Bank Account Closures:

Current Trends and Implications for Family Remittances

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This memo provides input on a current problem affecting family remittances: the bank account closures of money transfer companies. The memo analyzes the trends and presents some of the consequences and implications as identified in the research. It concludes by discussing solutions and recommendations suggested by industry experts.

The memo draws from multiple sources, including previous research,[1] interviews with remittance experts and members of the Remittance Industry Observatory,[2] and media[3] and data analysis in order to offer a fresh look at a persistent issue in the industry.

CHALLENGES IN MONEY TRANSFER OPERATIONS: BANK ACCOUNT CLOSURES

Since the early 2000s, the bank accounts of remittance service providers (RSPs)[4] have been subject to significant regulatory scrutiny from a wide range of public agencies and banking institutions. As a consequence, these accounts, which serve as vehicles for third-party cash transfers, are often identified and suspected for financial threats such as money laundering. Within the context of remittance transfer intermediation, RSPs need access to bank accounts in order to perform essential back-end operations.[5] Holding a bank account allows an RSP to receive deposits from its agents as well as to deposit funds for payers.

Regulators expect robust risk management mechanisms from RSPs, including various reporting obligations of suspicious activities, in order to safeguard their activities and maintain bank accounts. However, RSPs and their agents have been subject to an increased and somewhat systematic practice of account closures on the assumption of risk and as a measure of risk prevention.

The practice of closing accounts is occurring in the United States, but is not limited to the US context. Remittance-related account closures are most visible in migrant host countries, and have been reported as an important issue in Canada, Australia, and the United Kingdom. A recent study by The World Bank Group surveyed 13 governments, 25 banks and 82 money transfer operators (MTOs) in countries around the world. Among its findings, 46% of MTOs have received notifications from their banks regarding the upcoming closures of their accounts. Of the 25 banks, 5 indicated they do not offer services to MTOs, and 15 indicated they do not open accounts for agents of MTOs.[6]

On the recipient side, according to interviews carried out for this memo, banks are also feeling pressure from their international correspondent banks to close agent accounts. For local banks, their

[1] See, for example, Manuel Orozco, "Family Remittances and Business Intermediation: The Challenge of Account Closures," Inter-American Dialogue, 2013.
[2] RIO is an Inter-American Dialogue initiative involving more than a dozen remittance service providers, including banks and MTOs, that promotes collaborative research and engagement with the remittance industry. For more information, see http://www.thedialogue.org/remittance-industry-observatory/
[3] The Inter-American Dialogue analyzed and classified over 300 news stories about account closures from 36 countries around the world. News stories were identified using the term "Bank account closures" on google news, and covered the period January, 2004 – September, 2015.
[4] A remittance service provider is a business that provides cross-border money transfers. For the purposes of this memo, we will focus on one type, the money transfer operator (MTO), which is a non-banking financial institution. These MTOs conduct the large majority or over 80% of US-outbound flows to the world. See Manuel Orozco with Mariellen Jewers, "Economic Status and Remittance Behavior among Latin American and Caribbean Migrants in the Post-Recession Period," Multilateral Investment Fund, Inter-American Development Bank Group, 2014. Available at http://goo.gl/G9j8E9
[5] For a description of a typical money transfer operation see Orozco, 2013.
[6] World Bank, *Report on the G20 survey in de-risking activities in the remittance market,* 2015. Available at http://goo.gl/tRTSP1

correspondent bank relationships with US and international banks are key to their business, and they are hesitant to jeopardize them even for customers with whom they have long-standing relationships.

THE TIMELINE FOR ACCOUNT CLOSURES

Interviews with various money transfer operators show that account closures escalated shortly after the US Patriot Act was enacted. Research by the Inter-American Dialogue had documented many cases of MTO account closures as early as 2005. At that time, 10 RSPs reported a total of 68 account closures, though in only five instances was a concrete reason, such as risk, explicitly provided. In all other cases the explanation was diffuse and broad, reflecting the discretionary right of a bank to discontinue the account.

