



7 December 2015

CPMI Secretariat,  
Committee on Payments and Market Infrastructures  
Centralbahnplatz, 2  
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### **Re. CPMI Consultative Report on Correspondent Banking**

Dear Sirs: The Institute of International Finance (IIF) and BAFT (the “Associations”) are pleased to be able to respond to the CPMI’s consultation on Correspondent Banking and look forward to providing feedback to the CPMI as it confronts its very significant agenda for the coming year.

#### General comments

The industry welcomes the CPMI’s close attention to issues of correspondent banking and AML/CTF issues. The Associations particularly appreciate the fact that the Consultative Report recognizes some of the difficulties and ambiguities that banks face in evaluating and conducting the correspondent banking business, particularly rising risk-management costs and uncertainty about what is required.<sup>1</sup>

The Consultative Report is frank in acknowledging its limitations and the fact that its recommendations might alleviate some, but only some, of the costs and concerns that banks confront. Nonetheless, it makes a substantial contribution to the debate on these matters and, subject to the comments below, will be helpful in moving from the current situation to a more efficient and effective compliance situation, where the disincentives to engaging in correspondent banking will be minimized.

In commenting on the Consultative Report and the broader issues that banks confront in doing correspondent banking today, the Associations and the industry hope to make a similar,

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<sup>1</sup> The Associations also welcome the broader awareness of the international official sector to the issues of correspondent banking as reflected in the FSB’s recent *Report to the G20 on actions taken to assess and address the decline in correspondent banking*. Comments in this letter will essentially address similar points in that document.

constructive contribution to improving a situation that has become difficult. These comments are given on the basis of a profound commitment by the international banking industry to maintain and enhance the integrity of the international payments system and to helping the authorities to stop abuses.

It is recognized that some of the comments given here may cover points going beyond the bounds of the CPMI's specific remit; however, it is hope both that such comments will nonetheless help inform the CPMI in its continued work and will contribute to broader debates in the official sector under the auspices of the Financial Stability Board (FSB).

For clarity's sake, note that many of the comments here encompass the challenges of sanction screening as well as other aspects of AML/CTF compliance.

*Executive Summary, Section 1 and Box 1.*

The Associations strongly endorse the suggestion to establish “a formal liaison to increase the coordination between the various work streams and the relevant authorities” in order to understand the many issues involved, the motivations of the main players, and the impact of regulatory changes and potential solutions. Such a formal liaison would certainly facilitate achievement of the FSB's “action plan” as set out in its report to the G20.

To that very constructive suggestion, the Associations add the following:

- It is very apparent, for example from the private-sector, public-sector colloquium on AML/CTF issues and derisking organized in London on September 30 by the IIF and The Clearing House, that data-privacy and other restrictions are a major issue from all points of view. Restrictions raise problems for the transfer, storage and use of data within banking organizations; between banking organizations; between banking organizations and supervisors; between banking organizations and law enforcement; and especially across borders for all actors. This point is acknowledged in the Consultative Report but needs to be made up front and stressed much more prominently and in greater detail.
- As recent experience with a promising UK pilot program, the Joint Money Laundering Intelligence Taskforce (JMLIT), indicates, it will be important to involve in the overall discussion the principal law-enforcement authorities, Financial Intelligence Units (FIUs) and Ministries of Justice with respect both to understanding their needs and to achieving more efficient means of meeting them and in order to minimize the risk of otherwise-avoidable enforcement actions against banks making bona-fide efforts to comply with AML/CTF requirements. This is important because enforcement actions against banks can contribute just as much as regulatory and supervisory questions to the ambiguities and disincentives that banks face. Ultimately, it is such authorities who must make use of

the information generated by the AML/CTF apparatus to achieve the goals of the system. This dialogue should lever the knowledge and experience of the Egmont Group of FIUs. In addition, while the authorities deny any intent to institute a “zero tolerance” regime, the perception thereof in the private sector is persistent. Although regulations have not changed, expectations have. Banks perceive that examiners now expect them to identify essentially every potential risk and suspicious activity without fail. They are apprehensive about enforcement decisions against them that seem less than predictable.

