

**POLICIES TO ENFORCE THE
BANK SECRECY ACT AND PREVENT
MONEY LAUNDERING IN MONEY SERVICES
BUSINESSES AND THE GAMING INDUSTRY**

HEARING
BEFORE THE
COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE
ONE HUNDRED EIGHTH CONGRESS

SECOND SESSION

ON

EXAMINATION OF THE EFFECTIVENESS OF U.S. POLICIES TO ENFORCE
THE BANK SECRECY ACT AND TO PREVENT MONEY LAUNDERING IN
MONEY SERVICES BUSINESSES AND THE GAMING INDUSTRY

SEPTEMBER 28, 2004

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TUESDAY, SEPTEMBER 28, 2004

U.S. SENATE,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Committee met at 10:02 a.m., in room SD-538, Dirksen Senate Office Building, Senator Richard C. Shelby (Chairman of the Committee) presiding.

OPENING STATEMENT OF CHAIRMAN RICHARD C. SHELBY

Chairman SHELBY. This hearing will come to order.

This morning, the Senate Banking Committee continues its examination of the use of banks and other financial institutions for the laundering of money derived from criminal activity and for the possible financing of terrorist operations. In fact, the subject of this hearing is not banks at all, except to the degree that they transition into the financial services sector, previously the domain of other institutions.

Previous hearings in the Committee's series on terrorist financing have logically focused on the banking industry. With primary jurisdiction over the banks and the Bank Secrecy Act, one of the principal legal mechanisms for combating money laundering, the Banking Committee has sought to draw as complete an understanding as possible of those institutions' continuing vulnerability to abuse by those who seek to harm this Nation.

The easy work, however, has been done. Today, comes the hard part. Relatively speaking, banks are easy. We can, to a large degree, get our arms around the problems they pose for preventing money laundering. Today's hearing, however, begins our examination into an entire other realm of financial institutions. If banks represent a fairly well-defined institution into which we can peer for insights and over which we can ensure some reasonable degree of oversight, money services businesses and casinos present problems on a scale that dwarf anything else. There are an estimated 15,000 licensed money services businesses and another 160,000 unlicensed ones. That excludes 40,000 post offices, each of which function as a money services business by issuing money orders. If our regulatory agencies are overextended trying to maintain adequate oversight of banks—and history indicates there is vast room for im-

provement—then the challenge of preventing abuse of nonbank money services businesses is of several magnitudes greater.

Similarly, casinos exist for the sole purpose of transferring cash, generally from your pockets to the casinos' vaults. The amount of money that filters through the hands of casinos has always been immense, and that was when Las Vegas and Atlantic City represented the sum total of legalized gambling in the United States. Today, we have legalized gambling in 800 casinos in 30 States and territories. Riverboats ply the Mississippi with the same goal as those of Las Vegas casinos. Internet gambling presents literally a virtual challenge heretofore unimaginable to those with responsibility for regulating gambling. How we ensure that the explosion in legalized gambling is not abused by those seeking to launder the proceeds of crime or to finance criminal or terrorist activity is the challenge before us.

Helping us to understand the challenge are two panels of experts. Our first witnesses are responsible for monitoring money services businesses and casinos and helping ensure their integrity against criminal activity is maintained. First up, is a regular here: William Fox, Director of the Financial Crimes Enforcement Network, or FinCEN. Following Mr. Fox will be Kevin Brown, Commissioner of the Small Business/Self-Employed Division of the Internal Revenue Service; and last, but not least, we hear from Diana Taylor, Superintendent of Banks for the State of New York. Ms. Taylor will provide valuable insights into the difficulties of regulating money services businesses, drawing in part from her State's experience with both major and small businesses.

Our second panel will be comprised of Mr. Frank Fahrenkopf, President and CEO of the American Gaming Association; Mr. Joseph Cachey, Vice President of Global Compliance for Western Union; and Mr. Ezra Levine, Counsel to the Non-Bank Funds Transmitters Group, and Partner with Howrey, Simon, Arnold and White. Mr. Levine is an expert on money services businesses and the regulatory environment in which they function. We will welcome all of our witnesses now.

Senator Dole.

STATEMENT OF SENATOR ELIZABETH DOLE

Senator DOLE. Thank you, Chairman Shelby.

The September 11 Commission points out in their report that terrorist financing is as likely to come from legitimate sources as it is from illegal sources. For that reason, as we continue to review the findings of the Commission, the issue of preventing money laundering, in money services businesses and the gaming industry, is critical. I believe it is time to consider possible legislation to strengthen our Nation's efforts to combat such terrorist financing.

Over time, we have learned that Al Qaeda operatives have access to checks, credit cards, ATM cards, wire transfer system, and brokerage accounts throughout the world. They know exactly how our system of payments functions and what level of activity is likely to be detected. Clearly, terrorist cells know how to manipulate our financial system. Because of this, we must continue to be vigilant. We must consider areas within our economy where our tracking efforts have not been as effective. Furthermore, we need to remove

structural limitations that handicap Government's efforts to identify and track suspicious activities.

It is my understanding that prior to September 11, we did not receive suspicious activity reports from nonbank financial institutions and casinos. Today, this infrastructure is in place. However, on April 29 of this year, this very Committee received testimony from the Financial Crimes Enforcement Network, FinCEN, that said until they are able to put their BSA Direct system into operation; "FinCEN presently lacks the capacity to detect Bank Secrecy Act form filing anomalies on a proactive, micro level." While "microlevel anomalies" in the short-term may not sound too serious, the testimony also went on to explain their previous difficulty in detecting a catastrophic failure to file forms, as was experienced in one case where a casino failed to file over 14,000 currency transaction reports in an 18-month period.

I am told that an interim step has been taken to provide an "early warning system" in the event a catastrophic failure to file forms would occur. FinCEN, working with the IRS' Detroit Computing Center, has developed a monthly query system to identify casinos with significant variances in their BSA filings. Although this interim step is encouraging, I think it is very important that FinCEN move as quickly as possible to implement the BSA Direct system in order to enhance its capabilities to monitor these filings in a more timely and sophisticated manner.

Our Government continues to make a vigorous effort toward finding those proverbial needles in the haystack, those low-level transactions that are essential to the funding of terrorists' activities. I am confident this Committee will continue to provide our Government with additional legislative tools to enhance the Treasury's capability to track, block, and seize terrorist assets. Hopefully, these tools will help identify the financial infrastructure of terrorist organizations and dismantle their fundraising abilities. We must work to ensure that terrorists no longer have access to the international banking system.

