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FSB Action Plan to Assess and Address the Decline in Correspondent Banking

Progress Report

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Executive summary

The decline in the number of correspondent banking relationships in many countries around the world remains a source of concern for the international community because, in affected jurisdictions, it may have an impact on the ability to send and receive international payments, or drive some payment flows underground, with potential adverse consequences on growth, financial inclusion and international trade. While impacts on the stability and integrity of the global financial system have not been identified, concerns remain at the national and regional level.

In November 2015, the Financial Stability Board (FSB) launched a four-point action plan[1] to assess and address the decline in correspondent banking relationships, coordinated by the Correspondent Banking Coordination Group (CBCG)[2]. The four areas of the action plan are:

- Further examining the dimensions and implications of the issue;
- Clarifying regulatory expectations, as a matter of priority, including through guidance by the Financial Action Task Force (FATF) and the Basel Committee on Banking Supervision (BCBS);
- Domestic capacity-building in jurisdictions that are home to affected respondent banks;
- Strengthening tools for due diligence by correspondent banks.

This is the sixth progress report under the initiative.[3]

SWIFT data as of end-2018 shows continued declines in the number of correspondent banking relationships during 2018. The number of active correspondent banks declined by 3.4% in 2018, which is a slight slowing of the rate of decline compared to 2017. As announced in November 2018, CPMI has assumed from FSB the publication of data updates on correspondent banking following the approval of a new 'Business Intelligence (BI) Partnership' with SWIFT.

The decline in correspondent banking relationships affected all three major currencies in 2018, although it was more pronounced for USD (-5.9%) compared to EUR (-4.6%) and GBP (-3%). Declines in 2018 affect the vast majority of jurisdictions, and 20 out of 22 regions, the two exceptions being Polynesia and Micronesia, although Polynesia remains one of the regions with the largest cumulative decline since 2011.

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1 FSB (2015), *Report to the G20 on actions taken to assess and address the decline in correspondent banking*, November.

2 The CBCG's membership comprises senior representatives from international organisations and standard setters and national authorities in the FSB and its Regional Consultative Groups.

3 The previous progress reports, for August 2016, December 2016, July 2017, March 2018 and November 2018, are available on the FSB website.

The slower rate of decline is particularly noticeable for small economies, as it is now below the world's average, although this group continues to be the most affected when looking at the cumulative decline since 2011.

As in previous years, the number of messages sent through SWIFT continues to increase, although this may be partly a consequence of longer payment chains, with more intermediaries and therefore more messages needed between them to process the same payment, at least in some regions.

Increased concentration in 2018 is indicated through a smaller number of correspondents per corridor, a higher number of messages per correspondent, and a smaller number of foreign correspondents per country. An increase in the concentration of the correspondent banking market increases the market share of remaining participants, and hence could affect competition, raise costs, and especially lead to more fragile networks since failure of a participant could have larger effects on the market and the economy. At the same time consolidation could strengthen the remaining correspondent banking relationships over the medium term as larger volumes address some of the business-related drivers of termination, leading to economies of scale due to increased efficiencies from the remaining correspondent and respondent banks. To assess the impact of concentration, the monitoring of correspondent banking data will give greater emphasis to the number of countries that have very few correspondents.

There is growing evidence of the concrete implementation of regulatory clarifications on the ground, as shown by recent workshops organised by the Asian Development Bank (ADB) and the World Trade Organisation (WTO) and industry papers such as a "Respondent's Playbook" by the Bankers Association for Finance and Trade (BAFT). For instance, the more supportive guidance on indirect correspondent banking relationships is being put in practice in projects relying on regional banks to help small local banks within the respondent's region obtain access to the international financial system. Detailed clarifications are also being implemented in the area of trade finance on expectations concerning the validation of the price of the goods financed. Such concrete measures are encouraged.

In addition to technical assistance (TA) by official sector providers, which still requires ongoing coordination, initiatives by the industry are gaining traction, especially the additional guidance developed by the Wolfsberg Group to implement their Correspondent Banking Due Diligence Questionnaire.

The technical measures recommended by CPMI to improve the efficiency of due diligence procedures and reduce compliance costs are now generally available for use, but their concrete implementation still requires continued focus by industry and the official sector. The Wolfsberg Group Due Diligence Questionnaire is still in the process of being deployed across the industry in accordance with the Group's proposed implementation plan.[4] The option to use the Legal Entity Identifier (LEI) in payment messages will not be implemented by banks before November 2021, and a number of steps remain necessary to ensure that the initiative can truly reduce costs. This is illustrated by the FSB peer review on the implementation of the LEI: such steps include reaching a sufficient number of LEIs, and reducing the costs and

4 The Wolfsberg Group (2018), Correspondent Banking Due Diligence Questionnaire (CBDDQ), Publication Guidance, February, page 6.

administrative burden of LEI issuance and maintenance. Further practical steps may also support effective information sharing, such as the effective use of requests for information by banks, or more structured data in suspicious activity reports relating to trade finance, as suggested under an ADB initiative.

Concerning the access of remittance service providers to banking services, positive steps have been taken in a number of areas to implement the recommendations published by the FSB in 2018. The FSB has published in May 2019 a monitoring report on implementation to date of the recommendations.[5] The report finds that jurisdictions have adopted or implemented a number of good practices and procedures to improve their supervisory framework and enhance coordination; authorities are responding to and accommodating innovative technology approaches in their regulatory frameworks; and significant technical assistance is being directed at the issue both at a global level and directly to affected jurisdictions.

