial institution or business unit could be used for ML.



TF RISK

The risk that a country, financial institution or business unit could be used for TF. While in many respects this is like ML risk, TF risk has features that may be different.



COMPLIANCE RISK

This is a risk that arises due to non-adherence to regulatory requirements, breaching of laws, guidelines, industry standards, internal policies and procedures including best practices. This can lead to fines and penalties for financial service providers (FSPs) as well as reputational damage. Compliance risk can be a major reason for de-risking* in the financial services sector, however this may vary with regions. Additionally there are jurisdictions that comply with their regulatory requirements but are still being de-risked.



RISK OF FINANCIAL EXCLUSION

The risk of excluding customers due to lack of robust AML-CFT information is that people can be deprived of financial services and this can lead to large unregulated informal sectors. This is a vulnerability that can be exploited for ML and illicit financial flows.



ILLICIT FINANCIAL FLOWS RISK

Illicit financial flows are defined as the illegal cross-border movement of funds and resources. They have a significant impact on development outcomes by reducing tax revenue to governments (Cooper et al., 2018).



Source: Cenfri, 2018; FATF, 2016

¹¹ Financial Action Task Force. 2014. FATF Guidance for a Risk-Based Approach: The Banking Sector. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/Risk-Based-Approach-Banking-Sector.pdf>

2.4. WHY ALIGN FINANCIAL INCLUSION AND FINANCIAL INTEGRITY?

Aligning financial inclusion and financial integrity refers to the implementation of effective, risk-based and proportionate AML-CFT regimes which take account of financial inclusion objectives as set out in the NFIS, and which advance the financial inclusion and financial integrity agendas together.

It is important to align financial inclusion and financial integrity because they have complementary objectives, such as national development, enhanced outcomes, and better livelihoods for society. In addition, financial exclusion itself is a risk to financial integrity, as noted by the FATF in its guidance notes detailed in Box 1. Moreover, the application of measures which enable more people to use formal financial services will increase the reach and the effectiveness of AML-CFT regimes. Financial inclusion is, therefore, a key objective for financial integrity.

However, if financial inclusion and financial integrity are implemented separately or without any collaboration, they can diminish one another. For example, pursuing financial integrity without considering financial inclusion or financial exclusion risk, may lead to the restriction of highly inclusive financial products. On the other hand, only focusing on inclusion without considering integrity can lead to the entrance of a wide range of new, potentially inclusive technologies that may be susceptible to abuse for ML-TF purposes. Implementation of financial inclusion and financial integrity initiatives, therefore, requires an aligned approach whereby the two are complementary and supported by a collaborative approach from the stakeholders involved. This enables a strong understanding of the trade-offs and impacts that the initiatives will have.

There are various opportunities for the integration of financial inclusion and financial integrity. For example, this can be represented by the integration of NRA results into national AML-CFT strategies and the NFIS. Alternatively, it could be represented by the incorporation of financial inclusion considerations into an NRA. The extent of alignment between the two, or the inclusive financial integrity baseline, can be determined by examining a country's context, financial inclusion and financial integrity objectives, and progress already made towards achieving them. Tools that are useful for this purpose include national financial inclusion diagnostics informed by supply-side and demand-side surveys, rapid financial inclusion assessments, Finscope and Fin-Access surveys and so

on, which are leveraged to establish a country's state of financial inclusion. The baseline will reveal how much ground there is still to cover in achieving the alignment.

2.5. WHAT DOES SUCCESS LOOK LIKE?

A first step towards aligning financial inclusion and AML-CFT is for all relevant national stakeholders to define a shared vision based on what "success looks like" when inclusive financial integrity has been achieved. This can be seen as the contextualization of the inclusive financial integrity process according to the country's specific peculiarities, including its NFIS and policies, its AML-CFT strategy and policies, and the national stakeholders involved in formulating and implementing these. In some countries, it is uncommon for financial inclusion and AML-CFT stakeholders to consistently coordinate with one another towards aligning their respective policy objectives and actions.

Therefore, it is imperative that a shared vision be consultatively formulated and then clearly stated and that the relevant national stakeholders reach a consensus on what success in achieving inclusive financial integrity looks like. Only then will there be an increased, collaborative effort to take appropriate policy actions towards that end. It is crucial to catalyze this inclusive, cross-agency and cross-sectoral coordination from the very beginning so that the country's journey towards achieving inclusive financial integrity be comprehensive and continuous. This is explored in further detail in *Chapter 3: AML-CFT policy, strategy, and accountability*; *Chapter 4: AML-CFT considerations in a national financial inclusion strategy (NFIS)*; and *Chapter 9: Inter-agency coordination in NRAs and MEs*.

Additionally, the progress and impact of the policy actions taken towards achieving the shared vision should be periodically monitored and evaluated even beyond external assessments being undertaken in-country, such as MEs. This practice of self-assessment will promote rigorous improvements in the country frameworks and processes that are needed to achieve inclusive financial integrity.

Some components of an AML-CFT framework can be leveraged to achieve inclusive financial integrity. This is illustrated in Figure 2.

Figure 2 identifies some of the major components of an AML-CFT framework that can be leveraged to achieve the shared vision of inclusive financial integrity. As a start, a country's AML-CFT strategy and policy should be developed considering all the components and should

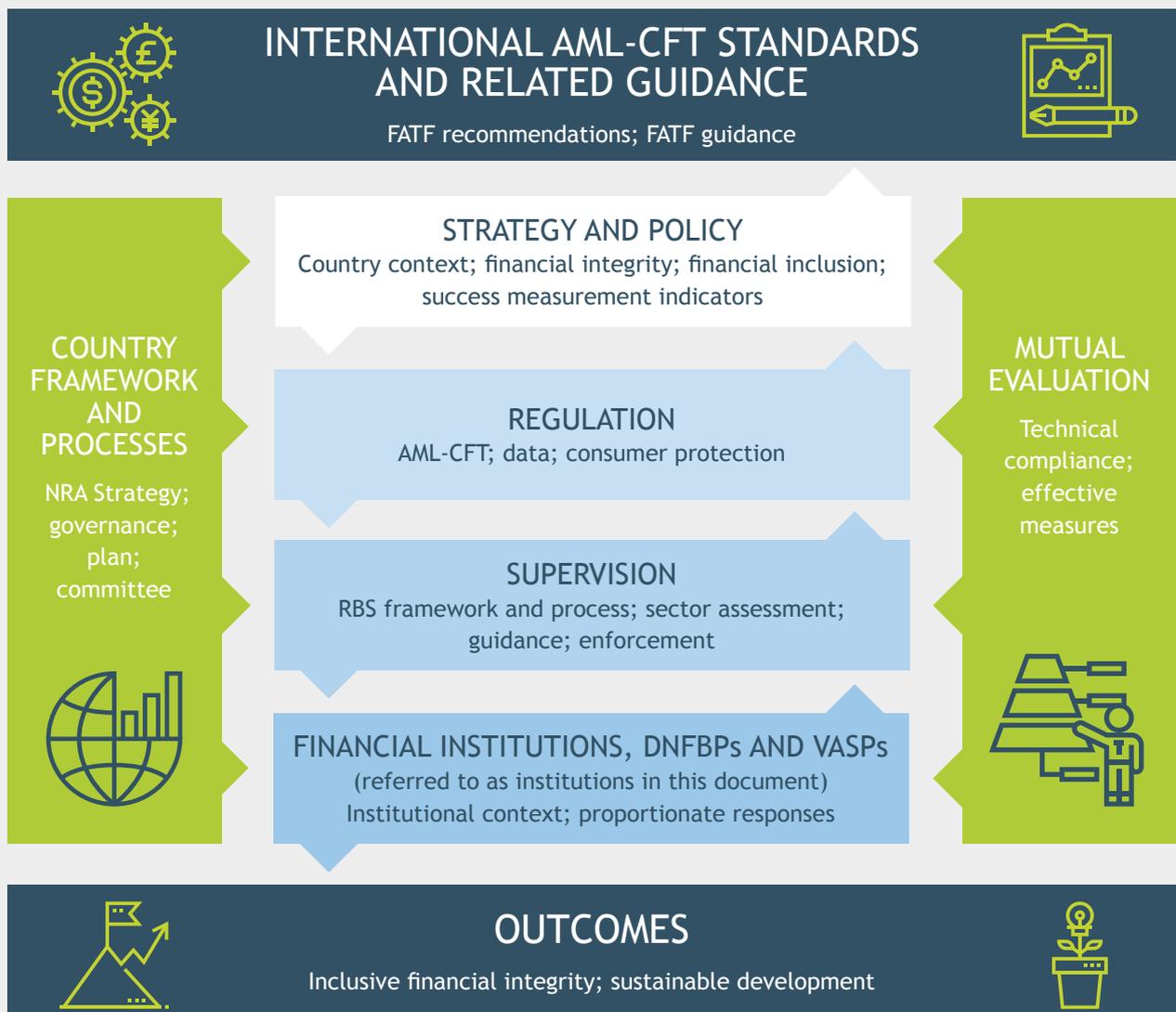
support the development of measures that can be tracked towards the achievement of inclusive financial integrity. This should inform the design, development and implementation of all other components of the framework. Implementation, continuous engagement and consultations will also make opportunities available for bottom-up and not just top-down strengthening of the framework. Each component should work in a coordinated manner with the others to achieve both financial inclusion and financial integrity policy objectives. This will be explained throughout the chapters of this toolkit. It is noted that Figure 2 includes reference to the chapter numbers of this document. This will assist in linking each chapter to the overall context of an AML-CFT framework.

Figure 2 captures the major components but does not represent the entirety of an AML/CFT regime. For example, it does not include law enforcement authorities and their role in AML-CFT since these may not have as much influence in the financial inclusion agenda. As such, countries should include additional, relevant components to complete their unique AML/CFT framework as appropriate to their context.

SUCCESS FOR FINANCIAL INCLUSION

Success for financial inclusion means that previously excluded segments of a country’s population can access and use quality formal financial services to meet their specific needs. It also means there is assurance that those who already have access to formal financial

FIGURE 2:



services are not excluded based on any misperception of risks or other unjustified reason, and consequently driven to use informal financial services. This can be measured by various means. As mentioned in Chapter 1.1, a good start is to first establish a definition of financial inclusion that incorporates all the dimensions which will catalyze policy actions that lead to the desired outcomes.¹² It would then be good to align measurement indicators with the definition so that these outcomes can be effectively measured. AFI members would normally include aspects like access, usage, convenience, affordability, consumer protection, and target groups in their financial inclusion definitions and develop measurement indicators accordingly.

This typically involves going beyond traditional indicators such as “number of bank accounts” towards indicators, which look at uptake, usage, and the actual impact of financial inclusion products on the livelihoods of target groups (AFI, 2017).¹³ The 2017 Global Findex Data shows that - from an access perspective - financial inclusion has been increasing steadily and significantly in developing regions across the world, rising from 23% in 2011 to 43% in 2017.

However, there are more in-depth indicators that can reveal the actual success of financial inclusion, including through examining whether policy actions are really meeting the financial needs of the target groups. For example, if resilience is a dimension of the financial inclusion definition, then uptake and usage of insurance products by vulnerable or disadvantaged groups could be a measurement indicator against which progress can be monitored and evaluated.¹⁴

SUCCESS FOR FINANCIAL INTEGRITY

According to the FATF,¹⁵ the high-level objective of AML-CFT is to ensure “financial systems and the broader economy are protected from the threats of money laundering and the financing of terrorism and proliferation, thereby strengthening financial sector integrity and contributing to safety and security.” This provides a broad context for the development of AML-CFT policy at the country level.

At a more granular level, success for financial integrity is measured from a technical standpoint in terms of compliance with the FATF Recommendations and from an effectiveness perspective against the 3 intermediate outcomes and related 11 immediate outcomes.¹⁶ The mutual evaluation assessment (ME), which is undertaken according to the FATF methodology¹⁷ is the tool that measures the above technical and effectiveness outcomes (FATF, 2019).¹⁸

While the understanding of success in financial integrity has been commonly viewed as obtaining favorable ME results, this should not be perceived as the end goal. Rather, more focus should be on how achieving effective compliance with global AML-CFT standards enables positive development outcomes. It is recognized that financial integrity interventions (including AML-CFT policy, regulatory obligations and supervision measures) that also support financial inclusion have the further potential to create stable investment environments, promote sustainable development and stimulate inclusive growth as they reduce financial crime, corruption and the size of the informal financial sector. These are important considerations and should be the ultimate focus of inclusive financial integrity measures. Financial integrity, as is the case with financial inclusion, should be understood as a building block for creating long-term, sustainable economic and social environments. The setting of financial integrity success criteria should therefore recognize and incorporate the various risks in Box 1 and align them with the respective country context, policy and strategic imperatives.

SUCCESS FOR INCLUSIVE FINANCIAL INTEGRITY

Success for inclusive financial integrity refers to a situation whereby a safe financial system that has adequate and effective measures in place to identify, assess, understand and mitigate ML-TF risks and to act as soon as the risks have been detected, is equally able to provide greater access to and usage of quality formal financial services in a way that enhances livelihoods and drives sustainable development.

12 Financial Action Task Force. 2014. FATF Guidance for a Risk-Based Approach: The Banking Sector. Available at: <http://www.fatf-gafi.org/media/fatf/documents/reports/Risk-Based-Approach-Banking-Sector.pdf>

13 Alliance for Financial Inclusion. 2017. Defining Financial Inclusion. Available at: https://www.afi-global.org/sites/default/files/publications/2017-07/FIS_GN_28_AW_digital.pdf

14 FinNeeds Toolkit. Collaboration between insight2impact and the Alliance for Financial Inclusion: Available at: http://access.i2ifacility.org/Measurement_framework/

15 Financial Action Task Force. 2013. Assessing Technical Compliance with The FATF Recommendations and the Effectiveness of AML/CFT Systems. Available at: <https://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%20Methodology%2022%20Feb%202013.pdf>

16 Financial Action Task Force. 2019. Methodology for Assessing Technical Compliance with the FATF Recommendations and the Effectiveness of AML/CFT Systems. Available at: <https://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%20Methodology%2022%20Feb%202013.pdf>

17 Financial Action Task Force. 2019. Procedures for the FATF Fourth Round of AML/CFT Mutual Evaluations. Available at: <https://www.fatf-gafi.org/media/fatf/documents/methodology/FATF-4th-Round-Procedures.pdf>

18 Refer to the updated FATF Methodology (2019): <http://www.fatf-gafi.org/media/fatf/documents/methodology/FATF%20Methodology%2022%20Feb%202013.pdf>.

Measures to establish a framework for successful inclusive financial integrity include aligning financial inclusion and AML-CFT policy objectives and processes; ensuring the outcomes and decisions from the two processes feed into one another; strongly linking the financial inclusion and AML-CFT processes with national sustainable development objectives and processes such as national development plans and sustainable development goals; interfacing financial inclusion and AML-CFT coordination structures so that both sets of stakeholders can coordinate their efforts; and sharing information and data that can subsequently be analysed together to inform policy decisions. In addition, the indicators of success for inclusive financial integrity should be aligned with the desired outcomes that would have been developed based on the shared vision of this success. As previously mentioned, these should be established collaboratively between relevant national stakeholders at a country policy level and should subsequently be addressed in an ongoing and dynamic process that is continuously improved by self-assessments to ensure that implementation is on track.

Despite the importance of achieving inclusive financial integrity, it is taking a long time for stakeholders to get the alignment right and make meaningful progress on their inclusive financial integrity journeys. Engagements with stakeholders in technical assistance programmes as well as research by Symington et al. (2011, 2017) attribute this to the following reasons, among others:

- > There are challenges preventing the effective conduct of NRAs, such as capacity for data collection and analysis
- > The RBA is still taking root in several countries, particularly where they are just moving away from a rules-based approach.
- > Some countries still, to some extent, perceive financial inclusion and financial integrity to be competing policy objectives.
- > In other countries, even though there is a theoretical recognition of complementarity, there are practical challenges in aligning incentives. In practice, different sets of actors are responsible for financial inclusion and financial integrity and, as a result, the processes are often not joined up or harmonised.
- > The timelines of NFIS and NRAs are often not synchronized, which makes it difficult for both processes to feed into each other.

- > National policymakers and private sector actors such as financial institutions are incentivized to act conservatively due to strict penalties and fines from regulators and the threat of de-risking. The pervasiveness of zero tolerance¹⁹ to risk by some regulatory authorities and financial institutions incentivizes this conservative behavior.
- > There are underdeveloped governance and accountability systems in both public and private institutions.
- > There is outdated national legislation that is incompatible with innovative compliance practice.
- > Inappropriate responses from institutions such as overly strict application of CDD and de-risking
- > Limited AML-CFT capacity and ability to implement measures effectively in both the public and private sectors.

