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# Financial Technology (FinTech) as a Catalyst for the Growth of Digital Payments

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## Introduction

FinTech, defined as the use of technology to deliver financial solutions, has emerged as a transformative force within the global financial system, significantly reshaping the provision of financial services. FinTech innovations are substantially driving the rapid growth of digital payments, as evidenced by the rapid increase in digital transactions in emerging and developing economies from 55 transactions per adult in 2017 to 251 transactions per adult by 2024 (Fareed, et al., 2025). FinTech firms have introduced a diverse range of innovative payment solutions such as mobile wallets, Quick Response (QR) code-based payment systems, mobile banking applications, internet banking platforms, payment gateways and government led platforms.

## Value Creation Through FinTech Driven Digital Payments

FinTech enabled digital payments significantly reduce reliance on cash and legacy payment infrastructure, while enhancing speed, security, lowering transaction costs, and improving overall convenience for individuals and businesses (BIS,

2018). Further, FinTech enhances the resilience and efficiency of the financial system through increased decentralisation and diversification. By enabling a wide range of digital platforms and service providers, it reduces systemic vulnerabilities, mitigates the impact of financial shocks, and strengthens overall system stability (FSB, 2017).

Notably, FinTech serves as the technological driver of digital payments, which in turn, acts as the principal gateway to global financial inclusion by expanding access to financial services. The expansion of digital connectivity has extensively contributed to the increase in global account ownership<sup>1</sup> from 51 per cent in 2011 to 79 per cent in 2024, driven largely by mobile based financial solutions supported by widespread mobile phone ownership (Klapper, et al., 2025). This in turn promotes financial inclusion among households, Small and Medium Enterprises (SMEs) and supports inclusive and sustainable economic growth (FSB, 2017).

<sup>1</sup> Key indicator of financial inclusion. It indicates individuals' access to formal financial services such as savings, payments and credit.

## Global Models of Digital Payment Ecosystem

Many countries have implemented successful models of FinTech driven digital payment ecosystems. Among peer countries, Fonepay, Nepal's largest interoperable payment network, regulated by the Nepal Rastra Bank, connects over 60 financial institutions, more than 20 million users, and 1.7 million merchants. Highlighting the rapid growth and widespread adoption in Fonepay, the platform exceeded one million daily QR transactions on 30 March 2025, with a total transaction value of Nepalese Rupee 2.62 billion (Anon., 2025). Further, India's Unified Payment Interface (UPI), introduced in 2016, has grown rapidly by significantly reducing reliance on cash. Currently, UPI processes over 18 billion transactions per month through platforms such as PhonePe and other FinTech and Bank mobile applications, surpassing other global electronic payment systems and positioning India as a global leader in fast payments (Copestake, et al., 2025). According to Khurana et al. (2025), digital payment adoption is strongly linked to financial inclusion in India, with 10 per cent increase in adoption resulting in an approximate 7.8 per cent increase in the inclusion index. Further, this study suggests that targeted expansion of UPI enabled banking access<sup>2</sup> in rural areas can considerably narrow the financial inclusion gap. Meanwhile, FinTech adoption in China has resulted in an advanced digital payment ecosystem, evidenced by platforms like Alipay and WeChat Pay, while in Kenya, FinTech solutions based on M-Pesa (M-Mobile, Pesa-Money), the country's leading mobile e-money service, have significantly enhanced financial inclusion and contributed to poverty reduction (Fareed, et al., 2025).

2 Through third party FinTech Apps (PhonePe, Google Pay, Paytm) and Bank Mobile applications.

## Growth of Digital Payments in Sri Lanka

Digital payment adoption in Sri Lanka has progressed notably supported by initiatives and oversight by the Central Bank of Sri Lanka (CBSL), together with FinTech developments through technological advancements. This has reduced reliance on cash and improved access to secure, efficient and cost-effective digital payment solutions. Further, the growth of Sri Lanka's FinTech sector has been accelerated by the expansion of communication infrastructure, particularly high internet penetration (110 per 100 persons) and cellular phone penetration (136 per 100 persons) by the end of 2025, thereby facilitating the country's transition towards a more digital and inclusive financial ecosystem.

Digital payments represent the leading segment within Sri Lanka's FinTech ecosystem. The introduction of the Common Electronic Fund Transfer Switch (CEFTS) in 2015 has been instrumental in enabling real time interbank transactions, underpinning FinTech enabled payment methods such as JustPay, LANKAQR, LankaPay Online Payment Platform (LPOPP), and GovPay, reflecting a significant shift towards instant payments. It enables customers to transfer funds seamlessly across banks using interoperable payment applications, including both FinTech and bank, regardless of the payment service provider. In 2025, CEFTS processed over 260 million transactions with a total value of Rs. 23.1 trillion, equivalent to more than 70 per cent of Sri Lanka's GDP, compared to 15.4 per cent in 2020, highlighting its increasing significance in the retail payments landscape. LANKAQR has enhanced interoperability and enabled low-cost digital transactions across banks and FinTech platforms, benefiting SMEs through an affordable alternative to traditional point of sale infrastructure. Meanwhile, initiatives such as GovPay have

strengthened the digital payment ecosystem by enabling efficient and transparent public service payments. These initiatives thereby expand financial access, particularly among unbanked and underbanked populations. Furthermore, CBSL facilitates FinTech development through its Regulatory Sandbox, which provides a controlled environment for testing and developing new financial technologies, with the aim of enhancing financial system efficiency and advancing financial inclusion.

## Conclusion

FinTech has emerged as a powerful catalyst for the growth of digital payments, transforming traditional financial systems into more efficient, secure, cost effective and inclusive ecosystem, thereby facilitating the transition towards a less cash economy. However, FinTech driven digital payments require well balanced regulatory frameworks and safety mechanisms that mitigate risks related to cybersecurity, enhance consumer protection and data privacy, while promoting interoperability, public-private collaboration, and effective coordination with existing payment infrastructure. Further, addressing infrastructure constraints and financial literacy gaps is critical to strengthening the role of FinTech driven payments in enhancing financial access and supporting sustainable economic growth and financial stability.

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# Getting Too Warm to Ignore: Rethinking Monetary Policy Amidst Climate Change

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## What is Climate Change?

Among a myriad of risks and vulnerabilities faced by both developing and developed nations, climate change is increasingly becoming a major concern for policymakers, general public and academia. Overall, climate change refers to the continued change in temperature, rainfall and wind patterns, and other aspects of the Earth's climate system, owing to a combination of natural and anthropogenic factors. Since the Industrial Revolution, rapid advancements in living conditions of humans have been supported by high natural resource usage, triggering an acceleration in climate change. It has widespread impacts, influencing ecosystems, economies, and societies around the world. The effects of climate change are being felt by countries across the world, regardless of their level of contribution to global carbon emissions.

Climate change is resulting in rising global temperatures and frequent extreme weather events (Thomas, Albert, & Hepburn, 2014) that cause massive economic and social losses. Between 2000 and 2021, a total of 441 extreme weather-related disasters have occurred worldwide, affecting approximately over two billion persons-time cumulatively. These events resulted in over

1.5 million casualties, including around 0.5 million deaths and over one million injuries, and led to the evacuation of about a million people. Furthermore, they caused direct economic losses exceeding US dollars 1.5 trillion (Academy of Disaster Reduction and Emergency Management, 2022). In the context of Sri Lanka, combined average annual loss from natural disasters over the long term is estimated at US dollars 0.4 billion in relation to infrastructure, agriculture housing, and relief (Asian Development Bank, 2021). Climate change induced natural disasters such as floods and storms could damage infrastructure, reducing long term productivity across sectors in the economy, while increasing costs for reconstructions and insurance. Natural disaster-prone economies would face more macroeconomic instabilities due to high inflation, exchange rate depreciation pressures and economic contractions. Further, climate change induced natural disasters and gradual changes in climate conditions could reduce the agriculture sector productivity in the long run. Meanwhile, rising temperatures are permanently transforming ecosystems, threatening the existence of various species of flora and fauna. This, coupled with rising sea levels that erode coastal areas, would threaten tourism and fisheries sectors. Additionally, governments and businesses would be compelled

to spend more on disaster response, insurance, adaptation, and mitigation efforts, thereby diverting limited resources from other productive areas of development. For example, the Government of Sri Lanka had to allocate Rs. 500 billion in relation to disaster relief and recovery expenditure due to Ditwah Cyclone that devastated the country in December 2025. Overall, these factors could dampen economic growth and create uncertainty for markets and livelihoods. Given that low-income households and vulnerable segments in the economy tend to be disproportionately affected by the natural disasters, climate change could exacerbate the inequalities within the population. As climate change-related disasters are becoming increasingly frequent and severe, policymakers including central banks can no longer afford to ignore the challenges posed by climate change.

### **What are the Mandates of Central Banks?**

Central banks are generally responsible to maintain price stability. However, in some instances, achieving economic stability or full employment may also be part of the central bank's mandate<sup>1</sup>. Therefore, central banks need to evaluate how climate change affects inflation, economic growth, interest rates, and the frequency and severity

1. Most central banks are responsible for securing the financial system stability also. In this regard, central banks may be required to monitor and assess the climate change impact on individual financial institution, overall financial system and strengthen the regulatory framework to manage climate risks to ensure financial system stability. Further, the central banks may actively promote climate resilience investments through regulations. However, this article only focuses on the nexus between the central banks' role in price and economic stability and does not cover the financial system stability aspects.

