FINANCIAL SERVICE CENTERS OF AMERICA, INC.
A NATIONAL TRADE ASSOCIATION

Statement of

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Before the
U. S. House Committee on Financial Services
Subcommittee on Oversight and Investigations

Regarding
Suspicious Activity and Currency Transaction Reports: Balancing Law Enforcement Utility and Regulatory Requirements

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Chairman Watt, Ranking Member Miller, and esteemed Members of the Subcommittee, my name is Scott McClain. I serve as Deputy General Counsel to the Financial Service Centers of America, also known as FiSCA. On behalf of the FiSCA membership, I am grateful for the opportunity to appear today to discuss Suspicious Activities and Currency Transaction Reporting by the community financial services industry, and the regulatory burdens on this industry resulting from the current CTR/SAR reporting regime.

FiSCA is a national trade association representing over 6,000 neighborhood financial service providers operating throughout the United States. Our members are classified under the Bank Secrecy Act ("BSA") as "money services businesses" or "MSBs," and as such are subject to stringent federal anti-money laundering reporting and recordkeeping requirements. By way of introduction, our membership is comprised of community-based financial institutions, which serve millions of customers from all walks of life, including those with bank accounts as well as the "unbanked." Our members provide a range of financial services and products, including check cashing, remittances, money order sales, and utility bill payment services, to name a few. Our industry includes large, publicly traded entities operating thousands of locations, down to corner grocery store "mom and pop" establishments offering ancillary financial services.

The success of the community financial services industry is a direct result of its ability to respond to the needs of our customers; in this regard we specialize in delivering three basic commodities that today's consumers need with regard to their finances: convenience, liquidity and choice. The marketplace has shown us that check cashers and other MSBs are best positioned to deliver these features to our customers; a recent national FiSCA survey found that 97% of our customers rate our services from "excellent" to "good."

The MSB industry is not a "shadow economy" operating on some imaginary parallel track with more traditional financial institutions, and serving a separate consumer base. We serve the working men and women of this country in the communities in which they live – and we are very much a part of the mainstream of a vibrant national economy.

FiSCA and its members have committed significant resources in the fight against money laundering and financial crime. As an industry, we recognize the need for strict adherence to BSA compliance requirements, and the need for comprehensive education of MSB personnel. Some of our compliance initiatives have included development of specialized industry guidance materials and manuals, creation of Internet-based compliance courses, and issuance of model compliance policies and procedures to assist the industry in meeting requirements under the USA PATRIOT Act. Additionally, FiSCA hosts an annual conference, where we offer seminars, workshops and materials on BSA compliance.

FiSCA and its members continue to work with FinCEN and IRS, as well as our

state regulators, in reaching out to the broader community financial services industry, and in supporting an effective and rational national anti-money laundering strategy.

Mr. Chairman, in accordance with your May 3, 2007 letter, you have invited us to address the regulatory and cost requirements to financial institutions with regard to current SAR and CTR regulations, and their impact on the community financial services industry. We are grateful for this opportunity to make the following general observations and recommendations:

1. Information generated from SARs and CTRs is reported to be valuable to the goals of law enforcement in combating money laundering and financial crime. Clearly, however, regulatory pressures and the lack of clear guidance in this area have resulted in a tremendous number of defensive SAR filings, and duplicative CTR filings, at a tremendous cost to industry. Critical analysis of the efficacy of the current SAR and CTR regulatory framework, and its impact on the MSB industry, is needed.

2. Increased compliance, transaction monitoring and operational costs associated with SARs and CTRs have significantly burdened the MSB industry, as well as the banks that serve us. These growing costs translate into a downward pressure to increase transaction fees charged to our customers in order to sustain existing revenue levels. In those states where MSB transaction fees are governed by statute, MSBs are caught in a vice and must find other means of covering these expenses. The value of SAR and CTR information to law enforcement should be weighed against its cost to the MSB industry and consumers.

3. MSBs provide critical financial services in communities across the U.S., and provide an infrastructure for remittance flows that support economies in many countries. An unintended consequence of the federal anti-money laundering policy has been a trend among banks and other depositories to terminate their MSB customers. This trend threatens the legitimate MSB industry, and may ultimately cause MSB customer transactions to migrate to untraceable channels. In the interests of federal anti-money laundering policy, depositories should be relieved of excess regulatory burdens applicable to serving the MSB industry.

