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MIGRANT MONEY

Regional Harmonization of Remittance Policies in the Intergovernmental Authority on Development (IGAD)

SOMALIA POLICY DIAGNOSTIC REPORT

February 2023

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ABOUT THIS REPORT

This is a diagnostic report for Somalia as part of a wider project on harmonizing remittance policies in the Intergovernmental Authority on Development (IGAD) region, prepared by the United Nations Capital Development Fund (UNCDF) and the IGAD Secretariat, with the objective of improving the IGAD countries' current and ongoing policy and regulatory framework development and other initiatives relating to remittances.

The United Nations Capital Development Fund makes public and private finance work for underserved communities in the world's 46 least developed countries. With its capital mandate and instruments, UNCDF offers last-mile finance models that unlock public and private resources, especially at the domestic level, to reduce poverty and support local economic development. UNCDF's digital agenda for migration and remittances falls within the organization's broader corporate strategy, set forth in 2019, of Leaving No One Behind in the Digital Era. On the other hand, the Intergovernmental Authority on Development (IGAD) is a regional economic community (REC) created by its Member States—Djibouti, Eritrea, Ethiopia, Kenya, Somalia, South Sudan, Sudan, and Uganda—to enhance regional cooperation in three priority areas of food security and environmental protection, economic cooperation, regional integration, and social development, peace and security. The founding leaders of IGAD were motivated by a vision where the people of the region would develop a regional identity, live in peace, and enjoy a safe environment alleviating poverty through appropriate and effective sustainable development programmes.

Remittances can act as a catalyst for sustainable development at the individual, household, community, and national levels as a source of greater disposable income for migrant families that can lead to increased consumption and investment. The size and scale of global remittances create the possibility of harnessing these flows through digital channels toward productive investment in health, education and local businesses, thus contributing to the long-term development of countries around the world. An effective policy and regulatory framework that balances innovation and risk will be critical to this transition from cash to digital.

This diagnostic report has been prepared through a desk research review of relevant policies, laws and regulations, followed by extensive stakeholder consultations and benchmarking with relevant countries' initiatives, policies and regulatory frameworks. The authors of this report have prepared a roadmap with a country-level mapping of possible enablers, inhibitors and policy options. It is recognized that implementation of the roadmap requires further engagements with the regulatory and policymaking bodies to determine what options can be taken up.

ACRONYMS

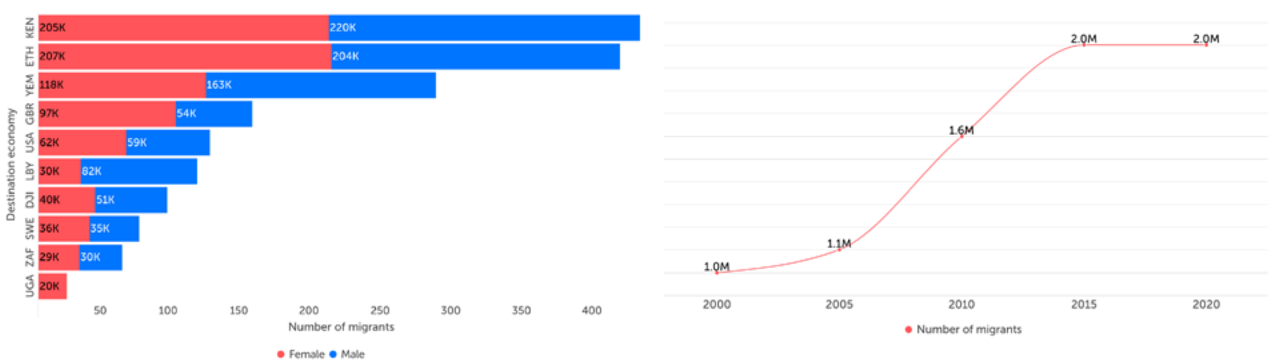
ACH	automated clearing house
AML/CFT	anti-money laundering/combating the financing of terrorism
API	application programming interface
ATM	automated teller machine
CBS	Central Bank of Somalia
CDD	customer due diligence
EFT	electronic funds transfer
EFTPOS	electronic funds transfer at point of sale
e-KYC	electronic know your customer
FATF	Financial Action Task Force
GDP	gross domestic product
IGAD	Intergovernmental Authority on Development
ISO	International Organization for Standardization
KYC	know your customer
MFI	microfinance institution
MFS	mobile financial services
MNO	mobile network operator
MTB	money transfer business
MTO	money transfer organization
NGO	non-governmental organization
NID	national identification
NPS	national payment system
POS	point of sale
PSP	payment system provider
QR code	quick response code
RSP	remittance service provider

RTGS	real-time gross settlement system
SIM	subscriber identity module
UNCDF	United Nations Capital Development Fund
USSD	unstructured supplementary service data

COUNTRY CONTEXT

Somalia is the fifth-highest country of origin for forcibly displaced people worldwide.[1] Somalia is significant as a country of origin for mixed migration in the Horn of Africa. Conflict, insecurity, poverty and drought have led to massive emigration, especially over the last two decades.[2] As Somalia has become relatively more stable in recent years, return migration has increased. A lack of infrastructure and livelihood opportunities may result in returnees re-migrating.[3] Little research exists on Somalis' labour migration or migration to Somalia. Somalis have opened businesses and small shops in Ethiopia, Kenya, South Africa, and Uganda, earning them a reputation for their entrepreneurial abilities. In Yemen, they work as farmers, herders, and traders. Somalis also work as casual and domestic workers in the IGAD region, Yemen, the Gulf countries, and the Middle East. Moreover, according to the seasons, pastoralists move across borders in the region to trade and find pasture and water for their livestock.[4] Labour migration to Somalia is limited due to insecurity. According to the Somali Ministry of Labour and Social Affairs, there are approximately 25,000 migrant workers in Mogadishu, some of whom are regular migrants with work permits. Many of these migrant workers originate from the IGAD region and the Middle East. War in Syria has brought Syrian migrants to Somalia, some of whom are highly skilled and work in the health sector.

