World Council

April 20, 2021

Delivered Via Email: pscf@fatf-gafi.org

David Lewis
Office of FATF Secretariat
FATF/GAFI
2, Rue André Pascal
75775 Paris Cedex 16 FRANCE

Re: Mitigating the Unintended Consequences of the FATF Standards

Dear David Lewis:

World Council appreciates the opportunity to comment on the Financial Action Task Force's call for comment on the FATF standards.[1] 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 over 85,000 credit unions in 118 countries with USD 2.1 trillion in total assets serving 274 million physical person members.[2]

World Council fully supports FATF's "new project to study and mitigate the unintended consequences resulting from the incorrect implementation of the FATF Standards"; specifically focusing on de-risking, financial exclusion, suppression of NPOs, and threats to fundamental human rights. World Council acknowledges the objectives FATF has accomplished in addressing areas supporting financial inclusion and proportional regulations.

We applaud FATF's efforts to date on understanding the effects of its regulations on financial inclusion and the broader ability to provide responsible financial services to vulnerable or underserved markets. FATF recognizes that heavy regulatory burden on financial institutions facilitates money laundering and terrorist financing by discouraging financial institutions from providing services and encouraging populations to use more opaque cash transactions and non-formal intermediaries.

The FATF has been the most successful case of an international standard setter in setting practical guidance for proportional regulation. FATF has issued streamlined standards which require simple identification to open accounts, alternative documents as sufficient identification for smaller financial accounts or transactions, and then more rigorous identification documents for higher value transactions. FATF further suggests exemptions and tiered requirements for AML/CFT and KYC controls for specified types of limited lower risk transactions and services.

---

[1] See, Public consultation on FATF's Mitigating the Unintended Consequences of the FATF Standards, see: http://www.fatf-gafi.org/publications/financialinclusionandnpoissues/documents/unintended-consequences-project.html.

[2] World Council of Credit Unions, *2018 Statistical Report* (2019), *available at* http://www.woccu.org/publications/statreport.

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

However, national-level regulators are often reticent to tailor regulations for smaller, not-for-profit cooperative institutions for fear that a deviation may subject them to criticism from other nations or fear of an unintended consequence as a result of right-sizing regulations. As a result, World Council agrees that the failure of national-level regulators to properly and proportionally tailor regulations or failure or non-implementation of the FATF's risk-based approach is a serious issue. This is particularly critical in relationship to encouraging financial inclusion.

Credit unions are non-profit, member-owned institutions without stockholders that demand a market rate of return on their investment, therefore, a credit union can only pass along earnings directly to their member-owners and not to outside investors. The risks associated with a member-owned financial institutions are greatly reduced because of the smaller size in assets, the size of loans and issued credit, less complex structure, and diminished profit driven motivations because they are not beholden to stockholders.

The failure to apply a risk-based and proportional approach to regulation, especially when given instruction to do so, threatens the ability of financial institutions such as credit unions who provide necessary services to the underserved community. Adhering to overburdensome standards has proven costly for credit unions and detracts from the services they provide to its members who are oftentimes SMEs or individuals who are part of an underbanked community existing outside of the financial system. World Council therefore requests that FATF deliver explicit direction to national-level regulators to use not only a risk-based approach, as prescribed in the FATF standards, but proportional application based on the size, risk, and complexity of the financial institution. National-level regulators tend to apply the strictest standards when given a sliding scale such as a risk-based approach. In order to preserve financial inclusion, national-level regulators need clear indication that smaller, less complex institutions should not exist under a strict establishment of rules.

While international standard-setting bodies have embraced proportionality, more effort and discussion need to occur regarding how day-to-day supervision at the national level should be tailored to reflect the systemic importance, complexity, and risk profile of regulated entities. National-level regulators are often reticent to tailor international norms and standards for fear that a deviation may subject them to criticism from other nations or fear of an unintended consequence as a result of right-sizing regulations. This is evident in that proportionality strategies used to tailor regulatory requirements vary markedly across jurisdictions, including the scope, exemptions and modifications, or is some instances replacement of rules. The lack of international guidance on proportionality is in part a contributor to this disparate treatment. To remedy this situation and to assist in advancing financial inclusion, it is imperative for national-level regulators to work in connection with the international standard setting bodies to fully adopt proportional tailoring of regulations.

