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THE FIRST LINE OF DEFENSE: THE ROLE OF FINANCIAL INSTITUTIONS IN DETECTING FINANCIAL CRIMES

HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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THE FIRST LINE OF DEFENSE: THE ROLE OF FINANCIAL INSTITUTIONS IN DETECTING FINANCIAL CRIMES

Thursday, May 26, 2005

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 9:40 a.m., in Room 2128, Rayburn House Office Building, Hon. Sue W. Kelly [chairwoman of the subcommittee] presiding.

Present: Representatives Kelly, Paul, Royce, Kennedy, McHenry, Gutierrez, Moore, Maloney, Davis of Alabama, Cleaver, and Scott.

Also present: Representative Crowley.

Chairwoman KELLY. The committee will come to order. Today the committee is going to hold a hearing on The First Line of Defense: The Role of Financial Institutions in Detecting Financial Crimes.

The Bank Secrecy Act requires financial institutions across the United States to know their customers and to keep track of large cash transactions and suspicious activity. FinCEN is statutorily responsible for administering the BSA. Through FinCEN, power is delegated to eight different agencies for examining financial institutions and determining their compliance with the law.

Through this system, Suspicious Activities Reports (SARs) and Currency Transaction Reports (CTRS), are collected by FinCEN for analysis and distribution to law enforcement and intelligence units. Unfortunately, the utility and relevance of these reports has come to be doubted by many in the financial services industry, and in Congress. FinCEN is still seen by many as a library of data rather than an active part of our Nation's defense as our finance intelligence unit and analysis center.

These views need to change. This skepticism about the utility of the BSA process has been reinforced by the pendulum swing responses to failures in the BSA system this subcommittee has examined in the past. There is a widely held view that frontline regulators now take an unreasonable, overly aggressive approach with institutions that they are examining.

Financial institutions feel pressure from examiners to increase their filing of SARs, and many view this pressure as creating new burdens for institutions without any real sense of the utility of the information being provided to the government. Institutions have

felt pressure to drop MSBs as clients, financial institutions, feel they have lost their ability to exercise the discretion granted to them in the law by using their best judgment in identifying potentially suspicious transaction.

The compilation of these concerns has led many to believe that there must be a pushback on the regulators so that they will ease up. There are valid, critical, important points about undue burdens and about the dearth of feedback from the government that must be addressed promptly. But our focus must not dwell simply on the short term, on how we might best pull back the ratings on the regulators compensating for failures of the past.

We need to look more broadly at the system we have in place for ensuring the BSA compliance. We should not focus exclusively on what may be an overreaction to failures of the past, but also on how those failures of the past came to be. Informed by these facts, we can move forward toward a better clarity in the future.

Our focus should be on achieving a system that is effective in preventing crime and generating useful intelligence without placing unnecessary costly burdens on financial institutions and their customers. It is a difficult balance to strike, but we must continue working toward this ideal.

I hope this hearing today will help illuminate the government's efforts in creating a more effective and coherent regime. In this hearing we will hear from Director Fox and Agent Morehart about the utility of data collected under the BSA and improvements within the examination and data collection system. That will ease the burden on financial institutions.

On the second panel, we will hear from New York State Banking Superintendent Diana Taylor about the recent MOU between her agency and FinCEN on the impact of the current system on New York banks.

We will also hear from representatives of the American Banking Association, Western Union, the American Financial Service Centers Association, about their perspectives on the BSA and ways that the data collection, examinations, and feedback from FinCEN might be improved.

I now yield to the gentleman from Illinois for his opening statement.

Mr. GUTIERREZ. Thank you very much, Chairwoman Kelly, for calling this hearing. I also want to thank you on the record for your help yesterday with my amendment providing a liability shield to GSEs, in which they disclose expected or actual mortgage fraud to their regulator.

We have worked very well together on issues related to financial crime and terrorist financing. I look forward to continuing our excellent working relationship.

I am pleased to see all the witnesses here today, but in particular, I want to welcome Diana Taylor, the New York Bank Superintendent with whom I have worked on the OCC preemption issue. I expect to work with her on this issue in the future.

I am also looking forward to hearing from Director Fox, and I have to thank him for the work of his very responsive staff, particularly William Langford and Joyce Lin.

It is good that we are joined today by Mr. Morehart, a representative of the FBI—an agency we don't often see represented in this hearing—and from whom we can gather more help.

As many of you know, I have worked on issues around the remittances since I was a member of the Chicago City Council and have offered legislation to provide for fair and full disclosure of the often exorbitant and often hidden fees charged by certain money transmitter companies.

Now I know that Mr. Cachey of Western Union and Mr. McClain, representing the money transmitters, will disagree with me here, but I think that more of these transactions ought to be handled directly by banks—why it is certainly preferable to have people sending money through licensed MSBs than through underground channels. It is even better to have these transaction handled by a regulated financial institution. More banks entering the market means more competition and disclosure, and lower prices in the end for consumers.

I am not trying to put the money transmitters out of business, but I think they need competition from banks to bring prices down. I am pleased that guidance was finally issued on April 26th for banks regarding money service businesses. While, as I mentioned, I would prefer that the banks provide these services directly to consumers, until enough banks and credit unions enter this market, MSBs will necessarily fill the gaps and service for many communities. I want you to be able to stay in business serving populations who send remittances for those who are currently unbanked.

As MSBs are currently thriving, the top four U.S. nonbank money transmitters—one of which is Western Union—increased their global market share from 12 percent in 2000 to 18 percent in 2003, when they handled 40 percent of outbound remittances from the United States. This is in spite of the fact that more than half of the Latin American immigrants hold accounts at banks and credit unions.

So a significant number of people are still using money transmitters to send remittances even though they have a bank account. Clearly, not only do more financial institutions need to offer this service, but they need to do outreach and make sure the community knows they offer remittances services. Some banks have recognized the opportunities in this market, particularly Bank of America, which is now offering free remittances to their customers to Mexico. This is not merely the right thing to do, it is simply good business.

Furthermore, getting unbacked remittance senders into banking relationships has additional advantages. I have encouraged the financial services industry to take into account an individual's documented remittance payments to family members abroad as evidence of creditworthiness when making decisions regarding the extension of a mortgage or a credit line to those without a significant credit history. Frequently, families are remitting a large portion of their income and demonstrating incredible financial discipline, but these payments do not count toward the building of a credit history.

I believe that the entire financial services industry will soon recognize that the risk is minimal when lending to these customers.

As they demonstrate, say, a record of remittance sending, their fiscal responsibility and creditworthiness will become apparent.

Many financial institutions currently offer I–10 loans because they recognize these customers can be a good financial risk. I hope they continue to look for nontraditional ways to give worthy customers access to capital.

In fact, along with Congressman Barney Frank, I have asked the National Credit Union Administration and several individual banks to look into the feasibility of offering loan products that take remittance-sending into consideration. I think that this will also help greatly in getting the business of remittances into regulated financial institutions for fees or generally less—in Bank of America's case, nonexistent.

At the appropriate time I would like to hear from Mr. Byrne, who has testified before us many times on financial crimes issue, what the financial services industry and the ABA is doing in particular to encourage more—into the business of remittances.

Thank you, Congresswoman Kelly, for calling this hearing. I yield back my time.

Chairwoman KELLY. Thank you.

Mr. Morehart, I opened this hearing mispronouncing your name.

Mr. MOORE. That is all right, ma'am.

Chairwoman KELLY. I notice my ranking member followed suit. I want to offer you an apology.

Mr. MOORE. None needed.

Chairwoman KELLY. I also want you to know our staffs got it right. We are the people who got it wrong.

Mr. Moore.

Mr. MOORE. Madam Chairperson, I appreciate the opportunity to make an opening statement here, but I really would like to hear the testimony of the witnesses, and I think we will just proceed there.

I would—let me back up 1 minute and say this. I was a prosecutor, a district attorney for 12 years in my county back home and in a suburban county of Kansas City, Missouri. I understand the need for effective law enforcement and I understand what happened with the PATRIOT Act.

In fact, I voted along with a great majority of Members of Congress for the PATRIOT Act. I was willing to do that and give up on a temporary basis some of our individual personal liberties and freedoms to protect our country from another strike—and we didn't know what was going to happen. I think a great majority of Congress felt that way as well.

I am still very supportive of law enforcement measures, but I want to make sure that in this rush to renew the PATRIOT Act we don't give up our personal liberties and freedoms, because those are the things that separate us from almost every other country in the world to make our country greatest Nation in the whole world.

So I am here to listen today to what you have to say about the provisions of the Bank Secrecy Act, provisions of the PATRIOT Act, and I certainly will consider all of those. But I certainly think that all of us—and this should not be about Republicans and Democrats—this is about the thing that sets our Nation apart from every

other country in the world, is our Bill of Rights and the personal liberties and freedoms we have in this country.

So with that, I really appreciate your being here. I will listen with interest to your testimony.

Chairwoman KELLY. Thank you, Mr. Moore.

Mr. McHenry, do you have an opening statement?

Mr. Scott?

Mr. SCOTT. No, Madam Chair. I am anxious to get to the testimony.

Chairwoman KELLY. Thank you. Well, I am anxious to get to the testimony also.

Our first panel consists of Director Bill Fox from FinCEN and Michael Morehart, who is the Director of the FBI Terrorist Financing Operations Section.

Prior to his appointment as FinCEN's Director, Mr. Fox served as the Treasury's Associate Deputy General Counsel and Acting Deputy General Counsel. Since September 11, 2001, he has also served as the principal assistant and senior adviser to Treasury's general counsel on issues relating to terrorist financing and financial crime.

Michael Morehart has served as Director of the TFOS since March 2004. He is a 19-year veteran of the FBI and a CPA. Gentlemen, we look forward to your testimony.

Chairwoman KELLY. We begin with you, Mr. Fox.

STATEMENT OF WILLIAM J. FOX, DIRECTOR, FINANCIAL CRIMES ENFORCEMENT NETWORK, DEPARTMENT OF THE TREASURY

Mr. FOX. Thank you very much.

Chairwoman KELLY. Mr. Fox, please turn the microphone on.

Mr. FOX. Got it.

Chairwoman KELLY. Thank you.

Mr. FOX. Thank you, Congresswoman Kelly, Congressman Gutierrez, and other distinguished members of this committee. I wish to thank you for the opportunity to appear before you to discuss the Financial Crimes Enforcement Network's administration and implementation of the Bank Secrecy Act. We thank you for the support and policy guidance you and the members of this committee, on both sides of the aisle, have offered to us on these issues.

I would like to acknowledge the work of your staff that was very helpful to us in preparing for this important hearing today. They worked tirelessly and they are extremely well-informed. The committee is fortunate to have such dedicated and talented professionals. I have submitted a written statement for the record that outlines much of what we are attempting to accomplish at the Financial Crimes Enforcement Network. I will try to keep these remarks very brief.

I am very happy to appear here today with my good friend and colleague, Mike Morehart, who is the Chief of the Terrorist Financing Operations Section in the Counterterrorism Division of the Federal Bureau of Investigation.

Special Agent Morehart's office is working tirelessly to keep our country safe from terrorists. Every day the men and women in the

Terrorist Financing Operation Section accomplish that mission, utilizing some of the most valuable information to the government—financial information—in the process. I know—I have seen them at work, and I am aware of the fruits of their labor.

We have entered into a very deep partnership with the FBI that is allowing Mr. Morehart's office and other components of the Bureau to exploit information collected under the Bank Secrecy Act in a much more meaningful and relevant way.

This partnership, which will become part of our BSA direct paradigm, will make a significant difference in the way we interact with our key customers, ensuring that the valuable information we collect is put to the best use possible.

I hope we get to explore this more today with the committee, because I believe it is a true success story. In fact, I believe it is a model that the rest of the government could follow in sharing sensitive information.

I would also like to acknowledge Superintendent Diana Taylor from the New York Banking Department, who is appearing on the second panel this morning. As you know, we have entered into a very important information-sharing agreement with Superintendent Taylor's agency that I believe will add a great deal to ensuring that the Bank Secrecy Act is implemented properly. Superintendent Taylor exercised outstanding leadership in ensuring this agreement was reached and signed.

Everyone in this room knows that September 11th changed the world. What we may not have realized on that bright morning nearly 4 years ago, we now know for certain: September 11th revealed a new reality. What we know about this new reality is that information is the key to the security of our Nation, and information is what the Bank Secrecy Act is all about.

I believe that through the USA PATRIOT Act, the Congress recognized this new reality. You broke down walls that prevented the sharing of information between law enforcement and the intelligence community. Most significantly to the issues being addressed today, under the leadership of this committee on both sides of the aisle, you provided us tools to better acquire and share information both between the government and the financial institutions, and between financial institutions themselves.

These tools highlight a couple of important truths. First, that information sharing is necessary and important to the national security of our country; and, second, that these tools demonstrate the recognition that financial information, in particular, is highly reliable and valuable to identifying, locating, and disrupting terrorist networks that mean to do us harm.

That is why this hearing today is so timely and important. Your hearing has been entitled "The First Line of Defense: The Role of Financial Institutions in Detecting Financial Crimes."

Since the beginning of the year, I have traveled across the country and have spoken with bankers, broker dealers, money services businesses, and other financial institutions. These financial institutions have expressed candid concern about how the Bank Secrecy Act is being implemented. I am very grateful for the opportunity to try to outline for the committee those concerns, and what we are attempting to do to try to address them.

From my perspective, nothing is more important, simply because I do believe that financial institutions are the first line of defense to the security our financial system. We must make the partnership envisioned by the USA PATRIOT Act real, if we are truly to achieve our goals.

The goals of the Bank Secrecy Act are simple.

One, safeguarding the financial industry from threats posed by money laundering and illicit finance, by ensuring that the financial industry, the first line of defense, has the systems, procedures, and programs in place to protect the institution and, therefore, the system from these threats.

Two, ensuring a system of reporting that provides the government with the right information—relevant, robust, and actionable information—that will be highly useful in these efforts to prevent, deter, investigate, and prosecute financial crime. We must keep our eye on these goals.

It is my view that the best way to achieve these goals is to work in a closer, more collaborative way with the financial industry. This regime demands a partnership and an ongoing dialogue between the government and the financial industry if it is ever going to realize its true potential. It is why, for example, we are working so hard to implement section 314(a) of the USA PATRIOT Act in a much deeper way, which will result in a sensitive, yet systematic, two-way dialogue with the financial industry.

This dialogue will make our financial system safer and more transparent. I am convinced that the financial industry is committed to this partnership and dialogue. Our goal is to do all we can to ensure that the government lives up to its side of the bargain.

Madam Chairwoman—if you can bear with me, I would like to bring up one issue that is not directly related to the hearing today. I am happy to report to you that we have had very good conversations with the officials of the Kingdom of Saudi Arabia regarding their efforts to set up a financial intelligence unit. We are poised to offer whatever assistance the Kingdom will accept in setting this unit up.

Having an FIU in place in Saudi Arabia will add a great deal of transparency to the Persian Gulf region. Madam Chairwoman, I am convinced that we would not be having these conversations except for your direct, personal efforts on your recent travel to the Middle East.

I want to thank you for your efforts, and I want you to know that your efforts are having a real-world effect. I believe it shows what we can accomplish when our government works closely together hand-in-hand.

Again, I wish to thank the members of this committee for inviting me here today. I am happy to answer any questions you wish to ask.

[The prepared statement of Mr. Fox can be found on page 64 of the appendix.]

Chairwoman KELLY. Thank you very much, Mr. Fox.

Mr. Morehart.

STATEMENT OF MICHAEL MOREHART, DIRECTOR, TERRORIST FINANCING OPERATIONS SECTION, FEDERAL BUREAU OF INVESTIGATION

Mr. MOREHART. Thank you, Chairwoman Kelly, Congressman Gutierrez, and distinguished members of the committee. I appreciate the opportunity to appear before you to discuss the efforts of the U.S. Treasury's Financial Crimes Network, otherwise known as FinCEN, and the Federal Bureau of Investigation, particularly as they pertain to the utilization of information obtained pursuant to the Bank Secrecy Act, also known as BSA, as amended.

I am honored to appear before you today with William Fox—Bill, the Director of FinCEN, to discuss how FinCEN and the FBI work together closely to ensure the appropriate and successful utilization of BSA information in the war on terrorism. Over the years, the FBI has enjoyed a longstanding and productive relationship with FinCEN.

The importance and quality of this working relationship cannot be overstated. Under the leadership of Director Fox, our relationship as well as the quality and successes of our joint efforts have flourished. This mutually beneficial working relationship serves as a prime example of what can be achieved when agencies unite in a common effort to ensure the safety of our financial system as well as our Nation's security.

The critical role that financial information serves in investigative and intelligence matters cannot be overemphasized. This underlying premise was enumerated in the PATRIOT Act of 2001 and an example is as follows: Defects in financial transparency on which money launderers rely are critical to the global financing of terrorism and the provision of funds for terrorist attacks.

Financial information, lawfully acquired, significantly enhances the ability of U.S. law enforcement and intelligence community members to overcome defects in financial transparencies, as mentioned in the previous excerpt that I just read from the PATRIOT Act.

Likewise, BSA data is of incalculable value in this important effort. When combined with other data collected by law enforcement and the Intelligence Communities, investigators are better able to connect the dots.

More recently, BSA data has proven its utility relative to matters. For example, BSA data is used to obtain official information about subjects under investigation and their methods of operation. Analysis of BSA data permits investigators to acquire biographical and descriptive information to identify previously unknown subject associates and/or co-conspirators—and in certain instances, to determine location of those subjects by time and place.

The value of BSA data to efforts is reflected in the results of the review of the BSA data that the FBI has conducted. In this instance, the FBI, using information technology, reviewed approximately 71 million BSA documents for their relevance to, investigative, and intelligence matters.

The review identified over 88,000 suspicious activity reports and currency transaction reports that bore some relationship to subjects of terrorism investigations. The FBI also uses BSA data to identify trends and patterns of relevance to terrorism financing.

For example, 64 percent of the CTRs associated with cash deposits were for amounts which totaled less than $20,000. Conversely, the analysis showed that 75 percent of the CTRs associated with cash withdrawals were for amounts greater than $20,000.

This is consistent with traditional money laundering activity or structuring, which involves a deposit of small amounts, followed by the withdrawal of larger amounts. Director Fox and his staff clearly understand the importance of BSA data to the investigative and intelligence missions of the FBI, and, in turn, its critical importance to the protection of this Nation's financial infrastructure as well as its security.

This understanding is evidenced by FinCEN's assistance in helping the FBI develop new ways to access and to share the BSA data. As a result, BSA data has been integrated into the FBI's investigative data warehouse, otherwise known as IDW. By way of background, IDW is a centralized Web-enabled closed system repository for intelligence and investigative data.

The system maintained by the FBI allows appropriately trained and authorized personnel throughout this country to query information of relevance to investigative and intelligence matters. In addition to the BSA data provided by FinCEN, IDW includes information contained in a myriad of other law enforcement and intelligence community databases.

The benefits of IDW include the ability to efficiently and effectively access multiple databases in a single query. As a result of the development of this robust information development technology, a review of data that might have previously taken days or months now only takes minutes or seconds.

In conclusion, the partnership between the FBI and FinCEN is a model for the effective sharing of information. Director Fox has accurately identified a process which maximizes the information collected by FinCEN to be used by the FBI within the confines of current laws and regulations in the war on terrorism. The FBI has developed IDW as a tool to find the most critical pieces of information included in BSA data and other data sets to ensure that efforts of FinCEN and its banking partners are utilized as directed by Congress to protect the United States.

I would like to thank the committee for this opportunity and welcome the opportunity to answer any questions that you might have.

Thank you.

[The prepared statement of Mr. Morehart can be found on page 80 of the appendix.]

Chairwoman KELLY. Thank you very much, Mr. Morehart.

Director Fox, I am going to ask you three questions. Mr. Morehart, I would be interested in your responses as well.

I am wondering, Mr. Fox, can you discuss efforts over the last year to strengthen our BSA compliance regime? I have often spoken with you as well about my concern about the structural issues, which seemed to be presenting vulnerable areas of fragmentation and causing inefficiencies.

I know that the finalization last year of—the MOU was designed to help address some of the concerns so that a more unified and effective BSA compliance system could be achieved. But is it enough? It seems to be a highly segmented system at this point.

I want to know what we can do to ensure that it is an effective, synchronized and capable system providing a unified message about what is expected of the financial institutions.

Mr. FOX. Thank you very much, Chairwoman Kelly, for that question.

I think it is an interesting system in the sense that we administer the Bank Secrecy Act. Yet, the act is implemented by no fewer than eight separate Federal agencies that examine for its compliance. Working to make sure that all the folks involved are pulling the oar in the same direction is a challenge from time to time.

I will tell you that we have received outstanding cooperation from most of the regulators. The Federal banking agencies and the IRS, in particular, have been incredibly helpful in trying to coordinate this effort in a better way.

I think we are, today, more coordinated and working together with a single unified message than we perhaps ever have been.

I think this is evidenced by the guidance that has been recently issued. There has been joint guidance to the banking agencies, and I think that really helps depository institutions when their regulator joins with our guidance, even though technically our guidance is the definitive guidance when it comes to the Bank Secrecy Act.

That being said, I think I would not be completely candid with you if I didn't tell you that there are issues, and we hear—one of the things that I have heard from time to time, as I have discussed these issues with the banking industry in particular, but with other banking industry sectors as well, is there does seem to be a disconnect between the actual examination forces and the policymakers in Washington.

We are doing all we can to close that void. We are training examiners, together and jointly. We are making sure that there is no daylight between what we are saying both publicly and to our own people. We have created a FinCEN Office of Compliance, with this committee's help, to actually monitor this situation and to receive from the agencies what is actually happening out there as they examine—not just from the banking agencies—but hopefully from the other regulators in the Bank Secrecy Act milieu as well.

What I can tell you is that folks across this spectrum are trying very, very hard to make this work. We are doing all we can to lead this effort and to make sure that the government speaks with one voice. I think that is the very least that the industry can expect from us.

I also will tell you that, again, I believe that this system is critical to the national security of the United States. We can't get it wrong, and we can't be speaking with different voices. So we are going to watch this very closely, and we will certainly continue the dialogue that we have begun with this committee and other Members of Congress because I think it is a critical issue.