This is a very important issue, Mr. Chairman, and, unfortunately, today I have conflicting demands on my time, so I am going to miss much of the hearing. But I will review the transcript, and I want to thank the witnesses for joining us to help further our understanding of these vitally important issues.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you.

Senator Sarbanes.

STATEMENT OF SENATOR PAUL S. SARBANES

Senator SARBANES. Thank you very much, Mr. Chairman, for continuing the Committee's focus on enforcement of the Bank Secrecy Act. I am not sure. Is this the third or fourth hearing we have had on this subject?

Chairman SHELBY. Third.

Senator SARBANES. Third. Today, we are examining the Treasury's ability to oversee effectively compliance with the BSA by certain nonbank financial institutions, more particularly by money services businesses, MSB's, and by casinos.

It is estimated there are about 200,000 money services businesses in the United States, including the whole range of them, from large multinational financial services enterprises that sell travelers' checks or money transmission services, smaller regional money transmitters, the Postal Service, which is a major seller of money orders to check cashers and currency exchange businesses. And they operate in many forms. The largest money transmission businesses sell financial products both through proprietary locations and agents—hotels and supermarkets. Some have so many locations they never really have to send funds at all. They simply allow funds to be picked up at any location. Smaller transmitters use banks to wire funds to one or more locations here or abroad for payment to recipients through branches or proprietary locations. At the far end of the scale are the informal money transmission businesses that rely on couriers or that operate purely on the basis of their internal trust arrangements. Most of these businesses are subject to the Bank Secrecy Act.

The casinos that are subject to the Bank Secrecy Act—it is estimated 800 in all—are for the most part large, in many cases, public companies through which millions of dollars pass each week.

All of these money services business and casinos are heavily cash-intensive and, therefore, open to serious abuse by money launderers. Regrettably, though, only a small amount of Federal resources is devoted to auditing these institutions for compliance. The Internal Revenue Service has traditionally been responsible for civil compliance audits in this area. It is, in effect, the counterpart to the bank examiner. The IRS Small Business/Self-Employed Division, which is responsible for the task, however, devotes only about 320 individuals to the job on a nationwide basis.

The Treasury's own Inspector General for Tax Administration issued a report critical of IRS efforts in this area in the year 2000. In an update to that report, published this past March, the Treasury's Inspector General stated:

Overall, the IRS has improved its Bank Secrecy Act compliance program since our last review, but the risk of undetected noncompliance still exists. Specifically, the program does not have meaningful performance measures, management information system data are not fully analyzed, and case selection is not risk-based. Further, cases do not contain the documentation necessary to assess civil penalties, examiners cannot access suspicious activity reports for better case development, and education with outreach should be better coordinated with FinCEN.

The lack of Federal audit coverage appears to mean that significant Bank Secrecy Act compliance failures in this critical area are being discovered, if at all, only by agencies other than the IRS. For example, in December 2002, the New York State Banking Department fined Western Union, under its general supervisory authority, \$8 million, the largest MSB fine in New York State history, for failing to report hundreds of transactions as required by the Bank Secrecy Act.

I find it a matter of concern—and I applaud the State banking regulator—that it was the State banking regulator rather than the IRS which undertook what was ultimately a national audit. It seems to me, Mr. Chairman, that an aggressive Federal audit policy is a necessary part of BSA compliance programs in this, as in other parts of the financial sector. And I look forward to the testimony of these witnesses this morning.

Thank you.
Chairman SHELBY. Senator Bunning.

STATEMENT OF SENATOR JIM BUNNING

Senator BUNNING. Thank you, Mr. Chairman. Thank you for holding this hearing. I would like to welcome all of our witnesses.

These two hearings that we are having on this terrorist financing and money laundering are very important. Obviously, this is a very important issue in fighting the war on terror.

I am proud to have supported the USA PATRIOT Act after September 11. I think it is a valuable tool in our fight against terror, but we really need to fully implement it. The Bank Secrecy Act is another important tool, as Senator Sarbanes has said. I think the Chairman has very wisely brought together a good panel of witnesses so we can figure out how to make these tools work as well as we can.

We need to do a better job. There have been problems. The financial institutions need to do a better job in complying with the regulations, but the regulatory bodies also have to do a better job. We must implement the rules governing financial institutions. We also must aid the financial institutions, especially those who have never been subjected to this type of regulation before, in implementing the new rules.

I also think it is very important for the regulators to work with the institutions they are regulating. I think most of the financial institutions want to be a partner. I would guess that most want to do their part in combating terrorism. I think this is especially true of the small institutions. Many of the money services businesses, or MSB's, know their customers very well, and they have a tradition of working with local law enforcement.

The fact that a Las Vegas casino did not submit their reports and the fact that the FinCEN did not realize they suddenly stopped reporting is very disconcerting. We cannot allow these things to happen, especially since there is evidence that terrorists, including the September 11 hijackers, have used nonbank financial institutions. We need to work together and come up with a workable solution that gets to the heart of the problem and dries up the cash the terrorists need to attack us.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you.

All of your written testimony will be made part of the record in its entirety, if you could briefly sum up your comments. We will start with Mr. Fox. Welcome.

**STATEMENT OF WILLIAM J. FOX
DIRECTOR, FINANCIAL CRIMES ENFORCEMENT NETWORK
U.S. DEPARTMENT OF THE TREASURY**

Mr. FOX. Thank you very much, Mr. Chairman, Senator Sarbanes, and distinguished Members of this Committee. I appreciate the opportunity to appear before you to discuss the issues and challenges before us as we establish an effective and comprehensive anti-money laundering regulatory regime for two very diverse and important sectors of our financial industry: Money services businesses and casinos. We applaud your leadership, Mr. Chairman, as

well as the leadership of Senator Sarbanes and other Members of this Committee on these issues. We also appreciate the direct and personal support that you have shown the Financial Crimes Enforcement Network, over this past year, in particular. We are honored by this support, and we are doing all we can to live up to the faith that you have put into us.

The issues we deal with, including the specific issues we are addressing today, are critically important to the health of our Nation's financial system and, indeed, our national security. I have extended remarks that we are submitting for the record. I will keep this statement brief.

