

FEDERAL RESERVE BANK
OF NEW YORK

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STATEMENT OF PRINCIPLES ON MONEY LAUNDERING

*To the Chief Executive Officers of Each State Member Bank, Edge Corporation,
and Noninsured Branch or Agency of a Foreign Bank,
in the Second Federal Reserve District:*

The Committee on Banking Regulations and Supervisory Practices¹ was established by the central bank Governors of the Group of Ten industrialized countries in 1974. The committee's objective is to strengthen supervision over international banking activity among banks in the Group of Ten industrialized countries. The three Federal bank regulatory agencies are represented on the committee.

Members of the committee have long been concerned about the use of the banking system by criminal elements. Criminals can use the banking system to hide the true ownership of funds through nominees and to make payments and transfers of funds. These activities - when associated with monies derived from illegal activities - are commonly referred to as money laundering.

Each of the bank supervisory authorities represented on the committee has a different role and responsibility in suppressing money laundering. All member countries collectively believe that bank supervisors, regardless of their prescribed role, should ensure that ethical standards of professional conduct are being observed in the banking system. Members also believe that supervisors should encourage the implementation of effective policies and procedures to aid efforts to eliminate money laundering.

The members of the committee have developed and approved the enclosed Preamble and "Statement of Principles." In accordance with the principles set out, bank management is encouraged to establish policies and procedures to ensure: (i) proper identification of all persons conducting business with the institution; (ii) conduct of the bank's business in conformity with high ethical standards; (iii) cooperation with law enforcement authorities within the confines of applicable law; and (iv) proper staff training in all matters concerning that Statement of Principles. Bank management is encouraged to incorporate those principles into the existing procedures that are already required under the Monetary Control Act.

The enclosed materials are being released by all supervisory authorities represented on the committee.

¹This committee meets at the Bank for International Settlements in Basle, Switzerland, and includes representatives of the central banks and bank supervisory agencies from Belgium, Canada, France, Germany, Italy, Japan, Luxembourg, Netherlands, Sweden, Switzerland, the United Kingdom, and the United States.

E. GERALD CORRIGAN,
President.

Committee on Banking Regulations
and
Supervisory Practices

Prevention of criminal use of the banking system for the
purpose of money-laundering

Preamble

1. Banks and other financial institutions may be unwittingly used as intermediaries for the transfer or deposit of funds derived from criminal activity. Criminals and their associates use the financial system to make payments and transfers of funds from one account to another; to hide the source and beneficial ownership of money; and to provide storage for bank-notes through a safe-deposit facility. These activities are commonly referred to as money-laundering.

2. Efforts undertaken hitherto with the objective of preventing the banking system from being used in this way have largely been undertaken by judicial and regulatory agencies at national level. However, the increasing international dimension of organised criminal activity, notably in relation to the narcotics trade, has prompted collaborative initiatives at the international level. One of the earliest such initiatives was undertaken by the Committee of Ministers of the Council of Europe in June 1980. In its report¹ the Committee of Ministers concluded that "... the banking system can play a highly effective preventive role while the co-operation of the

1 Measures against the transfer and safeguarding of funds of criminal origin. Recommendation No. R(80)10 adopted by the Committee of Ministers of the Council of Europe on 27th June 1980.

banks also assists in the repression of such criminal acts by the judicial authorities and the police". In recent years the issue of how to prevent criminals laundering the proceeds of crime through the financial system has attracted increasing attention from legislative authorities, law enforcement agencies and banking supervisors in a number of countries.

3. The various national banking supervisory authorities represented on the Basle Committee on Banking Regulations and Supervisory Practices² do not have the same roles and responsibilities in relation to the suppression of money-laundering. In some countries supervisors have a specific responsibility in this field; in others they may have no direct responsibility. This reflects the role of banking supervision, the primary function of which is to maintain the overall financial stability and soundness of banks rather than to ensure that individual transactions conducted by bank customers are legitimate. Nevertheless, despite the limits in some countries on their specific responsibility, all members of the Committee firmly believe that supervisors cannot be indifferent to the use made of banks by criminals.

4. Public confidence in banks, and hence their stability, can be undermined by adverse publicity as a result of inadvertent association by banks with criminals. In addition, banks may lay themselves open to direct losses from fraud, either through negligence in screening undesirable customers or where the integrity of their own officers has been undermined through association with criminals. For these reasons the members of the Basle Committee consider that banking supervisors have a general role to encourage ethical standards of professional conduct among banks and other financial institutions.

