



BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

DIVISION OF BANKING
SUPERVISION AND REGULATION

SR 93-51 (FIS)
September 8, 1993

TO THE OFFICER IN CHARGE OF SUPERVISION
AT EACH FEDERAL RESERVE BANK

SUBJECT: Amendments to Money Laundering Laws and Related Legislation and Federal Reserve 1992 Report to Congress Regarding Administrative Enforcement and Criminal Investigatory and Prosecutorial Activities

Background

In October 1992, the Housing and Community Development Act of 1992 (the "HCD Act") was signed into law. One section of this new law, the Annunzio-Wylie Anti-Money Laundering Act of 1992 (the "Act"), contains numerous provisions related to enhanced anti-money laundering enforcement and related matters. Other sections of this legislation amend or establish new laws regarding the supervision of financial institutions.

Many of the provisions included in the Act are the result of recommendations of the G-7 Economic Summit Financial Action Task Force on Money Laundering ("FATF"). The FATF recommendations are intended to assure that all participating countries have uniform comprehensive domestic anti-money laundering programs to detect, deter, report and prosecute criminal activity related to money laundering. The FATF recommendations also are intended to assure the participation of law enforcement, banking supervisory agencies and bank and nonbank financial institutions in a concerted effort to detect and deter money laundering activities.

Set forth below is a summary of the provisions of these new laws that impact our supervision and enforcement activities with respect to domestic and foreign financial institutions subject to Federal Reserve jurisdiction. In general, the effective date of the new or amended provisions created by this legislation was October 28, 1992. In some cases, as noted below, a different effective date has been provided for in the legislation.

We have also attached for your information the Federal Reserve's annual report to Congress regarding our enforcement activities in 1992. This report is required by section 918 of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989.

Annunzio-Wylie Anti-Money Laundering Act

- **Appointment of Conservator** The Act provides Federal financial institution supervisory agencies with the authority to appoint a conservator to oversee the operations of a depository institution that is convicted of criminal violations of the money laundering [See footnote 1] or Bank Secrecy Act ("BSA") [See footnote 2] statutes. This provision

became effective December 20, 1992. [Section 1501][See footnote 3]

- **Revocation of License** The Act requires that, upon notification that a national bank, Federal branch or Federal agency has sustained a criminal conviction under the Federal money laundering statutes (i.e., 18 U.S.C. 1956 or 1957), the Comptroller of the Currency ("OCC") must notify the financial institution of its intention to terminate all rights, privileges and franchises of the financial institution and schedule a predetermination hearing for such purpose. The Act also provides that, upon notification that any of these institutions has sustained a criminal conviction under the BSA, the OCC may notify the financial institution of its intention to terminate all rights, privileges and franchises of the financial institution and schedule a predetermination hearing for such purpose. [Section 1502][See footnote 4]
- **Termination of Insurance** Similarly, the Act requires that, upon notification that a state insured depository institution has sustained a criminal conviction under the Federal money laundering statutes (i.e., 18 U.S.C. 1956 or 1957), the Federal Deposit Insurance Corporation ("FDIC") must notify the institution of its intention to terminate the insurance of the institution and schedule a hearing for such purpose. The Act also provides that, upon notification that any of these institutions has sustained a criminal conviction under the BSA, the FDIC may notify the financial institution of its intention to terminate the insurance of the institution and schedule a hearing for such purpose. [Section 1503][See footnote 5]
- **Factors for Revocation and Termination** In conducting the predetermination hearing for purposes of revoking the license or terminating the insurance of a financial institution, the appropriate Federal financial institution supervisory agency must take into account the following factors in its final decision:
 - the extent to which the institution's directors or senior management knew of or were involved in the criminal activity;
 - the extent to which the offense occurred despite the existence of policies and procedures designed to prevent the occurrence of such an offense;
 - the extent to which the institution has fully cooperated with law enforcement authorities with respect to the investigation of the offense of which the institution was found guilty;
 - the extent to which the institution has implemented additional internal controls to prevent the occurrence of any other similar offenses, since the commission of the offense for which the institution was found guilty; and
 - the extent to which the interest of the local community in having adequate banking services would be threatened by the closure of the institution.

