



BANGKO SENTRAL NG PILIPINAS

OFFICE OF THE GOVERNOR

CIRCULAR NO. 1078

Series of 2020

Subject: Guidelines on Correspondent Banking Relationships

The Monetary Board, in its Resolution No. 322 dated 27 February 2020, approved the attached guidelines on correspondent banking relationships.

Section 1. Section 923 of the Manual of Regulations for Banks (MORB), on Additional Preventive Measures for Specific Customers, is hereby amended to read, as follows:

"xxx

Correspondent banking. Covered persons shall adopt policies and procedures to prevent correspondent banking activities from being utilized for ML/TF activities, and designate an officer responsible in ensuring compliance with these regulations and the covered person's policies and procedures.

The Guidelines on correspondent banking relationships are provided in Appendix 140.

Supervisory enforcement action. Consistent with Section 002, the Bangko Sentral may deploy enforcement actions to promote adherence to the requirements set forth in this Section and bring about timely corrective actions.

Fund/wire transfer. xxx

xxx"

Section 2. This Circular shall take effect 15 days after its publication either in the Official Gazette or in a newspaper of general circulation in the Philippines.

FOR THE MONETARY BOARD:

A handwritten signature in black ink, appearing to read "Benjamin E. Diokno".

BENJAMIN E. DIOKNO

Governor

09 March 2020

Guidelines on Correspondent Banking Relationships **(Appendix to Section 923)**

I. Introduction

These guidelines articulate the specific regulatory expectations with respect to different types of correspondent banking relationships to enable banks to have improved understanding and management of money laundering (ML) and terrorism financing (TF) risks associated with correspondent banking relationships. The inherent nature and structure of transactions and relationships in correspondent banking renders it vulnerable to money laundering/terrorist financing activities. Correspondent banks execute financial transactions on behalf of customers of another bank (the respondent bank). As a result of this indirect relationship, the correspondent bank provides services for individuals or entities whose identities it has not actually verified. Meanwhile, the cross-border nature and amount of transactions involved in correspondent banking pose material threat to financial institutions. The layers involved in transactions processed through correspondent banking relationships pose a challenge in monitoring transactions and in identifying suspicious transactions. These should be considered in implementing a robust risk management system for correspondent banking relationships.

II. Applicability and Scope

These guidelines shall apply to covered persons engaged in correspondent banking as defined herein.

Banks shall perform the applicable customer due diligence on accounts and relationships opened upon the effectivity of these guidelines. For existing relationships, the requirements shall be applied upon updating as part of ongoing monitoring.

By virtue of the arrangements in correspondent banking services wherein the respondent bank is the customer of the correspondent bank, the rules on outsourcing under Section 112 of the Manual of Regulations for Banks shall not apply to correspondent banking relationships.

III. Definition of Terms

- a. *Correspondent banking* refers to the provision of banking services by one bank (the correspondent bank) to another bank (the respondent bank)¹ whose relationship can be domestic or foreign, as provided in Part V (Forms of Correspondent Banking Services) hereof.

¹ FATF Guidance on Correspondent Banking Services, October 2016

- b. *Correspondent bank* refers to the bank which processes and/or executes transactions for customers of the respondent bank, wherein the latter's account is used to process and/or execute the transactions of its customers. The correspondent bank generally does not have direct business relationships with the customers of the respondent bank, unless it provides payable-through-account services.¹
- c. *Respondent bank* refers to the bank that is the direct customer of the correspondent bank.¹
- d. *Relationship Management Application (RMA)* refers to the messaging capability enabling members of the Society for Worldwide Interbank Financial Telecommunication (SWIFT) network to exchange authenticated messages over the network.²
- e. *Customer RMA* refers to a relationship which is established for SWIFT message exchanges involving transactional or liability accounts.
- f. *Non-Customer RMA* refers to a relationship which is generally created when there is a request that the bank sends or receives messages to/from a third party (the non-customer) in support of a client's business and where the bank has no other relationship with that third party.
- g. *NOSTRO/VOSTRO Account* –Nostro, from the perspective of the depositor bank, refers to the account that a bank (i.e., accountholder, respondent bank) maintains with another bank (correspondent bank) to facilitate financial transactions, such as treasury or trade finance related payments and remittances. Vostro, from the perspective of the depository bank, is the account that the bank (correspondent bank) holds or manages for another bank (respondent bank).
- h. *Counterparty Financial Institution* refers to the financial institution where the bank maintains a relationship and wherein a counterparty limit is established for transactions coursed through the bank's Treasury, Trust or other relevant units.
- i. *Nested or Downstream correspondent banking* refers to the use of a bank's correspondent relationship by a number of respondent banks through their relationships with the correspondent bank's direct respondent bank to conduct transactions and obtain access to other financial services³.
- j. *Payable-through-account* refers to a correspondent account that is used directly by third parties to transact business on their own behalf.¹
- k. *Shell Bank* refers to a shell company incorporated as a bank or made to appear to be incorporated as a bank but has no physical presence and no affiliation with