Interviews in 2013 and 2015 show a similar trend, though with more widespread account closures. Obtaining new accounts has also become a more difficult process. Interviews with members of the Remittance Industry Observatory show that this trend of account closures may date as far back as the early 90s but increased after the Patriot Act came into force. Most recently, account closures have begun to affect payout partners, as the table below shows.

Table 1: Time Frame for Account Closures

ESTIMATED YEAR THEY BEGAN TO FACE ACCOUNT CLOSURES….	TIME FRAME
As MTOs	1990's to 2007
For MSB[7] partners	1990's to 2010
For Payout Partners	2000 to 2013

Source: Interviews with RIO members, 2015.

QUANTIFYING THE PROBLEM IN 2015

The number of banking[8] relationships an MTO has varies according to its business model. Regardless of size, companies that use agents tend to need more banking relationships in order to cover a greater geographical area. If access to nationwide banks becomes restricted, the need for more local or regional banking relationships may become greater.

Four out of ten remittance companies interviewed said they have had account closures ranging from 1 to 5 accounts per year. Typically, companies with account closures would see two banking relationships lost per year. When asked if they knew whether their agents had also been affected by closures, representatives reported up to 6 agents going out of the remittance business due to account closures in a single year.

[7] MSBs are money service businesses, which include remittance agents. For more information about types of money service businesses, see https://goo.gl/lqTqIL

[8] We include account-based relationships with credit unions.

Table 2: Accounts and Account Closures in 2015

ACCOUNTS AND ACCOUNT CLOSURES IN 2015		RANGE OF RESPONSES	AVERAGE
Accounts Held	Average banking relationships of MTOs	2 to 6	3.75
	Estimated number of accounts their MSB partners hold	1 to 3	—
	Estimated number of accounts their paying agents' partners hold	1 to 3 in the US; At least 1 per receiving country	—
Accounts Closed	Accounts closed in a given year for MTO	1 to 5	0.83
	Estimated accounts closed in a given year for MSB partners	1 to 6	—
	Estimated accounts closed in a given year for paying agents' partners	2 to 4	—

Source: Interviews with RIO members, showing those that answered each question if it applied to them.[9]

While account closures reduce the number of existing banking relationships, establishing new ones has become more difficult. MTOs mentioned that in a given year they have submitted up to 12 new account applications with no success. Two companies shared that negotiations to open a new account with a single entity took around one and a half years.

Table 3: Opening New Accounts, 2015

NEW ACCOUNTS AND ACCOUNT APPLICATIONS	TOTAL
MTOs that have attempted opening new accounts in the past year	5, or 50% of total
Attempts by MTOs to open accounts – total accounts	21, or 4.1 per company
Successful attempts for those MTOs that have tried to open accounts – companies	2, or 40% of companies that attempted
Successful attempts for those MTOs that have tried to open accounts – total accounts	3, or 14% of attempted accounts

Source: Interviews with RIO members, showing those that answered each question if it applied to them.[10]

CONSEQUENCES OF ACCOUNT CLOSURES

There are multiple consequences of account closures that affect customers, companies, and countries around the world. The effects of closures include increased operating costs, reputational risks, and dysfunctional intermediation as well as barriers to entry, innovation, expansion and competition.

[9] Companies that only generate transactions online were not considered since they do not have physical, brick-and-mortar agencies in the United States. Moreover, their transfers are account-based as opposed to cash-based, which is generally considered to be lower risk.
[10] For example, companies that only generate transactions online where not considered for averaging MSBs account closures.

