

Testimony of

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On Behalf of the

AMERICAN BANKERS ASSOCIATION

Before the

House Financial Services Subcommittee on Oversight and Investigations

On

Progress Since 9/11: The Effectiveness of U.S. Anti-Terrorist Financing Efforts

March 11, 2003



Madam Chairman and members of the Subcommittee, I am John Byrne, Senior Counsel and Compliance Manager with the American Bankers Association. The American Bankers Association appreciates this opportunity to discuss the myriad of challenges faced by the financial industry in addressing the scourge of terrorist financing.

The ABA 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. For further information regarding the ABA, please consult the ABA on the Internet at <http://www.aba.com>.

Seventeen months after the enactment of the USA Patriot Act, the effect of these new laws and regulations on terrorist financing and money laundering is still being assessed. ABA was particularly pleased to learn of the Treasury Department's commitment to continue to provide oversight in this area after the regulations have been finalized. More importantly, then Acting Secretary Kenneth Dam told Congress that:

Time and experience will allow reasoned reflection on the decisions we have made, and it is incumbent upon Treasury to make adjustments to these rules when it is necessary to ensure that they continue to achieve our goals.

The ABA has also been involved in “reasoned reflection” on the plethora of obligations facing our industry since October 26, 2001. As with any omnibus piece of legislation, time and experience produce evidence of the need for modifications to the law as well as recommendations of how to more efficiently implement statutory mandates. ABA has provided comments to the Treasury in this area and our views have been well received. We are also pleased that the Treasury and the regulators are addressing several of our previous recommendations.

Our Association has offered the following as needed areas of improvement to USA Patriot Act oversight.

ABA recommends:

- Creating an office for USA PATRIOT Act oversight;
- Immediate development of a Staff Commentary for Patriot Act and Bank Secrecy Act interpretation;
- Review of the 314 Demands for Record Searches
- Formal commitment from **all** functional regulators for uniform and consistent Patriot Act exam procedures;
- Coordination between the Treasury's Office of Foreign Assets Control (OFAC) and the financial institution regulators to improve advice to the regulated community; and

- Improved guidance and communication on all SAR related issues, particularly in the area of terrorist financing.

Office of USA Patriot Act Oversight

One of the major aspects of the USA Patriot Act is the broad-based coverage of the law on the vast array of financial services providers. While members of the American Bankers Association have long experienced the challenges accompanying compliance obligations with the Bank Secrecy Act, the federal money laundering laws and now the USA Patriot Act, the non-bank entities now subjected to these obligations are experiencing the same confusion we have faced. To assist this diverse group, we have advocated that the Treasury Department create a formal mechanism for responding to questions concerning interpretation of these obligations. ABA has recommended that there be an office within the Treasury to communicate guidance, interpretations and FAQs regarding all Patriot Act questions.

Representatives from all of the regulatory agencies could staff this office along with Treasury personnel. The key ingredient to success is a central location for industry questions to ensure consistency and assist in compliance. We would point out, Madam Chairman, that there have been several recent organizational changes that are moving toward this important direction.

For example, the announcement last week by the Treasury to create an “Executive Office for Terrorist Financing and Financial Crimes” is a welcome addition to the government’s efforts in this area. According to the announcement, this office will “participate in the department’s development and implementation of U.S. government policies and regulations in support of the PATRIOT Act, including outreach to the private sector...” ABA supports the creation of this office and the fact that it will provide “policy guidance” to both FinCEN and OFAC.

In addition, it should be noted that the Financial Crimes Enforcement Network (FinCEN) created a “hotline” immediately after 9/11 for the public to use when reporting potential “terrorist financing,” so we know that the government is capable of putting such a process in place.¹

Patriot Act and Bank Secrecy Act Staff Commentary

The American Bankers Association has long bemoaned the fact that the Treasury Department has never fulfilled the 1994 statutory mandate that it publish an annual staff commentary on the Bank Secrecy Act regulations (Section 5329). This indifference to congressional direction has contributed to industry confusion, examination conflicts and inconsistent interpretation of Bank Secrecy Act obligations.

There is broad support for a method of providing Patriot Act interpretations to the financial sector. As stated above, ABA believes that a centralized approach to industry questions is necessary and, for

¹ According to FinCEN’s website at the time, “This HOTLINE is intended to provide to law enforcement and other authorized recipients of SAR information the essence of the suspicious activity in an expedited fashion.” If the government can work quickly to develop a system for when it wants information from the public, it should be able to address the need for industry assistance in the same prompt manner.

