

This submission is made by the Centre for Financial Crime and Security Studies (CFCS) at the Royal United Services Institute (RUSI). It represents the views of the research team members who have contributed their expertise. It does not represent the views of RUSI itself. Further details of our programme can be found at the end of this submission.

The need for access and usage of the formal financial system is key in the effective implementation of the Financial Action Task Force (FATF) standards and to strengthening efforts to tackle illicit finance more broadly.¹ If individuals and/or entities are excluded from the formal financial system, they have little choice but to access the unregulated informal financial system where illicit finance flourishes. Over the last few years, we have carried out an extensive research project looking at the impact of global anti financial crime standards on financial inclusion, funded by the Bill and Melinda Gates Foundation. Our work has culminated in three research papers, set out below:

- [Assessing the Financial Action Task Force’s Impact on Digital Financial Inclusion](#)
- [Walk the Talk: How the Financial Action Task Force Can Prioritise Financial Inclusion](#)
- [Lessons Learned from the Fourth Round of Mutual Evaluations](#)

In collaboration with ACAMS and the Toronto Center, we have also developed online training modules about financial inclusion for the private sector and national regulators.

This submission is drawn from the research we have carried out on the impact of the FATF standards on financial inclusion and we have, therefore, confined our submission to comments on Section 5 of the draft guidance, *Guidelines on policies and controls for the effective management of ML/TF risks when providing access to financial services*.

Section 5 – Guidelines on policies and controls for the effective management of ML/TF risks when providing access to financial services:

2. Do you have any comments on the section ‘Subject matter, scope and definitions’? If you do not agree, please set out why you do not agree and if possible, provide evidence of the adverse impact provisions in this section would have.

We note that the definitions refer only to Money Laundering (ML) and Terrorist Financing (TF) risk and ML/TF risk factors. In October 2020, the FATF’s Recommendations 1 and 2 were updated to include the requirement for countries and the private sector to identify and mitigate risks related to Proliferation Financing (PF). Given that some of the actions taken by countries and institutions to mitigate the risks of PF may have an impact on financial inclusion, it would therefore seem appropriate that the ‘Subject matter, scope and definitions’ section also includes reference to PF and PF risk factors.

3. Do you have any comments on the section titled ‘General requirements’?

The ‘General requirements’ section sets out the overall approach that credit and financial institutions should take to mitigating higher ML/TF risks and the measures that should be considered prior to taking a decision to reject or terminate a business relationship. These include adjusted monitoring and applying restrictions to services or products, explored further in the following sections.

We welcome the guidance provided by the EBA and its objectives, in particular the distinction between ML/TF risk associated with an individual customer and those associated with a category of

¹ https://static.rusi.org/267_op_gates_financial_inclusion.pdf

customers, notwithstanding our comments above in relation to the need to include consideration of PF risks. The lack of distinction between individual customer risk and the risk associated with a category of customer has previously led to derisking behaviours which have had a hugely detrimental impact on particularly categories of customers, notably Non-Profit Organisations (NPOs) but also on geographical areas, such as the Caribbean. The emphasis in paragraphs 11 and 12 of the draft guidance on ensuring that institutions have considered all possible mitigating measures before refusing or terminating a business relationship is line with the position taken by FATF that the risk-based approach requires that institutions should seek to manage their ML/TF/PF risks rather than avoid them.²

Paragraph 14 requires that credit and financial institutions document the decision to refuse or terminate a business relationship and that this documentation should be available to supervisors. It is important that supervisors are encouraged to consider the extent to which their supervised population has followed this guidance and whether exit decisions are appropriately risk-based. Our research has shown that more effective financial inclusion could be encouraged by including consideration of it within the FATF Mutual Evaluation (ME) process, *“By capturing financial inclusion in the measurement of the effectiveness of a country’s anti-financial crime framework, the FATF would cement the ethos that a financial system cannot be fully effective from an anti-financial crime perspective if people face financial exclusion.”*³ Likewise, supervisors could encourage more effective financial inclusion measures if they considered how institutions effected financial inclusion within their policies and procedures as part of their supervisory activities.

Paragraphs 15 and 16 of the guidance refer to the right of access to a payment account with basic features and that the limited functionality of this type of account may mitigate the ML/TF risk. What the guidance does not explicitly state is that institutions should be encouraged to apply Simplified Due Diligence (SDD) for customers where it is assessed that there is a lower ML/TF/PF risk, as per FATF Recommendation 1. SDD is optional but it allows institutions to perform less-resource intensive checks on potential customers. It also allows institutions to apply some flexibility to the requirements for opening an account, for example the type of identity documents needed. This is an approach encouraged by FATF through guidance on using alternate forms of identification and assisting jurisdictions seeking to make their regulations more flexible by providing guidance for situations where SDD could be applied to make services more accessible.⁴

Despite the potential benefits of SDD, our research has shown that there are several barriers to its use including a lack of understanding of ML/TF/PF risks, a lack of support for SDD from supervisors and regulators, and a lack of incentives for the private sector to use it.⁵ It would therefore be beneficial for the guidance to provide some additional clarity as to circumstances in which SDD can be used and to use language which proactively encourages credit and financial institutions to apply SDD where appropriate. The EBA’s guidance on the use of flexibility within the regulatory regime when opening accounts for Ukrainian refugees following the Russian invasion of Ukraine in 2022 was a welcome example of where specific guidance on the use of SDD can be hugely beneficial.⁶

² <https://www.fatf-gafi.org/en/publications/Fatfgeneral/Rba-and-de-risking.html>

³ https://static.rusi.org/268_pb_gates_financial_inclusion_web_0.pdf, page 8

⁴ Chase, I. (2020) ‘Doing what is right: Financial inclusion needs better Incentives’. Available online: <https://rusi.org/explore-our-research/publications/commentary/doing-what-right-financial-inclusion-needs-better-incentives>.

