



August 5, 2016

Sent via email

Financial Action Task Force Secretariat
2 rue André Pascal - 75775
Paris, France
pdg@fatf-gafi.org

Re: Consultation of the Private Sector on Correspondent Banking

Dear Sir or Madam:

World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Financial Action Task Force's (FATF) *Consultation of the Private Sector on Correspondent Banking*. Credit unions are cooperative depository institutions and World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are 57,000 credit unions in 105 countries with USD 1.8 trillion in total assets serving 217 million natural person members.¹

World Council appreciates the FATF's efforts through this guidance to clarify the rules regarding financial institutions' anti-money laundering/countering the financing of terrorism (AML/CFT) responsibilities in the context of correspondent banking.

World Council strongly supports the proposed statements in Paragraph 3 and elsewhere that the FATF's *Recommendations* do not require financial institutions to conduct due diligence on their customers' customers. We urge the FATF to finalize these statements as proposed.

Question 1: Definition of correspondent banking (Para. 13 a): please share your views on the current FATF definition of correspondent banking (FATF Glossary). Would a change in the definition, and more specifically on the scope of the definition, help financial institutions address some of the de-risking challenges, or would it cause more uncertainty? If relevant, please explain why a change in definition would help to address some of the de-risking challenges, and give your views on whether this would have a significant, moderate or minimal impact on de-risking?

a. *The FATF Should Substitute "Financial Institution" for "Bank"*

World Council urges the FATF to revise the definition of "correspondent banking" to use the terms "correspondent financial institution" and "respondent financial institution" instead of "correspondent bank" and "respondent bank." We believe that using the term "financial institution" is more accurate because some types of depository institutions—such as credit unions, building societies, and savings and loan associations—are not called "banks" even though they are engaged in the business of banking including the provision of domestic and/or

¹ World Council of Credit Unions, *2014 Statistical Report* (2015), available at <http://www.woccu.org/publications/statreport>.



international payments services. Specifically, we urge the following edits to the first sentence of the definition of “correspondent banking” in Paragraph 13(a):

correspondent banking is the provision of banking services by one ~~bank~~ **financial institution** (the “correspondent ~~bank~~ **financial institution**”) to another ~~bank~~ **financial institution** (the “respondent ~~bank~~ **financial institution**”).

Using the term “financial institution” instead of “bank” would help reduce “de-risking.” This is because staff members at correspondent banks are not always aware that credit unions are depository institutions which are subject to the same AML/CFT regulations and compliance responsibilities as banks. In some cases, large banks have moved to close credit unions’ correspondent accounts, or refused to open such accounts, because their staff members did not appreciate that credit unions have AML/CFT compliance responsibilities which are the same as banks’ AML/CFT responsibilities.

Credit unions are engaged in the correspondent banking business both as correspondents and as respondents. Credit unions that serve physical persons (which are often called “natural person credit unions”) are typically respondents. Wholesale credit unions (which are usually called “central credit unions,” “corporate credit unions,” or “credit union federations”) act as correspondents for the natural person credit unions that are their members, and are also respondents of money center banks.

Using the terms “correspondent financial institutions” and “respondent financial institution” instead of “correspondent bank” and “respondent bank” would more accurately reflect the diversity of depository institutions engaged in the business of banking and therefore help reduce the phenomenon of “de-risking.”

b. This Guidance Should Also Address Domestic Correspondent Banking

World Council urges the FATF to include domestic correspondent banking relationships within its definition of “correspondent banking.” The FATF’s AML/CFT guidance on correspondent banking will be the de facto AML/CFT compliance standard for domestic wire transfers even if the FATF’s official remit is technically international in scope. Many wire systems are purely domestic, including most systems operated by central banks such as the Federal Reserve Wire Network (“Fedwire”) operated by the Federal Reserve System of the United States. The phenomenon of “de-risking” also commonly affects credit unions in the domestic wire transfer context as well as in the international wire transfer context.

We urge the FATF to revise the third sentence of the definition of “correspondent banking” in Paragraph 13(a) to include domestic wire transfers by deleting “international:”

Respondent ~~banks~~ **financial institutions** may be provided with a wide range of services, including cash management (e.g. interest-bearing accounts in a variety of currencies), ~~international~~ wire transfers, cheque clearing, payable-through accounts and foreign exchange services.



Credit unions that serve internationally active memberships—such as credit unions that serve the employees of international organizations including the United Nations, the World Bank, and the International Monetary Fund—engage in substantial volumes of international wire transfers that can exceed 10,000 international funds transfers per month. These credit unions typically are respondents of money center banks for correspondent banking services and have faced challenges establishing and maintaining such relationships in the past. Increased information sharing between correspondents and respondents, including standardized approaches such as the Wolfsberg Group’s *Anti-Money Laundering Questionnaire*,² have recently made it easier for these internationally active credit unions to establish and maintain correspondent banking relationships.