The mandate of the Central Bank of Sri Lanka is to achieve and maintain the price stability while the other objective is to maintain financial system stability. However, while pursuing the price stability objective, the Central Bank of Sri Lanka also need to consider, among other factors, the stabilisation of output towards the potential level.

of climate-related shocks. At the same time, climate-related financial risks can impair asset values and collateral quality, influencing central banks' balance sheets and monetary transmission mechanisms. Therefore, central banks will also have to take into account mitigating climate risks on monetary policy operations. On the other hand, the explicit mandate of few central banks (e.g., Hungary, China, Bangladesh) go beyond the core objective of price stability, requiring them to actively contribute to building climate resilience and transition to a low carbon economy. For such central banks, achieving the secondary goal on climate change without compromising the fulfilment of the core mandate would be a balancing act.

Even if addressing climate change is not an explicit mandate, central banks may nevertheless have to play a role in the transition to low carbon economy given that climate change would possibly challenge the achievement of the price stability mandate through frequent and intense supply disruptions and demand-side shocks. In the event where central banks are mandated with more broader objectives such as fostering economic prosperity, such objectives are construed to comprise climate change related goals. In addition, like many other public and private organisations, central banks may voluntarily opt to address climate change, though it is not a mandate of the entity.

### **Climate Change and Challenges for Monetary Policy**

Climate change creates significant challenges for the achievement of central banks' mandate on price stability, especially under inflation-targeting frameworks. Generally, natural disasters have transitory impact on the inflation and output. Therefore, central banks may choose not to respond to such transitory shocks since their effects

are expected to dissipate over time. However, climate change-induced natural disasters, when frequent and severe, can create persistent supply-side disruptions and lasting effects on potential output due to damages to infrastructure and lower productivity, while weakening the aggregate demand through losses in income and confidence. Distinguishing whether the effects of natural disasters are transitory or persistent, understanding the nature of their demand and supply side impacts, and determining the appropriate timing and magnitude of monetary policy responses remain key challenges for central banks.

Further, regular supply-side disruption could cause higher volatility in food, energy, and other prices, making it more cumbersome for central banks to maintain inflation at the target level or within the targeted range. Recurrent deviations of actual inflation from the target could diminish the credibility of monetary policy and the central bank, thereby de-anchoring inflation expectations.

Climate change complicates the central bank's assessment of its policy space. A central bank's monetary policy stance (i.e., whether the policy is accommodative, neutral or tight) is defined against the 'natural interest rate' (NIR).<sup>2</sup> The climate change can alter the NIR of an economy via various channels such as economic growth, savings behaviour, risk premia and technology, although the magnitude or the direction of the effect is ambiguous (Network for Greening the Financial System, 2020). For example, countries that are frequently affected by natural disasters may have a lower NIR due to lower growth and productivity as well as higher precautionary savings of the

population. On the other hand, investments in climate adaptation policies may raise the NIR. Hence, structural changes arising from climate change may cause the NIR to shift over time. Since the NIR is an unobservable variable that is inherently difficult to estimate, such climate-induced shifts could further complicate central banks' assessment of whether monetary policy is accommodative or restrictive, thereby increasing the risk of policy errors.

Intensified climate change effects could impair monetary policy transmission channels, making monetary policy less effective and the policy outcomes less predictable. Climate change could affect the overall monetary policy transmission through shifts in asset prices, credit conditions, exchange rates, inflation expectations and as well as risk premia. Consequently, the effects of monetary policy on consumption, investment, and inflation may become more difficult to calibrate, particularly due to the non-linear impacts of extreme climate events on the macroeconomy, increasing the risk of policy misjudgements and ineffective policy responses.

Meanwhile, transition policies for combating climate change could adversely affect potential output by disrupting production, lowering productivity, and requiring costly structural adjustments, although the exact magnitude of such effects remains uncertain. Transition measures such as carbon pricing and shifts toward greener technologies could potentially generate additional inflationary pressures, but the extent and persistence of such pressures are still not fully understood. While the transition to greener technologies is often associated with the shift from fossil fuels to low-carbon energy sources, such a transformation could also lead to broader economy-wide changes in relative prices, the composition of economic activity and consumption patterns, as well as

2. The real interest rate that is consistent with stable inflation and full employment is known as the NIR. If the central bank's policy rate is above (or below) the NIR, the money policy stance is considered to be tight (or accommodative).

the energy intensity of production (Lane, 2024). Consequently, the low-carbon transition may result in significant structural transformation across the economy. Therefore, it remains unclear to what extent and how the central banks' monetary policy should respond to such structural transformations in the economy.

In macroeconomic forecasting models, shocks that create temporary disturbances are often treated as risks to the forecast rather than being incorporated into the core forecasting framework, particularly when their effects are expected to be transitory. However, climate change and climate related natural disasters could alter supply and demand conditions in the economy in the short to long term. Hence, there is a growing case for incorporating climate related variables and scenarios into macroeconomic forecasting models, especially in climate vulnerable economies. However, this does not suggest that climate risks necessarily be an integral part of the core forecasting model of the central bank. Rather, climate change may deserve special focus in the macroeconomic framework due to its structural and recurrent nature and its ability to affect the transmission and effectiveness of monetary policy in the short to long term.

Climate change also poses challenges for the implementation of monetary policy operations, as central banks need to mitigate the impact of climate-related risks on their own asset portfolios used in such operations. This concern becomes particularly vital in the case of non-sovereign collateral holdings and asset purchase programmes, where central banks may be more exposed to climate-related financial and transition risks. Physical and transition risks pertaining to climate change could impact the valuation, liquidity, and creditworthiness of financial assets held by central banks. Hence, central banks would require to be equipped with adequate information

and analytical capacity to ascertain climate-related financial risks on its monetary policy operations over a longer time horizon. Although most monetary policy operations are conducted with a focus on relatively short time horizons, certain unconventional monetary policy operations such as asset purchase programmes may expose central banks to longer-term climate risks. From the second half of 2026, the European Central Bank (ECB) plans to safeguard the value of its asset portfolio used for monetary policy operations against climate-related risks by introducing a "climate factor" which will reduce the valuation of carbon-intensive assets pledged as collateral. In addition, stricter haircut requirements will be applied to carbon-intensive assets within the ECB collateral framework, alongside a strategic shift in asset holdings toward sustainability-related bonds and away from bonds issued by corporations with significant carbon footprints.

### **Challenges for Monetary Policy in Supporting Green Transition**

Moving beyond the mandate of achieving low and stable inflation, central banks may incorporate climate considerations into monetary policy operations to actively support the transition towards a greener economy. In this regard, monetary policy tools could be designed to reduce the cost of borrowing for environmentally sustainable sectors and increase borrowing costs for carbon-intensive sectors. For example, central banks may also consider climate-related risk factors when determining minimum reserve requirements (e.g., China). Magyar Nemzeti Bank, the Central Bank of Hungary, has an explicit statutory green mandate. It applies significant discounts on haircuts applicable for eligible green assets that are used as collaterals in monetary policy operations. Moreover, several central banks have adopted green lending operations in their monetary policy

operational activities (China, Malaysia, Japan and Hungary). Such measures could actively encourage the reallocation of financial resources away from carbon-intensive investments towards greener investments, thereby supporting climate transition objectives.

However, striking a balance between core mandate of the central bank and the climate initiative would be a key challenge for the central banks that opt to support green transition through monetary policy operations (Network for Greening the Financial System, 2026). Meanwhile, greening the monetary policy operations, collateral frameworks and asset purchase programmes, could amplify operational complexity of monetary policy, as it requires accurate and timely data, strong technical capabilities, as well as climate risk assessment techniques and methodologies. Further, such measures may also influence the monetary policy transmission mechanism, especially when the credit allocation is primarily shaped by environmental goals instead of macroeconomic considerations. From the financial institutions' perspective, higher compliance and reporting requirements associated with climate-related disclosures and risk assessments would be an added regulatory burden. Meanwhile, preferential treatment for environmentally sustainable sectors may lead to imbalances in the competitiveness across sectors, potentially creating unintended market distortions, especially if sustainable financing taxonomies are ambiguous or inconsistently applied. Hence, central banks need to carefully balance green objectives against the potential risks to practicality, policy effectiveness, financial system efficiency, and market neutrality.

## Conclusion

Against the backdrop of increasingly frequent and severe climate-induced natural disasters and rapid environmental degradation, and as well as growing

adoption of low-carbon transition policies, central banks are increasingly compelled to incorporate climate change considerations into monetary policy formulation and operations. Climate change and transition policies pose a multitude of challenges for the conduct of monetary policy through their impact on inflation, economic growth, policy transmission channels and financial stability. These challenges are amplified by the non-linear effects of extreme climate conditions and structural transformations arising from climate change and low carbon transition policies, creating room for policy errors.

Therefore, central banks may have to move beyond the traditional macroeconomic considerations and examine how climate mitigation and adaptation policies influence overall price levels, relative prices, economic activity, as well as consumption, saving and investment patterns. To this end, central banks may be required to monitor a wide spectrum of indicators, including weather-related data. In addition, they may also need to revisit existing macroeconomic models to better capture the effects of climate change and climate transition, particularly amidst rapid technological changes in relation to the transformation toward a greener economy. As climate risks may also influence the valuation and risk profile of asset portfolios used in monetary operations, it is vital for the central banks to reassess collateral eligibility, asset purchase frameworks, and risk management practices. Overall, central banks are compelled to redefine the conduct of monetary policy by expanding its scope to include climate-related risks and considerations to safeguard macroeconomic stability.

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# Strengthening AML/CFT Supervision of Restricted Dealers in Sri Lanka: Application of FATF Standards

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Restricted Dealers (RDs), including Licensed Money Changers, form an important component of Sri Lanka's foreign exchange framework. Under the Foreign Exchange Act No. 12 of 2017, the Central Bank of Sri Lanka (CBSL) is responsible for authorizing dealers in foreign exchange. While licensed banks operate as Authorized Dealers with full authority to conduct foreign exchange transactions, RDs are permitted to operate within a limited scope, subject to specific terms and conditions.

