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TESTIMONY OF

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ACTING COMPTROLLER OF THE CURRENCY

Before the

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

of the

UNITED STATES SENATE

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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 Shelby, Ranking Member Sarbanes, members of the Committee, I appreciate the opportunity to appear before you today to discuss issues arising in our nation's anti-money laundering efforts in the context of money services businesses (MSBs). My testimony will focus on the nature of money laundering risks posed by MSBs, MSBs' loss of access to banking services, and the OCC's position concerning banks' relationships with MSBs. We very much appreciate your leadership, and that of the Committee, in this vital area.

Money Services Businesses

A "money services business" is an umbrella term encompassing many different types of financial service providers. MSBs are defined broadly in the 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. According to a 1997 study by Coopers & Lybrand that was commissioned by FinCEN, and is currently in the process of being updated, it was estimated that there were over 200,000 MSBs operating in the United States providing financial services involving approximately $200 billion annually. Of these MSBs, approximately 40,000 were outlets of the U.S. Postal Service, which sell 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 can play in this process. MSBs provide financial services to segments of our society that do not have accounts with mainstream banks or for other reasons do not feel comfortable in a formal banking environment. 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 industry trade group information, up to 40 million Americans do not have mainstream bank accounts and satisfy most of their financial needs using MSBs.

However, some MSBs can also present a heightened risk of money laundering or terrorist financing. These businesses generally engage in a high volume of cash transactions and usually offer several types of services, including check cashing, money transmission, currency exchange, money orders, traveler's checks, and stored value mechanisms. They engage in transactions with third party customers who are unknown to the bank and, as a result of this indirect relationship, the bank has neither verified the identities nor obtained first-hand knowledge of these customers. As a result, transactions involving such entities could have the effect of moving the placement stage of money laundering one step away from the bank.

OCC compliance examinations over the years have also noted situations where extraordinary amounts of cash were deposited at national banks by MSBs. In such situations, the OCC or the national bank filed a suspicious activity report (SAR) and reported the transactions to law

enforcement. The OCC is also aware of situations where money launderers actually established MSBs (check cashers) to disburse and launder their excess cash to unsuspecting customers. Similar examples of money laundering through MSBs are noted by the Financial Action Task Force on Money Laundering in its Report on Money Laundering Typologies 2001-2002. The 2003 National Money Laundering Strategy, prepared jointly by the Department of Treasury and the Department of Justice, also specifically makes references to MSBs being used as conduits in various terrorist financing arrangements. For these reasons and others, the OCC has traditionally viewed MSBs as "high-risk" for money laundering.

State licensing, regulation and oversight of MSBs also varies. For example, some states require no licensing, some states license only certain segments of the money services businesses (*e.g.,* check cashers or money transmitters) while other states exercise strong regulatory oversight over all facets of the MSB industry. Furthermore, according to FinCEN, as of December 2004, only approximately 22,000 MSBs have registered with FinCEN as required by law. One could surmise from the 1997 study and its projections, that only about 10% of the over 200,000 MSBs that may be operating nationwide have complied with these registration requirements.

Notwithstanding the foregoing, not all MSBs are equally risky and most MSBs have never been tainted by or associated with money laundering. Some are nationally recognized and respected companies that have strong 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 or terrorist financing. The challenge for all of us is to

ensure that banks recognize these differences and that we, as regulators, are clear about our supervisory expectations to the banking industry with respect to MSB accounts.

Loss of Access to Banking Services

The OCC is well aware of, and 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 for MSBs' loss of access to banking services are complex and derive from a multitude of factors, including concerns about regulatory scrutiny, uncertainty about regulatory expectations, the risks presented by some MSB accounts, and the costs and burdens associated with maintaining MSB accounts.

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 from a money remitter that cashes checks, sells money orders, and sends wire transfers to customers in high-risk geographies.

Banks must expend resources just to identify those MSBs that are high risk and those that are not. In general, at a minimum they must: (1) apply their customer identification program requirements; (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 Bank Secrecy Act (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 significant. 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, some banks may simply decide to close the accounts or discontinue the business relationship.

These problems are further compounded by the huge number of unregistered and unlicensed MSBs, and the uneven regulatory scheme under which MSBs are supervised. Registration with FinCEN, if required, and compliance with any state-based licensing requirements represent the most basic of compliance obligations for MSBs, and an MSB operating in contravention of registration and licensing requirements would be violating Federal and possibly state laws. Nonetheless, there are tens of thousands of MSBs that are not registered with FinCEN, and there are a significant number of MSBs that are not licensed by the states.

Another factor is the lack of clear guidance on certain issues concerning supervisory expectations of banks that provide financial services to MSBs. This is especially true in the case of unregistered MSBs where clarity was needed as to 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. Similarly, we needed to clarify what minimal level of due diligence should be conducted on low-risk MSBs, or even the amount of due diligence expected of banks to conduct a risk assessment of their MSB customers.

Additionally, the general characterization of MSBs as "high-risk" by regulators over the years at times failed to highlight the fact that the risk profiles of MSBs vary depending on the circumstances of a particular MSB. Thus, incomplete or unclear guidance from regulators may have discouraged banks from doing business with certain MSBs even though most have never been tainted by or associated with money laundering.

Banks are also concerned about the risks of doing business with MSBs, including reputation risk. This may be due, at least in part, to several high-profile criminal cases brought against banks that have relationships with MSBs. For example, in January 2003, Banco Popular of Puerto Rico forfeited $21.6 million (the forfeiture to the Government satisfied a civil money penalty of like amount assessed by the Federal Reserve and FinCEN) and entered into a deferred prosecution agreement with the Justice Department in a case involving a single count of failing to file a SAR on an MSB customer in violation of the BSA.