Most credit unions, however, are localized institutions engaged in low-risk community banking activities and either do not engage in international wire transfers or only do so on occasion to accommodate a member who may be traveling internationally. Further, many credit unions that used to offer international wire transfers no longer do at least in part because of “de-risking.” These localized credit unions need to have access to correspondent bank accounts in order to receive loan payments from their members and disburse loan proceeds, as well as to access the interbank lending market and support other payments services.

Even a credit union that only offers savings and loans needs to have access to domestic correspondent banking services. In some jurisdictions—such as Australia, Canada, and the United States—small credit unions gain access to payments services through memberships in wholesale credit unions that provide correspondent banking services to their members. These natural person credit unions own the wholesale credit union, as its members, and are typically required to hold capital in the wholesale institution based on their level of usage of the wholesale institution’s services, like in other clearing-house arrangements.

Wholesale credit unions, as second-level cooperative organizations that are owned by their member-customers, were created to provide their member natural person credit unions with services at fair rates and therefore do not “de-risk” unreasonably. Of course, wholesale credit unions monitor the activities of their member credit unions in the same manner as other correspondent institutions, and will suspend or close a member credit union’s accounts in the event of suspicious activities that cannot be adequately explained through information sharing.

Not all jurisdictions have wholesale credit unions to provide payments and settlement services to natural person credit unions, unfortunately. In Great Britain, for example, there are no wholesale credit unions and natural person credit unions must therefore rely on high street commercial banks for correspondent banking services. The high street banks view credit unions as their competitors and are in many cases reluctant to provide even domestic correspondent banking services to small credit unions. Commercial banks have also sometimes closed credit unions’ correspondent accounts *en masse* as an AML/CFT “de-risking” strategy in other jurisdictions such as the United States.³

² Wolfsberg Group, *Anti-Money Laundering Questionnaire* (2014), available at <http://www.wolfsberg-principles.com/pdf/home/Wolfsberg-Anti-Money-Laundering-Questionnaire-2014.pdf>.

³ See, e.g., “Banks Close Credit Union Correspondent Accounts,” Heather Anderson, *Credit Union Times* (Apr. 23, 2013) (“As many as 30 credit unions in West Virginia and Ohio have been scrambling to establish new



We believe that this “de-risking” by banks in Great Britain, the United States, and elsewhere is the result of a combination of factors that intersect with AML/CFT compliance requirements, including: (i) because the level of profitability of bank’s correspondent banking relationship with a small credit union will be low compared to the perceived compliance and reputational risks; (ii) because the credit union is the bank’s competitor for loans, deposits, and payments services; and (iii) because most banks require senior management approval of correspondent banking relationships even if the correspondent account is purely domestic. The combination of these factors means that the branch manager of a bank with whom a small credit union’s manager is dealing may be reluctant to approach the bank’s senior management to seek approval for a low-profitability correspondent banking relationship with a small credit union that competes with the bank.

We urge the FATF to include domestic wire transfers within its definition of “correspondent banking.” Credit unions have faced “de-risking” in the domestic correspondent banking context as well as in the international correspondent banking context, and most banks de facto apply the FATF’s requirements, rules, and procedures regarding international correspondent banking to purely domestic correspondent relationships with credit unions.

Question 3: Assessment of the respondent institution’s AML/CFT controls (Para. 19): please confirm that the proposed high-level description reflects the process which correspondent institutions usually apply, and provide information on how this is being done in practice.

World Council urges the FATF to include the “Principle of Proportionality” under the Risk-Based Approach as part of its Paragraph 19’s high-level description on assessing the AML/CFT controls of respondent institutions, as follows:

19. In addition, the correspondent institution should critically assess the respondent institution’s AML/CFT controls. In practice, such an assessment could for example, involve reviewing the respondent institution’s AML/CFT policies and procedures and their implementation to assess if they are **proportional to the respondent institution’s AML/CFT risks as well as** in line with the applicable AML/CFT laws and regulations in the jurisdiction of the respondent institution, including targeted financial sanctions.

Most credit unions are engaged in low-risk community banking activities provided only to their members, who own the credit union and must hold at least one share in the credit union. These institutions are also usually legally prohibited from serving the general public: Credit unions typically have “common bond” restrictions set under national or provincial law that limit who

correspondent vendors after a regional and national bank terminated their accounts over the past few weeks . . . a letter . . . from Huntington [Bank] to a credit union said the decision to terminate the business relationship was the result of regulatory requirements, ‘some of which may be new or been amended since the credit union opened its account.’ The decision reflected a change in bank wide strategy, and was not a reflection on the credit union, the letter added.”), available at <http://www.cutimes.com/2013/04/24/banks-close-credit-union-correspondent-accounts?&slreturn=1470412727>.



can become a member of the credit union. Most natural person credit unions' common bonds limit their membership to people who live or work in a particular geographic area, such as a specific metropolitan area or province, or have common bonds limiting their members to the employees of particular businesses, government agencies, international organizations, military personnel, or members of a particular association. (These sponsoring organizations are also usually members of the natural person credit union.)

