Liberia

Financial Sector Development Implementation Plan

FIRST Initiative

ACKNOWLEDGEMENTS

The Financial Sector Development Implementation Plan (FSDIP) was produced by the Central Bank of Liberia (CBL) with technical assistance of the World Bank Group and financial support from the Financial Institutions Reform and Strengthening (FIRST) Trust Fund Initiative. This report has benefited extensively from inputs derived from reports prepared by various World Bank, International Monetary Fund (IMF), United Nations Development Program (UNDP), and United States Agency for International Development (USAID) missions to Liberia over the last year.

In preparation of this report, the task team met senior officials at the CBL and government ministries including the Ministry of Finance and Development Planning, the Ministry of Commerce and Industry, the Ministry of Justice; top management officials from commercial banks, insurance firms, venture capital firms; management of private sector firms ranging from micro enterprises to the largest corporate firms in the country; representatives of microfinance companies, women's, and professional associations; and other development partners.

The CBL provided strategic direction for the FSDIP with input and guidance from government ministries and the private and social sectors. A Financial Sector Steering Committee (FSCC) composed of *ex officio* senior officials of the institutions listed below identified the key elements of the FSDIP described in the Roadmap for Reforms and will monitor its implementation.

CBL
Ministry of Finance and Development Planning
Ministry of Commerce and Industry
National Social Security and Welfare Corporation (NASSCORP)
Liberian Bankers Association (LBA)
Liberia Business Association

The World Bank Group would like to thank all the government authorities and officials for the assistance, cooperation and logistical support provided, as well as the time generously donated by representatives of the private sector consulted as part of this work. We would also like to recognize and thank Julian Casal (GFMDR), Errol Graham (GMFDR), Thomas Lammer (GFMDR), Harish Natarajan (GFMDR), Marlon Rawlins (GFMFS), Valeria Salomao (GFMDR), Emiko Todoroki (GFMFS), and Cari Votava (GFMDR) for their valuable insights and comments to this plan.

PREFACE

The Government of Liberia (GOL) requested assistance in developing a coordinated, prioritized, and well-sequenced roadmap for financial sector reform. Through funding provided by the FIRST Initiative, a World Bank team from the Finance and Markets Global Practice visited Monrovia to work on the Liberia FSDIP.

The first mission to Monrovia was from July 28 to August 4, 2014.[1] The mission was intended to be a few days longer but was cut short due to the outbreak of the Ebola virus. A follow-up mission from January 13 to 23, 2015 was conducted, in coordination with the World Bank Ebola Economic Recovery Trust Fund activities, to make a preliminary assessment of the impact of the Ebola crisis on the financial sector and to seek to integrate activities related to the Ebola response to the FSDIP. The next mission, which took place July 20 to 31, 2015, included a meeting of the FSCC comprising representatives of all relevant public and private stakeholders.[2] An internal Quality at Entry Review took place on September 29, 2015, and many useful comments were received and incorporated. The last mission to Monrovia was from November 2 to 6, 2015, and in addition to the FSCC meeting, a successful stakeholder consultation took place with attendees from every financial institution and other major stakeholders.[3]

[1] The mission was comprised of Juan Costain (Lead Financial Sector Specialist and Task Team Leader, GFMDR), Sau Ngan Wong (Senior Counsel, GFMDR), Gary Fine (Senior Private Sector Development Specialist, GTCDR), Keith Jefferis (Consultant, Financial Economist) and Peter Hayward (Consultant, Banking Supervision Expert). Collista Harris provided support for the mission in Monrovia and Tim Bulman, Senior Economist, GFMDR, joined the mission for some meetings and contributed to the findings.

[2] This mission was composed of Juan Costain (Lead Financial Sector Specialist and Task Team Leader, GFMDR) and Henry N. Schiffman (Consultant, Financial Sector Policy and Legal Expert) and was assisted on matters related to mobile payments and mobile banking by Thomas Gibb, Field Lead, U.S. Global Development Lab, USAID Liberia and Michael Catalano, Senior Advisor – ICT and Digital Financial Services, U.S. Global Development Lab, USAID. Patrick Heittinger, (Economist), African Development Bank, participated in the kick off meetings.

[3] Over 70 participants attended the stakeholder consultation, including the Acting Minister of Finance.

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CURRENCY EQUIVALENTS
(Exchange Rate Effective March 31, 2016)
Currency Unit = Liberian Dollars (LRD)
US$1 = LRD 92.5

FISCAL YEAR
July 1 – June 30

ABBREVIATIONS

ACH	Automatic Clearing House
ACP	Automated Check Processing
ADR	Alternative Dispute Resolution
ATM	Automated Teller Machine
BRAC	Building Resources Across Communities
CBA	Core Banking Application
CBL	Central Bank of Liberia
CRS	Credit Reference System
CSA	Civil Service Agency
CSR	Civil Service Retirement Scheme
EBL	Ecobank Liberia Limited
ECOWAS	Economic Community of West African States
EIS	Employment Injury Scheme
FIA	Financial Institutions Act (1999)
FIRST	Financial Institutions Reform and Strengthening Trust Fund
FIU	Financial Intelligence Unit
FSB	Financial Stability Board
FSCC	Financial Sector Steering Committee
FX	Foreign Exchange
GDP	Gross Domestic Product
GOL	Government of Liberia
GTB	Guarantee Trust Bank
IADI	International Association of Deposit Insurers
IAIS	International Association of Insurance Supervisors

ICT	Information and Communications Technology
IFRS	International Financial Reporting Standards
IOSCO	International Organization of Securities Commissions
ISA	International Standards on Auditing
KYC	Know-Your-Customer
LBA	Liberian Bankers Association
LBDI	Liberian Bank for Development and Investment
LCUNA	Liberian Credit Union National Association
LEAF	Loan Extension and Availability Facility
LEDFC	Liberian Enterprise Development Finance Company
LFIU	Liberian Financial Intelligence Unit
LICPA	Liberian Institute of Certified Public Accountants
MDI	Microfinance Deposit-Taking Institution
MFDP	Ministry of Finance and Development Planning
MFI	Microfinance Institution
MNO	Mobile Network Operator
MSME	Micro, Small, and Medium Enterprise
NASSCORP	National Social Security and Welfare Corporation
NEMIL	Network of Microfinance Institutions of Liberia
NGO	Nongovernmental Organization
NIM	Net Interest Margin
NICOL	National Insurance Corporation of Liberia
NIR	National Identification Registry
NPL	Nonperforming Loan
NPS	National Pension Scheme
OECD	Organisation for Economic Co-operation and Development
POS	Point of Sale
RCFI	Rural Community Finance Institution
ROSC	Report on Standards and Codes
RSD	Regulation and Supervision Department
RTGS	Real-time Gross Settlement System
SME	Small and Medium Enterprise
SSA	Sub-Saharan Africa
SSS	Scripless Securities Settlement System
UBA	United Bank for Africa Liberia Limited
UNDP	United Nations Development Program
USAID	United States Agency for International Development
VSLA	Village Savings and Loan Association

WAMI	West African Monetary Institute
WAMZ	West African Monetary Zone
WAVF	West African Venture Fund
WOCCU	World Council of Credit Unions
WRF	Warehouse Receipts Financing

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EXECUTIVE SUMMARY AND RECOMMENDATIONS

This Executive Summary does not attempt to summarize the comprehensive analysis of the financial sector in Liberia, but rather highlights priority needs for reforms that can make the sector more sound and productive. The report as a whole is intended as a plan, identifying specific, actionable policy reforms for each subsector, rather than an overview of the financial sector.

With regard to financial sector stability and access to finance, Liberia compares well with its immediate peers, notably the other countries in the Mano River Union. Considerable progress has been made with financial institutions, regulation and supervision, and infrastructure but much remains to be done. The financial sector is dominated by banks which are essentially all privately owned[4] and well managed (with a degree of variation between institutions). The second largest sector is the pension sector which is managed by a state agency for both the private and public sectors. This sector has not benefited from the same degree of reform and technical assistance as the banking and insurance sectors, and has a number of legacy issues which require attention, particularly as the institutions will grow rapidly with increasing formalization attributable to the young population. For a country of its size and income, Liberia has a large number of insurance companies and this sector has benefited greatly from increased supervision and technical assistance in recent years and is on a positive trajectory.

The Financial Sector as a whole has survived the Ebola crisis of 2014–2015 however, certain subsectors have suffered badly, particularly banks and microfinance institutions (MFIs) oriented toward microfinance and micro, small, and medium enterprise (MSME) lending, adding to existing challenges and an already evident decline in outreach.

Banking Sector

Overall, the banking system is well capitalized and liquid but high nonperforming loans (NPLs) and low profitability remain significant challenges to the sector. There are currently nine commercial banks with one focused on microfinance banking and another focused on rural lending. Bank profitability has been *de minimis* or negative in recent years, largely attributable to NPLs and high operating costs, including challenging infrastructural constraints, such as electricity, which limits the banks' ability to increase credit to the economy. It is a source of concern that after years of sustained growth the banking sector assets, as a percentage of GDP, have declined since 2011. More disturbingly, banks are now expressing pessimism about the attractiveness of extending services to the unbanked.

A banks' inability to collect loans in full is, in many cases, the single largest drain on income and inhibits increased lending. The limited success of legal processes for debt recovery is an important reasons for this. Accelerating the breadth and efficiency of the credit information system, enhanced by a national biometric identification system, would improve a banks' ability to appraise credit and reduce moral hazard, which, in turn, would help reduce bad loans. All efforts in these areas should be a priority.

[4] One small bank is owned by the Asset Management Corporation of Nigeria, a government entity and the GOL has a significant minority stake in the Liberian Bank for Development and Investment (LBDI), the second largest bank.

Issues

(a) There is excess liquidity in the banking sector, particularly in Liberian dollars (LRD).

Recommendation: Introduce a Repo market related to government securities. Explore possibilities to increase scale of government bond issuance. Review operations of foreign exchange (FX) market and convertibility.

(b) NPLs are undermining the potential of the banking sector.

Recommendation: Introduce steps for improved financial reporting, debt resolution, and insolvency processes, conduct Creditor Rights Report on Standards and Codes (ROSC) for guidance.

(c) Liberia lacks key legislation to provide a financial safety net to limit losses in asset values in the event of a financial crisis.

Recommendation: Conduct a viability assessment for deposit insurance and, if favorable, develop appropriate legislation.

(d) Liberia has yet to participate in the Financial Sector Assessment Program (FSAP) implemented by the World Bank and IMF.

Recommendation: Formally request FSAP.

Insurance

The number of insurance companies operating in Liberia (20) remains large for the size of the sector (US$ 42.1 million total assets) and gross premiums are valued at US$ 31.8 million, around 1.6 percent of GDP as of September 2015, which is in line with other countries in Sub-Saharan Africa (SSA). There has been some rationalization of the sector since the CBL started regulating the sector in 2011 and it is anticipated that further consolidation will take place with the implementation of new minimum capital requirements. Liberia once held a leading role in the insurance sector in West Africa and returning operating standards to this earlier level is an urgent objective of both Government and market participants. There is a significant number of insurance agents and brokerage firms which are now being reformed. The CBL has prepared prudential and market conduct regulations to supplement the Insurance Act of 2013 which should be issued forthwith.

Issues

(a) The insurance sector is excessively fragmented for its small size.

Recommendation: Enforce capital requirements of the new Insurance Act of 2013 and coordinate transfer of business from companies not meeting minimum standards.

(b) Standards of reporting in the Insurance Sector are not yet at desired levels.

Recommendation: Adopt International Financial Reporting Standards (IFRS) in the insurance sector and ensure compliance.

(c) The National Insurance Corporation of Liberia (NICOL) has a monopoly on Government insurance business under the NICOL Act, but is not currently active.
Recommendation: Review the NICOL Act.

Banking and Insurance Sector Supervision and Regulation

Liberia has a centralized regulatory and supervisory system with the CBL being the only regulatory and supervisory agency overseeing banking and insurance, which constitute 92 percent of financial sector assets. Supervision under the CBL has shown significant advances in recent years, reflected also in the increased staffing of the Regulation and Supervision Department (44 staff).

Following the Global Financial Crisis, many countries established a multiagency dedicated macroprudential surveillance function to monitor threats to financial stability and take actions to prevent crisis or to manage crises to limit losses. Currently, the CBL has a Financial Stability Committee, which oversees issues and developments in the financial sector and recommends appropriate policy responses. The Financial Stability Committee is comprised of the Deputy Governor for Operations as Chairman, the Deputy Governor for Economic Policy, the Directors of Regulation and Supervision Department, Research, Policy and Planning, Banking, Finance as well as the Heads of Treasury Operations and Payment Systems and the Legal Counsel. However, consistent with the global trend, Liberia should evaluate establishing a financial stability council with the Ministry of Finance and Development Planning (MFDP) undertaking macroprudential surveillance and contingency planning for a financial crisis.

The financial safety net to confront a crisis or mitigate its impact usually has three components. Liberia has one (emergency liquidity arrangements for banks provided in the CBL Act). Liberia could explore extending this by establishing deposit insurance and enacting a modern law for financial institutions resolution.

Issues

(a) Basic legislation for financial institutions or for the enabling environment for the financial sector is missing in the areas of payments and insolvency, and the current laws for financial institutions and the central bank dating back to 1999 are in desperate need of revision.

Recommendation: Enact the pending payments law, accelerate enactment of a modern insolvency law, and amend the New Financial Institutions Act (1999) and the Central Bank Act to add missing best practice provisions and refine other provisions. Adopt clear procedures for regulatory governance to make supervisory and regulatory actions more transparent, responsive to industry concerns, and effective.

(b) Unlike many countries, after the Global Financial Crisis Liberia has not established a dedicated macroprudential surveillance function and financial crisis prevention and management regime.

Recommendation: Establish a financial stability council to undertake macroprudential surveillance and define macroprudential tools to address potential threats and procedures for contingency planning for prevention and management of a financial crisis.

(c) Prudential and market conduct regulations for the insurance sector await issuance.
Recommendation: Issue forthwith regulations for insurance companies for market conduct and prudent operations.

(d) Regulations covering related-party transactions, politically connected persons, and aggregation of large exposures are imprecise.
Recommendation: Review international best practices and amend as necessary.

Credit Information Systems

The establishment of a credit reference system (CRS), which will extend the coverage, improve the scope, and enhance the operating efficiency above what is provided by the existing scheme, remains a priority for the financial sector in Liberia. Increasing access to credit, particularly for small and medium enterprises (SMEs), is of the highest priority to develop the Liberian economy and an effective credit information system can play an important role to that end, especially if linked to a national ID system.

While undoubtedly constrained by the limited scale of the domestic financial sector, with the advancement of technology, systems are now viable on a smaller scale than in earlier years. Alternatives such as a public-private hybrid arrangement which will protect national priorities while allowing for inclusion of a broader range of financial sector participants and provision of data more finely tuned to private sector requirements, can be explored. The establishment of the Collateral Registry can significantly complement efforts to promote access to finance by the population at the "bottom of the pyramid."

Issues

(a) The absence of a credit information system meeting international norms remains an obvious opportunity for improvement in the lending environment.

Recommendation: Develop a proposal for PPP (public private partnership) in the credit reference bureau and implemented accompanying legal framework.

(b) The credit information regulations does not require positive and negative data on all borrowers in the financial system.

Recommendation: Amend regulations to require positive and negative data on all borrowers across all formal financial institutions (including MFIs).

Payment Systems and Digital Financial Services

While originally intended to form the backbone for interbank payments, prospectively within an integrated West African Monetary Zone (WAMZ), the current project to implement core payment infrastructures (Real-time Gross Settlement System [RTGS]/Scripless Securities Settlement System (SSS), an Automatic Clearing House (ACH)/Automated Check Processing (ACP), and a national switch) will also provide an important foundation for the development of digital financial services, which will modernize the financial sector and lower transaction costs, particularly in rural areas, and as a result extend financial inclusion. Moreover, by providing a record of transfers, digital financial services may help address the challenges of governance which have bedeviled citizen's financial interaction with government and frustrated the development of a credit culture. As in other countries, such as Bangladesh and India, a common digital platform can support communications and biometric identification services, which will be complementary to the financial application. USAID has been trying to develop the Partnership for a Digital West Africa as a possible coordinating mechanism to bring together these parallel areas of activity. The establishment of new payment systems will also facilitate interbank payments, and the national payments switch, currently being developed, will allow payment cards to be used in Automated Teller Machines (ATMs) and Point of Sale (POS) terminals of all issuers or for transferring payments between account holders at all banks. In addition, it could be leveraged for interoperability between different mobile money providers and/or mobile money and bank accounts.

The use of digital financial services is in its infancy and has the potential to increase financial inclusion and promote good governance in financial services. Therefore, initiatives such as promoting agent-based models for mobile money and the Government extension of G2P (Government to People) digital payments should be considered.

Issues

(a) The legislative and regulatory environment covering payment systems is outdated.

Recommendation: Develop and publish the Payment System Act and review the legal and regulatory framework for payments. Make an assessment against Payment Aspects of Financial Inclusion (PAFI) guiding principles and identify key actions.

(b) Payment cards from different issuers cannot be used in ATMs of other issuers or for transferring payments between account holders at all banks. Ongoing payments modernization is delayed.

Recommendation: Bring cards switch into operation, connect banks, develop a card scheme, and plan for connection of mobile network operators (MNOs). Bring ACH/ACP and RTGS/SSS into live operation.

(c) The digital financial services infrastructure is well below its potential for increased financial inclusion and good governance in financial services.

Recommendation: Develop a National Payment System Strategy, establish an oversight unit and, develop an oversight framework and guidelines. Coordinate with the Ministry of Interior regarding a linkage to the biometric national ID.

(d) Liberia still has limited access points and lack of business case for payment service providers.

Recommendation: Develop a regulatory framework for payment agent functions for mobile money and to promote G2P (Government to People) digital payments.

(e) Liberia has one of the highest levels of remittances to GDP but has not incorporated this into mobile payments.

Recommendation: Reassess the remittance market against the General Principles for International Remittance Services.

Social Security (NASSCORP)

From a pension perspective, Liberia is in a very favorable position because the workforce is young and growing, in contrast to the high dependency ratios of many developed countries. In consequence, the financial solvency of the pension scheme will not be realized for some decades but, the distant date of reckoning does not in any way detract from the importance of ensuring an optimal investment return and the greatest focus on the appropriate application of resources at the current time. It is of paramount importance that the Government makes good on its contribution liability with respect to state employees and that administrative expenses are maintained within international norms.

Especially since there is an absence of regulation and supervision of pension schemes in Liberia, beneficiaries should have assurance that their retirement schemes are operating on a sound financial basis and in their best interests. In order to preserve its long-term financial condition with respect to liabilities, realizable assets, and expenses, NASSCORP should share with stakeholders the findings and recommendations of its actuarial reviews.

Unfortunately the National Pension Scheme (NPS) may not be covering all employees who should be covered and there may be inequities in the benefits to be paid to those that are covered. Therefore, to remedy any anomalies, NASSCORP should conduct a review as to whether more employees could be covered by the NPS and revise the method for calculating benefits, including with respect to indexation and calculation of the reference wage.

Issues

(a) There is an absence of regulation and supervision of the two pension schemes in Liberia, and beneficiaries should have assurance that their insurers are operating on a sound financial basis and in their best interests.

Recommendation: Encourage NASSCORP to disseminate actuarial studies with respect to liabilities, realizable assets and expenses, and enact reforms to ensure that pension fund assets are administered in the best interests of the beneficiaries.

(b) With respect to public sector employees, the Government is not current in its contribution to NASSCORP.

Recommendation: The shortfall of Government contributions should be calculated and made good through the issuance of long-dated recognition bonds at market rates.

(c) NASSCORP lacks access to sound, long-standing investment instruments to match its liabilities.

Recommendation: Allow NASSCORP direct access to Treasury Securities' auctions and explore modality for overseas investment.

Financial Inclusion and Microfinance

Microfinance has the potential to raise the living standards of the poorer segments of the population, but the performance of most of the MFIs, in Liberia, in extending credit to approximately 25,000 borrowers has been disappointing. . MFIs, especially the non-deposit-taking institutions, have weak governance, poor credit appraisal practices, and little risk management, making them less productive than need be. The CBL as supervisor of these institutions should issue and ensure compliance with basic rules and procedures.

The Ebola crisis has exacerbated the already weak financial position of the microfinance sector but donor financing will be available to recapitalize the stronger institutions, and this may also present an opportunity for reshaping the Government's engagement with the sector. Credit Unions have fared the crisis better, and the recent initiative to promote rural community financial institutions offers promise (although a process which ensures long-term sustainability, including the cost of effective supervision, should be established from the outset).

Issues

(a) MFIs, especially non-deposit-taking institutions, are generally in uncertain financial condition because of poor governance and the lack of proper financial reporting.

Recommendation: Strengthen the financial condition of MFIs by requiring compliance with rules for governance by their boards of directors, credit underwriting standards, risk management, and financial reporting. Require financial accounts for all MFIs be filed with the CBL. Support training and IT modernization where necessary.

(b) The poorer segments of the population are especially financially vulnerable because of the lack of savings and access to affordable insurance.

Recommendation: Support initiatives for financial education, particularly those linked to social protection schemes and feasibility of microinsurance for life, health, credit, and crop failure.

(c) Rural coverage remains weak for access to financial services.

Recommendation: Work with donors to establish Rural Community Finance Institutions (RCFIs) in every county, promote extension of commercial banks and establish four Regional Credit Unions. Support transition to digital financial services for MFIs and Credit Unions.

Enterprise Access to Finance

Liberia's economy has faced severe shocks in recent years, most recently in the form of the Ebola crisis, but perhaps more pervasively through the significant fall in the price of commodities produced in Liberia (iron ore, rubber, and palm oil). While all sectors of the economy have been affected, it appears that the MSME sector has been most adversely affected, particularly by the Ebola crisis, and has been least well positioned to benefit from the inflows of donor assistance which followed. The importance of ensuring development in this sector is amplified by the leading role it plays in providing employment, especially for those at the bottom of the pyramid. In doing this, it will be necessary to address the fundamental constraints, such as inadequate financial accounting, poor skills, limited access to capital, unpredictable and costly judicial processes, and uncertain cash flows as well as providing financing. Use of new financial instruments such as financial leasing, warehouse receipts financing (WRF), asset-based lending using the Collateral Registry, and making more use of digital financial services could be usefully explored.

Issues

(a) Enterprise access to finance is constrained from both the demand and the supply side.

Recommendation: Work with financial institutions and donors to develop improved financial infrastructure tools, including redesigned credit guarantee schemes, to mitigate the risks of lending, as well as training for enterprises' management to improve accounting standards and the quality of financing proposals from SMEs.

(b) Asset-based financing techniques of invoice factoring and using warehouse receipts as collateral are not used in Liberia, but could be of benefit to SMEs and agricultural producers.

Recommendation: Determine whether there are any obstacles in the law that would prevent establishing contracts to implement these types of asset-based financing. If so, propose appropriate amendments.

Anti-Money Laundering/Countering Financing of Terrorism

Liberia is at the very early stages of developing and implementing systems to control criminal abuse of the financial system and it is alleged that money laundering attributable to fraud, corruption, and other financial crimes are widespread in the banking system. Although Liberia has begun to build anti-money laundering and countering the financing of terrorism (AML/CFT) controls, this system is in its infancy, and weaknesses in interagency and international cooperation systems as well as in the legal and criminal justice systems impede efforts of officials to bring perpetrators to justice even when they can be identified.

Issues

(a) The regime for AML/CFT is rudimentary and lacks important legal provisions and inspection procedures.

Recommendation: Amend the AML/CFT legislation and issue new regulations to meet international AML/CFT obligations. Include regulations on Cross Border Transportation of Currency, Suspicious Transaction Reporting and Politically Exposed Persons.

Laws and Regulations[5]

Liberia has undertaken extensive reforms in the legal and regulatory areas for the financial sector, including a revised commercial code that includes a title on secured transactions, a movable collateral registry, an enactment of an Insurance Act, and the establishment of a Commercial Court. The CBL has issued numerous prudential and market conduct regulations and guidelines for banking and microfinance including in areas of bank governance and AML/CFT.

Modernization of laws and regulations has the potential to make a material impact on the development of the financial sector in Liberia; enacting the pending payments law, accelerating enactment of a modern insolvency law, and amending the New FIA (1999) and the Central Bank Act to add best practice provisions should be priorities. New or amended regulations are required for mobile money, insurance, and AML/CFT. The CBL should determine the need for regulations for promotion of factoring and WRF.

Regulations for the insurance industry to supplement the 2013 Insurance Act and regulations for AML/CFT to enable Liberia to fulfill its international obligations are also priorities. The CBL should also adopt formal regulatory good governance practices to make its regulation more transparent, responsive and efficient.

[5] Annex 7 contains a Technical Note on the Legal and Regulatory Framework for the Financial Sector.

INTRODUCTION

The Vision for the Financial Sector

> **A stable, modern, and competitive financial system that provides a supportive infrastructure and access to quality and affordable financial services for all.**

1. A sound financial sector will promote healthy competition among strong financial institutions capable of providing diverse and appropriate financial services and products to individuals and enterprises. A competitive financial sector will increase the provision of private sector credit and lower costs. A more inclusive financial sector will increase access to finance to smaller enterprises and low-income households and individuals.

Financial Sector Reform Objectives

2. The overarching objective of the Bank's technical assistance is to facilitate financial sector reforms in Liberia by helping national authorities develop a comprehensive FSDIP that has a well-sequenced, time-bound, and prioritized roadmap for implementing reforms. The main objectives of the Bank's missions were to (a) engage with the CBL and other stakeholders to discuss FSDIP objectives and obtain a better understanding of the main issues at stake; (b) collect the relevant information for the necessary analytical work; and (c) finalize the stock-taking exercise of the recommendations provided by previous reports and studies related to financial sector development in Liberia.

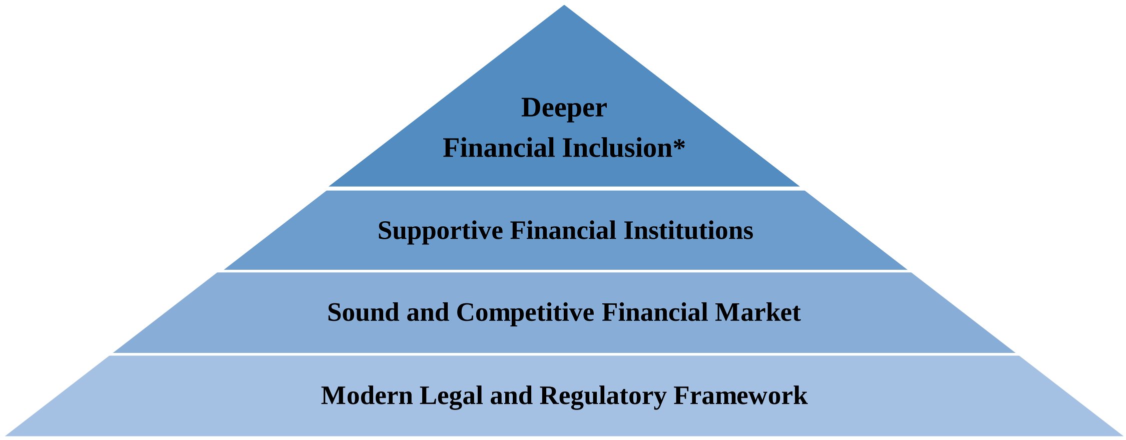
3. The main objective of the Government's FSDIP is to contribute to the development of Liberia's financial sector and provide the Government and private sector stakeholders with a clear roadmap in key policy areas for financial sector development, particularly in the areas of strengthening the financial institutions and financial sector infrastructure, increasing financial inclusion, and establishing new policy initiatives for institutional enhancements.

4. This document includes a sequenced implementation plan designed to lead to the expected outcome of enabling authorities to implement key financial sector reforms and interventions to achieve a more efficient, sound, and inclusive financial sector in Liberia on the basis of a coherent policy view. The ultimate goal of this plan is to reduce poverty and promote economic growth in Liberia.

5. Reforms in two basic areas must be accomplished to realize the vision. These were identified through a diagnostic of the financial services market and its corresponding legal and regulatory framework, which was undertaken by the World Bank Group in 2014–2015. First, there is a need for reforms of the financial sector, legal and regulatory framework, regulation and supervision of banks and nonbank institutions, including microfinance, as well as for interbank payments and digital finance. Second, processes and institutions that facilitate a sound and competitive financial market must be modernized for efficient allocation of credit and insurance, collection of loans, and secure and efficient payment services based on transaction accounts, as well as the protection of depositors and safety of the financial system. These reforms would contribute to improving the quality and affordability of financial services available to consumers and business of all sizes, particularly MSMEs and to low-income households.

The Objectives of the FSDIP

Figure 1: Building Blocks of Financial Sector Development for Liberia



Note: * Digital and inclusive safe savings, credit, insurance, and remittance products.

Objective #1: Modern legal and regulatory framework that is implemented efficiently

6. The foundation of a stable and sound financial system is the legal and regulatory environment that supports it. Towards this end, a comprehensive, coherent and effectively implemented legislative and regulatory system is needed to meet today's needs and those of the future.

Objective #2: A sound and competitive financial market

7. A sound and competitive financial market is a prerequisite for economic growth and development. While some believe that competition can be destabilizing[6] other academic research suggests that competition in the banking sector can add to banking sector stability.[7]

Objective #3: Supportive financial institutions

8. The financial sector can help consumers and businesses meet their own goals of investing and growing with financial security. Well-functioning credit and insurance markets provide lenders and insurers with comprehensive information on borrowers and the insured. Borrowers and the insured can leverage both their physical and reputational assets, and all consumers of financial services can have protection. Such markets will help consumers and business meet their needs. Robust, safe, efficient and accessible financial and information and communications technology (ICT) infrastructures are effective for the provision of transaction accounts services, and also support the provision of broader financial services.

Objective #4: Deeper financial inclusion

9. A sound, modern financial system with a well-developed financial infrastructure will expand the frontiers by reaching lower income segments and by introducing new products which bring the financially excluded into the system. Savings, credit, insurance and payment products leveraging digital technologies will further this objective.

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[6] Competition and Stability in Banking. Xaiver Vives. IESE Business School. January 2010.
[7] Bank Competition and Financial Stability: A General Equilibrium Exposition. De Nicolò, Gianni and Marcella Lucchetta. International Monetary Fund Working Paper, WP/11/295. 2011.

RECENT ECONOMIC AND FINANCIAL DEVELOPMENTS

10. The Liberian economy has been hit hard by sharply lower commodity prices as well as by the Ebola epidemic and the related health crisis. Real Gross domestic product (GDP) grew 2.6 percent in 2014 and only 0.1 percent in 2015[8]. For the first half of 2014, before the crisis, growth had been driven by the expansion in the mining sector (mainly iron ore) as well as increased activities in the construction sector spurred by public and private investment. Rubber, iron ore and palm oil production and exports have declined reflecting lower international prices and developments in the forestry sector have been adversely affected by weak administrative oversight capacity. Prospective investments in these sectors, as well as nascent initiatives such as gold, have been cancelled or delayed. Growth in manufacturing continued to be constrained by inadequate electricity and the generally weak business environment. The epidemic has resulted in disruption of production processes across several sectors, caused only partly by illness and death and mostly by fear associated with the outbreak. However, the major shocks can be seen in the mining and agriculture sectors (table 1). According to the IMF, average inflation increased to 9.9 percent in 2014 reflecting the impact of the Ebola crisis on agriculture and trade, but fell to 7.9 percent in 2015.

11. Monetary policy is focused on containing LRD-denominated inflation through the maintenance of exchange rate stability. The LRD-denominated treasury bills introduced by the CBL in early 2013 have been effective in mopping up some of the excess liquidity of local LRD in the banking sector. However, the effectiveness of LRD instruments as a monetary policy tool remains limited, given the high level of dollarization of the economy. Further, the absence of an anchor for monetary policy remains a key challenge. The weekly FX auctions are the Central Bank's primary instruments for maintaining exchange rate stability. The LRD depreciated by 4.3 percent between December 2014 and 2015. Growth in broad money, which recovered in 2013 growing by 28.7 percent, declined by 8.2 percent in 2014 reflecting the Ebola induced slowing of economic activities. Broad money grew by 10.2 percent between November 2014 and November 2015.

12. Liberia's near- and medium-term economic prospects have been severely affected by the Ebola crisis through its adverse impact on all sectors. Planned foreign direct investments in the natural resources sectors have been delayed. Public and domestic private sector investments, particularly in the construction sector, have also been delayed as the government has shifted resources to health and social protection. Medium-term growth and employment will be directly and indirectly affected by the delayed investments. Furthermore, potential downside risks from the deepening of the Ebola crisis could be more substantial, operating through the investment growth channel as well as through the fiscal revenue channel.

13. **The government's Agenda for Transformation envisages a more diversified economy with more inclusive growth that would lead to further reductions in poverty.** In the near term, growth is expected to be driven by the substantial inflows of foreign direct investments in the natural resource sectors including rubber, iron ore and oil palm as well as strong growth in the construction and services sectors. The emergence of a more diversified economy is constrained by the lack of infrastructure, inadequate human capital, insecure land tenure and limited access to domestic financing particularly to the agricultural sector, which has the potential to make a significant contribution to creating a more diversified economy with substantial employment and enhancement of food security.

[8] IMF forecasts a rebound in growth of 2.5 percent in 2016.

MACROECONOMIC BACKGROUND

14. The Liberian economy has recovered well since the ending of the civil war in 2003. Real GDP growth averaged 11.8 percent from 2006 to 2015, but registered only a 0.1 percent growth in 2015. Much of this growth has been driven by increased mining production. Despite rapid population growth, the overall growth rate has been fast enough to raise real per capita incomes, which rose 109.8 percent between 2006 and 2015. Nevertheless, Liberia remains a low-income country, with a per capita GDP of around US$469 in 2015 according to the IMF.

15. Reported inflation has been a persistent problem, averaging 9.4 percent in the past decade (2006-2015) and 8.5 percent over the last 3 years, according to the IMF. However, given the dual currency nature of the Liberian economy, true inflation is difficult to measure, and the reported measure applies to LRD-denominated prices and not to U.S. dollar–denominated prices (and is hence less relevant to the portion of the labour force that receives incomes in U.S. dollars). Given the nature of the economy and pricing, the main driver of recorded inflation is the LRD–U.S. dollar exchange rate, which directly impacts the LRD valuation of goods and services that are priced in U.S. dollars.

16. Government finances have been in reasonably good shape with a relatively small budget deficit, averaging 2 percent of GDP over 2011–2013. Government debt is manageable, at just under 31.7 percent of GDP at the end of September 2015. The main macroeconomic vulnerability stems from external balance problems. The current account deficit has averaged 32.9 percent of GDP for the past three years (2013-2015), even after taking into account remittances and development assistance grants. Imports (94.9 percent of GDP in 2014) are almost four times the level of exports (25 percent of GDP).

17. The Ebola outbreak in 2014 had a substantial negative economic impact. Real GDP growth, which was estimated at 12.4 percent in 2013, slowed to 2.6 percent in 2014 and 0.1 percent in 2015. Adverse impacts on the balance of payments have also been observed with the current account deficit widening from 28.2 percent of GDP in 2013 to 41.6 percent in 2015, mainly due to the sharp decline in exports caused by the Ebola and commodity price shocks. Similarly the overall fiscal balance sharply declined from a deficit of 1.9 percent in FY14 to a deficit of 8.1 percent in FY15, because of increased spending in the health sector.

OVERVIEW OF THE FINANCIAL SECTOR

18. The Liberian financial system is relatively undiversified but in aggregate is of a moderate size for a low-income developing country. Until recently it has been growing rapidly; however, the banking sector has suffered a modest decline in total assets as a percentage of GDP since 2011. The financial sector faces a wide range of challenges, some of which are typical for a country of Liberia's level of development, but with additional complications arising from the dual currency system.

Table 1: Overview of the Financial Sector

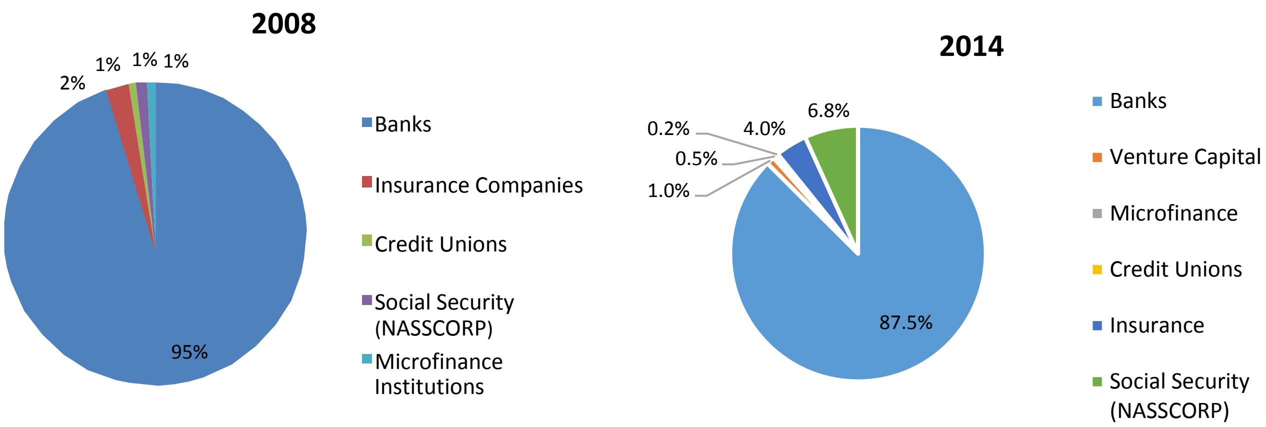
	Number	Assets (LRD, millions)	Assets (US$, millions)	Assets (Percentage of GDP)
Banks	9	79,927	864.1	42.9
Nonbank lenders				
Venture capital	3		10*	0.5
MFIs	20		5*	0.3
VSLAs	1,450			
Credit unions	400		2*	0.1
RCFIs	9			
FX bureaus	122			
Mobile money	2			
Insurance companies	20		42.1**	2.1
Pension funds	2	2,896*	35.1*	

Note: *Approximate figures from 2014 and ** from September 2015. VSLA = Village Savings and Loan Association. Banking sector data is from October 2015, while GDP is the IMF 2015 estimate.
Source: CBL 2015 Annual Report; FSDIP team, October 2015.

19. Liberia's financial sector is bank dominated, as is typical of low-income developing countries. There are nine commercial banks of varying sizes although some of the banks are very small and this could undermine profitability and efficiency. Physical outreach is limited as most of the banks are concentrated in Monrovia and there are limited branch networks across the country, although there has been significant increase in branches between 2006 and 2015. Use of non-branch facilities such as ATMs and POS machines is also underdeveloped.

20. Outside of the banking sector there is a limited range of nonbank financial institutions. There are a number of companies providing short-term insurance, but there is limited provision for long-term insurance. There is no private pension sector and essentially no capital market. There has been recent growth of small-scale financial institutions such as credit unions and village savings and loans associations (VSLAs), which should help to extend access to finance in rural areas. Given the high costs and low profitability of branch-based financial services, it is likely that branchless financial service delivery, such as agent-based delivery channels, will be important in extending access to finance. One of the MNOs offers a mobile money product, although generally mobile money and banking have been slow to take off.