The subsequent chapters provide key considerations in aligning financial inclusion and AML-CFT, considering the above. This is based on AFI member experiences, in particular, the challenges they faced when attempting to proportionately apply risk-based AML-CFT standards, as well as the practical lessons they learnt during such implementation. It is also based on the authors' experience while providing technical assistance to several countries in the sub-Saharan Africa region.

¹⁹ Zero tolerance to risk refers to the attitude or position by authorities or institutions to not allow ML-TF risk at all in their operations. This is a legacy of the rules-based approach and is not compatible with the risk-based approach. This approach seeks to avoid risk rather than manage it. Cenfri and partners have encountered this in South Africa and regional engagements with regulators and institutions in Africa.

3. AML-CFT POLICY, STRATEGY AND ACCOUNTABILITY

The purpose of this chapter is to describe the context for AML-CFT policies and to discuss considerations that should be considered in relation to an AML-CFT policy and accountability framework.

3.1. FATF CONTEXT

The international AML-CFT standards do not specify detailed requirements relating to the development of country-level AML-CFT policies, and guidance relating for this has not been provided. However, there is reference to the need for AML-CFT policy in the introduction to the FATF Recommendations and the following is stated: “Countries should have national AML-CFT policies, informed by the risks identified, which should be regularly reviewed, and should designate an authority or have a coordination or other mechanism that is responsible for such policies.”²⁰ This provides a general policy context, but nonetheless opens the door for discussion relating to the need for country AML-CFT policy.

There is reference to policies that are required by institutions in several of the interpretive notes to the FATF Recommendations. This recognizes the need for institutional-level policies, which would be addressed in country AML-CFT regimes and considered by supervisors in their supervision of institutions.

The country’s interpretation of the international AML-CFT standards is important. Throughout the policy process, there should be careful consideration of whether an action and a specific step is indeed an obligation under the FATF Recommendations or whether it is optional. For example, there is an obligation for countries, financial institutions, and DNFBPs to identify, understand, and assess their risks but this does not amount to an obligation to develop an NRA. Equally, countries need to have risk-based mitigation measures, but there is no obligation to have an AML-CFT strategy. NRAs and AML-CFT strategies are common and encouraged because these have been helpful for countries to establish their country risk profiles and put in place mitigation measures respectively.

“

A national AML-CFT policy and accountability framework would need to be framed with reference to FATF Recommendations and should consider relevant guidance relating to the RBA.

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3.2. AML-CFT POLICY, STRATEGY AND ACCOUNTABILITY OVERVIEW

A national AML-CFT policy and accountability framework would need to be framed with reference to FATF Recommendations and should consider relevant guidance relating to the RBA. This could be structured to encourage the achievement of both financial inclusion and AML-CFT outcomes from the very beginning, or when the opportunity presents itself. Additionally, it can be designed to be outcome-oriented and therefore provide specific actions that are accompanied by measurement criteria, established based on the policy’s goals. Several AFI members have strategic plans for implementing the FATF Recommendations, but few have developed comprehensive strategies that have been fully integrated into their country’s development plan. For example, a 2019 AFI member country interview conducted among select AFI members across the developing world indicated that only few countries have AML-CFT policies in place (AFI member country interviews, 2019).

In this regard, the objectives of financial inclusion and financial integrity should be addressed holistically at a country-policy level. Also, national-level AML-CFT objectives can be supported by implementing an RBA at the sectoral level, including the adoption or development of policy that is relevant within this context, i.e. aligned with the country AML-CFT policy.

²⁰ Financial Action Task Force. 2004. FATF 40 Recommendations. (Recommendation 2). Available at <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/the40recommendationspublishedoctober2004.html>

NATIONAL AML-CFT STRATEGY

A national AML-CFT strategy forms the base from which a country will achieve its financial integrity and financial inclusion objectives. In order to create an effective strategy for AML-CFT, countries need to understand their ML-TF risks. Conducting diagnostic studies of ML-TF risk in a country (such as through an NRA), among other tools, can be used to inform strategy. However, stakeholder interviews (AFI member countries, 2019) indicate that the impetus for strategy formulation often comes from an impending ME rather than from an ongoing commitment to the AML-CFT processes. All the key components highlighted in Figure 2 should be considered in developing an AML-CFT strategy. There should be recognition of the need to address all forms of illicit financial flows, including ML, TF, trade-based money laundering, resource smuggling and other financial crimes. Importantly, the ultimate objective of the strategy should include a reduction in ML-TF, but also improved financial inclusion and sustainable development outcomes development outcomes.

EFFECTIVE COLLABORATION AND COORDINATION

Effective coordination structures, working groups and technical committees play an important role in an AML-CFT policy framework. Money laundering and broader illicit financial flows are issues that cut across multiple mandates and, therefore, require ongoing cross-departmental and cross-agency collaboration. Effective policymaking processes enable collaboration between stakeholders and the opportunities determining clear objectives and empowering authorities that are responsible for investigating and prosecuting financial crime.

3.3. AFI MEMBER EXPERIENCE WITH AML-CFT POLICY AND ACCOUNTABILITY FRAMEWORKS

Stakeholder discussions (AFI member countries, 2019) indicate that countries do not generally have fully developed AML-CFT policy frameworks in place. However, some countries have national AML-CFT strategies that are used to support the efforts of stakeholders in implementing the measures required. Select examples of approaches taken by countries are reflected in Figure 3.

The need for an AML-CFT policy that can be used to effectively guide and support country stakeholders in the achievement of required outcomes remains urgent among AFI members.

FIGURE 3: EXAMPLES OF COUNTRY AML-CFT POLICY APPROACHES

<p>ZAMBIA</p> 	<p>Zambia has an accountability process in its action plan, which requires quarterly reporting on financial inclusion objectives progress especially on aligning AML-CFT and financial inclusion.</p>
<p>BHUTAN</p> 	<ul style="list-style-type: none"> > Bhutan has in place an AML-CFT Act & AML-CFT Rules and Regulations. > All reporting entities need to give input into the AML-CFT policy. > Onsite inspections ensure effective implementation of AML-CFT policy.

Source: Interviews (2019)

3.4. INCLUSIVE FINANCIAL INTEGRITY CONSIDERATIONS IN AML-CFT POLICY, STRATEGY AND ACCOUNTABILITY FRAMEWORKS

CONSIDERING RISK APPETITE AND RISK TOLERANCES

The concepts of risk appetite and risk tolerance are central to any risk management process. Risk appetite and risk tolerance refers to the level of risk an institution (generally private sector entities) is willing to tolerate in pursuit of its objectives and which define the acceptable amount of risks in light of their different individual business lines and overall commercial strategy. During interviews held with AFI member country stakeholders (2019), it was noted that AML-CFT authorities expect institutions to establish risk appetites as part of their RBAs. Where possible risk appetites and risk tolerances at country level could help inform institution level risks. While countries may not choose to develop risk “appetites and tolerances” in the same way that institutions do, the authorities should have an understanding of what an acceptable level of risk at the institution-level might entail vis a vis overall country considerations and circumstances. This will help provide better guidance to institutions as well as better assessments of the risk appetites of institutions.

ADDRESSING THE ROLES OF VARIOUS STAKEHOLDERS

The accountability and governance framework of a country should address the roles and responsibilities of policymakers, regulators, supervisors and institutions in relation to AML-CFT. The first step is to map the key stakeholders²¹ in the accountability matrix. This includes, among others:

²¹ Law Enforcement Agencies (LEAs) are not included in the list given that they are less relevant from a financial inclusion perspective.

- > **Policymaker and regulators:** Could include the central bank, insurance regulator, securities commission, and Ministry of Finance.
- > **Financial Intelligence Units²²**
- > **Supervisors:** Will include bank supervisor, insurance supervisor, and securities and exchange supervisor.
- > **Financial institutions, DNFBPs and VASPs:** Reporting or supervised entities such as banks, insurance, DNFBPs, and so on.

Consideration should be given to the separation of the policymaking process from regulatory responsibilities. An AML-CFT policymaker need not be a regulator and vice versa. This means that the respective stakeholders would be held accountable for AML-CFT outcomes relating to their specific roles and responsibilities. They are therefore addressed separately in the section below.

When drafting AML-CFT policy, jurisdictions should consider the roles and responsibilities of stakeholders. In broad terms, the following are worth considering:

- > **Policymakers:** They should be held accountable for ensuring risk-based AML-CFT policies are developed and maintained in a manner that results in risks being proportionately addressed and development promoted. The policymaking process should specifically consider that resources are available to regulators, supervisors and other stakeholders and how these should be focused on higher risks.
- > **Regulators:** They should be held accountable for ensuring that the AML-CFT obligations in place effectively address risks and do not result in unintended consequences that compromise financial integrity and overall development.
- > **Supervisors:** They would be held accountable for the risk-based supervision of AML-CFT obligations and compliance measures.
- > **Financial institutions, DNFBPs and VASPs:** They should be held accountable for compliance with AML-CFT obligations. This will entail consideration of the AML-CFT measures that are implemented and the effectiveness thereof in mitigating risk.

There should be an AML-CFT strategy that underpins an effective policy and accountability framework that advances inclusive financial integrity. The following mechanisms, which are important in the development of an accountability framework that promotes inclusive financial integrity, can be considered in this regard:

PUBLISHING REPORTS, PROGRESS UPDATES AND JOINT REVIEWS

AML-CFT authorities publish some of the outputs of NRAs. Where these reports are made available, stakeholders should use them to inform the development and application of AML-CFT measures. Further, the ME process also results in the production of a comprehensive evaluation report that is available to all stakeholders. Financial inclusion stakeholders should leverage the reports, progress updates, and joint processes resulting from NRAs and MEs to carefully inform the development of the NFIS, financial inclusion policies, and financial inclusion products of institutions. In order to ensure effective information sharing and collaboration towards that end, jurisdictions should build strong coordination structures and mechanisms so that inclusive financial integrity stakeholders can conduct joint reviews of the implementation of different strategies, policies, and so on.

LINKING IMPLEMENTATION AND EFFECTIVE COORDINATION

The implementation of certain aspects of an NFIS or AML-CFT regime can be linked to ensure inclusive financial integrity. For example, requiring that an NFIS strategy, or certain aspects of it, should not be finalized without the appraisal of risks for financial inclusion products and vice versa in the NRA process or during an ME. In addition, member countries may also require evaluations of FI products with involvement of AML-CFT authorities as well as periodic monitoring of processes by relevant stakeholders. Effective coordination within an AML-CFT regime is crucial and the authorities have a responsibility for developing an overall policy and accountability framework for cooperation and should require the role players to participate within the framework. Coordination can be viewed as a key performance indicator (KPI).

MONITORING

Continued monitoring of on-the-ground implementation of AML-CFT policy aids in identifying AML-CFT issues for timely policy intervention. For it to contribute to inclusive financial integrity outcomes, it should be done in close coordination with financial inclusion stakeholders.

²² Although these take different forms and have different powers in various countries, their main function is to receive and process financial intelligence to keep out money laundering and terrorist financing. Other FIUs may take the additional responsibility of supervising a specific sector e.g. DNFBP while others supervise several sectors.

4. ALIGNING FINANCIAL INCLUSION AND AML-CFT IN NRAs

The purpose of this chapter is to identify and describe considerations in aligning financial inclusion and AML-CFT in NRAs.

4.1. NRAs: A RECAP

The FATF requires that countries identify, assess and understand their ML-TF risks but is not prescriptive on the methodology for doing so. Countries may choose to address FATF Recommendation requirements through a single, country level risk assessment of both ML and TF, or through an approach that relies on sectoral risk and other assessments. However, an ideal way to proceed would be an NRA that is supported by sectoral risk assessments. An NRA provides an opportunity for financial inclusion issues to be considered and integrated in a holistic and strategic manner.

Indeed, an NRA is a process whereby ML-TF risks are identified, assessed and understood at the national level to inform the necessary AML-CFT measures to be taken. It should paint a holistic picture of the ML-TF profile of a country. Conducting an NRA is a multi-stakeholder endeavor, involving stakeholders from both the public and private sectors. The NRA process provides a basis for authorities to make informed and credible judgements regarding the ML-TF risks faced by countries. Additionally, the NRA process should assist in the prioritization, and thus efficient allocation, of resources by authorities when taking measures to mitigate ML-TF risks. It should also enhance the national coordination of stakeholders in addressing ML-TF risk faced (in light of FATF Recommendations 1 and 2).

The identification of assessment objectives in an NRA will inform the appropriate methodology to be employed by a jurisdiction. Figure 4 highlights the main steps involved in the NRA process. There are various methodologies available for countries when they conduct an NRA. AFI members largely use the World Bank tool and IMF methodology, but some develop their own methodologies based on FATF guidance. For example, AFI member countries such as Malaysia, South Africa²³ and Nigeria use the FATF guidance on national AML-CFT risk assessments as a template to develop their own country-specific NRA methodology.

Developed countries like the United States, New Zealand and the United Kingdom also develop their own NRA methodologies, which are anchored on the FATF NRA Guidance on National AML-CFT Risk Assessments (2013).

FIGURE 4: THE NRA PROCESS



Source: Based on Chapter 3 and others of FATF Guidance on National Money Laundering and Terrorist Financing Risk Assessment (2013) and case studies

Figure 4 is based on FATF guidance and provides an outline of the steps in an NRA process. While this will typically have a starting point and will conclude with the production of a report, much of it would be kept confidential but certain aspects can be shared with various national stakeholders. However, there is value in viewing an NRA as a continuous process with defined milestones. In addition to relevant institutions, data can also be collected from the public when conducting an NRA but this should be managed in line with the relevant data protection regulations. Further, it is advisable from an AML-CFT strategy-development perspective to consider the contribution of an NRA in relation to the other components of an AML-CFT regime, as illustrated in Figure 2.

23 The NRA for South Africa is underway at the time of writing.

4.2. COMMON CHALLENGES FACED BY AFI MEMBERS WHEN CONDUCTING NRAs

Irrespective of the methodology that has been used by countries in undertaking NRAs, common challenges have been highlighted by stakeholders from AFI member countries that participated in the survey and targeted interviews. Notably, data and information challenges appear to be the most significant when conducting an NRA. Figure 5 highlights common challenges that have been experienced.

UNAVAILABILITY AND POOR QUALITY OF DATA

Issues relating to historical data have been identified, i.e. where it is not readily available or not available at all and where the data that is not of the desired quality for determining an evidence-based and effective ML-TF risk rating for certain areas. Where data is available, it is often in a manual and unstandardized format, which makes it difficult to use. Data inconsistency issues, that were highlighted as a challenge during the study, often relate to stakeholders from one organization or institution providing different data relating to the same variable. There are indications of statistics that are not collected and updated on an ongoing basis.

While poor quality data is a problem broadly, it is even more so a problem for TF data as compared to ML data. Based on previous risk assessments, AFI member countries have typically found it challenging to obtain adequate TF data.

DATA CONFIDENTIALITY CONCERNS

AFI country members noted reluctance of some stakeholders to communicate certain information considered to be sensitive. Data confidentiality concerns extend to data on terrorism, partly as a result of the sensitivity of the data and compliance exposures relating thereto. This may also be attributed to challenges experienced in respect of tools used to identify and assess risks.

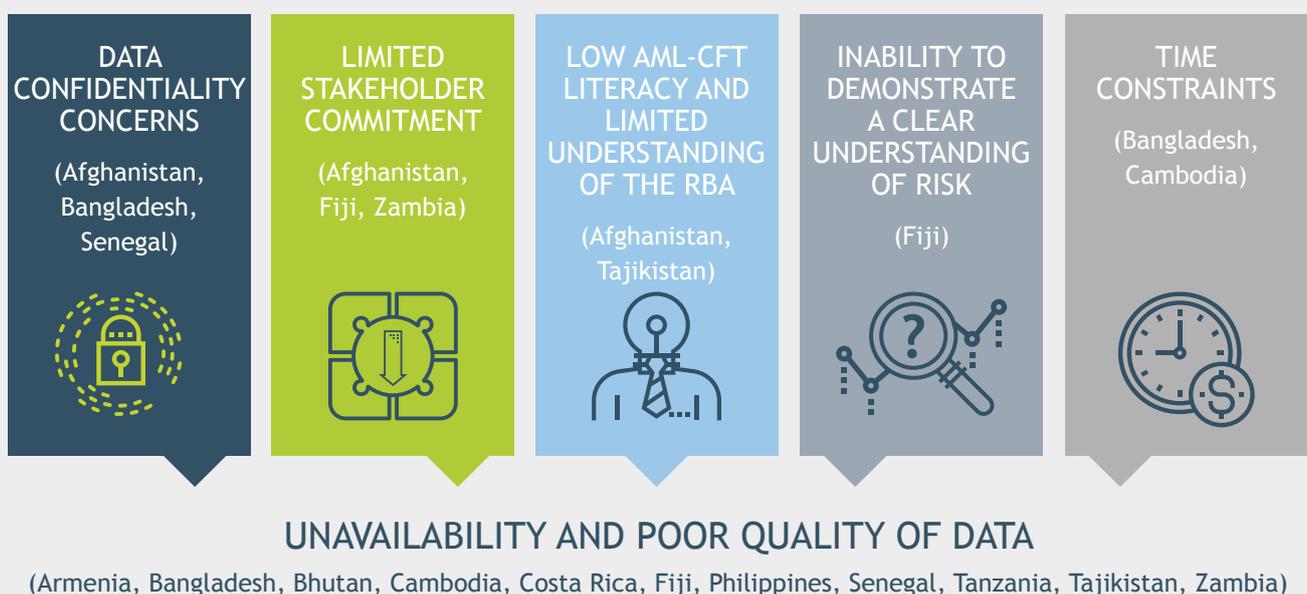
LIMITED STAKEHOLDER COMMITMENT

Challenges relating to stakeholder commitment to the NRA process were noted, for example, the absence of contributors at key meetings, ineffective participation and inability to share data and information in a timely manner. This refers to stakeholders from both the private sector as well as the public sector.

