FIBA

De-Risking

How is it impacting correspondent banking

What Does De-Risking Mean?

- The wholesale exiting of a region, country or class of customers in order to minimize risk without using a thoughtful approach

- Using a thoughtful risk based approach to analyze and mitigate certain kinds of risk as part of a sound risk management program

- Using a cost-benefit, or risk-reward, or profit cost analysis, to make sound business decisions in determining whether to serve certain customers

Whatever you call it, the results are still the same:

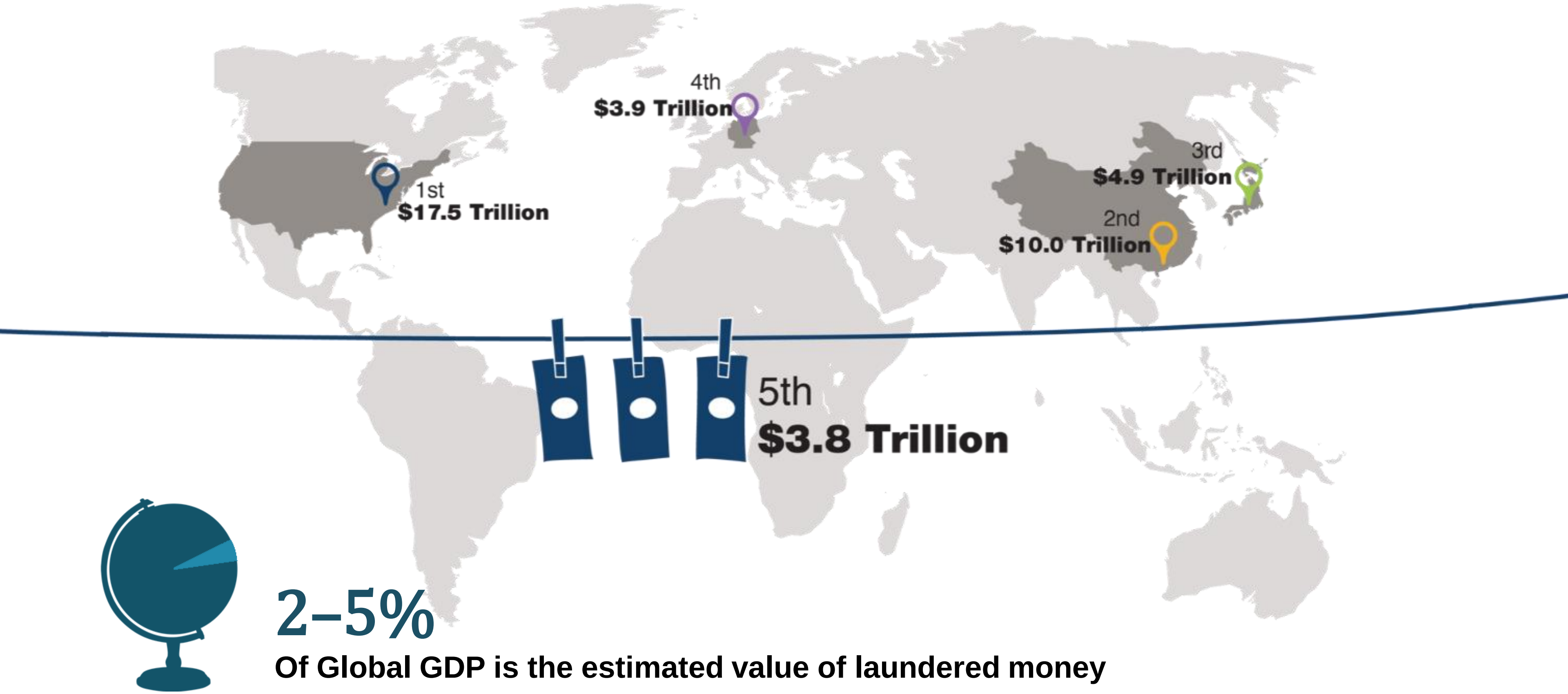
Certain regions, countries and classes of customers are unable to attain or maintain banking services

When Did De-Risking Begin?

