Who's driving the ship?
De-risking and governance of the AML regime

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I. Introduction

Research on money laundering and anti-money laundering (AML) leads to common frustrations about data.[1] Judging the effectiveness or efficiency of different interventions is impossible without reliable evidence, yet in such a fluid policy field, the need for empirical clarity is paramount.

The case of AML-related de-risking is an important and illustrative example. Around five years ago, AML industry professionals began using "de-risking" to identify a trend that saw financial institutions denying services to whole groups of clients. Crucially, institutions were reportedly not making those decisions based on the risk profiles of individual clients, as is standard, but on a categorical characteristic: for example, money remitters or banks in the Caribbean. Non-profit organizations got caught up in this financial dragnet, as well. The United States House Financial Services Committee held two hearings on de-risking and its effects.[2] De-risking quickly rose to the top of the agenda in AML compliance circles and beyond. Yet the empirical basis for that agenda was minimal at best.

FATF around this same time had begun pushing states to measure real effectiveness, a step all agreed was long overdue. Why was it not at the top of the agenda? Why was financial inclusion not a higher priority? It had been around longer. The answer helps us better understand governance within the AML regime more broadly. Who drives the agenda?

In this paper, we take a "sociology of knowledge" approach to the emergence and rise of de-risking on the AML agenda. We use it as a case study of AML governance more generally. For evidence, we draw on analyses of social media, official speeches, reports on the empirics of de-risking, and elite interviews. We also draw on our combined experience as participant observers in the AML world, especially through professional conferences. That includes the collective findings of a 2-day workshop on de-risking in the

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[1] We acknowledge the valuable research support of Malasia McClendon and Mark Klose.
[2] Those hearings are available on-line: https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=401187 and https://docs.house.gov/Committee/Calendar/ByEvent.aspx?EventID=108496.

Caribbean that involved a wide variety of voices: international financial institutions, NGOs, banking officials from the Caribbean, and US regulators.[3]

In short, the case of de-risking suggests there is a changing roster of hands guiding the AML ship. AML advocate states and experts had pushed the AML regime to a seemingly ever broader and deeper application, often over the objections of the regulated groups. It seems the targets of AML regulation now have found their voice and the de-risking agenda is the result. We show, first, that de-risking is a new concern with an identifiable beginning. As compared to the issue of effectiveness, which has seen its importance wax and wane over time, de-risking burst onto the agenda, rather than slowly moving up the agenda. It also has gained political importance within the regime. Second, we show that the prioritization of de-risking arose through informal channels: strategic chatter among industry professionals that worked its way to the attention of regulators and standard-setters. It did so, however, without a strong empirical basis to understand the causes, extent, and effects of de-risking. Third, various bodies have worked to provide an empirical basis for decision-making around de-risking, but there are still important gaps in our knowledge. As a result, the conversation around solutions to de-risking still outpaces the community's grasp of the empirical realities of the problem they seek to resolve. The available data on de-risking raise important questions about the assumption underlying most of the proposed solutions, especially those prescribing de-regulation.

This is not to suggest that de-risking should be ignored. Extensive de-risking--whatever its true drivers--poses serious risks to the wellbeing of developing countries and to the integrity of the international financial system. In line with this workshop, however, responses to de-risking should be founded in more empirical evidence than has been garnered to date. Otherwise, we increase the chance that the solution misses, or even exacerbates, the problem we are trying to address.

Our exploration of de-risking and its importance unfolds in four further sections. Below we discuss what a sociology of knowledge us analytically. In section 3, we lay out the empirics of de-risking, including a background on the term, how it emerged onto the AML agenda and within the broader compliance community, and then compare that with the data available at the same time. In section 5 we attempt to tie the pieces together in a comprehensive analysis. There we draw on two further bodies of empirics: an initial assessment of banks fines levied by the OCC and SWIFT data on trends in correspondent banking. We conclude by discussing the implications of our findings and our plan for future work.

II. Logic of Enquiry and Methodology

For the sake of this workshop, we refrain from diving into a full review of the literature on AML and the governance of illicit finance. Suffice it to say that scholars differ on who really steers the AML regime. Some argue that the US and/or EU specifically dominate.[4] Others suggest that a broader range of states matter, but agree that material concerns and material tools remain primary.[5] Some place great emphasis on the constitutive nature of the governance process itself, including all the state actors, but also increasingly

[3] The workshop was funded by the Americas Center at the Federal Reserve Bank of Atlanta. Participants followed the Chatham House Rule, so we do not attribute any information here to particular participants. We report them instead as general findings of the workshop.

[4] Drezner, D.W., 2005. Globalization, harmonization, and competition: the different pathways to policy convergence. *Journal of European Public Policy*, *12*(5), pp.841-859.

[5] Sharman, J.C., 2011. *The money laundry: Regulating criminal finance in the global economy*. Cornell University Press; Jakobi, A.P., 2013. *Common Goods and Evils?: The formation of global crime governance*. OUP Oxford; Morse, J., 2019. Blacklists, market enforcement, and the global regime to combat terrorist financing. *International Organization, Forthcoming*.

non-state actors.[6] Some emphasize that the ballooning compliance profession has a very strong influence on the content of AML governance.[7]

AML governance is also a fluid policy space.[8] Participation in the regime has grown significantly as the regime's reach has expanded to more and more issues and regions. What may have been true of AML governance in 1990 is likely untrue 30 years on. We use the de-risking agenda as a case study of AML governance today and for comparing it with governance in the past.

We conduct a sociology of knowledge of the de-risking agenda. Knowledge is "any and every set of ideas accepted by one or another social group or society of people, ideas pertaining to what they accept as real."[9] A core premise of the approach is that having some "reality" requires that we have knowledge to tell us about it.[10] With regard to de-risking, then, we ask what knowledge we had or have about de-risking. To what degree is there a consensus around the reality of de-risking and where did that consensus (or disensus) come from?

If knowledge is a set of ideas accepted by a social group, then the production of that knowledge is a reflection and source of power within the group. A sociology of knowledge prods us to ask how certain problems come to be defined as problems, which problems are ignored, and who gains what power from that "knowledge."