LOW AML-CFT LITERACY AND LIMITED UNDERSTANDING OF THE RBA

AML-CFT literacy challenges relate to limited knowledge and the inability of key stakeholders to understand the RBA and the NRA process itself. This issue arises despite the issuance of guidance on the application of the RBA by competent authorities. According to such guidance, “the effectiveness of an RBA depends on a common understanding by competent authorities and banks of what the RBA entails, how it should be applied and how ML-TF risks should be addressed”. However, in practice, effective communication is challenging and is

FIGURE 5: COMMON CHALLENGES FACED BY AFI MEMBERS WHEN CONDUCTING NRAs



Source: AFI survey and stakeholder interviews (2019)

dependent on a strong coordination structure. Capacity building and mechanisms to support the implementation and socialization of guidance play an important role.

INABILITY TO DEMONSTRATE A CLEAR UNDERSTANDING OF RISK

Differences in interpretation between local AML-CFT stakeholders and ME assessors is also a key challenge. This can arise due to various reasons including; low quality of NRAs, country’s lack of understanding of the ML-TF risk environment that they are exposed to, lack of clarity on mitigation measures adopted, unclear risk assessment methodology, among others). The differences in interpretation has also been noted in cases where some countries that have supported innovation relating to the concept of identity and imposed due diligence obligations (that in the view of the country are suitable), have experienced situations where ME assessors may not have the same interpretation and view of the trajectory of such developments and how they impact risk. In spite of the above, it remains important that countries can demonstrate to ME assessors that they understand their risks and have adequate measures to mitigate them in line with FATF Recommendations.

TIME CONSTRAINTS

Time constraint challenges relate to the inability to coordinate NRA processes within stipulated deadlines due to cascading challenges that delay subsequent steps, for example in respect of slow data collection processes that delay the analysis of the data.

CHALLENGES RELATING TO DNFBPs

While data and information challenges are experienced in all sectors, it is most pervasive in the DNFBPs sector. This limits the extent to which a jurisdiction understands its risks and, hence, the measures it puts in place to mitigate them. As such, this is at the core of opportunities to improve the effectiveness of AML-CFT regimes.

LIMITED SHARING OF NRA OUTCOMES

The sharing of the results of an NRA has been identified as a significant challenge. Most countries regard the NRA report/documentation as highly sensitive, and it is typically not shared with the private sector or limited information is shared. Other countries share only summary or sanitized versions of their NRAs, while in others very little information is shared.

POLITICAL WILL

Some politicians see an NRA as a “witch hunt” especially given the level of corruption in the public sector in many developing countries. This has

significantly delayed the commencement of NRAs in some jurisdictions and limited cooperation and sharing of information in others.

4.3. AFI MEMBER EXPERIENCES WITH DNFBPs IN AN NRA

Experiences of select AFI member countries in relation to DNFBPs are highlighted below:

TAJIKISTAN



- > The DNFBP sector was examined for ML-TF risks during the NRA.
- > The DNFBP sector was assessed within the framework of vulnerabilities of sectors developed by Tajik authorities in conjunction with Asian Development Bank experts.
- > The DNFBPs were engaged to provide a financial inclusion perspective for Tajikistan.

CAMBODIA



The main challenge with DNFBPs was a lack of available and adequate data, particularly in the accounting and auditing sector.

Source: Interviews (2019)

In view of the growing understanding of how to undertake an NRA, what methodology to use, and how best to use the tool to achieve required AML-CFT outcomes, it is recommended that consideration should be given to the establishment of an NRA forum and capacity development of that forum by regional experts. There is a growing NRA experience base from which to leverage insights to the advantage of AFI member countries, particularly in support of inclusive financial integrity objectives.

4.4. HOW DATA AND INFORMATION CHALLENGES CAN BE ADDRESSED

This section contains a description of how NRA-related challenges can be addressed.

Actions taken by AFI member countries are identified in the following table:

The following measures can additionally be considered to address data, information and other challenges:

- > Establish a coordination structure and mechanism for data collection and analysis, which can be part of an NRA working group or task force but that operates beyond the NRA so that data is regularly collected and

- analyzed to support the continuous risk-based and proportionate application of AML-CFT standards. It may be useful to identify who is going to lead the NRA working Group or Task Force beforehand for effective coordination.
- > Consider implementing a policy on standardizing the collection of data and digitization of data storage for adoption by all stakeholders.
 - > Identify data needs and gaps as early as possible and introduce systems to collect the required information, ideally several years before the completion of an NRA.
 - > Incentivize the participation of stakeholders by linking the NRA process to their respective sectoral and institutional priorities, which may also help in data and information sharing. Others have used different incentives, for example the Royal Monetary Authority of Bhutan issued certificates of participation to participants of Bhutan’s NRA.
- > Involve national data collectors and curators, such as the National Statistics Authority, to link the NRA process to data initiatives within the National Statistical System (NSS). This will avoid the duplication of efforts in data collection or expending unnecessary efforts to collect data that already exists. It will also enable the incorporation of NRA stakeholders within the NSS so that they routinely collect and share data on an ongoing basis, even beyond an NRA.
 - > Leverage national and regional protocols for data access and harmonization. Active involvement of key stakeholders in the NSS will make it easier for them to tap into statistical protocols agreed upon at regional and global levels. For example, in Africa there is the Strategy for the Harmonization of Statistics in Africa (SHaSA).
 - > CGAP’s I-SIP Toolkit (CGAP, 2018)²⁴ asserts that qualitative, or “soft” data is “better than no data

TABLE 1: ACTIONS THAT HAVE BEEN TAKEN BY AFI MEMBERS TO ADDRESS DATA AND INFORMATION CHALLENGES

ACTIONS TAKEN	JURISDICTION
<ul style="list-style-type: none"> > Creation of a coordination structure and mechanism such as a forum or inter-agency coordination body for data and information sharing among NRA stakeholders. > Ensure controlled access to databases and information. > Use of standardized data collection templates for survey information and quantitative data to address data availability and quality challenges. 	Costa Rica, Bangladesh, Nigeria, Tanzania, Zambia
<ul style="list-style-type: none"> > Submission of request for the Executive Department and Supreme Court to issue orders or circulars directing institutions to collect the relevant data. 	Philippines, Tanzania, Zambia
<ul style="list-style-type: none"> > Assignment of the FIU/FIC as the central repository for all NRA data and information to overcome confidentiality concerns. 	Tanzania, Zambia
<ul style="list-style-type: none"> > Use of cross-sectoral experts to avail and share data and information. 	Tajikistan
<ul style="list-style-type: none"> > Use of internal expertise/qualitative data where quantitative data is lacking or not collected. 	Tajikistan, Tanzania
<ul style="list-style-type: none"> > Collaboration with international and regional bodies to obtain assistance and support (e.g. Asian Development Bank). 	Bhutan
<ul style="list-style-type: none"> > Deployment of RegTech to integrate and consolidate data and information (e.g. Go-AML). 	Bhutan
<ul style="list-style-type: none"> > Use of surveys and other tools to obtain stakeholders’ high-level input (perception-based) especially where qualitative and quantitative data is unavailable 	Tanzania
<ul style="list-style-type: none"> > Establishment of supervisors’ forum to engage on NRA and inclusive financial integrity on an ongoing basis (beyond mutual evaluations). The forum has also provided a strong base for smooth information sharing on inclusive financial integrity and promoted collaboration and joint learning. 	Zimbabwe

Source: AFI Member Survey and interviews (2019); Cenfri (2018)

at all” and should be sought when quantitative data is absent. Such data can be gathered through consultations, focus group discussions and interviews.

- > Clearly communicate global AML-CFT standards and national AML-CFT policy to national stakeholders, particularly the policy frameworks that have been developed to support inclusive financial integrity and additionally do this to inform the formulation of measurable AML-CFT outcomes. This will, by design, encourage effective implementation of AML-CFT frameworks and processes that support inclusive financial integrity.

The application of an appropriate assessment methodology and the related tools, or combination thereof to use, depends on, among other things: the data and information that needs to be collected; the data and information culture of the country; the level of stakeholder engagement; and the strength of the coordination structure and mechanism already in place. It is important to remember that there is a trade-off between being comprehensive in stakeholder consultation and ensuring data consistency. The more stakeholders involved, the more different the forms and formats of data that need to be consolidated. Proportionality should be applied to the participatory nature of the data collection process.

4.5. OTHER CONSIDERATIONS IN ALIGNING FINANCIAL INCLUSION AND AML-CFT IN NRAs

WHAT DOES SUCCESS LOOK LIKE IN NRAs?

It is important that stakeholders, in both the public and private sectors, have a common vision of success for an NRA process. The key to success is identifying, assessing and understanding the ML-TF risk (FATF Recommendation 1) of a country through use of the appropriate methodology for the country’s context, which should be viewed in relation to required AML-CFT outcomes.

The focus of an NRA should be on the provision of AML-CFT-related assurance rather than the template used. This should lead to the development of action plans, national strategies and policies that aim to address and mitigate the identified risks. Determining the optimal frequency for conducting an NRA in line with changes in the ML-TF risk profile of the country, the international standards, political landscape, and the economic or legal framework of a jurisdiction is critical to achieving success and will vary from country to country. Successful NRAs additionally address the issues raised by stakeholders of the NRA process and the cycle of MEs. Some AFI member countries, such as

Bhutan, Mongolia and the Philippines, have reviewed and updated their AML-CFT legislation as an outcome of NRAs and MEs. NRAs are, therefore, very much a means to an end rather than an end in itself, and their findings should, accordingly, be used to enhance efforts to advance inclusive financial integrity objectives.

Other strategic considerations to ensure that an NRA contributes to inclusive financial integrity success include:

- > Encourage stakeholders to view an NRA as an ongoing process that feeds into the achievement of policy objectives. While a full scope NRA is generally seen as an event that is repeated periodically, there should be a mechanism to dynamically update AML-CFT perspectives as significant ML-TF issues evolve.
- > Govern NRAs in such a manner that they recognize the accountability and responsibilities of stakeholders, including policymakers, regulators, supervisors, other authorities and institutions.
- > Apply effective risk-based methodologies that address national and sectoral level ML-TF risks and understand these in relation to risk appetites and tolerances that are established.
- > Specifically consider factors and circumstances that have led to, or may lead to, de-risking and address these in the NRA process, particularly where de-risking has the potential to undermine inclusive financial integrity opportunities.
- > Establish a national risk appetite and tolerances to properly contextualise methodologies and address national and sectoral level ML-TF risks.

FINANCIAL INCLUSION CONSIDERATIONS IN AN NRA PROCESS

According to AFI member interviews (2019), the World Bank module on financial inclusion forms a basis for addressing products that promote financial inclusion and providing context for risk-based due diligence responses by institutions. However, the indications are that there is ground to cover in addressing the wider context of ML-TF risk in the formal and informal sectors.

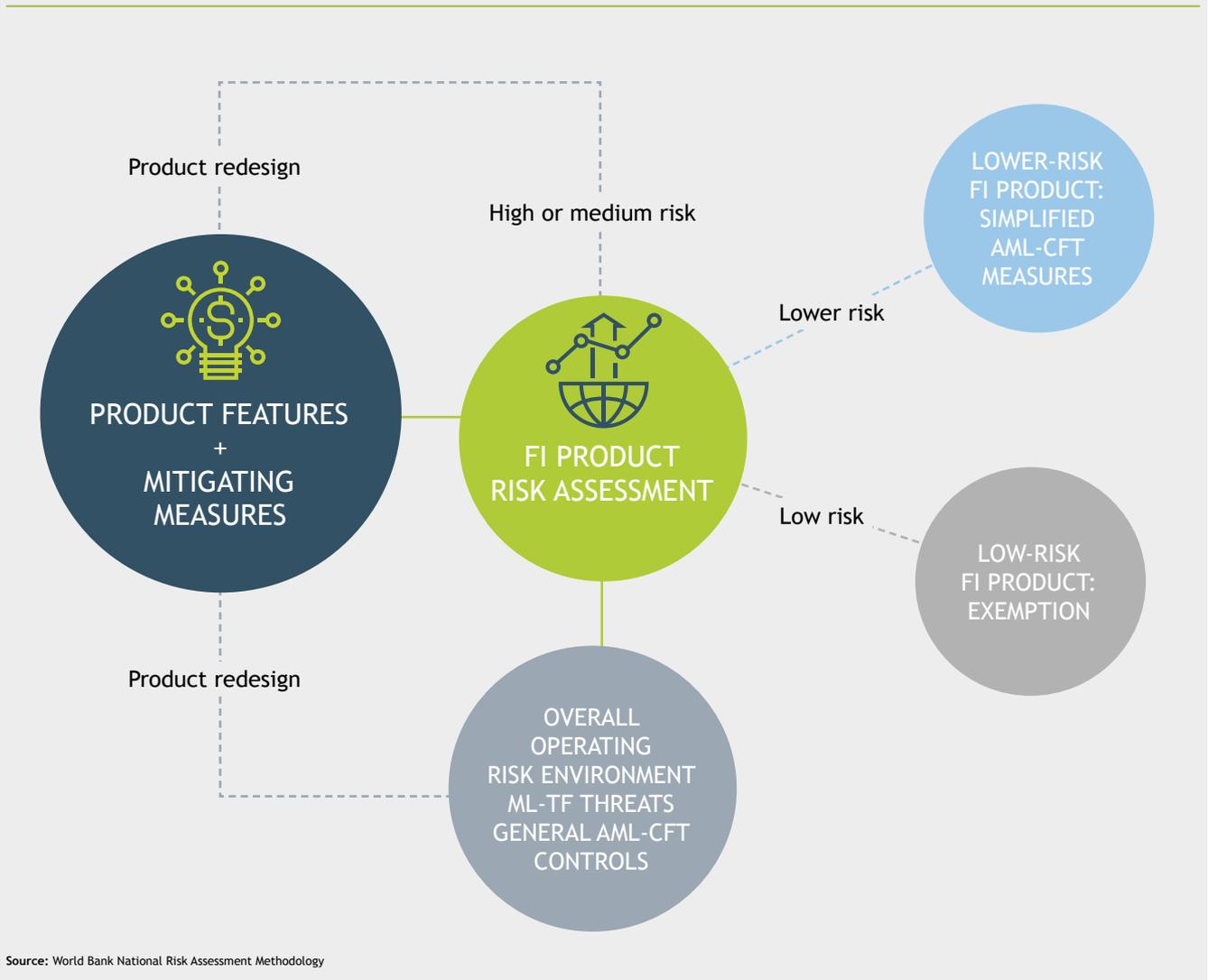
The incorporation of informal sector ML-TF risk considerations in an NRA is important in determining inclusive financial integrity outcomes. An example of a methodology to do this is found in Figure 6.

Figure 6 illustrates Module 9 of the World Bank methodology, which is the Financial Inclusion Product Assessment Module. This facilitates the evaluation of the risks in current, new, or emerging financial inclusion products. However, jurisdictions should go beyond these and adapt them to their specific country peculiarities relating to financial inclusion.

While the World Bank methodology has been widely used by AFI members, an increasing number are developing their own methodologies based on FATF

guidance as shown in Table 2. One of the strengths of the World Bank methodology is that it provides a focus on financial inclusion considerations. However, it does not address financial exclusion risks as experienced by a specific jurisdiction. It should also be pointed out that based on the AFI survey, the above methodologies seem to be viewed as ends in themselves as opposed to a means to an end. As previously highlighted, countries should be clear on what success looks like for financial integrity, financial inclusion and inclusive financial integrity. The various methodologies then are tools towards achieving these outcomes. Therefore, properly contextualizing a jurisdiction’s financial exclusion circumstances is paramount, irrespective of which methodology is used.