- Such issues as data impediments and the “zero tolerance” perception must be confronted directly, and it would be appropriate to involve the relevant regulatory and enforcement agencies at an appropriate stage in the discussions.
- Insofar as possible, future work should expand to cover measures that would help banks without access to correspondent banking services more easily to gain such access, which is out of scope of the present version per the statement at the bottom of page 1.
- Future workstreams will also have to consider the very rapid pace of technology development, which is affecting the entire banking industry, especially payments. Such “fintech” developments create new risks for banks. Importantly, there is also a widespread perception of level playing field issues because banks often seem to be subject to higher standards than new types of providers. Fintech developments are also likely to challenge the premises and the mechanics of current AML/CTF efforts by the authorities. At the same time, they may offer new opportunities for efficient combatting of financial crime. As the CPMI certainly recognizes, “blockchain” and similar technologies are believed by some to have the potential to revolutionize the overall payments business, and AML/CTF compliance must be part of any future changes of the global payments system.
- Technological issues also include the fact that higher costs and longer processing times resulting from regulatory requirements can have an impact on payments and the flow of commerce more broadly, at a time when businesses and consumers expect much faster and cheaper payments than in the past.
- As the JMLIT program demonstrates, there is much practical understanding to be gained from including the industry in such an overall program. Appropriate means should be found to include both developed-market and emerging-market banks and money transfer businesses in the search for greater effectiveness and efficiency. We note with appreciation that the CPMI has taken into account the work of the Wolfsberg Group and other private-sector sources in preparing the Consultative Report.
- Effects on end-users, whether corporations, SMEs or individuals, should be included more systematically in the analysis.
- Active consultation with private sector groups should be institutionalized.

While the general discussion in the Executive Summary and Section 1 is appropriate, there are some statements that are over-simplified. For example, in the fourth paragraph of the Executive

Summary, it is stated that banks have “cut back services for respondent banks that (i) do not generate sufficient volumes ...; (ii) are located in jurisdictions perceived as very risky; or (iii) provide payment services to customers about which the necessary information ... is not available.” While that may be true in some cases, it is important to note that many decisions to withdraw services to respondent banks are made following specific risk assessments of an individual respondent, which may include factors in addition to jurisdiction. Such assessments may deem respondents to constitute unacceptable risk or on balance not to be cost-effective to serve, based on the factors identified by official guidance, including adverse media reports, evidence of weak internal systems and controls, regulatory censure, high-risk customer or transaction profiles, or relationships with PEPs.

### *Section 2.1*

The Consultation Report comments on the description of correspondent banking, without actually offering a formal definition. The Associations believe that the CPMI in conjunction with the FATF should work toward risk-ranking the wide range of services and activities captured with current broad definitions of correspondent banking, such as those in the EU Fourth Money Laundering Directive and the USA PATRIOT Act.

In such a process, care should be taken not just to add another definition to the already-existing ones, but to find ways to agree on a uniform, risk-based and appropriate description. The description should also incorporate risk ranking of the activities and services captured by the existing definitions in order to clarify appropriate risk-based systems and controls.

Additionally, it should be noted that the current version of the Consultative Report does not address two important features: (a) a range of banking activities including trade finance and payments, and (b) the fact that correspondent banking is not just “cross-border” as stated, but also includes transactions between banks within one jurisdiction. On the first point, the effects of the current regime on trade finance payments as well as other payment services need to be considered. On the second, regional banks, notably in the US, rely on global financial institutions for cross-border needs such as making payments, providing access to foreign exchange, and issuing and authenticating trade-finance transactions. Whether within the US or elsewhere, respondent banks within a region may be affected by incentives to de-risking in a manner similar to international respondent banks.

Similarly, the Swift-based “RMA only” (Relationship Management Application) supports non-account relationships and is used to send authenticated messages between a sender and a receiver. Various message types exist to support transaction initiation for trade finance, and various message types also exist to support the communication of information, without initiating a payment. This authenticated communication is critical where an intermediary must be used to

link all parties in the chain. Disruptions to correspondent account relationships also disrupt RMA-only relationships, particularly affecting smaller regional or international banks. To minimize this result, the industry suggests that regulators accept an appropriate risk-based level of due diligence for a restricted form of RMA (RMA only) to be used for information and authentication only (e.g. trade finance or other specific information transmissions). Doing so would encourage banks to maintain RMA only non-account relationships with other banks.

