THE FINANCIAL SERVICES ROUNDTABLE

1001 PENNSYLVANIA AVENUE, NW
SUITE 500 SOUTH
WASHINGTON, DC 20004
TEL 202-289-4322
FAX 202-289-1903

E-Mail rich@fsround.org
www.fsround.org

RICHARD M. WHITING
EXECUTIVE DIRECTOR AND
GENERAL COUNSEL

May 4, 2005

Communications Division
Public Information Room, Mailstop
Office of the Comptroller of the Currency
250 E Street, S.W.
Washington, D.C. 20219
Attention: Docket No. 05-01

Regulation Comments
Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, N.W.
Washington, D.C. 20552
Attention Docket No. 2005-02

Ms. Jennifer J. Johnson
Secretary
1-5
Board of Governors of the
Federal Reserve System
20th Street and Constitution Ave., N.W.
Washington, D.C. 20551
Docket No. OP-1220

Mr. Robert E. Feldman
Executive Secretary
Attention: Comments/OES
Federal Deposit Insurance
Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Re: <u>Request for Burden Reduction Recommendations; Money Laundering, Safety and Soundness and Securities Rules; Economic Growth and Regulatory Paperwork Reduction Act of 1996 ("EGRPRA")</u>

Dear Sirs and Madams:

The Financial Services Roundtable[1] (the "Roundtable") appreciates the opportunity to comment to the Board of Governors of the Federal Reserve System (the "Board"), the Federal Deposit Insurance Corporation ("FDIC"), the Office of the Comptroller of the Currency ("OCC"), and the Office of Thrift Supervision ("OTS") (collectively, the "Agencies") on the regulations to reduce burden imposed on insured depository institutions, as required by section 2222 of the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Pub. L. 104-208, Sept. 30, 1996) ("EGRPRA").

The proposed rule is part of the Agencies' ongoing effort under EGRPRA to reduce regulatory burden. The proposal requests comment on anti-money laundering, safety and soundness, and securities rules.

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[1] The Financial Services Roundtable represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Roundtable member companies provide fuel for America's economic engine accounting directly for $18.3 trillion in managed assets, $678 billion in revenue, and 2.1 million jobs.

Roundtable Comments

The Roundtable appreciates the efforts of the Agencies to alleviate the burden on financial institutions. Currently, financial institutions are forced to commit extensive resources to comply with myriad rules and regulations. Since the enactment of the Financial Institutions Reform, Recovery and Enforcement Act ("FIRREA") in 1989, banking and thrift regulatory agencies alone have promulgated eight hundred and one final rules. In addition, insurance companies and securities firms are subject to numerous federal and state laws. Many of the more recent laws and regulations have been enacted by Congress as a response to new threats, such as terrorism, as well as recent corporate scandals.

For the purposes of this letter, the Roundtable will like to focus its comments on the anti-money laundering issues. Financial institutions are inundated with reporting requirements and compliance burdens associated with the USA Patriot Act of 2001 and the Bank Secrecy Act ("BSA"). In addition to reporting requirements, regulatory supervision and enforcement of the regulations have become more vigorous and created unreasonable and often unpredictable standards for depository institutions. Actions being brought against companies by federal financial regulators, the U.S. Department of Justice, and the State Attorneys General have amounted to regulation by enforcement, which is a process that lacks consistency, predictability, and transparency.

Anti-Money Laundering Regulations

Suspicious Activity Reports ("SARs")

A financial institution is required to file a SAR no later than thirty calendar days after the date of initial detection by the financial institutions of facts that may constitute a basis for filing a SAR. Failure to file a SAR can have serious consequences, including civil money penalties, cease and desist orders and even criminal actions taken against the financial institution.

The SARs process has traditionally been a process in which an institution files a report based on a perceived suspicion of wrongdoing. In a bulletin, dated November 10, 2004, the OCC stated, "The OCC recognizes that the decision to file a SAR is an inherently subjective judgment. A bank should not be cited for a violation if and when it fails to file a SAR in an isolated circumstance, unless the failure is significant or accompanied by evidence of bad faith, provided that the bank otherwise has adequate systems and controls in place. Before citing a violation, examiners will consider the:

- Severity of violations;
- Time span of violations;
- Frequency or isolated nature of violations; and

- Related finding on prior examinations."[2]

Roundtable member companies strongly support the government's effort to combat money laundering and terrorist financing. However, we believe that the current system of reporting suspicious activity is not working. Many disturbing trends have arisen surrounding the enforcement of the BSA. The number of SAR filings has increased dramatically over the years. Since 1996, national SAR reporting has increased 453 percent. FinCEN reported 81,197 filings in 1997 versus 288,343 filings in calendar year 2003. The record total of 2003 was easily surpassed in 2004 as depository institutions filed 297,753 SARs prior to October 28, 2004.[3] That number is projected to double in 2005.