FIGURE 6: STRUCTURE OF FINANCIAL INCLUSION PRODUCT RISK ASSESSMENT, WORLD BANK MODULE 9



Source: World Bank National Risk Assessment Methodology

4.6. AFI MEMBERS' EXPERIENCE IN ALIGNING FINANCIAL INCLUSION AND AML-CFT IN NRAs

Select AFI members' experience in aligning financial inclusion and AML-CFT in NRAs is highlighted below:

 TANZANIA	<p>During the NRA, Tanzanian authorities had a phase where they identified all financial inclusion products and assessed their risks.</p>
 ZAMBIA	<p>Outcomes from NRA used to:</p> <ul style="list-style-type: none"> > Shape products and services > Develop strategies for NFIS > Develop a standard definition of a basic savings account
 ESWATINI	<ul style="list-style-type: none"> > Eswatini has strongly linked financial inclusion to the NRA process. > A significant success is the interoperability between MNO CDD and mobile- money CDD.

The above highlights how certain countries have linked financial inclusion considerations to the NRA process (AFI member interviews, 2019). The Tanzania example is largely in line with other countries that also use the World Bank tool, e.g. Zambia and Eswatini.

Discussions with AFI member-country stakeholders indicates that there should be explicit consideration of financial inclusion and financial exclusion risk in an NRA to align AML-CFT and financial inclusion initiatives (considering country circumstances and realities), i.e. beyond the approach that is provided for by existing methodologies.

“

The NRA process should assist in the prioritisation, and thus efficient allocation, of resources by authorities when taking measures to mitigate ML-TF risks.

”

TABLE 2: NRA METHODOLOGY USED BY CERTAIN AFI MEMBERS

COUNTRY	WORLD BANK METHODOLOGY	IMF METHODOLOGY	OWN METHODOLOGY BASED ON FATF GUIDANCE
Afghanistan	✓		
Armenia	✓		
Bhutan		✓	
Cambodia	✓		
El Salvador			✓
Fiji			✓
Paraguay			✓
Philippines	✓		
Tajikistan			✓
Tanzania	✓		
Nigeria			✓
South Africa ²⁵			✓

²⁵ South Africa is currently undertaking its sectoral and national level assessments. The indications are that the country is proceeding with its own approach based on the FATF methodology.

BOX 3: FINANCIAL INCLUSION CONSIDERATIONS IN AN NRA: THE CASE OF ZAMBIA



In Zambia, an NRA was used to determine the risks in respect of current and emerging financial inclusion products. The findings were leveraged to further shape these products with a view to developing risk-based, proportionate customer due diligence responses. Stakeholders engaged in financial inclusion products, such as banks, microfinance institutions, insurance companies, mobile service providers, postal services and securities firms, were consulted to inform the analysis. The findings of the assessment informed an understanding of risk relating to financial inclusion products and supported the achievement of favorable financial inclusion outcomes.

The results of the NRA in Zambia additionally informed and contributed to the development of the NFIS. For example, the results informed the definition and features of a basic savings account, which includes the following:

- > Low opening and minimum account balance
- > Maximum of two withdrawals per month
- > No monthly maintenance fees
- > No other fees

The outcome of the NRA process also assisted financial sector supervisory authorities to rationalize the allocation of AML-CFT supervisory resources for sectors with low ML-TF risk such as microfinance institutions, insurance companies and securities firms. Furthermore, the Bank of Zambia reviewed the Banking and Financial Institutions Act and included an explicit provision for financial inclusion. In Costa Rica, AML-CFT stakeholders started focusing attention on simplified CDD when opening entry-level accounts after an ME that was conducted. Further, the Banco Central de Costa Rica created a free app that enables users to transfer money from one account to another. Costa Rica recognises that usage should also be a measurement indicator of financial inclusion, rather than merely access to finance, and this has contributed to the expansion of financial inclusion in Costa Rica.

4.7. CHECKLIST OF KEY CONSIDERATIONS FOR INCORPORATING FINANCIAL INCLUSION IN AN NRA

DECIDE ON AN NRA METHODOLOGY AND RELATED TOOLS BASED ON COUNTRY SPECIFIC OBJECTIVES

Consideration should be given to methodologies and tools that embed financial inclusion into an NRA, for example the World Bank, IMF, or other methodology developed by countries. The methodology used should explicitly address financial inclusion policy objectives. Tools such as focus group discussions, surveys and expert opinions can be used to complement the NRA methodology.

FORM WORKING GROUPS AND COMMITTEES AND CONDUCT BRIEFINGS AND COORDINATION MEETINGS

A review and appraisal of existing structures may be undertaken in order to identify gaps and form missing structures accordingly. This should include national financial inclusion structures where they have not been established. It would be useful to form a financial-inclusion- or financial-exclusion-specific working group or committee. However, it is not just the formation of working groups or committees that matters, but how they are coordinated and work, as well as how they meaningfully contribute the necessary financial inclusion perspective of an NRA. Consideration could be given to ensuring that a specific number of people in the working group or committee also participate in at least one or two other working groups to enhance cohesion.

National Financial Inclusion Strategies (NFIS) and any other relevant background information on financial inclusion, where these are already in place, should be used prior to conducting an NRA.

COORDINATE DATA COLLECTION FROM RELEVANT STAKEHOLDERS

The data collection role of an FIU should be determined. One of the following models may be appropriate:

- > The FIU may have the capacity that is necessary to play a central data collection role in an NRA and could use this capacity to be the primary data collection agency;

OR

- > The FIU may be partially independent and could collect some data in an NRA and work with other stakeholders in this regard.

Alternatively, a more systemic solution may be considered, such as the use of the National Statistics System (NSS) capacity to collect and handle data in

an ongoing and dynamic process. The protocols and arrangements for data collection, data sharing and so on should already be laid out in the NSS. The NRA and ME are processes that can make use of the NSS. Unfortunately, in several countries, the NSS appears to lack the capacity to undertake such a role, for example where it is only functional during limited-use cases (for instances in a census) or is not functional at all.

UPSKILLING OF STAKEHOLDERS

It may be helpful to upskill the stakeholders involved in an NRA to ensure that they have adequate knowledge and understanding of risk management principles and AML-CFT systems. The financial inclusion working group or committee could be involved in the review of findings and the presentation of the proposed action plan, as well as the review of an NRA's findings and presentation of a proposed action plan.

5. AML-CFT CONSIDERATIONS IN A NATIONAL FINANCIAL INCLUSION STRATEGY (NFIS)

The purpose of this chapter is to briefly describe AML-CFT considerations in an NFIS and provide recommendations to align financial inclusion and financial integrity processes.

5.1. NFIS AND AML-CFT POLICIES

NFIS and national AML-CFT policies are, in many respects, complementary, which means an NRA (which establishes the basis of risks at country, sectoral, and institutional level to inform responses) can inform the formulation of an NFIS and vice versa. There are, however, challenges in leveraging opportunities in that NFIS and NRA processes are often led by separate actors and have different timetables.

The development of an NFIS generally takes place in four phases, namely: pre-formulation, formulation, implementation, and measurement. Considering these stages, an NRA may inform the formulation of an NFIS in the following ways²⁶:

Suggestions for aligning financial inclusion and integrity in the respective phases are given below:

PRE-FORMULATION PHASE

During this phase, and when determining the vision of the NFIS, it is important to consider various guidance. For example, FATF guidance on the RBA and financial inclusion, typology reports that are published by the FATF and FATF-Style Regional Bodies (FSRBs) where these are relevant to the country, previous NRAs, among others. The involvement and specific roles of key AML-CFT-competent authorities should be clearly specified, for example, in a terms of reference (TOR) for all members of a coordination structure formed for the NFIS formulation. The key AML-CFT-competent authorities' role could include informing the diagnostic studies for the NFIS, providing NRA context to the NFIS process, contributing to the drafting of the concept note from an NRA perspective, helping to align financial inclusion with financial integrity policy objectives and so on. Importantly, the AML-CFT authorities can provide

FIGURE 7: WAYS IN WHICH AN NRA MAY INFORM THE FORMULATION OF AN NFIS

PRE-FORMULATION PHASE

- Consider updated FATF guidance on financial inclusion
- Consider previous National Risk Assessment outcomes as they relate to financial inclusion
- Determine appropriate coordination structures and mechanism and the role of the AML-CFT stakeholders (e.g. FIU, other NRA related structures) within it
- Include and define the role of the FIU and other stakeholders and emphasise their importance in the formulation of the NFIS



FORMULATION PHASE

- Include an assessment of the interaction of ML-TF risk with financial inclusion in the diagnostic studies (previous NRA results can be used)

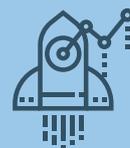


IMPLEMENTATION AND MEASUREMENT PHASE

AML-CFT stakeholder may be:

- Included in the NFIS implementation structure
- Consulted on the draft of the NFIS - can share feedback of their experience with FI products in terms of risk assessments
- Charged with aligning vision of success for financial inclusion with AML-CFT
- Assist in developing measurement indicators for monitoring and evaluation

Input, process and outcome measures for NFIS to be aligned with measures for NRA



Source: AFI Guideline Note 20

26 Alliance for Financial Inclusion. 2016. National Financial Inclusion Strategies: A Toolkit. Available at: https://www.afi-global.org/sites/default/files/publications/2017-07/FIS_GN_28_AW_digital.pdf

guidance on aligning the timelines of the NFIS process with those of the AML-CFT national policies, NRA and ME processes, and how each can properly feed into the other.

FORMULATION PHASE

During the conduct of a country's diagnostic studies, an in-depth assessment of the country's financial inclusion landscape could include an assessment of the interaction of ML-TF risks with financial inclusion. The FIU should be available to provide important data and information on the current AML-CFT landscape and the country's ML-TF risks. Reference to relevant NRAs as well as Mutual Evaluation Reports (MERs) is important. The AML-CFT authorities should be consulted throughout the formulation of the NFIS.

IMPLEMENTATION PHASE

The coordination structure for the implementation of an NFIS may be different from the one activated for its formulation. The AML-CFT authorities should be included in the stakeholder list for the implementation coordination structure, if not the structure itself (such as the steering committee or a working group). The competent authorities can share feedback from their experience with financial inclusion products within the context of risk assessments and support processes to ensure that these are considered during the implementation of the NFIS. It will also enable the authorities, particularly the FIU to inform and increase the understanding of relevant stakeholders of the country's current and future financial inclusion plans as well as products. Moreover, consistent effort to align the vision of success for financial inclusion with that of financial integrity can be maintained. This will articulate favorably with the process of measuring the success of financial inclusion in countries.

MEASUREMENT PHASE

There needs to be a sound Monitoring and Evaluation (M&E) framework in place to guide the assessment of the NFIS and the extent to which it is succeeding. A good M&E framework should track progress and provide real-time feedback. As noted in section 2, the measurement indicators should be set up in relation to the specific goals of the financial inclusion definition and aligned to outcomes of NRAs where these have been conducted. The M&E framework can then also be used to make changes to the formulation and implementation of the NFIS on an ongoing basis.

“

NFIS and national AML-CFT policies are, in many respects, complementary, which means an NRA can inform the formulation of an NFIS and vice versa.

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5.2. ALIGNING AML-CFT MEASURES AND FINANCIAL INCLUSION PROCESSES OVER THE NRA AND NFIS LIFECYCLES

Aligning the NFIS and NRA processes where neither are in place yet, is an opportunity to ensure that they feed into each other from the onset. However, where both are in place but not aligned or with limited alignment there may be a need to coordinate and align mid-term reviews and follow-up processes. It is important that both the NFIS and the NRAs have periodic review phases to update their risk assessments, monitor progress and address unintended, negative consequences.

In the case where an NFIS has already been formulated, the mid-term or end-term review of the NFIS can be synchronized with the NRA process. For instance, this can be done by considering the results of a recent NRA in the review. If the NFIS is adjusted based on the mid-term review, the NRA findings would then be well considered.

Irrespective of the sequence, that is whether an NFIS is in place before comprehensive an NRA or vice versa it is important to revisit, re-establish, and reach consensus on the shared vision of success for inclusive financial integrity. Where there is considerable fit and alignment between AML-CFT and financial inclusion processes, the structures that oversee financial inclusion could be similar to the structures that oversee NRAs (e.g. Zambia). In this way, the product, jurisdiction, and delivery channel lens can be used to favorably rate products with financial inclusion and sustainable development implications and hence promote alignment between financial inclusion and financial integrity. Simplified Due Diligence (SDD) measures can also be conducted on such products and where risk can be demonstrated to be lower.

6. REGULATORY FRAMEWORKS FOR INCLUSIVE FINANCIAL INTEGRITY

The purpose of this chapter is to highlight key regulatory framework challenges, describe features of regulatory frameworks that support inclusive financial integrity, and identify RegTech opportunities to strengthen regulatory compliance.

6.1. REGULATORY FRAMEWORK CHALLENGES

Regulatory frameworks play a crucial role in creating the alignment between financial inclusion and financial integrity. Laws, regulations, and guidance relating thereto will impose obligations that stakeholders must comply with and can be framed to support inclusive financial integrity outcomes. Despite FATF recommendations and related financial inclusion guidance providing sufficient flexibility to countries, policy and regulatory challenges continue for developing economies. Often, this is a result of limited proper or appropriate customization to the local context. This has, in turn, negatively affected the application of the RBA, which is critical to enhancing inclusive financial integrity.

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Regulatory frameworks play a crucial role in creating the alignment between financial inclusion and financial integrity.

”

6.2. FEATURES OF REGULATORY FRAMEWORKS THAT COULD SUPPORT INCLUSIVE FINANCIAL INTEGRITY

A regulatory framework that promotes the alignment between financial inclusion and financial integrity should, among other things:

- > Be aligned with the country AML-CFT strategy
- > Rely on the real value of risk assessments for its formulation so as to best achieve AML-CFT objectives

- > Implement risk-based application of AML-CFT standards appropriately so as to enhance financial inclusion as well as financial integrity.
- > Be informed by financial inclusion policy, meaning the AML-CFT regulatory framework should be informed by a country's NFIS by including the agency responsible for financial inclusion in the drafting, implementation and review of the AML-CFT regulatory frameworks
- > Ensure that financial inclusion initiatives are implementable to the extent that is optimal
- > Have established and monitored success factors against which stakeholders can be held accountable
- > Recognize the potential for technological innovations in addressing barriers to financial inclusion and exclusion impediments such as identity proof of address, distance from access points, financial illiteracy, socio-cultural norms, and so on.

Regulatory frameworks should allow for tackling challenges experienced in conducting risk assessments and should create an environment where NRAs are an ongoing national endeavor and not just an event (that is conducted prior to an ME). AML-CFT authorities may conduct a periodic review of AML-CFT-related policies, legislation, regulations and supervisory requirements after conducting risk assessments. NRAs that are conducted in a manner that specifically addresses financial inclusion considerations may be a valuable tool that can indicate whether there is a need for regulatory framework changes. This can help jurisdictions foster an environment that effectively aligns financial inclusion and AML-CFT. In addition, the impact of AML-CFT regulatory requirements and supervision should be monitored at a national level, and there should be ongoing consideration of the gaps in existing regulatory or supervisory obligations. Additionally, ongoing review of AML-CFT stakeholder mandates and accountability frameworks to identify gaps and collaboration opportunities will enhance inter-agency collaboration and inclusive integrity.

Key features of select AFI member country case studies relating to enabling regulatory frameworks are highlighted in Box 4.

Regulatory frameworks that support the alignment between financial inclusion and financial integrity should be based on a sound understanding of the ML-TF risks in jurisdictions. This understanding can be supported on an ongoing basis through technical assistance programmes.

BOX 4: AFI MEMBER REGULATORY FRAMEWORKS FOR INCLUSIVE FINANCIAL INTEGRITY

BANGLADESH

In Bangladesh, the ME outcomes resulted in the formulation of the Mobile Financial Services Guidelines (2018). These guidelines show how Bangladesh's regulatory environment is enabling the provision of an orderly and competitive environment that is extending the reach of financial services. Furthermore, the Risk-Based AML-CFT Supervision Manual will be in action soon, which will allow for clear risk-based supervision that will guide the implementation of the RBA in Bangladesh.

SOUTH AFRICA

South Africa's ME is currently ongoing, however the recent implementation of principles-driven regulations in the country's AML-CFT framework are likely to have a positive impact on inclusive financial integrity. The new regulatory guidance encourages institutions and stakeholders to move away from placing the focus of their measures on inputs (hardcoded set of documents required for due diligence purposes) to focus more on outcomes (particularly in the achievement of AML-CFT objectives). This has relegated the importance of proof of address as a key identifier. Such initiatives are expected to decrease the barriers to financial inclusion, while also maintaining financial integrity.

COSTA RICA

In Costa Rica, AML-CFT stakeholders started focusing attention on simplified CDD when opening entry-level accounts after an ME that was conducted. Further, the Banco Central de Costa Rica created a free app that enables users to transfer money from one account to another. Costa Rica recognizes that usage should also be a measurement indicator of financial inclusion, rather than merely access to finance, and this has contributed to the expansion of financial inclusion in Costa Rica.

