Legal Space for the Creation and Operation of *Fintech* in Ethiopia

Metages Tewabe[∝]

Abstract

The digital economy is reshaping the global financial system, driving the transformation and development of financial technology irreversibly. Financial technology (Fintech), which combines technology and financial services, has revolutionized how businesses could run. The use of such tools has been steadily increasing in Ethiopia in the last few years and is expected to grow fast. The country's financial regulator, the National Bank of Ethiopia, is amending a decade-old Payment System law, allowing foreign investors to set up business in this country. The delicate nature of financial systems imperatively requires legal and regulatory systems to regulate Fintech creation and operations. Yet activities related to Fintech are inadequately addressed by the current law in place. The legal or regulatory response is unclear due to the novelty of the products, services, and players. Because of these fragmented and inconsistent regulatory environments, examining Ethiopia's legal landscape and regulatory frameworks for Fintech has become critical. This article, dedicated to such end, analyze the legal regime for the creation and operation of Fintech under the national bank of Ethiopia regulatory framework. The investigation employed a mixed research methodology with dominant qualitative data generating tools. The evidences from the investigation show that the Ethiopian law in place today does not

[∝] The author holds LL. B and LL.M degrees in Commercial and Investment Law. He has served as a lecturer of law at Madda Walabu University, legal attorney at cooperative Bank of Oromia, and is currently working as an attorney at Awash Bank. This paper was written during their tenure at Cooperative Bank of Oromia, and the author expresses gratitude to the legal service process staff of the bank for their constructive comments on the initial draft. Additionally, the author acknowledges the valuable feedback provided by anonymous reviewers and the editor-in-chief of the journal. For further communication, the author can be reached via email at metytewabe@gmail.com.

include technology assessments for Fintech. Additionally, current regulations on Fintech are insufficient because they do not address consumer protection and maintaining consumer trust procedures. Accordingly, the evidences suggest that lawmakers need to create a comprehensive regulatory framework to manage Fintech and pave a way for a healthy development of financial technology.

Key Words: *Fintech*; Finance; Regulatory framework; technology

Introduction

Over the last two decades or so, the world economy has undergone a thorough modernization and digitalization across sectors. The enabling tools for such transformations are a package of financial technologies widely termed as *Fintech*. These set of tools combine the use of technological innovation and automation to improve financial services. The tools are increasingly recognized as key enablers for financial sectors, enabling more efficient and competitive financial markets worldwide.[1] In more unprecedented magnitude, digital *Fintech* tools are allowing access for financial services to unbanked areas in emerging economies. As such, they permit customers to access financial services at an affordable price, increase convenience, improve financial inclusion, and boosts productivity gains.[2]

[1] Boeddu,Gian Luciano and Chien,Jennifer, Consumer Risks in Fintech : New Manifestations of Consumer Risks and Emerging Regulatory Approaches : Policy Research Paper (English). Finance, Competitiveness and Innovation Global Practice Washington, D.C. : World Bank Group (2023) ,available at http://documents.worldbank.org/curated/en/515771621921739154/Consumer-Risks-in-Fintech-New-Manifestations-of-Consumer-Risks-and-Emerging-Regulatory-Approaches-Policy-Research-Paper last accessed on 23,January 2023.

[2] Banking evolution; how take on the challenge of Fintech, (Jan.19,2023), available at https://legal.thomsonreuters.com/en/insights/Articles/how-to-take-on-the-challenges-of-Fintech last accessed on 22,January 2023.

Such rapid advances in technology are changing the landscape of the financial sector with more products continually added to the developing system.

Fintech, as a recent concept, has no an agreeable definition. For financial practice experts such as Varga, it refers to companies that develop financial services and products by relying much on intense information technology[3]. Schueffel, a scholar, who reviewed more than 200 articles in the scholarly discourse,[4] defined this concept as a new financial industry that uses technology to improve economic activities. Apart from individual scholars and practitioners, institutions define the concept in terms of its role in institutional operation and transformation. To this end, Financial Stability Board (FSB)[5] describes it as "… Financial innovation made possible by technology that could lead to new business models, applications, processes, or products that would significantly affect financial markets and institutions as well as the provision of financial services."[6]Although there are some differences in the scope and perspectives of the definitions for this concept, there are three common core elements underlying its essence: new technological innovation, finance, and efficiency.

The three elements take the center stage in the definitions signifying that there is a symbiotic relationship between technological revolutions and business practices including legal operations of institutions. Experience shows that

[3] Varga, D. 'Fintech, the new era of financial services', Budapest Management Review, (November, 2017), p.12.

[4] Schueffel, P. Taming the beast: a scientific definition of Fintech. Journal of Innovation Management, Vol 4, No 4, (2016), p.32.

[5] The Financial Stability Board is an international body that monitors and makes recommendations about the global financial system. It was established after the G20 London summit in April 2009 as a successor to the Financial Stability Forum.

[6] Johannes Ehrentraud, &Denise Garcia, Policy responses to Fintech: a cross-country overview, Financial Stability Institute, FSI Insights on policy implementation No 23, (January, 2020), p.6, available at https://www.bis.org/fsi/publ/insights23.pdf last accessed January 26.

some technological innovations lead to the modification of business practices, and consequent changes in the law. But the pace of these changes varies. Legal systems may need time to reflect the implications of progressive technological changes and develop a consistent, predictable, and flexible response to new challenges.

The National Bank of Ethiopia, regulating the country's financial system, has made tremendous changes in the last decade or so. Among others, it is amending a Payment System law that has been in force for ten years. The new law is meant to allow foreign and domestic investors to establish businesses in Ethiopia as providers of digital financial services.[7] It will pave the way for *Fintech* to contribute to the growth of Ethiopia's economic and financial environment. Until recently, the payment services sector in Ethiopia was exclusively reserved for two types of financial institutions: banks and microfinance institutions. The major shift from such market players happened recently with the recognition of nonbank digital financial service providers (*Fintech*).

The regulatory Framework for *Fintech* is poorly defined worldwide.[8] Ethiopia as well does not have adequate regulatory laws covering *Fintech* in general. There are only sporadic laws, yet not concise enough to regulate the specific area of *Fintech*. This gap in the law is so clear that it requires formulation of sound regulatory systems addressing *Fintech* creation and operation. Moreover, due to the novelty of the products, services, players, and the sporadic legal/regulatory response, courts may risk making inconsistent ruling

[7] Hawi Dadhi. Why Ethiopian local Fintech are worried, (2022), available at https://qz.com/africa/2175298/why-ethiopias-local-Fintechs-are-worried, last accessed on February 4, 2023.

[8] Matthias Lehmann. Global rules for a global market place? Regulation and supervision of Fintech providers, Boston university international law journal vol. 38, No, 1, (2020), p. 142.

and swing towards approaches that may not always be the most appropriate option given the context of a specific jurisdiction.[9] Thus, ensuring a level playing field between regulated financial institutions and *Fintech* players and amongst them remains a challenge.

Financial services are among the most heavily regulated sectors in the world. Not surprisingly, regulation has emerged as governments' first concern as *Fintech* companies take off. As technology is integrated into financial services processes, regulatory problems for such companies have multiplied. In some instances, the issues are a function of technology. In others, they reflect the tech industry's impatience to disrupt finance.[10]

Looking into the service providers, one could find emerging *Fintech* organizations to provide financial services in Ethiopia. Some of them could be privately owned or owned by the government; it could also be independently providing financial services or with other financial organizations. These irregularities of regulation could constrain *Fintech* provider's customers, and this in turn might open a space for an individual to infringe on users' interests.

Against this backdrop, this article examines the Ethiopian legal regime in terms of its potential to regulate the creation and operation of *Fintech*. The study employed mixed doctrinal and empirical methodology to explore governing rules and the practical issues on the topic.

