Consumer Finance Monitor (Season 3, Episode 14): A Look at Two Recent OCC Bank Secrecy Act/Anti-Money Laundering Consent Orders: Lessons Learned

Speakers: Chris Willis, Peter Hardy, and Mary Treanor

Chris Willis:

Welcome to the Consumer Finance Monitor podcast, where we explore important new developments in the world of consumer financial services. And what they mean for your business, your customers, and the industry.

Chris Willis:

I'm your host, Chris Willis. And I'm the practice group leader of Ballard Spahr's Consumer Financial Services Litigation Group. And I'll be moderating today's program.

Chris Willis:

For those of you who want even more information, don't forget about our blog, consumerfinancemonitor.com. We've hosted the blog since 2011, so there's a lot of relevant industry content there. We also, regularly host webinars on subjects of interest to those of us in the industry. So, to subscribe to our blog or to get on the list for our webinars, just visit us at ballardspahr.com. And if you like our podcast, please let us know, leave us a review on Apple Podcasts, Google Play, or wherever you get your podcasts.

Chris Willis:

Now, today I'm joined by two very special guests, Peter Hardy and Mary Treanor, both in our white collar and litigation groups in our Philadelphia office. And we're going to be talking about recent OCC enforcement actions involving Bank Secrecy Act and Anti-Money Laundering issues. Peter and Mary, welcome to today's podcast, and thank you for joining us.

Mary Treanor:

Thank you for having us.

Chris Willis:

So, Peter let's set the stage, before we start talking about any specific recent OCC actions, what are some of the general issues that the OCC will look at in terms of BSA-AML compliance?

Peter Hardy:

Yeah. Thank you, Chris. And thanks everyone for joining us here today. So, the Office of the Comptroller of the Currency is authorized to take enforcement actions against a couple of different institutions. National banks, of course, federally chartered savings associations and their subsidiaries. Also, federal branches and agencies of foreign banks. And also, affiliates of the institutions as they're defined. But importantly, that includes individuals: officers, directors, employees, and sometimes even controlling stockholders, or agents.

Peter Hardy:

So, today, we're going to focus on two AML enforcement actions, AML related enforcement actions. We are not going to discuss everything that's been going on in terms of OCC enforcement actions. We're going to pick out two examples. One of them is an institution, and the other one is an individual. Now in general, Chris, and kind of keeping with your introductory

question, so the OCC puts out a lot of material and a lot of information. And one of the things that they've said in a bulletin is that, and not surprisingly, in terms of violations of the Bank Secrecy Act, Anti-Money Laundering policies one of the things that they definitely look at is anything that results in repeated or uncorrected BSA compliance problems. And that's probably the number one issue. And if you get to that, there is a statute that requires the OCC to issue a cease and desist order.

Peter Hardy:

Now, just looking at the BSA, for a moment in general, outside of the OCC... And, by the way, a lot of the stuff that Mary and I are going to talk about today, we're doing it through the prism of OCC enforcement actions. But, in many ways, what we're going to talk about can be really applicable to any sort of regulator. So, in terms of the Bank Secrecy Act, and we're going to keep it very high-level here, there's five basic pillars of any Anti-Money Laundering compliance policy for a financial institution.

Peter Hardy:

And those five pillars are as following, and you're going to hear these issues come up as we get into the details of these two enforcement actions. It's development of internal policies, procedures, and related controls. Designation of a compliance officer who, obviously, needs to know what he or she is doing. It's a thorough and ongoing training program. Independent review of compliance. And lastly, and most recently it's ongoing CDD, or customer due diligence. And this gets into the beneficial ownership rule.

Peter Hardy:

Now, looking at those five pillars and kind of back to some of the OCC's very broad communications and guidance, another thing that they absolutely stress is clear communication between the OCC and management, of course, and importantly, the board. And this is consistent with general concepts for BSA examinations across the board and the government. The BSA-AML examination manual states that the board is, ultimately, responsible for ensuring BSA compliance. And that the compliance officer has sufficient authority and resources, so he or she can do her job or his job.