² Wolfsberg Guidance on SWIFT Relationship Management Application (RMA) Due Diligence

³ Basel Committee on Banking Supervision (BCBS) *Guidelines on Sound management of risks related to money laundering and financing of terrorism* issued June 2017

a regulated financial group. It can also be a bank that (a) does not conduct business at a fixed address in a jurisdiction in which the shell bank is authorized to engage; (b) does not employ one or more individuals on a full time basis at this fixed address; (c) does not maintain operating records at this address, and (d) is not subject to inspection by the authority that licensed it to conduct banking activities.⁴

IV. Nature of Correspondent Banking Relationships

Correspondent banking facilitates global payments and transactions. The transnational nature of financial transactions, driven by trade, payments, remittances, and other financial activities, necessitate correspondent banking relationships. Through correspondent banking relationships, financial institutions are able to access international financial services and provide a wide-range of banking services, including wire transfers, cash management services, check clearing, payments, trade services and trade finance, and foreign exchange services, to their customers around the world. These relationships consist of a bilateral arrangement and are generally reciprocal in nature, wherein each bank provides services to the other. It often requires the exchange of authenticated messages between financial institutions to settle transactions. In correspondent banking, the customer of the correspondent bank is the respondent bank.

Domestically, activities of geographically dispersed customers, the nature of financial institutions and their delivery channels, may also require correspondent banking services. The developments in financial market infrastructure and electronic or digital payments affect the demand for domestic correspondent banking.

Correspondent banking is characterized by the continuing or recurring nature of the relationship. Consequently, it does not include one-off transactions or the simple exchange of SWIFT RMA in the context of non-customer relationships.¹

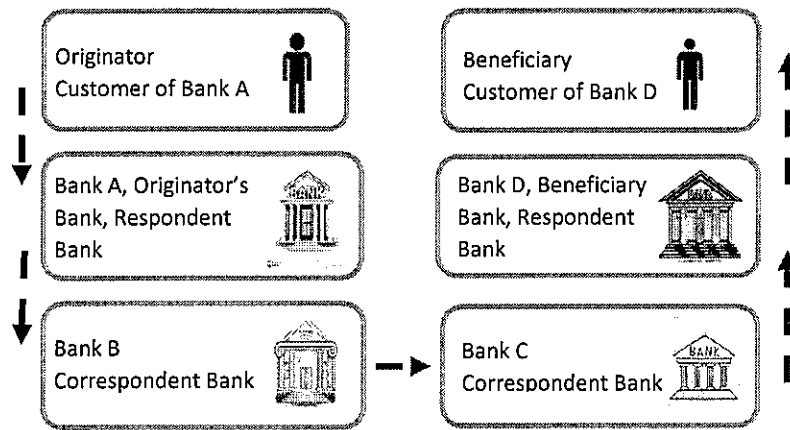
V. Forms of Correspondent Banking Services

Correspondent banking services can be traditional or non-traditional.

A. *Traditional correspondent banking* is established when a correspondent bank enters into an agreement with the respondent bank to execute payments on behalf of the respondent bank and its customers. The respondent bank's customers transact indirectly as they do not have direct access to the correspondent account. This is illustrated in Figure 1.

