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BANK SECRECY ACT'S IMPACT ON MONEY SERVICES BUSINESSES

HEARING

BEFORE THE

SUBCOMMITTEE ON
FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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BANK SECRECY ACT'S IMPACT ON MONEY SERVICES BUSINESSES

Wednesday, June 21, 2006

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:07 a.m., in room 2128, Rayburn House Office Building, Hon. Spencer Bachus [chairman of the subcommittee] presiding.

Present: Representatives Bachus, Baker, Kelly, Biggert, Feeney, Hensarling, Neugebauer, Price, McHenry, Maloney, Sherman, Moore of Kansas, Waters, Carson, McCarthy, Green, and Clay.

Ex officio present: Representative Frank.

Chairman BACHUS. Good morning. The subcommittee will come to order.

The purpose of today's hearing is to review the oversight and regulation of money services businesses (MSB's). More specifically, we will address the impact that the Bank Secrecy Act and related financial institution account discontinuances have had on MSB's.

Despite expressions of concern by members of this Congress to both regulators and financial institutions to treat MSB's fairly, I remain concerned that financial institutions continue to unjustifiably sever their relationships with MSB's.

MSB's provide a valuable service to consumers, and in some instances are the only financial services available to them.

No one disagrees that banks and MSB's should comply with any money laundering guidance issued by their regulator. Nonetheless, terminating an entire regulated industry and forcing its customers into the underground financial system itself creates a significant money laundering risk.

MSB's are regulated at the State level, and are required to comply with the Bank Secrecy Act at the Federal level. Currently, 28 States and the District of Columbia have regulations requiring MSB's to be licensed by the State banking agency, and some of these States have specific laws regarding transmittals abroad. In many of these States, an MSB has to submit to a rigorous review, including providing financial statements and internal audit reports and permitting background checks on owners and managers. Furthermore, the licensing process requires annual training, current BSA compliance programs, and the submission of a surety bond.

Since the adoption of the USA PATRIOT ACT, MSB's have been required to adopt a written anti-money laundering compliance program and to conduct independent reviews of their programs.

MSB's are also required to register with FinCEN and are examined for BSA compliance by the IRS. Certain MSB's are also required to file suspicious activity reports for transactions involving at least $2,000. In addition, MSB's are required to file CTR's for cash transactions of more than $10,000, and must also maintain information on fund transfers of $3,000 or more.

Despite the increased regulation of MSB's, the bank regulators and their examiners have classified all MSB accounts as high-risk, regardless of whether there have been any actual problems.

Banks have been required to investigate the money laundering compliance standards of the MSB's, forcing them to become the de facto regulator of these institutions.

FinCEN and the Federal banking regulators have issued guidance twice. Unfortunately, in my opinion, the requirements continue to be vague, subjective, and burdensome to the banks.

Over the past year, at least three national banks have ceased offering services to MSB's, and some State-chartered institutions have also discontinued service, and this is across-the-board blanket discontinuance by these institutions of all MSB's.

In response to concerns raised over the previous year by MSB's and financial institutions, FinCEN issued an advanced notice of proposed rulemaking in March 2006. The comment period for the ANPR ends on July 10, 2006.

I am hopeful that today's hearing and discussion will shed some light on this issue and be taken into consideration as FinCEN and the bank regulatory agencies move forward with the rule.

In closing, I would like to ask unanimous consent that Congressman Rangel, the ranking member of the Ways and Means Committee, be allowed to participate in today's hearing.

The Chair now recognizes the Ranking Member of the Full Committee, Mr. Frank, for his opening statement.

Mr. FRANK. Thank you, Mr. Chairman, I appreciate it, because I am not going to be able to stay, but this is something which I had raised.

We, on our side, received a letter from our extremely distinguished colleague, Mr. Rangel, who is the Ranking Democrat on the Ways and Means Committee, but who also represents a district in New York where the MSB's play a significant role.

Now, I should say that we have been concerned, many of us, from time to time, about potential consumer abuses with some of the irresponsible MSB's, and things like payday lending and elsewhere, but being concerned about abuses does not mean that you think that the function is useless, and I would like to get people at the lower end into banks. I think getting people banked is a good thing for them. We have pushed for that.

Our colleague from California, Ms. Waters, has been a leader in trying to get lifeline banking to try and encourage people into the banking system, but with all of that, there is still a role for the MSB's, and it is a role that many lower-income people are going to be relying on, and Mr. Rangel, who represents a district in which they play an important part, came to us, because he had

heard from some of these entities that service his constituents that they were being turned down by the banks, and when we checked, it was one bank, in particular, that was cited as having turned these down, and we asked the bank what was involved. The bank's top people for this came to see our staff and said it is the uncertain atmosphere that has been created in the regulatory area, and sometimes, I will say to my friends and regulators, people hide behind you unfairly. Sometimes they have a legitimate point.

It does seem to me that we have some uncertainty here, and obviously we want to prevent money laundering, but we all have a temptation to kind of overdo, in some cases, when the negative consequences of the overdoing do not fall on us, and I think this may be a case where the regulators have not been sufficiently sensitive to the impact uncertainty can have, and so, I am very glad that we have this hearing.

I hope what will come out of this is a further movement towards a situation in which there is all the regulation we need.

We obviously do not want there to be terrorist schemes being financed here.

On the other hand, from what Mr. Rangel has said, and from what we have gleaned, it does seem to me that the impact has been greater than would be called for by terrorism. I do not think all of these MSB's in Harlem are potential terrorist financing entities, although we will defer to New York State's expertise in this, but I think that we probably—I think that this is one of these areas where we have conceptual agreement that we want regulation so that we do not have abuses, but we do not want to put legitimate market entities out of business.

I do not think we have reached that level of accomplishment yet.

So, I look forward to our being able to work together, and we will hear from the regulators, and then we will hear from some of the people in the business.

I hope we can come out of this at some point fairly soon with a more specific set of regulations and with guidance and with some way for the businesses to look into it, because as I said, I think we are now in a position where the effect of the regulation is to shut down some businesses and deny people some services.

I do not think anyone is to blame in the sense of anybody's set out to do something bad, but the interaction of regulators, banks, and businesses here is nothing, and what we hope to be able to do is, particularly between the banks and the regulators, promote the right kind of interaction, so we can have a degree of confidence, never certainty, that we have done everything we can to reduce the abuses.

I also—as I said, I want very much to work with the regulators here, but also—I am a great believer in free speech, and I voted against fining people, people saying naughty words on television, but I would like to ban metaphors from use in discussions of public policy. I think it would be very helpful, but as long as it is still constitutional, I will say I do think, in the area—particularly in this area of regulation, we have told the regulators to find needles, and we should refrain ourselves from the instinct to build bigger and bigger haystacks as they look for the needles, and I think, in some cases, we may get into that direction.

Thank you, Mr. Chairman.

Chairman BACHUS. Thank you, Mr. Frank. Mr. Hensarling?

Mr. HENSARLING. Thank you, Mr. Chairman. For, I think, the second time this month, I find myself in complete agreement with the ranking minority member. I am not sure who should be more worried, him or me.

Mr. FRANK. Mr. Chairman, point of personal privilege.

Chairman BACHUS. You are recognized.

Mr. FRANK. I will drop it.

Mr. HENSARLING. I knew I would regret saying that.

Mr. Chairman, let me thank you first for holding this hearing.

Along with Mr. Moore of Kansas, I helped author the regulatory relief bill for financial institutions, and throughout that exercise in legislating, we knew that each and every regulation that had been imposed upon our banking sector at one point in time made a lot of sense. Frankly, there are a number of regulations that still create benefits for our economy, and for our Nation, but too often, we never go back and we look at the cost, the costs that are being imposed upon this same economy and same Nation, and we often find out that, among other things, both the bureaucracy and Congress can often exceed—excel at unintended consequences, and so, I am glad that you are holding this hearing, because now we see a fair amount of evidence, if not alarming evidence, that a number of our financial institutions are deciding to drop MSB's as customers, and I think principally due to increased cost, to a lot of uncertainty, due to a lot of ambiguity, and we have to take a very serious look at what that means to our Nation, what is happening to the cost associated with the MSB's as, increasingly, they get dropped as bank customers.

What is ultimately the impact upon low-income citizens, low-income neighborhoods?

Is our Nation really more secure if we start to drive MSB's into the non-banking sector?

Finally, how much duplication do we have here? Are we coming up with a system that essentially makes our financial institutions de facto regulators of MSB's when, apparently, on paper, we have a number of other institutions that are supposed to serve that purpose.

So, Mr. Chairman, again, I thank you for holding this very important hearing, and I yield back.

Chairman BACHUS. I thank the gentleman from Texas.

The gentlelady from New York, Ms. Maloney.

Mrs. MALONEY. I thank you so much, Chairman Bachus, for holding this very important hearing. The issue of bank discontinuance of check cashers is very important to my district, and to New York City, in general.

I joined Mr. Rangel in requesting this hearing and, at one point, was a member of the city council partially within the boundaries of Congressman Rangel's district. So, I know firsthand that the financial services industry, in many cases, made a decision not to open banks in that area, so the check cashers were really the only way that many people could achieve services.

So, they were very important, and I saw firsthand during my days on the city council the service that they provided to my constituents there, and continue to provide throughout New York City.

I would like to especially welcome all of the witnesses, but especially my constituents, Superintendent Taylor, and Gerald Goldman of the Financial Services Centers of America.

As a New Yorker, I know money services businesses form a very important part of the financial services district industry in my home town, and many of my constituents depend on their services for their financial needs.

There are about 150 money service businesses in New York City, in over 750 locations, mostly in neighborhoods not served by banks.

They employ about 4,000 New Yorkers, and serve many thousands more each day.

In recent years, the money services businesses in my district have repeatedly asked me to help them with the problem of banks discontinuing check cashers' and money transmitters' accounts.

Like all businesses, these need a bank account and access to bank services.

In fact, because of their substantial cash flows, they need a bank with a local presence.

This issue came to a crisis point 2 years ago in New York, when J.P. Morgan Chase, which serviced about 75 percent of the MSB's in New York State, announced that it was terminating all MSB customers.

This left North Fork Bank as the sole bank doing business in New York with check cashers, and I understand even they have stopped doing business with money transmitters.

In late 2004, shortly after the J.P. Morgan announcement, I spoke directly to senior J.P. Morgan Chase officers and asked them what their reasons were for discontinuing money services businesses.

They said that the OCC guidance effectively required them to do so.

I then called the Director of OCC, Jerry Hawke, and urged him to take a more balanced approach to this issue. I followed up with a letter, and he responded with a letter denying that the OCC was encouraging banks to cut off MSB's.

Basically, the banks were pointing fingers at the regulators, and vice versa.

I was, however, encouraged that the heightened scrutiny this issue was receiving from myself and others in Congress, including Chairman Bachus, led to the FinCEN conference in late spring of last year on this issue, which appeared from the reports to have been a very, very positive development.

Right after the conference, I had the opportunity to ask Bill Fox, then-director of FinCEN, and Julie Williams, acting head of OCC, whether FinCEN would continue to support MSB's as viable financial institutions.

Director Fox said, "The check cashers are critical to the Nation's economy and to the world's economy." Rebutting critics who assert that MSB's are not regulated, he said, "They are regulated by us and the IRS enforces those regulations," as well as by the States

that license them. He pointed out that MSB's are subject to the Bank Secrecy Act and make filings under that act.

Fox and Williams attributed the discontinuance problem to what Fox called, "a misperception by banks of the level of risk involved in doing business with this sector," and asserted, "We are having success in educating them."

Unfortunately, this does not seem to have happened. If anything, the situation seems worse now. Banks seem to have been frightened by the amount of work required by the guidance.

Even though the guidance said that banks should not arbitrarily treat MSB's differently, it requires banks to do much more due diligence than they have to for other types of business.

MSB's are on the OCC's list of high-risk businesses, but so are car dealers, lawyers, accountants, investment bankers, broker-dealers, travel agencies, and leather goods stores, just to name a few.

What does the OCC require in the way of due diligence for them? Is the standard higher for this particular industry?

I would like to see the regulators adjust the guidance to the real level of risk.

Frankly, FinCEN seems to have lost interest in advocating for a solution on this, and I am concerned that the other regulators do not see it as their responsibility to help MSB's function. I hope we can correct that by working together.

If we do not, we will only drive MSB's and their customers underground, where they are much more susceptible to money laundering and fraud.

Thank you very much for coming, and I look forward to the testimony.

Chairman BACHUS. Are there any more members wishing to make an opening statement? If not, at this time, I would like to introduce our first panel.

Mr. Don Carbaugh is the acting Associate Director for regulatory policy and programs, Financial Crimes Enforcement Network, FinCEN.

Ms. Eileen Mayer is the Director of Fraud/Bank Secrecy Act, the Small Business/Self-Employment Division of the IRS.

Ms. Ann Jaedicke is the Deputy Comptroller for Compliance Policy, Office of the Comptroller of the Currency.

At this time, I will ask Ms. Maloney to introduce our fourth witness.

Mrs. MALONEY. Thank you so much. It is my pleasure today to welcome my long-time friend, Diana Taylor, the superintendent of banks for the State of New York. Ms. Taylor has served in this position since 2003, and provides great insight and perspective into the field of financial services.

Having worked in both the public and private sectors, she acted as the deputy secretary for finance and housing to Governor Pataki, served as the chief financial officer for the Long Island Power Authority, and helped found M.R. Beal & Company, an investment banking firm.

I am looking forward, as always, to Ms. Taylor's testimony, as well as her responses to our questions about money services businesses.

Thank you so much for being here, Diana.

Chairman BACHUS. Thank you. Let's start with Mr. Carbaugh and proceed.

STATEMENT OF DON CARBAUGH, ACTING ASSOCIATE DIRECTOR FOR REGULATORY POLICY AND PROGRAMS, FINANCIAL CRIMES ENFORCEMENT NETWORK

Mr. CARBAUGH. Thank you, Mr. Chairman.

Chairman Bachus, Ranking Member Sanders, and distinguished members of the subcommittee, I appreciate the opportunity to appear before you today to discuss initiatives that the Financial Crimes Enforcement Network is implementing under the Bank Secrecy Act relating to the money services business sector.

Your leadership and commitment to understanding and publicly discussing the issues confronting this industry is critical not only to the safety and soundness of our financial system but also to our Nation's security.

I am pleased to be here today with Eileen Mayer from the IRS, Ann Jaedicke from the Office of the Comptroller of the Currency, and Superintendent Taylor from the New York State Banking Department.

Each of these agencies plays a vital role in implementing Bank Secrecy Act requirements. I am happy to say that we have forged a strong working relationship in our united effort to regulate the money services business industry.

The Financial Crimes Enforcement Network has regulated the money services business industry under the Bank Secrecy Act since the 1990's.

Issues surrounding the money services business regulatory regime, including the need to identify unlicensed and unregistered money services businesses, conduct robust Federal Bank Secrecy Act compliance examinations, and ensure access to banking services, continue to be at the forefront of our agenda.

As you are aware, there has been mounting concern among FinCEN financial regulators and the money services business industry regarding the ability of money services businesses to obtain and maintain banking services. Many banks have stated their uncertainty as to the appropriate steps that they should take under the Bank Secrecy Act to manage potential anti-money laundering and terrorist financing risks.

At the same time, the money services business industry has expressed concern that misperceptions of risk may be unfairly labeling them as unbankable.

Individual decisions to terminate account relationships, when compounded across the U.S. banking system, have the potential to result in a serious restriction in available banking services to an entire market segment. The money services business industry provides valuable financial services, especially to individuals who may not have ready access to the formal banking sector.

If money services business account relationships are terminated on a widespread basis, we believe that many of these businesses could go underground.

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 achieving the goals of the Bank Secrecy Act.

In March 2005, the Non-Bank Financial Institutions and Examinations Subcommittees of the Bank Secrecy Act Advisory Group jointly hosted a fact-finding meeting to solicit information from banks, as well as money services businesses, on issues surrounding the provision of banking services to the money services business industry. Subsequently, in April 2005, FinCEN and the Federal banking agencies issued interagency guidance to the banking industry on regulatory expectations when providing banking services to domestic money services businesses.

FinCEN issued a companion advisory providing guidance to money services businesses on what they should expect when obtaining and maintaining banking services.

Currently, based upon what we have learned at the March 2005 meeting, and in subsequent discussions with other Federal and State regulators, law enforcement, and the industry, we have developed, and are implementing, a three-point plan, which is detailed in my written testimony, for addressing these issues.

First, guidance that outlines with specificity Bank Secrecy Act compliance expectations when banks maintain accounts for money services businesses.

Second, education that provides banks and bank examiners enhanced education on the operation of the variety of products and services offered by money services businesses and the range of risks that each may pose.

Third, regulation that strengthens the existing Federal regulatory and examination regime for money services businesses, including coordinating with State regulators to better ensure consistency and leverage examination resources.

We also continue to work closely with our colleagues at the Internal Revenue Service to enhance the examination regime through the development of revised Bank Secrecy Act examination procedures, information sharing, and examination targeting.

Additionally, we continue to work closely with the Conference of State Bank Supervisors and State regulators on these issues.

Executing individual agreements with State banking agencies will ensure better coordination and synergy with State-based examiners and improve consistency in examination processes.

We also intend to continue working on developing indicators for law enforcement and financial institutions to help identify unlicensed and unregistered money services businesses.

By providing law enforcement, banks, and other financial institutions with indicia of illicit activity, they will be better able to help us identify money services businesses that choose to operate outside of the regulatory regime.

Lastly, I would like to comment briefly on our registration efforts.

Identification of money services businesses subject to the Bank Secrecy Act requirements is an essential first step in effective regulation.

Our effort to identify money services businesses begins with the Bank Secrecy Act requirement to register with FinCEN and maintain lists of agents.

However, the industry is largely composed of small, unsophisticated businesses whose primary business is often something other than the money services that they provide, frequently to the poor and unbanked.

Additionally, due to language barriers within certain communities, there may be confusion regarding the applicable regulations.

We recognize that the complexity of our current approach to MSB registration may be contributing to a lack of registration, and we are working on solutions to provide a more efficient and reliable method for identifying money services businesses.

In conclusion, Mr. Chairman, we are grateful for your leadership and that of the other members of the subcommittee on this issue, and stand ready to assist you in your continuing efforts to ensure the safety and soundness of our financial system.

Thank you for the opportunity to appear before you today.

I look forward to any questions you may have regarding my testimony.

[The prepared statement of Mr. Carbaugh can be found on page 75 of the appendix.]

Chairman BACHUS. Thank you, Mr. Carbaugh.

Ms. Mayer?

STATEMENT OF EILEEN C. MAYER, DIRECTOR, FRAUD/BANK SECRECY ACT, SMALL BUSINESS/SELF-EMPLOYED DIVISION, INTERNAL REVENUE SERVICE

Ms. MAYER. Good morning, Mr. Chairman, and members of the subcommittee.

I am pleased to be with you this morning to discuss the IRS's role in administering the BSA.

Specifically, the IRS is responsible for examining for BSA compliance all financial institutions not currently examined by a Federal functional regulator. These entities include money services businesses such as check cashers, issuers of traveler's checks, and money transmitters, casinos, certain credit unions, dealers in jewelry and precious metals, and insurance companies.

The largest of these groups is the MSB's. No one is sure just how big the universe of MSB's may be or how many of them are required to register with FinCEN under the BSA.

What we do know is that, currently, there are more than 24,000 registered MSB's. FinCEN maintains a list of registered MSB's on their Web site. The IRS is committed to our important role in enforcing the BSA.

In late 2004, we created the Office of Fraud/BSA within the Small Business/Self-Employed Division. That is the office I now head. This allows us to utilize field agents whose sole responsibility is to examine MSB's, casinos, and other entities covered by the BSA but not monitored by traditional Federal regulators.

Previously, agents conducting BSA exams were doing so as collateral duty to their more traditional income tax enforcement work.

Today, we have approximately 350 BSA examiners in the field, and it is my hope that we will get the number up to 385 in the not-too-distant future.

This increased workforce is reflected in the number of Title 31 exams we have been able to conduct. In FY 2005, we examined 3,680 MSB's.

Through late May of this year, we have almost exceeded that total, and expect to examine over 6,000 by the end of the fiscal year.

We are also leveraging our resources with those of the States.

In late April, Commissioner Everson announced agreements with 33 States and Puerto Rico to begin sharing BSA information.

These agreements will allow the IRS and the participating States to share information and leverage their resources to ensure that MSB's are complying with their Federal and State responsibilities.

We recognize, Mr. Chairman, that the money services business industry provides valuable financial services, especially to individuals who may not have ready access to the formal banking sector.

It is a longstanding treasury policy that a transparent, well-regulated money services business sector is vital to the health of the world's economy.

We find it regrettable that compliant MSB's are being rejected by banks over fears of potential non-compliance with BSA requirements. Our examinations do not support those fears.

Of the over 7,300 MSB's that we examined last year, and this year thus far, there have been only 41 cases that merited referral to FinCEN for consideration of civil penalties or the IRS criminal investigations unit for possible criminal penalties. For the most part, the violations that we find are minor or technical in nature and can be corrected easily.

When a minor or technical violation is noted, we issue a letter to the MSB listing the violation. Unless our letter is challenged, we expect those violations to be remedied in a timely manner, and to ensure that happens, our examiners will conduct a follow-up examination within 6 to 8 months.

If no violations are found in the original exam, we issue a different letter showing that the business has been examined and no violations were found.

Mr. Chairman, I hope my remarks this morning, as well as my written statement, submitted for the record, address many of the questions that the subcommittee has relative to the IRS's role with the BSA, and specifically its examination of MSB's.

I will be happy to respond to any additional questions that the members of the subcommittee may have.

[The prepared statement of Ms. Mayer can be found on page 107 of the appendix.]

Chairman BACHUS. Thank you, Ms. Mayer.

Ms. Jaedicke.

STATEMENT OF ANN F. JAEDICKE, DEPUTY COMPTROLLER FOR COMPLIANCE POLICY, OFFICE OF THE COMPTROLLER OF THE CURRENCY

Ms. JAEDICKE. Thank you, Chairman Bachus, and members of the subcommittee. I appreciate the opportunity to discuss the Bank Secrecy Act's impact on money services businesses.

Over the past couple of years, the OCC has taken many actions to help ensure that MSB's are not unfairly denied access to a bank account. For example, we participated in numerous meetings and conferences with representatives of the banking and MSB industries to help us understand the issues.

With the other regulatory agencies, we issued interagency guidance and examination procedures that address MSB issues. We have provided instructions and training to our examiners on MSB's.

As the regulator of national banks, the OCC has long been committed to ensuring that all Americans have fair access to the banking system and financial services. We recognize the positive role that MSB's play in this process, and the OCC is very concerned about the problems that MSB's are experiencing in obtaining banking services.

The reasons some MSB's have lost access to banking services are complex and derive from a multitude of factors, including the risks presented by some MSB accounts, the costs associated with maintaining MSB accounts, and banks' concerns about law enforcement and regulatory scrutiny. Notwithstanding these concerns, there is still a significant number of national banks that continue to provide accounts and banking services to MSB's.

OCC officials have met often over the last 18 months with various representatives of the MSB industry to better understand the problems MSB's face. For example, in March of 2005, OCC representatives attended the fact-finding meeting on MSB's hosted by FinCEN. Later that month, the OCC hosted a teleconference for the banking industry in which we discussed a variety of issues, including MSB's.

Also, the OCC participated in a nationwide teleconference on MSB issues hosted by the American Bankers Association. And, in April of 2006, the OCC again joined various Federal, State, and industry representatives at an MSB regulatory policy meeting sponsored by the ABA.

All of these initiatives have helped to further the understanding of all parties, and we at the OCC are committed to continuing this dialogue.

As our knowledge and understanding of MSB's and their issues have grown, our guidance has evolved. Along with FinCEN and the other Federal banking agencies, in April of 2005, we issued interagency guidance on MSB's. That guidance has since been incorporated into the Interagency Bank Secrecy Act and Anti-Money Laundering Manual and into our interagency training.

More recently, on March 10, 2006, FinCEN issued an advanced notice of proposed rulemaking to solicit updated facts concerning MSBs' access to banking services, as well as recommendations regarding additional guidance or regulatory action that might address these concerns. The comment period closes soon, and the

OCC will again work with FinCEN and the other Federal banking agencies to provide, if needed, different guidance to the banking industry that is clear and consistent. We commend the efforts of Director Werner for the leadership he has shown in addressing this important issue.

The BSA has been the focus of regulatory, Congressional, and media attention for the past few years, and, certainly, there has been an increasing sense of urgency for all of us since 9/11. The intense focus on BSA compliance may have led to misperceptions about the OCC's policies and practices relating to MSB accounts at national banks, so let me be clear.

First, the OCC is not the supervisor of MSB's and does not expect national banks to be the de facto regulators of their MSB customers. Second, the OCC does not, as a matter of general policy, require any national bank to close the accounts of an MSB or any other customer. Third, the OCC does not discourage banks from having MSB accounts. We expect banks that open and maintain accounts for MSB's to apply the requirements of the BSA, as they do with all accountholders, on a risk-assessed basis.

Finally, the OCC has taken many steps to ensure that our examiners are acting in conformance with our agency policies. For example, when the interagency guidance was issued, we provided copies to every national bank examiner with instructions that it was to be followed immediately. As previously discussed, the interagency guidance has been incorporated into the interagency BSA manual, and Comptroller Dugan has directed that the procedures in the interagency manual be used at every BSA/AML exam. We have trained our examiners extensively on the procedures in the interagency manual.

Perhaps most significantly, in the past year, senior OCC officials have held nationwide teleconference briefings with the entire national bank examination force. In those briefings, examiners were instructed that under no circumstances should they be directing or encouraging banks to close MSB accounts. We have been very clear in this regard.

Mr. Chairman, the OCC salutes your leadership in this vital area. We also believe that important objectives are achieved when MSB's have access to banking services, consistent with anti-money laundering laws and rules. We stand ready to work with Congress, FinCEN, the other Federal banking agencies, and the banking industry to achieve these goals.

Thank you.

[The prepared statement of Ms. Jaedicke can be found on page 93 of the appendix.]

Chairman BACHUS. Thank you.

Ms. Taylor.

STATEMENT OF THE HONORABLE DIANA TAYLOR, SUPERINTENDENT OF BANKS, STATE OF NEW YORK, ON BEHALF OF THE CONFERENCE OF STATE BANK SUPERVISORS

Ms. TAYLOR. Good morning, Chairman Bachus, Congresswoman Maloney—thank you very much for your kind introduction—and members of the subcommittee.

I am Diana Taylor, superintendent of banks for the State of New York.

I am pleased to be here today on behalf of the Conference of State Bank Supervisors to discuss the impact of Bank Secrecy Act compliance requirements on the availability of banking services through money service businesses.

The New York State Banking Department is responsible for licensing, supervising, examining, and regulating MSB's that operate within our State's borders. The MSB's that we currently oversee, by State law, include money transmitters and check cashers.

MSB's fill a need in many markets. For many individuals and families, especially in low-income and urban communities, MSB's may be the only means of access to cash or the only avenue for sending funds to family members abroad.

In New York State, there is an enormous concentration of money transmitters and check cashers in only a few banks. Two banks provide services to 42 percent of our money transmitters, and two different banks provide services to 87 percent of our licensed check cashers. The two banks in New York that are the most active in providing these services to money transmitters are currently considering exiting this business.

The departure will undoubtedly present a significant challenge to New York's MSB's, not only in the short term but in the long term, as well, as the decline in competition is likely to not only raise fees for these businesses but to make it that much more difficult to find any bank to do business with them.

So, how do we solve this problem? Our solution must create incentives that ultimately serve to protect consumers, the banks, and the MSB's. Piecemeal stop-gap legislation is not a viable solution.

The solution requires effort from all parties involved—the MSB's, the banking industry, State and Federal banking regulators, FinCEN, and the IRS.

First, FinCEN should revisit its definition of an MSB. The current definition is too broad, with a threshold so low that it may capture more entities than intended. The definitions hit target entities whose primary business is providing financial services, rather than the entities that offer financial services only incidentally to their core businesses, such as supermarkets cashing checks for their customers.

Two, regulators should consider further clarifications of standards.

We, as regulators, should be able to develop simplified standardized requirements for MSB's that serve a lower-risk client base.

This new standard could serve as a foundation for an advanced comprehensive BSA/AML program.

Additionally, while the joint guidance issued by FinCEN and the Federal banking agencies did help clarify regulators' expectations for banks that serve MSB's, further guidance may also be necessary in two areas—appropriate due diligence when maintaining accounts for foreign providers of money services and identifying entities that may be operating covertly as MSB's.

Third, we must continue to improve Federal and State coordination.

Thirty-nine States have signed a memorandum of understanding (MOU) with FinCEN, and 35 States have signed with the Internal Revenue Service, to set forth procedures for sharing certain Bank Secrecy Act information.

These MOU's, however, cannot entirely address a critical need for additional services at both State and Federal levels. We need access to additional training and a renewed commitment from FinCEN and the IRS to deliver on the promises of the MOU's.

Federal and State regulators, FinCEN, and the IRS need to continue our efforts to deliver a consistent message to the banking industry about their obligations and rights.

Fourth, we should create incentives to encourage banks to serve the MSB industry.

We might consider offering CRA credit to banks that provide services to MSB's, since a significant segment of these businesses' customers are low-income individuals, households, minorities, and new immigrants.

We should also seek out incentives for banks to offer MSB-type services in unbanked and underbanked communities across the country.

MSB's must continue to improve their risk-management systems, with continuing focus on the area of BSA/AML compliance.

As MSB's make their commitment to compliance clear, banks may become more willing to provide services to these businesses.

At the State level, we must continue to improve supervision of these entities.

New York supervisory protocol for MSB's takes an integrated approach that focuses on risk management, with an emphasis on the compliance function, inclusive of BSA.

Our FILMS evaluation system provides an early warning system about weakening conditions and a guide to where to look for noncompliance issues.

Both CSBS and its counterpart organization, the Money Transmitters Regulators Association, have made a commitment to provide additional training and resources for State MSB examiners across the country.

No silver bullet can solve this issue, and finger pointing is not helpful.

This is an industry that is vital for many people.

Licensing alone is not a panacea. It is also not helpful for banks to categorically refuse to do business with MSB's. Regulators must be consistent in their requirements for the industry. Everybody must work together.

I commend the subcommittee for holding a hearing on this very important issue.

Thank you.

[The prepared statement of Ms. Taylor can be found on page 126 of the appendix.]

Chairman BACHUS. Thank you.

Mr. Carbaugh, the SAR's that the MSB's are required to file—does law enforcement review those SAR's?

Mr. CARBAUGH. Yes, they do, sir.

Law enforcement around the country, through various, for example, high-intensity financial crime areas, have SAR activity review

teams that review and assess individual SAR's that come in, and they distribute them based on their jurisdiction. So, yes, they are being looked at on that level.

They are also being looked at on a more macro level at FinCEN to identify potential trends and patterns, and to look at the information in a more strategic way and to provide some proactive targeting of institutions when they are identified.

Chairman BACHUS. What is the last year that you all have reviewed those SAR's? Have you reviewed those that were filed last year?

Mr. CARBAUGH. One of the strategies that we have in place right now is actually looking at SAR's filed by depository institutions since the issuance of our guidance last year, where we said in our—in the guidance that if you identify a potential unregistered or unlicensed money service business that you believe is operating outside of the requirements—

Chairman BACHUS. Yes, I am talking about the licensed ones now. How long after they file the SAR's are you reviewing those SAR's?

Mr. CARBAUGH. Well, they come into the database very quickly, depending on how they are filed.

Chairman BACHUS. How many of the SAR's filed by MSB's last year resulted in criminal cases being brought?

Mr. CARBAUGH. I do not have that information. I would have to reach out to my law enforcement counterparts to obtain that.

Chairman BACHUS. Is that information available?

Mr. CARBAUGH. I would have to check with them.

Chairman BACHUS. Are you personally aware of whether any of them have resulted in criminal charges?

Mr. CARBAUGH. My understanding is that, yes, they have resulted in criminal actions, and we do have evidence that we put forth in our SAR activity review, which we publish twice a year, detailing cases where suspicious activity reports have resulted in prosecution.

Chairman BACHUS. Are the prosecutions from the SAR's that MSB's have filed—are they much greater in number and percentage than those filed by other financial institutions?

Mr. CARBAUGH. I do not have that information.

Chairman BACHUS. Could you get that information and supply it to the committee?

Mr. CARBAUGH. I would have to check with our law enforcement counterparts.

Chairman BACHUS. Okay.

Thank you.

Ms. Jaedicke, what is the OCC doing to discourage banks from severing their relationships with MSB's? I mean it is not working.

You know, there was another major announcement this week of another major bank that actually says they are not going to extend banking services to MSB's. Is the OCC powerless to stop this?

Ms. JAEDICKE. I hope not, sir. The intent of the guidance that was put out last year, under FinCEN's leadership, was to provide more clarity around this particular issue, so that banks would feel comfortable servicing MSB's, and MSB's would know how to provide information to banks that would make banks more com-

fortable. So, I would again say that we should take a hard look at the comments that come in from the ANPR that FinCEN has issued and see if there are some changes we can make in the guidance that might help the situation.

Chairman BACHUS. Let me ask both FinCEN and the OCC. You are aware that some of the largest banks in America say that they are not going to continue to serve MSB's, and I think you both said you are very concerned about this. My question is what are you going to do about it?

Ms. JAEDICKE. Sir, as I said, we do not tell national banks which accounts to open or close.

Chairman BACHUS. OCC is powerless—if a whole industry—if banks are saying we are not going to deal with this industry—the OCC—do you feel like you have any responsibility or any obligation to—

Ms. JAEDICKE. I think this is a multi-part problem, sir, that will require a multi-part solution.

Chairman BACHUS. Is there any obligation or responsibility on your part, when the major banks in this country say that they are not going to serve an industry, and they discontinue their services to that industry, do you—does the OCC have a statutory or regulatory duty or obligation to see that does not happen? It is not a loaded question. You are in charge of compliance.

Ms. JAEDICKE. Yes, sir.

I think our duty and obligation is to provide clear guidance in terms of what our supervisory expectations are, and that is what we have tried to do. We are very concerned about the situation with the money services businesses and the discontinuance. We want to do what we can, what is within our power, although we are not the regulator of the money services businesses, we do not write the regulations for MSB's, but certainly our banks are some of the banks that are providing services to them. So, I think the best place for us to have influence is in the information and the guidance we provide to the financial institutions.

Chairman BACHUS. I do not know the answer to this question.

Is there any statutory or regulatory obligation of banks to serve all industries, or can they categorically just announce that they will not serve certain industries or certain groups of people?

Ms. JAEDICKE. There are CRA obligations, sir, that have to do with lending, particularly lending to—

Chairman BACHUS. Or servicing accounts?

Ms. JAEDICKE. Right. Lending to a bank's communities, including low- and moderate-income areas.

Chairman BACHUS. If these are law-abiding companies that are subject to regulation, and they are complying with the regulations, is it a violation for banks to just publicly announce to the world that they are not going to deal with those companies anymore?

Ms. JAEDICKE. Not to my knowledge, sir.

Chairman BACHUS. Okay. Do you need such statutory power?

Ms. JAEDICKE. No, sir, I don't think so. I think the solution to this really lies with multiple parties. It lies with the OCC and the other Federal banking agencies. It lies with the States and the IRS, who need to provide even and vigorous supervision of the MSB's.

It lies with the MSB's themselves, who need to make sure that they are in compliance with the regulations that apply to them.

Chairman BACHUS. You know, some of them are complying. They have not been guilty of any violations, and yet, they have been denied banking services by some of the country's largest banks. You are aware of that?

Ms. JAEDICKE. Yes, sir.

Chairman BACHUS. Okay.

You said you do not like the regulations that have been imposed upon OCC or that you have to comply with? Is that the FinCEN regulations?

Ms. JAEDICKE. I am sorry, sir. Would you repeat that?

Chairman BACHUS. You made some statement that you did not like the regulations.

Ms. JAEDICKE. No, sir, I do not think I said that.

Chairman BACHUS. Okay.

All right.

Ms. Maloney?

Mrs. MALONEY. Thank you.

Superintendent Taylor, in your testimony, you state that FinCEN's definition of an MSB does not differentiate among levels of risk within the MSB industry, and you gave several suggestions about how that definition should change based on targeting the entities whose primary business is providing financial services rather than entities that offer financial services only incidentally to their core business.

What sort of a breakdown in definitions do you think would be helpful to properly regulate MSB's? If you would like to expand on any of your recommendations, you have the floor.

Ms. TAYLOR. Thank you.