The framework also draws attention to the contested nature of what different social groups might accept as knowledge on a given topic. Because the mastery or production of knowledge grants authority, contests over "knowledge" are rarely "just" differences of opinions or interpretations.[11] They are contests over authority. A sociology of knowledge framework also emphasizes that "all forms of knowledge, no matter how lofty or authoritative, have human origins and feed and fatten off groups' interests and needs."[12]

For some the assertion of no reality without knowledge or the idea of multiple knowledges may come across as post-modernity at its peak. History is rife with examples. One important example is medieval debates over science and the church. Knowledge about the nature and structure of the universe created "reality." When science produced new realities by producing new knowledge, no one talked about a sociology of knowledge. It is clear, however, that the parties involved understood perfectly well that a fight over the production of knowledge ultimately was a fight over authority.

Finally, knowledge is a *social* construct that cannot exist without transmission, so the transmission of knowledge is a vital part of the inquiry. This brings into focus the media of transmission, both for the content of that transmission as well as how the media themselves structure power among participants in the conversation. This perspective also encourages us to consider what has not been transmitted: what has not become part of the collective memory that comprises knowledge.[13]

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[6] Hülsse, R., 2007. Creating demand for global governance: The making of a global money-laundering problem. *Global Society*, *21*(2), pp.155-178; Nance, M.T., 2018b. Re-thinking FATF: an experimentalist interpretation of the Financial Action Task Force. *Crime, Law and Social Change*, *69*(2), pp.131-152.
[7] Tsingou, E. 2018. "New governors on the block: The rise of anti-money laundering professionals." *Crime, Law, and Social Change* 69: 191-205.
[8] Nance (2018) argues that this has been a defining characteristic of FATF from its founding. Nance, M.T., 2018. The regime that FATF built: an introduction to the Financial Action Task Force. Crime, Law and Social Change, pp.1-21.
[9] McCarthy, E. Doyle. *Knowledge as Culture: The new sociology of knowledge*. Routledge. P. 2.
[10] *Ibid*.
[11] *Ibid*, p. 3.
[12] *Ibid*., p. 5.
[13] Swidler, Ann and Jorge Arditi. 1994. "The New Sociology of Knowledge." *Annual Review of Sociology*, pp. 305-29.

With this framework in mind, we seek to meet X basic goals. First, we aim to trace the production of knowledge (or knowledges) around de-risking. What did and do we accept as knowledge and why? Who generated that knowledge? Second, how was that knowledge diffused? Third, how is that knowledge being used to attain particular political goals? Third, what does this tell us about governance of the AML regime?

We draw empirical evidence from three types of sources. First, we carefully trace the agenda itself, verifying when de-risking make its way onto the literal agendas of the main AML bodies, including major national regulatory bodies. This covers meeting agendas, formal statements, and speeches by AML leaders. It also includes preliminary interview research with key actors. The data establishes that de-risking has become an agenda item and determines when it broke through.

Secondly, we report on an analysis of social media as a means of "observing" the conversations that the compliance industry was having around de-risking. In this iteration of the paper we focus only on the timing and intensity of that conversation.[14] By itself this analysis is unable to answer any of the questions we have about de-risking, but it establishes that de-risking is a new topic within AML and that there is an inflection point, after which de-risking becomes a major topic of discussion among compliance experts. We provide more details about our use of social media in the relevant section below. Together, these two streams of evidence help us understand who is talking--or producing knowledge about--de-risking and how they understand the issue.

Finally, having established more clearly a timeline for the agenda, we look at existing data around de-risking, documenting what data was available and when. This evidence helps us understand whether the conversation around de-risking was a data-driven question, or whether there were other reasons it became topical.

III. The empirics of de-risking

IIIa. Background

In its broadest connotation, de-risking is a strategy to reduce the risk associated with a given investment. In the early 2000s, people were writing about de-risking through "liability-driven investing," a means of protecting pensions from market swings. The World Bank talks about ways to "de-risk" investments in infrastructure projects.[15]

In the past five years, however, de-risking has been given new meaning in the context of illicit finance. In an early article on the topic, *The Economist* described de-risking as a trend that saw big banks "culling banking relationships and retreating wholesale from markets, countries and lines of business that might attract the ire of regulators or prosecutors."[16] There are two components to the definition that bear highlighting.

First, the decision is a categorical one, affecting groups of people based on a group characteristic rather than clients' individual profiles. This could include any number of categories, such as sectors (e.g., money transfer services or marijuana production) or regions (e.g., the Caribbean, the Middle East). The second key component is an implied counter-factual. Were it not for fear of regulatory scrutiny, or of attracting "the ire

[14] Future iterations of the paper will include a substantive analysis of those posts, as well.
[15] See, for example: https://ida.worldbank.org/sites/default/files/pdfs/psw-updated-may-2017.pdf
[16] Economist. June 14, 2014. "Poor correspondents." Emphasis added.

of regulators or prosecutors," the service provider in question would render financial services to the potential customer.

The two characteristics are vital in separating AML-related de-risking from other forms. The denial of services due to particular personal circumstances is standard risk management. A denial of services because a service provider feels there is no profit to be made or because the customer poses some unreasonable risk other than regulatory attention also falls short de-risking as the concept evolved within AML. Some of the empirical work on de-risking we cite below tends to operationalize de-risking as a general decline in correspondent banking relationships (CBRs). While that is a likely observable implication of de-risking, banks might end CBRs for a variety of reasons beyond concerns over AML. De-risking that derives from AML regulation, de-risking driven by a concern over the stability of investments, and the ending of CBRs are substantively different phenomena. Whether intentional or not, blending those three into one vague notion about decreasing CBRs risks leading us to wrong conclusions about the drivers of de-risking and thus, to bad policy responses.

IIIb. De-risking on the agenda

We begin breaking down the central question of this paper--what drives the de-risking agenda--by looking at the most observable portion of the evidence: actual agendas. In other words, when did de-risking begin to show up on the AML agenda, broadly defined? When did it become a topic of discussion at international fora? When did leaders give speeches about it? When did organizations issue reports on it? Was it on national agendas before international ones? Did banks talk about it before regulators? Did actors from rich countries talk about it before actors in developing countries?

