FinCEN Plans Significant Update to AML Regulations

Overview: In September, the Financial Crimes Enforcement Network (“FinCEN”) issued an advance notice of proposed rulemaking (“ANPR”) to solicit public comments relating to potential amendments to the anti-money laundering (“AML”) regulations. The announcement signals a potentially significant update of the Bank Secrecy Act’s (“BSA”) AML rules, which the agency hopes will “modernize the regulatory regime to address the evolving threats of illicit finance, and provide financial institutions with greater flexibility in the allocation of resources.” The ultimate purpose of this modernization is to ensure that financial institutions provide information with a high degree of usefulness in the most efficient manner to government authorities. FinCEN is considering revamping the rules applicable to all of the industries that have AML program requirements under its authority.

Background and Context

The BSA generally requires covered financial institutions to develop, implement, and maintain an “effective anti-money laundering program” that is “reasonably designed” to prevent the financial institution being used to facilitate money laundering and the financing of terrorist activities. However, these key phrases have never been clearly defined by FinCEN. And in recent years FinTech innovations have caused rapid evolution of the financial services sector, which in turn presents new challenges faced by financial institutions that must maintain effective and reasonably designed AML programs that account for these rapid changes. FinCEN acknowledges that financial crimes have “changed considerably in scope, nature, and impact since the initial passage of the BSA.” In response to the changing landscape of financial crimes FinCEN has been collaborating with other governmental agencies, law enforcement, and the financial services industry.

The BSA requires FinCEN to establish an advisory group, called the Bank Secrecy Act Advisory Group, which includes representatives from regulated entities. In October 2019, the BSA Advisory Group endorsed a set of recommendations drafted by its AML Effectiveness Working Group. Those recommendations focused on providing clarity and guidance to regulated financial institutions. FinCEN issued the ANPR in response to the Working Group’s recommendations.
Overview of the ANPR

The ANPR outlines the elements of an “effective and reasonably designed” AML program, and requests public input regarding 11 core questions. Specifically, FinCEN proposes to define an “effective and reasonably designed” AML program as one that:

- identifies, assesses, and reasonably mitigates the risks resulting from illicit financial activity—including terrorist financing, money laundering, and other related financial crimes—consistent with both the institution's risk profile and the risks communicated by relevant government authorities as national AML priorities;

- assures compliance with BSA recordkeeping and reporting requirements; and

- provides information with a high degree of usefulness to government authorities consistent with both the institution’s risk assessment and the risks communicated by relevant government authorities as national AML priorities.

In addition to requesting comments about these three core elements and objectives of an effective and reasonably designed AML program, FinCEN is soliciting input on other ideas that center on the effort to provide regulatory clarity and efficiency. For example, FinCEN asks whether it would be appropriate to impose an explicit requirement for a risk assessment process. Currently, no regulation explicitly requires financial institutions to perform a risk assessment, but the financial regulatory agencies have consistently advised that a risk assessment is crucial to any reasonably designed AML program. FinCEN is therefore considering implementing a rule that expressly requires a risk assessment process, with guidelines as to what should be included in a financial institution’s risk assessment. Some additional key areas on which the ANPR seeks comment include:

- whether FinCEN should periodically publish a list of strategic AML priorities, which should be considered and integrated into financial institutions’ risk assessments;

- whether FinCEN should consider regulatory changes that appropriately reflect the differences in risk profiles between the broad variety of financial institutions; and

- how FinCEN can best ensure a clear and shared understanding of how AML resources should be appropriately reallocated to higher priority areas.

FinCEN has asked for comments on the impact to the public, the regulated industry, law enforcement, and regulators, as well as comments on all aspects of the ANPRM. Comments must be received by November 16, 2020.

Outlook: Because FinCEN is proposing significant changes to a fundamental part of its regulatory framework, the ANPR provides an important opportunity for regulated financial institutions to share input on rules that will directly affect their compliance programs. This rulemaking, combined with separate efforts by Congress and other federal regulators to reform AML laws, signifies a potential sea change for AML requirements over the coming months.
Financial Regulators Propose Rule on the Role of Supervisory Guidance

Overview: On October 20, 2020, federal banking regulators jointly released notice of proposed rulemaking that would govern the role of supervisory guidance (the “NPRM”). The proposed rule would make certain clarifications to, and codify, a joint policy statement issued in 2018.