I am pleased to be here today with Superintendent Diana Taylor of the New York Banking Department and Commissioner Kevin Brown of the Internal Revenue Service's Small Business/Self-Employed Division. Superintendent Taylor and I have begun what I believe to be a very good dialogue between our two agencies. We have high hopes that this dialogue will lead to a much closer and deeper relationship with the New York Banking Department that will prove to be mutually beneficial across the spectrum of financial institutions, but particularly the challenges sector of money services businesses.

I am also pleased to be here today with Commissioner Brown. As you know, the Secretary of the Treasury has delegated Bank Secrecy Act examination authority to the Internal Revenue Service for a variety of nonbank financial institutions, including money services businesses and casinos. Commissioner Brown's division is responsible for this program. Kevin and I are both relatively new to our respective jobs. When it comes to his office's work, I consistently remind Kevin that we are in the foxhole together—no pun intended.

In the short time I have worked with him, he has demonstrated that he and his people are dedicated to this effort and are taking the responsibilities under the Bank Secrecy Act quite seriously.

Today's hearing is focused on two very different sectors of the financial industry, each presenting its own set of challenges from a regulatory perspective. I would like to first briefly address casinos.

All casinos, including tribal casinos, with gross annual gaming revenue in excess of \$1 million are subject to regulation under the Bank Secrecy Act. Today, there are approximately 800 casinos and card clubs operating in at least 30 jurisdictions in the United States and its territories, while 10 or 15 years ago, the vast majority of casinos were located in Nevada and New Jersey.

The past few years, we have seen explosive growth of riverboat and tribal gaming across the country. While casinos are no strangers to comprehensive regulation, casinos are at risk to be used by money launderers and others engaging in illicit finance, including terrorist financiers.

Casinos are high-volume cash businesses, vulnerable to manipulation by criminals and possibly terrorists. Casinos often offer customers a broad array of financial services, such as deposit or credit accounts, funds transfers, check-cashing and currency exchange services that are similar to services offered by money services businesses. These risks mandate that we implement an effective and ef-

ficient regulatory regime for casinos that includes a robust examination program.

Money services businesses present a deeper and broader challenge for us in implementing a meaningful regulatory regime under the Bank Secrecy Act. This industry includes the following service providers: Currency dealers or exchangers, check casher, issuers and redeemers of travelers' checks, money orders, or stored value products, and money transmitters. We are facing significant challenges in implementing the Bank Secrecy Act's regulatory regime for this industry, and I have outlined many of those challenges in my written testimony.

This industry is incredibly diverse, ranging from *Fortune* 500 companies with worldwide reach to mom-and-pop convenience stores in inner-city neighborhoods where English is rarely spoken. The services provided can be particularly susceptible to terrorists and persons financing terrorist operations. In fact, in my view, money services businesses, because of their diverse nature and the products and services that are offered, represent the most significant risk of any financial industry sector under the Bank Secrecy Act.

We believe this risk must be addressed with a multifaceted approach, a combination of aggressive outreach and education, targeted compliance examinations, development of international standards and regulatory approaches, and appropriate civil and criminal enforcement, all coupled with extremely close coordination between law enforcement and regulators at both the State and Federal level.

We are fortunate that a large majority of both the casino and money services business industry are striving to be compliant. This majority, like other sectors of the financial services industry, has expended large amounts of money, time, and effort to develop anti-money laundering programs that ensure compliance with the recordkeeping and reporting requirements of our regulations. This majority is starving for guidance and education on how better to comply with these regulations, and we must collectively be there to answer the call.

We are listening to these industries to better understand their needs for guidance and feedback and to see if we can collectively figure out ways to achieve better and less burdensome compliance. We meet regularly with representatives from these industries, and we attend and participate in conferences and seminars relevant to these topics. Also, both industries have representative members on the Bank Secrecy Act Advisory Group, which is a very important dialogue among regulators, regulated industry, and law enforcement on these issues.

We are working more closely with Commissioner Brown's people at the IRS than we have in the past, and we need to work more closely with law enforcement and the State regulators of these sectors to ensure that we are leveraging resources as best we can to meet the challenges posed by these diverse and dynamic industries. We have taken steps at FinCEN, such as creating an Office of Compliance and devoting, for the first time, analytic muscle to our regulatory programs which will make a difference. We are building better and smarter technology—our BSA Direct project—that will

assist all players in this arena to approach these challenges in a better and smarter way.

Let me be clear, Mr. Chairman, notwithstanding all of that good work, a robust and properly resourced examination function for nonbank financial institutions is the keystone to the success of our efforts to ensure well-educated, properly compliant industry sectors. This is even more important as we bring other industries into the regulatory fold, which we are currently poised to do. We cannot afford the cynicism that breeds from a regulatory paper tiger. The issues are too important.

I want to assure you, Mr. Chairman and Senator Sarbanes, that we are keenly aware of the importance of our task before us. We know full well that it is critical to our national security. We are committed to move as far and as fast as we can with the resources we have been given to implement this regulatory regime in the best way possible.

We appreciate your kind attention, Mr. Chairman, and I am happy to answer any questions that you may have.

Chairman SHELBY. Mr. Brown.

**STATEMENT OF KEVIN BROWN
COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED
DIVISION, INTERNAL REVENUE SERVICE**

Mr. BROWN. Good morning, Mr. Chairman, and distinguished Members of the Committee. I appreciate the opportunity to be here today to discuss the Internal Revenue Service's efforts involving the Bank Secrecy Act. I would also like to thank your Committee staff members who assisted us during the preparation for this hearing.

Under the leadership of Commissioner Everson, we are strengthening the focus on enforcement at the IRS, while maintaining appropriate service to taxpayers. Within our enforcement priorities, detecting and investigating money laundering is an important part of our tax compliance activities. Money laundering not only is used by domestic and international criminal enterprises to conceal the illegal, untaxed proceeds of narcotics trafficking, arms trafficking, extortion, public corruption, terrorist financing, and other criminal activities, but it is also an essential element of many tax evasion schemes.

As part of its core tax administration mission, the IRS addresses both the civil and criminal aspects of money laundering. Specifically, in fiscal year 2004, the IRS devoted more than 1,100 full-time equivalents and \$131 million to ensuring compliance with the requirements of the Bank Secrecy Act.

On the civil side, the Department of Treasury has delegated to the IRS responsibility for ensuring compliance with the Bank Secrecy Act by money services businesses, or MSB's, casinos, and credit unions. Under this delegation, the IRS is responsible for three elements of compliance: The identification of MSB's, educational outreach to all these types of organizations, and the examination of those entities suspected of noncompliance.