Although their operational scope is narrower than that of banks, RDs play a vital role in facilitating foreign currency exchange for the public, particularly in tourism-related transactions and small-scale foreign exchange needs. However, the nature of their business particularly its cash-intensive character and involvement in foreign currency transactions exposes the sector to inherent Money Laundering and Terrorist Financing (ML/TF) risks. Accordingly, effective Anti-Money Laundering and Countering the Financing of Terrorism (AML/CFT) supervision is essential to safeguard the integrity of Sri Lanka's financial system.

## International Standards and the Risk-Based Approach

Global AML/CFT standards are set by the Financial Action Task Force (FATF), an intergovernmental body that develops policies to combat ML/TF and proliferation financing. The FATF's 40 Recommendations provide the internationally accepted framework for establishing preventive measures, supervisory mechanisms, enforcement actions, and international cooperation.

A cornerstone of the FATF framework is the Risk-Based Approach (RBA), which requires countries and supervisory authorities to identify, assess, and understand ML/TF risks and allocate resources proportionate to those risks. In practice, this means that supervisory attention is directed more intensively toward institutions or activities that present higher risk.

For RDs, risk factors may include high volumes of cash transactions, exposure to cross-border flows, customers with limited identification documentation, dealings with high-risk jurisdictions, and transactions involving Politically Exposed Persons (PEPs). Supervisors use risk

assessment tools, transaction data, and findings from the National Risk Assessment (NRA) to prioritize onsite inspections, thematic reviews, and follow-up examinations.

### **Core AML/CFT Obligations of RDs**

Supervision of RDs focuses on several key preventive measures aligned with the FATF Recommendations.

#### **1. Customer Due Diligence (CDD)**

CDD is a fundamental control that requires RDs to properly identify and verify their customers before conducting transactions. This includes obtaining reliable identification documents, understanding the purpose of the transaction, and assessing whether the transaction is consistent with the customer's profile.

Enhanced Due Diligence (EDD) must be applied where higher risks are identified particularly for PEPs, high-value transactions, or dealings involving higher-risk jurisdictions. Supervisory examinations assess whether RDs are consistently applying CDD procedures, maintaining accurate documentation, and updating customer information where necessary.

#### **2. Record-Keeping and Audit Trail**

Proper record-keeping enables the reconstruction of transactions for regulatory reviews or investigations. RDs are required to maintain records of customer identification, transaction details, and due diligence measures for the prescribed retention period.

Supervisors evaluate whether records are complete, accurate, retrievable, and securely maintained. Strong documentation practices enhance transparency and support the work of law enforcement and the Financial Intelligence Unit (FIU) when investigating suspicious activities.

#### **3. Suspicious Transaction Reporting**

Timely reporting of suspicious transactions is central to the AML/CFT framework. RDs are required to identify unusual or suspicious patterns such as structuring transactions to avoid reporting thresholds, unexplained high-value currency exchanges, or transactions inconsistent with the customer's known profile and report them promptly to the FIU.

Supervisory reviews assess both the timeliness and the quality of Suspicious Transaction Reports (STRs). Institutions must demonstrate that staff are adequately trained to detect red flags and escalate concerns internally before submission to the FIU.

#### **4. Beneficial Ownership Transparency**

Where customers are corporate entities or operate through complex structures, RDs must identify and verify the Ultimate Beneficial Owners (UBOs). Failure to identify the individuals who ultimately control or benefit from a transaction can allow misuse of legal structures for ML/TF purposes.

Supervisors examine whether RDs collect sufficient ownership information, maintain updated records, and conduct ongoing monitoring to detect changes in ownership or control.

## 5. Internal Controls and Compliance Function

Effective AML/CFT compliance requires more than procedural checklists. RDs must establish internal policies and controls tailored to their risk profile. This includes appointing a compliance officer, conducting institutional risk assessments, implementing transaction monitoring mechanisms, and providing regular staff training.

Supervisory assessments consider whether internal controls are proportionate to the size and complexity of the RD's operations and whether corrective actions are taken when deficiencies are identified.

### Supervisory and Enforcement Framework

Under Sri Lanka's AML/CFT legal framework, supervisory authorities are empowered to conduct examinations and take enforcement action where necessary. Onsite inspections, offsite monitoring, follow-up reviews, and thematic examinations are conducted to assess compliance levels and identify areas for improvement.

Where deficiencies are detected, supervisory authorities may issue warning letters, directives, or impose proportionate and dissuasive sanctions. Enforcement measures may range from corrective instructions and administrative penalties to suspension or revocation of authorization in serious cases of non-compliance.

The objective of enforcement is not merely punitive but corrective ensuring that identified weaknesses are addressed promptly and that systemic improvements are implemented to reduce ML/TF vulnerabilities.

## NRA 2024/2025 – Sectoral Risk Profile

The NRA update for 2024/2025 classifies the RD sector as presenting a **medium–low ML/TF risk**. This rating reflects both inherent vulnerabilities and the mitigating controls currently in place.

Inherent risks stem primarily from the cash-based nature of operations, foreign currency transactions, cross-border exposure, and, in some cases, limited technological infrastructure that may affect transaction monitoring capabilities.

However, the NRA also recognizes significant progress in strengthening sectoral controls. Enhanced supervisory engagement, increased onsite examinations, issuance of supervisory directives, and close monitoring of corrective actions have contributed to improved compliance across the sector. RDs have strengthened customer due diligence procedures, sanctions screening mechanisms, record-keeping practices, and the quality of suspicious transaction reporting.

Collectively, these measures have reduced the residual ML/TF risk, supporting the classification of the sector at a medium–low level.

### The Way Forward

Looking ahead, AML/CFT supervision of RDs will continue to evolve in response to emerging risks and international developments. Strengthening the risk-based approach remains a priority, with greater reliance on data analytics, targeted thematic inspections, and proactive supervisory engagement.

Further improvements in institutional risk assessments, PEP identification processes, sanctions screening, and the quality of STR

submissions will enhance sector resilience. Continued training and awareness programmes will support capacity building within RDs, ensuring that staff remain vigilant to evolving ML/TF typologies.

By aligning supervisory practices with FATF standards and leveraging insights from the NRA, Sri Lanka reinforces its commitment to maintaining a transparent and well-regulated foreign exchange sector. Effective supervision not only mitigates ML/TF risks but also strengthens public confidence, promotes financial stability, and

safeguards the integrity of the national financial system.

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# Open Banking – A Paradigm Shift in Digitized Banking

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## 1. Introduction

The banking sector, like many other industries, has reached a point where the delivery of products and services heavily relies on technology. The main driver for this change is ‘digitization’, which is a socio-technical process of applying digital technology across social and institutional domains (Eaton, Hallingby, Nesse, & Hanseth, 2014). However, digital technology is not a new phenomenon to the banking sector around the world, as banks have been using technology since 1960s when banks started to hold customer accounts electronically. Further digitalization occurred in 1970s when stock markets (NASDAQ) introduced electronic trading and later with the introduction of global communication networks through SWIFT system (Forester, 1985). However, the real ‘paradigm shift’ in digitization of financial services including banking business goes beyond a simple digitalization of customer accounts or stock market or communication to a level which fundamentally changed the financial industry (Currie, & Lagoarde-Segot, 2017) by deeply embedding and integrating digitization in to financial service delivery and business model design (Kazan, Tan, Lim, Sørensen, &

Damsgaard, 2018). Accordingly, this paper articulates one of the contemporary examples for “Paradigm Shift in Digitized Banking” in terms of Open Banking and the underpinning technology of Application Programming Interface (API) and the readiness of Sri Lanka to introduce Open Banking.

## 2. What is Open Banking?

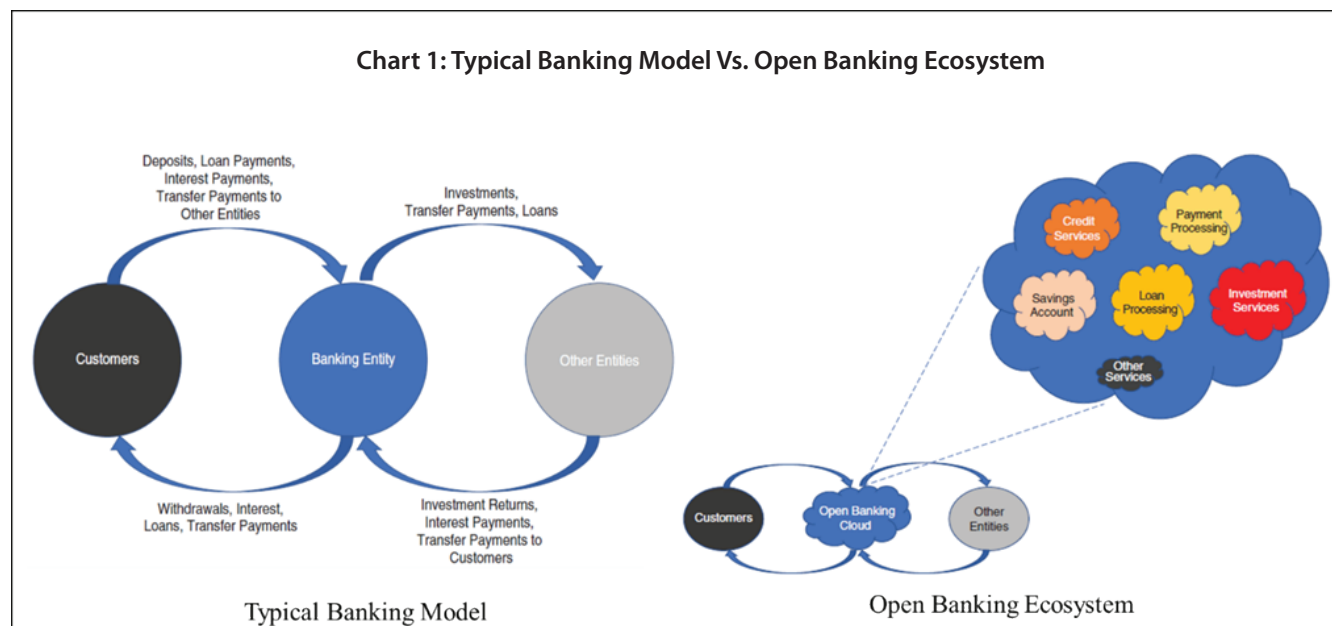
Open banking is a special kind of financial ecosystem that is governed by a set of application interfaces and security profiles. It is a banking model that allows third-party application developers to develop and build applications through the open APIs for improved customer experience and operations. The concept of open banking and the underpinning technology of API converts the impenetrable murky banking business model to a new open and transparent financial ecosystem that provides better choices and information to the participants enabling them to move funds within the ecosystem. As stated by Guibaud (2016), open banking enables banks to redefine their value propositions relating to servicing capabilities and raw data. It empowers individual customers and businesses to share their data with third

