

ANTI-MONEY LAUNDERING COMPLIANCE:
COMPLEX, EXPENSIVE & ESSENTIAL
By William M. Isaac*

It seems there are two kinds of banks in the United States: i) those that have been criticized by their regulator for their failure to comply fully with the anti-money laundering laws, and ii) those that have not had a compliance exam during the past year. The degree and fervor of regulatory scrutiny – and the resulting banker concern – have reached levels not experienced since the real estate bust in the early 1990s.

Any bank that is not paying a lot of attention to its anti-money laundering programs will likely not be under the same management a year or two down the road. Strong compliance in this area is complex and expensive – and absolutely essential. It is difficult to imagine how far regulation has evolved in the 30-some years since the Bank Secrecy Act was adopted in 1970. When I was general counsel of a regional bank in the 1970s, I recall that one of my concerns was whether the bank should respond to IRS subpoenas for customer records without first giving the bank customer notice and the right to seek court protection against the potential invasion of privacy.

Now banks are filing “Suspicious Activity Reports” with respect to customer accounts by the hundreds of thousands each year and in many cases are cutting off their banking relationships with those customers. Just last week, a Senate subcommittee recommended that banks go further and warn other banks when they shut an account because of money laundering concerns. There’s

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not even a whiff of due process in that recommendation, which could bring permanent irreparable harm to a customer falsely accused of being “suspicious.”

The first major wave of regulatory activity in the anti-money laundering area was directed at tax evasion and organized crime, which were usually fellow travelers. While banks grumbled about the compliance costs and the invasion of customer privacy, enforcement was not a major problem for most banks as the money laundering activity was centered in a few metropolitan areas and the sums of money were relatively large and easy to follow.

Then came 9/11 and the war on terror, which President Bush announced on September 24, 2001: “We will direct every resource at our command to win the war against terrorists, every means of diplomacy, every tool of intelligence, every instrument of law enforcement, every financial influence. We will starve the terrorists of funding.” Those few words changed the banking world forever.

Tracking the funds of organized crime is relatively easy compared to tracking terrorist funding. For the most part, law enforcement knows who the significant figures are in organized crime and where they are located, while terrorists hide in the shadows. And criminal organizations, particularly drug dealers, need to launder vast sums of money.

The Financial Crimes Enforcement Network (FinCen) puts it this way: “With only relatively small sums from the proceeds of traditional illegal activities, terrorist financing contrasts with the finances of a drug trafficking network, which earns virtually all of its profits from illegal activities and moves huge amounts of money. The financial dealings of a terrorist organization, whose members tend to live modestly and whose funds may be derived from

outwardly innocent contributors to apparently legitimate humanitarian, social and political efforts, are considerably more difficult to investigate than those of a drug trafficker.”

The war on terror requires a much more nuanced and sophisticated approach to anti-money laundering programs. And the potential cost to the civilized world of failure is much higher than the cost of failing to shut down a drug dealer.

My view is that our nation’s current approach to the anti-terrorist financing battle is not nearly as well designed and implemented as it must be if we are to succeed. We are using the heavy handed and obsolete machinery of the war on crime to fight a very elusive and evasive new enemy.

FinCen Director William Fox got it precisely right the other day when he said, “We cannot win the battle against terrorist funding without enlisting the banks as our partners. We need to have a collaborative relationship with the banks, not an adversarial relationship.”

Bankers are among the most patriotic and civic minded of all citizens. They want to help fight and win the war on terror. They absolutely do not want to unwittingly provide funds to terrorist organizations.

What bankers need is much better communication with and cooperation from the regulatory agencies. As Director Fox put it, “We cannot play ‘gotcha’ with banks on their failures to file individual SARs. We need to develop a risk-based system of regulation and oversight that is focused on making sure that the banks have the systems in place to catch most of the suspicious activities most of the time. And because terrorist funding can be so difficult to detect, we need to communicate more clearly to the banks what we are looking for to the extent we can do so without compromising our investigations.”

Criminalizing systems failures and imposing huge fines on respected banks – AmSouth, for example – is no way to create a partnership with the banking industry. It can only result in forcing banks to flood the system with large numbers of defensive SARS and/or to cut off access to the U.S. financial system by money transfer firms and foreign banks located in high risk areas of the world where we already have too few friends. In the end, terrorist funding will likely go further underground and out of sight.

Congress, in my judgment, needs to play a more constructive role in this area than it has thus far. Banks and bank regulators are struggling to get it right in this new war. When they make mistakes, as they did in the Riggs case, Congress needs to show some restraint in its criticisms. A public tarring of the Comptroller of the Currency in the Riggs case runs the risk of creating an unhealthy “zero tolerance” policy inside all of the banking agencies not unlike what we experienced in real estate examinations in the early 1990s, which caused incalculable damage to our financial system and economy.

The civilized world is engaged in what will surely be a long and difficult war against terrorism. One front on which we must prevail is curtailing the terrorists’ access to funding. This is a very difficult task under the best of circumstances – and an impossible task if the government and the private sectors are not locked arm in arm.