Peter Hardy:

And then, finally, and then I'm going to step back, in general, whether it be the BSA or any sort of banking violation, the OCC has issued guidance in its procedures manual stating that there's a presumption in favor of a formal bank enforcement action when any one of a couple of things happen. And, of course, these need to happen to a sufficient degree. And you'll not be surprised to hear that they include significant insider abuse. That there is systemic or significant violations of the laws or regulations against systemic. Getting back to that concept of repeat or uncorrected violations. That the board, again we're going to be repeating certain themes here, and management have disregarded, or refused, or failed to correct deficiencies that have been previously identified. And this, of course, includes failure to correct MRAs, or matters requiring attention, which have been brought up in correspondence from the OCC to the bank. So, that's kind of, in general, OCC enforcement, as well as through the prism of the Bank Secrecy Act.

Chris Willis:

Yeah, thanks, Peter. That's really helpful. And particularly for me, who doesn't know much about anti-money laundering and probably for a number of members of our audience. So, thank you for that.

Chris Willis:

Mary, there was a recent OCC consent order called M.Y. Safra Bank. Can you tell the audience a little bit about that consent order, and what lessons are in that consent order for financial institutions?

Mary Treanor:

Sure, Chris. So, in its consent order against M.Y. Safra Bank, the OCC signaled its enhanced scrutiny of virtual currencies and the money laundering risks that they specifically pose. The consent order also provided a blueprint of sorts regarding what it expects in a robust compliance program. And so, this consent order arose from M.Y. Safra Bank's decision to accept a variety of high-risk digital asset customers, also called DACs, without implementing the necessary AML controls.

Mary Treanor:

Interestingly, the OCC did not impose a monetary penalty against the bank. But they, instead, demanded that the bank implement and maintain a remarkably broad array of costly, extremely prescriptive measures to strengthen its AML program. And also, notably, the OCC specifically tasked the bank's board of directors with implementing, overseeing and reporting on these required measures.

Mary Treanor:

So, taking a step back for a minute, I just want to briefly talk about virtual currency and the money laundering issues it poses. Recently, money launderers have increasingly turned to virtual currency to conceal the origins of illegally obtained proceeds. Now, there are several features of virtual currency coupled with their global reach that make it particularly attractive for money launderers. These include the anonymity of trading virtual currency because of the limited identification and verification of participants. The ease of cross-border transfers and the lack of clear regulations that apply to virtual currency.

Mary Treanor:

So, now, I want to turn briefly to some of the systemic issues that the OCC found with M.Y. Safra Bank. So, in the OCC's examination of the bank, it found that from November 2016 to February 2019, the bank opened accounts for especially high-risk customers. DACs comprised of cryptocurrency related money service businesses, that's kind of a mouthful. They're also called MSBs. These customers from digital currency exchangers, digital currency ATM operators, crypto arbitrage trading accounts, and blockchain developers and incubators. These new customers, many of whom did business in and out of high-risk jurisdictions, significantly increased the bank's risk profile.

Mary Treanor:

For example, these DACs and MSBs substantially increased the volume of the banks domestic wires, international wires, and cross-border ACH transactions. Notably, however, the bank did not sufficiently assess the money laundering risks posed by these new clients. And so, as a result, the bank did not implement adequate controls and adequate monitoring to address this increased risk and prevent money laundering.

Mary Treanor:

Ultimately, as we'll discuss more in this podcast, this consent order underscores the OCC's expectations for banking higher risk clients. Namely, that banks must significantly overhauled their AML programs.

Chris Willis:

So, Mary, it seems like the OCC identified a number of things that went wrong in connection with M.Y. Safra Bank. But if I'm working at another bank, or I own my own bank, which I'd really like to do someday, what would my lessons be? What would my takeaway be from this consent order in terms of looking at my own operations from a BSA-AML standpoint?