Regulation of the MSB Industry

The community financial services industry is regulated on both the federal and state levels, and is subject to many of the same types of reporting and recordkeeping requirements as banks and other depositories. Money services businesses, as that term is defined under the Bank Secrecy Act, include check cashers, money transmitters and their agents, issuers and sellers of money orders, traveler's checks and other monetary instruments, currency dealers and exchangers, and issuers and sellers "stored value" products such as prepaid debit and gift cards.

In accordance with provisions of the USA PATRIOT Act of 2001, most types of MSBs are required to register with the Department of the Treasury, and renew their

registration status on a bi-annual basis. As of April 4, 2007, more than 36,000 companies were listed on FinCEN's public database of registered MSBs.

In accordance with Section 352 of the USA PATRIOT Act, all MSBs, regardless of size or location, are required to maintain 4-part anti-money laundering compliance programs, including written policies and procedures, appointment of compliance officers, employee training programs, and periodic independent examinations to ensure that anti-money laundering programs are properly and effectively administered. These systems must be specifically tailored to address the unique risk profile of each individual company, and the financial products and services that each provides.

As federally regulated financial institutions, MSBs are subject to rigorous compliance examinations by Internal Revenue Service agents. In a typical BSA examination, the IRS examiner will focus on key areas to ensure that the company's written policies and procedures are appropriate, that employees are properly trained, that the company has adequate cash controls, and controls for appropriate SAR and CTR reporting. In our view, IRS has done exceptionally well in identifying MSBs for examination, and in executing its overall MSB examination strategy. In larger metropolitan centers, virtually all licensed money transmitters and check cashers have been examined, and many have been the subject of multiple examinations. Moreover, IRS's educational outreach to the MSB industry has been exceptional.

A significant and growing number of state banking agencies also regulate their check cashers and money transmitters, including compliance with State and federal anti-money laundering requirements. Some states subject their MSB licensees to rigorous periodic inspection by state bank examiners. As a result of the recent "Memoranda of Understanding" between FinCEN and various state agencies, a process is now in place to permit information sharing between the state authorities and the federal government on MSB examinations. The Money Transmitter Regulators Association, which is made up of MSB regulators from across the U.S., has also worked with the MSB industry to promote industry-wide compliance.

Contrary to the perceptions of some, the MSB industry's record of compliance with the BSA is quite good. As noted by IRS Fraud/Bank Secrecy Act Director Eileen Meyer in her September 12, 2006 testimony before the Senate Committee on Banking, Housing and Urban Affairs, in the first 8 months of 2006, IRS had conducted examinations of 5,481 MSBs, which resulted in only 17 referrals to FinCEN for potential administrative action, and 14 referrals to IRS-CI for further criminal investigation. That translates into a referral rate of approximately .57%, of which only a handful will result in actual administrative action or criminal conviction.

With respect to the check cashing industry, in particular, since April 1999, FinCEN has assessed a total of $360,500 in civil penalties against check cashers for BSA violations – yet during the same period it assessed well over $60,000,000 against banks and other financial institutions. Since 9/11, only two check cashers have been cited by FinCEN for BSA violations, resulting in civil penalties of only $35,000. Citing

recent examples, BSA violations involving depositories frequently involve tens of millions of dollars. Moreover, since the passage of the USA PATRIOT Act, IRS has dramatically increased the number and scope of BSA examinations of check cashers. Nonetheless, there has not been a corresponding increase in BSA violations found within the check cashing industry.

In short, although the MSB industry is often regarded with suspicion by federal bank regulators who may not fully understand this market sector, when viewed with the "more traditional" banking industry, the record reveals that MSBs truly measure up.

Suspicious Activities and Currency Transaction Reporting Requirements

SAR and CTR filing requirements are the cornerstones of U.S. financial crime enforcement strategy. As the main anti-money laundering weapons in our federal arsenal, it is important that their efficacy to law enforcement be critically evaluated to ensure that they are indeed generating the most valuable data possible.