In short, the official conversation started in 2013/4. The earliest direct reference to AML-related de-risking appears to be from the 2013 "Semiannual Risk Perspective," produced by the US Office of the Currency Comptroller's National Risk Committee. The OCC is the primary regulator of banks in the US, including agencies of foreign banks. The OCC's National Risk Committee "monitors the condition of the federal banking system and emerging threats to the system's safety and soundness." Drawing on data from the first half of 2013, they write: "Some banks are addressing resource constraints and internal control challenges through a strategy of de-risking specific higher risk and unprofitable customers."[17]

In March 2014, then-comptroller of the currency, Thomas Curry, picked up on the theme in a speech. He noted that de-risking had become "a topic of much discussion lately," with some arguing that "in the current regulatory environment, there are whole categories of businesses that are too risky to bank." He also confirmed that AML was "an area of intense scrutiny, by banking regulators and law enforcement." But those acknowledgments are the build-up to his key point: "No matter what type of business you are dealing with, you have to exercise some sound judgment, conduct your due diligence, and evaluate customers individually. Even in areas that traditionally have been viewed as inherently risky, you should be able to appropriately manage the risk...Higher-risk categories of customers call for stronger risk management and controls, not a strategy of total avoidance."[18]

[17] p. 7.

[18] Remarks by Thomas J. Curry, Comptroller of the Currency, before the Association of Certified Anti-Money Laundering Specialists. Hollywood, Florida. March 17, 2014.

The same conversation was happening in Europe. Tracy McDermott, then head of the UK's financial regulator, the Financial Conduct Authority, addressed the issue in an April 29, 2014, speech at the SWIFT business forum. She reportedly said that the FCA '"would rarely expect" firms to exit business relationships to avoid risks and that a denial of services was unlikely to be the only solution to the problem. "We don't want to end up in a world where the fear of the consequences…will deny people access to legitimate services."' This claim--that de-risking was an overreaction or misreading of the rules--remains the central argument of US, UK, and EU regulators today.

De-risking first appears on FATF's agenda in July 2014, in a speech by in-coming FATF President Roger Wilkins. He addresses it more substantively in October that year at a speech at the Annual International Conference on Financial Crime and Terrorism Financing. He begins familiarly: "*There has been a lot of discussion recently* about the so-called "problem of de-risking."[19] He then takes on the charge from The Economist that the trend stems only from heavy-handed AML regulation. Banks, he said, have always dealt first and foremost in the assessment and allocation of risk. He continues:

> The FATF takes that insight seriously. The problem seems to be in the wake of the global financial crisis, in an atmosphere of growing apprehension about tomorrow; in a world where the reputation of big banks has taken a pounding; in a world where the increased prudential requirements are lifting; big banks are simply not prepared to play." He then notes that FATF would begin a discussion of the issue and emphasized the need to understand more about drivers of illicit markets, the dangers of financial exclusion, and the need for guidance in dealing with risk assessment.

Two weeks later, following a FATF plenary—the decision-making forum of FATF that meets roughly twice a year—the tone shifts toward greater certainty. It still emphasizes the banks' responsibility: "De-risking can be the result of various drivers, such as concerns about profitability, prudential requirements, anxiety after the global financial crisis, and reputation risk. It is a misconception to characterize de-risking exclusively as an anti-money laundering issue." The report notes that "recent supervisory and enforcement actions have raised the consciousness of banks and their boards about these issues," but then argues that those cases were exceptionally egregious. To use them to guide bank policy on de-risking, in other words, is not legitimate. In typical form for FATF, it commits to gather more evidence on "the drivers and scale of de-risking" and to work with other IOs that were tackling the same questions, including the G20, IMF, World Bank, and the Basel Committee.[20]

Around the same time, the fall of 2014, Transparency International UK also addresses de-risking. A document from them entitled "10 Tests: Can UK legislation tackle corrupt capital?" lists "'De-risking' by major banks" as a private-sector factor that inhibits the effectiveness of the UK's AML regime.[21]

In November of 2014, Mexico brings up concerns about de-risking in its IMF Art. IV country report and locates the discussion in the context of countries whose businesses are targets of de-risking. The authors write: "The authorities were concerned that as foreign banks decide to opt-out of cross-border transactions, including remittances, as part of de-risking decisions taken in response to stringent

[19] Emphasis added.
[20] FATF. 23 October 2014. Plenary Conclusions.
[21] P. 2.

requirements imposed by regulators in connection with AML/CFT procedures, facilities available to Mexican banks to carry out such transactions will be more limited. They express hope that as banks involved in such transactions, with the support of the competent financial authorities, are able to establish clear procedures, the restrictions will be alleviated."[22]

In January 2015, Tracey McDermott of the UK's FCA returned to the topic. It is worth providing a longer quote to convey the tone of her comments, which are very similar to those of Curry in the US:

> …[A]longside a number of enforcement cases here and overseas, firms are still getting this wrong when it comes to the really important and really high risk matters. So BNP Paribas can transfer $190bn in breach of US sanctions. HSBC can fail to adequately monitor over US$670bn in wire transfers from HSBC Mexico….But a new startup cannot open a bank account or your 87-year-old grandmother cannot transfer money without her passport. Something is awry here.
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> This is something in which we have been taking a particular interest… As I've said before, firms must take their responsibility to reduce the risk of financial crime seriously. To do that successfully requires firms to use their judgement and common sense. That is not about box-ticking or wholesale de-risking. It is about firms getting the basics right – understanding their customers, the risks they pose, and managing those risks proportionately and sensibly. It will be the case that some firms, having considered the customer, may still not wish to offer them a service. That is still their decision, but the money laundering risks of many firms can be - and we have seen examples of this - successfully managed. Wholesale approaches to an entire sector, or controls that allow staff no discretion to avoid the wrong outcomes, are not required by our rules and should not be required by your processes.