⁵ https://static.rusi.org/267_op_gates_financial_inclusion.pdf

⁶

https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Other%20publications/2022/1031627/EBA%20statement%20on%20financial%20inclusion%20in%20relation%20to%20Ukraine.pdf

We note that paragraph 19, in the section on adjusted monitoring, references some examples of situations where individuals may not have access to traditional forms of identity and recommends the steps that credit and financial institutions should take. This is, in effect, SDD and we would suggest that this section is moved to a new section titled 'Application of SDD' (or similar) to make it clear that the application of SDD is an essential part of financial inclusion and managing ML/TF/PF risks.

4. Do you have any comments on the section titled 'adjusting monitoring'?

As noted above, we suggest that paragraph 19 is moved to a new section on the use of SDD and that this section focuses on the use of monitoring. Ongoing monitoring, whether manual or automated, is particularly important in the context of financial inclusion as it may help to mitigate and manage ML/TF/PF risks associated with customers, particularly where they may have been limited KYC information collected.

Many institutions have implemented automated transaction monitoring systems to help them carry out ongoing monitoring of customer accounts. Automated transaction monitoring systems will generate alerts based on pre-defined rules that may indicate of unusual and/or suspicious behaviour. While automated transaction monitoring systems have many advantages, it is important to note that the underlying rules may be calibrated in a way that may impact disadvantaged customer segments and consequently limit their financial inclusion. It is important, therefore, that a system's rules and the underlying data are regularly reviewed to ensure that they are free from bias and do not disproportionately impact any groups of disadvantaged customers. For example, a transaction monitoring rule might be calibrated so that transactions associated with or made by customers from a particular disadvantaged group might be subject to excessive scrutiny. This may prevent those customers from being able to fully use their accounts. It is important to note that financial inclusion does not just depend on customers being able to access financial products and services but being able to use those products and services. We, therefore, recommend that the guidance provides further detail on how credit and financial institutions should ensure that their ongoing monitoring procedures do not adversely impact on financial inclusion.

It is also important that, as noted in the section on applying restrictions to services or products, such restrictions may be an important part of managing ML/TF/PF risks and therefore it is important that ongoing monitoring systems are able to identify any unpermitted usage. Ongoing monitoring may also indicate when a basic product or services is no longer meeting the needs of a customer and they may require a more sophisticated product or services (which, in turn, may require a further level of customer due diligence).

5. Do you have any comments on the section titled 'applying restrictions to services or products'?

As we note above, financial inclusion depends both on access and usage of services and products. There is also a third dimension to financial inclusion, that of quality. Services and products should be useful and affordable. While the restrictions identified by the EBA may be appropriate ways of managing ML/TF/PF risks, it is also important that the restrictions do not, in and of themselves, hinder financial inclusion for example by reducing the utility of a service or product to the extent that it does not provide any benefits to the consumer. The guidance, therefore, should make it clear that restrictions should be proportionate to the ML/TF/PF risk and should not be overly onerous.

6. Do you have any comments on the section titled 'Complaint mechanisms'?

It is essential that a complaint mechanism exists for those that feel that they have been unfairly financially excluded and we welcome the provision in the guidance. We note, however, that many of those that are more vulnerable to financial exclusion may not have the capacity or capability to make a formal complaint. There may, for example, be language or cultural barriers. The EBA should therefore try to ensure that the complaint mechanisms are accessible to all.

Our work has also shown that there are cases where politically motivated attempts are made to freeze or block accounts, typically citing some kind of financial crime investigation. The complaint mechanism might therefore benefit from being expanded to include asset freezes that are seemingly unjustified or where the account holder is given no explanation as to why their access to their account has been blocked.

About The Centre for Financial Crime and Security Studies (CFCS) at RUSI

The Centre for Financial Crime and Security Studies (CFCS) specialises on the intersection between finance and global security. Our pioneering analysis and actionable ideas aim to challenge the status quo and build resilience in the global response to illicit finance. Our work covers a range of state and non-state based security threats, which we examine through a financial lens. Since CFCS's inception in 2014, we have been driving change through our partnership-based approach and the development of viable solutions.

Our work has helped to unveil the scale and complexities behind international illicit finance, as well as to identify realistic policy responses across both the public and private sectors. We focus on putting our evidence-based research into practice through capacity-building and collaborative workshops. CFCS experts are regularly called upon to advise governments and international bodies, including the UN Security Council, the Financial Action Task Force, the UK and European Parliaments and US Congress. Through our public engagements and events, we aim to highlight to wider audiences the pivotal role of finance in global security issues.

One of our programmes is based in Brussels and fosters a more financially resilient Europe. By leveraging CFCS's global expertise, it spotlights financial crime challenges specific to the European context and provides recommendations and expertise to EU stakeholders, national policymakers, and EU partners. We spur improvements by working with a vast and vibrant network of private and public partners and civil society across Europe. The activities implemented by the Brussels-based team cover weaponisation of finance, EU sanctions, fighting corruption in Ukraine, and counterterrorist financing.