IMPACT ON COMPANIES: INCREASED OPERATING COSTS

One key consequence has been increased operating costs for MTOs, including increased banking service fees. From our interviews with remittance companies, 50% reported increases in banking fees over the past two years. One company representative noted that "banking costs have more than doubled in the past 5-7 years" for their company. Another company reported paying as much as 70 cents in banking fees for a transaction of approximately US$300. Consider that although a typical MTO's revenue per transaction is US$10, with about $4.50 for commissions to originating and paying agents, the remaining $5 must cover all other operating expenses (such as regulatory compliance, marketing, management, and customer service).[11]

Rising banking fees come in addition to increased in-house expenditures on compliance, which was reported among almost all companies. Investor reports from several publically-traded companies shed light on the extent of these expenditures. A 2014 Western Union quarterly report noted that "the decline (in the GAAP operating margin) from prior year is primarily due to increases in C2C retail commission rates and higher compliance expenses."[12] Likewise, MoneyGram has had to invest significant amounts of its revenue in compliance and risk management. According to a recent investor report, the company invested "$11.8 million as part of our compliance enhancement program, comprised of $7.4 million in operating expense and capital expenditures of $4.4 million. Total cash outlay projections for the compliance enhancement program remain unchanged at $80 to $90 million over the next three years."[13]

In addition, all company representatives interviewed also shared experiences of more frequent and thorough audits, with all the costs that these imply.

Companies reported that it was important to them to avoid passing increased operating costs on to consumers. Instead, they have looked for other cost-cutting measures. In some cases, companies have outsourced their support services to other countries, where the costs of labor and operations are cheaper. In other cases, they have re-evaluated their geographical coverage, deciding to maintain only the most productive agencies or corridors.

Companies have managed to shelter consumers from these rising costs, at least for the moment. As the table below shows, pricing has not increased despite these costs.

Table 4: Costs of Sending US$200 to Select Latin American and Caribbean Countries (%)

	2001	2010	2011	2012	2013	2014	2015
Colombia	10.1	5.8	5.82	5.8	5.3	5.30	5.60
Dominican Rep.	9.4	5.7	5.68	6	5	5.50	6.00
Ecuador	-	3.8	3.9	3.9	4	3.90	3.80
El Salvador	6.7	4.5	4.67	4.7	4.6	4.40	4.30
Guatemala	7.4	5	5.52	6.01	5.6	4.60	4.70
Haiti	9	6.4	4.95	4.9	5.8	-	5.70
Honduras	-	4.3	7.09	5.65	5.5	-	4.70
Jamaica	9.8	6.4	6.52	6.03	7	7.90	8.30
Mexico	8.8	6.2	6	5.71	5.5	4.50	4.90

Source: Inter-American Dialogue and World Bank.

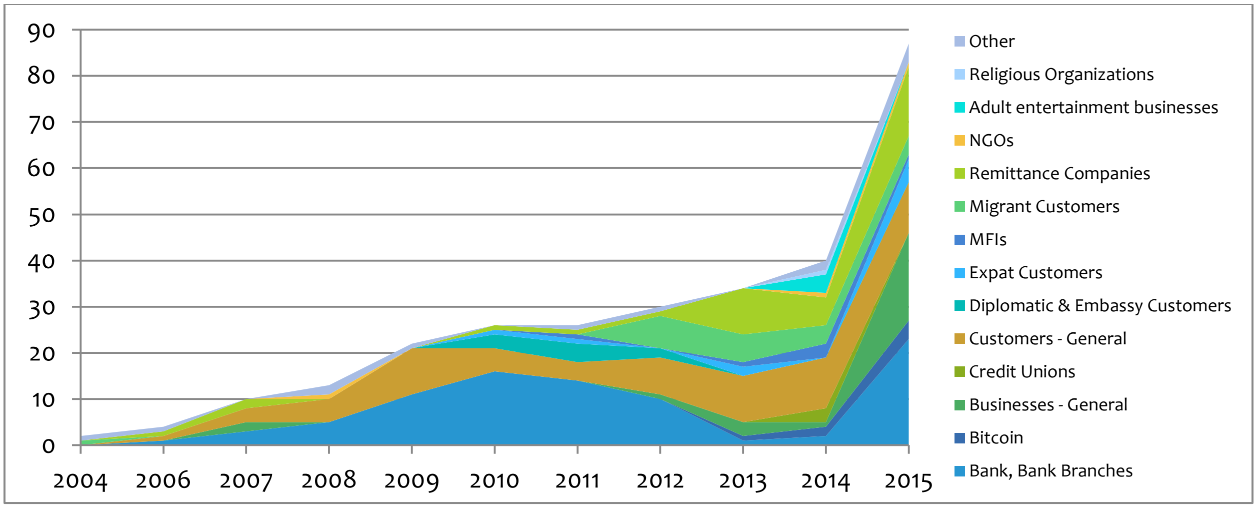
[11] It is important to consider the fact that MTOs are typically small, minority-owned businesses with annual revenues below US$50 million (most MTOs carry out 400,000 transfers per month). After commissions and operating costs, which take more than 70% of the revenue, profit margins are small.
[12] Western Union Q1, 2014 report.
[13] MoneyGram International Reports Second Quarter 2014 Financial Results.

