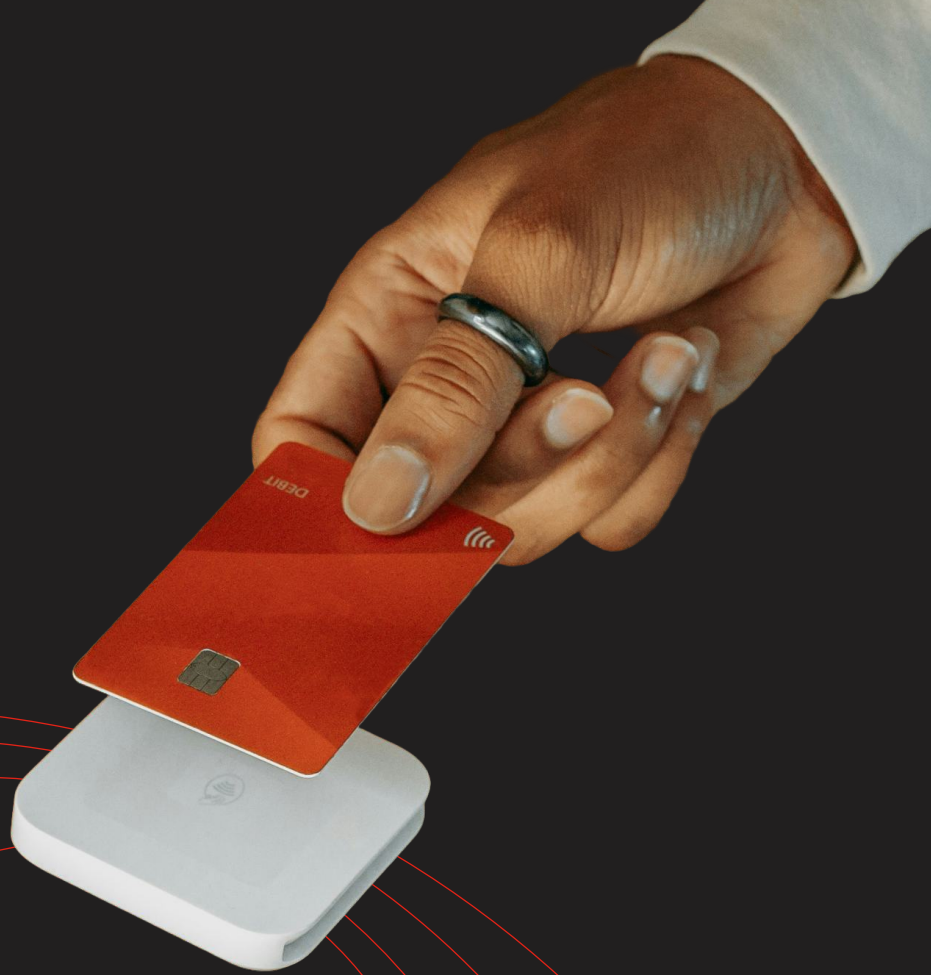




IMPACT BANKING

redefining wealth in the modern era

a litepaper by **defy** an xcube.co company

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Chapter 1

INTRODUCTION

As we navigate the complexities of the 21st century, our world faces unprecedented challenges—from climate change and mass migration to poverty and civil unrest. In this landscape, technology, finance, and policy must rapidly evolve to secure a just, equitable, and sustainable future. There is a pressing need for significant capital flow towards the UN Sustainable Development Goals (UN SDGs) with agents calling the top-down and the bottom-up action. The financial sector is uniquely positioned to wield its influence for good, channelling resources toward meaningful social and environmental change. Whilst impact finance offerings are growing, there remain very few accessible and affordable options for everyday people to participate.

Enter impact banking – a novel approach that seamlessly integrates banking services with a commitment to impact.

Enter impact banking—a novel approach that seamlessly integrates banking services with a commitment to impact. All too often financial and impact performance are pitted against each other: by embedding impact mechanisms within banking services, impact banking empowers retail customers to care for their financial health while actively contributing to positive change. It is not just a response to a demand; it is a transformative vision for the future of finance and an exciting opportunity for innovation in banking.