1. Overview of *Fintech* in General

[9] Financial Stability Implications from Fintech, Supervisory and Regulatory Issues that Merit Authorities' (Jan. 23,2023)available at https://www.fsb.org/wp-content/uploads/R270617.pdf last accessed on February23.2023.

[10] The Fintech Industry: Definition, Landscape, and Companies,(Jan.25,2023)available at https://academy.apiary.id/blog/the-Fintech-industry-definition-landscape-and-companies .last accessed on February 23,2023.

1.1. Meaning of *Fintech*

The supply of financial services is being challenged by a new industry called Financial Technology (*Fintech*), which combines cutting-edge technology and innovation to improve financial operations.[11] *Fintech* uses technology creatively to build and provide financial services and solutions. As such, *Fintech* often addresses every facet of the connection between a bank and its customers and develops cost-effective, more convenient, and generally more effective digital substitutes. It has developed into a platform that connects banks with essential service providers like utilities, telecom, transit, card programs, shops, healthcare, and education, among others.[12]

Since the internet technology began to penetrate the financial market, all financial fields involving computer technology such as block chain technology, cloud computing technology, digital information technology, and network communication technology have been called financial technology. *Fintech* refers to any digital service a consumer uses to manage their money, including online banking, payments, investing, savings, budgeting, and borrowing.[13] *Fintech* businesses can offer more creative and customer-focused business models. In contrast to traditional financial services, which came under urgent pressure to revisit their business models and change their

[11] Silva, L. A., Financial inclusion in the age of Fintech: a paradigm shift. Fourth FSI-GPFI conference on standard-setting bodies and innovative financial inclusion: implications of Fintech and other regulatory and supervisory Developments, Switzerland: Basel. (2018), p. 4.

[12] Mehrotra, A. Financial Inclusion through Fintech – A Case of lost focus. International Conference on Automation, Computational and Technology Management (ICACTM), Dubai, UAE. (2019), p. 5.

[13] Liudmila Zavolokina, & Mateusz dolata, The Fintech phenomenon: antecedents of financial innovation perceived by the popular press. (2016), P.16. Available at https://jfin-swufe.springeropen.com/Articles/10.1186/s40854-016-0036-7 last accessed on February 25.2023.

strategies to be more competitive, these disruptive businesses are steadily gaining market share and profitability.[14]

In Ethiopia, any business that seeks to become a digital financial service provider has two options. Either it can become a payment instrument issuer (electronic money issuer) or a payment system operator. Payment instrument issuers are digital wallet operators or digital banks obliged to guarantee their customers' electronic deposits with a guarantee deposit in one of the commercial banks of Ethiopia. This is an obligatory requirement to safeguard financial stability if they go bankrupt. According to Licensing and Authorization of Payment Instrument Issuers Directive No. ONPS/01/2020 Article 6(1), payment instrument issuer may be allowed to provide the following services:[15]

a. Cash-in and cash-out.
b. Local money transfers, including domestic remittances, load to the card or bank account, transfer to the card or bank account.
c. Domestic payments, including purchases from physical merchants and bill payments.
d. Over-the-counter transactions: and
e. Inward international remittances.

A customer of a payment instrument issuer has a daily transaction limit of 5,000 ETB and deposit limit of 30,000 ETB.[16] Its services are expected to cater to small-value retail transactions and peer-to-peer sending. The newly introduced Tele Birr mobile service is licensed under this category. In

[14] Nicoletti, B. The Future of Fintech. Rome, Italy: Palgrave Studies in Financial Services Technology, (2017), Available at https://link.springer.com/book/10.1007/978-3-319-51415-4 last accessed on 26, February 2023.

[15] Licensing and Authorization of Payment Instrument Issuers, Directive No. ONPS/01l2020,Article 6(1)

[16] Licensing and Authorization of Payment Instrument Issuers, Directive (amendment) No. ONPS/06/2022,Article 2

addition, all bank wallet services, such as Coop Pay, CBE Birr, and Amole fall into this category. As per Article 6(2),[17] based on written approval of the National Bank, a licensed payment instrument issuer under the full responsibility of and written outsourcing agreement with a regulated financial institution and pension funds may be allowed to provide Micro-saving products, Micro-credit products, micro-insurance products, or pension products.

On the other hand, payment system operators are *Fintech* companies that focus on payments between consumers and merchants. A payment system operator cannot perform cash in/out; it is expected to provide interoperable and interconnected payment services between buyers and sellers with its market-facing products. Such an operator is expected to collect the buyer's account information digitally through a mobile or a web as a customer touch point. Then the initiated payment will be sent to the national payment switch for clearing and settlement of payment transactions[18].

According to national bank Directive ONPS/02/2020 on licensing and authorization of payment systems operator, a comprehensive application must be submitted as one of the following by anyone seeking to operate payment systems:[19]

a. national switch operator
b. a switch operator

[17] Id., *supra* note 17, Article 6(2).
[18] Nurhassen mensur, Digital technologies and competitive strategies of commercial banks and Fintech in Ethiopia, Ethio- Fintech weekly Article by yene financial technology, (October 2021).p.4.

[19] Licensing and authorization of payment system operators, Directive no ONPS/02/2020, Article 4(3).

c. an automated teller machine operator
d. a point-of-sale machine operator
e. Payment gateway operator.

Upon submitting an application, both payment instrument issuers and payment system operators will become direct participants within the Ethiopian national payment system, which puts them on equal footing with any bank in Ethiopia when initiating, processing, and settling payments.

1.2. *Fintech* Developments

The evolution of finance has been influenced by technical advancement for centuries. Over the past few years, we have seen an increase in automation, specialization, and decentralization. In contrast, financial institutions have discovered ever-more-sophisticated and effective ways of leveraging enormous amounts of customer and firm data.[20] These are going through a significant shift due to the rapid development and adoption of new technology. Globally, *Fintech* emerged and flourished at the fastest intensity[21].

Fintech has evolved through three phases over the last 150 years. [22] The first stage is known as '*Fintech* 1.0' between 1886 -1987. In this stage, correspondent banking was established, and the financial institutions globally became interconnected. The second stage, known as '*Fintech* 2.0', occurred from 1987 to 2008; this stage witnessed the development of the traditional financial sector into digitized banks.[23] Also, this stage witnessed innovative

[20] Fintech and Financial Services, D. H.-G. Fintech, and Financial Services. IMF. (2017).
[21] The History and Evolution of the Fintech Industry, The C2FO team,(January.23,2022) ,available at https://c2fo.com/resources/finance-and-lending/the-history-of-Fintech-how-has-the-industry-evolved/ last accessed on February 27,2023).
[22] Douglas Arner, &Jànos Barberis. 'The Evolution of Fintech: A New Post-Crisis Paradigm?' University of Hong Kong Faculty of Law Research Paper. (2015), p.23.
[23] Id.

financial services provision outlets such as Automated Teller Machines (ATM), the adoption of stock exchanges, central clearinghouses, and international correspondent banking. The present stage is titled '*Fintech* 3.0 (from 2008 onwards).[12] This stage marks the evolution of new companies offering technology-enabled financial services and traditional institutions seeking to meet evolutionary trends in financial innovation.