In recognition of the importance of the IRS' role in the fight against terrorism and money laundering, we have just established a new organization within the IRS' Small Business/Self-Employed

Division called the Office of Fraud/Bank Secrecy Act. Steve Kesselman, the individual selected to head this office, is here with me today. Steve will have end-to-end accountability for compliance with BSA including policy formation, operations, and BSA data management.

The Office of Fraud/BSA consists of four territories and a staff of more than 300 field examiners who report to managers located in 33 field offices nationwide. In fiscal year 2003, we added 64 revenue agent field examiners to the program. These examiners and their managers are fully trained, and they are dedicated full-time to the BSA program.

The Office of Fraud/BSA also directs the processing and warehousing of all BSA documents into the Currency Banking and Retrieval System, also known as CBRS, which is housed at the IRS Detroit Computing Center. Currently, the CBRS has approximately 173 million BSA documents on file.

In carrying out our responsibilities under the Bank Secrecy Act, we are engaged in a close partnership with Treasury's Financial Crimes Enforcement Network, headed by Bill Fox. Currently, the IRS assigns senior analysts to act as the liaisons to FinCEN in both the civil and criminal arenas. We are working with FinCEN to use data-driven analysis to assist in the risk-based identification of workload, as well as to identify geographic locations of potential noncompliance. We also conduct joint monthly meetings to discuss BSA issues, trends, and examination results and continue to coordinate the establishment of examination priorities.

We are undertaking several initiatives to enhance the BSA program, which I would like to mention briefly today.

First, we are piloting the examination of MSB's at the entity's corporate headquarters level. Three such examinations of large MSB's are currently underway. Working with the businesses, we are identifying their agents with the highest risk of noncompliance. This is a new approach for the program, one which we believe will provide better customer service for the MSB's and maximize our use of resources. We are also examining some of the largest casinos in the country.

Second, we are centralizing the case identification process to incorporate leads from the field and the IRS' Criminal Investigative Division, as well as CBRS analysis. Our strategy for case selection is designed to consider not only the larger corporate headquarters entities, but also to ensure the unregistered MSB's are identified.

Third, we completed a model Federal/State Memorandum of Understanding, which provides both IRS and the participating State the opportunity to leverage resources for examinations, outreach, and training. We expect this Memorandum of Understanding, developed jointly with FinCEN, to be available for sharing with the States in the near future.

Finally, we have developed quality performance measures for the BSA program, including a centralized review process.

As I stated earlier in this testimony, the war on terrorism and the fight against money laundering are top priorities for the IRS. We are prepared to increase our commitment to the BSA program, and we will continue to coordinate our efforts closely with FinCEN.

Mr. Chairman, I thank you for this opportunity to appear before this distinguished Committee, and I will be happy to answer any questions you and the other Members of the Committee may have.

Chairman SHELBY. Thank you.

Ms. Taylor.

**STATEMENT OF DIANA L. TAYLOR
SUPERINTENDENT OF BANKS, STATE OF NEW YORK**

Ms. TAYLOR. Good morning, Mr. Chairman, Senator Sarbanes, thank you for holding this hearing on this very important and very problematical issue. I especially want to thank you very much for including a representative from the State regulators.

I am Diana Taylor, Superintendent of Banks for the State of New York. My department is the regulator for over 3,400 financial institutions in New York State with aggregate assets of over \$2 trillion.

I am honored to testify before you today on the issues that we confront as a State regulator with regard to enforcing the Bank Secrecy Act and the anti-money laundering programs in the nonbank sectors, the MSB's.

The New York State Banking Department is responsible for licensing, supervising, examining, and regulating the check cashing and money transmitting businesses in our State. In 2003 in New York State alone, these MSB's did over 130 million transactions worth more than \$100 billion. These MSB's are a portal into our Nation's banks, and through them into our financial system.

There are two major problems. The first is that supervision and regulation of this industry is very uneven across this country. For a number of reasons where MSB's are concerned, Federal laws have been passed to prevent financial institutions from unwittingly serving as a conduit for money laundering are not being enforced for MSB's to the same level from State-to-State.

Senator SARBANES. Ms. Taylor, I think if you pull that microphone a little closer. It moves, so you can pull it closer to you. Yes.

Ms. TAYLOR. Can you hear me now?

The second problem is that there has been a complete lack of coordination historically between the Federal designee for examination and enforcement authority, the IRS, and the State MSB regulators. We do not share information as we should. Yet, what is clear and undeniable is that the State regulators of MSB's can be a powerful tool for detecting violations and enforcing these Federal laws, but little has been done to capitalize on this opportunity.

I suggest that there are three actions that need to be taken to put us on the right track. First, we need formalized procedures for two-way communication and coordinated exams where necessary between the States, which are the licensors, regulators, and supervisors and examiners of MSB's, and the Federal Government. I understand that the IRS is developing an MOU that would have them sharing information on these issues with State tax collection entities, and I am very happy to hear that you have come up with an MOU that also shares information with States, and we are very much looking forward to seeing that. I think that is a very positive step, so thank you.

Second, in order to meet acceptable examination standards some States need Federal guidance in training their examiners to do

AML and BSA exams on these MSB's. It is important that the State regulators know what they are being trained to find. It is critical that the BSA be interpreted by the proper Federal authority which is FinCEN. FinCEN has made great strides in providing guidance for BSA examination and interpretation on the banking side. What we need is a similar process through FinCEN's new compliance unit on what is now largely a blank slate, which is the MSB's.

Third, and just as important, we believe that under New York banking law our department has the authority to make sure that its licensees are in compliance with all State and Federal laws including the BSA. Other States do not see themselves as so empowered. Congress should make it clear through an amendment to the BSA that State MSB regulators do have the authority to enforce the BSA/AML laws for MSB's in their States if they wish to do so.

Absent that unambiguous message you have a hodgepodge of activity on the States' parts that runs the gamut from aggressive to anxious anticipation. And what happens is something is amiss. We have the power to punish, either publicly or privately. Your State regulators should be looked to as a big part of the solution to move BSA/AML compliance forward with respect to MSB's.

But in order to do this we need open communication channels, guidance, training, and a clear signal through an amendment to the BSA that you want our help. We have the responsibility to protect our people, our businesses, and our financial system.