By this point, larger AML organizations began addressing de-risking more formally, as well. The Association of Certified Anti-Money Laundering Specialists (ACAMS) issues a report in August 2014, entitled "AML De-risking: An effective method of plugging AML control failures?" Ultimately, ACAMS argues that de-risking is counter-productive. Mass exit programs are difficult to manage effectively and likely leads those denied services to leave larger banks with more AML capacity for smaller banks with fewer AML resources.[23]

By the fall of 2015, international financial institutions were fully on board. In March 2015, the FSB asked the World Bank "to examine the extent of withdrawal from correspondent banking and its implications for financial exclusion/inclusion."[24] By the fall of 2015, the IMF, World Bank, G20, the Bank for International Settlements (Committee on Payments and Markets Infrastructure), and the Financial Stability Board had all issued reports on de-risking.

The IMF's references to de-risking illustrate the rapid change on this topic and underscores the puzzling nature of the change. In its 2013 "Global Financial Stability Report," the IMF warns banks "the process of balance sheet de-risking…is not complete and further progress is needed."[25] Mexico's Art. IV country report mentioned above is the first negative reference in the IMF. One year later, in "The Managing Director's

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[22] IMF Article IV Consultation Staff Report--Mexico. November 2014. IMF Country Report No. 14/319. P. 14.
[23] Adisa, Bukola. August 2014. "AML De-Risking: An effective method of plugging AML control failures?"
[24] FSB in IMF 2015, p. 9.
[25] IMF. April 2013. "Global Financial Stability Report: Old Risks, New Challenges." P. 16.

Global Policy Agenda" for the 2015 annual meeting, the conversation had turned to the need to help developing states deepen their regulatory systems in order to avoid the costs of de-risking by big international banks.

In short, the first reference to AML-related derisking shows up in 2013. By 2015, it was a topic across the agendas of the IFIs. What explains this significant shift in prioritization for de-risking?

IIIc. De-risking in traditional and social media

As noted above, scholars disagree on what drives the AML agenda: FATF, powerful states, networks of experts,and the compliance profession are all possibilities. In attempting to track the origins of de-risking, we turn now to social media. A sociology of knowledge framework emphasizes the importance of transmission. McCarthy writes the following about the ways that technology was affecting knowledge production:

> "What *is* decisively new today is not only the democratic ethos that tolerates and even invites such conflicts, but also the fact that the stage on which battles are waged is immediately visible to all (instantly so, and for permanent record and instant replay). What people know and what they think are events played out in the public arena, often and before innumerable audiences. The 'media event' only dramatizes Mannheim's contention that the questions 'What is reality?' is both urgent to our present condition and pre-eminently suited to sociological inquiry."[26]

If that was true in 1996, when McCarthy wrote that, then it is so much more the case today. By now, there is a fairly active space on social media for the compliance community. In this section we analyze that space as a medium of transmission, trying to understand the timing and content of the knowledge (not) being created and transmitted there.

Analysis of social media and internet activity shows that there was a spike in 2012, but then people began discussing the topic more frequently beginning in 2014. Using Google's trend tools, we can track the *relative* frequency with which users searched for a term, with 100 representing the maximum number of searches ("peak popularity" in Google's terms) for a given timeframe, 50 indicating half the number, and 0 indicating insufficient data, suggesting low numbers of searches. The results from January 1, 2004 (the earliest date for Google Trends data) to May 1, 2014 shows more volatility. As an indicator of that, the average weekly score for 2004-2014 is just over 25. For 2014-2018 it is just over 45. This does not show the absolute frequency of searches—the total number from 2004-2014 in theory could be higher, but just more volatile. It suggests that Google users searched for the terms more consistently in the second period.

Google Trends also shows related terms, or terms that users searching for de-risking also entered, which helps provide evidence on the motivations behind the searches. For 2004-2014, the top five related terms were, in descending order: pension, strategy, risk, investment, and finance. There is nothing in the top 25 that is obviously about illicit finance. From 2014-present, the top five related terms remain similar: pension, bank, definition,[27] risk, and investment. But also appearing on the top-25 list are: correspondent account

[26] McCarthy, p. 4.

[27] The arrival of "definition" may signify the spread of "derisking" to a new audience that was unfamiliar with the term's meaning.

(9th), money laundering (17th), Financial Action Task Force (19th), Bitcoin (23rd), remittances (24th), and financial crime (25th).[28]

Lexis-Nexis reveals this same shift in context for the term. A search for "de-risking" generates over 3000 returns. Filtering out articles with the word "pensions" cuts it to 433. Adding the term "laundering" drops it further still, to 195. The oldest is in October of 2014.

We can also look to social media. Figure 1 below is data generated by a search using Crimson Hexagon, a social media analysis tool that draws on the Twitter's complete record of tweets, not just a sample.[29] This includes Facebook posts, Reddit, and Tumblr, but 85% of the posts come from Twitter. It is a simple search for "derisking", "de-risking", and "de risking", excluding all posts that include the word "pension" or some version of that word.[30] The chart shows a clear increase in the frequency of the term.[31]

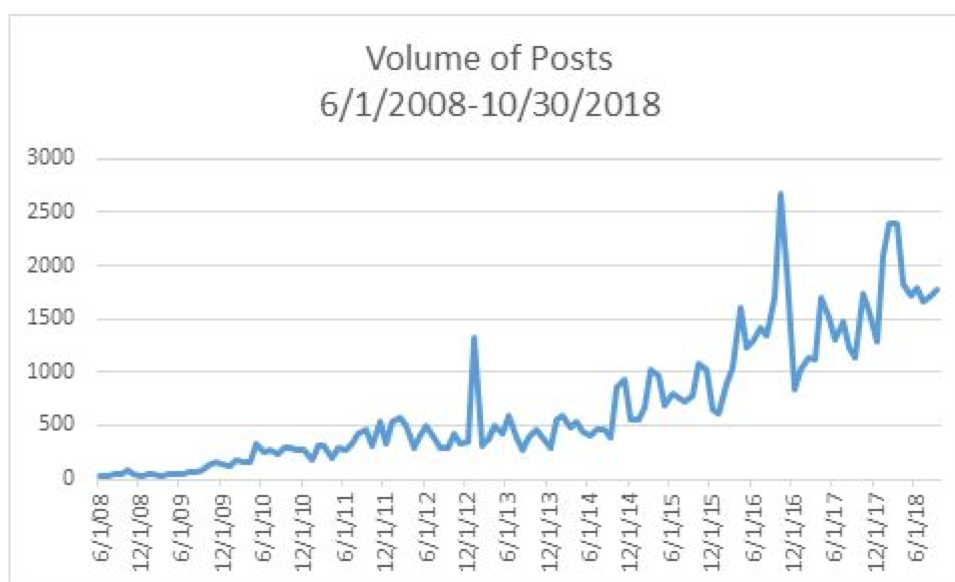

Fig. 1

Crimson Hexagon also generates theme wheels, which highlights words commonly used together. Fig. 2 is the wheel associated with de-risking posts from 2008-2014.