I am happy to report that folks are really trying, and I think it is getting better.

Chairwoman KELLY. It is a new system, so the concern is whether or not we are moving toward a unified message, and I think that is important.

Mr. Morehart, do you want to comment on that, please?

Mr. MOREHART. From the oversight standpoint, obviously, the FBI has no role in that. However, I can comment on it from this standpoint. I am often asked, particularly when I go out and deliver presentations and interact with our partners in the financial community—whether it be banks or whatever—what are the indicators of terrorism; financing, particularly? That is a very difficult question to answer.

They ask that question in this context. How will we know—how do we know, how are we supposed to know what to report on a suspicious activity report? And it is a very good question and a very logical question. Bottom line, it boils down to the same guidance that was given to financial institutions when the Bank Secrecy Act was implemented and throughout the past years in terms of what we call regular financial crimes, for instance, not terrorism, but know your customer.

The bottom line is if it seems unusual, report it. However, to address those issues, Bill and I have worked together. We are constantly trying to identify or provide a definition of what constitutes suspicious activity in terms of terrorist financing.

Bill—on the forefront again—we have had conversations, and he actually delivered to financial institutions a somewhat—not complete, but a start as to what indicators they might look for, so that they can appropriately comply with BSA requirements in terms of SARs specifically.

So we are making every effort, together, as a team to try to identify whatever information we can and provide it to the financial institutions and entities affected by BSA so that they know what to report, they know how to report it, when to report it, and what is appropriate.

As always, through our contacts, we make it clear that if there is a question, they should call.

Mr. FOX. Madam Chairwoman, if I could, I forgot one element of this issue.

Chairwoman KELLY. All right.

Mr. FOX. The States are a huge part of this. Each State has its own regulatory regime and bank regulator or regulatory services. I think our efforts to coordinate better with the States—which is our MOU within New York—is a real key aspect to this as well.

Chairwoman KELLY. As you know, the concern is an overabundance of information and sifting it out to get accurate appropriate information.

Mr. Gutierrez.

Mr. GUTIERREZ. Thank you.

I want to ask Director Fox, is FinCEN consulted by banking regulators when a bank has committed a Bank Secrecy Act violation? In other words, are you consulted in the determination of enforcement actions on BSA matters? How much input do you have in the final determination of what violations merit disciplinary action?

Mr. FOX. Thank you, Congressman. We are now, as a result of our MOU that we have executed with the Federal banking agencies, notified whenever the agencies determine, discover, or uncover a significant violation of the Bank Secrecy Act. The art, of course, is defining the word "significant" but I can tell you that the agen-

cies have been very good about providing the information to us when they uncover it.

This is a brand-new system. We are very pleased with the responses so far. The fact is agencies will—the agency has a responsibility that relates to safety and soundness—decide whether or not to issue a consent decree along those bases. But we are engaging with them in a fair way to determine what the appropriate enforcement action is.

Certainly, any action that rises to the point where simple monetary penalties are contemplated, it is our view that actually it must be a coordinated effort on behalf of the government. So we are working very, very hard so that when that extraordinary case happens, we do it together. We don't think it is fair to whipsaw the industry with separate enforcement actions that are based essentially on the same facts.

So if a regulator—one of your co-managers of the industry—will let you know if they believe it is substantial, then you will work together.

Mr. FOX. Yes, we do work together. If a conversation is started—in fact, I don't want to mislead you either. I don't think that agencies, particularly the banking agencies and certainly the SEC and CFTC all have their own enforcement capabilities through their safety and soundness responsibilities, and technically they can go forward without us on those issues.

But the reality is, at least so far, I am happy to report that this is not occurring, that we are enjoying the conversation that is occurring. I think we are having valuable input to it, we know about it, and it helps us to address the administration of the system as a whole.

Mr. GUTIERREZ. I asked the question, because—I mean, I understand it from a processing point of view. The financial institution would probably prefer, as you said, you just not get whipsawed. But at the same time, when more people are looking at it, let us say an OCC or someone sees something and they consult with you and others in terms of saying here it is, a substantial—and everybody is looking at it—I just think the public is better served. Our security and soundness is better even though you don't have that issue at FinCEN.

Mr. FOX. I agree. I will tell you it is critical that we make sure our enforcement actions are geared to achieving the policy goals of the statute. So I couldn't agree with you more.

Mr. GUTIERREZ. Let me ask you, following up on that same, I would like to ask Mr. Moore and you, Director Fox and Director Morehart, does the FBI also share information with FinCEN or is it a one-way street? Specifically, does the FBI provide information regarding situations where, perhaps, a crime hasn't been committed but the bank may be in violation of some regulatory statute? Do the regulators get this information so they can act on it?

So I understand what you might do, I guess I would like to hear what Mr. Morehart and his team might do if it is not a crime in the sense, but it is a violation, it is a regulatory violation.

Mr. MOREHART. Certainly. Obviously we comply with our guidelines in terms of the classified information and how it can be disseminated in terms of a nonclassified investigation, if you will, a

typical fraud. As one might expect, we provide as much information as necessary to obtain the information we require.

In other words, if Bill and I were working together on a particular investigation, it might be necessary for me to provide him certain parameters, certain guidelines, that would allow him to respond to my questions.

So the answer to that generally is yes. But obviously within the laws and within the guidelines as they pertain to, for example, 6(e) material, grand jury secrecy and so forth, as well as the classification requirements on information.

Does that answer your question?

Mr. GUTIERREZ. Yes. Let me just—in the spirit of clarity—so let me just ask you this question. Has there been an example, a situation, where the FBI is examining something, looking for fraud, but then finds regulatory flaws; that is, if they didn't respond? There was no fraud, but the financial institution didn't carry out all its responsibilities in terms of regulatory issues.

Mr. MOREHART. Honestly, I can't think of one off the top of my head, sir, but logic would dictate that if we did run across that type of violation, we would contact the appropriate regulatory body that would handle it.

Mr. FOX. I can tell you, Congressman, that we would work closely as well, not only with the Counterterrorism Division of the FBI, but also with the Financial Crimes Division. We have received such referrals from the FBI indicating that it appears something is going on here and you, FINCEN, ought to look at this. I think that this is really the important part of this partnership.

I would also like to emphasize that while we have picked the Bureau to be the first one to enter into this extraordinary relationship with the data because of their terrorism responsibilities, our goal is to have similar arrangements with other key Federal law enforcement agencies. We really do have a terrific relationship with those agencies.

The Bureau of Immigration and Customs Enforcement just announced a big action on unregistered MSBs this past week. We helped and supported that effort at ICE and it is that sort of information sharing that occurs all the time. It is part of what we try to make ourselves, and that is a network of information, and we try to be a hub for financial information.

Mr. GUTIERREZ. Thank you both, gentlemen. Thank you very much.

Mr. FOX. Thank you.

Chairwoman KELLY. Mr. Crowley.

Mr. CROWLEY. Are you recognizing me for questions? Or recognizing me to be on the committee? I am not a member of the—standing member of the subcommittee, so is that okay? Thank you.

Chairwoman KELLY. I am sorry. They would like—I have been asked by Mr. Gutierrez to allow you to ask questions. You are welcome to do that.

Mr. CROWLEY. Thank you very much, Ms. Kelly, I appreciate that very much. I represent a very, very diverse district in New York City, Queens and Bronx. I may have one of the most diverse districts in the country. I have many, many immigrants from various parts of the world.

Very recently it has come to my attention that a major bank—I won't mention the bank—was considering suspending the remittance program, where moneys that are derived here in the United States through work—more likely than not—from undocumented workers who are sending those funds back to their homelands. Their families, many of those families rely upon those dollars to get by in those developing countries.

But due to the fear that they possibly could be prosecuted under the PATRIOT Act, money laundering issues, etc., that they may be somehow financing unwittingly someone who is on the suspected terrorist list, that they are no longer providing those services. It is a real concern that we have.

On top of that has been what has been described as arbitrary enforcement, where some are being told this and others aren't necessarily getting that same direction.

Could you, either one or both actually, answer what actions you have taken and what will you be doing in talking to these companies or these banks to address the concerns about arbitrary enforcement and uneven regulation?

Mr. FOX. Thank you, Congressman. I actually think you know that this is clearly—this has clearly been one of the issues this past year in the area of the implementation of the Bank Secrecy Act relating to money services businesses and also remittances generally, and possibly a misperception on the part of the financial industry on the risks associated with that.

As you may know, we have implemented the Bank Secrecy Act through what we call a risk-based regulatory approach. We think that this is a very smart way to do it, just because of the nature of the problem. But it requires institutions to essentially study the risk that may be associated with its business lines or its customers, and then take appropriate safeguards to make sure that those risks are addressed.

I think there were a couple of problems. One, I think there was a lot of confusion about what was actually required under our regulations. We attempted to address that by issuing guidance, which we issued last month, that I believe—at least the feedback that we have initially received has been very helpful in sort of calming the waters, or at least gaining some understanding, some better understanding about these issues.

Now, I will tell you to the extent that we have not completely covered that field, we will work very hard and try to, because I agree with you that—I think it is certainly the position of my agency, the Department of Treasury, that remittances are an incredibly valuable part of the world's economy, an incredibly important part of the world's economy. So, I believe that they can be managed with the appropriate level of attention and risk by institutions.

What we hope to do, sir, is to make sure that folks understand clearly what we are expecting of them in the financial industry and to the extent that we can do that, these decisions will become business decisions for the institutions and not based on sort of misperceptions about what the risk may be.

Mr. MOREHART. Thank you, sir. I can't speak as to the uneven regulation, obviously. I am going to have to defer to Mr. Fox for that.

However, may I ask a question, sir, in terms of arbitrary enforcement? I assume you are talking about criminal laws as opposed to regulatory?

Mr. CROWLEY. Correct.

Mr. MOREHART. With that clarification, thank you, I would not characterize what the FBI does in terms of law enforcement, whether on the criminal side, or, if I may distinguish, on the terrorism side as arbitrary. Obviously we have to have appropriate predication to initiate an investigation. SARs, obviously, can be used for informational purposes, but not as probable cause, if you will, on a legal action. Nevertheless, they are of value. We rely on that information in terms of initiating investigations.

As you I am sure understand, sometimes those investigations lead to prosecutions, sometimes they don't. But our determination on whether to initiate an investigation is largely dependent upon what area of the country we are in. As you know, every United States Attorney's office has different persecutive guidelines in terms of dollar amounts and so forth. So that offers us some guidance as to what we look at and what we don't.

In terms of terrorism, obviously, it is a little different, if we are looking at threats as opposed to dollar values; if it poses a credible threat and if there is significant information to initiate an investigation into terrorist matter, potential terrorist matter, we will do that. But, again, it is based on threat. Does that answer your question?

Mr. CROWLEY. It does. I appreciate it. I think what puts the chilling effect on it is the potential criminal aspect. Not necessarily regulatory, because regulatory we can work through those issues and ask questions. When it is a threat of a criminal prosecution, it is a totally different subject.

One quick question, just for the record and not for response.

Mr. Fox, I am currently working on drafting some legislation that would require the Treasury Department, especially FinCEN, to conduct a feasibility study to force the greater consistency, greater transparency, and to improve accuracy and deliverability of information in a form that is more amenable for subsequent analysis by regulatory law enforcement agencies. May I request your assistance as I develop that information?

Mr. FOX. Yes.

Mr. CROWLEY. Thank you very much. I yield back.

Chairwoman KELLY. Yes. Mr. Royce.

Mr. ROYCE. There was a story today—there was a hearing yesterday, I think it was the Government Reform Subcommittee that was—the Homeland Security on the Senate side had a hearing on remittances and especially on financial crimes that are occurring in the United States. For example, just to take one segment of that, 20 to 30 million a year is the sum of financial crimes committed by Hezbollah, and admittedly we view it as a terrorist organization. Many of those who participate in this view it as a legitimate arm of Islamist liberation struggle.

But the fact is that these crimes are being committed in the form of identity theft and in the form of credit card fraud and other forms of financial crimes. Then our wire agencies are used to remit that money that then goes to fund Hezbollah.

The Bureau of Immigration and Customs Enforcement this week announced some significant action related to unregistered money remitters. In previous testimony, I think it was you, Mr. Fox, who stated that you believe there are as many as 250,000 money service businesses in the United States. But we only have 23,000 registered?

Mr. FOX. Approximately.

Mr. ROYCE. A quarter million. That gap is cause for concern. So I want to ask you, to what do you attribute that gap and what are you doing to address it?

Then my other line of questioning has to do with what can be done in terms of the user regulation on the problem with three States. Delaware is of particular concern to me, because we have Interpol officers who come over here looking to track money for companies that claim to be U.S. corporations, all right?

They set up in Delaware or one of these other two States that permit the formation now of what I think you and I would call shell corporations. The States collect, in these cases, no information about the identity of the officers, about the directors, no information about beneficial ownership.

So if we allow anonymous corporate shells, how are we going to be able to pressure other jurisdictions around the world to clean up our act?

I know a lot of what Congresswoman Sue Kelly and I work on is how to figure out how we bring pressure to bear internationally on some bad actors, some other State governments, but, you know, using your view that our treaty commitments and our international commitments on the proceeds of crime should make what these States are doing illegal here in the United States, and can you do that by regulation?

I would like you to look into that. Isn't it a fact that these issues have been raised against the United States when we have meetings with the FATF that our colleagues in the international community are bringing this up? Do we have similar problems with trusts and with some types of omnibus trust accounts? Are they also being set up under this same shell corporation system in Delaware and these other two States?

Mr. FOX. Thank you, Congressman Royce.

If I can address your second question first, it is a very timely and very good question. Yes, I believe, without speaking about the policies associated with the setting up of LLCs and other sorts of corporate mechanisms, from my perspective, which tends to be a perspective with blinders on, these entities pose great difficulty for us. I mean, it is a fact that we criticize other governments for similar-type activities, yet we are running into the same sort of problems here in the United States. It is just a simple fact.

What I can tell you is we are studying this issue pretty closely from an analytical perspective to try to determine what is required, what is not required, and also, the problems that those entities are causing for our law enforcement.

Mr. ROYCE. Have you put these three Governors on notice and asked them—

Mr. FOX. No, sir, we have not at this point.

Mr. ROYCE. I would think that would be one of the actions you would want to take, given the enormity of the significance of getting compliance on transparency with respect to some of our—some governments in the Middle East. When we are trying to track the flow on terror finance, it is enormously helpful to have our local jurisdictions complying with Federal law.

I would argue that they are out of compliance. I would give them the opportunity, these Governors, if I were you, of contacting the Governors, bringing this to their attention, explaining the consequences. I am sure you are aware also, if some of the meetings over here from Interpol and others who are hot on the trail of some very dangerous people, and asking them if they would like to be part of the solution by suggesting to the president pro tems and the speakers of their house of delegates and State senates, that they quickly move legislation to correct this.

Mr. FOX. I think that is actually a very good strategy, Congressman. I think what we are trying to do is make sure we fully understand the issue before we actually go and engage in some way like that. I want to make sure our ducks are in a row, if you will.

Mr. ROYCE. Line them up.

Mr. FOX. You have got it. So I think that this is an incredibly important question. I don't know whether Mike has any comments on that issue or not.

Mr. MOREHART. No, sir, I don't; not on that.

Mr. FOX. But it is a very important one that I think we need to address. Going back to your first question?

Mr. ROYCE. Please.

Mr. FOX. Yes, this is a very serious issue that we have identified and we realize we have to do something about it. Now the 200,000-plus number that you have comes essentially from a study that was conducted, I think if I am correct, in the late 1990's as we were beginning to think about how to regulate the money services business sector. It was a study that was done by one of the consulting firms, one of the big six or four or however many of them are left. The number actually includes outlets of the U.S. Postal Service, certainly every outlet of Western Union, MoneyGram and others, that are not required presently to register with FinCEN because of their agency relationship. There is an exemption for the U.S. Postal Service, so that can account for some of the gap but certainly not all of it.

Mr. ROYCE. Right.

Mr. FOX. We are convinced that there is a gap. How big the gap is, I am not sure. But I think what we are doing, and we are doing with some alacrity, is we are reviewing our regulatory scheme that was implemented in 2001, I believe, before September 11th, to determine whether or not that registration scheme makes sense. Because I think one of the very first things we need to do for law enforcement and for our purposes is to know where these businesses are conducting their business.

I think if we make the registration requirement easy; in other words, Web-based, or make it a very simple form, at least we will know where they are and then we can reach out and help them comply and add greater transparency to this important financial services sector.

So I think you can expect from us very soon regulatory action to address this issue. It is a very serious issue.

Mr. ROYCE. In closing, Mr. Fox, there is some urgency to this as well. $20 to $30 million in the hands of Hezbollah, that is a lot of dynamite.

Mr. FOX. It keeps me from sleeping at night, sir.

Mr. ROYCE. Thank you, Mr. Fox.

Chairwoman KELLY. Thank you, Mr. Royce.

Mr. MOREHART. May I comment on that, Madam Chairwoman?

Chairwoman KELLY. Yes, please.

Mr. MOREHART. Let me add this if I might, Congressman.

One of the databases that was provided to us by FinCEN is their money services database, which is a listing of all registered MSBs. In an open forum I can't go into great detail but I will add this comment, that we have a number of interagency initiatives with ICE and IRS, Treasury, you name it, ongoing to identify those types of businesses.

This is a perfect example of the value of the data provided to us by FinCEN on the BSA. It is important from the standpoint that we can immediately evaluate whether or not a subject of an investigation who may be involved or suspected of an involvement as an MSB, either witting or unwitting, is registered or not.

In addition, we have a number of proactive efforts underway, again interagency efforts, to identify these types of entities so that appropriate regulatory and legal action can be taken to resolve that issue.

We recognize the import of that. We recognize that these individuals may be being used to move money to facilitate terrorists whether it is Hezbollah, Hamas, PIJ, al Qaeda or any of them, quite candidly, and we take it seriously.

We are working every day, day-to-day, with Mr. Fox and his staff to utilize that information to exploit it to the interests of our country, to make sure that the financing that is out there is not being sent for terrorism purposes.

Chairwoman KELLY. Thank you, Mr. Morehart.

Mr. Scott.

Mr. SCOTT. Thank you very much, Chairwoman Kelly.

Mr. Morehart, may I start with you? Critical to the success of your job is being able to collect the transaction data, the BSA data, to be able to use that, is that not correct, as well?

Mr. MOREHART. That is correct, sir. Utilize it but not collect it, other than through FinCEN.

Mr. SCOTT. From what we hear from the banking community and the banks and the financial institutions, they are very critical that it is too much information, that it is overburdensome to them. Do you question why so much information, what is the Federal Government doing with that information, and are they in the eye of the storm as well? Can you address this conflict of opinion and share with us why you need this much information, and secondly, where is that burden with the banking finance community?

Mr. MOREHART. Start with the latter aspect of that question, sir. I am not sure I can answer where the burden would be with the community in general. That might be better addressed—

Mr. SCOTT. I meant why they feel that it is this burdensome and too worrisome and too much, and of course, you can address why, just the opposite, you need it.

Mr. MOREHART. The information we receive, the BSA data we receive and have received has been invaluable, as I mentioned in my opening comments. The information is not too much. I would wholly disagree with that.

I think the question here is perhaps that the financial sector of our country probably doesn't realize and in certain instances we can't tell them how we utilize that data nor would I think it prudent.

I can give you some examples of how we use that information and how valuable it is, and I will emphasize that our use of that information, in conjunction with FinCEN and the forward-thinking approach that Mr. Fox has worked with us to develop, has been critical. The information technology we have developed has allowed us to do things to exploit that data, to look at it, to use it like never before.

As I mentioned, in the old days, and I shouldn't say the old days, 20 years ago, as long as I have been in the Bureau, when I first joined, when we got information, back then they weren't SARs, and I forget what the documents were, 567s or whatever they were, we would actually have to flip those documents and look through them. A real person would look through those to identify a name or something of import.

That is no longer the case wholly. What we do is we take IDW, our Investigative Data Warehouse as I described, if I could characterize it as a Google on steroids, that is essentially what it is, and it is amazing. We can actually take millions of documents, BSA documents, and query them for a specific set of metrics within hours, within minutes sometimes, and even seconds.

For example, we may be interested in identifying CTRs or SARs, identifiable with a particular subject that we have intelligence that suggests they may be money laundering, whether for what I call typical crimes or terrorism purposes, we can run against all those billions of documents and in a very short period of time identify every document associated with that individual and pull them up.

After, we can analyze them and we can determine information quickly, very quickly. For example, we can identify the pattern of activity. We can identify what banks they have dealt with. We can identify the dollars and where they have been sent and biographical data that may help us locate that individual and/or an address, and those are just certain examples of the things we are able to do.

As to the volume of information provided, all things must be reasonable. We recognize that, and that is why there are limitations on dollar amounts with CTRs and things like that because it would be truly overburdensome if we had to report on every transaction.

I will point this out, however. SARs are very subjective in nature. What I mean by that is what is suspicious to me may not be suspicious to you. Nevertheless, it comes back to what we have always discussed with our banking partners or partners in the financial sector, is know your customer. If it is unusual, report it.

I would like to give you a couple of statistics in a moment that kind of prove what I am saying.

On the CTR side of the house, the Currency Transaction Reports, the current limit is $10,000—I know there has been some discussion as to whether it should be raised to $20,000. We are opposed to that. We think it is a huge mistake, and I think the numbers that I will give you will explain why.

Those are objective in nature. That is, there is no decision, either the amount of money is either deposited or withdrawn, i.e., $10,000 or more, or it is not and the information included on there, name, address, biographical information and so forth, can be extremely valuable in an investigation, whether it relates to terror or otherwise.

Let me just give you a couple of examples of some numbers that may bring this home.

The total BSA documents in IDW now are about 63 million, and they constantly increase as the banks send in data, and they in turn give them to us and we enter them into the database. We did a search that I would characterize as main hits; that is, all the subjects of current and closed FBI investigations were compared to that BSA data. Out of 63 million documents, there were 1.5 million hits.

Now, it is incumbent upon us to evaluate that information, particularly on those more threat-based cases that are of import, and that we send that information out to the field and/or they access it themselves through IDW. We have some 5,000, if I am not mistaken, users trained in FBI offices to access that data, which is immediately available to the investigator and can be of significant import.

