

# ROYAL MONETARY AUTHORITY OF BHUTAN

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## REGULATIONS FOR BRANCHLESS BANKING IN BHUTAN

# 1 Introduction

## 1.1 Background

In view of the limited access to financial services compounded by a low market penetration in Bhutan, the RMA has initiated various measures to institute legal and regulatory changes to support new technology-based products and services and enable increased outreach. The RMA's objectives to secure extension of financial services to the poor and unbanked clients shall be met through the establishment of Branchless Banking Financial service providers (BBFSP). Such services will not only supplement the banking system in Bhutan but would also promote financial inclusion by providing cheap, reliable, efficient financial services to the unbanked communities of Bhutan.

**Branchless Banking (BB)** means the delivery of the financial services outside conventional bank branches using information and communication technologies and non-bank retail agents.

## 1.2 Objectives

The objectives of these Regulations are:

- To define BB activities as a delivery channel to offer financial services in a reliable, efficient and cost effective manner.
- To broadly outline activities that can be provided by a BBFSP.
- To serve as a set of minimum standards of data & network security, Know Your Customer policy (KYC), customer protection and risk management to be followed by the BBFSP desirous to offer BB services.

## 2 Ownership and Capital Requirement

A BBFSP shall be a company incorporated under the Companies Act of Kingdom of Bhutan 2000, with a minimum paid up capital of Nu.20,000,000 (Ngultrum Twenty Million) which shall be increased to Nu. 50,000,000 (Ngultrum Fifty Million) within a period of five years after its operation.

In case of a FDI only a BB service provider will be permitted to provide BB services in partnership with domestic companies.

In terms of ownership limits the FDI partner shall be allowed only up to 49% of the total paid up capital.

### 3 Permissible Branchless Banking Models and Activities

These regulations are based on the two models of **BB – Bank Based** and **Non-Bank Based**. A **bank based model** is one under which every customer has a direct contractual relationship with a prudentially licensed and supervised financial institution—all though the customer may deal exclusively with a retail agent who is equipped to communicate directly with the bank.

In the **non-bank based model**, customers have no direct contractual relationship with licensed financial institution. Instead, the customer exchanges cash at a retail agent (or otherwise transfers, or arranges for the transfer of, funds) in return for an electronic record of value. This virtual account is stored on the server of a nonbank, such as a mobile operator or an issuer of stored-value cards. The balance in the account can be used for making payments, storing funds for future use, transferring funds, and converting back to cash at agents.

### 4 Permissible Distribution Channels

BBFSP shall be allowed to provide their services through the following channels:

(i) It can be implemented by using different agency arrangements between the BBFSP, Bank and Telco/non-bank and any other similar service providers as may be approved by RMA.

(ii) Besides, other distribution channels like post office, FCB Agents, Telephone booth operator, grocery shops/super market, Head of Cooperatives, retired teachers and other entities as may be approved by RMA.

### 5 Permissible Activities

Under these regulations, following products and services may be offered directly or indirectly by the BBFSP.

- (i) **Opening and maintaining a BB Account.** A *BB* account can be opened and operated by a customer with a bank through the use of BBFSP channels. Banks may associate such account to a centralized branchless banking unit in its head office. Opening of such account shall be permitted upon the fulfillment of the requirement with regard to CDD and KYC procedures as outlined under the relevant section of this regulation
- (ii) **Account-to-account Fund transfer:** Customers may transfer funds to/from their *BB* account from/to their other pre-registered accounts (current/saving bank

accounts, loan limit accounts, credit card accounts etc.)