Figure 2: Composition of Financial Assets by Sector: – 2008 and 2014



Sources: CBL, LACUNA, NASSCORP, Microfinance Unit (CBL), World Bank estimated.

THE BANKING SECTOR

21. The banking system has grown steadily in recent years. Total assets reached some LRD 79.9 billion (US $864.1 million) in October 2015 (or around 42.9 percent of GDP, compared with just US$157.5 million in 2006). Credit to the private sector grew 23.7 percent to US $367.9 or 16.9 percent of GDP. Demand deposits increased 7.6 percent from LRD 28.3 billion (US$305.7 million) in December 2014 to LRD 30.4 billion (US $328.9 million) in October 2015. Financial intermediation has become more effective and the gross loan-to-deposit ratio has risen from around 55 percent in the late 2000s to 63.3 percent in October 2015.

Figure 3: Size of Banking System

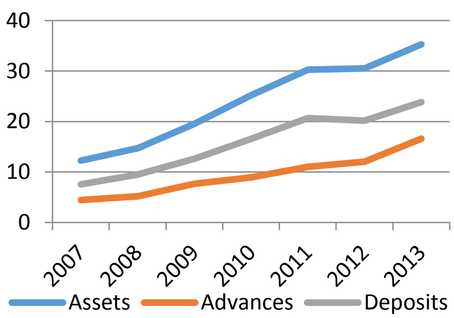
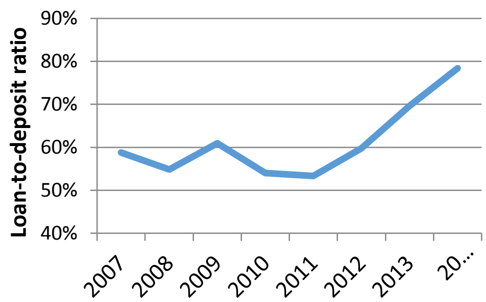


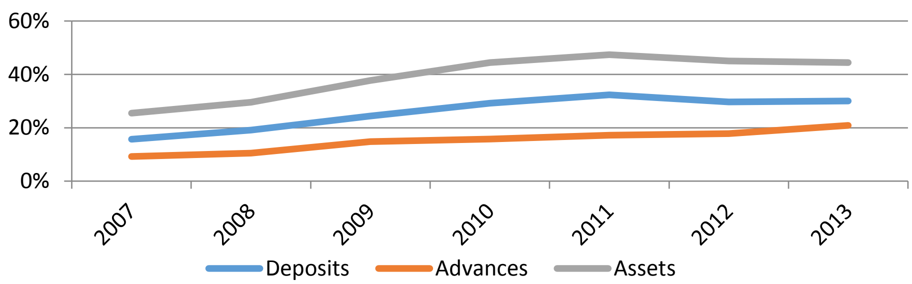
Figure 4: Loan-to-Deposit Ratio



Note: Real LRD billion, 2006 prices.
Source: Calculations based on data from the CBL, World Bank.

22. Banks are required to maintain a minimum liquidity ratio of 15 percent, in addition to the reserve requirement of 15 percent[9] for the U.S. dollar and 22 percent for LRD deposits. It has been suggested that these ratios impose a limit on how far banks can lend against deposits.[10] However, most of the growth in bank balance sheets occurred in the early years of the period when the reserves ratio was higher. Furthermore, the size of banks and the deposit base have fluctuated in recent years, with November 2015 asset and deposit figures ultimately settling around December 2013 figures.

Figure 5: Size of Banking System (Percentage% of GDP)



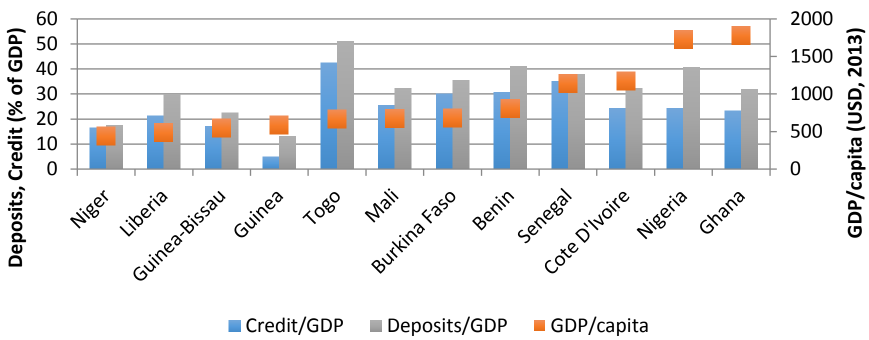
Source: Calculations based on data from the CBL, World Bank.

[9] Reduced from 22 percent during 2013.
[10] A direct application of the reserve and liquidity ratios would indicate that banks can lend up to 70 percent of their deposit base. In addition, banks can lend against capital/reserves, or other non-deposit-funding sources.

23. It is widely held that bank credit to the private sector is relatively limited in Liberia. However, this perception may now be somewhat outdated. At 16.9 percent of GDP, commercial bank credit is not unreasonable for a low-income country (the negligible size of the government debt market favors this comparison). Compared to the rest of ECOWAS,[11] Liberia does have a smaller banking sector—with regard to deposits and lending—than most other members. However, when real income levels are taken into account, Liberia has a larger banking system than other low income countries.[12]

24. Commercial bank lending has been constrained by the lack of means to help banks mitigate the risks of lending; although considerable progress has been made in the last few years to improve the soundness and capacity of the banking system. The CBL has been proactive in strengthening the legal and institutional framework and the financial infrastructure, and improving its own regulatory and supervisory capacity. The CBL has worked to establish a secured transactions regime and a modernized web-based movable collateral registry, both of which will help banks to better identify legal ownership of collateralized assets and the means to collect on them in the event of default. A Secured Transactions Law, which provides for comprehensive reform of the secured transactions framework, was approved in 2010, around the same time as the Commercial Code. This law provides for transparency, and consolidation of registration of movable collateral. There may be a need to also strengthen collateralized lending for immovable assets with regard to a similar web-based infrastructure or incorporation of such real property collateral registration in the registry established for movable collateral.

Figure 6: Bank Deposits &and Credit Relative to GDP, ECOWAS, 2013



Source: IMF Financial Access Database.

Money Supply

25. The broad money supply comprises currency in circulation (outside banks) plus bank deposits. For currency, the CBL reports only LRDs in circulation, and not U.S. dollars, for which there is no reliable data.

26. The CBL reports that U.S. dollars (excluding cash) accounted for 70.1 percent of broad money at the end of November 2015. This implies that U.S. dollar deposits make up 82.1 percent of bank deposits.

[11] Economic Community of West African States.

[12] Based on data from the IMF's Financial Access database. Data for The Gambia and Sierra Leone are not reported.

Table 2: Money Supply (LRD, millions)

	December 2014	November 2015
Currency outside banks	8,359.0	8,620.2
Demand deposits	28,275.5	30,418.3
Time, savings, and other deposits (quasi money)	17,062.4	20,152.0
Total deposits	45,337.9	50,570.3
Total broad money	53,696.9	59,190.5
US$ component (in LRD)	38,783.1	41,494.7
US$ component of broad money	72.2%	70.1%
US$ component of bank deposits	85.5%	82.1%

Source: CBL.

Banking Market Composition

27. The number of banks has grown steadily since the end of the civil war; by 2011 there were nine licensed banks, compared to only three in 2004. Eight of the nine banks have full or majority foreign ownership, and mostly originate elsewhere in West Africa. The banking sector is moderately concentrated, with the four largest banks accounting for 76 percent of banking sector assets. Most of the banks are full service commercial banks; however, Access Bank Liberia Limited focuses on microfinance/SME lending, while Afriland focuses on rural/agricultural finance.

28. Ecobank Liberia Limited (EBL) and the LBDI are the largest corporate as well as retail banks, with approximately 75 percent of all retail accounts. Only a few other banks have more than 10,000 accounts. A financial inclusion baseline survey conducted in 2015 by CBL with support from the Alliance for Financial Inclusion found that 28 percent of adults have an account with a formal financial institution. Since 30 percent of the population resides in Monrovia, most of the banks are concentrated in the capital city and have limited branch networks outside of Montserrado County. The major banks have branches in Ganta (Nimba), Buchannan (Grand Bassa) and Zwedru (Grand Gedeh) counties because of their high level of trade and economic activity. Inversely, and attributable to a lack of economic activity, 4 counties (Sinoe, Lofa, Grand Gedeh, Grand Cape Mount, Bomi) have only one bank branch each, and 4 counties (River Gee, River Cess, Grand Kru, Gbarpolu) have no branches.[13]

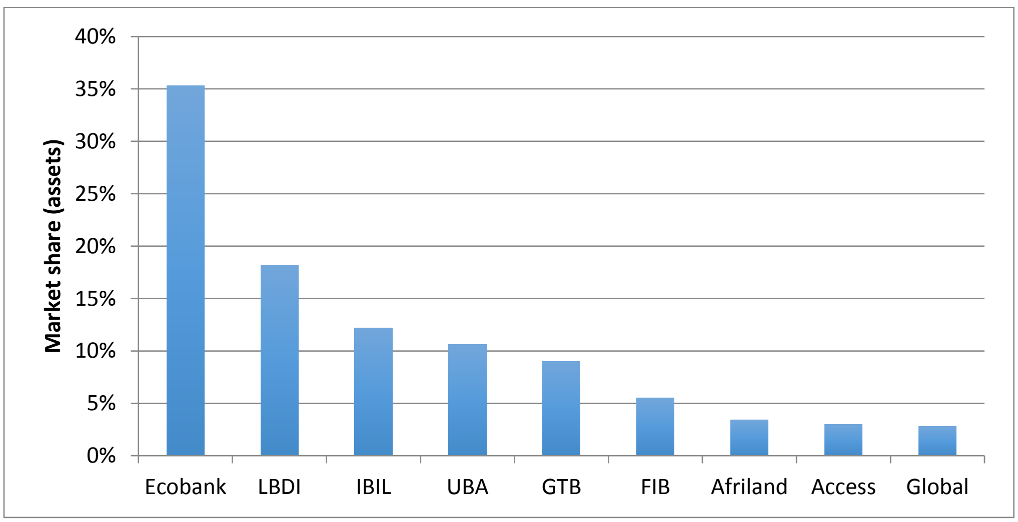
[13] Under a CBL-sponsored initiative RCFIs have been opened in Nimba, River Gee, Grand Kru, Gbarpolu, River Cess, Sinoe, and Lofa counties.

Table 3: Commercial Banks in Liberia and Their Ownership

Name	Ownership	Country of Home Jurisdiction	Year First Licensed
ECOBANK	Ecobank Transnational (100 percent)	Togo	1999
LBDI	Foreign (44.47 percent), including IFC Local 55.53 percent including government	Liberia	1965
International Bank Liberia Ltd	Trust Bank of the Gambia Databank Financial Services Ghana Pan African Capital Group	Liberia	2000
United Bank for Africa Liberia Limited(UBA)	Continental Trust Limited	Nigeria	2008
Guaranty Trust Bank Liberia Ltd	Guaranty Trust Bank plc	Nigeria	2009
First International Bank Limited	FI Bank Group (SLOK Holdings Nigeria)	Gambia	2005
Afriland First Bank Liberia Ltd	Afriland First Bank Group (65 percent) FMO (18 percent) Other private investors	Cameroon	2011
Access Bank Liberia Ltd	Access MFI Holdings (52 percent) IFC (18 percent) European Investment Bank (15 percent) African Development Bank (15 percent)	Germany	2009
Global Bank Liberia Limited	Keystone Bank[14]	Nigeria	2005

Source: CBL.

Figure 7: Banks' Market Shares



Source: CBL.

[14] Global Bank was acquired by Platinum Habib Bank Nigeria in 2009, however, Platinum Habib Bank was intervened by the Central Bank of Nigeria in 2011 and its operations assumed by Keystone Bank, which is owned by the Asset Management Corporation of Nigeria, a government entity.

Bank Credit to Sectors

29. Bank lending is primarily to the private sector (96.7 percent of the total as at November 2015), with the remaining 3.3 percent to the public sector (Government and public corporations). Within the private sector, the largest recipients are the Trade, Hotels and Restaurants sector (42.9 percent) and Construction (16.6 percent). The bulk of lending to trade in Liberia is similar to many developing countries. It is possible that the relatively low shares for services shown in table 4 (8 percent from end of October 2014) and for manufacturing (2.9 percent end of November 2015) is because of lack of adequate collateral that could be realized in the event of default, but it is likely that much lending for manufacturing for large firms comes from abroad. The data from the new movable collateral registry shows some US$260 million in overseas claims, giving some indication of the scale of foreign lending (relative to the total domestic loan volume of around US$367.9 million as of end of November 2015).[15] Many service businesses obtain credit from offshore sources, but the amount of such borrowing is not well documented. However, the fact that very little credit from domestic banks goes to the large and rapidly expanding mining sector indicates that external borrowing is likely to be substantial. Lending to individuals comprises 12 percent to total bank lending. The total number of loans recorded under the credit registry is about 39,000, pointing to the limited scale of the market (all loans granted by commercial banks are registered in the Credit Reference System; however, credit checks are required for only loans above US$1,000). A 2013 IFC report indicates the average loan life is 1.6 years, pointing to relatively short-term lending.

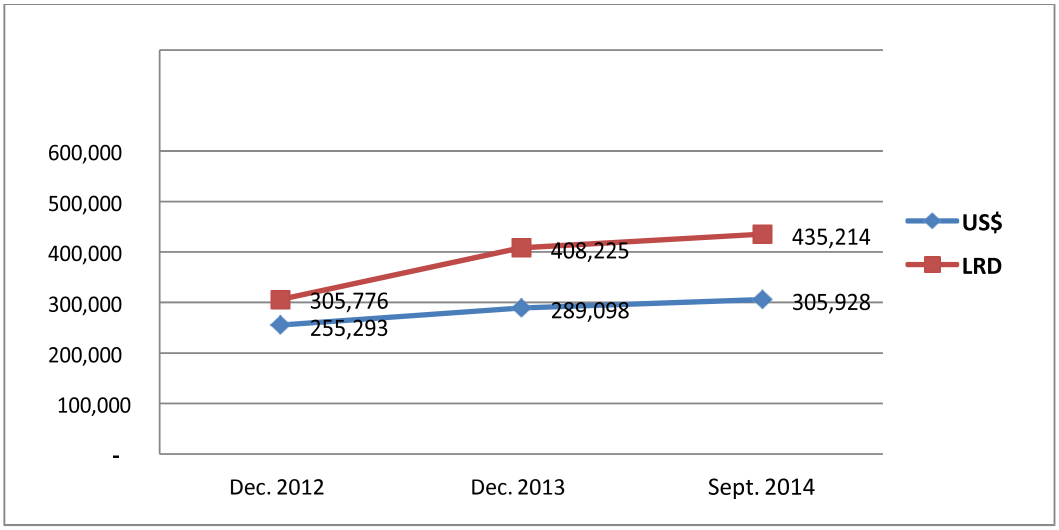
Table 4: Bank Lending, Number of Loans by Sectors at End-October 2014 (in LRD, millions)

Sector	Aggregate Loans	Percentage	Percentage Share of GDP (2013)
Agriculture	1,115	4	25.2
Construction	4,461	16	–
Communication	1,673	6	–
Services	2,230	8	43.9
Transportation	558	2	–
Manufacturing	558	2	7.3
Extractive	279	1	13.4
Oil and gas	–	0	–
Trade	10,316	37	–
Personal	2,788	10	–
Government of Liberia	279	1	–
CBL	–	0	–
Public corporations	279	1	–
Others	3,346	12	–

30. Banks lend in both LRD and U.S. dollars, the large majority of borrowing is in U.S. dollars. Since a slightly lower proportion of bank deposits are in LRD, as indicated in figure 8, this exposes banks to currency risk. While in the recent past the LRD has appreciated against the US$, this trend reversed in 2015, as the LRD depreciated 4.3 percent versus the US dollar between December 2014 and 2015.[16]

[15] The BIS data for overseas lending to Liberia shows unfeasibly large numbers, possibly attributable to the registration of shipping in Liberia.
[16] CBL 2015 Annual Report.

Figure 8: Commercial Bank Deposits (2012 to - September 2014)



Interest Rates

31. As of the end of November 2015, lending rates averaged 13.6 percent while time deposit rates averaged 4.60 percent. Inflation has remained in the single digits, but decreased in 2015 to 7.9 percent from 9.9 percent in 2013. The rise in inflation was not reflected in deposit rates, widening the negative real return on savings.

32. The trend in interest rates and inflation since 2007 are shown below. In the reporting of interest rates, no distinction is made between rates on deposits and lending denominated in LRD and US$. Discussions with banks indicated that there is little difference in rates in the two currencies, even though significant differences would be expected if rates were fully market determined.[17] Review of levels of interest rates suggests the following:

- There is little variation in lending rates to different sectors, even though rates would be expected to vary across types of credit depending on risk profile.
- Interest rates on deposits are significantly negative in real terms for LRD deposits.
- The average return on loans is relatively low for a banking system in a low-income African country.
- The spread between average deposit and lending rates is low relative to other low income countries in the region.
- Discussions with the banks indicated that the CBL seeks to establish informal ceilings on lending interest rates.[18]

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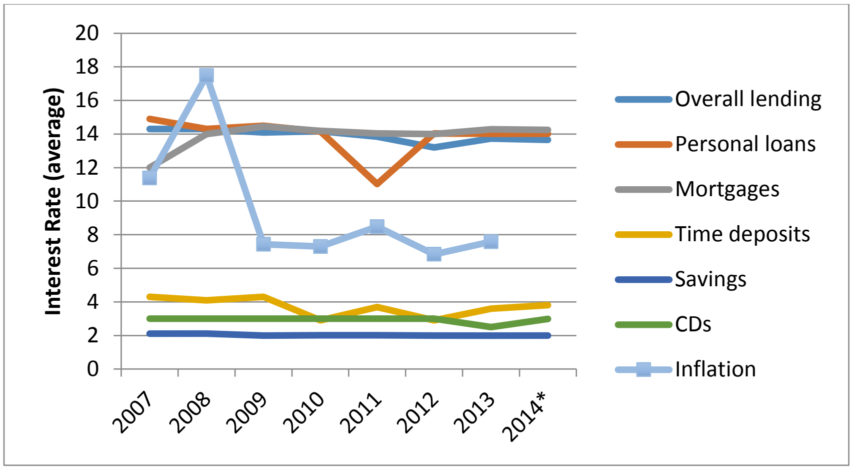
[17] For lending rates this may be as a large component of the absolute rate is made up of margin for risk and operating expenses, also there is a degree of moral suasion which caps rates. For deposits, it may reflect the excess liquidity in LRDs. In any case, the exchange rate between LRDs and U.S. dollars has been relatively stable.

[18] The CBL has clarified that it has neither a formal nor informal ceiling regime. However, the CBL frowns on the application of usurious lending practices. In response to CBL's concern about such lending practices, which are considered to be one of the key factors for the high default rates in the banking system, the banks on their volition, agreed to maintain fairly acceptable lending rates in the system and to guard against usurious lending practices.

Figure 9: Interest Rates



Source: CBL, World Bank.

Banking Sector Performance

33. The performance of the Liberian banking sector has been distinctly mixed across a range of financial soundness metrics. The overriding problem of the banking sector is that it is unprofitable, with return on assets (ROA) of -0.9 percent and return on equity (ROE) of -7 percent as of October 2015. Paradoxically, the Ebola crisis had a positive effect on the overall profitability of the banking sector, although this applied only to the commercial banks which earned fee income from donor flows; sector-wide return on assets and equity improved in December 2014 to 0.1 percent and 1.0 percent respectively versus a return on assets of −0.7 percent in 2013, and return on equity of −5.4 percent. This improvement, when considered against the increase in NPLs, highlights the reliance on fee income (56.7 percent of total income).

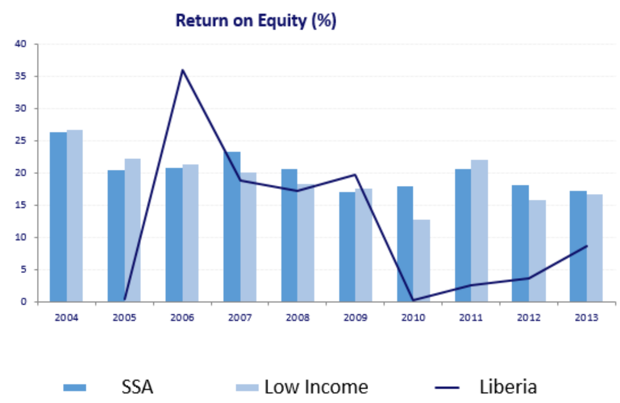
34. There are six main reasons for low bank profits:

- A high level of NPLs
- Low net interest margins (NIMs)
- Costly and unpredictable judicial processes
- A high operating cost base
- Dual currency economy
- Fraud by bank employees

35. The low/negative profitability of the Liberian banking system is unusual in Sub Saharan Africa, where banking systems are generally profitable, and in some cases highly profitable. Low profitability is of great concern, as it is indicative of deeper financial sector or economic difficulties.[19] It also points to possible stability concerns, as banks that are consistently unprofitable are at risk of failure. Low profitability also means that it is difficult for the banking system to expand to meet economic needs, as banks cannot use accumulated profits to expand their capital base and lending capacity.

[19] It is noted that the absence of a money market in Liberia has prevented banks allocating resources efficiently, this has been compounded by the limited scale of government debt issuance.

Figure 10: Liberian Banks' ROE



Source: The World Bank FINSTAT 2015/ Bankscope - Bureau Van Dijk.[20]

36. There is a danger that foreign shareholders, with alternative uses for capital, will be reluctant to support Liberian operations and will find more profitable outlets for investable funds elsewhere. At best, this could result in banks adopting a defensive strategy by lending only to customers with high-quality collateral or restricting operations to the more profitable and less risky business, for example, in Monrovia and closing unprofitable branches or lines of business. Some banks already appear to be taking this approach. There may also be a risk that banks, faced with reporting to their shareholders inadequate returns, could seek to disguise any credit-quality deterioration and delay required remedial action.

37. It is noteworthy that liquidity in the banking sector is high, even exceeding the CBL regulatory requirements, and the loan to deposit ratio is below regional averages. Together with the significant interest spread,[21] this would point to a reluctance to lend, leading to the relatively unusual circumstance of high interest spreads but low net interest margin and a greater dependency on fee income (cf. figures 11, 13).[22]

38. Regarding the question of CBL "guidance" on lending rates,[23] there are conflicting views as to what is the appropriate rate for lending in a highly dollarized economy. On the one hand it can be argued that rates beyond a certain rate are usurious and lead to adverse selection,[24] on the other hand, it is important that willing lenders are not restricted from financing viable projects. Constraining access to credit will inhibit the development of the system and its capacity to contribute to economic development more broadly, it may also lead to a greater degree of informality as borrowers revert to unregulated sources of finance. There can be consensus that the emphasis should be on improving the quality of loans and thereby the attractiveness of lending at an affordable rate. Issues of adverse selection need to be addressed through better information and enforcement so that good borrowers are offered appropriate rates.

39. An alternative explanation might be that competition is preventing banks from widening the margins (the issuance of licenses to a number of banks new to Liberia, in what is still a very small market, might support this); however, two of the banks are very specialized and some of the others are small, so the market leaders have substantial shares which, given the fairly rapid growth in lending business, might suggest that competitive forces may not be playing a major part in keeping margins low.

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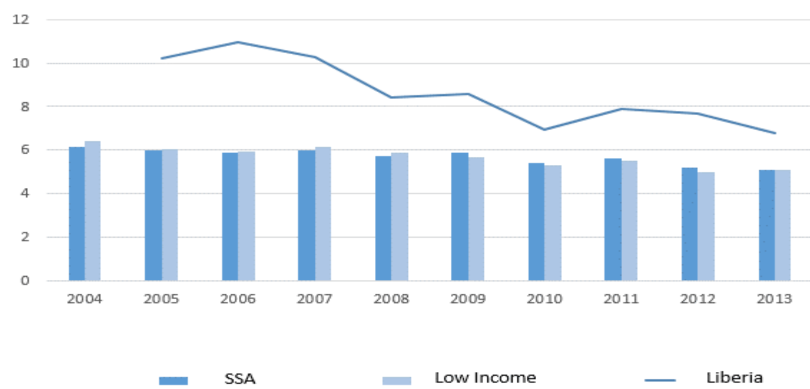
[20] Data from FINSTAT does not contain all banks, and while correctly reflecting direction of change, data from CBL is more exact.
[21] Particularly with regard to U.S. dollar financing.
[22] The apparent paradox of high spreads and low interest margin is explained by the low loan to deposit ratio and high provisioning costs.
[23] Eighteen percent was indicated as the borrowing rate ceiling guidance including fees and interest.
[24] Only risky borrowers will seek loans, or "good" borrowers will structure financing proposals so that the risk is commensurate with the rate.

40. Continued high credit risks and rising NPLs and high operating costs continue to squeeze profits and discourage lending activities of commercial banks. For example, bank operational costs (average non-interest expense per average earning asset) are high for Liberian banks with an average of 21 percent in 2011, while the net interest margin (average net interest income per average earning asset) is low at 6.2 percent as of October 2015. The low net interest margins lead banks to rely on noninterest income such as fees, wiring and remittances, which account for 57 percent of sector revenue as of October 2015. While certain individual banks are profitable, the sector as a whole is not, and has not been for several years. This continued absence of sector profitability represents a constraint for the further development of the sector. To some extent, this is the result of poor loan performance in the past but a number of other factors are hindering the expansion of the system.

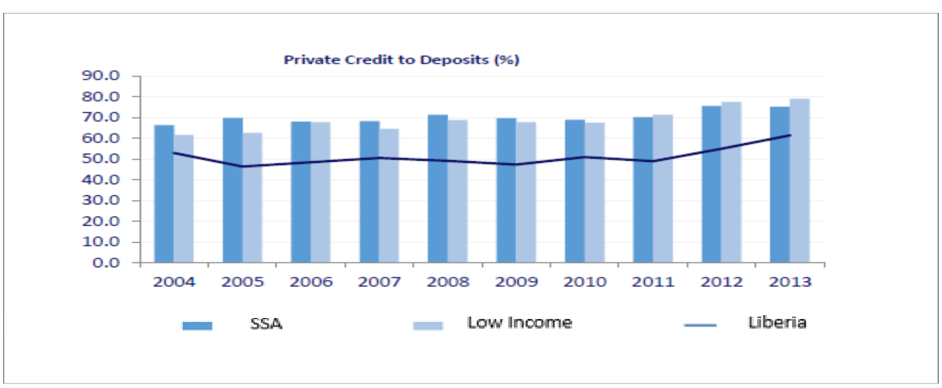
41. Some banks also draw attention to large loans in respect of government contracts, which are slow to be paid. The loans themselves are not guaranteed but such business is often done at low margins and may not be fully provisioned on the grounds that there is some implicit government support that will eventually ensure repayment; if unpaid interest on such lending is not converted into income, as should be the case, there will be a drain on profitability.

Figure 11: Interest Spreads Have Remained Consistently above Peers



Source: The World Bank FINSTAT 2015/ Bankscope - Bureau Van Dijk.[25]

Figure 12: The Transformation Ratio (Loans to Deposits) Has Been below Sector Norms

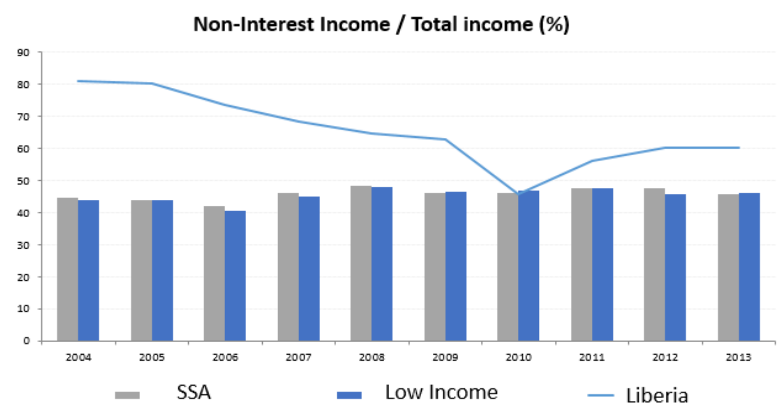


Source: The World Bank FINSTAT 2015/ Bankscope - Bureau Van Dijk.[23]

[25] Data from FINSTAT does not contain all banks, and while correctly reflecting direction of change, exact data from CBL should be used for exact data.

42. The second cause of low profitability is, as noted above, narrow interest rate margins. Especially where there are high NPLs, banks need to be able to price loans at a rate that is able to cover the risk of non-repayment. The net interest margin of 6.2 percent in October 2015 is relatively low by the standards of African banking systems. As a result of high NPLs and low NIM, banks are reliant on noninterest income (such as fees and commissions) for more than half (57 percent) of their revenue.

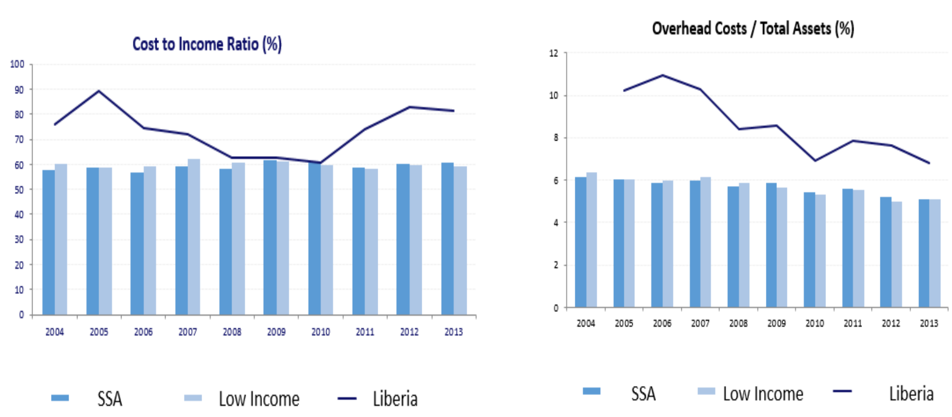
Figure 13: Unattractive Lending Environment Leads to Reliance on Fee Income



Source: The World Bank FINSTAT 2015/ Bankscope - Bureau Van Dijk.

43. A third contributor to low profitability is the high cost base of the banking system. With nine banks in a relatively small economy, Liberia may be on the verge of being overbanked. The banking business is characterized by significant economies of scale, and small banks may be relatively inefficient, high cost operations. Given the high fixed costs of banking (head offices, management teams, core banking and IT systems), small banks may not have the scale to spread these costs. In addition, it is expensive to run branch networks in Liberia, given unreliable power supplies and the high costs of transport and communications. Despite the relatively modest scale of the banking sector, seven of the banks are targeting more or less the same clientele (the urban commercial sector) and it may be appropriate to encourage consolidation. It is noteworthy that one of the smaller banks is owned by the bad-bank resolution agency of another country; in the recent international banking crisis, the standard practice has been that national resolution agencies divest overseas holdings.

Figure 14: Operating Costs Weigh Down Profitability



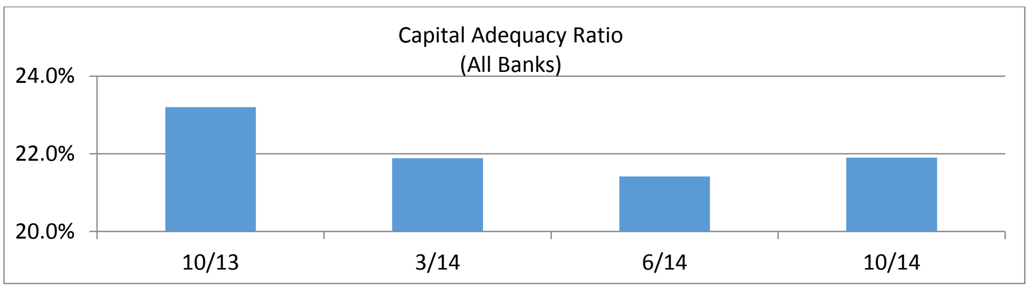
Source: The World Bank FINSTAT 2015/ Bankscope - Bureau. Van Dijk.

44. Fraud is reported to be widespread in the banking system, and the legal system not very effective at bringing perpetrators to justice even when they can be identified.

45. Another factor could be limited technical expertise and/or low-risk appetite of banks for lending in certain economic sectors, such as MSMEs, agricultural, manufacturing and housing sectors. Several banks have a strong record lending in these sectors in other countries, although it may be argued that the skills required for Liberia are different, and that the limited skill base in the workforce raises the cost of applying advanced banking techniques.

46. Despite low profitability, the capitalization of the banking system is high, perhaps too high given low bank profitability, which may induce the international banks that own most Liberian banks, to deploy capital elsewhere. Accounting standards are up to date and, if observed, assets should be adequately valued. If this is the case, then capital should be sufficient to support the current level of business. The capital adequacy ratio was 20.6 percent as of October 2015, down from 21.9 percent in October 2014 (due in part to loan write offs and losses),[26] but still indicating a well-capitalized banking system. The current capital requirement of US$10 million is relatively higher than some countries in the WAMZ.

Figure 15: Banks' Capital Adequacy Ratios 2013-–2014



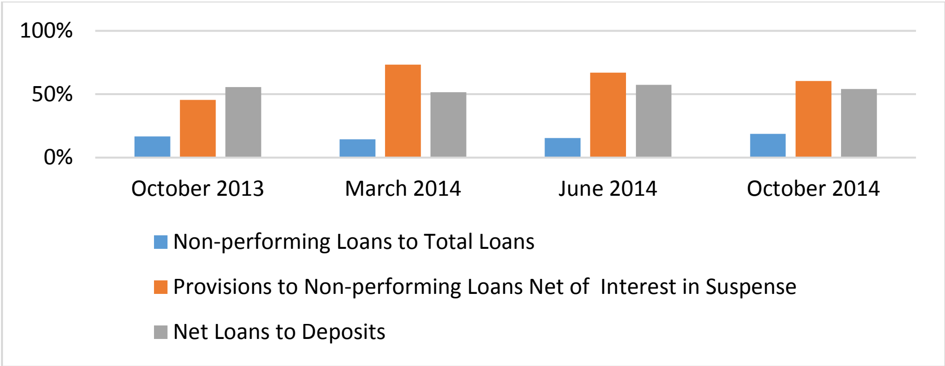
Source: CBL.

Asset Quality

47. NPLs have been one of the main causes of poor profitability. NPLs were reduced significantly between 2012 and 2013, due in part to stricter measures against delinquent borrowers, but have remerged in the last year, even before the Ebola crisis. Net of provisions, the present level is well supported by reported capital and if it were not for the low level of profitability discussed above, asset quality would not be a major concern. At one stage there was a significant problem caused by borrowers who were in a position to service their debts declining to do so with impunity. Such "strategic" NPLs have been a problem in many countries and require improvements in enforcement processes. In Liberia, the authorities have made substantial inroads to this problem by "naming and shaming" defaulters in newspapers, and denying them access to banking facilities. By depriving such borrowers of banking services, many of these offenders have been persuaded to honour their commitments. There appears to be a residual stock of such debts, presumably by now, adequately provisioned. Furthermore, some NPLs deemed unrecoverable were written off; this reduced the reported NPL rate, but came at a cost to profits and capital.

[26] CBL regulations require than loans categorized as "Loss" be written off within 2 years.

Figure 16: Key Loan Performance Indicators

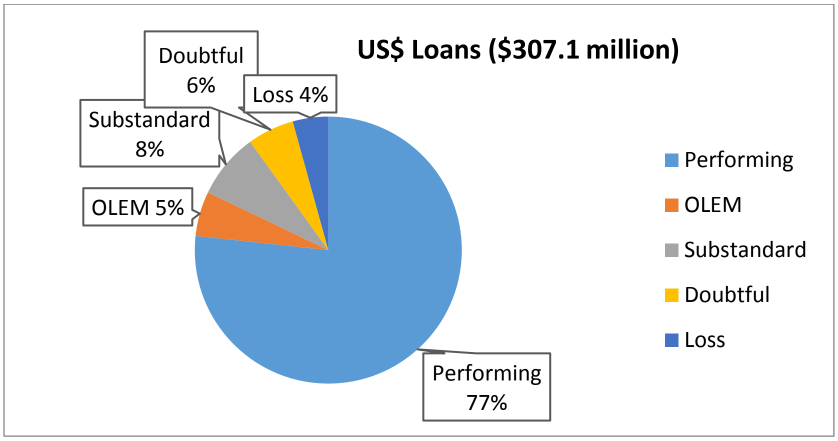


Source: CBL.

48. The high level of loan losses may also be attributed to poor underwriting standards at some banks, which makes recovery on some facilities difficult both operationally and legally.

49. As of November 2015, NPLs stood at 18.2 percent for US$ loans, substandard loans were 8 percent, doubtful 6 percent, and loss 4 percent. For LRD loans, doubtful loans are 11 percent of NPLs and other classification categories are similar to US$ loans. Between October 2014 and October 2015, NPLs decreased from 18.7 percent to 17 percent. Provisions to NPLs were 50.4 percent as at October 2015.[27]

Figure 17: Bank Loan Asset Classification in September 2014



Source: CBL.

50. A contribution to improvement in asset quality can be obtained by improving the ability of banks to secure their claims and to enforce the collateral they acquire. A step has been taken by establishing a registry for movable collateral. This is a useful reform, and should enable banks to expand lending for asset-based financing, benefitting the establishment of small businesses unable to offer fixed assets as security, but the bulk of collateral is still in the form of property. Moreover, some bankers maintain that even with registered collateral it is still necessary to go through the courts to realize a claim and the judicial process remains unpredictable and costly. Mortgage lending depends on the efficacy of the land register so that banks can be confident in the ownership of the asset pledged and can mitigate the risk of the asset being pledged to another creditor. The Liberian land register is very outdated and registering interest in land is slow and cumbersome, the system is manual and inefficient, and there are reports of properties being pledged multiple times.

[27] CBL regulations prescribe 100 percent provision for Loss category, 50 percent for Doubtful, 20 percent for Substandard and 5 percent for OLEM (Other Loans Especially Mentioned).

51. Cases are reported of conflicting claims, which effectively means that lenders have to treat loans against real estate as virtually unsecured if the pricing is to reflect the risk adequately. Reforming a land registry is a major task, which will take some time to complete and will need to be well designed. However, it should nevertheless be a priority for the authorities. The establishment of Land Reform Commission is a positive step in addressing this constraint.

52. Some progress has been made in the administration of the courts, with the establishment in 2009 of a specialized commercial court.[28] The Commercial Court is reportedly having some impact on promoting a repayment culture among borrowers (along with the process of naming and shaming defaulting borrowers). Banks have already taken action, or threatened to take action, through the court against a number of delinquent borrowers and this has resulted either in the rapid repayment of loans or the successful and relatively quick foreclosure on secured properties. However, banks report that they often do not have effective remedies in cases of nonpayment by borrowers attributable to court decisions that are inexplicable in relation to the applicable law; high legal fees of lawyers representing them based on a high percentage of the claim; and the need to post a bond for the amount of the claim[29] to lodge an appeal with the High Court. Recalcitrant borrowers know this and banks often compromise a claim for much less than they are owed which significantly affects bank income.