IMPACTS ON COMPANIES: REPUTATIONAL IMPACTS

Account closures also have reputational impacts for the institutions involved. An analysis of over 300 news articles on account closures helps to shed more light on these issues. Media coverage of account closures is not particularly widespread or frequent, but it has provided some coverage of the issue, particularly in the United States, Canada and several European countries.

As the graphic below shows, the media has covered account closures related to a wide variety of people and institutions. Media reports cover the impacts of account closures on migrant customers, including migrants of Middle Eastern descent who experienced bank account closures in the United States and Canada. MSBs, embassies, and other types of businesses are also covered in the news reports, as the graphic below indicates.

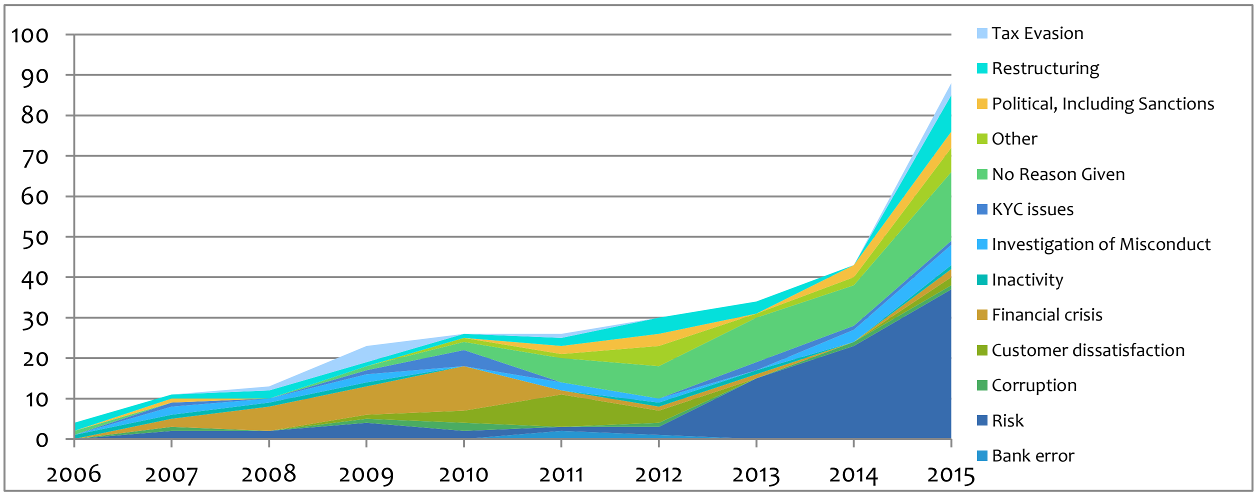
Graphic 1: Media Coverage of Account Closures, Types of Institutions Undergoing Closures



Source: Inter-American Dialogue, 2015.

Media coverage has focused on risk as a primary reason for account closures, as the graphic below shows.

Graphic 2: Total Reporting on Account Closings, by Reason Reported in Media



Source: Inter-American Dialogue, 2015.