parties including other banks, in a secure way and to manage their bank accounts without using their bank (Open Banking, 2017). Open banking enables lenders to access more comprehensive data about borrowers and thereby facilitates a more accurate assessment of credit risk and mitigates adverse selection problems by clearly distinguishing high-risk and low-risk borrowers with the near-perfect information. The modern financial world offers open banking in some form. Countries like Japan, Singapore, Malaysia, India and most of the European Union countries have made noteworthy progress towards open banking. However, as stated by Kim, Hwang, Jae, Jun, & Kwon (2016), open banking does not mean that any outsider (third-party) can access a bank's system at their will. Open banking should be practiced and permitted within a well-articulated and tested regulatory framework in order to preserve security and privacy of customer data.

When comparing open banking with traditional banking system, in a traditional banking

system, banks engage in deposit taking, lending and other authorized financial activities. Banks also facilitate financial intermediation with other entities and participate in the country's payment and settlement systems. On the other hand, in practice, customers of a bank generally interact with more than one financial institution. But moving funds between these entities under the traditional banking system is neither easy nor transparent in most cases. Therefore, customers generally accept the service package offered by their banks without 'mixing and matching' the services offered by different banking entities. For example, a customer may not have a current account with one bank, a savings account with another and credit card with yet another bank, instead may have all these facilities from one bank, mainly due to the difficulties in moving funds between these different accounts and due to the related transaction cost (Farag, Koirala, & McGowan, 2019).

On the other hand, with the open banking ecosystem in place, third-party financial



Source: Laplante, & Kshetri, (2021)

service providers can openly access financial data of customers from banks and other non-bank financial institutions through APIs, with customer consent. Open banking delivers financial services via a form of Software as a Service (SaaS) and the banking cloud (a collection of banks), using compatible APIs (Laplante, & Kshetri, 2021). Therefore, under this ecosystem there is no predefined customer relationship or supply chains of financial products, rather customers execute various transactions by moving funds (debits and credits) between financial entities/ accounts, aggregate information for analysis and set activity threshold via Dashboard Tools, at their discretions (Laplante, & Kshetri, 2021). This enables a cashless economy with digital payments but requires banks to open up their walls and democratize sharing of proprietary data available with them to third parties with the owner's permission to access it. An open banking ecosystem compared to a traditional banking model is graphically illustrated on the above (chart 1).

### 3. Requirements for Open Banking

In order to implement open banking in a country, it requires a legislative enactment, regulatory frameworks, a high-standard cybersecurity framework, API-standards and co-operation of financial entities and consumers. The United Kingdom implemented open banking in the country in 2016 and issued the open banking standards in 2018 defining the following four core requirements for open banking (Open Banking Standards, UK, version 3, 2018).

- (i) API specifications
- (ii) Security Profiles
- (iii) Customer experience guidelines

#### (iv) Operational guidelines

API specifications could be either read/write API specifications, open data API specifications, directory specifications, dynamic client registration specifications or management information reporting specifications. Security profiles could require the customer's interactions with the third party and the API provider on the same device and platform (Redirect) or allow the customer to authorize a request on a different platforms/device at a different time (Decoupled). These security profiles describe the security provisions for financial grade APIs and client-initiated backchannel authentications. Customer experience guidelines explain the processes that customers should follow in an open banking enabled app or website to ensure customer awareness of open banking related risks and rewards. Finally, operational guidelines support the account servicing payment service providers. They are expected to provide a dedicated interface to drive competition and innovation.

### 4. Challenges for Open Banking

Managing the security risk in terms of security of funds and security of personal data and managing the reputation risk are the most significant challenges for the open banking ecosystem. Further, open banking has to operate under a strict and changing regulatory environment and therefore, ensuring compliance with new regulations on the subject matter would become a time and cost intensive process for banks (Brodsky, & Oakes, 2017).

Another major barrier to open banking in many countries is the lack of legislation and regulation to support open banking. Japan amended its

Banking Act in 2018 to facilitate open banking. However, the implementation was made voluntary. Lack of regulations on open banking in the United States created unclarity among market participants relating to compliance requirements. In certain jurisdictions, for example, in India, the government took the lead role in developing digital infrastructure (India Stack) and open banking ecosystem through the implementation of interoperable payment system (unified payment interface – UPI) and a universal digital ID (Aadhaar) which played a key role in the development of open banking in India (Fintechnews, Singapore, 2021).

Prevalence of customer hesitation to share financial and personal data due to security and privacy concerns is another challenge faced by open banking. Customers are reluctant to share financial and personal information as it was viewed by them as more sensitive compared to other forms of data. As per the survey conducted by De Nederlandsche Bank in 2020, only 25% of Dutch customers had shared financial transactions related information with third parties (Laplante, & Kshetri, 2021).

## 5. Specification for a Regulatory Framework for Open Banking

Many banking sector regulators across the world have initiated implementing regulatory framework to regulate open banking. The European Union, the United Kingdom, the United Arab Emirates, India, Australia and Brazil had implemented regulations to facilitate open banking. Based on the regulatory framework implemented by these jurisdictions, the following can be considered as the minimum regulatory standards for Open Banking.

(i) Licensing criteria for providing and

marketing of open banking services.

- (ii) Overarching principles on sound governance, effective risk management, open banking standards, API standards, data and information security specifications for open banking and operational controls relating to customer data, open data and aggregated data.
- (iii) Requirements to implement data access permission Dashboard Tools.
- (iv) Data protection and privacy requirements relating to customer data, open data and aggregated data provided, gathered, shared or processed by financial institutions.
- (v) Customer data processing requirements to ensure security of customer data and protection against unauthorized or unlawful processing of data, or loss, destruction or damage to customer data.
- (vi) Rights and obligations of customers, including rights to provide consent and/or cancel the consent for processing data, rights to modify/ block customer data, right to transfer customer data to another controller and rights to get notified of hacking of data.
- (vii) A fees and charges structure for open banking services.
- (viii) Requirements to implement adequate level of technical, legal, and organizational measures to prevent unauthorized or unlawful access or transfer of customer data.
- (ix) Requirements to ensure appropriate level of security of data classification, sharing,

storing, processing and transmitting of customer data.

- (x) Requirements on consumer protection and ethical business conduct.

## **6. Sri Lanka's Readiness for Open Banking**

### **6.1 Benefits of open banking to Sri Lanka's economy**

Open banking offers many potential benefits to financial consumers, financial institutions and to the overall economy by transforming financial transaction data into a powerful tool to lower financial transaction costs, and greater financial access / inclusion and better financial management. Customers can view their financial transactions from different banks and financial institutions in a single dashboard for clear spending awareness, smarter payment options, fair lending rates and personalized fund management. For businesses, it will help them to lower transaction costs, provide deep visibility into financial health through real-time dashboards and faster access by SMEs to finance. Due to these benefits globally countries like UK, European Union, Japan, Hong Kong and Australia have already introduced open banking. Sri Lanka also can benefit from implementing open banking as it would, along with other digital financial services, contribute to achieve the expected growth in digital economy of Sri Lanka from the current value of around USD 4.5 bn or 3% - 4% of total economy to the expected value of around USD 15 billion by 2030 or 12% of total economy ([digital-economy-blueprint-2026](#)). The key to achieving this success is to build trust in data protection and security through proper regulations considering technological, customer protection and business aspects,

which Central Bank of Sri Lanka (CBSL) along with other stakeholders is in the process of implementing.

### **6.2 Current status and major gaps for implementation of open banking in Sri Lanka**

Currently, implementation of open banking in Sri Lanka is at a developmental stage with a view to promote FinTech innovations in Sri Lanka and to enhance access to finance through financial inclusion ([www.cbsl.gov.lk](http://www.cbsl.gov.lk)). In 2020, CBSL carried out a public consultation to develop an Open Banking Framework for safe financial data sharing. Accordingly, CBSL had requested the relevant stakeholders including banks, other financial institutions, payment service providers, FinTechs, government, non-governmental, multi-lateral agencies and experts in Information Technology, to share their knowledge and experience to help the processes of introducing an Open Banking Framework for Sri Lanka ([A200226 - PSD - Open Banking Framework 2](#)). Currently, in Sri Lanka JustPay which was launched in 2018 and operated by LankaPay (Pvt) Ltd allows bank accounts to be connected to third party apps via verification (JustPay is highly used). Therefore, the focus of a new Open Banking Framework would largely be on account information sharing through secure means. Currently, there are plans to facilitate API based banking and to provide the required regulatory framework to meet future market needs. As open banking evolves in the country, collaboration among banks, fintech companies, and regulators will be crucial to ensure a secure and efficient open banking ecosystem that benefits all stakeholders. However, the following major gaps need to be addressed for the smooth

transition towards open banking in Sri Lanka:

- (i) Many banks and financial institutions still operate on legacy core banking systems which require a substantial capital budget to integrate with modern API standards.
- (ii) Gaps in authentication or security mechanisms as banks and financial institutions still rely on SMS and OTPs for transaction authentication compared to AI driven solutions.
- (iii) Lack of a matured fintech eco system to securely leverage on open data.
- (iv) Lack of a regulatory framework on open banking for Sri Lanka.

