

Help Needed for the 'Unbanked'

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A foreign worker in New York needs to send \$200 to relatives in his home country. Instead of visiting a bank, he goes to a small office and makes his request to a man sitting at a simple desk with a fax machine and a note pad. Hours later the money is in the hands of his family on the other side of the world.

The worker used what financial regulators call an alternative remittance system. These informal money transfer operations are known by different names around the world: *hawala* in much of the Islamic world, *fei ch'ien* in Hong Kong, *padala* in the Philippines, *hundi* in India, *phoei kwan* in Thailand and the black market peso exchange in Latin America.

They all have one thing in common: They request little information from users. After the money is transferred, minimal records of the transaction are maintained. A code word, rather than identification, is often used to receive money. And operators rely on trust and ethnic relationships, not on documents and bank regulations, to ensure that transactions are fair and credible.

This secrecy and anonymity pose difficult problems for financial regulators and law enforcement officials. International requirements that financial institutions report suspicious transactions and know the identities of their customers are nonexistent with alternative remittance systems. They operate outside the control and supervision of government authorities.

The opacity of these systems makes them attractive for organizations that want to launder drug money, finance terrorist operations or hide funds for other illegal activities. Since the terrorist attacks in the United States on Sept. 11, 2001, some investigators have called for cracking down on alternative remittance systems.

But the situation is not that simple. These systems are used by millions of people around the world, many of whom are poor and have no access to banks. In some countries, a large percentage of money transfers is based on such informal methods. Often these systems predate the formal banking sector by centuries.

The fact that so many people use alternative remittance systems is testament to their effectiveness. They are usually shoestring operations that charge lower fees than bank wire transfers. They are often open 24 hours a day, seven days a week. In comparison with bank money transfers, which can take three to five days, these informal systems can move money across the globe in hours. Dealers in the alternative remittance system also operate even in very remote regions, such as the Pakistan-Afghan border, where there are few banks.

There are drawbacks to these systems. Operators sometimes exploit users with extraordinarily high fees, or they manipulate the foreign exchange rate. And there is little recourse for consumers, since they are using informal systems.

The legal situation surrounding alternative remittance systems is complex. They are legal in some countries and illegal in others. The majority of transactions are for legitimate purposes. The challenge is to protect the legitimate users of informal money transfer systems while rooting out the terrorists and other criminals. It will not be easy.

Attempts to register or license these operators are an important first step. This should be done carefully so as not to drive the systems further underground. It should also be coordinated with public awareness programs that inform people of the benefits of using licensed money transfer systems.

If users of such alternative systems were being adequately served by the formal banking system, they wouldn't need other options. Modernizing the formal banking sector in countries where these systems flourish is vital to providing an effective and transparent option for people to move money across borders.

In a study on the issue, the Asian Development Bank found that one midway point between alternative remittance systems and the long-term goal of establishing a more user-friendly formal banking sector is to design innovative, legal remittance methods that target certain groups. A special system could be used to deliver money for overseas workers in a specific country, for example.

Once people have a competitive legal option to send money, and they begin to move away from informal dealers, it will be easier for the authorities to track terrorists and criminals who still use the older system.

Improving the formal financial sector will bring millions of people into the banking system. The "unbanked," as people without bank accounts are called, have fewer opportunities for economic development. Reforming alternative remittance systems is not just a powerful law enforcement strategy; it is a way to improve the lives of millions of vulnerable people around the world.

The writer, a prosecutor in Tokyo and former counsel at the Asian Development Bank, has worked on terrorist-financing and money-laundering issues.

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