Figure 1: Migrant stock in destination economies - Top countries 2021



Source: KNOMAD-World Bank and UNDESA, https://www.un.org/development/desa/pd/content/international-migrant-stock (Accessed on 16 September 2022)

KEN=Kenya, ETH=Ethiopia, YEM=Yemen, GBR=United Kingdom, USA= United States of America, LBY=Libya, DJI= Djibouti, SWE=Sweden, ZAF=South Africa, UGA=Uganda, DEU=Germany, CAN=Canada, NOR=Norway, NLD=Netherlands, EGY=Egypt

1 United Nations High Commissioner for Refugees, Somalia: 1–30 June 2018: Fact sheet, https://reporting.unhcr.org/sites/default/files/UNHCR%20Somalia%20Fact%20Sheet%20%20-1-30%20June%202018.pdf. (Accessed on 16 September 2022)

2 International Labour Organization, *An Assessment of Labour Migration and Mobility Governance in the IGAD Region: Country report for Somalia* (2020), www.ilo.org/wcmsp5/groups/public/---africa/---ro-abidjan/---sro-addis_ababa/documents/publication/wcms_743318.pdf. (Accessed on 16 September 2021)

3 Katrin Marchand, Julia Reinold and Raphael Dias e Silva, Study on Migration Routes in the East and Horn of Africa, pp. 3–4 (Maastricht Graduate School of Governance, 2017). (Accessed on 16 September 2021)

4 William Avis and Sian Herbert, Rapid Fragility and Migration Assessment for Somalia: Rapid literature review (Governance and Social Development Resource Centre, University of Birmingham, 2016). (Accessed on 16 September 2021)

Political economy

Remittances are money transfers sent by migrants to their family members or other loved ones back in their country of origin.[5]

The World Bank reported that in 2021, the migrant remittance inflows were US$1,735 million, which is 23.5 percent of the gross domestic product (GDP).[6] High unemployment rates, including youth unemployment[7] and a fragile national economy, create a dependency on remittance flows, especially at the household level. Remittances and Somali migrants have played a key role in Somalia´s economy. Remittances are mostly used for household, education, and healthcare purposes and investment in the Somali economy. However, the remittance sender becomes vulnerable if he/she loses his/her job, becomes unwell, etc.

Money transfer businesses (MTBs) remain the most vital channels sustaining the flow of remittances into the country. Remittance flows from Europe and the United States have been influenced in recent years by changes in banking regulations and security procedures that have impacted MTOs and the cost and access to money transfers. The 2014 Financial Institutions (Money Transfer Business Registration) Regulations govern remittance services in Somalia. Remittance services to Somalia have also been severely impacted by bank de-risking. It is becoming increasingly difficult for MTBs to open bank accounts, even though they are a prerequisite for them to operate. This is due to bank de-risking, defined by the Financial Action Task Force (FATF) as financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk in line with the FATF's risk-based approach. The reputation of MTBs suffered from the 9/11 attacks, after which the US Government terminated the activities of Al-Barakaat, an RSP serving the Somali community.[8]

Therefore, it came as no surprise that, at the peak of the pandemic during lockdown restrictions, liquidity became an issue for this corridor. For this reason, MTBs were forced to implement limit restrictions on the value of transactions per sender until liquidity was restored.

While the Somali remittance industry used to be heavily reliant on cash, mobile money penetration is very high in Somalia, with mobile operators often partnering with MTBs to offer money transfer services.

By increasing supervision and compliance, Somali regulators are constantly working to improve the national regulatory framework for MTBs and mobile money services. The MTB system, also called *hawala*, is widely used as a trusted and affordable means of sending and receiving money, even in remote parts of Somalia.

5 https://migrantmoney.uncdf.org/wp-content/uploads/2021/09/4-FAQs.pdf (Accessed on 16 September 2022)
6 KNOMAD, *Remittances Data*, https://www.knomad.org/data/remittances.
7 In 2019, unemployment rate was estimated at 11.4 percent and youth unemployment rate was estimated at 17 percent. See International Labour Organization, Employment Programs and Conflicts in Somalia (2019). (Accessed on 15 September 2022)
8 Veronica Studsgaard and Melissa Erisen, The Somali Remittance Ecosystem: Developments and their social impact (2021), *The International Association of Money Transfer Networks*, www.iamtn-network.org/reports. (Accessed in February 2022)

Remittance landscape

MARKET

Banks: The Central Bank of Somalia (CBS) has licensed 13 banks to conduct banking business. All these banks are operational.[9]

Microfinance institutions: The Somalia microfinance industry is currently unregulated. There is no legal framework for MFIs, but they are operating. The CBS has implemented a board-level resolution that outlines the requirements for registering an MFI. MFIs have started to apply for registration certificates. The Financial Institutions Law of 2012 currently only recognizes commercial banks and MTBs as financial institutions but has been amended to include MFIs and is due for approval by the parliament.

Mobile network operators (MNO): The licensed mobile network operators (MNOs) in Somalia are Dalkom, Golis Telecom, Hormuud Telecom, Nationlink, Netco, Somafone, Somtel, Telcom Somalia, Telesom, Somlink, and Thuraya. So far, four MNOs (Hormund, Somtel, Somlink, and most recently Golis) have received licenses to offer mobile money services and have partnered with banks to create financial products. Hormudd Telecommunications has partnered with Salam Somali Bank to provide EVC plus mobile money, SomLink has partnered with the International Bank of Somalia (IBS) to provide the E-Besa product, and Somtel has partnered with Dahabshil bank to provide E-Dahab.

Non-bank remittance service providers: Somalia has 12 licensed MTBs in Mogadishu.[10] MTBs specialize in international remittances, which constitute their core business. MTBs also offer domestic money transfer services for a fee, but this business has mainly been taken over by domestic mobile money services, which handle these transactions for free.

PAYMENT INFRASTRUCTURE

Payment system: The Central Bank of Somalia (CBS) is mandated to provide oversight of the country's national payment systems. The CBS is making significant progress in implementing the Somalia Transaction and Reporting System "STARS". STARS provides interbank payments and clearing for licensed banks and comprises the Real Time Gross Settlement (RTGS), the Automated Cheque Clearing House (ACH), and the National Payment Switch. The RTGS and ACH were launched in 2021. However, the National Switch is yet to be launched. The ACH is primarily used for monthly bulk payments of public servant wages, and the average monthly transactions are close to $70,000. All licensed banks are also participating in the RTGS and the Central Bank. International Standards have been taken into consideration during the implementation of STARS, for example, the adoption of BIC Codes, ISO 20022 messaging standards, the use of a Virtual Private Network (VPN) between STARS and other systems needed for integration, settlement account, and a reserve account. STARS is open between 8 a.m. and 4 p.m. However, the RTGS has a 24hr uptime.