This issue needs to be worked through by the industry jointly conjunction with the FATF and other relevant parties in the public sector.

Footnote six directs the reader to the CPMI's 2014 work on "innovative payment service providers". Such a reminder is very helpful and we only note that the "ecology" of new technologies and innovative providers (or firms aspiring to become such providers) is changing rapidly.

Under current circumstances, payment traffic through non-bank payment services and "fintech" firms may be more opaque than payments through correspondent banks, bringing the risk of being unable to identify the underlying parties to a transaction.

Both for purposes of protecting the level playing field and for making sure that new loopholes are not created for money laundering, terrorism, or financial crime, the official sector will have to make a constant effort to update its understanding and analysis of such providers and respond appropriately to developments. Moreover, there is a strong perception of gross differences between the regulatory scrutiny to which traditional payments providers are subjected and that applied to new "innovative" providers. It will be essential to the effectiveness as well as the fairness of the AML/CTF system that new providers also be subject to the same level of rigor, albeit in ways that do not stifle innovation. The authorities in some countries are aware of this risk, but it is not clear to the industry that sufficient progress is being made in identifying and addressing the risks raised by the new providers.

## *Section 2.2.*

The trends discussed here have been developing for several years, at least since 2000. The new regulatory environment, as well as profitability and strategic concerns, have impelled banks to review relationships that in many cases are decades old and have continued well beyond their original business rationales. The phenomenon is thus a complex one, but is in very many cases initially driven by perceptions of higher risk.

The second bullet on page 8 is important. The use of the term "nested", which has taken on negative connotations, may distort the discussion. A better term would be "downstream

clearing”, which reflects a very useful feature of the traditional correspondent banking business. It is important to note (a) that “nested” accounts are both an important strategy (especially for USD payments) for emerging-market banks that do not have or have lost direct correspondent relationships for any reason (related to AML or not) and (b) much of the scaling-back that has occurred has been driven by regulatory issues about difficulties of identifying all intermediaries, originators or beneficiaries of payments through such relationships, and in some cases by specific supervisory concerns. This reflects the fact that “nested” relationships are seen as effectively equivalent to dealing with the underlying banks directly, but with less transparency of the underlying bank’s activity, making the correspondent’s risk management much more challenging. Withdrawal from “nested” activities is therefore driven by cost and risk (and risk appetite) as well as regulatory pressure. This is a significant part of the Know Your Customer’s Customer (KYCC) challenge. With improved information transfer and transparency, and clearer regulatory guidance, the downstream clearing model should be available under appropriate circumstances to support such banks and their underlying customers.

In addition to considering effects on banks and payment systems, it would be helpful if future work could also consider effects on, and costs generated for, the underlying customers who use the payment system, especially in emerging markets. Useful work is being done on downstream effects on customers, as part of the international effort on inclusion through the Alliance for Financial Inclusion<sup>2</sup> and private-sector groups such as the Association of Foreign Banks<sup>3</sup> and the Center for Global Development.<sup>4</sup>

### *Section 3.1*

The Associations and the industry generally support measures that facilitate managing the cost of risk management and efficient compliance with regulatory requirements that correspondent banking businesses and respondent banks have to meet. The recent AML/CTF colloquium in London largely focused on (a) the potential for greater public-sector and private-sector cooperation and collaboration, (b) the possibilities of creating utilities for KYC and for transaction monitoring purposes, and (c) the possibilities of technology, but also (d) the legal, regulatory, and data-protection, data-localization and other data-sharing impediments that have to be confronted to achieve better solutions.

Perhaps the greatest need is for greater clarity and consistency of supervisory and law-enforcement expectations, and of what is and what is not permissible for information exchange,

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<sup>2</sup> Alliance for Financial Inclusion, “G-24-AFI roundtable in Peru: Central bankers must act to stem the tide of de-risking,” October 12, 2015, available at <http://www.afi-global.org/news/2015/10/12/g-24-afi-roundtable-peru-central-bankers-must-act-stem-tide-de-risking>.

<sup>3</sup> Association of Foreign Banks, “De-Risking and the impact on foreign banks operating in the UK,” Position Statement, December 2014.

