Aspects of Legal & Regulatory Issues in Mobile Financial Services in the Developing World

Leon Perlman
Chairman, WASPA
www.waspa.org.za
leon@waspa.org.za

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MFS Paradigm & Players

“Use cellphones for banking, remittances & payments”

- **Varied Uses:**
  - POS, MFIs, Airtime/$$$ Transfers/Remittances,
  - Low-value micro payments via SMS eg buy ringtones

- **Varying Nomenclature:**
  - “Mobile Money” or “E-Money” or “Stored Value” or “MFS” etc

- **Two types of purses:**
  - Prepaid non-redeemable airtime purses [bespoke Mobile Money via PVAS from ‘01], and/or
  - Prepaid, redeemable fiat-based (ZAR, $,€) purses [new players]

- **MFS Targets Unbanked, underbanked**
  - “Branchless Banking” - Additive vs. Transformational “banking”
  - Includes “Cash in/Cash Out” cash & “deposit” via informal agents

- **Simple Technology:**
  - Use WAP, SMS & USSD (* & # keys) for phone commands

  > MFS focus is now more on payments (transactional) than savings

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Who’s Offering MFS?

- Bank-led
- Mobile Network Operator (MNO)-led
- Hybrid Bank-MNO
- MFSPs (eg Celpay, MAP International)
- MFIs
- WASPs
- Bank Subsidiaries (Branchless Banking)

Telecoms & Financial Players Well Positioned

“Copetition?”

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MNOs Want Piece of MFS Action

- Increased ARPU & promotes subscriber stickiness (loyalty)
- Leverage Two Prepaid Purses:
  - Prepaid, non-redeemable airtime purses for VAS/micropayments via SMS eg buy ringtones
  - Separate fiat-based redeemable value purses
  - Fiat “deposits” stored in trust account/s in separate MFS entity

- **NFC (proximity) payments coming, altho’ more in developed nations**
  - See Nokia smartphones; MTA NYC

- **90%+ of developing nation MNO users are prepaid, so no bills**

- **Challenges for regulators**
  - Access/Inclusion vs stability
  - Systemic Risk?
  - Banks concerned

  > Need for new e/m-money, payment, banking rules?

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Paucity Of Laws & Regulations

- Modest amount of material on regulatory frameworks for mobile payments by central banks.

- In absence of statute, widely-framed common law (ie interpretation/extrapolation/precedent) rules

  > Creates (good and bad) “loopholes” for emerging technologies

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Some Regulatory & Legal Issues

1. Stored value in prepaid airtime/money purses = deposits?
2. Systemic risk of private currencies
3. Legal Characterization of prepaid “money”
4. Licensing of non-banks/MNOs for MFS
5. Regulatory conflation/arbiterage
6. Proportionality of Regulation
7. Regulatory Coordination between supra/national govt departments
8. Treatment of Cash In/Out Agents who are human ATMs
10. Interoperability between systems
11. Settlement Issues
12. Anti-trust
13. Security Issues
14. AML/KYC/CDD (Customer Due Diligence)
15. Taxation etc etc

  > LARGE Pool of Unanswered Legal & Reg issues
Some Key Legal & Regulatory Issues

1. Is it Money?

2. Enabling Branchless Banking

3. Regulatory Co-ordination within Govts

1. Is Mobile Money (legally) MONEY?

Common Law/traditional (legal) definition of money:

- [Aristotle, Mann: Economic/Orthodox/School ("GAME") = Legal View]
  - Unit of account
  - Store of Value
  - Means of exchange

More suited to bespoke payments

New(ish) definition of money

- [eg Keynes/Austrian/Claim School]
  - Unit of account
  - Means of Payment

More suited to MFS

Æ Common Law legal systems not properly geared

1. 1. Is Mobile Money (legally) MONEY??

More suited to MFS

Æ Common Law legal systems not properly geared

3. Store of value(?)

Æ Common Law legal systems not properly geared

If its NOT money, then what is implication for eg:

- Consumer Protection Laws sounding in MONEY
- Anti MONEY Laundering
- Deposit of MONEY
- Ante nuptial contracts, wills: "You get/I leave you all my MONEY"

Æ Common Law legal systems not properly geared

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2. Enabling Branchless Banking

- Changes Traditional “Banking” Paradigms
  - Introduces non-bank players into the transaction flow
  - No bank branches
  - Allow use of “banking” agents for penetration & enhancing financial inclusion

- Role of Agents
  - Cash in/cash out (liquidity issues)

- Legal & Reg Issues:
  - KYC/CDD customers AND Agents
  - What are the contractual touch points?
  - Accept deposit? Mandatory/agency?
  - Labour regulations for agents?
  - Agent Liabilities?
  - Create rules for level playing field
  - Mandate Interoperability between systems?

Æ Enable Transformational banking w/o disrupting banking system & systemic risk

3. Regulatory Coordination

- Issues:
  - Banking supervision and/or payment supervision and/or telecoms supervision etc?

- Legal Rules
  - Make sure regs do not conflict with common law views on banking/payments
  - Legal status of agents & super-agents
  - Use of prepaid e-money/m-money as legal tender?