5. The Committee believes that one way to promote this objective, consistent with differences in national supervisory practice, is to obtain international agreement to a Statement of Principles to which financial institutions should be expected to adhere.

2 The Committee comprises representatives of the central banks and supervisory authorities of the Group of Ten countries (Belgium, Canada, France, Germany, Italy, Japan, Netherlands, Sweden, Switzerland, United Kingdom, United States) and Luxembourg.

6. The attached Statement is a general statement of ethical principles which encourages banks' management to put in place effective procedures to ensure that all persons conducting business with their institutions are properly identified; that transactions that do not appear legitimate are discouraged; and that co-operation with law enforcement agencies is achieved. The Statement is not a legal document and its implementation will depend on national practice and law. In particular, it should be noted that in some countries banks may be subject to additional more stringent legal regulations in this field and the Statement is not intended to replace or diminish those requirements. Whatever the legal position in different countries, the Committee considers that the first and most important safeguard against money-laundering is the integrity of banks' own managements and their vigilant determination to prevent their institutions becoming associated with criminals or being used as a channel for money-laundering. The Statement is intended to reinforce those standards of conduct.

7. The supervisory authorities represented on the Committee support the principles set out in the Statement. To the extent that these matters fall within the competence of supervisory authorities in different member countries, the authorities will recommend and encourage all banks to adopt policies and practices consistent with the Statement. With a view to its acceptance worldwide, the Committee would also commend the Statement to supervisory authorities in other countries.

Basle, December 1988

Statement of Principles

I. Purpose

Banks and other financial institutions may unwittingly be used as intermediaries for the transfer or deposit of money derived from criminal activity. The intention behind such transactions is often to hide the beneficial ownership of funds. The use of the financial system in this way is of direct concern to police and other law enforcement agencies; it is also a matter of concern to banking supervisors and banks' managements, since public confidence in banks may be undermined through their association with criminals.

This Statement of Principles is intended to outline some basic policies and procedures that banks' managements should ensure are in place within their institutions with a view to assisting in the suppression of money-laundering through the banking system, national and international. The Statement thus sets out to reinforce existing best practices among banks and, specifically, to encourage vigilance against criminal use of the payments system, implementation by banks of effective preventive safeguards, and co-operation with law enforcement agencies.

II. Customer identification

With a view to ensuring that the financial system is not used as a channel for criminal funds, banks should make reasonable efforts to determine the true identity of all customers requesting the institution's services. Particular care should be taken to identify the ownership of all accounts and those using safe-custody facilities. All banks should institute effective procedures for obtaining identification from new customers. It should be an explicit policy that significant business transactions will not be conducted with customers who fail to provide evidence of their identity.

III. Compliance with laws

Banks' management should ensure that business is conducted in conformity with high ethical standards and that laws and regulations

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pertaining to financial transactions are adhered to. As regards transactions executed on behalf of customers, it is accepted that banks may have no means of knowing whether the transaction stems from or forms part of criminal activity. Similarly, in an international context it may be difficult to ensure that cross-border transactions on behalf of customers are in compliance with the regulations of another country. Nevertheless, banks should not set out to offer services or provide active assistance in transactions which they have good reason to suppose are associated with money-laundering activities.

IV. Co-operation with law enforcement authorities

Banks should co-operate fully with national law enforcement authorities to the extent permitted by specific local regulations relating to customer confidentiality. Care should be taken to avoid providing support or assistance to customers seeking to deceive law enforcement agencies through the provision of altered, incomplete or misleading information. Where banks become aware of facts which lead to the reasonable presumption that money held on deposit derives from criminal activity or that transactions entered into are themselves criminal in purpose, appropriate measures, consistent with the law, should be taken, for example, to deny assistance, sever relations with the customer and close or freeze accounts.

V. Adherence to the Statement

All banks should formally adopt policies consistent with the principles set out in this Statement and should ensure that all members of their staff concerned, wherever located, are informed of the bank's policy in this regard. Attention should be given to staff training in matters covered by the Statement. To promote adherence to these principles, banks should implement specific procedures for customer identification and for retaining internal records of transactions. Arrangements for internal audit may need to be extended in order to establish an effective means testing for general compliance with the Statement.