SPOTLIGHT 4

Standards in Finance

Financial standards lay the foundation for effective financial systems, promoting trust, stability, interoperability, and inclusion. From those that form the basis for accounting rules that enable transparent financial reporting to those embedded in regulatory frameworks that oversee bank risk and fight financial crime, these standards help preserve the integrity and resilience of financial systems. They also play a key role in expanding access to financial services. Although there is a broad ecosystem of financial standards,[1] for brevity, this spotlight examines how four examples shape financial development and inclusion: the International Financial Reporting Standards (IFRS), the standards embodied in the Basel Framework, Financial Action Task Force (FATF) standards, and standardization in securities markets. These examples also illustrate the benefits and challenges of tiered approaches to the development of standards.

Accounting standards: The International Financial Reporting Standards

Reliable, comparable financial statements are prerequisites for effective prudential regulation, market-based finance, and the operations of securities markets. Accounting standards provide that foundation for financial markets.

The IFRS require companies to disclose relevant information clearly and consistently. Issued in 2003 by the International Accounting Standards Board (IASB), the IFRS are intended for private sector entities that are accountable to the public, such as financial institutions, insurers, state-owned enterprises, and companies listed on a stock exchange. Because smaller firms found the IFRS complex and burdensome, in 2009, the board issued the IFRS for small and medium enterprises (SMEs), meant for entities that are not accountable to the public but are nonetheless required by law to prepare financial statements. Although more than 140 jurisdictions have adopted the full IFRS, only about 80 use the IFRS for SMEs.[2] For many small firms in developing countries, implementing even the IFRS for SMEs may still be too costly. Some jurisdictions instead use them as a reference for developing their own set of accounting standards for SMEs.

Adopting accounting standards makes firms and countries more appealing to investors by enhancing financial transparency and decreasing the asymmetry between information available to firms and that available to potential investors in those firms. For example, adoption of the IFRS has increased foreign ownership of shares in mutual funds[3] and boosted inflows of foreign direct investment to developing countries.[4]

Standards for regulating bank capital: The Basel Framework

Once standards for accounting and financial statements are in place, prudential regulation of bank

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capital builds on the foundations these statements provide in order to ensure solvency, soundness, and resilience in banking systems. Bank capital, which mostly includes shareholders' equity and retained earnings, provides a cushion for absorbing losses during times of distress, thus contributing to financial stability. Higher levels of capital can also curb risk taking among banks because they put more of bank shareholders' skin in the game, since the latter could lose their equity if the bank fails. However, banks may not hold enough capital to remain solvent in episodes of financial stress if they expect to rely on safety nets, such as deposit insurance and bailouts, during times of crisis.[5] Bank failures also impose high social costs that bank managers and shareholders do not internalize.[6] Regulators thus use capital requirements to give banks incentives to ensure adequate management of risks.[7]

The primary developer of global standards for the prudential regulation of banks is the Basel Committee on Banking Supervision (BCBS). Countries that are committee members agree to fully implement BCBS standards for their internationally active banks; currently, 45 regulatory institutions from 28 jurisdictions are members. Nonmembers may adopt these standards voluntarily.