In addition, a regulatory framework for open banking is important to ensure a governance framework within which banks, other financial service providers, Fin Tech companies and

Telecommunications companies have to work in order to facilitate advance banking, innovative financial products and sharing of financial data through open APIs in a secure manner. In the meantime, the Ministry of Digital Economy is in the process of developing a strategy for digital financial services advancement in Sri Lanka. However, since most of the data on the development and implementation of open banking and digital financial services in Sri Lanka are currently classified as non-public data, the author expects to write more detailed articles on implementation of open banking and digital financial services in Sri Lanka, in the future.

### 6.3 Proposed Open Banking Implementation Roadmap

CBSL and the Government have already put in action several measures towards the implementation of open banking in Sri Lanka

**Chart 1: Implantation Roadmap Gant Chart – Open Banking**

| Implementation Phases                | Implementation timeline in Months |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
|--------------------------------------|-----------------------------------|---|---|---|---|---|---|---|---|----|----|----|----|----|----|----|----|----|----|
|                                      | 1                                 | 2 | 3 | 4 | 5 | 6 | 7 | 8 | 9 | 10 | 11 | 12 | 13 | 14 | 15 | 16 | 17 | 18 | 19 |
| <b>P1: Strategy &amp; Foundation</b> |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| a) Define Objective & Scope          |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| b) Select API Standards              |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| c) Build the Data Architecture       |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| <b>P2: Build the Technical Core</b>  |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| a) Implement API Gateway             |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| b) Design Consent Management         |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| c) Set Up Sandbox & Developer Portal |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| <b>P3: Governance &amp; Go-Live</b>  |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| a) Establish Operational Framework   |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| b) Phased Rollout                    |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| c) Compliance Validation             |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |
| <b>P4: Feedback Loop (on going)</b>  |                                   |   |   |   |   |   |   |   |   |    |    |    |    |    |    |    |    |    |    |

and the implementation roadmap depends heavily on the regulatory stance of CBSL and the policy stance of the Government. However, generally, the process of implementing a framework for open banking will take around 18 months under several phases. The roadmap should include defining the objective & scope, selecting API standards, building the data architecture, implementing API gateway, designing consent management, setting up regulatory sandbox & developer portal, establishing operational framework, phased rollout, compliance validation and feedback loops.

A proposed implementation roadmap based on the study of implementation roadmaps in the UK and EU is provided in the Gant Chart above.

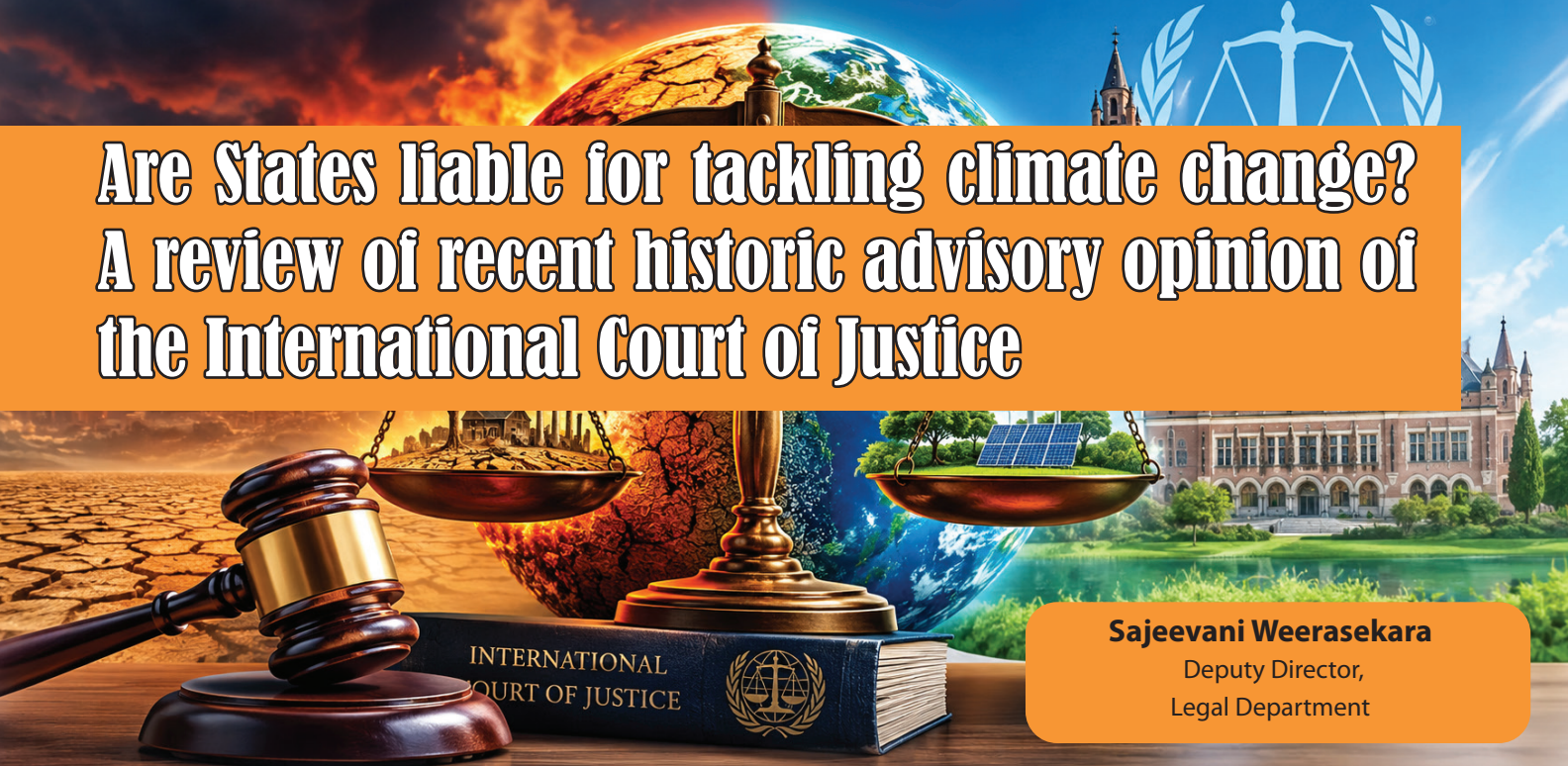
## Conclusion

Open banking is a special kind of financial ecosystem that enables banks to redefine their value propositions relating to servicing capabilities and raw data. It allows third-party application developers to develop and build applications through the open APIs, empowers customers to share their data with third parties including other banks in a secured way, facilitates a more accurate assessment of credit risk and mitigates adverse selection problems for financial institutions. However, open banking should be practiced and permitted within a well-articulated and tested regulatory framework in order to preserve security and privacy of customer data. Countries around the world offer open banking in some form, while certain countries have already implemented regulatory framework for open banking whereas many other countries are in the process of developing regulations to facilitate open banking. In Sri Lanka implementation of open banking is at

a developmental stage and a number of payment apps and infrastructures are being operated (JustPay is highly used). Certain legacy issues coupled with a lack of matured fintech eco system and a full fledged Open Banking Framework are the major challenges currently face by Sri Lanka to implement a full-scale open banking eco system and a standardized API. However, currently CBSL, along with other relevant stakeholders including the Government has already put in action several measures towards the implementation of open banking in Sri Lanka.

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# Are States liable for tackling climate change? A review of recent historic advisory opinion of the International Court of Justice

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## Introduction

The impact of climate change is now visible in every aspect of human lives, livelihoods, environment, and global economy more than ever. People all over the world face many challenges in protecting even their basic human rights due to food insecurity, water scarcity, health crises, and forced displacement. Developing countries are more prone to such climate related issues, which aggravate their social and economic vulnerabilities. In this context, the role of law and order within the State carries a significant responsibility in ensuring justice through institutional accountability, good governance, effective regulation, and the equitable enforcement of climate-related laws. This, in turn, requires States to adopt appropriate legislative, administrative, and enforcement measures to address environmental harm and climate change.

July 23, 2025, marks a remarkable day in history as the International Court of Justice (ICJ) delivered its long-awaited landmark advisory opinion on the obligation of States concerning climate change

under international law. In this opinion, the ICJ determined that the 1.5°C temperature target is legally binding under the Paris Agreement and that all States, in particular the largest emitters, must take ambitious mitigation measures in line with the best available science. This case is a significant milestone in International Law and climate change actions worldwide. Another important aspect of the advisory opinion is that it imposes legal duties on States to prevent “transboundary environmental harm,” with precaution, and take due diligence measures to reduce greenhouse gas (GHG) emissions and adapt to the adverse impacts of climate change (IISD, 2025). Although Sri Lanka’s contribution to global greenhouse gas emissions remains relatively small, both in absolute and per capita terms, the country is disproportionately exposed to the adverse impacts of climate change. Therefore, the significance of the advisory opinion for Sri Lanka lies not only in clarifying the obligations of States with respect to climate action, but also in reinforcing the responsibilities of major emitting countries whose actions have transboundary consequences

for climate-vulnerable nations. In this regard, the opinion provides an important legal and normative framework through which countries such as Sri Lanka may advocate for greater global accountability, enhanced mitigation efforts, and stronger international cooperation in addressing climate change. Further, while the opinion primarily focuses on the conduct of States, it further observes the responsibilities of institutions and corporate actors too, given their contribution to global emissions. In delivering its unanimous opinion, the Court described climate change as an ‘urgent and existential’ threat. As it explained the State’s international law obligations, the ICJ elaborated that States have a duty to prevent significant harm to the climate system by exercising due diligence and using all means at their disposal to prevent activities carried out within their jurisdiction or control from causing said harm. The Court further emphasized that breaches of ‘any of the obligations’ identified in the Opinion could potentially constitute an internationally wrongful act and thereby potentially engage the international responsibility of the State concerned (McVey & Savaresi, 2025).