While banks are in many cases the institution that is closing the account, the phenomenon is widespread, and goes well beyond any specific bank. The 5 banks most frequently named as closing accounts, for example, amount to only 23% of all account closures reported in the media.

Table 5: Bank De-Risking, Banks as % of Media Coverage

BANK	% MEDIA COVERAGE
HSBC	10.0%
Barclays	6.0%
JP Morgan Chase	4.3%
Westpac (Australia)	2.0%
Banamex	1.0%

Source: Inter-American Dialogue, 2015.

IMPACTS ON COMPANIES: LIMITING ABILITY TO INNOVATE AND GROW

With restricted access to banking services and slim profit margins, companies have also been limited in their ability to expand and grow. In some cases, while migrant communities are spreading out geographically,[14] companies have had to restrict their geographic presence as a result of reduced access to banking services in a certain state. In interviews, 30% of companies working in the US outbound flows to Latin America and the Caribbean reported that account closures were narrowing their geographic coverage. One company representative reported that when they receive an application for a new agent, the first thing they check is whether or not they have banking access close enough to the agent to make that relationship feasible.

Each company is affected differently. For example, for internet-based transfer companies, the challenge may be more about restrictions in innovation. Several of the internet-based remittance companies report that while they have not experienced account closures, they see that the regulatory environment presents a "barrier to innovation." That is to say, the current environment is so focused on risks that new products and ideas will face unusual and burdensome scrutiny, regardless of their actual risk level.

IMPACTS ON CONSUMERS

Bank account closures and denials also affect consumers and the services available to them. With restricted access to banking services, companies are less likely to be able to expand geographically, leading to reduced competition in some corridors. As a result, consumers may face fewer sending options, as well as higher costs over the medium to long-term. Customers also face a delay in accessing some of the most cutting-edge technologies as companies flounder through lengthy bank applications and regulatory processes.

Remittance senders and recipients may also experience frustrating limitations in the amounts they can send. For example, a person that needs to send $600 to their mother may face a $500 payout cap. According to interviews with RIO members, customers will sometimes send two transactions to two different people (say, the original recipient plus one additional family member) to ensure that the $600 arrives. To the customer, this activity means that the transaction has become more expensive and complex. To the recipient, it means that the funds do not arrive directly in their hands, and are therefore less secure. Overall, the activity becomes less transparent.

In extreme cases, such as Somalia, customers may face interruptions in service, meaning that they are unable to support their families abroad for certain periods of time.

[14] See, for example, Pew Research Center, "US Hispanic Population by County, 1980-2011," August 29, 2013. Available at http://goo.gl/LoFxkA

IMPACTS ON MARKETS: DYSFUNCTIONAL OPERATIONS

Account closures also disrupt the smooth functioning of operations. Although companies have responded to bank account closures by looking for creative solutions, this sometimes amounts to "banking gymnastics." For example, sometimes companies are settling accounts wherever it is easiest, even in third-party countries (that is, neither the country of origination nor the country of destination of the funds). In some cases, companies will pay for armored vehicles to transport cash across state lines to their nearest bank account. In other cases, companies have agents deposit the physical money into company accounts directly, since agents do not have access to bank accounts themselves.

The case of remittances from the Cayman Islands to Jamaica is one example of this type of dysfunction. When Fidelity Bank and Cayman National Bank (CNB) stopped offering banking services to remittance companies, remittance companies were forced to think very creatively. In order to minimize the disruption to consumers, companies limited their sending currency to United States dollars. They then bundled the dollars into small airplanes and deposited them directly in banks in the United States.[15] Outbound remittances from the Cayman Islands are estimated at well over 100 million dollars annually, or nearly US$2 million each week.[16] The prospect of moving this volume of cash via small planes is inefficient and insecure, to say the very least.

Although legal, these practices make transactions more expensive and less efficient, as fees have to be paid for each movement. In some cases, these practices also make the movements of money less transparent and more difficult for regulators to track, though this is certainly not the intention.