However, further work by national authorities, international organisations, remittance firms and banks, is needed to fully implement the FSB's recommendations to address remittance firms' access to banking services. The June 2019 monitoring report sets out a number of possible next steps – aimed at national authorities, international organisations, remittance firms and banks – that could build on the progress that has already been made.

[5] Available here: https://www.fsb.org/2019/05/remittance-service-providers-access-to-banking-services-monitoring-of-the-fsbs-recommendations/

1. Data collection and analysis to further examine the dimensions and implications of the issue

1.1 Correspondent Banking Data Report published by CPMI

As announced in November 2018, CPMI assumed from the FSB in 2019 the publication of data updates on correspondent banking, following up on the publication by the FSB. CPMI published in May 2019 the analysis of SWIFT data as of end-2018.[6] This data shows continued declines and greater concentration in the number of correspondent banking relationships during 2018.

Specifically the number of active correspondent banks declined by 3.4% in 2018. This is a slight slowing of the rate of decline compared to 2017 (-4.1%) and 2016 (-3.9%). This decline affected all three major currencies in 2018, although it was more pronounced for USD (-5.9%) than for EUR (-4.6%) and GBP (-3%). The number of correspondents for all other currencies taken together declined by 2.7%. For all currency groups, this is a slowing in the rate of decline (the decline was 7.0% for USD in 2017, 6.2% for EUR, 5.8% for GBP, 4.1% for other currencies).

Similarly to 2017, declines are widespread across countries and territories, as the vast majority (206 out of the 227 with available data) saw a decrease by more than 1%.

All 22 regions examined in the data update experienced a decline in the number of foreign correspondents except Polynesia and Micronesia. The most affected in 2018 are the Caribbean (-7.9%), Eastern Africa (-6.4%), Southern Africa (-6.2%), Southern Europe (-6.0%), Southern Asia and Central America (both -5.5%), Central Asia (-5.4%), South America (-5.3%) and Eastern Europe (-5.0%). Nevertheless, six of the 22 regions saw a slower decline in 2018, contrasting with 2017 when 16 experienced a faster decline. Over 2011-2018, the most affected are Melanesia and Polynesia (-42.9% and -36.5% respectively) as well as South America, the Caribbean and Northern Africa (between -32% and -34%).

In 2018, consistent with the ranking of Western and Middle Africa as well as Polynesia and Micronesia in the table below and despite the situation in the Caribbean, the very small economies were less affected than the world's average: The set of 52 countries with a GDP below USD 10 billion experienced a reduction by 2.2% of the ratio of the number of foreign counterparties per local banks, less than the countries with a GDP between 10 and 100 billion (-3.3%) and those between 100 and 1000 billion (-3.9%). However, the 15 very large economies (GDP above 1000 billion) are still doing better in 2018 (-1.8%), and over the entire period since 2012, the very small economies remain the ones with the largest reduction in this ratio (-25.1%), compared to the 115 economies with a GDP between 10 and 1000 billion (around -21 or -22%) and the 15 economies with GDP above 1000 billion USD (-10.1%).

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[6] CPMI quantitative review of correspondent banking data, https://www.bis.org/cpmi/paysysinfo/corr_bank_data.htm.

Number of correspondent banking relationships and of direct counterparty countries per region (based on the flow of MT 103 and MT 202 excluding MT 202COV)

Table 1

	Change in the number of correspondent banking relationships (%)				Counterparty countries			
	2016	2017	2018	2011-2018	change 2018 (%)	Change 2018 (%)	2011-	Number 2018
Caribbean	-7.8	-6.4	-7.9	-32.1	-8.8		-31.6	23.8
Eastern Africa	-7.5	-7.3	-6.4	-23.8	-5.9		-18.7	35.8
Southern Africa	-3.5	-5.3	-6.2	-22.7	-2.2		-15.2	71.4
Southern Europe	-2.6	-5.8	-6.0	-21.8	-5.0		-8.7	77.6
Southern Asia	-3.5	-3.9	-5.5	-24.8	-4.2		-14.6	53.2
Central America	-3.5	-6.2	-5.5	-19.4	-4.7		-18.8	32.9
Central Asia	-6.1	-7.1	-5.4	-26.4	-3.7		-12.0	36.6
South America	-4.7	-7.1	-5.3	-34.0	-2.4		-18.6	37.3
Eastern Europe	-3.5	-5.9	-5.0	-21.1	-2.8		-10.6	87.9
Northern Africa	-8.3	-4.7	-4.6	-32.1	-2.6		-16.6	61.8
South-Eastern Asia	-1.7	-6.0	-4.5	-17.8	-4.5		-16.8	67.4
Western Asia	-4.4	-5.9	-4.5	-25.2	-4.0		-12.8	68.2
Eastern Asia	-2.2	-4.2	-4.5	-12.3	-5.2		-9.4	102.0
Western Europe	-3.5	-5.6	-4.2	-21.5	-1.9		-10.4	157.8
Melanesia	-9.9	-17.9	-3.8	-42.9	-5.9		-40.2	35.4
Northern Europe	-4.0	-6.2	-3.7	-24.4	-4.2		-15.3	108.4
Western Africa	-4.0	-3.7	-3.3	-14.3	-2.1		-2.8	38.5
Middle Africa	-3.0	-4.8	-3.3	-10.8	-1.5		-1.1	30.0
Northern America	-2.4	-2.9	-3.1	-12.2	-1.0		-7.0	95.2
Australia and New Zealand	-2.9	-3.7	-2.9	-13.2	-2.2		-9.3	132.0
Polynesia	-18.9	-13.6	0.8	-36.5	-1.8		-34.5	18.0
Micronesia	-7.1	5.1	31.7	31.7	18.2		13.0	6.5