We believe there are several reasons for the large influx of SAR filings. First, the failure to file SARs has become a criminal issue. The U.S. Justice Department has aggressively pursued actions against institutions for not filing suspicious activity reports. The criminalization of the process presents a huge reputational risk for financial institutions. Fear of criminal prosecution has led institutions to file defensive SARs. Second, there are no clear standards for when SARs should be filed. Although guidelines are in place, these guidelines are not clear and are not consistently applied among examiners. In addition, financial institutions do not receive feedback from law enforcement on the type of information that should be included in the SAR. Third, Roundtable companies have reported that examiners' attitudes have changed in relation to these filings. Roundtable member companies believe that a "zero tolerance" policy exists among the Agencies. Regulators are not reviewing financial institutions' systems in their entirety. Instead, examiners are holding institutions accountable for every single transaction. Examiners have indicated that banks in higher risk business lines may be subject to review at the individual transaction level. This approach has prompted financial institutions to file SARs on even remotely questionable transactions. Fourth, compounding these problems are the multiple agencies with jurisdiction over financial institutions. The lack of coordination by examiners and law enforcement agencies often results in duplicate requests and multiple filings of SARs.

For all of these reasons, institutions have begun to file defensive SARs and those SARs are flooding the system. The Roundtable believes that the federal financial regulators need to devise a system in which financial institutions provide quality information that will help FinCEN and law enforcement officials in their efforts to combat money laundering and terrorist financing.

To address these concerns, the Roundtable *recommend*s the following:

- The Agencies should develop clear, simple guidance on SAR filings. Guidance can be achieved in several ways. Institutions could use more feedback from law

[2] See OCC Bulletin 2004-50, "Bank Secrecy Act and Anti-Money Laundering", p. 2-3 (November 10, 2004).
[3] See FinCEN's SAR Activity Review Reports at www.fincen.gov.

enforcement on the type of information they need to include in these reports. The Agencies could conduct outreach programs and set up toll free hotlines where regulators would respond to industry inquiries. And, to the extent possible, the Agencies could develop "safe harbor" regulations that will guide these practices and reduce the need for defensive filings. This safe harbor language would be useful when there is a question by examiners or law enforcement on whether or not a SAR should have been filed. The safe harbor would create minimum standards. If these standards were followed by the institution, it would be deemed to be in compliance. The safe harbor would also create clear guidelines allowing federal financial regulators, FinCEN and the Justice Department to bring actions against financial institutions that choose to operate outside the parameters of the system.

- The Roundtable urges the Agencies to draft regulations and/or guidance that focus on institutions' anti-money laundering programs, not individual transactions. These programs would be subject to internal review by financial institutions and audited by regulators. Financial institutions are required to have a sufficient BSA/AML program under 31 CFR §103.120. This includes proper systems, controls, independent audit and testing, designation of a compliance officer, and training for employees. The Roundtable *recommends* creating self-examination procedures for financial institutions that would allow them to review and audit their AML programs and cure defects by bringing information to the attention of regulators without significant penalty, including late filing of SARs. Late filings should not be judged as not having filed at all. Institutions are working hard to combat money laundering. As a practical matter, some transactions may not be caught initially, but may be discovered during an audit. Financial institutions should still be encouraged to file reports on these transactions.

- The Roundtable appreciates the Agencies' recent efforts to address deficiencies in the SAR filing system. For example, FinCEN has created a secure web site to encourage communication between law enforcement and the industry, and regulators are drafting an interagency examiner manual aimed at applying BSA standards consistently. Additional work needs to be done, however, in order to reduce the volume of SARs and improve the quality of information. The Roundtable *recommends* that the Agencies coordinate with each other on all examination procedures and provide consistent interpretations of the BSA. The Roundtable also *recommends* that, when applicable, the Agencies communicate more with the Justice Department and law enforcement officials. The SARs process will work only if regulators, law enforcement officials and the industry work together to fulfill their obligations under the BSA.

Cash Reporting Requirements

Another anti-money laundering requirement that should be reviewed is the requirement that U.S. financial institutions and all other U.S. businesses file reports on cash

transactions in excess of $10,000. The current Currency Transaction Report ("CTR") threshold of $10,000.00 was established almost forty years ago and has not been adjusted for inflation.

The resources spent on compliance with the cash reporting requirements are hard to justify, especially since suspicious cash transactions already are covered by SAR requirements. Even many of the most die-hard proponents of anti-money laundering regulations concede that the requirement to report cash transactions in excess of $10,000 produces virtually no information that is useful to regulators or law enforcement.

Recognizing that the burden imposed may not be justified, the government has supported a voluntary system that exempts some types of transactions from the scope of the reporting requirement, but for many institutions, using the exemption system is cumbersome and more resource-intensive than filing reports.

