

Being Compliance “User-Friendly” Can Help Preserve Banking Relationships

Faced with unprecedented domestic anti-money laundering (“AML”) regulatory pressure, U.S. banks are actively “de-risking” their foreign correspondent banking portfolios. This means that U.S. banks are aggressively terminating relationships (and sometimes exiting whole jurisdictions) perceived by them to present too much AML risk. Given that many Latin American financial institutions depend on U.S. correspondent relationships, “de-risking” may represent a significant new challenge. To solidify U.S. banking relationships, Latin American financial institutions need to be “compliance user-friendly.”

“De-risking” is a consequence of recent U.S. regulatory actions against some of the world’s largest banks that alleged systemic AML compliance deficiencies. These actions resulted in billion dollar settlements and required the U.S. banks to take on costly internal reviews and reforms. For some U.S. banks, maintaining high AML risk relationships is simply not worth the compliance effort. This is especially true when a regulator can always second-guess a seemingly sound decision, based either on shifting expectations or over-generalizations about country “risk.” To make matters worse, if one U.S. bank exits, other U.S. banks may feel pressured to do the same, and to make the “de-risking” decision quickly.

We believe that proactively addressing the AML concerns of U.S. correspondent banking partners is essential: if a U.S. bank decides to exit, it can be difficult or impossible to overturn its decision regardless of the merits. U.S. banks have almost complete latitude in deciding with whom they will or will not have correspondent relationships, even if the relationships are of long standing. If a U.S. bank expresses concern and threatens exit, it may be too late to resolve what otherwise could have been a resolvable problem. In the current U.S. regulatory environment, understanding what U.S. banks need from a due diligence perspective, and forming a strategy to provide it, may help solidify otherwise endangered banking relationships.

Latin American financial institutions that want to defend proactively against “de-risking” should pay close attention to the U.S. Federal Financial Institutions Examination Council Manual (the “FFIEC Manual”). The FFIEC Manual tells U.S. regulators what to look for when examining a U.S. bank’s correspondent accounts and defines “adequate due diligence.” It can also guide Latin American financial institutions that want to be “compliance user-friendly,” and help them develop strong compliance partnerships with their U.S. counterparts.

For example, the FFIEC Manual requires that U.S. banks understand their correspondent customer’s AML controls, and regulators will scrutinize U.S. banks for evidence of this understanding. In the past, a U.S. bank may have asked a correspondent customer to fill out a questionnaire and moved on. The FFIEC Manual, however, requires more, and U.S. banks are increasingly worried that such pro forma due diligence provides little defense to regulator-driven AML-related criticisms.

In conversations with regulators, U.S. banks often must demonstrate that their correspondent customer’s AML compliance controls are sufficient. For a U.S. bank, gathering and analyzing more detailed due diligence is expensive, especially when it maintains large numbers of correspondent accounts in multiple high AML risk jurisdictions. An individual customer, however, should be able to leverage its own compliance controls, and volunteer the required information to the U.S. bank in an

easily digestible, transparent form. A U.S. bank customer that does so may cement what otherwise could be a tenuous relationship given the current U.S. regulatory environment.

“De-risking” is not an entirely new concept, but its application is growing ever-more common. Proactively demonstrating that a Latin American financial institution is “compliance user-friendly” makes good sense at a time when “de-risking” is prevalent. Lewis Baach has advised numerous non-U.S. financial institutions and central banks on avoiding the consequences of “de-risking,” including in Latin America, and is able to assist Latin American financial institutions in such efforts.

For further information please contact either:

Arthur D. Middlemiss at arthur.middlemiss@lewisbaach.com or 212-826-7001

Manuel S. Varela at manuel.varela@lewisbaach.com or 202-659-7874

Cristian Francos at cristian.francos@lewisbaach.com or +54 [11]4850 1220

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