[Sections 1502 and 1503]

- **Successor Liability** The revocation of license and termination of insurance provisions, as described above, do not apply to a successor of the interests of, or a person who acquires, an institution that violated the criminal laws if the successor succeeds to the interests of the violator, or the acquisition is made, in good faith and not for purposes of evading this

statute. [Sections 1502 and 1503]

- **Prohibition and Removal** The Act amends section 8(e) of the Federal Deposit Insurance Act (the "FDI Act") (12 U.S.C. 1818(e)) to allow for the removal and permanent prohibition of an officer, director or other institution-affiliated party if:
 - an institution-affiliated party has committed a violation of the BSA and such violation was not inadvertent or unintentional; or
 - an officer or director of a financial institution has knowledge that an institution-affiliated party of the financial institution has violated any provisions of the BSA or the money laundering statutes.[See footnote 6]

[Section 1504]

- **Suspension** The Act amends section 8(g) of the FDI Act (12 U.S.C. 1818(g)) to allow for the immediate suspension or prohibition of an institution-affiliated party whenever such institution-affiliated party is charged with the commission of or participation in:
 - a crime involving dishonesty or breach of trust which is punishable by a term of imprisonment for a term exceeding one year; or
 - a criminal violation of the money laundering or BSA statutes

if continued service or participation may pose a threat to the interests of the financial institution's depositors or may threaten to impair confidence in the depository institution. [Section 1504]

- **Effective Period/Permanent Order** Prohibitions or suspensions under section 8(g) of the FDI Act(12 U.S.C. 1818(g)) must now remain in effect until the final disposition of the criminal charges. At that time, if the conviction is for a crime involving dishonesty or breach of trust, a permanent order of removal or prohibition order may be issued. If the conviction is for a violation of the money laundering or BSA statutes a permanent order of removal or prohibition order must be issued. [Section 1504]
- **Termination of Foreign Banking Operations** The Act provides that if:
 - a foreign bank that operates a state agency, state branch that is not an insured branch or a state commercial lending subsidiary;
 - a state agency;
 - a state agency that is not an insured branch; or
 - a state commercial lending subsidiary

has been convicted of a money laundering or BSA offense, the Federal Reserve must issue a notice of its intention to commence a termination proceeding. [Section 1507]

- **Know Your Customer** The Act permits the Department of the Treasury ("Treasury") to

issue regulations requiring financial institutions to maintain appropriate procedures to guard against money laundering. Treasury staff have indicated their intention to issue regulations requiring financial institutions to adopt "know your customer" procedures. [Section 1513]

- **Anti-Money Laundering Program** The Act provides that Treasury may require, through regulations, all financial institutions to carry out anti-money laundering programs to guard against money laundering, including, at a minimum:
 - the development of internal policies, procedures and controls;
 - the designation of a compliance officer;
 - an ongoing employee training program; and
 - independent audit function to test programs.

Currently, only depository financial institutions are required to have a program similar to the proposed program. For example, the Board's Regulation H requires the development of policies and procedures, similar to the proposed program, to ensure compliance with the BSA. Nondepository financial institutions are not currently required to maintain such programs. [Section 1517]

- **Reporting Suspicious Transactions** The Act provides that any financial institution that, in good faith, makes a disclosure of a possible violation of law or regulation cannot be held civilly liable under any law or regulation of the United States or any state or political subdivision thereof, as a result of such disclosure.

Additionally, under this provision, any financial institution that reports a suspicious transaction is prohibited from notifying any person involved in the transaction that the transaction has been reported.

This provision also allows Treasury to require financial institutions to report any suspicious transaction relevant to a possible violation of law or regulation. [Section 1517]

- **Funds Transfer Recordkeeping Regulations** The Act requires Treasury and the Federal Reserve to prescribe joint regulations requiring insured depository institutions, check cashing services, money transmitting businesses and businesses that issue or redeem monetary instruments (e.g., money orders, travelers' checks, etc.) to maintain records of international funds transfers and international book transfers. Any records required to be maintained under this section must be submitted to Treasury or the Federal Reserve upon request.

This provision also allows for Treasury and the Federal Reserve to prescribe recordkeeping requirements for domestic funds transfers if it is determined that the maintenance of such records will have a high degree of usefulness in criminal, tax or regulatory investigations or proceedings.[See footnote 7] [Section 1515]

- **Geographic Targeting** The Act prohibits financial institutions from disclosing the existence of geographic targeting orders that require financial institutions to file Currency

Transaction Reports ("CTRs") for amounts under \$10,000. [Section 1514]

