Anti-Money Laundering Reform Is Under Serious Consideration

Summary
A flurry of action in late 2017 and early 2018 by industry representatives and several congressional committees indicates substantial support for reform of the federal anti-money laundering (“AML”) regime. Below is an outline of the most recent developments in this arena and what it may mean for financial institutions subject to the Bank Secrecy Act.

Current AML Policy Framework and Its Glaring Gaps

Despite the partisan rancor enveloping Washington, there appears to be bipartisan support for efforts to reform current AML laws, which financial institutions and regulators alike widely acknowledge have become increasingly costly and burdensome.

Since it was passed nearly five decades ago, the Bank Secrecy Act (“BSA”)—the legislative framework for AML—has been expanded by Congress several times in an attempt to combat crime (particularly drug trafficking), prevent money laundering, and disrupt financial networks that support terrorism. To identify and prevent such abuses, the BSA requires regulated institutions to implement and maintain substantial customer identification, recordkeeping, reporting, and compliance programs. Compliance with these requirements is increasingly onerous for regulated institutions and industry stakeholders are increasingly raising questions about the benefits to law enforcement from compliance with the varying requirements. According to the Heritage Foundation, a leading conservative think tank, the cost of complying with current AML rules is roughly $5 to $8 billion per year, but there are fewer than 700 convictions per year (this means that each conviction effectively costs at least $7 million to prosecute). Further, the U.N. estimates that the amount laundered every year is roughly $800 billion to $2 trillion per year, but less than one percent is seized by law enforcement.

As more data like this is revealed, industry stakeholders and regulators have begun to acknowledge that it is time to revisit the existing AML framework, assess its effectiveness, and consider regulatory and statutory changes. Recent efforts to that end are summarized below.
Indications of Imminent AML Reform

Industry Action: In 2017, The Clearing House—the trade association that represents the largest U.S. banks—recommended a robust redesign of the entire AML compliance framework in an attempt to close some of the existing system’s gaps between cost and effectiveness. The Clearing House’s redesign highlights outdated and inefficient practices and recommends changes that could make the framework more effective for both law enforcement and compliance purposes. One of The Clearing House’s central observations is that, under the current framework, bank examiners are focused on ensuring compliance with myriad requirements at the exclusion of allocating AML resources to the particular processes that might be of greatest use to law enforcement. Another observation is that the current framework fails to take advantage of today’s data mining technologies and that these technologies could, and should, be leveraged to facilitate the flow of data from financial institutions to law enforcement. For example, a government agency could develop technology solutions to mine certain raw financial data from regulated institutions instead of requiring the institutions to expend significant resources developing paper trails and filing documents to report such data. This, combined with other changes—such as raising the dollar amounts that trigger certain reporting requirements from existing levels, most of which were set in 1996, to levels that more accurately reflect today’s financial figures and risks—could help close the gaps between increasing numbers of filings and declining value to law enforcement.

Congressional Action: Members of Congress have introduced several draft bills on this subject in 2017, including the Counter Terrorism and Illicit Finance Act (the “CTIFA”), which closely tracks The Clearing House’s recommendations. For example, the CTIFA, which has yet to be filed but has garnered much discussion, would raise the dollar amount thresholds for certain required reports, such as currency transaction (from $10,000 to $30,000) and suspicious activity ($5,000 to $10,000) reports. Another topic addressed by both documents is beneficial ownership information. In 2016, the Financial Crimes Enforcement Network (FinCEN) issued a final rule on Customer Due Diligence (CDD), which enters into effect on May 11, 2018. The rule requires regulated financial institutions to identify and verify the identity of the beneficial owners of its legal entity customers—those who own 25% or more equity interest in, or receive benefits that enable the person to control, manage, or direct, the entity. However, states are not required to record beneficial ownership information of the legal entities they incorporate; thus, regulated institutions must expend significant resources to investigate such information. The CTIFA, similar to a proposal in The Clearing House’s publication, would require legal entities to submit a list of their beneficial owners to FinCEN; FinCEN would use this information to create and maintain the first ever national database of beneficial owners that could be accessed by law enforcement and regulated institutions (with customer consent)—a move that is expected to not only cut diligence costs for regulated entities, but also to aid in criminal enforcement. Legal entities that fail to comply with the reporting requirement would be subject to civil and criminal penalties.

In November 2017, subcommittees of the House Financial Services Committee held a joint hearing to discuss, in part, the CTIFA. At the hearing, entitled “Legislative Proposals to Counter Terrorism and Illicit Finance,” industry experts expressed broad support for the CTIFA’s proposals, noting that AML reform was necessary and the CTIFA’s proposals had the potential to immediately increase the usefulness of AML information for law enforcement while reducing the burden on regulated entities.

In January 2018, the Senate Committee on Banking, Housing and Urban Affairs held hearings (and see here) at which witnesses, including the president of The Clearing House, expressed bipartisan support for, and gave recommendations regarding, modernizing the current AML framework. In a rare expression of agreement, Banking Committee Chairman Mike Crapo (R-ID) and Sen. Elizabeth
Warren (D-MA) agreed that the current framework is outdated by decades and needs to be reworked. Further, Senator Warren expressed support for increasing reporting thresholds and establishing new beneficial ownership requirements.

**Outlook:** The CTIFA contains the most significant changes to the AML framework in almost 20 years. Although it is too soon to assess whether, or how successfully, this legislation will move forward, it appears to have support from both sides of the political aisle—no easy feat in the current partisan climate. Whether it is through this legislation or another vehicle, broad support from industry members and regulators alike indicates that updates to the current AML framework are under serious consideration.

Craig Saperstein, a member of NACHA’s Government Relations Advisory Group, is an attorney in the Public Policy practice of Pillsbury Winthrop Shaw Pittman LLP in Washington, D.C. In this capacity, he provides legal analysis for clients on legislative and regulatory developments and lobbies congressional and Executive Branch officials on behalf of companies in the payments industry. Deborah Thoren-Peden is a partner and member of the Financial Institutions Team at Pillsbury Winthrop Shaw Pittman LLP. She provides advice to financial institutions, bank and non-bank, and financial services companies. Andrew Caplan is an associate and member of the Financial Institutions Group and the Privacy, Data Security, and Information Use Focus Team at Pillsbury Winthrop Shaw Pittman LLP. He counsels and defends financial institutions, technology companies, and other clients that offer consumer products or services on a range of issues related to credit, payments, data privacy, cybersecurity, and e-commerce. The information contained in this update does not constitute legal advice and no attorney-client relationship is formed based upon the provision thereof.