

Correspondent Accounts (Foreign) — Overview

Objective. *Assess the adequacy of the U.S. bank’s systems to manage the risks associated with foreign correspondent banking and management’s ability to implement effective due diligence, monitoring, and reporting systems. This section expands the earlier core review of statutory and regulatory requirements of foreign correspondent account relationships in order to provide a broader assessment of the AML risks associated with this activity.*

Foreign financial institutions¹⁸⁰ maintain accounts at U.S. banks to gain access to the U.S. financial system and to take advantage of services and products that may not be available in the foreign financial institution’s jurisdiction. These services may be performed more economically or efficiently by the U.S. bank or may be necessary for other reasons, such as the facilitation of international trade. Services may include:

- Cash management services, including deposit accounts.
- International funds transfers.
- Check clearing.
- Payable through accounts.
- Pouch activities.
- Foreign exchange services.
- Overnight investment accounts (sweep accounts).
- Loans and letters of credit.
- Lines of credit.

Contractual Agreements

Each relationship that a U.S. bank has with a foreign correspondent financial institution should be governed by an agreement or a contract describing each party’s responsibilities and other relationship details (e.g., products and services provided, acceptance of deposits, clearing of items, forms of payment, and acceptable forms of endorsement). The agreement or contract should also consider the foreign financial institution’s AML regulatory requirements, customer base, due diligence procedures, and permitted third-party usage of the correspondent account.

¹⁸⁰ The term “foreign financial institution” as defined in 31 CFR 1010.605(f) generally includes:

- A foreign bank.
- A foreign branch or office of a U.S. bank, broker/dealer in securities, futures commission merchant, introducing broker, or mutual fund.
- Any other person organized under foreign law that, if located in the United States, would be a broker/dealer in securities, futures commission merchant, introducing broker, or mutual fund.
- Any person organized under foreign law that is engaged in the business of, and is readily identifiable as, a currency dealer or exchanger or a money transmitter.

Risk Factors

Some foreign financial institutions are not subject to the same or similar regulatory guidelines as U.S. banks; therefore, these foreign institutions may pose a higher money laundering risk to their respective U.S. bank correspondent(s). Investigations have disclosed that, in the past, foreign correspondent accounts have been used by drug traffickers and other criminal elements to launder funds. Shell companies are sometimes used in the layering process to hide the true ownership of accounts at foreign correspondent financial institutions. Because of the large amount of funds, multiple transactions, and the U.S. bank's potential lack of familiarity with the foreign correspondent financial institution's customer, criminals and terrorists can more easily conceal the source and use of illicit funds. Consequently, each U.S. bank, including all overseas branches, offices, and subsidiaries, should closely monitor transactions related to foreign correspondent accounts.

Without adequate controls, a U.S. bank may also set up a traditional correspondent account with a foreign financial institution and not be aware that the foreign financial institution is permitting other financial institutions, or customers to conduct transactions anonymously through the U.S. bank account (e.g., payable through accounts¹⁸¹ and nested accounts).

Nested Accounts

Nested accounts occur when a foreign financial institution gains access to the U.S. financial system by operating through a U.S. correspondent account belonging to another foreign financial institution. If the U.S. bank is unaware that its foreign correspondent financial institution customer is providing such access to third-party foreign financial institutions, these third-party financial institutions can effectively gain anonymous access to the U.S. financial system. Unacceptable nested activity and other activity of concern may be characterized by transactions to jurisdictions in which the foreign financial institution has no known business activities or interests and transactions in which the total volume and frequency significantly exceeds expected activity for the foreign financial institution, considering its customer base or asset size. U.S. banks should also focus on nested account transactions with any entities the bank has designated as higher risk.

Risk Mitigation

U.S. banks that offer foreign correspondent financial institution services should have policies, procedures, and processes to manage the BSA/AML risks inherent with these relationships and should closely monitor transactions related to these accounts to detect and report suspicious activities. The level of risk varies depending on the foreign financial institution's strategic profile, including its size and geographic locations, the products and services it offers, and the markets and customers it serves. The Clearing House Association, LLC., and The Wolfsberg Group have published suggested industry standards and guidance for banks that provide foreign correspondent banking services.¹⁸² When dealing with foreign correspondent account relationships, it is important for the bank to keep in mind regulatory requirements related to special measures issued under 311 of the USA PATRIOT Act

¹⁸¹ Refer to the expanded overview section, "Payable Through Accounts," page 194, for additional information.

¹⁸² Refer to [Guidelines for Counter Money Laundering Policies and Procedures in Correspondent Banking](#) and [the Wolfsberg AML Principles for Correspondent Banking](#).

contained in the expanded overview section, “Special Measures” page 133. Additional information relating to risk assessments and due diligence is contained in the core overview section, “Foreign Correspondent Account Recordkeeping, Reporting, and Due Diligence,” page 111.

The U.S. bank’s policies, procedures, and processes should:

- Specify appropriate account-opening/on-boarding procedures, which may include minimum levels of documentation to be obtained from prospective customers; an account review and approval process that is independent of the correspondent account business line for potential higher-risk customers; and a description of circumstances when the bank does not open an account.
- Assess the risks posed by a prospective foreign correspondent customer relationship utilizing consistent, well-documented risk-rating methodologies, and incorporate that risk determination into the bank’s suspicious activity monitoring system.
- Understand the intended use and purpose of the accounts and expected account activity (e.g., determine whether the relationship serves as a payable through account).
- Understand the foreign correspondent financial institution’s other correspondent relationships (e.g., determine whether and how nested accounts are to be utilized).
- Conduct adequate and ongoing due diligence on the foreign correspondent financial institution relationships, which may include periodic site visits based on risk.
- Determine whether the foreign correspondent financial institution has in place acceptable AML compliance processes and controls.
- Ensure that appropriate due diligence standards are applied to those accounts determined to be higher risk.
- Ensure that foreign correspondent financial institution relationships are appropriately included within the U.S. bank’s suspicious activity monitoring and reporting systems.
- Follow up on account activity and transactions that do not fit the foreign financial institution customer’s strategic profile (i.e., transactions involving customers, industries or products that are not generally part of that foreign financial institution’s customer base or market).
- Establish a formalized process for escalating suspicious information on potential and existing customers to an appropriate management level for review.
- Establish criteria for closing the foreign correspondent financial institution account.

As a sound practice, U.S. banks are encouraged to communicate their AML-related expectations to their foreign correspondent financial institution customers. Moreover, the U.S. bank should generally understand and assess the quality of the AML controls at the foreign correspondent financial institution, including customer due diligence practices, suspicious activity identification processes, and recordkeeping documentation. They should

also have an understanding of the effectiveness of the AML regime of the foreign jurisdictions in which their foreign correspondent banking customers operate.