Source: AFI Member Survey (2019) and stakeholder interviews (2019)

6.3. REGTECH AS A REGULATORY COMPLIANCE TOOL

The broader use of digital channels and Financial Technology (FinTech) has allowed unprecedented growth and innovation in financial services and business models. However, technologically-enabled innovation does not only offer opportunities for FSPs, but also for financial authorities who are developing capabilities to research and explore the potential of new technologies towards improving methods and processes.

Jurisdictions may consider using Regulatory Technology (RegTech) as a regulatory compliance tool towards enhancing inclusive financial integrity outcomes. RegTech is essentially any technology (which can include artificial intelligence, machine learning, data science, but also more simple technology such as databases) that is used to enhance regulatory compliance and support regulatory objectives. In the beginning, it was leveraged by financial institutions to increase efficiency and effectiveness in regulatory compliance, but more recently financial authorities have also begun to leverage RegTech. Supervisory Technology (SupTech) is a subset of RegTech that is used to specifically to support supervisory objectives. It is explored in more detail in Box 5.

In this context, RegTech can be used to streamline data collection by requiring institutions whose data is relevant for risk assessment or other AML-CFT purposes to use RegTech as a means of meeting data submission requirements. This will reduce time-constraint challenges as RegTech can handle both structured and unstructured data as well as vast amounts of data, which is normally handled in multi-stakeholder endeavors such as NRAs and MEs.

Furthermore, RegTech may enable more collaboration and two-way dialogue between regulators, supervisors, and financial institutions. RegTech can also present an opportunity for data handling and data presentation to become standardized domestically, regionally, and internationally. This can greatly reduce the cost of conducting ongoing due diligence as well as onboarding, and consequently raise the business case of those who are currently financially excluded due to the high cost of onboarding them, which outweigh the benefits. It also enables regulators to collect disaggregated data and enable them to better monitor the impact of policies and regulations for specific groups including women, MSMEs, youths, and so on.

It is important to remember that technology and data is a "double-edged sword," which raises data policy, protection, regulation, and supervision challenges.

There should be a sound framework for compliance with privacy and data protection obligations, which should be effectively coordinated by competent authorities. Jurisdictions can also consider non-binding international standards and industry codes of conduct that have been developed to promote innovation while managing risks to both the financial system and consumers such as the 2016 G20 High Level Principles for Digital Financial Inclusion. There are additionally industry self-governing mechanisms, such as the GSMA Mobile Money Certification and the International Finance Corporation's (IFC) Responsible Investing in DFS Guidelines, among others.

Below are examples of RegTech applications in the context of AML-CFT:

- > **Artificial intelligence transaction monitoring:** RegTech solutions for real-time transaction monitoring and auditing
- > **Regulatory reporting:** A solution for processing data and distributing regulatory reports to relevant regulatory bodies
- > **Identity management and control:** RegTech for payment efficiency, compliant transactions, bank counterparty insight and AML screening
- > **Compliance:** RegTech that captures and monitors regulatory data so it can be read by machines and understood by humans
- > **Risk management:** Risk analytics that detect disruptive events in global financial markets and anticipate price movements.

BOX 5: SUPTECH APPLICATION BY THE COMISIÓN NACIONAL BANCARIA Y DE VALORES IN MEXICO

A subset of RegTech, Supervisory Technology (SupTech) is defined by the Financial Stability Institute (FSI) of the Bank for International Settlements (BIS) as the use of technology to specifically support supervisory activities. Regulators and supervisors in several countries are exploring the use of SupTech in its main areas of application, which can be argued to be data collection and data analytics for effective supervision. In July 2019 CNBV started the development of a SupTech platform that will allow the reception, storage, validation, and automated processing of information. The platform consists of the following: i) information exchange through Application Programming Interfaces (API) for financial technology institutions (FTI); ii) receipt and processing of large volumes of information for AML-CFT in a first phase and in a second phase, for general reporting by all sectors; and c) provision of analytical dashboards.

In October 2019, CNBV developed the project "Adoption and Implementation of Advanced Data Analytics for SupTech at CNBV" which is supported by the Inter-American Development Bank (IDB). The project is focused on the adoption and implementation of advanced data analytics at the CNBV. More specifically, the application of big data and Artificial Intelligence (AI) for predicting and classifying regulated financial entities and for the proactive monitoring of risk and compliance, in particular among Popular Financial Societies (SOFIPO) and FTIs. This has allowed CNBV to move from descriptive analytics (retrospective understanding), to advanced analytics (prediction and optimal use of data).

There are practical lessons that can be learned from CNBV's experience:

- > Identify organizational capabilities that need to be developed and enhanced.
- > Promote a culture of innovation and assign key leadership roles to foster organizational change and overcome cultural barriers.
- > Collaborate with other financial authorities, share knowledge, findings, and best practices.
- > Look for specialized support and select highly capable multidisciplinary groups that can demonstrate a strong vision for transformation.
- > Create innovation labs.
- > Develop and improve technical capabilities within the institution such as in the areas of data science, programming, data engineering, and identify robust technical staff with relevant (numerical and statistical) backgrounds.
- > Take a gradual approach to adopting and applying SupTech including related infrastructure, in accordance with supervisory needs and advances.
- > Recognize the role and knowledge of supervisory experts, as SupTech will not replace the strong analytical skills of supervisors.

7. ALIGNING FINANCIAL INCLUSION AND AML-CFT IN ONGOING PROCESSES: PROPORTIONATE AML-CFT RESPONSES

The purpose of this chapter is to identify key challenges in aligning financial inclusion and AML-CFT in ongoing processes and to discuss how AFI member countries are addressing these to promote inclusive financial integrity, as well as to discuss gender and forcibly displaced persons considerations in this regard.

7.1. FATF CONTEXT

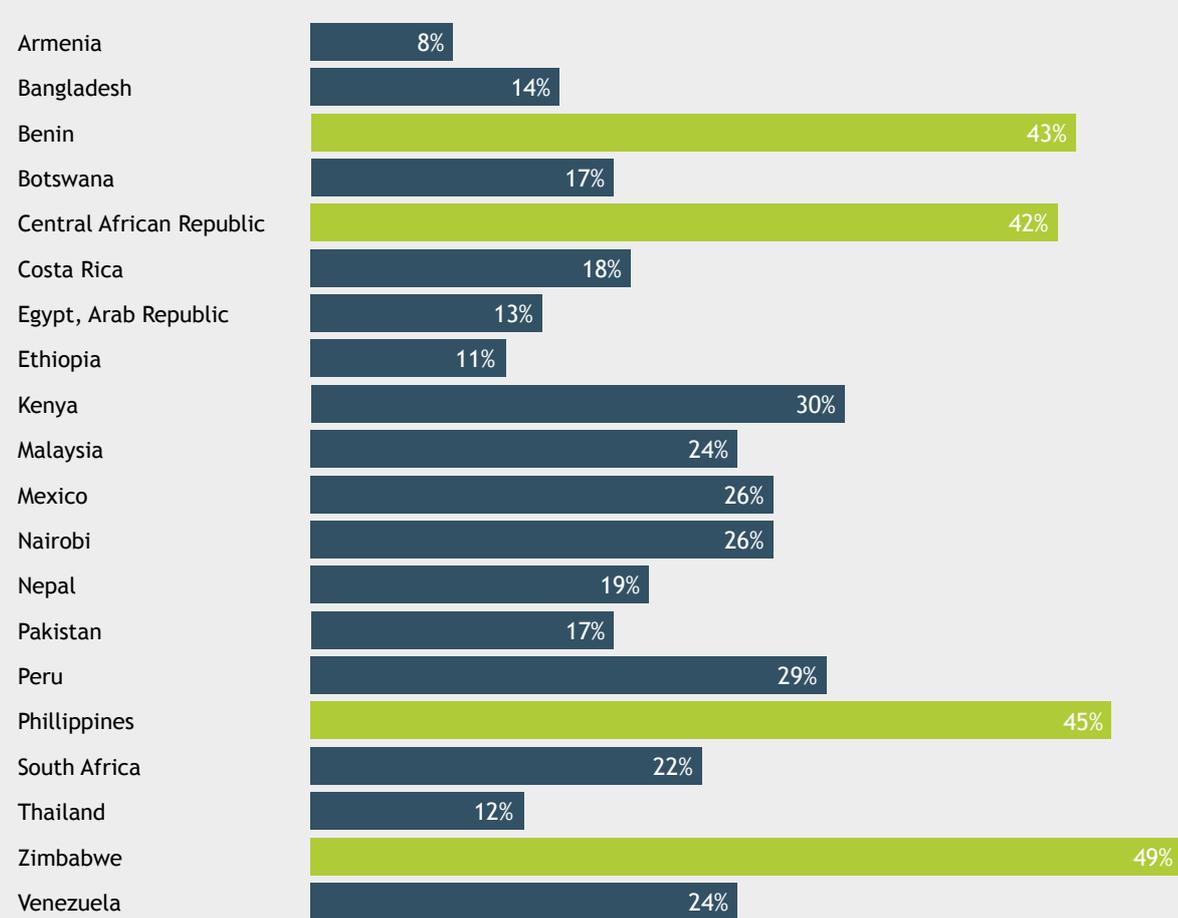
In achieving the alignment between financial inclusion and AML-CFT outcomes, it is important to focus on the FATF Recommendations, particularly in respect of due diligence requirements specified in Recommendation 10 and record-keeping requirements specified in Recommendation 11.

7.2. CHALLENGES IN ALIGNING FINANCIAL INCLUSION AND AML-CFT IN ONGOING PROCESSES

PROOF OF IDENTITY

Many individuals in developing countries lack proof of identity. This means that institutions struggle to adequately identify and verify them, and are often forced to turn them away. Figure 8 shows the percentage of financially excluded adults whose main reason for exclusion is lack of documentation.

FIGURE 8: PERCENTAGE OF EXCLUDED ADULTS WHO ARE FINANCIALLY EXCLUDED DUE TO LACK OF DOCUMENTATION



Source: World Bank Findex (2018)

DATA COLLECTION AND STORAGE COSTS

The cost of maintaining transactions records and CDD records for five years is high, especially where it involves storage of photocopied paper documents. It is also expensive to implement rigorous transaction-monitoring systems and to establish suspicion-reporting processes. In addition, the penalties for non-compliance with AML-CFT requirements have been shown to be high and unpredictable, incentivizing conservative approaches (AFI, 2011; Cenfri, 2011).

CHALLENGES IN IMPLEMENTING AN RBA

Even though the FATF requires the adoption of an RBA, jurisdictions have been slow to adopt this in national legislation and are not necessarily using a flexible or principles-based framework that fully supports risk-based, proportionate compliance responses. One of the challenges that member jurisdictions have cited is a limited capacity to undertake an NRA towards adopting an RBA. This means institutions find it challenging to implement innovative solutions, particularly where the regulatory obligations are framed in a rules format. Institutions are often incentivized to adopt conservative approaches to CDD that are safely within regulatory requirements and adopt conservative compliance measures, which may include applying identification and verification measures that are not commensurate to the risk.

The above challenges make it difficult for jurisdictions to achieve an alignment between financial inclusion and financial integrity. However, several AFI members have made progress in overcoming these issues as noted below.

7.3. HOW AFI MEMBERS ARE ADDRESSING THESE CHALLENGES TO PROMOTE INCLUSIVE FINANCIAL INTEGRITY

USE OF TECHNOLOGY FOR RISK-BASED, PROPORTIONATE CDD

(a) Biometrics and GPS

In the FATF Guidance for Digital ID, FATF defines digital ID systems as “systems that cover the process of identity proofing/enrollment and authentication. Identity proofing and enrollment can be either digital or physical (documentary), or a combination, but binding, credentialing, authentication, and portability/federation must be digital” (FATF, 2020). E-KYC is the electronic means to conduct the customer identification process, and it allows the digital or online verification of customer identity (FATF, 2017).

Some member countries are using biometrics in CDD onboarding processes. Biometrics, in combination with other attributes, can remove the need for customers to carry paper-based documentation and provide them with an alternative way to prove their identity. Biometrics are robust identifiers and have the potential to significantly reduce onboarding and record-storage costs by automating processes (Cooper et al., 2018).²⁷ Jurisdictions such as Nigeria, South Africa, Bangladesh, India and others have implemented biometrics into their national or sectoral identity systems, and these have enabled proportional approaches to onboarding.

BOX 6: THE BANK VERIFICATION NUMBER (BVN) IN NIGERIA HAS ENHANCED INCLUSIVE FINANCIAL INTEGRITY

On 14 February 2014, Central Bank of Nigeria along with its committee, launched the BVN Project, a biometric system. This project aimed to mitigate the risk of identity theft in Nigeria, which was quite prevalent as the traditional security system made use of passwords and PINs that could be stolen (Nwadinobi and Peart, 2018). The registration process requires that customers have their facial image and 10 fingerprints scanned and captured into a database (Olijo, 2018:29). After inputting the biometrics into the database, a unique BVN is generated for the client (Izogo, Jayawardhena and Kalu, 2018).

The BVN system provides a unique identity to customers that is verifiable across the Nigerian banking industry. To spur adoption, the central bank, through regulation, put in place enrollment targets for banks to achieve in a specified timeframe. This was important for ensuring industry-wide adoption. By 2017, there were 31 million registered BVNs and 44 million registered financial accounts linked to a BVN (Central Bank of Nigeria, 2018). According to Central Bank of Nigeria (2018), the BVN has had several benefits including reduced fraud by removing the ability to create multiple financial accounts under different identities as well as using BVN to fast-track the investigation of criminal cases involving transfer of funds or payments into accounts belonging to suspected criminals.

²⁷ Biometrics reduce costs by removing the need to store documents and reducing time taken to onboard.

For example, Nigeria has developed its own financial sector biometric identity. See Box 6 for more information on the Bank Verification Number (BVN) initiative.

In addition to providing innovative solutions to onboarding, biometrics can also make monitoring and ongoing due diligence easier and more accurate. For example, some banks in Brazil use a combination of biometric, behavioral and location data to securely, and with consent, monitor their customers' transactions and behavior to produce accurate risk profiles (AFI, 2019). GPS data is used to consensually track the location and nature of transactions made by customers. Moreover, fingerprints and facial biometrics are used to confirm the identity of the person making transactions.

The technique allows banks to have greater assurance of the identity of customers and to enable fraud detection. It also allows customers to develop detailed digital identities with additional aspects such as credit scores that assist them in obtaining other financial services. In implementing biometrics, countries should ensure that the privacy of individuals is protected adequately and that legal frameworks are in place to ensure that the personal information of individuals is not abused. Towards that end, there should be sufficient regulatory and implementation coordination with the national Data Protection Authority (DPA) as well as the national Identification Authority to coordinate the legal recognition of new, technology-based digital ID solutions providers.

(b Electronic storage of data references

A study undertaken by AFI (2019) on KYC innovations highlights that future developments in the way data is stored, owned and managed, and can significantly shape the CDD environment. According to FATF Recommendation 11, "Financial institutions should be required to maintain, for at least five years, all necessary records on transactions, both domestic and international, to enable them to comply swiftly with information requests from the competent authorities. In addition, the CDD information and the transaction records should be available to domestic competent authorities upon appropriate authority" (FATF recommendations, 2019). However, the FATF (2017) Guidance on AML and TF Measures and Financial Inclusion, with a supplement on CDD, notes that institutions could comply with this by simply "keeping electronic copies of the results of any electronic verification checks" (FATF, 2017).

BOX 7: DATA TOKENIZATION AND PROPORTIONALITY CAN POSITIVELY IMPACT INCLUSIVE FINANCIAL INTEGRITY

Tokenized data is an encrypted reference to data that can be used to unlock data held elsewhere but does not represent the data itself. Using complex algorithms, tokens store the history of the usage of the identity data. This provides a clear provenance of data by showing what the data has been used for and by whom. Having a clear audit trail assists in detecting unscrupulous use of the data and gives institutions a much clearer picture of the CDD risk of a potential client. Tokenized data allows for proportionality by reducing the cost of storage and enhancing the identity profile of the consumer.

This means that institutions do not need to store digital or physical copies of identity documents but could instead store the results of electronic verifications. These could, for example, have been obtained through matching a biometric to a digital-identity profile in a manner that uniquely and exclusively identifies customers. This is cheaper, more efficient and reduces the risk that is associated with storing personal identity data. A new technology, known as data tokenization, can further improve the robustness of these verification checks. Box 7 contains a description of the concept of data tokenization.

(c) RegTech, automated STR software and artificial intelligence (AI)

In addition to digitizing data storage, implementing digital technologies can reduce the cost and improve the effectiveness of suspicious transaction reporting. This is important for creating an aligned approach to AML-CFT. Many FIUs within AFI member countries have implemented real-time AML monitoring hardware and software systems such as goAML to automatically detect money laundering and illicit financial flow alerts.²⁸ When implemented with artificial intelligence these systems establish trends and correlations which further help with proactively detecting and monitoring ML. For example, systems that can map politically exposed persons (PEPs) to their networks and network of networks for ML purposes are already available.