What I was referring to is the entities that have a primary business of being an MSB. For instance, entities like a MoneyGram or a big check casher are subject, under the current regulations, to the same sets of rules and regulations as a—for instance, a grocery store that is cashing checks as, you know, a courtesy to their customers or entities that carry out more limited businesses—for instance, just cashing payroll checks or government checks or something like that—and I think this is an area that needs to be explored, where maybe we could be a little bit more pointed in which types of entities get regulated how, so you do not have everybody getting swept up under the same group of regulations.

I think that is something that we need to look into, and maybe we can do something there and maybe we cannot, but I think that we need to look at it.

Mrs. MALONEY. I would like to ask the Deputy Comptroller for Compliance in the OCC, Ms. Ann Jaedicke—one of the problems that we are hearing is, when I talk to some of the big banks—and I am not just talking about New York banks. I am talking about big banks in this country—a number of my colleagues, Mr. Frank and others, have mentioned that they have talked to these banks and they say we have to stop this service because the OCC is telling us to do that.

Now, when I wrote to Mr. Hawke, and in your comments, you are saying you are not doing that, but there definitely is some

misconnection, because they truly do believe that they are being told to discontinue the service, and so, that is my question.

You say that you are not telling them that, but whatever—there is a disconnect. They are pointing fingers back at you.

How can you clear this miscommunication up?

Ms. JAEDICKE. We tried to clear it up in March of 2005, as part of the interagency guidance on MSB's that we issued with FinCEN and the other regulators. In that guidance, we made it clear that it was the bank's decision whether to keep open an account or close it. Also, as I said in my testimony, we made it very clear to our bank examination staff that it was not their job to decide which accounts should stay open or be closed; that was the bank's decision.

Mrs. MALONEY. Well, I tell you, we work on this committee and we try to figure out how to get financial services into our country.

We are working very hard to try to get people who are unbanked into the banking system.

It is a better way to track money laundering and to just track what is happening in our country, and everyone says that they want to help, but nothing seems to be happening, and I would like to ask everyone to just talk about what you think should happen, but right now, I would like to ask Don Carbaugh, how many MSB SAR's were filed last year, and of those that were found to involve money laundering, how many do you expect will eventually reveal actual criminal activity?

Mr. CARBAUGH. Thank you, Congresswoman.

Last year, there were approximately 384,000 MSB SAR's filed by the money services business industry. Your question with respect to prosecutions or criminal activity, I cannot answer.

That is a question that will, again, be a question for law enforcement.

We at FinCEN do not have criminal investigative authority.

Mrs. MALONEY. Of those that were filed, do you know if any of them involved money laundering? Did any of them involve—I mean that is an important question.

Mr. CARBAUGH. Sure. The SAR's that are filed—there is information on the SAR's that the MSB has to check to determine what kind of activity they have identified, and many of those SAR's do indicate money laundering or Bank Secrecy Act violations.

Mrs. MALONEY. If you cannot get it to me today, I think a very legitimate question is how many MSB SAR's were filed and how many of them had money laundering or some problem with them, and so, I think it is important to see whether there is any correlation between criminal activities and your assertion that MSB's are high-risk.

It may be that there has not been any money laundering in MSB's, and therefore, the high risk level should be removed.

You may not have that information now, but you surely can obtain it, and I'd like to ask for it for the committee.

My time is up, but if you have a comment, I would love to hear it.

Mr. CARBAUGH. Again, there were 384,000 filed last year.

Just to your point, we do not suggest that all MSB's are high risk.

In the joint guidance that was issued last year to the banking industry, we indicated that there were various levels of risk in the money services businesses industry, as there are with any other account holders or businesses that depository institutions would bank.

Mrs. MALONEY. To my question, how many MSB SAR's had any type of money laundering, that figure has to be out there.

It may be that none of them had any money laundering. I do not know.

I think it is a legitimate question; maybe you could get back to us.

Mr. CARBAUGH. We can get that information. Again, it would be suspected money laundering.

Mrs. MALONEY. Thank you.

Chairman BACHUS. Mr. Hensarling?

Mr. HENSARLING. Thank you, Mr. Chairman.

Mr. Carbaugh, on page 3 of your testimony, I think you said that if the MSB account relationships were terminated on a widespread basis and these businesses go underground, that this could significantly damage our collective efforts to protect the U.S. financial system from money laundering and other financial crimes.

That is pretty strong language.

Could you elaborate just how serious of a challenge this would be to FinCEN?

Mr. CARBAUGH. Sure.

The challenge for us would be that, if there is a loss of transparency, then we have no indicators of activity that may be flowing through these types of businesses.

When we bring them under the AML regulations, they are filing reports to us that are then used by law enforcement, that are obviously indicators of potential suspicious activity.

So if, in fact, they go underground, that is that much information that we would not have available for law enforcement to potentially investigate,

Mr. HENSARLING. So, between the regulation and the legislation, if we do not get it right, these businesses are not necessarily going away; we are just simply going to lose their paper trail.

Is that a fair statement?

Mr. CARBAUGH. I think that there is evidence to suggest that, correct.

Mr. HENSARLING. Ms. Jaedicke, I peeked ahead at the testimony of the next panel, and Mr. Abernathy with the ABA states in his testimony that the interagency guidance has not provided a firm enough separation between the low-risk and high-risk profiles on the MSB's, causing, in the opinion of ABA—and I have not seen a statistic saying that most banks are prompted to use a high-risk due diligence criteria and applying that to the MSB's.

I think, in your own testimony, if I remember right, that banks are supposed to be using some amount of due diligence to differentiate between the two, but it sounds like they do not feel they have sufficient guidance on how to do that, and so, they are using the higher risk, which, to some extent, is perhaps helping the phenomena that Mr. Carbaugh is worried about.

Can you detail how this interagency guidance defines low-level risk versus high-level risk, and why, seemingly, financial institutions do not feel that they have too much ambiguity to apply it?

Ms. JAEDICKE. Certainly, sir.

The guidance has examples of what low-risk money services businesses might be versus what high-risk money services might be and supplies some attributes. For example, it explains a low-risk money service business to be something like a check casher that would cash payroll checks for a local employer, and that would describe many of the money services businesses that we have here in the United States. As an example of a high-risk money service business, it gives a wire remitter that was remitting large and frequent wires to a country that was of money laundering concern to some part of the United States Government, either Treasury or the State Department or some other organization. So, we tried to make differentiations, with FinCEN's help, in the types of MSB's and give the industry examples of low-risk versus high-risk.

Mr. HENSARLING. At what point, if any, does a financial institution ultimately become responsible for the BSA compliance of its customer, because I believe a number of our financial institutions believe that, de facto, they are.

Ms. JAEDICKE. At what point does the bank become responsible for its—

Mr. HENSARLING.—for the BSA compliance of one of its customers.

Ms. JAEDICKE. We would not say that the bank was responsible for the BSA compliance program of the MSB. MSB's are required by regulation to have a compliance program. What the bank typically would do would be to simply ask questions of the MSB, if the bank felt it was necessary to do so for their due diligence program, questions about the MSB's own program, perhaps.

Mr. HENSARLING. You understand that a number of the financial institutions—apparently a great number of them, as we will soon hear testimony—believe that, de facto, they are being asked to do that and that they do bear some responsibility.

You understand—

Ms. JAEDICKE. I do understand that, sir. All I can tell you is that the guidance was specifically intended to address that.

Mr. HENSARLING. Thank you.

I am out of time.

Chairman BACHUS. Mrs. McCarthy?

Mrs. MCCARTHY. Thank you, Mr. Chairman.

It has been interesting hearing each one of you speak, and also reading your testimony, and it seems to me, obviously, with all of you sitting in front of us, we are sitting here because we are thinking, okay, how are we going to fix this problem.

I know New York State is going to have some legislation in front of their committee—that was in your testimony—that would require banks to get your permission in order to close an MSB account. Could you go further into detail on your concerns with this requirement?

I think the one thing I am hearing is that everybody is going by these requirements, but nobody seems to be talking to each other on how to handle this.

New York State has, at least, come up with some solution, where the Federal Government—have you all talked together, all of you, to try and figure out what we can do to make sure that everybody is on the same page, so that our MSB's can serve the people they need to, and certainly protect our banks that have an obligation to make sure that we are not money laundering.

Ms. TAYLOR. I will start with the New York State legislation problem and then go to the Federal regulations to answer your question.

As far as the proposed legislation in New York State, what it would require is that any bank that told an MSB that it was going to close its account—it would have to get written permission from the superintendent of banks in order to do that.

I think this is a very, very bad idea for exactly the reasons that Ms. Jaedicke said before.

Regulators are not in the business of telling their regulated institutions who to do business with or who not to do business with.

We set up guidance and guidelines and regulations, and each bank in this free country of ours is free to do business with whomever they choose.

However, what we can do, and what we are trying very hard to do at the New York State Banking Department, is to put in place—which I think we have done—a system of rating and examining and supervising the MSB's, which hopefully will bring them up to par in the BSA compliance area. We have done a lot of work in this area, and it is starting to show some success.

The money transmitters who have gone through our system—they are on their second round. The first round, there were some very severe BSA compliance problems. Approximately two-thirds of the businesses were not up to standard.

The second time through, it is about two-thirds who are up to standard.

In the check-cashing area, there are some very severe compliance problems, and we are working with our constituents to make sure that they put the systems in place that they need in order to comply with the rules and regulations.

Mrs. MCCARTHY. Thank you.

Ms. JAEDICKE. I would just like to say that the Federal bank regulators and State bank regulators are spending a great deal of time trying to work on this issue. We have met repeatedly as a group, and we have met with the trade associations for the MSB's, and we have met with the ABA to try to find solutions.

Mr. CARBAUGH. I would add that, as was previously mentioned, FinCEN took the lead last year in conducting a fact-finding meeting on this issue, worked very closely with our counterparts in the Federal banking agencies to develop and issue a policy statement, as well as joint guidance, on this issue, and since there has been some evidence of continued discontinuance—and again, I think we are taking the lead in that, in March, we issued an advanced notice of proposed rulemaking seeking comment on this very issue, and that rulemaking closes on July 10th, and at that point, we will certainly assess all comments and recommendations provided to us, and make some decisions about appropriate steps to take at that point.

Mrs. MCCARTHY. I guess my concern is—because I am also hearing from my MSB's that, you know, as they try to go into new entities, you know, to join with a bank or a credit union, they will not even consider them anymore, because they are hearing of all the other larger banks that are actually pulling out.

Obviously, we want to work with the bankers. We also want to work with those that are serving the underserved communities.

So, I guess that is going to be up to us to see how we are going to come up with those answers.

I yield back the balance of my time.

Chairman BACHUS. Thank you.

Mr. McHenry.

Mr. MCHENRY. Thank you, Mr. Chairman.

Mr. Carbaugh, you say in your testimony that many banks have stated their uncertainty as to the appropriate steps that they should take under the Bank Secrecy Act to manage potential anti-money laundering and terrorist financing. Those are your words.

In your opinion, is this due to the lack of regulatory guidance?

Mr. CARBAUGH. No.

I think that there might be misperceptions about the guidance.

Again, we worked collaboratively with the Federal banking agencies when this issue was raised last year to develop some very specific guidance that details what our expectations are when they open and maintain accounts for money services businesses.

Those requirements and expectations are similar to that of any other business that a banking organization would bank, and the types of risk assessments that they would conduct pursuant to those types of accounts, as well.

Mr. MCHENRY. You also talk about certain MSB's going underground.

How would they do that?

Mr. CARBAUGH. One is not registering with FinCEN and not licensing with any potential State requirements, and then conducting business through, for example, a banking organization without being in compliance with those basic compliance requirements under Federal, as well as potentially State—

Mr. MCHENRY. Have you seen that?

Mr. CARBAUGH. Yes, we have evidence, through suspicious activity reports, of that occurring.

Mr. MCHENRY. How significant?

Mr. CARBAUGH. I think it is significant enough to certainly pay attention to, and we are certainly developing a strategy to identify unregistered money services businesses and put in place a broad spectrum of compliance and enforcement strategies to address that issue.

Mr. MCHENRY. I would like to also echo what the chairman requested, some statistics in terms of what—you talk about 385,000 suspicious activity reports last year, right?

Mr. CARBAUGH. Correct.

Mr. MCHENRY. You know, in terms of what that is doing, I mean how many of those have netted anything, we would like to hear that, because perhaps we are generating too much paper for you, or not enough, and you know, unless we have the statistics, we are not going to be able to judge.

Mr. CARBAUGH. We will get those statistics for you.

It is also important to note that it is a database of information, and one SAR that is filed will not necessarily result in an action, but looking at the database as a whole and linking different pieces of information together may present a very different picture, and that is important, too, I think.

Mr. MCHENRY. Moving to Ms. Jaedicke, you are popular today. I think it is because of your name, so easy to say.

Ms. JAEDICKE. Yes, sir, it is fun.

Mr. MCHENRY. Yes.

You mentioned the diversity in MSB's—size and mom-and-pop versus Fortune 500.

Ms. JAEDICKE. Yes.

Mr. MCHENRY. How are the regulations affecting these—is it across the board? Is it affecting certain areas more than others?

Ms. JAEDICKE. You mean in terms of the bank discontinuance issue?

Mr. MCHENRY. Yes.

Ms. JAEDICKE. Which types are losing accounts more frequently?

Mr. MCHENRY. Yes.

Ms. JAEDICKE. I do not know that I would have that information.

Maybe Ms. Taylor would know better for the State of New York.

Mr. MCHENRY. Ms. Taylor?

Ms. TAYLOR. I think the best way to answer that is to say that everybody is complaining about the same issue. If a bank says that it is not doing business with money service businesses anymore, that includes the big ones and the small ones.

I would say that you could ask the next panel that question, also, but it is our experience that it is pretty much across the board, I think.

Mr. MCHENRY. Is there a certain type that would have a greater risk for money laundering?

Ms. TAYLOR. Who are you asking?

Mr. MCHENRY. You, Ms. Taylor.

Ms. TAYLOR. Okay.

Well, it depends on the business. There are a lot of different characteristics of—

Mr. MCHENRY. That is what I am asking.

What characteristics would say that there is a greater risk?

Ms. TAYLOR. If money is being—large amounts of money are being transmitted overseas, large checks being cashed, if there—

Mr. MCHENRY. What I mean is the type of business—mom-and-pop versus a Fortune 500.

Ms. TAYLOR. It is hard to say, because it depends on the compliance systems.

If the compliance systems are in place to catch trends and transactions to lead people to go look at them, then that's one thing.

I think that any business, large or small, that does not have a good compliance system is a very high risk situation, no matter what kind of business it is conducting.

Mr. MCHENRY. Ms. Jaedicke, would you like to comment?

Ms. JAEDICKE. I would add to that that it sometimes can be more difficult—I am not saying they are inherently more risky—but it sometimes can be more difficult for the very small MSB's, the

mom-and-pop-type MSB's, to have robust compliance programs. Of course, they do not need as robust a compliance program as does a big MSB, but it is sometimes difficult for them to find qualified people to help them design a program, and that can make a difference sometimes in bank discontinuance.

Mr. MCHENRY. Thank you, Mr. Chairman.

Ms. TAYLOR. Can I add to that?

Mr. MCHENRY. Go right ahead.

Ms. TAYLOR. Thank you.

We had a situation recently where there was a newspaper article which was written about a city in western New York which complained that there were several—as in many—check cashers that were unlicensed, operating in the city, which were charging exorbitant rates to their customers. This is problematic on a couple of levels.

One, they are charging their customers exorbitant rates, which is not good.

Two, they were unlicensed, unregistered entities, and so, we need to know about those.

A lot of these mom-and-pops do not even know that they have to be registered.

So, the really small ones that are below everybody's radar screen—you have to actually go out in the community and see them before you can find out what they are doing and whether or not they are registered and licensed.

So, that is a very big problem, too, and those, I think, are very high risk.

Chairman BACHUS. Thank you.

Mr. Clay?

Mr. CLAY. Thank you, Mr. Chairman, and I thank you for holding this hearing today, and I appreciate the panel's participation.

Many banks cite the risk associated with dealing with unlicensed MSB's, and it is required that MSB's register with the Treasury.

The Patriot Act also prohibits anyone from knowingly operating or owning a money transmitting business without a license in a State that requires one or without registering the business with the U.S. Treasury.

This question is for the entire panel.

Why does it seem that all MSB's are generally put into the same category of risk regardless of whether they are licensed or have a strong record of compliance? How do banks quantify and distinguish between the risk of unlicensed MSB's and those that are licensed?

We can start with you, Ms. Taylor.

Ms. TAYLOR. One of the things that we have been very definite with our banks about is, if we find that they are doing business with unlicensed money service businesses, that is a very bad thing.

The first question they should ask any money service business that comes to them for an account is whether or not they are licensed.

Doing business with unlicensed money service businesses is not a good idea.

Mr. CLAY. What happens when you find out they are not licensed?

Ms. TAYLOR. We tell them, if they are not licensed, then we ask them to close the account, and we go to the money service business and tell them that they need a license in order to operate in this State, and if they do not get a license, you will be penalized.

Mr. CLAY. Ms. Jaedicke.

Ms. JAEDICKE. I would say that is a significant issue for the banks that we deal with, as well. One of the threshold questions for them when they're opening an account for an MSB is, are you registered with FinCEN, are you properly licensed with the State? Sometimes MSB's do not understand the licensing requirements, and the banks will, in some cases, try and help them to understand those requirements.

They will print the licensing forms off of the Web site; they will explain to the MSB what they need to do. But, if the MSB then does not follow through, that leaves the bank with what they view as a rather serious situation, because the MSB is operating outside of the requirements of the law.

Mr. CLAY. Then they are immediately stopped from doing business with the bank?

Ms. JAEDICKE. Well, I would not say they are immediately stopped. I would say that banks will close accounts for MSB's that have not gotten licensed and registered, once the bank has made the MSB aware of the requirement, if, indeed, they were simply unaware.

Mr. CLAY. Thank you.

Ms. Mayer?

Ms. MAYER. Congressman, as you know, the IRS is charged with enforcing compliance with the BSA by MSB's, and so, we do not have anything, really, to do with banks.

However, whether or not MSB's are registered is obviously an important issue for us, and at the moment, we are working with FinCEN, we have put a special emphasis on trying to find MSB's that are not registered and have pushed out several thousand non-registration cases into the field in order to find these MSB's that are not registered and to get them registered, to bring them into compliance with the law.

Part of what we do in our efforts is to educate businesses that we find through various sources and try to bring them into compliance with the law.

Mr. CLAY. Any idea of how many MSB's, percentage-wise, are not registered or that may be registered?

Ms. MAYER. That is the $64,000 question. You know, there are estimates all over the place of how many MSB's there really are.

We know that there are 24,000 MSB's that have actually registered.

Mr. CLAY. I see.

Okay.

Thank you.

Mr. Carbaugh, anything to add?

Mr. CARBAUGH. I would just echo that licensing with the State, if required, and registration with FinCEN, if required, is one of the most basic requirements under our regulations for MSB compliance, and we have outlined that, actually, in our guidance to the banking industry, as well, and the guidance also details the steps

that a banking organization should take when they do identify an institution that they believe is operating outside of the law, and therefore, in potential criminal violation under Title 18, and that is to file a suspicious activity report. We are looking at that information right now and providing data to the Internal Revenue Service for outreach and examination purposes.

Mr. CLAY. Do you see any flaws in the current guidance for banks and the guidelines for the banks? Do you see any flaws?

Mr. CARBAUGH. Well, I think the guidance is very detailed and lays out expectations, and it is important to note that we also, at the same time, issued a companion piece of guidance to the MSB industry indicating what they should expect whenever they open and maintain accounts at a banking organization.

One of the things, as I mentioned before, that we are doing is the issuance of the advanced notice of proposed rulemaking to ascertain if there is anything else we can do in this area as far as guidance or changes to regulations.

Mr. CLAY. Thank you. I thank the panel for their responses.

Thank you, Mr. Chairman.

Chairman BACHUS. Mrs. Kelly?

Mrs. KELLY. Thank you.

Ms. Jaedicke, the OCC ombudsman program allows banks to complain about examination issues in a forum that is free from negative consequences, but MSB issues do not appear in the ombudsman's summary of cases and published documents. How many cases have been raised with the ombudsman about the BSA and the MSB issue since last year, and what was their deposition?

Ms. JAEDICKE. I do not actually know, Ms. Kelly, how many have been raised. To my knowledge, there have not been any, but I will be happy to check and find out.

Mrs. KELLY. With the chairman's permission, I would like to insert in the record—I have here the summary of the cases, and there is not one case on MSB that appears here that was brought up to the ombudsman by the banks.

Chairman BACHUS. Without objection.

Mrs. KELLY. Thank you. It seems to me that we can err on the side of getting too much information, and I really appreciate, Mr. Carbaugh, that you are looking to try to figure out what to do.

It is a Catch-22, because we do not want people to go down under where we do not know what is going on financially. We need to see what is going on out there in order to protect America, but to do it right does require a very delicate hand in various ways.

It appears that no banks have complained to the OCC about the regulatory problems with MSB's, which may mean that they are simply refusing to take the MSB business, and this is a problem.

I had one president of a major bank say to me that he was getting rid of all of the MSB's.

This is a New York bank, and he said that he was not going to do any MSB business, and he just simply canceled all their accounts.

This is not helpful for them, it is not helpful for the bank, and it is not helpful for all of us as regulators, but what we need to do is not, I think, try to write a piece of regulation that is going

to impose something again, before we understand how to do it properly.

That is why I appreciate, Ms. Taylor, your being here and your talking about the fact that you are concerned about over-regulating. It would indicate to me, from your prior testimony to Ms. McCarthy, that you are going to recommend that the Governor of New York veto the bill that has passed the State Senate and the Assembly banking committee, because you think that it is a bad idea.

Is there a way that you can put in place a better situation than you have now with regard to rating and supervising the MSB's so that people will understand?

I think part of our problem is that the general public—and especially people who do not use banking systems and need MSB's—need to have education that there can be a certification out there, and they can go—when they are getting their check cashed—and find a certificate posted on the wall.

That may be all we actually need to see.

I would be interested in the comments of you, Ms. Taylor, on that, and then I have one more issue I am going to try to pick up here.

Ms. TAYLOR. Thank you, Mrs. Kelly, and that is really the crux of what we are trying to do in New York State to alleviate the situation, which is to educate people, especially in the money services businesses, to supervise, examine, and license them in a way that is very similar to how we license—or charter, supervise, and examine the banks.

We have put into place a system called the FILMS system, which is unique to the money services businesses.

They are different than banks. They are very short-term. It is not credit-based, so much. Liquidity is a big requirement. So, there are different characteristics that you look at in a money services business than you do in a bank.

So, what we are doing is, in taking our money services businesses through the licensing process, which has been made much more stringent over recent years than it was before—so, it is a lot harder to get a license, and it means something when you have a license, and our examination procedures are much more rigorous than they were in the past.

So, what we are hoping happens is that the banks become more comfortable with doing business with money services businesses licensed by us, knowing that they do—will have the compliance systems in place that are necessary, and I have to say, in addition to that, we have worked very hard with CSBS to take that system out to the other States in the country.

We have a pilot program—

Mrs. KELLY. I am going to run out of time here, but I do need to ask one more question of Ms. Jaedicke.

It is about the Arab bank in New York. It was fined by the OCC and FinCEN for BSA violations. The Arab bank, in spite of paying a record fine, continues to insist that they were the victims of persecution and that they violated no U.S. laws.

I would like to know when the OCC is going to release the summaries of their investigation.

I think that investigation's summaries show directly the threat that Arab Bank did pose to this country, and that we were justified, at the OCC, and FinCEN were justified in levying that fine.

When are you going to release those records?

Ms. JAEDICKE. That is a supervisory matter, and, to my knowledge, we do not intend to release the records.

Mrs. KELLY. Okay. Thank you.

Chairman BACHUS. Thank you. I would like to ask additional questions. Are there any other members that would like to do follow-up? All right.

My first question—and I will just ask this to OCC or FinCEN or IRS or even Ms. Taylor. Do you know of any instances where an MSB itself was convicted of money laundering or terrorist financing? I am talking about the MSB itself.

Any cases, Mr. Carbaugh? You all would maintain a database on that, wouldn't you?

Mr. CARBAUGH. Again, that would be law enforcement information, and I would have to defer to my law enforcement counterparts.

I do not know if Eileen can speak on behalf of IRS criminal investigations.

Chairman BACHUS. None that you know of. Is that right?

Mr. CARBAUGH. Well, I think we can point to the SAR activity review.

Chairman BACHUS. I am not talking about the SAR's which they file on their customers. I am talking about the MSB itself.

Mr. CARBAUGH. Right. I think we have some evidence in a publication that we have called the SAR Activity Review, in which law enforcement provides us information on cases that have been supported by the filings of suspicious activity reports, and I believe there are cases in there that relate to MSB's.

Chairman BACHUS. Are they licensed, registered MSB's?

Mr. CARBAUGH. It could be both. Again, I would have to get back to you.

Chairman BACHUS. Could you get me that information?

Mr. CARBAUGH. We can get you some information, yes.

Chairman BACHUS. Okay.

Now, as far as if their customers are engaged in money laundering, the indication of that would either be—I mean they would file SAR's and you would have to review that information.

So, it would be a good thing actually for them to go to MSB's, because that is a regulated industry, and then you would get a SAR, right, as opposed to going underground.

Mr. CARBAUGH. It is very important that they stay transparent to us, as I mentioned in my testimony.

Chairman BACHUS. So, it is actually very important that these customers—even if the customers are engaged in money laundering—very important that they go through a regulated industry so that law enforcement can discover those activities.

Mr. CARBAUGH. It would be important, also, for the MSB then to report that activity, pursuant to requirements.

Chairman BACHUS. Now, do you know of any evidence or any cases when MSB's were not reporting those transactions?

Mr. CARBAUGH. I would defer to Ms. Mayer on that from an examination standpoint.

Chairman BACHUS. Ms. Mayer?

Ms. MAYER. Mr. Chairman, I do not know specifically, but I would be happy to ask our examination folks if we have any information that we can share with you and get back to you.

Chairman BACHUS. You have the MSB itself, and you know, I have not heard that any of those are guilty—I have yet to hear any evidence or any testimony or anybody say, oh, yes, you know, there are—particularly licensed, registered MSB's which are engaging in money laundering or terrorist financing, and then the customers of the MSB's—as long as the MSB's are filing the reports and the SAR's they are supposed to file, I mean that is all you can ask them to do, I would think.

Mr. CARBAUGH. They have to have an anti-money laundering program that is designed to detect—

Chairman BACHUS. Right.

Mr. CARBAUGH.—and report and have appropriate controls in place, correct.

Chairman BACHUS. Would you supply me any cases where licensed, registered MSB's did not do that, you know?

Mr. CARBAUGH. Again, we will look at that, in cooperation with—

Chairman BACHUS. I guess there are literally thousands of examples of MSB's which have not been charged with any criminal activity or that have developed such programs, but despite that, the banks have discontinued their business with those MSB's. You know of some of those, I suppose, don't you? We hear reports every day.

Mr. CARBAUGH. Again, on the discontinuance issue, you know, I have to defer comment until the advanced notice of proposed rulemaking is final, so that we can then assess the findings and comments and recommendations.

Chairman BACHUS. You need to know some of this information I am asking you before you finalize the rule. I mean if you address the problem, you need to sort of be informed about what the problem is and the extent of the problem.

Mr. CARBAUGH. Sure.

Ms. JAEDICKE. Mr. Chairman, may I just add that there have been MSB cases subject to prosecution, and we can provide some of that information.

Chairman BACHUS. Sure.

Ms. JAEDICKE. I do not have it with me today.

Chairman BACHUS. I just looked at the information that is available on the internet, and there are three of them; one was in 2003, one was in 2004, and one was in 2006, and they actually—and one case involved, really, misconduct by the bank, not the MSB, is my understanding, just from reading the account. So I know of three cases.

I think this is, you know, Delta National Bank, Hudson United Bank, and Bank Atlantic.

Ms. JAEDICKE. Yes.

Chairman BACHUS. Not all of them actually involved the MSB. Sometimes it was a failure of the bank.

My last question—are banks responsible for reviewing the MSB's customers' activities and to monitor the transactions conducted by the MSB's customers?

In other words, the banks—are they responsible for monitoring the MSB's customers, and to what extent, and should they be, and are they capable of doing that?

Ms. JAEDICKE. I would say no. Specifically, the banks are not responsible for monitoring the individual customers of MSB's. That would be extraordinarily difficult to do, Mr. Chairman—

Chairman BACHUS. Oh, I agree.

Ms. JAEDICKE.—because some of the customers of MSB's do not necessarily have an ongoing, long-term relationship with the MSB.

Chairman BACHUS. Right.

Ms. JAEDICKE. But what we do often see banks do is have some general understanding of the type of customer that the MSB does business with.

Chairman BACHUS. Right.

Ms. JAEDICKE. They do not know the individual customer, but they know that the MSB is servicing a particular customer base that sends wires to a particular country or that kind of thing.

Chairman BACHUS. Sure.

In certain cases, it ought to be our policy, I would think, to encourage the MSB's to monitor those transmissions and to report them, but beyond that, you know, I am not sure that the MSB can even refuse—unless they have some grounds—refuse business.

Ms. JAEDICKE. The MSB's are required by regulation to have a BSA program that would include doing some of those types of things.

Chairman BACHUS. Sure.

So, it is my understanding that the answer to my question, though, is that the banks are not responsible for reviewing MSB customer activities, nor for monitoring in any way the transactions engaged in by MSB customers.

Is that right?

Ms. JAEDICKE. There is no overt obligation for them to do that. Where I think this becomes very confusing, though, sir, is when an MSB brings to the bank transactions that the MSB is facilitating on the part of a customer and the bank facilitates these transactions via a wire to somewhere else, then the bank becomes involved.

Chairman BACHUS. Does there need to be some clarification as to exactly what the bank's responsibility is, and as to whether any responsibilities extend to the MSB customers?

Ms. TAYLOR. I would say part of the problem here is it's very similar—and correct me if you think differently—to the correspondent banking problem.

You know, how far do you have to go down into your customer's customer, and what we really look at is patterns of activity. Is it something that is a pattern throughout, you know, a series of transactions and the bank does not pick that up, but we do. Then that becomes a little bit of a problem.

We try and—and we look at all of the businesses, you know, with the same sort of criteria.

Chairman BACHUS. Correspondent banks self-certify, right?

Ms. JAEDICKE. Yes.

Chairman BACHUS. Okay. I have no further questions.

Ms. Maloney.

Mrs. MALONEY. I would like to ask FinCEN—has FinCEN ever brought an enforcement action against an MSB?

Mr. CARBAUGH. Yes, we have. As a matter of fact, we brought a civil enforcement action last month against one MSB, and I think since 1999, we have had seven MSB-related enforcement actions, including in 2003, an enforcement action with Western Union.

Mrs. MALONEY. Well, this is becoming a tremendous problem in New York. Many banks are not providing any services, by their choice, and the two smaller banks that are now still doing business with MSB's—there are rumors that they may be bought by larger banks that will not provide the service.

So, this is a crisis in New York, and that is why you see the New York State assembly and Senate passing out a bill to maintain MSB support by banks, which the superintendent has raised some objections to, and others have raised objections to.

So, my question is, if banks decide they do not want this business and it is a service that many people need—we want financial services. We want the underground economy to go into financial services. What would be your reaction to legislation that would allow money service businesses to open up accounts directly with the Federal Reserve Bank? Would there be any objection? What would be your response to a legislative action for money service businesses to open up accounts with the Federal Reserve?

Mr. CARBAUGH. That is a policy issue that would really require some very senior-level input and coordination through various compartments of the Department of Treasury.

I am really not in a position to make a statement on that issue.

Mrs. MALONEY. I mean we have to have the service. So, if everybody is going to—we have to—what would your reaction be?

Mr. MAYER. I have absolutely no knowledge or experience in that, so I cannot really answer your question.

Mrs. MALONEY. OCC.

Ms. JAEDICKE. I do not either, Congresswoman Maloney.

Mrs. MALONEY. Ms. Taylor.

Ms. TAYLOR. That is something for the Federal Reserve to take up.

Mrs. MALONEY. What you have all said is that you are meeting, and that you are thinking about it.

What action are you taking? What policy are you putting in place?

Is there any comment from any of the panel—everybody is talking to everyone. You have been talking for years. There have been conferences.

What action are you taking?

Mr. CARBAUGH. Again, I think, as was mentioned in my testimony, FinCEN took the lead last year in pushing this issue forward, in holding the fact-finding meeting, and then working with our colleagues at the various Federal banking agencies to develop an issue—a policy statement on this issue.

Mrs. MALONEY. Do you have the policy statement?

Mr. CARBAUGH. The policy is that banks are not the de facto regulator of MSB's, and subsequent to that, we issued very specific joint guidance on expectations for the banking industry, companion guidance to the—

Mrs. MALONEY. Who is the regulator on MSB's? FinCEN?

Mr. CARBAUGH. At the Federal level, for compliance with the BSA, we have delegated examination authority to the Internal Revenue Service.

Mrs. MALONEY. So, the Internal Revenue Service is the regulator of MSB's.

Another approach is, should we have a separate regulator for MSB's?

Is that an approach that might help?

Mr. CARBAUGH. Again, that would be a policy-level decision, you know, of senior levels within the department, and certainly something for your consideration.

Mrs. MALONEY. Any comment on—what specific action are you taking?

Mr. MAYER. Well, at the IRS, we are actually delegated the examination authority to make sure that MSB's are in compliance with BSA. So, what we are trying to do is to be out and to be picking the places that we examine in a risk-based way, based on the knowledge that we have from our databases and from what we get—leads from law enforcement, so that the banking industry can be assured that MSB's are complying with the anti-money laundering regime, with the BSA, and so that they are not being used in a way that would in some way endanger their relationship with the bank.

That is what we can add to this mix.

Ms. JAEDICKE. I believe that we can try to do more to alleviate the uncertainty, if it exists, among national banks in terms of what their roles are vis a vis the MSB's, and to try to alleviate the concerns they have with the regulators and how they view these accounts.

Ms. TAYLOR. In New York State, we have instituted the FILMS rating system.

We have upgraded our examination and licensing of these institutions.

We will work toward trying to provide CRA credit to banks and other incentives for banks to do business with MSB's.

We actually have something in New York State called the Banking Development District Program, which creates incentives for banks to put branches in underserved areas, and we are working very hard, together with our Federal counterparts and the other States, through CSBS, to make more uniform the regulatory process and to educate the examiners and train examiners in these systems.

Mrs. MALONEY. Thank you very much.

Chairman BACHUS. Thank you.

Ms. McCarthy.

Mrs. MCCARTHY. Thank you, Mr. Chairman.

I guess the question I have to ask is—the MSB's—I mean, basically they are serving people that—of very small paychecks, and I would tend to think that if—certainly, all of us are concerned about

national security and money laundering—that if anybody deposited or tried to, you know, send a large amount of money out of the country, I would have to think that would be very minute and a red flag would go up.

I mean one of the problems that we have seen, especially in the underserved communities, is that banks do not want to go into those areas, for a number of reasons. Most of their customers are not going to open up a checking account or a savings account, because their weekly check is what they are living on, on a day-to-day basis.

So, I am having a hard time understanding the problems that we are having with the MSB's, because they are serving a community that the bankers do not—it would not be worth their effort to open up a bank in that area. They are serving a situation, and again, as far as the security goes, anyone that comes in and is going to be sending a large amount of money overseas, or tracking it, that is going to be a red flag.

So, I am having a hard time understanding this whole problem that we are dealing with.

Can someone clarify it?

Ms. TAYLOR. Thank you.

You are right. The majority of the transactions that take place are very small transactions.

However, we have found situations at check cashers in New York State where checks for $400,000 are being cashed. We have to find this.

These compliance systems have to be in place to find this. Nobody is going to tell us, you know, unless a SAR is filed.

It has to be a licensed institution.

So, there—these institutions are used for criminal purposes in some instances, and we need to have the systems in place to make sure that when that happens, we can find out about it and we can direct it to the appropriate authorities to look into what exactly is going on.

Mrs. MCCARTHY. I would take it that those particular areas where they are looking at those kind of checks being—coming in, and obviously, we should be—they are probably not licensed.

Ms. TAYLOR. Maybe, maybe not. We have several investigations underway right now, some licensed, some unlicensed.

Mrs. MCCARTHY. Well, that is where you prosecute, but I would tend to think that would be not the norm on the majority of MSB's serving the small communities.

Ms. TAYLOR. One would hope.

Mrs. MCCARTHY. Thank you.

Thank you, Mr. Chairman.

Chairman BACHUS. Thank you.

I appreciate the panel's testimony. I think it was very helpful to us.

Oh, I am sorry, Mr. Baker.

