



## **Update on Regulation of Branchless Banking in Russia**

**January 2010**

Note: This update of CGAP's 2008 "Notes on Regulation of Branchless Banking in Russia" incorporates research conducted by CGAP in January 2010 regarding relevant legal and policy changes through the end of 2009. It is one of 11 similar country updates produced by CGAP as a part of the work plan of the Access through Innovation Sub-Group of the G-20 Financial Inclusion Experts Group. However, CGAP alone is responsible for its content. Corrections may be forwarded to [yseltzer@cgap.org](mailto:yseltzer@cgap.org).



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### 1. Introduction

Since the fall of the Soviet Union, banks have been the main formal providers of financial services in Russia. However, new developments have emerged in the past several years, including the burgeoning business of payment terminals, operated both by banks and nonbanks. With recent changes in the law, it is expected that payment terminals will continue to dominate branchless banking in Russia. These changes include (i) permitting nonbanks to act as payment agents and to use sub-agents and (ii) providing an exemption from the anti-money laundering/combatting the financing of terrorism (AML/CFT) requirements for payments by individuals of 15,000 rubles or less. Other avenues that had been considered important to the development of branchless banking just two years ago—specifically, mobile banking (via partnerships between banks and mobile phone operators) and Web-based e-money issuers—now have a lower priority. Currently, policy makers are focused on developing a national retail payment card system and the possibility of establishing a post bank. However, if a new law on the national payment system and the regulation of e-money is adopted in the next year as expected, it will significantly change the regulatory landscape, particularly for mobile banking and Web-based e-money issuers.

### 2. Sector Overview

There are over 1,000 banks in Russia (half of which are registered in Moscow and Moscow Oblast) with approximately 3,200 bank branches and over 40,700 bank points of service.<sup>4</sup> The most substantial bank in terms of assets and points of service is Sberbank, which is 60 percent owned by the Central Bank of the Russian Federation (CBR) and has 19,750 points of service. Despite these numbers, even today there are

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<sup>1</sup> The 2008 "Notes on Regulation of Branchless Banking in Russia" was based on an analysis of existing legislation and regulations relevant to branchless banking approaches and on the CGAP research team's insights from interviews with a range of stakeholders. The original diagnostic assessment was carried out under the auspices of CGAP's Technology Program, which is co-funded by the Bill & Melinda Gates Foundation. The Russian diagnostic assessment was one of seven that provided evidence for CGAP & DFID's Focus Note 43, *Lyman, Timothy, Mark Pickens, and David Porteous. 2008. "Regulating Transformational Branchless Banking: Mobile Phones and Other Technology to Increase Access to Finance."* Washington, D.C.: CGAP & DFID, January."

<sup>2</sup> The research involved a review of new laws and regulations and interviews with Mikhail Mamuta (Russian Microfinance Centre), Oleg Ivanov (vice-president of the Association of Regional Banks of Russia, expert of the State Duma of Russia), and Victor Dostov (chairman, [Russian Electronic Money Association](#)).

<sup>3</sup> In September 2009, the G-20 called for the establishment of a Financial Inclusion Experts Group with two subgroups, one of which is the ATI Sub-Group. CGAP is a member of an experts group assembled to assist the ATI Sub-Group in its work, which includes updating information previously published on the policy and regulatory framework for branchless banking in various developing countries.

<sup>4</sup> Bank points of service include banks' credit-and-cash offices, operational cash offices, and additional bank offices (i.e., any office located within a certain distance from the bank's headquarters or any branch).



districts without a single bank branch.

There is also a wide range of nonbank institutions,<sup>5</sup> including payment service providers (PSPs), the Russian Post, urban and rural credit cooperatives, microfinance institutions, mobile phone companies, and Internet-based financial service companies. Given their physical infrastructure, technology, and accessibility, these nonbank institutions are well-positioned operationally to provide a broad range of financial services, though there are still certain legal and regulatory constraints as discussed below.