Note: Cells highlighted in red are those where the decline in the number of correspondent banking relationships was greater than the previous year, and cells highlighted in green are those with an increase. Source: SWIFT BI Watch and National Bank of Belgium in CPMI quantitative review of correspondent banking data May 2019.

The decline in correspondent banking relationships has also driven a decline in the number of active "corridors"[7] (by 1.9% in 2018) which means fewer direct connections between countries. This is a continuation of the trend of previous years (-1.7% in 2016 and -2.4% in 2017).

At the same time, the global total of SWIFT message volumes and values related to correspondent banking continue to increase (volumes, i.e. the number of messages, increased by 4.6% in 2018 and by 3.9% in 2017, and values by 0.6% and 11.2%). Such an increase is not necessarily due to an increase in underlying activity. As noted previously by CPMI and FSB, the reduction in the number of correspondent banking relationships and of direct connections between countries could require the same payment to go through more correspondent banks in

[7] Defined as country pairs that processed at least one transaction.

multiple jurisdictions to reach destination (a longer "payment chain"), inflating the number of messages. However, data to corroborate this hypothesis is currently unavailable.[8]

An increase in message volume and a decline in active correspondents also suggests an increase in concentration. The Gini coefficient on the number of active correspondents per corridor on a constant population of corridors continued to increase slightly in 2018, now reaching 0.75.[9]

Similarly, an indicator of the number of messages handled by correspondents increased in 2018 by 15% in Africa and Oceania and between 3 and 6% in other continents. Since 2011, the increase nears or exceeds 50% in all continents except Europe and the indicator is three times higher in Northern America than on any other continent.

Concentration also means that some jurisdictions rely on a smaller number of foreign correspondents. The number of jurisdictions with 20 foreign correspondents or less has slightly increased from 39 to 42 between 2016 and 2018 for EUR, and from 21 to 24 for USD, as did the number of jurisdictions that have between 21 and 50 foreign correspondents (from 34 to 38 for EUR and 34 to 42 for USD).

As noted previously, an increase in the concentration of the correspondent banking market increases the market share of remaining participants, and hence could affect competition, raise costs, and especially lead to more fragile networks since failure of a participant could have larger effects on the market and the economy. At the same time consolidation could strengthen the remaining correspondent banking relationships over the medium term as larger volumes address some of the business-related drivers of termination, leading to economies of scale due to increased efficiencies from the remaining correspondent and respondent banks.

As noted in other reports, SWIFT, as the most commonly used messaging platform for cross-border payments, captures a meaningful amount of correspondent banking activity and the data likely delivers an accurate picture of the trends in payment traffic between jurisdictions. However, the data does not represent a comprehensive account of correspondent banking cross-border financial flows. Because financial institutions have multiple means of exchanging information about their financial transactions, SWIFT message flows do not represent complete market or industry statistics.

1.2 Ongoing monitoring of trends in correspondent banking

On several occasions, most recently at a workshop hosted by the National Bank of Belgium in Brussels in February 2019, CBCG and CPMI discussed with SWIFT the continued use of SWIFT data to support monitoring correspondent banking trends. SWIFT agreed to continue to provide aggregated and anonymised data for five additional years through the National Bank of Belgium, starting in 2019. CPMI will use the data to prepare and publish data updates on a yearly basis. CBCG will continue to collaborate with CPMI on the preparation of the reports to inform its monitoring activities.

Agreement was reached to use the new methodology described in the FSB data report of November 2018, which relies on the analysis of payment messages. The alternative

8 As part of the SWIFT Global Payment Initiative, trackers allow to identify messages that are part of the same payment chain, and the lengthening of payment chains might be measured when their use becomes sufficiently widespread.

9 A Gini coefficient of 1 would mean that there is only one active bank

methodology relied on the analysis of account statements sent via SWIFT. While this approach was explored in 2018, it was not pursued because sending account statements via SWIFT was not consistently utilised during the review period. In fact, using SWIFT account statement activity, which has recently increased, and may continue to increase, could make it appear as if the number of CB relationships has also increased although there may not be a direct correlation.