⁴ Section 904, Manual of Regulations for Banks

Figure 1

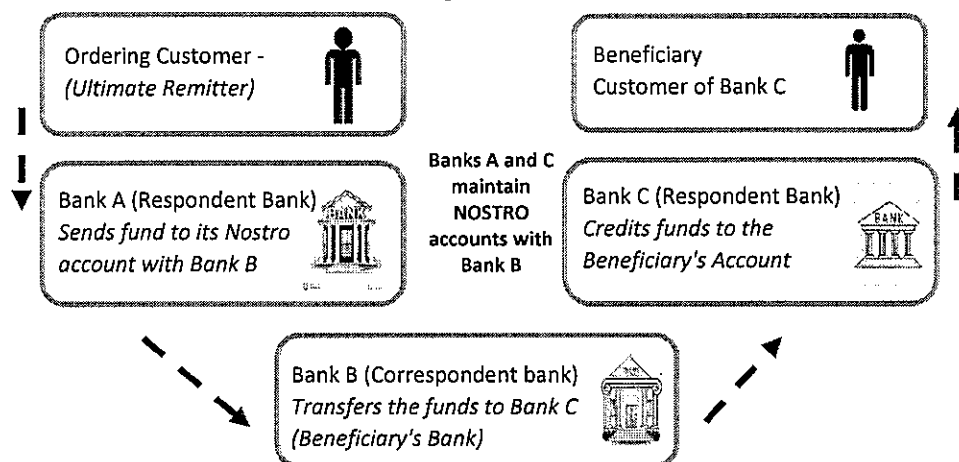


- (1) *Relationship Management Application (RMA)*. Correspondent banking usually involves the exchange of authenticated messages between parties to settle transactions. One such facility is the RMA which is used for sending and receiving SWIFT messages. RMAs can be established for both customers and non-customers.

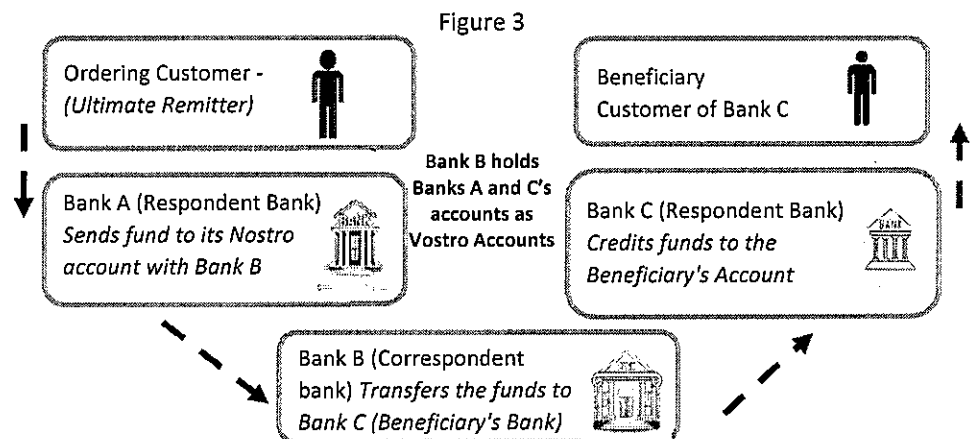
For this purpose, the interactions for non-customer RMA are limited to non-transactional messages, such as document exchanges, receipt of balance and transaction information on a customer's account at another bank (cash management), or exchange of messages with banks that have no direct payment relationship. The settlement of any transaction is decoupled from the document exchange and always made via a customer bank².