In this litepaper, we assert that impact banking is not merely a solution but a necessity. We explore its potential to reshape the banking landscape and drive global change where banking solutions sit at the front of innovation instead of lagging behind. Most importantly, we demonstrate the possibility of a banking system where doing well and doing good goes hand in hand.

Chapter 2

THE NEED FOR IMPACT FINANCE

It is estimated that achieving the UN 2030 Agenda will require an annual investment of US\$5-7 trillion however, government and development agency contributions fall short. To realise the triple bottom line of sustainability—people, profit, and planet—and meet the UN SDGs, significant financing is essential. The private sector is crucial in bridging this funding gap; mobilising just 7.76% of global assets under management (AUM) (an amount less than what transacts daily) could enable us to reach the UN SDGs.

Before delving into impact finance, it is crucial to distinguish between financing and funding. Funding refers to the traditional concept of mobilising resources through organisational and government accounts in order to close budget gaps in the pursuit of the UN SDGs at country level. Financing involves structuring various financial flows—both public and private, domestic and international—to advance the UN 2030 Agenda. Impact finance is a form of financing not funding. A scenario where financial institutions focus solely on financial metrics, while impact organisations prioritise only impact metrics, will not drive meaningful change. Neglecting to consider these elements together is both unsustainable and a missed opportunity hence the need for impact finance.