53. Finally, asset quality is crucially dependent on the quality of risk management in the banks. Liberia can benefit from the fact that most of the banks are subsidiaries of larger banking organizations operating in other countries, and can take advantage of training and procedures developed elsewhere within financial groups. The ability of the authorities to improve risk management in banks is limited, although an indirect effect can be obtained through the supervisory processes, and a guideline on risk management has been issued to the banks. There is also a need to upgrade the credit reference bureau (discussed below).

54. The CBL made it a specific policy objective in 2012 to broaden the scope of financial services. One of the measures is the development of a financial leasing capability. The development of leasing as a complement to bank loans would provide an alternative solution for financing capital investments such as equipment, and could expand the available pool of medium and long-term finance to SMEs, and make it easier to repossess leased assets than executing on collateral for an ordinary secured loan. There is now a chapter on financial leasing in the Commercial Code that was developed in collaboration with the International Finance Corporation (IFC).

Liquidity

55. The percentage of banks' liquid assets is relatively high compared to total assets and to short-term liabilities and to bank liquidity in many other countries. According to some banks this is attributable to the structure of their deposits, largely demand and short-term time deposits. This has a negative effect on the volume of credit to the economy; if deposits had longer maturities, bank loans could be for longer terms for simple asset-liability management which could finance capital expenditures for enterprise expansion. Demand deposits were 61.7 percent of total deposits at end-October 2015.

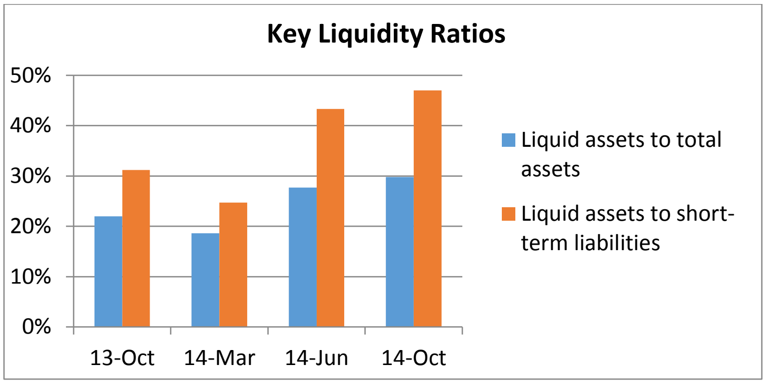
56. The pattern of deposit withdrawals should be well established and since banks can borrow from the CBL for liquidity needs if they have adequate high-quality collateral, holding excessive liquid assets may not be necessary. The development of a Treasury Bill market provides additional tools for liquidity management (and may also represent a new source of income for the banks).

[28] The Commercial Court, which came into operation in 2011, accepts cases above LRD 1 million. It consists of a panel of three judges.

[29] These insurance bonds are themselves expensive, as much as 10 percent of the claim amount.

57. As one measure to address the short-term liability constraint of banks, the CBL has made available to the banks longer placements at concessionary rates through various stimulus packages for lending to critical sectors in the economy such as MSMEs, agriculture and housing.[30]

Figure 18: Liberian Banks' Liquid Assets



Source: CBL.

Table 5: Selected Bank Performance Indicators

Indicator	October 2014	October 2015
Capital adequacy ratio	21.9%	20.6%
NPLs to total loans	18.7%	17%
Net loans to deposits (SSR 75)[31]	54.0%	63.3%
Liquid assets to net assets (SSR 76)	31.3%	27.7%
Liquidity ratio	48.2%	39.1%
Return on assets (SSR 70)	-0.6%	-0.86%
Return on equity (SSR 71)	-4.5%	-6.99%
Noninterest income to total revenue (SSR 73)	51.0%	57.0%
Net interest margin over average assets	6.5%	6.21%

SSR = Standard Statistical Return.
Source: CBL Annual Reports 2014, 2015.

Money Markets

58. The efficiency of markets for financial assets is important for financial sector development. The CBL and the Ministry of Finance and Development Planning have issued short-term high-quality debt instruments denominated in LRD, in the form of central bank bills and treasury bills, respectively. However, the primary market is still somewhat erratic and the rates derived from it have been volatile and the process does not yet appear to have reached a stage where it can be used as a benchmark for determining interest rates on nonmarketable bank assets and liabilities. Moreover, there is at present no secondary market so the instruments do not provide much source of bank liquidity. The banks have to rely as a result on excess reserves in the central bank for liquidity management purposes. To use treasury and CBL bills for this purpose, banks need to be able to invest sizable amounts and liquidate them without moving the price substantially against them.

[30] These facilities are discussed further below.
[31] The increasing difference between Gross and Net Loans reflects the high degree of provisioning.

59. Moreover, the absence of a market in liquid assets means that banks cannot offer fixed interest rate products as they cannot easily hedge their exposures. Increasing volumes of issues of the current instruments and experience of the market players will resolve some of these problems although there may be other more structural impediments that the CBL can address.

60. Consideration should be given to establishing a master repurchase agreement for transactions in the interbank market including between the CBL and banks. This would provide confidence for banks with less liquidity to lend more actively, on the understanding that they would be able to access liquidity through the repo market if required. To minimize the risks in the event of counterparty default, a framework convention for repo operations analogous to the framework conventions used internationally would provide that the lender (buyer of a financial instrument) stands in the position as the owner of the repoed financial instrument rather than as merely a secured creditor and would avoid any inefficiencies of the judicial debt collection process.[32] The use of Collateralized intraday lending based on T-Bills and CB Bills can also be used as a source of liquidity in the planned RTGS system.

Impact of the Dual Currency Regime on Banking

61. Liberia's dual currency regime, where both the LRD and the U.S. dollar are legal tender, introduces additional complications to the banking sector. With two legal tender currencies, banks may obviously take deposits and make loans in both currencies. Ideally, with no exchange controls, funds should flow freely between the two currencies depending on customer preferences and needs, and prices (including the exchange rate and interest rates) should adjust appropriately.

62. According to CBL figures, 93 percent of all loans were in U.S. dollars (October 2014) and around 82.1 percent of all deposits (November 2015). Banks report that there is a strong preference for borrowing in US$, in part because a significant part of bank credit is used to finance imports. Banking operations are essentially segmented: an excess of LRD deposits over lending results in excess LRD liquidity, which has to be absorbed by the CBL. The increased issuance of Treasury Bills, denominated exclusively in LRD, may ameliorate this imbalance. The excess LRD liquidity coexists with a shortage of US$ liquidity, where US$ deposits (minus reserve and liquidity requirements) are inadequate to fund US$ lending demands. This segmentation is compounded by the nature of the FX auction system, which does not allow funds to flow freely between the two currencies. As a result, importers are unwilling to borrow in LRD—even with a much lower nominal and real interest rate—because of uncertainty about their ability to convert LRD to US$ on demand. The dual currency system also reduces a usual source of bank income—FX trading—which is often an important revenue source for banks.

63. Liberia is unusual, but not unique in having a dual currency regime, use of a foreign currency deprives the authorities of the means of exercising monetary policy and the central bank of seigniorage income. The U.S. dollar has a long history of usage in Liberia, having replaced the West African Pound as the national currency in 1935. LRDs have circulated in parallel, originally circulating only as coins, from 1937, but also as notes since 1989. Liberia parallels the past experience of countries such as Israel and Cambodia in having introduced its own currency but having made limited progress in persuading users and intermediaries to use it in preference to the U.S. dollar. U.S. dollar deposits constitute 82.1 percent of the banking system deposits. However, not only is the U.S. dollar used in transactions in the banking system, but U.S. dollar notes also form a major part of the currency in circulation. Restrictions on the import and export of U.S. currency, even in the absence of other exchange controls, impede the efficiency of the FX market both for cash and bank deposits such as to inhibit further use of the LRD. The cost of obtaining U.S. dollar notes from the CBL, and for replacing old and damaged notes, is cited by the commercial banks as an important cost of doing business in Liberia.

[32] It also needs to be ensured there is a sound legal basis for ensuring protection of collateral rights.

64. The CBL's low income is also caused in part by the dual currency regime by reducing seigniorage income and is compounded by the low yields on investment of reserves in the current climate as well as by limited income from credit to banks because of high levels of bank liquidity at present.

65. A by-product of the bi-currency system is that much of the statistical framework is missing. It is difficult to draw a clear distinction between nonresident and resident transactions. Moreover, the absence of capital controls, combined with the domestic use of U.S. dollars makes it difficult to distinguish between overseas and domestic financing. Payments that appear to be to nonresident may in fact be resident but in US$ or involve an FX transaction. The market for US$/LRD appears to work in an unusual way. The auction run by the CBL has delivered rather unpredictable rates which appear to make bank customers, with US$ transactions to finance, reluctant to borrow in LRD as they will be faced with exchange rate uncertainty at the time of draw down although it might make sense to borrow in LRD if that is the currency which is the source of repayment. There are also complaints by banks that they are not permitted to import US$ currency directly and must obtain supplies from the CBL. For banks to be able to manage their US$ liquidity better will require a deeper FX market including a US$/LRD swap market.

Foreign Exchange Bureaus

66. The CBL had licensed 122 FX bureaus as of 2015, an increase of 9.9 percent from 111 FX bureaus in 2014. FX bureaus are permitted to participate in the CBL's foreign exchange auctions.

Training of Bankers

67. To encourage capacity building in the banking sector, the CBL, in collaboration with the Liberia Bankers Association (LBA), in 2012 supported the training program of the Banking Institute of Liberia for staff of commercial banks. Courses offered have included Treasury Management Operations, Credit Risk Management, and Internal Audit and Compliance. Meanwhile the Bankers Association in consultation with the CBL, intends to transform the Institute into a full-fledged training institution that will not only deliver training to bank staff but also for local college graduates looking for employment in the banking sector. Since its inception, the Banking Institute of Liberia has trained 254 staff of commercial banks in various areas of banking.

THE INSURANCE SECTOR

68. The insurance sector consists of 20 companies with 31 branches. Main lines of business underwritten are motor, group health, life, engineering project bonds, and marine cargo. Most of the companies concentrate on short-term insurance. The largest class of business is motor (which is in principle compulsory), and most insurance sales are to corporate clients; there is little business sold through brokers or agents. Except for brokering fronting arrangements directly between large international firms operating in Liberia and multinational insurers (thus bypassing the Liberian insurance market), brokers play a limited role. Total assets of the insurance industry as at September 2015 were US$42.1 million, total liabilities US$18.5 million, and gross premiums were US$31.8 million.[33] Total premium income, at around 1.6 percent of GDP, is in line with the average level of premium incomes in Sub-Saharan Africa.

69. The National Insurance Corporation of Liberia (NICOL) is government owned and has a monopoly on Government business. The NICOL Act provides that only the Corporation can insure assets belonging to the Government. Although viable before the civil war, the Corporation has been basically inactive since the war, largely attributable to undercapitalization and has ceased to underwrite new business since 2013. It is currently managed by an interim management team with a subsidy from the Government. NICOL falls under the Insurance Regulations and is not currently licensed to operate by the CBL. NICOL historically provided reinsurance for the Liberian market and since its cessation of operations there is no domestic reinsurer (although Liberia is a shareholder of Africa Re). Given the contradiction between the monopoly position to NICOL for government insurance and its current inactivity, the NICOL Act needs to be reviewed.

70. The 20 companies now operating represent a reduction from 24 before CBL regulation; however, a preliminary review of market participants suggest that only a small number of companies have appropriate professional capabilities and are financially strong. There is also scope for concern that in some cases premia collected may be less than what is needed to offset the risk in the market or adequately compensate for risk retained. The CBL placed a moratorium on issuance of new licenses and it may be necessary for consolidation to take place, to seek to ensure that insurance companies have the financial and managerial resources to comply with new regulatory requirements and to benefit from economies of scale.

71. There are three insurance brokers whose sales are relatively small. Most insurance is sold by employees of companies themselves. Much insurance is reinsured with offshore companies and given the limited financial capacity of Liberian companies, a more substantial portion of the premiums are paid to these reinsurers.

[33] CBL 2014 Annual Report, pp. 54-55.

BANKING AND INSURANCE SUPERVISION

72. Given the significance of banking for the financial sector in Liberia, maintaining sound banks is of vital importance. There are three essential components of effective supervision. The first is a comprehensive legal framework. The second is the possession of adequate skills and human resources. The CBL has clearly benefited from considerable technical assistance in developing its supervisory capacity and adopting modern risk-based methods. The CBL also continues to provide the needed and requisite support towards strengthening the Regulation and Supervision Department (RSD). In addition to participating in specialized professional examiners' training programs, staff of the RSD also participate in the Financial Stability Institute online tutorials.

73. The third, and often the most vital element, is effective enforcement. In many countries the powers are there and the problems are analyzed but effective action is not taken. An agreement of the bank supervisor with the board of directors of a bank for the bank to take remedial action for regulatory violations is often the most useful enforcement measure a supervisor can take. Reportedly the CBL has on a number of occasions signed such MoUs with more than one problem bank. In addition, the CBL has adopted a more rigid approach of issuing supervisory directives to the boards requiring enforcement of specific remedial actions by the board of directors of financial institutions, which has been as, if not more, effective than a MoU.

74. The legal framework for supervision is based on the Central Bank Act and the New Financial Institutions Act. Both of these date from 1999 and have not been materially revised since (amendments to the CBL Act were prepared in 2014 but have not been ratified). Although the laws have met the tests of time fairly well, they are certainly due for a review to reflect supervisory developments over the past 15 years. The limitations and controls over related-party transactions prescribed in the New Financial Institutions Act (1999) could be strengthened; the Act only places limits that such loans must not be on preferential terms and proscribes the remission of such debts.[34] The law and regulation on the aggregation of exposures for the purposes of the large exposure limits could also be given greater precision.[35] As the system is so dependent on banks with foreign shareholders, the CBL requires the ability to vet and approve actual or potential changes in ownership and needs robust powers to reject unsuitable applicants.

75. The CBL has powers under the laws, for example, Section 39 of the New FIA, to make regulations and issue guidance.[36] It has exercised those powers extensively and issued a number of regulations implementing the main supervisory rules and procedures that banks are obliged to follow. These are published (together with the laws) on the CBL's website. The style of the rules varies considerably, perhaps attributable to the sources of the advice on which they have been based, and there is a need for more precision in legislative and regulatory drafting, a clear distinction between wishful thinking and obligatory rules of conduct, and a more logical framework to make it easier for those affected to consult and implement them.[37] A review of the laws could therefore, be followed by a review of the regulations designed to catalogue them so as to make them more user-friendly. This process would also expose any gaps that supervisory practice might have revealed. The RSD has already taken step in this direction by establishing a Register of CBL Regulations, Directives and Supervisory Guidelines.

[34] Related-party transactions are a major source of risk and in other jurisdictions are often strictly limited in scale and require explicit disclosure.

[35] While CBL regulations state that "...the aggregate of the large exposures shall not exceed fifty (50) percent of the bank's total credit extensions", it does not clarify how to limit the number of borrowers.

[36] To become effective a regulation must be published in the Official Gazette and this is authorized by the Ministry of Foreign Affairs. This appears to be anomalous since presumably the Ministry could block regulations from being issued or require their amendment in inappropriate ways from the viewpoint of effective regulation.

[37] An example is the Regulation on Corporate Governance of Financial Institutions, CBL/SD/001/2012 which contains some rules that are for company law, rather than for regulations, and some that are impractical for being excessively onerous both for regulated entities and for the RSD.

76. With respect to the Basel II pillars, the Regulation and Supervision Department (RSD) of the CBL is adopting the standardized approach to capital adequacy, has a more risk-based approach to on-site supervision, and is working on enhanced disclosure by the banks for market discipline. In 2014, the CBL introduced a Resident Examiners Attachment Program (REAP) which involves the assignment of CBL examiners at various commercial banks, and is intended to further enhance the examiners' understanding of commercial banks' operations, risk profile and institutional setup, as a means of developing the appropriate supervisory strategy and plan for each bank, in line with the risk-based supervision framework.[38] In 2014, the CBL issued Stress Testing Guidelines for commercial banks to assist banks in preparing and implementing their internal stress testing frameworks, and to conduct one stress test, at least semiannually.

RSD Strategic Plan

77. The CBL adopted a 2014–2018 strategic plan for the RSD. One of the four strategic goals addresses strengthening the work of the RSD along the lines of the assessment recommendations. This includes conducting macro-prudential analyses; improving engagements with stakeholders of financial institutions; and improving the legal, regulatory and accounting frameworks for financial institutions. The plan also mentions projects for a crisis management framework and financial safety nets. These important projects, of course, go beyond the work plan of one department of the CBL and also involve the MFDP for crisis management and the National Assembly for a deposit insurance law, possibly an insurance policy holder protection scheme, and a modern financial institutions resolution law.

Reform of Bank Supervision Activities

78. In accordance with its current Strategic Plan, the Regulation and Supervision Department (RSD) is undertaking a review of the existing legal and regulatory framework to address weaknesses or gaps; develop frameworks for financial safety nets, including the establishment of a deposit insurance scheme to provide greater protection for depositors, develop a crisis management framework to manage crisis at both individual and systemic levels, and develop a procedural framework for the CBL's liquidity support to troubled banks.

79. The IMF conducted a review of bank supervisory capacity development in 2014; among the 17 recommendations for further strengthening of bank supervision were the following:

- Assess the technical and implementation dimensions before the introduction of new regulations and/or initiatives.
- Ensure a participative approach in discussions with stakeholders and provide sound, clear and persuasive rationalization for the relevance of proposed reforms.
- Develop and implement a financial stability/macro-prudential surveillance capacity.
- Review and update the Financial Institutions Act.

80. This FSDIP highlights some of these recommendations. The first two items are under the rubric of regulatory governance in annex 5 and the third item is discussed, including the consideration of a financial stability council, in annex 3. The need for revising legal provisions for the important matter of financial institution resolution is discussed in annex 4 and would be a key part of updating the New FIA (1999).

81. Other recommendations stemming from the IMF technical assistance include optimizing off-site supervision by including an automated banking supervision system; developing and implementing a structured on-site examination approach for corporate governance, risk management, internal controls, and internal audit; and developing and implementing a legal and regulatory framework for consolidated supervision.

[38] CBL 2014 Annual Report, p.52.

82. The RSD is also currently conducting a self-assessment with respect to the CBL's compliance with the revised Basel Core Principles (BCPs) for Effective Banking Supervision with the view of identifying areas of weaknesses in the existing legal framework and take actions to upgrade both the CBL Act and new FIA, where necessary. This exercise is expected to be completed by the end of the year. The Department recognizes the need for an external assessment in the near future as part of the reform efforts of the banking system.

83. To achieve its critical goals in line with its Strategic Plan, the RSD has established several task forces/working committees, which include the following:

- AML/CFT Task Force
- IFRS Task Force
- Self-Assessment of BCPs Working Group
- Financial Literacy Working Group
- Rural Community Finance Task Force

Insurance Supervision and Regulation

84. The CBL assumed supervisory responsibility for the insurance sector in 2011. In keeping with its mandate under the New Financial Institutions Act of 1999, there have been substantial positive developments in the legal, regulatory, and supervisory practices. There is a new Insurance Act consistent with IAIS Principles that came into force in 2013, a comprehensive set of prudential regulations have been drafted, and long-term training has been undertaken for the RSD Insurance Unit staff at the West African Insurance Institute and attachment programs with other insurance regulatory agencies in the sub-region.

85. The regulations include licensing, prudential requirements, business conduct, and reinsurance and appear to be consistent with best practices. Implementation will be a challenge for a sector that up to now had not been subject to comprehensive regulation. Regulations brought into place under the new law prescribe an increase of minimum capital requirements (US$1,500,000 for general insurance business, US$750,000 for life business, and US$5,000,000 for reinsurance business) which are to be paid over a 3-year period from 2015 through 2017. This requirement is likely to further reduce the number of insurance companies operating in Liberia and contingency plans for an orderly transfer of insurance business should be developed.

CREDIT INFORMATION SYSTEMS

86. In the 2016 "Doing Business" survey, Liberia ranked 109th for getting credit, up 51 places from 160 in 2015, this relatively low ranking, reflecting revised criteria, is largely due to Liberia's public credit registry coverage of only 1.8 percent of adults compared with 5.8 percent average in SSA and 11.9 percent average in high income Organisation for Economic Cooperation and Development (OECD) countries, and zero private credit bureau coverage compared with 25.6 percent of adults average in SSA. In the Bank's 2016 Doing Business survey, the ranking of Liberia for depth of credit information index is "0," mainly because the coverage is too low: 38,811 adults are reported in the credit registry, representing 1.8 percent of adults.[39]

87. The CBL currently operates an Excel worksheet–based system of collecting credit information from lenders which it regulates, the system is manual and does not allow for online access. This system was installed in 2009 and intended to be only a temporary measure. It has provided lenders (only banks) with basic information (not credit scores) on the credit exposure of prospective borrowers (both firms and individuals and without limitation on loan amount). Both positive and negative credit data is distributed, but only for the time of the query (historic data is not provided). Despite the improvement that the Excel information sharing system has enabled, it is prone to manipulation, fraud, human error and abuse.

88. The credit registry system developed by the CBL is intended to allow lenders to submit inquiries to the CBL and these inquiries are matched against a database representing all derogatory information concerning credit reported in the previous month. The purpose of the Liberian credit registry is to prevent a lender from granting credit to a credit applicant who is currently not meeting his/her repayment obligations. Historic delinquencies are not properly retained.

89. Data sharing and access to the system are facilitated by a highly manual process:

- **Data Sharing:** All 9 banks participate in this process and are obligated to report their NPLs to the CBL within 10 days at the beginning of each month. The data submission is performed by sending an Excel spreadsheet to the CBL where a staff member combines all spreadsheets into a workbook for the specific month. Lenders are not adhering to the homogeneous reporting standards prescribed by the CBL.
- **Data Access:** Inquiries are submitted in writing. The inquiry volume varies between 200 and 300 inquiries per day. An inquiring lender would submit a letter listing all credit applicants for which a check against the spreadsheet for the previous month is requested. The CBL commits to responding to all enquiries within 48 hours of receipt of the inquiry.

90. Major components that would be considered standard features of a credit information system are missing: (a) other than the last reported month, the system does not build and display performance histories; (b) data suppliers are required to continue to report delinquencies (even if they have been paid up) for two months; (c) matching is done on a purely manual basis.

91. The staff member performs a 'Find' function on the spreadsheet based on the name provided on the inquiry request letter and is therefore highly dependent on the inquired name and names contained in the spreadsheet to match. The search, match and merge processed are lacking any form of sophisticated match algorithm and are purely based on human intervention, accuracy, and creativity; (d) similar or identical names will lead to several possible matches, all of which are reported back to the inquiring institution; (e) no access control principles are employed and there is no track record of any changes that might deliberately or accidentally occur; (f) from a data security and privacy point of view, data collection and storage as well access control principles are inadequate; (g) there is no consumer access protocol and no dispute resolution process defined. Complaints about data inaccuracies are handled impromptu.

[39] This implies that the adult population is 2,283,000, out of the total population of 4,294,077.

92. The processes developed around an Excel spreadsheet do not meet any of the standards employed at even the most basic credit information systems around the world. In particular data security and privacy concerns coupled with the lack of dispute resolution capabilities and an unquantifiable high margin for error render this solution unsuitable for supporting the expansion of credit into currently underserved segments of the Liberian financial services market.

93. Further, the system in use in Liberia does not allow the CBL to perform off-site banking supervision of the system and the existing legal regime requires a comprehensive review by a legal expert with the view to improving the overall credit information-sharing environment and the adoption of international best practice principles.

94. The New Financial Institutions Act of 1999 and the Credit Reference Bureau Regulations of 2010 provide the legislative framework for credit information sharing by mandating licensed financial institutions to share credit information data with credit bureaus as well as consult a credit bureau when advancing credit. The current legislation allows for the sharing of positive and negative information without consent by licensed financial institutions but is silent about the requirement to obtain consent by non-licensed financial institutions. In general terms, the regulation in place, which was developed with technical assistance from IFC, contains the major elements of a framework for credit reporting; however, some of the requirements and obligations placed on the bureaus are very stringent and may discourage potential service providers from establishing a business in the country. Regulation 5.2 (i) states that "every data provider shall (a) inform any person with whom it enters into a contractual agreement relevant to this regulation; that it shall provide information in relation to such agreement to a credit reference bureau in accordance with this regulation." The 2010 regulations allow borrowers the right to access their data in the case of a private bureau (but this does not extend to the current system).

95. Credit Reference Systems are a critical part of financial sector infrastructure. They yield benefits that go beyond establishing the indebtedness of an individual to a financial institution at a point in time. If properly structured, they have the capacity also to provide the following benefits:

- A means to generate holistic credit histories of SMEs and entrepreneurs
- A means for responsible and credit worthy entrepreneurs and SMEs to take advantage of their credit histories by shopping among the banks for better credit terms
- Increased competition among the banks and therefore greater incentives to look at currently ignored sectors
- A means to regulate mobile money and ensure that such instruments do not breach anti-money laundering and antiterrorism financing rules
- A means to ensure effective oversight by the Central Bank of the banks' Know-Your-Customer (KYC) obligations

96. The CBL has also been debating the structure of a proposed credit reference bureau and has expressed desire to move forward with its development in the near future. As Liberia is such a small market, one option (similar to that adopted by many other similar jurisdictions globally) would be to adopt a "hub and spoke model" where the actual solution is hosted by an international credit reporting service provider. However, it is understood that the CBL preference is that the solution be onshore based on concerns of protecting client information and promoting local knowledge and capacity. This has hindered a private sector solution as volumes have not been sufficient for commercially viability and long-term sustainability.

97. There is continued, and in fact increased, interest in developing such a scheme and there is some hope that a public-private arrangement might be reached between the Central Bank and the commercial banks. The rudimentary Excel spreadsheet system which was established by a World Bank consultant in 2009 is now reaching the limits of its usefulness in the face of increased demand (and it is in any case vulnerable to abuse and error). Given the important role such a registry can play in improving the credit culture, it would be desirable to revisit the economics of the development of such a scheme.

98. An effective and widely used facility would enable banks and other financial institutions to assess credit risk more accurately and quickly. The existing system is fairly basic and was apparently designed only as a stop-gap measure. There are now much more efficient systems available off the shelf. The economy generally should benefit from a more efficient system incurring lower costs of financial intermediation especially if the system is available to all creditors including utilities and other providers of credit. An improved credit reference bureau would also improve the credit quality of small nonbank lenders.

Credit Reference Regulation

99. In general terms, the Credit Reference regulation of August 6, 2010 contains the major elements of a framework for credit reporting; however, some of the requirements and obligations placed on the bureaus are very stringent and may discourage potential service providers from establishing a credit reference business in the country.

100. The following is a brief analysis of the items in the law, with regard to the role of the Central Bank, that are challenging and the ones of most concern are highlighted in italic.

- Internal Credit Arrangement by the Central Bank:
    - The Central Bank may maintain and conduct its own credit reference bureau in accordance with this regulation until there is a privately operated credit reference bureau that the Central Bank deems capable of providing credit reference bureau services in Liberia. Upon such determination, the Central Bank shall cease its credit reference bureau operations.
- Licensing:
    - This section establishes the conditions for issuing, revocation or suspension of the license to the credit bureaus. Some of the most relevant are as follows:
        - Only registered companies can apply for license.
        - Non transferrable
        - *Licenses granted must be renewed every year*.
- Activities and duties of a Credit Bureau:
    - This section establishes the permissible activities of a credit bureau. However, it does not establish clear rules for the credit bureaus, but rather it gives the Central Bank the power to act independently in determining such rules as it deems convenient. The lack of clarity within the law may discourage some credit reporting companies from investing in the country. Some of the most relevant items in this section are as follows:
        - The Central Bank may establish a maximum fee that may be charged by the credit bureaus for its services.
        - A credit reference bureau shall not engage in activities not specified in this regulation, or directives or guidelines promulgated or issued by the Central Bank from time to time.
        - Every credit bureau shall accept the filing of information from the data provider on such terms as expressly permitted by the Central Bank.
        - Not prejudice the assessment of a person's creditworthiness merely on the basis that the credit reference bureau does not have credit information concerning that person. This is a decision that the credit providers make, not the credit bureau. The bureau only provides the information that was submitted to them. The only instance when a credit bureau may be considered to make an assessment of creditworthiness is when it develops credit scoring models which is a good general practice.

- The following are responsibilities assigned to the Credit Bureau, that are usually the responsibility of credit providers, since it is very difficult, costly and impractical for the Bureau to comply:
  - ✓ The Credit Bureau must verify that the recipient of the information (credit provider) has a lawful reason for obtaining such credit information. The Credit Bureau must receive certification in writing from the credit information recipient *in each instance in which a request for credit information is made*,[40] such that the recipient will use the information to:
    - ❖ evaluate credit risks in the granting, monitoring or extension of credit;
    - ❖ evaluate risks where the terms of the credit agreement are changed;
    - ❖ evaluate risks related to other transactions with deferred payments;
    - ❖ confirm the accuracy of information contained in a credit reference report;
    - ❖ underwrite insurance;
    - ❖ evaluate an employment application; or
    - ❖ further some other legitimate business needs relating to a transaction initiated by a person.

[40] From a practical perspective some kind of a master agreement concept could be used.

PAYMENT SYSTEMS AND DIGITAL FINANCIAL SERVICES

Current Payment Practices

101. In its present form, the Liberian payment system is predominantly cash based. Electronic funds transfers (EFTs) are available for intrabank transfers but not interbank (that is, within banks, but not between them). In 2001 the CBL started the operation of its mostly manual cheque clearing, which still forms the predominant interbank payment system in the country. Cheque volumes are relatively low, banks meet once daily to physically exchange cheques and the net positions are calculated by using an in-house developed PC-based system. The cheque clearing system has an interface to the CBL's core banking system (Bankmaster) for the settlement of the net positions. The maximum cheque clearing cycle is three days, however, the standard time within Monrovia is 1 day.

Table 6: Financial Infrastructure Indicators, for Selected ECOWAS Countries, 2013

	Benin	Burkina Faso	Cote d'Ivoire	Ghana	Guinea	Guinea-Bissau	Liberia	Mali	Niger	Nigeria	Senegal	Togo
Commercial bank branches per 1,000 km^2	1.68	0.79	1.76	4.1	0.48	0.92	**0.97**	0.35	0.11	6.21	1.9	3.36
ATMs per 1,000 km^2	2.25	0.9	2.2	5.7	0.36	1.35	**0.51**	0.28	0.09	14	2	3.51
Outstanding deposits with commercial banks (percentage of GDP)	41.07	35.48	32.22	31.91	13.06	22.51	**37.84**	32.36	17.55	40.68	37.81	51.08
Commercial bank branches per 100,000 adults	3.31	2.42	4.83	6	1.81	2.67	**3.9**	5.51	1.56	6.01	4.72	4.74
ATMs per 100,000 adults	4.43	2.74	6.04	8.32	1.34	3.91	**2.05**	4.37	1.34	13.54	4.97	4.95
Outstanding loans from commercial banks (percentage GDP)	30.78	30.12	24.33	23.27	4.98	17.14	**21.32**	25.55	16.43	24.39	35.07	42.52

Source: IMF financial access database.

102. At present there is high reliance on cash, with both U.S. dollars and LRD widely used; the latter tend to be used more for low value transactions. The current high level of reliance on cash is expensive and risky. Large volumes of cash are currently moved around the country due in part to the lack of bank branches. High use of cash also creates opportunities for fraud, over and above the risks of theft and robbery. Furthermore, the high use of cash and associated transactions costs restricts access to finance by making low value products such as micro-loans and micro-insurance unviable. Cheques are used mostly by the GOL, but the volume of cheques issued is very low (estimated at 3,300–4,400 per month). Cheques are supposed to clear within three business days. Manager's Cheques (similar to cashier cheques) and CBL cheques, which should have same day value, still require three business days to clear to prevent cheque forgery, which plagues the banking industry in Liberia. Cheque processing is manual. However, the WAMZ payments system project involves the automation of cheque processing. Machine readable (MICR) cheques are being introduced, along with processing equipment at bank branches and head offices, and a communications network linking bank head offices to the CBL. An automated clearing house (ACH) for processing cheque transactions is being installed at the CBL.

103. Interbank card transactions (ATM withdrawals or card payments) are only possible for customers of those banks that are part of international card networks. A local switch is currently being implemented. Several banks issue debit cards. Some are Visa or MasterCard branded and hence are usable internationally, and can be used at the ATMs/POS Terminals of other Liberian banks that have the same affiliation. Because of the lack of a local card schemes, cards issued without an international card brand can only be used at the issuing bank's own ATMs and/or POS terminals.

104. Liberia's dual currency system also introduces complications, not least by requiring payment systems to accommodate clearing and settlement in two currencies. With respect to cash, the LRD is used more for low value transactions, reflecting both available note denominations as well as preferences and risk aversion. The bulk of noncash transactions are in U.S. dollars.

105. Given the high costs of both cash and branch-based banking in Liberia, it can be anticipated that mobile phones and potentially other electronic/digital channels will play a crucial role as a platform to extend the reach of payment, banking and other financial services to those who are currently unserved or underserved by financial service providers, especially rural and low-income urban households. However, for the time being network coverage in rural areas is still not complete (but is still much better than bank branch coverage).

WAMZ Payments System Development Project

106. The CBL has embarked upon a payments system modernization project linked to theUS$30 million WAMZ Payments System Development Project in The Gambia, Guinea, Liberia and Sierra Leone funded by the African Development Bank in collaboration with West African Monetary Institute (WAMI). Payments system modernization will play a crucial role in financial deepening in the country and will help put the country's financial system on par with other countries in the sub region and beyond by transitioning the country's economy from cash based to one less dependent on cash. The payments system development project was expected to be concluded in June of 2014 but was suspended and only recently commenced after the Ebola outbreak had slowed down.

107. The main components of the project are as follows:

- Real Time Gross Settlements System (RTGS) and Scripless Securities Settlement Systems (collectively, RTGS/SSS) for high value transactions and inter-bank settlement and central securities depository and securities settlement system
- Automated Cheque Processing (ACP) and Automated Clearing House (ACH) (collectively, ACP/ACH) Systems based on machine-readable (MICR) cheques
- Core Banking Application (CBA)
- Infrastructure Upgrade

108. A Payments Systems Unit has been established within the CBL. The project involves a number of important components that are in the process of being implemented. A WiMAX network has been established in Monrovia to enable communications between the banks and the CBL. A new Payments System Act has been passed but as of June 2015 was awaiting presidential approval and publication before entering into force. Inter alia, it gives the CBL authority for payments systems oversight and regulation.

109. The WAMZ Payments System Development Project implementation in Liberia had faced delays before the Ebola outbreak, mainly attributable to challenges in engaging contractors for the infrastructural components and the fact that Liberia had been scheduled last among the four countries in the project plan. However, the project suffered a serious setback attributable to the escalation of the Ebola epidemic causing the contractors to withdraw their engineers from the country, however the launch is now imminent. The operation of the several payment systems will require the CBL to ensure to have properly trained operational staff available and that the payment operations are considered in the organizational structure of the CBL.

110. The major payment system infrastructure component missing in the WAMI project is a central payments switch, for which reason the CBL has started this project on its own. The CBL started the project in June 2014, with the objective to create interoperability between the currently proprietary ATM and POS networks. For the functional specification the CBL received support from USAID. All banks consider the central switch project as a crucial component of the National Payments System and fully support the project; the MNOs also showed interest in the central switch for their future mobile money transactions. The outbreak of the Ebola and the subsequent movement restriction to and from the country also impacted on the delivery of the central switch project. However, the team continued to hold regular meetings remotely with the vendor. A number of important deliverables which did not require the physical presence of the vendor had been accomplished.

111. The ACH/ACP is used to process paper instruments (mainly cheques), while the ACH system clears electronic payments like cheque data captured from the ACP system as well as electronic direct debits and credits. The net positions will be intended to be settled in the RTGS. All these processes are done in real time through a seamless interface with other components.

112. The Core Banking Application (CBA) Temenos T24 system has operated successfully since implementation with seamless interfaces with the ACH/ACP, RTGS, and SSS components since it went live. The CBL has also implemented and activated the Direct Credit Module for the direct payments of Government workers salaries and pensions. It hosts the current accounts of CBL customers such as Commercial Banks, Ministries, Departments, Agencies of Government and Special Projects.

113. It is not clear how much enthusiasm there is at the level of the banks for the cheque automation project, given the level of investment required, the low level of cheque usage, and the general phasing out of cheques as a payments instrument elsewhere.

114. The CBL intends to introduce a local switch for acquiring and processing card transactions. This would provide a link between banks without relying on international switching, and without requiring banks to participate in international networks for interoperability. The switch will initially cover three banks, but would, in due course, link all Liberian ATMs and POS machines, and mobile money transactions and facilitate transactions between mobile money accounts and bank accounts.

ICT Infrastructure

115. The quality of ICT infrastructure in Liberia, as in most developing countries, is very limited in rural areas. Voice, data and text messaging coverage and quality diminishes considerably outside the capital and main town centers. The situation has worsened since the Ebola outbreak. The operational capacity and business viability of the three principal mobile network operators (MNOs) has degraded. The largest MNOs are MTN Liberia (LoneStar) (market share of 49 percent as of end 2014), and Cellcom (41 percent), smaller ones are Novafone (8 percent), and Libtelco (1 percent). The Liberian Telecommunications Authority survey of 2014 indicates that 1.5 million people out of a population of 4.3 million are mobile phone subscribers.

116. MTN Lonestar has been offering MTN Mobile Money in cooperation with ECOBANK and GT Bank since 2011, based on a Fundamo platform (migration to Ericsson under way). Lonestar has 590,000 mobile money subscribers (up from 200,000 in 2013) and (as per end of 2014) 402 registered agents/merchants (a 100 percent increase from 2013). However, only 40,000 subscribers use the mobile money service at least once a month. The agent retains 40 percent of the mobile money fees and MTN plans to have an agent network of 1,000 by the end of 2015. There is no interoperability with other payment instruments and/or bank accounts.

117. Cellcom launched its mobile money service (called SMILE) on March 18, 2016, which is based on the M-Pesa model from Kenya. To serve its customers, Cellcom has constructed an extensive system of mobile money systems at Total gas stations for shop in shop concepts. It is now also offering mobile money via its stand-alone outlets. Cellcom is offering free person-to-person transfers. The existence of competition

will certainly result in the reduction in fees and the increase in uptake by the consumers. Cellcom plans to expand its agent network to 2,000 agents after 1 year, 5,000 after 2 years, and 15,000 after 5 years. Both MTN and Cellcom consider it difficult that mobile money services can be offered in an economically sustainable way in such a small market like Liberia, for which reason they would be interested in granting micro-loans or offering FX services, both activities are currently not allowed by the mobile money regulation though.

