

Bank Secrecy Act *and* Anti-Money Laundering

A western Missouri-based terrorist organization was indicted last spring for funneling more than \$1.4 million to Iraq by disguising itself as a charity to avoid detection—and solicit donations.

During a 12-year period, the Islamic American Relief Organization illegally transferred money from its bank accounts in Missouri to accounts in Jordan, and ultimately to Iraq. One of the organization's employees had also worked for Osama bin Laden, helping to obtain satellite phones to coordinate al-Qaida attacks on U.S. embassies in Africa.

More and more in the post-Sept. 11 world, these instances of money laundering challenge the country's financial institutions, which are the front line of defense in combating illicit

financial activity, says Susan Zubradt, vice president of examinations and inspections at the Federal Reserve Bank of Kansas City.

Compliance is tough and penalties are severe, but banks overall have embraced their important role in the fight against terrorism, Zubradt says.

The backbone of anti-money laundering compliance is the Bank Secrecy Act, which requires banks to have policies and procedures to guard against money laundering. This includes employee training, testing of the compliance program, and a system of internal controls to ensure compliance, including reporting suspicious financial transactions.

The Kansas City Fed has an active role in this effort, ensuring compliance as part of its examination process of member banks in the

Tenth Federal Reserve District. The District includes western Missouri, Nebraska, Kansas, Oklahoma, Colorado, Wyoming and northern New Mexico.

“The partnership among banks, bank supervisors and law enforcement has been integral in detecting and deterring money laundering,” Zubradt says.

These efforts are producing positive results, and illicit activity is being thwarted.

“These laws aren’t just about complying with regulations,” Zubradt says. “The ultimate goal is to safeguard our financial system from the abuses of financial crime.”

Banks’ role: Then and now

Several laws aimed at fighting financial crimes through the years have led to the complexity of today’s Bank Secrecy Act, dating back to its own inception in 1970 when the focus was stopping large amounts of drug trafficking cash from entering the banking system, says

efforts,” Thompson says, “the events leading to the passage of the PATRIOT Act pointed out just how complicated the world had become. Sept. 11 added more requirements and raised expectations in terms of the importance of this part of our examination process.”

As a result of increased globalization, technology and the complexity of transactions, moving money had become easier for criminals while financial institutions’ ability to detect and monitor illicit activity had become more difficult.

Traditional money laundering involves illicit cash transactions such as deposits made in amounts less than \$10,000 (to avoid the institution filing a report), multiple times. Or, cash amounts of less than \$3,000 used to purchase money orders, cashier’s checks or traveler’s checks, also to avoid reporting requirements.

New methods of money laundering include the use of stored-value cards. Some of

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Andrew Thompson, a Bank Secrecy Act expert based at the Fed’s Denver Branch.

Banks were asked to report cash transactions of more than \$10,000. As a way around this, criminals moved money via check cashing organizations, money services businesses, the postal system and casinos, which eventually became subject to the Act as well.

By 1986, money laundering and related activities became a federal crime. Because of further prompting from Congress, in 1992 banks and others were required to file reports on suspicious activity their institution identified.

Congress strengthened this law following the Sept. 11 terrorist attacks with the USA PATRIOT (Uniting and Strengthening America by Providing the Appropriate Tools Required to Intercept and Obstruct Terrorism) Act.

“Although we had more than 30 years of experience with anti-money laundering

these “pre-paid” cards can access cash at ATMs internationally—funds can be loaded, and often reloaded, onto a card in one country, and accessed at an ATM in another country.

Evolved money laundering techniques require enhanced monitoring and detection procedures, Thompson says.

Key players

There are a number of important players involved in regulating and enforcing the Bank Secrecy Act:

- Banks: Must have a formal, written compliance program, including regular training and demonstrated systems to ensure anti-money laundering compliance;
- Financial institution regulators: Review entities for compliance during examinations and ensure correction of deficiencies;
- Financial Crimes Enforcement Network (FinCEN): Compiles and coordinates the

distribution of the reports submitted by financial institutions, and issues both the compliance guidance to the industry as well as the fines (along with the regulators) for serious compliance deficiencies;

- Law enforcement: Reviews and investigates reports of suspicious activity filed by banks and other entities and prosecutes offenders.

In general, banks' most common and significant Bank Secrecy Act deficiency is the failure to report suspicious activity, Zubradt says.

To ensure compliance across the banking industry, several agencies are responsible. The Fed examines its member banks to assess their financial condition and check for compliance

In Kansas City, participants in monthly meetings include the IRS, FBI, Department of Homeland Security, regional U.S. Attorneys' Offices and local police. Staff from the Kansas City Fed and other regulators attend to offer technical assistance with banking laws and regulations, Zubradt says.

These reports and involvement from all parties have played a key role in the prosecution of criminal activity, including illegal transfer of funds to the Middle East, international drug trafficking, and insider embezzlement and fraud.

While the reports have been useful to investigations, bank resources dedicated to compliance can be significant. Recently the Treasury Department announced a four-prong

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with banking laws and regulations. State-chartered banks that are not members of the Fed are examined by the FDIC; the Office of the Comptroller of Currency examines nationally chartered banks.

Suspicious Activity Reports

The Bank Secrecy Act requires institutions to file Suspicious Activity Reports, which cover 21 categories of activity, including terrorist financing.

While there has been a significant increase in reports citing mortgage loan fraud and consumer loan fraud recently, about half of the reports filed are related to money laundering. More than 4 million reports have been filed nationwide since 1996, and nearly 1,000 are filed each year by state member banks in the District.

After a bank files a Suspicious Activity Report, it is reviewed by an examiner and reports of “insider abuse” are flagged. Law enforcement officials regularly review the reports and meet periodically as a group to follow up.

plan to ease the demands of complying with anti-money laundering laws and regulations:

- Develop a more risk-focused anti-money laundering compliance review for smaller and less complex institutions.

- Narrow the definition of money services business to better focus resources on those that present a significant risk of money laundering.

- Make anti-money laundering regulations easier to understand.

- Offer more feedback via FinCEN to participating agencies on the data they receive and analyze.

“The Federal Reserve Bank of Kansas City stands ready to assist with any new anti-money laundering laws as part of its mission to supervise financial institutions and ensure sound banking practices,” Zubradt says.



BY BRYE STEEVES, SENIOR WRITER