When Did De-Risking Begin?

- Origins date back to 2002 and the passage of the Patriot Act
- Treasury Department establishment of the Public/Private Sector Dialogues
- Subsequent regulations: Dodd Frank, FATCA, Basel III
- Operation “Choke Point”
- Shifting role of banks: Regulator, Law Enforcement, Tax Authority

If the money laundering "business" were an economy, it would be the fifth most important in the world.



2–5%

Of Global GDP is the estimated value of laundered money

Fines that banks have paid to US regulators.

Selected BSA/AML penalties at large banks

Fined Company	Holding Company	Date	Penalties paid to	Penalties
BNP Paribas SA	BNP Paribas SA	06/30/14	Justice Department, Fed, NY Department of Financial Services, Treasury	$8.97B
JPMorgan Chase Bank NA	JPMorgan Chase & Co.	01/07/14	Justice Department, OCC, FinCEN	$2.05B
HSBC Bank USA	HSBC Holdings Plc	12/11/12	Justice Department, Fed, OCC, FinCEN, Treasury	$1.92B
U.S. Bank NA	U.S. Bancorp	02/15/18	Justice Department, Fed, OCC, FinCEN	$613M
Rabobank NA	Cooperative Rabobank U.A.	02/07/18	Justice Department, OCC, FinCEN	$369M
Banamex USA	Citigroup Inc.	07/22/15	FDIC, California Dept. of Business Oversight	$140M
Banamex USA	Citigroup Inc.	05/22/17	Justice Department	$97M
Citibank NA	Citigroup Inc.	01/04/18	OCC	$70M

Data compiled Feb. 20, 2018.
Source: S&P Global Market Intelligence

THE ACT OF DE-RISKING

Correspondent Banking Challenge

- The US expectations have created three regulators in the region:
  - the in-country regulator
  - the U.S. regulator
  - the correspondent bank

- The resources and essential tools, specialized human capital, systems and budgets are scarce, or unavailable;

- ***Transparency of transactions*** *– "KYCC or Know Your Customer's Customer";*

Correspondent Banking Challenge

- There is a **perception** that the Caribbean nations have not done enough in terms of money laundering, corruption and terrorist financing; (CFATF)

- Recent expansion of OFAC sanctions beyond narcotics trafficking;

- Basel III reforms and regulations have also created new risks and unintended consequences;- LCR for example

- Correspondents prefer to offer **low risk services with higher margins** rather than low revenue high risk services.

- If the relationship is not profitable it must be closed.

Compliance Costs

- Compliance cost (approximately $300 spent billion annually)
- Essential Technology and Tools
- Specialized Human Capital
- Increasing Operational Costs, Oversight and Monitoring

