General Council for Islamic
Banks And Financial Institutions

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CIBAFI

المجلس العام للبنوك
والمؤسسات المالية الإسلامية

مؤسسة منتمية لمنظمة التعاون الإسلامي
تأسست بمرسوم ملكي رقم ٢٣ لسنة ٢٠٠١م

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Jaime Caruana
General Manager
Basel Committee on Banking Supervision
Bank for International Settlements
CH-4002
Basel
Switzerland

Dear Mr. Caruana,

CIBAFI response to the Basel Committee's Consultative Document "Sound Practices: Implications of fintech developments for banks and bank supervisors"

The General Council for Islamic Banks and Financial Institutions (CIBAFI) presents its compliments to the Basel Committee on Banking Supervision (BCBS) and takes this opportunity to express its appreciation of the work that the BCBS is doing to provide sound practices for the implications of fintech developments for banks and bank supervisors.

CIBAFI is an international body representing Islamic financial institutions globally, who offer financial services and products complying with Islamic rules and principles (Shariah). CIBAFI acts as the voice of the Islamic finance industry, and has a membership of over 120 banks and non-bank financial institutions, both large and small, from 32 countries and jurisdictions.

We welcome this opportunity to offer our comments and recommendations on the BCBS's Consultative Document (CD) "Sound Practices: Implications of fintech

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developments for banks and bank supervisors". The comments contained in this letter represent the views of CIBAFI Secretariat and feedback received from our members.

Firstly, the CD sets out five scenarios for the way the banking industry may change, ranging from one in which existing banks adopt new technology to improve their services (but customer relationships remain essentially unchanged), to one in which banks become essentially irrelevant, as customers interact direct with individual financial services providers, who may include new entrants (such as peer-to-peer platforms) and globally active technology players. CIBAFI believes that, while major banks in the most developed countries may be able to adapt to most of these scenarios, and will themselves have a role in determining which will occur, this is less obviously so for smaller banks in less developed countries. Most Islamic banks are of this kind, and there are questions whether they have the ability, knowledge, and resources for such changes, albeit that these may arrive more slowly than in more technologically advanced countries. The new technologies do, however, have some positive aspects, not only for financial inclusion. One example is that the traceability, auditability, and accountability features associated with blockchain may help banks in ensuring compliance with Shariah.

Secondly, the BCBS implicitly recognises that fintech firms may have a greater impact in some markets than others. The suggestion is that in less developed banking markets, and particularly where financial inclusion is relatively low, new entrants may be able to use technology to reach consumers who have no, or limited, existing banking relationships. However, although many Islamic banks operate in less developed and low financial inclusion markets, for Islamic banking in particular, the threat of new entrants is smaller due to the Shariah compliance requirements. It is thus possible that the preferred model will be for Islamic banks to collaborate with fintech firms to enhance financial inclusion.

Thirdly, the CD lays emphasis on the need to maintain Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) controls in fintech enabled transactions, though it recognises the assistance that some new technologies, including artificial intelligence may offer. CIBAFI believes that the AML/CFT issues may have

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greater impact on Islamic banks that intend to use fintech solutions, since many Islamic banks are in countries that are regarded as sensitive from an AML/CFT standpoint. The technology to manage AML/CFT will thus be particularly important to these banks.

Fourthly, even though the CD mentioned many risks associated with fintech engaged activities, Islamic banks may have other risks and issues arising from the need to address Shariah compliance. They will need to consider how they can ensure that the end to end transactions are in line with Shariah, including the rights and ownerships at each stage. They will also need to consider not only whether there is a valid contractual relationship between the parties involved, but how that relationship is to be characterized in terms of Islamic financial jurisprudence.

Fifthly, while Recommendation 9 deals with licensing regimes, including the question of when fintech firms should be licensed as banks, CIBAFI considers that there is more work to be done here. Important issues scarcely mentioned here include the application of capital adequacy regimes to such firms, and their treatment by insolvency regimes (including, for example, the protections offered to their customers). Both are likely to depend on how the firms are characterized for regulatory purposes.

Sixthly, although the CD deals, in Recommendation 7, with the human resources and skills that will be necessary in supervisors, it says less about the skills that will be needed in banks to assess and manage the new technologies. While larger banks have in general invested heavily in such skills, it cannot be assumed that smaller banks, of the kind that CIBAFI largely represents, will have done so.

Seventhly, although there is some discussion of business continuity issues, notably under Recommendation 4, one specific question is at what point it is appropriate for business continuity requirements to be placed on fintech firms themselves, especially when they are supplying services to banks. If a firm supplies services to multiple banks, it may not be appropriate for this simply to be dealt with by each bank separately as part of its outsourcing policy.

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Finally, our members have pointed out that more comprehensive researches might be needed to assess the macro level effect of fintech, the effect on economy, financial stability, and the way the central banks may still influence the economy via the monetary and other policies. There may also be tax issues, including whether tax regimes provide incentives or disincentives for fintech firms. We recognize that the issues mentioned in this paragraph lie outside the responsibility of the BCBS, but hope that it will draw the need for such work to the attention of those who do have competence in these areas.

We remain at your disposal should you need any further clarifications on the above.

Yours sincerely,

Abdelilah Belatik
Secretary General

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