In October 2003, Delta National Bank and Trust Company, which has its principal office in New York City, paid a $950,000 criminal fine and pled guilty to a criminal information charging the bank with one count of failure to file a SAR in connection with transactions involving two MSB accounts at the bank.

Finally, in March 2004, Hudson United Bank, a state chartered bank which 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 MSB accounts as required by the BSA.

These and other cases have understandably caused considerable anxiety among bankers that have MSB accounts. In some cases, where a bank has been criminally investigated or prosecuted, the investigation began as an investigation of the MSB customer of the bank, and eventually led to the bank itself becoming a target of the investigation because it allegedly failed to properly administer the MSB account. Moreover, many bankers are concerned with what they characterize as the "criminalization" of the SAR process, and in light of the billions of transactions going through the U.S. banking system, at least one banker has analogized this process as running a railroad and being expected to monitor everyone who takes your train to see if their trip is legitimate.

Without question, the stakes in this area have been raised in part due to the risk of terrorist financing and national security concerns, consequently, the risk exposure of guessing wrong is very high. 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 Position Concerning Banks' Relationships with MSBs

To accomplish 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. The OCC's examination procedures were developed in conjunction with the other federal banking agencies, based on our experience in supervising and examining national banks in the

area of BSA compliance. The procedures are risk-based, focusing our examination resources on high-risk banks and high-risk areas within banks. We continue to work to improve our supervision in this area and 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 with FinCEN and the other Federal banking agencies to issue a new, interagency BSA examination handbook by June 30 of this year. This is a major step toward interagency consistency in how we conduct our exams in this area.

We have also provided specific guidance on MSBs to our examiners and to national banks. Since September 1996, the OCC has had guidance in its BSA Handbook addressing non-traditional financial entities, including MSBs. Last year, in response to concerns about unregistered and unlicensed MSBs, the OCC issued Advisory Letter 2004-7, providing guidance to banks with respect to unregistered or unlicensed MSB customers. FinCEN and the Federal banking regulators are providing additional guidance to banks about MSBs and we will adjust our existing guidance to conform to this interagency guidance.

On several occasions in the last six months, the OCC has participated in various forums to better understand MSB issues and to educate the industry and our staff. For example, OCC representatives attended the March 8, 2005 hearing on MSBs hosted by FinCEN. Also, in March of this year, the OCC hosted a teleconference for the national banking industry in which we discussed a variety of BSA concerns, including MSB issues. Approximately 1,000 sites listened to the teleconference, mostly at national bank locations. These sites included between 4,000 and

5,000 listeners. We conducted the same teleconference for our examination staff in the week preceding the industry call.

As our knowledge and understanding of MSBs and their issues have continued to grow, our guidance has continued to evolve and develop. On March 30th of this year, 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.

Along with FinCEN and the other Federal banking agencies, we also are issuing Interagency Interpretive Guidance on Providing Banking Services to MSBs 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 for banking organizations.

Concurrent with this guidance, FinCEN will issue guidance to MSBs to emphasize their BSA regulatory obligations and to notify them of the type of information that they may be expected to produce to a banking organization in the course of opening or maintaining an account relationship. We are hopeful that this guidance will further clarify our expectations regarding banks' relationships with their MSB customers. 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 Fox for the leadership he has shown in addressing this important issue. His efforts to foster interagency collaboration and cooperation have been extraordinary.

The BSA has been the focus of regulatory, Congressional, and media attention for much of the last year. Clearly, these are very important issues to the banking industry, the OCC and the United States. This emphasis and attention on BSA has prompted the industry to feel that the regulators have adopted a "zero tolerance" approach to BSA/AML supervision and enforcement – that any deficiency in a bank's BSA processes equates to a violation triggering a cease and desist order. At the OCC we take this assertion seriously – because it is flat wrong. Perhaps it arose in response to monetary fines related to money laundering and to enforcement actions by the bank regulators, yet the actual number of actions is less than what one might think, given the level of concerns raised. For example, the OCC fined two banks for BSA violations in the past

twelve months. During the fourth quarter of 2004, we conducted 368 examinations at which BSA compliance was reviewed, and cited four banks for violations of our BSA compliance program requirement. Overall, in 2004, we issued eleven cease and desist orders concerning BSA – less than 1 percent of our population of national banks.

The intense focus on BSA compliance has led to other misperceptions about the OCC's policies and practices relating to MSB accounts at national banks. In concluding, let me set the record straight on several key points: first and foremost, the OCC does not supervise MSBs and does not expect national banks to supervise their MSB customers. Rather, it is our job to assess the systems and controls that banks employ to comply with the BSA, and it is the banks' job then to develop and successfully implement such systems and controls.

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 expects banking organizations that open and maintain accounts for money services businesses to apply the requirements of the BSA, as they do with all accountholders, on a risk-assessed basis. We 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.

Moreover, we absolutely are not saying that because a particular type of business or product is high-risk, that a national bank should not be involved with it. We absolutely are saying, however, that national banks must have systems commensurate with – and adequate to identify, monitor, manage, and control – those risks. A crucial question today may well be whether a bank has or is willing to incur the cost to have such a system of due diligence and controls sufficient to reduce the bank's risk to a level that satisfies the regulatory standards that apply *and* is within the bank's own risk appetite.

Conclusion

Mr. Chairman, Senator Sarbanes and members of the Committee, the OCC salutes your leadership in this vital area and strongly shares the Committee's goal of preventing and detecting money laundering, terrorist financing, and other criminal acts and the misuse of our nation's financial institutions. We also believe that important objectives are achieved when MSBs have access to banking services, consistent with the goals of the anti-money laundering and terrorist financing laws. We stand ready to work with Congress, FinCEN, the other financial institutions regulatory agencies, and the banking industry to achieve these goals.