Mr. Baker is recognized.

Mr. BAKER. Thank you, Mr. Chairman. I slipped in late, and just wanted to present a few observations for the record.

I do not recall whose testimony that it was I read attributing these facts. It appears that there are about 40 million people who

are unbanked, who have need of financial services. Individuals who, for example, may be in south Louisiana, who get a Social Security check and need to have that cashed for their daily activities.

The trouble that I think has occurred is that, if that person is cashing and the money service entity is required to substantiate the activity, therefore report back to the bank and the bank take responsibility for that conduct, what we are missing is an appropriate nexus between the act of negotiation and the requirement to report, as opposed to someone who has, for example, a check from Casino Rouge in Baton Rouge for $128,000, who appears to be cashing these checks on a regular basis, who the money service organization may have reason to conclude that there is a reason for me to ask these questions, as opposed to the wholesale requirement creating the potential regulatory liability for the institution, the financial institution, who has no reason nor ability to conclude the difference between the 80-year-old cashing of the Social Security check and the 30-something cashing of the $100,000 casino check.

Now, has there been—anybody can give me a study that shows there is statistical prevalence—are there regions of the country—say, New Orleans—where we have aberrantly high criminal records relating to liquidity, or if we are going to get into Oklahoma, where we have maybe a aberrantly high number of retireds and they are cashing Social Security—has there been any kind of study to say this is why we are pulling the trigger on this gun, or is it just a systemic, let's check everybody out and make sure nobody is sneaking by us that we do not know about? Could anybody comment on that, please?

Mr. CARBAUGH. I would say that the system that we have in place with respect to the anti-money laundering requirements for the money services business is a risk-based system, and certainly, it is up to the money service business, under their obligations, to assess the risks of all of—

Mr. BAKER. Let us back up just one second. From the money service business back to your level, what is it, or is there anything, that triggers this high level of responsibility based on data, analysis, formula? How do you determine it?

In other words, in rural communities, where there is very little probability of somebody money laundering at a $100 level, as opposed to someone in an urban area who is money laundering at $100,000 per week, is there a difference between the two, or are the standards uniformly the same?

Mr. CARBAUGH. The standard is a risk-based standard, and the reporting requirement for MSB's is activity that is $2,000 and above. So, there is a threshold requirement for reporting suspicious activity.

Mr. BAKER. So, if somebody sells a bass boat and deposits $2,200, they are in.

Mr. CARBAUGH. If it is deemed suspicious.

Mr. BAKER. How would one know? Is it the way they approach the check casher or their clothing? You are not going to tell me this is racial profiling, I hope. I mean you are telling me it is a risk-based model. Describe the risk. How is it imposed?

Mr. BAKER. Again, it would be up to the institution to determine—

Mr. BAKER. So, it is a risk-based model where the check casher has to determine what the risks are.

Mr. CARBAUGH. Correct.

Mr. BAKER. Can you understand why there would be resistance to that level of responsibility? It would be like me hiring a guy to paint my house. I do not tell him what color, but when it is done, I will tell him if I like it or not.

That is an unacceptable regulatory standard.

If we are going to apply sanctions in the market for inappropriate conduct, we have to describe what the inappropriate conduct looks like. You have not described it. We are saying that there is a risk associated with laundering money, but we are not telling the person at the gatekeeper level what it is they must look for. We are saying you describe the risk, you enforce it, and if you get it wrong, we will tell you about it later.

Mr. CARBAUGH. We have provided some guidance and indicia of suspicious activity.

Mr. BAKER. I am sorry to be picking on you, but you had the misfortune of answering me.

The point is, from our side and policy side, if we are going to pass this criminal statute and we are going to say you go to jail because you do something, we have to be very specific, and then artful defense lawyers take us to task that we have not been specific enough, and therefore, the person gets off.

In this case, we have generally described a conduct which we do not like, and we find unbecoming, but we have not really said what it is, and yet, there is a market consequence to a regulatory determination that this institution did not oversee the MSB with sufficient degree of professionalism, therefore there is a consequence, and a result, financial institutions withdraw from the market, and people who have that $800 Social Security check, or $2,200 Social Security check, are left without services.

All we are saying is that there is a social consequence to this policy that is unacceptably high in light of an undefined, ill-defined, or improperly defined risk.

Sure, we know there is money laundering, but it happens at videotape rental stores, where people come and pay for rentals, but they do not rent the movie.

Hello?

That is a real problem. Or people who pay for professional service for which there is no service. That is a whole lot different from a low-dollar—and $2,000 is an incredibly low standard.

I think anybody in the money laundering business who is really in it is going to looking at a significantly higher cash-out number than $2,000.

There are a lot of used trailers—and I am an expert on used trailers in Louisiana—and bass boats and a lot of other items that are sold customarily in the cash market for under $10,000 on a regular basis, and although the outside view may be different, most of them are legitimate and without question.

I thank the chairman for his leniency on the time, and I yield back.

Chairman BACHUS. Thank you, Chairman Baker.

Ms. Carson, you are recognized.

Ms. CARSON. Thank you very much, all of you distinguished and informed panelists, for being here today. I have two concerns.

Number one, I read just yesterday that the overdraft fees that are collected by financial institutions far exceed the profit that you derive from any other investment. My concern is, do you want to continue to rely on that as the stabilizing asset, the overdraft fees that you collect from consumers—

Chairman BACHUS. Ms. Carson, this is actually a hearing on the MSB's.

Ms. CARSON. Sorry about that.

Chairman BACHUS. Okay.

Ms. CARSON. I just thought I would catch them while they were here.

I apologize, Mr. Chairman.

Chairman BACHUS. Thank you.

I am not sure that this panel handles those issues. I mean if you do, and you wish to respond to Ms. Carson's statement, I am sure it would be helpful.

Ms. CARSON. I will let you off the hook. I do not think you want to respond.

Thank you very much.

Chairman BACHUS. Thank you, Ms. Carson. I am not sure, in fairness to the panel, if they were prepared to answer.

Ms. CARSON. Right.

I have a visitor out here, and I will be right back, Mr. Chairman.

Chairman BACHUS. Thank you.

That concludes the testimony of this panel.

In closing, I would like to ask unanimous consent that Congressman Rangel, a member of the Ways and Means Committee—in fact, the ranking member—be allowed to offer a written statement into the record.

I also have a written statement submitted by Western Union Financial and an additional statement by Isaac Warsame that I would like unanimous consent to introduce into the record.

This panel is discharged. Thank you for your attendance.

At this time, we would welcome the second panel.

Mr. Price is going to chair the second panel, and I have read the testimony of the second panel and commend them for their testimony.

Mr. PRICE. [presiding] Good morning, almost afternoon. We appreciate your joining us today and your patience on our schedule.

I also want to just mention that, although there may not be many members here, your statements and your input into this process is extremely important and greatly appreciated.

The second panel we will have before our subcommittee today—I want to welcome Mr. Philip Milne, president and CEO of MoneyGram International; Mr. Gerald Goldman, general counsel for Financial Service Centers of America; Mr. Wayne Abernathy, executive director for financial institutions, policy, and regulatory affairs for American Bankers Association; and Mr. David Landsman, executive director of the National Money Transmitters Association.

I want to also say that, without objection, your written statements will be made a part of the record and that each of you will

be recognized for a 5-minute summary of your testimony, and we thank you so much for joining us today, and with that, I recognize Mr. Milne.

STATEMENT OF PHILIP W. MILNE, PRESIDENT AND CEO, MONEYGRAM INTERNATIONAL, INC.

Mr. MILNE. Good morning, Mr. Chairman, and members of the committee. My name is Phil Milne and I am the president and CEO of MoneyGram International. I am very pleased to speak with you today about the bank discontinuance problem and anti-money laundering compliance by MSB's.

MoneyGram is a payment services company operating in 170 countries through more than 92,000 agent locations. We are licensed by the States and comply with the Bank Secrecy and USA Patriot Acts.

MoneyGram is also a member of the Money Services Round Table, along with American Express, Western Union, Comdata, Travelex, Sigue, and Ria.

The bank account problem is not a stand-alone issue. It is tied to compliance and the challenges faced by MSB's in complying with the Federal laws and the variety of interpretations of those laws by State banking departments that regulate MSB's.

We believe fixing the bank discontinuance problem will also improve overall compliance by MSB's.

We are dedicated to the fight against money laundering and terrorist financing, but we also need banking services and the Federal Government's help to ensure continued access to banks.

Initially, the bank account problem impacted mom-and-pop stores and check casher locations.

However, 2 months ago, Bank of America informed MoneyGram that it would be terminating its long-term relationship with us.

This was not just a simple deposit account but, rather, a global banking relationship that generated millions of dollars in fees annually for Bank of America.

While Bank of America is only one of the many banks with which MoneyGram conducts business, its decision to terminate our account relationship was, and is, a serious issue.

In the meantime, in order to help our agents, MoneyGram has been negotiating with banks to establish special accounts, and hiring armored cars to serve agents who have had bank accounts closed. These actions, however, increase MoneyGram's cost.

A key point that gets lost in the discussion regarding bank relationships and compliance requirements, is that all of these issues cost money, which, in turn, leads to higher fees for consumers.

So, what is driving this exodus by the banks from MSB's? We believe it is the banks' fear of their own regulators.

The guidance increased the problem because it raised bankers' fears that they are responsible for policing the compliance programs of MSB accountholders.

Now, I would like to offer the committee a few suggestions on how this issue might be solved, as well as how compliance by MSB's might be improved.

First, the existing guidance must be rescinded. New guidance must clarify that banks are not required to evaluate the quality of

an MSB's compliance program, nor are they expected to monitor the activities of MSBs' customers. A draft of new guidance which embodies these concepts is attached to my testimony.

Second, an incentive should be provided to banks to resume serving MSB's, such as the Community Reinvestment Act credit.

Other incentives might also be effective, but there must be something to entice banks to reestablish accounts for MSB's.

Third, consistent enforcement of the anti-money laundering laws as they apply to MSB's is needed. Many States are interpreting the Federal money laundering laws in their own way, which has caused confusion and compliance challenges for MSB's.

MoneyGram urges Treasury and FinCEN to establish their preemptive authority to interpret and enforce the Bank Secrecy Act and related Federal laws.

An important offshoot of this suggestion is the need to create a system that can provide a consistent regulatory framework for the MSB industry.

MoneyGram is proposing an optional Federal licensing regime for MSB's that would be available to entities that operate in multiple jurisdictions and would be mandatory for any entities that operate in States that do not license their activity.

A Federal license would also help banks gain greater confidence in the regulatory oversight applied to MSB's.

Fourth, standards for MSB's as to what constitutes an effective compliance program must be established. We understand FinCEN is working with the IRS on an exam manual, and we applaud this effort. The absence of standards has left the MSB industry with no clear direction on which measures to take in order to establish an effective compliance program.

MoneyGram appreciates Congress holding a hearing on this important issue.

We recognize that Congress cannot solve the problem by ordering banks to serve MSB's, but we believe that, through its oversight and budget authority, Congress can compel Federal regulators to take appropriate action. MoneyGram requests that Congress continue to monitor the bank discontinuance problem and that Congress hold Federal regulators accountable for implementing a workable solution by years-end.

In conclusion, I want to thank you, Mr. Chairman and members of the committee, for the honor of having the opportunity to present testimony on behalf of MoneyGram. We appreciate your concern with this issue, Mr. Chairman, and we hope you will view us as a partner in this effort and call upon us for whatever assistance we can provide.

Thank you again.

[The prepared statement of Mr. Milne can be found on page 114 of the appendix.]

Mr. PRICE. Thank you, Mr. Milne. We appreciate your testimony, and your full testimony, as I mentioned, will be made a part of the record.

Mr. Goldman, general counsel for Financial Service Centers of America, we welcome you.

STATEMENT OF GERALD GOLDMAN, GENERAL COUNSEL, FINANCIAL SERVICE CENTERS OF AMERICA

Mr. GOLDMAN. Mr. Chairman and members of the committee, my name is Gerald Goldman. I serve as general counsel to FISCA, a national trade association of over 6,000 neighborhood financial service providers in the United States.

We serve millions of people engaging in tens of millions of small financial transactions.

As every business does, we rely on banks for our connection to the American financial system. For the past 6 years—this is not a new issue. For the past 6 years, banks have been abandoning us, first as a trickle and then continuously accelerating, so that now few banks are willing to service us, and when they go, that will be a disaster for the people we serve.

Six years ago, in response to my questions, then-FinCEN-Director Sloan said that the bulk of MSB's are law-abiding individuals, are providing legitimate services, and that, in his view, the MSB industry as a whole is no more a risk than any other business.

He said that 6 years ago.

Six years have passed.

In the course of those 6 years, two FinCEN directors, the Secretary of the Treasury, the Comptroller of the Currency, and the ABA and many Members of Congress have all, on the record, acknowledged that our industry is a key component of a healthy financial sector and that it is very important that we have access to banking services. In fact, in 2004, in a letter to Congresswoman Maloney, which she mentioned, OCC Comptroller Hawke noted the important role that money service businesses play, and stated that, absent extraordinary circumstances, the OCC would not direct or encourage any national bank to refuse their accounts. Just 6 months earlier, Comptroller Hawke, appearing before this very committee, stated that MSB's should not be dropped by banks as a class, and should be treated on a case-by-case basis.

All of these same public officials acknowledge that our industry has an exemplary record of Bank Secrecy Act compliance, and you heard today the flimsy aspects of a number of violations.

In fact, former Director Sloan stated that our industry—and I am quoting him now—"has set the standard for the financial services industry in the fight against money laundering, financial crimes, and terrorism," and the record shows that there have been very few violations.

Most of these public officials believe that bank discontinuance of our industry is just plain wrong.

We all agree on that.

In the past 12 months, there have been no less than three hearings—one in the Senate, one in the House, one by FinCEN itself—documenting the bank discontinuance problem. To its credit, the ABA has courageously recognized this problem and supports a solution.

In April 2005, we know that FinCEN issued its guidance, which has gotten nowhere.

Despite all of these valiant efforts, despite all of these statements, results have been illusory and to no avail. Not one bank has

reversed its termination policy. In fact, no banks are even here today—terminating banks.

Banks continue to terminate check cashers. None of those banks, as I said, are here.

For 6 years, we have had support by public officials, we have had no evidence of money laundering and no evidence that we discovered any terrorists, and yet bank discontinuance continues.

We conclude—this is our conclusion, on behalf of the industry that I represent—all efforts at regulatory change have failed and will continue to fail and will not solve this problem.

Regulation is not the answer. Its effort is hopelessly mired, and you saw it here in the last 2 hours, in a bureaucratic maze. We believe that it is time for legislative intervention before more real damage is done.

It is time for either absolution or compulsion. It is time to absolve banks of an unreasonable burden upon them to monitor and regulate our industry.

The only alternative to absolution is to compel the banks to treat us fairly, as they would any other business, and it is clear to me and to us that this compulsion alternative is politically less achievable.

We believe that there will be wide support by banks and MSB's for legislation which gives force to the policy of the MSB guidance that banks will not be held responsible for their customers' compliance with Bank Secrecy Act or other regulations.

To accomplish this, we are supporting a legislatively adopted self-certification program where MSB's will certify that they are in compliance with all the requirements of anti-money laundering laws, with swift and strong penalties for false certification.

We believe that our industry has taken and must continue to take responsibility for its own compliance obligations. Banks should not be called upon to become our regulators, and that is what has happened, no matter how you slice it.

We also believe that any legislation should eliminate the OCC designation of our industry as being high-risk, which took us down this road in the first place.

This would send a strong, clear message to the banks and other regulators that, by legislative action, we are going to turn a corner.

Finally, we stand ready to work with members of this committee, the ABA, and other MSB's on an urgent basis to craft the legislation proposed.

We believe that if this is not done, we will be back here a year from now talking about the same problem or, even worse, talking about a bigger problem.

So, let us go back to fighting money laundering. Let us not destroy a viable industry which serves hundreds of thousands of customers.

The facts demand no less.

Thank you.

[The prepared statement of Mr. Goldman can be found on page 82 of the appendix.]

Mr. PRICE. Thank you so much, Mr. Goldman. I appreciate your passion.

Mr. Abernathy, we welcome you today. Mr. Abernathy is executive director for financial institutions policy and regulatory affairs with the ABA.

STATEMENT OF WAYNE A. ABERNATHY, EXECUTIVE DIRECTOR FOR FINANCIAL INSTITUTIONS POLICY AND REGULATORY AFFAIRS, AMERICAN BANKERS ASSOCIATION

Mr. ABERNATHY. Thank you, Mr. Chairman, and members of the subcommittee.

Our anti-money laundering program today increasingly focuses on the legal activities of law-abiding people rather than on detecting and deterring crime and stopping terrorists.

Of course, this is not what we all intended, but it is the result that we have, and nowhere is this more evident than in its application to money service businesses.

In many situations, banks have raised fees to cover added compliance costs.

Some banks have discontinued accounts for MSB customers after a case-by-case analysis of their perceived money laundering regulatory risk.

Other banks have concluded that serving MSB's, in general, is not an attractive option, given the bank's reputation risk or regulatory risk tolerance.

The result has been unfortunate for all parties. Banks lose customers, customers lose access to banking services, and too many financial activities move off of the financial main street and into the shadows.

It will take supervisory, regulatory, and perhaps even legislative change to redress this.

Last year, FinCEN and the banking agencies took the important step of issuing interagency guidance and an interagency examination manual.

Despite all the good intentions, the guidance and the manual have fallen short of their goals.

More is needed to fulfill the policy pronouncement that ensured banks are, "not expected to act as the de facto regulators of the money services business industry,".

It is increasingly evident that the IRS and the States have taken concrete steps to oversee compliance by MSB's with the BSA and AML obligations.

If any gap remains, it is not for the banks to fill but for State and Federal Governments to address by applying direct MSB supervision.

The guidance in the manual should be amended to reflect and reinforce this reliance on the established Federal-State supervisory regime.

Supervisory expectations that a bank consider whether an MSB operates consistent with its legal obligations should be satisfied by a questionnaire executed and certified to by the MSB, reciting its implementation of the components of an AML compliance program. Similar questionnaires, for example, have been developed and used by banks to ascertain the BSA compliance posture of foreign correspondent banks.

Our members know the importance of providing all legitimate customers throughout all segments of society with banking services.

An underlying challenge is that there exists in the United States and in all countries a large pool of individuals outside of the financial mainstream. These individuals are often accustomed to using informal—and sometimes very informal—financial services providers. Governmental actions that discourage people from entering banks also make anti-money laundering goals far more difficult to achieve.

Therefore, it is the view of the ABA that the current MSB bank regulatory environment must change if we are to advance the goals of effectively serving all market segments, while reducing the risks of money laundering and terrorist financing.

ABA urges that State regulators not criminalize the efforts of banks that, in good faith and with reasonable diligence, enable MSB's to conduct business. Otherwise, the risks of unwarranted criminal litigation and unfounded injury to reputation will adversely impact a bank's risk assessment for providing account services to MSB's, and those services will likely diminish.

ABA believes that consistency in implementing regulatory policy can be promoted by conducting joint industry and agency training. Placing bank staff, MSB agents, and examiners in the same room to hear the same explanations helps ensure a consistent message, consistently communicated, and most importantly, it reinforces the teamwork approach that is likely to prove most successful in cutting off the flow of funds for criminal activities.

Neither banks, their customers, nor our BSA/AML efforts are served by driving a regulatory wedge between banks and legitimate MSB's, pushing large segments of America's economy into the shadows.

The members of the ABA will continue our support for efforts to improve the regulatory process so that we can all focus more on stopping criminal activities and avoid efforts that too often target legitimate businesses and their customers.

Mr. Chairman, we thank you and the members of this subcommittee for your leadership in this effort.

[The prepared statement of Mr. Abernathy can be found on page 61 of the appendix.]

Mr. PRICE. Thank you very much, Mr. Abernathy. We appreciate your participation today and your entire testimony.

Now, Mr. Landsman, executive director of the National Money Transmitters Association, we welcome you.

STATEMENT OF DAVID LANDSMAN, EXECUTIVE DIRECTOR, THE NATIONAL MONEY TRANSMITTERS ASSOCIATION, INC.

Mr. LANDSMAN. Thank you, Mr. Chairman. I am David Landsman, executive director of the National Money Transmitters Association.

The NMTA was founded in 1999 to voice the concerns of State-licensed remittance companies, or LRC's, of the United States.

Currently, we have 43 member companies, which collectively handle over $17 billion a year in migrant worker remittances.

I would like to thank the subcommittee on behalf of our members for allowing me to appear before you today. I would also like to express our gratitude to Congressman Charles Rangel, who has consistently shown his concern for the negative impact these account closings are having on our customers and their families, on the many countries that depend on remittances for their survival, and on the effectiveness of our Nation's anti-money laundering, or AML, strategy.

No one knows the exact amount, but we estimate that outbound remittances from the United States total at least $60 billion annually.

The approximately 620 American LRC's that handle these remittances have never faced more peril than we do today.

Banks are crucial to the operation of our business, and they are no longer willing to work with us, citing regulatory concerns.

These regulatory concerns are well-founded, but not because of any real money laundering risk. Banks get into trouble for having us as customers because Federal banking regulators have incorrectly classified all money service businesses, or MSB's, as high risk, and make no distinction within that stereotype between licensed and unlicensed remittance companies.

Now, these attempts to protect the banking system from the risk LRC's pose have backfired badly by threatening to destroy the best ally law enforcement has in the fight against money laundering.

If financial institutions are the first line of defense in our Nation's war against terrorist funding, then we LRC's are the special forces.

No sector of the financial industry has better compliance programs, a cleaner record, or is more essential to our Nation's AML efforts than LRC's.

The average remittance we send is approximately $243, hardly a size conducive to money laundering.

Although regulators say that they do not hold banks responsible for our supervision, that is exactly what is happening.

Under such conditions, it does not make sense for any bank to keep us as a customer, no matter how profitable our accounts are for them.

According to the New York State Banking Department's own survey, 42 percent of New York LRC banking relationships hang by a thread and are concentrated at only two banks.

If this situation is not remedied, and soon, then the ranks of LRC's all across the country, not just New York, will be decimated.

Unscrupulous, unlicensed operators will no doubt fill the void left by our departure.

Regulators without legislative guidance have steadfastly refused to grant any sort of protection that would allow banks to rely on our State licenses.

In order to solve this problem, we recommend the following steps.

Number one, remove the onus of supervising us from the banks' shoulders by law as soon as possible.

This may be done by officially recognizing some or all State licenses, defining all measures a bank is expected to take when opening our accounts, and making those measures practicable.

Banks would still have to verify our licenses and remain alert for red flags, as usual.

The LRC may be required to sign a self-certification form similar to the one used in foreign correspondent banking relationships.

Number two, start regulating LRC's at the Federal level with a voluntary, non-preemptive Federal AML certification that would involve initial application and vetting, published rules and standards that must be followed to maintain certification, and regular examinations and reports.

The current regulation of MSB's we have at the Federal level is not good enough. Create an MSB supervision department at FinCEN, and end the unfortunate division of AML responsibilities that currently exist between FinCEN and the IRS.

Let the MSB registration program gradually be replaced by something more meaningful that would give those firms that so desire a pathway to the credentials that it takes to get bank accounts.

Regulate the agent population through licensees like us, rather than trying to herd over 200,000 retail locations, most of which are mom-and-pop shops.

number three, our industry needs to take the first steps toward self-regulation. This would involve industry-driven training, standard setting, certification, and disciplinary procedures. While this is something that we ourselves need to do, government can help by encouraging LRC's to join together.

I thank the subcommittee once again for the opportunity to have our opinions heard.

[The prepared statement of Mr. Landsman can be found on page 105 of the appendix.]

Mr. PRICE. Thank you so much, Mr. Landsman. We appreciate your testimony and that of each of you. I want to once again assure you that all staff and members have received your full testimony and that it will be included in the record.

I would like to ask a few questions, just to try to shed a little light, because Mr. Goldman, your frustration and passion is clear, and it is shared by many folks. I think one of the things that is not understood by most folks is the consequence of having the banks go, and their service for MSB's, to not you and not me but to the individual on the street, if you would not mind commenting a little bit about what those real-life consequences are, and maybe some others would like to comment, as well.

Mr. GOLDMAN. I think it is pretty clear that the millions of people who use our services are the people who benefit from the fact that our services are serviced by banks.

If we eliminate the bank from the process, we cannot perform the service, and if we cannot perform the service, I do not know where it is going to go, but it will go someplace, because the need for our service will be the same with or without the banks.

Mr. PRICE. So, what does that mean to Mr. or Mrs. Smith on the street?

They would pay more for the services that you all are currently providing?

Mr. GOLDMAN. Well, Mr. and Mrs. Smith certainly, I believe, would pay more in an underground economy, unregulated, than it

is now, and so, the people in those income groups, who now rely on us, are going to have an enhancement in the course of their receiving their financial services, and the banks are not—the banks are not going to pick up that service.

They have rejected serving us to serve these people. They are not going to serve them.

They have not up to now, and they are not going to serve them directly.

Mr. PRICE. Mr. Abernathy?

Mr. ABERNATHY. Although I would generally agree with that, I would differ with it a little bit. Banks are increasingly providing services to populations of all stripes and locations and financial situations, but it is very difficult to penetrate many particular population groups for cultural reasons and a host of other causes, all causes that we are trying to overcome. That is why that important role is played by money service businesses.

It is painful to a banker to tell somebody no, we cannot provide services to you. We are in the business of providing services.

What it means to a Mr. or Mrs. Smith, when they cannot have that access, is they are further alienated not only from financial services but from the mainstream of our society, in general, and I think that there are multiple consequences that come from that.

Mr. PRICE. I think that we have done a poor job educating folks on that point.

Mr. Milne, did you have a comment?

Mr. MILNE. Yes. I think there are many consequences, Mr. Chairman.

I think one is access. As our agents are shut down, it limits the access points for consumers for these valuable products and services.

Two, I think, as was brought out in the panel this morning, we provide very valuable information to law enforcement in terms of anti-money laundering and law enforcement activities, and once again, those activities will get pushed underground as access is limited for those consumers, and then, finally, as I pointed out in my testimony, as we scramble to get the agents that provide our products and services to consumers bank accounts, we are ending up hiring armored cars, setting up bank accounts for them, and we have been really working hard to drive the pricing down for things like wire transfers, and this is going to increase our costs.

Mr. PRICE. Mr. Landsman?

Mr. LANDSMAN. Yes. One of our members is a company called Dahabshil, and the subcommittee has his testimony, Mr. Isaac Warsame. Around the time that he was getting his major bank account notification of closure, 2 weeks ago, the Islamic fundamentalists were taking over Mogadishu, and they are the largest transmitter to Somalia.

I think that is pretty clear.

So, the consequences to the consumer, of course, will be understandable.

They will pay higher prices.

They will have to give cash to friends and relatives who are traveling there.

It will take longer, it will be less convenient for them, but the consequences to national security are tremendous.

Dahabshil has an excellent compliance program. They take ID, they make reports, and they keep records, and most of their wire transfers are incredibly small, they are like $25, but if they do not survive, then all of this money will be going to a very dangerous place in the world with absolutely no control on this end.

Mr. PRICE. Given those comments and given the fact that I think it is readily apparent and certainly all would agree that no one desired to make the banks a de facto regulator of the MSB's, and not meaning to put you on the spot, but given the 5- to 6-year history of this recognition, clearly, by all involved, why do you think that no change has occurred in a positive direction? I will let anybody fall on that sword who wants to.

Mr. GOLDMAN. First, it took a few years for these regulators to really recognize and acknowledge the extent of the issue.

So, we will give them the first 3 years, and the last 3 years, I think there is some inherent bureaucratic inertia, and you know—very interesting—I would like to make two observations.

One is that we have not heard from the banks that have terminated.

You know, we have never really talked to the—and I think there is a wealth of knowledge that we could get from the banks that have terminated, and I suspect that they would agree that there is no clarity. They are being asked to be the regulators.

You will get all the war stories, and I think it is that there is no czar here.

There is nobody who is prepared or willing in the regulatory system to take the bull by the horns and say—I would say Mr. Fox, with all due respect, did really take the bull by the horns. I think, unfortunately, he left for a bank, but the reality is that he started to take the bull by the horns, and even he, himself, if you were to talk to him in the quiet of his office, recognized his own limitations. I mean all you have to do is re-read the testimony, and I'm not here to criticize the regulators, okay, but you reread the testimony of the regulators, and you know, they do not have all the answers, they do not have any direction, they all have pieces of the action, you know, but nobody has—nobody has taken it by the horns, and that is why I have said that I really believe, genuinely, that it has come time for the legislative body to make a statement, a legislative body to pass legislation and say, you know, no more blanket high risk and no more banks being asked to regulate the industry, and until that happens, we are having a lot of meetings, we are having a lot of conferences, we are having a lot of hearings, but nothing is happening.

The other thing I did want to say, to correct the record with Mr. Abernathy, is that he is correct. I mean the banks are making an effort in their own way to service non-bank customers.

The reality, I think, is that that is a long-term process, but the answer to your question, I think all you have to do is reread the testimony of the regulators today, and you have to ask yourself a lot of questions.

They are proving the point that somebody has to take the bull by the horns, and as far as we can see, the real candidates for doing that are the legislators.

Mr. PRICE. My time has expired, but if anybody else has a comment about that—

Mr. ABERNATHY. Just briefly, Mr. Chairman, I think that there has been a lot of progress, but it has been insufficient.

You can heat water up, but until it gets to 212 degrees, it does not boil, and the progress has been sort of one step forward, one step back.

We did get guidance.

The guidance did not quite do it. It is better than it was before.

It said some good things, but while saying some good things, it also created some ambiguities. When you give the ambiguity to an examiner without clear guidance, then the banks are left in the lurch, and that is a real problem that we have.

The way the law is written, there is a position of leadership, and that is at FinCEN.

It is interesting, the way the BSA is written, the Treasury Secretary, FinCEN—they have the responsibility for administering BSA. It is delegated from there to the bank regulators, but the policy maker is at FinCEN.

While Mr. Fox was there, I think a lot of progress was being made.

We would like to see that kind of progress continue, and then maybe we can get the water to boil and get something done.

Mr. PRICE. Let me recognize Ms. Maloney for a round of questions.

Mrs. MALONEY. I would like to thank everyone for their testimony, and I would like to ask, what steps do you take to ensure that the members of your association or agents who are part of your network are reputable, and what kind of screening do you perform?

Mr. GOLDMAN. Well, first of all, we provide manuals which have gotten the respect and support of FinCEN.

We were the first industry to provide manuals about responsibilities.

We provide training programs.

We have numerous meetings with members of our association.

I think that, without question, anti-money laundering—the imposition of anti-money laundering compliance is—it is not—it is our second most important priority. It is only second to the issue of bank discontinuance, and we are participants with FinCEN in DSAG, starting back when Peter DeGinis was there.

We worked from the beginning—we have worked for 15 years to be compliant, and I think that the proof is in the pudding.

When you get the results that you asked from FinCEN, you are going to find that there is little, if any, noncompliance, other than technical noncompliance, with Bank Secrecy Act laws. So, you know, we are kind of beating a dead horse here.

I mean the point of the matter is that we have not—notwithstanding what Mr. Abernathy said, with all due respect, we have not made progress. Not one bank has come back.

Not one bank that terminated us in the last 6 years has seen fit to come back, and not—and in fact, more banks are terminating us, and what I am saying is that you reach a point where you say something dramatic has to be done, and what we are suggesting is that it may be time for Congress to make a statement, because as I said, Madam Maloney, when you were not here for the moment, that my fear is that we are going to be back here next year listening and saying the same things that we said this year, and we said if you look back at the testimony in prior Congressional hearings on this issue, you will see the same things were said then.

So, we are kind of—we have to accept the fact that we bogged down and mired down.

Without placing responsibility on anybody—I am not even placing responsibility on a particular regulator. I am saying the regulatory process is not working, and I think it needs some direction, and I said in my oral testimony, I think two areas that we have to—I noted two areas that I think we have to deal with.

Mr. MILNE. Mrs. Maloney, maybe I could just touch on that question, as well.

At MoneyGram, we really take compliance and anti-money laundering very seriously, and really consider ourselves a partner with FinCEN and Treasury and the IRS in combatting that.

We start from the basic level of know your agent. We do background checks on all the agents that our services are provided through, run them through the OFAC list, look at criminal records.

We provide them with anti-money laundering training and compliance materials, help them set up their program, always go back and review that training with them at a later date, and of course, we run all the transactions through our computer system, looking for suspicious activity and any types of patterns.

So, we have a comprehensive compliance and anti-money laundering program, not only because we have to, but because it is the right thing to do.

Mrs. MALONEY. Well, as I testified and said earlier, in New York City, we have roughly 150 money services businesses in over 750 locations.

They employ 4,000 New Yorkers and serve many thousands each day, and with this discontinuance, it is causing a huge problem.

You heard the superintendent of banks speak forcefully against the New York State legislature's action to force the banks to do this business, and the banks have repeatedly said that they do not want to be the regulator; they are not a regulator.

I would like to ask each member of the panel, what do you think of the proposal that I put forward earlier that if the banks are not providing this service, then have the—let us legislate and have the Federal Reserve serve as a bank to this financial service industry, the MSB's, and starting with you, Mr. Goldman, what is your response to that proposal?

Mr. GOLDMAN. I wish I had one.

I am not familiar enough with how that would work and whether it would or not.

Mrs. MALONEY. They would serve as a bank, and you would be able to use, you know—they would be the bank to the MSB's.

Mr. GOLDMAN. I am not sure whether they could do that on a local basis. I am not clear on whether—

Mrs. MALONEY. With legislation, they could. They cannot now. If we pass legislation that said, since there is no banking services for the MSB's and they are providing services that are needed by thousands of people, that as a last resort, MSB's can bank through the Federal Reserve.

Mr. GOLDMAN. Well, as I said, if they could serve as the check cashers' bank, at least on its surface, it appears to me that we would have no objection. At least we know we would have one bank.

Mrs. MALONEY. Mr. Milne, do you have a comment?

Mr. MILNE. I am not an expert on what level of service the Federal Reserve could provide on a local level for the depository requirements that these smaller MSB's have, although I do agree with you that Federal preemption, I think, is a necessary part of this, and whether it is the Federal Reserve or it is FinCEN, somebody who has oversight on MSB's at a Federal level, an optional—maybe charter at a Federal level—I think would bring a lot of credibility to the industry, and I think would help on an interpretation, a consistent interpretation of AML and compliance laws across the country.

So, I think, you know, preemption at a Federal level from a regulatory standpoint would be a huge step forward.

Mrs. MALONEY. Mr. Abernathy?

Mr. PRICE. The gentlelady's time has expired, but you are welcome to continue.

Mr. ABERNATHY. Certainly, Mrs. Maloney, this would be with the benefit of only having the chance to think about it since you presented the question and not having given it long-term thought. I would wonder whether such a proposal would change fundamentally the nature of the Federal Reserve, which right now serves as a backstop to the retail financial system. To then put them into that posture might move them into the retail sector of the economy, and I am not sure that that is where we want the Federal Reserve to be.

Mrs. MALONEY. If the retail banks in our country refuse to provide this service—and we are a country that believes in free enterprise, we believe it has made this country great.

The superintendent of banks raised constitutional questions of requiring them—the banks are saying it is unfair, that they are not regulators, they are providing services.

If this service is not provided anywhere else and it is a service that benefits people—you know what I find unusual about this—and I want to share this with the chairman.

We constantly have meetings, in this committee and others, about how we provide services to needy neighborhoods.

Here we have MSB's—they are in all neighborhoods, but in certain neighborhoods in New York, they are the only financial services there.

So, sometimes there are proposals—let us create a Federal bank or a State bank that will go in and provide these services, and yet, that would be great expense, great overhead, and yet, a service that is there is essentially being cut off to many people, and we

need to have some answer that respects free enterprise, respects the fundamentals of this country, but the fact that the New York State legislature and the New York State Assembly and Senate are passing bills requiring banks to do business in certain areas—this shows the crisis level that it has reached in New York State.

There are rumors that the two smaller banks may be bought by bigger banks that will not provide the service. Therefore, this whole service, reaching hundreds of thousands of New Yorkers, would not be there. Then, if that was cut off, immediately there would be a crisis meeting in this committee, how do we get the banking services and check cashing services into the communities.

You know, so we have to think creatively of how we can work in the free enterprise system and our constitution to provide these services, and if the Federal Reserve is the backstop, maybe they need to be the backstop to this.

Maybe they need to create a place where we can have this transaction take place so that the service continued to help hundreds of thousands of people.

So, that is where the thought came from, because there are a lot of problems here, but everyone agrees that the service should continue, and maybe if you put the bill forward, maybe FinCEN and OCC would come out with some regulations that clarify where we should go.