The CBS has a core banking system and an enterprise resource planning (ERP) system that supports other bank functions and is integrated with the core banking system. Other integrated systems include the Integrated Financial Management Information System (IFMIS). Security-wise, the systems conform to ISO/IEC 27001. Regarding ownership, the RTGS and

9 Central Bank of Somalia, *Licensed Banks*, https://centralbank.gov.so/licensed-banks/. (Accessed on 10 March 2023)

10 Central Bank of Somalia, *Licensed Money Transfer Businesses*, https://centralbank.gov.so/licensed-money-remittance-providers/ . (Accessed on 16 September 2021)

ACH are fully owned by the CBS. The National Switch is a Public Private Partnership (PPP), with the government owning 51 percent, and the private sector (Commercial Banks) owning the other 49 percent. Banks are authorized to connect directly to the RTGS. Non-banks are not restricted to connecting directly to STARS. However, the practice has been to encourage non-banks to work with banking institutions, providing indirect access to the RTGS. The commercial banks are also provided with a back-office system integrated with the CBS Core Banking System.

Personal identification cards: Somalia does not have a single national identification (NID) card but rather several fragmented identity initiatives, including the Benadir ID card, Puntland ID, passports, local electoral lists, and Somali national registration. The key challenges Somalia faces in establishing a national identity system include a lack of trust in the system by citizens, the lack of any legislation regarding personal data protection, high cost, and a lack of interoperable systems. The existing payment infrastructure is not integrated with identity systems, thus making it costly for customers to open accounts and use financial services.

Automated teller machines and point-of-sale terminals and cards: Banking networks, transaction infrastructures, such as those for automated teller machines (ATMs) and electronic funds transfer at point of sale (EFTPOS), or other networks of agents are not very extensive, especially in rural areas, creating a physical access problem for many receivers. Most RSPs are located in Mogadishu.

PRODUCTS

There is a lack of accurate data on the remittance environment of Somalia and no data on products available to Somali migrants beyond being able to send and receive money through MTBs. As only about 15 percent of Somalis have bank accounts, the main financial intermediaries for sending money are MTBs. MTBs allow Somalis to send money more safely compared to informal transmission methods without armed groups' interference. These businesses provide a vital service and care deeply about the well-being of their customers.[11]

11 Veronica Studsgaard and Melissa Erisen, *The Somali Remittance Ecosystem: Developments and their social impact* (2021), The International Association of Money Transfer Networks, www.iamtn-network.org/reports. (Accessed in February 2022)

ROADMAP

The assessment and stakeholders' consultations have resulted in developing remittance-related enablers, inhibitors, and recommendations for reform. Enablers are factors that contribute to the enhancement of remittance flows, while inhibitors are factors that restrict efficient remittance flows. Recommendations are options to improve the current enabling policy, regulatory, and payment infrastructure environment to increase remittance flows. All of these have been categorized under five key areas:

i. **Legal and regulatory framework**: This includes options for reform relating to authorities, roles, responsibilities, and mechanisms for coordination, including legal and regulatory factors that support cross-border remittances.

ii. **Financial and payment system infrastructure**: This includes options for reforming policies, standards, and rules related to national payment systems, improving the network of access points, promoting access to interoperable systems and platforms, and establishing national ID systems that support e-ID and ID requirements adjusted on a risk basis.

iii. **Market practices**: This includes options for reforms supporting cross-border remittances, especially on a foreign exchange regime that provides clear guidance and mechanisms to capture remittance-related data at the transaction level, as well as data analysis and sharing.

iv. **Consumer protection**: This includes options for reforms related to data protection, privacy, and confidentiality for remittance-related data and relevant components of consumer protection laws that guide consumer protection and complaints resolution mechanisms for financial services, including cross-border remittances.

v. **Cooperation and collaboration**: This includes recommendations on establishing mechanisms and processes to foster coordination between different stakeholders, including through memoranda of understanding and bilateral (or multilateral) agreements; public-private collaboration mechanisms on matters related to the development and implementation of cross-border remittance policies; harmonization of laws and regulations; and establishment of regional bodies to coordinate regional initiatives, and mechanisms for coordinating and implementing policy issues at the regional level. This aspect includes leverage and consistency with other regional and subregional instruments and institutions.

Tables (a)-(e) present enablers, inhibitors, and recommendations for reform across the five key areas listed above.

(a) Legal and regulatory framework

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
A draft National Payment System (NPS) Act is in place, awaiting to be passed by parliament. Subsequently, two regulations that will tentatively be used have been drafted out of the Act. These are the Regulations on Payment Services 2021 and Regulation on Oversight and Operations of Payment Systems regulations 2021.	Somalia has no regulatory framework governing the national payment system establishment, licensing, and operations. MTBs are unable to connect to the NPS. Lack of correspondent bank relationships due to de-risking. "*If we had correspondences/ international banking with banks abroad, it would be easier for MTBs to deposit their money and settle their dues in those accounts abroad. But since the international banks have de-risked and no longer accept that cash, our MTBs thus offset and settle in Dubai. Cash is carried physically.*" – CBS staff	The CBS can fast-track promulgating the NPS regulatory framework. The legal framework of the NPS can allow non-bank MTBs to access payment systems. It can improve the efficiency of the retail payment system by increasing competition, potentially lowering costs, and broadening the set of alternatives open to end-users. Non-bank RSPs can contribute expertise that the banks lack and cooperate with the banks to provide innovative services such as mobile payments. The CBS may consider improving existing payment arrangements to support the requirements of the cross-border payments market, aiming at attaining straight-through processing, aligning processes, and increasing the operation hours across systems.	Short-term: can be implemented within one year
The CBS has established a board-level resolution outlining the requirements for registering an MFI. MFIs have started to apply for registration certificates.	Somalia lacks a regulatory framework for MFIs.	The CBS can promulgate a law regulating MFI businesses in the country. Regulation and supervision may help create an enabling environment for establishing specialized formal financial institutions that provide financial services to underserved communities. They may also encourage MFIs to offer a wide range of products, including domestic and international remittances, and foster standardization and transparency in the sector.	Short-term: can be implemented within one year