In addition to the data showing changes over a given period, SWIFT also agreed to the publication of data on the absolute number of correspondent banking relationships per country, although this information is provided by buckets (e.g., x countries with 20 correspondents or less). Because of confidentiality concerns and methodological limitations, it is not possible to publish data on the absolute number of remaining active foreign correspondents per country.[10]

As noted in previous reports, because these confidentiality constraints restrict the data analysis that can be done at the global level, detailed concentration analysis may be best conducted at the national level, using for instance the IMF methodology published in their Working Paper *Understanding Correspondent Banking Trends: A Monitoring Framework*.[11] To date, at least 10 countries have used this possibility,[12] and authorities interested in a deeper analysis are encouraged to implement such monitoring complementing the analysis of global trends. For instance, the IMF has published that the number of correspondent banking relationships has declined for Cabo Verde from 65 in 2015 to 62 in 2017 and number of active correspondents (foreign banks providing at least one correspondent banking relationship) also declined from 38 in 2015 to 33 in 2017 (22 for EUR and 16 for USD).[13] They also analyse the extent to which lost active correspondents were material (percentage of total value) and discuss possible reasons for the decline, impact on concentration, potential consequences and recommended solutions. While the CPMI report provides a list of countries with the largest declines in 2018, this level of granularity and insights is not available in the SWIFT data accessible to the CPMI and FSB.

2. Clarifying regulatory expectations

The action plan addressed the need for guidance to clarify regulatory expectations and as noted in the progress report of March 2018, the CBCG workstream dedicated to supporting a coherent and consistent clarification of expectations has completed its task with the publication of

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[10] An absolute number relying on the methodology used for the global monitoring, i.e. the analysis of MT 103 and MT 202 received (other than MT202 COV) could be misleading for several reasons: banks may use other channels than SWIFT (underestimating relationships) and in some cases (cover method, as described in previous FSB correspondent banking data reports), the exchange of an MT 103 does not reflect the existence of a relationship (overestimating relationships). These difficulties are more easily overcome at the national level. At the global level, the focus on trends reduces the impact of these issues, as notably the use of the cover method appears stable over time, at least at the global level.

[11] IMF (2017), *Understanding Correspondent Banking Trends: A Monitoring Framework*, October. This framework can be used by central banks and supervisory authorities, which can access more granular data concerning the banks they regulate to monitor the developments of correspondent banking relationships in their jurisdiction.

[12] IMF staff have provided TA on this tool to: Guatemala, Samoa, Jamaica, Guyana, Bahamas, Cayman and Belize. For 2019 TA is planned for the East Caribbean Central Bank and Turks and Caicos. The tool has also been used in IMF's surveillance (Article IV) in, amongst others, Cabo Verde, Belize and Seychelles (for Belize and Cabo Verde, Special Issue Papers have been published) and is also being used in IMF's Financial Sector Stability Review engagements (e.g. Paraguay and Cambodia).

[13] IMF Country Report No. 18/105, Cabo Verde, March 2018.

guidance by FATF and BCBS, and was therefore disbanded. [14] In the period since the last progress report, the FSB has continued to monitor the implementation of the guidance.

Implementation of the guidance by regulators has occurred mainly through updated domestic guidance or outreach measures such as circulars, discussions and communications with industry. The November 2018 progress report described these efforts based on surveys conducted by FATF and BCBS. Since that time, there is growing evidence that the national authorities have effectively put these clarifications into practice:

- FATF and BCBS provided clarifications concerning nested, or downstream, correspondent banking, which refers to the fact that a correspondent bank may be indirectly providing correspondent banking services to the respondents of its respondents. It was clarified that these arrangements are an integral and generally legitimate part of correspondent banking, provided adequate due diligence are taken to mitigate the fact that these arrangements can obscure financial transparency and increase ML/FT risks. The FSB had noted that nesting may be a way for regional banks to help small local banks within the respondent's region obtain access to the international financial system or to facilitate transactions where no direct relationship exists between banks. Participants at the WTO Expert Group on Trade Finance meeting of February 2019 reported projects in two regions (Middle East and Pacific) to build on nested relationships to increase the availability of correspondent banking services.
- The BCBS in its updated Annex on Correspondent Banking suggested a respondent bank consider having more than one correspondent banking account for its payment services, where necessary for its continued operation. In their "Respondents' playbook"[15] published in March 2019, BAFT notes that while a respondent could concentrate its business on fewer correspondents to ensure that an adequate amount of business covers the fixed costs of establishing and maintaining a correspondent banking relationship, the maintenance of at least two or three correspondent banking relationships is considered as a best practice by a majority of the twenty largest global correspondent banks that contributed to the document. BAFT also notes that "correspondents appreciate a respondent's need to mitigate the risk of rejection by engaging with more than one partner."

As explained in the previous progress report, the ADB collected from industry participants perceived challenges in the interpretation or implementation of regulations specifically related to correspondent banking and trade financing, with a focus on material and recurring issues.[16] ADB organised a workshop at the end of March 2019 in Singapore, with the participation of the FSB, IMF and WTO, to support public and private sector engagement to address issues

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[14] FATF issued further guidance in the area of correspondent banking, in cooperation with the BCBS AML/CFT Expert Group (AMLEG), including the *Guidance on Correspondent Banking Services* (FATF, October 2016), *Guidance for a Risk-Based Approach for Money or Value Transfer Services* (FATF, February 2016) and the Annex on Correspondent Banking to the *Guidelines on Sound management of risks related to money laundering and financing of terrorism* (BCBS, June 2017). In addition, in February 2018, the BCBS, CPMI, FATF and FSB welcomed the Correspondent Banking Due Diligence Questionnaire published by the Wolfsberg Group as one of the industry initiatives that will help to address the decline in the number of correspondent banking relationships by facilitating due diligence processes. See FSB (2018), BCBS, CPMI, FATF and FSB welcome industry initiative facilitating correspondent banking, March.

