BSA/AML for nonbanking institutions

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WHO SHOULD READ THIS?

Money services businesses, residential mortgage lenders, and other nonbanks subject to BSA/AML laws.

WHY READ THIS?

Money services businesses, residential mortgage lenders, and other nonbanks may be subject to significant regulatory, enforcement, and reputational risk if they fail to develop and maintain effective and sustainable Bank BSA/AML programs.

Failure to implement an effective program could impair relationships with banking partners and make it more difficult for companies to maintain a bank account.

The requirements of the Bank Secrecy Act and anti-money-laundering laws are pervasive and longstanding, yet they continue to vex companies trying to comply with them. Regulators have hit virtually all large banks, and many nonbanks, with BSA/AML-related enforcement actions, resulting in large fines, deferred prosecution agreements, criminal consequences, and reputational damage.

New BSA/AML requirements are making compliance more, not less, challenging. The Financial Crimes Enforcement Network's Customer Due Diligence rule,[1] for example, has led to massive de-risking of bank accounts for money services businesses and other customers. This has made it more difficult for customers to maintain accounts and added to the demanding nature and already high cost of BSA/AML compliance.

The nexus between BSA/AML requirements and law enforcement and national security concerns will ensure that compliance remains a top priority for regulators and the Department of Justice. Understanding exactly what is required of an institution from a BSA/AML perspective is therefore more critical than ever.

BACKGROUND

The BSA, enacted in 1970, is primarily a recordkeeping and reporting statute. Its purpose is to require certain reports or records where they have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism.[2]

Tax evasion was BSA's initial purpose, but it has become a primary weapon in the fight against narcotics, money laundering, terrorist financing, elder abuse, and other illicit activity. The Patriot Act[3] passed after 9/11 expanded BSA beyond banking, and now most nonbank financial institutions have BSA-related obligations, including compliance programs and suspicious activity reporting. Even entities not subject to the BSA often assume compliance responsibilities because they contract with an entity subject to the BSA.

1. *See* Customer Due Diligence Rule, 31 C.F.R. § 1010.230.
2. *See* Bank Secrecy Act, 31 U.S.C. § 5311.
3. *See* P.L. 107-56, 115 Stat. 272 (2001).

Chief among this expanded scope of institutions subject to BSA are money services businesses (MSBs) — money transmitters, check cashers, providers of prepaid access, and dealers in foreign exchange, among others — and residential mortgage loan originators (RMLOs). The specific requirements for these categories of institutions are discussed in detail below.[4]

REQUIREMENTS FOR MSBs

Compliance program. The fundamental BSA requirement for MSBs is the development, implementation, and maintenance of a BSA/AML compliance program that is reasonably designed to prevent the MSB from facilitating money laundering and financing terrorist activities. The written compliance program must be commensurate with the risks posed by the location, size, and the nature and volume of the financial services provided by the MSB, and made available to the Department of Treasury for inspection.

These programs must incorporate what are referred to as the four pillars:

- Policies, procedures, and internal controls that are reasonably designed to assure compliance with the BSA, including procedures to verify customer identification (applicable only to providers or sellers of prepaid access); file reports; maintain records; and respond to law enforcement requests.
- A designated person to assure day-to-day compliance with the program.
- Education and training of appropriate personnel.
- Independent review to monitor and maintain an adequate program.

Registration. MSBs (other than providers of prepaid access) are required to register with FinCEN, and renew that registration every two years; states where the MSB does business often require registration, as well. Agents generally do not have to register.

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Reporting. MSBs have specific reporting requirements, the most important of which are currency transaction reports on cash transactions exceeding $10,000 and suspicious activity reports on cash transactions exceeding $2,000. Businesses must retain both CTRs and SARs for five years from the date of filing.

A MSB may only disclose SARs to a limited group: FinCEN, a federal authority (such as the IRS), a state authority with power to examine the MSB for compliance with the BSA, and federal, state, and local law enforcement. Strict confidentiality requirements apply, with criminal penalties for unauthorized disclosure. The business may share facts, transactions, and documents underlying an SAR with other institutions, and in limited circumstances (permitted by regulation or regulatory guidance) may share the actual report within the organization. MSBs are protected from civil liability extending from SAR filings. FinCEN and its delegates are responsible for examining MSBs for compliance with these requirements.

REQUIREMENTS FOR RMLOs

RMLOs are subject to program requirement similar to those applicable to MSBs. While RMLOs are not required to submit CTRs, they are required to file similar reports (Form 8300) when receiving cash payments of over $10,000. They are also subject to SAR requirements, though the filing threshold is $5,000. The SAR recordkeeping and confidentiality requirements also apply, as well as the safe harbor from civil liability. As with MSBs, FinCEN and its delegates conduct compliance examinations.

4. Much of the subsequent discussion of the requirements of BSA/AML laws and related compliance obligations are descriptions drawn from 31 C.F.R. §§ 1010, 1022, and 1029. For more information, see https://www.law.cornell.edu/cfr/text/31/subtitle-B/chapter-X.

SANCTIONS

Sanctions are not formally part of the BSA, but are related and important. Compliance with the sanctions regime is required for all U.S. persons, not just financial institutions. The Office of Foreign Assets Control is responsible for administering U.S. sanctions. There is no formal program requirement, but regulators expect banks and most nonbanks to have an effective filtering process to screen accounts and transactions involving individuals and entities that are on the Specially Designated Nationals and other lists or OFAC-sanctioned jurisdictions, such as Iran and North Korea. Companies are expected to block or reject (depending on the exact sanctions) attempted transactions that result in hits and report them to OFAC. Sanctions compliance is under intense scrutiny in recent years, and violators have received large fines. However, under the current administration, the appetite for such scrutiny is less clear.

CONCLUSION

While nonbanking companies are generally not regulated for BSA/AML and sanctions compliance to the same degree that banks are, they are widely perceived as vulnerable to illicit activity and, therefore, subject to significant scrutiny. Enforcing agencies include FinCEN, DOJ, and OFAC, as well as federal, state and local regulators. As fines over many years have made clear, the costs of getting it wrong in this area can be severe. Institutions subject to the BSA/AML requirements should, therefore, take care to develop, implement, and maintain procedures covering the following areas:

- Risk assessment
- Customer identification
- Customer due diligence/enhanced due diligence (CDD/EDD)
- Customer risk rating
- Monitoring
- Investigation
- SARs
- CTRs

The primary purpose of these procedures is to help companies develop a deep enough understanding of their customers to be aware of which ones present AML risks, and then help companies successfully manage those risks while identifying and reporting suspicious transactions.

Given the expanding role of nonbanking companies in the payment system and the overall economy — and the persistent focus on money flows implicating national security or law enforcement concerns — BSA/AML compliance is poised to be an area of increasing importance for the foreseeable future.

ABOUT THE AUTHOR

Dan Stipano, who previously served as the OCC's Deputy Chief Counsel, and Director of the Enforcement & Compliance Division, advises on all aspects of bank regulatory and compliance issues, and provides assistance in establishing, maintaining, and monitoring BSA and AML compliance programs.