- **Access to CTRs** The Act provides state financial institution supervisory agencies with increased access to CTRs. [Section 1506]
- **Nonbank Financial Institutions** The Act requires Treasury, by January 1, 1994, to prescribe regulations requiring banks to identify and obtain information about customers that are nonbank financial institutions and allows for the imposition of civil money penalties of up to \$10,000 per day for failure to report or for material misstatements or omissions in reporting. [Section 1511]
- **Collection of CTRs** The Act provides that Treasury may require financial institutions to obtain CTRs from their nondepository financial institution customers that file CTRs. [Section 1562]
- **Money Transmitters** The Act makes it a Federal crime to own or operate an illegal money transmitting business that is operating without an appropriate state license and provides for the forfeiture of any property involved in such a crime. [Section 1512]
- **Right to Financial Privacy Act ("RFPA")** The Act amends the RFPA (12 U.S.C. 3412(f)) to allow for the disclosure of customer information by financial institutions to Treasury for criminal investigative purposes relating to money laundering and other financial crimes. [Section 1516]
- **Anti-Money Laundering Training Team** The Act requires Treasury and the Department of Justice ("Justice") to establish a team of experts to provide training to foreign governments in the investigation and prosecution of money laundering and related violations. [Section 1518]
- **Structuring Transactions** The Act prohibits the structuring of transactions to avoid the recordkeeping requirements for the purchase of monetary instruments of between \$3,000 and \$10,000. [Section 1535]

The Act also prohibits the structuring of transactions with regard to the import or export of monetary instruments to evade Treasury's Currency or Monetary Instrument Reporting requirements. [Section 1525]

- **Notice of Grand Jury Subpoenas** The Act amends the RFPA (12 U.S.C. 3420(b)(1)(A)) to preclude the disclosure of the existence of a grand jury subpoena to possible suspects for bank records in investigations related to money laundering, the BSA or controlled substances. [Section 1532]
- **Negligent Violations of the BSA** The Act allows Treasury to impose a civil money penalty of not more than \$500 for any negligent violation of the BSA by a financial institution and a civil money penalty of not more than \$50,000 for any pattern of negligent violations of the BSA by a financial institution. [Section 1561]
- **Studies and Reports** The Act requires the Attorney General, in consultation with the Secretary of the Treasury and the Board of Governors, as well as other appropriate parties, to conduct a study on the feasibility of reimbursing financial institutions for assembling or

providing financial records on corporations and other entities. [Section 1541]

The Act also requires Treasury to establish an advisory group that will provide a means by which it can inform the private sector as to the ways in which BSA and voluntary suspicious transaction reports are being used. The advisory group is also tasked with making recommendations on modifying the recordkeeping and reporting requirements of the BSA. [Section 1564]

- **Preservation of Privilege** The Act adds section 11(t) to the FDI Act (12 U.S.C. 1821(t)) which allows the Federal financial institution supervisory agencies to share information between agencies without waiving certain well established privileges, such as the work product or attorney-client privileges.[See footnote 8] [Section 1544]
- **Information Sharing Related to Safety and Soundness** The Act requires that the Justice and Treasury Departments and all other agencies and instrumentalities of the United States, unless prohibited by law, disclose to the appropriate Federal banking agency any information that such department or agency believes raises significant concerns regarding the safety or soundness of any depository institution doing business in the United States. [See footnote 9] [Section 1542]

Regulatory and Miscellaneous Provisions of the Housing and Community Development Act

- **Amendments to Federal Reserve Act - Insider Loan Provisions** The HCD Act clarifies the current Board position that section 22(h) of the Federal Reserve Act (the "FRA") does not apply to transactions between a member bank and its bank holding company, but rather that sections 23A and 23B of the FRA apply to such transactions. This provision also gives the Board the authority, under section 22(h)(9)(D) of the FRA (12 U.S.C. 375b(h)(9)(D)), to exempt by regulation from the limitations on insider loans transactions deemed by the Board to pose minimal risk. [Section 955]
- **Compensation Authority** The HCD Act amends the FDI Act to provide that the compensation standards that are to be set pursuant to section 39(d) of the FDI Act (12 U.S.C. 1831(d)) may not make reference to specific levels or ranges of compensation for directors, officers or employees. However, this does not affect the ability of a Federal banking agency to restrict compensation under other provisions of law or to restrict compensation paid to a senior executive officer of an undercapitalized depository institution under the prompt corrective action provisions of the Federal Deposit Insurance Corporation Improvement Act of 1991. [Section 956]
- **Clarification of Agency Discretion as to Certified or Licensed Appraisers** The HCD Act clarifies existing law added by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, and codified at 12 U.S.C. 3341, to provide that the appropriate Federal banking agency may set higher thresholds for transactions requiring certified or licensed appraisers if no safety and soundness issues are raised by changing the threshold. The General Accounting Office is ordered to conduct a study on the effects of the appraiser requirements on the cost and quality of housing credit. [Section 954]
- **Additional Grounds for Assessment of Civil Money Penalties** The HCD Act adds to the grounds for assessment of civil money penalties violations of section 39 of the FDI Act (12 U.S.C. 1831s) relating to regulatory operational and managerial standards, asset quality,

earnings and capital standards, and compensation standards. [Section 1603(d)(3) and (4)]