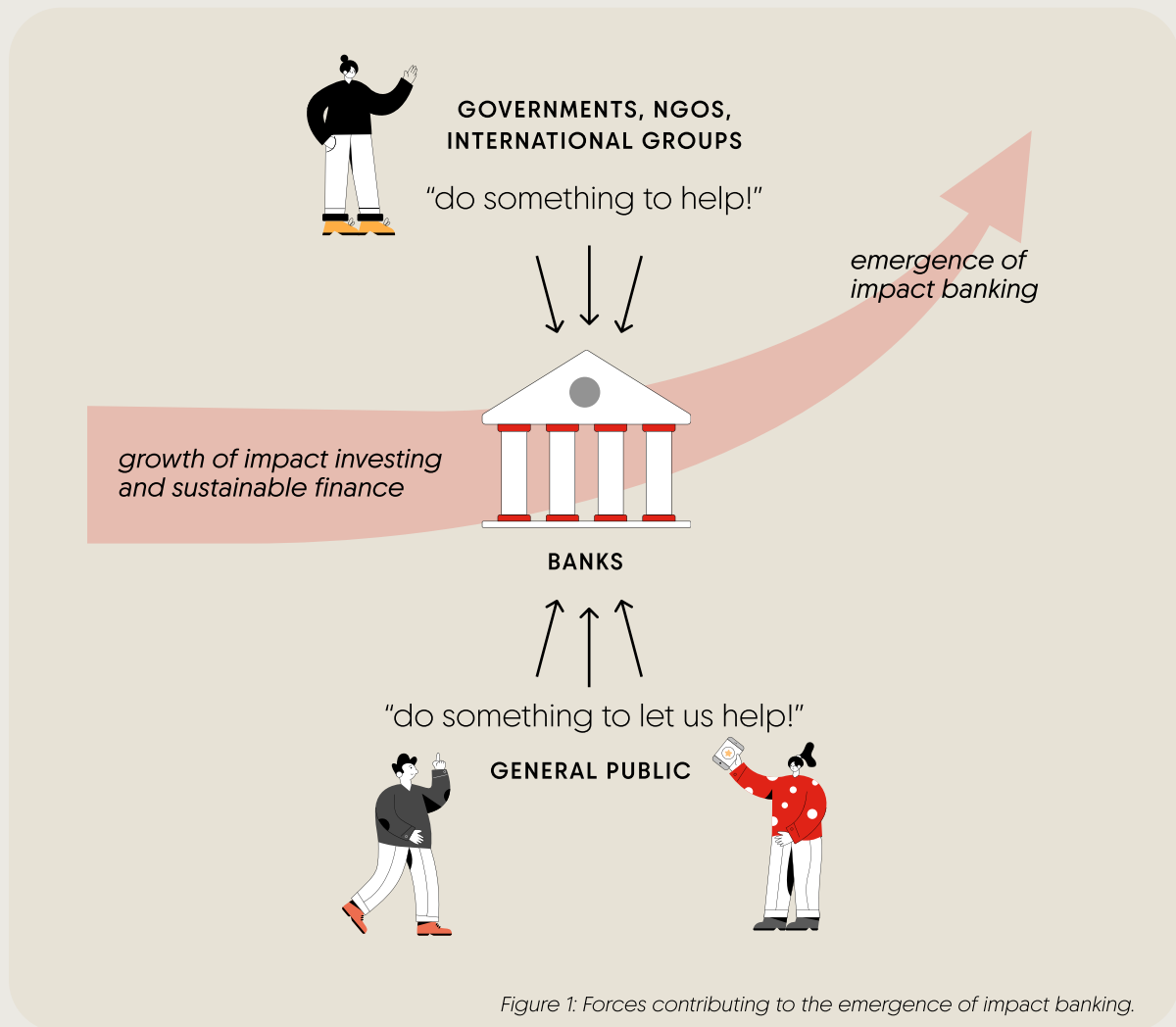


Impact investing...has surged in popularity over the past decade, reaching US\$1.2 trillion in assets under management (AUM).

Between traditional finance and philanthropy lies a spectrum of financial vehicles that can address both financial and impact objectives. The market for impact finance products has grown significantly including retail investing apps, crowdlending platforms, and institutional impact funds.

Impact investing occupies the middle ground between a strict focus on financial returns and a sole emphasis on impact. The Global Impact Investing Network ([GIIN](#)) defines impact investing as “investments made with the intention to generate positive, measurable social and/or environmental impact alongside a financial return.” This investment approach has surged in popularity over the past decade, reaching US\$1.2 trillion in assets under management (AUM) in 2022. Impact investing is a specific and measurable strategy emphasised by both the UN and GIIN as essential for achieving the UN SDGs and lays the foundational principles for all impact finance vehicles, including impact banking.

National bodies and economic experts make it clear the urgent need for impact finance and diverse channels of capital to drive social, environmental, and economic change. However, this call for action is not solely coming from institutional voices. Consumers and investors are increasingly seeking responsible finance opportunities, with a growing demand for financial products that align with their personal values and provide opportunity to contribute to collective action. The rising generations of Gen Z and Millennials are particularly shaping this trend. They are more informed about global issues and recognise the pivotal role that financial institutions play in shaping the future of the planet and its inhabitants. They expect these institutions to take responsibility for their contributions to the UN SDGs and to facilitate everyday retail participation in impact finance. Gen Z and Millennials change the makeup of today's banking clients markedly from those of the past: they are digitally native, values-driven, and poised to inherit significant wealth. This shift in lifestyle and philosophy necessitates new services, and presents an opportunity for banking to come back on top as an institution contributing to the common good.



To meet these evolving demands, banking institutions must innovate; failure to do so risks leaving a growing number of retail customers underserved and missing out on the growing market of values-led consumerism. As consumer expectations change and international pressure mounts to accelerate progress toward the UN 2030 Agenda, financial institutions cannot evade their responsibility. There is an increasing expectation for them to enable pathways for impact capital—not merely by funding charitable initiatives or the UN SDGs, but by empowering retail clients to contribute positively while also securing their own financial wellbeing. Moving forward, the integration of impact into traditional finance, and specifically mainstream banking, is essential for fostering a more sustainable and equitable future.



Chapter 3

INTRODUCING IMPACT BANKING

The pressing challenges of our time demand innovative financial solutions that transcend traditional profit motives. Impact finance has emerged as a promising response, yet the accessibility and credibility often fall short. Authentic impact finance solutions typically require high account minimums and significant due diligence, making it inaccessible to average retail investors. Meanwhile, retail banking options are widely available but often lack clarity regarding their impact claims or missions. This landscape reveals a significant unmet need for affordable and accessible financial services that deliver credible, meaningful impact. By applying the principles of impact investing across financial services, we can tap into the unrealised potential of retail capital. We believe that the greatest commercial and impact opportunities lie within the banking sector.