<sup>4</sup> Center for Global Development, “Unintended Consequences of Anti-Money Laundering Policies for Poor Countries,” CGD Working Group Report, November 9, 2015, available at <http://www.cgdev.org/sites/default/files/CGD-WG-Report-Unintended-Consequences-AML-Policies-2015.pdf>.

including within international groups. The Associations therefore share the analysis of the FSB Report that clarifying regulatory expectations should be a top international priority.

*KYCC.* In particular, there is still confusion around KYCC. In addition to the ambiguity of current FATF guidance, which says KYCC is generally not required but may be required in certain higher-risk situations, there is uncertainty about variations from jurisdiction to jurisdiction. For KYCC in particular, global *consistency* of reasonable, well-defined expectations will be an essential component of improved *clarity*.

*Data impediments.* It would be very helpful if the next phase of the CPMI's work were to confront the legal, regulatory and data-protection impediments that were (appropriately in the initial stage) taken as a given in preparing the Consultative Report. For purposes of this work, "data protection" should be understood broadly, including all restrictions on the usage, transfer or storage of data, and including data privacy, consumer protection, bank secrecy, data localization and restrictions on the transmittal of AML-related information such as SARs.

While the industry accepts its duty to manage its costs and revenues and to identify solutions that will improve the efficiency of correspondent banking, it is very clear from all discussions, such as the recent colloquium noted above, that many of the obstacles to a better overall system are beyond the unilateral control of the industry.

Clarification of regulatory, supervisory, and law-enforcement expectations, resolving contradictions between and among AML/CTF regulations and other bodies of regulation will be needed to achieve an optimal result. Data privacy protections and other restrictions on the use and transfer of data will need to be reviewed and in some cases new legislation will be required.<sup>5</sup>

The needs of banks carrying out AML/CTF obligations should be taken into account as the authorities work on better coordination and exchange of information to stop the flows of funds to terrorists, as mandated by the Antalya G20 Summit.<sup>6</sup> Recognition of and action on the current legal and regulatory impediments to effective use of data for AML/CTF purposes by banks should be an important part of such efforts.

One idea that might help would be to increase regional consultation and collaboration: the FSB or World Bank or some other agency might establish "financial crime working groups", say in the MENA region, Latin America, or other areas. This would have two main benefits. First, it would facilitate exchanges of information about problems, procedures, and solutions among

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<sup>5</sup> We note with appreciation that the FSB report cited above recognizes the importance of clarifying regulatory expectations and suggests some ways to do so.

<sup>6</sup> The Group of Twenty (G20), "Communiqué: G20 Finance Ministers and Central Bank Governors Meeting," September 4-5, 2015, available at <https://g20.org/wp-content/uploads/2015/09/September-FMDBG-Communique.pdf>, p. 3.

AML/CTF experts, potentially leveraging the examples of firms with strong practices. Second, by raising the level of knowledge, such groups would improve implementation of sound practices, and ultimately mitigate the perceived risk concerns of correspondent banks and their supervisors about dealing with banks from such regions.

In addition, as discussed at the September 30 colloquium, many banks that are active correspondents are considering what they can do to assist respondent banks to perform better. Going beyond that, it would be very helpful if an international official-sector group, such as the World Bank or IMF, undertook training and assistance programs for respondent banks to help them understand and thus better satisfy international AML/CTF standards and requirements that correspondents must meet. This might ultimately lead to a certification program whereby respondent banks (and perhaps specific officers such as CROs) could be certified as having attained an adequate level of expertise, which would require periodic renewal, of course.

### *Section 3.2 KYC Utilities*

KYC utilities have considerable promise, as described in this section. Banks are highly interested in the potential of such utilities, but also have to be realistic about confronting the hurdles to effective reliance upon such utilities. Cross-border restrictions on data transfer, storage, and usage are often hard to interpret but clearly make some vital information unavailable to certain entities under many circumstances, even to entities within the same group.

Without resolving the problems created by such data restrictions, the KYC utility concept will remain unworkable in many situations. This is one of the major disincentives to conducting a correspondent banking business today.

The discussion of data issues is helpful but incomplete. Data-definition and standardization are indeed major technical problems to overcome, and maintaining data quality will be an issue for any future utility. Any such data standardization effort should aim at data requirements for all aspects of the AML/CTF and sanctions regimes, including due diligence, transaction monitoring, screening of customers, and (to the greatest extent possible), ad-hoc official requests for information. But, as stated above, most the basic impediment is the many, varied and often inconsistent data restrictions that banks now face.