Due to recent legal developments, it appears that PSPs will take a front seat (for the foreseeable future) in the development of branchless banking. Specifically, in June 2009, the government passed new laws (fully effective 1 April 2010) that permit any legal entity or individual entrepreneur to act as payment agent or bank payment agent and that exempt from AML/CFT identification requirements payments by an individual for 15,000 rubles or less.

A draft law on the national payment system has been deliberated by the government and CBR over the past three years, and it could be introduced into the Duma in early 2010. The draft covers two topics: (i) the regulation of noncash payments (which would cover both bank and nonbank payment systems, such as terminals and possibly e-money)<sup>6</sup> and (ii) special regulation and provisions for the national card (retail) payment system. Because of the magnitude of the business and the opportunity for huge profits, policy makers are keenly interested in the national card payment system and which institutions will be the card issuers and the processing operators. Recently the processing Vnesheconombank–Development Bank (VEB) publicly announced that it is ready to create a national retail payment system, but the idea had not yet been vetted by the Ministry of Finance.

In addition VEB is exploring the possibility of a joint venture with the Russian Post and VEB's subsidiary bank, Svyaz-bank,<sup>7</sup> to establish a post bank with VEB as processor. This venture would produce a bank network twice the size of Sberbank, but there would be an overlap of customers. (Sberbank's customers are primarily low-income and older.)

## **2.1 Banks and Nonbank Payment Terminals and Outlets**

The main opportunity for branchless banking in Russia currently is retail payments, which until recently has been dominated by banks, particularly Sberbank (the largest bank in Russia, majority-owned by CBR). As of October 2009, it is estimated that there were more than 250,000 automated payment terminals (only cash; no card option) and approximately 60,000 additional payment or cash-in outlets (e.g., supermarkets and staffed kiosks). Although some banks have set up their own networks of terminals,<sup>8</sup> a

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<sup>5</sup> In these Notes, the term “nonbank institutions” refers to institutions that are not “credit organizations” as defined in the Banking Law. Credit organizations (banks and nonbank credit organizations) are subject to licensing and other requirements of the Banking Law.

<sup>6</sup> See Section 3.3.

<sup>7</sup> With financial assistance from CBR, in 2008, VEB purchased Svyaz-bank to rescue the bank from collapse. At that time, Svyaz-bank had more than 15 million pensioners' accounts.

<sup>8</sup> Banks are increasingly replacing staffed terminals with automated terminals that offer cash-in services. The reasons for this appear to be relatively high labor costs and the time-consuming process of handling small transactions, which was leading to delays in serving other customers.



significant percentage of terminals are owned and operated by nonbank payment service companies. These terminals offer the possibility to make payments for goods, works, and services as well as taxes and other government fees and dues for transactions of less than 15,000 rubles.<sup>9</sup> Until the June 2009 passage of the new law on payment agents, a large majority of the nonbank terminals operated without an agency agreement with a bank and thus in a legally ambiguous space.<sup>10</sup>

According to estimates, the payment terminals have more than 50 million users across the country and process US\$1.9 billion in retail payments per month in the Moscow region alone.<sup>11</sup> CyberPlat, the largest payment processing system in Russia, has at least 40,000 cash acceptance points that processed 1.4 billion transactions worth US\$6.5 billion in 2008. First Processing Bank (former RIK Bank), has at least 180,000 terminals that processed over 3 billion payments in 2009 using its QIWI payments system. The explosive growth in payment terminals and other outlets is viewed, in part, as a response to two related problems faced by Russian banks: crowded branches and the high costs of setting up a branch. Other factors are also relevant, including the importance of prepaid mobile phones (i.e., the payment terminals can satisfy the significant 24/7 demand for top-ups) and the general paucity of payment options (e.g., Russia does not have a retail checking system).