What is Impact Banking?

Impact banking is defined as “banking services that embed mechanisms to generate intentional and measurable, positive social or environmental impact with transparency and integrity, without detriment to the quality of financial return or service”.

This concept meets the needs of underserved retail banking customers who seek quality banking services coupled with trustworthy and transparent impact, whilst also addressing the unmet financing needs of the UN 2030 Agenda. Impact banking does not aim to replace existing impact finance vehicles; rather, it complements them by balancing commercial viability and quality services with the generation of positive social and environmental outcomes.

...with "The Great Wealth Transfer" underway and their (GenZ and Millennials) progression through the workforce—impact banking will be crucial for these values-driven, time-constrained individuals.

Unlike traditional banking, which primarily focuses on financial returns, impact banking emphasises the importance of impact alongside profitability. Furthermore, as Generation Z and Millennials become increasingly influential—with "The Great Wealth Transfer" underway and their progression through the workforce—impact banking will be crucial for these values-driven, time-constrained individuals. Impact banking allows them to create meaningful change while accessing quality financial services and maintaining their financial health.

Key features of impact banking

- 1. Dual rewards:** this approach prioritises both financial performance and measurable impact, ensuring clients experience the advantages of their financial choices. Through impact investing within the chosen finance vehicle, clients generate financial return and impact.
- 2. High-quality financial services:** by integrating impact investing principles, impact banking provides tangible social and environmental impact while maintaining and without detriment to quality financial services.
- 3. Cognitive ease:** by embedding impact mechanisms within the banking process and providing transparency on the impact measurement and management, impact banking reduces the cognitive burden on users, making it easy for them to contribute positively without additional effort.
- 4. Authentic impact:** by making impact a core component of business operations, impact banking combats "impact-washing," ensuring that claims of social and environmental benefits are genuine rather than mere marketing tactics.
- 5. Active engagement:** through behavioural models like voting rights, users can take an active role in creating impact in the areas they care about. By fostering a sense of purpose and fulfilment, such models incentivise continuity of contribution and customer retention.

In an evolving societal landscape, impact banking positions financial institutions as catalysts for change, reinforcing the idea that finance can effectively address the world's most pressing challenges while achieving sustainable growth. By embedding impact into everyday banking, individuals are empowered to contribute to a better future without sacrificing their financial wellbeing.

Chapter 4

IMPLEMENTATION OF IMPACT BANKING

Impact banking seeks to bridge the world between doing well and doing good. It is an approach that allows people to operate their everyday banking matters whilst making an impact through embedded impact mechanisms. **There are two components to implement impact thesis and financing mechanism**

1. Impact Thesis

Constructing an impact thesis is crucial for ensuring direct and measurable impact. The impact thesis itself is highly personal and must be tailored to the institution's reach, internal mandates, and desired customer acquisition. Impact theses can be anything from gender equality in the manufacturing industry, to climate action in Vietnam, to electrification in Zambia, to political literacy in under 30s.

The focus of impact is a case by case choice, but the implementation must follow the same tenets: positive social or environmental impact that is intentional and measurable. Financial institutions and services must adopt proper impact measurement and management (IMM) practices to uphold credibility, effectiveness, and industry standards. The Global Impact Investing Network (GIIN) has established standards for IMM; these are inherently iterative and comprises of four distinct facets which can be tailored for impact banking.



Impact Measurement and Management for Impact Banking

Adapted from [GIIN's impact investing IMM principles](#).