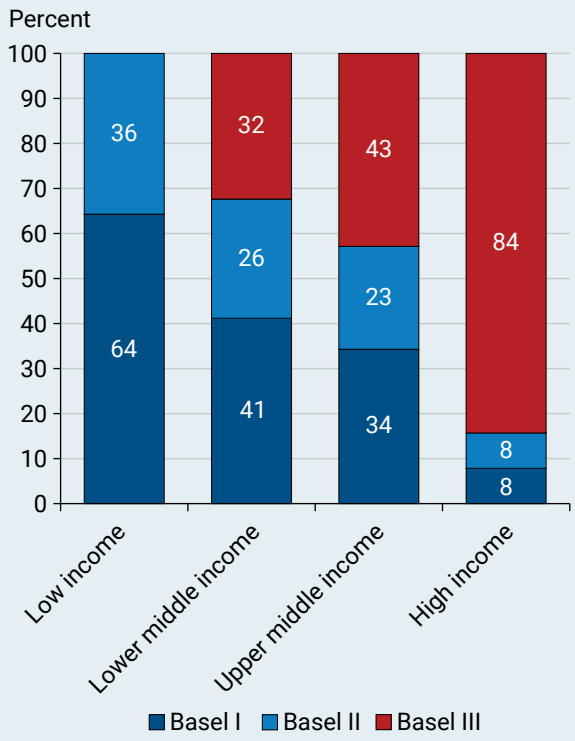
In 1988, the BCBS published its first set of minimum capital requirements for banks, now known as the Basel I accord or simply Basel I, in response to an international debt crisis that originated in Latin America. Basel I categorized assets according to four levels of credit risk and assigned each level a weight: 0 percent, 20 percent, 50 percent, or 100 percent, with the weights increasing according to the riskiness of the underlying assets. (Cash, for example, carried a risk weight of 0 percent, whereas commercial loans—the balances of which banks include as assets on their balance sheets—were assigned the highest risk weight, 100 percent.) Banks use these weights to calculate their *risk-weighted assets* (as opposed to simply their total assets, which had proven an inadequate metric for capturing banks' level of risk). Basel I required banks to hold minimum amounts of capital equal to 8 percent of their risk-weighted assets; this meant that banks had to hold more capital if they had higher levels of risky assets and that two banks with nearly identical levels of total assets could theoretically be subject to very different capital requirements. Most regulators worldwide ended up adopting Basel I,[8] helping to ensure that supervisory effectiveness would be adequate and consistent across member jurisdictions.

Basel I's four categories of risk proved to be too simple, limiting its effectiveness.[9] In practice, loans assigned the same risk weight under Basel I could have very different risk levels. For example, Basel I assigned all commercial loans a risk weight of 100 percent, but loans to small firms are often riskier than loans to large firms. In 2004, the BCBS therefore introduced Basel II, which included a more granular formula for measuring risk-weighted assets. It even allowed some banks to use their own models to calculate the credit risk their asset mixes posed.

The global financial crisis exposed weaknesses in Basel II as well, prompting the BCBS to propose Basel III in 2009. Basel II, as it turned out, did not require banks to hold enough high-quality capital, and the complexity of calculating risk-weighted assets made it difficult to monitor banks' risk exposures. Among other changes, Basel III (1) restricts what bank holdings qualify to be considered capital; (2) includes two capital buffers, which are extra amounts of capital that banks are required to have on hand during times of financial distress or economic downturns; (3) revokes, for certain risks, the use of internal models that was permitted under Basel II; and (4) adds a requirement regarding banks' leverage ratios, specifically, that banks' capital needs to equal at least 3 percent of their total assets, which is easier to measure and monitor than risk-weighted assets.

All 134 countries responding to the World Bank's most recent Bank Regulation and Supervision Survey, conducted in 2016, reported using one of the Basel regimes, but many were still using Basel I or Basel II (refer to figure S4.1). The adoption of Basel III is related to country income level. As of 2016, 84 percent of high-income countries had adopted Basel III, followed by 43 percent of upper-middle-income countries and about one-third of lower-middle-income countries. By contrast, no low-income countries reported using Basel III, and almost two-thirds still used Basel I.

Figure S4.1 Many developing countries are still using Basel I or Basel II bank capital requirement regimes



Source: Bank Regulation and Supervision Survey (dashboard), World Bank, https://www.worldbank.org/en/research/brief/BRSS.

Note: The Basel accords outline minimum capital requirements for banks. Basel I dates from 1988, Basel II from 2004, and Basel III from 2009. The sample includes 134 countries. Constituent percentages in each bar may not sum to exactly 100 percent because of rounding.

As noted earlier, regulators from countries that are not members of the BCBS may still adopt Basel standards to strengthen the resilience of their banking systems. Additionally, adoption of Basel II or III can signal sophistication and advanced standards, which can help attract foreign direct investment and improve the international competitiveness of countries' domestic banks. It can also facilitate coordination between home and host country supervisors of international banks.[10] However, in lower-capacity environments, regulators may choose to stick with the simpler requirements of the Basel I accord and make building up supervisory capacity their priority instead.

