

December 7, 2015

Secretariat of the Committee on Payments and Market Infrastructure
Bank for International Settlements
CH-4002 Basel
Switzerland

Via email to cpmi@bis.org

Dear Sir/Madam:

The American Bankers Association¹ appreciates the opportunity to provide comments to the Committee on Payments and Market Infrastructure (CPMI) on its Consultative Report on Correspondent Banking² (the Report) issued on October 6, 2015.

ABA supports further exploration of certain recommendations made in the Report that could make improvements to the cross-border payments marketplace, but it is vital to note that one key factor leading to the decline in correspondent/respondent banking relationships is the heightened regulatory burden on banks related to anti-money laundering and counter terrorism compliance. Even though it is identified as a causative factor, steps to alleviate the regulatory burden are not addressed in the Report.

Consultative Report Overview

The Bank for International Settlements (BIS) directed the CPMI to draft the Report addressing concerns related to the correspondent banking marketplace. BIS' concerns center on the current trend where correspondent banks are terminating relationships with respondent banks due to the high costs of compliance with extensive regulatory requirements. Some correspondent banks are making the rational decision to reduce their regulatory and reputation risk by reducing exposure to respondent banks. As the number of formal bank relationships declines, BIS believes the risk of upsetting the current cross-border payments structure increases.

BIS acknowledges that high regulatory compliance expectations placed on correspondent banks have caused them to reevaluate their relationships with some banks. The types of regulation creating the most friction include Anti-Money Laundering, Countering the Financing of Terrorism (CFT), and Know-Your-Customer (KYC). For example, one of the new expectations is that banks will closely monitor transactions that are conducted through correspondent accounts, particularly foreign correspondents. Due to these regulatory burdens, correspondent banks have reduced the number of relationships with banks that don't generate enough volume to offset compliance costs, are located in perceived geographically risky areas, or provide payment services to customers who can't be adequately rated for risk.

In the Report, the CPMI notes that regulatory oversight is the primary driver of the shifts in the correspondent banking ecosystem. However, the recommendations in the report do not address this subject. Rather, the Report poses four recommendations that may reduce the friction

¹ The American Bankers Association is the voice of the United States' \$15 trillion banking industry, which is comprised of small, regional and large banks that together employ more than 2 million people, safeguard \$11 trillion in deposits and extend more than \$8 trillion in loans.

² Bank for International Settlements, Published October 6, 2015, <http://www.bis.org/cpmi/publ/d136.pdf>

involved in correspondent banking, but the “...measures will not immediately help the banks without access to correspondent banking services to gain such access.” The Report attempts to make improvements around the margins of the problem, but does not address the problem itself. The Report actually makes no direct recommendations. Instead, it suggests that all four of the recommendations be reviewed by other relevant stakeholders to be refined and to determine their merit.

The four technical recommendations proposed in the Report are:

Increase the use of KYC utilities by standardizing the templates and data fields to reduce the administrative burden associated with multiple requests for similar information made by banks to payments senders and receivers. The Wolfsberg group is recommended to consider this proposal in more depth.

Promote the use of Legal Entity Identifiers (LEIs) to identify parties to facilitate the use of KYC utilities and information-sharing arrangements. The Wolfsberg Group is recommended to consider this proposal in more depth.

Request the Financial Action Task Force (FATF) and the Basel Committee on Banking Supervision AML/CFT Expert Group (AMLEG) provide clarity on the due diligence recommendations for upstream banks including details on what is expected of knowing a customer’s customer. The Report also recommends promoting the use of information-sharing mechanisms, if possible, within the constraints of local privacy laws. FATF and AMLEG are recommended to consider this proposal in more depth.

Determine whether the MT 202 COV payment message is efficient and meeting expectations or whether the industry should rely solely on the MT 103 message. The Wolfsberg Group is recommended to consider this proposal in more depth.