- (iii) **Person-to-person Fund Transfers:** Customer can transfer funds from/to their *BB* or regular account to/from *BB* or regular accounts of same or some other bank (depending on the model capabilities) or to mobile numbers of other non-*BB* account holders.
- (iv) **Cash-in and Cash-out:** Customers may deposit and withdraw funds to/from their *BB* account using a variety of options including bank-branch counters, ATM machines and authorized agent locations. Such recipients need to become a *BB* account holder after completion of formalities to utilize these funds. The message (SMS) of funds transfer to such recipients should always be generated by the FI and must contain necessary procedural details to be followed by the recipient in order to utilize those funds. The recipients should also be able to utilize these funds for making utility (electricity, gas, phone/mobile phone) payments without becoming formal *BB* account holder.
- (v) **Bill Payments:** can be used to pay utility bills (e.g. Gas, Electricity, Phone etc.)
- (vi) **Merchant Payments:** can be used to make payments for purchases of goods and/or services.
- (vii) **Loan processing/disbursement/recovery follow up:** BBFSP may facilitate collection and processing of loan application and disbursement of small loan amounts to their borrowers having *BB* accounts. The same accounts may be used by customers to repay their loan installments. The BBFSP, can also follow up for recovery of loans.
- (viii) **Remittances:** Can be used to send/receive remittances inside and outside Bhutan, subject to existing regulations. To the extent possible BBFSP shall use the RMA's payment system particularly National Electronic Fund Transfer System(NEFTS), NECS (Debit) and NECS (Credit).
- (ix) **Other Payments:** Can be used to facilitate any other transactions like: receiving dividend, receiving pension payment and any other third party payments.

However only services under serial (i,ii,iii & iv) shall be offered only by BBFSP directly, where as other services may be permitted directly by agents/distribution channels of BBFSP.

## **6 Customer Due Diligence and KYC norms (Bank based model)**

In order to facilitate the outreach of *BB* to the unbanked poor without undermining the requirements of AML/CFT, all BBFSP are required to fully comply with the CDD and the KYC policy outlined below:

### **KYC requirements:**

- (i) Filling and signing an account opening application form.
- (ii) Photo copy of National ID card/pass port/labor permit and other legal documents.
- (iii) A biometric finger scan and a digital photo taken by a BBFSP to be submitted to the bank and the RMA on a regular basis.
- (iv) The maximum balance limit in the BB account (debit/credit) shall be limited to Nu. 50,000.
- (v) The maximum transaction limits (debit/credit) shall be Nu. 20,000 per day and Nu. 60,000 per month and Nu. 350,000 per year.

Besides the above BBFSP must ensure that their transaction processing system is capable of:

- (i) Imposing above limits to avoid any breach.
- (ii) Sending alerts to the users if they are close to a limit (These regulations do not suggest that the banks must send such alerts. However, the capability needs to be there.)
- (iii) Identifying suspicious transactions and to report the same to the FI's and the RMA.
- (iv) BBFSP clients shall have the option to view at least the last 10 transactions free of cost. The BBFSP shall provide printed statement of account (for a period not more than past 12 months) by paying a nominal fee.

## **7 Customer Due Diligence and KYC norms (Non-Bank Based)**

Under the NBB model the BBFSP shall require its customer to open a virtual account which is stored on the server of the BBFSP.

### **KYC requirements:**

- (i) Filling and signing of application form

- (ii) Photo copy of National ID card/pass port/labor permit and other legal documents
- (iii) a digital photo taken by a BBFSP
- (iv) The maximum balance limit in the virtual account (debit/credit) shall be limited to Nu. 25,000
- (v) The maximum transaction limit shall be Nu. 20,000 per day and Nu. 60,000 per month and Nu. 350,000 per year.

Notwithstanding the requirements under section (KYC/CDD) BBFSP are advised to ensure that they carry out suitable due diligence in respect of the entities proposed to be appointed as their agents/ distribution channels and also institute additional safeguards that may be considered appropriate to minimize the agent risk.

## **8 Roles & Responsibility of the BBFSP Management**

(i) The management of the BBFSP shall ensure to safeguard itself against liabilities which might arise out of the actions of its distribution channels, service providers or partners.

(ii) All BBFSP shall establish a management board with a minimum of four members, one from the RMA, one from its correspondent bank which has the highest customer base. This board shall be responsible for strategic decisions effective oversight and compliance and internal control functions to ensure adherence to rules regulations and other guidelines.

(iii) The senior management of the BBFSP shall remain responsible for maintaining an effective system of internal control and for providing active oversight of the agent's activities/functions.

(iv) There shall be a contingency plan to mitigate any significant disruption, discontinuity or gap in agent's function, particularly for high-risk areas.