However, impediments to sharing data, as discussed above, especially across borders, is the most critical issue. This point is acknowledged in the fourth bullet on page 14 but is much more fundamental than is apparent from that discussion. The private sector stands ready to work with the public sector in such a standardization effort, but it will need leadership from the public sector to resolve the many legal, regulatory, and technical issues that will need to be tackled. The Global Legal Entity Identifier System (GLEIS) offers both a good model of cooperation



between the private and public sectors and a considerable amount of learning about the process of standardization that could be useful in other standardization projects.<sup>7</sup> Perhaps the Antalya declaration on information sharing will be the needed catalyst to crack this problem.

A further fundamental issue is that banks will need some assurances that the regulatory, supervisory, and law-enforcement authorities approve of and will recognize the appropriateness of reliance upon any such utility. Without such approval and the ability to rely on utilities, much of the incentive to invest in and to use them would be lost.

While, under the current system, it may be that banks “cannot simply delegate their responsibility” for due diligence, as indicated in the first bullet after Box 2 (p. 13), clarity about the extent of reliance that is permissible will be essential if utilities are to reach their full potential to alleviate the issues. It is understood that there has generally been reluctance on the part of regulators and law-enforcement authorities to define “safe harbors”; however, the industry will definitely need assurances that bona-fide reliance upon any such utility will be respected.

Data from existing utilities can be helpful especially where information is validated to public sources, but because of insufficient assurances about recognition of the appropriateness of reliance thereon, banks have sometimes concluded they should treat such data as essentially the same as receiving data from the client itself, and therefore subject to an obligation to identify and verify the information, so the efficiency gains may be substantially less under present conditions than would appear at first glance.

As the Consultative Report suggests, in order for banks to rely upon any such utilities, there must be proper audit and verification, regularly updated, including confirmation of conformity to data-quality and confidentiality procedures. It is not clear what is meant by “verification” in the Consultative Report, however.

Serious consideration should be given to establishing international standards for the regulation by appropriate national authorities of such utilities in order to bolster banks’ ability to rely upon them (and to create greater assurances of achieving official AML/CTF goals). Such regulation standards should include standards for “verification” that national authorities could administer or supervise.

Alternatively, some kind of officially recognized certification process for the compliance of utilities or other vendors with recognized international standards for data quality, the type and amount of information required, database maintenance and upkeep, audit and governance would

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<sup>7</sup> See GLEIF.org for information about the GLEIS.

help a great deal.<sup>8</sup> While the industry is eager to work with the vendors on further developing utilities, the official sector will have to be involved to make sure that appropriate standards are defined and that banks get the assurances they need to use such utilities, given all the pressures they are under.

Thus, we share the perception that KYC utilities are a promising tool for speeding up compliance and cutting costs. Although complete standardization may be infeasible, the statement at the end of Section 3.2 (p. 14) to the effect that this is “due to the risk-based approach for AML/CTF” needs to be taken cautiously. Yes, there may be cases where a bank would need more information than standardized data could provide, but that does not in itself constitute a reason not to seek the maximum international standardization of those data that can be standardized.

Such standardization of information requirements (or templates) could be extended to include international standardization of basic due diligence information and “enhanced due diligence” information for higher-risk relationships. A correspondent bank could have the option to request the “enhanced” information when deemed necessary in accordance with its own risk-based approach. Standardizing such information would assist correspondent banks that need the information to maintain or establish relationships with respondents. Respondents would know better what to expect and could prepare responses much more efficiently and uniformly. No template or standardized questionnaire could cover all possible situations, nor would it preclude a correspondent from asking additional questions that it deems necessary, but at least the basic standardization would give both parties a ground of basic expectations to build upon in making judgments about how to do business. It could eliminate a degree of unnecessary duplication of effort and costs. Standardized information requirements or templates could be supplemented by periodic FAQs as issues develop or points needing clarification emerge.

Development of such standards will require correspondent, respondent, and official-sector input, but official sector sponsorship will probably be necessary to make the effort worthwhile.