ANALYSIS AND RECOMMENDATIONS

Increase the use of KYC utilities

The Report describes KYC utilities as entities that “...store in a single repository relevant due diligence information.” This simplifies the process where correspondent banks must request voluminous documents from each respondent bank then review it during the due diligence process. Respondent banks must respond to these requests for each of the correspondent banks it works with. Using a KYC utility would make it more efficient for respondent banks that would now only have to provide documents to one source and to correspondent banks that would have one central place to access information.

The Report notes that several utilities are in operation currently, but that there is no standardization in the type and format of information that is gathered. The inconsistent gathering of information limits the value of the current services.

The Report recommends that the Wolfsberg Group review the KYC utility marketplace to review the templates and procedures used currently to compile the “most appropriate data fields” that should be collected and for banks to rely upon when conducting due diligence.

ABA supports the recommendation that the Wolfsberg Group explore the possibility of leveraging KYC utilities although we do not believe this contributes substantively to solving the stated problem of costs associated with heightened regulatory compliance within a reasonable amount of time. For this solution to be effective, in addition to harmonizing the data and formats, it would be necessary to have the global regulatory community clearly state that correspondent banks can rely on the information in the utilities for the purposes of compliance. If

correspondent banks do not have this assurance they will continue to conduct their own individual due diligence data gathering, negating the value of KYC utilities.

Promote the Use of Legal Entity Identifiers (LEIs)

LEIs are unique alpha-numeric codes that identify specific legal entities that are counterparties to financial transactions. At the end of 2014, more than 330,000 LEIs had been issued in 180 countries. LEIs contain information such as name and address for each associated entity. This is valuable because the same information is required for cross-border transactions. LEIs could be applied to the payor and payee as well as being used to identify the banks in the transaction. Using LEIs could make screening for prohibited parties simpler.

The Report acknowledges that LEIs will not provide a complete solution for identifying payment stakeholders because they cannot be applied to individuals and even assigning them to all commercial entities will take a very long time.

Another challenge to overcome is integrating the Business Identifier Code (BIC) into the LEI system. BICs are used as a routing code and account identifier for cross-border transactions. Correspondent bank information technology systems that are built around that data stream would need to have a mapping utility to associate BICs to LEIs that does not exist currently.

The Report recommends that the Wolfsberg Group consider the promotion of LEIs as applied to legal entities as well as for all banks involved in a transaction to be used in KYC utilities and information-sharing arrangements. The Report also requests the Wolfsberg Group consider promoting a BIC to LEI mapping mechanism.

ABA supports the recommendation that Wolfsberg Group explore this issue. As with the previous recommendation, the global regulatory community will need to allow banks to rely on LEI information with regard to KYC regulations. Without that clear safe harbor, banks would be required to continue to conduct their own costly due diligence regardless of the inclusion of LEI information.

A second challenge, would be the process of mapping BICs to LEIs and inclusion of the LEI in payment messages. This will provide more value once the global regulatory community has approved the concept that banks can rely on LEIs to identify parties for compliance purposes. A consultative group representing the public and private sectors can be formed to address any technical challenges posed by expanding the use of LEI.

Similarly to the first recommendation above, we agree that using LEIs in cross-border payments may add some efficiencies in the long term. However, in spite of ABA's support of the LEI through its CUSIP Global Services facility (CUSIP assists in the assignment and maintenance of LEIs in some markets), we recognize that the LEI in itself will not provide relief to correspondent banks making the decision to discontinue ongoing respondent bank relationships due to rational concerns about regulatory risk.

Information-Sharing

Correspondent banks' KYC responsibilities may increase when they do business with certain customers. If a customer operates in a jurisdiction with a higher risk for money laundering the

correspondent bank's obligations are greatly increased to properly assess and address the commensurate risk.

Meeting these expectations can be challenging for many reasons, including that the respondent bank may be restricted in what information it can share on its customers with the correspondent bank due to privacy regulations in their jurisdiction. Further, even if correspondent banks do receive the information, it would be incomplete if they don't have knowledge about transactions conducted with other banks or the identities of the counterparties. Also, respondent banks may have relationships with multiple customers making providing the same information to multiple correspondent banks administratively burdensome and expensive.