Mr. SCOTT. My time is about up. I did have one follow-up on that when I set that question up because we want to make sure that the system of data collection that is in place is exactly what you need. I do think that we need, because the banks have to give it to you, but maybe there is some things we can do to make sure there is nothing too burdensome that prevents us from giving you the information.

Do you think that the system of collection of this data that we have with the BSA is sufficient to catch, say, what I think is one of the main sources, the hawalas; are we okay with that?

Chairwoman KELLY. Mr. Scott, we are running out of time here.

Mr. SCOTT. Just give me a response.

Chairwoman KELLY. Can you give a quick response to that, please?

Mr. MOREHART. It is difficult for me to assess whether it is perfect or not, by any stretch of the imagination. I think that is a very subjective measure. However, I would say that the BSA data we get is critical, and I repeat that, critical to the identification of those types of activities, whether witting or unwitting, in support of terrorism or otherwise.

Chairwoman KELLY. Thank you.

Mr. Davis.

Mr. DAVIS OF ALABAMA. Thank you, Madam Chairwoman.

Mr. Fox, I direct these questions at you. As you may know in the last several years, various States, I think about 17, have entered

into voluntary alliances that are loosely called FraudNet and what happens is that financial institutions within the member States or the partner States agree to share information regarding suspicious credit activities.

There has been some controversy and some discussion since the renewal of FCRA last year as to, number one, the utility of alliances like FraudNet, and number two, of whether or not they somehow violate FCRA.

I recognize that obviously other agencies will make the determination as to whether they are violative. Let me get you to comment for a moment.

Do you perceive the FraudNet alliances as being in any way in violation of FCRA?

Mr. FOX. Congressman, I am sorry I have not analyzed FraudNet from the FCRA, but we would be happy to do that in a question for the record and at least give you our view of it. We have not looked at FraudNet, in particular, against that standard.

Mr. DAVIS OF ALABAMA. Well, moving beyond the legal interpretation of whether or not there is a collision with FCRA, can you a comment for a moment just on the utility of alliances like FraudNet?

Mr. FOX. I think if I understand FraudNet correctly, I believe that Gramm-Leach-Bliley sort of made FraudNet capable or enabled it, so to speak, and I am somewhat familiar with it. I have seen it. And I believe, frankly, that it is a very useful—it is kind of a bulletin board where folks post—I think if I'm not mistaken it has been sponsored by the Florida Bankers Association, or underwritten by them. I know that they have significant instances where fraud has been either halted or stopped as a result of the sharing of that information, and from that perspective it seems to me to be quite valuable.

I will tell you that one of the things that we must do a better job of is living up to the mandate that you all gave us in section 314(a) of the USA PATRIOT Act and that is to create a conversation with the financial industry on issues relating to money laundering and terrorist financing, and I am very keen to do that at FinCEN.

In my view, we have not done enough there, and I think it is important that we do much more. In fact, we have created a secure Web site that may form the platform for the sharing of some of this information that might be valuable in this context. To be very candid, FraudNet's idea or concept was one that we utilized when we thought of how to do this platform. It is not fully implemented yet, but we are working very hard to get there.

Mr. DAVIS OF ALABAMA. Let me go for a moment back to Mr. Scott's questions and Mr. Royce's questions. One of Mr. Scott's questions regarding the FCRAs, do we have any indication, even an approximate, of how many SARs are filed in the United States in a given year?

Mr. FOX. The number has been roughly between, if I could just correct my statement later if I need to, but I think roughly around 400,000 has been the number. We have, however, seen a significant spike in that during the past year.

Mr. DAVIS OF ALABAMA. Do we have any ability to quantify how many of those 400,000 lead to a detection of either domestic or foreign illegal activity?

Mr. FOX. Currently, no. It is our hope, sir, with the development of our BSA Direct system, and this is why we are so excited about the partnership with the FBI, that we will be receiving feedback on the utilization of these reports and will be able to report back, not only to the Congress but to the industry as well, in a much more robust way about the value of those reports, almost on an individual basis.

Now, we are never going to see a situation I think where every report results in some action. It is just not going to be the way that we do things, but I think that, frankly, we know how valuable this information is because a lot of that data is being used as a basis for investigation.

Mr. DAVIS OF ALABAMA. Let me ask you one quick follow-up. Do we have any sense of how much time or how many manpower hours are consumed on chasing what amount to false positives or chasing what amount to misreads that come out of SARs because obviously, as I wrap up, clearly we have a concern about you having enough data, but the consequence of sometimes having too much data is that time is wasted chasing false leads? So can either of you briefly comment on that?

Mr. FOX. I don't have any metrics for you today. What I will tell you is this is a great concern of ours, and there are a number of ways to address it.

I think we have a problem here in this country, particularly over the last year, with a phenomenon that we are calling defensive filing. It is where institutions are filing to protect themselves from any regulatory or reputational risks that is associated with some adverse action.

I think it is very important for us also from a regulator's standpoint to try to point the institutions in the right direction.

If I can give you a trite example that I am not prepared to implement yet, but I am just about ready to, I think, every morning on my machine at FinCEN I get an e-mail from a Nigerian fraud scam. I am sure we have all seen them, and we have a number of suspicious activity reports that relate to Nigerian fraud scams. It is clearly suspicious activity. It would fall within the bounds of our current regime for reporting, but I think law enforcement generally, particularly at the Federal level, has decided that unless there is some real pecuniary loss on the part of a person, that we are just all going to get smart about it by educating our public who these messages are aimed at. You know, it is kind of a financial literacy issue to be honest with you.

I would think we would get much better bang for our buck if we educate the public about these scams, tell them to ignore them, tell them to delete the e-mail, and then tell institutions don't waste your time reporting on Nigerian fraud scams; we would rather have information about X, Y, or Z.

I think we have to get much better at sharpening the reporting on suspicious activity and I think it will only make it more relevant and more robust, and we will get more reports that are of higher value.

Mr. DAVIS OF ALABAMA. Thank you.

Mr. MOREHART. May I add to that, please?

Chairwoman KELLY. Please do.

Mr. MOREHART. I think I can give you at least a metric that will sort of answer the question, sir, in terms of SAR usage and how we view that. We haven't done a study in terms of how many cases have been opened, how many cases have been advanced as a result of that.

However, of the data we have, as I mentioned, we have about 63 million BSA documents in our Investigative Data Warehouse. For SARs specifically, we have approximately 1.7 million documents in that database. We ran that database against the FBI's databases for references and main subjects. We came back with 5.7 million hits, i.e., IDENTS against 1.7 million documents. Again, I cannot specify which ones of those resulted in case openings or resolutions or that kind of thing, but I strongly suggest that that information is of great value.

Let me just define hits again. It is for example an individual compared to the BSA data, you would get a hit or not. So there may be more than one individual listed on a SAR for example. That is why you might have more hits than there are actual documents, but these statistics in metrics would tend to suggest that that information is of extreme value to our investigators out in the field.

Chairwoman KELLY. Thank you very much, Mr. Morehart.

Mr. Cleaver, have you any questions for this panel?

Mr. CLEAVER. No.

Chairwoman KELLY. Thank you. As you know, gentlemen, this subcommittee has been looking very closely at actions taken by the OCC with regard to the Arab Bank's New York City branch.

In respecting the limitations on what can be said at the moment because this is an ongoing investigation, I would like to hear more about how our government is responding to some of the serious concerns that have been raised there. In this subcommittee's last hearing, Under Secretary Levey talked in detail about the issue and said that OCC and FinCEN were working together on the case.

So I am wondering if you could elaborate as to how the different entities within the Treasury are working together to address the issue.

In addition to OCC and FinCEN, I have read reports that OFAC has been involved, and it might be useful for us to hear which entities are involved and what they are doing and how they are working together to make sure that there is a fair and effective response from the government, yet we as the citizens are protected.

I would also like to hear your perspective as to where this particular situation might fall within the context of our ongoing efforts to combat money laundering and terror finance. What does it mean to the important issue that we are really addressing here today? Does it illuminate any of the systemic weaknesses in our regulatory regime and are we working, having found that information, to fix those?

I know those are several questions. I'll start with you, Mr. Fox.

Mr. FOX. Thank you. You are right, Madam Chairwoman. There is really not much I can say at the table today in this forum about this matter because it is an active and ongoing matter with our of-

fice. The only thing I can tell you is that we are working very closely with the agencies that you identified to ensure, as we have said previously this morning, that if an action is actually taken, it will be coordinated and it will achieve the purpose of the action, which is compliance with the regime, greater financial transparency, and to ensure that the U.S. Financial system is at least protected from the threats of money laundering and terrorist financing.

So we are working very hard to resolve the matter. We think it is in everyone's interest to resolve it quickly or as quickly as possible, and we are working very, very closely with, and again I am happy to report we have received very good cooperation from, all the agencies that you mentioned.

Chairwoman KELLY. Thank you. Mr. Fox, during the 1990's, FinCEN was described fairly or not as the elephant graveyard of the U.S. Treasury Department. I have had the opportunity to work with a number of very talented and very intelligent FinCEN employees who are so smart, I really am very impressed with the quality of what has been happening at FinCEN. I wonder if you would describe for the committee your agency's recruitment process and your work on building a sense of mission.

Mr. FOX. Thank you, ma'am. I will take that compliment. We are trying very, very hard to develop FinCEN into what I believe it can be, and that is a model of a financial intelligence unit as that concept is conceived.

FinCEN is a relatively young organization. It began in 1990 as sort of a law enforcement fusion center. In fact, it is not odd that FinCEN is new. Our money laundering laws have only been around since 1985. The Bank Secrecy Act has only been around since 1970. So I think the issues revolving around financial crime have been relatively new developments in this area.

FinCEN has worn some different hats and I appreciate your characterization because I have heard that as well. Again, it started out as sort of a fusion center. During the mid-1990's, FinCEN was instrumental frankly in the development of the FATF as a robust, international body. Also, FinCEN was one of the six founding members of the Egmont Group, which has now expanded to 102 members from around the world of financial intelligence units sharing key, relevant information to further the investigation and detection and prevention of financial crime. I think those were incredibly noble efforts and very important.

Recently, one characterization I have heard about FinCEN is that FinCEN is a library. It houses BSA data and its analysts are essentially librarians that help law enforcement sort of get at the data but do not do much else.

I have to tell you we are changing that. I have redefined the mission at FinCEN to safeguarding our financial system from the abuses of financial crime, and that is a very hard mission to reach but it is one that I think is worth a stretch. And I think what we are really trying to do is to make FinCEN a fully functioning financial intelligence unit.

It is starting to pay off, I think. First of all, we have to remember that FinCEN is also, and maybe the key thing that it is, is the administrator of the Bank Secrecy Act and it is a regulatory agency. If you think about this in intelligence terms, our whole regulatory

effort, in many respects, is that of managing the collection of the information that the Bank Secrecy Act mandates, the reporting that it mandates. I think that is why we have to exercise leadership on the regulatory side and make sure that we are collecting information that is relevant and robust for law enforcement.

On the analytic side, ma'am, I will tell you that it is my goal to make our analysts the best financial analysts in the world. I have with me today something that we published recently. It is a document that I think some of your staff may have. It is not a document for public consumption outside the government, but it's a reference series on wire transfers. I will tell you that we have developed this manual for the benefit of law enforcement and other policy-makers on issues relating to a very key method of moving money, and that is, funds transfers. The feedback we have received has been terrific and we are actually quite proud of it.

I think you will see similar analytic product from us, and we are doing our very best under the constraints of the system to attract the most energetic, highly talented people that we can to try to move the agency into a better place.

Chairwoman KELLY. I thank you for that. You do have a high energy level. It is tough, hard work, but your people are very smart, and I have enjoyed working with them. I hope that continues.

Mr. Morehart, I have a question for you about what this committee has been doing on the Terror Finance Task Force in Congress, and I have been following, we have all been following, the career of Charles Taylor very closely. We are concerned that he has not been brought to justice. The FBI promised to establish an office to help us bring Charles Taylor to justice and to stem the flow of terrorists in West Africa, but our information so far is that this office has not been established.

I want to know if you can tell the committee whether you are actively assisting in the effort to bring Charles Taylor and that criminal conspiracy that he is in charge of to justice.

Mr. MOREHART. Yes, ma'am. In terms of the LEGAT, if you will, the legal attache that is to be established, I am not familiar with the status of that, but we can find that out for you. That is in a different section, if you will, a division than is under my purview.

In terms of the investigation of terrorists, if you will, on the whole, from public documents obviously I have kept up with this issue and otherwise, and I think the suggestion is that Mr. Taylor is perhaps not a terrorist in and of himself but somewhat of a facilitator if you could characterize it that way, other than perhaps obviously the war crimes and those kinds of things, if you would define those as a terrorist, but there have been allegations obviously publicized that he has been facilitating, for example, al Qaeda's negotiation of conflict diamonds and those kind of things.

Obviously, we are very interested in any information that anyone would provide us that would allow us to further that type of investigation to bring that individual to justice. I cannot say that I am involved in every aspect of what might be going on in that realm. However, I will say from a terrorist financing standpoint, my section, my division, the Counterterrorism Division, obviously is very, very concerned with any terrorists, any facilitator, or any individual and/or entity that wittingly supports those types of individ-

uals. So we are making every effort to do everything we can, not only in that realm but quite candidly every other realm where there is a threat.

Chairwoman KELLY. Well, thank you, Mr. Morehart. I am extremely concerned about the Charles Taylor case. We have good people who have put their lives on the line whose lives are really literally under the gun, and until we move Charles Taylor to justice those people are under great threat. We owe them a debt of gratitude for what they have done. It is extremely important, and I would like very much to have you give me back that information. This committee is very interested in this issue.

I would like to go back to you, Director Fox, and ask you a question about what steps—first of all, let me just say, I want to know if you can discuss the completion of BSA Direct and how that is going to improve the security of the SARs but also what steps you are taking in response to the IG report on data security. That is a big issue we need to quickly address.

Mr. FOX. Thank you, ma'am. BSA Direct, as the committee knows, is probably the highest priority for my agency because it will form the platform through which we will eventually collect all of the BSA data, house it, analyze it and disseminate it, even in the extraordinary circumstance of some key law enforcement partners like the FBI.

It will house feedback and information about how the data is being used, and it will also provide us with the security to ensure the data so that we know who is hitting it.

This system will provide law enforcement, at the State and Federal level, with a very modern and robust data query and mining system. So we are moving very, very quickly. We are building the heart of that system now, a modern data warehouse that will be completed this October, and that will take care of sort of the dissemination end of the data.

We have also an E-file system that will connect to BSA Direct. We are building BSA Direct in a way that all of these different components, whether it is our E-file system, or what we used to call Gateway, where we captured information about those people who are hitting the data, all of those components will be knitted into one solid project.

I think having the entity that is responsible for administering the act, for collecting the data, for disseminating the data, in charge of the data, makes perfect sense. If there is then a problem, you can hold me directly accountable and you should because this data is very sensitive with serious privacy concerns. I think it is not something that should be dispersed across agencies of the government.

We are moving with all speed that we can muster, based on funding and other issues, to get this system completely built so that we can then control the data from collection all the way through to dissemination.

Chairwoman KELLY. I want to thank you very much for responding with great strength to that. That security is extremely important.

I also want to thank you for the guidance that you sent out to the delegated examining agencies and the work that the BSAAG is

doing to make the BSA process more effective and user friendly. I am concerned that OFAC is not a member of the BSAAG. Given the complementary nature of their missions and the institutions that are affected by their missions, I am wondering why OFAC is not a member of this.

Mr. FOX. The Bank Secrecy Act Advisory Group, as you know, is a statutorily created body. It is really a gift from this committee and the Congress. I will tell you I think it is one of the most effective government/private partnerships that I have ever been a part of. I served on some other advisory committees and because of the exemption from the FACA you actually can have robust conversations, real conversations, candid conversations on key policy issues.

One of the things the BSAAG is tackling, ma'am, is this issue about CTRs and whether or not we have too many of them and how we can get rid of the obvious ones that none of us are really interested in, the McDonalds and the Wal-Marts.

Turning to your specific question about OFAC, I know in the interest of time we would be happy to expand on this too if you want for the record, but the BSAAG was technically created to address issues relating to the Bank Secrecy Act, and OFAC does not have any direct responsibilities relating to the Bank Secrecy Act.

I suspect, ma'am, if you ask Director Warner about whether or not he would love to have a similar entity to deal with issues relating to sanctions, I think he would be very keen to do that. I don't want to presume to speak for him, but I think we all recognize the value of having the government as a whole, regulators, policy-makers, law enforcement, meeting with affected regulated industry and working.

So I think we are actually probably constrained from having OFAC participate on that issue, but we can look at that as well.

Chairwoman KELLY. You know, yesterday, this committee voted for legislation that required the GSEs to report suspected activity or financial crimes that they thought they were experiencing. Are you working with OFHEO to provide the kind of necessary assistance for that, and are you going to be working with the new Federal housing finance authority if it is passed into law to establish a robust system there. Will you be working with them?

Mr. FOX. Yes, ma'am, absolutely. I think we have in the past and I think we will continue to do so. I will tell you that none other than the Deputy Attorney General has brought this to my plate about the concerns that the Justice Department and the FBI have about mortgage fraud, as does the industry by the way.

I think the key thing about that provision of law is that we make sure that reporting, when it does occur, is accessible to all of law enforcement and we can actually put that to good use. So we would be happy to work with the committee, and OFHEO, and the new regulator if it is created to make sure that this happens. It is a very important problem that we are aware of and it needs to be addressed.

Chairwoman KELLY. Good. I am glad to here that. Mr. Cleaver, you have a question now.

Mr. CLEAVER. Director Fox, I apologize for coming in late. I am a new Member and still trying to find my way around, and I ended up at the Spy Museum. So excuse me.

Is EDS now under contract to build BSA Direct?

Mr. FOX. Yes, sir.

Mr. CLEAVER. Now, is there any concern over the cost? The IG found that Treasury's HR Connect is up and running at $173 million, and I mean the cost is Herculean compared to the work they have done for the Coast Guard and Agriculture. Is there a reason for this?

Mr. FOX. Well, sir, I can't comment on the HR Connect issue. I am vaguely aware of it, being a Treasury official and being a user of the HR Connect system. It actually works pretty well now, gladly. I am not sure that EDS was the contractor for HR Connect, it may have been, I don't know whether they were or not.

Mr. CLEAVER. Does anybody?

Mr. FOX. We can get back to you certainly with that and let you know that.

I will tell you that we are pleased so far with the progress on our BSA Direct project, and we believe that we are building this system at a very reasonable price. I think to build the heart of this system, just to build the heart of it is less than $10 million. That is still, to me, an awful lot of money but I think when you compare it with other systems, it is a pretty reasonable deal and we are on target, sir.

So I think the system as a whole over 5 years, including maintenance and operations, I think is a little over $18 million. I think we all agree, in fact we have gotten a lot of push back from folks saying you are trying to do this too cheaply, and I think we can do it well and do it keeping in mind that we are stewards of the taxpayers' money here.

Mr. CLEAVER. Well, is there anyone from your staff here—I mean, maybe you will have to get back with me to find out further—to talk about the HR Connect.

Mr. FOX. What I can do, sir, is we can certainly—we don't actually own that system but I think the Treasury's Chief Information Officer, Ira Hobbs, is the owner of that system. I am more than happy to let Mr. Hobbs know you are interested in this and maybe they could come up and provide you a briefing. I am more than happy to convey your question.

Chairwoman KELLY. Mr. Cleaver, we will follow up on that and get the appropriate person to respond to that question.

Mr. CLEAVER. Thank you.

Chairwoman KELLY. Mr. Scott, you have another question?

Mr. SCOTT. Yes, I do, Chairwoman. Thank you.

I want to talk for a moment, Mr. Fox, about the situation over at Treasury. First of all, you are doing a great job.

Mr. FOX. Thank you, sir.

Mr. SCOTT. But there has been a failure to make some key personnel appointments over there. I think you have an Assistant Secretary Zarate, I believe is his name, who is leaving soon. There is an Assistant Secretary under the Under Secretary that has not been appointed. I am wondering what impact is this having on your being able to do your job and is help on the way here?

Mr. FOX. Without knowing, sir, because it is a process that I am not intimately involved in or even familiar with, but I will tell you that it is my understanding that help is on the way, and it will be

welcome help. It is a big loss for the Treasury Department to lose Assistant Secretary Zarate. He has been a leader on issues relating to terrorist financing and financial crime.

I worked shoulder-to-shoulder with Juan after September 11th, and I think actually the country will be served well by him as Deputy National Security Adviser. I think he is really a significant talent.

Having said that, I know that Under Secretary Levey, who is the leader for terrorism and financial intelligence and we report to, he is doing an outstanding job of keeping everything together, even given the vacancies. I believe Janice Gardner, who is the current Deputy Assistant Secretary in charge of intelligence has been nominated for the position of Assistant Secretary for Intelligence. Janice is wonderful and we are working very closely with her and coordinating her office's work with our office's work. So, actually, from our little corner of the Treasury Department things are going well.

I used to be at Treasury and I know that there are vacancies, and those vacancies do cause concern, but I think the Secretary is doing everything he can to get them filled as quickly as possible, and I know he is working very hard to move that process forward.

Mr. SCOTT. I think you are, too, and I want to take a moment, before I finish my last part of my question, to compliment our chairwoman here, Mrs. Kelly, for taking the leadership. I think that we are at the front line on this fight on terror because the only way we are going to end this war is to get our hands around the financing of it, and so Chairlady, I certainly want to compliment you for the excellent job we are doing on this committee.

Let me go back to you, Mr. Morehart. I left off with the last part of my question on the hawalas, and since I have been on this committee I have been trying to follow that. I have been trying to illuminate more information because I believe that therein with the hawalas and that sort of cultural way for many years of many of the Arab speaking people who are here and other parts of the world are transporting funds back, they have been doing it sort of for their families, but tell us how serious that is. We know there is a serious element to it. It appears to me that there is some sensitivity to handling it because there is some legitimacy to the Arabs' argument that that is used as a way of getting moneys back to the families, and as a matter of fact, many of their leading spokespersons are saying that this is harassment against us.