- (2) NOSTRO account is used to facilitate financial transactions of the respondent bank in another bank (correspondent bank), on its own or on behalf of the respondent bank's customers. This is treated as an asset account in the books of the respondent bank. Transactions processed may include cross-border treasury and/or trade finance related payments and remittances. This is illustrated in Figure 2:

Figure 2

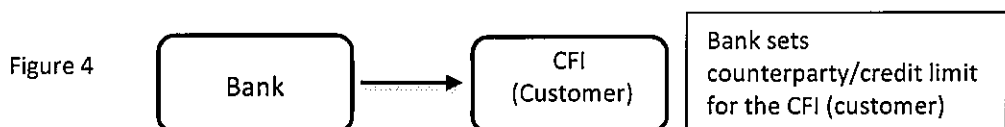


VOSTRO account is an account used for settlement of the transactions of a domestic/foreign counterpart (respondent bank). It is an arrangement under which one bank (correspondent bank) provides payment and other services to the local and/or foreign respondent banks. This is treated as a liability account in the perspective of the correspondent bank. This is illustrated in Figure 3:



(3) Counterparty Financial Institution (CFI)

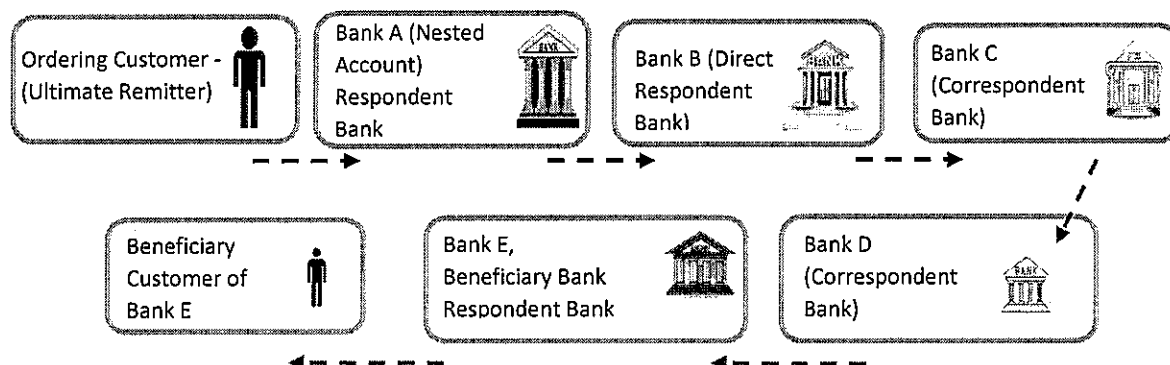
Banks may establish relationships with CFIs for the transactions of the various business units through its Treasury, Trust or other relevant units. This involves setting of counterparty limits or credit lines informed by credit risk and business needs assessment, as warranted. This is illustrated in Figure 4:



B. *Non-traditional correspondent banking* is established when a correspondent banking relationship is extended to the respondent bank's customers to obtain access to other financial services. This type of relationship takes the following forms:

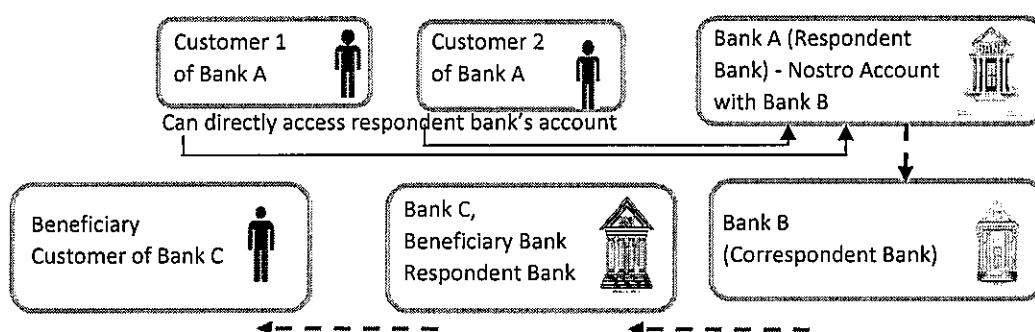
1. *Nested correspondent banking relationship* wherein the respondent banks conduct business through their relationships with the direct respondent bank to execute transactions and obtain access to other financial services. Nested or downstream correspondent banking relationships is a way for larger banks to help small local or domestic banks obtain access to the international financial system or to facilitate transactions where smaller banks do not have direct relationship with correspondent banks abroad. This is illustrated in Figure 5.