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
The 2016 AML/CFT Act, Article 5, provides customer due diligence (CDD). The law recognizes the need for risk-based know-your-customer (KYC)/CDD.	There are no guidelines for proportional CDD to the specific risks of the remittance services. A lack of proportionate risk management levels can also help avoid barriers to new entrants or unwarranted burdens on lower-risk MTBs and remittance activities. There are no established guidelines for e-KYC.	The CBS can introduce guidelines for proportionate CDD to implement the existing anti-money laundering/combating the financing of terrorism (AML/CFT) law on risk-based customer supervision so that the market players do not place an unwarranted burden on lower-risk MTBs. Consider guidelines that will clarify that compliance with AML/CFT obligations in the law does not require financial institutions to refuse, or terminate, business relationships with entire categories of customers that they consider presenting a higher overall money laundering/terrorist-financing risk. The guidelines can also allow for e-KYC to help women and men migrants and their families to open bank accounts remotely in their country of origin. The central bank can introduce guidelines for conducting outreach and education for risks covered under AML/CFT regulatory frameworks. The guidelines can provide for outreach and educational programmes to raise awareness between the entities and the wider community of the risks associated with money laundering and the financing of terrorism and proliferation and to avoid prohibitive implementation of some legal clauses.	Short-term: can be implemented within one year
The Financial Institution Law No. 130 of 2012 provides a basis for regulating MTBs.	Lack of a comprehensive regulatory framework for MTBs. Lack of risk-based capital for MTBs. All MTBs are required to maintain performance security of US$ 60,000 regardless of the size and scope of operations.	The CBS can consider adopting a consistent legal approach for licensing and authorization of non-bank MTBs. This may mean amending the existing Financial Institutions (Money Transfer Business Registration) Regulations. Consider regulatory frameworks based on proportionality that provides for the requirements for licensing, or procedures to obtain registration or approval for conducting remittance business, mode and scope of operations, consumer protections and dispute resolution mechanisms, market conduct, adequate disclosure, transparency, reporting requirements, handling of AML/CFT issues, etc. The CBS can consider introducing risk-based capital for non-bank RSPs in the regulatory frameworks based on risk and scope of operations. Non-deposit taking RSPs usually provide only a minority of a sender's overall payment needs and do not require the application of heavy prudential requirements, as the failure of an RSP is unlikely to cause systemic risk. The CBS can consider introducing mutual recognition criteria in the regulatory frameworks. A certain level of confidence may be placed in the partner state's regulatory regimes such that minimum requirements for operation and supervision are put in place for establishing branches and subsidiaries from partner states. In this case, a licence issued by a central bank in one of the partner states is recognized by the CBS supervisory authorities. The licensed RSPs can be allowed to operate in all partner states upon simple notification to the supervisory authority of the host state. Supervision of the RSP can be mutually agreed upon among the Member States with a preference toward supervision by the migrant's country of origin or shared by the migrant's country of destination and origin.	Short-term: can be implemented within one year

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
CBOS encourages self-regulation for MTB agents. The regulation on Money Transfer Business Operations, 2015, states that Money transfer businesses may conduct their services through agents, in line with the regulation. It also guides who can qualify as an agent.	Lack of comprehensive agent regulations.	The CBS may consider introducing an agent regulation to specifically define activities that can be carried out by an MTB agent, provide a framework for offering agency business services, including registration requirements and conditions, and set minimum standards of customer protection and risk management for the conduct of agency business service, etc. The agent regulations can allow MTBs to use MFIs' outlets to provide their services and financial service providers to use non-financial service providers' agents for service provisions. The regulation can expressly discourage MTBs from imposing exclusivity conditions on agents, thus fostering competition (i.e., the regulatory framework should allow universal agent categorization). Universal agent categorization helps to identify efficient cash-in and cash-out services across all payment service providers (PSPs). Agent networks are critical in linking providers and customers. There should be room for a universal agent model for bank and mobile money users through an interoperable agent network platform. Agent regulations can be part of the MTB Regulation.	Short-term: can be implemented within one year
Fintech in the payment space is steadily growing in the financial sector within the region.	There is a lack of regulatory framework for fintech that allows market participants to test new financial services or models with live customers, subject to certain safeguards and oversight, to support digital innovations and fintech. The CBS capacity constraints to support the remittance market and the slow regulatory approval rate weakens innovation.	The CBS can consider having regulatory sandboxes in place to encourage market entry. This regulatory and authorization framework supports experimentation, test-and-learn and deployment processes. It is a temporary experiment of innovative financial products, services, and business models or delivery mechanisms in the NPS ecosystem. This framework can provide a conducive environment for innovation in payment services while ensuring that the protection of consumers and public interest is upheld. The aim is to introduce new service offerings targeting fintech, and innovation among existing MTBs and, subject to a detailed review, consider the need to widen the scope of players who can be authorized to participate in the NPS ecosystem to increase competition and choice. The CBS can also monitor the market to determine trends in fintech and financial innovation (e.g., the growth of mobile money in Somalia to determine which ones to encourage).	Medium-term: can be implemented within 2-3 years