Wherein lies the truth here? How serious is the hawala problem, and as much as you can share with us—we don't want you to give too much information. We are not the only ones paying attention here, but do we have a handle on it? Is it the threat that it is and what is the FBI doing about it? And in that line, what kind of cooperation are we getting from the Arab world?

Mr. MOREHART. Well, I think the first thing that needs to be recognized is that a hawala is not necessarily an illegal thing. A hawala is simply a method to informally transfer value; i.e., money, and those have been in existence under different names and different regions of the world for hundreds if not thousands of years to conduct that business.

Now I think the issue, of course, here, sir, is what threat does that represent to us in terms of terrorism, if I might characterize it that way. That is difficult to answer candidly. I think there are a lot of issues that we are attempting to resolve, and one of those issues we brought up a little while ago was in terms of MSBs and you might consider an hawala an MSB, is it registered or not.

A lot of times I think that people would assume those type of activities are illegal and, as I mentioned, they are not necessarily illegal. Those things have been established for many, many years and have worked very well for those particular cultures that use them.

Now are they of concern? Certainly they are of concern. Any type of value transfer system that might be used by terrorists or their facilitators is of concern to us. They can be used for laundering perhaps. They can be used to transfer money if they are not registered.

Mr. SCOTT. Let me just ask this point because we have a vote to get to. You are using words like might, maybe, they are. Do we have any concrete evidence that any hawalas are being used to finance terrorist operations?

Mr. MOREHART. Sir, I hesitate to answer the questions in open forum because I probably would have to give examples. I will say this. I don't know the characterization that they are being used to finance is accurate. Being used to move money to facilitate is probably a more apt description. I know it is somewhat semantics, but it is important because typically these are middleman who move money or middlewomen who move money depending upon the circumstances.

As in any other situation, I think the key here is, one, are they registered in accordance with our laws? If not, they should be. We are concerned if there are methods of moving money out there obviously that we have not detected, and I think that is the more important issue for us to discover, whether it is through hawala or through cash couriers or through some other method. That is the primary issue we are concerned about.

Are we working towards identifying those things? Certainly. Every single day. We have a number of projects underway where we are trying to identify those things, and I will emphasize again, as I mentioned earlier, the Bank Secrecy Act data which we are given allows us to do that analysis, allows us to do that patterndetection which might then identify that type of activity which then might either wittingly or unwittingly be utilized to move money to terrorists.

Mr. SCOTT. Thank you.

Chairwoman KELLY. Thank you. We have been called for a vote. I want to remind this panel that, without objection, your full written statements will be made part of the record and the Chair notes that some members may have additional questions for the panel which they may wish to submit in writing. So, without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

I appreciate very much your time, your patience here, gentlemen. I hope that the financial industry has an ear into what you have said. It appears to me that this is beginning to be effective, and I

appreciate the hard work on the part of both of you but also the people in your agencies. We are all safer because of it, I believe.

With that, this panel is excused, and I am going to recess this committee until we are able—we have two votes. It will possibly be 20 to 30 minutes before we will reconvene for the second panel.

[Recess.]

Chairwoman KELLY. Our second panel this afternoon consists of Superintendent Diana Taylor of the New York Banking Department, John Byrne of the ABA, Scott McClain of the Financial Service Centers of America, and Joseph Cachey of Western Union.

Chairwoman KELLY. Ms. Taylor, I am delighted to have you here. You represent my State of New York, and you have served as Superintendent of Banks for New York since 2003.

Ms. Taylor has more than 20 years of experience serving in both the public and private sectors. She most recently held the position of Deputy Secretary for Finance and Housing to Governor Pataki. Prior to that she served as Chief Financial Officer for the Long Island Power Authority, a company with annual revenues of $2.4 billion and assets of approximately $8 billion.

I think we will start with you. I can't find the rest of what I have here. I am just going to go ahead and say we will start with you, Ms. Taylor.

Without objection, your written statements will be made part of the record. You each will have 5 minutes in which to make a summary of your testimony. Let us start with you, Ms. Taylor.

STATEMENT OF DIANA TAYLOR, SUPERINTENDENT OF BANKS, NEW YORK STATE BANKING DEPARTMENT

Ms. TAYLOR. Thank you, Madam Chairwoman. Good morning, Chairwoman Kelly and other members of the committee. Thank you for holding this hearing on an issue that is of great interest to us, those who oversee the financial services industry at the State level.

It is interesting being on a panel with some of those we oversee as opposed to being on a government panel. We are all very concerned about the sometimes conflicting priorities of regulation, law enforcement and the ability of necessary businesses to operate. I would like to address the three points you mentioned in your letter.

First, as you heard earlier this morning, FinCEN and the Federal banking servicers have received crucial guidance on BSA/AML compliance for banks doing business such as MSBs, such as check cashers and money transmitters. This welcome development promises a strong step in the direction of clarifying for the banks their BSA/AML requirements with respect to money service customers.

One very important issue that was made clear in the guidance is that banks are not expected to become or act as MSB regulators. At the same time, separate guidance was issued by FinCEN to MSBs clarifying their BSA/AML requirements.

Significant progress has been made toward a plan to achieve a coordinated approach among the regulators. Over the winter, the Conference of State Banking Supervisors worked diligently with all of the States, our Federal bank regulatory counterparts, FinCEN and the IRS to produce two model memoranda of understanding setting forth procedures for the exchange of certain BSA informa-

tion between the States and FinCEN and the IRS concerning bank and MSB examination and information respectively. This is great progress.

New York was the first State to sign on. On June 1st, more than 30 States plan to take part in an MOU signing ceremony at the CSBS annual meeting.

A very important aspect of our agreement is that the States will receive analytical tools from FinCEN that will maximize resources and highlight areas and businesses with higher risk for money laundering. The agreement with the IRS will allow for examination sharing to reduce duplicative efforts and establish an ongoing working relationship. This is an unprecedented cooperative agreement, as it acknowledges that State regulators are an important part of the solution. We have all recognized that no one of us can be effective in this area without the others.

Both FinCEN and the IRS have been exceptionally cooperative in this endeavor, and I will be happy to keep you and your committee informed on how this cooperation continues.

With regard to the second issue you highlighted in your letter—challenges we are facing with regard to BSA/AML compliance in the MSB area—you are, of course, already aware of the fact that many banks have decided not to do business with MSBs as a result of the BSA compliance issues. The guidance and MOUs I just referred to will hopefully ameliorate this issue. We will keep you informed on this also.

But there are other challenges. One that is particularly worrisome to us is the issue of who, if anyone, should regulate the agents that the MSBs employ to do their business; and if so, what should that regulation entail? Mr. Fox touched on this a little bit in his answer to Mr. Royce's question earlier this morning.

In New York State, there are approximately 73 money transmitters, but there are 29,000 agents. Clearly, regulating them would be an enormous task, not to mention what to do about the hundreds of thousands of nonbank ATM machines in the State.

Then there is the issue of SARs. In the current environment, financial institutions are worried that they will be punished severely for seemingly minor infractions, even when they have a history of operating responsibly and have or are developing state-of-the-art compliance systems. We need to realize now that there is no system in the world that is going to catch every single instance of illegal activity. The only way to do that is to shut down the whole system.

For regulators, the goal is to prevent and detect criminal activity, not to close down financial institutions. We regulators have a long way to go in coordinating and communicating with law enforcement. We need to make sure that everyone understands the standards to which we are being held and that those standards make sense.

We are all united in our concern over choking off the supply of money to terrorists and other criminal elements. This is a critical task.

We need to work together to make sure that the laws are having the intended consequences, which are to stop and punish criminal

and terrorist activities but at the same time to allow our financial system to operate efficiently and effectively.

The third issue that you mentioned was interaction with the IRS when monitoring MSBs. We are looking forward to building our relationship with the IRS with regard to MSB supervision. As we are just now beginning this cooperative arrangement, I cannot give a progress report at this point, except to say, so far so good. However, I am looking forward to giving you a progress report of our accomplishments and mutual achievements when we have developed a track record.

The lesson that is learned is that to have a real and lasting effect on illegal activity it is essential that the agencies involved in the regulatory, investigative and enforcement framework for banks proactively cooperate with each other.

Just as we have forged an MOU between the States, the Federal banking agencies, FinCEN and the IRS, I think we need to come to an understanding, perhaps an MOU, with the Department of Justice so that its actions and those of the U.S. attorneys are not at cross purposes to those of the regulators. We must brainstorm together to find a way to allow our financial system to operate efficiently and effectively while also preventing its use for criminal purposes. To achieve this crucial goal we must all work together.

Thank you.

[The prepared statement of Ms. Taylor can be found on page 83 of the appendix.]

Chairwoman KELLY. Thank you, Ms. Taylor. I in particular want to applaud your working with FinCEN in a very forward thinking manner.

We turn to you, Mr. Byrne.

STATEMENT OF JOHN J. BYRNE, DIRECTOR, CENTER FOR COMPLIANCE, AMERICAN BANKERS ASSOCIATION

Mr. BYRNE. Subcommittee Chairwoman Kelly, members of the subcommittee, ABA appreciates this opportunity to discuss how the financial industry is addressing many of the compliance issues with suspicious activity reporting and the challenges of providing bank services to money services businesses. As we told this subcommittee on May 4th, there has been clear movement and commitment for further action from the highest levels of the Federal banking agencies for a uniform approach to BSA compliance.

However, ABA would again remind the subcommittee that the industry remains concerned about the quality of communication that exists between these same agencies and the field examiners. In fact, we will highlight one particular issue that occurred after the May 4th hearing to emphasize our concern. We do, however, remain optimistic that the commitment mentioned above is real and will resolve the issues quickly.

Your May 20th letter of invitation asks us to address three issues, an update on what is being done to standardize BSA compliance challenges, why the industry is engaged in defensive filing of suspicious activity reports and what BSA compliance concerns are associated with MSBs.

I will take the three issues together. The pending interagency exam procedures will provide an opportunity for both the industry

and the Federal banking agencies to work together to prevent confusion and second guessing. We urge Congress to seek an update on the practical effect of these procedures in early 2006.

As we told the subcommittee earlier this month, it is counterproductive to label an entity high risk without also issuing guidance on how to mitigate that risk. The agencies finally agreed with us and produced an interagency guidance on working with MSBs.

I must take issue with my friend, Mr. Fox, who said it was a misperception on the part of the banking industry. It was no misperception, it was comments from field examiners who told us to eliminate these accounts because they were in fact high risk. The good news is we have the interagency guidance. While it is early for a complete assessment, the direction of the guidance is a strong first step for clarity.

Defense of SAR filings are the result of the dearth of useful guidance and the lack of a balanced approach to examiner oversight. The Federal banking agencies must insist that their field examiners not second guess SAR decisions made by the financial sector or the volume of SARs will continue to skyrocket.

Madam Chairwoman, the uniform exam procedures scheduled for a June 30th release date will assist the industry concerns about exam inconsistency and the continued threat of zero tolerance by these same errant examiners. We strongly urge Congress to ensure that all banking agencies engage in industry outreach when the procedures are made public. The agencies appear committed to this outreach, and we believe that a nationwide series of town hall meeting events will ensure that both sides will know what to expect in this complicated compliance area.

A major challenge facing the banking industry has been how to fulfill our obligations regarding appropriate relationships with MSBs. We understand and appreciate the need to analyze the level of risk involved with maintaining these relationships. We know the importance of providing services to all segments of society.

For some, the remittance services that MSBs frequently provide are an essential financial product. Remittance flows are an important and stable source of funds for many countries and constitute a substantial part of financial inflows for countries that have a large migrant labor force working abroad.

The problem, however, is how much analysis is sufficient. At times banks appropriately exit relationships due to the risks inherent with the particular MSB. At other times we want to continue those valued relationships. The agencies again did issue an interagency policy statement on March 30th and sorely needed guidance on April 26th. The guidance now must be clearly communicated to the examiners.

I would like to report that at least one large southwestern bank reported to ABA that its current BSA exam showed that that oversight agency was well versed in the MSBs guidance. This is indeed a positive sign.

Finally, with the increased number of entities required to file SARs as well as a heightened scrutiny on SARs regulators and programs, it is essential for the regulatory's law enforcement and FinCEN to assist filers with issues as they arise.

As stated above, there are several problems affecting banks and the AML process related to SARs. ABA has previously mentioned the many examples of examiner criticisms received by our members during reviews of their SARs programs. Whether it has been criticized for the number of SARs filed or the second guessing by examiners as to why a SARs was not filed, we remind Congress that this situation demands immediate attention.

Regulatory scrutiny of SARs filings has caused many institutions to file defensively to stave off unwarranted criticism or second guessing. In fact, The American Banker reported that in March of 2005 the industry filed 43,000 SARs, a 40 percent increase from a year earlier. That is not because there is more criminal activity.

We would like to commend Director Fox for addressing our previous recommendations made in 2004 by creating a Bank Secrecy Act subcommittee to look at SARs issues. I would note that we have already held the first meeting, and the defensive issue of filings is a top priority. Our members continue to express their concern on the rampant second guessing that continues.

For example, just last week a bank told us that it had extensive documentation on why it had not filed a SAR, only to be told by the examiner that it must file. This example—which is not isolated—is a major reason why banks feel they have no other option but to err on the side of filing. Our hope continues to be that the exam procedures and additional interpretation on SAR issues will result in returning SARs to their original place, forms filed only after careful analysis and investigation with no second guessing by regulators.

We commend the Treasury Department, the banking agencies and FinCEN for their recent efforts to ensure a workable and efficient process. We will continue to support those efforts, and we would be happy to answer any questions.

[The prepared statement of Mr. Byrne can be found on page 46 of the appendix.]

Mr. PAUL. [presiding] Thank you, Mr. Byrne.

We will move next to Mr. Joseph Cachey, Compliance Chief, Western Union Financial Services, for your statement.

STATEMENT OF JOSEPH CACHEY, III, COMPLIANCE CHIEF, WESTERN UNION FINANCIAL SERVICES, INC.

Mr. CACHEY. Thank you. Good morning, I would like to thank this subcommittee on behalf of Western Union for the opportunity to address this important topic. Since the use of suspicious activity reporting regulations took effect for money services businesses just 3 years ago in January of 2002, Western Union has created an industry leading compliance program in a relatively short period of time.

Today I would like to discuss an important part of that anti-laundering compliance program, suspicious activity reporting and our dealings with law enforcement based on those reports which we filed.

Western Union files tens of thousands of Suspicious Activity Reports, or SARs, each year, representing a small fraction of our total number of transactions. We know that SARs lead to investigations, because there is direct follow-up from law enforcement for a num-

ber of these reports that we file. The filings may lead to a number of actions taken in conjunction with law enforcement. I would just like to cite a few examples.

Last year, Western Union, based on our internal suspicious activity filing criteria, filed six SARs on four customers who were receiving transaction in what most of us would consider higher risk countries. These SARs resulted in the opening of an expansive investigation, now being conducted by two Federal agencies.

Western Union continues to support these investigative efforts by responding to subpoenas targeting the identified customer transactions, and in addition we share emerging insights on these customers' money transfer patterns involving the investigation subjects.

Western Union also cooperates with Federal law enforcement efforts through agreements that assure certain agent locations are kept open during an ongoing investigation. For example, the owner of a Western Union agent location in the Midwest was indicted this past April on 43 counts of money laundering after a 5-year investigation. It was Western Union's agreement to keep that location open and not terminate our relationship with that agent, which would have been our typical business practice that allowed law enforcement to gather sufficient evidence to come forward with these indictments.

As is typical though with money laundering schemes, risks—and these are all risk-based programs, as Director Fox mentioned earlier this morning—may shift as we all obtain more information and analyze that information.

For the industry to better focus its resources, the regulator in this case, FinCEN, must provide ongoing communication to industry about emerging risks and money laundering patterns so that we can direct our compliance efforts towards the most critical areas of risk.

By not giving us the guidance, we do tend to overfile on things that may not be helpful with law enforcement and create a lot of "noise in the system".

One primary example of this potential noise is the reporting of simple structuring. The majority of SARs Western Union files report low-level structuring activity, that is individuals that come in—and we suspect—are trying to avoid information at the $3,000 transaction level which is required by the Bank Secrecy Act.

Frankly speaking, we believe that most of this activity does not result from an evil intent, but from the average American's unwillingness to share their Social Security number and other sensitive personal information with a third party. Together, we need to question whether financial institutions reporting activity at this low level is helpful to law enforcement.

A word on defensive filing of SARs. As we discussed, a big issue for MSBs is the filing of a SAR to report low-level structuring. Such filing is not defensive because structuring for any reason is technically a crime.

But while such a reporting is not defensive, it may not be all that helpful to law enforcement. There has to be a better approach. Much of the guidance given on filing SARs is too broad in today's regulatory environment. Creating gray areas leads to more SARs

filings. One example of this is what we call high-volume customers, individuals that send significant portions of money through our system. Western Union strives to identify and learn more about these customers, typically telephonically.

But what do we do if a customer doesn't return our phone call. Should we file a SAR not knowing anything else about that customer activity? Many State examiners' position appears to be if you can't prove that the consumer is wholly innocent, then they are guilty, file the SAR. This attitude leads to excessive SAR filings because it follows the more equals better approach.

Western Union is attempting to build a more surgical approach in its SAR filings to provide quality information, not more information. We hope that law enforcement and the regulatory community would support that approach. Thank you very much.

[The prepared statement of Mr. Cachey can be found on page 54 of the appendix.]

Mr. PAUL. Thank you, Mr. Cachey.

We will move to the next panelist, Mr. Scott McClain from Financial Service Centers of America.

You can go ahead with your statement.

STATEMENT OF SCOTT K. McCLAIN, WINNE, BANTA, HETHERINGTON BASRALIAN, P.C., REPRESENTING THE FINANCIAL CENTERS OF AMERICA, INC.

Mr. MCCLAIN. Thank you very much. Members of the subcommittee, I am very grateful for the opportunity to be here today to discuss BSA compliance issues involving the community financial services and check cashing industry.

FiSCA is a national trade association representing over 5,000 neighborhood financial service providers throughout the United States. We provide a range of services and products to our customers, including check cashing, money order sales, money transfers and utility bill payments.

Our members are classified under the Bank Secrecy Act as money services businesses. U.S. Treasury Secretary John Snow acknowledged in a recent address to the Florida Bankers Association that MSBs are key components of a healthy financial sector, and it is very important that they have access to banking services.

In short we serve the local communities of the United States, we serve the working man and woman, and we are very much a part of the mainstream of a healthy financial industry. We are committed to the fight against money laundering, and our industry has committed significant resources in this regard.

In 1993, we issued the first compliance manuals for its nonbank financial services industry. Following passage of the USA PATRIOT Act, FiSCA issued an anti-money laundering complaints program to assist the industry in meeting new requirements under the PATRIOT Act. Most recently in 2004, FiSCA launched an Internet-based compliance training and examination program which includes courses for both MSB tellers and compliance officers. To date, approximately 6,000 MSB employees in more than a dozen States have sat for the online courses and examination. We hope to double the program's performance in 2005.

The check cashing and MSB industry suffers greatly from the perception that we are inordinately high-risk as compared with other financial institutions or businesses. It would appear that this conclusion has been reached by Federal bank examiners and adopted unfortunately by banks with little attention to the actual compliance record. This has resulted in a staggering number of banks terminating services to the entire industry and has caused thousands of check cashers to scramble to find new banks among an already limited number. As we had witnessed time and again, when banks have terminated their check cashing customers due to compliance problems, it is more likely that the compliance problem is with the bank than with the MSB customers.

This point was underscored by the recent enforcement actions against AmSouth and Beach Bank in Florida. In each case, the bank was cited for substantial regulatory violations unrelated to the activities of its check cashing customers. Yet in each case the bank responded by terminating all of their check casher accounts. The fact is check cashers are simply not good vehicles for money laundering. They do not take deposits and the dollar amount of the transactions are typically low. They are subject to stringent and far-reaching controls.

In our experience the current BSA reporting system has been largely effective. Certain reporting issues should be addressed, and we are happy to work with the committee in this regard.

First with regard to suspicious activity reporting requirements, we recognize that reliable MSB SAR data is key in the battle against money laundering and financial crime. We are concerned that the current SAR form may be unduly complicated for the typical business. Better guidance is also required for the SAR narrative section in order to maximize the data collection. As well, the SAR reporting thresholds should be reconsidered.

Office of Foreign Assets Compliance continues to be a confusing problem. There is need for OFAC guidance concerning risk assessments in regards to this industry. Although IRS has greatly improved the level of education of its agents relating to MSB examinations, there is clearly a need for consistency in the examination process. Most importantly, there must be a process for communication between the community financial services industry and the banking industry.

They are subject to many of the same AML requirements yet seem to be operating in separate tracks. Although the FinCEN guidelines concern services to MSB, MSBs are a step in the right direction. We know of no banks which have reconsidered or are willing to entertain the service industry. We attempted to bridge the gap in this regard. Obviously, it is in our best interest to cause the banking industry to be reassured that servicing check cashers is both safe and profitable.

Additionally, it is critical that the recent FinCEN guidelines be evaluated. FiSCA will be hosting on September 26th the forum to discuss the guidelines and to determine whether they have stanched the flow of banks leaving the industry and hopefully reassured the others to return.

We intend to invite not only MSBs but also the banks, key banking regulators and decisionmakers, who will ultimately determine

whether the guidelines have achieved their purpose. We ask for your support in this process.

In conclusion, it is critically important that we protect the integrity and legitimacy of our industry. It is equally critical, however, that our industry be recognized as being part of a healthy financial industry and a partner in the war on financial crime. We again thank you for your time today, and I am happy to answer any questions you may have.

[The prepared statement of Mr. McClain can be found on page 73 of the appendix.]

Mr. PAUL. Thank you very much for your statement. Before I make a brief statement and ask a brief question, I would like to ask unanimous consent enter into the record a statement for the Center for Financial Privacy and Human Rights.

From what I hear from the testimony, this is not exactly cost free. There is a cost for what we are doing, a burden placed on the financial industry. I also hear that there is a bit of inefficiency in doing what we do, too many reports being filed and overburdening law enforcement. Then we do talk about, sometimes, the question of law enforcement benefit that we get from this, assuming—it is generally assumed when we talk about the law enforcement benefits that we would not have those if we didn't have this burden and that this is a permissible cause.