- 1. Identify thesis & set goals/expectations:** the impact thesis should be clearly defined and target a specific area of impact. Goals should consider the effects of capital flow from impact banking on people and/or the planet, and balance banking clients' expectations for risk, return, liquidity, and impact.
- 2. Define strategies:** select or outline strategic goals that are more relevant to your impact banking activities (both for impact thesis and finance vehicle). The [GIIN's IRIS+](#) platform and [UNDP Private Finance for the SDGs](#) includes commonly deployed strategic goals backed by best practices and evidence.
- 3. Select metrics & set targets:** tailor your impact measurement choosing metrics and targets that reflect your impact thesis. For example, the GIIN's IRIS+ core metrics sets are evidence best-practice-based sets used to assess the effects of investment and capital flow.
- 4. Measure, track, utilise, and report:** IMM is more than just counting metrics. It means considering information about financial return and impact to learn, adjust, and improve investment decision-making. Regular review and iteration is necessary to conduct high quality IMM and meet financial and impact expectations.

Fundamentally, impact mechanisms need to be embedded throughout banking, from the retail client experience to the financial professional conducting the services. The impact banking thesis must be a cornerstone of the bank's mission, from the value proposition to the revenue model to the communication of performance. That is, impact should be found throughout the value chain and not to the detriment of the quality of service. These guiding principles combined with the financial mechanisms outlined below will create a highly specific and effective impact banking solution for any financial vehicle and any impact thesis.

2. Financing Mechanism

As each institution offers a range of financial services, impact banking must be tailored to the financial vehicles on offer. Detailing the financing mechanism for each service is beyond the scope of this litepaper; further details are provided in the full [whitepaper](#) and extensive resources are provided by the [UNDP Private Finance for the SDGs](#). Transcending financial service, all core impact banking structures and mechanisms should look similar to the following:

Impact Fund Structure

Creation of an impact fund that would serve as a centralised liquidity pool to finance various impact projects via impact investing. This fund would aggregate liquidity through leveraging banking products and services, while giving customers voting rights to allocate funds. This will look different according to financial vehicle for example:

- **Retail Banks:** a portion of the interest earned on specially designated "impact savings accounts" directed to the fund. For example, 0.1% of the interest rate.
- **Commercial Banks:** a small percentage of the fees earned from trade finance activities contributed to the fund, especially for transactions and services with low or negative impact.
- **Private Banks:** a small percentage of the fees earned from managing client portfolios allocated to the fund, especially for portfolios with a low impact focus.



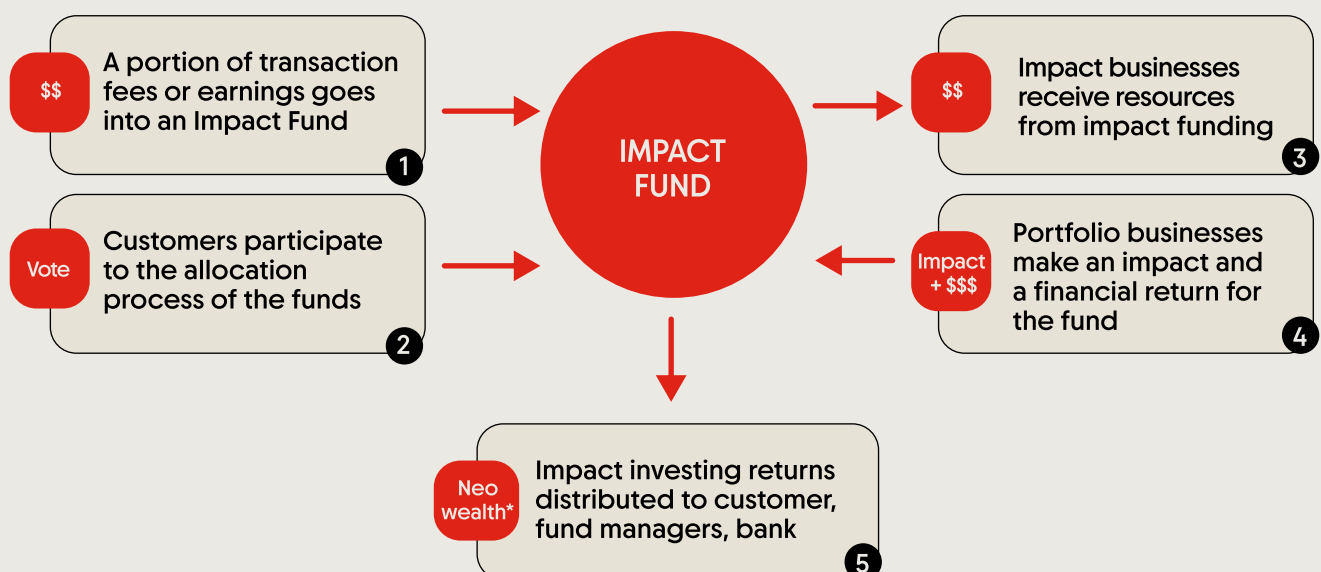
The liquidity can be generated in numerous ways, even within institution, but the deployment of funds is to be via impact investing. Following the GIIN's and Operating Principles for Impact Management, the practice of impact investing should feature: intentionality, investment with return expectations, range of expectations and asset classes, and impact measurement. The impact fund is not a concessionary pool of liquidity and the tolerance of risk to return to impact is to be determined by the fund manager.