The Ethiopian baking practice has more or less passed through these stages. As of 1931, shortly after Emperor Haile Selassie assumed power, the country's financial sector expanded. It was a very new phenomenon in comparison to other jurisdictions. Even more, *Fintech*'s emergence is a relatively recent trend. Although there is no fully developed *Fintech* industry in Ethiopia, commercial banks have incorporated *Fintech* into their operations. Examples include online payment systems, payment transfers, automated teller machines, digital lending, and other financial services banks offer through *Fintech*. The first ATM was unveiled by the Commercial Bank of Ethiopia in 2001.[24]

M-BIRR plans to launch a mobile banking service in Ethiopia in early 2013 as financial technology with the view to allow people to carry out fundamental financial transactions from their mobile phones, such as sending and receiving money, paying bills, receiving salaries and other government or non-governmental benefits, and repaying loans.[25] Belcash of the Netherlands also introduces Hello Cash. Banks and microfinance organizations in Ethiopia

[24] Gardachew Worku, Electronic -Banking in Ethiopia- Practices, Opportunities and Challenges, Journal of internet Banking and commerce (2010), p. 5. available on https://www.icommercecentral.com/open-access/electronicbanking-in-ethiopia-practices-opportunities-and-challenges-1-8.php?aid=38390 last accessed on February 26,2023

[25] M-Birr national mobile money service, Ethiopia, InclusiveBusiness.net (Jan. 16, 2023) available on https://www.inclusivebusiness.net/IB-Universe/ib-companies/m-birr-national-mobile-money-service-ethiopia, last accessed on February, 27, 2023.

offer Hello Cash, a mobile money service.[26] With this platform's help, consumers can make deposits, withdrawals, transfers, and payments using mobile devices. The previous ten years have seen the introduction of several platforms for financial services, including Chapa, Coop pay, Amole Mobile, Tele birr, CBE-Birr, etc.

Another key milestone in the development of payment system operators in Ethiopia was the establishment of the Ethiopian e-Payment and Settlement System. Three banks, namely, Nib International Bank S.C, Awash International Bank S.C, and United Bank S.C, linked their ATM networks into a single network known as a "premier switch solution" for the first time in February 2009 to facilitate the country's electronic payment system.[27] Later, three additional banks joined this network: Birhan International Bank, Addis International Bank, and Cooperative Bank of Oromia. Although developing a shared system began in 2009, it wasn't operational until July 5, 2012. Following the realization of this shared system, a customer of one member bank may use the ATMs of any other member bank, regardless of whose bank he currently uses.[28] Even though the country's first shared network was the premier switch solution due to the NBE's national payment project, all commercial banks, the NBE, and the Ethiopian Bankers Association banded together in 2011 to establish the Ethswitch national shared ATM network. This nationwide payment system has also been combined with Premier Switch Solution.[29] The Ethswitch payment system is a centralized electronic payment system that facilitates secure and efficient

[26] Payment platform in Ethiopia, (Jan 16, 2023) available at research proposal.docx> l a s t accessed February 28, 2023.

[27] Tajebe Getaneh Enyew, Shared Automated Teller Machine (ATM) Network in Ethiopia: Appraisal of the Competition Concerns, Bahir Dar University Journal of Law, Vol.9, and No.2 (June 2019), p. 233.

[28] Id.

[29] Id.

electronic fund transfer, clearing, and settlement of financial transactions. Lastly companies such as chapa, Arif pay, Santim pay, Addis pay, etc. joined this sector. Now it has become the backbone for various payment system operators and enables interoperability between financial institutions and service providers.

1.3. Need for regulation of *Fintech*

The *Fintech* regulatory framework aims to take care of specific areas. These areas include possible regulatory mechanisms for the beginning (innovation) of the *Fintech* industry, regulation of cybercrime and fraud, consumer protection and data protection, regulation of the creation of the *Fintech* industry, and regulation of the operation. Regulating bank *Fintech* can be justified on several grounds. Yet the major one is to maximize benefits to financial institutions and the overall macroeconomic health of the nation. *Fintech* introduces a lot of possibilities of making the financial markets accessible to the public and serving as a tool to generate income. The availability of investing, getting personal or company loans, obtaining mortgages, and even buying insurance has increased because of *Fintech.*[30] To leverage such demands as a means of ensuring growth in the industry and the economy, regulatory bodies must govern *Fintech* to maximize their benefits.

One of the elements covered by *Fintech* regulatory frameworks is the innovation of *Fintech* startups. *Fintech* startups are beginner companies that provide financial services.[31] This *Fintech* policy establishes a specialized

[30] Fintech and its Role in the Future of Financial Services,(2018),available on https://center-forward.org/wp-content/uploads/2018/02/Fintech-3.pdf,last accessed on March 29,2023.

[31] Henner Gimpel, Daniel Rau &Maximilian Roglinger, Understanding Fintech stArt-ups– a taxonomy of consumer- oriented service offerings, FIM Research Centre, University of Augsburg, (2018), p. 247.

environment for innovation, company development, and testing new ideas in a safe and controlled setting. It does this by deploying a regulatory sandbox[32]. It creates a specialized setting for testing new ideas and conducting business development in a safe and regulated environment. [33]

Fintech companies handle sensitive financial information and conduct transactions on behalf of consumers. Without proper regulation, there is a risk of fraud, data breaches, and other unlawful activities that can harm consumers. Regulation ensures that *Fintech* companies have adequate safeguards in place to protect consumer interests. Fraud also includes depriving another person or an institution of a benefit to which they are legally entitled. *Fintech* fraud may be manifested as identity theft, hacking, and deep fakes.[34] *Fintech* policy helps to ensure that *Fintech* companies had adequate procedures to prevent these illegal activities.

Another area that requires regulation in the *Fintech* era is data protection. *Fintech* companies collect and process vast amounts of consumers' personal and financial data. The law can help protect consumer privacy and ensure that *Fintech* companies handle and store this data responsibly, minimizing the risk of data breaches or unauthorized access. Data protection mainly involves defending sensitive information from loss, compromise, or corruption[35].

[32] RBI regulatory sandbox: How this Fintech uses block chain for cross-border pay,(2018) available at https://www.livemint.com/companies/stArt-ups/rbi-regulatory-sandbox-how-this-Fintech-uses-blockchain-for-cross-border-pay-11631690871141.html , last accessed on March 6, 2023.

[33] Id.

[34] Edlyn Cardoza, 9 types of fraud the Fintech industry needs to beware of in 2022,(2022),available at https://ibsintelligence.com/ibsi-news/9-types-of-fraud-the-Fintech-industry-needs-to-beware-of-in-2022/ accessed on July 26 ,2023

[35] What is data protection, (2021) available at < https://www.techtarget.com/searchdatabackup/definition/data-protection last accessed on June 21, 2023.

Customer protection guards consumers of financial services against substandard goods, dishonest and fraudulent corporate practices.[36] Additionally, it helps the customer feel secure and guaranteed.

It is essential to balance regulation and innovation in the *Fintech* sector. While regulation is necessary to mitigate risks, protect consumers, and maintain financial stability, it should not stifle innovation or hinder the industry's growth. Therefore, a flexible and adaptive regulatory approach is needed to address such *Fintech's* unique challenges and opportunities.

1.4. The Global Experience in Regulating *Fintech*

The global experience in regulating *Fintech* is characteristically dynamic and an evolving one. As technology continues to disrupt and transform the financial industry, regulators worldwide have been working to strike a balance between promoting innovation and protecting consumers and the financial system's stability. Countries and regions have taken varied approaches to regulate *Fintech* based on their unique circumstances, priorities, and regulatory frameworks.

USA, India, and Kenya are jurisdictions with the richest experience in relation to *Fintech* concerning payments and digital lending. This review draws insights from the reservoir of best practices in these jurisdictions.

1.4.1. United States of America (USA)

The United States of America (USA) has been actively involved in regulating the *Fintech* sector over the past decades. The regulatory landscape for *Fintech*

[36] Consumer protection laws, (2021), available at https://www.law.cornell.edu/wex/consumer_protection_laws last accessed on July 2, 2023.

in the USA is a complex mix of federal and state regulations, varying depending on the type of *Fintech* activity being conducted.

