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TESTIMONY OF
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Before the

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

November 29, 2018

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.

Introduction

Chairman Crapo, Ranking Member Brown, and members of the Committee, thank you for the invitation to appear before you today to discuss initiatives to reform and modernize the Bank Secrecy Act (BSA)/Anti-Money Laundering (AML) regulatory and supervisory regime. We at the Office of the Comptroller of the Currency (OCC) support the purpose of the BSA to combat money laundering and terrorist financing (illicit finance). Toward this end, the OCC is committed to ensuring that the institutions under its supervision have robust controls in place to safeguard them from being used as vehicles to launder money for drug traffickers and other criminal organizations, or to facilitate the financing of terrorist acts. Together, with the other federal banking agencies and the law enforcement community, our goal is to prevent the misuse of our nation's financial institutions.

Under Comptroller Otting's leadership, the OCC is working to improve our system for addressing illicit finance by focusing agency resources and those of the entities that we supervise on the areas of highest risk. We are working collaboratively with other federal agencies and the private sector to improve the efficiency and effectiveness of the BSA/AML framework, including regulations, supervisory policy, and examinations in order to protect the integrity of the U.S. financial system. I am pleased to share some of the OCC's initiatives to further these objectives, as well as some recommendations for legislative action that would reduce unnecessary industry burden and promote information sharing.

The OCC charters, supervises, and regulates more than 1,300 national banks, federal savings associations, and federal branches of foreign banks ("banks"). These banks

collectively hold \$11.8 trillion in assets—roughly 67 percent of the assets of the commercial banking system. The vast majority of these 1,300 banks are smaller, community banks with less than \$1 billion in assets. As fundamental to its mission, the OCC requires banks to soundly manage their risks, meet the needs of their communities, comply with laws and regulations, and provide fair access to financial services and fair treatment of their customers.

In 2016, the OCC created an executive-level unit dedicated to enhancing the agency's focus on compliance issues, including BSA compliance. The Compliance and Community Affairs (CCA) line of business is focused on the agency's ability to comprehensively identify and address BSA/AML compliance risk, issue timely guidance and examination procedures, and communicate effectively about emerging compliance issues throughout the OCC and the banking industry. CCA develops AML policy and examination procedures and serves as the agency's technical expert to support consistent and effective implementation of BSA/AML supervision. In my role as Senior Deputy Comptroller of CCA, I have represented the OCC on domestic and international interagency groups and task forces addressing issues of illicit finance. I also regularly engage in dialogue with representatives of the banking industry and other stakeholders on this important issue. As well, I have established strong working relationships with my counterparts in the other federal banking agencies, the Department of the Treasury (Treasury), the Financial Crimes Enforcement Network (FinCEN), and law enforcement agencies. As stakeholders with the shared responsibility of protecting our financial system from misuse, our paramount goal has been, and will continue to be, preserving and enhancing the integrity of the U.S. financial system. Working collaboratively to

focus our combined authorities, objectives, and interests on deterring the misuse of our nation's financial institutions by illicit actors is a strong and enduring characteristic of our interagency efforts.

OCC's Risk-Based Supervision

Banks play a critical role in providing consumers and businesses across the nation with financial services and serve as key sources of credit for economic growth and job expansion throughout the United States. As a result, the OCC and other regulators are vital in ensuring the financial services system remains capable of meeting the needs of consumers and businesses in the United States and globally.

Regulatory oversight is particularly important because the safety and soundness of an institution can be threatened when a bank lacks appropriate risk management systems and controls around the products or services it provides, the customers it serves, or the geographies in which it does business. For this reason, banks must have effective BSA compliance programs. The OCC monitors compliance with the BSA and its implementing regulations by applying the examination procedures in the interagency BSA/AML Examination Manual.¹ Community banks are examined on a 12- or 18-month cycle, most midsize banks are examined on an annual cycle, and the largest banks are examined on a continuous basis by a dedicated team of examiners. Examination procedures are applied on a risk basis and direct examiners to focus on high-risk areas within banks. Every bank's BSA/AML compliance program must have, at a minimum, a system of internal controls to ensure ongoing compliance, independent testing for compliance, a designated individual responsible for coordinating and monitoring