(b) Payment Infrastructure

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
Release of the mobile money regulations amended in 2020. Mobile money is preferred to cash due to the high circulation of fake money in the market. Three MNOs are licensed to engage in mobile money operations and have partnered with banks to create financial products.	Mobile money providers face several challenges, including inadequate interoperability, network coverage, availability, power, and security. Implementing separate infrastructure to cater to MFS from other retail payments presents additional or duplicate costs. Likewise, maintenance costs of the separate infrastructure increase recurring costs.	The CBS can consider implementing an integrated infrastructure interoperable with mobile network operations. Consider fostering collaboration between mobile money providers to reduce the cost of improving the infrastructure. An example is shared telecommunication infrastructure.	Long-term: can be implemented within a period of 3 years or longer
Implementation of a national retail payment switch infrastructure is underway, which was envisaged to go live in the second half of 2022. Having a national payments switch will support last-mile retail infrastructure such as ATMs, POS, QR Codes, etc. In addition, once completed, the switch will be interoperable with mobile money.	Somalia is yet to implement the national payment switch that could facilitate interoperability and provide for an efficient clearing and settlement platform of digital financial services transactions for all payment service providers, with less cost.	The CBS can improve the payment infrastructures by developing retail payment systems that cover wide geographical areas. Fast-tracking introduction of the national switch could be one of the steps forward. The retail payment systems may also include new infrastructures. They may champion efforts to encourage institutions with extensive branch networks and/or de facto local monopolies (e.g., post offices, major retailers) to offer multiple services, including remittance services, where appropriate. This can reduce risks and costs associated with using cash and cheques and support the central banks' interest in achieving financial inclusion with all geographic regions and income groups. The CBS can consider integrating the RTGS and retail payment systems. The remittances will be efficient and well-functioning when the RTGS, retail payment, and settlement systems are well-integrated and allow interoperability with mobile money. Establishing a national switch can help non-bank RSPs access the payment systems through the switch.	Medium-term: can be implemented within 2-3 years

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
The National Communications Authority is in the process of drafting policies and guidelines relating to cyber security. The Somalia Computer Emergency Response Team/Coordination Centre (SomCERT/CC). The SomCERT/CC was formed to respond to Cybersecurity incidents. In case of system failures, this and Business Continuity guidelines will improve confidence in adopting digital or formal channels for remittances.	Cyberattacks on all infrastructure, including payment systems, threaten confidence in the payments ecosystem. A lack of harmonized and coordinated cyber reporting undermines the collective efforts to implement sufficient safeguards. System failures and channel downtime associated with digital payment instruments cause delayed payment, thus affecting consumers' willingness to use digital payment services and increasing account dormancy and dominance of cash, especially for low-value retail payments. Customers lack adequate assurance that payments will reach the intended recipients at the right time, reducing their willingness to use digital payment services.	The CBS can introduce guidelines for cyber security reporting for the members of the different payment systems. The cyber-reporting framework is the first step for collective efforts and sharing of experiences necessary to implement sufficient safeguards. A standard security framework, ISO/IEC 27001, can be adopted, similar to what the CBS implemented internally. The CBS can consider introducing guidelines for business continuity plans for banks and other members of the RTGS and future national switch. The guidelines should also make business continuity plans mandatory for all PSPs. This includes requiring RSPs and MTBs to put in place appropriate governance and risk management practices to improve the safety and soundness of remittance services and help protect consumers.	Long-term: can be implemented within a period of 3 years or longer

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
There is some interoperability achieved with card schemes. Mobile Network Operators have bilateral agreements in place for interoperability. Partial interoperability has been established as non-banks are not restricted from connecting directly to STARS. However, the practice has been to encourage non-banks to work with banking institutions.	There is limited last-mile distribution infrastructure to support retail payments. Even where the infrastructure network exists, it is partially interoperable with other domestic retail payment systems such as mobile money, and is mainly concentrated in the towns and cities such as Mogadishu.	The CBS can consider issuing guidelines on improvements in transaction infrastructures through the adoption of common and internationally agreed standards for messaging (ISO 20022). The CBS can consider introducing guidelines to harmonize API protocols for data exchange across payment infrastructures to enable more efficient payment data and digital identifier exchange in cross-border payments. Such action could help achieve improved coverage and reduce the cost to end-users of remittance services. The guidelines could encourage technology providers to provide standard API to enable other players to develop interoperable applications. Developing a payments system by establishing a national switch and automated transfer system will help integrate RTGS and ACH functionality onto a single platform with seamless links between the CBS, commercial banks, and mobile money. Later, mobile money should be integrated with the national retail payments switch. These developments will open the opportunity to interconnect the country to international payment schemes (such as Visa and Mastercard) and international MTOs from a single payment platform.	Long-term: can be implemented within a period of 3 years or longer
Somalia has several fragmented identity initiatives, including the Benadir ID card, Puntland ID, Passports, Local-based electoral lists, and Somali national registration. Plans by the commercial banks are underway to work on a financial/ digital ID that can be used in the financial sector.	The existing payment infrastructure is not integrated with identity systems, thus making it costly for customers to open accounts and use financial services. The lack of a national ID and robust identification system makes it hard and costly to securely identify beneficiaries, a major prerequisite for gaining access to digital forms of payments. The inability to promptly confirm the beneficiary's identity causes delays and increases costs.	The ID databases need to be standardized and digitized. Digital ID is paramount to increasing the adoption of formal financial services. Identifying specific policy interventions to boost the implementation and usage of digital ID is critical to its role as an enabler for remittance services as it supports effective identification and onboarding of customers/user segments, facilitates authentication and verification of cross-border transactions, facilitates effective AML/CFT supervision of cross-border transactions and expands the digital footprint of the underbanked to enable their access to a broader range of financial services. Where necessary, legislation related to privacy and data protection should be implemented. Integrate the ID systems with the payment infrastructure. Once the ID system is improved, the payment infrastructure can also be enhanced to integrate with digital identity systems. Access to CDD information will play a significant role in lowering the risk perception of persons and reducing the cost of compliance.	Long-term: can be implemented within a period of 3 years or longer

