COMMENTS OF THE ALLIANCE FOR FINANCIAL INCLUSION (AFI) ON THE DRAFT UPDATED CORE PRINCIPLES FOR EFFECTIVE BANKING SUPERVISION

AFI represents 86 central banks and other financial sector policymaking institutions from 82 global south jurisdictions. The membership of AFI can be viewed here: [Members | Alliance for Financial Inclusion (afi-global.org)](). For purposes of this consultation on the draft updated core principles, the AFI Management Unit consulted with the membership via the Global Standards Proportionality Working Group (GSPWG), a platform comprising 59 of the AFI member institutions that provides technical support to developing and emerging country policymakers to implement global standards for financial stability (e.g. the Basel Framework) and financial integrity (e.g. Financial Action Task Force Recommendations) proportionately and without unintended negative consequences for financial inclusion. Our comments are divided into (a) general comments and observations on updated Core Principles (b) the opportunity to link the implementation of the core principles to financial inclusion outcomes (c) specific additional textual suggestions.

(a) General Comments on the updated Core Principles

AFI supports the updating of the Core Principles, noting that the last substantive update was in 2012, and that there have been significant developments since in respect of the digitalization of financial services; increasing diversity in the financial sector including non-bank financial institutions; and the recognition of the need to integrate environmental and climate risks into financial stability frameworks.

Sound prudential regulation and supervision is a precondition for financial stability, itself a key foundation for financial inclusion by enhancing trust and confidence in formal financial institutions, particularly important in times of global uncertainty and economic shocks. In this sense the implementation, and assessment, of the core principles globally, provides an important foundation to build more inclusive financial systems, as well as more stable ones. In turn, as the BCBS has previously recognized, "financial inclusion can introduce potential benefits to the safety, soundness and integrity of the financial system".[1]

AFI particularly welcomes the continuing emphasis on the importance of applying proportionality in the application of the Core Principles "to reflect jurisdictions' circumstances and supervisory capacity", and also notes and welcomes the complementary 2022 BCBS guidance on proportionality, which aligns to AFI's body of work to advance peer learning on proportionality in practice in the application of global standards.

[1] BCBS: Guidance on the application of the Core Principles for Effective Banking Supervision to the regulation and supervision of institutions relevant to financial inclusion (2016), p.1

AFI also welcome both the updating of the core principles to reflect the need to consider climate related financial risks, whilst also acknowledging that "both banks and supervisory practices may consider climate-related financial risks in a flexible manner, given the degree of heterogeneity and evolving practices in this area".[2] In the view of the AFI membership, this is particularly important given the potential for overly stringent, or insufficiently tailored, standards to negatively affect jurisdictions and vulnerable populations already disproportionately impacted by the adverse effects of climate change.

(b) the opportunity to link to financial inclusion outcomes

Given the interrelationship and complementarity of high-quality banking supervision, financial stability, and financial inclusion, we note that the revised core principles do not make any specific reference to financial inclusion goals or outcomes. Whilst appreciating that the focus of the document is on supervisory standards, there may nonetheless be an opportunity to more explicitly acknowledge this interrelationship and complementarity. This is particularly important given:

- the universal nature of the core principles, applicable "to all banks in all jurisdictions", including many global south jurisdictions for whom financial inclusion is an important national policy priority, often driven by central banks and supervisory authorities;
- the opportunity for continuity with past BCBS work to identify the complementarity and interrelationship of its work with financial inclusion outcomes, particularly the 2015 Range of Practice in the Regulation and Supervision of institutions relevant to financial inclusion, and the 2016 Guidance on the application of the Core Principles for Effective Banking Supervision to the regulation and supervision of institutions relevant to financial inclusion;
- the strong influence of the Core Principles, given their utilization as a key global standard within Financial Sector Assessment Programs (FSAPs).

In this regard, there appear to be several opportunities in the text of the revised Core Principles where the interrelationship with financial inclusion goals and outcomes could be acknowledged:

(i) In the Foreword to the Core Principles (p7), and particularly the statement that *"the Committee issues the Core Principles as its contribution to strengthening the global financial system"*, there is an opportunity to highlight the complementarity and reinforcing nature of financial stability, financial integrity, and financial inclusion, each of which are supported and bolstered by high quality supervision underpinned by global standards;

(ii) In the discussion on proportionality, and particularly the statement on p.9 that *"the objective of proportionality is not to dilute the robustness of standard but to reflect jurisdictions' circumstances and supervisory capacity"*, there is an opportunity to highlight the importance of proportionality as a means to mitigate

[2] BCBS Consultative Document: Core Principles for Effective Banking Supervision (2023), p.11

the risk of unintended consequences, such as financial exclusion, arising from implementation of the standards;

(iii) in the discussions of the digitalization of the financial system, and particularly the highlighting (p.11) that "new products, new entrants and the use of new technologies present both opportunities and risks for supervisors, banks and the banking system", it could be highlighted that digital innovations – such as mobile money, agent banking and e-wallets - have been a key driver of greater inclusivity in the global financial system, bringing more than 1.5 billion adults into the formal financial system since the last revision to the Core Principles in 2012.[3]

(c) Additional specific comments

- AFI supports the statement (p.22, 30.6) that *"Effective crisis management frameworks and resolution regimes help to minimise potential disruptions to financial stability arising from banks and financial institutions that are in distress or failing"*. In this regard particular emphasis could be given to the extension of crisis management and resolution regimes to non-bank financial institutions which can be identified as having reached a systemic scale, and which may in some cases lack the protections and legal frameworks in place for the banking sector. This is particularly important given the role that NBFIs may play in extending access to the financial system to previously unbanked consumers.

- In discussion of "supervisory tools and instruments" (e.g. p.77, 99.13), and particularly in the context of the document's broader highlighting of the effects of digitalization, it may be beneficial to highlight the role of supervisory technology applications such as those which have enabled real-time and higher quality data reporting by both banks and non-bank financial institutions, to their supervisory authorities.[4]

- AFI welcomes the updating of the Core Principles "to better align requirements with the latest Financial Action Task Force (FATF) recommendations" (p.5), and particularly support for "risk based Customer Due Diligence (CDD)" (p.68, 40.66), the correct application of which has been recognized by the FATF as being important to avoid unintended consequences arising from its standards. In this regard, in the ensuing list of 'essential criteria' in addition to highlighting the essential nature of 'enhanced due diligence on high-risk accounts', it could be similarly considered to highlight the essential nature of 'simplified due diligence on low-risk accounts'. This would be in line with the risk-based approach of FATF, and consistent with its recognition that the 'optional nature of simplified measures' may deter national authorities from their correct application.[5]

[3] See for example World Bank: The Global Findex Database 2021 (2022) https://www.worldbank.org/en/publication/globalfindex

[4] See for example AFI: Regulatory and Supervisory Technologies for Financial Inclusion (2022)

[5] FATF: High-Level Synopsis of the Stocktake of the Unintended Consequences of the FATF Standards (2021)