## **2.2 Russian Post**

An interesting player in the branchless banking space is Russian Post, which earns 46 percent of its revenue from financial services and has a network of 42,000 post offices with 29,500 in rural areas and 12,000 in villages of fewer than 500 people. (By contrast, a majority of bank points of service are concentrated in cities with a population of at least 50,000.) Post offices are used for domestic and—to a lesser extent—international money transfers, for accepting payments, and for paying out pensions to people without a bank account. In 2008, the Post paid out 21.8 million pensions (almost 57 percent of total pension payments in Russia). Together with the payment of federal allowances, the payments made by the Post in 2008 totalled 20.1 billion rubles. Although the Post is not permitted to act as an agent for banks, it does perform a type of money transfer service for individuals for the repayment of bank loans. (In 2007, the amount was estimated at US\$7–8 billion.)

## **2.3 E-Money Issuers**

Web-based “e-money issuers” (a term not yet defined under Russian law) are a significant component of branchless banking. They have signed up large numbers of customers and claim huge and growing transaction volumes. The private actors include

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<sup>9</sup> The Banking Law had, prior to the June 2009 amendment, limited the types of payments bank agents could make (i.e., only payments for utilities, rent, and telecommunications).

<sup>10</sup> Prior to the June 2009 amendment, the Association of Russian Banks and others had argued that payment services could be provided only by a bank or an operator pursuant to an agreement with a bank. Issues such as this were debated in a working group on branchless banking that the Russian State Duma convened in 2007 which brought together representatives of all relevant public bodies, including the Ministry of Information and Communication Technology, the Ministry of Finance, the Ministry of Economic Development and relevant units of the Russian Central Bank.

<sup>11</sup> Turnover in 2009 by these terminals was reported to be over US\$15 billion; with an average 4.5% commission, providers realized revenues of approximately US\$700 million.  
[http://english.ruvr.ru/rtvideo/2010/01/05/video\\_3429704.html](http://english.ruvr.ru/rtvideo/2010/01/05/video_3429704.html)



WebMoney and Yandex, which together have more than 90 percent of the market.

The mechanics of the Web-based e-money issuers are as follows: Customers enter money into the system through banks, cash-in terminals, automated teller machines (ATMs), the postal network, other Web-based e-money systems (such as PayPal), and prepaid cards. Customer may use e-money for Internet purchases, domestic and international money transfers, repayment of consumer loans, utility payments, and other services. For the most part, customers are not identified and, although some of the players state that they require notarized identity documents from customers, it appears that in fact this is only required if the customer is interested in making a transfer to a bank account or withdrawing funds from a bank. (For instance, with WebMoney, except for transfers to and from bank accounts, a customer is assigned a digital number, but there is no assurance that the name entered by the customer is the customer's legal name.) These Web-based e-money issuers have created, to some extent, a parallel settlement system in which customers can transfer electronic currencies with some degree of anonymity.

Currently there is no specific legal provision governing Web-based e-money issuers. (For example, the amendment to the AML/CFT law with respect to payments by individuals through agents isn't applicable because the law doesn't recognize nonbank e-money issuers). However, it is expected that there will soon be e-money regulation (whether it is incorporated as part of the planned law on the national payment system or adopted as free-standing regulation). Partly in anticipation of this development, the leading Russian e-money issuers and others interested in the topic have formed the Russian Electronic Money Association.

## **2.4 Mobile Network Operators**

Although there was great anticipation regarding the potential of mobile banking, the interest of mobile network operators (MNOs) has largely dried up since the change of priorities in 2009 in the Ministry of Telecommunications, which had been a vocal proponent of mobile banking. Today, the main profit center and focus for MNOs is communication services, not financial services. Still, there has been activity from MNOs. First, Beeline, one of the three largest nationwide MNOs, has demonstrated a significant interest in branchless banking. Beeline has teamed with Tavrishesky Bank to offer Beeline customers a prepaid financial product: mobile payment based on the PayCash Payment System.<sup>12</sup> Each Beeline customer opening a PayCash "account" signs an agreement with Tavrishesky Bank pursuant to which the customer agrees to deposit funds for her prepaid virtual PayCash "account" from her prepaid phone account at Beeline into a designated account at Tavrishesky.<sup>13</sup> A customer pays a merchant for goods and services by placing an order with Beeline for the transfer of money to the merchant's Tavrishesky Bank account. (Therefore, each merchant must also enter into an agreement with Tavrishesky Bank.) Customers can also do person-to-person

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<sup>12</sup> In fact, Tavrishesky Bank designed the product with the intention that it will be offered by various mobile operators.