Financial exclusion is a fundamental issue surrounding overburdensome standards and regulations for credit unions. Credit unions per their mission are agents for financial inclusion, mainly serving underserved and underbanked communities, which in turn contributes to global growth and stability. Anytime financial institutions that are seminal to the fostering of financial inclusion are affected by burdensome regulations, it hinders its ability to provide much needed services to these underserved and underbanked communities. For example, credit unions have limited resources and capacity to monitor unlikely AML/CFT risks. Some credit unions are so small, they mostly issue nano loans for nominal amounts, but are required to maintain three

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

AML compliance officers in order to comply with the regulations. Credit unions often have minimal financial and staff resources because of the relatively small size of their assets, as such, regulatory burden is a significant issue for credit unions. The amount of staff, training and money required to monitor AML/CFT proves to be overreaching for credit unions, especially because the risk of AML/CFT violations are so low. Credit unions usually cannot afford to provide the additional measures requested by regulators to mitigate risks that do not necessarily exist.

The link between proportionality and financial inclusion has been well studied and documented as it allows the expansion of a financial institutions' ability to serve people outside the financial system. Proportionality allows national-level regulators to tailor those rules that are often designed for large, internationally active banks in such a manner that will allow a local, community based financial institution to operate. This in turn allows institutions such as credit unions to serve those underserved markets.

FATF also recognizes that **de-risking** can affect access to financial services, therefore expanding obstacles related to financial inclusion. Many of the issues arise out of the application of AML/CFT regulations and in particular the lack of proportional application of these provisions, but also from the corresponding burden associated with many of the post-crisis reforms. Further, financial institutions involved in de-risking oftentimes struggle with determining responsibility under AML/CFT requirements. Due to the fact that credit unions are member-owned financial cooperatives, banks often believe they are responsible for conducting due diligence on all credit union members. FATF has made it clear that due diligence is only necessary for credit unions board members, however, banks are often concerned that they may still incur some risk. Furthermore, the ability to conduct information sharing on a cross-border basis for AML/CFT purposes is sometimes difficult due to differing privacy standards in different countries or a lack of understanding of privacy regulations on a cross-border basis. This contributes to the unwillingness to serve smaller financial institutions.

In the recent Progress Report on FSB's Action Plan to Assess and Address the Decline in Correspondent Banking[3], the financial Stability Board notes that the decline in the number of correspondent banking relationships remains a source of concern for the international community, as the number of active correspondent banks declined by 3.4% in 2018, bringing the cumulative decline since 2011 to 19.3%, with concentration increasing with fewer correspondent banks handling payments. This remains a concern for many of our credit unions who are often challenged to establish relationships to provide effective banking solutions, often to underserved populations.

World Council appreciates the Financial Action Task Force's efforts to address concerns regarding financial inclusion, de-risking, suppression of NPOs and threats to human rights and its objective to mitigate the unintended consequences of the FATF Standards. We respectfully request that FATF direct national-level regulators to apply not only the appropriate standards under a risk-based approach, but also a proportionate approach to the standards specifically tailored to credit unions based on the size, risk and complexity of the institution. If you have questions about our comments, please feel free to contact me at pmonford@woccu.org or +1-202-510-9347.

---

[3] Financial Stability Board, *Progress Report, Action Plan to Assess and Address the Decline in Correspondent Banking* (May 2019) *available at* https://www.fsb.org/wp-content/uploads/P290519-1.pdf*.*

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org

Sincerely,

Panya Monford, Esq.
Assistant General Counsel of Advocacy
World Council of Credit Unions

World Council of Credit Unions, Inc.
99 M Street SE, Ste 300, Washington, DC 20003 • +1-202-638-0205 • +1-202-638-3410
www.woccu.org