The one issue that I think that we are careless about—and I want to get your opinion about this—is the concern for privacy, true privacy. You know, there was a time in this country when we could go to a bank and open up an account and fully assume that this was a private account, that they were like our personal papers held in our household and that we deserved it and our Constitution protects this privacy. I don't think anybody believes that any more, because these are broad nets placed out, all these reports put out. It seems to me like too often it is sort of a bureaucratic overkill in what we are trying to do.

My question is whether or not you think we have gone too far and what would happen if we followed what I consider the rules very strictly. When law enforcement agents suspect there is a problem any place, especially before the PATRIOT Act—you know, one of the things we did was we went to a judge and we asked him permission, and there had to be reasonable cause, and then we went and looked for the evidence that we might need. Today that isn't even considered. It means that we have to look at everybody, everything they do, hoping that we will put it together and catch some criminals, and we sacrifice a bit of our personal liberty.

Is that something that anybody on the panel thinks about, or do you think that—what would happen if we did approach these problems this way? Does anybody care to comment?

Ms. TAYLOR. Yes. Thank you very much for asking that question. I think that, as in all things, there is a balance between the reality of the situation and personal privacy. I totally agree with you that people's financial records ought to be kept as private as possible. That is one reason that SARs are incredibly sensitive, confidential documents. We are not even allowed to say publicly that we are looking at a SAR from a particular institution.

So one of the pillars, if you will, that regulatory oversight is based on is confidentiality. That is one of the reasons why these agreements that we have put together with the Federal agencies have been so painstakingly constructed. Privacy has been at the absolute forefront of everybody's minds, and we need to make sure that private information remains private and that only under circumstances when there is probable cause or some reason to suspect wrongdoing do we actually look into those particular records. Thus, that is something that we are very, very concerned about.

On the other hand, there are terrorists out there, there is money laundering, and we need to have the tools to be able to ferret it out and prosecute it.

Mr. PAUL. Thank you very much. I am a physician, and I think about the responsibilities—I have to keep records private. In some ways your argument would say to the physician, well, you know, there is an important reason—as a matter of fact, this is occurring these days—I can be a little bit careless because if I spread this information about disease we might do some good by doing more research, and we are moving into that direction where medical records aren't very private any more.

So I would suggest that sometimes I think we get rather careless.

Anybody else care to make a comment?

Mr. BYRNE. Congressman, the only point I would make is obviously the banks are somewhat caught in the middle. We obviously have a strong history, we believe, of protecting data. Obviously there are issues with that. We are working hard to address those issues.

But the only point I would make regarding some of the forms, I certainly don't think all of the information is valuable, although we have made that clear. But sometimes the reporting is done on behalf of the bank, so that it can protect itself and the shareholders from the fraud committed against the institution. So in some instances if you left it all to law enforcement, we would lose some of the ability to help our own account holders if they have been defrauded.

There is a balance, but I certainly can recognize your point that the balance seems to have shifted to some degree.

Mr. PAUL. Thank you very much. I now defer to the gentlelady from New York.

Mrs. MALONEY. Thank you, Mr. Chairman. I would like to welcome all of the panelists today and thank you for your testimony very much, but in particular I welcome the superintendent, Diana Taylor, from the great State of New York.

As the financial center of the Nation, New York has been on the leading edge of regulation and enforcement in this area. So your insights and testimony are especially welcomed. Good to see you again, Diana.

Ms. TAYLOR. Thank you.

Mrs. MALONEY. I welcome all the members from the public and private sector in the financial services industry.

I would like to express how pleased I am that the State Banking Department of New York has signed an information sharing agreement with FinCEN. I understand that FinCEN will try to forge

similar agreements with the other States. They are trying hard to do in other States what we have done.

In the meantime, will you work together to share information with the banks about matters such as the wide disparity between States on regulation of money service businesses, the MSBs. I understand that about half a dozen States do not regulate businesses at all, while other States like ours, Superintendent Taylor, have very stringent requirements.

Does your agency directly regulate MSBs, and how do you communicate to banks whether an MSB is in good standing?

Ms. TAYLOR. Thank you for asking that question. It is a very good one, actually. Yes, we do regulate MSBs. We regulate money transmitters and check cashers in the State of New York, among others. We also regulate the mortgage industry, budget planners, in addition to the banks.

We have taken great pains over the last couple of years to beef up our regulation of those entities. We have come up with a new system of looking at them. We have gone from just licensing them and doing minimal examinations to actually looking at them from more of a safety and soundness point of view. Do they have a business plan? Are they financially sound? What are their IT systems like? Are they complying with all of the rules and regulations in the Bank Secrecy Act? What is their management like?

We, through CSBS and through direct efforts with the other States, have worked with the other States on a lot of these things. Anybody who wants to partake of our knowledge of this, we are more than willing to work with them.

We think it is very important that we have standards throughout the country for MSBs that are reasonably consistent, so that MSBs operating in one State don't have advantages, shall we say, over those operating in other States.

Mrs. MALONEY. Have you shared with other States what the standards are that you have for MSBs? Are you working with other States on this? How many other States have followed New York's lead in regulating MSBs?

Ms. TAYLOR. I don't know the answer to that question, but I can certainly get it for you.

Mrs. MALONEY. Thank you so much. It is so good to see you.

Ms. TAYLOR. Thank you.

Mrs. MALONEY. I would like to ask Scott McClain—but I would like to preface it by the fact that at one point I represented a very poor district. It was parts of the South Bronx and East Harlem. Many of the banks left the neighborhood. It is a free enterprise system, but in many cases did not even leave an ATM machine.

I am very supportive to check cashers, really, and to credit unions and anyone who will provide financial service industries in needed neighborhoods. I think that as we work together we can make sure that these services are there for all people throughout our country.

I wanted to ask you, Mr. McClain, in the financial services sector we need to be extremely careful that in the process of combating money laundering we don't unduly burden any sectors of our financial services industry or unfairly advantage one sector over another. I know that your association has been a good citizen in this

respect. You have worked with Treasury's Financial Crimes Enforcement Network, FinCEN, to set up the registration system for the check cashers and the FinCEN website, and your members are registered. You have implemented a four-part anti-money laundering program for your programs that include policies and procedures such as customer verification procedures and the SAR and CTR reporting requirements.

Second, a compliance officer, third, an employee compliance training program and, fourth, an independent audit function. Each of these steps demonstrates that the check cashers you represent are willing to make serious efforts to prevent your businesses from being knowingly used to facilitate money laundering and the financing of terrorism, and that is critical.

In light of these efforts, I can understand your concern and frustration at the increasingly critical problem of banks discontinuing check cashers accounts. This issue came to a crisis point in the city that I represent, when J.P. Morgan Chase announced that it was terminating all check casher customers. This decision really threatened most of the check cashers in New York City to shift their businesses to the sole remaining bank that does business with check cashers, North Fork, or go out of business.

I know that along with others I wrote a letter, you know, to FinCEN, and they have responded to that situation with new guidance. Has that had a positive effect, or what further steps are needed?

I just wanted to add, we certainly want to combat terrorism. We want to combat money laundering. We want to crack down. But at the same time, we don't want to cut off financial services. In some neighborhoods the check cashers are vital, in some cases the only source of financial services that are there.

So could you respond to the new guidances that came out of FinCEN and what else needs to be done?

Mr. MCCLAIN. Thank you very much, Congresswoman Maloney. I appreciate your perspective on the issue.

Initially to respond, I would say that we are extremely, extremely grateful for the amount of attention and diligence that has been given this by FinCEN. They initially held on March 8th a fact-finding session on the problem. We had some 43 speakers from industry, both the MSB industry and also bankers, speak on the issue. We learned at that time, as we had known internally for quite a period, that the problem is truly critical, and to our not necessarily surprise, but to our satisfaction, we heard from the bankers who expressed a tremendous amount of frustration over the problem and the fact that in many cases they have been banking check cashers for decades and in some cases generations. It was with much dismay that they had to terminate their long-standing check cashing customers. It was largely due to some misguided pressure from some Federal banking examiners who essentially caused them to terminate their accounts.

The guidance materials we think are certainly a step in the right direction. We feel at this point—they were just replaced April 26th— it is too early to assess whether or not they are going to sort of stop the flow of banks exiting the industry and whether or not it is going to cause some to return. That is certainly our hope.

But key for the guidelines to be effective, I think, is advocacy on the part of government, advocacy on the part of the same Federal agencies that in some part, maybe indirectly, caused the situation to develop. We need essentially the high risk assessment to be critically examined and the guidelines to do that in some measure.

Additionally, in terms of the additional advocacy we would like to see some sort of an advisory board created, preferably some statutorily created body to essentially monitor the situation and create a forum for industry, both the check cashing MSB industry and also the banking industry, and also a forum for the Federal banking regulators to be heard as well.

But as I said, it is too early to see whether or not the guidelines have been effective. But without that added attention from government, we are somewhat circumstance expect.

As I mentioned in my presentation, we are going to be convening a forum on February 26th. Hopefully at that point in time we will have a better assessment as to the ultimate success of the guidelines.

Mrs. MALONEY. My time is up. But if you will allow me for 2 seconds to be parochial—and since the superintendent is sitting here—I don't think we want to close down services in neighborhoods. We have a wonderful Federal system where we can come up with new creative ideas. This might be a way that you could have some form of oversight that says that this is okay. Because we certainly don't want to lose our financial services or the access to it. In some neighborhoods in New York, check cashers are the only form of financial services that are there, in some cases credit unions.

So I thank you. It is great to see all of you.

Mr. PAUL. I thank the gentlelady.

The Chair notes that some members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 30 days for members to submit written questions to these witnesses and to place their responses in the record.

I want to thank the panel, and the panel and the committee hearing is now adjourned.

[Whereupon, at 12:32 p.m., the subcommittee was adjourned.]

A P P E N D I X

May 26, 2005

Testimony of

John J. Byrne

On Behalf of the

American Bankers Association

Before the

House Financial Services Oversight and Investigations Subcommittee

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Subcommittee Chairwoman Kelly and Members of the subcommittee, I am John Byrne, Director of the Center for Regulatory Compliance of the American Bankers Association (ABA). ABA appreciates this opportunity to discuss how the financial industry is addressing the many compliance issues with suspicious activity reporting and the challenges with providing bank services to money services businesses (MSBs).

ABA, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership – which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks – makes ABA the largest banking trade association in the country.

ABA and our members continue to work with our government partners in training financial institution employees to effectively detect and report the myriad of financial crimes that involve money laundering and terrorist financing. For example, we plan to address the expected June 30 interagency Bank Secrecy Act (BSA)/anti-money laundering (AML) examination procedures in a number of education programs with the government later this year. All in all, the Association has trained hundreds of thousands of bankers since the passage of the Money Laundering Control Act in 1986.[1] The industry's commitment to deterring money laundering continues unabated.

Among other things, ABA holds an annual conference with the American Bar Association on money laundering enforcement, produces a weekly electronic newsletter on money laundering and terrorist financing issues, offers online training on BSA compliance, and has a standing committee of more than 80 bankers who have AML responsibilities within their institutions. In addition, we provide telephone seminars on important and often confusing issues such as MSB relationships and compliance with Section 326 of the USA PATRIOT Act.

[1] A 2003 survey by ABA Banking Journal and Banker Systems Inc., found that Bank Secrecy/AML/OFAC was the number one compliance area in terms of cost to the banking industry. It is also interesting to note that in banks under $5 billion in assets, 75.6 percent of the employees said that compliance was not their only job.

As we told this subcommittee on May 4, "there has been clear movement and commitment for further action from the highest levels of the federal banking agencies" for a uniform approach to BSA compliance. However, ABA would again remind the subcommittee that the industry remains concerned about the quality of communication that exists between these same agencies and the field examiners. In fact, we will highlight one particular issue that occurred after the May 4 hearing that emphasizes our concerns. ABA remains optimistic that the commitment mentioned above is real and will resolve the issues quickly.

Madam Chairwomen, your May 20 letter of invitation asked us to address three issues:

- An update on what is being done to "standardize" BSA compliance challenges;
- Why the industry is engaged in the "defensive" filings of suspicious activity reports (SARs); and,
- What BSA compliance concerns are associated with MSBs.

To update Members on the issues presented by the letter of invitation, we offer the following observations and recommendations:

1. The pending interagency examination procedures will provide an opportunity for both the industry and the federal banking agencies to work together and prevent confusion and second-guessing. We urge Congress to seek an update on the practical effect of these procedures in early 2006.

2. As we told this subcommittee earlier this month, "it is counterproductive to label an entity 'high risk' without also issuing guidance on how to mitigate that risk." Finally, the agencies agreed and produced the interagency guidance on working with MSBs. It is early for a complete assessment, but the direction of the guidance is a strong first step for clarity.

3. Defensive SAR filings are the result of the dearth of useful guidance and a lack of a balanced approach to examiner oversight. The federal banking agencies must insist that their field examiners not "second-guess" SAR decisions made by the financial sector or the volume of SARs will continue to skyrocket.

Consistent Examination Procedures Should Address the Current State of Confusion

ABA has previously emphasized to Congress that the banking agencies need to reach agreement on how the financial services industry will be examined for compliance under the USA PATRIOT Act and the other AML requirements. We are pleased to note that the final interagency procedures are now planned for release June 30. These procedures, if implemented appropriately, should address a glaring problem – the assessment of the adequacy of SAR programs.

ABA is pleased that the agencies are exhibiting a commitment to greater consistency in 2005. For example, not only has FinCEN Director William Fox expressed public support for uniform assessments, but he has also directed the Bank Secrecy Act Advisory group (BSAAG) to form a subcommittee on examination issues. As an aside, I would note that the congressionally created Bank Secrecy Act Advisory Group should be a model for government-private sector cooperation.

This subcommittee, co-chaired by ABA and the Federal Reserve Board, has met several times – as recently as April 29 – to discuss the pending interagency examination procedures.

Uniform exam procedures will assist with the industry concerns about examination inconsistency and the continued threat of "zero tolerance" by these same errant examiners. However, we strongly urge Congress to ensure that all banking agencies engage in industry outreach when the AML exam procedures are made public. The agencies appear committed to such outreach and we believe a nationwide series of "town hall" meeting events will ensure that both sides will know what to expect in this complicated compliance area.

MSBs and Banks: An Example of Regulatory Confusion

A major challenge facing the banking industry has been how to fulfill our obligations regarding appropriate relationships with MSBs. The banking industry certainly understands and appreciates the need to analyze the levels of risk involved with maintaining MSB relationships. We know the importance of providing banking services to all segments of society. For some, the remittance services that MSBs frequently provide are an essential financial product. Remittance flows are an important and stable source of funds for many countries and constitute a substantial part of financial inflows for countries that have a large migrant labor force working abroad.

The problem, however, is how much analysis is sufficient. At times, banks appropriately exit relationships due to the risk inherent with a particular MSB. At other times, banks want to continue certain valued relationships.

Officially recorded remittances received by developing countries are estimated to have exceeded $93 billion in 2003. They are now second only to foreign direct investment (around $133 billion) as a source of external finance for developing countries. In 36 out of 153 developing countries, remittances were larger than all capital flows, public and private combined.

Remittance flows go through both formal and informal remittance systems. Because of the importance of such flows to recipient countries, governments have made significant efforts in recent years to remove impediments and increase such flows. At the same time, however, there has been heightened concern about the potential for remittance systems, particularly those operating outside of the formal banking system, to be used as vehicles for money laundering and the financing of terrorism. It is believed that the risk of misuse of remittance systems would be reduced if transfers were channeled through remittance systems that are subject to regulations by governments.

To address the risks, a two-pronged approach is evolving: One prong involves efforts by governments to encourage the use of formal systems (such as banks) by lowering the cost and increasing the access of users and recipients to the formal financial sector. Such efforts should concentrate on the reduction of artificial barriers such as unnecessary regulatory standards that impose costs ultimately borne by consumers.

The second prong includes initiatives by governments to implement anti-money laundering standards for entities such as MSBs. This has clearly been occurring in the United States and, as we have heard from other witnesses, the MSB regulatory infrastructure is robust and effective.

A challenge that underlies this situation is that there exists in most countries a large pool of "unbanked" individuals. Such individuals are often accustomed to using both formal (and regulated) financial institutions and very informal (and unregulated) financial services providers. Economic and social incentives that move this group towards "underground" financial services providers ultimately harm the interests of the unbanked, of law-abiding financial services providers, and of the general public. Moreover, the underground financial services providers may service both law-abiding unbanked persons, as well as criminals. Thus, governmental actions that discourage the unbanked from entering depository institutions may have the effect of also making anti-money laundering goals far more difficult to attain. These facts have helped make it clear that the MSB-bank environment needs radical change.

The necessary services that MSBs provide are being severely hampered by regulatory excess. The federal banking agencies issued an interagency policy statement on March 30 and sorely needed interagency guidance on April 26, but this guidance now must be clearly communicated to examiners.

On March 8, I had the opportunity to co-chair a meeting of BSAAG on the MSB problem. For eight hours, we heard dramatic examples from 44 witnesses of lost business, economic failures and rampant regulatory confusion. The theme of confusion was echoed by all of the banks. FinCEN and the federal banking agencies are to be commended for working toward guidance to address this policy morass. On May 4, we urged the agencies to act swiftly and inform examiners to adjust their reviews of MSBs that are associated with banks. I would like to report that at least one large southwestern bank reported to ABA that its current BSA exam showed the oversight agency to be well-versed in the MSB guidance. This is indeed a positive sign.

Lack of SAR Guidance Results in Unnecessary Filings

With the increased number of entities required to file SARs as well as the heightened scrutiny by regulators on SAR policies and programs, it is essential for the regulatory agencies, law enforcement, and FinCEN to assist filers with issues as they arise.

Government advisories and other publications are a critical source for recognizing trends and typologies for money laundering and other financial crimes. As the industry emphasized in the April 2005 issue of the interagency-authored publication, **SAR Activity Review**, there are a number of examples of activities that are characteristic of financial crimes and that can be used as teaching tools. This information is extremely useful for training purposes. As the private sector co-chair of the **SAR Activity Review**, I can assure you ABA supports the efforts of FinCEN and the participating agencies in crafting a publication that provides necessary statistical feedback to the SAR filing community. The **SAR Activity Review** has provided a variety of examples of suspicious activities that offer tell-tale signs of such diverse activities as identity theft, bank fraud, and computer intrusion.

We are pleased that the 2004 edition of the **SAR Activity Review** provided, for the first time, summary characterizations of all of the major suspicious activity categories. This should assist filers in advancing their understanding of the reporting requirements.

As stated above, there are several problems affecting banks in the AML exam process related to SARs. ABA has previously mentioned the many examples of examiner criticisms received by our members during reviews of their SAR programs. Whether it has been criticism of the number of SARs that the institution has filed or "second-guessing" by examiners as to why a SAR was not filed, we remind Congress that this situation demands immediate attention.

Moreover, regulatory scrutiny of SAR filings (and the recent civil penalties assessed against banks for SAR deficiencies) has caused many institutions to file SARs as a purely defensive tactic (the "when in doubt, file" syndrome) to stave off unwarranted criticism or second guessing of an institution's suspicious activity determinations. In fact, the *American Banker* has reported that, in March 2005, the banking industry filed 43,000 SARs: a 40 percent increase from a year earlier.

As FinCEN Director William Fox stated so eloquently in the April **SAR Activity Review**:

> *While the volume of filings alone may not reveal a problem, it fuels our concern that financial institutions are becoming increasingly convinced that the key to avoiding regulatory and criminal scrutiny under the Bank Secrecy Act is to file more reports, regardless of whether the conduct or transaction identified is suspicious. These "defensive filings" populate our database with reports that have little value, degrade the valuable reports in the database and implicate privacy concerns.*

We would like to commend Director Fox for addressing our previous recommendation, which we outlined in testimony in May 2004, by creating a BSAAG subcommittee on SAR issues. I would note that the first meeting has already occurred and the issue of defensive filings is a top priority.

Our members continue to express their concerns on the rampant second-guessing that still continues. For example, just last week a bank told us that it had extensive documentation on why it did not file a SAR, only to be told by the examiner that it must file. This example, which is not isolated, is a major reason why banks feel they have no other option but to err on the side of filing. Our hope continues to be that the examination procedures and additional interpretations on SAR issues will result in returning SARs to their original place – forms filed only after careful analysis and investigations with no second-guessing by regulators.

Revamping the Outdated CTR System

Another way of ensuring that government and industry resources are used effectively in the area of financial crime detection is to remove unnecessary data collections.

As ABA has previously testified, the 35-year-old rules related to cash transaction reporting (CTR) have become redundant and lost their usefulness. ABA believes that the time has come to dramatically address this reporting excess by eliminating CTR filings for transactions conducted by seasoned customers through their bank accounts.

ABA notes that the purpose of Subchapter II of Chapter 53 of Title 31 establishing the BSA regulatory regime is to require certain reports or records when they have "a high degree of usefulness" for the prosecution and investigation of criminal activity, money laundering, counter-intelligence and international terrorism. ABA and its members strongly believe that the current CTR reporting standards have long departed from this goal of achieving a high degree of usefulness.

ABA members believe that CTR filing has been rendered virtually obsolete by several developments:

- formalized customer identification programs;
- more robust suspicious activity reporting; and,
- government use of the 314(a) inquiry/response process.

We believe that CTRs are no longer analyzed to identify unknown criminal agents. Rather they are used, at most, to try to match already known suspects to locate potential account activity. As noted above, section 314(a) is much more efficient for identifying account activity of known suspects because it has the value of capturing accounts involving more than just cash transactions.

We believe that combining improved monitoring conducted by institutions as part of their SAR processes with better mining of SAR data by law enforcement as well as judicious use of the 314(a) process yields a more effective approach to law enforcement investigation of patterns of fraud, money laundering and terrorism funding. Consequently, we believe the time has come to recognize the redundancy of CTR filings for seasoned customers with transaction accounts and to eliminate this inefficient use of resources by bankers and law enforcement.