(c) Market aspects

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
The CBS acknowledges the importance of financial literacy and public awareness for the payment system stakeholders. Currently, they conduct financial literacy training in-house and for commercial banks.	Low financial and digital literacy levels for women and men Somalis affect their ability to use digital payments. This is further exacerbated by complex and non-intuitive steps to effect payments, thereby inhibiting the use of digital payment services. (National adult literacy rate in Somalia is 5 percent, where the literacy rate for men is 7 percent and 4 percent for women.[12]) Customers also lack the financial literacy to identify and compare alternative remittance services. This significantly limits the accessibility of remittance services, even if the market is potentially competitive. MTBs lack knowledge about the market, such as the market size in key corridors. With little knowledge, they regard remittances as unattractive because senders typically have relatively low incomes. Therefore, senders find that some services (such as those based on bank accounts) are not readily available. Some migrants are unaware that they must seek appropriate identification to access certain services, particularly when they do not have the relevant documents.	The ministries responsible for foreign affairs can hire a liaison officer who will communicate with and inform the diaspora and the associations of women and men migrants on the one hand, and the administrations involved in the promotion of investment in the country on the other hand. They should also liaise with RSPs of interest to their country to disseminate literacy courses. The liaison officer can prepare public education and awareness programmes, particularly for women and men migrants. The education seminars should cover customer-journey mappings, such as steps involved in sending remittances, pre-departure opening of a bank account and/or mobile wallets to be used by the remittance recipients, electronic cards security and other important features such as safety, practicality and ease of use, and available financial products. The education and awareness initiative should involve the central banks, informing how various payment mechanisms and products can easily be accessed. The liaison officer should coordinate with embassies and consulates to participate in developing databases, including names, jobs, and contacts. Online communication and virtual meetings can be organized to strengthen proximity with migrants in the long term and to better understand their concerns and expectations. Networking with non-governmental organizations and associations of women and men migrants abroad will ensure a better channelling of remittances to projects in their country of origin. The liaison officer can also develop online tools. This makes it possible to network migrant skills abroad to mobilize them for advice, expertise, and remittances to their country of origin. The liaison officer can encourage the entry of new operators into the remittance space. One of the easiest ways to lower transaction costs is to encourage the entry of new legitimate operators in a given corridor and to inform migrants about their ability to choose among existing remittance-transfer mechanisms. This supports increased competition among MTBs, thereby improving efficiency and lowering costs.	Medium-term: can be implemented within 2-3 years

12 https://data.worldbank.org/indicator/SE.ADT.LITR.ZS?view=chart&locations=SO

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
The CBS Act Law No. 130 of 22 April 2012, Section 32, mandates the government to decide on the system (floating, fixed, or any variation thereof) that shall apply for establishing the value of the Somali shilling in relation to foreign currencies (the foreign exchange regime).	The lack of effective monetary policy has caused local currency to be very volatile and fluctuate rapidly against foreign currencies. Consequently, the exchange rates are set by members of the business community and the economy is dollarized. Lots of Somali currency in the market is counterfeit. The lack of a monetary policy encourages remittances to be channelled through unregulated channels that have unpredictable exchange rates and present risks to consumers and the financial system. These unregulated channels can be linked to money laundering, financing of terrorism, human trafficking, and other abuses. Even when no criminal activity is involved, informal channels deprive governments of a clear understanding of their inbound and outbound currency flows, distorting the accurate picture of their balance of payments.	The CBS can consider allowing market-driven exchange rates while remaining on top by introducing sound monetary policies that stabilize the local currency. These measures may foster the flow of remittances through formal and regulated channels and encourage market operators to develop new services and remittance products. In addition, the government will achieve greater transparency, which brings about an enhanced ability to combat money laundering and financing of terrorism. It may be helpful for the CBS to address issues around restrictions on international financial transfers with counterpart countries to determine a more secure and trusted way forward.	Long-term: can be implemented within a period of 3 years or longer
Existence of some partnership arrangements between banks and international money remittance agents that allow the inflow of remittances.	Other than some attempts to incentivize diaspora deposits by offering higher interest rates, there are no migrant-centric products and services that are attractive to women and men migrants for them to be motivated to send money to their country of origin. The lack of migrant-centric products results in low uptake and usage of digital remittance services.	The government, philanthropists, and the private sector, including fintech, can adopt a broader view of how to tap financing for development through remittances by designing various appropriate products that will attract women and men migrants. Women and men migrants' direct investment is potentially valuable. Financial institutions can also develop a broader range of investment products targeting migrant investors, such as basic low-cost payment accounts and services for retail clients, diaspora micro-savings bonds, endowment accounts, pension schemes, and insurance policies, which could then be used for remittances. The findings of the 2016 Somali Diaspora Investment Survey Report, which sets out priority sectors for diaspora investment, closer private sector collaboration, and strengthening/enacting trade/investment law that supports diaspora investment, can be enhanced, and financial products can be based around the findings of the report.	Short-term: can be implemented within one year

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
The government collects some data on remittances. MTBs are expected to submit monthly and quarterly reports that state the volumes of their transactions. The data is received in Excel spreadsheets via email.	No data collection system exists (no International Transaction Reporting System (ITRS)). Data is reported at an aggregated level with information on the country of origin and remittance inflow/outflow on a monthly basis. The data is not used to assist in formulating and implementing policy responses. The Central Bank of Somalia does not collect or estimate any data on remittances sent/received via informal channels.	Develop a remittance transaction reporting system for remittance data collection, analysis, monitoring, and use. This will involve assessing the already existing central bank data collection systems and developing a platform to define appropriate remittance data architecture, data collection and repository systems, data measurement and analytics processes, and data monitoring and use. Reliable data on remittances is key to enhance the accuracy and completeness of balance of payment data, to effectively manage issues related to AML/CFT compliance, to understand the true impact of remittances on the economy, and to form more effective policies for managing remittances, including policies to incentivize their contributions to the economy. Remittance data collection, analysis, monitoring, and use are important for decision-making processes relating to remittance services. Consider collecting gender-disaggregated data. This will ensure that the unique needs of women and men migrants are considered during decision-making. At a later stage, consideration could be given to working with national statistics offices and related ministries (e.g., trade, investment, labour, and foreign affairs) to develop a more nuanced understanding of remittance receipts and usages, through the administration of surveys. Efforts should also be made to understand the scope, usage, and impact of informal remittances on the domestic economy.	Short-term: can be implemented within one year