²⁸ goAML is a software solution that enables real-time reporting; effective analysis of STRs, CTRs and complaints; and communication between the FIU, regulated entities, and other stakeholders.

SIMPLIFIED DUE DILIGENCE AND REGULATORY FLEXIBILITY

Apart from technological innovations, several AFI members employ regulatory interventions or simplified due diligence to promote risk-based CDD. The FATF suggests applying simplified due diligence where there is confirmed lower risk. They give the following example of lower risk in the guidance paper on AML-CFT and financial inclusion (2017):

“

...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.

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The FATF notes in its financial inclusion guidance (2017) that the flexibility granted by the RBA, particularly in applying proportional requirements for confirmed lower-risk clients, is important for financial inclusion purposes. However, it should be noted that the guidance requires a holistic approach to be taken so that proportional requirements takes into account not just the risk profile of the customer, but also the risk of the financial inclusion product or service. Additionally, “proportional” could mean applying alternative, rather than less strict identifiers for CDD. Many AFI member countries have taken advantage of this. For example, in Palestine there is no specific requirement for proof of address because it is not a requirement under FATF (AFI, 2019). In South Africa, the new approach to AML-CFT, as reflected in Guidance Note 7, does not, in a rules format, state which identifiers institutions should use for CDD purposes. They use the findings from their risk assessment to decide on the appropriate level and type of CDD that they will apply to a customer. The significance of this development is that it moves away from stating the documents needed for CDD (e.g. proof of address which is a weak and high-risk identifier), to focusing on the required outcome of CDD which ML-TF risk mitigation is. This gives institutions the opportunity to use more proportionate measures to identify customers in line with risk. For example, they may choose not to require proof of address for a lower-risk client who typically does not own this document, thus reducing CDD costs while advancing financial inclusion.

Sometimes a lack of clear direction or guidance relating to AML-CFT obligations can cause institutions to act conservatively and hinder aligned approaches. In such cases, guidance can be provided to support an RBA. This has been done by various AFI members, specifically where a one-off transaction is confirmed as lower-risk and thus simpler or lower CDD measures can be applied in that instance. For example, in Russia, consumers who want to conclude a one-off transaction valued at no more than USD250 could have simplified due diligence applied (using their passport as opposed to their passport and proof of address). This is important for financial inclusion as it provides an option for those individuals wanting to make one-off payments with relative ease (AFI, 2019). Countries such as Russia, Zambia, Nigeria and many others have also included tiered CDD as part of their CDD requirements to help guide institutions in applying a proportional approach. In a tiered CDD approach, institutions apply specific CDD measures for each tier, as allowed in the AML-CFT regime. In Nigeria, tier 1 is the lowest-risk tier and, therefore, allows for the lowest level of CDD, with tier 2 and 3 requiring higher levels. Box 7 provides an overview of Nigeria’s tiered CDD framework.

BOX 8: TIERED CDD IN NIGERIA HAS ENHANCED INCLUSIVE FINANCIAL INTEGRITY



Tier 1 accounts are described as low-value accounts. They have a maximum balance of USD831 and a transaction limit of USD8.27. Customers may provide an ID photo, name, place of birth, date of birth, gender, indication of where they live and telephone number. These details do not need to be verified.

Tier 2 accounts are described as medium-value accounts. They have a maximum balance of USD1,385 and a transaction limit of USD28. They are subject to the same identity requirements as tier 1 with the addition of their BVN. The customer information must additionally be verified against a database.

Tier 3 accounts are described as high-value accounts. They have no maximum balance limit and there is a transaction limit of USD276 for banking products. Full CDD requirements will be applicable as specified in the AML-CFT regime.

Source: Hougaard et al. (2018)

BOX 9: KINGDOM OF ESWATINI'S MNOs AND MOBILE MONEY INTEROPERABLE SYSTEM ENHANCES CDD EFFICIENCY



In October 2014, the FATF released RBA guidance for the banking sector. Based on this guidance, Eswatini is currently implementing an RBA and aims to have a proportionate approach to AML-CFT. The Kingdom of Eswatini's main AML-CFT regulation consists of the Money Laundering and Financing of Terrorism Act (2011) and the Suppression of Terrorism Act (2008). Accountable institutions are required to ascertain the identity of customers or beneficial owners before entering a business relationship.

The Kingdom of Eswatini has not formally defined "identity", but the financial systems adopts the identity card with a personal identification number as the primary means of identification. A significant success in the Kingdom is the interoperability between MNO CDD and mobile-money CDD. This has allowed for an efficient CDD process for SIM and mobile-money registrations. Additionally, individuals can verify other individuals that live with them in shared households. An affidavit can be signed by the owner of the title deed or utility bill, stating that the applicant lives in the same household. This is acceptable for CDD purposes and helps reduce exclusion and the inherent risk associated with a lack of documentation in AML-CFT processes.

Source: AFI member country interviews, 2019

7.4. GENDER CONSIDERATIONS IN ALIGNING FINANCIAL INCLUSION AND AML-CFT

Policies, regulations and laws are not gender²⁹ neutral,³⁰ and policy frameworks that implement global standards for AML-CFT are no exception. In-country implementation of the standards may have unintended consequences for both women and men due to prevailing sociocultural and gender norms. Being aware of this possibility can be the first step in identifying whether women and men are affected differently by the implementation of AML-CFT standards and addressing the potential or real impacts through financial inclusion policy and regulatory responses. Indeed, full financial inclusion will not be possible without policies that take the diverse needs of different populations into account, including those based on gender.

Policy responses to global AML-CFT standards have the potential to make a positive contribution to women's financial inclusion and, in turn, to gender equality

and empowerment. However, this will require careful consideration by financial inclusion policymakers and the adoption of proportionate RBAs to implementing AML-CFT standards and rolling out initiatives like tiered CDD, women-targeted financial products and digital ID systems to overcome the identification challenges faced by women who are financially excluded or underserved. This will not only give financial regulators and policymakers the opportunity to manage ML-TF risks effectively, but also contribute to closing the financial inclusion gender gap.

Based on the AFI Guideline Note 31,³¹ it is recommended that financial regulators and policymakers:

- > Incorporate gender considerations in risk assessment processes
- > Consult with gender and women's financial inclusion stakeholders in any NRA process
- > Implement proportionate identification and verification requirements in line with the RBA
- > Encourage institutions to take concrete action to better understand the female market segment and serve women clients effectively
- > Encourage the collection of sex-disaggregated data on identification documents to highlight any gender differences
- > Measure the impact of risk-based AML-CFT regulations, such as simplified CDD on financial inclusion, to quantify the benefits
- > Consider the potential of biometric identification to support the CDD process in line with global AML-CFT standards and ensure enough enrollment of women and girls in such programmes;
- > Consider the legal differences in women's and men's access to different forms of identity documents and the potential impact of these differences on women's financial inclusion
- > Consider specific initiatives to raise awareness among women of the personal identification documents needed to meet CDD requirements. This may involve engaging with women's business associations,

29 "Gender" refers to social relations between men and women that are socially constructed and can change over time and from place to place.

30 Alliance for Financial Inclusion. 2016. Policy Frameworks to Support Women's Financial Inclusion. Available at: https://www.afi-global.org/sites/default/files/publications/2016-08/2016-02-womenfi_1_0.pdf; AFI and Women's World Banking and CGAP (Mann). 2015. Banking on Change: Enabling Women's Access to Financial Services. Available at: <https://www.cgap.org/blog/banking-change-enabling-womens-access-financial-services>

31 Alliance for Financial Inclusion. 2018. Gender Considerations in Balancing Financial Inclusion and AML-CFT. Available at: <https://www.afi-global.org/publications/2910/Gender-Considerations-in-Balancing-Financial-Inclusion-and-AML-CFT>

producer groups and other channels to reach low-income women.

In Bangladesh, as part of its national drive for empowerment of low-income women, women are only required to present their national identity card or birth certificate as well as their Livelihood Security Cards issued by the Department of Women Affairs Bangladesh. There are no account charges or fees attached to the account. For women entrepreneurs, the requirement is to present a national identity card or birth certificate as well as a certificate of their business activity signed by an authority, such as the headmaster of the local school. This account has a loan limit of USD600.

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The FATF notes in its financial inclusion guidance (2017) the flexibility granted by the RBA, particularly in applying simplified due diligence lower risk clients, is important for financial inclusion purposes.

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7.5. ALIGNING FINANCIAL INCLUSION AND AML-CFT FOR FORCIBLY DISPLACED PERSONS (FDPs)

CDD initiatives, both regulatory and technological, can be applied specifically to targeted population groups who may be particularly disadvantaged and/or vulnerable. This is particularly useful for situations of forced displacement, as it allows these groups to access financial services with greater ease and improve their conditions. Financial inclusion is important for forcibly displaced persons (FDPs) who are represented by stateless persons, asylum seekers, refugees, internally displaced persons (IDPs), returnees (refugee and IDP returnees) and other Persons of Concern (POC). Financially including FDPs means that they can access formal financial services in a dignified manner and are empowered to store money safely, make savings, send money home, secure employment, insure themselves against risks and so on.

FDPs do not typically have acceptable identification to satisfy CDD requirements to gain access to formal financial products and services. However, some AFI member countries have taken measures to overcome FDP financial exclusion within their jurisdictions. These are briefly described in Box 10 below.

BOX 10: OVERCOMING FINANCIAL EXCLUSION OF FDPs IN MEMBER COUNTRIES

BIOMETRIC IDENTIFICATION OF REFUGEES IN JORDAN

In 2015 Jordan released the United Nations High Commission for Refugees (UNHCR)-led, Ministry of Interior (MoI) biometric identification cards (AFI, 2019). These cards are for Syrian refugees living in Jordan. They are nationally recognized and can be used by refugees as consistently and securely as locals use their respective identity cards. Refugees are even able to access UNHCR cash aid through biometrically enabled ATMs.

SIMPLIFIED CDD FOR IDPs IN THE PHILIPPINES

The Philippines created a special exemption for persons who have been internally displaced by natural disasters within the borders of the jurisdiction. These IDPs do not need to present a robust identity document to access financial services. This account is then significantly restricted, but the individual is at least able to access services. It should be noted that it is much easier to apply simplified CDD in these contexts since IDPs are citizens and because they have been forcibly displaced by a natural disaster as opposed to conflict which presents a different level of risk.

SIMPLIFIED CDD FOR FDPs IN ZAMBIA

Bank of Zambia granted approval to money service providers such as Airtel Money, Zoono, Kazang, Zamtel Kwacha and MTN Mobile Money to provide mobile financial services (within transaction and balance limits for mobile money or e-money) to refugees by using refugee identification cards or registration documents issued by the Ministry of Home Affairs to satisfy CDD requirements. It also collaborated with the Zambia Information and Communication Technology Authority (ZICTA) to facilitate the provision of phone sim cards to refugees using the above identification documents. All SIM cards need to be registered with the Communications Authority in Zambia. Following this authorisation by Bank of Zambia, one of the mobile money service providers in partnership with the United Nations Capital Development Fund (UNCDF) and UNHCR has started providing more affordable phones (this was one of the hindrances as refugees do not have the resources to purchase mobile phones) and mobile money services to refugees in Zambia.

BOX 10: CONTINUED

SIMPLIFIED CDD FOR FDPs IN TANZANIA

Before including refugees in the formal financial system, to access credit, savings, insurance and other services, the Government and the Bank of Tanzania worked closely with the FIU on an NRA to establish the level of risks that can be posed by refugees in the financial system. This helped to inform the formulation of the National Financial Inclusion Framework II, Tanzania's second NFIS, and in the development of tiered CDD processes. In parallel, the Bank of Tanzania encouraged banks and MNOs to develop products that are suitable for FDPs. Finally, as the Chair of the Financial Inclusion National Council, the Bank of Tanzania works hand in hand with the National Identification Authority (NIDA) to ensure that FDPs are registered and issued with the unique identification to support them in opening an account at a bank. The ID will also help in transactions with MNOs.

INTER-AGENCY IDENTITY VERIFICATION EXERCISE IN RWANDA

The Government of Rwanda through the Ministry In Charge of Emergency Management (MINEMA), previously Ministry for Disaster Management and Refugees (MIDIMAR), the National Identification Agency (NIDA), and Immigration together with the UNHCR have launched a joint verification exercise of refugees and asylum seekers residing in Rwanda for the purpose of updating information and verifying their physical presence in the country through biometric data. This has positively impacted refugees by giving them greater access to identity documents which facilitated their ability to access Government services, employability and ability to move more freely in the country and abroad as well as accessing services from financial institutions (e.g. opening bank accounts and mobile money accounts).

For example, refugees in Nyabiheke, Gihembe and Kigeme camps have been receiving cash digitally through mobile money services instead of in-kind support such as food packages or vouchers. The refugees have been provided a mobile phone, which in turn enables them to receive mobile remittances. The Equity Bank has signed a Memorandum of Understanding (MOU) with MINEMA to send staff to camps and help refugees to open accounts with the help of the UNHCR. The National Bank of Rwanda together with partners will visit the camps to conduct awareness raising on financial consumer protection regulations as well as encouraging the adoption of cashless means of payments.

Source: AFI Member Survey 2018, 2019

ADDITIONAL CONSIDERATIONS FOR INCLUSIVE FINANCIAL INTEGRITY

Given the challenges listed in Chapter 2.5 “What does success for inclusive financial integrity look like?” on page 10, and the ways in which AFI member countries have addressed them as described throughout this toolkit, the following list provides additional considerations to achieve inclusive financial integrity:

(a) Focus on the objectives of due diligence

The objectives of due diligence include obtaining an understanding of customers in the formal financial sector in order to improve the integrity of financial systems. Improved financial integrity and reduced financial crime is important for broader sustainable growth and economic development. As such, CDD should not be perceived as a compliance burden, but rather as a building block for financial inclusion and financial integrity.

(b) Develop a better understanding of risk

Building on the above, jurisdictions should commit adequate resources to understanding risk within their local context. A sound understanding of risk will enable the development of proportional due diligence. The focus should not be on simply complying with global standards, but on developing an understanding of risk at country/sectoral levels and within institutional contexts, in order to achieve favorable inclusive financial integrity outcomes.

(c) Address the concept of identity

Identity goes beyond what a person has or possesses. In order to resolve the challenge of identity, jurisdictions should consider the concept of identity so that customer identification obligations do not revolve around a limited number of identifiers (often based purely on documents) that are not necessarily effective in a dynamic environment. This involves recognizing that identity also refers to “who someone is”, for example in relation to biometrics, and not merely what “someone possesses” such as an identity document.

(d) Explore different approaches to enhance proportionality

In line with the above, regulators should explore measures that can be implemented to build on past narrow definitions of identity and what must be done to identify customers, as well as support a better understanding of risk. As raised in the report, these include:

- > Biometrics in identification
- > Removing low-value identifiers like proof of address where there are other forms of effective identifiers

easily available to lower-risk transactions

- > Simplified and tiered due diligence, especially for vulnerable groups
- > Use of Legal Entity Identifiers (LEIs) to help in speeding up the verification process for account opening or onboarding of a company especially in cross-border scenarios
- > RegTech for STRs and management of risk profiles

(e) Create an environment for Fintech and innovation

New innovations like data tokenization need space to grow within an environment that is conducive to innovation. To facilitate such innovation, jurisdictions could consider “test and learn” approaches to RegTech and Fintech. This can enable innovation in CDD and support the efforts of regulators in responding to the evolving environment and in implementing necessary regulations as the risks associated with the new technologies become clearer. For example, Bank Negara Malaysia’s regulatory sandbox facilitated the development of e-KYC processes.

(f) Support and strengthen Non-Profit Organizations (NPOs) to further inclusive financial integrity

Non-profit organizations (NPOs) are vital for the organizational capacity, capacity building and empowerment of FDPs, women, MSMEs and other vulnerable groups. However, they are adversely affected by AML-CFT frameworks that are not inclusive and have been on the end of unjustified de-risking. Countries should consider including NPOs as target groups in their financial inclusion agendas and should explicitly link this to the financial integrity strategy. To further enhance the role of NPOs, it is also important to:

- > Increase NPO expertise within financial institutions so that appropriate AML-CFT risk assessment is undertaken
- > Capacitate NPOs to improve their knowledge of financial sector requirements and AML-CFT requirements

The COVID-19 pandemic is an example of why NPOs should be supported and strengthened. The FATF has acknowledged the critical role of NPOs during the COVID-19 pandemic in providing their services to those who are most in need. In line with this, it has released a public statement to highlight that the FATF Standards are not intended to prevent all financial transactions with jurisdictions where there may be high ML/TF risks, “but rather to ensure these are done through legitimate and transparent channels and money reaches

its legitimate intended recipient. National authorities and financial institutions should apply an [RBA] to ensure that legitimate NPO activity is not unnecessarily delayed, disrupted, or discouraged (FATF, 2020).”