We also have the responsibility for keeping legitimate money flowing unimpeded to where it needs to go, but we must put a ring of protection around that portal. We cannot afford to do less.

Thank you very much.

Chairman SHELBY. Thank all of you.

Mr. FOX, as you know, this Committee is very interested in the progress of the transition to greater electronic filing and processing of reports, and the promise such filing offers for the analytical component of your mission.

It is for this reason that I have been trying, in working with you, to increase funding for the BSA-Direct Program through the appropriation process. Such funding, it seems to me, is vital if this essential program is to come online on schedule. Do you foresee any difficulties in getting the BSA Direct program up and running on schedule, and could you share with the Committee your assessment of how FinCEN's mission will be enhanced by implementation of the BSA Direct program?

Mr. FOX. Thank you, Mr. Chairman. Currently, I am happy to report that the BSA Direct Project is on time and on budget, and we plan to implement that system in October 2005.

Chairman SHELBY. What is it going to do for you?

Mr. FOX. Sir, it is going to completely change the way that we do business. We will not only be able to provide this very critical data to our customers, law enforcement and, in some cases, intelligence customers in a much more rich and robust way, but in fact, this system will also permit them to make use of this data through sophisticated data mining tools, bouncing it off of data in their possession.

We are going to be able to enhance our regulatory programs. We are developing sophisticated industry member profiles so that we will know, and be able to catch, problems such as the Mirage Casino issue. I also think it is going to create a much better interface for sharing this data with State regulating bodies.

Chairman SHELBY. Take a minute and tell us about the Mirage Casino.

Mr. FOX. Sure. I believe from 2001 to 2003, there was a period of time where the Mirage Casino in Nevada failed to file, I believe, nearly 18,000 currency transaction reports. This anomaly, if you will, went undetected. The supervision of the Mirage Casino has been delegated to the Nevada State Gaming Commission, and they missed that anomaly as did we.

Now, we have taken a band-aid step, Mr. Chairman. We are working with the IRS at the Detroit Computing Center to raise a flag when we see an anomaly like that, but candidly, I think our BSA Direct system will be much more sophisticated and much smarter about it.

Numbers of filings is not always the answer, but it certainly can be a red flag that would point an examiner in the right direction to say, hey, we had better pay attention, something is amiss here.

Chairman SHELBY. But there were 18,000 transactions that were not reported?

Mr. FOX. We have gotten them in the system since. I thought that was a correct number, sir, but I have a correction and the number of CTR filings was 14,000.

Chairman SHELBY. Mr. Brown, do you anticipate any difficulties working with FinCEN after they get this up and running?

Mr. BROWN. No, Mr. Chairman, absolutely not. We look forward to the system. In fact, we are the biggest user right now of the data in the system, and all we ask is that we remain a preferred customer of their new system. Bill Fox has assured me that we will have the same level of access we currently have. So, we are looking forward to this new system rolling out.

Chairman SHELBY. Mr. Fox, can you think of any way that the Government, you, Mr. Brown, and others, can let the financial people know exactly what it wants from them, so that you can better look for it in their back rooms and identify that activity which is most useful to law enforcement?

Mr. FOX. Yes, Mr. Chairman.

Chairman SHELBY. You are trying to educate them too, are you not?

Mr. FOX. Yes, sir. Mr. Chairman, I view this as one of our central core missions at FinCEN. It really relates to the mandate that the Congress gave us under Section 314(a) of the USA PATRIOT Act, and that is to establish a two-way communication channel between the Government and the financial industry to help them better understand what we are asking them to do. If you think about the Bank Secrecy Act, sir, as an intelligence collection statute, which in many ways it is, this is really about pointing the collector in the right direction. I think we have a responsibility as a Government, and FinCEN particularly, in providing information in an appropriate way to the financial services industry to be able to point them in the right direction.

We get a lot of reporting, sir, on things like the Nigerian fraud scam, and while those are terrible things, we really want them to be paying attention to those things critical to our national security and other matters.

Chairman SHELBY. Mr. Brown, what is the IRS service's record of detecting money laundering in its oversight of the MSB in gaming industries?

Mr. BROWN. In the gaming industries, I cannot tell you right now our level of success our criminal investigation division is very active and has a number of investigations ongoing that I am not free to talk about here. But I can tell you that approximately 9 percent of the casinos are currently under examination, including three of the largest in this country to make sure they are in compliance with the Bank Secrecy Act provisions.

Chairman SHELBY. What about cooperation between FinCEN and IRS and the role you play respectively with BSA regulation? Is this relationship continuing to evolve?

Mr. BROWN. Yes, it is. Both Bill Fox and I are new to the job. I have been on the job 3 months. Bill has been on just a little bit longer. I think, frankly, the relationship was not always where it should have been between the IRS and FinCEN, and I think that we have taken a number of steps to improve that. Bill and I meet regularly. In fact, we met even before I got on the job. So, I think we are going to work very closely, and it is absolutely critical that we work closely to make this program work effectively.

Chairman SHELBY. Senator Sarbanes.

Senator SARBANES. Thank you very much, Mr. Chairman.

Mr. Brown, Mr. Fox really fingered you here this morning. Let me just read from his statement.

As you know, the Secretary of the Treasury has delegated Bank Secrecy Act examination authority to the Internal Revenue Service for a variety of nonbank financial institutions, including money services businesses and casinos. Commissioner Brown's division is responsible for this program.

So he put you on the spot right here this morning.

Mr. Fox, I do not want to let you fully get away with that right here at the outset. You are the administrator of the Bank Secrecy Act; is that right?

Mr. FOX. Yes, sir.

Senator SARBANES. All aspects of it?

Mr. FOX. Yes, sir.

Senator SARBANES. How many members of your office of regulatory compliance are devoted to the money services businesses dimension of the Bank Secrecy Act if any?

Mr. FOX. We do have people devoted, by approximately 7 people at present are devoted to money services businesses.

Senator SARBANES. Seven?

Mr. FOX. Yes, sir.

Senator SARBANES. I see. What is their role?

Mr. FOX. Well, it is principally—

Senator SARBANES. To communicate with Mr. Brown's people?