IMPACTS: A GLOBAL PERSPECTIVE

For some countries, like Somalia, bank account closures have halted the flow of remittances for significant periods of time, with troubling humanitarian implications. Somalia receives an estimated US$1.3 billion in remittances each year, which amounts to a very sizable portion of its GDP. Remittances are a lifeline for many Somalis, providing them with a means to meet their immediate needs for food, shelter, clothing, and other basic necessities as well as the ability to open and sustain small businesses, send children to school, and invest in their communities.[17] Bank account closures have resulted in the halt of formal remittance services to Somalia from the United States and the United Kingdom, with serious humanitarian implications. The Somali case shows just how essential bank accounts are to the smooth, reliable and secure transfer of remittances at a national level.

In the Caribbean, bank account closures have also disrupted the flow of remittances at a regional level. "The sudden closure of money-transfer services in the Cayman Islands threatens to render thousands of people here, and thousands more of their family members across the world, in immediate and intractable financial straits," a local newspaper reported in July of 2015.[18] In addition to its very significant human impact, the disruptions may have caused reputational damage to a country whose "status as an international financial center is predicated upon the mobility and fungibility of currency."[19]

Inter-American Dialogue research shows that bank account closures affect numerous institutions and countries around the world, from community financial institutions (SOFOMES) in Mexico to Iranian-Canadian customers

[15] "Remittances: Have Cash, Will Travel," Cayman Compass, September 23, 2015. Available at: http://goo.gl/YASey0
[16] According to the World Bank's Bilateral Remittance Matrix, outbound remittance flows from Cayman Island amount to US$84 million in 2014. The Cayman Islands Monetary Authority reports a larger amount, which probably comes down to methodological differences. The Monetary Authority reports US$107 million in remittance outflows under CI$500 for 2014. They also report $73 million in outflows larger than CI$500 for 2014. For more information, see http://goo.gl/eslXLT
[17] Manuel Orozco and Julia Yansura, "Keeping the Lifeline Open: Remittances and Markets in Somalia," Oxfam America, 2013. Available at http://goo.gl/FDE6AG
[18] "Cayman's Remit: End of Money Transfers Impacts Thousands," Cayman Compass, July 23, 2015. Available at http://goo.gl/rSSGbA
[19] "Cayman's Remit: End of Money Transfers Impacts Thousands," Cayman Compass, July 23, 2015. Available at http://goo.gl/rSSGbA

in Canada, from foreign embassies in the United States to Bitcoin exchanges worldwide. The map below shows every country that account closures affect, according to media reports from the past 10 years.

Graphic 3: Account Closures Globally, Media Reports

Source: Inter-American Dialogue, 2015.

LOOKING FOR SOLUTIONS

The problem of account closures has generated a large discussion regarding the practice known as de-risking.[20] Terminology aside, what matters is identifying viable solutions to this issue.