The Recommendation on the use of KYC Utilities is useful as a starting point for discussion, as far as it goes, but will likely remain a dead letter unless the authorities address the issues discussed above, especially data issues.

### *Section 3.3 LEI*

The Associations and the industry generally have endorsed and worked to implement the LEI project since its inception, as the global solution for identification of entities in the broad financial markets. In fact, the industry has said repeatedly that various agencies of the official

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<sup>8</sup> The US Bank Service Company Act, providing for examination of relevant service companies, would be a useful point of departure for developing international regulatory or certification standards.

sector should do more to mandate use of the LEI for all types of financial reporting and supervisory purposes.

As discussed in this section, LEIs do have considerable promise for use in the correspondent banking business, which should become more and more evident as the LEI is adopted for use in many market and business contexts. This is likely to be the case in the near term in the context of institutional business in developed markets, for example, for identifying legal entities in a chain of custody. This point was discussed at the colloquium noted above. But use of LEI is expected to expand greatly in the next two to three years as more than 40 new and existing rules and regulations requiring or requesting use of the LEI come into force.<sup>9</sup> The number of LEIs is expected to expand rapidly into the millions, providing increasingly good coverage for correspondent banking purposes.

The Associations concur with the assessment that BICs are currently the cornerstone of the global payments network as the mechanism for message routing and as an account identifier. However, it is important to recognize that LEIs are a reliable tool to identify parties to financial transactions unambiguously. As a result, both need to be considered in any complete solution. As part of such a solution, it would be helpful to consider the creation of a mapping facility to allow for the easy mapping of routing information in payment messages to the relevant LEI. The industry stands ready to support this effort. Note that some messaging systems are currently exploring including the LEI in their messages, for example, ISO 15022 category 5 messages for securities activity. It is expected that further inclusion of LEIs in payments systems for entity and account identification will evolve over time as the value of this global standard continues to rise.

However, while the LEI system is developing rapidly and will certainly be increasingly helpful for correspondent banking purposes, its limits must be recognized, at least for now.

The current cost of LEIs may be an obstacle, especially for smaller SMEs in emerging markets. The current cost of about USD150-200 for initial registration and about half that for ongoing maintenance is expected to decrease over time as the number of LEIs in the system increases, so the problem can be expected to diminish for entities eligible for LEIs.

More significantly, of course, the LEI does not cover individual beneficial owners unless acting in a business capacity.<sup>10</sup>

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<sup>9</sup> See the recent regulatory report from the LEI Regulatory Oversight Committee (ROC) to the Financial Stability Board, "LEI ROC progress report on the Global LEI System and regulatory uses of the LEI", November 5, 2015, available at [http://www.leiroc.org/publicaitons/gls/lou\\_20151105-1.pdf](http://www.leiroc.org/publicaitons/gls/lou_20151105-1.pdf).

<sup>10</sup> The ROC issued guidance in November, 2015 permitting LEIs to be issued to individuals acting in a business capacity. The ruling can be obtained from the LEIROC.org website under Press Releases and Publications. Possible analogous digital identifiers for individuals, in particular in emerging markets, are being explored and were discussed at the September 30 colloquium; however, such technologies are in their early stages of development and may face significant legal and cultural obstacles in some countries. See the discussion of identification of

Attention should be given to inclusion of LEIs in MT103 messages in an orderly change process as such messages are reviewed and revised in the normal course, given the steady growth, encouraged by the FSB, of use of LEIs for many purposes.

Overall, LEIs clearly merit further consideration for AML/CTF purposes, although they will not alone solve the difficulties that have arisen in the correspondent banking business that give rise to incentives to “de-risking”.

While the penultimate bullet on p. 16 notes that LEIs cannot be a substitute for customer due diligence, which is true, it would be helpful if the authorities could work toward specific regulatory recognition of LEIs for AML/CTF purposes, given that a robust global system has been created and is expanding rapidly, with FSB oversight of LEI quality and governance. With such recognition, banks could be enabled to put substantial reliance on LEIs as part of the customer due diligence process,

### *Section 3.4 Information sharing*

The industry welcomes the fact that the FATF and other international bodies are working on further information and guidance on risk-based decision-making as described on page 19.