Table 7: Key Facts regarding Mobile Money Infrastructure 2014

4	# Active GSM MNOs
1	# Mobile money deployments
450	# Mobile money agents
90 %	Mobile network coverage (interrupted)
47 %	SIM cards penetration
47 %	Percentage population covered by at least 1 MNO (2009)
30.01 %	Estimated unique subscribers of mobile services (of 4.3 mm)
1,290,430	Estimated number of subscribers of mobile services
590,000	Estimated registered mobile money customers (approx. 30 percent of unique subscribers)[41]

Sources: GSMA mobiledevelopmentintelligence.com, gsmaintelligence.com.

Legal, Regulatory, and Oversight Framework

118. In maximizing the potential impact of using mobile financial services, various challenges still need to be addressed, including the following:

- Liberia's dual currency regime
- The need for an extensive, well-functioning and liquid agent network
- Ensuring an open mobile ecosystem that encourages innovation and participation by a diverse range of institutions including banks and NBFIs such as insurers, MFIs and other savings and credit providers as well as MNOs
- Developing appropriate KYC regulations that balance AML/CFT-related risks with the need to promote access to finance[42]
- Moving beyond over-the-counter transactions, payments and savings by enabling information on individuals' usage of mobile products and services to be used to facilitate access to credit and other financial services
- Developing cross-border mobile payments capacity to support remittances and trade

119. The CBL is collaborating with UNCDF[43] in a "Mobile Money for the Poor" programme that aims to address some of these issues.

120. A credit infrastructure measure of a biometric ID system would be useful to prevent fraud, provide a basis for creditworthiness assessment, and enable borrowers to establish credit histories in a credit information database for "reputational collateral." Many borrowers have the same names and no official identification card is currently issued to the citizens of Liberia. The National Identification Registry Act of 2011 and the establishment of the National Identification Registry (NIR) are important steps towards e-ID in Liberia, while the enabling environment (both technologically and legally) has still to be established. About 10 percent of the population of Liberia is registered in a civil registry, managed by the MoH, and about a quarter of children are registered at or around birth. Today, at least five digital identity programs are being run by different government agencies in Liberia. These programs provide useful services though

[41] It is estimated that less than 10 percent of this number use the service every month.
[42] To some extent these issues are addressed in the mobile money regulations.
[43] United Nations Capital Development Fund.

are specific to the individual needs of each government agency, but are not interoperable and scalability to a national ID is considered difficult. The Civil Service Agency started in 2008 to enroll regular government employees (so far around 22,000 have been enrolled with fingerprint and biometric photo and 10,547 ID-cards have been issued). The ID-cards issued so far are for employees of smaller Ministries, the large ones (Internal Affairs, Education, Health, and Justice) were supposed to follow later. But because of the Ebola outbreak the biometric center in Monrovia had been closed since summer 2014 and only reopened at the end of March 2015. Also the field visits to the counties for enrolment have stalled.

121. In 2011, the Government of Liberia (GOL) enacted the National Identification Registry Act of 2011, to allow for digital means of identification. The law called for the setup of a National Identification Registry (NIR) to be responsible for issuing a biometric-based identification card to each citizen and resident. Since the enactment of the law, a Board of Registrars, headed by the Minister of Internal Affairs, has been setup as a governing body and has convened multiple times. The NIR was finally established in 2015 as autonomous agency, to "develop and implement a modern, stable and sustainable National Biometric Identification System that provides a secure and safe environment for citizens and residents in Liberia while protecting people's privacy and supporting the planning and allocation of resources, benefits and services." The invitation for an Expression of Interest for a consultant to support the development of the National Biometric Identification System ended in March 2015.[44]

122. Given the limited number of bank branches and ATMs in Liberia, the potential for mobile money is important to increase financial inclusion. The 2013 Payments Systems Act, provides a framework for e-payments and provisions for mobile money.

123. In an effort to advance financial inclusion in Liberia, the CBL consulted with all banks, MNOs and international NGOs to revise the mobile money regulations to ensure that financial services would be easily accessible to all Liberians. The revised regulation was released in May 2014, and it allows both banks and nonbanks to have a mobile money license, encourages interoperability and non-exclusivity of the agent network, and provides provisions for lower tiered KYC data.

Table 8: KYC Mobile Money Rules

Account Type	Identity Required	Daily Transaction Limits (in US$)	Monthly Transactions Limit
Level 1	Village chief/clan head letter	250	Maximum balance limit of US$1,000, aggregate monthly transaction limit of US$2,000
Level 2	Driver's license, passport, voter identification, provide name, address, telephone numbers. Businesses can provide a business registration certificate.	1,000	Maximum balance limit of US$4,000, aggregate monthly transaction limit of US$8,000
Level 3	Same as Level 2 but customer will also provide a utility bill, tax certificate, or bank statement. Available to government and limited liability companies	2,000	Maximum balance limit of US$10,000, aggregate monthly transaction limit of US$20,000
Over the counter transactions	Not specified	100	

*If a customer has two Mobile Money Accounts with the same Mobile Money provider, one in U.S. dollars and one in LRD, the limits apply to the aggregate balance and transaction limits of each account.
**Business to person transfers generated by limited liability companies can have higher limits, if specifically authorized by the CBL.

[44] http://emansion.gov.lr/doc/NIR-EOI.pdf

124. The 2013 Payment Systems Act, contains the necessary provisions to support a modern payment system. The Act, developed with the support of the WAMI and provides the legal framework for oversight and regulation of the National Payments System.

125. In 2014, the CBL issued a Consumer Protection and Market Conduct Regulation aimed at the promotion of transparency and to allow for informed decision making by consumers. Furthermore, among the stated objectives of this regulation, are high quality of financial services offered and the implementation of efficient and effective complaint mechanisms by financial institutions. In addition, it mandates the Liberian Bankers Association (LBA) to develop a code of conduct for commercial banks to promote ethical and professional standards in the banking industry. By means of this Regulation, the Consumer Protection Unit at the CBL (established in 2011), should have an effective instrument at hand to further improve consumer protection and trust in the National Payment System.

126. In 2014, the CBL issued the Mobile Money Regulation and is currently preparing a regulation for agent banking, the latter will allow banks to offer their services via agents. The mobile money regulation replaces the guidelines for mobile money which were issued in 2011 and based on which a nonbank financial subsidiary of MTN Lonestar has been granted a license to provide mobile money services and maintaining a mobile money agent network. The regulation opens up the provision of mobile money services, which the Guidelines previously restricted to commercial banks, to nonbanks. The regulation is well drafted and takes all elements, typically considered relevant to mobile money regulations, into consideration. Nonbanks that wish to provide mobile money services must be established only for the purpose of providing mobile money services, the minimum initial capital is set at US$100,000. Each parent company is only allowed to establish one subsidiary for the provision of mobile money services. The regulation defines mobile money services as opening and maintaining the mobile money account, cash-in/cash-out, account-to-account transfers (to/from bank accounts, in-between mobile money accounts), bill payments, government payments, and a variety of more use cases. 100 percent of all outstanding customer funds have to be held in liquid assets with one or more banks and ring fenced from any other operations of the mobile money provider.

127. Furthermore, interoperability, agent non-exclusivity, consumer protection, reporting requirements, and so on are clearly defined. Banks who want to offer mobile money services also have to apply to the CBL, as for other products and services (under CBL Directive No. CBL/SD/001/2009 concerning the introduction of Financial Products and Services for Commercial Banks), but they do not have to establish a separate entity.

128. The regulation was developed with the help of, USAID, GSMA and in consultation with national stakeholders. MTN Lonestar and Cellcom both have applied for a license under the new regulation, the two smaller MNOs have not done so far. At the time of the mission, none of the two had been granted a license yet. In the case of MTN Lonestar, the CBL indicated that the license is likely to be issued soon, ones a few open issues have been clarified with MTN Lonestar.

Transaction Account and Payment Product Design (including Mobile Money)

129. Only 18.8 percent of the population (age 15+) have access to an account at a regulated financial institution.[45] Among the banks, LBDI has the largest number of account holders (200,000), followed by Ecobank (165,000), International Bank (75,000), UBA (45,000) and GT Bank (30,000).

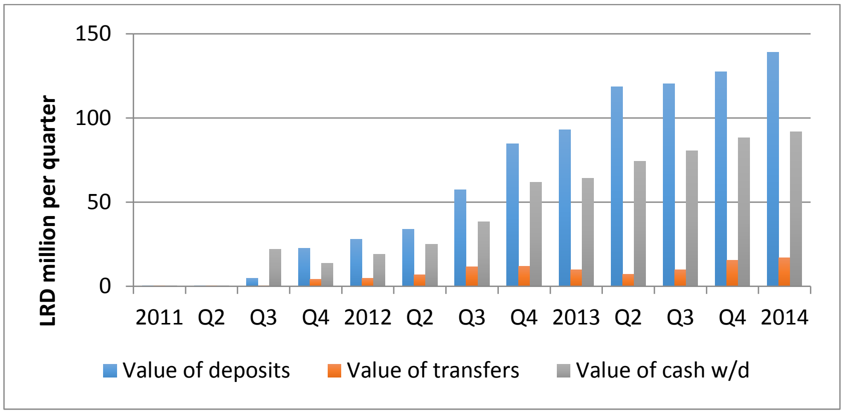
130. Given the usage of mobile phones in Liberia and the extent of network coverage, a mobile platform can potentially play a crucial role in extending access to transaction accounts and electronic payments instruments and prospectively to savings/store of value, credit and micro-insurance. Mobile money in combination with agent-based models has the advantage of being low cost and widely available and may facilitate competition between service providers.

[45] This data is based on FINDEX 2011, since FINDEX 2014 did not cover Liberia.

131. Mobile money is currently exclusively denominated in LRD. The system, used by the MNO, does not accommodate dual currencies, although a dual currency system is planned (the CBL maintains that if only one currency is used, it must be LRD).

132. Data on mobile money accounts is poor. However, some conclusions can be gleaned from the limited data that are available. Although the MTN/Lonestar system was originally designed around mobile money transfers (from one customer to another), this does not seem to be the main use, or at least not directly. Of LRD 459 million deposited into mobile money accounts in 2013, only 28 percent was sent through mobile money transfers. However, two thirds of the value of deposits was withdrawn as cash. This may mean that customers are using mobile money accounts for short-term savings, or alternatively that customers are depositing money directly into recipients' mobile money accounts, rather than using money transfers.[46]

Figure 19: Mobile Money Deposits, Transfers, and Withdrawals



Readily Available Access Points (ATMs, POS etc.)

133. There are 61 deployed ATMs (the vast majority of them on-site ATMs) and 117 POS-terminals, mostly in Monrovia, but ATM and POS machine usage is underdeveloped. Only four commercial banks (Ecobank, GT Bank, International Bank, and UBA) issue debit cards for the time being and those debit cards are mainly used for ATM withdrawals rather than payments. Because of a lack of interoperability, debit cards can only be used if the acquiring and the issuing bank are one and the same. Two of the card-issuing banks issue visa cards in addition to their proprietary debit cards. According to FINDEX 2011 figures, only 3.3 percent (15years+) of Liberians have a debit card.

134. The POS network does not allow cash back option and it is characterized by merchant surcharges to recover the cost associated with the merchant discount rate.[47] This is an impediment to the usage of prepaid cards to pay government cash transfer recipients who could benefit from collecting from POS operators.

135. **Additional access points are remittance and mobile money agents as well as collection offices.** The CBL offers collection services for customs, taxes, fees, and fines to the Liberia Revenue Authority via seven collection counters in Monrovia, and three more planned. The mobile money service offered by MTN Lonestar in cooperation with GT Bank and Ecobank, registered 402 agents by the end of 2014 (of which around 50 percent are located in Montserrado county and which also include the bank branches of the two partner banks). The two largest money transfer operators Western Union and MoneyGram have each around 70 agents and Ria around 10 and are present in most district capitals. Because of non-exclusivity, however,

[46] The gap between deposits and cash withdrawal may also be attributable to the requirement for agents to prepay and hold e-money balances. This "float" then allows them to make transfers into the mobile money accounts of customers.
[47] Merchant Discount Rate is the charge associated with the swiping of a debit or credit card at the merchant's business. It is a rate that the bank sets and is paid by the merchant. The customer should not be affected by this charge.

there is a large overlap between the remittance agents of different MTOs as well as remittance agent locations and mobile money agent location.

Large Volume Use Cases: Government Payments

136. **USAID-GEMS started in 2012 and is a five-year technical assistance project, funded by USAID, to support the Government of Liberia's initiatives to improve service delivery to the Liberian people.** Among the objectives of USAID-GEMS is the establishment and utilization of the national payment system "in line with international and regional standards, and that enables accurate and timely processing and reconciliation of GOL payments to vendors and civil servants, utilizing mobile technologies where feasible."

137. Mobile money payments to teachers have been piloted with 58 persons from July 2014 to March 2015, under the guidance of the USAID GEMS project.

138. **Social Cash Transfers are still largely affected in cash, but some mobile money pilots have been conducted.** Among these pilots have been USAID's "Advancing Youth Project" (MoE pays 100 teachers a monthly US$50 supplemental stipend), the Ministry of Youth and Sports "Liberia Youth Employment Program" (819 beneficiaries were receiving their US$85 monthly stipends via mobile money in 5 counties), the Presidential "Back-To-School Program" (5,000 students were registered and paid within one week), and Ministry of Gender and Development "Social Cash Transfer Program" (designed to provide funds to impoverished, disabled and at risk populations in 4 counties—some 1,000 beneficiaries out of over 10,000 have been paid via mobile money, intend to scale up).

Remittances

139. **Liberia is one of the countries with the highest GDP/remittance ratio worldwide.** According to the Bank's World Development Indicators 2014 personal remittances totaling US$495.2 million were sent to Liberia, which represents 24.6 percent of the annual GDP for 2014. However, this figure seems to include all SWIFT transfers, for which reason the real value of international remittances is likely lower. The World Bank conducted a Review of the Market for Remittances in Liberia on the basis of the General Principles for International Remittance Services in 2011. A number of recommendations based on this assessment have already been implemented by the CBL (for example, non-exclusivity, consumer protection unit).

Mobile Money Strategy

140. The CBL has requested USAID for the support in the development of a national mobile money strategy for Liberia. The draft strategy is the CBL's initial view of how Liberia will enhance its payments system to benefit all consumers using a simple technology, which is highly affordable and essentially ubiquitous.

141. The strategy is in the consultation phase, but core activities are as follows:

- The CBL will support the development of the requisite mMoney ecosystem by fostering the development of branchless banking (which uses independent agents to perform financial transactions on behalf of authorized financial institutions).
- To strengthen branchless banking and incentivize agent participation, the CBL will continue to support the GOL policy of paying for the initial cash-out fee for the payment of GOL salaries, recognizing the pivotal and central role of the GOL as an important economic catalyst.
- To expand the options for access to cash up-country, the CBL will authorize the deployment of independent ATMs and promote the development of a National Payments Switch.

- mMoney will initially be predominantly an alternative to cash transactions and transfers, and the CBL is committed to expanding financial inclusion, especially up-country, and will foster the incorporation of mMoney into banks, credit unions, MFIs, village community savings institutions and informal savings clubs (Susu).
- The CBL will increase public awareness of mMoney and promote financial literacy in collaboration with relevant stakeholders.

142. The CBL will sponsor the establishment of the National Mobile Money Steering Committee (MMSC) as the focal point for mMoney expansion. The MMSC will be led by the CBL and comprise representatives of the MNOs, banks, insurers microfinance and rural financial institutions (RCFIs, Credit Unions), NGOs, donors and Government. It will help to coordinate both public and private sector activities.

143. It is anticipated that implementation of mobile money in Liberia will consist of four phases:

(a) Government Salaries and Bulk Payments: Payroll, Stipends, Expense Reimbursements, Pensions and Benefits.

(b) Point-of-Sale: Retail, Tuition, Utilities.

(c) Revenue Collection: GOL Taxes, Customs, License Fees.

(d) Financial Services: Remittances, Banking, Credit, Insurance.

SOCIAL SECURITY (NASSCORP)

144. Liberia has two formal pension schemes, run by the National Social Security and Welfare Corporation (NASSCORP) and the Civil Service Agency (CSA). The Act creating the NASSCORP, first passed by the National Legislature on July 10, 1975, and was reinstituted in 1980 by the People's Redemption Council. The Employment Injury Scheme (EIS) was launched on February 1, 1980 followed, in September 1988, by the National Pension Scheme (NPS) a mandatory, contributory, partially funded defined benefit pension scheme for employees in the formal sector. NASSCORP also administers the EIS and a Welfare Scheme. The Welfare Scheme is not currently operational and is awaiting funding from the Government to commence operations. Members of the Board of NASSCORP are appointed by the President of Liberia; there is no regulator (or direct ministerial oversight). The CSA operates a noncontributory, unfunded scheme for civil servants, financed from tax revenues.[48]

145. As of December 2014, the NPS has a membership of 7,706 beneficiaries receiving benefits and 129,774 contributors. Of the membership in 2013, around 22,000 workers are in the Civil Service and are contributors as well. There are some exemptions from contributing to NPS, the most notable of which is members of the Armed Forces. There are no opt-out provisions in the Law which would enable people to choose another scheme for their mandatory contributions.

146. Pensioners are identified by specific cards and are paid into their bank account. NASSCORP maintains a US$ and a LRD account in 8 different banks. While pensions are typically paid monthly, very low pensions might be paid over a longer period (for example, twice or only once a year). All active pensioners have a bank account on preferred terms, transaction fees are paid by NASSCORP. NASSCORP revalidates the eligibility of its recipients every two years. Pensioners have an ID card, issued by NASSCORP.

[48] The CSR is the main arrangement for government employees. It is an unfunded noncontributory arrangement. Benefits are linked to years of service with a minimum of 25 years of service required to obtain a pension of 33⅓ percent of final salary and a practical maximum of 60 percent after 40 years of service.

Financial Performance

147. Although the NPS is in principle funded and contributions are used to build up an investment fund for the payment of future pension benefits, most benefits are in fact paid out of current contributions. NASSCORP cash deposits and investments amounted to US$40.1 million as of September 2014, with total net assets of US$65.9 million. It is noteworthy that a substantial amount of the total assets (US$10.8 million in September 2014) is represented by a claim presented to the Government for unpaid contributions for civil servant members of the NPS. NASSCORP investments, amount to just over 2 percent of GDP. Investments are mostly in real estate, much of which is commercial property that it has developed itself, with only a small proportion of investment assets held in the form of financial assets (33 percent in 2014). It does not invest outside of Liberia.[49]

Table 9: Summary of NASSCORP Financials (December)

	2011	2012	2013	2014
US$, millions				
Contribution receipts	14.8	21.0	23.2	25.6
Investment income	0.5	0.2	0.76	1.01
Benefit payments	-3.1	-2.8	-3.6	-3.7
Administrative expenses	–	-6.8	-7.0	-7.2
Other expenses	–	–	–	-2.4
Investment assets	19.1	21.7	30.3	39.5
Total net assets (September)				66.0
Percentage				
Return on investment assets	2.5	0.9	2.5	2.6
Assets/GDP	1.7	2.0	2.0	3.3
Investment assets/GDP	1.2	1.3	1.6	1.9
Financial assets/investment assets	26.1	18.2	16	33

Source: NASSCORP website (www.nasscorp.org.lr).

148. While NASSCORP's investment returns have improved in recent years to around 2.5 percent, it is less than clear what is being counted as "investments" in as much as that cash holdings appear to be large and are earning a lower return. NASSCORP also has very high operating costs, amounting 30 to 40 percent of what is classified in the accounts as income. Internationally, the average for a defined benefit scheme is about 5 percent. The excessive costs have been attributed to the cost of running an investment portfolio that is dominated by real estate, where NASSCORP is on occasion acting as a landlord for commercial properties and sometimes as property developer. However, the majority of what is classified as income is in fact receipts of pension and EIS contributions from employees and employers. It will be extremely challenging to achieve long-term financial viability with such a large portion of contributions being eaten up by expenses. Moreover, in the 2014 accounts an additional item of US$2.4 million "other" expenses is recorded. There is also a lack of clarity as to how the contributions from Government are being treated. The NASSCORP accounts (on the NASSCORP website) do not distinguish between NPS and EIS.

149. In a fully funded pension scheme, contributions would be used to build up investment assets that would in turn be used to generate investment returns, which would be used to pay pension benefits and operating costs. In the case of NASSCORP, investment income is too small to finance benefit payments and operating costs: in recent years income covered only 20 to 25 percent of benefit payments, and 8 percent of benefit payments plus operating costs. Hence the majority of benefit and operating expenses were paid out of members' contributions. In 2014, 52 percent of contributions were used to pay benefits and expenses, which meant only 48 percent of contributions was actually used to build investment assets and pension

[49] NASSCORP has an equity investment in Ecobank Transnational and may explore other markets.

reserves. In practice, therefore, the NPS operates largely as an unfunded pay-as-you-go (PAYG) scheme. The contribution rate is very low—3 percent from employers and 3 percent from employees. It has been further undermined by the failure to receive some of the contributions from the Government.

150. An actuarial assessment of the NPS carried out in 2012 noted that membership and contribution records were poor, and that information was lacking to conduct a proper valuation of the assets in which pension funds were invested. However, assuming that assets were appropriately valued and were realizable, NPS will inevitably face serious solvency and liquidity problems at some future stage if the current status continues, which would require the Government of Liberia – the guarantor - to fund any shortfall. The actuarial assessment recommended a substantial increase in contribution rates to fund pension benefits.

151. It is understood that the current noncontributory CSA pension scheme is to be replaced by a new contributory scheme, with employees contributing 3 percent. A full actuarial valuation of the liabilities under the old and the new CSA schemes is needed, and a determination of whether the proposed new scheme is likely to be liquid and solvent with such a low contribution rate. It is not clear if there will be a co-contribution from the employer (Government).

152. With mandatory membership of the NPS, and no provision for employees or employers to opt out and join an occupational pension scheme or provident fund, there is limited demand for other, privately run schemes, although it is understood that there are some voluntary pension/provident schemes in existence. These may offer improved benefits as compared to the NPS, although small size could lead to a problem with high administration costs.

153. There is no legal framework for pension funds or for the investment of their assets, and no regulation or supervision. Consideration needs to be given to the establishment of such a legal framework, with the primary objective of protecting pension fund members. This would include the accreditation or licensing of pension funds. The legal framework should cover the NPS and the new Civil Service Scheme. Consideration should be given to permitting employees and employers the right to opt out of the NPS and join accredited private occupational pension funds.

154. A number of actions are necessary to improve the effectiveness of the NPS to ensure that it functions as intended.

- An immediate rectification in government employer contributions for civil servants;
- A significant increase in contribution rates (the actuarial assessment recommended an increase from 6 percent to 13 percent);
- Establishment of a formal investment policy and an improved investment management function; the investment policy should increase diversification, reduce the share of assets invested in real estate, invest more in financial assets, and allow some international investments;
- Reduction in NASSCORP's administration costs closer to international norms;
- A proper actuarial valuation of liabilities;
- Reviewing benefit entitlements to remove inequities and inconsistencies;
- Separate accounting for the NPS and EIS.

Other Schemes

155. Contributions to NPS are mandatory and there is no provision for either employers or employees to opt out of the arrangement. Notwithstanding, there is anecdotal evidence that other schemes exist on a voluntary basis. Discussions with ICA revealed that it acts as agent for one unidentified occupational scheme and three provident funds. There were also indications of other defined benefit occupational

schemes that are in operation mainly for employees of international companies operating in Liberia. There are no local laws covering the operations of these schemes and provident funds and no supervision function.

156. Annex 6 contains a further discussion of the pension schemes contributions and benefits and areas for reform.

FINANCIAL INCLUSION

157. The Government's 2008–2012 financial inclusion strategy that has been implemented in cooperation with development partners and has six components:

1. Delivery of financial services
2. Enhancement of access to financial services
3. Integration of the informal sector
4. Improved regulation
5. Financial literacy
6. Consumer protection

158. Central to this strategy is the activities of MFIs most of which are affiliated with NGOs. Thus, in addition to finance, these MFIs provide education for financial literacy and training in business management.

159. Microfinance activities in Liberia operate predominantly in urban areas, especially in Monrovia, and finance mainly trade.

Types of Microfinance Institutions

160. Microfinance[50] is conducted by six types of institutions, as follows:

1. Commercial banks' microfinance departments
2. Rural Community Financial Institutions (RCFIs) that have bank licenses
3. Deposit-taking MFIs
4. Non-deposit-taking MFIs (mainly NGO affiliated)
5. Credit unions
6. VSLAs

Non-deposit-taking Microfinance Institutions

161. There are 20 registered, non-deposit-taking MFIs. Among such institutions, three tiers have developed with regard to geographic outreach, quality of operations and financial performance. BRAC, an MFI, is the leader, accounting for more than two-thirds of non-deposit-taking MFI loans. Tier two is composed of three MFIs that have financial and technical support from international organizations, Foundation for Women, Liberty Finance, and the Liberia Entrepreneurial Asset Development. The others, mainly offshoots of NGOs or whose activities are comingled with those of NGOs, have little or no such international support

162. Non-deposit-taking MFIs receive funding from donors and from the CBL under the Loan Extension and Availability Facility (LEAF) program. The financial performance of the non-deposit-taking MFIs shows it is difficult to realize profitable operations. BRAC has reduced the number of its branches and LEAP[51] (an MFI) ceased operations. Others report continuing losses that are subsidized by donors.

163. Factors that impede profitability are the high cost of appraising creditworthiness of prospective borrowers, especially in rural areas, lack of peer support and dishonesty among members of solidarity borrowing groups, lack of a credit reference system for credit history of prospective borrowers, and the lack

[50] There is no universally accepted definition of microfinance but a usual definition is as follows:
Microfinance refers to loans, savings, insurance, transfer services and other financial products targeted at low-income clients. Source: International Year of Microcredit 2005.

[51] Local Enterprise Assistance Program.

of practical enforcement mechanisms to induce borrowers to repay their loans. Public opinion manifest in local newspapers and radio stations often criticize efforts by MFIs to collect microloans, which impedes collection actions. Thus, there is a question of the long-term sustainability of this class of MFIs.

Table 10: Non-deposit-taking Microfinance Institutions [52]

Select Aggregate Data at September 30, 2013
(Financial Data in US$)

Number of active borrowers	23,790
Of which BRAC	13,177
Number of active women borrowers	21,804
Loans disbursed	1,211,565
Of which BRAC	1,141,875
Mandatory savings	13,219
NPLs > 30 days (average percentage)	20
Number of branches	51
Number of staff	775

Source: CBL.

164. Non-deposit-taking institutions are currently not subject to any CBL prudential regulations and it is not clear what would induce them to conduct their business in a safe manner and that is fair to customers. The institutions with foreign support generally have better managed operations. The expectation was that as the sector matured, competition would lead to higher standards and that some MFIs would exit the sector.

165. The Network of Microfinance Institutions of Liberia (NEMIL) is the Apex organization for the non-deposit-taking MFIs. At September 30, 2013, aggregate loans approved were US$3,081,089[53] among 23,790 active borrowers or an average loan amount of US$130. NEMIL provides technical support to its members, including with financial reporting. Its emphasis under its recent new leadership is on capacity building for member institutions.

166. NEMIL has a Code of Conduct for its members which include requirements to be audited by an auditor registered with the auditing professional association, to provide fair advertising, and to disclose their rights to customers. The Disciplinary Committee of its Board is to investigate alleged violations of the Code and may order a member to remedy a violation or suspend or expel a member, depending upon the outcome of the investigation.

Rural Community Finance Institutions

167. 9 RCFIs were established in seven rural counties in 2014 and up until August 2015. The first Liberian Financial Inclusion Strategy (2009–2013) focused on the establishment of a sustainable microfinance industry in the country. In 2013 the CBL committed in a Maya declaration to increase access to financial services offered by authorized institutions, increase the number of access points, improve consumer protection and promote the establishment of rural community finance institutions. Under a grant from the Alliance for Financial Inclusion, CBL began to update the Liberian National Strategy for Financial Inclusion in 2013 based on a baseline survey on access to finance in the country.[54]

168. The minimum required capital for an RCFI is US$50,000 and they have local shareholders. RCFIs can offer savings products, loans, checking accounts, over-the-counter transactions, and remittances (including WU and MoneyGram).

[52]Data generally from 11 or 12 reporting institutions of 18 institutions. Three reported mandatory savings figures.
[53] The difference between loans approved and disbursed constitutes largely constitutes repayments.
[54] Conducted by the CBL with support from the Alliance for Financial Inclusion (AFI) and conducted by Top Consulting, Inc.

169. At present, all the RCFIs receive technical assistance from Afriland Bank that includes credit underwriting procedures[55] and the CBL with regard to financial support and capacity building. One of the RCFI products is loans to teachers whose salaries are paid into the RCFI from which they have a loan and from which account the loan is repaid. The plan is for RCFIs to extend these types of services to a larger clientele beyond teachers.

Credit Unions

170. The 2015 CBL annual report lists the number of credit unions as 400; however, precisely what constitutes a credit union is vague. The Liberian Credit Union National Association, LCUNA, was given the role as an Apex organization to professionalize the sector in 2013 with a grant from UNDCF of US$2.45 million over 4 years and technical assistance from the World Council of Credit Unions (WOCCU). Credit unions have boards of directors, which appoint management. Most credit union members are both borrowers and lenders with only 30 percent depositing savings only. Under the reform program guided by WOCCU, LCUNA has developed four regional credit unions that provide operational support including financial reporting software. Periodic financial statements of credit unions are submitted to LCUNA for submission to the CBL. WOCCU is providing training to credit unions. Draft prudential and market conduct regulations for credit unions are being developed. The plan is to roll up the smaller credit unions into the four regional credit unions.

171. A draft regulation intended to establish a formal regulatory and supervisory regime over the credit unions sector has been developed and submitted for approval of the CBL. The new regulation will bring credibility and confidence to the sector and help its growth and development.

Village Savings and Loan Associations

172. There are 1,450 VSLAs which often consist of 25–30 members, mostly women. Members borrow on the basis of solidarity that is to provide peer support to enable individuals to repay their loans. Interest on loans is 10 percent and loans are extended for a term of 2 or 3 months, for working capital for a micro business or for temporary personal needs.

173. MFIs do not currently offer micro insurance. Micro insurance provided by MFIs in other countries may be for health, life, crop failure, and loan repayment.

Supervisory and Regulatory Framework

174. In February 2010 the CBL issued guidelines on the Microfinance Regulatory and Supervisory Framework (MFI Guidelines) to seek to organize and energize the deposit-taking MFI sector. As of July 2015, there was only one licensed deposit-taking MFI. The guidelines contain various desirable objectives for the microfinance sector, including the following:

- To cover the majority of the poor but economically active population by 2020 thereby creating thousands of jobs and reducing poverty.
- To increase the share of micro credit as a percentage of total credit to the economy.
- To eliminate gender disparity by improving women's access to financial services.
- To increase the number of linkages among commercial banks, specialized finance institutions, and MFIs.

[55] The program is called MC2 for "means and competence of community." The CBL is also offering training and has lent half the capital for RCFIs on an interim basis, an approach seen elsewhere in West Africa apparently to stimulate financial services in underserved areas, but which creates a conflict of interest between roles as investor/promotor and regulator.

175. The framework classifies types of MFIs, lists basic permissible financial services for deposit-taking MFIs and provides for their registration (for non-deposit-taking institutions), licensing, reporting to the CBL, and, for deposit-taking MFIs, their regulation and supervision.[56]

176. The discussion below on MFIs relates to MFIs in general. It must be recognized that with such diverse types of providers of microfinance, all observations do not apply to all MFIs in all instances.

177. Stakeholders, including the CBL, indicate the microfinance sector needs training in operations (financial reporting, risk assessment, auditing), equipment for its operations (computers, electrical generators, and bicycles), and increased funding if it is to be self-sustaining.

Governance

178. A major general issue affecting the performance of MFIs is governance by its directors. Only deposit-taking MFIs are subject to Regulation CBL/SD/001/2012 on 'Corporate Governance for Financial Institutions.' Non-deposit-taking MFIs are not subject to prudential regulations, only certain reporting requirements. There is a need for some regulations but not as stringent as those under the 2012 regulation. There should be some affirmative requirements as to education, expertise, and years of professional experience, as well as disqualifying factors.

179. According to Guidelines for the Effective Governance of Microfinance Institutions of the MicroFinance Network, effective microfinance boards consist of members with a range of characteristics, as follows: social and commercial skills; strategic and operational skills; math and people skills; and stature in the community and involvement. The CBL should make MFIs aware of the need for diverse talents and encourage an upgrade of boards where needed.

Market Conduct Rules: Consumer Protection for Microfinance Services

180. The poorer segments of society in Liberia often have limited knowledge about financial transactions and may be reticent in dealing with financial institutions so it is important that the law or regulations afford them with transparency about financial transactions and protection from deceptive or abusive practices and with effective recourse if they become subject to such practices.

181. Consumer protection in financial services has three basic elements—transparency and disclosure of conditions of loans, deposits and other services; fair treatment of customers; and effective recourse for consumer complaints.

182. The Prudential Regulations for Microfinance Deposit-Taking Institutions (MDIs) contain certain market conduct rules to protect consumers. Section 20 requires transparency of interest rates, commissions, and related fees and requires that interest be calculated on the outstanding loan balance. If the CBL determines that information conveyed by a MDI is false or misleading, it may prohibit its publication and order remedial action. There is also an important requirement that an MDI ascertain that a prospective borrower would have the ability to repay a loan. There must be a written loan agreement setting forth some dozen conditions of the loan and rights of borrowers. The CBL has established a Consumer Protection Unit to investigate complaints of consumers and may reject or modify an action of a MDI and take other supervisory action.

183. For non-deposit-taking MFIs, the MFI Guidelines contain only a requirement for microfinance service providers to:

> "Strictly observe their fiduciary responsibility, remain transparent and accountable in protecting savers' deposits."

[56] The guidelines were largely superseded for deposit-taking institutions by prudential regulations in 2012.

184. This requirement appears too imprecise to provide adequate guidance for institutions on consumer protection. However, the RSD of the CBL adopted a 2014–2018 Strategic Plan. Strategic Goal II is as follows:

> "To promote sound ethical practices in the financial system, consumers' empowerment and good market conduct practices"

185. Strategic objectives under this goal contain measures which, if implemented, would strengthen considerably consumer protection for microfinance customers. These include the following:

- Establishing a standard set of disclosure requirements for banks and other financial institutions
- Providing financial education to the public using several media
- Reviewing contracts (specimen) involving financial institutions and their customers to ensure transparency and adequate disclosure of relevant information about the financial product and/or services involved
- Ensuring the establishment of robust and effective internal dispute mechanisms at each financial institution, including hotlines and/or inquiry/suggestion boxes at the premises of financial institutions.

186. The actions to be undertaken could also benefit from a focus on fair treatment with respect to particular types of financial services by monitoring whether there are defaults on particular types of loans or customer complaints concentrated in a particular financial service to address specifically abuses in these areas.

Institutional Strengthening and Capacity Building

187. The CBL, NGOs and donor agencies continue to work with MFIs to encourage the expansion of branches into rural areas. In 2012 a workshop was convened by the CBL to reactivate the apex organization of the sector, NEMIL. The intention was to engage with MFIs, assess their needs for support and upgrading of their activities and to establish an advocacy organization for microfinance. Elections were held for a new corps of officers and another workshop was sponsored to facilitate the development of a code of ethics for the sector. A number of additional workshops were held during the period, including on Strategic, Business Planning and Risk Management for members of the board of directors, managing directors, branch managers and staff of credit unions and MFIs.

188. Under a Bank/FIRST supported project, CBL staff received training in 2011 to support their operations in supervising MFIs. This included field examination of a number of MFIs, operational risk assessment, and computer assisted examination techniques.

189. The Microfinance and Financial Inclusion Unit of the CBL should be the focal point for defining precise programs to be undertaken in these areas; designing parameters for measurement of achievements, with timelines; and rallying the resources required internally and externally. NEMIL should also seek grants for its members. The reform measures should be modified as appropriate if they do not produce the desired results.

ENTERPRISE ACCESS TO FINANCE

190. Despite an annual credit growth rate of 23.7 percent between December 2014 and November 2015 and an estimated 17.7 percent increase in private sector growth as a percentage of GDP in 2014, access to credit remains a key constraint for most MSME businesses in Liberia. Credit is currently concentrated in the trade sector and remains low in productive sectors, such as agriculture. The lending rates in Liberia, at 13.6 percent in November 2015, are among the lowest in the region. However, the major challenge is the lack of access to loans, indicating credit information deficiencies which undermine the financial sector's confidence to lend to MSMEs.

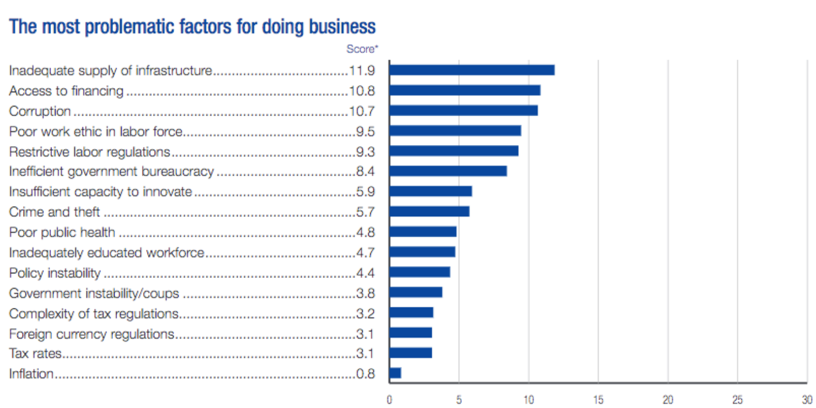
191. Liberia has a relatively poor comparative ranking on ease of credit access, below the SSA average. This is explained by (a) a depth of credit information index (which measures the availability, extent and coverage of credit information) of only 0 in Liberia compared with 2.3 on average in sub-Saharan Africa and 6.57 in the OECD; (b) a public credit registry coverage of only 1.8 percent of adults in Liberia compared with 5.8 percent average in SSA and 11.9 percent average in high income OECD countries; and (c) zero private credit bureau coverage in Liberia compared with 7.1 percent of adults average in SSA and 66.7 percent average in high income OECD.

192. The need for credit among local businesses is high but access is limited. In a 2013 World Economic Forum survey, 60 percent of surveyed businesses indicated a need for credit but only 20 percent of this number have been able to access a formal loan in the past. Demand for loans is driven by both short and long-term needs. The most frequently cited reasons for seeking financial credit include working capital financing (34 percent) equipment and machinery purchases (24 percent), funding business expansion (17 percent) and for contract pre-financing (16 percent). 64 percent of surveyed businesses have dedicated business bank accounts, but only 39 percent are able to get a bank guarantee, which is often a prerequisite for participation in bidding for large private sector tenders. High collateral demands, at 125 percent of loan value, constitute the most pressing obstacle to local business access to formal credit. When available, credit tends to be short-term in nature and, therefore, unsuited to the long-term capital investment needs of local businesses.