[28] Search most recently conducted: 10/31/18.

[29] Crimson Hexagon is a social media analysis tool developed by political scientist Gary King. Pew Research, which uses the software to assess social media, and especially Twitter, notes that the software "examines all publicly available tweets and has access to Twitter's entire 'firehose.'" In other words, it is not a sample of tweets, however large, but a complete record of tweets. Retweets are included in the analysis. Pew Research wrote about their verification of the CH algorithm at http://www.journalism.org/2015/04/01/methodology-crimson-hexagon/. The method behind the software is laid out at: Daniel Hopkins and Gary King. 2010. "A Method of Automated Nonparametric Content Analysis for Social Science." American Journal of Political Science, 54, 1, Pp. 229–247. Copy at http://j.mp/2ovQqd5

[30] We excluded "pensions" because initial queries showed the term overshadowed de-risking in other contexts.

[31] The spike in January 2013 is a World Economic Forum panel called "De-risking Africa" where heads of state debated whether countries in Africa had put in place "the right policies" to continue the continent's above average growth that it had shown in the two years prior to the panel.

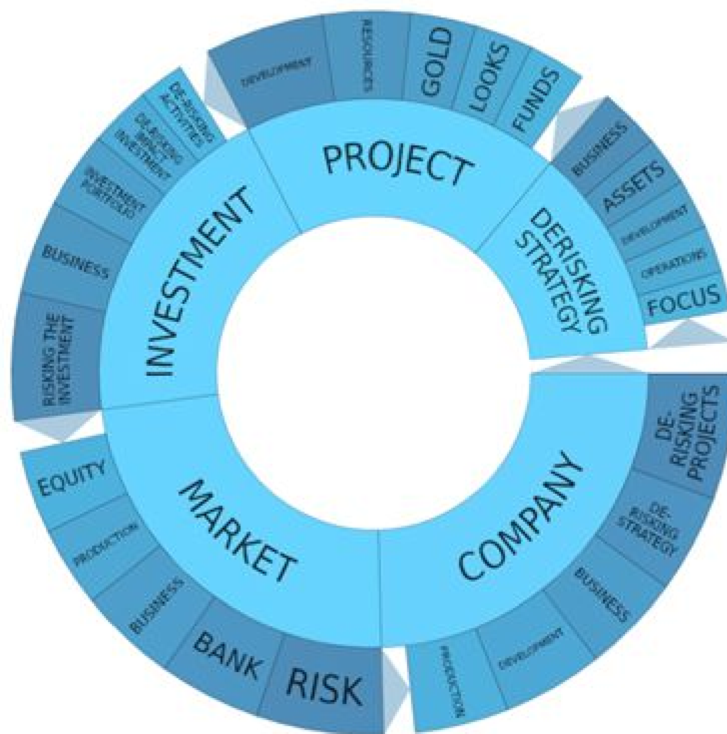

Fig. 2

In contrast, Fig. 3 is the theme wheel for 2014-2018. While there were no AML-related topics before, from 2014-2018 we see AML, regulation, and correspondent banking. Those reflect derisking within the AML framework.

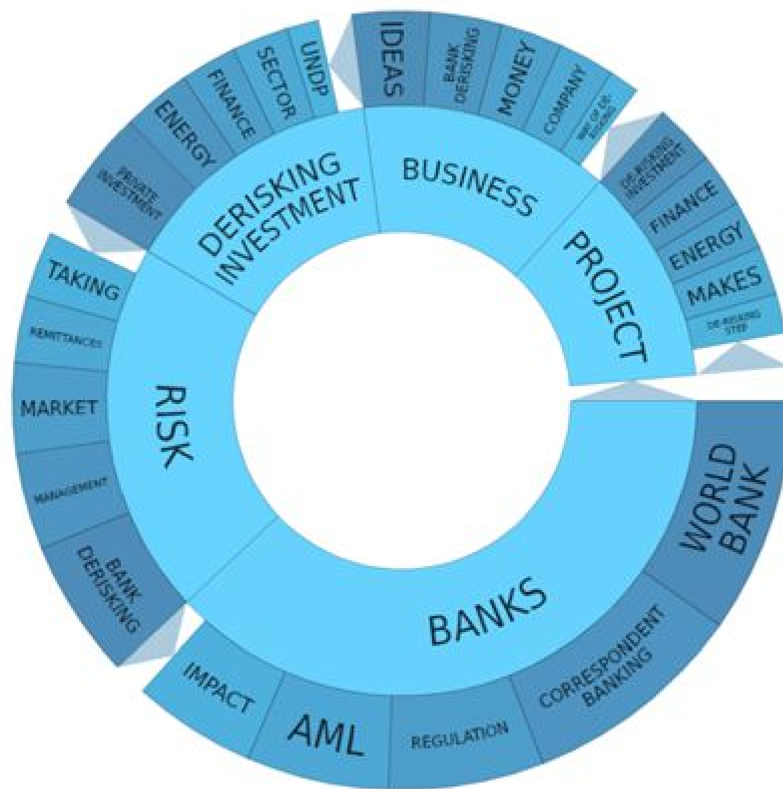

Fig. 3

These charts and graphs reflect the birth of an idea. Prior to 2014, de-risking was not a topic associated with AML. By 2014, it clearly had become a major concern in AML banking circles.

