World Council

April 14, 2014

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

Re: *Draft Revised Guidance for a Risk-Based Approach for the Banking Sector*

Dear Sir or Madam:

World Council of Credit Unions (World Council) appreciates the opportunity to comment on the Financial Action Task Force's (FATF) *Draft Revised Guidance for a Risk-Based Approach for the Banking Sector* on anti-money laundering and countering the financing of terrorism (AML/CFT). World Council is the leading trade association and development organization for the international credit union movement. Worldwide, there are nearly 56,000 cooperatively owned credit unions in 101 countries with approximately US$ 1.7 trillion in total assets.

Please find attached with this comment letter a version of the *Draft Revised Guidance for a Risk-Based Approach to the Banking Sector* with World Council's comments incorporated as specific redline proposals, as requested. This comment letter also includes our specific redline proposals as well as World Council's support for other aspects of the draft guidance as written.

World Council supports most aspects of the proposal but has included proposed additions that would help clarify the risk-based approach (RBA) with respect to:

- Business activities that have lower money laundering/terrorist financing risks;
- Less complex financial institutions;
- Promotion of financial inclusion; and
- The concern that some banks may be "de-risking" their customer relationships by ceasing to provide correspondent banking services to credit unions and other types of businesses which handle funds on behalf of members/customers.

<u>World Council's Comments</u>

- **Paragraphs 12-16:** World Council supports the "Rationale for a New Approach" and the "Application of the Risk-Based Approach" as expressed in paragraphs 12 through 16.

- **Paragraph 16:** World Council strongly supports the statements in paragraph 16 concerning: (1) supervisors acknowledging "the degree of discretion allowed under the national RBA" for a bank or credit union to assess its money laundering/terrorism financing (ML/TF) risks; and (2) that "where the ML/TF risk is lower, standard AML/CFT measures may be reduced."

- **Paragraph 19:** In paragraph 19, we believe that supervisors providing insight into the relative risks of particular banking activities would be especially useful in jurisdictions with lower anti-money laundering/countering the financing of terrorism (AML/CFT) capacity, and urge the FATF to revise the final sentence of paragraph 19 as follows:

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"In such cases, a more prescriptive implementation of the RBA (for example, where competent authorities specify the risks typically presented by common retail banking activities as well as how particular risks are to be mitigated) may be appropriate until national AML/CFT expertise is strengthened."

- **Paragraph 22:** World Council supports revising paragraph 22 as follows in order to help clarify that a bank or credit union needs staff with skills and expertise sufficient for the operational complexity of the institution (rather than based on the operational complexity of the jurisdiction's banking industry in general, since a particular institution may be more or less complex than average):

  "Assessing and understanding risks means that competent authorities and banks need to have skilled personnel and be technically equipped to carry out this work to a degree commensurate with the complexity of the bank's operations."

- **Paragraph 28:** World Council is concerned that paragraph 28, as proposed, could be read by some out of context to nullify the impact of the FATF's guidance on financial inclusion,[1] which does not appear to be the FATF's intent.

  World Council urges the FATF to clarify paragraph 28 by incorporating the "holistic approach" language regarding financial inclusion and ML/TF risks that appears later in this RBA guidance in "Box 8," and also to provide more detail on when simplified due diligence for financial inclusion purposes may not be appropriate.

  In addition, World Council believes that the FATF should delete "a poor credit rating" as a reason impliedly justifying financial exclusion in the AML/CFT context; having poor credit does not indicate likelihood to be involved in ML/TF and many unbanked individuals have poor credit simply because they lack a credit history (i.e. they have "no credit" since the formal financial system has not extended credit to them yet).

  World Council urges the FATF to revise paragraph 28 to read as follows:

  "However, being potentially financially excluded does not automatically equate to low or lower ML/TF risk; rather, it is one factor in a holistic assessment. Financial exclusion can have many reasons, including ~~a poor credit rating or~~ a customer's criminal background and institutions should not, therefore, apply simplified due diligence measures or exemptions solely on the basis that the customer is financially excluded, especially when indicia of potential ML/TF are present."

- **Paragraph 29:** Paragraph 29 mentions supervisory agencies taking ML/TF risks into account when allocating their supervisory resources; credit unions and banks similarly have limited compliance resources and we urge the FATF to mention expressly allocation of banks' and credit unions' compliance resources based on the RBA as well:

  "The RBA to AML/CFT aims to ensure that measures to mitigate ML/FT risk are commensurate to the risks identified. In the case of supervision, this applies to the way supervisory authorities allocate their resources. It also applies to supervisors discharging their functions in a way that addresses the application of a risk-based approach by banks, and to the bank's allocation of its compliance resources."

[1] Financial Action Task Force, *Anti-Money Laundering and Terrorist Financing Measures and Financial Inclusion* (2013), *available at* http://www.fatf-gafi.org/topics/financialinclusion/documents/revisedguidanceonamlcftandfinancialinclusion.html.

- **Paragraph 34:** World Council supports proposed paragraph 34, including the statement that "[f]or individual banks, supervisors will take into account the nature and complexity of the bank's products and services, delivery channels, customer profiles and countries of operations."