More recently, the BCBS has published considerations regarding simplified standardized approaches to Basel III that are based on proportionality. Countries can develop such approaches and apply them to smaller, non-internationally-active banks that are not able to implement the more resource-intensive approaches the accord requires, and some jurisdictions with simpler banking systems could adopt such approaches for their entire banking sectors.[11] However, using a proportional approach also poses challenges for a country's regulators. In a joint survey of 90 jurisdictions conducted by the World Bank and the Bank for International Settlements (BIS), respondents mentioned challenges they encountered during the design phase of such approaches, such as how to define which banks can follow a simplified approach and how to avoid regulatory arbitrage, in which banks adjust their characteristics or location to become eligible for simplified standards, as well as challenges after countries implement proportionality, including how to ensure that financial positions are still comparable across banks.[12]

Capital requirements have different effects on financial development in the short and long terms. Increased capital requirements tend to reduce bank lending in the short term,[13] particularly among banks that are less capitalized relative to other banks before the requirements

go into effect.[14] This reduction in lending primarily affects SMEs that previously had no loans with any bank.[15] However, in the long term, banks that have more capital increase their lending relative to other banks,[16] perhaps because holding extra capital lowers banks' costs of debt and equity.[17] Evidence from Spain shows that capital requirements smooth banks' credit supply and, in bad times, support the performance of firms receiving bank loans, increasing employment and firm survival.[18] Although higher capital requirements impose some short-term costs, the benefits of reduced probability and impact of banking crises tend to more than offset these costs.[19]

Fighting financial crime and promoting financial inclusion: FATF standards

Countries across the globe have begun cooperating over the past few decades in response to crime and related financial flows that cross national borders, with key elements of such cooperation embodied in several United Nations (UN) conventions that create binding obligations for ratifying parties. In 1989, the FATF was established as a technical intergovernmental body responsible for providing the necessary technical details for and supporting the implementation of instruments facilitating this cooperation, which are typically high level, and setting international anti–money laundering standards and standards for combating the financing of terrorism as well as the financing of proliferation of weapons of mass destruction.[20]

The FATF currently has 40 member jurisdictions representing major economies and financial hubs. It maintains a framework of measures known as FATF Recommendations,[21] which more than 200 countries and jurisdictions have committed to implementing. With the help of nine associate member organizations and other global partners like the International Monetary Fund (IMF) and the World Bank, the FATF monitors these countries and jurisdictions to ensure, through a continuous process of peer evaluation, that they implement these measures. Failure to implement them effectively can result in public warnings to noncompliant countries, which in turn create pressure on these countries to address any compliance issues to maintain their access to the global financial system (refer to box S4.1).

The FATF recommendation most directly relevant to financial inclusion is that regarding customer due diligence, which includes customer identification and verification, often referred to as *know-your-customer* procedures. Strict rules regarding customer due diligence can cause banks to exclude customers or potential customers if they lack ID or other documents the banks require for identification purposes.[22] Some 1.3 billion adults worldwide do not have a financial account, often because of documentation requirements, according to the World Bank's Global Findex Database.[23] In Sub-Saharan Africa, 44 percent of adults without such accounts and without ID cite lack of documentation as a barrier to having a mobile money account, compared with 19 percent of adults without an account but with ID (refer to figure S4.2).

Box S4.1 Promoting correspondent banking relationships and international standards on fighting financial crime in Pacific Island countries

When a bank in one country (the *correspondent bank*) provides banking services to a second bank in another country (the *respondent bank*), the two banks are engaging in a cross-border *correspondent banking relationship*. Correspondent banking relationships are at the core of the global system for international payments, enabling cross-border transactions that facilitate international trade, tourism, and remittances, as well as disaster relief and humanitarian financial flows.