Figure 5



2. *Payable-through accounts* are similar to nested correspondent banking, but in this case, the respondent bank allows its intermediate customers to access the correspondent account directly to conduct business on their own behalf. This is illustrated in Figure 6.

Figure 6



VI. Requirements for Correspondent Banking Relationships

A. Risk Assessment of Correspondent Banking Relationship

In accordance with Part 9 of the Manual of Regulations for Banks (MORB), banks shall identify, understand and assess the ML/TF risks in correspondent banking relationships. Given the diverse nature of correspondent banking relationships, some correspondent banking activities may pose higher degree of risk than others. The results of the risk assessment will enable banks to establish bespoke risk mitigation measures to manage the identified ML/TF risks in its correspondent banking relationships and define appropriate due diligence procedures. Where the correspondent bank has identified higher risk correspondent banking relationship, it should apply enhanced measures that are in line with the risks associated to that relationship, such as closer interaction with the respondent bank.

Correspondent banks shall assess the risk posed by their respondent banks, and consider all relevant risk factors, including, but not limited to the following:

1. Nature of the service to be provided, such as:
 - (a) Type, purpose and intended nature of the correspondent account;
 - (b) Expected correspondent account activity;
 - (c) Manner of offering the correspondent banking services to customers of respondent bank, such as existence of nested accounts or use of payable through accounts which pose higher risk.
2. Profile of the respondent bank, such as:
 - (a) Management and ultimate beneficial owners of the respondent bank, including whether it is owned or controlled by an individual with public or high-profile position;
 - (b) Business model or significant activities, products/services offered;
 - (c) The customer segment or types of customers the respondent bank intends to service through the correspondent banking relationship;
 - (d) Quality of the respondent bank's AML/CFT controls, including regulatory status and history, criminal or adverse regulatory actions, based on publicly available materials; and
 - (e) Nature and duration of the respondent bank's relationship with the correspondent bank.
3. The respondent bank's operating environment, which includes:
 - (a) Respondent bank's and/or its Parent Bank's jurisdiction (such as whether it operates in a sanctioned country);
 - (b) Quality of AML/CFT regime and regulatory framework of the jurisdiction that issued license to the respondent bank; and
 - (c) Jurisdiction in which its subsidiaries and branches operate, as well as the location of third parties who use the correspondent banking relationships.

B. Due Diligence on Respondent Banks

Traditional Correspondent Banking

1. *Establishment of RMAs with NOSTRO/VOSTRO Accounts*

Banks shall develop risk-based policies and procedures in establishing RMAs and Nostro/Vostro accounts. In establishing customer RMAs, correspondent banks shall:

- (a) Identify and verify the identity of the respondent bank using reliable, independent source documents, data or information. This includes gathering sufficient information and performing due diligence checks about the respondent bank, including the ownership and management structure, to understand fully the nature of the respondent's business, and determine the reputation of the institution and the quality of supervision, including whether it has been subject to ML/TF investigation or regulatory action. Sources of information include the respondent bank, publicly available references, such as the FATF or FATF-style regional bodies mutual evaluation reports and statements on

countries having strategic AML/CFT deficiencies, or reliable third-party databases that contain relevant information on banks;

- (b) Assess the respondent bank's AML/CFT controls. These may include: (i) evaluating the respondent bank's responses to AML/CFT Questionnaire, such as the Wolfsberg Correspondent Banking Due Diligence Questionnaire; (ii) assessing the respondent bank's AML/CFT processes and systems; (iii) reviewing internal and external audit reports; (iv) interviewing compliance officers; and (v) conducting on-site visit to have an overview of the respondent bank's ML/TF risk management framework, as warranted. The correspondent bank shall assess the ML/TF risks associated with the relationship, and document results of such assessment;
- (c) Obtain approval from senior management when establishing new correspondent relationships; and
- (d) Clearly understand and document the respective AML/CFT responsibilities of each institution.

A correspondent bank may rely on the customer identification process undertaken by other banks (third party that may already have correspondent relationship with the respondent bank), provided that the rules on third party reliance are satisfied. The ultimate responsibility for customer due diligence (CDD) still remains with the correspondent bank.