- **Paragraph 41:** World Council supports the concept expressed in paragraph 41 that supervisors should compare a credit union's or bank's AML/CFT program with its peers; however, we urge the FATF to clarify this paragraph to ensure better that the peer group selected for comparison includes credit unions and banks of similar operational complexity:

  "To support their understanding of the overall strength of measures in the banking sector, supervisors should be able to compare a bank's AML/CFT programme with those of the bank's peers to inform their judgment of the quality of the bank's controls. Supervisors should, however, note that under the RBA, there may be valid reasons why banks' controls differ: supervisors must be equipped to evaluate the merits of these differences, especially when comparing banks with differing levels of operational complexity."

- **Paragraph 46:** World Council supports proposed paragraph 46 concerning supervisors issuing guidance on the RBA—especially in the case of financial inclusion guidance—however, we believe that such guidance is best developed through a consultative process with relevant stakeholders because of important rule-of-law and transparency principles, especially in the case of detailed guidance that will likely be treated as a de jure or de facto compliance requirement. We suggest revising paragraph 26 to read as follows:

  "Supervisors should communicate their expectations of banks' compliance with their legal and regulatory obligations after engaging in a consultative process with relevant stakeholders. This may be in the form of high-level requirements based on desired outcomes, risk-based rules, information about how supervisors interpret relevant legislation or regulation, or more detailed guidance about how particular AML/CFT controls are best applied. Supervisors should also consider issuing guidance to banks on how to comply with their legal and regulatory AML/CFT obligations in a way that fosters financial inclusion."

- **Paragraph 55:** World Council strongly supports the following statements in paragraph 55 regarding less complex financial institutions, as written: "A bank's risk assessment need not be complex, but should be commensurate with the nature and size of the bank's business. For smaller or less complex banks, (for example where the bank's customers fall into similar categories and/or where the range of products and services the bank offers are very limited), a simple risk assessment might suffice." We believe this guidance will help smaller institutions concentrate their AML/CFT resources on the areas of highest ML/TF risk and limit unnecessary compliance burdens.

- **Box 2:** World Council supports the "Examples of ML/TF risk associated with different banking activities" provided in Box 2 and believes that these examples will help both institutions and supervisors perform their risk analyses.

- **Paragraph 60:** World Council urges the FATF to clarify proposed paragraph 60's statements regarding a financial institution not entering into risky client relationships because we are concerned that this paragraph could have the effect of causing more banks to "de-risk" their client relationships so that credit unions and similar businesses with no connection to ML/TF have trouble maintaining access to correspondent banking services.

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Since the issuance of Recommendation 17 ("Reliance on third parties"),[2] some large commercial banks in Great Britain and the United States of America have ceased doing business with credit unions. We believe that these banks have "de-risked" their client relationships because Recommendation 17 says that "the ultimate responsibility for [customer due diligence (CDD)] measures remains with the financial institution relying on the third party" and also does not allow the bank to rely on the third party's "ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship" with the third party's customer.

In other words, these banks providing correspondent services to credit unions read Recommendation 17 as making them responsible for double-checking the credit union's CDD on its members and also requiring the banks to conduct ongoing monitoring of the transactions made by the credit union's members through the credit union if the bank processes those transactions as a correspondent. Although the FATF recommendations and guidance do not prohibit these banks from continuing to provide services to credit unions, the compliance costs and risks of serving a credit union after promulgation of Recommendation 17 apparently outweigh the potential income the bank would earn to a degree sufficient for these banks to exit this line of business.

We urge the FATF to study further the impact that Recommendation 17 is having on access to correspondent banking services for credit unions and other institutions that handle funds on behalf of their members/customers, such as small banks, money services businesses, trusts, and so forth.

For purposes of this RBA guidance, however, we urge the FATF to add the following language to the first bulletpoint of paragraph 60 in order to clarify that paragraph 60 is not intended to require a bank's senior management to "de-risk" the bank's client relationships when ML/TF risks can be mitigated effectively:

"Senior management should . . . create a culture of compliance where ML/TF is not acceptable: although a bank should not "de-risk" its customer relationships unreasonably, senior management should send a clear message that the bank will not enter into, or maintain, business relationships that are associated with excessive ML/TF risks which cannot be mitigated effectively;"

Thank you for the opportunity to comment on the FATF's *Draft Revised Guidance for a Risk-Based Approach for the Banking Sector*. If you have questions about our comments, please feel free to contact me at medwards@woccu.org or +1-202-508-6755.

Sincerely,

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

Attachment: Copy of *Draft Revised Guidance for a Risk-Based Approach for the Banking Sector* with World Council's proposed additions redlined in tracked changes.

[2] Financial Action Task Force, *International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation - the FATF Recommendations* at 18 (2012), *available at* http://www.fatf-gafi.org/topics/fatfrecommendations/documents/internationalstandardsoncombatingmoneylaunderingandthefinancingofterrorismproliferation-thefatfrecommendations.html.