The threshold dollar amount for MSB SAR filing is $2,000, whereas depositories must file at the $5,000 level. MSBs are required to file SARs (FinCEN Form 109) for transactions of $2,000 or more that are suspected of involving money laundering or other crimes. SARs are required in any instances where the MSB suspects that the funds involved in the transaction are derived from illegal activity or are being used for a criminal purpose, or where the transaction has no legitimate business purpose or is designed to evade a reporting requirement (e.g., a CTR filing). SARs are not limited to hard currency transactions; any suspicious use of funds transfers, monetary instruments or currency exchange should be reported. Although SARs are not mandatory in connection with check cashing transactions, check cashers may file SARs on a voluntary basis, and still enjoy the benefit of certain "safe harbor" provisions of the BSA.

MSBs have only been required to file SARs since April 13, 2000. As evident from figures published by FinCEN, the MSB industry has embraced its regulatory responsibilities in this area. During the first 6 months of 2006, MSBs filed some 270,718 SARs across the broad spectrum of MSB products and services. During this same period, banks and depositories filed 279,703 SARs.

With regard to Currency Transaction Reports, MSBs must file CTRs (FinCEN Form 104) on each deposit, withdrawal, exchange of currency or other payment or transfer, by, through, or to such financial institution which involves a transaction in currency of more than $10,000," conducted by or on behalf of the same person during the same business day. Examples of reportable transactions would include customer purchases of money orders, funds transfer requests, or check cashing transactions in excess of $10,000.

In fiscal year 2006, U.S. financial institutions, including banks and MSBs, filed nearly 16 million CTRs. As previously reported by FinCEN, it is suspected that as many as 30% of CTR filings are repeat filings on routine customer transactions. These

requirements create significant filing and recordkeeping burdens on MSBs and other financial institutions. Moreover, all of the data generated by these filings place significant demands on the federal government to ensure that the information is properly processed and analyzed, and that the information remains secure.

Direct Cost Factors

SAR and CTR compliance requirements have resulted in direct and substantial costs across the financial services landscape, including the MSB industry. Our members have identified Bank Secrecy Act compliance as among the largest costs facing community financial service providers. Generally, these costs are experienced in several key areas including increased labor, information technology costs, professional and service fees, and banking service charges.

With respect to the labor component, MSBs are required to train employees with regard to SAR and CTR requirements, including dollar thresholds, customer identification requirements, and identification of reportable transactions. Training must be provided on an ongoing basis. Moreover, MSBs are required to designate specific compliance officer personnel who are charged with the responsibility of ensuring that suspicious activities are investigated and documented, and that SAR and CTR reporting is accurate and completed in a timely manner. These requirements not only place more responsibilities on individual employees, but it also distracts them from their primary role in serving customers. These added duties must be satisfied either by hiring additional personnel, or expanding roles of existing personnel, both of which result in additional operational costs to MSBs.

Broken down, the man-hour driven component of compliance includes: (a) the development and maintenance of written policies and procedures (in the areas of customer identification, filing reports, creating and retaining records, and responding to law enforcement requests); (b) appointment of compliance officers to oversee compliance programs on an ongoing basis; (c) development and implementation of employee training programs, including written training materials, initial and ongoing training and testing; and (d) periodic independent reviews of compliance programs by qualified examiners to ensure that programs are properly administered.

The increase in information technology costs has been very significant. In an effort to meet ever increasing compliance requirements, a growing number of MSBs have been required to implement costly information systems designed to isolate reportable transactions, create and track customer transaction histories, and generate and store filed CTR and SAR information. Although estimates vary by financial institution, these costs have increased across the board. MSBs with multiple agents or branches are being required to implement advanced systems that have the ability to aggregate transaction information generated from different locations. As a result of BSA requirements that all records be maintained for at least 5 years, electronic data storage costs have also become a significant cost factor. Smaller MSBs, who have felt

the pressure to adopt information systems in order to meet ever increasing compliance responsibilities, have been particularly hard-hit.

Another significant cost factor has been in the area of increased professional and service fees to MSBs. BSA regulations require that MSBs must be subjected to periodic, independent examinations of compliance programs and systems to ensure that they are properly functioning. Frequently, MSBs look to outside experts and consultants to perform this highly specialized function. In many instances, MSBs are required by their depository institutions to retain counsel or outside compliance specialists as a condition of maintaining account relationships. On-site compliance audits and reporting, which is typically performed on an annual basis, can run from $1,000 per location into the tens of thousands of dollars, depending on the size and nature of the MSB.