¹ *Bank Secrecy Act/ Anti-Money Laundering Examination Manual*. Federal Financial Institutions Examination Council. 2014 (https://bsaaml.ffiec.gov/documents/BSA_AML_Man_2014_v2.pdf).

compliance (BSA officer), and training for appropriate personnel. Examiners assess the adequacy of each bank's BSA/AML program, relative to the risk profile of the bank, by evaluating the implementation and effectiveness of the bank's policies, procedures, systems, and controls. We also assess the effectiveness of the bank's program to ensure that transactions do not involve entities subject to sanction programs administered and enforced by the Office of Foreign Assets Control (OFAC).

For banks, BSA compliance requires analyzing large volumes of transactions to identify features that are suspicious, in the context of criminal and possibly terrorist elements that are dedicated to, and expert in, concealing the true nature of the transactions they undertake. As banks' BSA compliance programs have advanced to address these requirements, so has the sophistication and determination of money launderers, terrorist financiers, and other criminals in finding other ways to gain access to our institutions. Risks are constantly evolving, as criminal elements alter their tactics to avoid detection. As part of the supervision process, OCC examiners analyze BSA data trends, including currency transaction reports (CTRs) and suspicious activity reports (SARs), to aid in identifying areas of potential risk that may require supervisory attention. In cases where examiners identify areas of concern, deficiencies, or violations, the examination scope typically includes performing transaction testing in targeted areas to determine the scope of the potential problem and requirements for corrective action.

One tool that the OCC has developed to help assess BSA/AML and OFAC risk in community banks is the Money Laundering Risk (MLR) System, an annual data collection, review, and assessment process that allows the OCC to identify potentially higher-risk areas within the community bank population. The MLR data collection

process identifies indicators of BSA/AML and OFAC risk at an institutional level by identifying the products and services offered by these institutions, as well as the customers and geographies they serve. Examiners utilize this information regarding a bank's overall risk activities to appropriately scope and plan examinations. This approach not only allows the OCC to focus its resources, but also affords the agency flexibility to shift examination emphasis in response to the ever-changing money laundering typologies and criminal schemes that are present in the environments in which our banks operate. The MLR System also gives the agency a horizontal view of the quantity of BSA/AML risk, and trends in that risk, across the OCC's portfolio of community banks.

OCC's Reform Initiatives

It is critical that the nearly 50-year-old BSA/AML regime be updated and enhanced to address today's threats and better utilize the capabilities of modern technology in protecting the financial system from illicit activity. Therefore, the OCC in 2018 has taken a leadership role in coordinating discussions with the Federal Deposit Insurance Corporation (FDIC), Board of Governors of the Federal Reserve System (FRB), National Credit Union Administration (NCUA), Treasury, and FinCEN (collectively, the "agencies") to identify and implement ways to improve the efficiency and effectiveness of BSA/AML regulations, supervision, and examinations, while continuing to meet the requirements of the statute and regulations, support law enforcement, and reduce BSA/AML compliance burden.

The agencies have taken a number of actions to further these objectives. For example, the agencies established a working group earlier this year, which currently is focused on a number of work streams designed to: promote innovative and proactive

approaches to identify, detect, and report financial crime, and meet BSA/AML regulatory obligations; and clarify that the agencies do not have a zero-tolerance approach to BSA/AML supervision and enforcement but rather employ a risk-based approach to the examination process. The agencies are committed to modernizing the regulatory regime in ways that encourage institutions to dedicate resources to the areas of highest risk for illicit finance activities. The working group also recognizes that one important path to enhancing BSA/AML effectiveness is to encourage banks to develop innovative approaches to risk management and compliance by using new technologies and processes.

The agencies, through the efforts of the working group, recently released a joint statement clarifying ways in which community banks with a lower BSA risk profile may be able to increase efficiency and reduce burden in their BSA/AML compliance programs through the sharing of BSA resources. The statement describes how these banks can effectively use collaborative arrangements to share human, technology, or other resources related to BSA compliance to reduce costs, increase operational efficiency, and leverage specialized expertise.