Background

In 2018, the Office of the Comptroller of the Currency (“OCC”), the Federal Reserve Board of Governors (“FRB”), the Federal Deposit Insurance Corporation (“FDIC”), the National Credit Union Administration (“NCUA”), and the Consumer Financial Protection Bureau (“CFPB” and together, the “Agencies”) issued a joint statement about the role of supervisory guidance (the “2018 Statement”). The Agencies established that while supervisory guidance “outlines the agencies’ supervisory expectations or priorities” for a given area, it “does not have the force and effect of law, and the agencies do not take enforcement actions based on supervisory guidance.” Supervisory guidance comes in many forms, including (among others) interagency statements, advisories, bulletins, policy statements, questions and answers, and FAQs. According to the Agencies, supervisory guidance is important in that it provides insight to regulated entities in a transparent way and helps maintain a consistent regulatory approach. However, the Agencies were careful to specify that supervised institutions would not be cited for not strictly complying with supervisory guidance. The Agencies also expressed an intent to limit the use of specific bright-line standards, such as numerical thresholds, in supervisory guidance. The joint statement was published after numerous financial services industry stakeholders in recent years criticized agencies’ use of supervisory guidance to bring enforcement actions against financial services companies, even though such guidance does not have the force of law and therefore cannot establish a basis for legal violations. On behalf of regulated financial institutions, the Bank Policy Institute and American Bankers Association submitted a petition for rulemaking, which urged the Agencies to codify the 2018 Statement as a rule. The petition strongly supported the 2018 Statement, but expressed concern that the 2018 Statement “may nevertheless leave room for examiners to continue to base examination criticisms on matters not based in law.” The petition requested two rulemaking actions:

- that the Agencies propose and adopt the content of the 2018 Statement through the notice and comment process of rulemaking; and
- that the proposed rule include a clear statement that Agency criticisms, sanctions, or actions will be based only on a violation of a statute, regulation, or order.

The Proposed Rule

The NPRM released in October states that the Agencies are seeking comments on a proposed rule that would codify the 2018 Statement, with certain clarifying changes that appear responsive to the industry petition. The proposed rule would also make the 2018 Statement, as amended, binding on the Agencies. The Agencies do note that, in some situations, examiners may reference supervisory guidance to provide examples of compliant conduct or practices, but reiterate that they will not issue an enforcement action on the basis of non-compliance with supervisory guidance.

The proposed rule makes certain clarifying changes to the 2018 Statement, largely in response to industry concerns expressed in the petition for rulemaking. Specifically, these changes include:
• The term “criticize” will include the issuance of “matters requiring attention” and other supervisory criticisms, including those communicated through board letters and supervisory recommendations.

• A clarifying statement that criticisms will not be based on a “violation” or “non-compliance with” supervisory guidance, but that “in some situations, examiners may reference (including in writing) supervisory guidance to provide examples of safe and sound conduct, appropriate consumer protection and risk management practices, and other actions for addressing compliance with laws or regulations.”

• Language reflecting the policy that supervisory criticisms should be specific about practices, operations, financial conditions, or other matters rather than “generic” or “conclusory” references to safety and soundness.

• Language making the 2018 Statement, as amended, binding on each of the Agencies.

In addition to a general request for comments on any aspect of the proposal, the Agencies have specifically requested public comments about: (i) the situations in which examiners providing examples of permissible conduct from supervisory guidance would be appropriate or inappropriate; (ii) whether it is sufficiently clear what types of agency communications are supervisory guidance; and (iii) any additional helpful clarifications to the 2018 Statement.

Outlook: The comment period is scheduled to run for 60 days after the date the proposed rule is published in the Federal Register. As of October 27, 2020, the proposed rule has not yet been published in the Federal Register. The 2018 Statement was generally well received by the industry, and this step by the Agencies to respond to industry concerns could further improve supervisory clarity and transparency.