Unlike some jurisdictions, there is no single central entity in the United States that mandates payment criteria and improvements for the entire industry.[37] Instead, various payment systems and service providers are subject to a multitude of laws, rules, and regulations, all aimed at safeguarding end users' interests[38]. Operators, providers, and rule-making bodies for payment systems also establish specific rules and agreements. However, depending on the types of payment services they offer, *Fintech* providers are required to comply with various laws, rules, and money transmission licensing requirements in each of the 50 states.[39]

Fintech providers typically do not offer the same range of products and services as financial institutions, and they may not be subject to the same types of regulation. The Consumer Credit and Protection Act[40], in particular, governs online lending in the United States. Banks and *Fintech* institutions may conduct loans offered via *Fintech*. The majority of pertinent legislation in the USA are consumer protection laws[41]. The Consumer Financial Protection Bureau (CFPB) oversees consumer protection and fair lending practices. It has been actively monitoring and taking enforcement actions against *Fintech* companies that violate consumer protection laws.

[37] Payment system in USA,(2023),available at https://fasterpaymentstaskforce.org/payment-landscape/payments-in-the-u-s/ last accessed July 21, 2023.

[38] Id.

[39] Id.

[40] Fintech laws and regulation 2021 in USA, (2022), available at https://www.globallegalinsights.com/practice-areas last accessed July 2, 2023.

[41] Samuel Girma, the legal and regulation crypto currency in Ethiopia, Thesis Submitted in PArtial fulfilment of the Requirements of LL.M Degree in Business Law(2011) , p. 20.

The USA has also seen the emergence of regulatory sandboxes, which are controlled environments where *Fintech* companies can test their products and services under the supervision of regulators. These sandboxes allow companies to innovate and experiment with their offerings while ensuring consumer protection.

Overall, the regulatory environment for *Fintech* in the USA is evolving and adapting to keep up with technological advancements. The federal and state governments are working to balance encouraging innovation and protecting consumers, ensuring that the *Fintech* industry can thrive while maintaining regulatory oversight.

1.4.2. India

India has made significant progress in regulating the *Fintech* industry in recent years. The country has recognized the potential of *Fintech* to promote financial inclusion, increase transparency, and accelerate economic growth.

The Reserve Bank of India (RBI) introduced the concept of regulatory sandboxes in 2016 to enable *Fintech* startups to test their innovative solutions in a controlled environment.[42] The objective is to allow these startups to experiment with new technologies, products, or services without being subjected to the full burden of regulatory compliance.

Fintech institutions may offer in-bank and out-bank payment services when using *Fintech*. India has recognized both[43]modalities. *Fintech* as a whole and

[42] RBI regulatory sandbox is shaping the future of Indian banking,(2022) ,available at https://www.finextra.com/blogposting/22907/rbi-regulatory-sandbox-is-shaping-the-future-of-indian-banking last accessed on July 2, 2023

[43]Payment system in India, available at https://www.rbi.org.in/scripts/PaymentSystems_UM.aspx last accessed at July 2, 2023.

payment via *Fintech*, in particular, have no complete and unified regulatory document[44]. According to the Payment and Settlement System Act of India 2007, master directions on issuing and operating prepaid payment instruments are among the regulations of payments in India, which primarily focus on the beginning of payment provider entities[45]. Payment service providers must be licensed and registered upon commencement and starting up.

In India, digital lending is a recent phenomenon. Different lending models are possible with digital lending; the most popular ones are person-to-person, business-to-business, person-to-business, and business-to-person[46]. Lender exposure criteria and aggregate borrowing limits were prescribed and regulated by regulations and guidelines since 2017[47].

As *Fintech* services gain prominence, protecting consumers from potential risks and fraudulent activities becomes critical. Accordingly, the RBI has adopted a customer-centric approach, emphasizing the need for data privacy, cyber security, and dispute-resolution mechanisms.[48] The regulations focus on safeguarding customer interests and promoting fair practices by *Fintech* players.

1.4.3. Kenya

[44] Fintech laws and regulation in India,(2021),available at https://www.globallegalinsights.com/practice-areas last accessed at July 2, 2023

[45] Id.

[46] Reserve bank of India, Report of the Working Group on Digital Lending including Lending through Online platforms and Mobile Apps (2012), p. 25.

[47] Id.

[48] Das flags concerns on digital lending including usurious rates, data privacy issues,(2022),available at https://www.thehindu.com/business/das-flags-concerns-on-digital-lending-including-usurious-rates-data-privacy-issues/Article65914787.ece last accessed at July 3,2023.

Kenya has been a pioneer both in east Africa and Africa in *Fintech* provision for mostly unbanked populations for decades ago. Hence, it increased the number of populations in the country's financial inclusions, for it is easy and fast to be accessed with lesser costs than traditional banks' lending services.[49] In recent years, Kenya has emerged as a leader in *Fintech* innovation, particularly in mobile money services. The country's most notable *Fintech* success story is M-Pesa, a mobile phone-based money transfer and microfinance service.[50]

The central bank of Kenya introduced a regulatory sandbox framework. This enables *Fintech* startups to test their innovations in a controlled environment, allowing them to experiment and refine their products or services before full-scale deployment. Kenya has also enacted data protection laws, such as the Data Protection Act to safeguard the privacy and security of individuals' personal data. *Fintech* companies are required to comply with these to protect consumer information. The central bank of Kenya has put in specific regulations to supervise and monitor mobile services, including-money laundering and consumer protection measures[51]. This has helped institutions promote financial inclusion and access to financial services for a large segment of the population.

The Central Bank of Kenya must grant authorization as Payment Service Providers to *Fintech* businesses working in Kenya's payments sector[52]. The National Payment Systems Act (NPSA) and the National Payments Systems

[49] Kenya and Its Fintech Ecosystem in 2022, available at https://theFintechtimes.com/kenya-and-its-Fintech-ecosystem-in-2022/ last accessed at July 2, 2023.

[50] Id.

[51] Rodgers Musamali, Bhavish Jugurnath, &Jackson Maalu,Fintech, in Kenya: a policy and regulatory perspective journal of smArt economic growth, vol. 8, no.1,(2023), p. 36.

[52] Id.

Regulations (NPSR), which are currently in effect, govern the beginning and operation of payments made available by *Fintech*[53]. In contrast, CBK has the authority to regulate and license digital credit service providers, including banks[54]. Digital lending and payment through *Fintech* are recognized and regulated, but cryptocurrencies are not recognized as legal cash in Kenya.

Company Act is one of the relevant legislations applicable to Kenyan digital lending service-providing legal frameworks starting from stipulating minimum establishment requirements for service-providing companies passing through their operations to providing legal grounds for their dissolutions.[55]

Kenya's approach to regulating *Fintech* has aimed to leverage technology to drive financial inclusion, encourage innovation, protect consumers, and maintain financial stability. The country's success in fostering a thriving *Fintech* ecosystem makes it a regional leader and an example for other countries to follow.[56]

1.5. *Fintech* Regulatory Approaches

Fintech may be governed and regulated in various ways, with sub-sectors occasionally determining the possible approach. Four regulatory approaches namely, wait and see/hands off, test and learn/case-by-case forbearance,

[53] Id.
[54] Central Bank of Kenya Act, Chapter 491 of the Laws of Kenya (as amended by the Central Bank of Kenya (Amendment) Act.
[55] The Kenya Companies, Act No. 17 of 2015.
[56]Fintech in Kenya: Towards an enhanced policy and regulatory framework,(2022),available at https://www.thecityuk.com/our-work/Fintech-in-kenya-towards-an-enhanced-policy-and-regulatory-framework/ last accessed at July 2,2023.

structured experimental/innovative approach, and regulatory laws and reforms are widely in use today. This paper discusses the features and potentialities of these approaches for the desired end.