<sup>13</sup> This designated account is a pooled account for Beeline customers. Individual "account" information is held by a processing center, which is a legal entity separate from Beeline and from Tavrishesky Bank. Although each customer must sign an agreement with Tavrishesky Bank, the customer is not required to open a bank account. (The payment instrument used in this scheme is a prepaid payment card issued by Tavrishesky in accordance to CBR Instruction #266-P "On the Issuance of Bank Cards and on Transactions Carried Out with Payment Cards," 24 December 2004.)



transfers between each other's mobile phone accounts, with or without mediation by Tavrishesky. Cash-in is possible through nonbank agents, such as mobile phone payment outlets and payment terminals. There were more than 1 million active users in the fourth quarter of 2009. A similar project was launched by Megafon (a nationwide MNO with approximately 31 million subscribers) in 2009.

Many retail banks enable their customers to manage their accounts via mobile phone. For instance, a project involving Megafon, Sberbank, and Visa International—called Verified by Visa—offers the possibility of making payments from one's bank account in Sberbank via a mobile phone and is referred to by the sponsors as “a mobile wallet for electronic purchases.”

## **2.5 Moscow Social Card**

In 2001, a joint project among the Bank of Moscow, the Moscow Government, and Visa developed the Moscow Social Card. This card is one of many that have been set up by municipalities in Russia. The card, which is issued to pensioners, students, school children, war veterans, and other eligible people, carries a contactless chip, a bar code, and magnetic strip, along with the VISA Electron payment application issued by the Bank of Moscow. It allows cardholders to redeem social benefits, discounted fares for the Moscow Metro, and medical benefits. Cardholders can use this card to withdraw cash at network ATMs and to make payments if the cardholder has activated the payment function.

## **3. Current Legal Framework for Branchless Banking**

### **3.1 Banks' Use of Agents**

Article 5 of the Banking Law defines banking operations to include: taking deposits; crediting and investing deposited funds; opening bank accounts; clearing payments; collecting cash, bills, and payment documents; buying and selling foreign currencies; and handling remittances by individuals (who may or may not have a bank account). Unless the law provides otherwise (see below), any activity falling under the definition of one of the banking operations requires an institution to be licensed as a “credit organization,” a term which, as used in the Banking Law, includes banks and nonbank credit organizations. As a result, many activities that in other countries are routinely undertaken by institutions falling outside the banking law—such as foreign exchange transactions and payment services—are, in Russia, in the exclusive domain of credit organizations licensed under the Banking Law.

Pursuant to a June 2009 amendment to the Law on Banks and Banking Activities (Banking Law), effective as of 1 January 2010, banks may use bank payment agents to accept cash funds from *individuals* as payment for goods, works, or services, as well as taxes and other government fees and dues. Bank payment agents may also credit cash funds to individuals' bank accounts and conduct operations with the use of payment cards. The law does not permit bank payment agents to use sub-agents.

This amendment presents a significant change in law; however, banks have indicated that the bank payment system is more expensive than the nonbank payment system, in



part due to the ability of nonbank payment agents to use sub-agents. Also, banks have additional administrative costs, including the costs of regulatory compliance.

Banks are fully liable for their agents.

### 3.2 AML/CFT

AML/CFT issues are regulated under the 2001 Federal Law on Countering the Legalization of Illegal Earnings (Money Laundering) and the Financing of Terrorism. The AML/CFT Law applies to a number of institutions, including credit organizations, the postal network, payment agents (i.e., those who contract with merchants to accept payments),<sup>14</sup> and, since August 2009, credit cooperatives. The statutory AML/CFT control obligations are not imposed on mobile phone providers, although there are limited customer identification requirements under the Law on Communications. Because the AML/CFT Law applies to institutions and not to functions, PSPs and e-money issuers are covered under the law only if they operate under any of the legal forms mentioned.