Mr. FOX. In part, policy development, development of guidance, provision of guidance to industry members, and to assist the Internal Revenue Service in training examiners and auditors on these issues. And as you know, sir, we have a plan to develop an Office

of Compliance that will hopefully—well, not hopefully—it will take a much more active oversight role in the way the regulatory regimes are being implemented, including money services businesses. Finally, we are also devoting, for the first time, significant analytic resources to this effort. FinCEN has not done that in the past. What we will do is devote analysts, close to about a third of our analysts, frankly, on becoming smarter about where we are going to examine, and to try to make examinations risk-based, as you suggest in your statement.

Senator SARBANES. Mr. Brown, how large is the workforce of your division?

Mr. BROWN. Total workforce of the division is about 44,000 people currently.

Senator SARBANES. Forty-four thousand

Mr. BROWN. Yes, for the entire Small Business/Self-Employed Division.

Senator SARBANES. How many of those work on Bank Secrecy Act cases?

Mr. BROWN. Four hundred fourteen. That is just in the Small Business/Self-Employed Division. Counting the Criminal Investigation Division, IRS wide, it is about 1,100 people.

Senator SARBANES. You have 44,000 in your division?

Mr. BROWN. Yes, Senator.

Senator SARBANES. And 414 of them work on Bank Secrecy Act questions?

Mr. BROWN. That is correct.

Senator SARBANES. How did you set that ratio out of this big universe of 44,000? On what evaluation was this challenge or problem or however you want to describe it, determined that it warranted what I would say just or only 414 people?

Mr. BROWN. I have been here 3 months and this is one of the first things I noticed, that this looked a little out of balance.

Senator SARBANES. Yes.

I am encouraged that you noticed.

[Laughter.]

Mr. BROWN. I immediately asked someone to take a look at this top to bottom. The Treasury Inspector General has had some valid criticisms, as recently as this year, that we did not have meaningful performance measures and that we did not have a risk-based method for case selection. They have had a number of valid criticisms we are working to remedy very quickly. Steve Kesselman, who is with me here today, is now running this program. He is undertaking a rapid top to bottom analysis of this program to find out what the right level is. Of course, we need to partner very closely with FinCEN to have them tell us what they believe the right level is, as well.

Senator SARBANES. With respect to that partnership, let me ask you this question, Mr. Fox. Have the Secretary of the Treasury and the Commissioner of Internal Revenue ever met to discuss this question of the ability of the IRS to carry out this particular mission? Has this ever been the subject of a top level meeting between the Secretary of the Treasury and the Commissioner of the Internal Revenue Service?

Mr. FOX. Senator Sarbanes, I know the Commissioner and the Secretary meet about a number of things. I have no specific knowledge that they have met about this particular issue, but it would not surprise that they have not.

Senator SARBANES. That they have or have not?

Mr. FOX. I believe they probably have, my guess is.

Senator SARBANES. Have?

Mr. FOX. I know how seriously the Secretary takes his responsibilities under the Bank Secrecy Act, but I have no specific knowledge of that, sir.

Senator SARBANES. Could you ascertain that and report back to us whether this particular subject has been a matter of discussion between the Secretary of the Treasury and the Commissioner of Internal Revenue, and if so, how recently?

Mr. FOX. I would be happy to.

Senator SARBANES. Did you want to add something, Mr. Brown?

Mr. BROWN. Yes, Senator Sarbanes. I served as Commissioner Everson's Chief of Staff until just 3 months ago, and I do not recall a specific agenda item in any meeting with the Secretary, but I do know that the Commissioner has met several times with Deputy Secretary Bodman on this subject. So they have had conversations.

Senator SARBANES. We had Deputy Secretary Bodman here, and there was some question at that time how much of what was happening in terms of coordination and so forth. This was when we were focusing on the bank regulators. I do understand that subsequent to that hearing the Secretary of the Treasury has had a high-level meeting with the bank regulators with respect to the Bank Secrecy Act. Is that correct, Mr. Fox?

Mr. FOX. Yes, sir.

Senator SARBANES. And those are now going to be on a continuing basis?

Mr. FOX. Yes, sir. We are actually very encouraged at the way that issue is developing. We are working very closely with the bank regulators to enter into an understanding regarding the information that we need to better inform not only the Secretary but also this Committee and others about the health of the system, and we are very encouraged, by the way.

Senator SARBANES. I have the sense though that you need to do some serious work in the area we are discussing this morning.

Mr. FOX. I agree with you, sir.

Senator SARBANES. Mr. Chairman, if I could just ask one quick question here.

Chairman SHELBY. Sure.

Senator SARBANES. I found the testimony of Ms. Taylor very helpful here this morning, and I want to commend the New York State Banking people for their work in this area and their effectiveness.

Mr. Brown, let me ask you two questions real quick. First, did I understand from your response that you are now preparing a Memorandum of Understanding with the State banking people that would parallel what you have developed with the tax collection entities; is that right?

Mr. BROWN. Yes, sir.

Senator SARBANES. Ms. Taylor, you expect that to meet your request in your first point of your statement?

Ms. TAYLOR. I will reserve judgment, thank you, until I see it.

Senator SARBANES. That is a wise thing to do.

[Laughter.]

Second, Ms. Taylor suggested that the Federal authorities provide some help, guidance and so forth, to train State examiners to do BSA exams with respect to the money services businesses. Could that be done?

Mr. BROWN. As a matter of fact, it is being whispered in my ear that actually is included in the Memorandum of Understanding.

Senator SARBANES. That is going to be part of it?

Mr. BROWN. Yes.

Senator SARBANES. So if we get an appropriate Memorandum of Understanding—and Ms. Taylor raised a reasonable questioning about that—but if we get an appropriate one, points one and two of her suggestions would be taken care of; is that correct?

Mr. BROWN. Yes, sir.

Senator SARBANES. Thank you, Mr. Chairman.

Chairman SHELBY. Senator Bunning.

Senator BUNNING. Thank you, Mr. Chairman.

Mr. Brown, as you know, many of the MSB's are mom-and-pop check cashing businesses or pawn shops. They have a long tradition of working with local law enforcement on things like receiving stolen property. Has an effort been made to reach out to the local level on some of these MSB's, or are you still focused more on corporate level problems?

Mr. BROWN. No, we are really focused on all ends of the spectrum. It is important to maintain a balance, and obviously we take our direction here from FinCEN as to how most wisely to that. A key component, as Bill Fox mentioned earlier in his opening statement, is education, making sure that people understand what their recordkeeping requirements are and what their filing requirements are. We endeavor to make sure that all ends of the spectrum are educated with regard to those requirements.