(g) Expect digital ID and e-KYC to become the “new normal”

The COVID-19 pandemic and its significant, rippling impact on financial systems and economies worldwide, have highlighted the urgency for financial policymakers and regulators to become better prepared for such crises. Developing effective digital solutions and systems for remote customer onboarding and financial transactions for a time when in-person transactions are not possible due to the risk of infection is key in addressing this. In response to COVID-19, many jurisdictions are leveraging digital ID and e-KYC to expedite digital payments, government transfers, and humanitarian cash transfers while mitigating ML-TF risks, especially for the most vulnerable segments of populations. Moving forward, there is potential for digital ID and e-KYC to become the “new normal,” even after the pandemic, and countries should consider the inclusion and integrity benefits of moving towards these systems.

8. RISK-BASED SUPERVISION

The purpose of this chapter is to identify and describe inclusive financial integrity considerations in the application of the risk-based supervision approach towards enhancing inclusive financial integrity.³³ It is important to understand risk-based supervision within two contexts;

- > The risk-based approach to supervision as conducted by supervisory authorities
- > The supervision of the risk-based approach as implemented by reporting entities.

While the supervisors need to understand, monitor and guide institutions on how they are implementing the RBA they need to use risk-based supervision to prioritize the key institutions as well as particular issues within institutions to focus (due to limited resources). Although the above approaches are separate, they are interrelated in practice. As such, this section will focus more on the former (that is RBA to supervision as conducted by supervisory authorities).

8.1. FATF CONTEXT

Supervision of AML-CFT obligations play a vital role in the success of a country's AML-CFT strategy and its implementation. Financial institutions, DNFBPs and VASPs should be subject to adequate regulation and supervision.³⁴ In this regard, supervisors should have adequate powers to supervise or monitor, and ensure compliance by, institutions with requirements to combat ML-TF.

Guidance and feedback provided by regulatory or supervisory authorities play an important role in relation to the RBA, notably in assisting financial institutions and DNFBPs in applying measures to combat ML-TF.³⁵ The use of the range of effective, proportionate and dissuasive sanctions, whether criminal, civil or administrative, available to deal with natural or legal persons that fail to comply with AML-CFT requirements, will play a role in the effective implementation of a risk-based supervision framework.

These should be applicable not only to financial institutions and DNFBPs, but also to their directors and senior management.³⁶ FATF RBA guidance has been published in respect of various sectors, specifically banking, insurance, and securities sectors, as well as DNFBPs.

In general, the international standards allow for flexibility in the formulation of country AML-CFT measures, including those relating to supervision of AML-CFT obligations. There is appreciation that a one-size-fits-all approach to AML-CFT is not appropriate and the supervision approach should be appropriate for the country's circumstances. This flexibility is crucial in the implementation of measures relating to products and services that serve the financially excluded or underserved.

8.2. RISK-BASED SUPERVISION

It is an FATF requirement that the supervision of AML-CFT requirements be risk-based.³⁷ The RBA to supervision refers to "the general process by which a supervisor, according to its understanding of risks, allocates its resources to AML-CFT supervision".³⁸ The use of a supervisor's resources in an effective manner is at the core of a risk-based supervision value proposition. Further, it can be described as the "specific process of supervising institutions that apply an AML-CFT risk-based approach".

Supervisors should understand the ML-TF risks within the sectors over which they have supervisory responsibilities. This involves evaluating institutional measures and recognizing that risk is not static and may change over time. They should have onsite and offsite access to all relevant information and data on the specific domestic and international risks associated with customers, products and services of the supervised institutions, including the quality of the compliance function of institutions. The frequency and intensity of onsite and offsite AML-CFT supervision of institutions should be based on ML-TF and related risks.

33 This chapter has been drafted with reference to the Cenfri and Compliance & Risk Resources report on risk-based supervision (RBS)

34 FATF. 2004. FATF 40 Recommendations. (Recommendations 26 and 28). Available at: <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/the40recommendationspublishedoctober2004.html>

35 FATF.2004. FATF 40 Recommendations (Recommendation 34). Available at: <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/the40recommendationspublishedoctober2004.html>

36 FATF. 2004. FATF 40 Recommendations. (Recommendation 35) Available at: <https://www.fatf-gafi.org/publications/fatfrecommendations/documents/the40recommendationspublishedoctober2004.html>

37 Refer to Interpretive Note to Recommendation 26, Recommendation 8 and/or the FATF Methodology

38 Interpretive Note to Recommendation 26 (Regulation and Supervision of Financial Institutions) of the FATF Methodology

They should also be based on policies, internal controls and procedures associated with the institution, as identified by the supervisor's assessment of the institution's risk profile, and on the ML-TF risks present in the country.

The FATF Recommendations require institutions to develop AML-CFT programmes. As part of a supervisor's role, these programmes will be reviewed to ensure that they are effectively addressing ML-TF risks faced. A supervisor's review of an institution will include consideration of the following, among others: governance, RBA framework, RBA process, due diligence, monitoring, reporting, training, record keeping and compliance.

The approach that is adopted by supervisors in discharging their supervisory obligations will have a significant impact on the institutions that are subject to such supervision. In broad terms, institutions take note of the expectations of supervisors when designing and implementing their AML-CFT measures. For example, where it is believed that there is zero tolerance for ML-TF risk in relation to measures that are put in place by institutions, this will tend to steer them towards being overly conservative in their RBAs, which can have a negative impact on financial inclusion.

8.3. FINANCIAL INCLUSION CONTEXT

Supervisors should be deliberate in taking into consideration financial inclusion within their risk-based supervision plans, and such plans should be appropriately formulated in relation to the associated ML-TF risks³⁹. Information and data relating to relevant factors should be considered by supervisors in identifying, assessing and understanding these risks, particularly in respect of institutions' products and services, delivery channels, clients, geographic reach, and other factors where these impact on financial inclusion.

In addition, there are opportunities to encourage risk-based, proportionate compliance responses through various mechanisms where supervisors play a lead role. For example, in the Philippines, supervisors have effectively incorporated financial inclusion into their supervision processes (AFI member country interviews, 2019). Simplified due diligence is allowed for products that are lower risk, and financial inclusion can be a lower risk factor. When the ML-TF risk of products is assessed, institutions should consider the implications that the products have on financial inclusion (and ultimately, risk) and use this to influence decision-making. If products are deemed to be lower risk by

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There is appreciation that a one-size-fits-all approach to AML-CFT is not appropriate and the supervision approach should be appropriate for the country's circumstances.

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taking various factors into account - particularly financial inclusion, then simplified due diligence can be applied. There are active links and coordination between the financial integrity supervisors and financial inclusion working groups in their country, which facilitates collaboration on such matters.

Financial integrity supervisors can advise on products that qualify for simplified due diligence measures, i.e. considering ML-TF risk and financial inclusion considerations. In this regard, Bangladesh provides for the application of simplified due diligence measures for confirmed lower risk products that have financial inclusion considerations. Products with significant financial inclusion considerations are, in certain circumstances, and where a full and adequate risk assessment has been undertaken, deemed to be lower risk and so lower levels of due diligence are allowed.

In Zambia, the NRA provided important insights in terms of where the major threats and risks in the economy were located. This information has shaped the understanding of risk within institutions and led supervisors to require stricter internal controls from specific institutions⁴⁰.

The following are additional inclusive financial integrity considerations in the application of risk-based supervision:

- > Supervisors can consider deep dives in high-risk areas or institutions while applying lighter supervision of low-risk institutions.
- > In aligning financial inclusion and financial integrity processes, it is important to ensure that financial-inclusion-related products and institutions with financial inclusion business models are given enough space to grow. Strict regulatory and supervisory environments that do not result in proportionate outcomes may not be conducive to facilitating this.

39 Member country interviews (2019)

40 Member country interviews (2019)

- > Assessments of risk should not be static as risks will change over time depending on how circumstances develop and how threats evolve. For example, once an understanding of risk is established, supervisory approaches should allow for changing circumstances, particularly where this will support proportionate outcomes.
- > The risk-based supervision approach should be informed by appetites and tolerances for risks, which should be appropriately communicated, thus providing institutions with valuable insights to assist them in applying risk-based and proportionate measures. This is important for creating a dialogue and understanding between stakeholders. Institutions would consider their risk appetite and tolerances along with that of their supervisors' but will be held accountable in terms of the capacity they have to deal with the risks.

9. INTER-AGENCY COORDINATION IN NRAs AND MEs

As described in previous chapters, inter-agency coordination especially between financial inclusion and AML-CFT actors is crucial to the achievement of inclusive financial integrity. The purpose of this chapter is to explore inter-agency coordination challenges within the NRA and ME processes, and highlight possible solutions to overcome them.

9.1. THE IMPORTANCE OF INTER-AGENCY COORDINATION

Inter-agency coordination refers to coordination among various public and private sector NRA and/or ME stakeholders. The key stakeholders include, among others:

- > Financial Intelligence Unit
- > Banking and non-banking supervisors including the central bank and other financial authorities
- > Public sector departments from different ministries
- > Public sector departments from the same ministries
- > Public and private sectors
- > Departments/ministries from different countries/ jurisdictions
- > Law enforcement agencies
- > Other relevant institutions

Inter-agency coordination is important during an NRA and ME. It pools and optimizes resources and expertise, reduces duplication, facilitates information availability and promotes buy-in and ownership of the outcomes. Due to the crucial role that is played by inter-agency coordination, this topic is being addressed as a standalone issue.

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Inter-agency coordination especially between financial inclusion and AML-CFT actors is crucial to the achievement of inclusive financial integrity.

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9.2. AFI MEMBER EXPERIENCES WITH INTER-AGENCY COORDINATION

Inter-agency coordination represents a major challenge during an NRA or ME (stakeholder interviews, 2019). According to a survey conducted by AFI (2018), AFI stakeholder engagements (2019) and AFI training in 2019, jurisdictions experienced the following barriers to effective inter-agency coordination:

- > Slow responses from public authorities
- > Lack of data or different forms and formats of data
- > Limited capacity and expertise to understand AML-CFT and the importance of an NRA and ME (This resulted in more time being taken to onboard agencies and stakeholders not familiar with NRAs and MEs.)
- > Differing mandates within agencies
- > Confidentiality issues around sharing data and information
- > No pre-established structure and mechanism for coordination
- > Limited AML-CFT capacity and expertise within the agencies
- > Varied buy-in and commitment levels from different agencies
- > Limited understanding of which stakeholders to include in the assessment process
- > Difficulty in sustaining stakeholders' participation
- > Difficult deciding which stakeholders to include and exclude as stakeholder groups may end up being unnecessarily large
- > Lack of instruments or formal arrangements to collaborate in information-sharing

The AFI member jurisdictions interviewed have responded to these challenges as highlighted in the table below. The first column in the table describes various solutions while the second column gives examples of how member jurisdictions have specifically applied such solutions. The list is not necessarily exhaustive and does not cover all member jurisdictions but serves to provide examples.

TABLE 3: AFI MEMBERS' SOLUTIONS TO INTER-AGENCY COLLABORATION CHALLENGES

SOLUTION	JURISDICTION
<p>USE OF DECREE OR PRESIDENTIAL CABINET</p> <p>Departments are more likely to cooperate in an NRA through sharing of information and data if the initiative has significant political backing. Member jurisdictions have used various methods, including executive orders from the office of the president, to show political backing and urgency of the initiative.</p>	<p>Philippines: The Office of the President issued an executive order to show the political will for an NRA exercise. This was disseminated to the public sector. It required the participation of a senior official by the agencies.</p> <p>Costa Rica: The presidential cabinet signed off on a letter to institutions informing them of the importance of the project and the need for urgent participation.</p> <p>Bhutan: There is provision in the AML-CFT Act that mandates the involvement of senior staff in the AML-CFT coordinating body. The national coordination committee meets twice a year and they are held accountable for how effective they have been to implement the action plans.</p> <p>Zambia: The cabinet was involved in an NRA and gave authority to the FIU to request information.</p>
<p>ENSURING KEY STAKEHOLDERS ARE INVOLVED</p> <p>It is important to ensure the right stakeholders are involved in an NRA and the NRA working groups. It is also important that the mix of stakeholders is as comprehensive as possible, encompassing multiple different sectors.</p>	<p>Tanzania: Tanzania established nine working groups for its NRA. These referred to: threat analysis; national vulnerability; banking; insurance; securities; DNFBPs, and financial inclusion. The inclusion of private sector and key market players was important for gathering information. It also prepared these institutions for their own risk assessments.</p> <p>Afghanistan: The NRA working group consisted of 5 teams from 17 public and private sector agencies. These related to the banking sector, threat analysis, vulnerability, DNFBPs and financial inclusion.</p> <p>Zambia: Zambia engaged stakeholders such as banks, microfinance institutions, insurance companies, mobile service providers, postal services, retails shops, securities exchanges, brokers and fund managers.</p>
<p>LEVERAGING EXISTING STRUCTURES</p> <p>Making use of existing structures reduces costs and increases effectiveness. Jurisdictions that were able to leverage structures that already existed were in much better positions to obtain the necessary information promptly and to facilitate coordination between institutions.</p>	<p>Armenia: Armenia leveraged its AML-CFT committee which was established prior to the NRA. This was a high-level public committee with representatives from the central bank, Ministry of Justice, Ministry of Economics, Financial Monitoring Center and the private sector, among others.</p> <p>Bhutan: There is an ongoing two-level committee on AML-CFT which was leveraged for an NRA.</p> <p>Mongolia: The Cooperation Council was established in 2006 to ensure implementation of laws and regulations pertaining to AML-CFT and to ensure inter-agency collaboration. The Council works alongside the financial intelligence unit, and consists of the Ministry of Foreign Affairs/Relations, Ministry of Finance, Ministry of Justice and Internal Affairs, Prosecutors Office, Bank of Mongolia, Financial Regulatory Commission, General Police Department, General Intelligence Agency, General Tax Department, and General Customs Department.</p>

TABLE 3: CONTINUED

SOLUTION	JURISDICTION
<p>INCENTIVIZING PARTICIPATION</p> <p>Member jurisdictions have used different tools to ensure that institutions initially and continually participated in the NRA and ME processes. These include certificates as well as meetings and trainings on the purpose of an NRA.</p>	<p>Bhutan: Provided stakeholders with certificates that confirmed participation in the NRA and ME.</p> <p>Zambia: Had in-depth interviews/meetings with relevant stakeholders to explain the relevance and importance of NRA. Once the stakeholders understood the context, they were more willing to share information promptly.</p> <p>Philippines: Drafted letters and had discussions with the private sector to explain the importance of the event. They did the same for the public sector but were also assisted by a presidential decree.</p>
<p>NDAs AND MOUs</p> <p>In some cases, data confidentiality issues cause institutions to be inclined to withhold data and information. Jurisdictions addressed this by drafting MOUs and NDAs to ensure confidentiality. Data can also be anonymized.</p>	<p>Nigeria: MOUs are signed by principals and then operationalized by assigning responsible directors and point people for regular liaison. Thereafter, all issues and interactions are normalized. There is also an interregulator forum to coordinate, at a higher level, the need for more detailed bilateral MOUs as above.</p>
<p>FOCAL POINTS</p> <p>Another strategy for enhancing collaboration within institutions is to establish focal points within each institution. These are normally senior level executives who serve as the communications touchpoint for each organization. They are responsible for coordination with other relevant public and private sector institutions, providing necessary data and information.</p>	<p>Bangladesh: Identified over 25 different organizations in public and private sectors and appointed two people within each organization to act as a focal point for that organization. Each institution signed formal agreements to ensure clarity and accountability.</p> <p>Philippines: Sent a formal request to each agency explaining the importance of the exercise and requested them to appoint an official who will be responsible to represent the agency, respond to queries and serve as an official communication link. A relatively senior person would serve as the focal point.</p>
<p>SUPERVISOR'S FORUM</p> <p>Establish a supervisor's forum as a platform for ongoing coordination on inclusive financial integrity, NRA and ME.</p>	<p>Zimbabwe: Zimbabwe established a supervisor's forum to better coordinate various supervisors on inclusive financial integrity, NRA and ME. As opposed to doing this one-off during specific ME and NRAs, the forum provides a mechanism to focus on these issues on an ongoing basis and reduce instances of different supervisors requesting the same information from institutions at different times.</p>

9.3. ADDITIONAL CONSIDERATIONS

FREQUENTLY REVISIT MANDATES AND ACCOUNTABILITY FRAMEWORKS TO ENSURE ONGOING INTER-AGENCY COLLABORATION

Inadequate interdepartmental/agency collaboration is often a pointer of deeper AML-CFT governance issues. A lack of adequate data and/or incompatible data sources indicates that there are development opportunities relating to ongoing AML-CFT processes and collaboration between stakeholders. It is important to review and revise the governance and accountability frameworks to ensure that they are fit for purpose. It is also important to ensure that stakeholder mandates and incentives are aligned, particularly in respect of key national processes such as NRAs and MEs. With the right incentives in place and common objectives, inter-agency coordination should become an ongoing process rather than an ad hoc/one-off event.