Mary Treanor:

Well, board of directors really need to take note of this order. In this consent order, the OCC emphasized that the bank's board of directors bears the primary responsibility for ensuring. And, in fact, proactively verifying that the bank complies with a myriad of costly compliance requirements. These requirements demanded of the bank are numerous and extremely prescriptive. And, frankly, it would take me over an hour to describe them in sufficient detail. But, at a high-level, these requirements include, first, appointing a three person compliance committee to meet monthly. This committee is tasked with

overseeing the bank's compliance with the OCC's consent order, taking minutes of each meeting, and submitting written progress reports to the bank's board of directors.

Mary Treanor:

Second, writing and adhering to a strategic plan for the bank to set forth, among other things, its desired overall risk profile and liability structure, and a three-year plan to adequately monitor high-risk accounts. Third, hiring an independent and qualified BSA officer with adequate resources, and subject to an annual review. Fourth, writing and maintaining a written AML compliance program that adequately monitors, and identifies suspicious activity, including by routinely adjusting appropriate thresholds for the bank's automatic monitoring system. Fifth, implementing an independent audit program to assess via a written report with supporting documentation, the bank's AML strengths and weaknesses in several specified areas. And to identify immediate action needed to address such weaknesses.

Mary Treanor:

Sixth, proposing an independent third-party consultant to review and provide a written report on the bank's suspicious activity monitoring. Seventh, creating a written system of internal controls and processes to guarantee compliance with the bank's suspicious activity report, otherwise called SARS filing requirements. Eighth, implementing and updating every 12 months a written institution-wide BSA-AML risk assessment that identifies the bank's vulnerabilities and strategies for addressing them. Ninth, implementing and maintaining a robust customer due diligence program that complies with the OCC's specified requirements. And, as a whole, ensures that the bank understands its customers and develops accurate and holistic customer profiles. And 10th creating system-wide and job specific BSA-AML training programs for bank employees.

Mary Treanor:

Now, I know I threw a lot out there, but that's actually a summary of 30 pages of very detailed measures that M.Y. Safra Bank must implement. And in the near future. And, interestingly, for each of these requirements, the OCC expressly placed the ultimate supervisory authority or responsibility, excuse me, on the bank's board of directors. So, in doing so, the OCC really dramatically reshaped the role of boards of directors, both at M.Y. Safra Bank and beyond to one in which they must assess, monitor and update their BSA-AML programs on a detailed and, basically, daily basis.

Chris Willis:

Well, all this talk about the board of directors, Mary, makes me think of something that Peter sort of ominously referenced in his opening comments in the podcast. And that is the prospect of potential individual liability. Peter, how does that factor into this conversation?

Peter Hardy:

Yeah, thanks, Chris. It definitely is an important factor. And although instances of the OCC, or other banking regulators pursuing individuals have not been commonplace, I think there is a perception that they are on a general, relatively speaking, uptick. And Mary talked a lot about what the board and that bank is going to be required to do. But there definitely is kind of a tension, shall we say, that can arise between specific individuals and the institutions they serve, particularly when they are, ironically, in a compliance function. So, I want to chat for a moment about a particular enforcement action. And then, I want to just kind of step back and talk about the general considerations regarding potential individual liability in the AML space, and how they kind of factor into this case.

Peter Hardy:

So, last year, and again because folks may be thinking there's a lot in the media right now about a high profile OCC enforcement action regarding certain individuals. We're not going to be talking about that. We're going to be picking out some other examples.

Peter Hardy:

So, last year, the OCC issued a pretty extraordinary announcement regarding the decision of the former Bank General Counselor of Rabobank, which is based, I believe, in the Netherlands. In which he entered into a consent order with the OCC. So, in that consent order, he agreed to a couple things. He agreed to be barred from the banking industry, which is in these matters fairly standard, and then pay a $50,000 fine. So, the consent order itself, again this is fairly standard, its language is relatively generic. You got to go to the notice of charges issued by the OCC that led up to the consent order. And that's the more interesting document, and it kind of walks you through what the allegations are.