Senator BUNNING. Mr. Fox, I am going to go back to the Mirage thing. No transaction reporting between 2001 and 2003, none.

Mr. FOX. Sir, there was an 18-month period, sir, where that occurred.

Senator BUNNING. Okay, call me a liar for 6 months.

Mr. FOX. No, no, no, sir, not at all.

Senator BUNNING. But there was a big problem.

Mr. FOX. Yes, sir.

Senator BUNNING. And neither the Treasury or you or someone in your place discovered that at all. It was done by a regulator from a State that gave you the red flag, correct?

Mr. FOX. Actually, sir, I think they missed it at first too.

Senator BUNNING. No, it was not done by Vegas or it was not done by Nevada.

Mr. FOX. Right.

Senator BUNNING. It was done by someone from out of that area.

Mr. FOX. Right.

Senator BUNNING. How in the world, can you just tell me how it happened.

Mr. FOX. Sir, it is, to be candid with you, it is a terrible mistake. There is no question.

Senator BUNNING. How many more are there like that around the United States?

Mr. FOX. Well, we are certainly hoping not any more. I will tell you, we have tried to take steps with the technology that we have to enhance it and to make sure that a flag pops up when this type of anomaly occurs, sir. The technology we are developing will prevent this thing from happening again.

Senator BUNNING. It seems to me with the technology we now have as far as the Internet and as far as reporting transactions of certain amounts, that that would never be able to be done.

Mr. FOX. Yes, sir. Unfortunately, currently we do not have that. We are working to get it.

Senator BUNNING. You do not have the technology?

Mr. FOX. We are working to get it.

Senator BUNNING. You are the only one that does not have the technology.

Mr. FOX. I do not want to be specious here, sir, but we currently do not have the technology that will allow a sophisticated study of industry members across the spectrum of the financial industry as it exists today.

Senator BUNNING. Or nonfinancial industry.

Mr. FOX. I guess they are all the financial industry from Bank Secrecy Act perspective.

Senator BUNNING. That is correct.

Mr. FOX. That is what we are working very hard to develop. Now, again, the existing technology that we have does not we have been working very closely with the people in Detroit from the IRS, who own that technology, and have developed a band-aid, that at least will, I think—

Senator BUNNING. Give you a red flag?

Mr. FOX. Yes, sir, so that we can prevent this from at least happening again. It is a terrible mistake.

Senator BUNNING. One other question. Have you seen any evidence of the terrorist networks using the U.S. Postal Service to launder and wire money?

Mr. FOX. Not that I am aware of, sir.

Senator BUNNING. Not that you are aware of.

Mr. FOX. Not that I am aware of.

Senator BUNNING. I hope that your sophisticated technology would include the U.S. Postal Service because there is an awful lot of things going through the U.S. Postal Service that you may not know about and that we should know about.

Mr. FOX. Yes. Let me caveat that as well. We have people looking very closely and carefully, not just at FinCEN but around the Government, at the data we collect to include the data that is collected from the Postal Service. But I will tell you, it is certainly possible that it is occurring.

Senator BUNNING. I hope that you include that in your scope of operation.

Mr. FOX. Absolutely, sir.

Senator BUNNING. Ms. Taylor, why do you believe the IRS rather than FinCEN should spearhead communications between the Feds and the State?

Ms. TAYLOR. I do not.

Senator BUNNING. You do not believe that?

Ms. TAYLOR. No.

Senator BUNNING. You believe that—

Ms. TAYLOR. I think FinCEN should spearhead it. I believe that FinCEN was given the job by Congress of spearheading the BSA.

Senator BUNNING. So you think that they should be the spearhead, and they should report then to the IRS?

Ms. TAYLOR. I think that FinCEN has the capability to do it. It is in their mandate to spearhead the BSA at the Federal level.

Senator BUNNING. Are you reaching out to work with the MSB's, especially the smaller ones, on terror financing as the local law enforcement works with them on other crimes?

Ms. TAYLOR. We regulate, license, and supervise all of the MSB's within the State of New York, which are the check cashers and the money transmitters. In the licensing process we make sure that they have the policies and procedures in place that they need to have, and controls, which include BSA types and AML abilities. We are responsible for making sure that they have compliance officers set up and that they have the education and training on their staffs to make sure that they comply with the laws at the Federal and the State level on all of them.

We also go in and examine them on an annual or biannual basis for BSA-related activities in addition to their other activities.

Senator BUNNING. Thank you. I just want to emphasize the fact that Treasury and FinCEN have a level of cooperation here that must be attained. It is like the intel community before September 11 and after September 11. If you do not get that job done, I do not care how good you do individually, you are not going to really get it done the way we want it done. So we are going to be watching very closely that what you continue to do, and I would—not going to make any suggestions to the Chairman or not, but I think we should continually monitor this situation as it goes down the pike.

Chairman SHELBY. We are going to.

Senator BUNNING. Thank you very much.

Chairman SHELBY. Senator Carper.

STATEMENT OF SENATOR THOMAS R. CARPER

Senator CARPER. Thanks, Mr. Chairman.

To our witnesses, welcome. Thank you for being here.

I am going to slip out of here before too long. We are working on the September 11 Commission bill on the floor, restructuring intelligence services for our country, and Senator Lieberman's asked me to come over and help manage the bill, which is probably an invitation for disaster. We will see. I look forward to it.

I am from Delaware, and we have become the home of financial services for a lot of people in that particular business. We have also seen, over the last decade or so, a number of racinos, horse-racing tracks which have slot machine gambling as well. They call them racinos. The subject of our hearing today is policies to enforce the

Bank Secrecy Act and prevent money laundering in money services businesses and the gaming industry. That is a mouthful.

I am going to ask you just to give me some examples of what is going on, and I do not know if you can give me an example or two in what I call the racino business, horse racing combined with slot machine gambling, for example. How is it actually occurring? And before we can figure out how to enforce the Bank Secrecy Act and prevent money laundering, it would be helpful for me at least to know how is it actually taking place? If you can give us an example or two of how that is occurring, particularly in that area, I would be grateful.

Mr. FOX. Sir, I actually think that racinos presently are not licensed as casinos and, therefore, are not subject to Bank Secrecy Act reporting in the same way that other casinos are. We do have examples every day, if I caught your question right, Senator, where information that is being filed by both of these industries is being very helpful to law enforcement. I think that this same information that is being filed is helpful to law enforcement and is also demonstrative to the fact that there are things happening in these industries that really present a risk, not only to our financial system but also to our national security. I cannot underscore enough how important we believe addressing the risks associated with these industries are, including the money services businesses in particular. I do not know whether that got to your question or not.