Could we hear Mr. Landsman's—

Mr. PRICE. That is what I was about to say. I appreciate you sharing that with me and the committee, and if Mr. Landsman would comment, please.

Mr. LANDSMAN. The NMTA is the primary sponsor of the bill you are referring to, and I agree with you, it is a desperation measure.

We are concerned that it not be interpreted as a coercive measure against the banks. Rather, we are trying to find some way to give them the safe harbor, the protection that they can feel comfortable banking with us without having people point fingers at them.

In fact, your suggestion was used by the Government of Dubai, I understand, when they had similar problems because of severe money laundering concerns. The banks were closing the accounts of money exchangers there, but the money exchangers were incredibly important money transmitters, because of all their migrant labor that comes from south Asia, mostly.

So, the central bank did step in there, but Dubai is a very small country.

The thing that we need the banks for very much is to get small deposits from the agent location into the branches of the major banks that are right next door.

So, if an agent of ours has 1,000 or 2,000 dollars that he has collected from the public, he can walk right next door and deposit it to our account.

That is the fastest, cheapest, and safest way for us to run our business.

Other than that, we have to send an armored car, and it just does not pay, because the money that it costs for an armored car service and the additional delay is practically all the money we ever make on it.

Mr. PRICE. Thank you for that. The gentlelady's time has expired. I appreciate your participation.

I want to thank each of the panel members again for your participation and your testimony.

The Chair notes that some members may have additional questions for this panel which they may wish to submit in writing, and 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, and with that, this hearing is adjourned.

[Whereupon, at 12:43 p.m., the subcommittee was adjourned.]

A P P E N D I X

June 21, 2006

STATEMENT OF CHAIRMAN SPENCER BACHUS
SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT
"THE BANK SECRECY ACT'S IMPACT ON MONEY SERVICE BUSINESSES"
JUNE 21, 2006

Good morning. The subcommittee will come to order. At today's hearing we will review the oversight and regulation of Money Service Businesses (MSBs). More specifically, we will address the impact that the Bank Secrecy Act and related financial institution account discontinuances have had on MSBs. After years of studying this issue, I remain concerned that financial institutions continue to sever their relationships with MSBs and hope today's hearing will help stem the tide of financial institutions that terminate their relationships with MSBs. MSBs provide a valuable service to consumers and in some instances are the only financial services available to them. Banks and MSBs should comply with any money laundering guidance issued by their regulator; nonetheless, terminating an entire regulated industry and forcing its customers into the underground financial system creates a massive money laundering risk.

A business is generally considered to be a MSB if: 1) it offers one or more of these services: money orders, traveler's checks, check cashing, currency dealing or exchange, or stored value; and 2) the business either conducts more than $1,000 in those activities with the same person in one day or provides money transfer services in any amount.

MSBs are regulated at the State level and are required to comply with the Bank Secrecy Act (BSA) at the Federal level. Currently, twenty-eight

states and the District of Columbia have regulations requiring MSBs to be licensed by the State banking agency, and some of these States have specific laws regarding transmittals abroad. In many of these States, a MSB has to submit to a rigorous review, including providing financial statements and internal audit reports and permitting background checks on the owners and managers. Furthermore, the licensing process requires annual training, current BSA compliance programs, and the submission of a surety bond.

Since the adoption of the USA PATRIOT Act, MSBs have been required to adopt a written anti-money laundering compliance program and conduct independent reviews of their programs. MSBs are also required to register with FinCEN and are examined for BSA compliance by the IRS. Certain MSBs are also required to file Suspicious Activity Reports for transactions involving at least $2,000. In addition, MSBs are required to file CTRs for cash transactions more than $10,000 and must also maintain information on funds transfers of $3,000 or more.

Despite the increased regulation of MSBs, the bank regulators and their examiners have classified all MSB accounts as "high risk," regardless of whether there have been any actual problems. Banks have been required to investigate the money laundering compliance standards of the MSBs, forcing them to become the de facto regulator of these institutions. FinCEN and the Federal banking regulators have issued guidance twice. Unfortunately, the requirements continue to be vague, subjective, and burdensome to the banks. Over the past year, at least three national banks have ceased offering services to MSBs, and some state-chartered institutions have also discontinued service.

In response to concerns raised over the previous year by MSBs and financial institutions, FinCEN issued an Advance Notice of Proposed Rule Making (ANPR) in March. The comment period for the ANPR ends on July 10, 2006. I am hopeful that today's discussion will shed some light on this issue and be taken into consideration as FinCEN and the bank regulatory agencies move forward with a rule.

In closing, I would like ask unanimous consent that Congressman Rangel, the Ranking Member of the Ways & Means Committee, participate in today's hearing. We welcome him to the Committee and thank him for all of his work on this issue.

The chair now recognizes the Ranking Member of the Subcommittee, Mr. Sanders, for any opening statement that he would like to make.

Statement of the Honorable Sue Kelly

Thank you Chairman Bachus for holding this important hearing.

Securing our financial system has been an important goal of this committee since the September 11, 2001 attacks on our country. With the leadership of Chairman Oxley and this committee, we have strengthened the Bank Secrecy Act, given more resources to FinCEN, helped create the Office of Terrorism and Financial Intelligence in Treasury, and worked to improve financial defenses overseas in our friends and allies.

In the course of making these improvements, we have confronted many complexities, many of which we have yet to fully resolve.

Money Service Businesses are an area where many complexities still exist. This is something we must keep working on, which is why I appreciate Chairman Bachus and Ranking Member Maloney holding this hearing today.

We of course cannot ignore an area that has been prone to exploitation by Al Qaeda or those supporting state sponsors of terrorism like Iran or Syria.

But we also must acknowledge the importance of MSBs to our financial system and to many law-abiding people.

We cannot let our system for protecting the financial system to be pulled along by the swinging pendulum of government regulators compensating for mistakes of the past.

The circumstances we are currently facing with the BSA are no doubt exacerbated by the highly-fragmented structure of the anti-money laundering system, making it even more important for us to work together in finding a unified approach that examiners, financial institutions and the general public can understand and adhere to.

Discontinuance of innocent MSBs is often seen as a symptom of overzealous examiners.

And there are reasons for being concerned about the regulator's responsiveness to these concerns.

MSB issues did not rate a single line in the OCC ombudsman's most recent report.

The last two times OCC has testified before this subcommittee MSB issues were not even mentioned.

The OCC and its Ombudsman's office must give more focus to ensuring MSB customers of banks are treated fairly by OCC examiners and banks. This should include compiling specific data on MSB related appeals and asking questions about the treatment of MSB issues in the examination questionnaire banks fill out for the Ombudsman's office.

While the OCC states in its testimony that "The OCC, does not, as a matter of policy, require any national bank to close the accounts of an MSB or any other customer," we must all recognize that the closures continue, along with an accompanying, misleading impression that all of the affected MSBs must be at fault.

MSB's should not be the scapegoat for regulatory failures.

Failure to act diligently on this matter directly questions how effective OCC and other **delegated** BSA examiners are, and raises concerns about whether more needs to be done to accentuate the BSA's center of gravity at FinCEN.

Testimony of

Wayne A. Abernathy

On Behalf of the

AMERICAN **BANKERS** ASSOCIATION

Before the

Subcommittee on Financial Institutions and Consumer Credit

Of the

Committee on Financial Services

United States House of Representatives

On

"Bank Secrecy Act's Impact on Money Services Businesses"

June 21, 2006

Testimony of Wayne A. Abernathy

on behalf of the

American **Bankers** Association

before the

Subcommittee on Financial Institutions and Consumer Credit

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Committee on Financial Services

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June 21, 2006

Mr. Chairman and members of the Committee, I am Wayne Abernathy, Executive Director for Financial Institution Policy and Regulatory Affairs with the American Bankers Association (ABA). ABA appreciates this opportunity to discuss how the recent enforcement and supervisory priorities of the regulatory agencies with respect to the Bank Secrecy Act has impacted the banking industry's relationships with 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 closely with the Financial Crimes Enforcement Network (FinCEN), our supervisory agencies and other government authorities in the challenging area of detecting and reporting the myriad financial crimes that involve fraud, identity theft, money laundering and terrorist financing. Despite our mutual support for cooperation, there are a number of concerns regarding how to achieve compliance. These problems are illustrated by the current challenges experienced by banks seeking to serve MSBs while meeting regulatory expectations for Bank Secrecy Act (BSA) and anti-money laundering (AML) due diligence.

Recent Developments

Historically, virtually all banks have had customer relationships with businesses engaged in a range of money services. However, the general regulatory approach toward bank BSA/AML compliance, particularly demonstrated in its application toward MSB customers, has lately adversely impacted those relationships by changing the cost/benefit calculus of maintaining MSB accounts.

Increased costs from the regulatory oversight of MSB activity have caused all banks to take a harder look at the risks and benefits of serving MSBs. In many situations banks have raised fees to cover the added compliance costs of serving MSBs. Some banks have discontinued accounts for MSB customers after a case-by-case analysis of their perceived money laundering regulatory risk. Finally, a few banks have re-evaluated their business strategies and concluded that serving MSBs in general is not an economically attractive option given the bank's reputation risk or regulatory risk tolerance.

The result, of course, while predictable has been unfortunate for all parties. Banks lose customers, customers lose access to banking services, and some financial activities move out of the supervised financial mainstream. It will take supervisory, regulatory, and perhaps even legislative change to redress this. The good news is, I believe, that all involved are earnestly engaged in the effort to find solutions to this situation.

Last year, FinCEN and the banking agencies began the attempt to redress the trend toward discontinuance of bank services to MSBs, particularly where attributable to unintended or uncertain regulatory expectations with respect to BSA and AML obligations of insured banks vis-à-vis their MSB customers. An important step was issuing the Interagency Interpretive Guidance on Providing Banking Services to Money Services Businesses Operating in the U.S. (the Guidance) and the Interagency BSA/AML Examination Manual (the Manual). Despite all parties' good intentions in developing these resources, the Guidance and the Manual have fallen short of their goal to stem bank discontinuance of MSB accounts. They were an essential part of the process, but more needs to be done.

ABA believes that more success is needed to match the policy pronouncement that insured banks are "not expected ...to act as the *de facto* regulators of the money services business industry" with the specific standards recited in the Guidance and interpreted by examiners. In order to strengthen this alignment, ABA recommends the following steps:

- Announce that the federal banking agencies rely on FinCEN, the state licensing authorities, and the Internal Revenue Service (IRS) to regulate and supervise the BSA/AML obligations of MSBs and amend the Guidance and the Manual accordingly;

- Recognize that licensed MSBs that serve low-income or emerging markets in their communities are generally not high risk and deserve basic commercial customer due diligence;
- Decriminalize the compliance obligations of banks that serve their communities' MSBs in good faith; and
- Initiate joint industry/government training of bankers, MSBs and examiners on BSA/AML obligations, procedures and supervisory scenarios.

MSBs, Banks, and Responsible Regulatory Oversight

In the Spring of last year, the cooperative efforts of industry and government representatives on the Bank Secrecy Act Advisory Group (BSAAG) and its subcommittees on examinations and non-bank financial institutions resulted in interagency guidance intended to clarify regulatory expectations for banks conducting BSA due diligence for their customers who were MSBs. The hope was that the Guidance would enable banks to develop appropriate BSA risk assessments of MSB activity without imposing regulatory burdens that would discourage banks from serving such customers.

Unfortunately, the Guidance has not provided a firm enough separation between low and high risk profiles and their corresponding due diligence expectations to achieve its intended ends.

Rather, the banks' experiences with their internal auditors and their examiners have prompted the adoption of the high risk due diligence criteria as a minimum standard by most institutions serving MSBs. Although MSBs are only customers, not agents of banks, this distinction is often lost when applying the Guidance. The resulting level of regulatory impact is often excessive and unwarranted by the true risk profile of the MSBs, but it is

frequently deemed necessary for those banks still serving MSBs in order to avoid supervisory criticism.

Some institutions have discontinued serving particular MSBs or large segments of the MSB sector. They have evaluated their business options in light of the costs of performing extensive due diligence on MSB accounts and their exposure to the reputation risk derived from the threat of aggressive supervisory or enforcement activities, including those from local law enforcement officials. They have concluded that despite established relationships and proffers of elaborate MSB programs backed by extensive independent testing, the risks/costs outweigh the benefits of maintaining accounts that in many cases bring in relatively marginal revenues for the banks.

Reliance on the Responsible Regulatory Authorities Covering MSBs is the Key

As administrator of the Bank Secrecy Act, FinCEN establishes the BSA/AML regulatory requirements for all participants in the financial services industry. Each industry segment's respective supervisory agency is then responsible for overseeing compliance and undertaking enforcement. This division of regulatory responsibility can be key to apportioning the compliance obligations properly among the various industry participants and their regulators.

This is entirely consistent with the Frequently Asked Questions (FAQs) issued with the Guidance. The FAQs denied that any educational obligation was being imposed on banks with respect to their MSB customers and went on to state unequivocally that "the Bank Secrecy Act does not require, and neither FinCEN nor the federal banking agencies expect, banking organizations to serve as the *de facto* regulators of the money services businesses for which they maintain accounts."

It is increasingly evident that IRS and the states have taken concrete steps to oversee compliance by MSBs with their BSA/AML obligations. The recently announced milestone of IRS achieving information-sharing agreements with 33 states and Puerto Rico covering BSA compliance among MSBs illustrates that the rightful regulators of the money services industry are mobilized to leverage their resources for enforcing registration, cash transaction reporting, and suspicious transaction reporting obligations. The IRS has also expanded its BSA examination capacity with the dedication of significantly more agents to the task of evaluating MSB compliance. If any gap remains in MSB regulatory oversight, it is not for the banks to fill, but for the state and federal governments to address by applying direct MSB supervision and by appropriating the necessary regulatory agency resources.

The federal banking agencies must make it clear to their own examiners and to the banking industry that they rely on FinCEN, the states that license MSBs and the IRS to regulate, supervise, examine and enforce against MSBs whatever BSA/AML compliance obligations they must observe. This should be expressly stated in the Guidance and the Manual and underscored in any internal agency directions to examiners and their managers. Unless this Washington policy position is instilled in the examiner culture, and bank examiners are assured that exercising their judgment consistent with the policy is supported by their superiors, no supervisory differences will result at the field level, and current bank reluctance to serve MSBs will persist.

Amend Guidance and Manual to Reinforce Responsible Regulatory Oversight

The Guidance and the Manual must be amended to reflect and reinforce this reliance on the established federal/state supervisory regime. Currently, the Guidance recites a checklist of "actions as part of an appropriate due diligence review or risk assessment of a money services business seeking to establish an account relationship." With the possible exception of on-site visits, each of the suggested actions is a "review" intended to evaluate the operation of the MSB's anti-money laundering program. Each of these components rightfully belongs in the exclusive realm of the MSB's government regulator.

Such supervisory expectations are plainly inconsistent with the Guidance's commitment not to hold banks responsible for their customers' compliance with BSA. In addition, this degree of involvement could expose banks to liability for deficiencies in the compliance program of the MSBs, a position that no banker can feel comfortable occupying. It is inconsistent with good supervisory principles, which should rely upon parties being responsible for their own actions. It follows that the due diligence elements recited in Part II of the Guidance effectively require banks to be *de facto* regulators, and therefore these elements should be eliminated.

Permit Certified Questionnaire Responses to Satisfy Due Diligence Expectations

The bank's treatment of any MSB that actually deserves categorization as high risk should parallel that expected of other commercial customers in such a category by applying appropriate heightened monitoring to the MSB's own financial activity, not monitoring the activity of the MSB's customers. As with other regulated financial services' customers, any supervisory expectation that a bank consider whether an MSB operates consistent with its

legal obligations should be able to be satisfied by a questionnaire executed, and certified to, by the MSB reciting its implementation of the components of an AML compliance program appropriate to its own risk profile.

ABA believes that suitable certification forms can be developed as part of the normal course of business between banks and high risk MSBs. Similar questionnaires, for example, have been developed and used by banks to ascertain the BSA compliance posture of foreign correspondent banks.

Obtaining such certification should serve as appropriate due diligence that supervisory agencies expect from banks concerning a high risk MSB's BSA compliance program. To do otherwise forces upon banks not only an unfunded mandate, but a mandate they are not able or legally deputized or authorized to enforce.

More Accurately Reflect the Risk Profile of Community MSBs

Our members know the importance of providing all legitimate customers, throughout all segments of society, with banking services. For low-income and emerging markets, simple check-cashing and financial transactions are essential financial products that consumers seek through MSBs as well as banks.

At current regulatory thresholds, many small businesses find themselves swept into the scope of check cashing by virtue of cashing payroll checks at their convenience stores, supermarkets and other similar community business locations. These so-called non-core MSBs have a low level of money laundering risk, but even in these instances the basic hurdles of registration or licensing and simple BSA controls are matters that impose significant compliance challenges often beyond their resources or expertise.

In addition to check-cashing, money transmitters are a common form of MSBs serving the emerging markets. Remittance flows are an important and stable source of funds for many countries and constitute a substantial part of financial inflows for countries with a large migrant labor force working abroad, financial flows that are usually much more successful in providing financial help to needy families than are government and international aid programs. Where there is a concern that remittance systems can be misused, surely the risk of misuse would be reduced if transfers were channeled through remittance systems that are part of the supervised financial mainstream.

To address the risks, a two-prong approach is evolving – one prong involves efforts by governments to encourage the use of formal systems (such as banks and licensed MSBs) by lowering the costs 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 clear, direct, and effective anti-money laundering standards for entities such as MSBs. These initiatives are progressing in the United States and, as we have heard from other witnesses, the MSB regulatory infrastructure is increasingly robust and effective.

An underlying challenge is that there exists in the United States and most other countries a large pool of individuals outside of the financial mainstream. Such individuals are often accustomed to using both formal (and regulated) financial institutions and informal (sometimes very "informal") financial services providers. Economic and social incentives that move this group towards "underground" financial services providers ultimately harm

the interests of the individuals, of law-abiding financial services providers, and of the general public. As we can easily surmise, the underground financial services providers may service law-abiding persons as well as criminals. Thus, governmental actions that discourage people from entering banks and other depository institutions may have the effect of also making anti-money laundering goals far more difficult to achieve. Therefore, it is the view of the ABA that the current MSB-bank regulatory environment must change if we are to advance the goals of effectively serving particular market segments while reducing the risks of money laundering and terrorist financing.

FinCEN and the federal banking agencies should underscore their policy endorsements for bringing more people into the financial mainstream by including among the ranks of low-risk activities recited in the Guidance those MSBs that have effective programs that reach out to these individuals.

The banking industry certainly understands and appreciates the need to analyze the levels of risk involved with maintaining MSB relationships. Each bank must evaluate those risks and match them with their business capabilities and prospects. At times, banks will appropriately exit relationships due to the risk perceived with a particular MSB. This practice is consistent with the service relationships it has with any customer. At other times, banks may want to continue valued relationships. In either instance, the best decisions of each individual bank will be made when an MSB's BSA risk is fairly evaluated based on a true understanding of the underlying business operations and banking history of the customer and not skewed by a plethora of red tape and potential regulatory pitfalls when in reality there are low BSA/AML risks applicable to a substantial majority of established MSB customers.

ABA is preparing specific suggestions on modifying the current Guidance to delineate better the differences between low risk and high risk MSBs that it will submit as part of its comment letter in connection with the pending Advanced Notice of Proposed Rulemaking issued by FinCEN to address the issue of access to banking services by money services businesses.[1] We will be pleased to provide our suggestions to this subcommittee as well.

Decriminalize BSA Compliance

As then Acting Comptroller of the Currency Julie Williams noted in her Senate testimony last year, state and municipal prosecution of banks for serving MSBs when the customers of the MSBs have engaged in money laundering have contributed to bank reluctance to continue banking MSBs. Prosecutors who pursue banks for the activity of a customer's customer ignore the responsibility of their own state agencies to regulate effectively the AML compliance of their licensed MSBs and their agent networks. ABA urges state regulators to place the onus for MSB anti-money laundering compliance on their licensees and not criminalize the efforts of banks that in good faith and with reasonable diligence provide accounts to enable their communities' MSBs to conduct business. If zealous prosecutors blame banks for the failure of state licensing oversight, the risks of unwarranted criminal litigation and unfounded injury to reputation will adversely impact a bank's risk assessment for providing account services to MSBs—and those services will likely diminish.

[1] See, 71 Fed. Register 12308 (March 10, 2006.)

Frankly, ABA believes that the state regulatory bodies and their associations, such as the Conference of State Bank Supervisors and the Money Transmitters Regulatory Association, are well-positioned to oversee MSB BSA compliance without the intervention of criminal sanctions against banks. Accordingly, ABA urges FinCEN, as Treasury's outreach agency to law enforcement, to work with state regulators, state attorneys general and county district attorneys to strengthen MSB enforcement at the source and to reinforce the apportionment of BSA compliance oversight among federal and state authorities consistent with the regulatory responsibilities in a dual financial services system.

Conduct Joint Industry/Agency Training

ABA believes that consistency in implementing regulatory policy can be promoted by conducting joint industry/agency training. ABA has encouraged this type of initiative in prior testimony and urges its application in this instance. Placing bank staff, MSB agents and examiners in the same room to hear the same explanations and authorized interpretations helps ensure a consistent message consistently communicated. Having a mixed industry/agency audience work through supervisory case studies improves all participants' comprehension and judgment in applying available guidance. And, most importantly, it reinforces the teamwork approach that is likely to prove most successful in cutting off the flow of funds for criminal activities.

ABA offers to work with all involved to develop such joint training not only on the MSB guidance, but with respect to BSA compliance generally, or on any of its component topics.

Conclusion

In the past several years, both banks and money services businesses have made enormous strides in improving BSA/AML programs and enhancing their detection and reporting of suspicious transactions. Yet despite these advances, federal regulatory pressures continue to make serving licensed MSBs unattractive to banks on a cost/benefit basis and jeopardize long standing business relationships. As we build on the progress made, let us take the next steps to make the first steps effective. Neither banks, nor their customers, nor our BSA/AML efforts are served by driving a regulatory wedge between banks and legitimate MSBs, pushing large segments of America's economy into the hands of informal, poorly monitored, and often illicit payment mechanisms. Such an outcome should be anathema to the goals at the core of the Bank Secrecy Act and national anti-money laundering policy.

Mr. Chairman and members of the committee, ABA has been in the forefront of efforts to develop a strong public-private partnership to combat financial crime, including money laundering and terrorist financing. This partnership has achieved important successes, but we know that more can be accomplished. ABA will continue our support for these efforts and will contribute its constructive and specific suggestions to improve the regulatory process going forward, so that we can all focus more on stopping criminal activities and eliminate efforts that too often target legitimate businesses and their customers.

STATEMENT OF ACTING ASSOCIATE DIRECTOR
FOR REGULATORY POLICY AND PROGRAMS
DON CARBAUGH
FINANCIAL CRIMES ENFORCEMENT NETWORK
UNITED STATES DEPARTMENT OF THE TREASURY

BEFORE THE
HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON
FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

JUNE 21, 2006

Chairman Bachus, Ranking Member Sanders, and distinguished members of the Subcommittee, I appreciate the opportunity to appear before you today to discuss initiatives that the Financial Crimes Enforcement Network is implementing under the Bank Secrecy Act relating to the money services business sector. Your leadership and commitment to understanding and publicly discussing the issues confronting this industry is critical not only to the safety and soundness of our financial system, but also to our nation's security.

I am pleased to be here today with Eileen Mayer, Director of the Small Business/ Self Employed Division of the Internal Revenue Service; Ann Jaedicke, Deputy Comptroller for Compliance Policy at the Office of the Comptroller of the Currency; and Superintendent Diana Taylor from the New York State Banking Department. Each of these agencies plays a vital role in implementing Bank Secrecy Act requirements. I am happy to say we have forged a strong working relationship in our united effort to regulate the money services business industry.

The Financial Crimes Enforcement Network (FinCEN) has regulated the money services business industry under the Bank Secrecy Act since the 1990s. Issues surrounding the money services business regulatory regime, including the need to identify unlicensed and unregistered money services businesses, conduct robust federal Bank Secrecy Act compliance examinations, and ensure access to banking services, continue to be at the forefront of our agenda.

As you may already know, the term "money services businesses" under our regulations refers to five distinct types of financial services providers: (1) currency exchangers; (2) check cashers; (3) issuers, sellers, or redeemers of traveler's checks, money orders, or stored value; (4) the United States Postal Service; and (5) money transmitters.

Bank Secrecy Act regulations require money services businesses to: establish written anti-money laundering programs; file Currency Transaction Reports and Suspicious Activity Reports (certain money services businesses only); maintain certain records with regard to customers who purchase monetary instruments with cash; record certain information about funds transfers; and include certain information in the transmittals of orders for such funds transfers. In addition, certain money services businesses are required to register with FinCEN and maintain a list of agents.

Money services businesses provide various financial products that have traditionally been provided at banking institutions. For example, a money services business customer can take his or her paycheck to a check casher and convert it into cash. Customers can also purchase money orders or transfer the funds, both within the United States and abroad, using the services of a money transmitter. All such services are available without requiring the customer to establish an account relationship.

Access to Banking Services

As you are aware, there has been mounting concern among FinCEN, financial regulators, and the money services business industry regarding the ability of money services businesses to obtain and maintain banking services. Many banks have stated their uncertainty as to the appropriate steps that they should take under the Bank Secrecy Act to manage potential anti-money laundering and terrorist financing risks. At the same time, the money services business industry has expressed concern that misperceptions of risk may be unfairly labeling them as "unbankable."

Individual decisions to terminate account relationships, when compounded across the U.S. banking system, have the potential to result in a serious restriction in available banking services to an entire market segment. The money services business industry provides valuable financial services, especially to individuals who may not have ready access to the formal banking sector and require bank accounts.

Consequently, it is important that money services businesses that comply with the requirements of the Bank Secrecy Act and applicable state laws remain within the formal financial sector, subject to appropriate anti-

money laundering controls. Equally important is ensuring that the money services business industry maintain the same level of transparency, including the implementation of a full range of anti-money laundering controls as required by law, as do other financial institutions.

If money services business account relationships are terminated on a widespread basis, we believe many of these businesses could go "underground." 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.

In March 2005, the Non-Bank Financial Institutions and the Examination subcommittees of the Bank Secrecy Act Advisory Group jointly hosted a fact-finding meeting to solicit information from banks as well as money services businesses on issues surrounding the provision of banking services to the money services business industry. Subsequently, in April 2005, FinCEN and the federal banking agencies issued interagency guidance to the banking industry on regulatory expectations when providing banking services to domestic money services businesses. FinCEN issued a companion advisory providing guidance to money services businesses on what they should expect when obtaining and maintaining banking services.

Guidance, Education & Regulation

Currently, based upon what we learned at the March 2005 meeting, and in subsequent discussions with other federal and state regulators, law enforcement, and the industry, we have developed and are implementing a three-point plan for addressing these issues:

1. Guidance – That outlines with specificity Bank Secrecy Act compliance expectations when banks maintain accounts for money services businesses.

In March 2005, FinCEN and the federal banking agencies took the first step toward addressing the concerns expressed by banks and money services businesses by issuing a Joint 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 banks 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.

Shortly after issuing this Joint Statement, we issued the more specific guidance that I mentioned earlier in my testimony on the compliance expectations for both banks and money services businesses. Since that time, we have issued additional guidance to banks and money services businesses, addressing issues ranging from development and implementation of anti-money laundering programs to registration and de-registration of money services businesses and record keeping obligations. We strongly believe that this guidance has assisted in further clarifying Bank Secrecy Act requirements and supervisory expectations as applied to accounts opened or maintained for money services businesses.

However, we neither believe that this guidance can solve all issues of concern relating to money services businesses nor that it will repair all relationships between money services businesses and banks. Nonetheless, we are committed to continue working with the federal banking agencies and other federal and state partners, law enforcement, banks, and money services businesses to do everything we can to clarify expectations.

2. Education – That provides banks and bank examiners enhanced education on the operation of the variety of products and services offered by money services businesses and the range of risks that each may pose.

As the regulatory regime for money services businesses has developed, FinCEN has taken a number of steps to reach out to this historically unregulated industry in order to educate it about the Bank Secrecy Act and applicable regulatory requirements.

We have developed a website devoted solely to money services businesses (www.msb.gov) and provided Bank Secrecy Act compliance materials to the industry in a nationwide outreach program and through ongoing regulatory guidance. We are also in the process of updating and publishing our educational materials in seven foreign languages.

3. Regulation – That strengthens the existing federal regulatory and examination regime for money service businesses, including coordinating with state regulators to better ensure consistency and leverage examination resources.

Within the last year, we have proposed to revise, simplify, and shorten the money services businesses Suspicious Activity Report form. Our expectation is that this will enhance the ease of completing and filing the form while still obtaining critical information needed by law enforcement. We will also reexamine our registration requirement for money services businesses and ensure that it is achieving the purpose intended in the law; that is, to identify the universe of lawfully operating money services businesses so that law enforcement can focus on those businesses that are operating outside the law.

With respect to the issues surrounding the provision of banking services to money services businesses, we are considering additional actions, guidance, and outreach necessary to address this issue. For example, in March 2006 we published an advance notice of proposed rulemaking to seek additional information from the banking and money services business industries on this issue. We will be receiving comments through July 10th and giving those comments our serious consideration.

We are also continuing to work closely with our colleagues at the Internal Revenue Service, to enhance the examination regime through the development of revised Bank Secrecy Act examination procedures, information sharing, and examination targeting. Additionally, as noted previously, we will continue to work closely with the Conference of State Bank Supervisors and state regulators on these issues. Executing individual agreements with state banking agencies will ensure better coordination and synergy with state-based examiners and improve consistency in examination processes.

We also intend to continue working on developing indicators for law enforcement and financial institutions to help identify unlicensed and unregistered money services businesses. By providing law enforcement, banks, and other financial institutions with indicia of illicit activity, they will be better able to help us identify money services businesses that choose to operate outside the regulatory regime.

It remains vital that we strike the appropriate balance between education and outreach, and criminal enforcement. We will continue to reach out to those businesses that remain uninformed about the regulatory requirements, while at the same time, support aggressive criminal enforcement of those businesses that do not intend to operate within the law and are engaged in furthering potential underlying criminal activity.

Registration with FinCEN

As noted, identification of money services businesses subject to Bank Secrecy Act requirements is an essential first step in effective regulation. Our effort to identify money services businesses begins with the Bank Secrecy Act requirement to register with FinCEN and maintain lists of agents. However, the industry is largely composed of small, unsophisticated businesses whose primary business is often something other than the money services that they provide – frequently, to the poor and unbanked. Additionally, due to language barriers within certain ethnic communities, there may be confusion regarding the applicable regulations.

Undoubtedly, our efforts to identify money services businesses have not been entirely effective. First, there are a substantial number of money services businesses that are not required to register, and many money services businesses required to register have not done so. Second, the current registration requirement is confusing and unwieldy, requiring a principal money services business to register – but not the principal's agents.

For example, the regulation requires that Western Union register with FinCEN as a money services business and keep accurate records of its 70,000-plus agents, but it does not require those agents to register (unless they provide money services business services as a principal in addition to those provided solely as an agent for Western Union). Notwithstanding that they do not have to register, these same agents are still defined to be money services businesses and thus have an independent obligation to comply with all other applicable Bank Secrecy Act requirements. Furthermore, these agents often provide other services unrelated to their agency relationship, such as check cashing, which – often unbeknownst to the independent agent – gives rise to an independent duty to register with FinCEN. Moreover, the regulation does not require the principal money service business to identify its agents to FinCEN or any appropriate law enforcement organization absent a specific request. This has created a significant gap in our efforts to identify the number of money services businesses currently operating.

We recognize that the complexity of our current approach to MSB registration may be contributing to a lack of registration and we are working on solutions to provide a more efficient and reliable method for identifying money services businesses.

Additionally, we plan to better leverage our state information sharing agreements. Most states require certain money services businesses (mostly money transmitters or check cashers) to be licensed; additionally, although most state requirements are geared toward consumer protection interests, more and more states are incorporating anti-money laundering requirements into their licensing regimes. We have executed information sharing

agreements with 41 state regulatory agencies, including those responsible for licensing and examining money services businesses. As a result of these agreements, we will be better able to compare and use our respective examination findings and other information to identify money services businesses and ensure their compliance with the Bank Secrecy Act.

We are also developing internal analytical products as well as working closely with the Internal Revenue Service and with law enforcement, in particular the Federal Bureau of Investigation and Immigration and Customs Enforcement, in our effort to identify possible unregistered money services businesses. Once we identify unregistered entities, we have developed outreach procedures for educating these businesses as to their obligations under the Bank Secrecy Act, and refer for prosecutorial investigation those entities that fail to register after appropriate outreach.

In conclusion, Mr. Chairman, we are grateful for your leadership and that of other members of the Subcommittee on this issue and stand ready to assist in your continuing efforts to ensure the safety and soundness of our financial system. Thank you for the opportunity to appear before you today. I look forward to any questions you have regarding my testimony.

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

Statement of

GERALD GOLDMAN
General Counsel

Financial Service Centers of America

Before the
U. S. House of Representatives
Committee on Financial Services
Subcommittee on Financial Institutions
And Consumer Credit

Regarding
Bank Secrecy Act's Impact on Money Services Businesses

Washington, D.C.

June 21, 2006

www.FISCA.ORG

NATIONAL HEADQUARTERS: COURT PLAZA SOUTH, EAST WING • 21 MAIN ST •PO BOX 647 •HACKENSACK, NJ 07602 •TEL. 201-487-0412 • FAX 201-487-3954
WASHINGTON, D.C. OFFICE: 1730 M STREET N.W. • SUITE 200 • WASHINGTON, D.C. 20036 • TEL. 202-296-3522 • FAX 202-296-7713

Mr. Chairman, Members of the Committee, my name is Gerald Goldman. I serve as General Counsel to the Financial Service Centers of America (FiSCA). I thank you for the opportunity to appear today to present our views with regard to the alarming number of banks making wide-scale terminations of their check casher customers. Those views will provide you a description of the serious plight of our industry, the tremendous efforts we have made thus far to find a solution to the problem, and the apparent indifference we continue to experience on the part of most banks and some federal regulators.

FiSCA is the national trade association representing over 6,000 neighborhood financial service providers throughout the United States. FiSCA's members provide non-traditional financial services including check cashing, funds transfers, money orders and utility bill payment services. We serve millions of customers, both banked and un-banked, who use us for the advantages that we provide: convenient access, service and the ability to obtain instant liquidity. The most important service that we offer is a place for hard-working people to cash their paychecks, a necessary service that they cannot always obtain at a bank, or choose not to. We serve customers from all walks of life, including urban communities and the under-banked, groups that the Financial Crimes Enforcement Network (FinCEN) and the federal banking agencies have stressed as being underserved by more traditional financial institutions.

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

to banking services." We are very much a part of the fabric of a healthy economy, yet our industry remains in peril.

As we have reported time and again, the MSB industry is experiencing a growing crisis of banks making wide-scale terminations of their accounts. In the State of New York, for example, there are some 640 licensed check cashers which last year cashed 35,687,745 checks with a total value of $15,509,239,471. Fully 87% of the state's check cashers are now served by only two banks. If one of those banks should terminate, the result may be disastrous. (One has already terminated its licensed money transmitters.) Other areas are experiencing similar trends. Moreover, of the banks that continue to serve the industry, many are refusing new accounts, or are placing onerous requirements on the accounts they currently maintain.

The MSB and banking industries are in agreement that the problem stems from a perception by federal bank regulators that check cashers and other MSBs are "high risk" for money laundering and financial crime. The trend gained momentum in 2000 following the OCC's issuance of a BSA Handbook and an advisory letter (Advisory Letter 2000-3) placing check cashers and other MSBs in high risk account categories. As a result of this guidance and heightened attention to anti-money laundering following passage of the USA Patriot Act, coupled with existing prejudices, federal bank examiners have been exerting undue pressure on banks servicing the industry. There is no question but that banks are required to expend greater resources in maintaining MSB customer compliance and monitoring systems, which has directly impacted the profitability of servicing this market sector. Banks have decided to invest resources in more profitable business lines. In some instances banks have terminated check

cashers due to direct criticism from bank examiners. In some cases the decision has been due to nebulous "reputational risk" concerns. In many cases banks refuse check cashers simply because we are MSBs; to be labelled an MSB is to be branded with a scarlet letter.