Changing the thinking about mandating the collection of routine cash data would have the following benefits:

- The vast majority of the over 13 million CTRs filed annually would stop, saving many hours a year in filling out forms;
- Wasteful SARs would cease. These SARs amount to almost 50 percent of all BSA-required SARs. Rather than filing specious structuring reports, banks could focus their energies on detecting suspicious handling of currency regardless of artificial thresholds;
- Bank systems and resources could be redirected from CTR monitoring to support further improvement in suspicious activity reporting;
- Regulatory criticism of technical mistakes with CTR filings would cease;
- Issues surrounding the CTR exemption process would be eliminated; and,
- Law enforcement could redirect resources to better evaluating SARs.

While BSAAG has been reviewing the cash transaction system with an eye toward simply modifying elements such as the exemption process, ABA believes that a more comprehensive approach overall is needed.

Conclusion

ABA has been in the forefront of the industry efforts to develop a strong public-private partnership in the areas of money laundering and now terrorist financing. This partnership has achieved much success, but we know that more can be accomplished. We commend the Treasury Department, banking agencies, and FinCEN for their recent efforts to ensure a workable and efficient process. ABA will continue our support for these efforts.

Thank you. I would be happy to answer any questions.

TESTIMONY
BY

JOSEPH CACHEY III
FIRST DEPUTY CHIEF COMPLIANCE OFFICER

WESTERN UNION FINANCIAL SERVICES, INC.

BEFORE THE
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS
OF THE U.S. HOUSE OF REPRESENTATIVES
FINANCIAL SERVICES COMMITTEE

HEARING ON

"THE FIRST LINE OF DEFENSE: THE ROLE OF FINANCIAL INSTITUTIONS IN DETECTING FINANCIAL CRIMES"

MAY 26, 2005

GOOD MORNING. I'D LIKE TO THANK YOU ON BEHALF OF WESTERN UNION FOR THE OPPORTUNITY TO ADDRESS THE SUBCOMMITTEE ON THE IMPORTANT TOPIC OF THE ROLE OF FINANCIAL INSTITUTIONS IN DETECTING FINANCIAL CRIMES THROUGH SUSPICIOUS ACTIVITY REPORTING.

WESTERN UNION IS A LEADER IN WORLDWIDE MONEY TRANSFER. OUR SERVICES ARE AVAILABLE IN OVER 195 COUNTRIES THROUGH SOME 225,000 AGENT LOCATIONS. WESTERN UNION IS A PART OF FIRST DATA CORPORATION, A PUBLICLY-TRADED FORTUNE 300 COMPANY WITH OVER 30,000 EMPLOYEES WORLDWIDE. FIRST DATA PROVIDES CREDIT CARD AND PAYMENT PROCESSING SOLUTIONS TO A WIDE RANGE OF CLIENTS INCLUDING OVER 1400 BANKS, MILLIONS OF MERCHANT LOCATIONS, AND EVEN GOVERNMENT AGENCIES, SUCH AS THE INTERNAL REVENUE SERVICE. FIRST DATA AND WESTERN UNION ARE SUBJECT TO A BROAD ARRAY OF STATE AND FEDERAL REGULATIONS THAT ENSURE SAFE AND SOUND SERVICES TO OUR CUSTOMERS.

SINCE THE SUSPICIOUS ACTIVITY REPORTING REGULATIONS TOOK EFFECT FOR MONEY SERVICES BUSINESSES ("MSBs") IN JANUARY, 2002, WESTERN UNION HAS CREATED AN INDUSTRY LEADING COMPLIANCE PROGRAM IN A RELATIVELY SHORT PERIOD OF TIME.

WESTERN UNION MAINTAINS AN ANTI-MONEY LAUNDERING ("AML") COMPLIANCE DEPARTMENT OF OVER 180 DEDICATED EMPLOYEES LOCATED IN 13 LOCATIONS AROUND THE WORLD TO PROMOTE THE SAFE AND SOUND OPERATION OF ITS MONEY TRANSFER SYSTEM. THIS DEPARTMENT'S PRIMARY OBJECTIVES ARE TO PROVIDE SUPPORT AND GUIDANCE TO WESTERN UNION'S DIVERSE AGENT BASE, DETECT AND REPORT SUSPICIOUS ACTIVITY IN THE UNITED STATES AND FACILITATE REGULATORY AND LAW ENFORCEMENT OUTREACH AND RESPONSE. WE PRIDE OURSELVES IN WORKING WITH LAW ENFORCEMENT, WHEN APPROPRIATE, AROUND THE WORLD.

I AM HERE TODAY TO DISCUSS AN IMPORTANT PART OF OUR ANTI-MONEY LAUNDERING COMPLIANCE PROGRAM: SUSPICIOUS ACTIVITY REPORTING AND OUR DEALINGS WITH THE LAW ENFORCEMENT COMMUNITY.

EVEN TODAY, WESTERN UNION CONTINUES TO ENHANCE ITS OWN TRANSACTION MONITORING CAPABILITIES TO BETTER DETECT AND REPORT SUSPICIOUS ACTIVITY AND LARGE CURRENCY TRANSACTIONS TO THE FINANCIAL CRIMES ENFORCEMENT NETWORK (FINCEN). WE HAVE DEVELOPED OUR OWN PROPRIETARY SOFTWARE FOR OUR UNIQUE MONEY TRANSFER SYSTEM. WE BELIEVE THAT GETTING THE RIGHT INFORMATION INTO THE HANDS OF LAW ENFORCEMENT IS OUR PRIMARY ANTI-MONEY LAUNDERING COMPLIANCE MISSION.

WESTERN UNION FILES TENS OF THOUSANDS OF SUSPICIOUS ACTIVITY REPORTS ("SARs") EACH YEAR, REPRESENTING A SMALL FRACTION OF OUR TOTAL NUMBER OF TRANSACTIONS. WE KNOW THAT SOME SARs LEAD TO INVESTIGATIONS BECAUSE THERE IS DIRECT FOLLOW-UP FROM LAW ENFORCEMENT, USUALLY THROUGH A COURT-ISSUED SUBPOENA, FOR FURTHER INFORMATION. THE FILING OF A SAR MAY LEAD TO A NUMBER OF ACTIONS TAKEN IN CONJUNCTION WITH LAW ENFORCEMENT. I'LL CITE JUST A FEW EXAMPLES WITHOUT GOING INTO SPECIFICS THAT COULD JEOPARDIZE ANY INVESTIGATION OR OUR MONITORING SYSTEMS.

LAST YEAR, WESTERN UNION, BASED ON INTERNAL CRITERIA, FILED SIX SARs ON FOUR CONSUMERS WHO WERE RECEIVING TRANSACTIONS IN HIGHER RISK COUNTRIES. THESE SARs RESULTED IN THE OPENING OF AN EXPANSIVE INVESTIGATION NOW BEING CONDUCTED BY DUAL FEDERAL AGENCIES. WESTERN UNION CONTINUES TO SUPPORT THESE INVESTIGATIVE EFFORTS BY RESPONDING TO SUBPOENAS TARGETING IDENTIFIED CONSUMER TRANSACTION INFORMATION. IN ADDITION, WE HAVE ALSO SHARED EMERGING INSIGHTS INTO CONSUMER NETWORK PATTERNS INVOLVING INVESTIGATIVE SUBJECTS, AND HELP FACILITATE COORDINATION AMONG SPECIAL AGENTS FROM EACH OF THE RESPECTIVE AGENCIES.

WESTERN UNION ALSO COOPERATES WITH FEDERAL LAW ENFORCEMENT EFFORTS THROUGH AGREEMENTS THAT ASSURE CERTAIN AGENT LOCATIONS ARE KEPT OPEN DURING ONGOING INVESTIGATIONS. FOR EXAMPLE, THE OWNER OF A WESTERN UNION AGENT LOCATION IN THE MID-WEST WAS INDICTED IN APRIL 2005 ON 43 COUNTS OF MONEY LAUNDERING AFTER A FIVE YEAR INVESTIGATION. WESTERN UNION'S AGREEMENT TO WITHHOLD NORMAL BUSINESS INTERVENTION AND KEEP THE LOCATION OPEN ALLOWED LAW ENFORCEMENT TO GATHER SUFFICIENT EVIDENCE IN PREPARATION FOR THE INDICTMENT.

IN ADDITION, WESTERN UNION CONTINUALLY COOPERATES WITH STATE AND FEDERAL AUTHORITIES BY MAINTAINING A "HANDS-OFF" POSTURE ON CERTAIN CONSUMERS UNDER ACTIVE SURVEILLANCE IN SEVERAL STATES. IN EACH OF THESE EXAMPLES ARE CONSUMERS OR AGENTS THAT WESTERN UNION HAS IDENTIFIED AND WOULD TYPICALLY STOP DOING BUSINESS WITH BUT FOR LAW ENFORCEMENT REQUESTS. SUCH COOPERATION IS IMPERATIVE TO PREVENTING SUCH ACTIVITY FROM MOVING UNDERGROUND AND OUT OF REGULATORY VIEW.

AS IS TYPICAL WITH MONEY LAUNDERING SCHEMES, RISK MAY SHIFT AS MORE INFORMATION CAN BE OBTAINED AND ANALYZED, AND SO MUST OUR FOCUS. FOR INDUSTRY TO BETTER FOCUS ITS RESOURCES, THE REGULATOR, IN THIS CASE FINCEN, MUST PROVIDE ONGOING

COMMUNICATION TO INDUSTRY ABOUT EMERGING RISKS AND MONEY LAUNDERING PATTERNS SO THAT WE CAN DIRECT OUR COMPLIANCE EFFORTS TOWARDS THE MOST CRITICAL RISK AREAS. THIS TYPE OF ONGOING COMMUNICATION SHOULD NOT ONLY RESULT IN MORE MEANINGFUL REPORTING OF SUSPICIOUS ACTIVITY TO LAW ENFORCEMENT BUT ALLOW THE INDUSTRY TO REDUCE THE FILING OF NON-USEFUL REPORTS WHICH MAY CREATE "NOISE" IN THE SYSTEM AND UNDERMINE THE EFFORTS OF LAW ENFORCEMENT.

ONE PRIMARY EXAMPLE OF POTENTIAL "NOISE" IS THE REPORTING OF SIMPLE STRUCTURING. THE MAJORITY OF THE SARs WESTERN UNION FILES REPORT LOW LEVEL STRUCTURING ACTIVITY. CURRENTLY, THE SUSPICIOUS ACTIVITY REPORTING THRESHOLD IS AT $2000 AND STRUCTURING MAY OCCUR JUST BELOW THE $3000 BSA RECORDKEEPING REQUIREMENT. FRANKLY SPEAKING, WE BELIEVE THAT MOST OF THIS ACTIVITY RESULTS NOT FROM EVIL INTENT – BUT FROM THE AVERAGE AMERICAN'S UNWILLINGNESS TO SHARE THEIR SOCIAL SECURITY NUMBER AND OTHER PERSONAL INFORMATION WITH A THIRD PARTY. TOGETHER WE NEED TO QUESTION WHETHER FINANCIAL INSTITUTIONS REPORTING ACTIVITY AT THIS LEVEL IS HELPFUL TO LAW ENFORCEMENT. WE WOULD ENCOURAGE FINCEN TO ANALYSE ITS SAR DATA ACROSS THE FINANCIAL SERVICES COMMUNITY AND PROVIDE MORE GUIDANCE ON WHAT TYPE AND LEVEL OF ACTIVITY PRESENTS THE BEST INTELLIGENCE TO LAW

ENFORCEMENT. IT IS POSSIBLE THAT BY FOCUSING ON HIGHER LEVELS OF ACTIVITY WE CAN REDUCE THE NUMBER OF NON-USEFUL REPORTS, ASSIST LAW ENFORCEMENT IN MORE RAPIDLY IDENTIFYING MONEY LAUNDERING SCHEMES AND DRIVE OUR COLLECTIVE RESOURCES TO WHERE THE RISK REALLY LIES.

BUT HOW CAN THE REPORTING SYSTEM BE IMPROVED? FIRST, I'D LIKE TO COMMEND DIRECTOR FOX AND FINCEN FOR INCREASING THE DIALOGUE WITH OUR INDUSTRY ABOUT THESE ISSUES. AS YOU ARE AWARE, FINCEN HAS PROPOSED A NEW SAR-MSB FORM AND WESTERN UNION LOOKS FORWARD TO COMMENTING ON THE FORM IN THE NEAR FUTURE. HOWEVER, WE BELIEVE THE PROCESS SHOULD BE EVEN FURTHER SIMPLIFIED FOR OUR AGENTS. AGENTS SHOULD BE REPORTING SUSPICIOUS ACTIVITY ON A SIMPLE, ONE-PAGE FORM PROVIDING ONLY BASIC INFORMATION. ANY LAW ENFORCEMENT INVESTIGATION TRIGGERED BY SUCH A SAR WILL INEVITABLY LEAD TO REQUESTS FOR UNDERLYING INFORMATION HELD BY THE SERVICE PROVIDER SO NOTHING IS LOST BY ALLOWING AN AGENT TO USE AN ABBREVIATED FORM. FURTHER, THE FORM SHOULD BE IN BOTH ENGLISH AND SPANISH IN RECOGNITION OF THE GROWING HISPANIC SEGMENT OF OUR POPULATION. I NOTE THAT WESTERN UNION PROVIDES TRAINING MATERIALS IN ENGLISH, SPANISH, MANDARIN, PORTUGUESE, FRENCH, KOREAN, RUSSIAN, ARABIC AND POLISH

IN RECOGNITION OF THE WIDE VARIETY OF AGENTS SERVING A VERY DIVERSIFIED CONSUMER BASE.

IN THE AREA OF PROVIDING BETTER INFORMATION TO LAW ENFORCEMENT, THERE ARE TWO AREAS OF CONCERN. FIRST, FROM OUR EXPERIENCE, LOCAL LAW ENFORCEMENT AGENCIES AND STATE ATTORNEYS GENERAL OFFICES ARE NOT FULLY UNAWARE OF FINCEN'S GATEWAY SYSTEM WHICH ALLOWS THEIR AGENCIES TO CONDUCT THEIR OWN RESEARCH AND ANALYZE BSA DATA EXTRACTED FROM THE HUNDREDS OF THOUSANDS OF SARs FILED EVERY YEAR. BETTER EDUCATING LOCAL LAW ENFORCEMENT WILL RESULT IN FEWER REQUESTS GOING TO MSBs FOR INFORMATION THAT IS ALREADY AVAILABLE.

SECOND, THERE MUST BE MORE INFORMATION FLOWING FROM LAW ENFORCEMENT TO THE INDUSTRY ON EMERGING CRIMINAL AND MONEY LAUNDERING PATTERNS. THE "TWO-WAY" CONVERSATION BETWEEN THE GOVERNMENT AND THE PRIVATE SECTOR MUST MOVE FROM A WHISPER TO A ROAR IF COLLECTIVELY WE ARE GOING TO SUCCEED IN PROTECTING OUR NATION. WE BELIEVE THAT THE SHARING OF MORE NON-PUBLIC INFORMATION BETWEEN THE PUBLIC AND PRIVATE SECTOR WILL SIGNIFICANTLY IMPROVE ALL OF OUR EFFORTS IN THIS AREA.

A FINAL WORD ON THE "DEFENSIVE" FILING OF SARs. AS DISCUSSED, A BIG ISSUE FOR MSBs IS THE FILING OF A SAR TO REPORT LOW LEVEL STRUCTURING. SUCH FILING IS NOT DEFENSIVE BECAUSE STRUCTURING FOR ANY REASON IS TECHNICALLY A CRIME. BUT WHILE SUCH REPORTING IS NOT "DEFENSIVE", IT MAY NOT BE ALL THAT HELPFUL. THERE HAS TO BE A BETTER APPROACH.

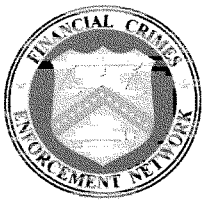
THERE ARE STILL MANY QUESTIONS SURROUNDING THE REPORTING OF STRUCTURING ACTIVITY. DOES IT HAPPEN OVER A SINGLE DAY, A WEEK OR CAN IT OCCUR AND THEREBY REQUIRE REPORTING OVER A PERIOD OF MONTHS? SOME PUBLIC PRONOUNCEMENTS SUGGEST THE ANSWER IS YES, BUT THERE IS NO CLEAR GUIDANCE CONCERNING TRANSACTION LEVELS OR A TIMEFRAME FOR THE ACTIVITY TO BE MONITORED. MUCH OF THE GUIDANCE GIVEN HAS BEEN TOO BROAD AND IN TODAY'S REGULATORY ENVIRONMENT GRAY AREAS LEAD TO MORE FILINGS.

AN EXAMPLE OF A GRAY AREA IN SAR FILING DECISION-MAKING IS "HIGH VOLUME" CONSUMERS. WESTERN UNION HAS FOUND THAT MANY OF OUR HIGHER VOLUME CONSUMERS HAVE VERY LEGITIMATE REASONS FOR THE USE OF OUR SYSTEMS. WE STRIVE TO IDENTIFY AND LEARN MORE ABOUT THESE CONSUMERS BY CONTACTING THEM TELEPHONICALLY. HOWEVER, STATE BANK EXAMINERS HAVE STATED THAT THEY "FEEL" THAT ANY HIGH VOLUME USER OF AN MSBs' SERVICES MUST BE SUSPICIOUS. SO IF WE TRY

TO CONTACT THE CONSUMER AND HE DOES NOT RETURN THE CALL – MUST WESTERN UNION FILE A SAR WITHOUT ADDITIONAL INFORMATION RELEVANT TO THIS ACTIVITY? RIGHT NOW, OTHERS WE HAVE CONSULTED WITH ANSWER, YES – FILE THE SAR TO PROTECT YOURSELF FROM A POTENTIAL NEGATIVE EXAMINATION FINDING.

MANY EXAMINERS' POSITION APPEARS TO BE "IF YOU CANNOT PROVE THAT A CONSUMER IS WHOLLY INNOCENT – THEN THEY ARE GUILTY – FILE THE SAR." THIS ATTITUDE LEADS TO EXCESSIVE SAR FILINGS BECAUSE IT FOLLOWS THE "MORE EQUALS BETTER" APPROACH. WESTERN UNION IS ATTEMPTING TO BECOME MORE SURGICAL IN ITS SAR FILING TO PROVIDE QUALITY INFORMATION, NOT MORE INFORMATION. WE HOPE THE LAW ENFORCEMENT AND REGULATORY COMMUNITY SUPPORTS THIS MORE THOUGHTFUL APPROACH.

NO COMPLIANCE PROGRAM SHOULD BE STATIC AND NOR SHOULD THE GOVERNMENT'S APPROACH TO FIGHTING MONEY LAUNDERING AND TERRORIST FINANCING. WHAT WAS PUT IN PLACE THREE YEARS AGO MIGHT NOT ADDRESS TODAY'S CONCERNS. WE WOULD LIKE TO SEE A REVIEW OF LAW ENFORCEMENT'S EXPECTATIONS OF WHAT TYPE OF ACTIVITY SHOULD BE FILED ON BASED ON TODAY'S REALITIES AND YESTERDAY'S LEARNINGS. SUCH A REVIEW AND DIALOGUE WILL LEAD TO A MORE EFFICIENT AND FOCUSED REPORTING REGIME. THANK YOU.



STATEMENT OF WILLIAM J. FOX, DIRECTOR
FINANCIAL CRIMES ENFORCEMENT NETWORK
UNITED STATES DEPARTMENT OF THE TREASURY

BEFORE THE
UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

MAY 26, 2005

Chairwoman Kelly, Congressman Gutierrez, and distinguished members of the Committee, I appreciate the opportunity to appear before you to discuss the Financial Crimes Enforcement Network's administration and implementation of the Bank Secrecy Act, as amended. We thank you for the support and policy guidance you and the members of this Committee have offered to us on these issues. We are more certain than ever that the efforts undertaken by both the government and the financial industry under the Bank Secrecy Act are critical components to our country's ability to utilize financial information to combat terrorism, terrorist financing, money laundering and other financial crime. In addition, the systems and programs that are mandated by the Bank Secrecy Act that have been developed and are continuing to be refined make our financial system safer and more transparent.

Much has transpired since I last had the honor of testifying before this Committee. Significantly, Treasury's Office of Terrorism and Financial Intelligence has been stood-up and staffed. This has been a very positive development for the Financial Crimes Enforcement Network. Thanks to the leadership of Under Secretary Stuart Levey and Assistant Secretary Juan Zarate, Treasury, its bureaus, and offices that work on issues relating to financial intelligence, financial crime and sanctions are not only better coordinated, but also are developing previously uncovered synergies utilizing Treasury's unique tools, capabilities and financial perspective. This work has helped address the significant strategic threats of our time such as terrorism, drug trafficking, the proliferation of weapons of mass destruction and addressing rogue regimes.

In June of last year, because of the direct support of the Congress – especially Chairman Oxley and you, Madam Chairwoman – the Financial Crimes Enforcement Network awarded a contract to EDS to build the heart of the system that we are calling BSA Direct. This system, when complete, will revolutionize the way information under the Bank Secrecy Act is collected, housed, analyzed, disseminated and exploited. EDS is building the data warehouse that will eventually connect to our already existing e-filing system and other systems that control the access and dissemination of Bank Secrecy Act data. Scheduled for completion in October, BSA Direct's data warehouse will provide law enforcement, regulatory and other government officials, who are authorized to access Bank Secrecy Act data, a secure, modern, web-based data environment with robust and flexible search and data mining tools. BSA Direct, when fully complete, will for the first time enable the Financial Crimes Enforcement Network to discharge its most important responsibility – to collect, house, analyze and properly disseminate information collected under the Bank Secrecy Act – in an effective manner.

As the administrator of the Bank Secrecy Act, there is no duty I view as more critical than the effective collection, management, and dissemination of the highly sensitive and confidential information collected under that Act. If the Financial Crimes Enforcement Network does nothing else, we must ensure that we properly perform these functions. This is our core responsibility. There are a number of significant issues surrounding the collection and use of Bank Secrecy Act reports, and I welcome this opportunity to discuss those issues with you. A recent report issued by the General Accounting Office identified disturbing security problems related to the systems that currently handle Bank Secrecy Act data. The GAO reported recently that security problems in those systems exposed Bank Secrecy Act data to potential unauthorized access by users in the facility that houses the systems. We are profoundly concerned about the issues the GAO identified. The Financial Crimes Enforcement Network is the delegated steward of this data and is ultimately responsible for its security. We will move very quickly to take all appropriate steps to ensure this data is protected.