Global Rankings for Enterprise Finance

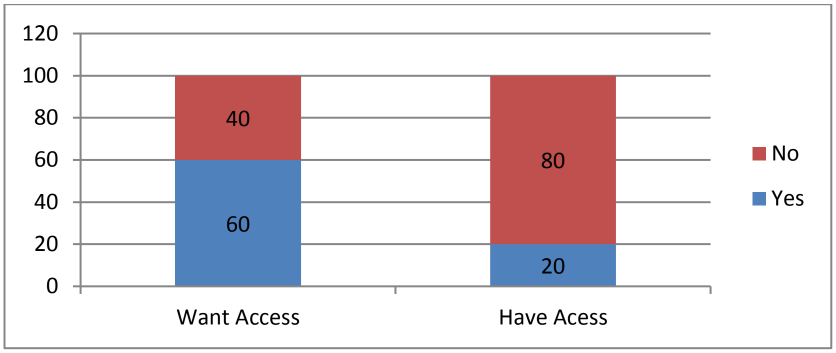
193. A number of published reports have underlined the difficulties experienced by small businesses in obtaining credit in Liberia. In figure 20, taken from the World Economic Forum's 2015-2016 Global Competitiveness Index, indicates that access to finance was the business obstacle second most frequently cited by Liberian enterprise respondents to its survey.

Figure 20: Obstacles to Doing Business in Liberia



Source: World Economic Forum 2015-2016, Global Competitiveness Index - Liberia Survey.

Figure 21: Local Businesses' Desired and Actual Access to Credit



Source: Building Markets, 2014.

194. A new Secured Transactions Law, which provides for comprehensive reform of the secured transactions framework, was approved in 2010 and is functioning as intended in registering security rights to moveable property. This should stimulate more asset-based lending because lenders have a registry to consult to determine whether they would have first priority to execute on an asset that is pledged to secure their loan, or, if they find they would be a secondary pledgee, they can determine whether the asset has enough value to secure their interest as creditor.

Venture Capital

195. Sources of venture capital and other financing for start-up and early stage companies are quite limited. The Liberian Enterprise Development Finance Company (LEDFC) was created in 2007. It was set up as a nonbank financial institution in the form of a partnership between the U.S. Overseas Private Investment Corporation as majority shareholder with up to US$20 million in loan capital, and the Robert L. Johnson Foundation, and managed by the international NGO Cooperative Housing Foundation International. Its intention was to provide Liberian or diaspora owned SMEs with loans of between US$25,000 and US$1 million at commercial interest rates for fixed assets and working capital. Repayment periods were 3–5 years for investments and 3–12 months for working capital.

196. Despite the challenges of Liberia's post-conflict environment, eight loans to SMEs, mainly start-ups, were made in the first year. Taking into account early difficulties encountered, the minimum loan size was later reduced to US$10,000 and limited to establish operating companies and borrower criteria were broadened to allow loans to joint ventures with non-Liberian investors. In the years that followed LEDFC provided loans totaling more than US$7 million to more than 90 SMEs across a number of sectors including agribusiness, mining and quarrying, manufacturing, construction, hospitality, transportation and retail trade. However the results were disappointing compared with the initial target of financing 1,500 businesses in 5 years.

197. A number of problems were reportedly faced by LEDFC.[57] These included a shortage of available investment projects, particularly among previously marginalized groups and outside Monrovia, poor-quality business plans attributable to lack of skills in the SMEs, including business management skills, inability of applicants to meet the collateral requirements of a minimum of US$25,000, and a poor repayment culture resulting in NPLs even higher than in the commercial banking sector. LEDFC was sold in June 2013 to the Ghana Growth Fund, a private equity fund, which intends to continue financing SMEs with a focus on the construction sector. The Fund has recently changed a focus to provide pre-financing against committed contracts to firms in the construction sector.

[57] Gorlorwulu, John, Global Center for Development. 2011. Constraints to Enterprise Financing in Post-Conflict Liberia.

198. In its U.S. Overseas Private Investment Corporation supported incarnation, LEDFC made only around 100 loans compared to the target of financing 1,500 businesses in 5 years. Loans totaled about US$8.3 million of which US$3.7 million have been repaid, leaving a current portfolio of US$4.6 million.

West African Venture Fund

199. In 2010 IFC set up the West African Venture Fund (WAVF) to expand access to finance for Liberia and Sierra Leone and is based in Monrovia. The WAVF reports that it has invested in 53 projects (between the two countries). In 2013, about half of these companies were in Liberia with an invested amount of US$3.7 million. Unique Venture Capital, a Nigerian registered fund manager, was selected to raise $40 million in equity capital and IFC is acting as anchor with a pledge of US$13.5 million in equity and US$2 million in business support services to SMEs before and after investment. Sectors targeted include agriculture and agribusiness, manufacturing, retail, tourism, real estate, mining and financial services. The aim is to make equity investments of between US$100,000 and US$500,000 in a minimum of 40 "bottom of the pyramid" SMEs in each country and to achieve returns of 25–30 percent on equity. The model combines equity investments with large amounts of hands-on technical and management assistance, but only after investment is made.

200. WAVF reports having invested more than $32 million in some 53 projects in Sierra Leone and Liberia. Sectors included agribusiness, manufacturing, logistics, hospitality, construction, finance, ICT and education. Projections for the end of 2014 were in excess of 1,050 new jobs created and several multiples of this in indirect jobs created. Challenges encountered by the WAVF in Liberia include slow absorption of equity finance, low level of basic infrastructure, lack of skilled staff and difficulties in exit. The market has not presented the opportunities anticipated nor is firm management capacity as prepared for investment—or as eager to bring in outsider shareholders—as hoped.

Ignite Fund

201. A recent entrant, the Ignite Fund, supported by Spark Stichting (a Dutch foundation) has commenced operations to provide financing for SMEs, investors include Chevron and Virgin (Richard Branson). To date activities have centered on training and capacity building, however it is anticipated that investments will be made below US$500,000.

Developing Alternative Financing Instruments

202. While there is a need for availability of term loans longer than the 18-month to two-year tenor common today, there is also a need for innovative financing for SMEs that meet specific needs. For example, the occasional pre-financing of contracts of suppliers to larger, more established corporations is in its infancy, but carries the potential for considerable demand among SMEs as their working capital available to meet contractual production requirements are often limited. Pre-financing can serve as a catalytic tool to enable funds to flow along the supply chain in advance of final product delivery. SMEs that receive contracts from concessions and other FDIs will require bank pre-financing, but these firms should be able to develop their own supply chain and provide pre-financing as a means to provide working capital to cash-strapped firms producing raw and intermediary products to the 'lead' firm.

Factoring

203. Invoice factoring is a financial product that addresses the inability of SMEs to perform under a contract attributable to insufficient working capital. This insufficiency is often the result of delays in payment from large customers of as much as 120 days. Developing the invoice factoring market could assist many businesses in cash flow management and leverage existing receivables to facilitate additional sales cycles. Factoring as a process can be easy to implement because it requires only a contract to sell, or assign, receivables. The security for the loan comes from the customer of the borrower rather than only from the

borrower itself.[58] However, for a factor to be successful, it must be familiar with the sector to which sales of the issuer of the invoices are made to determine whether the customer of the borrower has good prospects of receiving income from its business to enable it to pay the invoice.

Financial Leasing

204. Financial leasing provides SMEs the ability to acquire the use of equipment without having to offer additional collateral, while providing banks with a financial product that does not require a thorough analysis of a firm's cash flow potential. The new leasing law should pave the way for the creation of an equipment leasing industry in Liberia. Support should be given to the development of the recently initiated movable assets and secured transactions regime, the clarification of repossession procedures, ensuring that there remains no bias against leasing in the tax rules, and ensuring that the insolvency regime clearly affirms the ownership rights to leased equipment in case of insolvency of the lessee. Banks may be interested in setting up leasing operations, although leasing is often carried out as a core business of independent companies. In any case, the finance lease regulation issued by the CBL should enable banks to finance the procurement of equipment for startup businesses while enhancing risk management in the credit activities of the banks.

Warehouse Receipts Financing (WRF)

205. Development of WRF would provide one of the few opportunities for agricultural producers in Liberia to obtain formal financing at reasonable rates. Warehouse receipts represent a form of collateral—rights to stored commodities, with well-defined rights, liabilities, and duties of each party to a warehouse receipt (for example a farmer, a bank, or a warehouse operator). They must be freely transferable by delivery and endorsement and the holder of a warehouse receipt must be first in line to receive the stored goods or their fungible equivalent on liquidation or default of the warehouse.

206. The introduction of WRF in Liberia would allow small and marginal farmers to extend their sales period beyond the harvest season, providing them with cash at a time in which they are in the greatest need of liquidity. Because of demand and supply, prices fall to their lowest during harvest time and gradually rise during the lean season. WRF allows small farmers to smooth out these irregular cash flows and benefits farmers by giving them the flexibility to sell when prices are higher. Additionally, because WRF requires wide dissemination of crop prices, in practice it can result in better price discovery for famers allowing them to negotiate better terms of sale and help them avoid being classic "price takers," cut off from the flow of market information. In many countries aggregators and other buyers will purchase from small farmers who are ignorant of market conditions, at much reduced prices. With the advent of WRF, prices for most crops would be widely publicized.

207. At present Liberia lacks the warehouse infrastructure needed to implement this type of financing as the war destroyed most of the warehouses in the country and there are no financial institutions (banking or otherwise) widely offering this type of lending. There is therefore very little expertise available to implement it. However at least one bank indicated that they have occasionally used it for larger customers that they know well. And Afriland Bank uses receipts for cash crops deposited in its own warehouse as collateral for loans to agricultural producers.

Special Lending Initiatives

208. There are a series of directed credit initiatives available in Liberia, mostly launched by the Central Bank. Special lending programs are as follows:

[58] This would be recourse factoring—with recourse to the borrower if the invoice is not paid in full. Nonrecourse factoring, where the lender has a claim on only the issuer of the invoice, is also possible.

209. Small-Medium Enterprises Credit Stimulus Initiative: loans to Liberian-owned SMEs. Aiming at enhancing credit to the economy, the CBL launched the initiative in January 2010 by placing long-term U.S. dollar deposits at commercial banks. The CBL placed US$4 million with commercial banks for on-lending through medium-term loans,[59] at regulated interest rates. As of December 2015, $3.6 million has been dispersed to 151 businesses. Funds are provided by the CBL to the banks at 3 percent, who can lend the funds at 7 percent. The objective is to encourage a better maturity structure for loans to Liberian entrepreneurs and making the cost of credit more affordable. The annual on-lending interest rate to SMEs for this facility was capped at 8 percent and with a minimum and maximum tenor of 12 and 60 months, respectively. This approach carries potential risks to both the CBL and the participating commercial banks if too much moral suasion is exerted to provide finance to possibly noncredit worthy clients. Banks report that NPLs on the facility are high, and the margin is insufficient to make it profitable. This program has not been as successful as hoped, as banks cite the CBL's practice of debiting banks' accounts directly when funds come due, regardless of whether SMEs are repaying loans on a timely basis, which they perceive as a risk. The CBL is considering how additional medium-term resources for targeted lending can be provided.

210. Loan Extension and Availability Facility (LEAF): During the course of 2012, the CBL made available over LRD 200 million to MFIs, Credit Unions and VSLAs throughout the country through the LEAF as a means of boosting financial inclusion and enhancing output and employment. The program was intended to provide soft loans to MFIs, credit unions and VSLAs. The program provided loans to these institutions for a 3-year period, later extended to 5 years, at 3.0 percent to facilitate onward lending to their clients and members. The institutions lend these funds at their usual customer rates. It is noted that not all MFIs receiving funds through the LEAF program are providing financial statements as is required under CBL regulations.

211. Mortgage Stimulus Initiative: The CBL also launched a US$10.0 million CBL Mortgage Stimulus in 2012 for long-term loans (8–10 years) for property construction, purchase and renovation. This program is intended to provide, for the first time in Liberia, the opportunity for Liberians to access loans for home ownership.

212. Agricultural Stimulus Initiative: loans structured to meet the repayment needs of agricultural producers. In November 2012 a US$7.5 million Agricultural Stimulus Initiative was launched through Afriland bank to help provide access to finance to the agriculture sector. This is an opportunity to make medium- to long-term credit facilities available to farmers stimulate private investment in the agricultural sector and create employment.

The aggregate CBL credits under the Credit Stimulus program disbursed in 2012 were as follows:

Table 11: CBL Credit Stimulus Program
2012 Disbursements

Program	US$	LRD
Agriculture	5,000,000	1,250,000
Mortgages	10,000,000	217,500,000
SME finance	4,000,000	72,500,000

Source: CBL.

Ministry of Commerce and Industry SME Loan Program

213. The Ministry of Commerce and Industry is planning to set up a matching grant fund (LIFE Fund) for supporting development of SMEs. The fund will be managed by an independent fund manager and $1 million in financing will be sourced, 50 percent from Government and 50 percent from LBDI.

[59] Originally for a term of three years but because of the Ebola crisis have been extended for two years.

Partial Credit Guarantees

214. While the CBL interventions are basically lines of credit, USAID's Development Credit Authority has a loan guarantee program with funding up to US$500,000 through Ecobank and US$1.2 million through International Bank. The program guarantees 50 percent of loan principal in the event of borrower default. While a number of other banks have expressed an interest in participating in the program, results to date have not been encouraging as only eight loans (totaling US$1.2 million) have received guarantees (of which one defaulted and the bank called on the guarantee, in the amount US$20,000), with average tenors under two years.[60] A key reason cited is the lack of longer-term financing demanded by companies.

215. Another reason cited for the low utilization of the loan guarantee program was the lack of preparedness of companies. The USAID-sponsored Investing for Business Expansion (IBEX) program, which focuses on preparing both companies and lenders on accessing/providing credit, has cited the lack of preparedness of companies and their managements to access credit, in particular their lack of three years of credible financial statements, a basic requirement of lenders.

216. Therefore consideration should be given to initiating medium-term capacity building support to companies to prepare them for lenders' requirements, rather than focusing on bank financing when it may be premature for them. This could be aligned with the Private Sector Development Strategy, which contemplates a small grant program (based on a business plan competition) which would be married with TA for a three-year period, after which successful companies would be eligible for a matching grant program (requiring their own contribution) and would likely be more attractive to lenders, especially those participating in the credit guarantee program.

217. Finally, another constraint is the large skills gap among financial institutions themselves, across the whole range of financial services activities. Loan officers have less difficulty working with larger corporate clients who are more likely to have access to the accounting and other skills needed to prepare bankable loan proposals, than with SMEs. Lending to the SME segment requires a different skill set for loan officers, more like the hands-on outreach skills employed in microfinance, and these are often not available within the banks.

[60] IB loans were to borrowers in the agriculture sector and mostly for equipment/asset purchases. They averaged approximately US$105,000 with an average tenor of 1.7 years. Ecobank loans were primarily to the agriculture sector and were smaller, averaging about US$16,000, and shorter-term, averaging just over one year.

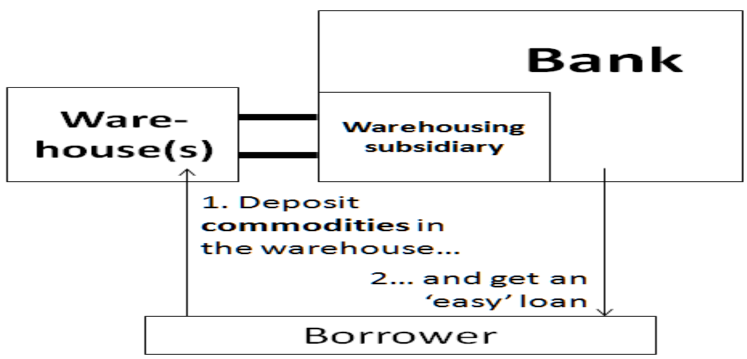
Box 1: Financial Products to Support MSMEs

Leasing. Leasing provides an alternative to bank lending for financing capital investments such as agricultural and agri-processing equipment, and could significantly expand the pool of medium and long-term capital available to SMEs. Leasing focuses on the firm's ability to generate cash flow rather than on its credit history or its ability to pledge collateral. Leasing can be used to finance a broad range of equipment across the Liberian agribusiness value chain, from simple tools to vehicles to equipment for agro-processing.

Factoring. Factoring works by providing upfront payment, at a discount, to a company awaiting payment of an invoice presented to an international or bilateral organization whose payment, which is as good as guaranteed, may nevertheless take several months to process. The introduction of invoice factoring could reduce the payment wait time and provide businesses in the agri and agribusiness sectors, as well as other sectors, with liquidity to better manage their working capital. With the estimated US$850 million annual inflows from concessionaires, U.N. agencies and other foreign entities,[61] there is a great opportunity to expand local procurement to benefit SMEs, if factoring could help address the challenge of cash flow management for SMEs.

Warehouse receipt financing (WRF) is a collateralized loan in which goods are stored in a warehouse and used as collateral against financing. This type of financing is particularly appropriate for agricultural commodities. As illustrated in the diagram below, typically, products of a defined quantity, quality and grade are deposited in a warehouse, which in turn issues a receipt. In well-functioning markets, these receipts are negotiable instruments that can be sold, traded, used as collateral or accepted for delivery of future contracts. In more rudimentary markets, as portrayed in the figure below, a bank may pay against the receipt, in essence providing an advance to the farmer or trader against goods warehoused. In either case, the end result is a substantial improvement of the efficiency of the market by converting inventories of agricultural and other products into readily tradable, liquid instruments. With the use of the storage, WRF allows small farmers to choose the timing of sales and smooth out price fluctuation caused by seasonal demand and supply.

Schematic of Warehouse Financing Receipts



[61] Team estimate based on information from the Heritage Foundation Index of Economic Freedom 2013 (FDI) and the Bank (net official development assistance received).

OTHER MAIN ISSUES

Capital Markets

218. The Liberian capital market is very underdeveloped. The Government of Liberia has only recently recommenced issuance of debt in the domestic market and, at present, is limited to the Treasury Bill market. This reflects two factors. First, the experience of the mandatory savings bond scheme of 1981, which was never repaid, and left a legacy of suspicion towards government financial instruments. Second, the GOL has access to concessionary external finance, which from a budgetary point of view are preferable (because of lower costs and longer duration) than bonds issued on commercial terms.

219. The GOL commenced issuing short-term LRD-denominated Treasury Bills in mid-2013. A total of LRD 1,077 million of 91-day bills was issued between May and December 2013, at an average rate of around 2 percent, of which LRD 320.5 million was outstanding at the end of the year. In June 2014 a longer maturity 52-week bill was introduced. In 2015, LRD2.8 billion in T-bills were issued. Only banks are permitted to bid for T-Bills.

220. The CBL also commenced issuance of short-term paper for liquidity management purposes in July 2013. The amounts are larger than those of T-Bills: Between July and December 2013, CBL bills totaling LRD 2,328 million were issued, with an outstanding balance of LRD 1,130 million at the end of 2013. Most CBL bills are 91 days but there have been two issues of 180 day bills. CBL bill auctions are open to nonbank participants (for example, major private sector companies).

221. The rules on eligibility for T-Bills and CBL bills are unusual: It is more common for T-Bill ownership to be open to both banks and nonbanks (companies and individuals), and for central bank bills to be restricted to banks only. T-Bills (and longer-term government bonds) are a savings/investment instrument, while central bank bills are primarily for liquidity management in the financial system.

222. The Framework for the Development of Capital Markets in Liberia, prepared by the FIRST Initiative and the World Bank in 2012, concluded that while there was some scope for issuing GOL bonds, these would initially have to be relatively short term (one to two years), and that demand would be quite limited. For the foreseeable future, there is likely to be only modest supply of, or demand for, securities in Liberia, although there is a very pressing demand to provide long-term government debt obligations to NASSCORP, starting with recognition bonds for the unfunded government contributions. The analysis further suggests that there will be insufficient demand for capital markets activity to sustain a securities exchange (with associated clearing and settlement) and that alternative means should therefore be found for encouraging, facilitating, and regulating any developing capital markets activity.

223. There have been a few commercial issuances of capital market instruments. One of the mobile network operators, Cellcom, issued debentures totaling US$7 million through a mixed private placement and public offer, although the company noted that there was limited public demand for the instrument (only US$2 million of the US$5 million on offer was taken up) and the private placement was taken up in full by the underwriting bank. Moreover, as there is complete freedom for inward and outward capital flows, there is every opportunity for companies wishing to raise large sums to do so on overseas markets. The role of international financing is already seen in the substantial amount of FDI financing in the commodity sector (primarily mining but also agriculture). Net FDI in Liberia was as high as 22.8 percent of GDP in 2012 and 20.9 percent of GDP in 2014. Liberia is well positioned to participate in regional financial markets such as Ghana or Nigeria, particularly given the existing presence of financial institutions linked to those countries. Moreover, as the U.S. dollar remains the predominant currency, it is practical for both individuals and institutions to make investments in overseas markets, particularly as many Liberians have strong connections with the United States.

224. Typically, the main domestic demand for purchasing and holding capital market instruments comes from institutional investors—pension funds and life insurance companies. Given that membership of the NASSCORP NPS is compulsory for formal sector employees, and that there is no provision for opting out

if employees join other pension funds, there is unlikely to be significant development of alternative private pension providers in the short- to medium-term. However, a reformed NPS, with increased contribution rates, could provide the basis for institutional demand for capital market instruments in Liberia. Demand for life insurance (and related policies such as funeral insurance) will grow only slowly as real incomes rise and as the private sector develops (creating demand for group life policies etc.).

225. The banks are potential candidates for issuing securities and, in some cases, have done so. LBDI raised capital by making a public offer of its securities to its customers and others. The bank had been hoping to raise some US$10 million in equity. However, the offer only resulted in 50 new shareholders. The majority of investors were already shareholders in LBDI and the Liberian investors only subscribed some US$ 300,000. The remainder of the $10 million was raised through loans rather than equity. In addition, Ecobank sold its customers shares in its holding company, which is listed in Nigeria, Ghana and on the BRVM exchange. The offer was part of a regional offer of US$1 million and some shares were sold to a small number of Liberian shareholders. There is no data available as to whether these shares were sold to existing or new shareholders. In the case of both LBDI and Ecobank offers, there was no legislation or regulations governing the way the sale of securities were conducted, although Ecobank issued guidelines on selling practices to its own staff. Both banks were unable to explain how shareholders could sell the shares once acquired and noted that, in a number of cases, the shareholders had approached the bank seeking a return of their funds as if their investment had been a deposit.

Anti-Money Laundering/Countering Financing of Terrorism (AML/CFT)

226. In 2012, Liberia repealed its AML/CFT law by replacing it with a package of laws[62] and amendments to existing laws[63] aimed at meeting international AML/CFT obligations. This series of laws provided an improved legal framework to establish a financial intelligence unit, criminalize terrorist financing, money laundering and other predicate crimes, and establish the legal basis to freeze assets of designated terrorists, as well as provide and request mutual legal assistance in ML/TF cases. Despite this extensive legislative effort, some important deficiencies in the AML/CFT legal framework remain because during the process of adopting these laws, some critically important provisions (AML/CFT preventive measures) that were contained in the draft laws were removed.

227. As the AML/CFT preventive measures serve as the most critical foundations of an effective AML/CFT system, the AML/CFT legal framework of Liberia remains seriously deficient and the preventive measures provisions need urgently to be restored by amending relevant laws. This is not only important to meet international AML/CFT obligations,[64] but also to ensure reliable links to foreign correspondent banks in view of the increasing threats and risks of money laundering and related financial crimes, including corruption and terrorism/terrorist financing in West Africa, and more specifically in countries facing serious challenges with regard to resources and institutional capacity to support effective systems of regulatory governance. Additionally, lack of progress in implementing international AML/CFT obligations can be met with official countermeasures imposed by countries with financial links to Liberia as well as blacklisting by international AML/CFT standard setting bodies.

228. In an effort to help Liberia avoid such countermeasures, World Bank experts in the Financial Market Integrity Unit (GFMDR) have been supporting efforts of Liberian officials to undertake progress in strengthening the legal framework for the national AML/CFT system. As a result, since 2012, Liberia has made progress in implementing some provisions of the new AML/CFT framework, including. These efforts, summarized below, have been hampered by the recent Ebola crisis.

[62] Anti-Money Laundering and Terrorist Financing Act of 2012; Financial Intelligence Unit Act of 2012; Fraud Act of 2012; Mutual Legal Assistance in Criminal Matters Act of 2012; and United Nations List of Terrorists and Terrorist Groups Act of 2012.

[63] Act to Amend Civil Procedure Law to provide provisional remedies for proceeds of crime; and Act to Amend Penal Law on extortion, environmental crime and illicit trafficking.

[64] A formal assessment of effectiveness in Liberia meeting international AML/CFT obligations is scheduled to be conducted by GIABA in Oct 2020.

229. **The Liberian Financial Intelligence Unit (FIU)** was set up in 2013, staffed with strong leadership and is working with advisory and technical support from the World Bank (GFMDR/FMI unit) and other donors to (a) build FIU operational capacity; (b) further amend and implement AML/CFT laws and regulations; (c) coordinate AML/CFT compliance monitoring of reporting entities under FIU supervision; and (d) establish effective systems for interagency cooperation.

230. **The CBL** has been working with support from World Bank experts (GFMDR/FMI unit) in designing and implementing an effective AML/CFT Inspection System to implement AML/CFT preventive measures among entities under CBL supervision (financial institutions and insurance companies), in addition to drafting a new AML/CFT Regulation which was issued in July 2013.

231. **National AML/CFT Risk Assessment (NRA):** Liberia has formally requested assistance[65] of the World Bank and the ECOWAS Inter-Governmental Action Committee Against Money Laundering (GIABA) to provide technical assistance to Liberia to undertake a National AML/CFT Risk Assessment using the World Bank NRA Tool.[66]

232. While Liberia has recently (2012) enacted new laws to serve as a basis on which to build an AML/CFT system, implementation is slow attributable to lack of resources for implementation. A serious deficiency in the AML/CFT laws is that during deliberation of the draft laws most of the important AML/CFT preventive measures were deleted. These need to exist in the form of enforceable laws and regulations and be effectively implemented. Additionally, Liberia needs to conduct a National AML/CFT Risk Assessment to identify the most serious ML/TF risks to prioritize systems to mitigate them in ways that can be supported by available resources. The CBL should be closely involved in these efforts, as well as in building systems for interagency and international cooperation to fight ML/TF.

233. AML/CFT preventive measures that meet international AML/CFT standards need to be promulgated to ensure they are mandatory and legally enforceable with adequate sanctions for noncompliance. To date, no sanctions for violation of AML/CFT obligations have been imposed and compliance supervision is very weak, however, the World Bank Group is working with the CBL to design and implement a system for AML/CFT supervision for banks and nonbank financial sectors.

Accounting and Auditing

234. The accounting and auditing practices in Liberia have shown marked steps towards improvement in recent years, particularly in the adoption of a new act, the Liberian Institute of Certified Public Accountants (LICPA) Act; 2011, which established LICPA as the self-regulatory body. The LICPA has also been engaged with the World Bank implementing reforms guided by an Accounting and Auditing ROSC conducted in 2011. However, there remain varying compliance gaps in both accounting and auditing practices stemming from inadequate technical capacities of the auditors and regulators, absence of mandate on applicable standards, lack of independent oversight of the auditing profession, and shortcomings in professional education and training.

235. The accounting and auditing sector in Liberia comprises 10 member firms listed in the LICPA and 3 registered practicing accountants (RPAs) who can conduct business but are not eligible to join the institute. The total membership of the LICPA is 55. International firms are increasingly present in Liberia; PWC, PKF and Baker Tilley have resident offices in Liberia and three local firms work in association with KPMG, Ernst & Young and Deloitte. The LICPA is gradually stepping into its new role and has issued two regulations and conducted its first public hearing in March 2014. There is an association of accountancy bodies in West Africa (ECOWAS plus Cameroon) to which LICPA belongs. The ATSWA (Accounting Technicians Scheme West Africa) provides a foundation exam, however the LICPA uses the Institute of

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[65] Dated January 30, 2014.

[66] International AML/CFT standards were revised in 2013 to require all countries to conduct a National AML/CFT Risk Assessment to ensure the AML/CFT systems are more effectively designed based on the actual ML/TF risks a country faces, and to ensure that scarce resources can be allocated to the more serious risks.

Chartered Accountants of Ghana qualification as its admission exam. The cost of preparation of audited financial accounts ranges from US$2,500 to over US$100,000.

236. There remains much to be done in the auditing sector, for example there is no effective mechanism exists to enforce requirements for accounting and financial reporting. The Association Law (the Liberian equivalent of the Companies Act) does not include the fundamental requirement to present audited financial statements to shareholders annually. As a result, most companies, especially SMEs, do not generally feel obligated to prepare financial statements. Accountants often prepare a "statement of affairs" rather than audited accounts. Moreover, the Revenue Code of Liberia 2000 does not require companies to submit annual financial statements with their annual tax returns. In addition, there is no legal mandate for corporate entities to follow IFRS or any national standards in preparing financial statements, and national or International Standards on Auditing (ISA) in conducting audits. The CBL, since 2008, has adopted IFRS for preparing its own financial statements and mandated these standards for commercial bank financial reporting from December 2012, however, many prudential regulations are consistent with GAAP rather than IFRS. Those local firms that are members or correspondents of international networks of accounting firms do follow ISA as required by the international networks to which they belong.

237. In Liberia statutory auditors are not specifically prohibited from providing some non-audit services, including tax advocacy and representation before tax authorities. There is a strong perception among the various stakeholders that such involvement may pose a threat to auditors' independence.

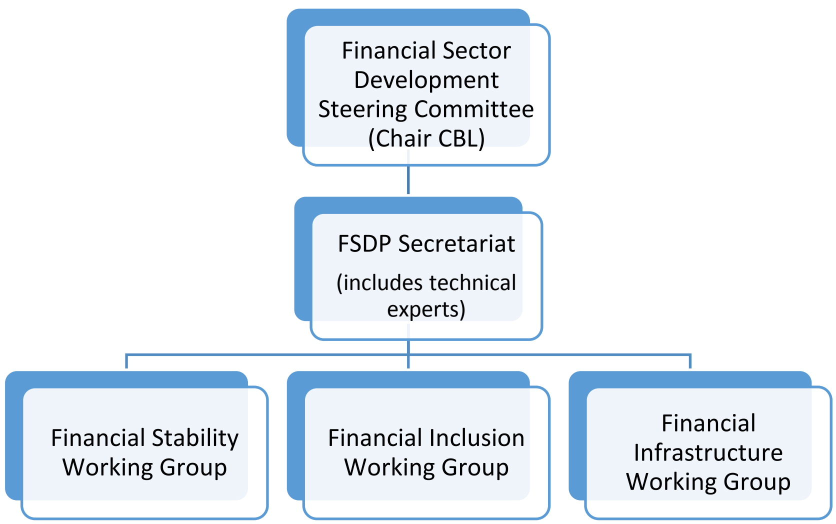
238. Within the LICPA framework there is provision for an Audit Quality Assurance Board which has representatives from the Ministry of Finance, the CBL and Ministry of Justice but this role has yet to be fully operationalized (it would also have been preferable that the Board be an independent entity under the Ministry of Finance and also that it include the Auditor General.

239. With specific reference to the financial sector, both the CBL and the commercial banks have adopted the IFRS. To ensure uniformity of standards, it will be prudent that the LICPA pursue national adoption of the IFRS. The current reporting practices of IFRS and GAAP for tax purposes create complications in the analysis of financial statements and assessment of the performance of the banks.

IMPLEMENTATION, MONITORING, AND EVALUATION OF THE FSDIP

- The Financial Sector Steering Committee (FSSC) that has been established will play the principal role in overseeing the implementation of the FSDIP. Its members are senior-level representatives from the CBL, the Ministry of Finance and Development Planning, Ministry of Commerce and Industry, Ministry of Justice, NASSCORP, and the Bankers Association. The Committee will be chaired by a Deputy Governor of the CBL.
- A technical team composed of representatives of these same organizations will be responsible for managing the implementation of the FSDIP and will supervise the thematic working groups that are established by the FSSC with representation from the public and private sectors. A small FSDIP Secretariat should be established by and report to the Financial Sector Steering Committee. The role of the Secretariat is to support the work of the technical team and working groups. Figure 22 shows a proposed governance structure for the FSDIP.
- At the preparation phase of the reform process, each of the technical teams will be responsible for developing cost estimates and results targets for the distinct work channels. These will be consolidated and assessed by the FSSC for realism and value for money. The Steering Committee will work with development partners in this process and pass on recommendations to Government for final approval.

Figure 22: Governance Framework for the FSDIP



Monitoring and Evaluation

240. The Technical Committee will be responsible for the supervision of the implementation of the plan. It will prepare a four-year Gantt chart with benchmarks for actions and review and adjust the chart as needed. Much of the work will require the active participation of private and public sector financial institutions as well as other public and private nonfinancial entities. These institutions will be an essential part of the thematic working groups and for implementation of components of the plan that affect them.

241. To enable the FSSC to oversee progress in implementation of the plan, each working group should report its progress quarterly to the FSDIP Secretariat for transmittal to FSSC members. The FSSC will prepare a semiannual report on its activities and progress in implementation of the Roadmap of reforms. In addition to this reporting, a strong measurement and evaluation system is needed to track progress relative to the objectives of the plan. This will aid in the identification of successful programs that can be replicated, obstacles that need to be removed, unintended consequences that result and/or tactical readjustments of the plan as needed.

242. Key to this measurement and evaluation framework is conducting a demand-side financial sector survey every two years after first establishing a baseline survey. The Technical Committee will explore options for how best to conduct the survey using existing resources or new resources. In the demand-side surveys attention will be given to the uptake and usage of new or enhanced products, services, and processes envisaged in the plan to assess their impact.

ROADMAP FOR REFORMS

#	Policy Action	Priority	Working Group[67]	Target Completion
		Banking Sector		
1	Adopt Master Repurchase Agreement for interbank transactions.	Medium	Financial Infrastructure	8/17
2	Expedite adoption of new or revised financial sector legislation (Payments Act, Insolvency Act, the CBL Act etc.).	Medium	Cross-cutting	5/17
3	Coordinate with the Debt Resolution project of the Law Reform Commission and Judiciary for Alternative Dispute Resolution and mediation within ambit of commercial court. Establish Mediation Rules for Commercial Court and promote consideration of the draft Insolvency Law.	High	Cross-cutting	5/17
4	Conduct Insolvency and Creditor Rights ROSC (Review on Observance of Standards and Codes) and establish action plan based on findings.	Medium	Financial Inclusion	8/17
5	Assess viability of a deposit insurance law that complies with the core principles of International Association of Deposit Insurers (IADI).	High	Financial Infrastructure	5/17
6	Conduct an external assessment with Basel Core Principles under an FSAP.	High	Financial Stability	12/17
7	Commission study on other countries' experience of dual currency regimes. Specifically assess potential risk to banking system of adoption of Liberian dollar as sole legal tender.	Medium	Financial Stability	8/17
		Insurance Sector		
8	Enforce capital requirements of new Insurance Act and initiate processes to supervise the orderly transfer of business from companies not meeting capital requirements.	High	Financial Inclusion	11/18
9	Adopt IFRS in the insurance sector.	High	Financial Inclusion	8/17
10	Review the NICOL Act.	Medium	Financial Inclusion	11/17

[67] Cross-cutting denotes members from up to all three groups, including the possibility of outside members.

Banking and Insurance Supervision				
11	Strengthen capacity of Consumer Protection Unit to ensure enforcement of regulations, including on-site inspection.	Low	Financial Inclusion	8/17
12	Review regulations issued under the New FIA (1999), including with respect to the bases for CBL intervention and tools for enforcement, considering realistic prospects for compliance	Medium	Cross-cutting	2/18
13	Review and amend CBL regulations and guidelines to differentiate recommendations from legally binding rules. Establish predictability of sanctions for noncompliance.	Medium	Cross-cutting	2/18
14	Develop and publish internal rules of regulatory procedure for the CBL reflecting new procedures for regulatory governance to enhance CBL transparency, responsiveness to regulated institutions and the public, and efficiency.	Medium	Cross-cutting	2/18
15	Establish a Financial Stability Council for macroprudential surveillance and reporting; prepare and publish an annual financial stability report.	Medium	Financial Stability	9/17
16	Develop a modern financial institutions resolution law with key elements of EU Directive 2014/59 to replace articles 40 and 47–55 of the New FIA.	Medium	Financial Stability	11/17
17	Establish a crisis management framework including guidelines for management of systemically important problematic financial institutions and financial crises. Establish contingency plans for financial crisis management and arrangements for the exercise of CBL role as LOLR, including in cases of systemic liquidity pressures.	High	Financial Stability	5/17
18	Develop a bank resolution framework, including triggers for corrective action and bank resolution.	High	Financial Stability	5/17
19	Clarify limits on aggregation of large exposures in bank regulations.	High	Financial Stability	5/17
20	Determine international best practice for related party transactions for both Banking and Insurance industries and establish appropriate regulations.	High	Financial Stability	5/17
21	Adopt prudential and market conduct insurance regulations now in draft form.	High	Financial Inclusion	5/17
22	Supervise insurance business conduct for selling practices that compromise claims paying ability.	High	Financial Inclusion	Ongoing

Credit Information Systems				
23	Implement legal framework for credit reporting to ensure comprehensive credit information (positive and negative) is available on all formal borrowers.	High	Financial Infrastructure Financial Inclusion	5/17
24	Develop proposal for PPP credit information system, including microfinance/rural sector, insurance and NBFIs.	High	Financial Infrastructure Financial Inclusion	11/17
Payments Systems & Digital Finance				
25	Complete the planned RTGS/SSS, ACH/ACP and core banking for central bank. Implement interoperability arrangements for card payments.	High	Financial Infrastructure	8/17
26	Coordinate with Ministry of Internal Affairs regarding biometric National ID system and prospective linkage to credit information database.	High	Financial Infrastructure Financial Inclusion	02/19
27	Establish dedicated payments oversight function/division within the CBL with oversight policy framework and oversight guidelines.	High	Financial Infrastructure	02/17
28	Development of a Government Payment program with the objective to migrate all disbursements (incl. social cash transfers), collections, and payrolls to electronic payments, based on the USAID-GEMS initiative.	High	Financial Infrastructure Financial Inclusion	9/18
29	Develop National Payments System strategy including a comprehensive Retail Payments Strategy aiming at increased access to transaction accounts, use of electronic payments, expansion of access points and supporting measures (e.g. interoperability).	High	Financial Infrastructure Financial Inclusion	9/17
30	The CBL to develop a database for the comparison of fees for account and payment services and requiring banks and nonbank providers to provide the respective data.	Medium	Financial Infrastructure Financial Inclusion	11/17
31	Coordinate with Presidential Delivery Unit for the transition of all G2P (Government to People) payments (salaries and transfers) to a digital platform.	Medium	Financial Infrastructure Financial Inclusion	5/17
32	Reassess remittance market against general principles.	Medium	Financial Infrastructure	11/17
33	Make an assessment against PAFI guiding principles and identify key actions.	Medium	Financial Infrastructure Financial Inclusion	8/17
34	Establish National Payments Council.	Medium	Financial Infrastructure	2/17

35	Implement Mobile Money Strategy.	Medium	Financial Infrastructure Financial Inclusion	8/17
Social Security (NASSCORP)				
36	Ensure Government contribution to NASSCORP is funded (including an assessment of the accrued to date liabilities for employees who are covered under the Civil Service arrangements).	High	Financial Inclusion	11/18
37	Review NASSCORP actuarial review both in relation to the accrued to date liabilities and the open system liabilities; and seek to ensure long term sustainability (Establish whether the asset values used in the projection of the future cash flow deficits in NPS are realizable values and review administrative expenses to ensure efficiency and alignment with participant interests).	High	Financial Inclusion	11/17
38	Establish process for consolidation of Public Service Pension Scheme within NASSCORP on a fully funded basis.	Low	Financial Inclusion	2/18
39	Complete the collection and revision of member data for members of both the CSA and NPS.	Medium	Financial Inclusion	11/17
40	Address the issue of lack of indexation in NPS and possible inequities in the calculation of the reference wage in NPS.	Medium	Financial Inclusion	11/18
41	Improve the enforcement of mandatory membership of NPS to lift the coverage rate from the present 59% of the formal workforce.	Medium	Financial Inclusion	2/19
42	Explore feasibility of shift to digital payments (electronic funds transfer or mobile money) for all pension payments (security services as well as NPS and CSA).	Medium	Financial Infrastructure Financial Inclusion	8/17
Financial Inclusion				
43	Establish and enforce regulations for governance, credit appraisal and risk management.[68] Arrange for training in these areas.	High	Financial Inclusion	8/11
44	Ensure all regulated MFIs provide audited financial statements within 3 months of end of financial year. Unaudited reports to be submitted within one month of end of year and half-year.	High	Financial Inclusion	8/17
45	Require MFIs to separate financial operations from social support activities, with separate accounts.	Medium	Financial Inclusion	8/18
46	Coordinate with donors for support for hardware and software limited to MFIs[69]	Medium	Financial Infrastructure Financial Inclusion	11/17

[68] For registered MFIs, licensed deposit-taking MFIs, and VSLAs; credit unions and RCFIs have draft regulations in development.