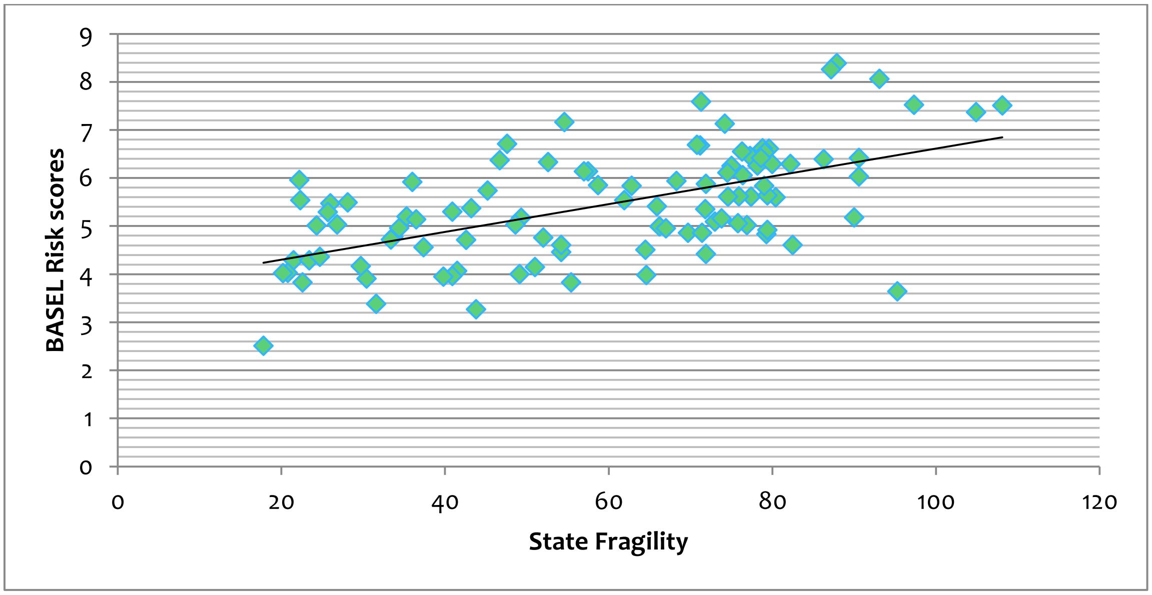
Overall, remittance transfer operators are considered able to manage risk with their existing prevention mechanisms and are in line with US government regulations.[21] In fact, while there is a strong correlation

[20] De-risking is generally defined as “the phenomenon of financial institutions terminating or restricting business relationships with clients or categories of clients to avoid, rather than manage, risk in line with the FATF’s risk-based approach.” Currently, the FATF recommends to “require financial institutions to terminate customer relationships, on a case-by-case basis, where the money laundering and terrorist financing risks *cannot be mitigated*.” http://goo.gl/UdY49t

[21] See for example, p.53, *National Terrorist Financing Risk Assessment 2015*. US Department of Treasury.

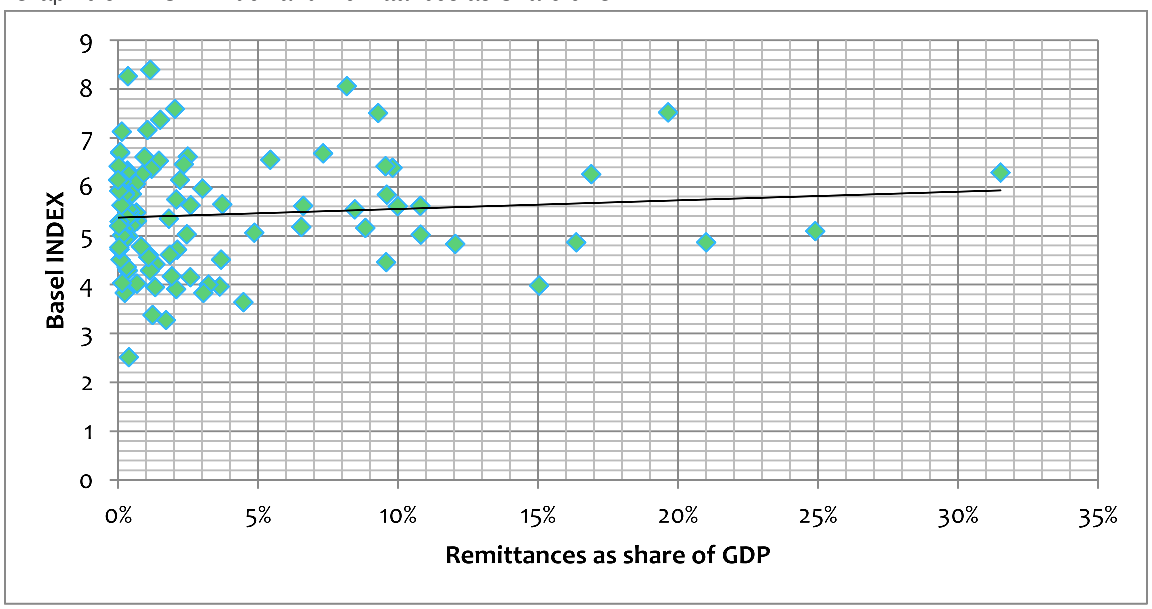
between AML risk[22] and fragile states,[23] the same is not the case with AML risk and remittance recipient countries.