Peter Hardy:

Now, I just want to step back for a moment and remind people that Rabobank, itself, also got into hot water. It actually ended up, and I think this is important, agreeing to a criminal penalty of $360 million over its alleged AML violations. And there was a lot going on, I am not going to belabor the details of that. But the allegations in a very high-level was that there as a broad scheme across the bank, so not just one person, many people to permit, look the other way, if you will, according to the government. And then, conceal transactions that were involved in international drug trafficking.

Peter Hardy:

So, the backdrop of this is that there's a pretty serious case brought by the Department of Justice against the institution. So, then what happens to the individuals? Well, in the matter that we're talking about, which again involves the former general counsel, what the allegations are is that there was a new Chief Compliance Officer, and this is a tale that may sound familiar to folks across enforcement actions. A new Chief Compliance Officer came into the bank and, in her view, identified serious deficiencies in the AML program. Okay. She communicated those to bank management. Management disagreed. All right so, then the OCC began an examination of the bank and, shortly thereafter, and partly in response to these concerns raised by the Chief Compliance Officer, the bank contracted with another firm to provide, not surprisingly, an independent and written assessment of the bank's AML program. Okay so, far so good.

Peter Hardy:

Okay so, let's talk about this audit report that they performed. So, allegedly, the findings of the audit report corroborated the concerns of the Chief Compliance Officer that the AML program is deficient in several ways. Now later, and here's another familiar tale. The Chief Compliance Officer actually turned into a whistleblower and gave the audit firm's report to the OCC. And, at that point, the OCC responded by resuming its examination of the bank's AML compliance program. But, of course now, they were armed with the solder report that had been given to them by a putative whistleblower.

Peter Hardy:

So, long story short, according to the notice of charges, the bank responded to an OCC letter. And here we get into good communications regarding potential AML deficiency as follows. And bear in mind, folks, this is the government's version. So, the bank didn't disclose the existence of the audit report, or acknowledges its findings. And, of course, the OCC wasn't happy about that because, in the view of the OCC, the audit report corroborated its view of the bank's AML programs. And, instead, the bank's response, which was drafted in part by the former general counsel, disputed the OCC's preliminary conclusions.

Peter Hardy:

Now, there's other things going on in the notice of charges. And, again, this is all against the backdrop of this larger enforcement action against the bank itself. But I think that that's a pretty extraordinary theory for an OCC enforcement action. One can, certainly, understand their perspective that they were misled. But the heart of this notice of charge, which of course led to an industry bar and a substantial fine, really comes down to the fact that an internal audit report was not turned over, which is maybe the more demonstrable error here. And, of course, there was a difference of opinion in terms of whether or not it accurately portrayed problems in the bank's AML program.

Peter Hardy:

Now, another thing is this is the general counsel. Now, of course, banks and lawyers have to be honest with everyone, particularly their regulators. But I don't think it's totally uncommon for a general counsel to, basically, view their role as trying to protect their institution and maintain privilege. Now, this audit was not a privileged document, but it is a fairly unusual enforcement action. I'm not aware of anything that's precisely quite as focused on whether an audit report was or was not provided. And, obviously, it's a wake-up call to folks at financial institutions in terms of when they're dealing with the regulator. And it also gets into an issue that we're going to chat about just a little bit at the tail end of this, regarding what it means for consultants and auditors of financial institutions when they're looking at AML deficiencies.

Peter Hardy:

The final thing I just want to note is that this was an unusual theory, but I think that what we can see in cases, and whether it be AML or anything else, when you have this tension between the individual compliance officers or lawyers and the institution as a whole. Now, here, the compliance officer actually turned into a whistleblower. The compliance officers, of course, are the tip of the spear of any institution testing for potential red flags. And here's the pickle they can get in. So, if you're deemed to be willfully ignorant of compliance failures, well, that can lead to liability.