IIId. A data driven agenda?

A reasonable explanation for the rise de-risking on the global financial governance agenda would be evidence of a new problem: an issue that comes up through FATF mutual evaluations or IMF monitoring. Ultimately that does not seem to have been the source. Rather, those reports followed the chatter. It bears emphasizing that this is not in and of itself a bad sign. Governance bodies arguably should "keep their ear to the rail" and investigate concerns expressed by those they govern.

While the first report focused on de-risking came from the Financial Stability Board in 2015, by that same year, as noted above, FATF and other institutions were quickly ramping up their work on the subject. The FSB reports 4 sources of data: a World Bank survey on correspondent banking services, a G20 survey on remittance flows, an IMF survey of the Union of Arab Banks, and a report from the Committee on Payments and Market Institutions "gathered mainly…through interviews with selected financial institutions."[32]

[32] Financial Stability Board. "Report to the G20 on actions taken to assess and address the decline in correspondent banking." 6 November 2015 (p. 2).

The most important source of evidence comes from the World Bank report. The World Bank writes: “For some time now, stories and anecdotes have been circulating in media and international policy that large international banks…” are de-risking. Their survey aims to “explore the basis for these stories and provide concrete evidence” of de-risking.[33]

The survey largely confirms a decline in the number of correspondent banking relationships. But it also notes that the FSB reports an increase in the total volume of money that is being moved. Two other trends are worth noting here. First, banks in the United States drive most of this decrease in the number of correspondent banking relationships. It is by far the biggest source of de-risking. Second, the impact of de-risking varies. The authors of the World Bank report write that the Caribbean has been the hardest hit. In personal correspondence, however, personnel involved in the project noted that there was “very low coverage” in the Caribbean, which casts some doubt on results as applied in the region.[34] Evidence made available since that report’s publication, however, confirm this finding.

The question of drivers is also important. The World Bank report emphasizes two categories of canceled relationships: one based on economic assessments (expected profitability) and one based on regulatory and risk-based uncertainty. Importantly, banking authorities and banks gave different reasons. Among banking authorities that responded, 48% listed concerns about money laundering and terrorism financing risks, making it tied for the third most commonly cited reasons for a decline. Changes in the regulatory requirements in the jurisdiction or overall risk appetite of the correspondent were ranked as high or higher. The most commonly cited reason was a lack of profitability of the relationship. Among large banks, the given reasons were different. 95% listed concerns about money laundering and terrorism financing, 85% listed lack of compliance with AML regulations, 85% listed overall risk appetite, and 80% listed lack of profitability. There is an obvious difference in what the two “sides” believe is driving de-risking.

Finally, the FSB reports that an IMF survey of 117 banks that cover most members of the Arab Monetary Fund indicated “that there has not been a systematic wholesale reduction of correspondent banking in this region, except for banks in countries subject to economic and trade sanctions.” That is noteworthy: banks in the region of the world that often portrayed as presenting the greatest risk for terrorism financing have not seen widespread de-risking. This suggests that profit, not regulation, is playing a role in de-risking. A later IMF study reports that 63% of responding banks reported the closure of CBR accounts, versus 33% in 2012.[35] However, 60% of banks reported no significant change, 5% reported an increase, and 1% had no response. 70% of those who reported an increase in the loss of relationships were able to find a replacement.

Looking in particular at the early days of the phenomenon, it seems that the conversation around de-risking was not driven by systematic evidence of a specific problem. That gap arguably remains, even as the conversation about solutions has moved forward. We know that some banks are de-risking, but we do not know why.

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[33] World Bank. “Withdrawal from Correspondent Banking: Where, Why, and What to Do About It?” November 2015.

[34] E-mail on file with the author.

[35] IMF. “Withdrawal of Correspondent Banking Relationships (CBRs) in the Arab Region: Recent trends and thoughts for policy debate.” September 2016.

IV. Analysis

Put directly, the evidence suggests the de-risking agenda originates outside the states and groups that have pushed for a strong AML regime. While this may seem obvious at first, recall that many observers argue that the AML regime is primary guided or shaped by something other than the industry itself, as arguably it should be. To imagine it in simpler terms, there are many who find that the AML regime is driven by the regulators, not the regulated. The case of de-risking suggests that the regulated may have found their voice and re-gained their political power within the AML regime, which for a long time they have found to be a politically tricky target. There are several pieces of evidence.

The first is the timeline created when we compare the sections above on the agenda, social media discussion, and production of reports with data. The World Bank produced the first direct data on de-risking in its 2015 report, which then served as an important data source for the FSB's 2015 report, as well. But as indicated in the media analysis above, the "take off point" for de-risking had already passed roughly a year prior to that with that noticeable spike coming nearly three years before that report, in 2012. The agenda pre-dated any data on the subject; the conversation pre-dated the agenda.

A second piece of evidence is found in theme common across reports. The IMF's initial report on de-risking, for example, notes: "For some time now, stories and anecdotes have been circulating in media and international policy that large international banks (predominantly US/Europe/Canada based) are terminating or severely limiting their correspondent banking relationships with smaller local/regional banks from jurisdictions around the world...This development is considered by many to be part of an apparent 'de-risking' trend, according to which financial institutions are limiting their exposure to the perceived risk posed [by] certain classes of customers or partners."[36] The initial article in *The Economist* suggests the same, reporting what a senior official says is happening. But it provides no data. Comptroller Thomas Curry's early comments on de-risking note that the issue "has been a topic of much discussion lately."

Third, in an on-record interview via E-mail, Curry confirmed that the topic came up through conversations between regulators and banks' compliance officers: "The OCC conducts regular outreach activities with supervised banks and their BSA/AML compliance officers where industry concerns are raised informally."[37] He also notes the conversations that happen between US regulators and their peers from other countries and institutions: "The OCC and other U.S. regulatory and law enforcement agencies are in regular contact with foreign bank supervisors and international NGOs in a variety of settings including the Financial Stability Board, Basel Committee on Bank Supervision, FATF, IMF, and World Bank." Both domestic and international conversations highlighted de-risking, but Curry emphasized that most conversations the OCC has are with its supervised entities.