Graphic 4: BASEL Risk Scores and State Fragility



Source: Data compiled by the author based on various sources, including the Index on State Fragility, the World Bank data on remittances and the Basel AML risk index.

Graphic 5: BASEL Index and Remittances as Share of GDP



Source: Data compiled by the author based on various sources, including the Index on State Fragility, the World Bank data on remittances and the Basel AML risk index.

Despite this evidence, concerns over MTO supervision persist. According to a 2015 World Bank report, only 13 out of 25 banks surveyed (52%) believe that the remittance sector is adequately supervised.

[22] As measured through the Basel AML Index, an annual ranking assessing country risk regarding money laundering/terrorism financing. It focuses on anti-money laundering and counter terrorist financing (AML/CTF) frameworks and other related factors such as financial/public transparency and judicial strength. For more, see https://index.baselgovernance.org/
[23] As measured by the Fragile States Index of the Fund for Peace. For more, see http://library.fundforpeace.org/fsi

Table 6: Opinions on MTO Supervision and Guidance[24]

	GOVERNMENTS	BANKS	MTOS
Differing perspectives on MTO supervision			
Remittance business sector is adequately supervised	11/13 (84%)	13/25 (52%)	72/82 (87%)
Banks can rely on adequate supervision to inform their risk-based decisions on opening/maintaining accounts for MTOs	11/13 (84%)	12/25 (48%)	74/82 (90%)
Differing perspectives on regulatory guidance			
Guidance has been issued to the MTO sector	11/13 (84%)	__	75/82 (91%)
Guidance has been issued to banks on the provision of accounts and services to MTOs	6/13 (46%)	13/25 (52%)	__
Guidance was helpful	__	6/13 (46%)	68/75 (90%)

Source: The World Bank Group, 2015.

The US government has recognized the seriousness of account closures and has stressed at least three strategies to tackle it. First, improve the "understanding of the scope, nature, and drivers of the problem through better data collection." Second, "explore the scope for FATF and financial supervisors to further clarify regulatory expectations regarding AML/CFT, while at the same time working to promote and help build the capacity for more consistent compliance with AML/CFT regulations in all economies, large and small." Third, "facilitate effective communication among stakeholders across borders. This includes sharing AML/CFT information through a number of channels, including supervisor-to-supervisor, bank-to-bank, and supervisor-to-bank, in both directions."[25]

Along these lines, money transfer industry experts have suggested some steps in the direction presented by the US Treasury. Among these are the following tentative solutions that can help deal with risk mitigation and the systematic effort to reduce account closures. Specifically, it may be important to establish better confidence-building metrics and initiatives among money transfer companies, banks and regulators. These include

- ❖ Improving knowledge and communication of the cross-border money transfer business among banks and regulators by improving the content of regular reporting systems.
- ❖ Improving transparency by creating money transfer screening boards composed of money transfer companies, banks, and regulators from the US Treasury Department. These boards could consist of a shared data clearinghouse that would aggregate and analyze all transactions originating from all MTOs and agents, thereby helping regulators and MTOs identify patterns of risk.

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[24] *Report on the G20 Survey on De-risking*, International Bank for Reconstruction and Development of the World Bank Group, October 2015. It is important to note out of the 13 banks, nine are net senders of remittances and 4 are net receivers. Regarding banks, only Mexico (6 banks) was represented from Latin America or the Caribbean. The most represented banks where those of the US (8 banks).

[25] Remarks by Under Secretary Nathan Sheets at the Center for Global Development, US Treasury Department Office of Public Affairs, November 12, 2015.

- Improving the process and problem resolution when accounts are in danger of being closed ("rebuttable presumption").
- Better clarifying, defining, and measuring risk as it relates to the source of the financial activity, rather than the financial entity.