Peter Hardy:

On the flip side is the pursuit and investigation of knowledge can then, just lead to plain, old-fashioned, straight up clear knowledge, which of course can also lead to liability. Concerns over this can lead to tensions with the institution. It can lead to the compliance officers creating, for example, overly defensive memos to file. Conversely, it can lead to boards inappropriately ignoring or underplaying the messages that are being sent by the compliance officers regarding problems at the institution. And the upshot is that you can just see how this is going to create a conflict within the institution. And it is ironic that in many of these actions, certainly not all, the individuals that are actually the target of the government's enforcement action are the compliance officers.

Chris Willis:

Thanks a lot, Peter. So Mary, turning to you, what are sort of the basic for individuals, who work in financial institutions about things to do to protect themselves? In other words, what are the factors that we should consider as making it more likely for an individual to be targeted in one of these enforcement actions? And how does that inform us about how we should behave when we work for a financial institution?

Mary Treanor:

So, there's certain factors that you frequently see in enforcement actions where the regulators pursue individuals rather than the entities themselves. These factors include instances where the AML program failures involve systemic repeated breakdowns, and where issues continue unabated for very long periods of time. Instances in which the AML failures inflict significant harm on customers. Instances where access was allowed for those engaging in criminal behavior. And also, where red flags were consistently ignored by the individuals.

Mary Treanor:

And then, in terms of steps to try to minimize potential liability I think one of the most important is ensuring that your AML program is properly tailored and implemented. And this needs to be reevaluated on a pretty frequent basis. Also, not getting in over your head as an individual. Particularly for compliance officers, it's a very challenging job, but they have to be up to the task, and they have to have adequate resources and staffing to effectively carry out their duties. Individuals have to ensure that there's effective employee training, so that employees really understand the money laundering risks. And in the M.Y. Safra Bank enforcement action, the OCC required really extensive training not only for employees, as a whole, to understand money laundering, in general, but for it to be tailored to their specific jobs.

Mary Treanor:

Another way to minimize individual liability is to raise internal awareness of the external regulatory environment, which kind of goes along with training. Maintaining communication with regulators on a regular basis. The example of Rabobank, where the individual did not disclose this audit report, is a prime example. In instances where red flags are identified, documenting them, escalating them, and notifying the proper chain of command. And, as you saw in the M.Y. Safra Bank enforcement action, boards of directors need to exercise actual oversight of management, and not just act as mere rubber stamps. So, I think the biggest takeaway of this is that individuals in these compliance roles, they must follow up on problems. They can't turn a blind eye to them. And they also can't repeat mistakes.

Chris Willis:

Thanks, Mary.

Chris Willis:

Now, Peter, you teased a second ago another aspect of the Daniel Weiss consent order, and what it can tell us about the use of third-party compliance consultants in this area by financial institutions. What can we learn in that regard?

Peter Hardy:

Yeah, thanks Chris. So, that is, as we've been chatting, an unusual aspect of this. And the theme of the notice of charges is that the OCC continually sought, from the bank, the audit firm's report. And that, instead, the former general counsel, according to the government, knowingly and willfully made false statements regarding the bank's possession of the report. And also, of course, made substantive assertions regarding the bank's compliance with the Bank Secrecy Act contrary to the contents of the report. And that's really the heart of the government's claim in this enforcement case.

Peter Hardy:

So, certainly, one can understand the motivations of the government, assuming the allegations are true. It is still, nonetheless, a little unnerving that the government is going to focus its enforcement case on an alleged failure to turn over a third-party report who was hired, of course ironically, here's another irony, to enhance compliance. Remember, the bank hired this person to look, presumably in good faith, into the concerns that have been raised by the Chief Compliance Officer.