It is very clear that this work needs to confront the KYCC problem head-on, and to recognize the fact that the disincentives for banks created under the risk-based approach as currently interpreted and applied will continue to push banks toward restricting their correspondent banking business for higher-risk countries and counterparties. The industry certainly agrees that it would be appropriate to encourage the FATF and BCBS “to increase clarity in this area given that some of the factors that are lessening the attractiveness of the correspondent banking business relate to the uncertainties around due diligence vis-à-vis the respondent banks’ customers ...”.

The comment at the bottom of page 19 regarding including appropriate clauses in customer contracts to facilitate forwarding relevant information to correspondent or intermediary banks is laudable in principle; however, the comment needs to be more heavily caveated than in the present draft because such clauses may not be allowed in some jurisdictions; may not be permissible in some cases to allow information to be passed to utilities or centralized databases; and may be restricted by rules in addition to data privacy rules. As a result, requiring such clauses could cause control and compliance difficulties. Banks would no doubt have to monitor a situation where such clauses were permissible for some but not all categories of customers and counterparties. It is unrealistic to suggest such clauses for multi-jurisdictional business if the result would be that banks would face complex compliance burdens to identify clients who could or could not be asked to include such clauses and jurisdictions or types of entities to which

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individuals in the Center for Global Development working group report, *Unintended Consequences of Anti-Money Laundering Policies for Poor Countries* (November 9, 2015, p. 52). In some cases, subject to local law and practice, tax identification or similar numbers may be adaptable for this purpose.

information could or could not be passed. On the other hand, if clear and consistent international standards permitting the use of such clauses were in place, it could make a huge difference in facilitating AML/CTF processes, to the benefit of clients, banks, and the enforcement process.

Thus, the simple contractual idea is likely to require some concerted international official action to be useful to any great extent.

Centralized databases, such as discussed on page 20, do appear to have a great deal of promise in principle, subject, again, to coming to terms with restrictions on the use, storage and transfer of data, especially across borders.<sup>11</sup> It is worth noting that these same impediments are being confronted in other areas, such as banks' compliance with the requirements on Risk Data Aggregation (Basel 239) and the FSB's data hub project to collect data of macroprudential interest for supervisors. The issues are largely similar and should perhaps be addressed across these issues, rather than just through the AML/CTF silo. But, in this context, the serious impediments of the overlapping data restrictions that now exist create substantial doubts about the potential for such databases.

The discussions of the Mexican initiative in Box 4 and of Section 314(b) of the USA PATRIOT Act are good and indicative of useful things to do. This information, while useful, will need to be used with caution. Section 314(b) is limited to domestic entities, does not address cross-border issues, and has perhaps not lived up to its potential hitherto; however, the US banks, law firms, and regulators are doing a great deal of work to make its potential more readily available. Any use of 314(b) as a model needs to take into account the reasons for its restricted uptake and the efforts now being made to make it more flexible.

More broadly, anything that can be done to encourage information exchange among banks and with the authorities would be useful, recognizing the constraints of the various forms of restrictions on information and data exchanges. It may be, as with JMLIT, that some degree of informal exchange can be encouraged under appropriate circumstances; however, banks cannot participate in such exchanges without a substantial degree of legal comfort for doing so.

The first bullet on page 22 says that information sharing might reduce costs but "correspondent banks always remain responsible for performing adequate due diligence. Information-sharing mechanisms do not alter these basic responsibilities." While this is true and well understood by banks, the official sector needs to provide much greater clarity about the extent to which banks can rely upon such information-sharing mechanisms as part of due diligence if any progress is to be made on the problem of disincentives to the correspondent banking business.

The Associations very much welcome point (i) of the Recommendation that the FATF and AMLG provide additional clarity on due diligence recommendations for upstream banks,

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<sup>11</sup> Clear standards would also be required for the ownership and protection of confidentiality of data in accordance with all applicable legal and regulatory requirements.

especially as to the extent to which banks need to know their customers' customers. However, points (ii) and (iii) are not ambitious enough. While point (ii) on clarifying data privacy concerns is helpful as far as it goes, further clarity is not likely to be very helpful unless it is accompanied by specific recommendations on how to manage the problems created by laws that restrict data. This would have to include attention to all forms of restrictions on data usage, storage and transfer, not just data privacy. Point (iii) on detailing appropriate information-sharing mechanisms is also a good idea, but should extend to making clear how banks could expect to be able to use information subject to such mechanisms.