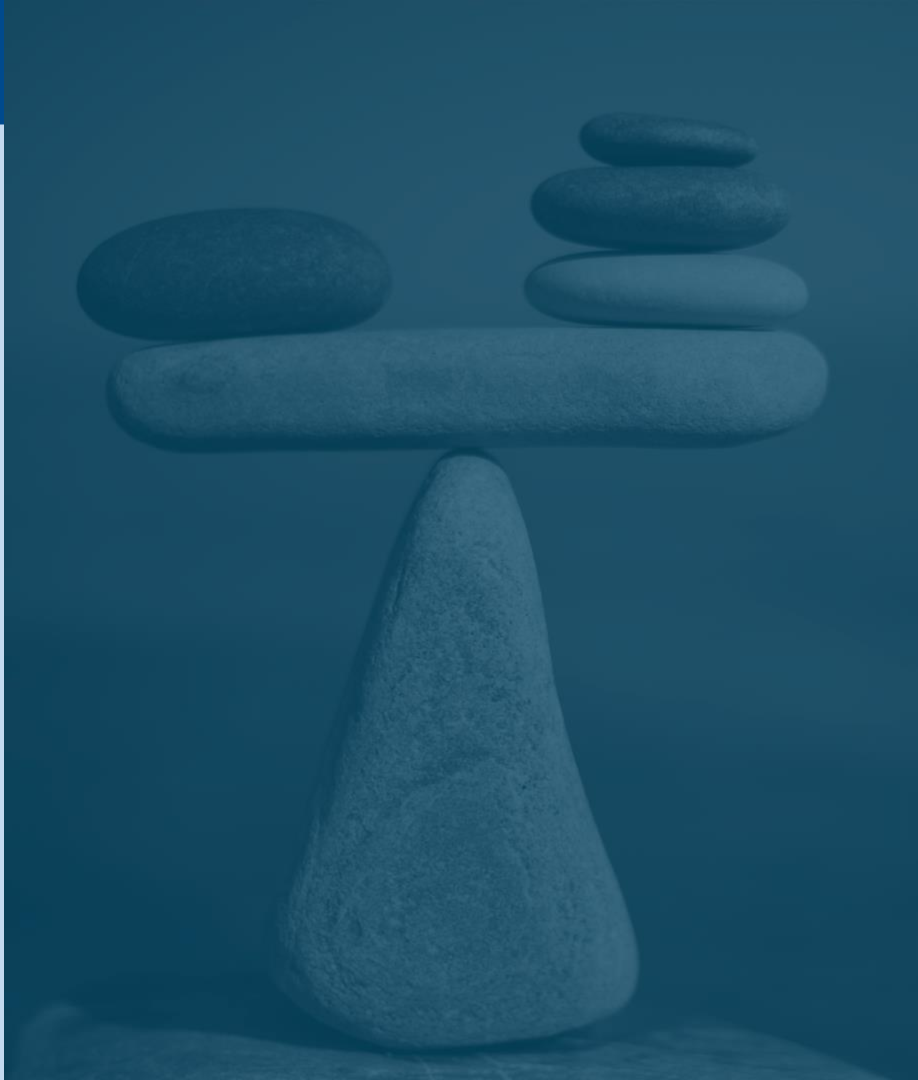
Profitability

The cost/benefit analysis of a correspondent relationships

Banks look for products with higher margins and lower risk.

If the relationship is not profitable, then it may be closed.

$$\frac{\textbf{Compliance cost + Regulatory Risk}}{\textbf{Profitability}}$$



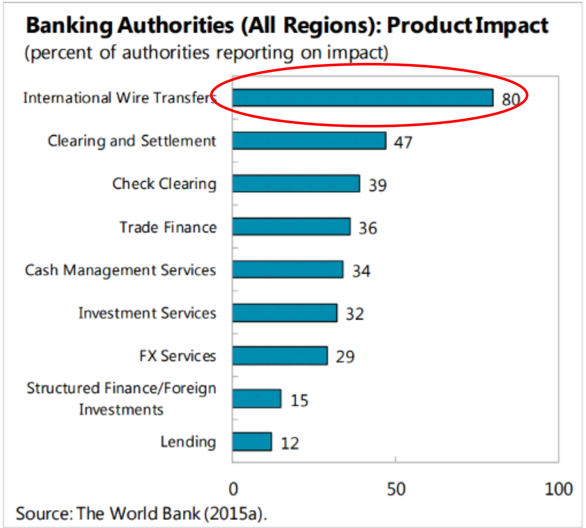
IMPACT ON THE CARIBBEAN

Regulatory Risk

- A victim of this paradigm shift is correspondent banking itself, as the large financial institutions have distanced themselves from the scene;
- Payments/remittances become less transparent;
- Inter-Regional De-Risking of perceived higher risk customers to avoid the possible loss of U.S. correspondent relationships;
- **The demand from the correspondent bank** to exclude high risk customers (MSBs, Casinos, IBCs, Marijuana) from the client base;