Voting Rights Allocation

Each participating customer receives voting rights proportional to their contribution to the liquidity pool. For example, this could be based on account balances, transaction volumes, total contributions generated. Behavioural mechanisms like voting rights fosters engagement conducive to customer retention and continued participation in impact banking.

Project Selection and Funding

Impact businesses seeking funding submit proposals outlining their objectives and needs, aligned with impact thesis selection criteria. Periodically, the fund presents a curated list for customers to vote on their preferred initiatives using their allocated voting rights. Based on the votes, resources are allocated to the selected projects, ensuring that funding reflects contributors' values and priorities. This democratic approach fosters community engagement and aligns with the fund's overall impact thesis. It encourages active engagement similar to that of shareholder advocacy, allowing stakeholders of the impact fund (banking clients) a voice in the management of the fund.



**Neo wealth redefines capital by valuing intangible assets and integrating social and environmental factors into measures of economic success (the conceptualisation of neo wealth is beyond the scope of this litepaper).*

Benefits of the Impact Fund Structure

- **Sustainable liquidity:** by embedding the fund contributions into everyday banking activities, the structure ensures a consistent inflow of capital.
- **Reward & return:** by adopting an impact investment approach within the fund, customers and financial service providers get to see impact and financial return.
- **Customer engagement:** the voting mechanism actively involves customers in the impact finance process, nurturing their agency in and commitment to sustainable finance.
- **Diversified impact:** the fund can support a wide range of businesses within or across various impact areas, mitigating risk, and maximising potential positive outcomes.
- **Scalability:** as more customers opt into the associated banking products, the fund's capacity to support impact projects grows.

Impact banking combines elements of impact investing and traditional banking to create a powerful tool for channelling capital towards impactful businesses and engaging customers in the process, all while sustaining financial returns for all stakeholders.

Chapter 5

REGULATORY CONSIDERATIONS

Impact banking operates within a complex regulatory landscape as it sits across two verticals: impact and finance. Navigating these regulations is crucial for impact banking solutions, as they strive to balance profitability with their mission of driving positive societal change while maintaining trust with stakeholders.



1. Financial Regulations

It is important that banking solutions remain diligent in fulfilling their fiduciary duties and custodial regulations, regardless of impact theses. The financial institutions offering impact banking must adhere to their licensing requirements and restrictions and ensure to meet intra- and inter-jurisdiction guidelines for their practice.

Key regulatory considerations include:

- 1. Data privacy:** compliance with data privacy regulations such as GDPR, to protect customer data and ensure confidentiality.
- 2. Customer due diligence (CDD):** adherence to KYC processes that fulfil CDD requirements, including the verification of customer identities, and the screening and monitoring of transaction activities for suspicious behaviour.
- 3. Jurisdictional regulations:** compliance with various laws and regulations in different jurisdictions where services operate and are licensed, focusing on data protection, system security, and mitigating risks associated with technology and cyber threats.
- 4. Consumer protection laws:** adherence to laws and regulations in different jurisdictions where services operate and are licensed, that protect customers from misleading, deceptive, or unsuitable sales practices, which include processes for complaint handling and investment suitability assessments.
- 5. Reporting obligations:** requirements for reporting suspicious transactions to regulatory authorities and maintaining comprehensive audit trails.