[69] Registered MFIs, licensed deposit-taking MFIs.

	which are compliant with regulations and reporting for credit underwriting analysis and financial reporting.			
47	The CBL to conduct training in governance for the boards of MFIs[70] including on risk management, for those not supported by international partners.	High	Financial Inclusion	8/17
48	Evaluate the feasibility of introduction of micro insurance for certain MFIs for life, health, credit, and crop failure.	Low	Financial Inclusion	2/18
49	Support transition to digital financial services by microfinance and rural financial institutions.	High	Financial Infrastructure Financial Inclusion	8/17
50	Launch a comprehensive program of Financial Education, focused on key teachable moments where insurance, the wise use of credit, savings and payments can be beneficial.	Medium	Financial Inclusion	9/17
51	Develop regulatory framework for establishment of payment agent (“Agency Banking”) functions in connection with mobile money (digital financial services).	High	Financial Infrastructure Financial Inclusion	8/17
52	Establish Rural Community Finance Institutions in every county.	Low	Financial Infrastructure Financial Inclusion	8/19
53	Promoting the Expansion of Branches of commercial Banks in southeast and Western Counties.	Low	Financial Infrastructure Financial Inclusion	8/19
54	Establish Four Regional Credit Unions.	Low	Financial Infrastructure Financial Inclusion	8/19
Enterprise Access to Finance				
55	Explore opportunities for financial leasing (including structures which allow extrajudicial recovery of leased property).	Medium	Financial Inclusion	8/17
56	Map existing and planned government-wide economic stimulus initiatives (MFI, mortgage, and SME etc. to identify synergies and overlaps.	Low	Financial Inclusion	8/17
57	Support strong auditing and accounting infrastructure and implementation of international standards.	Medium	Financial Inclusion	2/18
58	Evaluate potential for warehouse receipts financing including review of the legal, regulatory, accounting and tax rules.	Medium	Financial Infrastructure Financial Inclusion	2/19
59	Revise the Association Law of 1976 make mandatory the submission of audited financial statements for all public interest entities using IFRS and ISA as mandatory standards and simplified reporting requirements for SMEs.	Medium	Financial Inclusion	2/18

[70] Registered MFIs, licensed deposit-taking MFIs, and VSLAs.

Anti-Money Laundering/Countering Financing of Terrorism				
60	Draft and submit regulations on Cross Border Transportation of Currency, Suspicious Transaction Reporting (STR), Politically Exposed Persons (PEPs & Currency Transaction Reporting (CTR) for AML/CFT reporting entities.	Medium	Cross-cutting	8/17
61	Initiate preparations for National AML/CFT Risk Assessment utilizing the World Bank NRA Tool.	Medium	Cross-cutting	11/17
62	Draft and adopt AML/CFT Inspection Procedures for banks and insurance companies.	Medium	Cross-cutting	8/17
63	Review and amend existing AML/CFT laws to remedy legal framework deficiencies and ensure adequate legal basis to meet international AML/CFT obligations.	Medium	Cross-cutting	11/17

Annex 1: Key Policy and Institutional Reforms

Macroprudential Surveillance and Crisis Prevention and Management

After the recent global financial crisis, many governments, international organizations, and academic institutions came to the conclusion that there was an insufficient focus on macroeconomic conditions as they affect financial stability. Instead, the focus was more on individual financial institutions, which had failed to prevent the financial crisis. To this end, it was also determined that there was a strong need to improve financial sector stability by clarifying financial authorities' functions to strengthen their role in financial sector stability policy and application of macroprudential instruments and financial safety nets for risk mitigation. The forum for such focus for many countries was a new financial stability council.

Financial Stability Councils

The Financial Stability Councils established to exercise macroprudential oversight of the financial sector usually consisted of the Ministry of Finance, the Central Bank, the bank supervisor, and the supervisors of nonbank credit institutions and of capital markets institutions (securities firms, asset managers, insurance companies, and pension funds), and sometimes the deposit insurance agency.

Having a body of the authorities responsible for the financial sector as well as the Ministry of Finance whose activities can have a direct as well as indirect effect on financial markets is a means to institutionalize coordinated action to seek to maintain financial stability by adopting a macroprudential approach to supervision of financial institutions and to address crises. The CBL has recognized the need for emphasis on financial stability from a macroprudential perspective although there is some question as to whether a multiparty council is more suited to advanced economies with diversified financial sectors.[71] Annex 3 contains a discussion of the functions of such council and recommended reforms for Liberia to seek to prevent and, should the need arise, manage a financial crisis.

Regulatory Governance

Now that the RSD has developed basic regulatory rules and supervisory capabilities in banking, insurance, and other nonbank financial institutions supervision along the lines of standards issued for the sectors by the Basel Committee on Banking Supervision and the IAIS, it is appropriate to refine the quality of its regulation under the theme of good regulatory governance.

Proper regulatory governance promotes transparency, responsiveness to the regulated sectors and the public, accountability of regulators, and efficient and smart regulation. At its most basic, regulatory governance requires that a regulatory authority have the legal authority to fulfill its mandate—adequate powers to issue obligatory rules for regulated entities and to enforce those rules, rather than rely on a ministry in the first instance.[72] Poor-quality regulations generate a range of broader social, environmental and equity costs, such as ineffective enforcement and providing incentives for corruption.[73]

Unlike for financial sector supervision or corporate governance or where there are well established international best practice standards like the 'Basel Core Principles for Effective Banking Supervision' and the IAIS Insurance Core Principles, there is no recognized standard for regulatory governance. However, certain standards with other principal objectives advocate or include elements of good regulatory governance.

[71] CBL notes that in Nigeria, the issue of financial stability lies largely in the purview of the Central Bank, as the CBN has set up a Financial Stability Department to deal with financial stability and macroprudential issues, which may be an appropriate model for Liberia.

[72] See the Basel Committee's Core Principles for Effective Banking Supervision (www.bis.org/publ/bcbs129.htm) Principle 1.

[73] Tools and Approaches to Review Existing Regulations, The World Bank Group, 2010, p. 2.

For example, Principle 1 of the ‘Basel Core Principles’ encourages “transparent processes, sound governance and adequate resources” without prescribing any specific elements for such purposes while Part II of the International Monetary Fund’s ‘Code of Good Practices on Transparency in Monetary and Financial Policies’ in respect of Open Process for Formulating and Reporting Monetary Policy Decisions provides for certain elements of transparency and accountability.[74]

The need for improved regulatory governance was cited in the IMF’s review of the RSD in its August 2014 report of recommendations and Comments of financial institutions to the July 2015 mission were to the same effect.

(a) Assess the technical and implementation dimensions before the introduction of new regulations and/or initiatives;

(b) Ensure a participative approach in discussion with stakeholders and provide sound, clear and persuasive rationalization for the relevance of proposed reforms.

Key Elements

Annex 5 contains a discussion of the background of regulatory governance and key elements of good regulatory governance that the CBL could consider adopting, as indicated in table 12.

[74] www.imf.org/external/np/mae/mft/code/index.htm

Annex 2: Macroprudential Surveillance and Financial Crisis Prevention and Management

After the recent global financial crisis, many governments determined that there was a strong need to improve financial sector stability by clarifying financial authorities' functions to strengthen their role in financial sector stability policy and application of macroprudential instruments and financial safety nets for risk mitigation.

This task was often assigned to a new Financial Stability Council. Annex 2 contains a detailed discussion of the role of a financial stability council.

The Role of a Financial Stability Council

A Financial Stability Council as understood internationally has three basic functions:

(a) Monitoring from a macroprudential policy perspective systemic risk to the financial sector

(b) Employing macroprudential instruments or making recommendations for use of such instruments to prevent or mitigate systemic risk

(c) Coordinating management and managing a financial crisis

The CBL has a Financial Stability Committee, which could be enlarged with the addition of the MFDP to become a Financial Stability Council to routinely and systematically monitor the financial sector from a macroprudential perspective and implement or recommend application of macroprudential instruments to prevent or mitigate systemic risk.

Such a body would be similar to those established in many countries after the recent global financial crisis. In monitoring systemic risk, the Council should consider structural factors such as systemically important financial institutions, funding markets, impediments to financial institutions' performance in the legal system, deficiencies in prudential regulations, and difficulties in bank resolution. Cyclical factors that should be considered include excessive leverage by financial institutions and real sector borrowers, excessive asset valuations, excessive credit growth, excessive credit concentration, an elevated level of NPLs in the banking system, undercapitalized banks, fiscal imbalances, excessive inflation, and the vulnerability of enterprises and households to adverse changes in exchange rates.

To prevent or mitigate systemic risk with respect to structural factors, macroprudential policy actions that can be taken include periodic stress testing of systemically important financial institutions, increased capital and liquidity requirements for those institutions, stronger asset classification and income recognition rules for banks, and loan recovery and bank resolution legal reforms. To address cyclical factors, for example, leverage levels and asset and liability maturity mismatches could be limited.

To modernize and rationalize the approach to dealing with financially distressed financial institutions, the FIA should be amended and a new law on financial institutions resolution enacted. A deposit insurance scheme should also be established.

For managing a financial crisis, contingency plans should be established regarding thresholds for action, coordination of actions among responsible authorities, and communications to the public.

To enable the Council to receive quality analyses on financial market institutions and markets with respect to actual and likely systemic risks, the Council should establish a formal agreement on information sharing between the Council members.

For transparency and accountability, in its financial stability reports, the Council should report on its activities, macroprudential actions taken, and the effect of such actions. Annex 3 contains a discussion of activities of a financial stability council including tools and areas of focus for analysis and macroprudential policy responses.

Financial Institutions Resolution

A key element of the toolkit to seek to maintain financial stability and to manage a failure of a systemically important financial institution is a comprehensive modern law for financial institutions resolution. Articles 24, 40, and 47–55 of the New FIA (1999) relate in part to resolution but without the focus or precision found in modern resolution laws.

Financial institution resolution should occur when, based on actual or expected insolvency or illiquidity of a systemically significant institution, the supervisory authority takes control of its governance and management and seeks to effect an orderly change of control or transfer of some or all of its assets, liabilities and/or functions to other sound institutions. The intended objectives of such actions are to maintain stability in the financial sector by the preservation of financial services and to maximize the value of the assets of the financially distressed institution to protect the interests of depositors or insurance policy holders and other creditors and spare the budget of providing financial support for such institutions.

Resolution is not supervisory action to remedy violations of the law or regulations with respect to prudential or market conduct matters or corporate governance as in Article 40 that is not proximately related to insolvency. The critical distinction is that in resolution an institution will not continue to exist in its former state with respect to ownership, governance, and management. It may be sold to another institution or other public or private sector shareholders as an institution, or its assets and liabilities may be transferred in whole or in part to other institutions or to a bridge institution or to an asset management vehicle. Thus, as a practical matter, its owners, governing body, and senior management will change in whole or in part.

Annex 3 contains a discussion of a modern financial institutions resolution law and how it differs in some respects from provisions in the New FIA (1999).

Annex 3: The Activities of a Financial Stability Council

After the recent global financial crisis, many governments determined that there was a strong need to improve financial sector stability by clarifying financial authorities' functions to strengthen their role in financial sector stability policy and application of macroprudential instruments and financial safety nets for risk mitigation.

Background

The Financial Stability Councils was established following the global financial crisis to exercise macroprudential oversight of the financial sector usually consisted of the ministry of finance, the central bank, and the supervisors of nonbank credit institutions and of capital markets institutions (securities firms, asset managers, insurance companies, and pension funds), and sometimes the deposit insurance agency.

Having a body of the authorities responsible for the financial sector as well as the ministry of finance whose activities can have a direct as well as indirect effect on financial markets is a means to institutionalize coordinated action to seek to maintain financial stability by adopting a macroprudential approach to supervision of financial institutions and to address crises.

A model charter of such council would be like the following:

- The council determines public financial stability policy by (a) monitoring from a macroprudential policy perspective actual and emerging risks to the financial sector; (b) recommending that its members take action individually for which they have authority or recommending to other bodies actions to prevent or mitigate systemic risk to the financial sector; and (c) coordinating management of public responses to serious threats to financial stability.

Macroprudential Policy

According to the Group of 30, macroprudential policy includes the following characteristics[75]:

- Oversee and deliver appropriate policy responses to the financial system as a whole rather than focusing on individual institutions.
- Dampen systemic risks via interconnectedness and pro-cyclicality.
- Apply tools to reduce systemic risk and increase resilience to risks.

Also according to the G-30:

> "…the focus of macroprudential policy must be on the financial system as a whole and on specific institutions only as they affect that system. Since a primary concern of macroprudential policy is…the interconnectedness of financial institutions and markets and the resulting speed of propagation of risks through the financial system, its application must begin before such risks have propagated through the system. As a result, macro-prudential supervisors must recognize, analyze data regarding, publish anticipatory guidance on, and address systemic risks as they emerge."

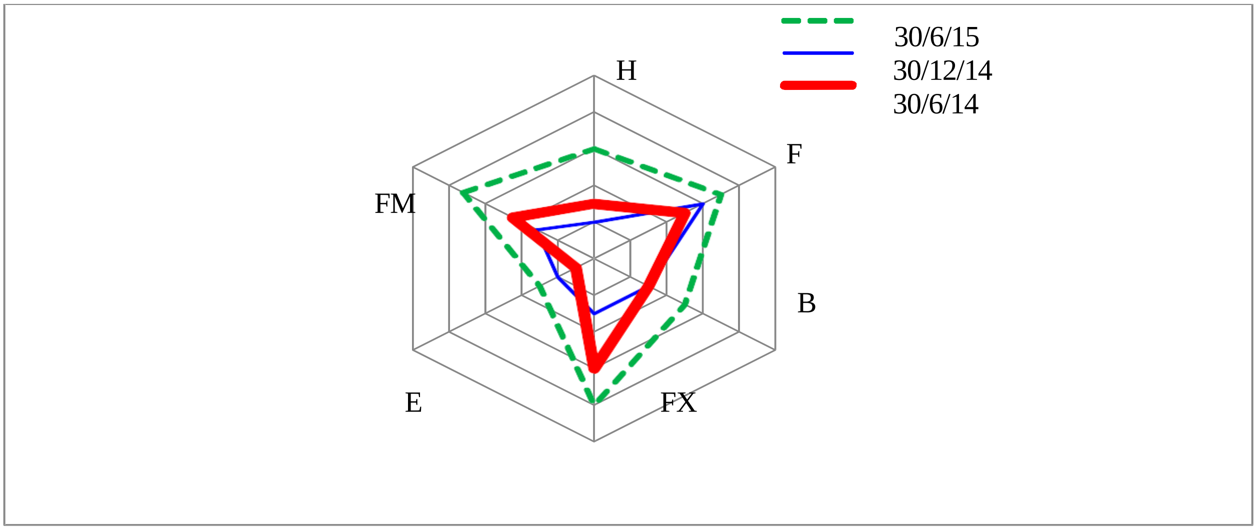
Thus, the council should consider its work to be primarily the conduct of macroprudential policy.

[75] Enhancing Financial Stability and Resilience, 2010.

Macroprudential Analytical Tool

The Council secretariat for its macroprudential analysis and for publication in financial stability reports should develop a spider graph Financial Stability Map to provide a graphical summary and a reference point for further analysis that captures a diverse range of potential sources of financial sector systemic risk. The spider graph in Figure 23 can be used to assess the degree of risk in six sectors and markets over three periods of time.[76]

Figure 23: Degree of Risk in Sectors and Markets over the Period June 2014–June 2015



Note: H = household soundness; F = fiscal imbalances; FX = exchange rate volatility; B = bank soundness; E = economic conjuncture; FM = financial markets.

This example illustrates that in the most recent period the condition of the banking sector is an emerging threat to financial stability and that financial market conditions and fiscal imbalances are also a cause for concern.

The key notion underpinning such map is that financial stability cannot be distilled into a single indicator but is better understood by identifying underlying risks and conditions that could give risk to a systemic threat. The map should extract information from variables which describe vulnerabilities in different sectors and markets in an economy.

The Council will determine which sectors and markets are considered relevant for financial stability in Liberia. However, for example, for six factors, the following could be assessed: (a) risks in the private sector (household financial soundness); (b) public sector (fiscal imbalances); and (c) banking sector (bank soundness); (d) financial markets; (e) domestic economic conjuncture; and (f) external vulnerability economic conditions.

"Household Financial Soundness" would measure credit stress in household balance sheets. "Fiscal imbalances" result from unsustainable fiscal paths and rising debt burdens that affect interest rates and asset quality of government securities. Under "Bank Soundness," various types of risks that banks face are captured with financial soundness indicators. Domestic economic conditions ("Economic Conjuncture") affect financial stability through various channels; for example, production, wage income, and consumption underpin credit risk, and inflation/deflation risk can impact real debt burdens. "Financial Market Conditions" gauge the cost and availability of funding via volatility in the bond, stock, and FX markets.

[76] The discussion in this paragraph and those below on Financial Stability Map indicators is adapted from Brazil: Macroprudential Policy Framework, Technical Note, IMF/MCM, January 2013.

"External Vulnerability" captures potential impact from external shocks, for example that affect capital flows.

The following are examples of indicators that cover important aspects of risks in each segment.

- Household Financial Soundness: Loan default rate, households' debt-to-income ratio, average real income growth, savings deposits to GDP, consumer confidence index, and household debt service to income ratio.
- Fiscal Imbalances: Public net debt to GDP (percent), budget deficit to GDP (percent), JP Morgan Emerging Market Bond Index Plus sovereign spread, and foreign reserves to imports.
- Bank Soundness: Regulatory capital to risk-weighted assets, NPLs to total gross loans, return on assets, liquid assets to total assets, and FX net open positions to capital.
- Economic Conjuncture: Growth rate of industrial production (y/y), private consumption growth rate (y/y), CPI (y/y), average real income growth rate (y/y), and current account to GDP.
- Financial Market Conditions: Volatility estimated models of indicators such as policy interest rate, stock price index, nominal FX rate (MNT/US$), domestic liquidity index (interbank overnight borrowing), and FX liquidity index (FX interbank overnight borrowing).
- External Vulnerability: FX rate volatility, current account and capital account BOP volatility.

Macroeconomic and Macroprudential Policy Distinction

The G-30 publication also makes this distinction:

> "Macroprudential policy and macroeconomic policy often complement each other since both take a broader view of the economic system rather than emphasizing the fate of individual institutions. Historically, however, macroeconomic policy has looked at single economic measures in isolation or at the interaction among a small set of such measures. Most notably, macroeconomic policy has focused on the interaction between interest rates and inflation attempting…to stabilize the aggregate price of goods and services in the economy…"

Macroprudential Policy Instruments

Based on its assessment of actual or likely systemic risk, the Council members should consider the application of various macroprudential policy instruments, some of the most common of which are described below. Macroprudential policy employs some of the same tools as prudential regulation but from the perspective of the system as a whole and not from that of individual institutions.[77]

- To strengthen capital adequacy:
  - Capital multipliers based on growth of credit or maturity mismatches.
  - Increased capital against the securities trading book.
  - Countercyclical capital buffers.

[77] According to the G-30, "The prime example is capital regulation, which is used in the prudential supervision context to ensure the safety of an individual firm under stress, but can also be employed in the macroprudential context both to ensure the resilience of the overall system and to mitigate the risk created by network effects within the financial system and pro-cyclical behavior."

    - Gross leverage ratio.
    - Capital surcharge for SIFIs.
- To strengthen liquidity:
    - Limit asset growth based on less stable funding.
    - Limit maturity mismatches in funding.
    - Capital surcharge on inadequate liquidity.
- Other macroprudential measures that can be taken are as follows:
    - Adjusting regulatory treatment of NPLs.
    - Limiting credit to particular sectors of the economy.
    - Establishing requirements such as loan to value ratios for loans for particular purposes where there are excessive asset valuations.

The G-30 publication also provides an example of the distinction between a prudential and a macroprudential approach to asset valuation:

> "[I]n the fall of 2008, the values of complex financial instruments, including those created through securitization, held by many banks became impossible to determine, although prices were clearly lower than they had been when these instruments were purchased. A prudential supervision approach would, for the safety of individual financial institutions, encourage each institution to resolve such assets as quickly as possible. However, the actions of an individual financial institution could cause unrealistic valuations to be recorded for all financial institutions, precipitating capital or funding problems, "fire sales," and an evaporation of liquidity."

Thus, in the interest of financial stability, ordinary prudential regulations sometimes should be modified or suspended as appropriate.

Focus of the Council on Financial Subsectors

Banks account for approximately 90 percent of financial sector assets in Liberia so the focus of the Council's macroprudential policy should be predominantly on banks. Nevertheless, consideration should be given to whether microfinance or other credit institutions or insurance activities should be monitored for possible adverse systemic implications.

The life insurance sector could also be considered systemically significant if it sells savings products to a large segment of the population. Its failure could also hinder development of life insurance for some time.

Fiscal Imbalances as a Threat to Financial Stability

If the government borrows excessive amounts because of excessive fiscal deficits, the value of the government's debt could decline based on new fiscal developments and lead to losses for banks that hold government securities when securities are marked to market. This was the primary cause of bank failures in recent years in Greece and Cyprus. Such government borrowing can also raise the general level of interest rates and lead to declines in banks' income when their liabilities reprice faster than the prices of their assets, as is often the case.

There is a Public Financial Management Act of 2009 that provides for discipline in fiscal management that should avoid fiscal imbalances that pose a threat to financial stability. Nevertheless, the government's fiscal position should be monitored by the Council based on data and analysis from the MFDP and international financial institutions and if there is a cause of concern, this is an appropriate matter for Council deliberations and recommendations to the MFDP.

Concern by the Council with Fiscal Policy and Monetary Policy

The Council could, of course, deliberate on any matter that it wishes. With respect to fiscal policy and monetary policy, however, given the limited resources of the secretariat, it should perhaps focus not on the causes for and formulation and implementation of these policies but on the effects of these policies on risk to the financial system. In addition to the staffs of the MFDP and of the CBL, guidance on appropriate fiscal policy is also provided by the IMF and World Bank and guidance on monetary policy to the CBL by the IMF. There are also analyses of the macroeconomic condition of Liberia by private sector entities and other international organizations that can be consulted by the Council secretariat.

Macroprudential Policy Focus and Action

To provide for the effectiveness of the Council in surveillance of actual and likely threats to financial stability and for taking action to prevent or mitigate such threats, the Council's charter or bylaws could include the following:

(a) At each of its regular meetings, the Council shall consider the following matters if, in the judgment of the Council Secretariat, one or more of the following situations pose an actual or likely risk to financial stability:

   (i) The condition of systemically significant financial institutions;

   (ii) The state of the interbank market;

   (iii) The state of the interbank payments and the mobile money payment systems;

   (iv) Fiscal imbalances;

   (v) Interest rate volatility;

   (vi) Household indebtedness;

   (vii) Enterprise indebtedness[78];

   (viii) Current account and capital account balance of payments volatility (EWS analysis);

   (ix) Commodity exports price volatility;

   (x) FX rate volatility;

   (xi) Asset bubbles;

   (xii) Financial asset price volatility;

   (xiii) Undesirable incentives in the management of financial institutions;

   (xiv) Unlicensed or fraudulent financial services or transactions.

(b) At each of its regular meetings, when the Council agrees that a situation exists that poses an actual or likely threat to financial stability, the Council shall recommend that macroprudential instruments be deployed to prevent or mitigate such threats to financial stability.

   (i) If new legislation is required to deploy such instruments, the Council shall prepare such draft legislation and present it to the National Assembly.

(c) When macroprudential instruments have been deployed, at each of its regular meetings, the Council shall consider the effectiveness of such instruments and the need for their adjustment or for the deployment of additional instruments.

[78] For example, debt to cash flow (EBITDA—earnings before interest, taxes, depreciation and amortization).

Financial Safety Nets: Crisis Prevention and Response Instruments

There are three so-called financial safety nets to prevent or mitigate threats to financial stability—emergency liquidity arrangements for banks, deposit insurance, and insurance policyholder protection schemes.[79] The Council should ensure that emergency liquidity arrangements for banks and deposit insurance are designed to be useful for their purposes.

Central Bank Credit to Banks

The most basic instrument to support a financially distressed bank that is systemically significant is credit from the central bank. This has been referred to in recent years as "Emergency Liquidity Assistance" or ELA. Section 32 of the Central Bank of Liberia Act provides ample authority and flexibility for the CBL to provide credit to troubled bank, including, in Section 32(2), the power to grant credit that is unsecured, on "an exceptional basis, or to protect the integrity of the banking system."[80]

However, Section 44(1) (a) could limit its ability to support a systemically significant bank by the prohibition on the CBL to "participate directly or indirectly in the ownership of any financial… or other enterprises…" During financial crises, including the recent global financial crisis, some finance ministries and central banks purchased preferred shares in banks as the means to provide financial support as equity. Equity injections in banks would preferably be the role of the MFDP, but for extreme circumstances, the central bank should have the legal authority to provide such support. Thus, this provision could be amended to provide a limited exception for equity support to systemically significant banks. Preferred shares are functionally similar to subordinated debt.

Deposit Insurance

Deposit insurance provides one of the key financial safety net elements to mitigate the effect of bank failures and prevent runs on banks other than a failed bank. The quality of deposit insurance laws is assessed against the International Association of Deposit Insurers (IADI) 'Core Principles for Effective Deposit Insurance Systems.' The CBL is considering a recommendation for such a law. A function of the Council could be to determine whether a new deposit insurance agency is equipped administratively to implement the new law.

The most important provision of a law on deposit insurance is the circumstances under which insurance will be paid. For financial stability, depositors should have confidence that if they cannot withdraw their deposits from a bank, the insurance will be paid to them promptly within the limits of the insurance.[81]

Otherwise, if segments of the public know that the deposit insurance system is ineffective, this knowledge could cause a run on other banks and cause a financial crisis that deposit insurance should be designed to prevent, when it is only one bank that has failed and perhaps even a small one.

Bank Loan Collection

High levels of banks' NPLs, which is currently the case in Liberia, usually pose a threat to bank solvency. These obstacles constitute structural factors that can cause systemic risk and the Council should consider means for facilitating debt recovery to reduce NPLs and increase bank income. For example, one or more

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[79] Life insurance is undeveloped in Liberia and when it becomes more developed consideration should be given to establishment of such a scheme. In other countries certain types of life insurance products are considered by many savers and investors to be bank deposit substitutes and can be relatively large among financial sector assets. Thus, a safety net for certain types of life insurance policies could provide stability in time of stress.

[80] "On an exceptional basis" is a questionable basis if unrelated to financial stability.

[81] Principle 17 of the IADI Core Principles for Effective Deposit Insurance Systems provides that "the deposit insurance system should give depositors prompt access to their insured funds." This is generally considered to mean payment of insurance within one week from the cessation of payment of deposits.

of the following recommendations after consultations with systemically significant banks in Liberia, could be issued by the Council:

> "To improve their loan asset quality and reduce their stock of NPLs, banks should: strengthen their loan underwriting practices; use more dynamic assessments of prospective borrowers' creditworthiness; design loan agreements for large loans to specifically relate to the business of the borrower; and closely monitor compliance by borrowers with loan agreement covenants. As part of its risk-based supervision, CBL examiners should verify that banks' practices comply with these recommendations."

Reportedly collecting a loan through court proceedings is costly and often has inexplicable results in relation to the applicable law. Thus, the Council should consider ways to eliminate the courts from the adjudication of execution on collateral by banks and licensed MFIs.

Financial Institution Resolution

A law for the efficient resolution of failing financial institutions is a key element of financial crisis prevention and response. Prevention because if the law is properly designed in accordance with recent best practices, shareholders will realize that if their bank is near failure they will lose the value of their investments and management will understand that they will lose their employment and then stronger incentives are created to seek to ensure that their bank does not fail.

Thus, in assessing Liberia's financial crisis preparedness, the Council must consider the adequacy of the Liberian regime for addressing distressed banks in Sections 40 and 55–67 of the New FIA (1999).

Much has been learned in the past twenty years about resolution of financially distressed banks and other financial institutions. This is based on the experience acquired in three waves of bank and other financial institution failures, first, in the early to mid-1990s when some 2,000 failed in Eastern and Central Europe and Central Asia, then in 1997–1998 when some 200 failed in East Asia during the Asian financial crisis, and recently in the 2008–2009 global financial crisis when perhaps 500 institutions failed.[82]

This learning has fairly recently been centralized and documented in the aftermath of the last crisis. Both the Financial Stability Board (FSB), whose predecessor was initiated by the G20 and assisted by the IMF and the World Bank, and the European Union Commission, have issued comprehensive documents containing recommendations for initiating and managing bank and other financial institution resolutions.[83] EU countries will have to conform their laws to new directives to intervene in systemically significant institutions much sooner and provide the resolution authority with new and extraordinary powers to efficiently resolve an institution.

The key legal issues for financial institution resolution are exceedingly complex and relate to four critical areas[84]: (a) the criteria for initiation of a resolution proceeding; (b) the objective of a resolution proceeding; (c) the administration of a resolution proceeding; and (d) resolution powers and legal effects for efficient resolution proceedings.

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[82] Unlike in the first two waves, more recently distressed institutions were not closed and liquidated but many were recapitalized by their governments or merged with other institutions that was facilitated by government or deposit insurance agency financial assistance.

[83] Key Attributes of Effective Resolution Regimes for Financial Institutions (http://www.financialstabilityboard.org/publications/r_111104cc.pdf) published in 2011 and a Proposal for Directives of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms ("EU draft directive"), issued June 6, 2012.

[84] Since there are significant adverse effects on property rights of various stakeholders in financial institution failures that must be prescribed by law, the basic legislation is the key to resolving these situations.

The New FIA (1999) does not seem to contain comprehensive provisions for financial institution resolution in the modern sense. It makes the compulsory liquidation of a bank the decision of a court and a resolution should be an administrative procedure. The law is wanting especially with respect to resolution tools and to resolution powers and legal effects to facilitate resolution proceedings and to provide safeguards to creditors. Thus, the law should be amended to conform to appropriate modern requirements with respect to resolution tools and powers and legal effects.

Institutional Coordination and Management of Financial Crises

The Council should be the focal point for financial crisis preparedness and management to facilitate a rapid response and coordinated action if needed[85, 86]

For response to serious threats to financial stability, the Council members and the deposit insurance agency, if one is established, should prepare a handbook on financial crisis management with contingency plans and during crises or impending crises meet frequently to report on or determine the following:

- The state of preparedness of their institutions for crisis response.
- Coordination of information sharing on immediate financial sector vulnerabilities and on surveillance of financially distressed systemically significant financial institutions.
- Needs for examinations of particular financial institutions or groups or for suspect types of transactions conducted by financial institutions.
- Whether an adverse event has systemic impact such that crisis management should be initiated.
- Responsibilities of each of the Council members and any deposit insurance agency in the event of a crisis.
- A public information strategy and public announcements.

Capacity Building for an Effective Council Secretariat

Once there are at least three staff, there should be structured training perhaps led by a university professor of economics who is knowledgeable about the causes of the global financial crisis and has studied many of the publications that have resulted including those on macroprudential supervision and regulation. The training should include required reading of pronouncements by the Financial Stability Board, the European Union, and the G30 and excerpts from other relevant publications including financial stability reports of other countries. Probably a minimum of fifty hours of instruction over several weeks would be required for academic training; the rest would be on-the-job training.

A study tour for the secretariat staff should be taken to two countries; one, a G7 country that conducts state-of-the-art macroprudential supervisory policy and another country that has more limited resources to devote to the Council secretariat but known to produce a quality financial stability report. A simulation exercise of a financial crisis should also be conducted by the World Bank as part of the training.

The ability of the Council secretariat to perform proper macroprudential analysis of the financial sector depends in large part upon the quality of the data and financial market intelligence that is available to it and the ability of staff in statistical analysis and in understanding the nature and effects of various financial instruments including derivatives. The secretariat will need data and financial market information from the CBL concerning especially systemically significant banks that is not publicly available such as on credit underwriting standards of banks, securities investment portfolio and securities trading portfolio policies of

[85] See Technical Note: Crisis Management, Emergency Lending and Safety Net Issues in the Trinidad and Tobago Financial System, International Monetary Fund, December 2005.

[86] Crisis management related to stability of the financial system is different from business continuity plans in the event of a natural disaster or civil disturbance for which plans should be developed especially for systemically significant institutions.

banks, nonperforming and restructured loans, interest rate and maturity mismatches, currency mismatches, measures of risk such as Value at Risk (VaR) and Loss Given Default (LGD), and use of nontraditional financial instruments.

Projections on the budget outcome from the Ministry of Finance would also be useful.

The Council should establish an agreement among its members to provide information requested by the Council secretariat both on a routine and ad hoc basis. Shared databases among Council institutions for macroprudential analytical purposes should be established. Whether Council members' institutions now receive required information or whether their staffs require training to produce the necessary analysis also must be determined.

Liaison of Council Secretariat with the CBL, MFDP, and IFIs

Rather than attempt to do considerable research and analysis independently, the Council Secretariat should liaise with relevant divisions of departments of the CBL and the MFDP and with IFIs to avoid unnecessary duplication of effort or the use of data and analysis that is inferior to that of others.

The persons with whom the Secretariat liaises in the two Council authorities could be considered coordinators. A formal agreement should be established between the Council Secretariat and the members' of the Council to establish this liaison.

The Secretariat should also liaise with World Bank, IMF and African Development Bank economists and financial sector specialists who analyze the economy and financial sector in Liberia.

The Secretariat should decide what market intelligence, data, and analyses it needs and rely to the extent possible on what has already been produced and synthesize the information for purposes of determining the financial sector risk profile in regard to the sectors and markets that the Secretariat analyzes for monitoring actual and likely risks to financial stability.

Transparency and Accountability of the Council

As for all governmental authorities, the Council should be transparent to an appropriate degree as to its activities and accountable for fulfilment of its responsibilities.

For transparency and accountability of the Council, reports should include comprehensive information, as appropriate, on the Council's activities and results, as follows:

- Actual threats to financial stability detected during the period since the previous report;
- Likely threats to financial stability detected during the previous period;
- Macroprudential policy actions taken by the MFDP and the CBL to prevent or mitigate actual or likely treats to financial stability during the previous period;
- Recommendations made to other authorities to prevent or mitigate actual or likely treats to financial stability during the previous period;
- Results during the previous period of macroprudential actions taken in the past by the authorities represented on the Council;
- Results of recommendations made to other authorities for macroprudential actions to be taken to prevent or mitigate threats to financial stability;
- Results of actions taken by other authorities to prevent or mitigate threats to financial stability.

Inclusion of such information is analogous to Monetary Policy Statements issued by central banks to ensure their transparency and accountability and there are now many models of financial stability reports of central banks or financial stability councils.

Annex 4: Financial Institutions Resolution

Resolution in the legal sense is a fairly recent concept. It is similar to bankruptcy or insolvency legal proceedings in the criteria for initiation, but differs in important respects from conventional bankruptcy in the legal effects and the outcome. This is because resolution relates to only financial institutions and given the importance of financial institutions for economies of all countries, special legal measures apply that would not be appropriate for ordinary industrial or commercial companies.

Financial institution resolution is the situation when, based on actual or expected insolvency or illiquidity of a systemically significant institution, the supervisory authority takes control of its governance and management and seeks to effect an orderly change of control or transfer of some or all of its assets, liabilities and/or functions to other sound institutions. The intended objectives of such actions are to maintain stability in the financial sector by the preservation of financial services, to maximize the value of the assets of the financially distressed institution, to protect the interests of depositors and other creditors and to spare the budget from providing financial support for systemically significant institutions.

Unlike insolvency or bankruptcy laws for ordinary enterprises, the new resolution regimes add the need for systemically important financial institutions to prepare recovery plans and resolution plans that must be approved by supervisors. Recovery plans indicate what an institution would do to remedy a severe threat to its financial condition and resolution plans enable the resolution authority to act quickly and knowledgeably when using resolution tools. These latter plans include the corporate and management structure including subsidiaries and affiliates, which liabilities should be sold first and with what approximate loss of value, who are the institutions counterparties, and what collateral has been given or received for transactions.

Resolution is not supervisory action to remedy violations of the law or regulations with respect to prudential or market conduct matters or corporate governance that is not proximately related to insolvency. The critical distinction is that in resolution an institution will not continue to exist in its former state with respect to ownership, governance, and management. It may be sold to another institution or other public or private sector shareholders as an institution, or its assets and liabilities may be transferred in whole or in part to other institutions or to a bridge institution or to an asset management vehicle. Thus, as a practical matter, its owners, governing body, and senior management will change in whole or in part.

Criteria for Initiation of a Resolution Proceeding

The FSB Key Attributes recommend that the resolution legal regime should be applicable to "any financial institution that could be systemically significant or critical if it fails." Since resolution as advocated by both the FSB and the EU in its directive provides for extraordinary legal powers of the resolution authority and deprivation of property rights of numerous stakeholders, it is appropriate for resolution to apply only in cases of systemic significance. The emphasis in the EU draft directive is on financial stability and saving public funds which necessarily relates to systemically significant institutions. In Liberia it is mainly banks that are systemically significant but the law as amended should apply to a broader range of financial institutions, at least to financial infrastructures, bank holding companies and insurance companies in addition to banks.