(d) Consumer protection

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
There are regulatory frameworks in Somalia that are related indirectly to consumer protection, such as Section 111 of the Financial Institutions Law No. 130 of 22 April 2012, which provides for the confidentiality of all information of customers. The regulation on Money Transfer Business Operations 2015 states that any money transfer business shall disclose the fees, charges or commissions to their clients and other conditions applicable to the money transfer business offered. It also states that any money transfer business shall establish an effective, readily accessible mechanism for consumers to file complaints The central bank requires MTBs to have customer care and complaints policies that cover the fees and charges/commissions involved. They report on these to the CBS, on these aspects.	There is still a lack of transparency by MTBs, which does not disclose the total price, speed of the service, and exchange rates to be used. To know the total price of the transfer, the sender needs to know the exchange rate to be used. The practice at the moment is that different MTBs use different exchange rates, which also vary from day to day. There are provisions in various laws, for example, the licensing regulation on complaints handling mechanisms for consumers. Still, it is unclear and complex due to various laws touching on consumer protection issues and the lack of enforcement mechanisms. Furthermore, no recourse mechanism has been purposely built for digital channels. An overlap in the legal mandates of different financial consumer protection authorities can lead to inconsistent and ineffective supervision. There is no harmonized financial consumer protection framework to ensure that data and money are well secured during cross-border transactions, especially in cybersecurity and data protection.	The CBS could develop a harmonized financial consumer protection framework to ensure that data and money are secured and to foster consumer trust and confidence. These guidelines, which would apply to all MTBs licensed, registered and supervised by the corresponding authorities, would protect and empower senders and recipients of remittances, especially in the key areas of (i) cybersecurity; (ii) data protection and privacy; (iii) complaints management; (iv) transparency and disclosure; (v) float and agent liquidity management; and (vi) financial education and customer awareness. • Cybersecurity: Cybersecurity policies will protect users and data, enabling users to enjoy frictionless and safe money transactions. • Data protection and privacy: Legal frameworks can clarify and strengthen data protection regulations, especially from financial and payment data perspectives. This should include how financial, payments and other digital payment data are collected, held, stored, accessed and shared, as well as pertaining to ownership and intellectual property rights, if any, and consumer consent and protections. The overall objective should ensure that payment data are used safely and securely to enhance users' privacy and customer-centricity. • Complaints management: The guidelines can provide for complaint-handling mechanisms and refund procedures. Guidelines should require RSPs to develop a complaints management plan, including the establishment of (i) a separate unit responsible for digital finance and remittance payments; (ii) a manual of operations that clearly explains how consumer complaints are addressed and reported, with clear responsibilities for each step of the process; and (iii) appropriate communication channels to address inquiries and complaints from digital finance and remittance consumers. If the complaint is not resolved to the customer's satisfaction, an out-of-court alternative dispute resolution (ADR) mechanism can provide further options for recourse. • Transparency and disclosure: The guidelines could require proper disclosure at the advertising, shopping, pre-contractual and contractual stages (upon request), in line with Principle 3 of the G-20 High-Level Principles on Financial Consumer Protection, which states "all financial consumers should be treated equitably, honestly and fairly at all stages of their relationship with financial service providers". Guidelines should also require RSPs to provide information about any other relevant aspects of their service, such as: (i) the ability, if any, of the sender to revoke the transfer after it has been paid for; (ii) whether the RSP will inform the receiver when the funds are available; (iii) information about the rights of the consumer in the event of any problems (e.g., dispute or error resolution); (iv) the customer's ability to transfer products or services to another provider with reasonable notice; and (v) contact information. • Float and agent liquidity management: The guidelines can also consider introducing a code of conduct on float management because this is an implicit charge. Its effect is that the remittance service is slower, and the intermediary entity earns interest income from the funds. • Financial education and customer awareness: RSPs could establish financial education programmes for remittance consumers to raise awareness of basic information about remittance products and services, including charges and fees. The CBS could rationalize its financial consumer protection legal frameworks by ensuring that the entities responsible for financial consumer protection have clear mandates, sufficient capacity and expertise, and effective mechanisms for coordination and collaboration with internal and external stakeholders.	Medium-term: can be implemented within 2–3 years

(e) Cooperation and collaboration

Enabler(s)	Inhibitor(s)	Recommendation(s) for reform	Timeframe
Somalia has memberships in various regional and international fora, including membership to IGAD, Community of Sahel-Saharan States (CENSAD) and COMESA.	Unharmonized policies, laws and regulations related to cross-border remittance across regional blocks. Lack of cooperation on AML/CFT measures on cross-border remittance flows among member countries in the region, including sharing information.	The CBS can consider harmonizing remittance regulations within the IGAD region and other corridors. It can be challenging to use regional payment systems if the regulation in each participating system is not harmonized or if operating standards are different. Trade arrangements and financial liberalization commitments, especially those linked to the operation and licensing of financial entities, including MTBs, can be built upon. Somali ministries, departments, and agencies can evaluate actions to collaborate in connecting or enhancing domestic and cross-border regulatory cooperation. This could be done by assessing the existing arrangements and challenges, creating building blocks of a response to improve the current regional cross-border remittance arrangements, and putting forth a roadmap of practical steps (with time frames) needed to achieve harmonization. An intended outcome is increased efficiency, affordability, and security of intraregional and cross-border fund transfers. Given the importance of remittances to the Somalia economy, and the limitations arising from international transfers related to the West, it may be useful for Somalia and the IGAD Member States to work out optimal mechanisms that work for Somalia, IGAD, and their Western partners.	Short-term: can be implemented within one year

KEY TAKEAWAYS AND NEXT STEPS

Somalia is implementing developments that include regulatory frameworks such as the NPS Act and the board-level resolution to guide the microfinance sector. The central bank is making efforts to develop a vibrant remittance market. UNCDF and the IGAD Secretariat have provided a comprehensive diagnostic review and consultations on the specific and fundamental question of optimizing migrant remittances. We recognize that the various recommendations also require various levels of effort and timeframes to implement.