2. Impact Regulations

Generating and reporting impact is an increasingly regulated space. Depending on impact thesis and jurisdiction of operations, impact banking solutions need to be mindful of their reporting requirements and the frameworks they must adhere to. The financial vehicle offering impact banking must adhere to disclosure and marketing regulations and ensure to meet intra- and inter-jurisdiction guidelines for their practice.

Key regulatory considerations include:

- 1. Operational disclosures:** all financial institutions/service providers must regard their impact, regardless of their impact finance offerings. Compliance with frameworks such the UN Principles for Responsible Banking and ESG disclosures is crucial, alongside voluntary disclosures related to sustainability targets (e.g., SBTi, WWF Sustainable Banking Assessment). The UN PRI 2023/4 report provides additional legal context for impact frameworks.
- 2. Impact measurement & reporting:** given the diverse nature of impact, impact banking solutions must adopt the appropriate measurement frameworks tailored to their impact thesis. The GIIN sets the industry standard for IMM, offering its own impact metric database, IRIS+. Another core framework is the Operating Principles for Impact Management, developed by public-private sector participants. Some impact verticals may follow specific regulations such as GRI or CDP reporting frameworks.
- 3. Impact-washing:** the sector is susceptible to impact-washing, where impact claims are exaggerated for marketing purposes. Although there are no universal regulations, specific verticals face their own reporting obligations, guidelines, and regulations. Greenwashing is a high profile example, with increasing scrutiny on environmental claims across regions. Recent legislation in the EU and actions by the UK Advertising Standards Authority (ASA) highlight accountability for misleading environmental claims, exemplified by bans on companies like HSBC for greenwashing advertisements.

Chapter 6

FUTURE OUTLOOK

The future of impact banking looks bright as awareness of social and environmental issues continues to grow among investors and consumers. With more financial institutions prioritising sustainability, we're likely to see impact metrics becoming part of standard banking practices with impact banking being one channel of impact capital. Innovations in technology, like blockchain and fintech, will also improve transparency and help measure social outcomes more effectively whilst enabling a wider range of participants in the financial ecosystem. Plus, increased regulatory support and alignment with global sustainability initiatives will strengthen the sector's credibility.

To maximise the potential of impact banking, the development of impact investing practices is essential. On the impact side, a key priority is the establishment of robust frameworks for measuring and managing impact. The GIIN provides valuable standards, and its IRIS+ platform offers thousands of metrics that allow impact finance vehicles to be tailored to specific theses. On the finance front, there is much to explore in the way liquidity is collected for impact funds and how financial return is distributed between the bank, fund management team, and the customers.

Collaboration among policymakers, financial institutions, academia, and think tanks can foster both financial literacy amongst the general public and specialised impact finance literacy within finance professions.

Imperative to the success of impact banking (and impact finance more broadly) is literacy. Education and general awareness of impact finance remain insufficient, contributing to confusion and misinformation within the sustainable finance space. This lack of clarity hampers progress toward viable and integral sustainable finance options. Collaboration among policymakers, financial institutions,

academia, and think tanks can foster both financial literacy amongst the general public and specialised impact finance literacy within finance professions. Such partnerships will empower individuals and institutions to make informed decisions that align with their values and ensure impact banking solutions are appropriately implemented.

Chapter 7

CONCLUSION

In conclusion, impact banking presents a significant opportunity for the financial sector to merge profitability with purpose. As consumer expectations shift towards sustainability and pressure is felt from governmental bodies and international organisations, financial institutions must evolve to provide accessible impact finance options for retail clients.

By integrating impact investing principles into everyday banking, we can direct substantial capital towards the UN Sustainable Development Goals, making individual financial choices part of a larger movement for positive change. The future of banking relies on this dual focus, enabling clients to drive meaningful impact while also achieving their financial objectives. Ultimately, embracing impact banking is set to play a crucial role in securing a more equitable and sustainable economy.



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