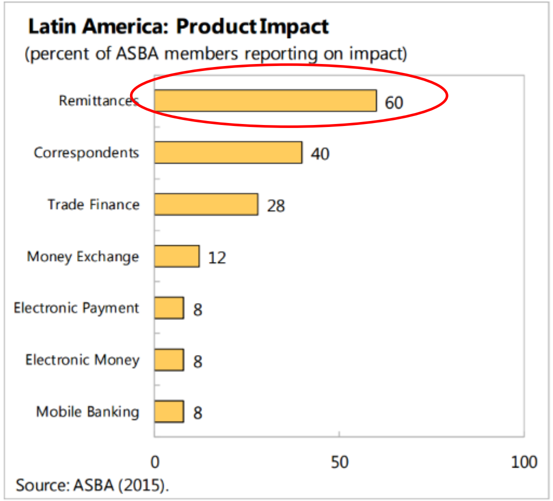
The Consequences

While 80 percent of authorities have indicated that U.S. dollar wire transfers have been affected...



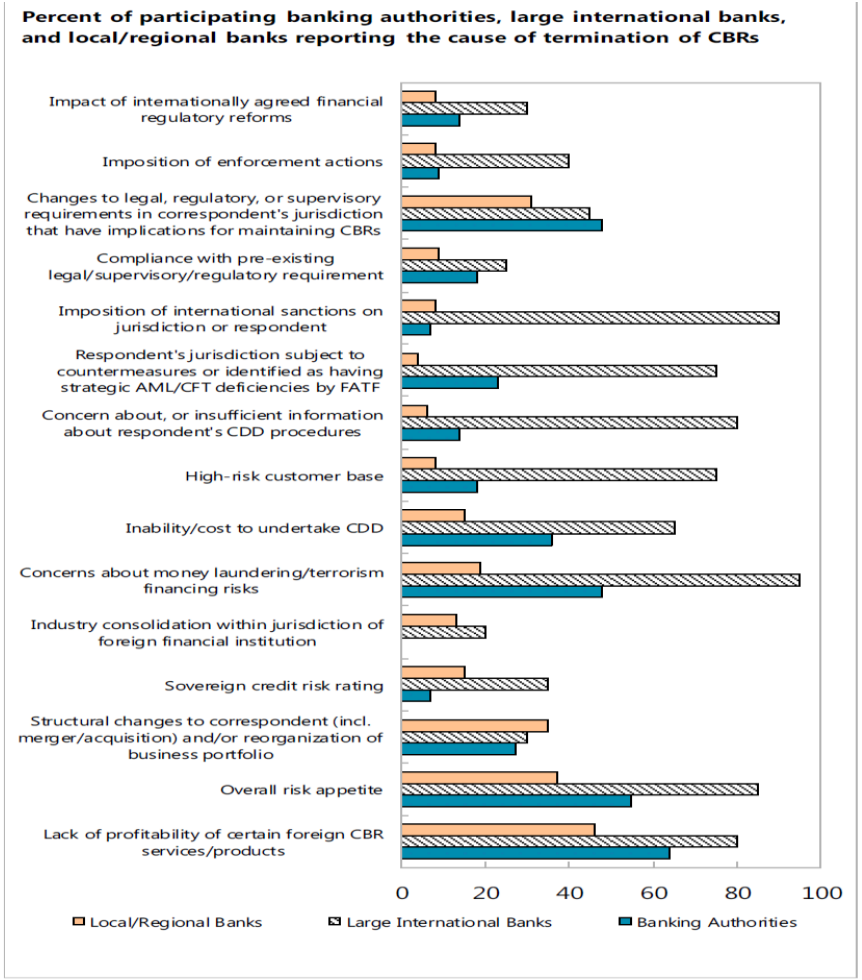
Electronic transfers in US dollars, remittances, trade finance, have been particularly affected.

...in the Americas, 60 percent of ASBA members report that remittances have been affected.