The high risk designation is a red herring. FinCEN, IRS and numerous state officials have publicly acknowledged that there is no palpable money laundering problem within the regulated check cashing industry. Moreover, significant government oversight of the industry presently exists. As MSBs, check cashers must register with the federal government and are subject to periodic IRS examination. In many states, check cashers are required to be licensed, and must undergo background screening and financial review. Licensing authorities typically impose recordkeeping and reporting requirements, and subject licensees to periodic examination by state (often banking department) examiners. As the result of recent Memoranda of Understanding between FinCEN and the various states, information gathered in examinations of check cashers is now shared between IRS and state authorities. Notwithstanding our objectively low risk profile, we continue to suffer discrimination and account terminations.

There is a consensus among FinCEN and the federal banking agencies that a bank discontinuance problem clearly exists, and that termination of MSB accounts is not in the interests of national security, and threatens access to financial services in urban communities and to the under-banked. Notwithstanding a clear acknowledgment of the problem, a regulatory solution has not been achieved and the terminations are continuing unabated.

We have worked long and hard to find a solution to the problem. I first reported the emergence of a bank discontinuance problem to FinCEN in November of 2000. Since that time, we have met with federal and state legislators, we have suggested legislation, we have written letters to scores of banks, we have met with FinCEN, OCC, and other bank regulatory agencies. We have testified before congressional sub-committees; in May of 2005 I testified on the issue before the U.S. Senate Committee on Banking, Housing and Urban Affairs. We have proposed that Treasury form an advisory group made up of representatives of the federal banking agencies, banks, and MSBs, for the sole purpose of ensuring access to banking services. More recently, we met with the American Bankers Association and other banking groups to develop a unified strategy. We have even called for a moratorium on MSB account terminations until a more permanent solution could be found. We have seen some progress; we were encouraged when FinCEN held hearings on the issue in March of 2005, and spearheaded the issuance of the April 26, 2005 Interagency Interpretive Guidance on Providing Banking Services to Money Services Businesses (the "MSB Guidance"). Unfortunately, any progress thus far has been illusory.

All of our efforts and the efforts of FinCEN have been for naught. No major banks that previously terminated their MSBs have returned to the industry. If anything, last year's MSB Guidance has merely exacerbated the situation; many banks view the MSB Guidance as just adding to the regulatory load in serving MSBs, and some banks have terminated their check cashers as a result of the Guidance.

It is time for either absolution or compulsion. We must either absolve banks of their obligation to act as the functional regulators of their check casher customers and

free them of their current regulatory burdens – or we must compel them to stop discriminating against this industry. It must be recognized that regulatory efforts will not work because even with regulatory reform, many banks have become so intransigent in their position that they are writing off the entire industry. Absent a lifting of the regulatory burden, the only way to resolve the problem is to compel banks to refrain from discriminating against this industry. Nothing short of a statutory solution will bring the banks back because this is discrimination. It is time to stop the charade. This situation requires legislative intervention.

We appreciate the efforts and support of the American Bankers Association on this issue, but we see no evidence at all that the banks that need to listen are getting the message. At our Annual FiSCA Conference in September 2005, we hosted a Bank Forum, the purpose of which was to bring together key players from the MSB industry, banks and regulators in an effort to improve relationships and address the misimpressions that serve to perpetuate the problem. Not one single bank that has terminated its MSBs agreed to attend.

Recently, an "Underbanked Financial Services Forum" was held in Chicago, at which numerous panel discussions explored the ways that banks can better serve the under-banked, a group that is now perceived as the next growth market for the banking industry. It is no small irony that while banks now see a value in serving the under-banked, banks are at the same time denying us the opportunity to serve this same group.

From the inception of this problem to today, banks have been reluctant to step forward and testify, as evident from their absence from any of the hearings and forums

on the issue. In truth, at no point during this ongoing situation have any of these banks come forward to either defend their position, or work with us towards a solution.

As we have previously proposed, because of the deep seated bias that now exists a legislative approach may be required. We must mandate that financial institutions may not discriminate against check cashers solely on the basis of their status as MSBs, or due to alleged "reputation risks." Additionally, legislation should impose a requirement that a bank may only terminate an MSB customer for cause.

Alternatively, there must be a paring down of the regulatory burden on banks servicing the MSB industry. What is needed is legislation which gives force to the policy in the MSB Guidance that banks "will not be held responsible for their customers' compliance with the Bank Secrecy Act" or other regulations. Banks should be relieved of the burden of reviewing the compliance programs of their licensed and registered check casher customers. MSBs are already subjected to several levels of oversight by IRS and, in many cases, their state regulator. Banks should not be required to conduct their own redundant and costly review and monitoring of customer BSA compliance programs.

As suggested by prominent banking industry representatives, a more reasonable alternative would be a cross-industry practice whereby the MSB would provide primary compliance information (i.e., state license and MSB registration) to its bank, together with a certified statement by the MSB to the effect that the MSB does maintain appropriate BSA policies, procedures and controls. This self-certification, together with existing regulatory oversight by IRS and state regulators, should expressly relieve the bank of further due diligence obligations. FiSCA supports a certification process. We

agree that the MSB customer must take responsibility for its compliance obligations, and must be able to certify to its depository that it maintains appropriate controls. We are in accord that banks should be relieved of this burden, including the attendant costs and regulatory exposure.

Both the banking and MSB industry have also suggested legislation that would limit enforcement actions against banks that service MSBs in good faith. Although regulators express a reluctance to grant any form of "safe harbor," there is little question but that administrative enforcement actions against banks have had a chilling effect on access to depository services to the MSB industry. In one notable example, a multi-million dollar penalty was assessed against a Florida bank due to the bank's internal BSA deficiencies. Although the bank also served many check cashers, none were implicated in connection with the bank's regulatory violations or internal compliance deficiencies. Nonetheless, the bank responded to FinCEN and FED sanctions by terminating its check cashers, a result clearly not intended by the enforcement action.

In short, banks should not be held responsible for the compliance deficiencies or potential illegal activities of their MSB customers, however rare. Legislation is needed to provide that a bank that services check cashers or other MSBs in good faith will not face administrative enforcement action for the compliance lapses of its customer. Although bank and non-bank financial institutions cannot remain willfully blind to suspicious activity, banks should not be held accountable for the conduct of their check casher customers occurring outside of the depository relationship.

Additionally, there is a need for legislation expressly removing regulated check cashers from the category of "high risk," and imposing a presumption that such

accounts are "low risk." Before 2000, there were few problems between check cashers and the many banks that served them. Check cashers and other MSBs were simply among the numerous commercial customers regularly and profitably served by their depositories. The shift in climate was not the result of a rash of money laundering convictions among check cashers. There is no legitimate nexus between the current trend and money laundering within our industry. To our knowledge, no check casher has ever been implicated in a terrorist financing situation.

Likewise, we are unaware of any situation where a bank has been penalized due to money laundering or BSA violations by its check casher customer. Nonetheless, the tendency among federal bank examiners has been to treat all MSBs as high risk. With respect to the regulated check cashing industry, this presumption is inaccurate and damaging. As compared with other financial sectors, the industry's BSA enforcement record is quite good. Although the FinCEN website lists many multi-million dollar civil penalties against banks and other financial institutions, there have been only a few assessed against check cashers – and only one since 9/11. Moreover, since passage of the USA Patriot Act, IRS has greatly increased the number and scope of Title 31 compliance examinations, yet we have not seen a corresponding increase in BSA enforcement actions within the industry. The record shows that the regulated check cashing industry is not high risk for money laundering, and this fact must be driven home to the bank regulatory agencies that are compelling banks to terminate our accounts. The "high risk" label must be eliminated.

Other solutions to the bank terminations problem have been proposed by various industry leaders. Some have suggested that the current crisis could be alleviated by

granting MSBs direct access to depository accounts at Federal Reserve Banks, placing MSBs on par with credit unions and savings and loans. Others have suggested that a Community Reinvestment Act ("CRA") type process be implemented to determine how well banks are servicing the MSBs in their area, or, alternatively, granting CRA credits to banks that continue to service this industry. FiSCA is fully supportive of both of these concepts.

In sum, the current regulatory regime is not catching more criminals, but is harming scores of legitimate businesses and the customers they serve. Further regulation simply is not the solution. Regulators on all sides agree that bank discontinuance is a problem, but the fact is that there is not a sufficient resolve among the banking agencies to forge an inter-agency regulatory solution. As we have seen, FinCEN's recent attempts to bring relief to the situation have not been successful. Whether due to fear of regulatory reprisal, or indifference, banks are still not coming to the table. We are at a point now that a legislative solution, providing either absolution or compulsion, is the only solution.

We appreciate the opportunity afforded us to testify before you today with respect to this very important issue. We hope that the Subcommittee will consider favorably our recommendations. We remain committed to continuing to work with the Subcommittee and all interested parties in this regard.

Thank you.

Gerald Goldman
General Counsel
Financial Service Centers of America

Gerald Goldman
General Counsel
Financial Service Centers of America

Gerald Goldman has served as General Counsel for the Financial Service Centers of America, Inc. from 1987 to the present. He is also General Counsel for the Check Cashers Association of New York, Inc. (1986 to present) and the New Jersey Check Cashers Association (1979 to present). He is a partner with Winne, Banta, Hetherington & Basralian, P.C. in Hackensack, NJ.

Goldman was appointed by New Jersey Governors Byrne and Cahill to the State Commission on Regulatory Efficiency and the State Law Enforcement Planning Commission from 1973 to 1978. In 1993, he was appointed by the Financial Crimes Enforcement Network (FinCEN), an agency of the US Treasury, to serve as a member of the Bank Secrecy Act Advisory Committee for eight years.

Goldman is one of today's foremost authorities on the bank discontinuance issue and its effect on the financial services industry. To this end he testified at the joint meeting of nonbank institutions and examination subcommittees of the Bank Secrecy Act Advisory Group in March, 2005. He also testified on this topic before the US Senate Committee on Banking, Housing and Urban Affairs in April, 2005. He has been a participant in numerous industry panels and discussions and has written extensively on the bank discontinuance problem over the past several years.

In addition to his distinguished career in financial services, Goldman served two terms as the mayor of Passaic, NJ from 1971 to 1978. He received his Bachelor's degree from the University of Vermont (1956) and his J.D. from New York University in 1959.

For Release Upon Delivery
10:00 a.m., June 21, 2006

TESTIMONY OF

ANN F. JAEDICKE

DEPUTY COMPTROLLER

OFFICE OF THE COMPTROLLER OF THE CURRENCY

Before the

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

of the

COMMITTEE ON FINANCIAL SERVICES

UNITED STATES HOUSE OF REPRESENTATIVES

June 21, 2006

Statement required by 12 U.S.C. 250:

The views expressed herein are those of the Office of the Comptroller of the Currency and do not necessarily represent the views of the President.

I. INTRODUCTION

Chairman Bachus, Ranking Member Sanders, and members of the Subcommittee, I appreciate the opportunity to appear before you today to discuss the Bank Secrecy Act's impact on money services businesses (MSBs). My testimony will focus on the nature of the MSB industry, concerns over whether MSBs are losing access to banking services, and the OCC's perspective concerning banks' relationships with MSBs. Over the past two years, the OCC has taken many actions to help ensure that MSBs are not unfairly denied access to a bank account. Those actions, which I will describe in greater detail, include numerous meetings and conferences with representatives of the banking and MSB industries; the issuance of an interagency policy statement, guidance, and examination procedures; and instructions to examiners and training. We very much appreciate your leadership, and that of the Subcommittee, on this vital issue.

Money Services Businesses

"Money services business" is an umbrella term encompassing many different types of financial service providers. MSBs are defined broadly in the Bank Secrecy Act (BSA) regulations to include: (1) currency dealers or exchangers; (2) check cashers; (3) issuers of traveler's checks, money orders or stored value; (4) sellers or redeemers of traveler's checks, money orders or stored value; and (5) money transmitters. A 1997 study by Coopers & Lybrand commissioned by FinCEN, estimated that over 200,000 MSBs were operating in the United States, providing financial services involving approximately $200 billion annually. A majority of the MSB population is made up of agents of the major businesses (*e.g.,* Western Union and MoneyGram) and, in 1997, approximately 40,000 MSBs were outlets of the U.S. Postal Service, which sells

money orders. This 1997 study also estimated that check cashers and money transmitters would grow at a rate of at least 11% per year. The MSB industry is extremely broad and very diverse, ranging from Fortune 500 companies with numerous outlets world-wide, to small independent "mom and pop" convenience stores offering check cashing or other financial services.

As the regulator of national banks, the OCC has long been committed to ensuring that all Americans have fair access to the banking system and financial services, and we recognize the positive role that MSBs play in this process. MSBs provide financial services to individuals who, for a variety of reasons do not have accounts with mainstream banks. MSBs generally offer convenience, neighborhood locations and a variety of financial services that appeal to these customers. Furthermore, some of the products and services offered by MSBs (*e.g.*, foreign remittance services) may not be available at the local neighborhood bank. According to an industry trade group, as many as 40 million Americans do not have mainstream bank accounts and satisfy most of their financial needs using MSBs.

Some MSBs can present a heightened risk of money laundering. The 2005 U.S. Money Laundering Threat Assessment prepared jointly by the Departments of Treasury, Justice, and Homeland Security; the Board of Governors of the Federal Reserve System and the United States Postal Service devotes an entire chapter to MSBs and states that:

> MSBs in the United States are expanding at a rapid rate, often operate without supervision, and transact business with overseas counterparts that are largely unregulated. Moreover, their services are available without the necessity of

> opening an account. As other financial institutions come under greater scrutiny in their implementation of and compliance with BSA requirements, MSBs have become increasingly attractive to financial criminals.

Recent testimony provided by the FBI before this Subcommittee during hearings on the seasoned customer exemption for filing currency transaction reports noted that seventy-three percent of MSB suspicious activity report (SAR) filings involved money laundering or structuring.

State licensing, regulation and oversight of MSBs can also vary greatly between jurisdictions. For example, some states require no licensing, some states license only certain segments of the MSB industry (*e.g.*, check cashers or money transmitters) while other states exercise strong regulatory oversight over all facets of the industry. Furthermore, according to the 2005 Threat Assessment, despite repeated outreach efforts, only a small fraction of the nation's MSBs - approximately 23,000 - have registered with FinCEN as required by Federal law. Many small MSBs are aware of the registration requirement, but they nonetheless may fail to register because of language, culture, cost, and training issues.

Notwithstanding the foregoing, not all MSBs are risky and most MSBs have never been tainted by or associated with money laundering. Some are nationally recognized and respected companies that have strong anti-money laundering (AML) programs and are licensed and supervised, while others are small businesses such as local grocery stores whose products, services and customer base present little to no risk of money laundering. The challenge for all of

us is to ensure that banks recognize these differences and that our supervisory expectations with respect to MSB accounts are clear.

Loss of Access to Banking Services

The OCC is very concerned about the problems that MSBs are experiencing in obtaining banking services. As with any business enterprise, a bank account is essential for the success of an MSB's business. The reasons some MSBs have lost access to banking services are complex and derive from a multitude of factors, including the risks presented by some MSB accounts, the costs and burdens associated with maintaining MSB accounts, and banks' concerns about law enforcement and regulatory scrutiny. Notwithstanding these concerns, there are still a significant number of national banks that continue to provide accounts and banking services to MSBs. In fact, about half of the national banks supervised by the OCC have MSB accounts, including accounts for several large MSBs with nationwide operations.

Given the sheer number and the variety of services offered by MSBs, the differences in risk profiles among MSBs can be profound. For example, a small grocer cashing checks as a convenience to its customers has a much different risk profile than a money remitter that cashes checks and sends wire transfers to customers in high-risk geographies.

The OCC acknowledges that there may not have been clear guidance in the past concerning supervisory expectations of banks that provided financial services to MSBs. However, the Interagency Interpretive Guidance on Providing Services to Money Services Businesses Operating in the United States (Interagency Guidance), issued April 26, 2005, specifically

addressed these issues and provided additional clarity as to: (1) the minimal level of due diligence that should be conducted on low-risk MSBs; (2) the amount of due diligence expected of banks to conduct a risk assessment of their MSB customers; and (3) whether banks are expected to file SARs, close accounts, or take some other action upon discovery that its MSB customer has not complied with Federal or state licensing requirements.

Under the Interagency Guidance, banks must, at a minimum: (1) apply their customer identification program; (2) confirm FinCEN registration, if required; (3) confirm compliance with state or local licensing requirements, if applicable; (4) confirm agent status, if applicable; and (5) conduct basic risk assessment to determine the level of risk associated with the account. If the MSB is categorized as high risk, additional resources must be expended by the bank to ensure that it is fulfilling its obligations under the BSA.

It is easy to see from this process that the costs and resources that must be expended by a bank to open and maintain an MSB account, while complying with its obligations under the BSA, can be substantial. As in all businesses, these additional costs are factored into the pricing of the products offered to MSBs, and certainly some banks have found that the costs are too high or that they are unable to transfer the costs to the MSB customer. Thus, due to market forces, banks may simply decide to close the accounts or discontinue the business relationship.

Banks are also concerned about the reputation risk associated with doing business with MSBs. This may be due, at least in part, to several high-profile criminal cases brought against banks that have relationships with MSBs. In the current environment, banks have become understandably

highly risk-averse and may simply close the accounts of businesses that present more risk than they are willing to tolerate.

The OCC's Perspective Concerning Banks' Relationships with MSBs

To carry out our supervisory responsibilities, the OCC conducts regular examinations of national banks and federal branches and agencies of foreign banks in the United States. These examinations cover all aspects of the institution's operations, including compliance with the BSA, and are conducted using procedures in the Interagency Bank Secrecy Act and Anti-Money Laundering Examination Manual (Interagency Manual). The Interagency Manual was released in June 2005 and was developed in conjunction with the other Federal banking agencies and FinCEN, based on our collective experiences in supervising and examining national banks in the area of BSA compliance. The Interagency Manual includes a section devoted to non-bank financial institutions, which includes MSBs. We continue to work to improve our supervision in this area. We will revise and adjust our procedures to keep pace with industry changes, technological developments, and the increasing sophistication of money launderers and terrorist financers. In this regard, we are presently working closely with FinCEN and the other Federal banking agencies and expect to issue updates to the Interagency Manual shortly.

Over the last eighteen months, the OCC has participated in various forums to better understand MSB issues and to educate the industry and our staff. Moreover, senior OCC officials have met regularly and often with various representatives of the MSB industry to discuss the issues and problems they face in obtaining bank accounts. For example, in March 2005, OCC representatives attended the fact-finding hearing on MSBs hosted by FinCEN; the OCC also

hosted a teleconference for the banking industry in which we discussed a variety of BSA concerns, including MSB issues; and the OCC participated in a nationwide teleconference on MSB issues hosted by the American Bankers Association.

As our knowledge and understanding of MSBs and their issues have continued to grow, our guidance has continued to evolve and develop. On March 30, 2005, the Federal banking agencies and FinCEN issued an Interagency Policy Statement to address our expectations regarding banking institutions' obligations under the BSA for MSBs. This statement specifically states that the BSA does not require, and neither FinCEN nor the Federal banking agencies expect, banking associations to serve as the *de facto* regulator of the MSB industry. It provides that banking organizations that open or maintain accounts for MSBs should apply the requirements of the BSA on a risk-assessed basis, as they do for all customers, taking into account the products and services offered and the individual circumstances. Accordingly, a decision to accept or maintain an account with an MSB should be made by the banking institution's management, under standards and guidelines approved by its board of directors, and should be based on the banking institution's assessment of risks associated with the particular account and its capacity to manage those risks.

As previously discussed, along with FinCEN and the other Federal banking agencies, we issued the Interagency Guidance to further clarify our expectations for banking organizations when providing banking services to MSBs. The guidance sets forth the minimum steps that a bank should take when providing banking services to MSBs, specific steps beyond minimum compliance obligations that should be taken by banking organizations to address higher risks, as

well as due diligence, ongoing account monitoring, and examples of suspicious activity that may occur through MSB accounts. The guidance is intended to provide additional clarity regarding existing anti-money laundering program responsibilities but is not intended to create new requirements or impose additional burdens on banking organizations. The guidance has since been incorporated into the Interagency Manual and FFIEC anti-money laundering training.

National banks appear to be following the Interagency Guidance. We have found that national banks are differentiating between lower risk and higher risk MSB customers and are applying certain due diligence procedures depending on risk in the accounts. As a result, some national banks are choosing to close some MSB accounts while continuing to service other MSB account relationships. We have also found that national banks, in keeping with the guidance, are obtaining from their MSB customers information about the status of required registrations and licenses. Furthermore, although not required by the guidance, some banks are even providing assistance to smaller, less sophisticated MSB customers in understanding the registration and licensing processes, in order to continue to provide services to these customers.

On March 10, 2006, FinCEN issued an Advance Notice of Proposed Rulemaking (ANPR) to solicit additional information concerning MSB access to banking services as well as recommendations regarding the extent to which additional guidance or regulatory action under the Bank Secrecy Act might address these concerns. The comment period will close on this ANPR on July 10th. The OCC will continue to work with FinCEN and the other Federal banking agencies to provide guidance to the banking industry that is clear and consistent, and we

commend the efforts of Director Werner for the leadership he has shown in addressing this important issue.

Finally, on April 24, 2006, the OCC attended, along with the other Federal banking agencies, FinCEN, IRS, the Maryland Office of Financial Regulation, banking and MSB trade groups, an MSB regulatory policy meeting sponsored by the American Bankers Association. The meeting and discussion focused on understanding the challenges facing MSBs and banks in maintaining financial services relationships.

The BSA has been the focus of regulatory, Congressional and media attention for the past few years, and certainly there has been an increasing sense of urgency since 9/11. Clearly, these are very important issues to the banking industry, the OCC and the United States. The intense focus on BSA compliance may have led to misperceptions about the OCC's policies and practices relating to MSB accounts at national banks. To be clear: first and foremost, the OCC does not supervise MSBs and does not expect national banks to be the *de facto* regulators of their MSB customers. Moreover, while we are cognizant of the risks that some MSBs present, and appropriately address those risks through our risk-based supervisory approach, we have not singled out MSBs as a focus of our supervisory efforts.

Second, the OCC, does not, as a matter of policy, require any national bank to close the accounts of an MSB or any other customer (except in the context of administrative enforcement actions, where due process protections apply). The determination of whether to open, close, or maintain

an account is a business decision made by the bank following its own assessment of the risks presented, in accordance with policies and procedures approved by the bank's board.

Third, the OCC does not discourage banks from having MSB accounts, and we expect banking organizations that open and maintain accounts for MSBs to apply the requirements of the BSA, as they do with all accountholders, on a risk-assessed basis. We fully recognize that, depending upon the circumstances of a particular MSB, the risks presented are not the same, and it is essential that banking organizations neither define nor treat all MSBs as posing the same level of risk. Banks need to calibrate the level of due diligence that they apply to MSBs, and it is entirely appropriate to conduct a lower level of diligence for those MSBs that present lower levels of risk.

The OCC has taken steps to ensure that our examiners are acting in conformance with agency policy on this issue. For example, when the Interagency Guidance was issued, we provided copies of it to every national bank examiner with the instruction that it was to be followed immediately and in all cases. As previously discussed, the Interagency Guidance has been incorporated into the Interagency Manual, and the Comptroller has directed that the procedures in the Interagency Manual be used at every BSA/AML examination. We have also trained our examiners extensively on the procedures in the Interagency Manual. Perhaps most significantly, in the past year, senior OCC officials have held nationwide teleconference briefings with the entire national bank examination force, at which they were instructed that, under no circumstances, should they be directing or encouraging banks to close MSB accounts.

Conclusion

Mr. Chairman, the OCC salutes your leadership in this vital area. We also believe that important objectives are achieved when MSBs have access to banking services, consistent with anti-money laundering laws and rules. We stand ready to work with Congress, FinCEN, the other financial institutions regulatory agencies, and the banking industry to achieve these goals.

The National Money Transmitters Association, Inc.

12 Welwyn Road, Suite C
Great Neck, NY 11021
tel (516) 829-2742
fax (516) 706-0203
www.nmta.us

Statement of David Landsman
Executive Director of the National Money Transmitters Association
Before the United States House of Representatives Committee on Financial Services'
Subcommittee on Financial Institutions and Consumer Credit
Hearing Entitled "Bank Secrecy Act's Impact on Money Services Businesses"
June 21, 2006

I am David Landsman, Executive Director of the National Money Transmitters Association. The NMTA was founded in 1999 to voice the concerns of the state-licensed remittance companies (or LRCs) of the United States. Currently, we have 43 member companies, which collectively handle over $17 billion a year in migrant worker remittances.

I would like to thank the Subcommittee on behalf of our members, for allowing me to appear before you today. I would also like to express our gratitude to Congressman Charles Rangel, who has consistently shown his concern for the negative impact these account closings are having on our customers and their families, on the many countries that depend on remittances for their survival, and on the effectiveness of our nation's anti-money laundering (or AML) strategy.

No one knows the exact amount, but we estimate that outbound remittances from the US total at least $60 billion annually. The approximately 620 American LRCs that handle these remittances have never faced more peril than we do today. Banks are crucial to the operation of our business, and they are no longer willing to work with us, citing regulatory concerns.

These regulatory concerns are well-founded, but not because of any real money laundering risk. Banks get into trouble for having us as customers because Federal banking regulators have incorrectly classified all Money Services Businesses (or MSBs) as 'high-risk' and make no distinction within that stereotype between licensed and unlicensed remittance companies. Regulators think that banks must detect potential evil-doers in advance, no matter how much time and expense it requires and, if the bank stumbles at any point along the way, the bank itself deserves condemnation as if it were a direct failure of the bank's own AML program. Although none of the compliance fines we have seen levied against banks involved any LRC, the atmosphere has been supercharged due to the severity of those fines.

Now, these attempts to 'protect' the banking system from the 'risk' LRCs pose have backfired badly by threatening to destroy the best ally law enforcement has in the fight against money laundering. If financial institutions are the 'first line of defense' in our nation's war against terrorist funding, then we LRCs are the Special Forces. No sector of the financial industry has better compliance programs, a cleaner record, or is more central to our nation's AML efforts than LRCs. The average remittance we send is approximately $243, hardly a size conducive to money laundering.

Although regulators say they do not hold banks responsible for our supervision, that is exactly what is happening. Under such conditions, it does not make sense for any bank to keep us as customers, no matter how profitable our accounts are for them.

In her May 8th comment on FinCEN's Advance Notice of Proposed Rulemaking, New York Banking Superintendent Diana Taylor reports that, according to her Department's own survey, 42% of New York LRC banking relationships hang by a thread, and are concentrated at only two banks. If this situation is not remedied, and soon, then the ranks of LRCs all across the country will be decimated. Unscrupulous, unlicensed operators will no doubt fill the void left by our departure.

email: david@nmta.us
cellular: (917) 921-9529

The National Money Transmitters Association, Inc.

12 Welwyn Road, Suite C
Great Neck, NY 11021
tel (516) 829-2742
fax (516) 706-0203
www.nmta.us

Regulators, without legislative guidance, have steadfastly refused to grant any sort of protection that would allow banks to rely on our state licenses. Whose liability should it be then, if 'something' goes wrong with an LRC, the banks'? Why then have licenses at all? No, the truth is it should not be anyone's liability, except the MSB's. It is exactly this type of 'guilt-by-association' thinking that has caused the situation we face today: too much due diligence responsibility imposed on the banks, and drastic consequences to the banks for any failure, no matter how technical. Regulation is the job of government, and cannot and should not be delegated to banks.

In order to solve this problem, we recommend the following steps:

1. Remove the onus of supervising us from the banks' shoulders, by law, as soon as possible. This may be done by officially recognizing some or all state licenses, defining *all* measures a bank is expected to take when opening our accounts, and making those measures practicable. Banks would still have to verify our licenses and remain alert for red flags, as usual. The LRC may be required to sign a self-certification form similar to the one used in foreign correspondent banking relationships.

2. Start regulating LRCs at the federal level with a voluntary, non-preemptive federal AML certification that would involve initial application and vetting, published rules and standards that must be followed to maintain certification, and regular examinations and reports. The current regulation of MSBs we have at the federal level is not good enough. Create an MSB supervision department at FinCEN and end the unfortunate division of AML responsibilities that currently exists between FinCEN and the IRS. Let the MSB registration program gradually be replaced by something more meaningful that would give those firms that so desire, a pathway to the credentials that it takes to get bank accounts. Regulate the agent population through us licensees, rather than trying to herd over 200,000 retail locations, most of which are mom and pop shops.

3. Our industry needs to take the first steps toward self-regulation. This would involve industry-driven training, standards-setting, certification and disciplinary procedures. While this is something that we ourselves need to do, government can help by encouraging LRCs to join together.

I thank the Subcommittee once again for the opportunity to have our opinions heard.

email: david@nmta.us
cellular: (917) 921-9529

WRITTEN TESTIMONY OF
EILEEN C. MAYER
DIRECTOR OF FRAUD/BANK SECRECY ACT
INTERNAL REVENUE SERVICE
BEFORE
HOUSE COMMITTEE ON FINANCIAL SERVICES' SUBCOMMITTEE ON FINANCIAL INSTITUTIONS AND CONSUMER CREDIT
ON
MONEY SERVICE BUSINESSES
JUNE 21, 2006

Good morning Chairman Bachus, ranking Member Sanders, and members of the Subcommittee on Financial Institutions and Consumer Credit. My name is Eileen Mayer and I am the Director of Fraud/Bank Secrecy Act (BSA) within the Small Business/Self Employed (SB/SE) division of the Internal Revenue Service (IRS). My office is assigned the responsibility to fulfill IRS' obligations under the Bank Secrecy Act as well as coordinating the establishment of Service-wide fraud strategies, policies, and procedures. My office also provides fraud referral coordination for all operating divisions of the IRS.

IRS' role in administering the BSA is derived from statutory authority given to the Secretary of the Treasury to administer the provisions of the Act. He in turn delegated that authority to the Director of the Financial Crimes Enforcement Network (FinCEN). FinCEN retained some authorities but delegated others. Specifically, the IRS was delegated the authority to examine, for BSA compliance, all financial institutions not currently examined by a Federal functional regulator. These entities include money service businesses (MSBs), such as check cashers, issuers of traveler's checks, and money transmitters, casinos, certain credit unions that are not otherwise regulated by the Federal Government, dealers in jewelry and precious metals and insurance companies.

Emphasis on Customer Service

Under the leadership of Commissioner Everson, the IRS has taken a balanced approach to tax compliance, one that emphasizes service as well as enforcement. Many MSBs are small businesses and in some cases sole proprietorships. As a result, they may not fully understand their responsibilities under the BSA.

An important part of fulfilling our responsibilities under the BSA is to work closely with our office of Communications, Liaison and Disclosure (CLD) to identify those areas where education and outreach efforts can be most productive. We also have BSA outreach specialists located in the six top high risk money laundering and related financial crime areas – Miami, New York, Chicago, Houston, San Francisco, and Los Angeles.

In addition, we are also revising our BSA Internal Revenue Manual and once it is finalized we will make that available to all MSBs – including posting it on the internet so that it is readily available to everyone. We plan to convert the manual to a more user friendly format similar to the manual created by the Federal Financial Institutions Examination Council.

Coordination with Other Groups

In our efforts to assure compliance with the provisions of the BSA, we have been pleased to partner with the other groups represented at the table today. While each of the groups has distinct responsibilities relative to the BSA, we all must work cooperatively to be most effective in monitoring and preventing questionable transactions. As evidence of that cooperation, Commissioner Everson was pleased to announce in late April that we had reached agreements with 33 states and Puerto Rico to begin sharing BSA information. The agreements will allow the IRS and the participating states to share information and leverage their resources to ensure that MSBs are complying with their federal and state responsibilities to register with the government, to create and maintain anti-money laundering programs and to report cash transactions and suspicious activities. This would have not been possible without the support and assistance of the Conference of State Bank Supervisors (CSBS)

In addition, we have a very close working relationship with FinCEN. We have a memorandum of understanding in place which provides for exchanges of information to help FinCEN fulfill its role as administrator of the BSA and to assist us in conducting examinations of MSBs to assess BSA compliance. IRS and FinCEN work closely on such things as setting examination priorities, review of the BSA Internal Revenue Manual, and training. As I will discuss in more detail later, we also refer all potential BSA civil penalty cases to FinCEN for appropriate action.

IRS Enforcement

In recent years, the IRS has strengthened the focus on enforcement, while maintaining appropriate service to taxpayers. Detecting and investigating money laundering activity is an important part of tax compliance for the IRS. In addition, the failure to file forms required by the BSA and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, often have a direct link to tax evasion and money laundering. In some cases, because the schemes are sophisticated and because we may not be able to obtain evidence from some foreign countries, it is almost impossible to conduct traditional tax investigations. In these circumstances, money-laundering violations frequently are the only possible means to detect tax evaders.

Money laundering not only is used by domestic and international criminal enterprises to conceal the illegal, untaxed proceeds of narcotics trafficking, arms trafficking, extortion, public corruption, terrorist financing, and other criminal activities; it is also an essential element of many tax evasion schemes. With the globalization of the world economy and financial systems, many tax evaders exploit domestic and

international funds transfer methods to hide untaxed income. These schemes often involve the same methods to hide money from illegal sources and to hide unreported income. Both activities generally use nominees, wire transfers, multiple bank accounts, and international "tax havens" to avoid detection.

Money laundering is the financial side of virtually all crime for profit. To enjoy the fruits of their crime, criminals must find a way to insert the illicit proceeds of that activity into the stream of legitimate commerce in order to provide the resources necessary for criminal organizations to conduct their ongoing affairs.

IRS' Role in BSA Compliance

As part of its core tax administration mission, the IRS addresses both the civil and criminal aspects of money laundering. On the civil side, the Department of the Treasury, through FinCEN, has delegated to the IRS responsibility for ensuring compliance with the BSA for all non-banking financial institutions not otherwise subject to examination by another federal functional regulator, including MSBs.

Under this FinCEN delegation, the IRS is responsible for three elements of compliance: – (i) the identification of MSBs, (ii) educational outreach to all these types of organizations, and (iii) the examination of those entities for compliance.

Currently, there are over 24,000 MSBs registered and posted on the FinCEN website. However because the true universe of potential MSBs is unknown, we utilize several methods to identify unregistered MSBs. One method is to utilize information from the states that identifies businesses that are registered at the state level but not with FinCEN. We also review our Currency Banking and Retrieval System (CBRS) data base to discover suspicious activity reports (SARs) or currency transaction reports (CTRs) that emanate from entities that should be registered. We also get leads from other Federal agencies such as Immigration and Customs Enforcement. Finally, we receive anecdotal reports on entities that are not registered but who are doing check cashing or other financial activities that would subject them to registration requirements

Through these various means, we have identified more than 2,000 cases of businesses not registering as required under the BSA and we will be pushing these cases to the field shortly.

Our outreach program is designed to reach both registered and unregistered MSBs. We focus special attention on those industries where FinCEN has issued a threat alert. For example, currently we are working with the convenience stores owners and gasoline retailers, many of whom are MSBs and may not even realize it. We work closely with the trade associations that represent specific MSBs making sure they understand the requirements that their members face. We also make ourselves available for seminars at association events and as exhibitors at their trade shows. We also look at industries where we suspect that there may be high incidences of non-registration and work closely with them to make sure they understand the registration requirements.

From a criminal perspective, IRS' Criminal Investigation (CI) Division is responsible for the criminal enforcement of BSA violations and money laundering statutes related to tax crimes. CI uses the BSA and money laundering statutes to detect, investigate, and prosecute criminal conduct related to tax administration, such as abusive schemes, offshore tax evasion, and corporate fraud. CI also investigates the non-filing of BSA forms and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, which frequently have a direct link to both tax evasion and money laundering.

The IRS CI Division has increased its emphasis on BSA responsibilities significantly, with particular focus on improving the effectiveness and efficiency of Suspicious Activity Report (SAR) Review Teams. CI now hosts approximately 80 SAR Review Teams located throughout its 30 Criminal Investigation field offices. These teams are made up of federal, state and local law enforcement officials and work closely with Assistant United States Attorneys. The expansion in the number of teams improves analysis of SARs because each team can focus on the geographical area with which it is most familiar. Increased use of technology, primarily data-mining tools, is assisting teams in efficiency analyzing the ever increasing number of SARs being filed.

MSB Compliance

The BSA imposes several requirements on money service businesses. These include:

- The development and implementation of an adequate Bank Secrecy Act or Anti-Money Laundering (AML) program. An effective program is one that is reasonably designed to prevent the money service business from being used to facilitate money laundering and the financing of terrorist activities. Such a plan must include the following elements: (a) a system of internal controls to assure compliance; (b) the designation of an individual responsible for coordinating and monitoring day-to-day compliance; (c) the provision of training for appropriate personnel; and (d) the provision for independent review to monitor and maintain an adequate program.