Since last year, we have focused great attention on issues relating to our responsibilities for administering and implementing the Bank Secrecy Act. Under the leadership of Associate Director William Langford, we have changed the way we interact with the regulators who have the responsibility of examining financial institutions for compliance with Bank Secrecy Act requirements, resulting in better coordination and communication with the industry. Because these issues go to the heart of the hearing today, I will discuss them in greater detail later.

We are changing the way we analyze information at the Financial Crimes Enforcement Network. We are moving away from the notion of "FinCEN as a library," with FinCEN analysts acting as librarians assisting customers with efforts to retrieve and understand Bank Secrecy Act data. Our new analytical paradigm requires higher-level research and analysis utilizing all sources of information to understand and explain the cutting-edge problems relating to money laundering and illicit finance, including terrorist

financing. Our goal is nothing short of being as good as, if not better than, any other analytic unit focused on financial issues in the world.

We have reengaged internationally, working with our colleagues in other financial intelligence units in ways that go far beyond simple information sharing. We are utilizing the powerful tools granted to us in Section 311 of the USA PATRIOT Act to safeguard the U.S. financial system from jurisdictions and institutions that are of primary money laundering concern. These actions have very serious and real effect, bringing change where change is needed, and at the same time letting the world know that we will not tolerate jurisdictions or institutions with little transparency or lax controls.

Finally, we are changing the way we interact with our law enforcement customers. I am very happy to appear here today with my good friend and colleague Mike Morehart, who is Chief of the Terrorist Financing Operations Section in the Counterterrorism Division of the Federal Bureau of Investigation. Special Agent Morehart's office is working tirelessly to keep our country safe from terrorists. Everyday, the men and women in the Terrorist Financing Operations Section quietly, and often thanklessly, accomplish their mission to identify, locate, disrupt, deter and capture terrorists attempting to harm the citizens of our country. They do their job utilizing some of the most valuable information available to the government – financial information – in the process. I know, as I have seen them at work, and I am aware of the fruits of their labor. As you will learn today, the Financial Crimes Enforcement Network has entered into a very deep partnership with the FBI that is allowing Mr. Morehart's office and other components of the Bureau to exploit the information collected under the Bank Secrecy Act in a much more meaningful and relevant way. We now provide wholesale access to the Bank Secrecy Act data to the FBI, which incorporates the Bank Secrecy Act data in their own Investigative Data Warehouse, where FBI users can query and analyze Bank Secrecy Act data in context with other information collected by the FBI. As we build BSA Direct, the Bureau will provide us in an automated way, the audit and other information necessary for us to discharge our responsibilities relating to the use of the data and to perform our networking function. The early results of the FBI's use of the data have been astounding, and I am sure Special Agent Morehart will share some of these statistics with you today. I am certain that this partnership makes us all safer. I am also certain that this partnership enables the Financial Crimes Enforcement Network to better achieve its mission to safeguard the financial system from the abuse of financial crime.

Everyone in this room knows that September 11th changed the world. What we may not have realized on that bright morning nearly four years ago, we now know for certain: September 11th revealed a new reality – a new paradigm. All the way back to Rome, the paradigm has been that governments can protect their citizens with military might or walls. We learned on September 11th that threats to our nation can no longer solely be met with military might or walls. Our enemies can come from within. They can be neighbors; people shopping at the same grocery store; getting gas from the same stations; using the same ATMs; or, taking the same flight. This new threat demands a

different way of looking at things, a different way of protecting our citizenry. No longer can any of us be passive about the defense of our country. The government cannot do it alone. What we know about this new reality is that *information* is a key to the security of a nation, and information is what the Bank Secrecy Act is all about.

I believe that through the USA PATRIOT Act, the Congress recognized this new reality. You broke down walls that prevented the sharing of information between law enforcement and the intelligence community. Most significantly to the issues being addressed today, you provided us tools to better acquire and share information both between the government and financial institutions, and between financial institutions themselves. These tools highlight a couple of important truths. First, that information sharing really is necessary and important to the national security. Secondly, these tools demonstrate the recognition that financial information, in particular, is highly reliable and valuable to identifying, locating and disrupting terrorist networks that mean to do us harm.

That is why this hearing is so timely and important. Your hearing today has been titled: "The First Line of Defense: The Role of Financial Institutions in Detecting Financial Crimes." Since the beginning of the year, I have traveled across the country and have spoken with bankers, broker dealers, money services businesses, and other financial institutions. These financial institutions have expressed candid concern about how the Bank Secrecy Act is being implemented. I am certain many of you have heard from constituent financial institutions expressing the same concern. Today, we will try to outline for the Committee those concerns, and what we are attempting to do to address them. From my perspective, nothing is more important, simply because I believe that financial institutions are the first line of defense to the security of our financial system. Consequently, we must proceed with the financial institutions in a collaborative way. It must make the partnership envisioned by the USA PATRIOT Act real, if we are to truly achieve our goals.

The goals of the Bank Secrecy Act are simple: (1) safeguarding the financial industry from the threats posed by money laundering and illicit finance by ensuring the financial industry – the first line of defense – has the systems, procedures and programs in place to protect the institution and, therefore, the system from these threats; and, (2) ensuring a system of recordkeeping and reporting that provides the government with the right information - relevant, robust and actionable information that will be highly useful in efforts to prevent, deter, investigate and prosecute financial crime. It is my view that the best way to achieve these goals is to work in a closer, more collaborative way with the financial industry. This regime demands a partnership and an on-going dialogue between the government and the financial industry if it is ever going to realize its true potential. It is why, for example, we are working so hard to implement Section 314(a) of the USA PATRIOT Act in a much deeper way, which will result in a sensitive, yet systemic, two- way dialogue with the financial industry. This dialogue will not only help make our country safer, but also it will educate our financial industry about the risks associated with its business lines and its customers. Knowing more about that risk will

make our financial system safer and more transparent. I am convinced that the financial industry is committed to this partnership and dialogue. Our goal is to do all we can to ensure that the government lives up to its side of the bargain.

As you are aware, while the Financial Crimes Enforcement Network is responsible for ensuring compliance with the Bank Secrecy Act regulatory regime, we do not examine financial institutions for compliance. Instead, we have delegated examination responsibilities to other federal regulators. Even in the absence of examiners, we have a critical role in supporting the examination regime created through our delegations. Following the events of last summer, with the support of Congress generally and this Committee in particular, we made dramatic changes within the Financial Crimes Enforcement Network to enhance our ability to support the examination function and better ensure consistency. We created an entirely new Office of Compliance, within our Regulatory Division, devoted exclusively to supporting and coordinating the examination function being carried out by other agencies. To ensure better utilization of our data, we devoted a significant portion of our analytical resources to supporting our regulatory functions. Within this broad framework, our role in the examination process begins with the issuance of regulations, continues with the provision of prompt Bank Secrecy Act interpretive guidance to regulators, policy makers and the financial services industry, and culminates with ensuring the consistent application of the Bank Secrecy Act regulations across industry lines. We promote Bank Secrecy Act compliance by all financial institutions through communication, training, education and outreach. We support the examination functions performed by the other agencies by providing them access to information filed by financial institutions in suspicious activity reports, currency transaction reports, and other Bank Secrecy Act reports. We also facilitate cooperation and the sharing of information among the various financial institution regulators to enhance the effectiveness of Bank Secrecy Act examination and, ultimately, industry compliance.

As my colleagues in the regulatory agencies and I are well aware, financial industry members across the spectrum are genuinely concerned about the heightened levels of scrutiny being placed upon their institutions. Unfortunately, we continue to see some institutions with very basic compliance failures that have a significant impact, while at the same time, we see institutions across the spectrum working harder than ever to ensure compliance with this regulatory regime. These institutions perceive a significant regulatory and reputation risk being placed upon their institutions by examiners, prosecutors and the press. This perception is not unfounded. Institutions are trying hard to determine what it takes to comply with the Bank Secrecy Act regulatory regime in this time of heightened scrutiny.

Financial institutions have stated loudly and clearly that they are concerned about the regulatory and reputation risk associated with their compliance with the Bank Secrecy Act. There is a perception held by institutions that their examiners have changed the rules of the game. There is also a palpable fear amongst institutions that a Bank Secrecy Act failure today will subject the institution to scrutiny by the Department of Justice and

a potential criminal action. We believe these concerns have had two principal consequences in the past year.

First, we believe many institutions are now filing some of their suspicious activity reports "defensively." In other words, institutions are filing on activity that does not meet the threshold set forth for filing by the regulations and guidance issued about when to file a report. Secondly, we believe that concern about the regulatory and reputation risk associated with the Bank Secrecy Act has led many financial institutions to reassess the risks associated with some of their customer base. This reassessment of risk is not a bad thing; in fact, many in the financial industry have told us that the heightened emphasis on Bank Secrecy Act compliance has caused their institutions to "know" their customers better. However, the ongoing reassessment of risk has also led many institutions to conclude that certain customers pose too much risk for the institution to continue to maintain an account relationship. These institutions have begun to terminate their so-called "risky" account relationships, the money services businesses sector, embassy banking and certain correspondent banking relationships are all industry sectors that have suffered the widespread termination of banking services. Unfortunately, we are concerned that often decisions to terminate account relationships may be based on a misunderstanding of the applicable Bank Secrecy Act requirements, or on a misperception of the level of risk posed.

With respect to the "defensive filing" of suspicious activity reports, at risk is the quality of the information reported. These reports not only provide law enforcement, regulatory agencies and other authorized officials leads indicative of illicit activity, but also provide a fertile source for identifying trends and patterns of illicit activity, as well as compliance-related deficiencies.

We estimate that if current filing trends continue, the total number of suspicious activity reports filed this year will far surpass about 700,000, an increase of more than thirty-seven percent over last year. Preliminary analysis of some of these filings supports the fact that some of this increase is attributed to defensive filing. While the volume of filings alone may not necessarily reveal a problem, it fuels our concern that financial institutions are increasingly becoming convinced that the key to avoiding regulatory and criminal scrutiny is to file more reports, regardless of whether the conduct or transaction identified is indeed suspicious. Such defensive filing results in our database becoming populated with reports that should not have been filed, diluting the value of the information in the database and implicating privacy concerns. Financial institutions from the smallest community banks and credit unions to the largest money center banks are telling us that they would rather file than face potential criticism after the fact.

If these trends continue, consumers of the data – law enforcement, regulatory agencies and intelligence agencies – will suffer. While the most sophisticated analytical tools and data warehouses, including the BSA Direct system, allow users to more efficiently exploit the data, no system can effectively cull defensively-filed reports. Without a review of underlying supporting documentation, it is often impossible to

determine from a review of a suspicious activity report that it has been filed on events or transactions that are not suspicious. Moreover, we are concerned that as financial institutions spend time and resources on increased filing, the quality of reporting on truly suspicious activity will degrade.

It is no great insight to conclude that the conception of a single, clear policy on suspicious activity reporting, combined with consistency in the application of that policy, is the key solution to the defensive filing phenomenon. Addressing the defensive filing phenomenon, like the other important Bank Secrecy Act compliance issues, is our responsibility. We must issue more and better guidance, adding clarity to the requirements for reporting suspicious activity. We must also work with the federal and state regulatory agencies that examine for Bank Secrecy Act compliance to ensure better that all are examining to achieve proper compliance that is consistent with the goals of the Bank Secrecy Act. I reaffirm my pledge to continue to work closely with the industry and all others to ensure the consistent application of the suspicious activity reporting regulation.

The recent situation involving the termination of certain "high-risk" accounts is also a vexing problem. What has happened to the money services business sector provides an important illustration. It is long-standing Treasury policy that a transparent, well-regulated money services business sector is vital to the health of the world's economy. It is important that all sectors of the financial industry comply with the requirements of the Bank Secrecy Act and applicable state laws, and that they remain within the formal financial sector and subject to appropriate anti-money laundering controls. Equally as important is ensuring that the services provided by money services businesses are subject to the same level of transparency, including the implementation of a full range of controls as required by law. If account relationships are terminated on a widespread basis, we believe many of those who use these services could go "underground" and this potential loss of transparency would, in our view, significantly damage our collective efforts to protect the U.S. financial system from money laundering and other financial crime – including terrorist financing. Clearly, resolving this issue is critical to our achieving the goals of the Bank Secrecy Act.

We have already taken both immediate and longer-term steps to better ensure that money services businesses that comply with the law have appropriate access to banking services. The first step was to eliminate the confusion that had arisen concerning the view of the Financial Crimes Enforcement Network and the Federal Banking Agencies concerning the importance of providing banking services to money services businesses that comply with the law. On March 30, 2005, we issued, jointly with the Federal Banking Agencies, a statement on providing banking services to money services businesses. The purpose of the joint statement was to assert clearly that the Bank Secrecy Act does not require, and neither the Federal Banking Agencies nor we expect, banking institutions to serve as *de facto* regulators of the money services business industry. The joint statement also made it clear that banking organizations that open or maintain accounts for money services businesses are expected to apply the requirements of the

Bank Secrecy Act to money services business customers on a risk-assessed basis, as they would for any other customer, taking into account the products and services offered and the individual circumstances.

The specific interpretive guidance to banks followed a few weeks later. Once again, jointly with the federal banking agencies, we issued guidance that outlined with specificity the minimum anti-money laundering controls banks should apply to money services businesses, risk factors associated with certain money services activity, and requirements for filing suspicious activity reports in connection with money services businesses. We believe that this guidance is a significant step forward, not only for the specific issue of money services businesses securing access to banking services, but also for a model of how we can identify and react to Bank Secrecy Act compliance issues, working closely with the federal regulators.

The money services businesses issue also underscores the need for uniform Bank Secrecy Act examination procedures. To that end, we are working together with the Federal Banking Agencies to develop a set of examination procedures for Bank Secrecy Act compliance. We expect to roll out the procedures this summer, along with an aggressive education and outreach campaign. Moreover, we have already begun joint examiner training through a partnership with the Federal Financial Institutions Examination Council that will provide a forum to provide consistent training related to the conduct of examination procedures.

I am also pleased to announce that we are moving forward on an initiative to enhance our coordination with state level regulatory authorities. Working closely with the Conference of State Bank Supervisors, we have developed a model information sharing agreement that we are seeking to execute with regulatory authorities in the various states that conduct examinations for Bank Secrecy Act compliance. As noted earlier, last month, the State Banking Department of New York became the first signatory to such an agreement, reaffirming their commitment to ensuring the uniform application of the Bank Secrecy Act. We are working with many states now to execute similar agreements and hope to complete this process as soon as we are able.

Finally, we are developing a series of free training seminars for industry, regulators, and law enforcement that will undertake many of the issues that are currently vexing all interested parties. Again, we believe that the successful implementation of the Bank Secrecy Act begins with ensuring that we have taken the time necessary to reach the whole of the financial industry.

Coordination among the regulators, industry, and law enforcement is the lynchpin of effective Bank Secrecy Act compliance. We view this as our responsibility as the administrator of the Bank Secrecy Act. We believe this kind of coordination will help clarify the Bank Secrecy Act requirements and supervisory expectations. While we are not so naïve as to believe that these efforts will solve all issues, we are committed to continue to work with the Federal Banking Agencies and our other federal and state

partners to do everything we can as responsible and responsive regulators, to issue guidance, clarify expectations, and answer questions.

Perhaps the best outcome of the events of late has been the express recognition of the need for all the stakeholders in the Bank Secrecy Act arena to work more closely together to reach our collective goals in a consistent manner. We are working closer with the regulatory agencies than ever before. Not only are we issuing joint guidance and developing uniform examination procedures, but we also are sharing information in a deeper and broader way, as well as developing synergies to the benefit of the regulatory regime as a whole. We are also working more closely with law enforcement. For example, we have formed an interagency working group that brings together regulators and law enforcement to work collectively to identify and address money services businesses that may not be complying with the law and regulations. We have entered into a very productive dialogue with the Department of Justice that will ensure better coordination. Finally, we are setting the stage by building platforms, systems and technologies such as BSA Direct that will allow us to leverage information in a way that we never have before.

Madam Chairwoman, Congressman Gutierrez, distinguished members of the Committee, the importance of your personal and direct support of these efforts cannot be overstated. Your oversight will ensure that we meet the challenges that we are facing. I know how critical it is that we do so and we hope you know how committed we are to meeting those challenges. Thank you.

FINANCIAL SERVICE CENTERS OF AMERICA, INC.
A NATIONAL TRADE ASSOCIATION

Statement of

SCOTT K. McCLAIN
Deputy General Counsel

Financial Service Centers of America

Before the
U. S. House Committee on Financial Services
Subcommittee on Oversight and Investigations

Regarding
The First Line of Defense:
The Role of Financial Institutions
in Detecting Financial Crimes

Washington, D.C.

May 26, 2005

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WASHINGTON, D.C. OFFICE: 1730 M STREET N.W. • SUITE 200 • WASHINGTON, D.C. 20036 • TEL. 202-296-3522 • FAX 202-296-7713

Ms. Chairwoman, Members of the Subcommittee, my name is Scott McClain. I serve as Deputy General Counsel to the Financial Service Centers of America, also known as FiSCA. I represent FiSCA on the BSA Advisory Group, and I am grateful for the opportunity to appear today to discuss the BSA compliance experience of the community financial services and check cashing industry.

FiSCA is a national trade association representing over 5,000 neighborhood financial service providers throughout the United States. Our members are classified under the Bank Secrecy Act as "Money Service Businesses" or "MSBs." We provide a range of financial services and products to our customers, including check cashing, money order sales, money transfer services, and utility bill payment services. The industry includes many types of businesses, including publicly traded entities down to corner grocery store "mom and pop" establishments offering ancillary financial services. In responding to the needs of our customers, we provide three things consumers need with regard to their money: liquidity, access and service. Fundamentally, check cashers have the ability to deliver these features at an affordable price; the marketplace has shown us that more traditional financial institutions cannot.

U.S. Treasury Secretary John Snow, acknowledged in a recent address to the Florida Bankers Association, that MSBs "are key components of a healthy financial sector, and it is very important that they have access to banking services."

Julie L. Williams, acting U.S. Comptroller of the Currency, agreed, stating recently that "MSBs play a vital role in the national economy, providing financial services to individuals who are not otherwise part of the mainstream financial system." The check cashing and MSB industry is unquestionably a product of the powerful market forces which have shaped us. We have grown out of a need for convenient, accessible financial services. In short, we serve the working communities of the United States. We serve the working man and woman – and we are very much a part of the mainstream of a healthy financial industry.

The MSB industry has taken significant measures to ensure BSA compliance.

The community financial services industry is clearly on the frontline in the war on money laundering and terrorist financing, and has committed significant resources in this regard. As an industry, we recognize the critical need for strict adherence to BSA compliance requirements, and the need for comprehensive education of MSBs and personnel.

As this Subcommittee is well aware, the MSB industry is subject to many of the core BSA requirements as banks and other financial institutions. These requirements include currency transaction reporting for qualifying transactions in excess of $10,000, suspicious activity reporting, monetary instrument sales record-keeping for money order and travelers check sales, and recording requirements for electronic money transfers. Check cashers and MSBs are now required to be registered with the Treasury, and are required under Section 352 of the USA Patriot Act to have compliance programs

including written AML policies and procedures, compliance officers, employee training programs, and independent compliance examinations.

The industry has taken great measures to ensure wide-scale compliance. In 1993 the National Check Cashers Association (known since 1999 as FiSCA) issued two compliance manuals for the industry: The *FiSCA Compliance Manual* and a corresponding *FiSCA Employee Handbook*. These manuals were the first of their kind for the non-bank financial institutions industry – and were favorably reviewed by FinCEN and utilized by IRS as guidance materials in connection with Title 31 examination procedures. The manuals, which pre-dated USA Patriot Act requirements by nearly a decade, have been periodically updated and supplemented based on amendments to the BSA.

Following the September 11, 2001 terrorist attacks and implementation of the USA Patriot Act, FiSCA issued a *Model Anti-Money Laundering Compliance Program* to assist the industry in meeting new requirements under the Act. The *Model Compliance Program* provides guidance to MSBs for development of internal AML policies and procedures, and employee training programs.

Most recently, in the fall of 2004 FiSCA launched an Internet-based compliance training and examination program, which includes courses for both MSB tellers and compliance officers. The program, also the first of its kind for the MSB industry, provides comprehensive and uniform training to those employees on the front line. The courses include training on the identification of structured transactions and other financial crimes particular to the services and products offered by check cashers/money remitter agents. To date, approximately 6,000 MSB employees in more than a dozen states have sat for the on-line courses and examination. We hope to double the program's performance for 2005.

The FiSCA training and compliance programs have also received generous support over the years from Western Union and MoneyGram, and have been favorably reviewed by federal and state regulators.

Additionally, the major wire remitters have provided extensive BSA support to their thousands of agents across the United States. Virtually all check cashers are agents of Western Union, MoneyGram, or one of several other remitters. These companies are subject to rigorous BSA compliance requirements of their own. They are careful to verify the credibility, responsibility, and compliance programs of their agents. Moreover, these companies provide excellent BSA support materials and training sessions, and also conduct on-site agent examinations.

In addition to its own efforts, the industry has received significant BSA educational support from both FinCEN and IRS. In our experience, FinCEN's recent MSB outreach program has been generally successful in reaching and educating the check cashing and MSB industry as a whole. The guidance materials issued by FinCEN have been widely disseminated. The materials are written in a clear and

concise manner, and have been very well received by the industry. The materials include a "Money Laundering Prevention - An MSB Guide" and corresponding "Recognizing and Reporting Suspicious Activity Relating to Financial Crimes." Moreover, FinCEN and IRS representatives have over the past few years spoken at numerous seminars and workshops sponsored by the national and state MSB associations, and private companies.

We cannot stress enough that FinCEN and IRS have done an exceptionally good job of educating the nation's 20,000+ registered MSBs in the short period since the enactment of the USA Patriot Act in 2001. We grateful for their efforts and continuing support.

The MSB Compliance Record.