It would also be helpful if the Recommendation clarified what is meant by stating that use of information-sharing systems "could be promoted as the first source of information by default, which ... could be complemented bilaterally with enhanced information should there be a need." This phrase seems promising and suggests guidance on the extent of permissible reliance upon such mechanisms; however, to be fully useful it should be much more explicit that the authorities should provide such guidance.

As noted above, including relevant provisions in customer contracts, while certainly a good idea, is likely to be of limited use in multi-jurisdictional cases until the legal issues are sorted out and thus the Recommendation should make clear that the potential for use of such contracts would be substantially enhanced by internationally consistent rules permitting their use.

### *Section 3.5 Payment Messages*

Payment messages are of course the subject of ongoing industry attention and work by Swift and other parties. We will not attempt a full discussion here, but are confident the CPMI is aware of developments in payments and can adapt the Recommendations accordingly.

One technical point that may be worth mentioning is that XML messages (pacs 008/pacs 009) allow more information to be transferred in a structured way. Encouragement of further uptake of the XML standard whenever appropriate would make sense as a means of facilitating information sharing.

Although the "serial method" is described as being perceived to be safer, it is important to add that it is associated with significant negative impacts on (a) the cost of cross-border transactions and (b) the timing of payment processing, both with negative impacts on ultimate consumers.

The Recommendation under this section could be enriched by calling for work to consider whether a field for identifying the "clear purpose of the payment" should be included and whether such a field should be mandatory (as many in the industry recommend). Provision for easy extraction of intermediary banks involved in a payment would also be worth concerted examination. Finally, the analysis should include consideration of effects on underlying clients, especially with respect to costs and payment timing.

### *Section 3.5.3 Usage of the LEI in Payment Messages*

See the discussion of the LEI above.

#### *Conclusion*

The Associations agree that the proposed measures “should be subject to a formal consultation and further analyzed by all relevant stakeholders in order to gauge the potential impact of each measure and to avoid unintended consequences.”

As discussed above, such consultation should ideally be in a wider context, aiming to address more of the fundamental problems that both correspondent and respondent banks confront, as well as to address the relatively technical issues raised in the present document.

Fundamentally, what is needed to address the “de-risking” issue is engagement of regulators and other involved international and government agencies in a concerted program to examine the challenges that correspondent banks face and the incentives created by the present system, consider the legal and regulatory impediments that exist, determine how much more could be done through technology and utility systems (both under present circumstances and if impediments were corrected), rethink past policies on giving actionable guidance as to what procedures banks can rely upon, and undertake renewed efforts to bring countries and business sectors that appear to be lagging up to international standards. Ultimately, this may include redefining the roles and responsibilities of stakeholders for elements of the processes of due diligence, transaction reporting, and detecting and preventing money laundering, terrorist finance, and sanctions violations through correspondent banking, and ultimately for determining which entities and jurisdictions pose material threats and what measures are necessary – and sufficient -- to mitigate such threats insofar as the correspondent banking business is concerned. Such a process should ultimately enable a rebalancing the global control system with the new attention of the G20 and FSB to inclusion issues to arrive at balanced, proportionate, and effective pursuit of the goals we all share of keeping the global payments system as free as possible of inappropriate transactions.

As the FSB report to the G20 recognizes, if well-regulated banks are induced to de-risking, the result is likely to be more risk and opacity in the international payments system; therefore, addressing all the disincentives now affecting banks conducting correspondent banking, trade finance and related payment services would improve the overall performance of the AML/CTF and sanctions regime, and enable banks to offer such services on a reasonable basis more widely.

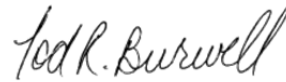
The Associations stand ready to work with the CPMI, and the FSB, BCBS, FATF and other agencies to achieve the dual goals of managing down disincentives to conducting correspondent-banking and payment services and reducing use of the system for financial crime.

Should you have any questions about these comments or wish to pursue discussions with the Associations or their members, please contact David Schraa ([dschraa@iif.com](mailto:dschraa@iif.com)) or Stacey Factor ([sfactor@baft.org](mailto:sfactor@baft.org)).

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