



## PACIFIC ISLANDS FORUM SECRETARIAT

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### FORUM ECONOMIC OFFICIALS MEETING

### FORUM ECONOMIC MINISTERS MEETING

10-12 August 2022

Port Vila, Vanuatu

#### AGENDA ITEM 7D:

### CLOSURE OF CORRESPONDENT BANKING RELATIONSHIPS AND NON-COOPERATIVE TAX JURISDICTIONS (NCTJ)

#### Purpose and Recommendations

##### Purpose

This paper:

- i. Highlights the issue of de-risking and its impact on the closure of corresponding banking relationship in FICs; and
- ii. Raises the issue of EU's list of Non-cooperative Jurisdictions on Tax and the concerns it is having on Members countries, especially those on the list.

#### A. Issue

Correspondent banking connects Pacific Island economies, as every other country, with the international financial system. This enables:

- cross-border payment services,
  - aid flows,
  - international
  - trade,
  - foreign direct investments, and
  - remittances flow.
2. However, correspondent banking services is declining in the Pacific and globally due to:
    - Rising risk management and compliance cost resulting from AML-CFT requirement;
    - Profitability concerns;
    - Reputational risk.
    - Change in business strategy;
    - Risk avoidance
  3. The impact of de-risking in correspondent banking varies from country to country depending on the robustness of its economy, the depth of its financial system and the relative importance of international

trade and finance on the economy. For Pacific Islands the consequence of de-risking is especially acute due to:

- i. The relative importance of remittance to small economies
- ii. The limited number of correspondent banking providers in the region
- iii. Challenging commercial conditions
- iv. Immature regulatory compliance and capabilities.

## **B. POTENTIAL CONSEQUENCES**

4. On the worst-case scenario, a near-loss of correspondent banking relationships will:
  - a. Limit a nation's access to the international financial system;
  - b. Limit the ability to perform payment services and currency exchange and therefore limit remittance and trade;
  - c. Risk of worsening financial exclusion;
  - d. Risk of jeopardizing poverty alleviation efforts.
5. Withdrawal of New Zealand and Australian Banks may drive Pacific islands to replace good quality banks with lower quality ones and pay for more expensive services that may raise the cost of remittances in the region and may raise financial stability risk.

## **C. CURRENT REMEDIAL STRATEGY**

6. Electronic-Know Your Customer (E-KYC) Initiative:
  - 34<sup>th</sup> South Pacific Central Bank Governors Meeting in 2019 endorsed a project to develop a regional KYC project.
  - In 2020 the Steering Committee was formed with senior representatives from central banks and IMF to govern the project.
  - The 35<sup>th</sup> South Pacific Governors meeting agreed that the steering committee develop a business case on the potential implementation of a regional e-KYC facility by November 2021.

In progress

7. IMF efforts:
  - Strengthening AML-CFT supervision and compliance via a combination of training through STI and TA programs.
  - Suggestions to enhance remittances options.
  - G20 Cross-Border payment roadmap for remittance corridors.

## **D. KEY QUESTIONS AND OBSERVATIONS**

8. Are the strategies currently being pursued to address de-risking of correspondent banking services enough to reverse the trend?
9. If the current remedial actions are limited, then our leaders have a responsibility to collectively raise their concerns through this Forum, for a fairer and more leniency in AML-CFT standards that takes into account the vulnerability, the shallowness of the economies, and the smallness of the Pacific Islands nations when standardizing AML-CFT risk assessment framework, the main factor behind de-risking in correspondent banking.

Pacific Islands Forum Secretariat  
10 August 2022