The check cashing and MSB industry suffers greatly from the perception that we are an inordinately "high risk" as compared with other financial institutions or businesses. It would appear that this conclusion has been reached with little attention to the actual compliance record of the industry. Notwithstanding all of the concern and recent attention given the topic, there is a paucity of actual cases involving check cashers and money laundering.

Since April 1999, FinCEN has assessed a total of $327,500 in civil penalties against check cashers for BSA violations – yet during the same period it assessed well over $55,000,000 against banks and other financial institutions. Citing recent examples, BSA violations involving depositories frequently involve tens of millions of dollars. Since the passage of the USA Patriot Act, IRS has dramatically increased the number and scope of Title 31 examinations of check cashers. Nonetheless, there has not been a corresponding increase in BSA violations found within the check cashing industry.

As we have witnessed time and again, when banks have terminated their check casher customers, it is more likely that the bank, and not the check casher, has run afoul of compliance requirements. Our experience in Florida, over the last year alone, makes this point clear.

First, in an action that will undoubtedly be familiar to this Subcommittee, on October 12, 2004, FinCEN and the Board of Governors of the Federal Reserve System announced that they had jointly assessed a $10 million civil money penalty against AmSouth Bank of Birmingham, Alabama, for violations of the BSA. A Cease and Desist Order was also issued requiring AmSouth and its parent bank holding company to take certain corrective actions. The penalty against AmSouth was based upon the assessment by FinCEN and the Federal Reserve Board that the bank had failed to establish an adequate anti-money laundering program and the failure to file accurate, complete and timely SARs. The agencies found systemic defects in AmSouth's program with respect to internal controls, employee training and independent review that resulted in failures to identify, analyze and report suspicious activity at the bank. Notably, none of the examples cited by the agencies in the Assessment of Civil Money

Penalties were related to the activities of the bank's check casher customers. Despite all of this, the immediate reaction of AmSouth was to issue notices to its check casher customers throughout Florida, Alabama and Mississippi, terminating their accounts.

Shortly thereafter, on November 5, 2004, the FDIC issued an Order to Cease and Desist to Beach Bank of Miami Beach, Florida. As with AmSouth, the deficiencies noted were those of the bank, not the bank's check casher customers. Nevertheless, Beach Bank terminated its relationship with all of its dozens of check casher customers. This sacrificial offering came despite the fact that the Cease and Desist Order did not require it, and despite the fact that the check cashers were exemplary customers. Further, Beach Bank failed even to examine into the modest measures that would have been required for it to come into compliance. Like the actions of AmSouth, Beach Bank's reaction to the FDIC Order left the innocent parties, check cashers, scrambling to find new banking relationships on short notice.

These are but two examples of a nationwide trend. The fact remains that check cashers are simply not good vehicles for money laundering: they do not take deposits, and the dollar amounts of their transactions is typically low. They are subject to federal and often state compliance examinations. They are required to report qualifying transactions and suspicious activities. More fundamentally, check cashing transactions require the disbursement of funds, rather than the receipt of currency. Virtually any cash-based business, whether it be a restaurant or retail store, presents a far greater risk of money laundering than does a registered, licensed check cashing operation. Virtually any bank in the land will happily open a new account for a gas station or bar, and will accept that customer's cash without question as to its source. Check cashers and other MSBs are unfairly subjected to a different standard.

Current Issues Concerning BSA Compliance.

In our experience, the current BSA reporting system has been largely effective with regard to the check cashing and MSB industry. The industry's compliance record is good. We are, however, aware of the March 23, 2005 Office of the Inspector General Report (OIG 05-033) and the issues raised therein concerning SAR data quality. There are clearly several issues that should be addressed to improve the quality of industry reporting, and also the general BSA enforcement scheme as it affects this industry. We welcome the opportunity to work with this Subcommittee in this regard.

First, with regard to Suspicious Activities Reporting requirements, we recognize that reliability of MSB SAR data is key in the battle against money laundering and financial crime. We are concerned that the current MSB SAR form (TD F 90-22.56) may be unduly complicated for the typical community financial services business. The instructions alone are fully three and one-half pages, are overly technical and incorporate terminology not common to the industry. In several areas, the SAR form applicable to depositories is actually easier to understand.

Obviously, the "Suspicious Activity Information – Narrative" section of the MSB

SAR form is of critical importance to law enforcement. The narrative section is designed to capture the essential details of the suspicious activity and individuals involved. As we have learned from our own experience and the recent Inspector General report, there have been data quality problems with regard to narratives completed by MSBs.

Although FinCEN recently issued a new MSB SAR form for comment, even that form may be unnecessarily complex. We would recommend that the form be completely re-evaluated, and that a more particularized form be created specifically for the community financial services industry, and tailored to the limited services and products we offer.

Referring again to the March 23, 2005 Inspector General Report, concerns have been raised with regard to the number of apparently incomplete SARs filed by both MSBs and depository institutions. While this raises many potential issues, one problem in the data collection scheme is immediately apparent. The MSB SAR threshold for virtually all consumer transactions is $2,000. The threshold, however, for recording monetary instrument sales information is $3,000. This disparity creates a significant data collection gap. Clearly, the scheme requires re-evaluation to cure any related systemic defects.

Moreover, due to the very nature of certain types of suspicious activity, it must be underscored that it is impossible to gather complete data on all suspicious transactions. The classic example includes a situation where a customer attempts a transaction at the $10,000 CTR threshold level, and when he is asked to produce identification the customer leaves the establishment. Clearly, the MSB would not have an opportunity to obtain the individual's identification or other information sufficient to file a fully completed SAR form. Ironically, although a SAR missing key information is facially inadequate, on another level it is indicative of the fact that the general BSA scheme is working to thwart financial crime.

Additionally, OFAC compliance continues to be a confusing problem for the community financial services industry. There are no implementing guidelines for the MSB industry with respect to OFAC. Although the Office of Foreign Assets control did issue in late 2004 a guidance memorandum to MSBs, the notice was limited to money transfers. There is a need for additional OFAC guidance concerning risk assessment in regards to the other products and services provided by the community financial services industry. Moreover, although OFAC compliance is technically not a BSA issue, it would be helpful to industry if the Office of Foreign Assets Control were represented on the BSA Advisory Group.

Consistency of Title 31 examinations by IRS continues to be problematic. Although IRS has greatly improved the level of education of its agents in regards to the community financial services industry, there is clearly a need for consistency in the examination process. As we have experienced, records or documentation that appear to be satisfactory to one agent may be completely insufficient for another. Additionally,

there is no appeal process whatsoever with regard to an agent's determination as to whether an MSB's AML program is insufficient. As the process currently works, if an agent determines that a program does not satisfy BSA requirements, the MSB is issued a form (1112) letter outlining the deficiencies. The MSB has no ability to actually correct the IRS's determinations, even where the agency findings are clearly erroneous. Inasmuch as the examination results may affect the MSB's overall compliance record and banking relationships, there is a clear need for some corrective process at this level.

Most importantly, there must be creation and a process for lines of communication between the community financial services industry and the banking industry. The two industries seem to be operating in separate tracks, without regard to the fact that we serve the same market and are subject to many of the same AML requirements. Although the FinCEN guidelines concerning banking MSBs are a step in the right direction, notwithstanding the recent flurry of activity, not much appears to be happening.

We understand that much of the tension between the community financial services industry and the banking industry stems from a misunderstanding about the nature of the services we provide, and the level of potential risk to the banks that serve us. We prepared to bridge the gap in this regard. Obviously, it is in our best interests to cause the banking industry to be reassured that banking check cashers is safe and profitable.

Additionally, it is critical that the recent FinCEN guidelines be evaluated to determine whether they are, in fact, providing federal bank examiners and banks with the necessary tools and information to make informed decisions concerning MSBs. FiSCA will be hosting on September 26, 2005 a forum to discuss the guidelines, and to determine whether they have staunched the flow of banks leaving the industry, and, hopefully, reassured others to return. We intend to invite not only MSBs, but also the banks, key banking regulators, and decision-makers who will ultimately determine whether the guidelines have achieved their purpose. We ask for your support and involvement in this process.

In conclusion, the community financial services industry is committed to the ongoing battle against money laundering and terrorist financing. As with other sectors of the United States financial system, it is critically important that we protect the integrity and legitimacy of our industry. It is equally critical, however, that our industry be recognized as being a part of a healthy financial industry, and partner in the war on financial crime.

Again, we thank you for the opportunity to present these views.

Statement of Michael F.A. Morehart, Section Chief
Terrorist Financing Operations Section
Counterterrorism Division
Federal Bureau of Investigation

United States House of Representatives
Committee on Financial Services

May 26, 2005

Chairperson Kelly, Congressman Gutierrez and distinguished members of the Committee, I appreciate the opportunity to appear before you to discuss the efforts of the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) and the Federal Bureau of Investigation (FBI), as they pertain to the utilization of information obtained pursuant to the Bank Secrecy Act (BSA), as amended.

I am honored to appear before you today with William J. Fox, the Director of FinCEN, to discuss how FinCEN and the FBI work together closely to ensure the appropriate and successful utilization of BSA information in the U.S. war on terrorism.

Over the years, the FBI has enjoyed a long-standing and productive relationship with FinCEN. The importance and quality of this working relationship cannot be overstated. Under the leadership of Director Fox, our relationship as well as the quality and successes of our joint efforts have flourished. This mutually beneficial working relationship serves as a prime example of what can be achieved when agencies unite in a common effort to ensure the safety of our financial system as well as our nation's security.

The critical role that financial information serves in investigative and intelligence matters cannot be over emphasized. This underlying premise was enumerated in the USA PATRIOT ACT of 2001 (PUBLIC LAW 107-56-OCT. 26, 2001), which, in part, states:

> "...defects in financial transparency on which money launderers rely, are critical to the financing of global terrorism and the provision of funds for terrorist attacks" [31 USC § 5311, SEC. 302 FINDINGS AND PURPOSES, (2)]

Financial information, lawfully acquired, significantly enhances the ability of U.S. law enforcement and intelligence community members to overcome defects in financial transparency as mentioned in the previous excerpt from the U.S.A. PATRIOT Act. Likewise, BSA data is of incalculable value in this important effort. When combined with other data collected by the law enforcement and the intelligence community, investigators are better able to "connect the dots."

More recently, BSA data has proven its utility relative to counterterrorism matters. For example, BSA data is used to obtain additional information about subject(s) under investigation and their methods of operation. Analysis of BSA data permits counterterrorism investigators to acquire biographical and descriptive information, to identify previously unknown subject associates and/or co-conspirators, and, in certain instances, to determine the location of subject(s) by time and place.

The value of BSA data to counterterrorism efforts is reflected in the results of a recent review of BSA data. In this instance, the FBI , using information technology, reviewed approximately 71 million BSA documents for their relevance to counterterrorism investigative and intelligence matters. The review identified over 88,000 Suspicious Activity Reports (SARs) and Currency Transaction Reports (CTRs) that bore some relationship to subjects of terrorism investigations.

The FBI also uses BSA data to identify trends and patterns of relevance to terrorism financing. For example, 64% of the CTRs associated with cash deposits were for amounts which totaled less than $20,000. Conversely, the analysis showed that 75% of the CTRs associated with cash withdrawals were for amounts greater than $20,000. This is consistent with traditional money laundering activity or structuring which involves the deposit of small amounts followed by the withdrawal of larger amounts.

Director Fox and his staff understand the importance of BSA data to the investigative and intelligence missions of the FBI and, in turn, its critical

importance to the protection of the financial infrastructure and the security of the United States. This understanding is evidenced by FinCEN's assistance in helping the FBI develop new ways to access and share the BSA data. As a result, BSA data has been integrated into the FBI's Investigative Data Warehouse (IDW).

By way of background, IDW is a centralized, web-enabled, closed system repository for intelligence and investigative data. This system, maintained by the FBI, allows appropriately trained and authorized personnel throughout the country to query for information of relevance to investigative and intelligence matters. In addition to the BSA data provided by FinCEN, IDW includes information contained in myriad other law enforcement and intelligence community databases.

The benefits of IDW include the ability to efficiently and effectively access multiple databases in a single query. As a result of the development of this robust information technology, a review of data that might have previously taken days or months now takes only minutes or seconds.

In conclusion, the partnership between the FBI and FinCEN is a model for the effective sharing of information. Director Fox has accurately identified a process which maximizes the information collected by FinCEN to be used by the FBI, within the confines of current laws and regulations, in the war on terrorism. The FBI has developed IDW as tool to find the most critical pieces of information included in BSA and other data sets to ensure that the efforts of FinCEN and its banking partners are utilized as directed by Congress to protect the United States. I would like to thank the committee for allowing me to provide this information and welcome the opportunity to answer any questions that the committee may have at this time.

Testimony of
DIANA L. TAYLOR
NEW YORK STATE SUPERINTENDENT OF BANKS

Before the

FINANCIAL SERVICES SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

UNITED STATES HOUSE OF REPRESENTATIVES

May 26, 2005

Testimony of Diana L. Taylor
New York State Superintendent of Banks
May 26, 2005

INTRODUCTION

Good morning Chairwoman Kelly, Congressman Gutierrez and members of the Subcommittee. I am Diana Taylor, Superintendent of Banks for the State of New York.

The New York State Banking Department is the regulator for more than 3,400 financial institutions and financial service firms in New York State. This number includes state-chartered banking institutions, the vast majority of U.S. offices of international banking institutions, all of New York State's money transmitters, check cashers, mortgage brokers, mortgage bankers and budget planners. The aggregate assets of the companies and institutions supervised by the Banking Department are nearly $2 trillion.

Thank you for holding this hearing on an issue that is of great interest to those of us who oversee the financial services industry at the state level, and who are very concerned about the sometimes conflicting priorities of regulation, law enforcement, and the ability of necessary businesses to operate. This has become a very serious concern as issues of financial crimes, especially money laundering, figure so prominently today.

On 9/11 the New York State Banking Department, from its vantage point two blocks south of the World Trade Center, learned only too well how destructive terrorism can be. But in the days that followed, as we helped the financial system to recover, we saw how crucial that system is to maintaining our way of life in America. The entire country held its breath as first the banks, the bond, and then the equity markets got back on their feet. In the aftermath, financial institutions, regulators and law enforcement gathered together in a series of meetings to brainstorm on how to detect and prevent our financial system from being used to further terrorist aims. Today, rather than working together to defeat terrorism, these three sectors are often working at odds with each other.

I would now like to address the three points you mentioned in your letter, Chairwoman Kelly: the recent Memoranda of Understanding between my Department and FinCEN and the IRS; challenges we are currently facing with regard to BSA/AML compliance in the Money Services Business (MSB) area; and our interaction with the IRS when monitoring MSBs.

1. IRS and FinCEN MOUs

First, FinCEN and the federal banking supervisors released crucial guidance on BSA/AML compliance for banks doing business with MSBs such as check cashers and money transmitters. This very welcome development promises a strong step in the direction of clarifying for the banks their BSA/AML requirements with respect to MSB customers. This guidance assists banks in determining the measures they should undertake. One very important issue that was made clear is that banks are not expected to become or act as MSB regulators. At the same time, separate guidance was issued by FinCEN to MSBs clarifying their BSA/AML requirements.

Second, significant progress has been made toward a plan to achieve a coordinated approach among regulators. Over the winter, the Conference of State Bank Supervisors (CSBS) worked diligently with all of the states, our federal bank regulatory counterparts, FinCEN and the IRS to produce two model Memoranda of Understanding (MOUs) setting forth procedures for the exchange of certain BSA information between the states and FinCEN and the IRS, concerning bank and MSB examination information, respectively.

This is great progress. I was proud to be the first to sign these MOUs on behalf of my state of New York and am thrilled to be able to tell you that on June 1st more than 30 states plan to take part in an MOU signing ceremony at the CSBS Annual Meeting.

Another aspect of our agreement is that the states will receive analytical tools from FinCEN that will maximize resources and highlight areas and businesses with higher risk for money laundering. The agreement with the IRS will allow for examination-sharing to reduce duplicative efforts and establish an ongoing working relationship.

This is an unprecedented co-operative agreement. This effort recognized that the state regulators are an important part of the solution. We have all recognized that no one of us can be effective in this area without the others. Each one of us has resources needed by the others to do their jobs effectively.

Both FinCEN and the IRS were exceptionally cooperative in outreach efforts to answer all state questions about the agreements, and as a regulator who is keenly concerned about the MSBs enjoying a viable and visible future, I am deeply grateful for this. Not only will these agreements provide additional information to the regulators, the more information FinCEN receives and is able to analyze, the better the guidance from state and federal regulators will be.

I will be happy to keep you and your committee informed on how this co-operation continues.

2. Challenges we are facing with regard to BSA/AML Compliance in MSB area

You are aware of the fact that many banks have decided not to do business with MSBs as a result of BSA compliance issues. The guidance and MOUs I just referred to will hopefully ameliorate this issue. We will all keep you informed.

There are other challenges. One that is particularly worrisome is the issue of who, if anyone, should regulate the agents that MSBs employ to do their business, and if so, what should that regulation entail? In New York State, there are approximately 73 money transmitters, but there are 29,000 agents. Clearly, this would be an enormous task.

Then there is the issue of SARs. In the current environment, financial institutions are worried that they will be punished severely for seemingly minor infractions, even when they are operating responsibly and have state of the art compliance systems in place. There is no system in the world which is going to catch every single instance of money laundering or terrorist financing.

The Financial Services Roundtable agrees that there should be some room for error. In their May 10th petition, the FSR recommends that FinCEN and law enforcement agencies provide additional guidance on SARs that includes 'safe harbor' language. I hope that this recommendation will be given serious consideration, as I believe that automatically penalizing banks for isolated instances of late filings or missed filings in the context of an otherwise solid compliance history is an unhelpful practice, as it gets us no closer to those who are actually committing the crimes.

We have a long way to go in coordinating and communicating with law enforcement. The issue of "defensive SARs" is a symptom of a much larger problem. There are some who perceive that prosecutors are going after financial organizations for failure to file SARs – sometimes a single SAR, without giving due consideration to prior compliance and SAR filings. Because of this, some regulators are telling institutions that if they are at all suspicious of a transaction, file a SAR, which has resulted in FinCEN being inundated and begging people not to file "defensive" SARs. We need to make sure that everyone understands the standards to which they are being held, and that those standards make sense.

While we have taken great steps forward in terms of cross-agency communication, particularly in the area of the MSBs, we have a long way to go before we can agree on a sensible protocol that keeps our financial entities

secure, and succeeds in isolating and prosecuting the real evil doers. The protocol should envision regulators playing their traditional role in helping their regulated entities stay on the straight and narrow, knowing what is expected of them; law enforcement sharing information with regulators in tracking down the bad actors and prosecutors going after the people who have intentionally done something wrong – not a bank that neglected to file a SAR.
I believe that the basic problem lies in the way we play our respective roles. For instance, law enforcement may expect SAR filings to be a simple matter and, as a result, they have high expectations; yet they've issued little guidance. Some financial institutions may still look at SAR requirements as a burden that they should not be required to shoulder. Finally, prosecutors may look to indict without fully appreciating or understanding the complexity and operational volume of the financial industry, of which a SAR is but one piece. These different expectations and roles, shaped as they are by a partial understanding of each other's mission is at the root of our problem. I hope that the recent progress in carving out the MOUs shows that we can work to better understand and be responsive to each sector's needs.

At the same time, we are all very concerned with choking off the supply of money to terrorists and other criminal elements. This is a critical task. I agree with Bill Fox, when he said about world changes that after 9/11 the Bank Secrecy Act moved to the front and center of the banks', regulators' and law enforcement world and, as he put it: "...the changes in orientation that have occurred relating to the Bank Secrecy Act are...here to stay."

We need to work together to make sure the laws are having the intended consequences, which are to stop and punish criminal or terrorist activities, but at the same time to allow our financial system to operate efficiently and effectively.

3. Interaction with IRS when monitoring MSBs

We are looking forward to building our relationship with the IRS with regard to MSB supervision. As we are just now beginning this cooperative arrangement, I cannot give a progress report at this point, except to say 'so far so good'. However, I am looking forward to giving you a progress report of our accomplishments and mutual achievements in the not too distant future.

The real lesson of this discussion is that to have a real and lasting effect on illegal activity, it is essential that the agencies involved in the regulatory, investigative and enforcement frameworks for banks proactively cooperate with each other.

Just as we forged an MOU between the states, the federal banking agencies, FinCEN and the IRS, I think we need to come to an understanding, perhaps an MOU, with the DOJ so that its actions and those of the US attorneys are not at cross-purposes to those of the regulators. We must once again brainstorm together to find a way to detect and prevent our financial system from being used to further terrorist aims. To achieve this crucial goal, we must all work together.

Center for Financial Privacy and Human Rights

Free markets are a necessary condition of liberty, prosperity and tolerance.

For Immediate Release: http://www.financialprivacy.org
Thursday, May 26, 2005

The Center for Financial Privacy and Human Rights applauds Rep. Sue Kelly (NY), chair of the House Financial Services Subcommittee on Oversight and Investigations, for her leadership reversing the lack of Congressional oversight of our anti-money laundering programs.

"We should honor the principles of good government and end policies that don't work," said J. Bradley Jansen, executive director. "Flooding law enforcement with a deluge of reports of normal behavior by law-abiding citizens undermines our security."

The Center urges the subcommittee to recognize the benefits to security of stronger privacy policies. Today's newspapers report both bank and state government employees selling information to identity theft rings—a mode of terrorist financing. The subcommittee should examine the cost to benefit analysis of our policies. The additional regulations of Title III of the USA PATRIOT Act place a disproportionate burden on smaller institutions that contributes to a consolidation of assets in the financial system and limits consumer choice. Care must be taken to protect innocent victims against abuses reporting inherently subjective "suspicious" behavior.

For more information, please contact:
J. Bradley Jansen
bjansen@financialprivacy.org

Bretigne Shaffer
Bretigne@financialprivacy.org
(646) 226-4011

The Center for Financial Privacy and Human Rights, a non-governmental advocacy and research organization, was founded in 2005 to defend privacy, civil liberties and market economics. The Center is the only non-profit human rights and civil liberties organization whose core mission recognizes traditional economic rights as a necessary foundation for a broad understanding of human rights.

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