- A requirement that MSBs file a report of each deposit, withdrawal, exchange of currency or other payments or transfer which involves a transaction of currency of more than $10,000; and

- A requirement that "suspicious transactions" be reported. The BSA and its implementing regulations have defined what might be classified as a suspicious transaction. They include such things as transactions that involve funds gained from illegal activities or designed to evade reporting or recordkeeping requirements under the BSA, or transactions in which the particular customer would normally not engage.

IRS Examinations

It is important to point out that all of our BSA examiners and their managers devote 100 percent of their examination time to examinations of BSA-related cases. This contrasts with our efforts in 2004 and before when BSA work was a collateral duty of revenue agents who were engaged in traditional income tax audits.

In choosing which MSBs to examine, we are utilizing a centralized case selection process. The Treasury Inspector General for Tax Administration (TIGTA) has previously scrutinized our work selection process observing that current processes create a significant risk of undetected non-compliance and inconsistent program delivery. As a result we are developing a systematic, risk-based inventory selection process. This process is based on a scoring system that uses data from the Currency and Banking Retrieval System (CBRS) to identify the best candidates for examination. We are currently field testing that scoring system.

Once we identify a particular MSB for examination, our first step is to request from the entity a copy of its anti-money laundering compliance program and a copy of the independent audit of the compliance program. The examiner will then prepare a risk based assessment that essentially determines the scope of the rest of the examination.

During the course of the exam, the examiner will identify the entity's AML risks, evaluate policies, procedures, and internal controls and assess whether breakdowns in the AML compliance program place the institution at risk for money laundering. We will then perform selective transactional testing.

Upon completion of the examination one of four outcomes will occur. First, if no violations are found, we will issue what we call Letter 4029 which gives the entity documentation that a review has occurred and that no violations were identified. This is important because we are well aware that many MSBs are facing increasing difficulty in finding banks willing to do business with them. These banks, both large and small, seem to believe that opening new or maintaining existing accounts for money service businesses will be too costly, pose a potential threat to their reputation, or expose them to greater regulatory scrutiny.

This is regrettable. The money services business industry provides valuable financial services, especially to individuals who may not have ready access to the formal banking sector. 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 money services businesses that comply with the requirements of the Bank Secrecy Act and applicable state laws remain within the formal financial sector, subject to appropriate anti-money laundering controls.

It is equally important to ensure that the money services business industry maintains the same level of transparency, including the implementation of a full range of anti-money laundering controls required by law, as do other financial institutions. If account relationships are terminated on a wide-spread basis, we believe many of these businesses could go "underground." This potential loss of transparency would significantly damage

our collective efforts to protect the U.S. financial system from money laundering and other financial crime – including terrorist financing.

The second possible outcome of an examination would be the issuance of a Letter 1112 (L-1112). The L-1112 would be issued if violations are found, but they are technical, minor, infrequent, isolated, and non-substantive. This letter will detail the violations and ask that the entity commit to correct the apparent violations. It also provides the business with the opportunity to disagree with the findings and to provide us within 30 days, an explanation of any disagreement.

It is important to realize that the issuance of an L-1112 involves no fines or other penalties on the MSB. It merely says that we have found these violations and by signing the letter, the business agrees to correct the deficiencies that were noted.

The third potential outcome of an examination is an instance where a significant BSA violation or deficiency is identified. In this instance, the case is referred to FinCEN for consideration of civil penalties. Examples of this would be if the violation was flagrant, demonstrated bad faith or was committed with disregard for the law or the consequences to the institution. Other factors in considering whether to refer a matter to FinCEN include: (a) the frequency of the violation; (b) whether the violation is intentionally concealed; (c) whether the business fails to cooperate in correcting the violation; and, (d) the history of prior violations and/or poor compliance. Field examiners are given a clear list of criteria to consider in determining whether to refer a case to FinCEN.

Once a case is referred to FinCEN, the IRS is no longer involved. FinCEN will make the determination of what, if any civil penalty is appropriate.

Finally, if the examiner believes that there may be a willful criminal violation involved, the case would immediately be referred to IRS-Criminal Investigations when the relevant facts have been developed. CI will evaluate the case and determine whether the case reaches the level of criminal behavior and meets certain minimum case selection criteria. From a legal perspective, one of the most difficult issues facing CI in deciding if a case is worthy of a criminal investigation is documenting sufficient evidence of affirmative acts to establish willfulness. Willfulness can be difficult to prove and when dealing with the Bank Secrecy Act violations it often requires documenting a subject's knowledge of their obligations under the BSA.

From a practical perspective, case selection is another key factor in determining whether a case will be successfully prosecuted. Our CI division has vast experience in determining the prosecution potential of cases selected for investigation, evidenced by a 96.3% acceptance rate at the Department of Justice and 92.2% acceptance rate at the United States Attorneys Offices for Fiscal Year 2005.

If CI makes the determination that they will not refer the case to the Department of Justice for review, it comes back to us and we decide whether to then refer it to FinCEN for consideration of possible civil penalties.

If an MSB believes that an examiner has made a mistake in his or her assessment of potential violations, there is recourse. As noted above, if the MSB is issued an L-1112 letter, it has 30 days in which to respond explaining why the examiner is wrong. The MSB can also elevate the issue to the BSA Territory Manager or contact FinCEN through their hot line number posted on their website.

To give you an idea of the universe of cases we audit, in FY 2005, we examined 3,680 MSBs. We issued L-1112 violation letters to 1,337 of these. We referred 21 cases for criminal investigation and referred 7 cases to FinCEN.

As of May 26 of this fiscal year, we have examined 3,668 MSBs and issued violation letters to 2,414 entities. We have also issued 1241 Letters 4029, indicating clean examinations. We have referred 10 cases to CI and 3 cases to FinCEN.

One of the questions raised by the subcommittee's staff prior to this hearing was whether our field examiners ever provide feedback to the principal when we complete the exam of an MSB agent. We do not. We have discussed this issue with FinCEN and the problem comes down to the possibility of making unauthorized disclosures. The fact is that many MSBs offer multiple services as agents for more than one principal. For example, an MSB might issue both American Express and Visa traveler's checks. Or, the MSB may transmit money as an agent of Western Union and also sell money orders as an agent of MoneyGram. By informing one principal of violations, we may be making an unauthorized disclosure involving other principals. Therefore, FinCEN has required that we not provide any feedback to an agent's principal(s).

Conclusion

As I stated earlier in this testimony, the fight against money laundering and terrorist financing are top priorities for the Internal Revenue Service. We are prepared to increase our commitment to the BSA Program, and we will continue to coordinate our efforts closely with FinCEN and the other groups represented here this morning.

We will also not forget the importance of assisting MSBs whenever possible in understanding and complying with their responsibilities under the BSA. As Commissioner Everson has said often, service plus enforcement equals compliance.

Mr. Chairman, I thank you for this opportunity to appear before you this morning and will be happy to respond to any questions that you or members of the Subcommittee may have.

TESTIMONY
BY

PHILIP W. MILNE, PRESIDENT AND CEO,
MONEYGRAM INTERNATIONAL, INC.

BEFORE THE UNITED STATES HOUSE OF REPRESENTATIVES
FINANCIAL SERVICES SUBCOMMITTEE ON
FINANCIAL INSTITUTIONS AND CONSUMER CREDIT

HEARING ON
BANK SECRECY ACT'S IMPACT ON MONEY SERVICES BUSINESSES

JUNE 21, 2006

Good morning Mr. Chairman and members of the Committee. My name is Phil Milne, and I am the President and CEO of MoneyGram International. I am pleased to have the opportunity today, on behalf of MoneyGram, to speak with the Committee about the ongoing bank discontinuance problem for Money Services Businesses[1] (MSBs), and to offer a few suggestions that MoneyGram believes could improve the situation, as well as enhance overall anti-money laundering compliance by MSBs. The bank discontinuance problem is not one that will go away on its own. It must be resolved by the federal banking regulators by removing the onus they have put on banks, either directly or impliedly, that the banks perform due diligence analysis on the compliance programs of their MSB account holders. I should also mention that I'm joined today by Tom Haider, MoneyGram's Chief Compliance Officer and Vice President of Government Affairs, who can assist in answering any of your questions.

Company Background

MoneyGram is an international payment services company conducting business in more than 170 countries and territories, through more than 92,000 locations. The locations that sell MoneyGram's services, commonly referred to as "agents," include banks, credit unions, supermarkets, convenience stores, and other retail locations. MoneyGram's services are sold through such well-known businesses as Wal-Mart, Albertson's, CVS Pharmacy, US Bank, and many small, independently owned "mom and pop" convenience stores. In the US, MoneyGram is licensed and regulated as a money transmitter by the majority of states, typically through the respective state's banking department. In addition, MoneyGram fully complies with the Bank Secrecy Act, the USA PATRIOT Act, and is registered with the Treasury Department as an MSB. MoneyGram is also a member of the Money Services Round Table, which is a coalition of the leading money transmitters in the US and whose other members include: American Express Travel Services, Western Union, Comdata Network, Travelex Americas, Sigue Corporation, and Ria Financial Services.

[1] Money Services Businesses "MSBs" are defined in 31CFR103.11uu, and include money transmitters, money order issuers and sellers, check cashers, travelers check issuers and sellers, and stored value providers.

As we discuss the bank discontinuance problem, it is important to keep in mind that it is not a stand alone issue. It is part and parcel tied to anti-money laundering compliance and the challenges faced by the MSB industry in complying with the federal anti-money laundering laws, as well as the variety of interpretations of those laws by the state banking departments that regulate the industry. By fixing the bank discontinuance problem, federal regulators will also help improve overall compliance by the MSB industry. We are dedicated to continuing our partnership with law enforcement in the fight against money laundering and terrorist financing, but we need banking services and we need the federal government's help to ensure continued access to banks by the MSB industry.

Bank Account Concerns

Now I would like to address in greater detail the bank discontinuance issue, which is continuing to cause serious problems for many MSBs, including MoneyGram and its agents. The problem is one in which banks are either closing the accounts of existing MSBs, or refusing to open new accounts for them. The businesses are being told by banks, some of which they have had relationships with for years, that the business must choose between closing their account or ceasing to offer any kind of MSB services. When they ask their bankers "why?" they are frequently told that the bank's regulator considers MSBs to be high-risk and the regulator advises the bank to avoid doing business with such entities.

At MoneyGram, we have heard from dozens of agents that this situation is forcing them to consider stop serving as an agent. The agents who sell MoneyGram's money orders and money transfers do so mainly as a means of generating foot-traffic in their stores. The small amount of revenue that money order and money transfer sales generate for the agents simply does not justify the risk of losing their bank accounts.

Initially, the "mom and pop" stores and check casher locations were the MoneyGram agents that experienced the majority of the banking relationship problems. However, this problem is no longer limited to small businesses. Two months ago Bank

of America informed MoneyGram that it would be terminating its long-term relationship with MoneyGram. This was not just a simple deposit account, but rather a global banking relationship that generated millions of dollars in fees annually for Bank of America.

While Bank of America is only one of many banks with which MoneyGram conducts business, its decision to terminate our account relationship was a serious issue. That is because Bank of America, with its global footprint, had become the leading bank that MoneyGram was using to develop new master/sub-account relationships to address its agents' banking problems. Furthermore, Bank of America was an important partner for MoneyGram's international banking needs. But Bank of America is not alone in exiting the MSB industry. As noted in the American Banker on Monday, June 12, 2006, many other banks have also chosen to discontinue or curtail providing account services to certain MSBs, including Bank of New York, HSBC, KeyCorp, PNC, SunTrust and Chase. One point that is often overlooked is the number of entities that qualify as MSBs. It includes nearly every major grocery and convenience store chain in the country because they are leading sellers of money orders and money transfers. So, if the bank discontinuance problem continues, it could seriously damage the banking relationships of large corporations, or it could force a significant part of the distribution network for money orders and money transfers to exit the market.

Fortunately for MoneyGram and the MSB industry, FinCEN has continued to focus on the bank discontinuance problem and attempted to find a solution that would work for banks and MSBs. Last year, FinCEN took the lead on this issue by holding an informational meeting for interested parties. Then, FinCEN joined the Federal Banking Agencies in developing Interagency Interpretive Guidance on Providing Banking Services to MSBs, known as the "Guidance," which was issued on April 26, 2005. We now know the Guidance did not work as intended by the regulators. So, once again FinCEN has stepped forward and issued an Advanced Notice of Proposed Rulemaking on March 10, 2006, to solicit comments on the problem and to request suggestions for improvement. We appreciate FinCEN once more taking leadership in trying to resolve

this issue. MoneyGram, and more than 65 other MSBs, banks and trade associations have submitted comments to FinCEN. MoneyGram's principal suggestion, and the one that most other comments echoed, is that the existing Guidance is not working and needs to be replaced. MoneyGram has encouraged the federal regulators to replace the Guidance with a new version that eliminates the banking community's obligation to conduct due diligence reviews of MSBs' compliance programs.

In the meantime, in order to help our agents, MoneyGram has been negotiating with several banks to offer special accounts that consist of a master MoneyGram account with sub-accounts for the agents, but this is far from an ideal solution. It is very expensive for MoneyGram to maintain such accounts and it is difficult for our agents. In some cases, agents have not been able to use this arrangement because they cannot afford to be away from their store for the length of time it takes them to travel to new banks that are located much farther away than their old bank that was in their neighborhood. In order to retain some agents, MoneyGram is now paying for armored car service to collect the funds from these agents, which adds even more costs to conducting the business. These added costs present a difficult challenge to MoneyGram as we strive to maintain our value proposition to our customers in a rising cost environment. Too often that is a key point that gets lost in all of the discussion regarding banking relationships and compliance requirements. We simply forget that all of these issues cost money and, in turn, lead to higher costs for consumers.

Reasons for Bank Discontinuance

So, what is driving this exodus by the banks from the MSB industry? We believe it is the banks' fear of their own regulators. MoneyGram sympathizes with the regulatory pressure that banks are under. MoneyGram faces similar pressure from its own regulators, the state banking departments, which are interpreting and enforcing federal anti-money laundering laws.

Unfortunately, the Guidance issued by the federal banking regulators in April 2005 only heightened the bank discontinuance problem, because instead of reducing

banks' concerns, it actually increased their fears that they are responsible for policing the anti-money laundering compliance programs of their MSB account holders. The Guidance placed so much emphasis on the due diligence banks are to conduct on their MSB account holders that more of them stopped serving MSBs. Those banks decided the effort and risk exceeded the benefit from providing account services. From an anecdotal standpoint, the most glaring example of this worsening effect is demonstrated by the fact that there are no reports of banks, which previously terminated their relationships with MSBs, reversing course and re-establishing accounts for MSBs based on the new Guidance.

One of the most troubling aspects of the Guidance is that it makes no distinction between an MSB that serves as an agent versus an MSB like MoneyGram that engages exclusively in MSB services. The scope of compliance programs between such entities is naturally quite different. A "full service" MSB, like MoneyGram, should have a risk based compliance program, but agents need more objective criteria. As noted earlier, the majority of MoneyGram's agents are "mom and pop" convenience stores for which the sale of money orders and money transfers is just a small part of their business. They do a good job with the Bank Secrecy Act's quantifiable recordkeeping and reporting requirements, but asking them to develop their own, risk based compliance program is extreme and defeats the ultimate goal of having them detect suspicious activity.

In order to assist its agents with their compliance obligations, MoneyGram provides them with written anti-money laundering training tools in eight different languages. In addition, MoneyGram has anti-money laundering specialists who visit select agents to provide updated compliance training. Furthermore, all MoneyGram transactions are ultimately reviewed by MoneyGram's in-house compliance team. Thus, our agents are looking for suspicious activity that may occur at their store counter, while MoneyGram is searching for the criminal who structures his transactions to avoid detection by conducting smaller transactions through multiple locations. Therefore, the use of objective, non-risk based criteria by agents does not weaken their compliance effort because their transactions are also reviewed by MoneyGram.

Recommendations

MoneyGram appreciates the opportunity to offer the Committee a few suggestions on how the bank discontinuance issue might be resolved, as well as suggestions on how compliance with anti-money laundering laws and regulations by MSBs might be improved. The two issues are linked, since improving anti-money laundering compliance should help banks and their regulators gain confidence in the MSB industry. With regard to the bank discontinuance issue, MoneyGram believes the biggest part of the problem is the Guidance that was issued in April 2005. It simply added confusion to the issue and caused greater consternation among banks. MoneyGram is therefore offering four straightforward suggestions to help correct the bank discontinuance problem and at the same time improve overall anti-money laundering compliance by MSBs. Those suggestions are as follows:

First, the federal banking agencies must rescind the existing Guidance and issue new Guidance. The current Guidance is flawed and patchwork amendments will only make the problem worse. New Guidance must make it absolutely clear that banks are not required to evaluate the quality of a MSBs' compliance program, nor are they expected to monitor the activities of a MSBs' customers. Instead, Guidance should enable banks to rely on their MSB account holders certification that: (1) they have a written anti-money laundering compliance program that addresses the requirements of the Bank Secrecy Act, and which contains a significant employee training component that includes the detection of suspicious activity and structuring; (2) they or their principal is licensed by the appropriate state regulator; and, (3) they or their principal is registered with FinCEN. Likewise, the bank should be free to request additional, general information about the MSB, such as the type of services provided and volume of transactions, in order to gain greater knowledge of the entity to determine whether its banking activity is appropriate for the business. MoneyGram, along with its fellow members of the Money Services Round Table, is pleased to offer a draft of new Guidance, which embodies these concepts, for consideration by the Federal Banking Regulators and FinCEN. (See attached Exhibit A.)

Second, some kind of incentive should be provided for banks to resume serving the MSB industry. One suggestion is to provide banks with Community Reinvestment Act credit for opening and maintaining accounts by MSBs. Without some type of incentive, the MSB industry is not confident that banks will voluntarily re-enter the market and begin offering account services to MSBs. In particular, the "mom and pop" shops that lost their bank accounts do not likely represent such an attractive opportunity that many banks will reverse their position on offering them accounts. Other incentives might also be effective, but there must be something to entice banks to re-establish accounts for MSBs.

Third, consistent enforcement of the anti-money laundering laws as they apply to MSBs is needed. MoneyGram is well aware of the recent efforts by FinCEN and the IRS to enter into Memoranda of Understanding (MOUs) with the states for the sharing of anti-money laundering information. MoneyGram supports those efforts and recognizes their importance in the fight against money laundering and terrorist financing. However, at the same time many states have been interpreting the federal anti-money laundering laws in their own way, sometimes inconsistently with each other, as well as inconsistently with the intentions of federal regulators. This variety of interpretations has only caused confusion for the MSB industry and adversely impacted the industry's efforts to develop standardized compliance programs for themselves and their agents. As an initial step in providing consistent enforcement, MoneyGram is requesting that the Treasury Department and FinCEN establish their preemptive authority to interpret and enforce the Bank Secrecy Act, and related federal anti-money laundering laws and regulations. This will help provide the consistency that is needed for anti-money laundering compliance by MSBs.

An important offshoot of this suggestion is the need to create a system that can provide a consistent regulatory framework for the MSB industry. Towards that goal, MoneyGram is proposing an optional federal licensing regime for certain segments of the MSB industry that would enhance compliance with anti-money laundering laws and close

any regulatory loopholes that criminals may try to exploit in those states that do not regulate all MSBs within their borders. Such a regime would be available to entities that operate in multiple jurisdictions, and be mandatory for any entities that operate in states that do not license their activity.

One of the reasons that some banks are not comfortable serving MSBs is that banks are unable to determine what laws the MSBs should be following due to the wide variety of state requirements. A federal license would bring greater consistency to MSBs' compliance programs and would help the bank community gain a higher degree of confidence in the regulatory oversight applied to the MSB industry. Furthermore, just as various regulators and law enforcement officials have expressed concern that the ongoing bank discontinuance problem poses a serious threat that some aspects of the MSB industry will be driven underground, there is also a threat that criminals will operate underground in those states that either do not license MSBs or which only regulate a portion of the industry.

Fourth, standards for MSBs as to what constitutes an effective anti-money laundering compliance program must be established. We understand that FinCEN is working with the Internal Revenue Service (IRS) on an examination manual that IRS staff will use when analyzing MSBs' compliance programs. We applaud these efforts, and MoneyGram, and the other members of the Money Services Round Table, are ready and willing to lend FinCEN and the IRS their full support to help with this effort. The absence of such a manual or set of standards has left the MSB industry with no clear direction on what measures to take in order to establish an effective compliance program. As previously noted, that challenge is made even more difficult due to the variety of interpretations of the federal money laundering laws by the state banking departments that are charged with regulating the MSB industry for safety and soundness.

What can Congress do?

MoneyGram appreciates Congress holding a hearing on this very important issue. Last year, the Senate Banking Committee held a similar hearing and we were very encouraged at that time that legislative interest, combined with the Guidance issued by the Federal Banking Agencies, would solve the bank discontinuance problem. We know now that it wasn't. But it was not due to lack of effort. Many members of this body, and many regulators, worked hard to come up with a solution that would work for all interested parties. This time, though, we must get it right.

MoneyGram recognizes that Congress can not solve the problem by ordering banks to serve MSBs. But we do believe that, through its oversight and budget authority, Congress can compel the federal regulators to take appropriate action. MoneyGram requests that Congress continue to monitor the bank discontinuance problem and that Congress hold federal regulators accountable for implementing a workable solution by the end of the year.

Conclusion

In conclusion, I want to thank you, Mr. Chairman and members of the Committee, for the honor of having the opportunity to present testimony on behalf of MoneyGram International. We truly appreciate your continued interest in this issue, Mr. Chairman, which we believe will help ensure a successful resolution to the bank discontinuance problem and long-term improvement in the MSB industry's compliance programs. We at MoneyGram are proud of our company's strong efforts in the fight against money laundering and terrorist financing, and we remain dedicated to working with Congress, regulators and law enforcement officials to defeat the attempts by criminals to use any of our services for illegal purposes. Mr. Chairman, we hope that you will view us as a partner in this effort and will call upon us for whatever assistance we can provide. Thank you again.

EXHIBIT A

Revised Interagency Interpretive Guidance on Providing Banking Services to Money Services Businesses Operating in the United States

On April 25, 2005, the Financial Crimes Enforcement Network ("FinCEN"), along with the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, the National Credit Union Administration, Office of the Controller of the Currency and Office of Thrift Supervision ("Federal Banking Agencies") issued interpretative guidance to clarify further the requirements of the Bank Secrecy Act and its implementing regulations (including the parallel provisions issued by the Federal Banking Agencies) to banks when providing account services to Money Services Businesses ("MSBs") operating in the United States.

The goal of the prior interpretive release was to confirm "that banking organizations have the flexibility to provide services to a wide range of money services businesses while remaining in compliance with the Bank Secrecy Act." In short, banks were told that they "will not be held responsible for their customer's compliance with the BSA and other federal and state laws and regulations."

Notwithstanding the intent of FinCEN and the Federal Banking Agencies, there is significant evidence both anecdotal and documented in submissions to FinCEN in response to the Advance Notice of Proposed Rulemaking, that the April 26, 2005 Interagency Interpretive Guidance did not have the desired result of easing bank concerns with regard to the level of scrutiny and responsibility imposed on a bank in opening or maintaining an account for an MSB. In fact, there is some indication that the articulation of "due diligence for high risk customers" set forth in the interpretive guidance was read by some regulators and banks as constituting the imposition of more stringent obligations on banks with regard to MSB customers. As a result of this apparent confusion since the issuance of the Interagency Interpretive Guidance more than a year ago, both national and regional banks have canceled accounts of MSBs at an accelerated rate. The cancellations have occurred nationwide and threaten the viability of the MSB industry.

Clearly, it was not the intent of FinCEN and the Federal Banking Agencies to hasten the closure of MSB bank accounts. As emphasized in numerous public releases of the Treasury Department, MSBs provide essential financial services to the public and the widespread discontinuance of the availability of these services inevitably will lead to the migration of funds to the underground. Such a prospect is contrary to the national interest and undercuts government efforts to curb terrorist financing and stem money laundering.

Since the Interagency Interpretive Guidance has not had had the desired effect, FinCEN and the Federal Banking Agencies are issuing this further interpretive clarification designed to provide clear guidance to banks, MSBs and the banking regulators that **banks need not undertake special compliance procedures with regard to MSB accounts**.

Therefore, in case there is any doubt from the prior guidance, banks should take the following steps with regard to MSB accounts:

1. NEW MSB ACCOUNTS -- Banks should perform the following due diligence when opening new MSB accounts:

    - Obtain evidence that the MSB is licensed if required in that state or verification that it operates as an agent for a licensed MSB.

    - Obtain evidence that the MSB is registered, if necessary, with FinCEN.

    - Obtain information about the nature of the MSB's business and expected activity.

    - Confirm that the MSB has an AML compliance program. **NOTE: The bank is not required to assess the adequacy or quality of the MSB's anti-money laundering program or "audit" or "examine" the quality of the MSB's internal AML controls and procedures.**

2. EXISTING MSB ACCOUNTS -- With regard to established accounts, banks are required only to monitor unusual or suspicious activity and changes in the nature of such activity. **NOTE: Banks are not responsible to review the MSB's customers' activities and/or monitor the transactions conducted by the MSB's customers.**

In sum, it is the intention of FinCEN and the Federal Banking Agencies that banks are not under an obligation to police the activities of the customers of their MSB account holders. Likewise, if banks perform the steps above referenced, and notwithstanding anything to the contrary in the prior interpretive guidance or in the FFIEC Bank Secrecy Act Anti-Money Laundering Examination Manual, banks will satisfy their obligations under the Bank Secrecy Act in opening or maintaining MSB accounts.

TESTIMONY OF

DIANA TAYLOR

NEW YORK STATE SUPERINTENDENT OF BANKS

On behalf of the

CONFERENCE OF STATE BANK SUPERVISORS

before the

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT

UNITED STATES HOUSE OF REPRESENTATIVES

June 21, 2006

Good morning, Chairman Bachus, Representative Sanders, and members of the Subcommittee. I am Diana Taylor, Superintendent of Banks for the State of New York and a member of the board of directors of the Conference of State Bank Supervisors (CSBS). I am pleased to be here today on behalf of CSBS to discuss the impact of Bank Secrecy Act (BSA) compliance requirements on the availability of banking services to Money Services Businesses (MSBs). MSBs are a varied and segmented industry that involves many constituents: banks, check cashers, money transmitters, other types of MSBs, agents of MSBs, and customers.

CSBS is the professional association of state officials who charter, regulate and supervise the nation's approximately 6,240 state-chartered commercial banks and savings institutions, and nearly 400 state-licensed foreign banking offices nationwide. CSBS gives state bank supervisors a national forum to coordinate, communicate, advocate and educate on behalf of the state banking system.

The New York State Banking Department, like the majority of state banking departments nationwide, is also responsible for licensing, supervising, examining and regulating MSBs that operate within our state's borders. According to the most recent CSBS survey, 43 states, the District of Columbia, Guam and Puerto Rico all license some type of MSB, and legislation is currently pending in several of the states that have no law in place. Thirty-one of these states, including New York, examine MSBs for compliance with federal BSA and anti-money laundering regulations. We, like most of our colleagues, use the Federal Financial Institutions Examination Council (FFIEC) manual and other guidance issued by regulatory agencies, including the Financial Crimes Enforcement Network (FinCEN), as the foundation of our examination procedures.

The MSBs that New York currently licenses, supervises and examines are money transmitters and check cashers. In 2005, money transmitters in New York State alone processed more than 92 million transactions totaling in excess of $96 billion; the New York State check cashing industry processed more than 34 million checks totaling in excess of $15 billion.

Like all commercial businesses, MSBs range in complexity, from a small business operating in a single location to a sophisticated, complex national provider operating in multiple states. The risk profiles also vary significantly among different types of MSBs. Money transmission and check cashing activities are vastly different types of financial services, with much different risk profiles.

FinCEN's current definition of an MSB is very broad: an MSB is a money transmitter or any entity that offers money orders, travelers' checks, check cashing services, currency dealing or exchange, or stored value cards with a transaction threshold of $1,000 or more for any one person on any given day. This definition captures not only businesses that consider money services their primary function, but also those for which money services are incidental, such as grocery stores that provide check cashing services for customers without a fee.

FinCEN's definition of an MSB also does not differentiate among different levels of risk within the MSB industry. Money transmitters, for example, take in funds for transfers and transfer a sizable portion of those funds overseas. Check cashers, on the other hand, pay out funds and service a specific locality or neighborhood. It would seem, therefore, that a money transmitter might be at higher risk for participation in terrorist financing than a check casher.

The Need for Money Services Businesses

MSBs do fill a need in many markets. They provide convenient access to financial services in many neighborhoods with few or no bank branches. Some individuals and families are unable or unwilling to obtain traditional banking services; for these groups, which often include immigrants and low-income households, MSBs may be the only means of access to cash, or the only avenue for sending funds to family members abroad. Billions of dollars in micropayments pass through these MSBs every year, and these payments make up a significant percentage of the gross national product in many developing countries.

The Nature of Money Services Businesses

MSBs engage in short-term transactions. Money transmission and check cashing activities settle within days, making MSBs essentially pass-through settlement companies that are portals to our banking system.

The short-term, pass-through nature of an MSB creates factors that increase the industry's risk profile if not properly controlled. Although an MSB may have a core of repeat customers, a good portion of its customer base still consists of transient populations – thus, much of its business is one-time customer transactions. Money transmitters, in particular, may conduct their operations through multiple locations. MSBs by their nature are cash-intensive, fee-based entities that handle a large volume of transactions. These factors alone elevate an MSB's operational, liquidity, legal and reputational risks.

Other external factors may affect the risk profile of an MSB. Legitimate customers and businesses are vulnerable to fraud and exploitation at the hands of unlicensed or unregistered MSBs. These unlicensed and unregistered MSBs pose a reputational risk to their legitimate counterparts, which may be held guilty by association.

In addition, since MSBs are portals to the banking system, they can be vulnerable to customers who try to use them to gain access to the banking system for the purposes of money-laundering or other financial crimes. These customers may prefer to seek out MSBs in an attempt to avoid recordkeeping requirements, thinking the MSB is one step removed from the banking system. These customers may not realize that MSBs must have compliance programs that adhere to BSA/Anti-Money Laundering (AML) provisions, or may expect an MSB to have a weaker compliance program.

Are MSBs high risk? The risk profile of an MSB certainly is at a higher risk than other commercial entities that operate in more traditional non-financial service segments, such as manufacturing. However, all commercial entities have risk. The more important question is how MSBs manage these risks. Can management properly identify, monitor and control risks so that high risk activities or high levels of risk can be brought to acceptable levels?

MSB management must be willing and able to manage its business risks, including the standards required for a BSA/AML program. If an MSB is unable or unwilling to meet these standards, it cannot expect to be able to maintain a bank account or a banking relationship. Certain MSB industry participants may be unwilling or unable to meet the BSA/AML standards; as a result, we would expect to see consolidation within the MSB industry.

The Relationship Between Banks and Money Services Businesses

When banks provide services to their customers, they must weigh the risk profile of each customer and price their services accordingly.

MSBs require specific banking services. These services include the establishment and maintenance of a bank account, transaction processing, and currency processing (both currency draws and currency deposits). MSBs also require a variety of credit facilities, such as lines of credit for liquidity purposes. Not only does the MSB require access to a bank account, but an agent of an MSB must also have access to that bank account.

Relationships between a bank and an MSB generally work better if the bank and MSB are in close proximity to each other. Close proximity between these two entities makes it easier for the MSB to make a deposit as carrying currency draws or deposits over great distances creates a security issue for the MSB, or it forces the MSB to incur the additional cost of contracting for secured transportation.

In the case of an MSB's agents, it is more efficient, effective and secure for an agent to deposit transmission activity daily and transfer the funds to the transmitter via the Automated Clearing House (ACH) network, rather than use some form of physical transportation that may require more than one day to settle.

The banking relationship is vital for an MSB to stay in business. Without the access to the payments system that a bank provides, MSBs cannot clear or collect checks or transfer funds. An MSB also represents a customer base that can generate revenue for the bank. This customer relationship is primarily transaction based.

The decision of two large banks to discontinue their services to MSBs in New York in 2005 required approximately 30 money transmitters and 180 check cashers to change their banking relationships. All of those businesses, except for two that had other issues, were able to establish new banking relationships with other institutions, and the transition was orderly. Twenty-nine banks currently provide services to money transmitters in New

York, with two banks providing 42% of these relationships. Only 12 banks provide services to check cashers, and 87% of our licensed check cashers do business with only two of these banks.

The two banks that are most active in providing services to money transmitters are currently considering exiting this business. This departure will undoubtedly present a significant challenge to New York's MSBs, not only in the short term but in the long term as well, as the decline in competition is likely to raise fees for these businesses.

Banks and MSBs: Finding a Solution

So how do we solve this problem?

We clearly do not want to see one bank holding the vast majority of MSB accounts. It is better for the safety and soundness of the entire industry if MSB accounts are spread out across a diversity of banks. Therefore, our solution must create incentives that ultimately serve to protect consumers, the banks and the MSBs.

Piecemeal, stop-gap legislation is not a viable solution.

The New York State legislature, for example, is currently considering legislation that would prevent any banking institution in the state from denying banking services to an MSB on the basis of the Bank Secrecy Act without the prior approval of the Superintendent of Banks. My department strongly opposes this bill, which would set a dangerous precedent. The role of a regulator is not to mandate who a regulated entity should or should not do business with. It would be entirely inappropriate for any government entity to require that banks provide service to a particular type of business.

The solution requires effort from all parties involved: the MSBs, the banking industry, state and federal banking regulators, FinCEN and the IRS.

The following recommendations, while not comprehensive, form the basis of a solution.

Revisit the FinCEN definition of an MSB. The current definition seems too broad, with a threshold so low that it may capture more entities than intended, which leads to further uncertainty for banks. The definition should target the entities whose primary business is providing financial services, rather than entities that offer financial services only incidentally to their core business.

Consider further clarifications of standards. Regulators should be able to develop simplified, standardized requirements for MSBs that serve a lower-risk client base. This new standard could serve as a foundation for an advanced comprehensive BSA/AML program. A single-location check casher that serves a low-risk client base, such as cashing only payroll checks without any money transmission activity, could be deemed a low risk MSB, particularly in the area of terrorist financing. This type of business would be an ideal candidate for a simplified standardized BSA/AML program.

Additionally, while the joint guidance issued by FinCEN and the federal banking agencies did help clarify regulators' expectations for banks that serve MSBs, further guidance may also be necessary in two areas: appropriate due diligence when maintaining accounts for foreign providers of money services; and identifying entities that may be operating covertly as MSBs.

Congress and the federal regulatory agencies changed the federal requirements for BSA/AML procedures because of real and potential weaknesses in our existing system. Changes in the MSB industry as a result of these new legal requirements were not only inevitable, but necessary and desirable. We need to review the current foundation of BSA/AML to see whether we can clarify the standards further.

Continue to improve federal and state coordination. Thirty-nine states have signed a Memorandum of Understanding (MOU) with FinCEN and 35 states have signed a similar MOU with the Internal Revenue Service (IRS) to set forth procedures for sharing certain Bank Secrecy Act information. Among other elements, we agree to share information about FinCEN's administration of the Bank Secrecy Act; the individual states' policies and procedures for BSA compliance examinations; significant BSA examination findings; proposed enforcement actions, and analytical data.

Sharing this information helps both the states and FinCEN fulfill our missions as supervisors and enforcers of applicable law. These MOUs improve and enhance cooperation among agencies, reduce duplication of effort, and ensure consistency in the application of federal standards. Through this enhanced cooperation and coordination, we hope to achieve our ultimate goal of helping all financial institutions identify, deter and prevent all forms of financial crimes, including terrorist financing and money laundering.

We also hope and expect that improvements in coordination, communication and consistency will boost banks' confidence in their ability to manage the risks involved with providing services to MSBs.

These MOUs, however, cannot entirely address a critical need for additional resources at both state and federal levels. The number of check-cashing outlets alone exceeds 11,000 nationwide. In order to carry out our responsibilities effectively and efficiently we need access to additional training and a renewed commitment from FinCEN and the IRS to deliver on the promises of the MOUs.

Federal and state regulators, FinCEN and the IRS need to continue our efforts to deliver a consistent message to the banking industry about their obligations and rights. In New York, the Office of the Comptroller of the Currency (OCC) has adopted an approach of concurrent jurisdiction with respect to MSBs. The OCC requires that MSBs that are operating subsidiaries of national banks retain their state MSB licenses and continue to be subject to state regulation, supervision and examination. At the same time, the OCC retains its own jurisdiction. We commend the OCC for this teamwork approach, which

has optimized oversight over MSBs, and call for Congress to support this approach and urge that it be continued on a nationwide basis by the OCC and be extended to the Office of Thrift Supervision (OTS).