Correspondent banking relationships in which the respondent banks are located in certain emerging market and developing countries have declined over the past decade.[a] Globally, these relationships declined by about 30 percent between 2011 and 2022. Some of the largest declines, averaging about 60 percent, have been in Pacific Island countries. These countries are especially vulnerable to the withdrawal of correspondent banking relationships given the countries' heavy reliance on trade, tourism, and remittances—often equivalent to more than 40 percent of GDP—as well as disaster relief and humanitarian financial flows.

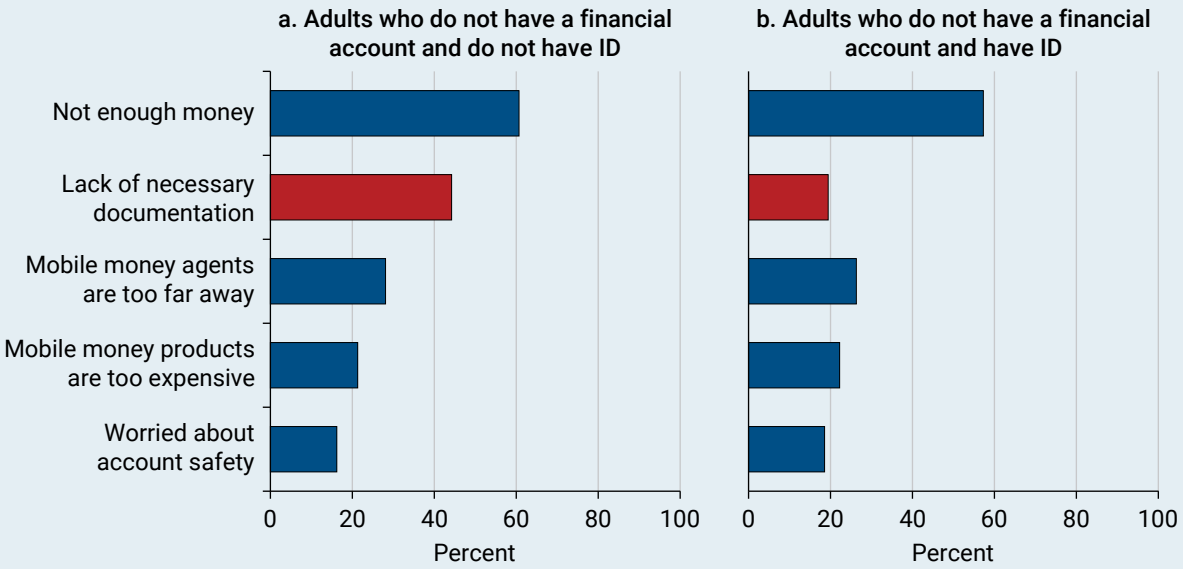
Correspondent banking relationships in Pacific Island countries have declined mainly for two reasons. First, international correspondent banks increasingly consider such relationships a high-risk, low-return business because they require a certain transaction volume to make them sufficiently profitable to justify correspondent banks engaging in them, and individual Pacific Island countries tend to have low volumes of transactions. Second, some Pacific Island countries do not fully comply with anti–money laundering standards and those related to combating the financing of terrorism.[b]

To address the threat of a continuing decline in or even loss of correspondent banking relationships involving respondent banks in Pacific Island countries, the World Bank in 2024 approved a project covering the economies of Fiji, Kiribati, the Marshall Islands, Samoa, Tonga, Tuvalu, and Vanuatu.[c] The project aims to enable continuous access to services in these economies that are typically provided through correspondent banking relationships. First, it will provide temporary access through the recruitment of a service provider that will serve eligible countries facing loss of such relationships in key currencies. Second, it will support increased compliance with anti–money laundering standards and those related to combating the financing of terrorism standards and improved oversight of payment systems, as well as regional regulatory harmonization to facilitate economies of scale.

Sources: Pacific Islands Forum 2023; World Bank 2024.

a. The withdrawal of correspondent banking relationships in response to concerns regarding anti–money laundering and combating the financing of terrorism is also known as *derisking*. A broader term for the withdrawal of such relationships that encompasses other concerns is *debanking*.
b. Pacific Islands Forum (2023).
c. World Bank (2024).