BSA issues, long overdue. Unfortunately, the recent attempts by FinCEN to publish guidance on BSA issues, while laudable, has lacked agency input and is not communicated effectively.² Given the Treasury's stated commitment to remaining engaged in Patriot Act oversight, we urge that now is the time to announce and implement a formal annual staff commentary.

Section 314 Demands for Record Searches

There is no better example of a positive public policy goal not being met than the implementation of section 314 of USA Patriot Act. While we recognize that government is faced with tremendous challenges to track terrorist funds, section 314 warrants a thorough review to ensure consistency with both congressional intent and the need to establish a workable system.

According to the Senate Report addressing the relevant part of this section:

Section 314 requires the Secretary of the Treasury to issue regulations, within 120 days of the date of enactment, to encourage cooperation among financial institutions, financial regulators and law enforcement officials, and to permit the sharing of information by law enforcement and regulatory authorities with such institutions regarding persons reasonably suspected, based on credible evidence, of engaging in terrorist acts or money laundering activities. Section 314 also allows (with notice to the Secretary of the Treasury) the sharing of information among banks involving possible terrorist or money laundering activity, and requires the Secretary of the Treasury to publish, at least semiannually, a report containing a detailed analysis of patterns of suspicious activity and other appropriate investigative insights derived from suspicious activity reports and law enforcement investigations.³

Then Ranking Minority Member of the Senate Banking Committee. Phil Gramm (R-TX) pointed out, on October 16, 2001 that Section 314:

“Add[s] a requirement that the government help banks focus on up-to-date money-laundering threats by sharing with banks specific money-laundering concerns, enabling institutions to know what to be on the lookout for. This is expected to result in better enforcement and cooperation, *while reducing the burden of unnecessary paper chases* (emphasis added). The amendment would also permit financial institutions to share with each other relevant information about suspected money-laundering activities.”

Congress has obviously directed the Treasury to craft a rule that will facilitate information sharing for the purpose of combating terrorism and money laundering. The final rule, for the reasons expressed below, does not meet that directive.

² A recent example bears this out. On November 2, 2002 the Financial Crimes Enforcement Network posted an interpretation to 103.29 of the Bank Secrecy Act. The interpretation, that institutions are required to comply with certain record keeping provisions regarding monetary instrument purchases, is contrary to a September 2000 statement from the Bank Secrecy Act examination procedures of the Office of the Comptroller of the Currency that “formal records as required by 31 CFR 103.29 are not necessary” under the same circumstances. Neither the OCC nor any of the examining agencies were consulted on this change in interpretation.

³ The SAR Activity Review, prepared by a subcommittee of the BSA Advisory Group, which ABA co -chairs, will now be published quarterly, thus complying with 314 (d).

According to the preamble, 314(a) “seeks to create a communication network linking federal law enforcement with the financial industry so that vital information relating to suspected terrorist and money launderers can be exchanged quickly and without compromising pending investigations.” As FinCEN points out, this part of the rule is an attempt to formalize the current “control list” procedures.

ABA believes that this part of the rule goes far beyond those procedures and is not consistent with congressional intent that information be “shared” with the financial institutions. In addition, the proposed rule does not “encourage” information sharing with the government; it is, instead, a new regulatory obligation. We have now witnessed the resumption of the record “requests” under section 314 and it is clear that the system still needs modification.

In November 2002, FinCEN and the primary federal regulators issued a Joint Agency Notice to put into place a brief moratorium on the section 314(a) information requests and compliance with existing requests. This moratorium was a direct result of the confusion faced by the recipients of the requests. The information requests went to employees no longer with the bank, came in bunches several times a day, and had a seven-day response deadline. In addition, many of our members complained that there was no apparent connection to terrorism or money laundering in the demands. Instead, the “requests” seemed to be a dumping ground for law enforcement cold cases.

Since that time, the regulators, law enforcement and Treasury made adjustments and according to FinCEN, the process was revised to “address a number of logistical issues and to develop additional guidance on the information request process.”

The announced changes include the following:

- 314(a) requests from FinCEN will be batched and issued every two weeks, unless otherwise indicated in the request.
- After receiving a 314(a) request, financial institutions will have two weeks, rather than one week, to complete their searches and respond with any matches.
- Searches will be limited to specific records and, unless otherwise noted, will be a one-time search.
- If a financial institution identifies a match for a named subject, the institution need only respond to FinCEN that it has a match and provide point-of-contact information for the requesting law enforcement agency to follow-up directly with the institution.

