



De-Risking is a Threat to the International Financial System

The severing of correspondent banking relationships is having a severe impact on the Caribbean region, leaving many businesses and individuals cut off from their money and making it difficult for new businesses to establish operations. This was revealed by Central Bank of Barbados Governor, Dr. DeLisle Worrell as he presented the findings of a Caribbean-wide survey at the Financial Stability Board's (FSB) meeting in Tokyo last week.

According to Worrell, who attended the meeting in his capacity as co-Chair of the Financial Stability Board's Regional Consultative Group, Americas (FSB/RCG_A), Belize has experienced terminations in correspondent bank relationships that account for more than half of their banking assets. Belize's central bank has sought to provide assistance, but some customers in that country still have no access to their funds.

While Belize has been the jurisdiction most affected, other territories in the region are also facing challenges. In Jamaica, where remittances are a major source of foreign exchange, the number of money transfer businesses and foreign exchange traders has declined as a result of the severance of correspondent banking relationships; Guyana and the countries of the Eastern Caribbean Currency Union have experienced terminations; and business has slowed in the International Business and Financial Services sectors in the Cayman Islands, The Bahamas and Barbados.

Eight correspondent banking relationships in Barbados' IBFS sector have been severed, and although several of these businesses have been able to establish relationships with other financial institutions, others have not. A further concern, says Worrell, is the loss of new business in the sector due to correspondent banks' unwillingness to take on new customers.

Worrell explained that the terminations being experienced in the region are not based on any wrongdoing on the part of businesses, but rather are the result of the increasingly high cost of compliance with the regulatory framework outlined by Basel, the Foreign Account Tax Compliance Act (FATCA), the Global Forum and other bodies. In many cases, correspondent banks are also challenged by guidelines that are unclear or inconsistently applied.

The de-risking phenomenon has already affected countries in Asia, Africa and Latin America in a major way, and more terminations of correspondent accounts and loss of banking services can be expected worldwide. This is because many correspondent banks have weighed the marginal profits earned from doing business against the potential large fines and penalties due to lack of compliance as well as the reputational damage that could result and deemed it too much of a risk to continue to pursue business in these jurisdictions.

Worrell says that a solution needs to be found that will reduce the burden on banks of collecting and reporting detailed information for a variety of purposes, which has made retail and correspondent banking unprofitable in some areas, and for some activities. He argues that there also needs to be

consistency among regulators about the information that is required as well as limits to banks' liability to fines and penalties in cases of inefficiency, where there has been no proven illegal activity.

He asserts that if a solution is not found, the countries and individuals who no longer have access to the services of international banks, either directly or through the correspondent relationship of local banks, will have to conduct their financial and foreign exchange transactions outside of the international system of licensed financial institutions. This will make international transactions much riskier, and it would mean that no information on these transactions would be reported to the regulators.

The issue of de-risking was previously discussed at the FSB/RCG_A meeting that was held in Barbados in December 2015, which was attended by the IMF and the Bank of International Settlement as well as countries from the Caribbean and Central and South America. Follow-up discussions have been planned for later this month in Jamaica, where regional representatives will hold talks with the US Treasury and again at the FSB/RGC_A meeting in Montreal.

In addition to the current challenges being experienced with correspondent banking, the Tokyo meeting also featured discussion about a range of issues related to the stability of the international financial system.

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