In addition, pursuant to the June 2009 Law on Acceptance of Payments from Individuals by Payment Agents, fully effective as of 1 April 2010, payment agents are required to register with the Federal Financial Monitoring Service (FFMS) for AML purposes and to have their internal control rules approved before accepting payments.<sup>15</sup> Payment agents are not permitted to accept payments through payment terminals or through sub-agents if identification of the payer is required.<sup>16</sup> (See below regarding exemption for transactions of 15,000 rubles or less.)

Know-your-customer (KYC) rules can be found in the AML/CFT Law itself and in regulations and instructions issued by FFMS and CBR. Subject to certain exemptions described below, the law requires, among other things, that subject institutions (i) identify the customer through government-issued identity documents and (ii) establish the customer's residential address.<sup>17</sup> A CBR Instruction on account opening by credit organizations that had required an official from the credit organization to carry out the identification (thereby prohibiting remote account opening) was amended in May 2008 to provide that client identification *may* be provided by bank staff.<sup>18</sup> Banks have concluded that the new wording permits the post office to identify bank's clients for the bank.<sup>19</sup> A few of banks (e.g., Home Credit Finance Bank) are now opening individual's accounts and extending loans *via* post offices.<sup>20</sup>

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<sup>14</sup> AML/CFT Law, Art. 5. Payment sub-agents (i.e., an agent of a payment agent) are not referred to in the law.

<sup>15</sup> Payment agents are not required to register. However, all transactions processed by agents go through the information technology system of the operator and will be subject to AML/CFT rules.

<sup>16</sup> Compliance with the law is to be monitored by a specified government agency, but it is doubtful that there will be sufficient resources if there are thousands of agents.

<sup>17</sup> AML/CFT Law, Art. 7, item 1.

<sup>18</sup> Instruction 28-I.

<sup>19</sup> The AML Law defines the post office as an organisation that may to identify clients.

<sup>20</sup> Although other institutions are permitted by the AML Law to identify clients – including pawn-shops, securities market brokers, insurance companies, leasing companies, factoring companies, asset managers – banks are thus far using only the post.



The AML/CFT Law was amended in June 2009 to exempt from the mandatory identification requirements all person-to-business payments below 15,000 rubles (approximately US\$500) made by individuals, a significant change, particularly for payment agents. (Prior to the amendment, the law had exempted only certain types of payments, including rent, telecommunications, utilities, taxes, and other payments to government bodies.) In addition, all payments made with payment cards are exempt. Buying and selling of foreign exchange is also exempted from KYC requirements if the amount is below 15,000 rubles (approximately US\$500).<sup>21</sup>

All domestic and international money transfers remain subject to the general KYC requirements under the AML/CFT Law as long as they are provided by credit organizations or Russian Post.

All institutions covered under the AML/CFT Law must report all “mandatory controlled transactions” as well as any suspicious transactions to FFMS (established in November 2001) by the end of the next working day.<sup>22</sup> In the first quarter 2009, 1.5 million transactions were reported, of which 4,000 were investigated. This led to 1,300 criminal cases and ultimately 35 court sentences.

### **3.3 Regulation of E-Money**

There are currently no laws, regulations, or policies defining e-money or specifically governing e-money and the transfer of or payment by e-money. However, as noted, regulations on e-money are expected, perhaps as soon as the coming year. The Ministry of Finance and Russian Central Bank are leading the initiative to craft e-money regulation for the vibrant industry that has grown up in this space. Some argue that nonbank entities should be prohibited from issuing e-money. Yet others urge consideration of a special regulatory status that would permit both bank-issued and qualified nonbank-issued on e-money, along the lines permitted in the European Union's new E-Money Directive.<sup>23</sup> Another question, as yet not finally determined, is whether e-money regulation will be incorporated into the planned law on the national payment system (which is already far along in development) or adopted later as free-standing regulation.