Even more significantly, the Court mentioned that States’ obligations pertaining to the protection of the climate system and other parts of the environment from anthropogenic GHG emissions, in particular the obligation to prevent significant transboundary harm under customary international law, are owed *erga omnes*. This means that all States or all State parties, depending on the international legal provisions invoked, have a legal interest in ensuring compliance, thereby entitling them to invoke the responsibility of other States that fail to meet these obligations (ICJ, 2025; McVey & Savaresi, 2025).

Hence, being an apex institution in economic policy and the regulator and the prudential authority of the financial sector, it is critical for the Central Bank to be cognizant of such significant advisory opinion and the obligations imposed on States, given the increasing relevance of climate-related risks to both price stability and financial system stability.

Against this backdrop, this article pursues to highlight the scope and content of States’ climate obligations under international law, with particular emphasis on the corresponding responsibilities of State institutions, including central banks and financial regulators, in order to prevent regulatory and policy failures that may amount to State non-compliance with international climate obligations.

## 2. Background

This remarkable advisory opinion is a result of a small initiative of 27 law students at the University of the South Pacific, who came together in 2019 and started a campaign to persuade the leaders of the Pacific Islands Forum to bring the issue of climate change and its impact on human rights before the ICJ (PISFCC, 2025). Being inhabitants of low-lying, climate vulnerable island States which are affected by extreme climate situations such as sea level rise, cyclones, and coastal erosion, the group of students has adequate evidence to believe that climate change is not a distant problem but a current existential threat. Hence, their small initiative later spread to more than 100 supporters across the Pacific. As a result of their unwavering actions, in 2022 Pacific Island Forum decided to request an advisory opinion from the ICJ on the obligations of States on climate change and its impact on human rights. In 2023, supporters of the campaign brought the matter to the United

Nations General Assembly (UNGA) to pass it as a resolution of the UNGA. Accordingly, after three rounds of negotiation UNGA unanimously adopted Resolution 77/276 calling on the ICJ to issue an advisory opinion on the obligations of the State. The proceedings of ICJ comprise several rounds of written submissions and oral hearings. During those proceedings, 96 States and 11 international organizations made their oral submissions to the ICJ (PISFCC, 2025). On 23 July 2025, the court delivered the historic advisory opinion on Obligations of States in respect of climate change, which is an extraordinary advisory opinion of the ICJ in recent years and years to come.

The ICJ's motivation for considering the request made in accordance with Article 96 of the Charter of the United Nations, to request the ICJ, is based on the following reasons;

- ICJ was convinced that the threat of climate change on small islands like Vanuatu, the Pacific, Caribbean, and elsewhere, on developing countries, due to rising seas, stronger storms, frequent cyclones, etc., is exponential. It is a threat to the livelihood of people and the sovereignty of countries. However, such small nations are not the major emitters of GHG (ICJ,2025).
- Gaps in the existing legal framework, including climate treaties, such as the Paris Agreement under the UN Framework Convention on Climate Change (UNFCCC), which are important; has many deficiencies. Further, ICJ acknowledged that the obligations should be interpreted more broadly within the international law framework, including principles such as transboundary environmental rights, human

rights, and States obligations on precaution and due diligence therein (ICJ,2025).

- As a number of supporting States and other activists believe climate change is not just an environmental or technical problem, but it is a justice issue, as many consequences of high emission is not faced by countries that emit high GHG, but all other States. Hence, emitters should be responsible towards damaged nations (ICJ, 2025).

The ICJ decided to consider this important matter under international law and human rights law framework particularly with regard to the Charter of the United Nations, the International Covenant on Civil and Political Rights, the International Covenant on Economic, Social and Cultural Rights, the United Nations Framework Convention on Climate Change, the Paris Agreement, the United Nations Convention on the Law of the Sea, the duty of due diligence, the rights recognized in the Universal Declaration of Human Rights, the principle of prevention of significant harm to the environment and the duty to protect and preserve the marine environment (ICJ,2025).

Accordingly, such treaties, conventions, and declarations were considered by the ICJ with regard to the following aspects.

- (a) What are the obligations of States under international law to ensure the protection of the climate system and other parts of the environment from anthropogenic emissions of greenhouse gases for States and for present and future generations?
- (b) What are the legal consequences under these obligations for States where they, by their acts and omissions, have caused significant harm

to the climate system and other parts of the environment, with respect to:

- (i) States, including, in particular, small island developing States, which, due to their geographical circumstances and level of development, are injured or specially affected by or are particularly vulnerable to the adverse effects of climate change?
- (ii) People and individuals of the present and future generations affected by the adverse effects of climate change (ICJ,2025).

In considering the above aspect in arriving at its ultimate decision, the ICJ has taken into account both scientific evidence and relevant laws and other legal instruments relating to climate change, environmental protection, and human rights.

### **3. Scientific considerations of ICJ**

Other than the legal framework, which comprises many local and international treaties, conventions, and statutes, the science behind the climate change phenomenon is also being considered for the opinion. Accordingly, the scientific aspects of the following scenario were considered: an increase in GHG in the atmosphere, which disrupts the solar radiation, is the main offender of the global warming phenomenon, leading to broader climate change around the world. While GHG emission is not only caused by human activity, it is scientifically established that the increase in concentration of GHGs in the atmosphere is mainly due to human activities, such as the burning of fossil fuels, and weakening or destruction of carbon reservoirs and sinks, such as forests and the ocean, which store or remove GHGs from the atmosphere. Consequently, the changing climate affects both

the natural environment and human populations. Primarily, rising temperatures are causing the melting of ice sheets and glaciers, leading to sea level rise and threatening coastal communities with unprecedented flooding. Further, extreme weather events, such as hurricanes, droughts, and heatwaves, are becoming more frequent and intense, devastating agriculture, displacing populations, and exacerbating water shortages. Moreover, the disruption of natural habitats is pushing certain species toward extinction and leading to irreversible loss of biodiversity. Human life and health are also at risk more than ever before. It reflects the increased number of incidences of heat-related illnesses and the spread of climate-related diseases, etc. (ICJ, 2025).

Accordingly, the Court held that, in determining the issue, scientific considerations should be treated as an essential component, operating in tandem with the legal analysis. This study mainly focuses on the legal aspect considered by the ICJ in this historic opinion.

### **4. Applicable International Treaties and Laws**

In identifying the applicable laws, the ICJ recognised the relevance of a wide-ranging body of international instruments extending beyond the climate treaties. Among others, three main treaties were considered by the courts, namely the United Nations Framework Convention on Climate Change (UNFCCC), the Kyoto Protocol, and the Paris Agreement. While the UNFCCC sets out the ultimate objective, basic principles, and general obligations of States in respect of climate change, the Kyoto Protocol and the Paris Agreement translate these basic principles and general obligations into a set of more specific interrelated obligations of States.

Other than that, the ICJ considered the United Nations Convention on the Law of the Sea and the treaties relevant to the ozone layer and biodiversity. In addition, customary international law and international human rights are considered as other applicable laws. By doing so, the Court explicitly rejected the *lex specialis* (specific law overrides a general law on the same subject) argument put forward by some parties in the proceedings, and hence an array of laws was considered broadly for the advisory opinion.

#### **4.1 Considerations under the United Nations Framework of the Convention on Climate Change (UNFCCC)**

The ultimate objective of UNFCCC is to achieve “... stabilisation of greenhouse gas concentrations in the atmosphere at a level that would prevent dangerous anthropogenic interference with the climate system” (Article 2, UNFCCC).

The Court observed that the UNFCCC establishes an obligation for parties to cooperate in different fields, such as

- i. the conservation and enhancement, as appropriate, of sinks and reservoirs of all greenhouse gases, including biomass, forests and oceans as well as other terrestrial, coastal and marine ecosystems.
- ii. adaptation to the impacts of climate change.
- iii. scientific, technological, technical, socioeconomic, and other research.
- iv. exchange of relevant scientific, technological, technical, socioeconomic and legal information.
- v. education, training and public awareness related to climate change.
- vi. facilitating public participation in addressing

climate change and its effects and developing adequate responses (ICJ,2025).

The rationale for cooperation in the UNFCCC may be found in the treaty’s preamble, which provides that “the global nature of climate change calls for the widest possible cooperation by all countries and their participation in an effective and appropriate international response” (UNFCCA, 2008).

Further considering this convention, the Court highlighted that the Framework of Convention provides for certain obligations for developed country Parties and other Parties to provide financial assistance, technology transfers, and other forms of support to developing country parties, especially those countries that are particularly vulnerable to the adverse effects of climate change, to assist them in meeting their commitments under the UNFCCC. Accordingly, the court recognized the importance of such actions by States in order to minimize the impact of climate change, and it induced the phenomenon in least developed and developing countries (ICJ, 2025).