Banks that service MSBs have likewise experienced mounting compliance and account monitoring costs associated with BSA requirements. Typically, these additional compliance costs are passed on to the bank's MSB customers in the form of increased service fees and charges. One FiSCA member reported that its bank now charges a "monthly compliance monitoring fee" of $2,000 in addition to all regular banking charges for each MSB account. Other FiSCA members have reported that their banks have tacked on flat monthly monitoring fees ranging from a few hundred to a few thousand dollars, regardless of actual account activity. Banking fees for MSBs have increased significantly since enactment of the USA PATRIOT Act.

Clearly, increased compliance and operational costs associated with SARs and CTRs have significantly burdened the MSB industry, as well as the banks that serve us. Studies by state MSB associations have demonstrated that these growing costs translate into a downward pressure to increase transaction fees charged to MSB customers in order to sustain existing revenue levels. In states where MSB transaction fees are governed by statute, MSBs are caught in a vice and must find other means of absorbing these expenses. Unlike depositories or other commercial enterprises, fee-regulated MSB's do not have the option to pass along increased regulatory compliance costs to the consumer.

In sum, MSBs truly bear the cost of our national BSA enforcement strategy. The MSB sector has been given little to no relief from the cost burden associated with their SAR and CTR compliance measures. Any analysis of the value of SAR and CTR information to law enforcement should take into account its cost to the MSB industry.

Defensive SAR Filings

It is common knowledge that following the events of 9/11 and implementation of USA PATRIOT Act, there has been a tremendous increase in regulatory scrutiny of the financial services industry. Across the board, all sectors of the financial services industry have responded to these pressures by engaging in a practice of defensive SAR filings. MSBs are persuaded that the key to avoiding sanctions under the BSA is to file reports on transactions involving even marginally irregular activity. As a result, FinCEN

and law enforcement agencies are deluged with and must process reports that are of dubious value. The information that these reports generate is largely useless, or worse, may serve to obfuscate otherwise valuable direct and statistical data.

We have seen that the pressure towards defensive filings emanates in many cases from field-level examiners who "second guess" decisions by compliance personnel. Our members have reported examples where examiners have been critical of MSBs who had not filed enough SARs, and examples where MSBs have been cited for not filing SARs on transactions that they knew to have a legitimate purpose. In response, rather than scrutinize and investigate anomalous customer activity (with the possibility of uncovering truly valuable information) MSBs and other financial institutions are adopting a "when in doubt, fill it out" philosophy and are filing simply to cover their backs.

The MSB industry has not been provided information as to the value SARs actually have to law enforcement. We have no sense as to the number of reports that lead to criminal investigations, and the number of those investigations that result in money laundering convictions. Without information regarding the actual value these reports serve, the MSBs submitting the reports become disillusioned with the bureaucratic red-tape. The underlying purpose and importance of accurate SAR filings is not communicated to industry, which further encourages defensive SAR filings.

To the extent that field examiners continue to be critical of SAR filing decisions, the trend towards defensive filings will be perpetuated. Clearly, further examiner guidance in this area is required.

Additionally, the value of the current $2,000 threshold for MSB reporting of suspicious activities should be reevaluated. Transactions at the $2,000 level are clearly within the realm of normal consumer activity, thus the current threshold should be adjusted upward based on current economic realities.

Need For Adjustment of the CTR Threshold

MSBs file millions of CTRs annually. Unlike depositories, there is no exemption procedure for MSBs permitting them to be relieved of CTR filing obligations on certain designated transactions. As outlined above, the CTR filing process has resulted in significant costs to the community financial services industry and its customers.

FiSCA supports an increase in the reporting threshold for currency transactions. The present $10,000 CTR threshold was established in 1970. Since that time, the threshold has not been increased and has been rendered out-dated due to inflation. Adjusting for inflation, $10,000 as of 1970 would be the equivalent of $52,963 in today's dollars. Considering the current volume of routine business activity in the $10,000 range, a failure to adjust the CTR threshold is causing the reporting system to be clogged with transaction information that is of little practical value to law enforcement.