In the meantime, e-money issuers argue that e-money may be issued over the Internet and by mobile service operators, relying on a variety of laws. For example, WebMoney, which describes the transfer of e-money as an “agreement on property rights transfer by means of digital units,” has invoked a 1929 Russian decree as the legal basis for issuing e-money. Others have argued that a bank may issue e-money only as a “virtual” card pursuant to a 2004 Central Bank instruction that permits a bank “to issue a bank pre-paid card (or other card) in electronic form.”<sup>24</sup>

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<sup>21</sup> *Ibid*, Art. 7, item 1.2.

<sup>22</sup> *Ibid*, Art. 7.4. Mandatory controlled transactions apply only to transactions involving more than 600,000 rubles (approximately US\$24,500).

<sup>23</sup> It is in part to explain the benefits of the latter approach and debate risk mitigation, that nonbank e-money issuers have formed the “Electronic Money Association” described in Section 2.3, to engage in dialogue with the Central Bank and other interested policy makers and regulators.

<sup>24</sup> Regulation No. 266-P, “On the Issuance of Bank Cards and on Transactions Carried Out with Payment Cards,” 24 December 2004, as amended through 21 September 2006.



### 3.4 Payment Systems Regulation

One of CBR's three stated objectives is to ensure an efficient and uninterrupted payments system.<sup>25</sup> There is no national payments systems law, although a draft law has been proposed. In the absence of such a law, The Civil Code and CBR regulations provide the legal framework for payments systems, their administration, and regulation.

As result of the June 2009 Law on Payment Agents, the provision of payment services is clearly no longer by law the exclusive domain of banks and Russian Post.<sup>26</sup> (Although nonbank payment terminals have been a significant player since 1998, prior to passage of the Law on Payment Agents, they had operated in an ambiguous legal space, arguing that their operations were permitted by the Civil Code's provisions on agency.<sup>27</sup>) The Law on Payment Agents permits nonbanks' payment agents to accept cash funds from individuals (but not from legal entities) as payment for goods, works, or services, and transfer such funds to the supplier as well as taxes and other government fees and dues.<sup>28</sup> All other payments services, including domestic and international money transfers, arguably may still be provided only by prudentially regulated credit organizations or Russian Post.

Nonbank payment agents may use sub-agents and terminals. Payment agents operate the electronic payment system, providing the interface and infrastructure, while sub-agents own the terminals, receiving payments from the payers. However, the Law specifies that a sub-agent may not be used if a payment requires identification for AML purposes—i.e., is in excess of 15,000 rubles.<sup>29</sup> (The same applies to payment terminals.) Payment agents may not conduct operations using payment cards (as banks may do using their own bank terminals as permitted under the Banking Law).

Payment agents must have an agreement with a supplier to accept payments on the supplier's behalf. Agents are permitted to charge service fees to the payers; the monetary obligation of a payer is discharged upon transfer of funds to a payment sub-agent. The law does not establish any specific requirements (e.g., licensing) for payment agents other than to register for AML purposes (see Section 3.2).

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<sup>25</sup> Federal Law on the Central Bank, Art. 3. The other two objectives are (i) to protect and provide for a stable national currency and (ii) to develop and consolidate the Russian banking system.

<sup>26</sup> Russian Post is exempt from the requirement to have a bank license when offering money transfer and payment services.

<sup>27</sup> A specific provision in the Civil Code permits an agent to engage in payment collection on behalf of the principal.

<sup>28</sup> As stated, the 2009 amendment to the Banking Law permits banks to outsource payment services (i.e., payments by natural persons).

<sup>29</sup> There is nothing to stop a payer with a payment to make in an amount greater than 15,000 rubles from dividing the transaction into several smaller transactions that can legally be made via a terminal. This is easy to do, as payments using terminals can be made in less than a minute.