Recently, the OCC, working with FinCEN and the other agencies, took additional action to reduce compliance burden and enhance the risk focus of the BSA regime. On September 28, 2018, the agencies, with the concurrence of FinCEN, issued an order granting an exemption from the requirements of the customer identification program rules (CIP) implementing section 326 of the PATRIOT Act for certain loans.² The affected loans are those extended by banks and their subsidiaries to commercial

² OCC Bulletin 2018-35, “Order Granting Exemption from Customer Identification Program Requirements for Premium Finance Lending.” September 28, 2018 (<https://occ.gov/news-issuances/bulletins/2018/bulletin-2018-35.html>).

customers to facilitate purchases of property and casualty insurance policies. These are generally referred to as insurance premium finance lending or premium finance loans. The agencies determined, and FinCEN concurred, that providing this exemptive relief is consistent with the purposes of the BSA and safe and sound banking.

The OCC also is engaged with other members of the Federal Financial Institutions Examination Council (FFIEC) and FinCEN to revise the FFIEC's BSA/AML Examination Manual. We expect that these revisions will further define the FFIEC members' application of their risk-based approach to supervision. Such additional clarity will support resource management efforts so banks can better meet their BSA compliance obligations.

OCC Supervisory Improvements

SAR and CTR Filings

The requirement for banks to identify and report suspicious financial transactions is an important part of the BSA's regime for protecting our financial system. SAR filings provide law enforcement access to information needed to initiate and conduct investigations of possible illicit finance transactions. There are literally millions of SARs in the centralized database maintained by FinCEN, and the vast majority have been filed by OCC-supervised banks. The massive number of filings represents a significant workload for the industry, and it is important that the significant human, financial, and compliance resources used to file SARs are focused on providing information that is truly useful to law enforcement.

The OCC is engaged with banks to evaluate the effectiveness of their SAR systems to ensure that the information being reported is timely and compliant. To better

clarify the instances when a SAR is required to be filed, and to maximize the value of information contained within each SAR, the OCC supports additional collaboration among banks, examiners, law enforcement and other stakeholders to consider how the types and content of SAR filings can be improved. For example, the OCC supports setting up communication channels through which law enforcement can clarify the types of SAR data that is most and least useful in criminal investigations so that bank and examiner resources can be better targeted and ultimately used more effectively. The OCC is committed to working with the key stakeholders on this effort to appropriately target activities and transactions that warrant the scrutiny of law enforcement.

Likewise, with respect to CTR reporting, the OCC is working with FinCEN and the other agencies to identify ways that the process can be made more efficient, and to clarify the agencies' approach to examinations for compliance with the CTR requirements. In this regard, the OCC intends to explore a range of CTR requirements with the other agencies, FinCEN and law enforcement including the appropriateness of the current CTR threshold, opportunities to tailor the content of the CTRs, and efficiencies for banks filing relatively few CTRs each month to file their CTRs on a quarterly basis. Our objective would be to identify ways to provide burden relief for institutions with lower risk profiles while balancing law enforcement's need for information. If agreement is reached on recommendations in these areas that require legislative action, we will provide them to Congress.

Technological Innovation

Technology generally has been used across the financial sector to increase customer convenience, access to financial products, and operational efficiency.

Likewise, there is significant potential for technological innovation to transform BSA/AML compliance. In addition to assisting banks' efforts to control their costs, innovation is increasingly necessary to counter constantly changing threats, as illicit financing methods evolve to exploit vulnerabilities in existing systems.

New technologies such as artificial intelligence (AI) and machine learning offer banks opportunities to better manage their costs and increase the ability of their monitoring systems to identify suspicious activity, while reducing the number of false positive alerts and investigations. Technology can provide significant advancements for the future of BSA/AML compliance and some banks have already begun researching available technology and applying it to their programs. For example, some banks have started using AI to more accurately identify suspicious activity and generate information that will assist law enforcement in more accurately detecting transaction patterns and threats. At the same time, other banks have explored ways to limit compliance costs including by contracting with third parties with specialized technology and knowledge to provide them with BSA/AML services.