1.5.1. Wait-and-See

This approach is characterized by institutional actions of observing and monitoring innovation trend(s) from afar before intervening where and when necessary. Over time, however, as regulators gain capacity in innovation and technology and start to adopt it by licensed entities over time, policymakers may incrementally change regulations.[57] A *wait-and-see* approach has commonly emerged when there is regulatory ambiguity on whether an activity falls under the remit of a particular institution. Alternatively, this approach offers regulatory forbearance to allow innovations to develop unhindered under situations where there is a need to further build regulator capacity before issuing a response. Still in other instances, depending on its application, it also includes a do nothing response, which involves the use of soft laws. Many jurisdictions have applied this approach when there is a collective need to understand better the technology and its possible application in the financial market[58].

1.5.2. Test-and-Learn

This approach involves creation of a custom framework for each business case, allowing it to function in a live environment (often with a *no objection*

[57] World bank, How Regulators Respond to Fintech Evaluating the Different Approaches—Sandboxes and Beyond pdf, Fintech Note ,No 5 ,(2020), p. 10.avalable at https://documents1.worldbank.org/curated/es/579101587660589857/pdf/How-Regulators-Respond-To-Fintech-Evaluating-the-Different-Approaches-Sandboxes-and-Beyond.pdf last accessed at Jan.20.2023.

[58] Id.

letter from the regulators). However, the scope of supervision, oversight, and safeguard measures vary across jurisdictions. Policymakers have sometimes followed a *light touch* without close supervision. In others, policymakers follow more extensive frameworks on a case-by-case basis that involved stringent supervisory attention and oversight.[59]

1.5.3. Innovation Facilitators

Innovative approaches involve top-down moves, unlike the learning and test approach. Further, they tend to be more resource intensive than the other approaches. Their use characteristically involves several regulators setting up new units requiring staff with specialized skill sets.[60] Such operation constitutes a point of contact or a structured framework environment to promote innovation and experimentation. This may take such forms as Innovation Hubs/ Offices, Accelerators, and Regulatory Sandboxes as different types of facilitators.[61]

1.5.4. Regulatory Laws & Reforms

Regulatory law reforms include introducing new laws or licensing requirements that are both overarching and product specific in response to innovative firms or business models. In some cases, countries use new laws to

[59] How regulator respond to Fintech, available at https://www.wdronline.worldbank.org/bitstream/handle/10986/33698/How-Regulators-Respond-To-Fintech-Evaluating-the-Different-Approaches-Sandboxes-and-Beyond.txt?sequence=6 last accessed on January 16, 2023.

[60] Policy challenges and approaches to innovative Fintech, available at https://www.itu.int/hub/2021/06/policy-challenges- and-approaches-to-innovative-Fintech/ > last accessed on, January 18, 2023.

[61] World bank, How Regulators Respond to Fintech Evaluating the Different Approaches Sandboxes and Beyond ,(2021) p.10 available at https://www.wdronline.worldbank.org/bitstream/handle/10986/33698/How-Regulators-Respond-To-Fintech-Evaluating-the-Different-Approaches-Sandboxes-and-Beyond.txt?sequence=6 ,last accessed Jan.20.2023.

expand their mandate, to build capacity, or to raise awareness over accountability while supporting the development of more discreet, secondary reforms and amendments to existing frameworks. One or more of such moves might eventually lead to regulatory reforms.[62] The National Bank of Ethiopia (NBE) is responsible for issuing licenses and regulating the activities of *Fintech* companies in the country. The government periodically reviews its policies and regulations related to *Fintech* to ensure recent relevance of the technological products. *Fintech* companies are also required to obtain relevant licenses and to comply with regulations in place in the country. Ethiopia adopted this regulatory approach to support and regulate the growth of the *Fintech* sector. It is particularly taking a proactive regulatory approach, striking a balance between supporting *Fintech* innovation and ensuring consumer protection and financial stability. These regulatory approaches aim to foster a thriving *Fintech* ecosystem and contribute to the country's economic growth and financial inclusion goals.

2. Ethiopian Legislative Documents Relevant to *Fintech*: An Overview

2.1. Policies and strategies related to *Fintech*

Governments are inherently in constant move to devise mechanisms that best regulate and benefit their financial systems. Such moves may be policy actions that the government decides to take,[63] or a strategic move with a comprehensive plan or a method of doing multiple policy activities. A closer look into the Ethiopian macro strategic documents or financial policies shows that there are only limited policies or strategies relevant to *Fintech* in the country. Those documents include the national digital strategy, National

[62] Id.

[63] Public polices, available at, https://www.civiced.org/project-citizen/what-is-public-policy , last accessed on Jan.18, 2023.

digital payments, NBE monetary policy framework, and national information and communication technology policies and strategies.

The Federal Democratic Republic of Ethiopia formulated the national Digital Ethiopia 2025-A Strategy for Inclusive Prosperity in Ethiopia.[64] This new fourth industrial revolution (4IR) is advancing across the globe at an unprecedented rate, and Ethiopia proactively embraces it to ensure societal benefit from this technological tool and to cultivate innovation among the youth who should get ready for a different future world.[65] From the strategy, sectors and institutions can design and/or align action plans to create inclusive prosperity, leveraging technology that will catalyze the realization of Ethiopia's broader development vision: job creation, forex generation, and becoming a middle-income country.

While such vision is set out in the strategic documents, Ethiopia's digital economy is still in its infancy, with few private firms providing online services and some government-driven initiatives to go digital. To scale up the capacity of the system, the proposed digital strategy is committed to achieving the following key goals: proposing an inclusive digital economy that accelerates the realization of a broader development vision; becoming a visionary umbrella from which sectors and institutions design action-oriented strategies; highlighting the need for urgency, mobilizing stakeholders that enable an inclusive digital economy; coordinating and strengthening current initiatives under the most strategic and pragmatic path possible.

[64] Ethiopian Digital strategy, 2020, available at (https://mirror.explodie.org/Ethiopia%20Digital%20Strategy%202020.pdf ,last accessed on February 2,2023.

[65]Digital Ethiopia 2025 – Summary digital Ethiopia ,available at https://mint.gov.et/wpcontent/uploads/2022/01/Summary_of_Digital_Strategy_Final_English1.pdf ,last accessed on February 5,2023,

In addition to this, National strategy for digital payments (NDPS) Strategy for 2021-2024 is another package that the National bank of Ethiopia has prepared. This strategic plan, which constitutes 32 action plans, will support a cash-lite and a financially accessible economy, which aim to create a secure, competitive, efficient, innovative, and responsible payment ecosystem[66]. Compared to preceding financial products, this approach is unique and thorough for digital payments, incorporating positive international experiences.

By providing incentives, NDPS encourages *Fintech*[67]. The goal of the incentives is to launch *Fintech* and consumer protection. In addition, NDPS advise enacting strict consumer protection legislation to foster/increase customer confidence and trust by promoting security, safety, and transparency.[68] Complaint resolution mechanisms are essential for consumer protection and trust-building.[69]

Ethiopian Financial Inclusion is also another strategy dedicated to the same end. By assessing the current financial exclusions and developing strong frameworks to hasten the planned financial inclusion, the 2017 national financial inclusion strategy aims to accelerate the nation's overall economy. Numerous regional studies suggest that, despite the current progressive financial development, the Ethiopian financial service provisions are full of gaps or exclusions.[70] For instance, a 2014 poll by the index found that 56% of

[66] NBE’s strategy, National Digital payment strategy (NDPS) (2021-2024), p. 19.
[67] National strategy for digital payments (NDPS) Strategy for 2021 to 2024, p. 37.
[68] Id, page 51
[69] Id.
[70] Financial inclusion strategy, 2017, NBE, available at https://nbebank.com/wp-content/uploads/pdf/useful-links/ethiopian-national-financial-Inclusion-strategy.pdf. , last accessed on Febuarary.23, 2023.

individual citizens did not owe any money but instead saved, borrowed, and used informal measures to protect themselves against hazards.

Several plans with priority activities to overcome related barriers to financial inclusion are prepared as part of implementing the national financial inclusion strategy. Therefore, it is believed that the primary strategic areas to be concentrated on are strengthening financial and other infrastructure, ensuring the supply of an adequate range of suitable products, services, and access points, developing a strong financial consumer protection framework, and improving financial capability.