2. Establishment of CFI Relationships

In establishing CFI Relationships, a correspondent bank shall conduct risk assessment and perform the applicable customer due diligence requirements as provided in the table below.

In case of NOSTRO/VOSTRO Accounts and CFI Relationships, the correspondent bank shall ensure the authority of the officer or person representing the respondent bank or counterparty. This may include requiring a Board resolution duly certified by the Corporate Secretary authorizing the signatory to sign on behalf of the entity, or other appropriate measures applicable for electronic platforms or messaging facility.

3. Establishment of Non-customer RMAs

Banks shall segregate RMA requests between customer and non-customer relationships and adopt risk-based due diligence policies for each. Where an RMA holder has a customer relationship, CDD requirements under this rule will apply. In case of non-customer RMAs, banks may apply a lower level of due diligence, as follows:

- a. Obtain name and address;
- b. Conduct sanctions screening against relevant sanctions list;
- c. Conduct a review against red flag lists which may include, but not limited to, prior unusual transaction/message history and negative media reports;

- d. Evaluate risks of the potential RMA based on the above information to identify whether a financial institution may require further review based on internal risk tolerance; and
- e. Obtain Management approval as defined in the bank's policy.

The table below summarizes the CDD requirements for different types of accounts and relationships. The role of the bank in the CBR and type of transactions that will pass through the account, among other factors, determine the level of due diligence.

CDD Requirement	RMAs		RMAs with Accounts		Counterparty Financial Institution*
	Customer	Non-customer	NOSTRO	VOSTRO	
Customer Information	✓	✓ **	✓ **	✓	✓
Identification Documents ⁵	✓			✓	✓
Identification of the Ultimate Beneficial Owner (UBO) (as defined under Section 904 of the MORB)	✓			✓	✓
Management Structure ⁶	✓			✓	✓
General Profile, information on the respondent's reputation, major business activities, customers, location, target markets and customer base	✓			✓	
Condition and quality of banking regulation and supervision (AML/CFT laws and regulation) in the respondent bank's country ⁷	✓			✓	
AML Questionnaire or equivalent document such as the Expanded Wolfsberg Questionnaire	✓			✓	✓
Risk Assessment with corresponding AML Risk Score/Rating	✓			✓	✓
Senior Management Approval	✓			✓	✓
Correspondent Banking Agreement or equivalent document	✓		✓	✓	✓
Sanction Screening	✓	✓	✓	✓	✓

* Banks may conduct credit due diligence in addition to the required due diligence for AML/CFT.

** Name and address of the counterparty FI

⁵ Proof of company registration, certificate of incorporation/memorandum of association, banking license or equivalent document

⁶ List of directors and senior officers (such as President, Treasurer).

⁷ Information may be gathered from FATF mutual evaluation reports and statements on jurisdictions identified by the FATF as either being subject to countermeasures or having strategic AML/CFT deficiencies

For this purpose, the customer information, except for non-customer RMA and NOSTRO account, includes those provided in Part 9 of the Manual of Regulations for Banks. The required specimen signature of authorized signatories need not be obtained for transactions executed through electronic trading platforms with embedded security controls to authenticate transactions.

Non-traditional Correspondent Banking

1. Nested Correspondent Banking Relationships

Correspondent banks, shall develop policies and procedures in identifying and assessing risks involving nested correspondent banking relationships (i.e. downstream banking). In addition to the due diligence on respondent banks, correspondent banks should understand the respondent bank's control framework and assess risks posed by the nested relationships. It should be informed of nested relationships and the operations and transactions of customers of the nested institutions. The locations in which the nested institutions conduct business should be transparent and understood by the correspondent bank. The payment instructions should include all involved parties for monitoring and screening purposes.

The correspondent bank should have measures in place to detect any undisclosed nested relationship. Appropriate follow-up actions should be taken when a respondent bank does not disclose nested relationships.

2. Payable-through accounts

"Payable-through accounts" pose high risk considering that control or access to account is shared with customers. In this respect, correspondent banks shall ensure the presence of a robust risk management system and satisfy themselves that the respondent bank:

- (a) Has performed customer due diligence obligations on its customers that have direct access to the accounts of the correspondent bank; and
- (b) Is able to provide relevant customer due diligence information upon request to the correspondent bank.