The Report proposes that creating information-sharing mechanisms could be a possible solution to this challenge. These databases would be populated by banks with information about their customers and their customers' transactions. Respondent banks would provide the data one time to a central location and correspondent banks would be able to pull data as needed. This clearing house model would increase efficiency by reducing the number of transfer points between correspondent and respondent banks. Aggregating the data would allow comprehensive tracking of customer activity even if they use multiple banks.

The Report recommends that FATF and AMLEG review the concept with regard to clarifying the due diligence obligations as well as the data privacy concerns in the area of correspondent banks. The Report also recommends the group work to identify the type of data that information-sharing mechanisms could store and distribute to be effective.

While conceptually promising, the practical application of information-sharing mechanisms has significant obstacles to overcome. Many jurisdictions have strong privacy and data security laws and regulations that provide different levels of protection for safeguarding customer information. Sharing information across borders makes complying with these laws even more difficult. The value of the information-sharing data base is only as good as the information that it houses, in turn placing a large responsibility of respondent banks to provide accurate information. In addition, regulatory changes may be needed granting correspondent banks a safe harbor if they rely on information supplied by the correspondent banks.

ABA supports efforts by FATF and AMLEG to develop an effective information-sharing mechanism to support correspondent and respondent banks to meet their regulatory obligations. But, again, we expect this to be a long-term project requiring regulatory coordination across multiple jurisdictions and it will not serve to benefit correspondent/respondent bank relationships in the near term.

ABA endorses an approach where authorities recognize what information is actually available to a bank and does not create unrealistic expectations that banks will gather information that is not ordinarily obtained in the normal course of business. Additionally, authorities should recognize that intermediate banks that lack a relationship with the customer or the beneficiary, should not be expected to have sufficient knowledge about the transactors to make definitive determinations about the transaction. As FATF and AMLEG consider this issue we recommend that they consider the information that is actually available to banks in practice.

Payment Messages

The Report outlines the process flows for two different types of cross-border transactions. The serial method uses the MT 103 payment message, where the payment message and settlement

instructions travel together. Alternatively, the cover method uses the MT 202 COV payment message that decouples the payment message from the settlement instructions. MT 202 COV payments must contain all of the information required for AML/CFT compliance for the use of any intermediate banks that touch the payment.

The Report describes the differences between the serial method and the cover method that was introduced in 2009. It acknowledges that the MT 202 COV was the result of a common effort and long consultation process within the industry, but notes that there have been some anecdotal concerns that these payment messages may not be as safe as MT 103 payments for AML/CFT purposes.

The Report recommends that the Wolfsberg Group review whether MT 202 COV payments are efficient as they were intended or whether the industry should rely solely on MT 102 serial payments.

ABA opposes the Report's recommendations that MT 202 COV payment message be considered for elimination by the Wolfsberg Group in lieu of the MT 103 payment message. The MT 202 COV payment was developed after significant international effort to provide the appropriate level of transparency in international wires. Discarding that mechanism would resurrect the problems that the MT 202 COV was designed to address.

Any perceived difference in AML/CFT risk does not lie in the type of payment message used. The risk lies in the party that supplies the required information. A bad actor could provide misleading information in either type of payment message. It is important to work with the entire industry to ensure that valid data travels with both types of payment message, but allow the banks to choose the message type based on the business needs of the customer.

ABA appreciates the Committee's efforts to make correspondent banking more efficient and we are grateful for the opportunity to comment on the Consultative Report. We support exploring three of the Report's four recommendations to improve the correspondent banking marketplace, but we must reaffirm our position that these recommendations are focused on limited corrective actions that will have minimal impact on the stated problem of decreasing correspondent/respondent bank relationships. The central challenge of complying with heightened AML/CFT and KYC obligations is the primary driver of this trend and it is not addressed in the Report. Should you have any questions, we are available to discuss any of these issues in detail.

Sincerely,

A handwritten signature in dark ink, appearing to read "Stephen K. Kenneally". The signature is fluid and cursive, with the first name "Stephen" and last name "Kenneally" clearly distinguishable.

Stephen K. Kenneally
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