[15] Respondent's playbook for obtaining and maintaining a correspondent banking relationship, 2019.

[16] Beck, S. and Malaket A., (2018), *The Trade Finance Scorecard: Regulation and Market Feedback*, September.

identified in the ADB diagnostic tool. The workshop discussed several issues, some of which relate to the clarity of regulatory expectations:

- Whether further clarifications and efficiencies could be achieved concerning the identification of parties to the transactions, and the extent of banks' due diligence on non-customers (such as those involved in the shipment of goods).
- Expectations concerning the validation of the price of the goods financed, which may help detect hidden transfers through over- or under-invoicing, but is difficult due to the wide range of legitimate price variations. The International Chamber of Commerce banking commission is currently working on guidance on price checks building on the clarifications already brought by regulators in jurisdictions such as the US and Singapore.
- How to mitigate the possibility that individual examiners from regulatory agencies depart from the expectations from their agency, with the risk that "over-compliance" diverts resources and prevents the effective implementation of risk-based due diligence. Participants also discussed how adequate training of examiners at regulatory agencies on complex transactions such as trade finance could avoid misunderstandings that may result in unclear regulatory expectations.

3. Domestic capacity-building in jurisdictions that are home to affected respondent banks

Jurisdictions exited by correspondent banks are often those with actual or perceived weaknesses in their supervisory and regulatory frameworks, including frameworks for compliance with Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) standards. Concerns about weaknesses in respondent banks' risk management practices also can play a central role.

The third element in the FSB action plan supports coordination of domestic capacity building to improve and build trust in the supervisory and compliance frameworks of affected jurisdictions. Capacity building in this context extends not only to public sector initiatives, but also to the private sector.

3.1 Assessment of weaknesses and technical assistance by the official sector

National and multilateral institutions provide critical technical assistance (TA) and training activities to jurisdictions and sectors, including to those that have been affected by or are concerned with the withdrawal of correspondent bank relationships. The CBCG held a workshop in October 2018 that brought together relevant public sector TA sponsors/providers and the private sector to discuss: (1) efforts to enhance the coordination of capacity building activities; (2) how TA itself can be made more effective; (3) how the public and private sectors can collaborate to address the decline in correspondent banking relationships; and (4) next steps.

Participants noted that the cause of the decline in the number of correspondent banking relationships is not only the result of AML/CFT concerns, but include for instance business considerations, such as insufficient volume to cover the fixed costs of maintaining a relationship. As such, TA needs to be broad in its scope. That said, a considerable amount of assistance is being directed at performing national risk assessments and use of the risk-based approach. In this regard, participants thought that the effectiveness of TA would benefit from a greater degree of consistency across TA providers. Participants also suggested that the FATF-Style Regional Bodies could potentially play a greater role in the coordination and delivery of TA. It was observed that an area of focus for future capacity building could be assistance with the development of national AML/CFT guidance.

In addition to the aforementioned workshop, the CBCG has received and responded to requests for support and assistance at various public and private capacity development initiatives, conferences and other events, some of which are discussed elsewhere in this report.

3.2 Encouraging private sector training and assistance initiatives

The Wolfsberg Group published its Correspondent Banking Due Diligence Questionnaire (DDQ) in February 2018,[17] along with Publication Guidance, Completion Guidance, Frequently Asked Questions and a Glossary. The Wolfsberg Group has since been developing tutorials to help train respondent banks in completing the questionnaire and facilitate implementation.

This additional guidance will set out the purpose of each question, why the question is important and why the answer matters from a financial crime risk management perspective. The guidance will take the form of both documentation and recorded webinars, which will be made available for use not only by the industry, but also by those who provide TA either to supervisors and banks. This additional guidance is being developed not only to support a consistent interpretation of the requirements of the questionnaire as intended by the Group itself, but also to support TA across as many types of providers, whether in the public or private sector, as possible.

In March 2019, BAFT published a *Respondent's Playbook for Obtaining and Maintaining a Correspondent Banking Relationship*,[18] which provides detailed practical information to inform respondent banks about expectations of correspondents, and increase the chances that these expectations will be met. The handbook was developed based on contributions from most of the major correspondent banks, both from a business and compliance perspective.

Individually, some correspondent banks are also organising their own capacity building initiatives for respondent banks. For example, Standard Chartered's Correspondent Banking Academy initiative has been attended by more than 3,600 senior bankers from over 1,120 banks in 71 countries. The FSB Secretariat presented the FSB action plan at the Standard Chartered Academy in November 2018 to an audience of banks and regulators from the Middle East.

The CBCG assists in coordinating support for capacity building that disseminates AML/CFT regulatory guidance to the private sector. Although the mandate of most official sector authorities does not allow them to provide TA to the private sector, in some circumstances synergies can be found. The IMF has been seeking for instance to coordinate its capacity development events with TA providers assisting the private sector, to foster synergies.

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[17] The Wolfsberg Group (2018), *Correspondent Banking Due Diligence Questionnaire (CBDDQ)*, February.

[18] BAFT (2019), *Respondent's Playbook for Obtaining and Maintaining a Correspondent Banking Relationship*, March.