Although some law enforcement officials have opposed any adjustment of the current CTR threshold due to concerns that valuable data may be lost, the propriety of the current threshold should be evaluated based on prevailing economic realities. An immediate benefit to law enforcement would be a more accurate data system, unburdened with information from millions of normal transactions. Moreover, it should be noted that an increase in the reporting threshold would in no way relieve financial institutions of the responsibility to report structured transactions or other suspicious activity at levels below the CTR threshold.

Bank Account Terminations

In addition to these direct cost factors, the post-9/11 BSA enforcement regime has inadvertently given rise to an indirect, yet very costly burden to the MSB industry: the termination of MSB bank accounts. The emergence of a bank discontinuance problem was initially reported by FiSCA to FinCEN in 2000. Since that time, the industry has seen an increasing trend of banks making wide-scale terminations of their check casher and money transmitter accounts. A growing number of banks presently serving the industry are refusing to open new accounts, or are placing onerous requirements on the accounts they maintain. Any assessment of the utility of SAR and CTR information to law enforcement should also take into account the impact that BSA compliance has had on the MSB industry.

Banks refer to undue regulatory pressure and attendant costs as the primary reason driving MSB account closures. There is no question but that depositories that service MSBs are faced with significant regulatory burdens, and are required to expend ever greater resources in maintaining MSB customer compliance and monitoring systems. Due to this uncertain regulatory environment, many banks have opted to discontinue their check casher and money transmitter customers.

The importance of the domestic MSB industry cannot be underestimated. MSBs provide critical financial services in communities across the U.S., and provide an infrastructure for remittance flows that support economies in many developing countries. Remittance flows from the U.S. to Latin America exceeded $62 billion in 2006. MSBs, by their very nature, are critically dependent on access to depository accounts and banking services in order to conduct business.

Thus far, a regulatory solution has eluded us. The MSB industry as a whole was encouraged by FinCEN's efforts in convening the March 2005 fact-finding hearing, and in spearheading the resulting Interagency Interpretive Guidance on Providing Banking Services to Money Services Businesses Operating in the United States (the "MSB Guidance"), issued April 26, 2005. Two years later, however, it is clear from reports from our membership that the MSB Guidance has not achieved the purpose of creating greater access to banking services for the industry. Since issuance of the MSB Guidance, there has been a net loss in the overall number banks willing to serve MSBs. We are aware of no major bank which, having previously terminated its MSB customers, has returned to the industry.

Loss of MSB bank accounts threatens to drive MSB customer transactions underground through unregulated channels, including bulk cash smuggling and other means. It is critical to the interests of national security that transparency of MSB transactions be maintained by ensuring that MSBs remain part of the regulated financial community and continue to have access to depository services.

FiSCA supports the introduction of an appropriate legislative solution designed to relieve our banks of excessive regulatory burdens in serving MSBs. Banks should not be expected to serve as the *de facto* regulator of their MSB customers, and should not be called upon to assess the effectiveness of the compliance systems of their MSB customers – a role clearly regulatory in scope.

In this regard, FiSCA has been instrumental in the formation of an MSB Coalition to examine possible solutions to the present accounts termination problem. The MSB Coalition is made up of representatives from all segments of the MSB community, including the check casher industry, money transmitters, money order processors, and others with interests in the MSB community. The goal of the MSB Coalition is to examine possible solutions to the bank discontinuance problem, linked to providing regulatory relief to banks servicing MSBs. The Coalition is reaching out to all members of the MSB community, as well as key state and federal regulatory bodies, in an effort to increase awareness and encourage participation in solutions on this and related issues.

Conclusion

In conclusion, regulatory pressures and the lack of clear guidance in this area have resulted in a tremendous number of defensive SAR filings, and duplicative CTR filings, at a tremendous cost to industry. Existing reporting thresholds should be reevaluated, and the current SAR/CTR reporting system and its cost to the financial services industry should be critically assessed.

The community financial services industry is committed to the ongoing battle against money laundering and terrorist financing. As with other sectors of the U.S. financial system, it is critically important that we protect the integrity and legitimacy of our industry. It is equally critical, however, that the MSB industry be recognized as being a part of a healthy financial industry, and partner in the war on financial crime.

Again, we thank you for the opportunity to present these views.