#### **4.2 Considerations under the Kyoto Protocol**

Following UNFCCC, the Kyoto Protocol was established in 1997 to pursue the objectives of UNFCCC, especially to “quantified emissions limitation and reduction commitments”, within specified “commitment periods”. Accordingly, it included quantified emission limitations and reduction commitments for certain States and has agreed on two commitment periods (2008-2012 and 2013-2020). However, no further commitment period after 2020 has been agreed upon, which was one concern of the activists and the court.

In the absence of such a commitment period after 2020, several participants submitted that the Kyoto Protocol is no longer relevant and need not

be addressed by the Court in these proceedings. However, the Court noted that the absence of a new commitment period does not deprive the Kyoto Protocol of its legal effect. Accordingly, the Court emphasized that the Kyoto Protocol remains in force and its provisions may still serve as, *inter alia*, (i) interpretative aids for the identification of obligations under the climate change treaty framework and (ii) substantive provisions to assess the compliance of parties with applicable emission reduction targets. Therefore, non-compliance with emission reduction commitments by a State may constitute an internationally wrongful act (ICJ,2025).

#### **4.3 Considerations under the Paris Agreement**

The Paris Agreement was adopted in 2015 by the UNFCCC to pursue the Convention's objective of "strengthening the global response to the threat of climate change" by enhancing the implementation of the Convention.

The ICJ notes that it sets a goal of limiting the global average temperature increase to well below 2°C above pre-industrial levels, with 1.5°C as an additional target. Most importantly, it provides for "nationally determined contributions" to the global response to climate change by all States. These three frameworks complement each other. The ICJ determined that the 1.5°C temperature target is legally binding under the Paris Agreement and that all States, in particular the largest emitters, must take ambitious mitigation measures in line with the best available science.

The ICJ (2025) also notes that the Paris Agreement contains several obligations of conduct and result, which are mutually supportive, noting that compliance with obligations of conduct under the Paris Agreement is assessed on the basis of

whether the party in question has exercised due diligence and employed best efforts by using all the means at their disposal in the performance of that obligation.

While UNFCCC creates the ultimate objective, basic principles and general obligations of States in respect of climate change, the Kyoto Protocol and the Paris Agreement translate these basic principles and general obligations into a set of more specific interrelated obligations of States (ICJ,2025).

#### **5. Obligations of States under the customary International Law relating to climate change**

The applicability and relevancy of customary international law were considered by the ICJ. In view of that, the court broadly considered the following customary law principles in delivering this historic advisory opinion.

- (a) the duty to prevent significant harm to the environment and
- (b) the duty to cooperate for the protection of the environment.

##### **(a) Duty to prevent significant harm to the environment**

The duty to prevent significant environmental harm is one of the important principles under customary international law that obligates States to use due diligence to stop activities that harm the climate and environment within their jurisdiction. The following cases decided before the ICJ considered that principle.

##### *i. Pulp Mills on the River Uruguay (Argentina v. Uruguay), I.C.J. 2010*

In this case ICJ Stated that “State is . . . obliged to use all the means at its disposal in order to avoid activities which take place in its territory, or in any area under its jurisdiction, causing significant damage to the environment of another State”. Further, the Court recognized that the duty to prevent significant harm to the environment is not limited to instances of direct cross-border harm and that it applies to global environmental concerns. Therefore, the customary duty to prevent significant harm to the environment also applies with respect to the climate system and other parts of the environment.

That judgement further Stated that the duty to prevent significant harm to the environment is an obligation to act with due diligence. Accordingly, the advisory opinion has considered several aspects of due diligence (ICJ,2025).

- (i) Taking appropriate measures, including, but not limited to, regulatory mitigation mechanisms that are designed to achieve reductions of GHG emissions, which is critical for the prevention of significant harm to the climate system.
- (ii) Making available the scientific and technological information and the necessary analysis of such information
- (iii) Standards which may arise from binding and non-binding norms but may also be reflected in certain decisions of the governing bodies of these treaties, which are the Conference of the Parties (COP) to the climate change treaties and in recommended technical norms and practices, as appropriate.
- (iv) Taking necessary actions at their disposal to protect the climate system in accordance

with their capabilities and available resources, even by less developed nations.

- (v) Providing scientific information regarding the probability and the seriousness of possible harm.
- (vi) Avoiding delays in taking actions of prevention in the face of scientific uncertainty.
- (vii) Timely assessment by States of the risks and impact of proposed activities contributing to GHG emissions to be undertaken within their jurisdiction or control, on the basis of the best available science.
- (viii) Coordination with other States by notifications and consultation in good faith about planned activities within their State and make collective efforts to address harm to the climate system, such as the implementation of policy changes in relation to the exploitation of resources linked to GHG emissions (ICJ,2025).

## ***ii. Corfu Channel (United Kingdom v. Albania), I.C.J. 1949***

The **Corfu Channel case** (French: Affaire du Détroit de Corfou) was the first public international law case heard before the ICJ between 1947 and 1949, concerning State responsibility for damages at sea (ICJ,2025).

The Court expressed the “no-harm principle” that States must not knowingly allow their territory to be used for acts contrary to the rights of other States. This principle forms the basis for the broader customary duty to prevent significant environmental harm, including in contexts like climate change.

## ***iii. Bosnia and Herzegovina v. Serbia and Montenegro, Judgement***

In this case, the ICJ considered that due diligence of States includes “calls for an assessment in concreto” of what is reasonable under the specific circumstances in which a State finds itself. This does not mean avoiding the identification of a required standard of conduct at a general level, depending on the overall risk to the environment. Further, the court emphasized that, due diligence “involves not only the adoption of appropriate rules and measures, but also a certain level of vigilance in their enforcement and the exercise of administrative control. As concerns on climate change require an amplified degree of attentiveness and prevention (ICJ,2025).

#### ***iv. Legality of the Threat or Use of Nuclear Weapons, Advisory Opinion, I.C.J. 1996***

In this opinion ICJ establishes that the obligation extends beyond direct, transboundary harm and applies to global environmental concerns, supporting its application to climate change despite the fact that in previous occasions ICJ established the existence of a general obligation for States to ensure that activities within their jurisdiction do not cause environmental harm to other States or to areas beyond national jurisdiction. These judgements were considered strongly when issuing current historical opinion (ICJ,2025).

#### **(b) Duty to co-operate for the protection of the environment**

The duty to cooperate with international counterparties is recognized by Article 1 of the Charter of the United Nations, which is an essential principle to ensure commitments of States to work together to solve economic, social, cultural, and humanitarian problems. This establishes the foundational principle that

cooperation is a general obligation of States. Further, Principle 24 of the Stockholm Declaration and Principle 7 of the Rio Declaration, which are foundational environmental instruments, also affirm that international cooperation is essential for environmental protection. These principles reinforce and express general State practice regarding environmental cooperation. Further, the Climate Change Advisory Opinion in 2024, the International Tribunal for the Law of the Sea (ITLOS) also recognized that climate change is part of international law in the environmental context. Similarly, in another instance, ITLOS emphasized that States have a duty to co-operation through information exchange, notification, and consultation in environmental matters.

In the current advisory opinion, the Court identified that the duty to cooperate leaves States some discretion in determining the means for regulating their GHG emissions. However, it further Stated that this discretion cannot serve as an excuse for States to refrain from cooperating with the required level of due diligence (ICJ,2025).

#### **6. Obligations of States under the Law of the Sea**

The ICJ recognized that anthropogenic GHG emissions qualify as marine pollution under the United Nations Convention on the Law of the Sea (UNCLOS) in this landmark advisory opinion. Hence, the Court declared that not only the law of the land but also the law of the sea imposes strict obligations on States. Accordingly, the court Stated that under Article 192 of UNCLOS, which is the duty to protect the marine environment and take all necessary measures, and under Article 194, which is taking measures to prevent, reduce, and control GHG-related pollution of the marine environment,

States must protect and preserve the marine environment. When doing these, States should be guided by due diligence, use the best available science and relevant international standards, and apply such measures to all activities.

Further, it is required to cooperate continuously under Articles 197, 200, and 201 of the UNCLOS by developing rules, sharing information, and promoting scientific research on climate impacts. Article 206 further obliges States to conduct environmental impact assessments when planned activities emitting GHGs may significantly harm the marine environment, including areas beyond national jurisdiction (ICJ, 2025).

## **7. Obligations of States under the Human Rights Law**

The protection of the environment and the protection of human rights have generally been recognised as interdependent since at least the Stockholm Declaration of 1972. The ICJ acknowledged that States have obligations under international human rights law to respect, protect, and ensure the enjoyment of human rights of individuals and peoples. Human rights are focused on the protection of individuals and peoples and are not limited to specific fields of activity. In order to respond to the questionable consequences of climate change, the Court first considered the adverse effects of climate change on the enjoyment of human rights. The Court then addressed the question of the right to a clean, healthy, and sustainable environment as a human right. In light of these considerations, the Court decided on obligations of States under international human rights law to protect the climate system and other parts of the environment.

During the proceedings, the court highlighted the preamble to the Paris Agreement.

*“climate change is a common concern of humankind, Parties should, when taking action to address climate change, respect, promote and consider their respective obligations on human rights, the right to health, the rights of indigenous peoples, local communities, migrants, children, persons with disabilities and people in vulnerable situations and the right to development, as well as gender equality, empowerment of women and intergenerational equity” (ICJ,2025).*

It proves interrelationship between human rights obligations and rules concerning the protection of the natural environment is complementary in nature. In light of the above, the Court considered that the core human rights treaties, including the International Covenant on Economic, Social and Cultural Rights (ICESCR) and the International Covenant on Civil and Political Rights, and the human rights recognized under customary international law, form part of the most directly relevant applicable law for the particular judgement.