If the push against de-risking started with banks, what sparked the conversation there? The standard explanation from banks, IFIs, and most outside observers is that the conversation stems from ramped up enforcement actions. As participant observers in a wide variety of fora, we have been party to multiple conversations with financial institution representatives where the argument is put forward. Some blame AML regulation in general. Some blame regulators, and US regulators, in particular. Still others emphasize

[36] World Bank 2015, p.9

[37] On file with the authors.

that the enthusiasm of individual regulators are the problem. FATF's early intervention on de-risking, cited above, puts it in measures tones: "Recent supervisory and enforcement actions have raised the consciousness of banks and their boards about these issues."[38]

Data on enforcement actions from the US' OCC at first glance support this explanation.[39] Through the 1990s, fines were rarely over $25,000. Most often those were restitution orders actions against individuals, not civil penalty fines against banks. Fines associated with bank civil money penalties seemed to increase substantially beginning in 2011.[40] The first big spike identified in Fig. 1 above corresponds with a bank civil money penalty of US$500 million issued by the OCC against HSBC.[41] The spike in late 2016 corresponds with a few large fines: three fines against JP Morgan Chase of $48 million, $35 million, and $20 million; $35 million against HSBC; $70 million against Wells Fargo. To be sure, the fines starting in 2012 seem to grow rather steeply.

A sociology of knowledge approach, however, helps us notice what is not being transmitted. Conversations around de-risking fail to provide the context we need to fully judge how responsible AML enforcement is for de-risking. For example, people rarely discuss the nature and extent of the violations. But the violations that large are generally for either violating AML laws or engaging in sanctions busting. Also excluded are the profit margins. The 2012 spike in social media discussions of de-risking correspond with major fines against HSBC; it faced a base fine of $500 million in 2012; other agencies often tack on more fines. As the quote from then FCA Tracy McDermott notes above, however, in the 2012 case, HSBC failed to monitor more than $670 billion worth of transactions and faced a fine from HSBC of $500 million. Furthermore, HSBC in that same period reportedly averaged a yearly profit of $13.3 billion, for a total profit of $93.3 billion.[42] If enforcement actions are to include a deterrence element, presumably fines would need to increase as bank profits increase.

Nor is it clear that the visible patterns of de-risking necessarily support the idea that counter-terrorism finacing is driving derisking. In an interview with a banking official from the British Virgin Islands, the official reported that no banks ending correspondent banking relationships with BVI institutions asked about terrorism financing, as we might expect if that was in fact what was "keeping them up at night." Early surveys on the problem also suggested that de-risking was not happening in the Middle East, which we would assume would be a larger target of scrutiny for terrorism financing than the Caribbean. And yet the Caribbean seems to have borne the brunt of de-risking, especially early on, in the phase of the agenda that we track most carefully in this paper.

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[38] *Supra.* n. 19.

[39] Future versions of the paper will include a more complete analysis of fines, including the kinds of fines and all relevant regulators. For this version, we treat the OCC's actions as indicative.

[40] These bank civil money penalties often have additional fines associated with them but are listed separately. Future versions of the paper will provide total fines issued at specific time periods to better encapsulate the fine associated with some compliance failure.

[41] These fines often have other agencies join the case, generating multiple fines. We are still building those databases and so have not included that information here. However, it seems that the OCC is often the primary agency in these cases.

[42] https://www.statista.com/statistics/224577/hsbcs-profit/ Accessed 9/19/2019.

For example, the Financial Stability Board in 2018 issued the first of a series of annual quantitative reports on CBRs globally.[43] The chart below, from that report, shows that the Americas, excluding North America, were the first to be hit, with a 4.1% drop in the number of active correspondents. The next highest was Asia, losing 1.6%. That trend continues for every year except one between 2012 and 2018. In total, the Americas, excluding North America, have lost 30.5% of their correspondents, considerably higher than other regions. This cuts against the argument that banks' fears of terrorism financing is driving de-risking.

Changes in the number of active correspondents by region (based on the flow of MT 103 and MT 202 excluding MT 202COV)[1]

Table 2

	Africa	Americas (excl. North America)	Asia	Eastern Europe	Europe (excl. Eastern Europe)	Northern America	Oceania
	%	%	%	%	%	%	%
2012	-0.5	-4.1	-1.6	-0.5	-1.4	-0.4	-1.2
2013	-1.5	-2.7	-2.5	-1.5	-2.0	-0.6	-3.2
2014	-3.2	-5.7	-2.0	-3.0	-3.8	-1.8	-1.1
2015	-3.7	-4.5	-2.3	-3.7	-4.0	-1.7	-2.8
2016	-5.8	-5.5	-3.0	-3.5	-3.5	-2.4	-5.4
2017	-5.4	-6.6	-5.2	-5.9	-5.8	-2.9	-6.7
2018	-5.2	-6.2	-4.6	-5.0	-4.5	-3.1	-2.5
2011-2018	-22.9	-30.5	-19.4	-21.1	-22.6	-12.2	-20.9

Sources: National Bank of Belgium; SWIFT BI Watch.

At the same time, it also confirms that de-risking is a global phenomenon, with de-risking happening across all regions. Even in North America, CBRs declined by 12.5% from 2012 to 2018. For all other regions, the drop was 20% or higher. Taken together, these data do not disconfirm the hypothesis that AML is driving de-risking, but nor do they disconfirm the argument that de-risking is a result of basic business decisions and global economic trends, rather than AML.