- **Clarification of Board's Authority to Review Creditworthiness of Institutions Under FDIC Control** The HCD Act clarifies that, notwithstanding FDIC conservatorship of an insured depository institution, the Board continues to be entitled to examine the institution in connection with the grant of advances or discounts to the institution. [Section 1603(e)(2)]
- **Foreign Bank Subsidiary Requirement** The HCD Act provides that foreign banks are required to establish subsidiaries for deposit taking only if the deposits are domestic retail deposits of less than \$100,000 requiring deposit insurance. [Section 1604(a)(11)]
- **Technical Amendment to Exception to Insider Overdraft Prohibition** The HCD Act clarifies that an exception to the general rule prohibiting a bank from paying an officer's or director's overdraft applies if the overdraft is paid either from: (i) a written preauthorized interest-bearing extension of credit specifying a method of repayment; or (ii) a written preauthorized funds transfer from another account of the officer or director at the bank. The exception, prior to this amendment, required that both prongs of the test be met. [Section 1605(a)(10)]
- **FDIC Backup Enforcement Authority** The HCD Act expands section 8(t) of the FDI Act (12 U.S.C. 1818(t)) to provide the FDIC with backup authority over institution-affiliated parties of insured depository institutions, as well as over the institutions themselves. This change means that we must notify the FDIC of any enforcement actions recommended against institution-affiliated parties of state member banks, as well as against the banks themselves. [Section 1605(a)(11)]

In the event that you have any questions concerning any of the matters described herein, please contact Richard A. Small, Special Counsel, at (202) 452-5235, or me at (202) 452-2620.

Herbert A. Biern
Deputy Associate Director

ATTACHMENT MAY BE OBTAINED FROM FEDERAL RESERVE BANK

Footnote: 1 18 U.S.C. 1956 or 1957.

Footnote: 2 31 U.S.C. 5322.

Footnote: 3 The section numbers of the relevant provisions of the Act being summarized appear in brackets.

Footnote: 4 This section requires the Office of Thrift Supervision and the National Credit Union Administration ("NCUA") to take similar action with regard to Federal savings associations and credit unions, respectively.

Footnote: 5 This section requires the NCUA to take similar action with regard to insured state credit unions.

Footnote: 6 Generally, with regard to money laundering offenses only, the Act eliminates the

requirement that an institution-affiliated party received a personal gain or a banking organization suffered a loss in order to effect a removal or permanent prohibition. Prior to this change in the law, it was difficult to remove or permanently bar an individual involved with money laundering activities under section 8(e) of the FDI Act because the law required a showing of either personal gain or loss to a banking organization--two factors that were often missing when, for example, a bank officer facilitated a money laundering scheme.

Footnote: 7 Staffs of the Board and Treasury have been working in close association to develop regulations required by this section of the Act. It is anticipated that the proposed regulations will be released prior to year end.

Footnote: 8 This new provision of law has had a significant impact on our ability to obtain critical supervisory information from the other Federal banking agencies, including the FDIC acting as receiver of failed banks. By providing in the statute that no privilege is lost through the transfer of information among the banking agencies, the most often expressed concerns of the FDIC's staff responsible for closed banks has been assuaged. We have, thus, been able to obtain information from particular closed bank files that were difficult to obtain in the past due to the assertion by the FDIC that the materials were covered by attorney-client or other privileges.

Footnote: 9 The staffs of the Federal banking agencies, in conjunction with Justice, developed an interagency notification regarding this provision of the Act, which was issued by Justice on May 3, 1993. The Justice notification alerted all Federal departments and agencies regarding their responsibilities to report information that significantly impacts on the safety and soundness of banking organizations to certain designated Federal banking agency representatives. At the Board, Herbert A. Biern, Deputy Associate Director, has been designated as the agency representative for the purposes of this new law.