The correspondent bank shall apply enhanced controls to monitor transactions/activity that are commensurate to the identified risk, and policies to enable it to identify the ultimate user of the account. It should be satisfied that the respondent bank has necessary controls to identify and monitor the transactions of those customers with access to the account.

Prohibition on dealing with shell banks

Banks are prohibited from entering into, or continuing, correspondent banking relationships with shell banks and should have measures to satisfy themselves that respondent banks do not permit their accounts to be used by shell banks.

Correspondent Banking Relationships within the Group

Considering the risk posed by correspondent banking even when services are offered to the correspondent bank's branches, subsidiaries and affiliates, wherever they may be located, correspondent banks shall assess the risks posed by the respondent banks and undertake risk-based customer due diligence measures on correspondent banking relationships within financial groups.

In situations where the respondent banks belong to the same banking group, the correspondent bank should consider the parent or group controls, and also independently assess the ML/TF risks presented by each business relationship, considering relevant factors, such as the specific jurisdiction involved or customer types served by the respondent bank.

C. Ongoing Due Diligence

1. Ongoing Monitoring of Correspondent Banking Relationships

Correspondent banks shall conduct ongoing due diligence of the correspondent banking relationship which shall include periodic due diligence reviews and sanction screening of CDD information on the respondent bank, its owners, directors, senior management and authorized signatories, based on materiality and risk. Risk re-assessment of the respondent bank should be performed whenever reviews reveal relevant changes in CDD information.

2. Ongoing Transaction Monitoring

Depending on the risks associated with correspondent banking relationships, correspondent banks shall develop an appropriate transaction monitoring system that will enable them to understand the usual or expected activities of the respondent bank and detect any unusual or suspicious transaction pattern of activity that is inconsistent with purpose of services provided to the respondent banks. Detection scenarios and parameters specific to the correspondent banking activities should be set in the transaction monitoring systems.

Correspondent banks shall establish relevant red flag indicators based on its risk assessment and monitoring of the correspondent banking relationship, such as:

- a) Purpose of transaction (transactional details) is not commensurate with expected account behavior and /or nature of business of underlying customers;
- b) Missing information in the transactional details;
- c) Transactions pass through multiple jurisdictions without legitimate purpose;
- d) Structured transactions such as transactions which are executed in multiple payments to avoid detection;
- e) Unexplained changes in account activity levels and underlying customers;

- f) Detection of nesting activities for high risk financial institutions and /or for an institution with which the bank has previously terminated its relationship; and
- g) Omission of required payment information for fund/wire transfers and re-submission of previously rejected transfers.

Correspondent banks shall develop policies and procedures in handling any flagged unusual activity, such as conducting further review and requesting transaction information from the respondent bank to justify the identified transaction. Examples of request for information (RFI) may include the following:

- a) Purpose of the respondent bank's customer's transaction, including supporting documents, as warranted;
- b) Risk profile of the customer and duration of customer's relationship with the respondent bank;
- c) Source of fund, and consistency of the transaction with the declared financial profile of the respondent bank's customer;
- d) Beneficial owner of the respondent bank's customer; or
- e) Affiliation of customer with a third party.

Respondent banks, as part of the correspondent banking agreement or other equivalent document, must respond to the RFI in a timely manner and ensure that supporting documents/information about the transaction and/or customer is available. In this regard, a respondent bank must have procedures to obtain the consent of customers regarding disclosure of information to the correspondent bank. Failure of the respondent bank to respond to RFIs may raise a concern on the ability of the respondent bank to identify and know its customers and manage its risk. It may lead to filing of suspicious transaction report by the correspondent bank, followed by a reassessment of the correspondent banking relationship and respondent bank's risk profile. As part of regular review or reassessment of the relationship, the correspondent bank should take into consideration the respondent bank's past behavior on the relationship, particularly any unsuccessful RFI.

For cross-border correspondent banking services, banks should be able to monitor the funds flow to sanctioned entities and countries and conduct necessary due diligence procedures and measures.