(v) The written engagement contract or service level agreement with the third party service provider/agent shall, at a minimum:

- a) Define the rights, expectations and responsibilities of both parties;
- b) Set the scope of, and the fees/revenue sharing structure, the work to be performed by the agent;

- c) State that the outsourced services are subject to regulatory review and that RMA inspecting officers shall be granted full and timely access to internal systems, documents, reports, records and staff of the agent;
- d) State that the third party service provider/agent will not perform management functions, make management decisions, or act or appear to act in a capacity equivalent to that of a member of management or an employee of the BBFSP;
- e) Specify that the third party service provider/agent must ensure safe-keeping of all relevant record, data and documents /files for at least five years; or alternately, such record is shifted to the BBFSP at regular pre-specified intervals which will then ensure safe-keeping of this record for at least five years.
- f) State that all information/data that the third party service provider/agent collects in relation to branchless banking services, whether from the customers or the FI or from other sources, is the property of the BBFSP, and the entity will be provided with copies of related working papers/files it deems necessary, and any information pertaining to the institution must be kept confidential; and
- g) Establish a protocol for changing the terms of the service contract and stipulations for default and termination of the contract.
- h) Mention suitable limits on cash holding by agents/distribution channels as also limits on individual customer payments and receipts.
- i) State the requirement that the transactions are accounted for and reflected in the BBFSP books by end of day or next working day.

## **9 Agent Due Diligence (ADD)**

(i) All BBFSP shall have clear, well documented ADD policy and procedures approved by the RMA. Amongst others these policies and procedures shall include minimum agent selection criteria.

(ii) Due diligence agent checks to be performed at specified intervals and a list of early warning signals and corrective actions to ensure proactive agent management. ADD should clearly specify roles and responsibilities of various functions in the BBFSP with regard to agent management.

(ii) Adequate publicity on the agent in the locality that he/she is going to serve supplemented by appropriate measures to avoid him/her being misrepresented

about the intermediary engaged by them as Agent and take measures to avoid being misrepresented.

(iii) Appropriate AML/CFT monitoring process to be complied by the agents.

(iv) All BBFSP shall execute and submit a service level agreement/ agency agreement and any amendments thereto, detailing the functions/activities to be performed, the respective responsibilities of the BBFSP and its third party service provider/agent and a confidentiality clause. The arrangements with the agents/distribution channel shall specify:

a) Suitable limits on cash holding by agents/distribution channel and also limits on individual customer payments and receipts

b) The requirement that the transactions are accounted for and reflected in the BBSFP books by end of the day or next working day and

c) All agreements/contracts with the customer shall clearly specify that the BBSFP is responsible to the customer for acts of omission and commission of the agents/distribution channel.

(v) BBFSP shall engage agents who are well established enjoying good reputation and having confidence of the local people.

## **10 Use of Third-Party Service Providers**

Third-party service (TPS) providers shall provide services related only to technological infrastructure etc. A proper service level agreement (as defined in Section 7 (v) ) must be put in place for all third-party service arrangements.

## **11 Risk Management Program**

BB entails various categories of risk, and therefore all BBFSP must have in place proper risk management program to measure, monitor and address risk at an appropriate level.

All BBFSP providing non bank based branchless services shall open accounts in commercial banks in Bhutan in its own name. This account shall be used for pooling and depositing the customer funds. An internal policy of matching the value in BBFSP virtual accounts on a one-to-one basis with funds deposited in its bank accounts shall be done on a regular basis.

BBFSP shall be liable to each client for the outstanding e-money in the clients account.

All BBFSB shall deposit in an escrow account with the RMA a sum of money equivalent to 50% of the total value of transactions in a month. However for a new BBFSP the

initial deposit shall be Nu.1, 000,000 which can be invested in the RMA approved securities.

All transactions pertaining to this account shall be permitted upon the approval of the RMA.

## **12 Adoption of appropriate technology**

(i)BBFSP shall adopt the most appropriate technology while implementing the BB service,

(ii) All BBFSP shall adhere to the applicable regulations of the RMA as and when intimated in writing by the RMA.

(iii) BBFSP providing non-bank BB services shall be required to fulfill the following requirements:

(a) an electronic money profile containing information on technical specification as well as e-money management mechanisms,

(b) first year business projections,

(c) proof of legal instrument readiness (i.e., concepts of the written key agreements with partners),

(d) proof of operational readiness (e.g. an organizational structure plan and equipment and business facility plan),

(e) proof of liquidity risk management readiness,

(f) an information technology audit from an independent auditor,

(g) a disaster recovery plan,

(h) identification of product risk and other risks like operational, legal, and reputational risks, and

(i) a description of the accounting information system to be applied to the e-money issuance.