2.2. Banking Business Proclamation

In Ethiopia, proclamation number 592/2008 and its amendment proclamation number 1159/2019 govern the banking industry. In the traditional sense, banking business refers to financial transactions involving a company that offers loans, credit, payment, currency exchange, savings accounts, and checking accounts[71]. Saving and receiving money, lending money for investments, purchasing and selling gold, sending money to domestic and international banks, dealing with bonds, agency banking, and digital financial services are all examples of financial transactions.[72]

Articles 2(2) (f) and 2(21) of the Banking (Amendment) Proclamation define digital financial services as a service offered by *Fintech*. The legislative provisions mentioned financial services such as payments, remittances[73], and

[71]Business banking, available at https://www.investopedia.com/terms/b/business-banking.asp, last accessed on 23 February 25,2023.

[72] Business banking proclamation, proclamation No. 592, Federal *Negarit Gazeta*, Year 14, No 57, (hereinafter referred to as banking business proclamation), Art. 2(2, a-f),

[73] Banking business (amendment) proclamation, No. 1159, Federal *Negarit Gazeta*, Year 25, No 88, (hereinafter referred to as Banking(amendment) proclamation), Art. 2(1, f &g.

digitally accessed insurance services as major *Fintech* services.[74] Yet other financial services categories such as digital loans and financial exchanges carried out by *Fintech* are left out of this classification. From the wording of this provision, it seems that the list of the subcategory of digital financial services is non-exhaustive.

Additional definitions of digital financial services include those for payments, remittances, and insurance that can be accessed and provided online[75]. Digital credit is not listed among the digital financial services in these provisions. Through a close reading of the provisions, one may observe that the legislature alludes to non-exhaustive list by including phrases like *other financial services.* Yet equally, anyone would argue that the Directive of Digital Financial Service, which has not yet been implemented, might remedy the gap[76]. The stipulations in the directive suggest that Ethiopia lacks a legal basis for introducing digital credit independently by *Fintech* or banks.

2.3. National Payment System Proclamation

Ethiopia issued the first national payment system proclamation in 2011 after recognizing the importance of the national payment system in ensuring the efficiency, effectiveness, and financial stability of the nation's overall economic growth. The proclamation also demanded that guidelines for creating, administering, and controlling the national payment system be provided[77]. The national payment system in Ethiopia encompasses a variety

---

[74] Banking business (amendment) proclamation 1159/2019 Art. 2/21.
[75] Banking business Proclamation no 1159/2019, Article 2(21),
[76] Id, Art 58.
[77] National Payment System Proclamation, No. 718, Federal *Negarit Gazeta*, Year 17, No 84, the Preamble (hereinafter referred to as National Payment System Proclamation).

of components, including both *Fintech* and conventional payment systems, along with associated processes, regulations, and technology.[78]

Apart from the issue of permits, the proclamation covers rules that apply to the payment made in the conventional bank and *Fintech*. Yet the regulatory provisions, the writer argues, are not strong enough to meet the needs of customers. For example, the user's growing confidence in payment methods and services offered by financial institutions, notably *Fintech*, is not adequately reflected in the regulatory rules. Trust must be there for economies, societies, and financial markets to be robust. Payment providers must adhere to data protection and privacy laws to safeguard customer information. They need to implement strong security measures and encryption protocols to protect financial data from unauthorized access or breaches, but this issue is not well regulated in this proclamation[79]. There are no strict requirements for a starting payment provider, particularly for *Fintech*, and there is no provision in the proclamation for harmonizing international payment system laws.

The law allows citizens to operate a firm as payment instrument issuers and Payment System Operators under their respective Directive.[80] Foreign nationals are also allowed to engage in a payment instrument issuer and payment system operator business or establish a subsidiary[81]. In addition, the Directive stipulates that anyone other than financial institutions must first get an NBE license to operate a payment instrument or to work as payment system operator. Financial institutions sometimes infringe on these

[78] National Payment System Proclamation, Proclamation No. 718, Art. 2(16, a-e).

[79] Ronald J. Colombo, The Role of Trust in Financial Regulation the Role of Trust in Financial Regulation, Villanova University Charles Widger School of Law,(2020), p. 26,

[80] National payment system (amendment) proclamation, no.1282/2023, Art.6 (8).

[81] The National payment system (amendment) proclamation no.1282/2023 Art. 6(8) and Art .6(7)

obligations by assuming that the National Bank of Ethiopia (NBE) has already granted them permission to offer banking services. However, according to the law, they may only utilize the payment system for the services associated with their regular financial transactions.[82]

Consumers will be reluctant to use the services if the industry is not trusted; this would, in turn, harm the industry and the national economy by limiting the amount of cash available for investment and productivity.[83] The National Payment System Proclamation lays out many rules for the Ethiopian payment system. Yet the payment service providers who carry out their activities using these rules may not have sufficient security measures to protect users' personal and financial information, leaving them vulnerable to data breaches and fraud. Inadequate governance can also result in poor dispute resolution processes, making it difficult for users to recover their funds in cases of unauthorized transactions or other payment-related issues.

A single provision alone cannot ensure users' transaction security. While Articles 20/1/ and /2/ of the proclamation outline the process for handling complaints, these stipulations may not effectively address users' concerns regarding security issues. Paradoxically, the course of addressing complaints typically comes into play only after the issue has been resolved.

The National Payment System Proclamation's Article 7/4/ specifies the startup requirements for *Fintech* payment platforms. These requirements include the system's proposal, technological specifications, security procedures, clearing and netting procedures, management and integrity

[82] Id., Art. 20.
[83] C V.D. Cruijsena,J.D.Haanb & R.Roerinka, Trust in financial institutions: A survey, University of Groningen, The Netherlands, (2020), p. 27.

experience, consumer interest, and policy implications.[84] The regulatory sandbox is a framework that allows innovators, startups, and financial technology (*Fintech*) companies to test their products, services, or business models in a controlled environment under the supervision of regulatory authorities.[85] Sandboxes allow financial institutions and *Fintech* firms to test out novel financial goods or services in a real-world setting, but only for a limited time and in a specific location. The objective is to foster innovation, promote competition, and ensure consumer protection in emerging sectors or new technologies. Yet despite the global popularity of and key role of regulatory sandboxes, no framework for the use of such tools has been established in Ethiopia.

Moreover, the innovation hub exam should also be added to the list of requirements before the launch of *Fintech* platforms.[86] The innovation hub exam is a formal assessment conducted by regulatory authorities to determine the eligibility and suitability of *Fintech* companies and innovators to participate in a regulatory sandbox. These requirements are crucial to guarantee quality and system caliber for *Fintech* startups. However, they are not included in the prerequisites.

Ethiopia has no specific sandbox and innovation hub regulatory framework for *Fintech*. While the National Bank of Ethiopia has conducted a pilot test, this test does not constitute a full-fledged sandbox and innovation hub.[87] Its primary purpose is to grant licenses for *Fintech* businesses rather than

---

[84] National payment system proclamation no 718/2011 Art. 7/4, a-h.

[85] Attery,A,M.Lesher & C.Lomax The role of sandboxes in promoting flexibility and innovation in the digital age, going digital tookili policy not, No2. (2020), p.36.

[86] Radostina Patarni, Sandboxes and Innovation Hubs for Fintech Impact on innovation, financial stability and supervisory convergence, European parliament committee, (2020), p. 33.

[87] Interview with Solomon Damxewu, NBE Director, payment and settlement system (July 5,2023)

providing a comprehensive sandbox environment[88]. Furthermore, it is worth mentioning that Ethiopia's Information Network Security Agency (INSA) primarily focuses on testing security issues related to *Fintech* and not on establishing a comprehensive sandbox and innovation hub, as is the case in some other countries[89]. No dedicated institution or regulatory body has the expertise and infrastructure to oversee such a hub. Thus, Ethiopia lacks both practical implementation and a regulatory framework for a sandbox and innovation hub.