- Harmony with Telecoms regulations
  - Cost of access to services (SMS/USSD), disclosure
  - Who has jurisdiction?
  - SIM Card Registration & Impact

- Consistency with E-Commerce/AML/Consumer Protection/Privacy Laws
  - Eg Reg E/Z; SA ECT Act; EU E-Commerce Directive; EU Payment Services Directive
  - Need consistency, grandfathering of regs

Æ Currently A Large Probability of Regulatory Arbitrage

International MFS ‘Regulations’

- South Africa:
  - Nov 2009: New SARB e-money paper (bank-led only)
  - Exemption 17/Circular 6 for agents

- EU
  - 2009: Payment services directive
  - 2009: E-money Directive v2

- India
  - New m-banking/payment rules Sep 09 (limited use by MNOs)
  - Sep 2010: MNO Bharti Airtel gets limited MFS license from RBI

- Kenya
  - May 2010: New rules allowing banks(!) to have agents
  - Awaiting publication of new regs on m-payments/m-banking

South Africa

- SA Competition Commission investigation into banking
  - Studies recommended opening up market to non-banks

- MTN Banking, FNB, Wizzit early movers
  - M-Pesa SA just launched through Vodacom(Vodafone)

- SA Reserve Bank require bank-led model
  - MNOs had lobbied for MNO-led, relaxed access/supervision

- Nov 2009: SARB e-money guidance
  - E-Money"monetary value represented by a claim on the issuer. This money is stored electronically and issued on receipt of funds, is generally accepted as a means of payment by persons other than the issuer and is redeemable for physical cash or a deposit into a bank account on demand."

  - Maintains bank-led model

- Anything else is “deposit-taking,” requiring bank license
  - No P2P Transfers allowed its st NPS Act, “as no payment due”
Kenya & MFS

- M-Pesa
  - M-Pesa Pilot on Safaricom 2005
  - Uses Cash In/Out Agents
  - Now 12m+ users
  - Allows P2P remittances and general payments
  - Seen as transactional account, not savings account
  - No Payment Systems Act
  - But not a "deposit" into Kenyan Banking Act as no interest given
- Irony is banks could not have agents into Banking Act
  - May 2010 - m-kesho system: Banks can use m-pesa agents
  - Interoperable to other Banks, NPS
  - Interest now paid on balances

India & MFS

- Circular 25 Jan 06
  - Allows banks to appoint MFIs & post offices as business correspondents for small deposit-taking
- General Rules [June 2008, Dec 2009]
  - Definition: "Mobile Payments" = information exchange between a bank and its customers for financial transactions through the use of mobile phones. Mobile payment involves debiting/to a customer's account on the basis of a funds transfer instruction received over the mobile phone.
  - Only licensed and supervised banks with physical presence in India
  - Restricted to bank accounts/credit card accounts KYC/AML compliant
  - Banks can use "Business Correspondents"
- New Rule Sep 2010
  - Bharti Airtel just received a licence from the RBI to launch MFS
  - "Semi closed wallet"
  - Allow users to exchange physical cash for virtual money which can be stored on mobile phones to pay for goods or services worth less than 5,000 rupees ($108).

Philippines & MFS

- High penetration of m-transaction usage
  - Particularly remittances
- GCash/GXI MFI
  - Uses agents for cash In/out
  - Banking/Payments controlled by Central Bank
- CB wants to limit risk of GCash
  - Daily, monthly transaction caps
  - Low cap on amount uses may leave in their account
  - GCX must submit monthly reports on its activities, although solvency not monitored
  - GCX holds net proceeds in licensed banks
- Circular 471 KYC
  - Agents must register with CB
  - Maintain records for 5 years

General Regulatory & Legal Conclusions

- No ready available supra-national answers to regulations
  - But regulators are meeting regularly to find answers [GSMA etc]
  - Can use EU, CPSIS, BIS, CGAP etc as guidelines
- Regs must be done at a country-specific level
  - Local exigencies
  - Common Law harmonisation
- Apply risk-based proportionality to regulation
  - Necessary & sufficient regulation
  - Don’t stifle innovation

Questions?

Thank You

Leon Perlman
LLB MSc
Chairman, WASPA
www.waspa.org.za
leon@waspa.org.za

High penetration of m-transaction usage

4. Proportional Regulation

- ISSUE: Regulation should be proportional to the extent of a risk.
  - Regulation impacts cost of implementation
  - MFI license classes/restrictions
- Consumer Protection/Security
  - Apply standard AML, KYC processes & rules?
  - Regulatory latitude to conduct lower-value transactions without KYC etc
  - Apply standard conflict resolution rules?
- Taxation
  - How will transactions be treated wrt GST, VAT, CGT etc?
  - Agency commissions
- Forex Rules
  - Remittances rules
  - Use of prepaid mobile airtime as remittance?
5. Interoperability

- **Allow Walled gardens?**
  - WG means consumers can only use exclusive payment gateways
  - Users cant send from one system/MNO to another
  - Bigger (bank/Visa/Mastercard or MNO) brands saturate market, exclude others
  - No ubiquitous P2P across brands and borders
  - Creates “islands of excellence”
  - WG may be necessary at initial phases of MFS launches, but may stifle general growth & ultimately increase costs

- **Challenge for regulators**
  - Reduce cost of cross-brand/WG transactions
  - Allow interoperability at edge of system
  - Grow market without penalizing early innovators
  - Control systemic risk of large number of participants
  - Avoid mandating specific technology & transaction solutions