Foreign Bank Correspondent Account Requirements

U.S. banks and broker-dealers spend millions of dollars to comply with requirements to obtain ownership and other information from each foreign bank with which they do business, and to confirm that each such foreign bank maintains a "physical presence" in some jurisdiction. In addition, financial institutions have reported a trend of regulators seeking information about their customers' customers, particularly with respect to foreign banks and other money services business ("MSBs").

There is simply no evidence that this type of information has any value in detecting the financing of terrorism or money laundering. Foreign banks have found the obligation to supply this information to their U.S. counterparts burdensome. The Roundtable *recommends* that the Agencies review the need to continue this practice and adjust the regulations accordingly. One solution may be to have FinCEN maintain a central depository of information on foreign banks for U.S institutions to access.

USA Patriot Act Issues- Customer Identification Program ("CIP")

Financial institutions appreciate the interpretive guidance on CIP in January 2004, but believe that further clarification is needed. In particular, the Roundtable *recommends* that the Agencies clarify discrepancies that exist between the requirement to maintain sufficient information to identify a customer under Section 326 of the USA PATRIOT Act and the Regulation B prohibition on maintaining information on the gender or race of a borrower. These rules need to be reconciled in order to ensure compliance with both provisions.

The Roundtable also requests that the Agencies provide more clarification in relation to customer identification standards, such as acceptable forms of identification and verification and when these forms are required. Roundtable member companies believe that inconsistent interpretations of BSA regulations by the Agencies will negatively

impact the level of customer service. For example, despite the fact that 31 CFR §103.121 requires institutions to verify the customer's identity for new accounts, some institutions have been informed by their primary regulator to discontinue relationships with existing customers who cannot produce proper identification. Adding to the confusion are state laws, particularly those that govern insurance, that provide strict governance on when a relationship with an existing customer can be terminated. In some cases, it is difficult to determine whether a client is a new or existing customer and what CIP requirements apply.

In addition, current regulations do not recognize the significant differences between a bank's relationship with individual and institutional customers. In the course of doing business, banks are required to obtain considerable information about institutional customers. Many of these institutional customers are themselves subject to BSA requirements and are knowledgeable about CIP programs. Some of the CIP requirements are unnecessary and duplicative for these customers. Roundtable member companies *recommend* that the Agencies make a distinction under the CIP rules for institutional customers and retail customers. We believe these regulations should be tailored to different businesses instead of a one size fits all approach. This type of distinction has been made for other regulations. For example, privacy notices under the Gramm-Leach-Bliley Act must only be sent to retail customers, not institutions.

Utility of Anti-Money Laundering Regulations

Unquestionably, the prevention of money laundering is an important goal. However, the utility of some of the existing anti-money laundering requirements is debatable. One of the first comprehensive studies of the entire set of anti-money laundering regulations, released late last year by the non-partisan Institute for International Economics, concluded that the "elaborate system of laws and regulations that affects the lives of millions of people and imposes several billion dollars in costs annually on the American public" is based on a set of "untested assumptions that do not look particularly plausible."[4]

The Roundtable believes the current regulatory environment is having a negative affect on financial institutions and the economy in general. The numbers in this area are staggering. U.S. financial institutions will spend $10.9 billion through 2005 on AML compliance alone. $695 million will be spent on software and hardware, $3.3 billion for information systems maintenance and the rest of the costs will be allocated toward employee training, reporting and other compliance costs.[5] A survey of the Roundtable CEOs indicated that the ratio of their overall regulatory compliance costs in relation to their total expenses have increased by an estimated 50% from 2002 to 2005. In addition,

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[4] "Chasing Dirty Money: The Fight Against Money Laundering", by Peter Reuter and Edwin M. Truman (November 2004),

[5] "Anti-Money Laundering: A Brave New World for Financial Institutions", Celent Communications Report (September 2002). .

the time spent by CEOs and their top executives on compliance has doubled over the same period.

These costs are directly affecting the business decisions of these companies. In a recent PriceWaterhouseCoopers global survey, 57 percent of 1,400 respondents stated that the current business climate is making companies "excessively" or "somewhat" risk averse.[6] Increased costs and allocation of valuable resources toward BSA compliance is impacting financial institutions' decisions to hire new personnel, create new products, purchase new systems, enter new markets and serve customers.

The Roundtable *recommends* that the Agencies carefully measure the impact of existing and future anti-money laundering regulations on the consumer and the economy in general, and weigh the possible benefits against these costs.

Conclusion

The Roundtable will continue to work with the Agencies to identify regulatory burdens and propose solutions. Roundtable member companies believe the current regulatory environment, with respect to money laundering regulations, is having an adverse impact on America's safety, the economy, and consumers. We strongly encourage the Agencies to review current anti-money laundering regulations in an effort to make them more effective.

If you have any further questions or comments on this matter, please do not hesitate to contact me or John Beccia at (202) 289-4322.

Sincerely,

Richard M. Whiting

Richard M. Whiting
Executive Director and General Counsel

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[6] See Innovating America; Recent Council on Competitiveness Report (December 2004).