Peter Hardy:

So, you can certainly envision scenarios where, if taken to extremes, kind of consequences for financial institutions, and the consultants and, for that matter, lawyers who are in their orbit. You can envision, again, this kind of a catch 22 situation with potentially perverse compliance consequences. Some institutions may be hesitant to hire an outside consultant. And, by the way just a footnote, you have to do independent auditing under the Bank Secrecy Act. That is a pillar that I mentioned of Anti-Money Laundering. So, I don't want to get confused on this point. I want to talk about, perhaps, additional compliance advisors. Or perhaps, I would say, a ferocity with which one engages a consultant to kind of dig into your systems.

Peter Hardy:

So, you could see how many people at some businesses, now, might be a little hesitant to get into hiring consultants because, frankly, they don't want to hear bad news, and they don't want to generate for the government a roadmap for potential future enforcement action. Nonetheless, you have an inconvenient report, it's in the file. And then it's, of course, going to be subject to request by regulators and the perspective of the OCC is that anything having to do with AML BSA is theirs. And there's no such thing as legal privilege.

Peter Hardy:

And just to comment and just in case somebody might say, "Well that's only a problem for financial institutions who don't want to confront their real problems." That may be, of course, in certain instances. But I also have to note, and I don't want to

sound cute here, but there are advisors out there, who stay in business by finding serious problems everywhere. So, I don't think this is just a purely theoretical concern.

Peter Hardy:

Now, again, we got to remember there were serious problems at Rabobank, according to the DOJ enforcement action, so everything's got to be put in its proper context. I don't think that this case means that there's going to be a parade of horribles in every instance.

Peter Hardy:

And just one final comment, I want to draw kind of an interesting compare and contrast between this and an action by the and New York Department of Financial Services against Mashreq Bank, that was in 2018, just a quick note, not going to go into the details, there was an enforcement action there against the bank. It's the oldest and largest private bank in the UAE. And it actually criticized the bank's use of a deficient third-party vendor. So, the problem wasn't that they didn't disclose the audit. The problem wasn't that they ignored the audit or the consultant's work. Rather, they just hired a consultant who, in the eyes of the regulator, wasn't very good. Nobody was trying to hide anything, apparently. He just, apparently, didn't do a good enough job when he was looking at the transaction monitoring.

Peter Hardy:

So, that's just yet another angle where regulators can maybe go after financial institutions. There was more going on in that case, of course, that's just one example. But I thought that's a fairly aggressive move by regulator. But it also tells us if you're a bank or another financial institution, you can't just hire anyone, and then rely on whatever they say. Ultimately, it's up to the board. And, ultimately, the institution itself is responsible for keeping its house in order.

Chris Willis:

Thanks, Peter. And it's probably evident to our audience and, certainly, is to me that this is a very highly specialized, and very complicated area, but one that also carries very significant risks for banks.

Chris Willis:

Mary, if our audience is interested in sort of keeping up to speed on current developments with regard to money laundering and BSA, is there a resource for them that you could point them to?

Mary Treanor:

Yes. So, Ballard Spahr has a very active blog on all issues money laundering. There's a large group of Ballard Spahr attorneys, who work on it. I'd say there's, at least, one new post a week, if not more. And we, also, occasionally have guest speakers who are... excuse me, guest writers who contribute. And so, if anyone is interested in learning more about money laundering in general or, for example, the M.Y. Safra Bank consent order, which I recently blogged about, they can go to www.moneylaundrynews.com. And you can also subscribe through Ballard Spahr.

Chris Willis:

Thanks very much. And Mary and Peter, I want to thank both of you for sharing your expertise in this very important area with our audience today. And thanks to everybody for tuning in today. Be sure to visit our website, ballardspahr.com, where you can subscribe to this podcast, and Apple Podcasts, Google Play, Spotify, or your favorite podcast platform. And don't forget to check out our blogs, consumerfinancemonitor.com and moneylaunderingnews.com for the insights into financial institution matters that we just talked about. If you have any questions or suggestions for the show, please email us at podcast@ballardspahr.com. And stay tuned each Thursday for a great new episode of our podcast. Thank you all for listening.