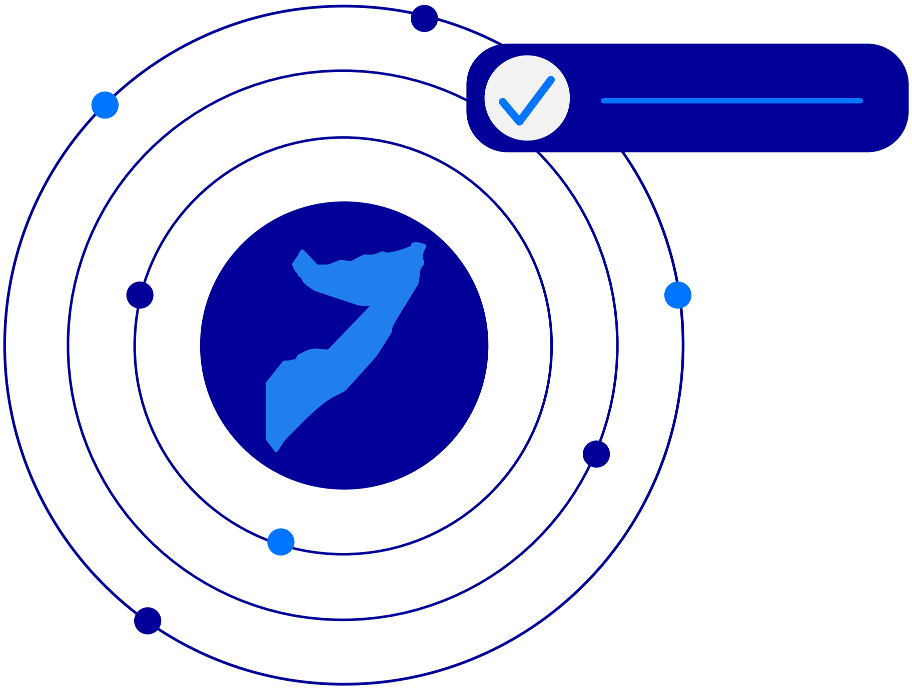
We look forward to reviewing this report in detail with key Central Bank of Somalia and Government stakeholders and identifying opportunities where UNCDF can provide specific support going forward. Along with consultations to review this report's contents, UNCDF and the IGAD Secretariat will keep Somali stakeholders up-to-date about the comprehensive work we will be pursuing around migration and remittances. That work includes:

- **Demand-side research**: Despite digital solutions' great potential to improve the lives of migrants and their families, both access and uptake remain a challenge. Many migrants may lack practical access to a digital transaction account (such as a mobile wallet), whether because such services are simply unavailable in the local area where the migrant is working or because the migrant lacks the necessary documentation to obtain such an account, or due to some other external factor. Where access is available, the migrant may lack the necessary digital literacy to know how to register for such an account. Finally, some migrants, even those digitally adept, may not see digital solutions as better than cash-based solutions, which is perhaps not surprising since the use cases for digital remittance channels remain limited to date. Unless human-centred financial product development, focused on the financial needs and mobility considerations of migrants, is responsively designed and supported by the requisite last-mile delivery infrastructure, commercially viable financial inclusion for migrants and their families will not be achieved. The demand-side research thus focuses heavily on human-centred design. We anticipate that the learnings from our human-centred design work will be applicable and valuable to the Somali context.

- **Supply-side research**: Access and uptake of digital financial services, including remittances, requires a robust and inclusive digital finance ecosystem. Such an ecosystem must ensure the active participation of traditional and non-traditional financial service providers to support commercially viable digital remittance channels. The supply-side assessment work is aimed at reviewing the constraints faced by the providers—agent networks, liquidity management, business models, products, and digital infrastructure, among other factors—that currently limit their capacity to advance the usage of digital products.

- **Learning and implementation**: In parallel with the roll-out of the research strategy, UNCDF and the IGAD secretariat will be pursuing an ambitious capacity-building and learning agenda. We are partnering with leading academic and learning institutions to advance our understanding of shared challenges and opportunities about building enabling ecosystems, pursuing evidence-based decision-making, and designing migrant-centric financial products.

Finally, as we begin collaborating with the Central Bank of Somalia to review this report, we also look forward to holistically considering the set of recommendations. The holistic approach is important for several reasons. First, all the work will ultimately support the central bank's efforts to improve remittance flows through regulated channels, thus giving regulators a more accurate picture of the actual balance of payments. At the same time, the work will also advance the financial inclusion of migrants and their families, thus advancing the financial inclusion agenda for the nation as a whole. UNCDF's recommendations in this report form a system; changes to any single factor will likely cascade through that system. Tackling the diagnostic recommendations systemically, rather than looking at individual recommendations in isolation, will make their inter-dependencies and linkages more visible and align with the country's monetary, financial inclusion, and digitalization agendas, and will ultimately create the best path forward.



Impact Capital for Development

MIGRANT MONEY

ABOUT IGAD

The Intergovernmental Authority on Development (IGAD) is one of the eight regional economic communities (RECs) and building blocks for the African Union. IGAD was established in 1996 to supersede the Intergovernmental Authority on Drought and Development (IGADD), which was founded in 1986. The new and revitalized IGAD was launched during the 5th Summit of IGAD Assembly of Heads of State and Government—Djibouti, Eritrea, Ethiopia, Kenya, Somalia, South Sudan, Sudan, and Uganda—held on 25-26 November 1996 in Djibouti. The Summit endorsed the decision to enhance regional cooperation in three priority areas of food security and environmental protection, economic cooperation, regional integration and social development peace and security. The founding leaders of IGAD were motivated by a vision where the people of the region would develop a regional identity, live in peace, and enjoy a safe environment alleviating poverty through appropriate and effective sustainable development programmes.

ABOUT UNCDF

The United Nations Capital Development Fund (UNCDF) is the United Nations' flagship catalytic financing entity for the world's 46 Least Developed Countries (LDCs). With its unique capital mandate and focus on the LDCs, UNCDF works to invest and catalyse capital to support these countries in achieving the sustainable growth and inclusiveness envisioned by the 2030 Agenda for Sustainable Development and the Doha Programme of Action for the least developed countries, 2022–2031.

UNCDF builds partnerships with other UN organizations, as well as private and public sector actors, to achieve greater impact in development; specifically by unlocking additional resources and strengthening financing mechanisms and systems contributing to transformation pathways, focusing on such development themes as green economy, digitalization, urbanization, inclusive economies, gender equality and women's economic empowerment.

A hybrid development finance institution and development agency, UNCDF uses a combination of capital instruments (deployment, financial & business advisory and catalysation) and development instruments (technical assistance, capacity development, policy advice, advocacy, thought leadership, and market analysis and scoping) which are applied across five priority areas (inclusive digital economies, local transformative finance, women's economic empowerment, climate, energy & biodiversity finance, and sustainable food systems finance).

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