Create incentives to encourage banks to serve the MSB industry. We, as regulators, might consider offering CRA credit to banks that provide services to MSBs, since a significant segment of these businesses' customers are low-income individuals and households, and are often minorities and new immigrants. Banks should be aware of the large populations these businesses serve, and think about ways to increase their access to these individuals and households, who often have no traditional banking relationships.

Seek out incentives for banks to offer MSB-type services in unbanked and underbanked communities across the country. In New York State, my department's Banking Development District program creates incentives for banks to open branches in underbanked areas by making them eligible to receive below-market, municipal deposits. This program has already led to branching in 27 underbanked communities throughout the state.

Continue to require better risk management systems for MSBs. MSBs must continue to improve their risk management systems, with continuing focus on the area of BSA/AML compliance. As MSBs make their commitment to compliance clear, banks may become more willing to provide services to these businesses.

Continue to improve state supervision of these entities. New York State has significantly strengthened its MSB licensing, supervision and examination program, as have many other states. Among many other standards, we require applicants for MSB licenses to submit information demonstrating compliance with the USA PATRIOT Act. This includes:

- Policies, procedures and internal controls designed to ensure compliance with BSA/AML requirements;
- A resume of the compliance officer responsible for day-to-day compliance with BSA/AML requirements and the entity's compliance program;
- Education and training programs for appropriate personnel;
- An affidavit that an independent review to monitor and maintain an adequate program will be performed.

Our supervisory protocol for MSBs follows a structure we call "FILMS," instead of the CAMELS program used for depository institutions.

- "F" stands for the financial condition of the business; examiners look at the balance sheet composition, profitability, capital level, and other elements in order to determine the business's financial stability.
- "I" stands for internal controls and auditing, an evaluation of the business's internal policies and procedures.

- "L" stands for legal and regulatory compliance, the critical issue of whether and how the business follows state and federal laws, inclusive of BSA/AML.
- "M" stands for the all-important management component, as examiners look at the licensee's ability to identify, measure and monitor risks.
- "S" stands for systems and technology, which is particularly important for money transmitters.

New York State takes an integrated approach that focuses on risk management with an emphasis on the compliance function, inclusive of BSA. Why is this important? We understand MSBs to be for-profit commercial entities that need a strong management system to identify, monitor and control risks. If an MSB is under financial stress, it will have to make certain business decisions. It will take on more risk, cut costs in non-revenue generating areas such as compliance, or both. This would translate into more risk but fewer resources for operational controls and compliance. Therefore, the weakening of the risk management system makes the MSB more vulnerable to BSA/AML violations and susceptible to money-laundering. Understanding how the FILMS components interact with each other provides an early-warning system about weakening conditions and a guide to where to look for noncompliance issues.

While the level of supervision is not yet consistent across the country, both CSBS and its counterpart organization, the Money Transmitters Regulators Association, have made a commitment to provide additional training and resources for state MSB examiners. CSBS has created a "boot camp" training course for BSA professionals in state banking departments, to ensure that state regulators have the most up-to-date information available on BSA policies and procedures. CSBS has also begun certifying examiners as BSA compliance practitioners. In cooperation with our staff, CSBS has developed an MSB Examiner Course that helps state MSB examiners to conduct examinations of money transmitting and check cashing businesses.

States have regulated and supervised MSBs for many years. State interest initially emphasized consumer protection, making sure that these businesses did not defraud or exploit the most vulnerable of our citizens. Over the past two decades, this mission has evolved to include financial and money laundering concerns. Although MSBs are not generally supervised on the federal level, the addition of FinCEN, in the area of BSA, as the federal enforcement agency and the designation of the IRS as the federal examination and investigating agency for MSBs has caused our role to evolve even further.

Conclusion

It is essential that we keep this industry viable for those who need it. Doing so will require a sustained effort on the part of all involved – the MSBs themselves, the banking industry, state and federal banking regulators, FinCEN and the IRS.

No silver bullet can solve this issue, and fingerpointing is not helpful. Licensing alone is not a panacea, despite the arguments of some MSBs. It is also not helpful for banks to

categorically refuse to do business with MSBs. Regulators must be consistent in their requirements for the industries. Everyone must work together.

I commend the Subcommittee for holding a hearing on this important issue, which is a case not of good vs. bad, but of several imperatives conflicting – the government's need to identify, deter and interdict terrorist and criminal financing; the banks' need to manage their risks; the money-services businesses' need for financial services; and the public's need for continued access to these services.

Balancing these needs will require constant communication among all parties involved. This hearing is a welcome addition to that communication, and I look forward to answering any questions the Committee may have.

Money Services Businesses – Part I

	Department Licenses Money Services Businesses (MSBs)			Department Examines MSBs for Compliance with Federal BSA Anti-Money Laundering Regulations	
	Yes/No	Entities Licensed by the Department	Other Agency Responsible for Licensing MSBs	Yes/No	Exam Procedures Examiners Utilize During an Examination of MSBs
Alabama	Yes	Payday lenders, small loan companies, finance companies, mortgage brokers, pawnshops, and title pawn shops	Money transmitters and check sellers are regulated by the Alabama Securities Commission. Pure check cashers are unlicensed in this state	No	N/A
Alaska	No	N/A	MSBs are not presently licensed in Alaska. Legislation is proposed for the 2006 session for our division to regulate them.	No	N/A
Arizona	Yes	Money transmitters	None	Yes	FFIEC Manual
Arkansas	No	No	State Board of Collection Agencies	No	N/A
California	Yes	Money transmitters, agents of money transmitters, issuers of money orders and travelers checks (payment instruments)	CA Department of Justice supervises check cashers	Yes	Detailed work program which includes a review for compliance with the Office of Foreign Asset Controls, transactions testing, review of CTR/SAR filings, verification (count of) CTS/SAR, and review for annual independent AML review which is required for all MSBs. Risk assessment is also required to determine if licensee is addressing BSA/AML issues. Limited data mining is also performed. In house and external training is supplemented with information from various law firms, FinCEN training information, IRS examination manual, FRB/FDIC manuals, and best practices recommended by the BASEL committee and ACAMS study guides (Financial Action Task Force 40 recommendations, plus 9 special recommendations issued in late 2004)
Colorado	Yes	Money transmitters	N/A	Yes	State of Colorado Manual
Connecticut	Yes	Money transmitters and check cashers	N/A	Yes	FFIEC Manual
Delaware	Yes	Money transmitters and check cashers	N/A	Yes	FFIEC Manual
District of Columbia	Yes	Money transmitters and check cashers	N/A	Yes	DC Examination Procedures are based on FFIEC and IRS guidelines
Florida	Yes	Office of Financial Regulation's Division of Securities and Finance licenses Funds Transmitters, Payment Instrument Issuers, Check Cashers, Foreign Currency Exchangers, and Deferred Presentment Providers.	N/A	Yes	Office of Financial Regulation is currently developing a composite set of exam procedures taking applicable portions of the procedures contained in the IRS guidelines and the FFIEC that are relevant to MSB's.
Georgia	Yes	Money transmitters, check sellers, and check cashers	N/A	Yes	Still under development for some categories, however, portions of the FFIEC Manual and IRS exam procedures, in addition to established internal procedures will be utilized in most cases
Guam	Yes	Money transmitters, check cashers, and agents of Western Union	N/A	Yes	IRS guidelines
Hawaii	No	N/A	No state agency has that responsibility	N/A	N/A
Idaho	Yes	Money transmitters, open system cash cards, payment instrument sellers and issuers, and wire transfer	N/A	Yes	To be determined.

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Money Services Businesses – Part I

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	Yes/No	Entities Licensed by the Department	Other Agency Responsible for Licensing MSBs	Yes/No	Exam Procedures Examiners Utilize During an Examination of MSBs
		agencies.			
Illinois	Yes	Check cashers	N/A	No	N/A
Indiana	Yes	Money transmitters and check cashers	N/A	Yes	IRS and FFIEC both.
Iowa	Yes	Money transmitters	N/A	Yes	Based on FFIEC Manual
Kansas	Yes	Money transmitters	N/A	No	N/A
Kentucky	Yes	Checks sellers, check cashers	N/A	No	N/A
Louisiana	Yes	Money transmitters and check cashers	N/A	Yes[1]	IRS/FinCEN guidelines and FFIEC Manual
Maine	No	N/A	Office of Consumer Credit Regulation	No	N/A
Maryland	Yes	Money transmitters and check	Compliance exam procedures	Yes	Compliance exam procedures developed in-house
Massachusetts	Yes	Foreign transmittal agencies, check cashers, and check sellers	N/A	Yes	The exam procedures are a combination of the FFIEC's manual and the IRS examination guidelines.
Michigan	Yes	Issuers of travelers checks and money orders	N/A	No	N/A
Minnesota	Yes	Money transmitters and check cashers	N/A	No	N/A
Mississippi	Yes; not in all instances	All consumer finance licenses.	N/A	No	However, money transmitters are examined for structuring.
Missouri	Yes	Money transmitters and money order companies	N/A	No	N/A
Montana	No	N/A	Licensing not required	No	N/A
Nebraska	Yes	Sale of check companies	N/A	No	N/A
Nevada	Yes	Money transmitters & check cashers	N/A	Yes	Incorporating into our processes ookk
New Hampshire	No	N/A	Legislation pending	No	Legislation pending
New Jersey	Yes	Money transmitters, foreign money transmitters, and check cashers.	N/A	Yes	Procedures for the review BSA for MSBs have been developed internally The FFIEC BSA Examination procedures were used as a guideline and some of the FFIEC procedures were incorporated into the State's program
New Mexico	No	N/A	They are not licensed in New Mexico	No	N/A
New York	Yes	Money transmitters and check cashers	N/A	Yes	FFIEC Manual and FinCEN Handbook
North Carolina	Yes	Money transmitters and check cashers	N/A	No	For application approval, MSB must prove that they are registered as an MSB with FinCEN. Agency is currently in process of developing MSB examination procedures for compliance with BSA/AML regulations.

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Money Services Businesses – Part I

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	Yes/No	Entities Licensed by the Department	Other Agency Responsible for Licensing MSBs	Yes/No	Exam Procedures Examiners Utilize During an Examination of MSBs
North Dakota	Yes	Money transmitters	N/A	Yes	Department plans on implementing procedures in next 90 days
Ohio	Yes	Foreign and domestic money transmitters; check cashers and check caser lenders	N/A	Yes	MTRA coordinated exam procedures developed by State of Texas
Oklahoma	Yes	Money order sellers	N/A	Yes	FFIEC Manual
Oregon	Yes	Money transmitters, payday lenders, pawnshops, and finance companies. We do not license or examine check cashers	The State of Oregon does not license check cashers	Yes	FFIEC Manual for the appropriate business type.
Pennsylvania	Yes	Money transmitters, check cashiers, and pawn brokers	N/A	Yes	We created an internal BSA examination for money transmitters
Puerto Rico	Yes	Money transmitters, check cashers, and pawn brokers	N/A	Yes	Custom made Examination Program in line with Federal and Local laws and regulations
Rhode Island	Yes	Money transmitters, check sellers, and check cashers.	N/A	Yes	It is our intent to utilize the FFIEC Manual in future examinations.
South Carolina	NR	NR	NR	NR	NR
South Dakota	Yes	Money order issues	N/A	No	N/A
Tennessee	Yes	Money transmitters and check cashers	N/A	No	N/A
Texas	Yes	Money transmitters, currency exchangers, money order issuers, travelers check issuers, third party gift cards, and issuers of stored value	N/A	Yes	MSB examiners utilize procedures developed in-house using BSA laws/regulations as guidelines
Utah	Yes	Money transmitters	Check cashers register with the Department, but are not issued a license.	Yes	Department developed questionnaire and BSA required compliance standards
Vermont	Yes	Money transmitters, check cashers, currency exchange companies	N/A	Yes	FFIEC manual
Virgin Islands	Yes	Money transmitters, check cashers, currency exchange, and non-ATM service	N/A	Yes	The Division has recently assumed jurisdiction of money service businesses and is currently putting in place examination procedures and guidelines
Virginia	Yes	Check sellers and money transmitters	N/A	No	N/A
Washington	Yes	Money transmitters, check cashers, and currency exchangers	N/A	Yes	Have own exam procedures along with federal guidance.
West Virginia	Yes	Currency transmitters, including check cashers, check sellers, and currency exchangers	N/A	No	N/A
Wisconsin	Yes	Sellers of checks (money transmitters) and currency	N/A	No	N/A

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Money Services Businesses – Part I

	Department Licenses Money Services Businesses (MSBs)				Department Examines MSBs for Compliance with Federal BSA Anti-Money Laundering Regulations		
	Yes/No		Entities Licensed by the Department	Other Agency Responsible for Licensing MSBs	Yes/No		Exam Procedures Examiners Utilize During an Examination of MSBs
Wyoming	Yes		exchanges (check cashers) Money transmitters	N/A	Yes		FFIEC Manual, as well as procedures and a work program created by the state's money transmitter examiner.
Totals	Yes	No			Yes	No	
	46	7			31	21	

NR: Not Reported.
N/A: Not Applicable.

[1] Money transmitters only.

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STATEMENT OF ISAK WARSAME

PRESIDENT OF DAHABSHIL, INC.

BEFORE THE

COMMITTEE ON FINANCIAL SERVICES
UNITED STATES HOUSE OF REPRESENTATIVE

SUBCOMMITTEE ON FINANCIAL INSTITUTIONS
AND CONSUMER CREDIT

JUNE 21, 2006

Mr. Chairman and Members of the Committee, my name is Isak Warsame. I am the President and Chief Executive Officer of Dahabshil, Inc, which is a money remittance company headquartered in Columbus, Ohio. Dahabshil, Inc. specializes in providing money transfer services to the growing population of Somali immigrants to the US. These immigrants use Dahabshil to send money to relatives in Somalia and in other countries on the Horn of Africa, including Kenya, Ethiopia, and Djibouti.

Dahabshil collects money from its customers in the United States and in most cases delivers it to their relatives in Somalia within 24 hours. Like many other remittance companies, the vast majority of Dahabshil's customers are immigrants. They are employed in manual and unskilled labor in industries like construction, health care, janitorial and maintenance services, and fast food. Virtually to a person, Dahabshil's customers are African and African-American. I am a US citizen, an immigrant from Somalia, as are almost all of my employees and agents.

Importance of Dahabshil's Services

I'd like to take the opportunity to tell you a little about Somalia and the importance of remittances there.

Somalia has suffered through more than fifteen years of civil war and lawlessness. Despite the efforts of the international community to bring peace and unity to Somalia, Somalia still has no functioning central government and no banking system. Because of this, Somalia is excluded from the international economy and receives little foreign aid and no World Bank/IMF assistance. There is prevalent violence in the South around Mogadishu, and you may have read recently about the violence there.

With no government and no banking system, Somalia has essentially no employment, no commercial economy, and no means of developing them without substantial assistance from the outside.

At present remittances from abroad – from Somali expatriate communities and from international development and charitable organizations such as the United Nations, Save the Children, the Red Cross and CARE – are the principal source of funds in Somalia. All of these remittances, all of this charitable aid, is delivered to Somalia by remittance companies like Dahabshil. This is a very important point. In the absence of a banking system, even international relief organization like the Red Cross and CARE must use remittance companies such as Dahabshil to fund their projects, meet their payroll and pay their rent. If remittance companies are unable to do business because of actions of the banking community in the US, it affects not only private remittances between family members, but also large-scale charitable efforts of the world-wide community.

It is impossible to overemphasize the importance of remittances from abroad to the Somali people. According to a 2003 study (the most recent data available), more than 73% of persons in Somalia live on less than $2.00 per day and more than 43% live on less than $1.00 per day. A recent United Nations and European Commission study on the Feasibility of Financial Services in Somalia concluded that remittances are by far the single largest source of hard currency in Somalia and annually account for some 22.5% of total family income. Remittances from the Somali diaspora ameliorate the crippling effects of Somalia's civil war, which include pervasive unemployment, hunger, disease, and poverty. In Somalia, the receipt of remittances from abroad means the difference between eating and starving, between having a roof over one's head and being on the street, between clothing and not clothing one's children and between health and sickness.

Challenges to Maintaining Dahabshil's Services

Despite the importance of its services to the country of Somalia and to the community of Somali immigrants here in the United States, Dahabshil's business is threatened because of actions of US banks, which are seeking to close the bank accounts of money service businesses on a systemic basis.

Dahabshil is a cash business and depends on banking services to stay in business. Customers come into Dahabshil offices with cash, usually between $50 and $300, and instructions on how it should be delivered. Dahabshil uses the US banking system at every stage of its transfers. Each of its offices deposits its daily receipts into local bank accounts and Dahabshil uses wire transfer services of large US banks to transfer funds through international accounts to Dahabshil's Somali partner for distribution to the designated recipients. If Dahabshil cannot maintain its bank accounts, it cannot continue to provide its services.

Unfortunately, bank after bank has closed Dahabshil's account or has refused to speak with Dahabshil about opening an account. And Dahabshil's experience is not unique. I have spoken with numerous other remittance companies over the past few years. Every one has reported bank account closures and threats of closure that imperil the company's business. Over the past year, Dahabshil has received letters from its banks in Ohio, Massachusetts, Georgia and Tennessee, announcing that the banks intended to close its accounts. Three of the banks refused to meet with Dahabshil to discuss the decision. Two of the banks, including Chase Bank which is Dahabshil's main banking relationship, referred specifically to the fact that Dahabshil is a money service business as the reason for the account closures. The other two failed to give any reason at all.

Dahabshil operates entirely in compliance with the law. It is registered with FinCen, and is licensed in [9] states, including Ohio, Tennessee, Georgia, Washington, Virginia, Utah and Massachusetts. Dahabshil operates in full compliance with the Bank Secrecy Act. Over the past four years, Dahabshil has invested hundreds of thousands of dollars in its Bank Secrecy Act and anti-money laundering compliance programs. It has proprietary software that automatically screens transactions in order to prevent payment to anyone identified as a terrorist or other international criminal. It submits reports required by the BSA like suspicious activity reports and currency transaction reports electronically. Dahabshil provides training and support for each of its agents and employees in identifying suspicious transactions. For the last three years, Dahabshil has hired an independent audit firm to assess its Bank Secrecy Act compliance program and suggest improvements. These audits have concluded that Dahabshil's management has a commitment to compliance, that Dahabshil has invested significant sums in compliance, and that there have been no transactions violating state or federal law. In short, Dahabshil has made every effort to assure that its services are used solely for personal and charitable remittances and not for any illegal or dangerous purposes. And it has been successful. But neither its efforts, its commitment nor its success has mattered to the banks that closed Dahabshil's accounts. All that matters to the banks is that Dahabshil is a money service business.

In conclusion, I would ask this Committee to consider whether it can take steps to slow or stop the bank account closures that threaten Dahabshil's business and the business of other reputable money service businesses operating in the United States. Last year, we saw some relief when FinCen held a series of public hearing and issued regulatory guidelines directing that Banks should undertake an MSB by MSB analysis before closing any account. The banks that have undertaken such analysis have found Dahabshil and other MSBs to be worthy partners and have maintained their relationship. Unfortunately, if recent trends continue, Dahabshil and other MSBs will be forced to close their doors and eliminate the financial lifeline we provide to Somalia and other developing countries. We are certain that the money will find alternative means to reach the needy but these means are the informal, unregulated and unsafe pathways that the BSA and related legislation were meant to close.

Thank you for your time and attention to this matter.

Statement for the Record
Submitted by Western Union Financial Services, Inc.

Financial Institutions and Consumer Credit Subcommittee Hearing
"Bank Secrecy Act's Impact on Money Services Businesses"
10:00 a.m., June 21, 2006

Western Union Financial Services, Inc. would like to thank the Chairman and Members of the Subcommittee for the opportunity to comment on the banking challenges being faced by money services businesses in the United States. We respectfully request that these comments – including the attachments – be entered into the official record of the hearing entitled "Bank Secrecy Act's Impact on Money Services Businesses" scheduled for 10:00 a.m. on June 21, 2006.

A very serious threat to payment infrastructure access is taking place now, right here in the United States. U.S. banks – both large and small – have been closing money services businesses bank accounts at an alarming rate.

Over the past 18 months, hundreds of Western Union Agents have either had their banking relationships terminated or have experienced significant difficulties in establishing or maintaining banking relationships. In 2005, Western Union received over 2,000 requests from or on behalf of its Agents seeking help finding banks that will accept their business, or satisfying new and sometimes onerous requirements for maintaining accounts. The number is on track to exceed 3,000 in 2006. Many money services businesses have been forced out of the remittance business, either because they cannot establish a banking relationship or because the costs of doing so have become prohibitive.

Some banks have sent letters to our Agents advising them that their accounts are being closed, often providing no more than 30-days notice. The letters generally offer no explanation as to why the accounts are being closed. Some banks have told us that their decision stems from a concern over Bank Secrecy Act obligations and potential liability. Smaller banks in particular have expressed concern that, in the current regulatory and enforcement environment, if a bank makes one mistake, it risks a penalty in the millions of dollars and damage to its reputation. Many say they simply cannot afford to run that risk.

By far, the most disturbing aspect of our experience is the nature of the businesses that are losing or having difficulty maintaining their banking relationships. These businesses are almost exclusively small, independent businesses located in low or moderate income areas in large cities and urban corridors, such as Boston, New York and Miami. These businesses are predominantly minority-owned and serve minority, ethnic and immigrant communities. As a result, the very communities that banks are supposed to be extending services to and who need access to banking services the most, are the ones who are being adversely impacted by the current situation.

Keep in mind, all of this is taking place after Federal regulators have tried to reassure banks by issuing guidance as to their anti-money laundering obligations and by emphasizing that the vast majority of money services businesses are legitimate, regulated businesses that require and deserve banking relationships. The guidance also points out that banks are not responsible for monitoring their customers' compliance with the BSA.

It seems the issue is being driven by conflicting interpretation of regulations within the same government agencies. While our hope is that this problem is temporary, this crisis is costing the industry dearly, shutting some consumers out of the financial system and, if it continues to worsen, driving transactions underground.

The following are our specific recommendations as to the actions we believe FinCEN and the bank regulatory agencies should take to address the current problem.

A. Issue Additional Guidance That More Clearly Defines and Limits Banks' Obligations With Respect to Money Services Businesses

First, banks should only be required to perform specifically defined due diligence when opening an account for a money services business. This should consist of obtaining evidence that the money services business is properly licensed and, if required, registered with FinCEN; basic information about the nature of the business and the expected activity in the account; and, if the bank deems necessary, confirmation that the money services business has an anti-money laundering program in place.

Second, banks should only be required to monitor account activity to identify unusual or suspicious changes in the nature of such activity, such as a sudden and significant increase in the amount of money being deposited on a daily or weekly basis. It should be made clear that banks are not required to "look through" the money services business and somehow monitor the transactions conducted by the business' customers.

Third, banks should be given reasonable assurance that, if they satisfy these basic due diligence and monitoring obligations, they will not be held accountable should a customer of their money services business accountholder engage in money laundering or other illegal activity.

B. Give Banks Community Reinvestment Act Credit for Opening and Maintaining Accounts for Money Services Businesses

As previously stated, the Western Union agents who are being adversely impacted by the current situation are predominantly minority or ethnic owned businesses located in low and moderate income urban areas serving minority, ethnic and immigrant communities. We doubt that our experience in this regard is unique. Since these are the very communities that the Community Reinvestment Act ("CRA") is designed to ensure receive banking services, we believe the federal bank regulators should explicitly recognize the provision of banking services to money services businesses as a qualified CRA activity. By so doing, the regulators would

send a clear message as to the value of such services and would give banks a significant incentive to provide them.

C. Allow Money Services Businesses to Maintain Accounts at Federal Reserve Banks

In order to alleviate this crisis, we believe that action should be taken at the legislative and regulatory level to allow money services businesses to directly open accounts with the Federal Reserve Banks. We believe such action is justified by the present situation, particularly since the problem has arisen in large part because of the regulatory environment created by the federal banking agencies. Precedent for the Federal Reserve Banks providing account services to non-members was established in the late 1970's when savings and loan associations, non-member banks and credit unions were allowed direct access to the Federal Reserve's account services. At that time, the infrastructure, including pricing and operating guidelines, was put in place to accommodate the provision of such services to non-members. That same infrastructure could be used immediately by the Federal Reserve to provide account services to money services businesses.

For your review and entry into the official hearing record, we have attached our response to FinCEN's Advanced Notice of Proposed Rulemaking on Provision of Banking Services to Money Services Business dated May 8, 2006. Also attached is the recommended Revised Interagency Interpretive Guidance on Providing Banking Services to Money Services Business Operating in the United States, which was prepared by the Money Services Round Table (formerly, the Non-Bank Funds Transmitters Group), of which Western Union is a member.

This crisis needs to be addressed immediately. We believe our recommendations provide both interim and long term solutions.

Thank you for your interest in this serious issue.

Attachments:

- Western Union response to FinCEN's Advanced Notice of Proposed Rulemaking on Provision of Banking Services to Money Services Business.
- Money Services Round Table recommended Revised Interagency Interpretive Guidance on Providing Banking Services to Money Services Business Operating in the United States.

Western Union Financial Services, Inc.
12510 East Belford Avenue
M21A5
Englewood, CO 80112

May 8, 2006

VIA E-MAIL (regcomments@fincen.treas.gov)

Robert W. Werner
Director
Financial Crimes Enforcement Network
P.O. Box 39
Vienna, Virginia 22183

Re: RIN 1506-AA85
Provision of Banking Services to Money Services Businesses
Advanced Notice of Proposed Rulemaking

Dear Mr. Werner:

Western Union Financial Services, Inc. ("Western Union") appreciates the opportunity to comment on the above-referenced Advanced Notice of Proposed Rulemaking ("ANPR"). Western Union is one of the leading providers of consumer payment services in the United States. Through our extensive agent network and various electronic channels, we provide money transfer services to people who periodically send funds to family and friends in other locations, who need to send and receive cash quickly in emergencies, or who want a convenient way to pay their monthly bills. Our agents range from large national and regional companies to small independently owned retail businesses. All of them require access to banking services in order to carry out their money transfer business and serve their communities. As a result, Western Union, our agents, and the consumers who rely on our services all have a significant interest in the subject matter of the ANPR.[1]

General Comments

As recounted in the ANPR, the problem of money services businesses being denied access to banking services led to a series of meetings and congressional hearings

[1] Money transfer services are also provided by our sister companies, Orlandi Valuta ("OV") and Vigo Remittance Corporation ("Vigo"). Both OV and Vigo offer their services and products through agent networks and, like Western Union, both they and their agents have experienced problems with either securing or maintaining banking relationships.

in early 2005 and culminated in the issuance of formal guidance by FinCEN and the federal bank regulatory agencies. Although the guidance was welcome, it has failed to stem the tide of account closures and related problems. The situation has reached the point where further action is necessary. While more guidance would be helpful, FinCEN and the bank regulatory agencies need to consider additional measures to ensure that money services businesses are able to obtain access to the banking system.

The seriousness of the problem is underscored by the fact that account closures have not been limited to money services businesses that, viewed by some set of objective criteria, arguably pose an unreasonable risk to banks. As discussed below, Western Union has had certain of its corporate banking relationships terminated, and many of our agents have lost long-standing banking relationships, been unable to establish new ones, or been subjected to burdensome demands in order to maintain or open an account. Western Union is a nationally recognized and respected company. We are registered with FinCEN, subject to the full array of Bank Secrecy Act ("BSA") requirements, and are licensed, regulated, and examined by nearly every state and the District of Columbia. We have a comprehensive anti-money laundering program which includes monitoring of transactions and oversight of our agents. Our agents themselves are money services businesses subject to BSA requirements, have anti-money laundering programs in place, and are licensed and examined by the majority of states. If banks are unwilling to offer their services to us or our agents, then clearly something is wrong.

The primary cause of the problem appears to be banks' continuing concerns about their obligations and liability under the BSA with respect to money services businesses. First, banks apparently feel the need for more definitive guidance in this area. In particular, we understand they would like a clearer statement that they are not expected to police the activities of the customers of their money services business accountholders. In other words, so long as they conduct appropriate due diligence into the money services business, they will not be held accountable should a customer of the money services business engage in money laundering or other illegal activity. Second, banks have reported conflicts between the 2005 guidance and what they are being told by their bank examiners. For example, we have heard reports that examiners continue to consider *all* money services businesses to be "high risk," thus requiring heightened due diligence and oversight in all cases. In addition, examiners have allegedly told banks that they are in fact responsible for monitoring the activities of a money services businesses' customers. Finally, banks' concerns about potential liability are understandably heightened by the size of recent civil penalties in BSA cases and the trend towards criminalizing BSA violations. Faced with potential fines in the tens of millions of dollars and possible criminal prosecution, many banks have concluded that the risks of offering services to money services businesses are simply too great.

As FinCEN is aware, when money services businesses lose access to banking services, the consequences fall disproportionately on those who are least able to bear them. To a significant degree, the people who use and rely on money services businesses are the so-called "unbanked" – lower income individuals and families, immigrants who send money back to their home countries to support spouses, children and other family members, and members of minority and ethnic communities. These individuals have traditionally been underserved by the U.S. financial system and are most in need of access to financial services. In addition, many money services businesses that have lost their banking relationships are themselves small business owners who operate in and serve economically disadvantaged and low-income communities. The legitimate needs of these communities should drive FinCEN's and the other regulatory agencies' commitment to pursuing effective solutions to the current situation.

Western Union's Experience

Over the last year and a half, hundreds of Western Union agents have either had their banking relationships terminated or have experienced significant difficulties in establishing or maintaining banking relationships. During this period, Western Union has responded to over 2000 requests from agents seeking help finding banks who will accept their business or satisfying new and sometimes onerous requirements for opening or maintaining accounts. Many of our agents have been forced out of the money services business, either because they cannot establish or maintain a banking relationship or because the costs of doing so have become prohibitive. The following summarizes our experience.

In 2005, a major national bank apparently adopted a policy of refusing to provide bank accounts to any business that derived more than a certain percentage of its revenues from money services activity. Although the bank denied that it was exiting the money services market, the implementation of its policy resulted in the termination of scores of money services business accounts. In addition, its policy disproportionately impacted small, locally-owned businesses. This same bank also advised Western Union that it was closing all of Western Union's corporate accounts that were related to our money services business.[2] The bank refused to provide any explanation for its actions other than to state that they resulted from a "portfolio review" and were based on a "risk-reward"

[2] The bank also advised that it was closing all corporate accounts of our sister companies, Vigo and OV, that relate to their money services business. In the case of Vigo, this resulted in over 2000 long-standing accounts being closed. Although Vigo has been able to establish new banking relationships for many of these accounts, the time and resources necessary to do so have been significant.

assessment. It refused to provide any details about the assessment and refused to disclose whether its action stemmed from anti-money laundering or BSA compliance concerns.

Some banks have sent letters to our agents advising them that their accounts are being closed, often providing no more than 30-days notice. The letters generally offer no explanation as to why the accounts are being closed. When we have contacted these banks offering to provide them with information to address any concerns they may have, some have been open to working with us, but many others have simply stood by their decision. Other banks have told us that they will continue servicing existing agent accounts but will not establish new ones. Some banks have told us that their decision stems from a concern over BSA obligations and potential liability. Smaller banks in particular have expressed concern that, in the current regulatory and enforcement environment, if a bank makes one mistake, it risks a penalty in the millions of dollars and damage to its reputation. Many say they simply cannot afford to run that risk.

Other banks have sent letters notifying our agents that they must provide various types of information in order to maintain their accounts. Examples of information requested include evidence that the agent is licensed, evidence that the agent or Western Union is registered with FinCEN, copies of the contract between Western Union and the agent, copies of or information about the agent's or Western Union's anti-money laundering program, and information about the agent's money services business activities. For the most part, these requests appear to be designed to satisfy the banks' due diligence obligations as described in the 2005 guidance and the FFIEC BSA Examination Manual, although some ask for information significantly beyond the scope of the guidance.[3] While these requests are often time-consuming and burdensome, we generally have not experienced situations where a bank has refused to provide banking services after the requested information has been provided.[4]

In some cases, banks have imposed other, more onerous requirements in order to continue servicing agent accounts. One bank demanded that our agents agree to be audited, at the agents' expense, by a third party selected from a list provided by the bank. In addition, although we have offered to meet with banks and explain our agent oversight and transaction monitoring programs, some banks have requested that we agree to

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[3] The variety of requests we have received from banks appears to reflect a general confusion as to the type and extent of due diligence required by the regulatory guidance.

[4] Adding to the difficulties is the fact that many agents who receive such requests are small business owners for whom English may be a second language. The letters are often legalistic and hard for agents to understand, and many banks have offered little or no help in determining what is being requested Although Western Union provides extensive assistance in addressing these requests, the agents often feel intimidated and embarrassed by the process and in some cases simply abandon the effort.

indemnify the bank should any problems develop. Other banks have significantly increased their account servicing or maintenance fees for money services businesses, ostensibly to compensate them for the heightened due diligence and monitoring they feel they are required to perform by the regulatory guidance. For many smaller agents, these fees have been prohibitively expensive, in some cases more than the revenues they derive from their money services activities. In such cases, the new fees effectively result in the termination of the account.

By far, the most disturbing aspect of our experience is the nature of the agents who are losing or having difficulty maintaining their banking relationships. Few of our larger national or regional agent networks have been affected. Whether this is because banks consider them lower risk or because banks do not want to jeopardize other commercial banking relationships they may have with these companies, we can only guess. Instead, the agents who are experiencing problems are almost exclusively small, independent businesses located in low or moderate income areas in large cities and urban corridors, such as Boston, New York and Miami. These agents are predominantly minority-owned and serve minority, ethnic and immigrant communities. As a result, the very communities to whom banks are supposed to be extending services under the Community Reinvestment Act are the ones who are being adversely impacted by the current situation.

Specific Recommendations

The following are our specific recommendations as to the actions we believe FinCEN and the bank regulatory agencies should take to address the current problem.

A. Issue Additional Interagency Guidance That More Clearly Defines and Limits Banks' Obligations With Respect to Money Services Businesses

We are concerned that, despite the 2005 guidance, banks feel they are being sent a mixed message by regulators as to their compliance obligations. On one hand, regulators have said that the majority of money services providers are legitimate businesses serving the legitimate financial needs of their customers. Regulators have also stated that international remittances, including those from domestic immigrant populations to their home countries, serve important and legitimate needs. Yet, on the other hand, regulators have identified international money transfers and cash-intensive businesses as raising heightened risks of money laundering, and money services businesses as a class are apparently still considered by some to be inherently high-risk entities. In addition, while the 2005 guidance states that banks are not expected to serve as *de facto* regulators of the money services business industry, the FFIEC BSA Examination Manual imposes risk-

based due diligence obligations on banks that are sufficiently ill-defined and open-ended as to lead banks to believe they are required to closely monitor all money services business accounts and effectively police the customers of their money services business accountholders.

Both banks and money services businesses are financial institutions for BSA purposes and both are independently subject to the full array of BSA requirements. There is simply no reason why one of those financial institutions – the bank – should be required to police the other financial institution's compliance with its independent BSA obligations. On the contrary, banks should be able to take comfort in and rely on the fact that their customer is a regulated entity subject to both BSA requirements and examination on the state and federal level. Indeed, the fact that money services businesses are regulated and subject to the BSA should be a factor that results in a lower risk rating and reduces or limits a bank's due diligence obligations accordingly. If banks are not allowed to rely on the fact that money services businesses are regulated and subject to the BSA to reduce their oversight obligations, then notwithstanding any statements to the contrary, they may well be justified in concluding that they are being asked to serve as *de facto* regulators of money services businesses.[5]

To remedy this problem, we recommend that additional interagency guidance be issued along the following lines:

- First, banks should be required to perform specifically defined due diligence when opening an account for a money services business. This should consist of obtaining evidence that the money services business is properly licensed and, if required, registered with FinCEN; basic information about the nature of the business and the expected activity in the account; and, if the bank deems necessary, confirmation that the money services business has an anti-money laundering program in place. With respect to the last item, the bank should not be required to assess the adequacy or quality of the anti-money laundering program or otherwise "audit" the money services business' internal controls or procedures. Otherwise, the bank is in effect being asked to serve as an examiner, a function it should not have to perform. Unless there are specific "red flags" – which must be something more than an inherent characteristic (such as providing international remittance services or dealing

[5] Western Union neither wants nor expects banks to supervise our business or our compliance with regulatory obligations. To the extent that regulators believe oversight of money services businesses needs to be strengthened or enhanced, they should deal with those issues directly through rulemaking, guidance, or the examination process.

in cash) of the money services business – this should satisfy the bank's due diligence obligations.

