

FATF clarifies risk-based approach: case-by-case, not wholesale de-risking

Paris, 23 October 2014 - The FATF Plenary discussed the issue of de-risking on 22 October. Generally speaking, de-risking refers to the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk in line with the FATF's risk-based approach. De-risking can be the result of various drivers, such as concerns about profitability, prudential requirements, anxiety after the global financial crisis, and reputational risk. It is a misconception to characterise de-risking exclusively as an anti-money laundering issue.

This issue is of crucial importance to the FATF for two main reasons:

De-risking can introduce risk and opacity into the global financial system, as the termination of account relationships has the potential to force entities, and persons into less regulated or unregulated channels. Moving funds through regulated, traceable channels facilitates the implementation of anti-money laundering / countering the financing of terrorism (AML/CFT) measures.

It is central to our mandate to ensure that the global AML/CFT standard is well understood and accurately implemented, and that countries and their financial institutions are provided with support in designing AML/CFT measures that meet the goal of financial inclusion.

Recent supervisory and enforcement actions have raised the consciousness of banks and their boards about these issues. However, it is important to put into context that these were extremely egregious cases involving banks who deliberately broke the law, in some cases for more than a decade, and had significant fundamental AML/CFT failings.

"De-risking" should never be an excuse for a bank to avoid implementing a risk-based approach, in line with the FATF standards. The FATF Recommendations only require financial institutions to terminate customer relationships, on a case-by-case basis, where the money laundering and terrorist financing risks cannot be mitigated. This is fully in line with AML/CFT objectives. What is not in line with the FATF standards is the wholesale cutting loose of entire classes of customer, without taking into account, seriously and comprehensively, their level of risk or risk mitigation measures for individual customers within a particular sector.

The risk-based approach should be the cornerstone of an effective AML/CFT system, and is essential to properly managing risks. The FATF expects financial institutions to identify, assess and understand their money laundering and terrorist financing risks and take commensurate measures in order to mitigate them. This does not imply a "zero failure" approach.

The FATF is committed to financial inclusion, and effective implementation of AML/CFT measures through proper implementation of the risk-based approach.

Given the importance of this issue, and in light of these discussions the FATF has agreed:

To gather further evidence and analysis on the drivers and scale of de-risking. The FATF's country assessments will be critically important in this regard, not least for FATF to reinforce its expectations on risk understanding and management. The FATF will also make full use of the work being conducted in other relevant international groups and forums, including the G20 Global Partnership for Financial Inclusion, the IMF, the World Bank Group, and the Basel Committee on Banking Supervision.

To continue to disseminate its various reports on risks, methods and trends allowing service providers to better understand money laundering and terrorist financing risks related to specific categories of customers and devise effective risk-based approaches.

To continue a number of existing activities and projects providing information and guidance to inform risk-based decision-making, including work on the risk-based approach for banks, the risk-based approach for money or value transfer services, best practices on combating the abuse of non-profit organisations, effective supervision and enforcement.

To stay abreast of developments in this area and to continue to interact with all actors relevant to this topic including the sectors most affected, regulators, supervisors, and banks.

To consider, on the basis of the evidence on the drivers and scale of de-risking, whether further work is necessary on specific issues. The FATF's Policy and Development Group will determine this during the February 2015 FATF Plenary.

The FATF is adopting at this Plenary Risk-based Approach Guidance for the Banking Sector which gives clear guidance on how to properly implement the risk-based approach, and is explicitly meant to be read in conjunction with the FATF Guidance on AML/CFT and Financial Inclusion. Banks who implement the risk-based approach, in line with the guidance given in these two papers, will be well-placed to avoid the consequences of inappropriate de-risking behaviour.

More reading:

Risk-based Approach Guidance for the Banking Sector

FATF Guidance on AML/CFT and Financial Inclusion

National money laundering and terrorist financing risk assessment

FATF Recommendations (Recommendation 1)