4. Strengthening tools for due diligence by correspondent banks

The mandate of FSB CBCG workstream 4 includes supporting the implementation of the recommendations in the CPMI report on correspondent banking of July 2016. The report included a package of measures that could help improve the efficiency of due diligence procedures, reduce compliance costs and help address perceived uncertainty, without altering the applicable rules and the basic channels for correspondent banking between correspondent and respondent banks.[19]

The FSB and CPMI are jointly supporting and monitoring the implementation of the recommendations in the CPMI report, which requires ongoing cooperation by a number of public sector and private sector bodies. As the bulk of the solutions' development at the international level is completed, the FSB has closed this CBCG Workstream on technical solutions, and CPMI has also closed its working group on correspondent banking. The remaining monitoring and outreach is conducted by the CBCG and CPMI, with the assistance of the FSB and CPMI Secretariats and other relevant working groups, such as the FSB Thematic Peer Review on the Implementation of the LEI.

In addition to the CPMI recommendations, other technical solutions addressing or offsetting the reduced availability of correspondent banking are also being proposed, including how technological innovations, such as big data and machine learning, might be usefully applied in generating and analysing information and facilitating due diligence processes.

4.1 Progress in the implementation of CPMI recommendations and next steps

1) Recommendation on the use of "know your customer" (KYC) utilities:

CPMI conducted in the second half of 2018 a survey of KYC utilities to assess the extent of adoption of the Wolfsberg Group DDQ by banks: a few hundred of responses had been collected by two major utilities, which constituted only a fraction of the population of respondent banks. This is however consistent with the progressive implementation of the questionnaire, with the large banks in the Wolfsberg Group expecting to have it implemented both for new and existing relationships by the end of 2019. This will replace the multiple bank-specific questionnaires used previously. While filling in the new questionnaire will initially increase the burden for respondents, filling in one questionnaire for all correspondents will bring later efficiencies. Another benefit of a broad use of the questionnaire is that it clearly sets a consistent expectation from correspondents to respondents.

The collection of the LEI by KYC utilities was also low, at around 8%, whereas the BIC-to-LEI mapping covers some 50% of the 40,000 BICs (excluding the branch BICs).

2) Recommendation on the use of the Legal Entity Identifier (LEI) in correspondent banking:

Implementation measures regarding the LEI include:

- ***General promotion of LEIs***: Adoption of the LEI continues to increase, with over 1.4 million LEIs having been issued as of end-April 2019, an increase by over 80,000 since

[19] http://www.bis.org/cpmi/publ/d147.htm

mid-November. The FSB published in May 2019 a report on its thematic peer review on implementation of the LEI. The report includes recommendations to fully respond to the G20 Leaders' 2012 call for "global adoption of the LEI to support authorities and market participants in identifying and managing financial risks".[20] Several recommendations, for instance on enhancing the business model, are meant to support large scale issuance of the LEI, including to non-financial entities, which is essential for a greater use of the LEI in payments.

- ***Mapping LEIs with other identifiers***: GLEIF and SWIFT are regularly publishing updates of the BIC-to-LEI[21] mapping, which covers 20,125 BICs as of February 2019 (+510 since August 2018), corresponding to 17,287 unique LEIs (+142).[22]
- ***Assessing potential uses of the LEI as a means of accessing reliable information to support customer due diligence in correspondent banking***. The BCBS has already encouraged the use of the LEI in some circumstances; for example in its *General guide to account opening*[23] and its revised guidance on correspondent banking[24]. As of end-March 2019, over 170,000 parent relationships were available in the LEI system (+30,000 since November).[25] As noted in previous reports, this may facilitate the access of this information in a standardised format and banks are encouraged to use this channel to exchange with each other information on their group structures, by registering their relevant entities and keeping the information up-to-date.

3) Recommendation on information-sharing initiatives:

The CPMI noted that privacy laws may prevent the transmission of additional information by the respondent to its correspondent concerning transactions, their originators and beneficiaries. In addition, the private sector identified this as a key issue that may lead banks to avoid high risk customers altogether, as banks may be prevented from sharing information that would clear suspicious transactions, or that would show that suspicious transactions are appropriately handled and reported. An industry group is also considering work to improve the efficient implementation of requests for information that correspondent send to their respondents when their monitoring raises an alert that requires additional information to be cleared.

The FATF *Guidance on Private sector information sharing* published in November 2017[26] highlighted that operational challenges such as inadequate IT tools, different data formats, and a general lack of appreciation of the value of information available both on the part of the public and private sector may act as barriers to information sharing, even when information is available. The Guidance also notes that templates (provided they are flexible enough), as well

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[20] FSB (2019), *Thematic Review on Implementation of the Legal Entity Identifier*

[21] Business Identifier Code. The BIC is used to identify banks in correspondent banking messages, but for historical and other reasons, a bank may have several BICs. The LEI is a unique identifier for legal entities.

[22] GLEIF (2018), Download BIC-to-LEI Relationship Files, February.

[23] BCBS (2017), *Guidelines: Sound management of risks related to money laundering and financing of terrorism*, Annex 4, June.

[24] BCBS (2017).

[25] This covers not only banks but any legal entity. Relationship data is available at GLEIF, Download the Concatenated Files.