- Second, banks should only be required to monitor account activity to identify unusual or suspicious changes in the nature of such activity, such as a sudden and significant increase in the amount of money being deposited on a daily or weekly basis. A bank's monitoring obligation should be based on the type of information that will normally be available for such accounts, such as bulk deposits and payments activity. It should be made clear that banks are not required to "look through" the money services business and somehow monitor the transactions conducted by the business' customers.

- Third, banks should be given reasonable assurance that, if they satisfy these basic due diligence and monitoring obligations, they will not be held accountable should a customer of their money services business accountholder engage in money laundering or other illegal activity.

As was the case in 2005, this guidance should be issued jointly by FinCEN and the bank regulatory agencies, and it should be made clear that it supersedes anything in the FFIEC BSA Examination Manual that could be construed to the contrary. It is essential that the regulators speak with one voice on this issue, especially since the present problem stems in part from perceived differences among the agencies as to their views on this issue.

B. Give Banks Community Reinvestment Act Credit for Opening and Maintaining Accounts for Money Services Businesses

As previously stated, the Western Union agents who are being adversely impacted by the current situation are predominantly minority or ethnic owned businesses located in low and moderate income urban areas serving minority, ethnic and immigrant communities. We doubt that our experience in this regard is unique. In addition, FinCEN and other regulatory agencies have repeatedly acknowledged that money services businesses provide essential services to low and moderate income communities that have traditionally been underserved by banks. Since these are the very communities that the Community Reinvestment Act ("CRA") is designed to ensure receive banking services, we believe the federal bank regulatory agencies should explicitly recognize the provision of banking services to money services businesses as a qualified CRA activity. By so doing, they would send a clear message as to the value of such services and would give banks a significant incentive to provide them.

The federal bank regulatory agencies have already acknowledged that remittance services serve an important community need for many low and moderate income individuals, particularly those who use such services to send money to family members in other countries.[6] In recognition of this and to give banks an incentive to provide such services, the agencies recently interpreted the CRA regulations to permit favorable consideration of remittance services in a bank's CRA evaluation. Specifically, in addition to being a retail service under the regulations, international remittance services that increase access to financial services by low and moderate income persons now qualify as a community development service for CRA purposes.[7] In recognizing the importance of international remittances to this underserved community, the agencies have by definition recognized the importance to this same community of businesses that provide such remittance services. Giving banks CRA credit for opening and maintaining accounts for money services businesses is therefore a logical and appropriate extension of action already taken.

Extending CRA credit to banks that provide accounts for money services businesses may also be necessary to avoid discriminatory treatment among banks. As things currently stand, a bank that offers remittance services directly to low and moderate income persons may receive CRA credit for doing so. A bank that provides such services indirectly by offering accounts to money services businesses receives no such credit. Thus, even though both activities serve a distressed and underserved community, only one bank receives CRA credit. Moreover, it is most likely large banks that currently have the advantage since few small- or medium-sized banks offer remittance services. Finally, giving CRA credit only for the direct provision of remittance services could provide banks with a regulatory incentive to deny banking services to money services businesses and to instead market their own remittance services to those businesses' customers.

C. Allow Money Services Businesses to Maintain Accounts at Federal Reserve Banks

Currently, numerous money services businesses are being forced out of the business because of their inability to obtain new or replacement banking relationships. Others are having to endure significant hardships, including suspending operations, while seeking out a bank that is willing to take their account. In order to alleviate this crisis, we believe that action should be taken at the legislative and regulatory levels to allow money

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[6] See letter dated June 3, 2004, from Alan Greenspan, Donald E. Powell, John D. Hawke, Jr., and James E. Gilleran to The Honorable Barney Frank, located at www.ffiec.gov/cra/pdf/060304.pdf.

[7] See Community Reinvestment Act; Interagency Questions and Answers Regarding Community Reinvestment, 71 Fed.Reg. 12424 (March 10, 2006).

services businesses to open accounts directly with the Federal Reserve Banks. We believe such action is justified by present circumstances, particularly since the problem has arisen in large part because of the regulatory environment created by the federal banking agencies. Although we can understand why private banks might have competitive objections to Federal Reserve Banks providing banking services directly to money services businesses, private bankers cannot be allowed to refuse to provide banking services on the one hand and at the same time block money services businesses from obtaining those services from an alternative provider.

Precedent for the Federal Reserve Banks providing account services to non-members was established in the late 1970's when savings and loan associations, non-member banks and credit unions were allowed direct access to the Federal Reserve's account services. At that time, the infrastructure, including pricing and operating guidelines, was put in place to accommodate the provision of such services to non-members. That same infrastructure could be used immediately by the Federal Reserve to provide account services to money services businesses. In addition, because it is the primary federal regulator of state member banks, the Federal Reserve has the expertise in its examination division to review money services businesses applying for accounts for compliance with applicable BSA requirements. Furthermore, the Federal Reserve Banks and branches are located in virtually every major city in the United States. That network footprint ensures that those money services businesses most in need – namely, those in low and moderate income urban areas serving minority, ethnic and immigrant communities – are able to continue in business.

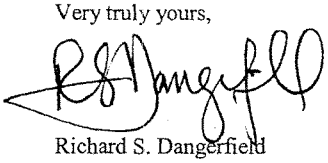
Depending on what other actions are taken and how successful they are in alleviating the current situation, this could be an interim solution. However, there is simply no justification for any money services business having to cease operations because it cannot obtain access to the banking system. Access to the Federal Reserve Banks would at least provide them with the safety net they currently need.

* * * * * * *

We appreciate the opportunity to provide our thoughts and recommendations on this critically important issue. We urge FinCEN and the bank regulatory agencies to take quick and effective action to ensure that money services businesses have access to the banking services they need to serve their communities. We look forward to continuing to

work with FinCEN on this issue and would be happy to answer any questions you may have regarding our comments.

Very truly yours,



Richard S. Dangerfield
Senior Counsel

cc: Honorable Wayne Allard
Honorable Spencer Bachus
Honorable Robert Bennett
Honorable Luis Gutierrez
Honorable Chuck Hagel
Honorable Tim Johnson
Honorable Sue Kelly
Honorable Carolyn Maloney
Honorable Ben Nelson
Honorable Ken Salazar

Randall S. James
Commissioner
Texas Banking Department

Diana L. Taylor
Superintendent of Banks
State of New York Banking Department

Brian Yuen
Acting Commissioner
California Department of Financial Institutions

J. Philip Goddard
President
Money Transmitter Regulators Association

Western Union cc:

Joseph Cachey III
Senior Vice President
AML Compliance, External Partnerships and Leadership

Susan Roser
Senior Vice President
AML Global Operations

David Schlapbach
General Counsel

Mark A. Thompson
Associate General Counsel

Revised Interagency Interpretive Guidance on Providing Banking Services to Money Services Businesses Operating in the United States

On April 25, 2005, the Financial Crimes Enforcement Network ("FinCEN"), along with the Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, the National Credit Union Administration, Office of the Controller of the Currency and Office of Thrift Supervision ("Federal Banking Agencies") issued interpretative guidance to clarify further the requirements of the Bank Secrecy Act and its implementing regulations (including the parallel provisions issued by the Federal Banking Agencies) to banks when providing account services to Money Services Businesses ("MSBs") operating in the United States.

The goal of the prior interpretive release was to confirm "that banking organizations have the flexibility to provide services to a wide range of money services businesses while remaining in compliance with the Bank Secrecy Act." In short, banks were told that they "will not be held responsible for their customer's compliance with the BSA and other federal and state laws and regulations."

Notwithstanding the intent of FinCEN and the Federal Banking Agencies, there is significant evidence both anecdotal and documented in submissions to FinCEN in response to the Advance Notice of Proposed Rulemaking, that the April 26, 2005 Interagency Interpretive Guidance did not have the desired result of easing bank concerns with regard to the level of scrutiny and responsibility imposed on a bank in opening or maintaining an account for an MSB. In fact, there is some indication that the articulation

of "due diligence for high risk customers" set forth in the interpretive guidance was read by some regulators and banks as constituting the imposition of more stringent obligations on banks with regard to MSB customers. As a result of this apparent confusion since the issuance of the Interagency Interpretive Guidance more than a year ago, there are no reported instances of banks resuming services for MSBs they had terminated, and both national and regional banks have canceled accounts of MSBs at an accelerated rate. The cancellations have occurred nationwide and threaten the viability of the MSB industry.

Clearly, it was not the intent of FinCEN and the Federal Banking Agencies to hasten the closure of MSB bank accounts. As emphasized in numerous public releases of the Treasury Department, MSBs provide essential financial services to the public and the widespread discontinuance of the availability of these services inevitably will lead to the migration of funds to the underground. Such a prospect is contrary to the national interest and undercuts government efforts to curb terrorist financing and stem money laundering.

Therefore, since the Interagency Interpretive Guidance has not had the desired effect, FinCEN and the Federal Banking Agencies are issuing this further interpretive clarification designed to provide clear guidance to banks, MSBs and the banking regulators that **banks need not undertake special compliance procedures with regard to MSB accounts**.

Therefore, in case there is any doubt from the prior guidance, banks should take the following steps with regard to MSB accounts:

1. NEW MSB ACCOUNTS -- Banks should perform the following due diligence when opening new MSB accounts:

    - Obtain evidence that the MSB is licensed if required in that state or verification that it operates as an agent for a licensed MSB.

    - Obtain evidence that the MSB is registered, if necessary, with FinCEN.

    - Obtain information about the nature of the MSB's business and expected activity.

    - Confirm that the MSB has an AML compliance program. **NOTE: The bank is not required to assess the adequacy or quality of the MSB's anti-money laundering program or "audit" or "examine" the quality of the MSB's internal AML controls and procedures.**

2. EXISTING MSB ACCOUNTS -- With regard to established accounts, banks are required only to monitor unusual or suspicious activity and changes in the nature of such activity. **NOTE: Banks are not responsible to review the MSB's customers' activities and/or monitor the transactions conducted by the MSB's customers.**

In sum, it is the intention of FinCEN and the Federal Banking Agencies that banks are not under an obligation to police the activities of the customers of their MSB account holders. Likewise, if banks perform the steps above referenced, and notwithstanding anything to the contrary in the prior interpretive guidance or in the FFIEC Bank Secrecy Act Anti-Money Laundering Examination Manual, banks will satisfy their obligations under the Bank Secrecy Act in opening or maintaining MSB accounts.

Comptroller of the Currency
Administrator of National Banks

Washington, DC 20219

August 14, 2006

The Honorable Spencer Bachus
Chairman
Subcommittee on Financial Institutions and Consumer Credit
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20515

Dear Chairman Bachus:

Thank you for allowing me to testify on behalf of the Office of the Comptroller of the Currency at the Subcommittee's hearing entitled "Bank Secrecy Act's Impact on Money Services Businesses" on June 21, 2006. During the hearing, you asked me to provide information on criminal cases involving money services businesses (MSBs).

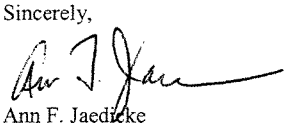
The only case against a national bank involving its MSB business that we are aware of was brought by the U.S. Attorney for the District of Maryland in October 2003 against Delta National Bank and Trust Company, which has its principal office in New York City (Delta). Delta ultimately paid a $950,000 criminal fine and pled guilty to a criminal information charging it with one count of failure to file a Suspicious Activity Report in connection with a customer's foreign currency exchange business that involved two accounts at the bank.

While we did not conduct a comprehensive review of criminal cases involving financial institutions and their MSB customers, we are aware of certain other cases involving banks that we do not regulate. For example, in March 2004, Hudson United Bank, a state chartered bank that has its principal office in Mahwah, New Jersey, agreed to a $5 million fine to settle accusations by the Manhattan District Attorney's Office that one of its New York City branches failed to monitor certain accounts held for foreign, non-bank financial institutions, such as off-shore money remitters, casas de cambio, and black market currency dealers doing business in South America, as required by the Bank Secrecy Act (BSA). More recently, in April 2006, BankAtlantic, a savings association located in Fort Lauderdale, Florida, signed a deferred prosecution agreement and forfeited $10 million to the U.S. Department of Justice for criminally violating the BSA. According to press reports, BankAtlantic chose to close all of its MSB accounts to ward off risks in 2002; however, the account manager for these MSB accounts

opened new accounts for those clients under different names and they were used to launder drug proceeds.

I hope this information is helpful to the Subcommittee. Please do not hesitate to contact me if we can be of further assistance.

Sincerely,



Ann F. Jaedicke
Deputy Comptroller for Compliance

Office of the Comptroller of the Currency **Quarterly Journal**
2006 OCC QJ LEXIS 4; 25-1 O.C.C. Q.J. 37

March, 2006

[*1] APPEALS PROCESS

Appeal 1: Of Composite and Component Ratings

TEXT:

Background

The bank's board of directors appealed the downgrade of its overall composite rating and the component ratings for consumer compliance, asset quality, and management. The bank had an overall composite rating of 1 for the last five examinations until the most recent examination when a 2 composite rating was assigned. The board was of the opinion that had the three component ratings been properly rated, a 1 composite rating would have been assigned.

The appeal states that management disagreed with the downgrade in the consumer compliance rating, because they believed the compliance program was sound and there had been no change from the previous examination. The Report of Examination (ROE) noted that the compliance program was satisfactory and stated a bank with a 2 rating is generally in a strong compliance position. It further stated that risk management systems were satisfactory and management responds promptly to audit and regulatory concerns. The ROE notes management plans to implement enhancements to internal controls in response to the OCC's 2004 Fair Lending examination and Bank Secrecy Act weaknesses. **[*2]** These issues were identified internally and confirmed by OCC examiners.

Management disagreed with the asset quality rating of 2 as they believed that asset quality remains strong as evidenced by the low level of classified assets, historical losses, past dues, and nonaccruals. The supervisory office stated that the downgrade in the asset quality rating was attributed to identified weaknesses in risk management practices in the commercial real estate (CRE) portfolio. Specifically, the weaknesses included portfolio and concentration management and reporting, market analysis, appraisal processes, policy exception reporting, and the allowance for loan and lease losses (ALLL). The overall level of risk had increased significantly from the prior examination without a commensurate improvement in risk management practices. Several of these weaknesses were noted at the previous examination.

Management disagreed with the management rating of 2 since they believed the downgrade was the result of the lack of credit risk management processes and weaknesses noted in their trust area. Management believed that the due diligence it performed on the group of trust accounts was adequate. Furthermore, **[*3]** they believed that the supervisory office was overly critical of

management's slower-than-expected development of loan concentration reports, analyses, and policies.

The supervisory office stated the downgrade was because of risk management practices lagging behind the bank's substantial growth and change in the loan mix and the lack of due diligence over a group of new trust accounts. Violations of law were noted related to the oversight of these trust accounts.

Management disagreed with the downgrade of the composite rating to 2, because they believed that, if the compliance, asset quality, and management ratings had been appropriately assigned a 1 rating, then this would have resulted in a 1 composite rating. The supervisory office stated that the downgrade was reflective of a higher risk profile, increased leverage, higher concentrations in the loan portfolio, and the need to strengthen credit risk management practices.

Discussion and Conclusion

The **ombudsman** conducted a review of the information submitted by the bank and supporting documentation from the supervisory office. The review included meetings with the bank's senior management team as well as with members**[*4]** of the supervisory office.

The **ombudsman** ruled that the conclusion reached by the supervisory office regarding asset quality was appropriate and well supported by the facts at the time of the examination. The ROE and other OCC communications with the bank outlined concerns with the bank's approach to managing and monitoring real estate-related concentrations in the loan portfolio. While the **ombudsman** agreed with management's quantitative assessment on asset quality, the overall level of risk had increased from the previous examination without a commensurate improvement in risk management practices. The **ombudsman** was particularly concerned with the board's and management's approach to managing and monitoring concentrations in the lending portfolio.

The **ombudsman** ruled that the conclusions reached by the supervisory office regarding consumer compliance and management were more reflective of a 1 rating. The **ombudsman** noted the existence of a strong compliance management program including an efficient system of internal controls. Bank management demonstrated that it understands and is committed to all aspects of compliance risk management. While the ROE did identify areas needing **[*5]** improvement in the compliance area, these can be addressed in the normal course of business and do not materially detract from the overall quality of the compliance program. Furthermore, the bank has a history of substantial compliance with laws and regulations.

The **ombudsman** noted that the board and management have demonstrated the ability to effectively administer the bank's affairs. This is evident in the strong audit and compliance culture, strong internal control structure, good historical financial performance, and management's depth and knowledge to plan and respond to risks as changes in business conditions occur. While the bank needs to strengthen the credit risk management processes recommended by the OCC supervisory office, the **ombudsman** believes management has demonstrated over multiple business cycles the ability to implement the needed controls during the normal course of business. Based on these

factors, the **ombudsman** concluded that a 1 rating is more reflective of the management component.

Finally, the **ombudsman** agreed with the concerns raised by the supervisory office, that the higher risk profile, increased leverage, higher concentrations in the loan portfolio, **[*6]** and the need to strengthen credit risk management practices support the assigned 2 composite rating. Additionally, the bank's low risk-based capital level at the time of the examination and the low ALLL provides little flexibility to handle unforeseen losses of substance.

Office of the Comptroller of the Currency **Quarterly Journal**
2006 OCC QJ LEXIS 5; 25-1 O.C.C. Q.J. 39

March, 2006

[*1] APPEALS PROCESS

Appeal 2: Of Composite and Component Ratings

TEXT:

Background

The bank's board of directors appealed the overall composite, capital, and management ratings. A downgrade to a 3 rating was assigned to the composite and capital components. There was no change to the management rating of 3; however, the board believed that based on projected strategic growth and profitability goals, an upgrade to a 2 was warranted. Additionally, the informal Memorandum of Understanding (MOU) issued as a result of the Report of Examination was appealed.

The board disagreed with the assigned capital rating of 3, because the bank had maintained capital above the regulatory minimum level. According to management, the bank's capital level either improved or stayed the same since the previous examination and contended that it was in full compliance with a strategic plan previously submitted to the OCC. Furthermore, management stated that the bank's principal shareholder had demonstrated the capacity to support the bank's capital needs. The supervisory office stated that the downgrade was because of declining capital ratios and the lack of a formal capital plan. Additionally, the supervisory**[*2]** office was concerned with the overall weak earnings trend and that the bank would need a capital injection by year-end 2005.

The board disagreed with the assigned management rating of 3 based on the implementation of their strategic plan. Management stated that the strategic plan was not fully implemented and that the bank had a demonstrated capacity for future growth. Additionally, core earnings were improving rapidly with potential improvement in profitability as the strategic plan continued to be implemented. The supervisory office stated that the key factor in rating management a 3 was the failure of the board and management to ensure that appropriate risk management processes were maintained over the lending area. The supervisory office believed that the bank's rapid loan growth, coupled with weak credit risk management, low capital, and weak earnings posed a high potential for future problems. Subsequent to the examination, the board replaced the president and senior credit administrator in an effort to improve credit administration and overall bank management.

The board disagreed with the composite rating, but provided little support as to why the rating was in error. Management**[*3]** stated that the condition of the bank had not deteriorated from the previous year, but instead had improved dramatically in all key areas. The supervisory office stated

that the composite 3 rating was assigned because of a combination of weaknesses in management, capital, and earnings.

The board appealed the MOU, but did not provide support as to what provisions of the MOU it believed were inappropriate. The supervisory office stated that it believed the MOU was appropriate to aid the bank in addressing its long history of weak management, poor financial performance, and weak credit risk management processes. Consideration was given to the fact that the present level of problem assets was not severe and the bank's principal shareholder had a history of providing financial support.

Discussion

The **ombudsman** conducted a review of the information submitted by the bank and supporting documentation from the supervisory office. The review included discussions with the bank's senior management team as well as with members of the supervisory office.

The **ombudsman** concurred with the supervisory office's conclusions of the bank's weak financial and managerial deficiencies existing**[*4]** at the time of the examination. While certain aspects of the bank's operations appear to have stabilized, overall financial performance was less than satisfactory. The bank's total asset growth had been erratic and earnings performance had been weak to nonexistent. Tier 1 leverage capital declined from a high of 10.09 percent at year-end 2000 to 6.85 percent at year-end 2004. While asset quality remained satisfactory, credit risk management practices warranted improvement.

Although the earnings rating was upgraded from a 4 to a 3, the **ombudsman** concluded that earnings from core operations were insufficient to support planned asset growth and augment capital. While nonrecurring items had affected the quantity of earnings, the quality of earnings as the primary source to support future operations was impaired by the bank's below-average net interest margin. Capital levels were insufficient without the capital injections by the principal shareholder.

Conclusion

In conclusion, the **ombudsman** concluded that the composite rating of 3 assigned at the examination was appropriate and complies with the factors provided in the Uniform Financial Institutions Rating System (UFIRS), (OCC**[*5]** Bulletin 97-1, "Uniform Financial Institutions Rating System and Disclosure of Component Ratings," January 3, 1997). The **ombudsman** also concluded that the ratings for capital, earnings, and management were appropriate as assigned. Additionally, the **ombudsman** ruled that the MOU entered into between the board of directors and the OCC was reasonable and in the best interest of the bank.

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 64; 24-3 O.C.C. Q.J. 31

September, 2005

[*1] APPEALS PROCESS

Appeal 1--Appeal of Semiannual Assessment Fee

TEXT:

Background

A bank formally appealed the OCC's right to retain the full semiannual assessment fee for the period of January 1 through June 30 since the bank converted to a state chartered commercial bank on January 1.

Discussion

The bank requested a full refund of its semiannual assessment because the supervisory responsibility shifted from the OCC to the state on January 1 and therefore no supervisory activities would be conducted by the OCC during the period covered by the assessment.

The **ombudsman** reviewed OCC regulations regarding payment of semiannual assessment fees. According to paragraph (5) under section (a) of 12 CFR 8 Assessment of Fees, "Each bank subject to the jurisdiction of the Comptroller of the Currency on the date of the second or fourth quarterly Call Report required by the OCC under *12 USC 161* is subject to the full assessment for the next six-month period." The OCC assessment is levied against all institutions that are in the national banking system as of December 31st and June 30th. Therefore, any bank that is a national bank on the assessment date**[*2]** is required to pay the full semiannual assessment for the upcoming six-month period.

Conclusion

After careful review of OCC regulations, and finding no basis for an exception, the **ombudsman** determined that no refund was due to the bank.

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 65; 24-3 O.C.C. Q.J. 31

September, 2005

[*1] APPEALS PROCESS

Appeal 2--Appeal of Composite and Component Ratings

TEXT:

Background

The bank's board of directors appealed the downgrade to a 3 of its overall composite rating and the component ratings for asset quality, management, and consumer compliance. Additionally, the board appealed the violations of law of the legal lending limit. The bank was placed under a formal agreement prior to filing the appeal.

Discussion

The appeal states that the report of examination (ROE) contains unfounded allegations regarding the bank's relationship with a third-party subprime mortgage vendor, which resulted in unsatisfactory ratings in asset quality, management, and consumer compliance. Furthermore, the board stated that the legal lending limit violations were based on the manner in which the lending program operated as opposed to the written agreements between the subprime mortgage vendor and the bank.

According to the appeal, even when considering the subprime nature of the mortgage loan portfolio, the bank had not experienced losses as a result of its relationship with the subprime mortgage vendor. Bank management stated that the supervisory office was advised of the bank's interest**[*2]** in purchasing participations from the subprime mortgage vendor and raised no objections. Management questioned the OCC's decision to pursue an administrative action, including civil money penalties, after the bank decided to wind down its participation with the subprime mortgage vendor. The appeal also stated that the component ratings that were downgraded in this examination had been assigned satisfactory ratings only four months prior. Finally, the appeal states that the bank has not done anything wrong, much less illegal, predatory or abusive, in its relationship with the subprime mortgage vendor.

The supervisory office stated that bank management failed to provide adequate oversight of its relationship with the subprime mortgage vendor. The lack of policies and procedures for the subprime mortgage portfolio, poor loan administration and risk management practices coupled with the predatory nature of the portfolio, exposed the bank to increased reputation and financial risk. Loan officers responsible for the subprime mortgage portfolio lacked the knowledge necessary to identify violations of law and regulation in the portfolio. This indicated a lack of proper training over consumer**[*3]** laws and regulations along with weak internal controls. Based on the

weaknesses noted in the areas of credit, risk management, and consumer compliance, including the resulting violations of law, management and board supervision were considered weak.

Conclusion

The **ombudsman** conducted a review of the information submitted by the bank and support documentation from the supervisory office. The review included meetings with the bank's senior management and legal counsel, as well as with members of the supervisory office.

Because the bank was operating under an enforcement action, the **ombudsman's** review was limited to a determination of reasonableness as defined in OCC Bulletin 2002-9, "National Bank Appeals Process," (February 25, 2002). Essentially, the **ombudsman** used a process similar to that of a federal appeals judge versus the de-novo review process that is customarily employed on non-enforcement-related appellate matters. Therefore, the review focused on whether the ratings were reasonable as assigned based on the condition of the bank at the time of the examination. Additionally, the violations of law were deemed to be outside of the scope of the appeal.

The **ombudsman [*4]** ruled that the conclusions reached by the supervisory office regarding asset quality, management, and consumer compliance were reasonable and well supported by the facts at the time of the examination. Additionally, the overall condition of the bank met the criteria of a composite-3-rated bank as prescribed by the Uniform Financial Institutions Rating System (UFIRS), (OCC Bulletin 97-1, "Uniform Financial Institutions Rating System and Disclosure of Component Ratings," January 3, 1997).

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 66; 24-3 O.C.C. Q.J. 33

September, 2005

[*1] APPEALS PROCESS

Appeal 3--Appeal of the Composite and Certain Component Ratings

TEXT:

Background

A bank, operating under a formal agreement, appealed the composite and component ratings for capital, asset quality, management, earnings, and liquidity assigned at the most recent examination.

Discussion

The bank's board of directors appealed the conclusions noted in the most recent safety and soundness examination that resulted in the downgrade of the bank's composite rating from 2 to 4. According to the appeal, the primary cause of the criticisms noted in the report of examination (ROE) can be traced to a former senior loan officer and were not reflective of overall bank supervision. The appeal further states that the downgrades for capital, asset quality, management, earnings, and liquidity were primarily based upon the perception that classified assets were increasing, and this increase would cause net losses and liquidity issues. Since the examination, the board believes that management has improved asset quality problems, created an adequate allowance for loan and lease losses, collected a significant amount of classified assets, and implemented proper policies and procedures**[*2]** in the lending area. Consequently, the perceived negative impact on capital, earnings, and liquidity did not materialize. Therefore, the board believes the composite, capital, asset quality, management, and earnings ratings each merit a 3 and liquidity should be rated 2.

The supervisory office response notes that the appeal discusses actions taken by the board post-examination but does not refute findings noted during the examination. As such, conclusions cited in the ROE are a valid representation of the bank's condition at that time. Asset quality was deemed unacceptable and credit risks were high. The board had failed to implement adequate procedures to prevent insider abuse and to implement an effective risk management system. Earnings performance was poor; loan losses and increased provision expenses led to net losses for the year and the current quarter. These factors as well as an increasing overall risk profile had an impact on capital adequacy. The diminishing level of secondary funding sources also affected liquidity. The supervisory office restated its position that the assigned composite of 4 and component ratings of 4, 4, 4, 4, and 3 for capital, asset quality, management, **[*3]** earnings, and liquidity, respectively, met the criteria in the Uniform Financial Institutions Ratings System (UFIRS).

Conclusion

The **ombudsman** reviewed the bank's submission as well as information supplied by the supervisory office. Because the bank was operating under an enforcement action, the **ombudsman's** review was limited to a determination of reasonableness as defined in OCC Bulletin 2002-9, "National Bank Appeals Process." Essentially, the **ombudsman** used a process similar to that of a federal appeals judge versus the de-novo review process that is customarily employed on non-enforcement-related appellate matters. Therefore, the review focused on whether the ratings were reasonable as assigned based on the condition of the bank at the time of the examination.

The **ombudsman** opined that the conclusions reached by the supervisory office were reasonable, well supported by the facts at the time of the examination, and met the definition of a composite 4 bank as prescribed by UFIRS. The **ombudsman** also found that the assigned component ratings for capital, asset quality, management, earnings, and liquidity were reasonable and accurately reflected the bank's condition at the**[*4]** time of the examination.

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 41; 24-2 O.C.C. Q.J. 37

June, 2005

[*1] APPEALS PROCESS

Appeal of the Composite CAMELSI Rating

TEXT:

Background

A bank formally appealed the composite CAMELSI (capital, asset quality, management, earnings, liquidity, sensitivity to market risk, and information technology) rating of 3 assigned at the most recent examination and asked the **ombudsman** to restore the composite rating to 2.

Discussion

The basis of the appeal is the most recent safety and soundness examination in which the bank's composite rating was downgraded from 2 to 3. The bank did not dispute all of the examination conclusions and stated that the primary conflict with the supervisory office was the difference in computing the impact of a 3-percent shock to the agency step-up bonds held in its portfolio. According to the appeal, the supervisory office's computations did not consider the step-up features and thus produced an unfavorable result regarding earnings at risk and interest rate risk (IRR) management. The appeal further states that the bank's computations were done by Bloomberg, resulting in a more favorable outcome than those produced by the supervisory office.

The supervisory office stated that the board of directors was advised, as far **[*2]**back as 1998, about the need to improve its IRR management systems and controls. The supervisory office further stated that neither management nor the board demonstrated sufficient knowledge of step-up bond features and the impact to earnings at risk. As such, this made it difficult for them to assess the aggregate level of IRR. Additionally, weak earnings performance and deficiencies in risk management of information technology also factored into the composite downgrade.

Conclusion

The **ombudsman** acknowledged that the bank's risk exposure resulting from a 3-percent shock to the agency step-up bonds, as computed by the supervisory office and Bloomberg, was not an absolute. However, the bank's risk management processes relative to IRR did not provide management with the assurances that it could withstand significant fluctuations associated with this product. Additionally, the **ombudsman's** review noted a combination of weaknesses in the areas of IRR and information technology that reflected a need for enhanced supervision by the board and management.

The **ombudsman** opined that the conclusions reached by the supervisory office were well supported by the facts at the time of the**[*3]** examination and met the definition of a composite 3 bank as prescribed by the Uniform Financial Institutions Rating System.

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 5; 24-1 O.C.C. Q.J. 73

March, 2005

[*1] APPEALS PROCESS

Appeal 1--Appeal of a Shared National Credit

TEXT:

Background

A bank appealed to the **ombudsman** a decision rendered by the Shared National Credit (SNC) Interagency Appeals Panel in July 2004. Initially, the SNC review team rated as substandard and nonaccrual two priority lien credit facilities secured by an assignment in an equity interest in the assets of two bankrupt commercial projects. Additionally, there was a guaranty from the parent company for an equity commitment to complete construction of the projects. The bank appealed the nonaccrual designation on both facilities to the SNC appeals panel. The SNC appeals panel determined that the bankrupt projects, including the priority lien credit facilities should be classified as "other assets," and the remaining unsecured portions of debt classified as loss.

The bank agreed with the classification of the affected credits as "other assets," however, it disagreed with the loss classification, and submitted an appeal to the **ombudsman.** According to the appeal, the bankruptcy documents supported that there were assets available to provide some relief to the unsecured creditors. The bank further cited inconsistent treatment**[*2]** among the SNC review teams in the classification of these credit facilities at other banks. Specifically, there were two other agent banks designated as unsecured creditors by the bankruptcy court, yet the SNC review teams at those banks gave value to varying degrees the underlying assets supporting the bankruptcy claims.

Management's view was that since the unsecured facilities would be treated equally in bankruptcy, they should be treated similarly in the SNC evaluation process. The fair value of the underlying assets should include value given to the bankruptcy claim on the underlying assets.

Discussion

In December 2002, the lender groups assumed effective control of the two projects by replacing management, obtaining the rights to sell the projects, and actively marketing the plants for sale. (The guarantor for equity to finish these projects had previously experienced severe financial difficulties, abandoned support of the projects, and filed for bankruptcy protection.) Consequently, both the primary and secondary repayment sources were in jeopardy.

The appeal states that the bankruptcy court has recognized the obligations of the guarantor, and they are subject to[*3] claim by the unsecured creditors. The appeal also states that there is a secondary market for these bankruptcy claims that precludes a full loss classification.

The **ombudsman** reviewed the information submitted by the bank and held discussions with the bank's senior management team, the SNC review team, the SNC appeals panel and OCC accountants. While sufficient information was provided for the **ombudsman** to render a decision as to the fair value to be assigned to the underlying assets of the bankrupt guarantor, doing so would not resolve the issue of inconsistent treatment among the banks holding similar bankruptcy claims. Therefore, the **ombudsman** determined that the best course of action was to convene a new SNC review team consisting of a representative from each of the primary federal agencies to make a classification decision applicable to the banking groups.

Conclusion

The new SNC interagency review team was convened in November 2004. In the time period between the initial SNC review and the review by the new SNC interagency review team, the guarantor emerged from bankruptcy and the lending group signed contracts for the disposition of assets. Consequently, the credits[*4] were reviewed in November 2004, based on this later information rather than the bankruptcy status at the time of the initial review, which would be the traditional approach employed in the appellate arena.

The SNC interagency review team concluded that credit factors were substantively unchanged from when the guarantor originally filed for bankruptcy, and insufficient to maintain carrying the exposed portions of the facilities dependent on its guaranty in the active loan portfolio.

Critical to this evaluation is the determination of whether the obligation under this guaranty was, and should remain, a "bankable asset" (as referred to in the interagency definition of loss n1). This does not mean the obligation has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off a basically worthless asset even though partial recovery may result in the future. In this assessment, credit factors should be present that provide assurances that the obligation is reasonably well secured and if not, at least in process for full collection with imminent closure expected. These are necessarily high standards because the obligor is in default [*5] and under the control of the bankruptcy court. The claim is unsecured, and the lenders were not entitled to adequate protection payments or any other regular distribution from the bankruptcy estate that might be considered interest income. The total unsecured claims against the bankruptcy estate, of which the bank group was a part of, substantially exceed estimated recoverable amounts from a potential sale of the operating assets of the guarantor. These factors do not provide adequate support for the bank group's portion of these claims to remain indefinitely in the active portfolio, even when charged down to estimated recoverable amounts. The foreseeable events, since the guarantor filed for bankruptcy, held considerable uncertainties for those estimated recoverable amounts, and their unfolding in recent months does not obscure the fact that collection efforts were best characterized as recovery.

n1 Interagency definition of loss: "Assets classified loss are considered uncollectible and of such little value that their continuance as bankable assets is not warranted. This classification does not mean that the asset has absolutely no recovery or salvage value, but rather that it is not practical or desirable to defer writing off this basically worthless asset even though partial recovery may be effected in the future."

[*6]
Thus, the classifications of the assignment of the equity interest in the commercial properties as "other assets" were upheld. Any remaining balance was deemed a recovery matter and directed to be charged off. However, since collection efforts were already in process, the banks were allowed to charge-off the losses consistent with the closing of the sales contracts scheduled for the upcoming quarter following this review. This decision was confirmed by the **ombudsman** and applied unilaterally to all banking groups.

Office of the Comptroller of the Currency **Quarterly Journal**
2005 OCC QJ LEXIS 6; 24-1 O.C.C. Q.J. 75

March, 2005

[*1] APPEALS PROCESS

Appeal 2--Appeal of Partial Assessment Fee

TEXT:

Background

A bank appealed to the **ombudsman** for a partial refund of its semi-annual assessment fee. The bank originally appealed to its supervisory office and was denied.

Discussion

The bank converted to a federal savings bank three months after paying its semi-annual assessment fee. According to the appeal, since the bank was no longer under the supervision of the OCC, it was entitled to a refund of the remaining assessment. The appeal included documentation to support the amount of payment made by the bank to the OCC for the six-month period.

Conclusion

The **ombudsman** reviewed the documentation submitted by the bank and OCC policies and procedures regarding payment of semi-annual assessment fees. According to paragraph (5) under section (a) of 12 CFR 8 Assessment of Fees, "Each bank subject to the jurisdiction of the Comptroller of the Currency on the date of the second or fourth quarterly Call Report required by the Office under *12 USC 161* is subject to the full assessment for the next six-month period." The OCC assessment is levied against all institutions that **[*2]** are in the national banking system as of December 31 and June 30. Therefore any bank that is a national bank on the assessment date is required to pay the full semi-annual assessment. Additionally, the Notice of Fees issued to all national banks on December 1, 2000, provided notification that the OCC planned to discontinue prorated refunds for institutions that leave the national banking system part way through an assessment period. This policy became effective as of January 1, 2001. Since the bank was a national bank on the date that the assessment was levied, the **ombudsman** opined that no partial refund was warranted.