REVIEW EXISTING INTER-AGENCY COORDINATION STRUCTURES AND MECHANISMS TO ENSURE THAT THEY ARE FIT FOR PURPOSE

Where there is already a structure for collaboration in respect of the national development plan or an NFIS, jurisdictions should assess the extent to which this could be leveraged. It could be adapted or AML-CFT matters could be covered therein. Duplication of effort could be avoided, and the optimal use of scarce resources could be promoted.

ENSURE EFFECTIVE COMMUNICATION PLANS ARE IN PLACE

For the inter-agency structures to be successful and efficient, they should involve the right resources at the right level. For example, since the time of a director general is scarce, they cannot be involved in every meeting. As such, it will be important to involve such persons where this is necessary and to leverage other resources, such as technical experts where appropriate. In addition, steps should be taken to ensure consistency in representation from the various stakeholders. If different people, or unqualified people, attend meetings, this may affect the continuity of processes. It is also important to have clear objectives and to appropriately motivate the inclusion of the stakeholders so that they buy into the process. A robust communication plan, including the use of focal points as described above, will go a long way to ensuring effective implementation of the inter-agency structures.

EXPLORE ALTERNATIVE WAYS TO ENGAGE WITH THE PRIVATE SECTOR AND NON-PROFITS

Private sector institutions and non-profit organizations hold valuable data pertaining to AML-CFT. In cases where they are not willing to share this, jurisdictions should consider bilateral sharing agreements between key stakeholders. This can be set up via MOUs and NDAs. Institutions should also consider anonymizing data shared (especially by private sector institutions) to ensure confidentiality or privacy protection. Jurisdictions should also consider sourcing data from other institutions like academic institutions and agencies within the NSS.

10. ALIGNING FINANCIAL INCLUSION AND AML-CFT IN MUTUAL EVALUATIONS (MEs)

The purpose of this chapter is to identify and describe key ME considerations in relation to financial inclusion for the benefit of countries that will undergo ME.

10.1. MEs: A RECAP

MEs examine the ongoing implementation of FATF standards by countries and the achievement of desired outcomes within the review period. An ME report provides an in-depth assessment of a country's system for preventing criminal abuse of the financial system as well as recommendations to the country to further strengthen its system. When conducting MEs, assessors typically use the country's own risk assessment(s) as a starting point for understanding a country's ML-TF risks, but do not uncritically accept a country's risk assessment. An ME report is produced at the end of the assessment, which provides a base from which to implement measures that will strengthen a country's ability to prevent and combat ML-TF.

10.2. CHALLENGES WITH MEs RAISED BY AFI MEMBERS

AFI members have indicated the following issues and challenges with the ME processes in their countries. Most of these are linked to the challenges already noted for NRAs in the previous chapter:

- > **Limited understanding of the ME process:** AFI member countries who were interviewed confirmed that domestic stakeholders may lack a detailed understanding of the ME process. This seems pervasive across countries.
- > **Jurisdictions are often reactive rather than proactive to an ME:** AFI members who were interviewed confirmed that stakeholders tend to be unprepared or underprepared as they only focus on an ME just before it takes place. Few resources and little buy-in is deployed well in advance of an ME.
- > **MEs are often viewed as events rather than being part of an integrated process:** Because they take place periodically, stakeholders tend to view them as events and standalone processes that are not necessarily linked to other development initiatives, such as financial inclusion and national development plans.
- > **Different opinions with assessors on evaluation outcomes:** Some interviewed countries confirmed the challenge of differences in opinion on the ME outcomes with the assessors. This may arise due to several issues including the above-mentioned challenges of limited data, buy-in, as well as concerns relating to the country risk profile. It should however be noted that the ME process is designed to minimize such disagreements and provides several opportunities for the assessed country to discuss the issues, make its case, and provide feedback on the assessors' conclusions (through both written comment and in-person discussions).
- > **Capacity and human resources constraints including stakeholder's unavailability to meet assessors (e.g. Mongolia):** The limited capacity of certain jurisdictions in terms of human and financial resources has limited the ability of stakeholders to engage with assessors in the ME process.
- > **Domestic stakeholder cooperation challenges:** Some countries have not adequately engaged with ME assessors over the course of an ME and not provided the cooperation that is expected of them.
- > **Data unavailability and consistency to demonstrate effectiveness (e.g. Zambia):** Limited data, as well as poor quality and consistency of data, was confirmed as a limiting factor to demonstrate the effectiveness of a jurisdiction's AML-CFT regime. There is FATF guidance on AML/CFT statistics and data which endeavors to help countries avoid these issues.
- > **Weak commitment and coordination among stakeholders:** Due to a limited understanding of the importance of the ME process by some country stakeholders, interviewed countries confirmed that weak commitment by stakeholders is a challenge. This is strongly linked to the reactive nature of stakeholders to MEs. Further, stakeholders tend to view MEs as events rather than ongoing processes. This approach forces countries to play "catch-up" shortly before each ME while leaving AML-CFT shortfalls to be addressed at a later stage.

10.3. INCLUSIVE FINANCIAL INTEGRITY CONSIDERATIONS WHEN PREPARING FOR A MUTUAL EVALUATION (ME)

When preparing for an ME, there is opportunity to integrate the following considerations to promote inclusive financial integrity. These considerations are discussed within each of the ME phases as below:

TECHNICAL REVIEW COMMUNICATION

Prior to providing updates and information relating to the AML-CFT context of a country or its ML-TF risk profile, in-country stakeholders may have formal and informal engagement with the secretariat or liaison point of the relevant assessment body (FATF, FSRB, IMF or World Bank). Countries may, often with the assistance of the assessing body, conduct pre-ME workshops with stakeholders to raise awareness on the evaluation process and this is open to all relevant stakeholders in the jurisdiction. This helps to enhance understanding of the AML-CFT system, and to increase literacy and competency levels among stakeholders that engage with the technical compliance questionnaire.

Such workshops provide an opportunity to involve relevant financial inclusion stakeholders and to identify financial inclusion and de-risking issues that are relevant to the assessment, i.e. at an early stage.

STAKEHOLDER ENGAGEMENT WITH ASSESSORS

Sound risk management principles should be considered in the design of an RBA for a country. This would include consideration of how ML-TF risk appetites and tolerances should be addressed. There should be recognition that, in practice, risk cannot be eliminated completely. An environment that acknowledges and encourages a zero-risk approach is not practical. This recognition is likely to support countries in moving relatively quickly along their development paths while being mindful of the different risks (ML-TF risk, compliance risk, financial exclusion risk and illicit financial flows risk).

This provides an opportunity to position financial inclusion innovations that may have some level of ML-TF risk but also the potential to financially include people, thereby reducing financial exclusion risk. Risk-based, simplified AML-CFT measures may be appropriate in such cases, in line with and as permitted under the FATF standards where risks are lower. The ME process represents a platform to increase focus on such measures.

Financial inclusion should be addressed upfront as a policy matter in the AML-CFT framework in the respective country. Consideration thereof in an NRA

or ME will provide a platform to address inclusive financial integrity objectives. An example of the need for appropriate engagement with assessors is seen in the introduction of the principles-based due diligence obligations in South Africa. This no longer specifies that the residential address of an individual must be obtained and verified. This appears to be appropriate within the South African context;⁴¹ however, the ME assessors may come from jurisdictions where there is an expectation that there should be residential address verification, i.e. in the absence of an exemption or arrangements designed to support financial inclusion. Documenting the basis for simplified CDD measures based on an assessment of lower risks will support effective communication with the assessors.

SCOPING EXERCISE FOR AN ME

Prior to the onsite visit, the assessment team will work with stakeholders from the country being assessed to identify any areas of higher and lower risks, as well as relevant contextual issues, which will be a particular focus of the ME. This scoping exercise, which may include analysis of a jurisdiction's previous NRA reports, provides an opportunity for AFI country members to clearly identify any relevant financial inclusion issues.

Where an economy is largely cash-based or informal, this will often be identified as an area of increased focus by the assessors, who will wish to examine what ML-TF risks arise and what impact financial exclusion issues have on the effectiveness of the country's system.

Countries may consider delivering a presentation on their AML-CFT context and the ML-TF risks at the commencement of an onsite visit. It is encouraged that such information is also provided well in advance of the onsite visit to aid assessors in scoping the higher and lower risk issues, and in preparing for the onsite. This will help to avoid situations where there are differing opinions between in-country stakeholders and assessors. Specifically, the financial inclusion and financial exclusion risk purview could be addressed.

Awareness and understanding of stakeholders' views of the country-AML-CFT regime, what is in the media, and what is contained in publicly available documents about the country is important as these also shape assessors' perspectives.

⁴¹ The South African ME is currently ongoing (at the time of writing), and the importance of this development in addressing risk is yet to be officially appraised under the Mutual Evaluation.

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The country should ensure that financial inclusion/exclusion issues are properly addressed in the relevant parts of the MER.

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EFFECTIVENESS REVIEW

Jurisdictions may conduct country assessments of the effectiveness of the AML-CFT regime. These could be used to demonstrate that its financial inclusion policies and frameworks are appropriately risk-based, and it will help assessors evaluate records of ongoing consideration of the impact thereof.

DRAFT ME REPORT (MER)

Countries should ensure that relevant stakeholders, including the financial inclusion body or responsible department, are involved in reviewing the drafts of an MER. This will assist in ensuring that financial inclusion considerations are appropriately incorporated into the MER. It would also encourage engagement with financial inclusion stakeholders at an early stage of the MER preparation process. The country should ensure that financial inclusion and exclusion issues are properly addressed in the relevant parts of the MER, including chapter 1 (which sets out the ML-TF risks and context), chapter 2 (which assesses national AML-CFT policies and coordination, including the assessment of risk), chapter 5 (which assesses the implementation of the AML-CFT preventative measures), and chapter 6 (which assesses AML-CFT supervision).

11. SUMMARY OF KEY TAKEAWAYS

This section contains key insights and recommendations from the toolkit. It draws on each section of the document to provide considerations that will be relevant in the development of country AML-CFT frameworks that achieve inclusive financial integrity objectives.

INCLUSIVE FINANCIAL INTEGRITY

Aligning financial inclusion and financial integrity refers to the implementation of effective and risk-based AML-CFT and NFIS regimes that advance the financial inclusion and financial integrity agenda. This can only be successful if the policy objectives of financial inclusion and financial integrity are viewed as mutually reinforcing, and if the pursuit of one does not adversely affect the other. Where countries strengthen this alignment, they will be better positioned to achieve favorable outcomes.

WHAT DOES SUCCESS LOOK LIKE FOR INCLUSIVE FINANCIAL INTEGRITY?

A first step towards aligning financial inclusion and AML-CFT is to define a shared vision based on what “success looks like.” The outcomes (success) of inclusive financial integrity should be considered in the design, development, implementation and communication of RBA frameworks.

This should be specifically addressed in AML-CFT and financial inclusion policy formulation processes and all other components of the framework. It is important that required outcomes should be determined and the achievement thereof monitored in an integrated manner. Notably, financial integrity measures (including AML-CFT policy, regulatory obligations and risk-based supervision) that support financial inclusion create stable investment environments, promote sustainable development and stimulate inclusive growth.

RISK DEFINITIONS ARE IMPORTANT FOR SUCCESS

ML-TF and related risks should be clearly defined in a manner that is appropriate for the country context. This will assist in facilitating the appropriate focus thereon in designing, implementing and maintaining measures that mitigate risks and have the potential to steer country-level policy towards addressing the broad challenges that are often experienced in relation to inclusive financial integrity, including financial exclusion risk and illicit financial flows risk.

NEED FOR AN INTEGRATED VIEW

There should be an integrated view of the AML-CFT framework of a country and stakeholders should recognize the need for synergy between the components thereof. There are a number of moving parts, as indicated in Figure 1, that interrelate and play an important role in serving as a framework for considering inclusive financial integrity imperatives, specifically: strategy and policymaking; regulation development; NRAs; MEs; risk-based supervision, and inter-agency cooperation, which all articulate into the achievement of inclusive financial integrity outcomes, and in turn inform the need for policy or framework changes in a dynamic and ongoing process.

AML-CFT POLICY AND GOVERNANCE FRAMEWORKS ARE CRUCIAL

AML-CFT policy should be well articulated and appropriate for a jurisdiction and the appropriate governance thereof will play an important role. It should be congruent with financial inclusion policy and there should be country frameworks and processes that facilitate alignment.

REGULATORY REGIMES PROVIDE THE BACKBONE FOR AML-CFT MEASURES

AML-CFT regulatory regimes play an essential role in framing the country and institutional-level obligations for AML-CFT. However, inflexible regulatory regimes are relatively difficult to change, and changes may take a significant amount of time. Countries will locate their approach within the continuum of rules- and principles-based obligations. This should be done in a manner that is responsive to the achievement of inclusive financial integrity outcomes.

SUPERVISORS SET THE TONE FOR INSTITUTIONAL AML-CFT MEASURES OF INSTITUTIONS

Supervisory leadership that supports inclusive financial integrity can have a significant influence on the behavior of supervised institutions and their propensity to adopt risk-based, proportionate approaches. Risk-based supervision approaches should recognize the need for processes that support favorable inclusive financial integrity outcomes. This should be undertaken in relation to country or sector risk appetites and the need to develop and maintain the effectiveness of AML-CFT measures.

NRAS ARE KEY TO EFFECTIVE RBAS AND PROVIDE A PLATFORM FOR ADDRESSING INCLUSIVE FINANCIAL INTEGRITY

A robust understanding of risk informs all of the moving parts of an RBA framework including policymaking, regulation development and risk-based supervision. There should be appropriate consideration of financial inclusion opportunities as an integral part of the risk assessment process, in a manner that supports clearly articulated inclusive financial integrity objectives.

MEs PROVIDE KEY INSIGHTS IN RESPECT OF FINANCIAL INCLUSION OPPORTUNITIES

MEs are an integral part of the AML-CFT apparatus of a country. They offer a key opportunity to obtain feedback in relation to AML-CFT measures and relevant risks, including financial exclusion risk, and provide insights into financial inclusion opportunities and policy options.

INCLUSIVE FINANCIAL INTEGRITY SHOULD BE ADDRESSED IN THE MANDATES OF AML-CFT AUTHORITIES

Countries have made progress in making use of tools that can be applied to assist with inter-agency and coordination challenges, in order to achieve effective, sustainable, interdepartmental collaboration. The need for such collaboration should be recognized in the AML-CFT policymaking process, which creates a mandate for inclusive financial integrity. This should provide a platform for accountability in relation to inclusive financial integrity measures.

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A first step towards aligning financial inclusion and AML-CFT is to define a shared vision based on what success looks like.

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RISK-BASED AML-CFT MEASURES FACILITATE THE INCLUSION OF WOMEN, YOUTH, SMES AND FDPS WHILE COMBATting ML-TF

Risk-based AML-CFT measures, particularly in relation to CDD, enable the efficient use of resources. This is key in facilitating financial inclusion and concentrating resources where there is higher risk. Regulatory and technical innovations, as illustrated in various countries, serve to promote risk-based measures and facilitate the inclusion of women, youth, SMEs, FDPS and others, while effectively combatting ML-TF.

DE-RISKING SHOULD BE ADDRESSED IN ALL PARTS OF AN AML-CFT FRAMEWORK

Policymakers, regulators, supervisors and other AML-CFT authorities should recognize the impact of de-risking on financial inclusion and integrity in a manner that supports the achievement of planned outcomes.

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ACRONYM LIST

AFI	Alliance for Financial Inclusion
AML-CFT	Anti-Money Laundering and Countering the Financing of Terrorism
BIS	Bank of International Settlements
CDD	Customer Due Diligence
CGAP	Consultative Group to Assist the Poor
DNFBP	Designated Non-Financial Businesses and Professions
FATF	Financial Action Task Force
FDP	Forcibly Displaced Person
FI	Financial Inclusion
FIU	Financial Intelligence Unit
FSI	Financial Stability Institute
FSRBs	FATF-Style Regional Bodies
FSPs	Financial Service Providers
GSMA	Global System for Mobile Communications Association
IDP	Internally Displaced Person
KYC	Know-Your-Customer
ME	Mutual Evaluation
ML-TF	Money Laundering and Terrorist Financing
MNO	Mobile Network Operator
MSMEs	Micro, Small and Medium Enterprises
NFIS	National Financial Inclusion Strategy
NPO	Non-Profit Organization
NRA	National Risk Assessment
NSS	National Statistical System
PEP	Politically Exposed Person
RBA	Risk-Based Approach
SDD	Simplified Due Diligence
SDGs	Sustainable Development Goals
VASPs	Virtual Assets Service Providers

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