While these changes appear helpful, the initial responses we are getting from the industry is that there are still tremendous operational and communication problems with the new round of 314(a) demands. We urge this subcommittee to seek a status report from FinCEN on how the new system is working. We should point out, however, that the Treasury Department has committed to meet with the industry and try to improve the system.

Uniform and Consistent Patriot Act/BSA/AML Examination Procedures

As we approach the release of final rules for the remainder of the Patriot Act regulations it is imperative that all affected industries be treated equitably. To accomplish this important goal, there needs to be agreement on how the financial services industry will be examined for compliance under these rules. Too often, institutions of the same approximate size, in the same geographic area and offering the same financial products are treated differently for compliance purposes. This should not continue.

ABA appreciates the fact that the OCC and the FRB have announced a joint effort to conform their new examination procedures but we strongly believe that all functional regulators need to be part of this project. We urge the Congress to call for the regulatory agencies to report on their efforts in this area and ensure that this process is truly a joint endeavor.

OFAC and the Regulated Community

There has been a long-standing debate in the financial community on how to handle the myriad of transactions received every day and not violate the laws administered by the Treasury's Office of Foreign Assets Control (OFAC). While the financial industry appreciates the recent attempts by OFAC to address a variety of issues through the posting of "FAQs" (frequently asked questions) on their website, the fact remains that confusion still exists.

For example, the answer to one of the most common questions "Does OFAC itself require that banks set up a certain type of compliance program?" gives the industry little solace. The answer, according to OFAC, is that OFAC is not a bank regulator and the institution should check with their regulators "regarding the suitability of specific programs to their unique situations."

Madam Chairman, ABA and our members need improved direction from both OFAC and the bank regulators on what is considered an acceptable OFAC compliance program as well as a reasoned analysis on the scope of these requirements. Our Association urges the Treasury to coordinate a meeting to address these issues as soon as possible.

SAR Guidance

Similar to Patriot Act interpretative questions, there remains an ongoing need for the regulatory agencies, law enforcement and FinCEN to assist Suspicious Activity Report (SAR) filers with issues as they arise. This need is particularly obvious in the area of "terrorist financing." This crime is difficult to discern as it often appears as a normal transaction. We have learned from many government experts that the financing of terrorist activities often can occur in fairly low dollar amounts and with basic financial products (e.g. retail checking accounts). Guidance in this area is extremely necessary for effective and accurate industry reporting.

An excellent example of providing guidance to SAR filers can be found with the relatively new issue of computer intrusions. The Federal Bureau of Investigation (FBI) advocated adding the crime of "computer intrusion" to the SAR and that change came with a description of the crime on the instructions to the SAR form. In addition, the instructions also described the types of activities that are not indicative of computer intrusions. (For example, "computer intrusion" does not mean, "attempted intrusions of websites.")

Another useful example from the SAR instructions is the description of what may constitute potential money laundering or violations of the Bank Secrecy Act. Similar examples and instructions to assist SAR filers with clear direction as to what may constitute SAR reportable activity are needed for activities such as “terrorist financing.”

As our Association pointed out in a recent comment letter on the “suspicious activity report,” the interagency-authored publication, the “SAR Activity Review,” often includes a number of examples of activities that represent reported financial crimes. This information is useful for training purposes. As the private sector co-chair of the SAR Activity Review, I can assure you the ABA supports the efforts of FinCEN and the participating agencies in crafting a publication that provides necessary feedback to the SAR filing community. The SAR Activity Review has provided examples of the characteristics of suspicious activity such as identity theft. The 2003 issue released last week covers a number of examples of terrorist financing activities. There should be more efficient coordination between the information needed to properly complete a SAR and the SAR Activity Review.

While ABA would prefer that examples of all financial crimes be included with the SAR instructions, we urge that, at a minimum, the SAR instructions refer to the SAR Activity Review for further information on the summary characterization of most of the suspicious activity categories.

Conclusion

Madam Chairman and members of the subcommittee, the ABA has been in the forefront of the industry efforts to develop a strong public-private partnership in the areas of money laundering and now terrorist financing. We continue to support the policy goals expressed by Congress but want to ensure a workable and efficient process. We encourage Congress to stay involved in this important oversight effort.