FSB Key Attribute 3.1 states:

> "Resolution should be initiated when a firm is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so. The resolution regime should provide for timely and early entry into resolution before a firm is balance-sheet insolvent and before all equity has been fully wiped out. There should be clear standards or suitable indicators of nonviability to help guide decisions on whether firms meet the conditions for entry into resolution."

Under these criteria a resolution would commence after the supervisor intervenes in a systemically significant financial institution because usually only in such event would it be possible for the supervisory authority to determine whether a "firm is no longer viable or likely to be no longer viable, and has no reasonable prospect of becoming so."

Whether viability is possible would depend on whether new or existing shareholders would invest new capital in an institution or whether another institution would acquire the distressed institution. Thus, an intervention known in some countries as conservatorship or special administration would, under the FSB definition, become a resolution if the supervisor determines that there is no reasonable prospect of viability.

Article 32 of EU Directive 2014/59 also provides for "failure" as the condition for initiation of resolution which is much more explicit and centered on insolvency. It provides in relevant part:

> "Conditions for resolution
>
> 1. Member States shall ensure that resolution authorities shall take a resolution action in relation to an institution referred to in point (a) of Article 1(1) only if the resolution authority considers that all of the following conditions are met:
>
> (a) the determination that the institution is failing or is likely to fail has been made…;
>
> (b) having regard to timing and other relevant circumstances, there is no reasonable prospect that any alternative private sector measures…would prevent the failure of the institution within a reasonable timeframe;
>
> (c) resolution action is necessary in the public interest.…
>
> 4. For the purposes of point (a) of paragraph 1, an institution shall be deemed to be failing or likely to fail in one or more of the following circumstances:
>
> (a) the institution infringes or there are objective elements to support a determination that the institution will, in the near future, infringe the requirements for continuing authorisation in a way that would justify the withdrawal of the authorisation by the competent authority including but not limited to because the institution has incurred or is likely to incur losses that will deplete all or a significant amount of its own funds;
>
> (b) the assets of the institution are or there are objective elements to support a determination that the assets of the institution will, in the near future, be less than its liabilities;
>
> (c) the institution is or there are objective elements to support a determination that the institution will, in the near future, be unable to pay its debts or other liabilities as they fall due;…"

Subparagraphs 4(b) and 4(c) are classic bankruptcy law criteria.

Objective of a Resolution Proceeding

The objectives for resolution proceedings and the tools recommended are similar in the FSB Key Attributes and in the EU draft directive. Article 31 of the EU draft directive on "Resolution objectives" is as follows:

> "1. When applying the resolution tools and exercising the resolution powers, resolution authorities shall have regard to the resolution objectives, and choose the tools and powers that best achieve the objectives that are relevant in the circumstances of the case.
>
> The resolution objectives referred to in paragraph 1 provide in part:
>
> 1. When applying the resolution tools and exercising the resolution powers, resolution authorities shall have regard to the resolution objectives, and choose the tools and powers that best achieve the objectives that are relevant in the circumstances of the case.

> 2. The resolution objectives referred to in paragraph 1 are:
>
> (a) to ensure the continuity of critical functions;
>
> (b) to avoid a significant adverse effect on the financial system, in particular by preventing contagion, including to market infrastructures, and by maintaining market discipline;
>
> (c) to protect public funds by minimising reliance on extraordinary public financial support;
>
> (d) to protect public funds by minimising reliance on extraordinary public financial support."

Thus, Article 31 provides for discretion to be exercised by the resolution authorities in their use of tools to effect resolutions. For example, if the main objective is to ensure the continuity of critical functions, the effort might be placed on having an institution's critical functions acquired by another institution that might leave some uninsured depositors unprotected, or on transferring critical functions to a bridge bank which would be capitalized by public funds. If the main objective is to protect insured depositors, the authority might effect a purchase and assumption transaction with assumption of only insured deposits and if no such other transactions were feasible, other depositors and other creditors of the institution in resolution would be paid to the extent of the proceeds received from the more piecemeal liquidation of the assets of the institution.

Articles 24, 40, and 47–55 of the New FIA (1999) relate in part to resolution but without the focus or precision found in modern resolution laws.

Resolution Tools

With respect to resolution tools, Article 37 of the EU directive provides in part:

> "1. Member States shall ensure that resolution authorities have the necessary authority to apply the resolution tools…
>
> 3. The resolution tools are:
>
> (a) the sale of business tool;
>
> (b) the bridge institution tool;
>
> (c) the asset separation tool;
>
> (d) the debt bail-in tool."

The sale of business tool includes sale of an institution to new shareholders or another institution, merger of the institution, or sale of assets and assumption of liabilities of the institution in resolution. The bridge bank tool is establishment of a new bank into which some or all assets and liabilities of the institution in resolution are transferred for a temporary period to maintain critical functions or stabilize the situation for the distressed bank's customers. The asset separation tool is used by transferring certain assets of the institution in resolution to an asset management entity, sometimes called a "bad bank" to dispose of assets that are not readily saleable to other institutions. The debt write-down tool is reducing liabilities of an institution to reflect the loss of value in its assets and/or conversion of some liabilities to equity to capitalize the institution in resolution.

Section 40 of the New FIA (1999) contains provisions that usually relate to insolvency but the provisional administrator may be appointed for many other matters, including failure to produce required reports or records or "violating any relevant law or regulation." The dire consequences that result from provisional administration should only result from actual or imminent institutional failure, based on the important legal principle of proportionality.

Sections 47–54 are somewhat duplicative with Section 40, as if two sections of different bank insolvency laws were transplanted to the New FIA. None of the provisions regarding distressed banks contain the explicit resolution tools of a bridge bank or debt write-down. There is a reference in Section 50 to a compulsory reorganization whose meaning is not clear and one of whose conditions is not realistic.

Resolution Legal Effects

Thus, the New FIA should be amended to be more explicit and add certain provisions on legal effects of resolution as described below, or, preferably, a new law on financial institutions should be enacted. Such a law is lengthy and would be the largest section of an amended FIA.[87]

The FSB's Key Attributes advocate and also embodied in the EU directive are powers of the resolution authority and legal effects to facilitate efficient resolution proceedings.[88] These are rather extraordinary even in comparison with substantive and procedural law for commercial insolvency or bankruptcy proceedings and no area of commercial law adversely affects property rights of various stakeholders as much as insolvency or bankruptcy law. Thus, the perceived need for extraordinary actions to preserve or restore financial stability when there are failures of systemically significant financial institutions has motivated the new proposals for legal frameworks for efficient resolution.

Transfer of Assets and Liabilities

This is another area in which the New FIA should be more explicit. To facilitate resolution, authorities should have the power to transfer selected assets and/or liabilities of the failed institution to a third-party institution, a newly established bridge institution, or an asset management entity. Any such transfer of assets or liabilities should not require the consent of any affected party or creditor to be valid; or constitute a default or termination event in relation to any obligation relating to such assets or liabilities or under any contract to which the failed institution is a party.

Financing contracts often provide, sometimes as an event of default, that if one party becomes subject to an insolvency-type proceeding or makes an arrangement with creditors, the obligation of that party is accelerated or terminated to protect the non-defaulting party. Depositors in a bank or holders of a bank's debt obligations understand that they have a claim on that bank and may resist the transfer of their claim to another institution. The transfer of assets powers for resolution overcome any such rights or expectations.

Setoff, Netting, Collateralization

The legal framework governing setoff rights, contractual netting and collateralization agreements should be enforceable during a financial crisis or resolution of firms, and should not hamper the effective implementation of resolution measures. Subject to adequate safeguards, entry into resolution and the exercise of any resolution powers should not trigger statutory or contractual setoff rights, or constitute an event that entitles any counterparty of the firm in resolution to exercise contractual acceleration or early termination rights provided the substantive obligations under the contract continue to be performed.

Should contractual acceleration or early termination rights nevertheless be exercisable, the resolution authority should have the discretionary power to stay temporarily such rights where they arise by reason only of the resolution proceeding. The stay should be limited to a short time period so as not to prolong uncertainty as to property rights; protect the integrity of financial contracts and provide certainty to counterparties; and not affect the exercise of early termination rights of a counterparty against the institution in resolution in the case of any default not related to the resolution proceeding.

[87] There is also a concern in some countries that once a law is open to amendment, unwelcome changes from the viewpoint of the supervisors are added.

[88] Much of the discussion in this section is adapted from the FSB's Key Attributes of Effective Resolution Regimes for Financial Institutions.

Creditor Safeguards

Since, especially for a systemically important financial institution, its resolution may be exceedingly complex when involving transfers of assets and liabilities and termination of financial and other contracts, the law should provide for compensation to creditors who are unduly affected by the entry of an institution into resolution. This is not a guaranty of payment of their claims against an institution but only of fair treatment in relation to their pre-resolution rights. For example, in bail-in of creditors, there may be involuntary rescheduling of payments on debt instruments or involuntary reduction in interest rates on debt. As another example, some subordinated creditors may receive guaranties for their claims to maintain Tier 2 capital while more senior creditors' claims are written off. In such cases the creditors whose rights are impaired should be entitled to compensation to the extent that they would have had claims with some or more value if the resolution powers had not been employed that affect their creditors' rights.

The EU directive on financial institution resolution specifies in Article 44(2) that debt write-down may not be applied to certain liabilities:

> "2. Resolution authorities shall not exercise the write-down or conversion powers in relation to the following liabilities…
>
> (a) covered deposits…;
>
> (b) secured liabilities…;
>
> (c) any liability that arises by virtue of the holding by the institution…of client assets or client money…;
>
> (d) any liability that arises by virtue of a fiduciary relationship…;
>
> (g) (ii) a liability to…a commercial or trade creditor arising from the provision to the institution…of goods or services that are critical to the daily functioning of its operations, including IT services, utilities and the rental, servicing and upkeep of premises;…"

The resolution powers should generally be exercised in a way that respects the hierarchy of claims and equal treatment of creditors of the same class while allowing for flexibility to depart from these rules to contain the potential systemic impact of an institution's failure or to maximize value of assets or of the franchise for the benefit of creditors as a whole

In general, creditors should have a right to compensation where they do not receive at a minimum what they would have received in a liquidation of the firm under the applicable insolvency regime ("no creditor worse off than in liquidation" principle). Thus, the New FIA (1999) should be amended or replaced for resolution to include these provisions.

Annex 5: Financial Sector Regulatory Governance

> *Ensuring the quality of regulation is a permanent and essential role of government…and institutional capacities should be designed around a clear view of the appropriate use of regulation in society.*[89]

Financial Sector Regulatory Governance

Now that financial sector regulatory authorities in developing and emerging market countries generally have developed basic regulatory and supervisory capabilities along the lines of standards issued for the sector by the Basle Committee on Banking Supervision, the IAIS, and the International Organization of Securities Commissions (IOSCO), it is appropriate to refine the quality of their regulation under the theme of regulatory governance.

Proper regulatory governance promotes transparency, responsiveness to the regulated sectors and the public, accountability of regulators, and efficient and smart regulation. At its most basic, regulatory governance requires that a regulatory authority have the legal authority to fulfill its mandate—adequate powers to itself issue obligatory rules for regulated entities and to enforce those rules, rather than rely on a ministry or courts in the first instance.[90] Poor-quality regulations generate a range of broader social, environmental and equity costs, such as ineffective enforcement and providing incentives for corruption.[91]

Unlike for financial sector supervision or corporate governance or where there are well established international best practice standards like the 'Basel Core Principles for Effective Banking Supervision' and the IOSCO 'Objectives and Principles of Securities Regulation,' there is no recognized standard for regulatory governance. However certain standards with other principal objectives advocate or include elements of good regulatory governance.

For example, Principle 1 of the 'Basel Core Principles' encourages "transparent processes, sound governance and adequate resources" without prescribing any specific elements for such purposes while Part II of the International Monetary Fund's 'Code of Good Practices on Transparency in Monetary and Financial Policies' in respect of Open Process for Formulating and Reporting Monetary Policy Decisions provides for certain elements of transparency and accountability.[92]

The OECD issued a 'Recommendation of the Council on Regulatory Policy and Governance' in 2012 that is for government-wide regulation including recommendations for 'ex ante' and 'ex post' cost-benefits analyses rather than defining pragmatic procedures for regulatory governance.[93]

The International Finance Corporation published in 2010 *Regulatory Governance in Developing Countries*.[94] It is concerned mainly with regulatory governance from a macroeconomic perspective, similar to the OECD Recommendation optic. The IFC publication describes the parameters of the terrain, and acknowledges the lack of a clear universal meaning of regulatory governance[95]:

> "The study of regulation is not new, and is rooted in economic, political science, legal, and public management disciplines going back a century or more. Theories of regulation have

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[89] Tools and Approaches to Review Existing Regulations, The World Bank Group, 2010, p.39.
[90] See IOSCO Objectives and Principles of Securities Regulation (www.iosco.org/library/pubdocs/pdf/IOSCOPD154.pdf), Principle A 3 and the Basle Committee's Core Principles for Effective Banking Supervision (www.bis.org/publ/bcbs129.htm) Principle 1.
[91] Tools and Approaches, op cit, p. 2.
[92] www.imf.org/external/np/mae/mft/code/index.htm
[93] www.oecd.org/dataoecd/45/55/49990817.pdf
5www.worldbank.org/external/default/WDSContentServer/WDSP/IB/2010/07/13/000334955_20100713050729/Rendered/PDF/556450WP0Box0349461B0GovReg01PUBLIC1.pdf
[95] Regulatory Governance in Developing Countries, p.4.

merged in different ways in the practice of regulatory reform. As a result, the concept of regulatory reform has assumed several meanings over the last 30 years.

> Most students of regulatory reform find that academics, donors, international organizations, and reformers use the basic "terms of the trade" in different ways without clear definitions. Sometimes it seems that those writing about regulatory reform are unaware that other definitions exist. This lack of precision masks important differences in the goals, design, and results of different varieties of regulatory reform."

The IFC publication defines regulatory governance as "a holistic term that refers to the systematic implementation and of government-wide policies on how to use regulation to produce quality regulation…" Regulatory quality includes efficiency, transparency, accountability, and flexibility. The general nature of the recommendations of the IFC publication does not seem especially relevant to the financial sector where stakeholders' savings are at risk. Two conclusions of the Chapter on Regulatory Governance and Economic Impacts are that "government regulations that impose direct business costs often reduce economic performance…" and "the negative effects of high regulatory costs, risks, and entry barriers seem particularly relevant to developing countries…" Financial institutions appropriately bear regulatory costs and entry barriers given the special nature of their liabilities.[96]

It would therefore appear to be valuable to establish principles and practices for regulatory governance of financial sector regulatory authorities with a more definite and pragmatic approach geared toward financial services than is currently found in the literature.

Administrative Law

In some countries regulatory governance with respect to transparency of regulatory authorities' actions, responsiveness of public sector regulatory authorities to the private sector, and accountability of authorities is embodied in law known as administrative law.[97] Countries in several regions have these types of administrative laws, some enacted fairly recently, which vary in their specific content. These include Western European countries as well as Japan, the United States, Brazil, Mexico and Argentina. Some fifty developing countries have adopted freedom of information laws that is one element of regulatory governance.

Some Latin American laws emphasize general principles applicable to administrative agency actions—impartiality, objectivity and efficiency, for example. Some laws are concerned more with procedures for administrative operations rather than transparency and responsiveness of government for regulations in general. Others are devoted substantially to appeals against governmental actions. Rather comprehensive laws are found in Mexico (2000), the Netherlands (1994), the State of Sao Paulo, Brazil (1998) and the United States (1974).

Key Issues in Regulatory Governance

The experience with administrative law especially in developing countries and the elements of regulatory governance within administrative law raise several issues:

- Constitutional democracy—ministries and regulatory agencies have improperly legislated, in effect, when legislatures have not provided proper standards for regulation. There should be a fundamental distinction between the legislature delegating power to executive agencies to, in effect, make law that is inappropriate, and delegating power to regulatory authorities to execute the law in accordance with legislative standards contained in the law.

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[96] Financial institutions are the repositories of savings of the public and banks are the medium of the payments systems which are the principal reasons for comprehensive regulation and supervision of the financial sector.

[97] Administrative law must be distinguished from administrative violation codes that socialist economies had and some former socialist economies still have that control conduct with political implications like publishing and political rallies and whose violation results in penalties less than those provided by the ordinary criminal law.

- Even when there are adequate standards, regulatory authorities have often exceeded their authority, but there have been inadequate mechanisms for accountability because there have not been proper rules on how regulations are to be implemented, inadequate transparency concerning actual regulations and regulatory actions, and absence of effective avenues for redress against regulatory abuse.
- In comparison with the vast amount of legal technical assistance and training in commercial law, financial law, and judicial reform that has been undertaken in the past twenty years by international financial institutions and NGOs, very little has been done in regulatory governance and that makes all the work in commercial and financial law and judicial reform much less useful than it could be.
- In designing a proper regulatory governance regime, there are the issues of how can regulatory authorities be made effective yet act lawfully; how can abuse of discretion be controlled; and how can regulators be effective in enforcement in the absence of competent, honest, and efficient courts that is a widespread phenomenon in developing countries. Regulatory authorities independent of political influence in the executive branch of government are desirable, yet how can they be kept honest?

All of these issues are relevant to financial sector regulatory authorities and given the importance of the financial sector for the economy of all countries, good regulation of financial institutions assumes even greater significance than regulation of some other sectors.

Basic Elements of Good Financial Sector Regulatory Governance

The Composition of Regulatory Authorities' Governing Bodies

A commission, board or other regulatory agency governing body should have representation in the majority by qualified persons external to the authority and who are independent from regulated entities and the officials of the authority in relation to family relationship or financial interest. This would promote a proper objective perspective by the governing body and give confidence to the public of the legitimacy of the regulatory authority. There should also be certain committees of the governing body with specific responsibilities to promote efficient governance.

Meetings of Government Agencies: Agenda, Public observation, and Published Minutes

Financial regulatory authorities should publish notices containing the agendas of the meetings of its governing body. This is valuable information for regulated entities including for financial services trade associations, so financial services firms can plan accordingly. The public could be allowed to observe (but not participate in) the meetings. However, some portions of meetings would not be open to public observation that relate to non-public commercial or financial information of financial institutions; personal information about individuals; and current or prospective enforcement actions. Agencies should provide on their website a transcript or video recording of the proceedings and summary written minutes to allow the public to know what transpired. The practices of many central banks is illustrative of good communications concerning actions taken at meetings of the monetary policy decision-making body.

Advisory Councils

Financial regulatory authorities should establish advisory councils consisting of representatives of the sectors that they regulate—banking, insurance, capital markets, for example. The councils would meet every three or four months with senior regulators to discuss the regulatory activities of the agency and new legislative or regulatory initiatives in their sectors. Such councils would provide an opportunity for financial regulatory authorities to learn of needs and concerns of the private sector and the private sector could gain insight into regulatory policies and practices that should lead to smarter regulation and better compliance.

Public Access to Information

Financial regulatory authorities should publish a description of their organization, procedures by which their functions are implemented, descriptions and purposes of their forms, regulations of general applicability, and how the public may obtain information from or make submissions to the regulatory agency. This would make regulatory authorities more accessible and responsive to the public and to regulated entities and therefor more effective. It would also decrease the scope for corruption where there have not been transparent rules of procedure and officials devise rules on a case-by-case basis. There should be a rule that if regulations are not published, a person or institution would not be required to comply with it.

Financial regulatory authorities should make available for public inspection and copying its records and documents including its regulations and guidelines and regulatory decisions in the adjudication of cases. Financial regulatory authorities should be required to reply to such information requests in a short timeframe and if the request is denied, explain the reasons. Some information would not be subject to disclosure, essentially the same subject matter that is exempt from open meetings—non-public commercial or financial information of financial institutions; personal information about individuals; and current or prospective enforcement actions.

Notice of Proposed Laws and Regulations and Opportunity for Comments

Financial regulatory authorities should publish a notice of their intention to propose a new law (for government or parliamentary action), or new regulations or amendments to regulations, the purposes of such proposals, a description of the issues involved, and the proposed text. Interested persons should be invited to submit written comments and certain proposals could require a public hearing. The financial regulatory authorities should be required to publicly acknowledge the comments received and explain why those recommendations that are rejected have not been accepted. Thus, the regulatory authority is not required to accept comments on proposals but if not it should explain the reasons. This, in effect, dialogue between the regulated private sector and the regulator should result in better designed and understood regulations.

Requirements for Issuance of Regulatory Decisions

To seek to ensure that financial regulatory authorities' actions are fair and transparent, rules that regulatory approvals should contain criteria for determinations, and decisions of agencies should be in writing accompanied by an opinion on each material issue of fact and law or regulation, containing findings and conclusions. Such requirements would enhance the quality of decisions and tend to discourage decisions based on other than objective reasons. Many banking laws and regulations, for example, contain requirements for prior approvals by the banking regulator for licensing and certain corporate actions by regulated entities without indicating criteria for decisions.

Principles for Regulatory Oversight That Focus on Matters of Significance

Financial regulatory authorities should have supervisory policies and procedures that focus on material matters including those of systemic significance for the financial sector and that require a risk-based focus to supervision rather than box ticking. Such policies and procedures would enable the authority to deploy limited regulatory resources more effectively and should avoid an excessive regulatory burden for the financial services affected.

Standards for Enforcement Actions

Financial regulatory authorities should employ consistency in choice of enforcement actions and focus on materiality—the sanction should fit the violation, in application of the legal principle of proportionality, and remedial actions should be preferred to fines. Regulated entities should be given credit for self-reporting of violations; for example, by deferred prosecution.

Codes of Ethics for Regulatory Authorities' Officials and Staff

Codes of ethics or conduct would promote objectivity, fairness and honesty in regulatory authorities' actions. The codes would include such matters as management of conflicts of interest to mitigate potentially adverse consequences of related-party matters, confidentiality of information obtained by virtue of service to the regulatory authority, fair dealing with regulated entities, a requirement for regulatory authorities' officials and staff to report illegal or unethical conduct by other officials and staff and protection of those making reports in good faith, and ways in which the code would be enforced.

Administrative Review of Agency Actions

Financial regulatory authorities' decisions should be appealed before the agency itself as a prior condition to appeal to a court of law. This is meant to resolve disputes more quickly at the agency level when possible before persons who usually have more expertise in complex regulatory and financial matters than the courts.

Judicial Review

Rules for appellate review by the courts should provide that the sole questions before a court in determining whether a financial regulatory authority acted unlawfully in taking an action are whether it did not have the legal authority, did not comply with established procedures, or the decision was not supported by substantial evidence. This provides deference to the decision of the regulatory authority that is usually to be preferred in a developing country because of limited expertise in financial regulatory matters and financial transactions in the courts.

Implementation of Good Financial Institution Regulatory Governance

Except for the "Composition of Regulatory Authorities' Governing Body" outlined above and rules for administrative and judicial review described in the subsections "Administrative Review of Agency Actions" and "Judicial Review," respectively, the regulatory authority itself could take the initiative to improve its regulatory governance and would not be dependent upon a change in law to adopt and implement the reforms advocated in this paper.

Evaluation of Impact of Regulations

In proposing to issue new regulations, the regulatory authority would be expected to consider the impact on the industry and on regulators and if proper priorities for regulatory activity are observed, the proposals should have an appropriate regulatory impact. If an ex ante assessment is deficient, feedback from the industry on the proposals should inform the regulatory authority of unforeseen effects.

In addition, a comprehensive system of regulatory governance should include quantitative and qualitative regulatory impact analysis with regard to costs and benefits before issuance of proposed regulations. However, such analysis is complex and may require skills that are not readily obtained in some countries. Similarly, systemic monitoring and evaluation of the effect of new regulations and the stock of regulations is advantageous but again requires specialized technical capacities and might best be considered in a second stage of regulatory governance reform. The twelve elements of good financial sector regulatory governance described above are largely procedural in nature and relatively easy to apply. If these elements are implemented, the effects should necessarily be beneficial and complex impact analysis may be of secondary importance.

Table 12: How Elements of Good Regulatory Governance Contribute to Accountability, Responsiveness to the Private Sector, Transparency, Efficiency, and Smart Regulation

Element	Accountability	Responsiveness	Transparency	Efficiency	Smart Reg.
The composition and duties of regulatory authority governing bodies	√		√	√	√
Meetings of regulatory agencies—public observation; published minutes	√		√		
Advisory councils		√	√	√	√
Public access to information		√	√		
Notice of proposed regulations; opportunity for comments	√	√	√	√	√
Requirements for issuance of regulatory decisions	√		√	√	
Principles for regulatory oversight that focus on matters of significance				√	√
Standards for enforcement actions	√		√	√	√
Codes of ethics for regulatory authorities' officials and staff	√		√		
Administrative review of agency actions				√	√
Judicial review	√			√	

Annex 6: Pension Schemes Contributions and Benefits

The benefits of the NPS are calculated in an unconventional manner. An employee who has contributed to the scheme for less than 100 months (8 years and 4 months) is entitled to a lump sum payment of his or her contributions and accrued interest only (current 3.5 percent nominal). The employer contributions are not vested in the employee at any stage and the employer contributions for an employee with less than 100 months are retained in NPS. The rationale for this action is that the retention of the employer contribution pays the expenses for administering the contributor's account. The employee is paid the amount as a lump sum and there are no provisions for either annuitization of the amount or receipt of the amount by way of phased withdrawal.

The mandatory retirement age is 65 although contributors are entitled to retire at 60 if they have enough contributory years. The Law requires that an employee with 100 months of contributions will receive a minimum pension of 25 percent of the reference wage. The pension entitlement increases by 1 percent for each 10-month period until it reaches a maximum pension of 40 percent of the reference wage after 180 months of contributions. The reference wage is the average of the last five years' wages of the retiree unvalorized.[98] The ceiling on the maximum pension is the minimum pension benefit recommended by the International Labor Organization from a defined benefit scheme. The level of benefits has not been altered since the commencement of the scheme in 1975.

Importantly, NPS provides survivor benefits—the widow or widower receives a pension of 50 percent of the entitlement of the worker or pensioner as the case may be. If there are dependent children aged less than 21 and at school or less than 18 and not at school, the dependent children receive 30 percent of the entitlement. The survivor benefits are payable irrespective of whether the deceased person was in the workforce or had retired at the date of his or her decease. The eligibility requirements for the payment of a survivor benefit where the person was in the workforce at the time of his or her death are that the deceased had to have made contributions for at least 50 months in the last 60 months before death. This is particularly relevant for the discussion of CSA later in this note. Pension benefits are not indexed.

NASSCORP commissioned a review by Alexander Forbes, Actuarial Consultants from South Africa earlier this year. The consultants estimated that the cash outflows for benefits and expenses would exceed cash inflows from contributions and earnings in 2017 and the scheme will have depleted its own reserves in 2019. This was predicated on the assumption that the assets representing the reserves are available and that the book value is in fact the realizable value. The investments of NASSCORP are heavily weighted towards commercial real estate, which NASSCORP has developed itself. An independent valuation of the developments by valuers with experience in the valuation of commercial developments

The Government of Liberia guarantees the payment of benefits; an estimation of the accrued to date liabilities[99] would be useful. NASSCORP informed the mission that the current data is not sufficiently reliable to calculate either the net accrued to date liabilities of the government or the open system

[98] Valorization is the process of revaluing earnings used in pension benefit calculations by pre-determined factors (such as wage growth or inflation) to adjust for changes in prices, wage levels or economic growth. For example a benefit based on life time earnings valorized to wage growth means that the base for the calculation of a pension benefit is the average of each year's earnings which are adjusted to the wage growth that has occurred between the year of earnings and the point of calculation of the benefit.

[99] Accrued to date liabilities are a measure of the obligations that a scheme has accrued to its existing members the date on which it is calculated. It is calculated as the present value of the future benefits that a scheme is liable to pay to both pensioners and contributors of the scheme accrued to that point. This is equivalent to a scheme being closed to new members and not receiving further contributions from existing members. Existing pensioners continue to receive pensions and existing active members receive benefits accrued at the date of closure upon retirement. The net accrued to date liabilities are the accrued to date liabilities minus accumulated assets.

liabilities[100] of the government into the future. The quality of data is an issue not only with NPS but also with CSA with significant loss of member records during the protracted Civil War that ended in 2003. NASSCORP is working to recreate as many member records as possible.

Alexander Forbes recommended an increase in the contribution rate from 6 percent to 13 percent to mitigate the impending cash issues. Discussions with NASSCORP suggested that it intended to ask the Government to amend the regulations, which would increase the total contribution rate to 10 percent rather than 13 percent as recommended. The rationale for the lower contribution rate is not known.

The investment strategy of the scheme is heavily concentrated in real estate with approximately 80 percent of the funds under management in this asset class. The rationale for this is the lack of alternative investment opportunities in Liberia and an internal policy, which prohibits investments abroad. NASSCORP is considering a leverage strategy where it will borrow against the real estate in the portfolio to improve its yield. Such a strategy is not appropriate for a pension fund because of the increase in risk and also begs the question as to how the additional funds are to be invested, given the lack of domestic opportunities and the reluctance to look at overseas markets.

The cost to income ratio of the scheme is approximately 30 percent. Internationally, the average for a defined benefit scheme is about 5 percent. The excessive costs have been attributed to the cost of running an investment portfolio that is dominated by real estate, where NASSCORP is on occasion acting as a landlord for commercial properties and sometimes as property developer.

There are several issues that need to be addressed in the near future:

- The rationale for the decision not to raise the contribution rate to the level recommended by the actuarial advice and the impact of the lower contribution rate on the financial position of NPS needs to be clarified.
- How the assets of NPS were valued by the actuaries in making their assessment of its financial position needs to be explain.
- The lack of indexation of benefits means that the real value of pensions is severely eroded over time.
- The maximum benefit of 40 percent is barely sufficient by international standards.
- The reference wage is not valorized meaning that the reference wage for the calculation of final benefits can be significantly adversely affected in periods of high wage growth.
- The failure to pay the employer contributions to retirees with less than 100 months of contributions is inequitable.
- The data on which to base standard actuarial work is not complete which means the Government cannot estimate its liabilities to NPS or the cost of not reforming the scheme.
- The investment portfolio of the scheme is not properly diversified.
- The strategy to leverage the scheme is not appropriate and is high risk.
- The increase in contributions proposed by NASSCORP seems insufficient to ensure that the scheme is solvent into the future.
- The costs of administering the scheme are excessive by international standards.
- The failure of the Government to remit the employer contributions to NPS regularly and punctually needs to be remedied.

[100] Open system liabilities show how the liabilities of a scheme will change into the future if the scheme continues to enroll new members.

Arrangements for Government Employees and Quasi-government Employees

The arrangements for these employees are not pension schemes in the true sense of the word. They are benefit provisions in a number of discrete Acts or parts of Acts. The Acts and parts of large Acts cover the following:

- Former Chief Justices and former Associate Justices of the Supreme Court.
- Former Presidents of the Senate, Speakers and deputy Speakers of the House of Representatives.
- Members of the National Legislature.
- President and Vice President.
- Foreign Service Officers.
- Special Security Services.
- National Police.
- Armed Forces.
- Civil Servants and other Government Employees.

The structure of the benefits for each of these classes of employees is similar with the exception of Foreign Service Officers, whose benefits were determined in 1973 to be in the range of US$1,500 to US$2,500 per annum depending on positions and do not seem to have been changed since they were originally determined.

The external consultant has recommended that all these arrangements be merged into one under the umbrella of the Government Services Pension Scheme. To affect this, amendments will be required to the Acts that provide for these benefits. The only exception to the merger is for members of the Armed Forces; it is customary to provide for the Armed Forces through a separate arrangement with generally more generous benefits to compensate for the increased risk in this kind of employment.

To date, all these arrangements appear to be on a defined benefit basis, are noncontributory and benefits are funded out of the current Government budget.

It is understood that there has been no comprehensive actuarial review of the costs of all these schemes so the Government is not aware of its accrued to date liabilities in relation to them.

The benefits are calculated based on years of service:[101]

- 25 years of service renders a benefit of 33⅓ percent of the reference wage.
- 30 years of service renders a benefit of 50 percent of the reference wage.
- 40 years of service renders a benefit of 60 percent of the reference wage.

The reference wage for the calculation is the final salary of the retiree.

The Civil Service Retirement Scheme (CSR)

The CSR is the main arrangement for government employees. It is an unfunded noncontributory arrangement. Benefits are linked to years of service with a minimum of 25 years of service required to obtain a pension of 33⅓ percent of final salary and a practical maximum of 60 percent after 40 years of service.

[101] Op cit page 9

There are several flaws in the design of the arrangement, most of which are detrimental to the members and one of which is to the members' benefit.

Survivors' benefits are restricted to the dependents of a deceased who died while in retirement. If a pensioner dies his or her widow or widower respectively is entitled to a pension of 50 percent of the pensioner's original pension. If the deceased has dependent children and the widow or widower is not entitled to a pension, the dependent children receive 50 percent of the pensioner's original pension. If the widow or widower is eligible to receive the pension (that is because the deceased person was a pensioner at the time of his or her death), the dependent children are not entitled to a pension. If the widow or widower is not eligible (for example if he or she remarries), the dependent children are entitled to a pension that in aggregate cannot exceed 50 percent of the pension of the deceased person. The pension payable by CSR is in addition to the pension payable by NPS meaning that a dependent of a person who dies when retired can receive up to 100 percent of the pension of the deceased.

However, if a member dies in service, his or her dependents are not eligible for any pension from CSR and must rely on the smaller pension from NPS. The dependent of a person who died while in service is a maximum of 50 percent of the deceased person's pension.

The situation with regard to disability pensions is, by contrast with the survivor's benefit, equitable between members of CSR and the rest of the formal work force. CSR does not pay any disability pensions and any person injured at work is entitled to a pension from NPS regardless of which arrangement he or she is a member.

The calculation of the reference wage is problematic. The reference wage used is the substantive salary of the member having reference to his or her position and grade. Government employees are remunerated with a combination of the substantive wage, allowances and gratuities which are confidential to the employee and which routinely increase the substantive wage significantly. Basing the reference wage on the substantive wage only results in a retiree receiving a much lower benefit than appears compared with what he or she was receiving before retirement. An ad hoc adjustment was made to the pensions of existing retirees in 2011, but this appears to have been a one-off initiative and there is no assurance that future pensions will be indexed.

Pension benefits are not indexed and therefore the real value of pensions is eroded over time.

The quality of records is an issue with CSR as it is with NPS. The CSA Division of Records, Research and Biometrics is working on the issue but this appears to be a long-term project. The lack of reliable records is particularly significant for CSR because benefits are based on years of continuous service and it has been impossible to establish the continuity of service of some employees during the Civil War. Furthermore, it is unjust to penalize those employees who were forced to break their service because of the conditions that prevailed during the Civil War.

The external consultant raised the matter of over compensation to long-term employees. A retiree who has forty years of service with the Government is entitled to a pension benefit of 60 percent of final salary. The retiree is also entitled to the maximum pension from NPS, which is 40 percent of his or her last five years salaries unvalorized. If these numbers were additive, the combined replacement rate for a person with forty years of service would be 100 percent which is well above the maximum in most developed countries of between 65 percent and 70 percent. As the definition of the reference wage in the two schemes are different, it is not possible to comment on the adequacy of pensions other than to note that the maximum replacement rate will be significantly lower than 100 percent.

The Current Position

The reform of the civil service arrangements received in principle approval from the Cabinet on August 8, 2012. A copy of the final proposal was not provided and the following is based on discussions with the

CSA. It is understood that the new arrangement will be contributory with the members contributing 3 percent of salaries.

The mandatory retirement age will be retained at 65 with the option of retiring early if the member has accumulated sufficient contributory years. The benefits will be graduated according to the length of service with a maximum of 45 percent. Benefits must be taken in the form of a pension, there are no commutation rights and the pensions will not be indexed.

There is no information whether the range of benefits will be extended to cover invalidity and survivorship for the dependents of members who die before retirement.

The scheme will be administered by NASSCORP. There has been no consideration as yet to the investment strategy but there are indications that NASSCORP will act as the investment manager.

It is not clear whether the scheme is intended to be co-contributory with the Government paying its contributions up front. The use of the accumulated funds in the new scheme is far from clear. The external consultant made a curious recommendation in his report.[102] He noted that “Although the proposed new scheme is contributory, the scheme is not intended to be funded. Contributions will not be accumulated beyond a prudent reserve of about three months of pension payouts. Hence, there would be no investment function beyond ensuring that any reserve funds received interest at the going rate. Contributions will be used to finance benefit enhancements, most notably pension increases during retirement.” It appears that under this recommendation, the pool of funds would be used to index existing pensions and the government would continue to pay the basic pension on behalf of the scheme. This brings to mind some intergenerational issues with current contributors’ funds being used to improve the benefits of existing retirees.

However, if the intention is that the funds of the scheme accumulated and are used to pay pensions rather than just the increment from indexation, there are questions about the adequacy of the contributions. While no forecasts have been made available, intuitively it seems that the scheme will be out of balance, based on the observation that a contribution rate of 6 percent is materially inadequate to fund the benefits of the members of NPS it should be inadequate for the purposes of the new scheme given that the benefits are comparable.

Other Schemes

Contributions to NPS are mandatory and there is no provision for either employers or employees to opt out of the arrangement. Notwithstanding, there is anecdotal evidence that other schemes exist on a voluntary basis. Discussions with ICA revealed that it acts as agent for one unidentified occupational scheme and three provident funds. There were also indications of other defined benefit occupational schemes that are in operation mainly for employees of international companies operating in Liberia. There are no local laws covering the operations of these schemes and provident funds and no supervision function.

[102] Op cit page 20

Annex 7: Technical Note on Legal and Regulatory Framework for the Financial Sector in Liberia

General Overview

Summary Outline of the Legal System

The legal system in Liberia is a mixed legal system of common law (based on Anglo-American law) and customary law. The Constitution is the supreme law of the Republic of Liberia. According to Article 2 of the Constitution, all laws and decisions by the state institutions must be in strict conformity with the Constitution. According to Article 91 of the Constitution, the initiative to amend the Constitution may come from either two-thirds of the membership of both the Senate and House of Representatives or a petition submitted for approval to the Legislature by not fewer than 10,000 (ten thousand) citizens.

Liberia has had two Constitutions. The first was the 1847 Constitution which was suspended on April 12, 1980, following the *coup d'état* which overthrew the presidency of H. E. William R. Tolbert, Jr. On July 3, 1984, the 1984 Constitution was submitted to a national referendum and approved. Article 35 of the Constitution outlines the process for the passage of Bills in the Legislature. Specifically, Article 29 states that both houses must pass on all legislation. The broad power of the executive, who has the constitutional authority to appoint government officials at almost all levels, limits the development of an effective system of checks and balances. To address this constraint, in 2012 a Constitution Review Committee was established.[103] Article 66 of the Constitution states that the Supreme Court shall be the final arbiter of constitutional issues. This means the court has the power to determine the ultimate Constitutionality of Legislation.

The primary sources of law are statutes and regulations made pursuant to these statutes and common law including court decisions.[104] Article 2 of the Constitution recognizes customary law. Therefore, customs are a recognized source of law in Liberia. According to the Constitution, statutory laws and common law of the formal legal system govern all Liberians, whereas the old Rules and Regulation Governing the Hinterland refer to the adjudication of cases for "civilized people" and "natives." According to Article 65 of the Constitution, the courts are empowered to apply statutory law as well as customary law in accordance with the standards enacted by the Legislature. The Rules and Regulations Governing Local Government officials of the Political Sub-Divisions of Liberia (Revised Edition 2000) provide a procedural framework for the adjudication of customary law cases.