Credit unions are also typically much smaller than commercial banks. In the United States of America, for example, there are approximately 6,000 credit unions with a median asset size of USD 27.8 million in total assets.⁴ In the European Union, there are approximately 1,000 credit unions with an average asset size of roughly EUR 20 million in total assets.⁵

These small credit unions engaged in community banking activities to a limited community have AML/CFT compliance programs that are commensurate with the institution's AML/CFT risks, but a small credit union's compliance program will be different from a large bank's AML/CFT compliance program. For example, while large banks will typically have dozens of AML/CFT compliance officers, many small credit unions engaged primarily in savings and loan activities and with limited operating hours do not have a full-time AML/CFT compliance officer. For these small institutions offering limited services, having a part-time AML/CFT compliance officer is proportional vis-à-vis the institution's AML/CFT risks under the Risk-Based Approach because their low volumes of new loans and new deposits do not require around-the-clock AML/CFT monitoring.

We urge the FATF to clarify Paragraph 19 to include the Principle of Proportionality under the Risk-Based Approach by stating expressly that a respondent institution's AML/CFT compliance program should be "proportional to the respondent institution's AML/CFT risks."

Question 4: Nested relationships (Para. 21): please provide information and examples of: (a) monitoring measures applied by correspondent institutions to detect undisclosed nested relationship; and (b) process put in place by correspondent institutions to understand the respondent control framework with respect to nested relationships

Nested correspondent banking relationships can exist between wholesale credit unions and their members, which are natural person credit unions serving consumers at the retail level. These nested relationships—i.e. when an institution has correspondent relationships with a number of respondent financial institutions—are typically disclosed to downstream correspondents through remittance transfer information identifying the originating institution. Many wholesale credit unions also post on their websites the names of the natural person credit unions that are its members and use its services.

Wholesale credit unions monitor the payments activities of their member natural person credit unions in the same manner as other correspondent banking institutions monitor their

⁴ Credit Union National Association of the USA, *U.S. Credit Union Profile: 1st Quarter 2016* (2016), available at <http://www.cuna.org/Research-And-Strategy/Downloads/NationalProfile/>.

⁵ See European Network of Credit Unions, "Credit Unions in Europe," http://creditunionnetwork.eu/cus_in_europe (last visited Aug. 5, 2016).



respondents. If a natural person credit union that is a member of wholesale credit union uses its accounts for suspicious activities, the wholesale institution will typically suspend the ability of a member natural person credit union's ability to transact on its accounts, or close the accounts, unless the suspicious activities can be explained adequately through information sharing.

A natural person credit union's members are usually physical persons and small businesses (such as sole proprietorships), which can sometimes include companies involved in money or value transfer services (MVTs) or their agents. It is rare that a natural person credit union would serve another financial institution other than a small MVTs company or MVTs agent because most financial institutions would not be eligible to join a credit union because of credit unions' "common bond" limitations on accepting new members. A wholesale credit union will generally engage in heightened monitoring on the accounts of a natural person credit union that has a disclosed nested relationship with an MVTs provider.

Regarding detecting undisclosed nested relationships, wholesale credit unions typically look for volumes of transactions from their member institutions that would be usually high for a natural person credit union engaged in community banking. A wholesale credit union will investigate an unusually high level of volume through information requests to determine if the natural person credit union has an undisclosed nested relationship with an MVTs business. A wholesale credit union will generally suspend or close the transactional accounts of a natural person credit union that is not able to explain its unusually high volumes of transaction, as well as inform the appropriate regulatory authorities about the suspicious activities and the account closure.

Generally, this includes informing the prudential supervisor of the natural person credit union about account closures because a credit union that is not able to access correspondent banking services presents safety and soundness concerns, including acute liquidity and solvency risks. This is because a credit union that does not have access to correspondent banking services will not be able to access the interbank lending market, receive loan payments from its members or disburse loan proceeds, and could default on existing financial obligations because it would not be able to pay them on time.

World Council appreciates the opportunity to comment on the FATF's *Consultation of the Private Sector on Correspondent Banking*. If you have questions about our comments, please feel free to contact me at medwards@woccu.org or +1-202-508-6755.

Sincerely,

A handwritten signature in black ink that reads "Michael S. Edwards". The signature is written in a cursive style.

Michael S. Edwards
VP and General Counsel
World Council of Credit Unions