Finally, also left out of the "knowledge" produced by those arguing that de-risking is the result of AML overreach is the full effect. There is no doubt that de-risking has the potential to pose tremendous costs, especially to small jurisdictions that are dependent on[44] their financial services sectors for income. The SWIFT data in the FSB 2018 report show that in 2018, 15 jurisdictions had fewer than 20 CBRs, most of which were small dependent jurisdictions with a population below 200,000.[45]

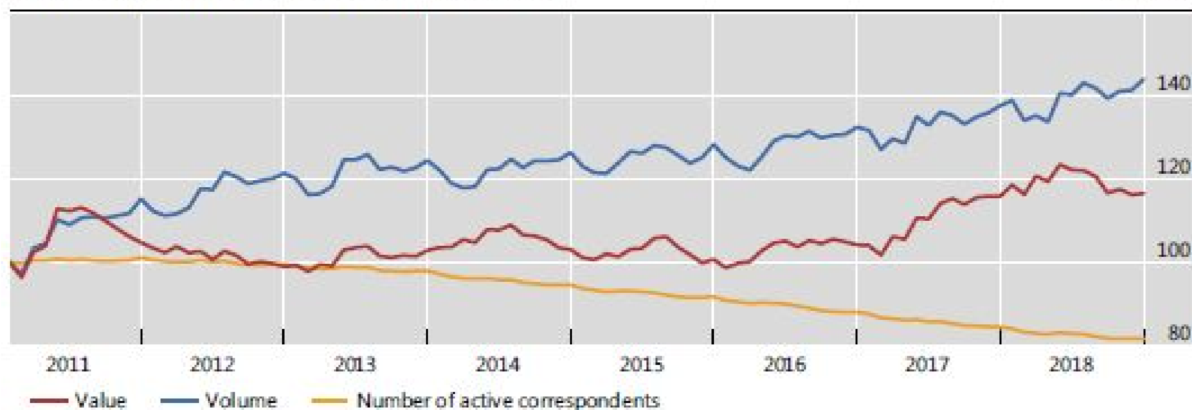
At the same time, most jurisdictions had more than 100 active correspondent banking relationships. As a function of that, the total volume of messages *and* the total value of those messages has increased since 2011, despite the total number of CBRs having decreased. At this time we do not venture to explain why that is. One likely answer is that jurisdictions and their allies are finding solutions to the problem. Another is

[43] Financial Stability Board. "Correspondent Banking Data Report." 2018.
[44] *Ibid*.
[45] Holden, Henry. 2018. Commentary on FSB Report on Correspondent Banking.

that there might simply have been an over-supply of CBRs for many regions. We need better data on the cost of those services before we can fully evaluate the significance of that trend.

Number of messages (volume), their total value in USD, and the number of active correspondents[1]

Three-month moving averages, Index Jan 2011 = 100 Graph 11



[1] MT 103 and MT 202 excluding MT 202 COV.

Sources: National Bank of Belgium; SWIFT BI Watch.

So what do we make of this jumble of data: textual analysis of agendas, social media analysis, interviews, changes in CBRs and total volume of money sent? The sociology of knowledge framework that we deploy here is helpful.

Many in the financial arena, and many outside observers, argue or at least accept that de-risking is a result of AML overreach. *The Economist*'s early article on the phenomenon defines de-risking as a trend that saw big banks "culling banking relationships and retreating wholesale from markets, countries and lines of business *that might attract the ire of regulators or prosecutors*." For these groups, the solution often involves some degree of de-regulation, or at least a re-regulation of the AML policy space. This represents one body of knowledge about de-risking.

It is not, however, the only knowledge. Recall that in the first report on the subject, the OCC's National Risk Committee reported that "Some banks are addressing resource constraints and internal control challenges through a strategy of de-risking specific higher risk and unprofitable customers."[46] This definition of de-risking emphasizes two drivers. The first is "internal control challenges," which implies AML/CFT violations. In other words, the banks are at fault for failing to implement effective AML systems, rather than the AML system itself being the culprit. The second is "resource constraints." Elsewhere the report had pointed to the challenges for some banks posed by the higher capital requirements of Basel III. This is most likely a reference to that problem. Again it lays the blame at the door of banks, not regulatory oversight.

[46] p. 7.

This body of "knowledge"--that de-risking is not the fault of AML, but rather the fault of banks who either misread the rules or simply do not want to provide services to customers for a variety of reasons--continues through the early debate until today. Again recall the words of the heads of the OCC and the FCA, both of whom emphasized that de-risking was an improper response. FATF maintains the same stance.

The two camps that generate these knowledges agree that there has been a decline in correspondent banking relationships. Beyond that observation, however, there are signs that the fault lines in the contestation of knowledge remain similar to what they were in the earliest days of the agenda.

Conclusion

Those contests are not "merely" academic. Rather, the body of knowledge that wins implies its own set of solutions. It is therefore imperative that the third camp--those seeking to better understand the problem--remain part of the debate.

An important implication of the evidence above is that a discussion of solutions around de-risking is still outpacing discussions of the drivers. That is problematic, as it makes it more likely that the proposed solutions fail to truly solve the problem.

Regardless of the drivers, de-risking entials far-reaching implications that have yet to be fully realized, especially at the policy level. Here we raise three for the sake of future discussion.

First, as the idea that de-risking is driven by AML gains wider acceptance, it would seem to make it easier for banks to exist relationships. It legitimizes or even valorises denial of services. After all, who can argue against efforts to counter terrorism financing? Rhetoric that has long served to justify the furtherance of AML is now pushing in the opposite direction. As AML proponents continue to argue, this works against efforts to improve oversight by excluding some transactions from the formal system. Development proponents also emphasize that this cuts against financial inclusion and the development that access to financial services can promote.

Second, as financial oversight has become a major tool of foreign economic and security policy, the severing of CBRs in particular becomes a decision with important foreign policy implications. For the US and Europe, this should be a concern. It is not clear, however, that this implication has become apparent.

Third, especially the sociology of knowledge interpretation of the de-risking agenda provided here raises the question of whether global finance should be regulated as a utility. Everyone in the debate over de-risking acknowledge the potential damage it entails. As we gather more evidence on the impact, it bears questioning whether there is a larger role to be played by government to ensure that financial services are accessible to all.

Finally, it bears emphasizing that more effective governance of finance requires that all stakeholders have a meaningful say in the process. Our interpretation of de-risking suggests that the voices of private, profit-seeking actors are being heard more and more within AML governance. That can be positive, so long as theirs is not the only voice. A vital role for government in this is ensuring that all stakeholders--in short, both sides of CBRs--are at the table, able to play a meaningful role in financial governance.