The Cooperative Bank of Oromia is the first financial institution to introduce an online credit system called "MICHU." It is digital lending for micro, small, and medium-sized businesses platform[90]. The platform evaluates SMEs' risk and growth potential, so lenders can decide whether to issue loans based on risk assessment outcomes. Cooperative Bank of Oromia launched this platform as a bank for the first time without needing a sandbox on this brand-new platform[91].

Lastly, the proclamation cannot regulate digital credit in the form of digital assets or crypto assets. No online credit is permitted on a block chain platform in the form of crypto currency[92] within Ethiopia's jurisdiction since NBE

[88] Id
[89] Id
[90] MICHU Uncollateralized Lending Platform, coop bank of Oromia available at https://coopbankoromia.com.et/michu/, last accessed on January 21, 2023.
[91] Interview with Abdi Fekede, Director, Digital products, and services. (March 8,2023)
[92] Crypto-asset could be defined as a form of digital currency based on a network that is distributed across a large number of computers. It is a virtual currency formulated to function as a medium of exchange like dollar, euro, and birr. A digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority. The main plat form deployed to establish decentralized crypto- asset is that block chain. Block chain is an online decentralized ledger technology that registers transactions between two pArties connected in a peep-to-peer ("P2P") network.

circulars prohibit digital assets. Additionally, this results in lack of regulatory capacity to control various digital credit forms, including businessperson, person-to-person, business-to-business, and person-to-business credits. This inadequacy leads to the mistreatment of consumer complaints, abuse of consumer interests, and mistrust.

2.4. Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation

The Ethiopian legislature passed the Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation to protect national security, to stabilize financial markets, and to boost the effectiveness of financial institutions[93]. The major goal of Anti-money laundering laws is to authorize and assist competent institutions in discovering and reporting suspicious conducts, including crimes that serve as a foundation for money laundering and terrorist financing[94].

Money laundering appeals to criminals in *Fintech* because it is made easier for them by the rise in transaction initiation in these systems, unlimited money flow, and anonymous accounts.[95] While the legislative's move on preventing and combating money laundering and terrorism financing is encouraging, it appears to place little emphasis on digital financial services and instead emphasizes traditional financial services. *Fintech* is currently updating itself continually at the fastest rate. Given this pace of developments and

---

[93] Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation, proclamation No. 780, Federal *Negarit Gazeta*, year 19, No 21, the preamble, (hereinafter referred to as Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation).

[94] Anti-money laundering law (AML), Rule and Guidance, available at https://www.finra.org/rules-guidance/key-topics/aml , last accessed on January. 19,2023.

[95] Anti-Money Laundering Guidance for Fintech, available at https://sanctionscanner.com/blog/anti-money-laundering-guidance-for-Fintech-167, last accessed on January 30,2023.

sophistications in *Fintech*, it is imperative to have a more advanced anti-money laundering regulatory framework at all levels of financial system operations. As such more legislative moves are required to balance the *Fintech* industry's development and the control of criminal activity such as money laundering and support for terrorism.

Referring to the proclamation's clauses, one could conclude that the definition of funds and property does not expressly cover *Fintech* payments and digital lending.[96] According to Article 2/9 of the proclamation, financial institutions include insurance companies, microfinance organizations, postal savings institutions, and money transfer institutions. *Fintech* and digital financial services are not expressly included in this proclamation.[97]

2.5. National Bank Directives Regulating *Fintech*

2.5.1. Licensing and Authorizations of Payment Instrument Issuers

To promote the safety and efficiency of the payment system by establishing clear and enabling regulatory requirements and protecting the interests of the users–in addition to mitigating associated risks and maintaining reliability[98]– the NBE issued D**irective No. ONPS/01/2020** as per the provisions of the National Payment System Proclamation[99] and the Amendment Banking Business Proclamation[100]. According to the Directive, a person who holds a license from NBE and issues tangible or intangible instruments such as cards,

[96] Prevention and Suppression of Money Laundering and Financing of Terrorism Proclamation 780, Art. 2(5).
[97] Id, Art. 2(9)
[98] NBE issues directive To licence ,Authorize payment instrument issuer-National Bank, available at https://nbe.gov.et/nbe-issues-directive-to-license-authorize-payment-instrument-issuers-2/ .last accessed on Feb1,2023.
[99] National Payment System Proclamation number. 718/2011, Art. 4(2, a) and 37(2).
[100] The amendment of banking business proclamation number.1159/2019, Art.58.

checks, and e-money that allow a person to make payments or transfer funds is referred to as a payment instrument issuer[101]. This Directive ensures that *Fintech* companies comply with relevant legislation and uphold consumer protection standards.

The payment instrument issuer may be permitted to offer standard banking services like cash-in and cash-out, local money transfers like domestic remittances, loading to the card or bank account, transferring to the card or bank account, domestic payments like purchases from merchants, bill payments, over-the-counter transactions, and inward international remittance services based on requests made and written approval by the NBE.[102] A licensed payment instrument issuer with full accountability and a written outsourcing agreement with regulated financial institutions and pension funds may also be permitted to offer micro-savings, micro-credit, micro-insurance products, and pension products with the written consent of the NBE.[103]

Laws in Ethiopia prohibit providing digital credit services, independently by Fin-techs. Such activities require a written outsourcing agreement with a regulated financial institution[104]. However, it is also important to examine the potential consequences of these restrictions. Digital credit services have the potential to bridge the gap in financial inclusion. Moreover, digital credit services can contribute to economic growth by enabling entrepreneurs and small businesses to access capital for expansion and investment. Another point to consider is the innovation and competition that *Fintech*s bring to the market. By restricting their ability to provide digital credit services, there

[101] The Licensing and Authorization of Payment Instrument Issuers Directive No. ONPS/01l2020. Art.2 (19).
[102] Id., Art, 6(2).
[103] Id., Art, 6(1).
[104] Id., Art, 6(2).

could be a dampening effect on innovation and consumer choice[105]. Also, regulations that are too stringent and inflexible may discourage *Fintech*s from operating in the country altogether. This could hinder the growth and development of the *Fintech* ecosystem.

Like the previous proclamation, no sandbox and innovation hub requirement is set as tests for the payment instrument issuer.[106] *Fintech* companies must put in place measures to protect customers' interests and ensure fair treatment. This may include providing clear and transparent information about fees, charges, and terms and conditions and addressing customer complaints and disputes. *Fintech* companies must comply with ongoing obligations, such as reporting requirements, maintenance of appropriate risk management systems, and ensuring the protection of consumer funds.[107] Yet all sets of issues are not well regulated under this Directive.

Disagreements and grievances are part of every economic transaction. Require substantive legislation to address those disagreements and complaints; no rule or legal clause currently deals with disputes and grievances brought up by digital credit platforms. Additionally, because digital credit operates differently than traditional loans, applying other pertinent laws to address disputes and complaints is challenging and confusing. In other words, the service providers decide everything, including who gets the loan, how much is borrowed, when it is due, how long it will take to pay it back, and the contract terms.

[105] Interview With Gelata Abate, Innovation hub director of Cooperative Bank of Oromia, (March 09.2023)

[106] Licensing and authorization of payment system operators, Directive no ONPS/02/2020, Art, 4, 4.6, a-i.

[107] What is regulation in Fintech? Available at https://www.idnow.io/Fintech/what-is-Fintech-regulation/ last accessed on July 3.2023.