Figure S4.2 Barriers to ownership of mobile money accounts in Sub-Saharan Africa



Sources: WDR 2025 team, based on data from Global Findex Database, World Bank, https://www.worldbank.org/en/publication/globalfindex/download-data; Identification for Development, World Bank, https://id4d.worldbank.org/; Klapper et al. 2025.

Note: Figure shows the percent of adults without a financial account citing a given barrier as a reason for having no mobile money account in 2024. Respondents to the Global Findex 2025 could choose more than one reason. Adults without accounts in Chad and Liberia are excluded because of lack of ID data. The red bars highlight that in Sub-Saharan Africa, the share of adults without an account and without an ID who cited lack of documentation as a barrier to having a mobile money account is more than twice as large as the share of adults without an account but with an ID. All other barriers are cited by about equal shares of adults in both subsamples.

In 2012, the FATF adopted a mandatory risk-based approach to anti–money laundering and combating the financing of terrorism that applies more scrutiny to high-risk customers while allowing simplified measures for lower-risk ones. This approach includes, for example, tiered customer due diligence, which enables financial institutions to provide basic, lower-risk financial services to customers with minimal identification and verification and additional services with further identification and verification. By replacing its previous rules-based standards, the FATF partly responded to evidence that its standards could lead to financial exclusion.[24] According to a 2023 World Bank survey of authorities in the financial sector, about half of the responding jurisdictions had implemented standards that permit tiered customer due diligence among commercial banks and nonbank issuers of electronic money.[25] Mexico, for instance, approved a successful tiered scheme for opening deposit accounts in 2011.[26] In the two years following the introduction of an account with simplified requirements for customer due diligence, 9.1 million accounts were opened (of which 77 percent were with simplified requirements), and 2.9 million prepaid cards issued for government programs were replaced with such accounts.

However, a risk-based approach to customer due diligence may fail to apply proportionality and underestimate the impact that financial exclusion has on risks to financial integrity.[27] Using proportionality requires regulatory capabilities that are often lacking in economies most in need of increasing financial inclusion. As a result, countries underuse simplifications and exceptions in this area.

In addition to the adoption of risk-based customer due diligence, investments and innovation in ID systems can ease constraints on financial inclusion imposed by requirements related to customer due diligence. Technology-enabled solutions, such as biometric identification,[28] can significantly lower the compliance costs associated with customer identification and verification.[29] For example, India's rapid growth in account ownership over the past decade has been in part due to a government policy launched in 2014 that leveraged biometric identification cards to boost account ownership among the unbanked.[30]

Standardization in securities markets

Beyond banking, standardization also plays a foundational role in the development of securities markets. By harmonizing terms of securities contracts (such as maturity dates, contract sizes, and settlement conventions), standardization reduces transaction costs, improves price discovery,[31] and lowers barriers for new participants in securities markets. This is particularly important for maintaining market liquidity, as standardized instruments are easier to trade, compare, and value.[32]

A classic example of the power of standardization in securities markets comes from the evolution of the Chicago Mercantile Exchange (CME). In 1964, the CME introduced live cattle futures contracts with precise, uniform specifications: fixed quantities (40,000 pounds), quality grades defined by the US Department of Agriculture (USDA), and designated delivery points. This transformed an opaque, bilateral market into a centralized one with transparent pricing and reliable settlement.[33] The use of standardized contracts enabled CME's clearinghouse to scale efficiently, build trust, and accommodate a growing investor base.[34] As a result, participation in trading of cattle futures and the volume traded grew explosively.

For developing countries seeking to deepen their securities markets, the experience of organized exchanges such as the CME offers several lessons. First, governments often devote significant effort to building sovereign yield curves, issuing bonds at different maturities that serve as reference prices for other securities. Concentrating issuance around a few standardized bonds with fixed maturities and regular calendars for issuance can strengthen this process by channeling liquidity into specific instruments and helping establish a clear benchmark yield curve.[35] Second, early investment in centralized infrastructure for clearing trades can enhance counterparty confidence and reduce reliance on bilateral trading relationships. Finally, simplifying contract terms can attract institutional investors, including foreign participants that face higher costs related to due diligence in opaque markets.