Overview of the Judiciary System

Liberia's judicial power is vested in a Supreme Court and subordinate courts similar in structure to those of the U.S. All courts are empowered to apply both statutory and customary laws recognized by the Judiciary Law of 1972.[105] Traditional and lay courts exist in the rural areas of Liberia.

The formal legal system, based on Anglo-American Common Law, is shadowed by, and frequently conflicts with, local customary law based on unwritten, indigenous practices, culture, and traditions. These competing and un-reconciled legal systems lead to frequent conflicts between Monrovia-based entities and those in rural communities. The judicial system suffers from inadequately trained and poorly compensated judges and other judicial officers, often leading to faulty proceedings and corruption. Obtaining hearing dates may take a long time because of inadequate resources and backlogs of cases.

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[103] A separate initiative was also launched by a group comprising all major political parties and civil society groups known as the Political Consultative Forum whose stated objective is to advance broad-based consultation in the constitutional review process.

[104] Case law can serve as a source of law or it can help to interpret the law. According to Article 66 of the Constitution, judgments of the Supreme Court are final and binding and shall not be subject to appeal or review by any other branch of government.

[105] The Law governing the traditional court system is included in the Revised Rules and Regulation Governing the Hinterland of Liberia of 2000.

The dysfunctional court system has led the GOL to explore the use of alternative dispute resolution (ADR) mechanisms to resolve land disputes. Historically, land disputes arose because statutory and traditional methods of allocating land were never reconciled. During and after the civil war, unscrupulous individuals falsified land deeds and sold properties to multiple buyers, compounding an already contentious situation. In 2010, a Land Commission was mandated to establish land use policy and clarify land ownership issues. The Land Commission has adopted best practices of ADR mediations from other post-conflict countries that have experienced land disputes.

As part of Liberia's judicial reform agenda, the national legislature enacted a new Commercial Code and established a Commercial Court in 2011. In theory, the court presides over all financial, contracts, and commercial disputes. In practice, because of a dearth of legislation, some cases remain unresolved. For example, the Law Reform Commission and relevant stakeholders are drafting a bankruptcy law to protect creditors' rights so that bankruptcy cases can be adjudicated.

Contract Enforcement and Insolvency Law

Liberia has enacted a Secured Transaction Law as part of a new Commercial Code (2010). It establishes a web-based registration system, together with a PPSA[106] type notice filing system. The Secured Transaction Law is chapter 5 of the Commercial Code. The Liberia Collateral Registry was launched in June 2014 with the support of the IFC.

The lack of appropriate mechanisms for recovery and enforcement impedes intermediation and access to finance. Enforcement upon default, and against uncooperative debtors, is crucial to creating the predictability in recovery. While the collateral registry will register security interests at the time of creation, if the loan defaults, enforcement against an uncooperative debtor needs to be done through the courts.

The current insolvency provisions in the Liberian Commercial Code (carried over from the prior law) are outdated and ineffectual. There are 18 articles and approximately 3 pages in total, and they are sparse and do not include basic insolvency provisions such as priority among creditors, moratorium on actions by creditors, qualifications of receivers/administrators, or procedures for disposal of assets and payment to creditors. They have not been used, most likely because they are insufficient to direct an insolvency proceeding. The insolvency framework under the Commercial Code is therefore outdated and needs urgent modernization. In addition, alternative dispute resolution, whether out of court or court annexed, is not available except at the new Commercial Court.

The Commercial Court in Liberia was created by a special Law in 2010, but it only started operations in the second **half of 2011.** The Commercial Court is the venue for insolvency and a substantial portion of debt cases. The Commercial Court has jurisdiction over insolvency matters and other commercial matters over US$15,000[107]. The mission is not able to determine if the Commercial Court is effective. However, according to an assessment made by an IFC mission in 2012, the Commercial Court caseload was 11 cases by March 2012. June 2012, the Commercial Court increased the caseload to 23 cases, amounting to total amount of US$10,203,246.00. Five of those cases have already been resolved through ADR within 90 days. Pursuant to the Commercial Court Act, only new commercial cases could be filed before the Commercial Court. Pending cases before the civil courts and debt courts should remain there. The civil courts and debt courts have concurrent jurisdiction with the Commercial Court and parties have a choice where to file, pending the full operationalization of the Commercial Court. The current Debt Courts caseload, based on reports provided, is approximately 100–150 cases per year. The annual caseload of civil courts is 2,232 cases on average, based on reports of the Supreme Court of Liberia for 2011 and 2012.

[106] Personal Property Security Act.
[107] LRD 1,000,000.

The lack of a modern and effectual insolvency regime in Liberia that is aimed at preserving value in businesses and business assets means the following:

- There are inadequate mechanisms to prevent the stripping of assets of companies in financial difficulty heading towards insolvency.
- Directors lack accountability.
- The insolvency profession is neither institutionalized nor regulated.
- ADR methods are underdeveloped.

Hence, a modern insolvency legal framework has to be developed. The skills of stakeholders including the judiciary and insolvency practitioners need to be strengthened so that value in distressed companies can be preserved through rehabilitation or efficient liquidation.

Financial Sector Regulation

Legal and Regulatory Framework for Financial Sector

The CBL is empowered to regulate banks and other financial institutions under the Central Bank Act of 1999 and the Financial Institutions Act of 1999.The key relevant statutes which govern the financial sector are as follows:

- Central Bank of Liberia 1999 (CBA and as amended);
- Financial Institutions Act, 1999 (FIA);
- Insurance Act 2014;
- The Money Laundering and Financing of Terrorism (Prevention) Act, 2012 (AML).

The draft Securities Markets Act appears to be still pending legislative approvals.

Institutional Issue: CBL Independence, Governance and Mandate on Financial Stability

The governance and transparency framework and independence of the central bank under the CBA appear to be in line with international best practices. Section 4 states that the CBL shall have functional independence and authority to carry out the full range of functions and powers conferred on it. Sections 12 and 13 of CBA that deal with appointment and removal of Governors and Board members are in line with international standards on independence of regulators[108] with a clear set of criteria provided in the law. The disclosure and conflict management framework under Section 18 of CBA for Governor and Board members seems adequate. The CBL also has the power to issue regulations for the administration of the CBA and FIA. Section 54 of CBL states that the CBL in carrying out its tasks shall enjoy autonomous regulatory powers.

There is no explicit provision in CBA and FIA of the objective of the CBL to maintain financial stability. The FIA and the CBA confer power on the CBL to establish methodologies for supervising financial institutions that will ensure stability in the financial sector. In this regard, the CBL has authority to grant and revoke financial institution's license, ensure that financial institutions are conducting their business operations in accordance with the prudential regulations and other applicable laws. Hence it can be implied that CBL supervisors have adequate power, at least theoretically, to ensure a stable financial system. Nonetheless, it would be more in line with modern supervisory practice for a specific financial stability objective of the CBL to be articulated in the CBA.

[108] There were discussions in the Senate in 2012 to subject the 5-year term appointment of the Governor and board members to confirmation by the Senate by way of amendment to the CBA but this proposal does not appear to have been proceeded with at the time of the mission in August 2014.

There appears no legal protection given to the CBL as supervisor of the financial sector against civil proceedings brought against the CBA and its employees in the course of their work if they act with good faith. Legal protection also does not appear to be available in the form of providing financial support to employees including the reimbursement of legal cost incurred by employees in defending an action against bona fide supervisory action. Consequently, supervisory effectiveness of the CBL as the financial sector supervisor may be hampered by insufficient legal protection.

Improving Legal and Regulatory Framework: Banking Sector

For the banking sector, apart from the FIA and CBA, there are a number of prudential regulations and guidelines which cover important matters such as minimum liquid assets, lending limits, etc. including the following:

- Regulations for Minimum Capital Requirements for Bank-Financial Institution 2008;
- Prudential Regulations Concerning Large Exposures and Credits 2011;
- Regulations Concerning Asset Classification, Provision for Loan Losses and Suspension of Interest on NPLs and Advances, 2014;
- Regulations for Liquidity Requirements 2013;
    - Regulations Concerning Corporate Governance of Financial Institutions 2008;
    - Credit Reference Bureau Regulations 2010;
- Regulations for Related-Party Transactions which defines insiders, requires Board approval of all insider loans which exceed 5 percent of unimpaired capital and reserves, and places an absolute cap of 30 percent of the "net worth" of a bank;
- Mobile Money Regulations 2014;
- Regulations for Deposit Taking Microfinance Institutions 2012;
- Guidelines for Supervisory Intervention 2009;
- Guidelines for Management of Foreign Exchange Risk Exposure and Placements Abroad by Commercial 2012.

While the FIA provides a sound legislative basis for the supervision of the banking sector, there are a number of gaps in the legal and regulatory framework which need to be addressed. As a first step, it is recommended that a detailed assessment of compliance with the Basle Core Principles for Effective Banking Supervision be undertaken to identify all of the areas where compliance needs to be strengthened.

Various definitions of similar terms in the CBA and FIA are phrased differently thereby creating confusion and legal uncertainty. These definitions relate to terms such as "banking business," "commercial bank," "bank financial institution," "nonbank financial institution," "credit institution," and "nonbank financial service." These definitions in CBA and FIA are given in annex 1 and the inconsistency in them is discussed below:

(a) **"Banking business" definition** is provided in both FIA and CBA and even though substantively they are similar, the phraseology is different as highlighted in yellow in annex1.
(b) **Definition of "commercial bank"** is not tied closely with definition of "banking business." Hence, it is possible for an entity to meet the test of carrying on "banking business" as defined in both FIA and CBA and yet not qualified to be a "commercial bank" if it does not provide checking facilities. In addition, one wonders of the utility of the definition of "bank-financial institution" (which is somewhat different from the definition of "commercial bank") when for all intents and purposes the term "bank-financial institution seems to refer to a commercial bank.

(c) **Definition of “nonbank financial services”** in FIA seems to cover more activities than the definition of the same term in the CBA. This includes credit cards and operations of building societies and stating that money remittances does not include acceptance of deposits on demand or for fixed term.
(d) **Definition of “credit institution”** in both FIA and CBA are substantively similar (with minor difference in phrasing) but may be confused with “nonbank financial institution.”
(e) **Definition of “related person” to an individual** appears deficient as it only includes personal relatives or vaguely “business interest.”
(f) **There is no definition of “financial institution”** as a generic term even though this term is used extensively in CBA and FIA to describe bank-financial institutions and nonbank financial institutions. It would be useful to introduce such a definition to provide legal certainty.
(g) **Definitions of “net worth”** provided in the FIA and Regulations Concerning Large Exposures and Credit Limits though substantively similar use different words as shown in annex 1.

The terms, conditions, and procedures for applying for a license as a financial institution are spelt out in the FIA. The Act specifically prohibits local and foreign financial institutions from conducting banking business in Liberia without a license granted by the CBL. Applicants must submit an application, accompanied by documentation, names and particulars of the managerial resources. A foreign bank must provide evidence that it is subject to comprehensive supervision on a consolidated basis by the home supervisor, who must provide written consent for the establishment of the Liberian affiliate. The CBL is authorized to conduct whatever investigations it deems necessary on the history and financial status of the applicant, the character and experience of its managers, its capital adequacy, etc. The FIA creates criminal liability for all damages sustained by financial institutions on directors, CEOs, managers or other officers of financial institutions who knowingly violate any laws or regulations in the course of their duties. The CBL has the authority to impose additional conditions on the licensee, including designating places where business may be conducted, and prescribing or restricting activities that may be carried out. No person other than a licensed financial institution may use the word “bank” or any of its derivatives in the name or description of the business.

Gaps in licensing: While the CBL has in practice followed a very restrictive policy as regards the licensing of new banks, there are a few gaps in the CBL’s licensing requirements which should be remedied, notably:

- **Information on shareholders**: There are some general requirements regarding information on the applicant for a bank license (and the CBL has the authority to require whatever information it deems necessary); there is some question as to the extent of the requirement to assess the ability of shareholders to provide future financial support in case of need, or to provide a letter of comfort or guarantee for such future support.
- **Fit and Proper Criteria**: There is a general provision that the CBL may investigate the character and experience of the future bank’s managers, but there are no stipulated fit and proper criteria established by law or regulation for shareholders, directors, or senior management of an entity seeking a license under the FIA. Directors of financial institutions and chief executive officers are required to be approved by the CBL under Section 74 and obliged to vacate their office should they be declared bankrupt, convicted of fraud, or who have been a director or manager of a financial institution that has been wound up under Section 71 of FIA. In this regard, a similar criteria can be adopted for assessment of fit and properness of directors and managers of an applicant financial institution.
- **Section 4(1) of FIA appears to deal with the transition of licenses granted under the 1974 FIA are deemed to be provisional licenses for 6 months during which those license holders would presumably be seeking a new license under the 1999 FIA**. If this is the correct interpretation, then one would assume the transitional period is way over and this comment would not be relevant. However, if it is not the case, it is not clear then why a different class of provisional licenses is contemplated and as to how a provisional license is converted into a “regular license.”

The FIA and the Regulations Concerning Large Exposures and Credit Limits specify limitations on risk concentrations and exposures. Licensed banks shall ensure that the aggregate of the large exposures shall not exceed fifty (50) percent of the bank's total credit extensions. However, in the area of determining large exposures and credit limits, there appears a conflict between what is provided in Section 20 of the FIA and the Prudential Regulations Concerning Large Exposures and Credit Limits 2011. The FIA provides that large exposures are defined in reference to 15 percent of the aggregate net worth of a financial institution as follows:

> **"Section 20 of FIA: Credit and Other Restrictions**
>
> 1. The total liabilities of any borrowing individual, partnership, corporation or any other form of business organization to any bank-financial institution resulting from one or more extensions of credit by that depository institution shall at no time exceed fifteen percent (15%) of the net worth of the institution. The amount of the purchase of equity securities of a borrower by the financial institution in question shall be deemed an extension of credit.
> 2. No financial institution, shall, directly or indirectly, except with the approval of the Central Bank on such terms and conditions as the Central Bank may prescribe:
>
>   (a) grant to any person any advances or credit facilities or make any guarantee so that the total value of the advances, credit facilities or guarantees in respect of such a person is at any time more than fifteen percent (15%) of the aggregate amount of the financial institution's unimpaired net worth: Provided, however that the limitation imposed herein shall not apply to transactions pertaining to the following:
>
>   i. discounts or payments of drafts secured by readily marketable goods in transit in which the depositor institution retains a security interest in and control over the goods;
>
>   ii. loans secured by readily marketable goods remaining under the control of the depository institution and in which the depository institution retains a security interest;
>
>   iii. loans secured by deposits in the depository institution with a value of at least one hundred and twenty-five (125%) percent of the loan;
>
>   iv. repurchase agreements covering readily marketable government securities; and
>
>   v. government-guaranteed securities."

However, Paragraph 3(10) of the Regulations provides that the aggregate exposure is 20 percent of aggregate net worth of a bank, as follows:

> **"Paragraph 3 (10) of Regulations: Large Exposure or Single Borrower Limit**
>
> In accordance with the provisions of Section 20 (2) of FIA, except with the approval of the Central Bank of Liberia (CBL) on such terms and conditions as the CBL may prescribe, no bank shall directly or indirectly grant to any person any advances or credit facilities or make guarantees so that the total value of the advances, credit facilities or guarantees or any other off-balance sheet commitment in respect of such a person is at any time more than twenty percent (20%) of the aggregate amount of the bank's net worth. The amount of the purchase of equity securities of a borrower by the bank in question shall be deemed to be an extension of credit."

There appears therefore a conflict in the determination of large exposure limits under the FIA and the Regulations. In the absence of a definition of "financial institution" (which presumably includes both bank-financial institution and nonbank financial institution), one is led to interpret that Section 20 of the FIA should prevail and there appears no power conferred on the CBL to vary the exposure limit of 15 percent of aggregate net worth of the financial institution, yet the Regulations that applies to licensed banks has raised the amount to 20 percent. Furthermore, Section 20(2)(a) of the FIA introduces the concept of "aggregate amount of the financial institutions' unimpaired net worth" when such a term is undefined and differs from the one that is used in paragraph (1) as well as in the definition of "net worth" in the FIA. Such loose usage of terms can create a high level of legal uncertainty and pose serious compliance problems by banks and efforts should be applied to rationalize them.

Supervisory Powers, Resources, and Capacity

The FIA authorizes the CBL to conduct regular on-site examinations of the operations of a licensed financial institution to determine if i) it is in a sound financial condition; ii) the provisions of the FIA are being complied with; and iii) its business is being operated in a prudent and sound manner. Financial institutions must produce all books, minutes, accounts, documents, etc. reasonably required by the examiners. Bank examiners are subject to confidentiality of information gained through their work. However, the CBL may publish or disclose information gathered under the FIA, provided that it might not publish information pertaining to an individual financial institution or customer without consent of the concerned party.

However, there appears no authority conferred on the CBL to share information with international regulators considering a number of foreign banks are operating in Liberia. It would also not be consistent with the licensing provision under Section 4 (5) (c) of FIA where an application from a foreign bank must be supported by a statement to the satisfaction of the CBL of the adequacy of consolidated supervision of solvency and liquidity of the branches and subsidiaries of the foreign bank. This would assume some level of mutual cooperation between the host and home supervisors and without an explicit authorization under the FIA or CBA, and in view of the confidentiality obligations of the CBL under Section 35 of FIA, this may hamper the CBL's ability to foster strong supervision by the home regulator of the foreign bank.

Section 22 of the FIA which mandates the CBL to carry out an on-site examination at least once a year may also pose difficulties in the CBL applying a risk-based supervisory approach in that it may apply a differentiated period for purposes of on-site examination. Section 23 gives examiners the right to have access to all the records and papers of FIs but does not impose specific obligation on staff to cooperate with examiners even though Section 23(2) of FIA creates a criminal offence against the defaulting institution or affiliate for failure to produce information or if false information is produced and directors and management of a financial institution fail to take reasonable steps to ensure compliance with provisions of FIA.

The CBL has a wide number of remedial enforcement measures at its disposal under the FIA and Guidelines for Supervisory Actions 2009 (which applies to banks). For example, if the CBL finds that the financial institution or any of its directors, officers, employees, or shareholders has engaged in unsound practices or violated provisions of the FIA or regulations to which it is subject. These include the following:

(a) Require the external auditor appointed by the financial institution to undertake a special audit covering the unlawful act or irregularity.

(b) Appoint a person who training and experience to advise the financial institution on the steps to be taken to rectify the matter.

(c) Conclude a written agreement for a program of remedial actions, including remedial measures of suspension and dismissal of the institution's officers and directors and limitation of operations of the financial institution.

(d) Submit a semiannual report in writing to the Central Bank on the following:

    (i) Increase or decrease or otherwise of its registered capital;

    (ii) Any loss on and of its adjusted capital or cessation of its payments;

    (iii) Any change in ownership and structure.

(e) Issue a cease and desist order.
(f) Revoke license of a financial institution or close its operations.
(g) Dismiss or cause to be dismissed, directors, officers and employees of financial institutions.
(h) Appoint provisional administrators or take control of a financial institution.
(i) Seize and take possession of a troubled financial institution.
(j) Regulate voluntary liquidations.

However, the CBL does not appear to have power to impose administrative penalties under the FIA against a financial institution. It is common that administrative penalties are imposed by the supervisor for minor infractions such as lodging reports after the specified time rather than invoking criminal penalties. Such provisions are found in the new Insurance Law 2014 and a similar approach can be adopted in the FIA when there is an opportunity to amend it.

The CBL has comprehensive resolution authority to designate problem bank under the FIA and the Guidelines of Supervisory Actions 2009. Explicit powers are given to the CBL to take prompt and corrective action according to different thresholds for capital adequacy, liquidity, asset quality, earnings and weak internal controls and management, decide on resolution method and appoint a provisional administrator**.** The resolution framework envisaged under FIA and Guidelines for Supervisory Actions 2009 appears to provide the CBL with a broad range of resolution tools for banks even though these provisions are not conveniently arranged to make easy reference. In addition, Section 13 (1) (a) of FIA permits the CBL to 'close down' an institution if it does not have a license. It is not clear what this term means.

It is not clear what is intended by Section 20(7) of the FIA in conferring the role on the CBL to be "intermediary for debt provisioning and rescheduling."

"Section 20 (7) FIA: Debt Provisioning and Rescheduling

(a) Indebtedness of and to, and owing by or to, a financial institution in the course of its business may be renegotiated to grant permissive delay of repayment for reasons of existing general debt repayment and servicing difficulties.

(b) **The Central Bank shall perform the role of intermediary and may, for supervisory purposes, set out, by regulations, a framework within which appropriate levels of risk exposure may be assessed**. The stages of the process for deciding appropriate levels of provisioning may include:

   (i) identification of debtors with current or potential repayment difficulties;

   (ii) identification of the nature of those difficulties, and extent to which they affect the debtor;

   (iii) determination of the proportion of the exposure that is unlikely to be paid in full:

   (iv) consideration of factors which may:

      1. evidence a borrower's inability to meet his obligation at the due date, due to extraneous circumstances;

      2. evidence a borrower's current difficulties in meeting his obligations;

      3. evidence the likelihood of persistence in repayment."

It would seem that the CBL in being able to interpose itself between the borrower and the licensed financial institution in the forbearance of debt repayment or renegotiate debt repayment may be in conflict with its supervisory responsibilities under the FIA. Clarification should be provided under what circumstances and what explicit criteria would the CBL apply in invoking this provision as part of its supervisory responsibilities.

Under Section 64 of FIA, saving and other deposits in a bank are given preference after liquidators' costs, wages to employees of failed bank 3 months before liquidation, taxes and fees and assessments attributable to the CBL. Yet, under Section 34, the CBL to establish a deposit insurance scheme and to make regulations in that respect. At this juncture, it would appear there are no definite plans to introduce such a scheme. However, should a deposit scheme be introduced, it would be necessary to review this "blanket" deposit protection as no limits are imposed under Section 64 of the amount of deposits that enjoy the preference over other claims against the financial institution.

Corporate Governance

The FIA and Regulations Concerning Governance of Financial Institutions 2008 contain basic corporate governance requirements. The minimum size of a Board shall be five members and the maximum shall not exceed 16 members and a majority of them must reside in Liberia to constitute quorum. The CEO must be a member of the Board, but cannot be Chairman. The Chairman shall not be a member of committees set up by the Board. At least two nonexecutive Board members must be independent Directors (who do not represent any particular shareholder's interest and hold no special business interest with the Bank) appointed by the bank on merit. No two members of the same extended family should occupy the position of Chairman and Chief Executive Officer or Executive Director of a bank at the same time. Several committees such as Audit Committee, Credit Committee and Asset and Management Committee must be set up and operate against principles provided in the Regulations. Transactions with directors, shareholders or officers are subject to approval (recorded in minutes) of a majority of independent directors or prior approval by the CBL, and must be on an arms-length basis.

Market Conduct

There are few provisions related to market conduct in the FIA, and the CBL does not explicitly granted authority to regulate and oversee market conduct of regulated entities, except in the following areas:

- Anticompetitive agreements are barred, and those engaging in such activity are subject to specified fines and/or imprisonment; and
- The CBL may regulate interest rates, fees and commissions, and may prescribe disclosure requirements related to interest and fees.

Section 39 (2) of FIA provides that the CBL may set minimum deposit balance requirements, establish limits for all fee and service charges and otherwise govern and regulate activities and relationship between financial institutions, their customers, creditors and debtors.

Nonetheless, the CBL issued a "Directive on the Introduction of Financial Products and Services for Commercial Bank" in 2009 to regulate and supervise "nontraditional banking financial products and services" by banks. "Nontraditional banking product and services" refer to those products and services not included in the definition of "banking" under Section 2 (1) of the FIA. Such a definition provides little legal certainty of the intent of the law especially in view of the onerous requirement that is imposed in requiring any bank that wishes to introduce any financial products or services to obtain the prior written approval of the CBL. The bank is required to submit to the CBL whole range of documents including customer guidelines including underlying agreements and cost and price structure of products and services.

The Directive as described above falls short of a comprehensive and effective financial consumer protection regime. Mechanisms such as complaints handling systems at the intermediary and CBL levels, alternative dispute resolution mechanisms as well as industry code of conduct together with advocacy mechanisms are missing. This is an area of weakness and the financial consumer protection framework and regulation of market conduct needs to be strengthened in the FIA and related regulations.

Accounting and Auditing Standards

The CBL regulates financial reporting of bank and nonbank financial institutions. It requires bank and nonbank financial institutions to prepare financial statements in conformity with its prudential guidelines. It prescribes formats for financial statements, including disclosure requirements that bank and nonbank financial institutions must follow. Due to lack of capacity, the CBL Department of Banking Supervision focuses more on compliance with prudential requirements. By focusing on enforcing mostly prudential requirements, the Central Bank appears to neglect other important regulatory activities such as ensuring that the general purpose financial statements of banks are in compliance with international accounting standards.[109]

With respect to prudential reporting by these institutions, the Department of Banking Supervision examines financial statements, approves the appointment of statutory auditors, and reviews communications between banks and their statutory auditors as appropriate. It may further convene a meeting with a bank's auditors to clear areas of disagreement with prudential guidelines before the bank publishes its financial statements. While this establishes a regular compliance review process, the Central Bank focuses more on prudential reporting than on general purpose financial reporting. Consequently, misstatements and errors in general purpose financial statements may remain undetected or not known to the public unless prudential considerations warrant it. Furthermore, even though the Central Bank adopted IFRS for its own financial reporting in 2008, it lacks the necessary technical capacity to ensure IFRS compliance by commercial banks for which IFRS has been prescribed for adoption in December 2012. As a result, there is the risk that serious regulatory compliance gaps with IFRS may not be detected by regulators.

Alternate Delivery Channels

The Mobile Money Regulations adopted in May 2014 has provided clarity on alternate delivery channels for services of financial institutions. These regulations appear comprehensive and in line with international best practices and cover alternate delivery channels, such as mobile phones or agents, to allow expansion of coverage and promote greater financial inclusion.

Insurance Sector

The new Insurance Law of 2013 was passed into law, replacing the 1973 Act and several new regulations, aimed at further strengthening the sector, including the new capital requirements which were also developed to be issued and published early 2015. The new Insurance Law gives both regulatory and supervisory powers to the CBL over all persons involve in general or life insurance business, or business as an insurance broker, agent or loss adjuster and set up a system for the licensing of insurers, insurance brokers, insurance agents and loss adjuster. Unlike the FIA, the Insurance law incorporates modern principles and standards of market and business conduct.

In general, the new Insurance law is comprehensive, logical, and well-constructed and is consistent with most of the requirements of the Insurance Core Principles of the IAIS. It is noted that the details covering prudential requirements, licensing and other matters are to be contained in Regulations to be made as part of the project and that the Insurance Law is to be framework law which is what is accepted as international best practices.

Nonetheless, the new Insurance Law does not appear to address the sharing of information either within the country or with other international regulators (as is the case in the FIA). Perhaps a preferred approach would be for the CBA can be amended to allow the CBL to share information with international regulators for all institutions that are under its supervisory purview.

[109] ROSC for Accounting and Auditing, the World Bank 2011.

There is uncertainty as to which law would be applicable in the event of insolvency of an insurer. In regard to the resolution of an insolvent insurer, one would assume that the FIA relevant provisions would apply to it along with the general Insolvency law. The relevant provisions of FIA relating to resolution regime apply to a "financial institution" which is not a defined term. This is complicated by the existence of a definition of "a licensed financial institution" which means a licensed bank; yet there are also definitions of "bank-financial institution and nonbank financial institution." Where there is conflict or ambiguity in interpretation of the law, the common law principle is for the more specific law namely the general Insolvency law to be applicable. This would not be desirable unless the authority and mandate of the CBL as resolution authority are stated clearly in the general Insolvency Law. Many jurisdictions elect to incorporate separate chapters in the sectoral law (as is the case under the FIA) to ensure there is no legal challenge or conflict to ensure expeditious and effective resolution. One approach could be just clarify in the FIA on the scope of coverage of these resolution powers of the CBL that they apply unequivocally to also all other intermediaries under its supervisory purview including insurers.

Effective implementation of the new Insurance Law should be a priority. The World Bank's Accounting and Auditing ROSC team noted in 2012 the serious lack of expertise and technical capacity in the supervision of insurance industry especially in regard to financial reporting by insurance intermediaries. Consequently, this seriously limits the Commission's capacity to verify whether or not the provisions relating to insurance contracts are correctly calculated, one of the most sensitive aspects of accounting by insurance companies.

Payment System

A new Payment System Act, aiming to cover the necessary provisions to support a modern payment system, was submitted to the national legislature for passage into law in 2012. The Act will provide the legal framework for oversight and regulation of the National Payments System in Liberia. The said Act has been enacted by the national legislative body and is awaiting presidential approval and publication to enter into force. The development of the physical infrastructure is still being worked on and completion date is set for February, 2014. The CBL, in partnership with the WAMI, is to implement series of reforms to modernize the payment system in the country in line with international standards. According to the report, the key components of the modernization include RTGS, Scripless Securities Settlement System (SSS, Automated Check Processing (ACP) and Automatic Clearing House (ACH) system. The goal is to upgrade the country's financial infrastructure to the level of other countries, like Ghana and Nigeria, in preparation for the launch of a single currency in the sub-region, said the report quoted by the Liberia News Agency.

Capital Markets

A draft Securities Law has been prepared for the CBL along with a Capital Market Development Strategy funded by FIRST and under the World Bank's supervision. The draft Securities Law appears to be in line with IOSCO Principles of Securities Regulation. In the meantime, the relevant provisions of FIA would apply to capital market services and intermediaries to the extent they operate in Liberia as they would fall within the definition of "nonbank financial institution." Be that as it may, there is to date no effective capital market or options for portfolio investment. The Liberian market offers the private sector few credit instruments. Private companies do not issue debt in part because there is no government benchmark, and in part because there is a perceived lack of appetite for such investment instruments. Proper development of a capital market requires appropriate legal and accounting infrastructure, necessary regulatory and institutional structures, and human resource capacity.

Crucial to capital market development is acceptable financial reporting quality which in turn requires a robust regulatory regime and effective enforcement mechanisms that would provide incentives for high-quality financial reports. The lack of qualified accountants has contributed to the low quality of financial reports. Based on the findings of the 2012 ROSC report in Accounting and Auditing Standards, the quality of audited financial statements is a concern to investors and other users of financial statements. The financial statements of companies are not readily available attributable to the perception that they are confidential. With the exception of banks and insurance companies, other public interest entities were reluctant to share copies of financial statements with the World Bank's ROSC team. There is a general perception among owners and top management of companies that the information in financial statements is confidential and should not be shared with anyone outside the company.

Other Relevant Laws

The Association Law of 1976 which applies to all banks, insurance companies and other nonbank financial institutions is outdated. The Association Law was obsolete even in 1976 when it lacked essential elements that are commonly found in a Companies' Law. Overall, it does not include the fundamental requirement to present audited financial statements to shareholders annually. It does not have any mandatory requirement for companies to prepare and submit annual audited financial statements to the Business Registry. The Association Law is seriously inadequate with regard to defining the framework for corporate financial reporting and does not reflect current realities in Liberia and international standards. It does not stipulate any legal sanctions for not preparing financial statements. As a result, most companies, especially SMEs, do not generally feel obligated to prepare financial statements. Some companies prepare financial statements only when it is required by regulators or needed to obtain an operating license or a loan from the bank. While it is somewhat easy to bring minority lawsuits, there are few and relatively weak laws pertaining to board disclosures and next-to-no liability laws constraining board and director actions. When investing in a Liberian company, therefore, the rule of the game is buyer beware.

Hence, it would be urgent to replace the Association Law of 1976 with a modern company's code that would address the following:

- Provide legal backing for accounting and auditing standards, specifying which entities should prepare financial statements and with which standards, and which entities should be audited.
- Empower the Business Registry to enforce applicable rules and requirements, including those relating to accounting and auditing.
- Include SMEs in the financial reporting arrangement in Liberia. Most businesses in the country are small or medium size, operating under the umbrella of the Liberian Business Association.
- Make mandatory the submission of audited financial statements of all public interest entities.
- Define auditors' duties and responsibilities in line with modern business environment and challenges.
- Specify who is qualified to be an auditor.
- Outline the auditors' liabilities and termination procedure.
- Grant more authority to regulators such as the Liberian Institute of Certified Public Accountants (LICPA), the CBL, and the Insurance Bureau for imposing appropriate administrative sanctions.

The CBL, in strengthening the legal and institutional environment to ensure that it remains safe and sound, continued to pursue policies and work in concert with relevant stakeholders, both local and international, to address issues of fraud, default on loans, illicit transactions, among other things. The CBL, along with other relevant entities of Government, worked to ensure the amendment of the Civil Procedures Law, intended to provide provisional remedies on proceeds of crime; amendment of the Penal Law regarding extortion, environmental crimes and illicit trafficking of human beings and migrant smuggling; enactment of the Fraud Act: mail fraud and fraud by wire, radio, television or other electronic communication; Anti-Money Laundering and Terrorist Financing Act and subsequent establishment of the FIU of Liberia; Legal Mutual Assistance in Criminal Matters Act; and An Act to Establish Procedures for the Distribution of United Nations List of Terrorists and Terrorist Group; and the validation of several national policies.

In addition, legislation has been passed by Parliament such as the Investment Law of 2010 and an Act establishing the Commercial Court with the aim of improving the investment climate and ensuring greater security for commercial transactions.

Anti-Money Laundering/Countering Finance of Terrorism (AML/CFT)

In 2012, Liberia repealed its AML/CFT law by replacing it with a package of laws[110] and amendments to existing laws[111] aimed at meeting international AML/CFT obligations. This series of laws provided an improved legal framework to establishment of a financial intelligence unit, criminalize terrorist financing, money laundering and other predicate crimes, and establish the legal basis to freeze assets of designated terrorists, as well as provide and request mutual legal assistance in ML/TF cases. Despite this extensive legislative effort, some important deficiencies in the AML/CFT legal framework remain because during the process of adopting these laws, some critically important provisions (AML/CFT preventive measures) that were contained in the draft laws were removed.

As the AML/CFT preventive measures serve as the most critical foundations of an effective AML/CFT system, the AML/CFT legal framework of Liberia remains seriously deficient and the preventive measures provisions need urgently to be restored by amending relevant laws. This is not only important to meet international AML/CFT obligations,[112] but also to ensure reliable links to foreign correspondent banks in view of the increasing threats and risks of money laundering and related financial crimes, including corruption and terrorism/terrorist financing in West Africa, and more specifically in countries facing serious challenges with regard to resources and institutional capacity to support effective systems of regulatory governance. Additionally, lack of progress in implementing international AML/CFT obligations can be met with official countermeasures imposed by countries with financial links to Liberia as well as blacklisting by international AML/CFT standard setting bodies.

In an effort to help Liberia avoid such countermeasures, the Bank experts in the Financial Market Integrity Unit (GFMDR) have been supporting efforts of Liberian officials to undertake progress in strengthening the legal framework for the national AML/CFT system. As a result, since 2012, Liberia has made progress in implementing some provisions of the new AML/CFT framework, including. These efforts, summarized below, have been hampered by the recent Ebola crisis:

- **The LFIU** was set up in 2013, staffed with strong leadership and is working with advisory and technical support from the World Bank (GFMDR/FMI unit) and other donors to (a) build FIU operational capacity; (b) further amend and implement AML/CFT laws and regulations; (c) coordinate AML/CFT compliance monitoring of reporting entities under FIU supervision; and (d) establish effective systems for interagency cooperation.
- **The CBL** has been working with support of the World Bank experts (GFMDR/FMI unit) in designing and implementing an effective AML/CFT Inspection System to implement AML/CFT preventive measures among entities under CBL supervision (financial institutions and insurance companies).
- **National AML/CFT Risk Assessment (NRA):** Liberia has formally requested assistance[113] of the World Bank and the ECOWAS Inter-Governmental Action Committee Against Money Laundering

[110] Anti-Money Laundering and Terrorist Financing Act of 2012; Financial Intelligence Unit Act of 2012; Fraud Act of 2012; Mutual Legal Assistance in Criminal Matters Act of 2012; and United Nations List of Terrorists and Terrorist Groups Act of 2012.
[111] Act to Amend Civil Procedure Law to provide provisional remedies for proceeds of crime; and Act to Amend Penal Law on extortion, environmental crime and illicit trafficking.
[112] A formal assessment of effectiveness in Liberia meeting international AML/CFT obligations is scheduled to be conducted by GIABA in Oct 2020.
[113] Dated January 30, 2014.

(GIABA) to provide technical assistance to Liberia to undertake a National AML/CFT Risk Assessment using the World Bank NRA Tool. [114]

The FIU aims to achieve the following activities by June 30, 2016:

(a) Draft, circulate for review and submit for adoption critically needed amendments to existing AML/CFT Laws to remedy legal framework deficiencies and ensure adequate legal basis to implement international AML/CFT obligations

(b) Draft and adopt the following AML/CFT implementing regulations:

   (i) Regulation on Cross Border Transportation of Currencies and Bearer Negotiable Instruments (currently pending Ministry of Justice review).

   (ii) Regulation on Suspicious Transaction Reporting (STR) and Currency Transaction Reporting (CTR) for AML/CFT reporting entities which will transfer responsibility for receiving/analyzing STRs and CTRs from the CBL to the FIU.

   (iii) Regulation to implement procedures for Distribution of UN List of Terrorists and Terrorist Groups.

   (iv) Regulation on Politically Exposed Persons (PEPs) to be harmonized with Asset Disclosure provisions of the Code of Conduct Law and Asset Disclosure implementing regulations.

   (v) AML/CFT Regulations for Designated Non-Financial Professions and Businesses (DNFPBs): These regulations will be tailored for each of the following subsectors:

   - Casinos
   - Real estate agents
   - Dealers in previous metals and stones
   - Lawyers, notaries, accountants and other independent legal professionals
   - Trust and company service providers

(c) Develop AML/CFT Inspection Manual for Designated Non-Financial Businesses and Professions (DNFPBs).

(d) Initiate preparations to undertake a National AML/CFT Risk Assessment utilizing the World Bank NRA Tool by:

- securing funding commitment from GIABA;
- identifying 8 NRA Working Group Leaders and Deputy Leaders;
- identifying requisite members for each of 8 NRA Working Groups; and
- coordinating dates with WBG and GIABA for delivery of (1) pre-NRA Preparatory Meeting and (2) Introductory (3 day) NRA Workshop.

The CBL aims to achieve the following by June 30, 2016:

(a) Adopt and commence implementation of new AML/CFT Inspection Procedures for banks

(b) Adopt and commence implementation of new AML/CFT Inspection Procedures for insurance entities.

[114] International AML/CFT standards were revised in 2013 to require all countries to conduct a National AML/CFT Risk Assessment to ensure the AML/CFT systems are more effectively designed based on the actual ML/TF risks a country faces, and to ensure that scarce resources can be allocated to the more serious risks.