The OCC encourages banks to explore technology that allows them to maintain their risk focus and gain process and system efficiencies. To this end, the agency is actively engaged in discussions with banks and other stakeholders regarding ways to explore enhanced technology usage while maintaining the current strong protections for the financial system.

Legislative Recommendations

The OCC has identified areas in which legislative changes could increase the impact and efficiency of BSA/AML regulation and compliance programs. The OCC

generally supports legislative changes that would reduce unnecessary industry burden and compliance costs, and allow for more effective information sharing related to illicit finance. We believe the changes described below could reduce compliance burden while still ensuring that regulators and law enforcement have the information they need to address illicit finance.

Review of BSA/AML Regulations

In 2016, the federal banking agencies initiated a comprehensive review of our regulations pursuant to the Economic Growth and Regulatory Paperwork Reduction Act (EGRPRA). During the process, BSA/AML regulations were the source of significant public comment. However, BSA/AML regulations are not subject to the EGRPRA process. As noted in the FFIEC's *Joint Report to Congress on EGRPRA* in March 2017, BSA/AML was one of the three most discussed issues during the agencies' review of regulations affecting the entities that we regulate. This is consistent with the significant number of comments the agencies received during the previous EGRPRA review in 2007, an indicator that BSA/AML is regularly a top priority for stakeholders. As the agency with rule-writing authority for most of the current BSA/AML regulatory regime, FinCEN could benefit from recommendations for regulatory improvement and to respond to public concerns about BSA/AML regulations.

Our experience has demonstrated that there is no shortage of ideas to reform the BSA and reduce the burden of BSA/AML regulations. Therefore, Congress could consider legislation requiring a regular review of the BSA/AML regulations, similar to the EGRPRA process, to identify those regulations that may be outdated, redundant or unnecessarily burdensome. Congress could direct this review to include: (1) consultation

with the federal banking agencies, law enforcement agencies, and other stakeholders, as appropriate; (2) solicitation of public comment, including specific comment on technology with the potential to reduce costs and burdens on financial institutions; and (3) submission of a report to Congress on the results of its review.

Technical Correction

Additionally, Congress may want to consider providing a technical clarification to the BSA's existing safe harbor to correct uncertainty caused by several court decisions. Currently, the BSA provides protection from civil liability for SARs made to appropriate authorities, including supporting documentation, regardless of whether such reports are filed pursuant to the SAR instructions. Because the SAR safe harbor does not address intent and some courts have imposed a "good faith" requirement, there is considerable uncertainty among institutions about the potential liability for filing SARs, if the suspicions underlying those SARs are not later fully investigated or proven through a criminal proceeding. As a result, many institutions are reluctant to file SARs voluntarily and even are concerned about liability for SARs filed pursuant to BSA requirements, which makes an already burdensome process more complicated. Legislation could clarify that an institution may file a SAR without running the risk that it will be exposed to civil litigation for simply complying with federal law.

Information Sharing

The OCC recognizes the importance of ensuring that the agencies' BSA/AML enforcement authorities remain current and relevant. We think there are opportunities, consistent with appropriate legal requirements, to modify the existing BSA safe harbor to encourage institutions to share information without incurring liability. The OCC would

support legislation to expand the information sharing safe harbor in Section 314(b) of the USA PATRIOT Act beyond money laundering and terrorist financing to include mortgage fraud, cyber fraud and other financial crimes, and to eliminate or modify the notice requirement to FinCEN, which may limit the ability of financial institutions to share information.

Conclusion

Comptroller Otting has placed a high priority on reforming and modernizing the BSA/AML regime. Aligning our supervisory policy more closely with the risks that are present in OCC-supervised banks, while at the same time supporting efforts to better rationalize and manage compliance costs and target resources to the areas of highest risk are key priorities that we balance with our commitment to preserving the integrity of the national financial system. Working with the other federal banking agencies, FinCEN, law enforcement, the financial industry, and Congress to maintain a regulatory environment in which OCC-supervised banks successfully combat illicit finance is key to achieving our mission. We believe that the actions currently underway, and proposed today, will further this goal.