## **8. Other applicable principle**

### **a. Sustainable development**

The Court further determined whether certain other principles are part of the applicable laws for the present Advisory Opinion. Participants of the Advisory Panel importantly considered that the Court should address the principles of sustainable development, given that climate change is directly connected to unsustainable practices and attaining Sustainable Development Goals (SDG) has now become one of the key priorities of States (ICJ,2025).

In a previous judgement on Gabčíkovo-Nagymaros Project (between Hungary and Slovakia) Judgement, I.C.J. Reports 1997, p. 78, para. 140) the ICJ acknowledged that the principle of sustainable development concerns the “need to reconcile economic development with protection of the environment”. In addition, the climate change treaties such as Article 3 of UNFCCC, Paragraph 4 of Kyoto Protocol, and Article 2 of Paris Agreement describe sustainable development as a “principle” by which “the Parties shall be guided” in their actions to achieve the objective of the Convention and to implement its provisions (ICJ, 2025). Given its continuous and uncontested universal recognition, the Court considers that the principle of sustainable development guides the interpretation of certain treaties and the determination of rules of customary international law, including the duty to prevent significant harm to the environment and the duty to co-operate for the protection of the environment. Under these obligations, the Court emphasized the importance of proper risk assessment including environmental risk assessments, and other procedural activities that need to be fulfilled in order to avoid significant adverse impact in a transboundary context. Hence, the States and entities of States have an obligation to ensure sustainable development under their policies and actions.

## **b. Intergenerational equity**

Intergenerational equity is an expression of the idea that present generations are trustees of humanity tasked with preserving honoured living conditions and transmitting them to future generations. As per Article 3 of the UNFCCC “the Parties should protect the climate system for the benefit of present and future generations of humankind, on the basis of

equity”. Further, as per the preamble to the Paris Agreement, “climate change is a common concern of humankind, parties should, when taking action to address climate change, respect, promote and consider their respective obligations on . . . intergenerational equity”.

Furthermore, the IPCC has highlighted that the effects of global warming will cut across generations by noting that continued emissions will further affect all major climate system components, and many changes will be irreversible on centennial to millennial time scales and become larger with increasing global warming. Without urgent, effective, and equitable mitigation and adaptation actions, climate change increasingly threatens ecosystems, biodiversity, and the livelihoods, health, and well-being of current and future generations (high confidence) (IPCC, 2023).

The ICJ expressed that intergenerational equity should be considered as a manifestation of equity in the general sense, and it should play a vital role in deciding matters in relation to climate change. Hence, due regard for the interests of future generations and the long-term implications of conduct are equitable considerations that need to be taken into account where States decide on and implement policies and measures in fulfilment of their obligations.

## **9. In what ways can States fail to comply with their obligations?**

As explained in this article, States have a significant responsibility to ensure that they have taken all necessary steps to comply with the limits imposed by international climate change treaties, customary international law, law of the sea, and international human rights law, etc. As clarified in

this remarkable advisory opinion, States may fail to comply with their obligations in numerous ways, including through acts or omissions. Such failures may arise where States do not adopt adequate legislative, regulatory, or policy measures to prevent or mitigate climate harm, disregard best available scientific evidence in decision making, or delay necessary action despite the foreseeable and serious risks posed by climate change. Noncompliance may also occur where States fail to regulate private actors under their jurisdiction, neglect their due diligence obligations, or pursue development policies that undermine sustainable development and human rights. Ultimately, these shortcomings collectively amount to a breach of both environmental and human rights obligations under international law. Crucially, the Court asserted that a State's failure to take appropriate action to protect the climate system, including through fossil fuel production and consumption, the granting of fossil fuel exploration licences, or the provision of fossil fuel subsidies, may constitute an internationally wrongful act attributable to that State. In this regard, the wrongful act lies not in the emission of greenhouse gases itself, but in the failure to regulate, an interpretation fully consistent with the ICJ's established jurisprudence on environmental harm.

In addition, States such as the United States, which have at times declined to ratify or have withdrawn from specific climate treaties, raise important questions regarding the scope of international legal obligations. While such States may not be bound by treaty-specific commitments during periods of non-participation, this Advisory Opinion clarified that obligations to protect the climate system arise not only from treaties but also from customary international law and general

principles of international law, which apply to all States irrespective of treaty membership (ICJ, 2025). In particular, the duty to prevent significant transboundary environmental harm and the obligation of due diligence bind all States equally (ICJ, 2025; American Society of International Law, 2025). Accordingly, even non-parties to climate treaties are required to ensure that their conduct is consistent with these overarching legal obligations, and failure to do so may still engage international responsibility (Voigt, 2025; The Guardian, 2025).

Furthermore, acts of the State include the conduct of State institutions. Hence, the actions or omissions of policymakers, central banks, financial regulators, and other public authorities entrusted with the formulation and implementation of macroeconomic and prudential policies may have direct or indirect implications for climate outcomes. In this context, the responsibility and accountability of central banks, as apex institutions in macroprudential regulation and economic policymaking, extend to the integration of sustainable development and green central banking principles within their mandates. Such considerations are becoming progressively relevant alongside other policy objectives, particularly as climate change mitigation and adaptation gain prominence under international law, in areas relating to financial stability, systemic risk, and long-term economic resilience.

In general, central banks worldwide are increasingly recognising the implications of climate change for the achievement of their core mandates, particularly in relation to price stability, financial stability, and the resilience of the financial system. While the extent of formal incorporation

of climate considerations into statutory mandates varies across jurisdictions, a growing number of central banks have begun to address climate-related financial risks through their existing supervisory, regulatory, and policy frameworks. In this regard, the Central Bank of Sri Lanka has also undertaken a range of initiatives, including the development of a Sustainable Finance Roadmap and a Green Finance Taxonomy, aimed at strengthening the capacity of the financial sector to manage environmental and climate-related risks (CBSL, 2019; CBSL 2022; Financial Stability Board, 2021). Although most central banks around the world do not yet explicitly recognise climate change as a standalone mandate, they are increasingly acknowledging the importance of preparing economic and financial systems for climate-related risks and supporting the transition to a low-carbon economy. Consequently, climate-related actions are increasingly being undertaken within existing legal and policy frameworks, reflecting an evolving global consensus on the need to address the economic and financial implications of climate change.

In addition, beyond central bank a wide range of climate-related policy and regulatory actions are being undertaken by the government and other financial sector authorities as part of a broader whole-of-economy response to climate change. Accordingly, other key institutions within Sri Lanka's financial sector, including the Securities and Exchange Commission of Sri Lanka, have introduced guidelines, requirements, and regulatory initiatives relating to sustainable finance, particularly in the areas of ESG reporting, climate-related disclosures, and sustainable investment practices, aimed at enhancing market transparency, strengthening investor confidence, and mobilising

sustainable investment (SEC, 2023). In addition, fiscal authorities and line ministries play a central role in implementing climate-related incentives, public investment programmes, and carbon-related policy instruments. At the national level, the government of Sri Lanka is increasingly integrating climate objectives into development strategies, including Nationally Determined Contributions (NDCs), climate adaptation plans, and sectoral policies aimed at reducing emissions and enhancing resilience. Taken together, these initiatives suggest that, as a small island developing nation highly vulnerable to the impacts of climate change, Sri Lanka has taken important steps towards fulfilling its climate-related responsibilities through legal, regulatory, and policy measures across various sectors. However, the effectiveness of these efforts depends on stronger coordination and a more integrated approach among financial sector regulators, government institutions, and other relevant stakeholders. Such coordination is essential to ensure policy coherence, avoid regulatory fragmentation, and enhance the country's capacity to address climate-related risks and support sustainable development objectives (OECD, 2020; NGFS, 2021).

## 10. Conclusion

The ICJ Advisory Opinion dated 23<sup>rd</sup> July 2025 marks a milestone in the history of international law. The advisory opinion offers numerous important considerations as to why climate change should be a priority for States. The Opinion clearly establishes that States have detailed and concrete legal obligations under international law to address the climate crisis. It further acknowledges the importance of adhering to obligations stipulated under international treaties in relation to climate

change.

Accordingly, the advisory opinion considered that the obligations of States under international law to ensure the protection of the climate system and other parts of the environment from anthropogenic emissions of greenhouse gases for States and for the benefits of both present and future generations, and legal consequences under these obligations for States where they, by their acts and omissions, have caused significant harm to the climate system and other parts of the environment,

Moreover, the applicability and relevancy of customary international law were considered by the ICJ. In view of that, the court broadly considered the duty to prevent significant harm to the environment and the duty to cooperate for the protection of the environment.

The advisory opinion further elaborated the interconnectedness between customary international environmental laws and international human rights law. It provides one of the most convincing articulations of the essential relationship between the protection of the climate system and human rights, which go hand in hand. However, the ICJ's Opinion also highlights the structural limitations of international law and of its judicial function when confronted with the scale and complexity of the climate crisis. Most importantly, the Court recognises that climate change is a global, urgent threat affecting all life and the health of the planet. This problem is so vast and complex that courts alone, even international courts, cannot resolve it, highlighting the need for action by States, policymakers, and other actors worldwide.

Accordingly, while the integration of climate-

related considerations into macroeconomic and financial governance frameworks is increasingly recognised as an important dimension of responsible State conduct within the evolving landscape of international law, Sri Lanka, as a small island developing nation particularly vulnerable to the impacts of climate change, has undertaken a range of measures aimed at strengthening climate resilience, supporting sustainable development, and addressing climate-related economic and financial risks. In this context, key institutions including the Central Bank, operating within the scope of their mandates, are well-positioned to contribute constructively to broader national and international efforts aimed at strengthening financial stability, addressing systemic climate related risks, and advancing long-term economic resilience and sustainable development.

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