Conclusion

Financial standards are essential for building stable, transparent, and inclusive financial systems. IFRS improve transparency in accounting and attract investment, whereas the Basel Framework enhances banking resilience through requirements regarding bank capital. Similarly, FATF standards strengthen financial integrity but can inadvertently limit financial inclusion; adopting risk-based approaches and digital ID systems helps mitigate these effects.

A common theme in financial standards is that one size may not fit all. To reap the benefits of such standards while maintaining access and inclusion for smaller and lower-capacity market participants, standards development organizations typically implement tiered approaches to application of the standards they develop.

Standardization also supports the development of securities markets by reducing the costs associated with transactions conducted in those markets and improving the markets' liquidity.

Overall, well-designed standards not only safeguard financial systems but also promote broader access to and investment in them, as well as market development, particularly when the standards are adapted to local capacities and needs.

Financial standards offer valuable lessons for current debates on digital assets like stablecoins and cryptocurrencies. The key lesson from IFRS is that transparency and comparability are essential for building trust: Disclosure frameworks for digital assets must reduce opacity in regard to reserves, governance, and risk. From the Basel Framework, the lesson is that prudential safeguards and proportionality are key: Just as rules regarding capital requirements balance resilience with capacity, rules for digital assets must adjust requirements regarding reserves, liquidity, and leverage based on the risks posed by different actors while remaining manageable across jurisdictions.

The FATF's experience shows that integrity standards can foster trust but also pose the risk of exclusion: designing know-your-customer and anti–money laundering procedures for digital assets should incorporate proportionality and technology-enabled solutions for identification to avoid excluding those who most need financial access. And the history of standardization in securities markets teaches us that interoperability and uniformity lower costs and increase liquidity: Standards and settlement protocols for tokens could serve the same purpose for digital finance.

Overall, the main takeaway of the discussion in this spotlight is that standards for digital assets should evolve through adaptation, alignment, and eventual authoring—balancing ambition with compliance capacity—to ensure they protect stability while encouraging innovation. Achieving this will require strong international cooperation.

Notes

1. Refer to FSB (2025).
2. Perera (2024).
3. DeFond et al. (2011).
4. Akpomi and Nnadi (2017); Gordon et al. (2012); Lungu et al. (2017).
5. Calomiris (2012).
6. Aiyar et al. (2015).
7. World Bank (2012, 2020).
8. Goodhart (2011).
9. Ferguson (2003).
10. Jones et al. (2018).
11. BCBS (2022b).
12. World Bank and BCBS (2021).
13. Refer to Behn et al. (2016) on Germany; Fang et al. (2022) on Peru.
14. FSB (2019).
15. Fišera et al. (2025).
16. Gambacorta and Shin (2018).
17. BCBS (2022a).
18. Jiménez et al. (2017).
19. BCBS (2019).
20. For an overview of the history of the current international framework for addressing financial crimes, refer to de Koker and Goldbarsht (2024).
21. FATF (2003).
22. Refer to World Bank (2023) for information about a World Bank survey of documentation requirements among financial authorities around the world.
23. Klapper et al. (2025).
24. Jeník et al. (2024).
25. World Bank (2023).
26. AFI (2011).
27. FATF (2021).
28. Meagher (2019).
29. D'Silva et al. (2019).
30. Demirgüç-Kunt et al. (2022); Sankritik and Shetty (2025).
31. "Price discovery" refers to how trading activity reveals the fair value of securities.
32. Diamond and Verrecchia (1991); Loon and Zhong (2014).
33. Lambert (2010); Paulson (2024).
34. Central clearing of contracts increases the liquidity of the markets for those contracts only when the contracts are sufficiently uniform to allow for opposing positions across counterparties to be more easily offset, thus reducing counterparty risk (Duffie and Zhu 2011).
35. "Bond yield curves" refer to the relationship between bond yields and maturities.

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