The international payment system is essential and facilitates international trade and remittance. Digital payments made through *Fintech* are more convenient[108] than other mechanisms. Yet for national security reasons, direct payment conducted through digital manner is restricted. All payments are like the traditional banking system; they need the presence and physical conduct of the customer to the bank. Different payment platforms for international payment need no physical presence and are made online through normal electronic devices. For instance, PayPal, venom, and eBay are among the online global payment platform. Globally, there is a digital platform for remittance and exchange of foreign currency[109]. However, the Ethiopian jurisdiction has no direct online payment system for national security purposes[110]. Moreover, those platforms are nonexistent due to the absence of regulatory framework for such international payment. Even though building a regulatory capacity to oversee a sophisticated payment system can be time-consuming, waiting indefinitely to acquire regulatory capacity might not be a viable approach. International transactions and cross-border payments are becoming increasingly common in today's interconnected world. The absence of a direct online international payment system could slow down or restrict economic growth, hinder cross-border trade, and potentially put at disadvantage businesses or individuals who rely on global transactions[111]. It is important to find a balanced approach in this situation.

[108] The report of United Nations Capital Development Fund (UNCDF) in collaboration with NBE, Ethiopia remittance review; assessment of payment and financial markets infrastructures, (2020) ,p. 6.

[109] Guide; how to get started as a payment system operator in Ethiopia, available at, https://shega.co/post/guide-how-to-get-stArted-as-a-payment-system-operator-in-ethiopia/, last accessed on Febuarary.3.2023.

[110] Interview with Muluken Mirehetu, NBE legal expert. (February 25,2023)

[111] Solomon, *supra* note 89

2.5.2. Licensing and Authorizations of Payment System Operators

The second Directive affecting *Fintech* is ONPS/02/2020, which deals with the licensing and authorization of payment system operators. As one can observe from its name, the primary focus of this Directive is the payment system. It specifies the criteria, procedures, and documents required for obtaining a license, such as company registration, financial statements, business plan, and proof of technical capability.

The Directive stipulated that anyone other than financial institutions must first get an NBE license to operate a payment instrument. They are considering that NBE has already granted them a license to offer banking services. However, they may only utilize the payment system for their own services associated with their regular financial transactions.[112]

A payment system operator is defined under the Directive as a licensed financial institution by NBE that owns, operates, and administers a payment system,[113] a system that is used to settle the transfer of funds/financial transactions (the system includes the institutions, the people, the rules and procedures, standards, and the technology that make the financial transaction possible) upon authorization by the NBE. The Directive at hand allows only Ethiopian nationals and foreign nationals of Ethiopian origin to engage in the payment system operating business. It also provides that the applicant for provision should be established as a company, where the ownership should be vested in Ethiopian nationals and foreign nationals of Ethiopian origin.

Further, the Directive prohibits payment system operators from engaging in other business activities. On the other hand, an entity or person engaged in

[112] Payment System Operators Directive No. ONPS/02l2020. Art. 20.
[113] Payment System Operators Directive No. ONPS/02l2020. Art. 2(34).

business activity and interested in the payment system operators' business must form a separate company exclusively engaged in payment system operation, fulfilling the requirements provided under the Directive. The National Payment system operator, Ethswitch, is also established under this Directive to facilitate the overall interoperability between financial transactions in the country. The private payment system operators are also invited to join Ethswitch upon fulfilling the prerequisites stipulated under this Directive.

As such the directive covers five categories of licenses: the National switch operator Payment Switches, ATM Operators, POS Operators, and Online payment gateway operators' services.[114] A company can apply for one or multiple licenses, as the need arises. At the same time, the regulation prohibits a payment system operator from engaging in other business activities, including payment instrument issuer business such as Mobile money[115].

2.5.3. Financial Consumer Protection

A new directive, Directive 01/2020, was issued to regulate the protection of financial consumers. This bylaw was enacted based on Article 57 of the amended banking business proclamation that stipulates national banks to issue directives with minimum conditions for consumer protection.[116]

---

[114] Licensing and authorization of payment system operators Directive no ONPS/02/2020.Art. 4(3).

[115] African Fintech state of the industry, African Fintech summit, Is an Ethiopia Market Map from the Africa Fintech State of the Industry Report,(2020), available at https://africaFintechsummit.com/wpcontent/uploads/2021/08/AFTS_StateoftheIndustry_2020_final.pdf last accessed on Febuarary.12,2023.

[116] Amendment of banking business proclamation Number 1159/2019, Art .57.

The directive, which is special due to its inclusiveness, applies to all financial institutions and financial services[117]. As such, it targets all financial institution consumers. Accordingly, digital lending service consumers (borrowers) are entitled to exercise rights provided under the Directive at hand, including the right to access accurate and appropriate information about the lending service they are requested for, including the interest rate, terms, and conditions of the agreement, protection against misuses of their personal data, fair and dignified treatment, easy, speedy and accessible dispute resolution mechanisms, etc.

General principles such as fair treatment, transparency and disclosure, suitability, data protection (confidentiality), complaint handling, and dispute resolution are generally regulated under this directive. To this effect, Article 2.11 of the Directive defines digital financial service by stating what it is and listing the categories. Payment, remittance, and insurance are among the list provided by the Directive. From this, we could conclude that digital crediting is not included under the definition; In addition, the Directive focuses on traditional bank services. So, legal protection given by this Directive to consumers of digital finance, to the *Fintech* consumers, is minimal. Comparatively, payment-related *Fintech* is regulated slightly.

CONCLUSION

Fintech has become a popular catch-all for technology-enabled financial solutions. A customer uses every digital financial service to manage their finances, including online banking, payments, investing, and borrowing and lending money.

National Digital Ethiopia 2025, Ethiopian Financial Inclusion Strategy, and NDPS are all taken from an evaluated legislative document. Ethiopian-related

[117] Financial consumer protection Directive, Directive ,No FCP/01/2020, the Preamble

Fintech policies are incomplete and lack specific provisions for *Fintech*. In the meantime, NDPS appears to be a recent and comprehensive *Fintech* law about payments. However, NDPS is insufficient on its own to address all *Fintech* categories.

To set minimum requirements and prerequisites for providers to launch the service, the current regulatory environment for *Fintech* is insufficient. The *Fintech* regulations do not cover the listing criteria, particularly technology assessments. These technological trials could be innovation Center trials or sandbox trials for regulations. The lack of an innovation hub and sand box impacts users' interest. However, neither in law nor in practice are there now any technology tests.

Fintech also needs a thorough document that governs matters connected to safety, security, consumer protection, and the duties of regulatory agencies by focusing primarily on payment-related *Fintech*. In addition, it is suggested to assess the regulatory perimeter and update it on a timely basis. Regulators need to have a proactive framework that responds to fast changes in the *Fintech* space and regularly implement or contribute to a process to review the regulatory perimeter.

The amendment to the Banking Business Proclamation No. 1159/2019, as outlined in Articles 2(1)(f) and 2(2), permits banks to engage in digital financing, or *Fintech*, exclusively for payment, remittance, and insurance purposes. This clause should be revised to also encompass online lending activities. NBE should outline different startup requirements and prerequisites for various bank *Fintech* types. Proclamation 718/2018 and its amendment proclamation 1282/2023, Directive NO FIS/01/2012, Directive NO ONPS/2/2020, and other legislation should manage digital financial services in a special way that increases consumer confidence to uphold and sustain consumer trust.

Finally, Digital credit is sub-categories of *Fintech*. Ethiopian laws forbid *Fintech* companies from offering independent digital credit services and demand a signed outsourcing arrangement with a licensed financial institution. This might hamper expansion and development of the ecosystem for fin-tech in the country.

In addition to allowing digital credit by *Fintech* in Ethiopia, various types of digital lending, including person-to-person, person-to-business, business-to-business, and business-to-person lending, the NBE needs to give due consideration and be governed by different legislations. Therefore, due to the multiple gaps in the pertinent laws, Ethiopia's regulatory environment for *Fintech* is not adequately regulated and needs an enabling comprehensive law.