## **13 Customer Protection**

BBFSP must have in place appropriate customer protection against risks of fraud, loss of privacy and even loss of service to establish trust among consumers as trust and customer confidence is the single most necessary ingredient for growth of *BB*. Besides in view of the

fact that BBFSP will be dealing with a large number of first time customers with low financial literacy level, they need to ensure that adequate measures for customer protection, awareness and dispute resolution are in place.

All BBFSP are required to fulfill the following criteria:

- (i) To provide adequate financial education to all their clients with regard to the services provided by them.
- (ii) To provide a list of all their distribution channels including their services on their website and on an annual basis in the media.
- (iii) To ensure the privacy & confidentiality of customer information in the custody or possession of the BBFSP.
- (iv) To have in place appropriate grievance mechanism, that should be widely published and also placed in their website.
- (v) The details should be displayed at the premises of their distribution channels and also be made available by the BBFSP at the request of the customer.
- (vi) All service charges on account of delivery of BB Service directly or indirectly should be approved by the RMA. This service charges should be reasonable and be made available on the premises of the distribution channel on a notice board visible to the customers.
- (vii) Agents and persons working on behalf of the BBFSP shall be prohibited from charging any fee to the customers directly for services rendered by them on behalf of the BBFSP.
- (viii) All charges/fees to be paid/received by any party involved in the BB business directly or indirectly shall be fixed at reasonable rates and be approved by the RMA.
- (ix) BBFSP shall develop suitable training modules in the local dialect, in order to provide proper attitudinal orientation and skills to their agents/distribution channels.
- (x) Customers may also be given the option of obtaining loss insurance. However, the voluntary nature of this insurance must be clearly communicated to the customer.

ICT solutions that ensure proper authentication and other security measures may be adopted to minimize the risk while scaling-up the models as already advised. Further BBFSP may ensure that while appointing the above entities as agent, distribution channels,

the fundamental principles that the individuals are residents of the area in which they propose to operate as agent/distribution channels, stands fulfilled.

## **14 Branchless banking setting up procedures**

### ***14.1 Preparation***

Only authorized BBFSP can provide Branchless Banking services as stipulated in these regulations. The authorization shall be given upon fulfillment of the requirement under this regulation.

### ***14.2 Authorization procedure***

BBSFP desirous in providing BB services shall submit to the RMA, an application describing the services to be offered and its infrastructure. The application shall be accompanied by a certification signed by proposer to the effect that the proposed BBFSB has complied with the minimum pre-conditions requirement as provided in this regulation.

A non-refundable application fee of Nu. 50,000 (Ngultrum Fifty Thousand) in cash/draft/cheque shall be deposited in licensing/registration account maintained with the RMA and shall be used for expenses incurred for licensing of such providers.

A licensing processing committee shall be formed comprising of members from the following organizations:

- FRSD, RMA
- Representative from Ministry of Economic Affairs ( Registrar of Companies)
- Representative from Commercial Bank
- Representative from Telecom Company

## **15 General on-going requirements**

(i) All BBFSP shall report to the RMA on regular basis information pertaining to their transactions. Besides, the BBFSP shall also provide the financial statements on a yearly basis. This statement shall include at the minimum the balance sheet, P&L statement & the summary of transactions.

(ii) All BBFSP shall be subject to on-site inspection and off-site supervision as deemed necessary by RMA.

(iii) All BBFSP are required to appoint/open distribution channels/agents in at least in two gewogs of each Dzongkhag, within the first two years of operation.

(iv) All relevant officers and employees of BBFSP who are directly involved in the cash

operation must undergo the training in AML/CFT regulations conducted by the RMA. Subsequently, they must train their agents/distribution channels on a continuous basis

(v) All BBFSP/agents/distribution channels must:

- For each remittance (inward as well as outward) complete a KYC/CDD process on the sender /receiver which entails an application form and presenting a government issued identity document along with two passport size photograph/digital photo.