*Source: IMF Staff Discussion Note 2016

2015 Survey



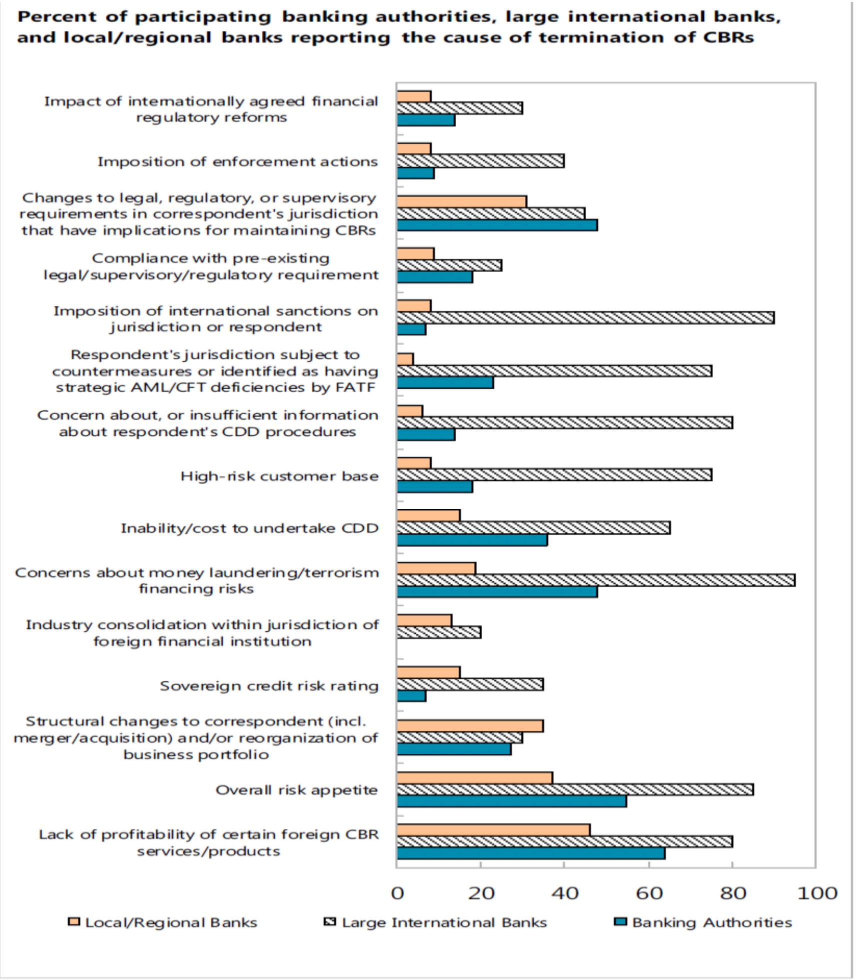
Source: World Bank (2015a).
Note: Respondents were allowed to choose multiple options.
[1] The evidence from the World Bank (2015a) covers the period 2012-mid-2015.

Imposition of International sanctions

Information of CDD Procedures

Money Laundering and terrorism

Risk Appetite



Source: World Bank (2015a).
Note: Respondents were allowed to choose multiple options.
[1] The evidence from the World Bank (2015a) covers the period 2012-mid-2015.

2019

Imposition of Enforcement Actions

Jurisdiction identified as having strategic AML/CFT deficiencies

High Risk Customer Base

Lack of Profitability

Other Reasons or Concerns

- Reputational Risk
- Sovereign Solvency
- Negative News
- Anti Bribery and Corruption (ABC) Concerns
- “Last Man Standing”
- Financial Inclusion
- Contagion

HOW CAN WE IMPROVE THE SITUATION?

A Balanced Approach - **What is needed?**

- A balanced regulatory focus (there is no global, “one-size fits all” regulatory scheme or solution);
  - Effective regulation and supervision, in line with international standards, is crucial to building trust, reducing risks, and making countries’ markets more attractive to global banks

- Culture of Compliance and Transparency:
  - The sustainability of business models that rely on opaque or offshore structures may therefore have to be reassessed.
  - Opaque corporate structures and arrangements can be misused to conceal beneficial ownership – use for illicit purposes, including tax evasion, money laundering and evasion of sanctions.

- Removing impediments to information sharing. Wholesome implementation of regulations and an active enforcement regime

- Education and training both of bankers and regulators


FIBA
Thank You