[26] FATF (2017), *Guidance on Private sector information sharing*, November.

as standardisation of data formats may promote data sharing by enabling integration. The ADB workshop of March 2019 discussed that greater standardisation of certain information included in Suspicious Activity Reports (SARs) could enhance their usability for law enforcement, especially across border. This standardisation could also increase the likelihood that criminal flows be effectively disrupted and that banks receive feedback from their SARs filing, thereby facilitating a more accurate assessment of risks and more informed decisions on the allocation of monitoring resources and provision of trade finance. Participants discussed how the industry could, in cooperation with Financial Intelligence Units, develop suggestions for more structured reporting of suspicious activities on trade finance. For instance, a tag signalling suspected trade-based money laundering could help direct the report to relevant experts in FIUs. The use of the LEI, and in the future other identifiers currently under development within ISO (Unique Transaction Identifiers and perhaps a natural person identifier) could help FIUs identify automatically that the same transaction has been reported by several institutions, and also that the same entities have been reported several times. This would help address the risks of trade based money laundering with enhanced analytical capabilities, rather than risk avoidance through a reduced provision of trade finance.

4) ***Recommendation on payment messages, with a focus on the correct use of available methods for payment.***

As described in previous reports, recommendations have been issued by the BCBS (on supervisors' expectations regarding the quality of payment message content) as well as by the Payments Market Practice Group (PMPG) in June 2017 (on the correct use of the MT 202 COV payment messages[27]) and by the Wolfsberg Group in October 2017 (revised version of their Payment transparency standards[28]). Furthermore SWIFT announced that migration of correspondent banking payment messages to ISO 20022 should start in November 2021, which as noted by the Wolfsberg Group would support addressing the lack of sufficient capacity in certain payment message fields to transmit all the information (although the transition will take some time, during which truncation issues will subsist).

5) ***Recommendation on the use of the LEI on an optional basis as additional information in payment messages:***

In November 2017, as recommended by CPMI, the PMPG published an option for identifying the originator and beneficiary of wire transfers in current message formats by using an LEI.[29] However, banks are reluctant to invest in upgrading the current formats, given the preference for replacing current message formats with ISO 20022, where the LEI was added in early 2019 as a defined data type. The FSB LEI Peer Review report notes that the completion of these options to insert the LEI into payment messages may be an opportunity to propose an internationally agreed timeline for the effective use of the LEI in payment messages.[30] The

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27 PMPG *Guidelines for the use of MT 202 COV*, June 2017, https://www.swift.com/resource/guidelines-use-mt-202-cov.

28 https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/wolfsberg-standards/1.%20Wolfsberg-Payment-Transparency-Standards-October-2017.pdf.

29 PMPG *LEI in the Payments Market*, November 2017,.

30 FSB (2019), *Thematic Review on Implementation of the Legal Entity Identifier*

Correspondent Banking Coordination Group will work with LEI Regulatory Oversight Committee (ROC) and Global LEI Foundation (GLEIF) and industry bodies such as the Wolfsberg Group and PMPG.[31] The aim of this collaboration will be to document the efficiency gains that could be achieved through substantive use of the LEI, determine whether the information currently available in or through the Global LEI System (GLEIS) is adequate to support due diligence or needs to be augmented (e.g. beneficial owners, directors, industry sector), and whether there are types of entities for which LEI adoption should be prioritised. Such discussions will also be coordinated with the examination by the LEI ROC and GLEIS of enhancements to the GLEIS business model meant to facilitate LEI issuance and reduce costs.

In February 2019, the FSB Secretariat organised a meeting between the World Customs Organisation (WCO), the GLEIF, the LEI ROC and the WTO to discuss potential synergies between the Trader Identification Number (TIN) defined by the WCO and the LEI. The TIN is the combination of a two-digit alphanumeric ISO country code and another identifier used by customs in that country, creating uniqueness and standardisation of the identification number and its underlying entity information at global level. Participants discussed the similarities in the population of legal entities covered, for instance when importers or exporters hedge their forex risks with derivatives, and use their LEI when reporting these transactions. Participants also reviewed the potential complementarity, as the LEI would bring for instance information on parent relationships or successor entities, whilst TIN includes information on regulatory status of the entity (e.g. as an Authorized Economic Operator - AEO). Participants agreed to continue discussions on how the synergies could materialise. A wider use of the LEI by multiple players in trade could reduce costs, facilitate due diligence, and contribute to manage the higher risks that may deter correspondent banks from accepting to process trade finance transactions, at least in some jurisdictions. Similarly, the TIN specifications and data exchange mechanism foster greater standardisation and efficiency in cross border trade transaction and enable international cooperation between customs and other government agencies (of the exporting, transiting as well as importing countries) such as in the area of mutual recognition of control.

4.2 Potential public sector involvement in other technical solutions

No further developments were reported on the scope for public sector actions, at the national, regional or international level, to support technical solutions addressing or offsetting the reduced availability of correspondent banking since the publication by the IMF of their April 2017 report *Recent Trends in Correspondent Banking Relationships – Further Considerations*.

4.3 Potential applications of financial technologies

In response to a request from the Japanese G20 Presidency, the FSB will publish a report in June 2019 on the financial stability implications of decentralised financial technologies for the governance of financial regulation. The analysis, which is conducted by a working group under

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[31] In its Discussion paper "LEI in the Payments Market" of November 2017, the PMPG noted that "the ability to clearly identify the originating and beneficiary parties with LEI (and therefore having additional transparency on these parties) could bring significant quantitative and qualitative benefits on a strategic basis, mainly for compliance and risk management functions", for instance, "eliminating potential delays during payment processing from false hits in compliance and sanctions screening; optimized and more accurate AML controls and detection of suspicious activities and ability to identify ordering and beneficiary customer as meaningful information for correspondent banks acting as intermediary in the payments chain".

the FSB Standing Committee on the Analysis of Vulnerabilities, will include the impact of decentralised technologies on correspondent banking and trade finance.

5. Monitoring of recommendations to improve remittance service providers' access to banking services

As stated in the G20 Hamburg Action Plan of July 2017, the FSB is coordinating work, together with the FATF and the Global Partnership for Financial Inclusion, to address remittance service providers' access to banking services that are not already being dealt with through existing initiatives. In March 2018, the FSB published a report that set out 19 recommendations in four main areas that, if implemented, may contribute to greater access of banking services by remittance service providers.[32] The four categories of recommendations are as follows:

- Promoting dialogue and communication between the banking and remittance sectors;
- International standards and oversight of the remittance sector;
- The use of innovation in the remittance sector and its possible role in enabling greater access of remittance service providers to banking services; and
- Technical assistance on remittance-related topics.

The FSB has published in May 2019 a monitoring report on implementation to date of the recommendations.[33]

The reduction in correspondent banking relationships has had a significant impact on remittance service providers' (RSPs') ability to access banking services, particularly acute in those developing countries where remittance flows are a key source of funds for households. In many of these jurisdictions remittances represent a significant percentage of Gross Domestic Product.[34]

The cost of sending remittances also remains a concern to the international community, which has supported efforts to reduce those costs to end-customers; indeed, costs have declined over the past decade and as of the fourth quarter of 2018, the cost of sending USD 200 was 7.01%. Nevertheless, this remains well above the United Nations' Sustainable Development Goal target of 3%.

The FSB's focus has been on work to address RSPs' access to banking services that are not already being dealt with through existing initiatives. The FSB's 2018 stocktake report identified a variety of intertwined drivers for the termination of banking services to RSPs, including profitability, the perceived high risk of the remittance sector from an AML/CFT perspective, supervision of RSPs that ranges from active and effective to complete absence and, in some jurisdictions, weak compliance with international standards, particularly those relating to AML/CFT.

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[32] FSB (2018), *Stocktake of remittance service providers' access to banking services*, March.

[33] FSB (2019), *Remittance service providers' access to banking services: Monitoring of the FSB's recommendations*, May

[34] As noted in the FSB March 2018 report, based on World Bank data, inflows from remittances were equivalent to more than 10% of 2015 GDP in 29 countries, and more than 20% in eight of them. See World Bank (2017), Migration and Remittances Data, November.

The May 2019 monitoring report follows up on the recommendations in the 2018 report and finds that, while positive steps have been taken in a number of areas, further work by national authorities, international organisations, RSPs and banks, is needed.

Jurisdictions have adopted or implemented a number of good practices and procedures to improve their supervisory framework and enhance coordination; authorities are responding to and accommodating innovative technology approaches in their regulatory frameworks; and significant technical assistance is being directed at the issue both at a global level and directly to affected jurisdictions.

Dialogue between RSPs, banks and authorities responsible for supervision of the remittance sector has been useful, but has not led to tangible next steps. In order to make further progress, it is important to have a common understanding of issues facing RSPs in their access to banking services and banks' expectations concerning RSPs' AML/CFT compliance.

As stated in the 2018 report, international standards relevant to RSPs appear sufficient. However, while implementation of international standards is taking place at the domestic level, the state of progress varies quite widely: many jurisdictions do not appear to have robust supervision for RSPs and quite a few do not effectively supervise them at all. Guidance by national authorities to RSPs on AML/CFT obligations, strengthening of supervision and further dialogue with banks and RSPs concerning regulatory expectations are all areas in need of attention.

Innovation is a helpful solution to the challenges faced by RSPs, but it is likely only part of a broader solution. National authorities are encouraged to continue facilitating innovation through regulatory sandboxes and innovation hubs, and supporting the developing FinTech firms while ensuring that they are subject to appropriate AML/CFT requirements.

Significant amounts of TA have been directed to the remittance sector, but there is a need for better coordination of TA and more focused TA on oversight of the remittance sector and the development of national risk assessments.

The May 2019 monitoring report sets out a number of possible next steps – aimed at national authorities, international organisations, RSPs and banks – that could build on the progress that has already been made, as follows:

- FATF (in cooperation with the BCBS for issues pertaining to risk management in the context of banking supervision):
  - to continue monitoring actions by national authorities to implement standards and guidance as they relate to remittance firms through mutual evaluations and follow-up reports.
  - to consider organising a workshop for national authorities to identify and share effective practices on supervision, licencing and enforcement in the remittance sector.
- FSB to coordinate:
  - provision of remittance-related TA, through the CBCG TA workstream.
  - development of guidance on communication strategies for jurisdictions in explaining the steps they have taken to address perceived weaknesses in

regulatory frameworks for remittance firms (using as a model the guidance it has provided on communication strategies relating to regulatory frameworks for correspondent banking).

- FSB to convene the official sector, banks and remittance firms:
  - to encourage banks and remittance firms to work together to develop guidance on information that RSPs should provide to banks to facilitate due diligence.
  - to discuss the scope for development of standardised tools targeted towards remittances that would facilitate customer due diligence and reduce costs.