Senator CARPER. Let me ask you, in a different way, what would be helpful for me in understanding what we need to do to prevent this practice is to understand some examples of where it actually has occurred in the gaming industry.

Mr. FOX. Off the top of my head, sir, I do not have anything, but we would be happy to get something for you. I know we have them off the shelf. I do not have anything off the top of my head that I can think of, but I can get that for you, sir.

Senator CARPER. Let me ask Mr. Brown and Ms. Taylor to take a shot at that.

You are from New York, are you not?

Ms. TAYLOR. Yes, but we, the Banking Department, does not regulate the casinos.

Senator CARPER. Do you have casinos or do you have racinos? What do you have?

Ms. TAYLOR. We have casinos, and we have racing tracks.

Senator CARPER. Do you have any financial services in New York still?

[Laughter.]

Ms. TAYLOR. We have a lot of financial services.

Senator CARPER. Just kidding.

Ms. TAYLOR. They are all coming to Delaware, but we are trying to keep them in New York.

Senator CARPER. Not all of them, a couple of them. Just give us your crumbs, and we will be grateful for that.

Ms. TAYLOR. I really do not have any because it is not my area, and I do not want to talk about something I do not know that much about.

Senator CARPER. Well, we do that all the time, so why should it preclude you?

[Laughter.]

Senator SARBANES. I know, but it shows that Ms. Taylor has a lot more wisdom than we do.

[Laughter.]

Senator CARPER. Maybe she does. You would not be the first person to make that observation.

Mr. Brown.

Mr. BROWN. As to racinos, I cannot say anything. I would defer to Bill on that.

As to casinos, obviously, there are several hundred in this country, and we have approximately 9 percent of them currently under examination.

Senator CARPER. What is going on there that we are trying to prevent?

Mr. BROWN. I think money laundering is the main thing. The whole idea of the Bank Secrecy Act is really to leave a financial trail, and this is to make sure that we have the records necessary to follow that financial trail and to find—

Senator CARPER. Again, I do not think I am going to get—or the answer to least the question I am asking is give me some examples of what is going on that we are trying to present in the casino or in the gaming industry, and maybe our next panel can—

Mr. BROWN. I also do not have anything that comes off the top of my head, but Bill Fox and I can get together and see if we can talk to our staffs.

Senator CARPER. If you could give us a response for the record.

Mr. BROWN. We would be happy to do that, sir.

Senator CARPER. Mr. Fox.

Mr. FOX. We would be very happy to do that, sir.

Senator CARPER. Good. Thanks very much.

My last question, and I ask each of you to take a stab at this is where do we go from here? Where do we go from here, those of us who serve on this panel in the Senate? Where would you have us go from here?

Mr. FOX. I think we all have to pay very close attention. I do not pretend to have any specific wisdom on this right now, and I am probably not authorized to give it to you if I had it, but I would suggest, Senator, that I thought that the September 11 Commission did a terrific job of analyzing this issue as it relates to finance. I think their ultimate conclusion that following money trails or their ultimate conclusion as it relates to this issue of following money trails really must remain a very important part of the U.S. Government's counterterrorism efforts.

And I think what we are trying to study now is whether or not we have the actual tools available to detect those money trails. Much of the rules and much of the statute that we administer here and work with were set to detect and prevent money laundering, which is a little bit of a different problem than illicit finance or terrorist finance, if you will.

If you think about it this way, money laundering is almost looking at the problem through a telescope, trying to watch big wads of dirty money and watch people trying to clean that money and be able to use it. Whereas, terrorist financing is almost looking at the problem through a microscope, where you are trying to watch

maybe small amounts of possibly even clean money or from a clean source being put to evil purposes. These are two very different things, and I think bear different tools.

So, if I could be so bold to say that I think this issue would be a good place to focus on as we go and would very much look forward to working with this Committee and others to do that.

Senator CARPER. Thank you.

Mr. Brown and Ms. Taylor, briefly, where would you have us go from here?

Mr. BROWN. I would make sure that the IRS and FinCEN are working very closely together, that we are devoting sufficient resources to this program, and that we are making good use of the resources; one, we are examining the right entities and, two, we are making the examinations count.

Senator CARPER. Thank you.

Ms. Taylor, the last word?

Ms. TAYLOR. I think that you have gone a long way with this hearing. I think that it is very important that you take advantage of all of the resources available to combat this problem. And, in my testimony, I had three suggestions as to what could be done. The first two have actually I think hopefully been taken care of with the MOU that FinCEN and the IRS is putting together and, as I said, I will reserve judgment until I see it, but from hearing what is in it, it sounds like I am very encouraged.

And the third, and just as important, I think, as far as the BSA goes itself, it is very important for Congress to make sure that all departments, and State Banking Departments, know that they have the authority to enforce the BSA. We, in New York, under our banking law do, and that has been opined upon by FinCEN, also, but I think that there is a little bit of ambiguity there. So, if that ambiguity could be taken out, I think it would be very helpful.

Senator CARPER. My thanks to all of you.

Thanks, Mr. Chairman.

Senator SARBANES. Mr. Chairman, could I get a clarification from Mr. Brown?

Chairman SHELBY. Go ahead.

Senator SARBANES. You say you have 9 percent of the casinos currently under examination?

Mr. BROWN. Approximately.

Senator SARBANES. Does that mean that the other 91 percent have not been examined or that they were examined or some of them might have been examined at an earlier time and are not currently under examination?

Mr. BROWN. The latter statement is the correct one. The cycle time generally can run from a few months to a year or so to do an examination and then when it is closed—

Senator SARBANES. What percent of the casinos would you say have not been examined at all?

Mr. BROWN. I do not have a number on that. I would be happy to see if we could find that for you.

Senator SARBANES. Do you have any idea—more than half?

Mr. BROWN. I could not even hazard a guess at this point.

Chairman SHELBY. Senator Allard.

STATEMENT OF SENATOR WAYNE ALLARD

Senator ALLARD. Thank you, Mr. Chairman.

In the communication between the IRS and FinCEN, are you comfortable with your ability to communicate back and forth or do you think there needs to be some changes in law that would facilitate that?

Mr. FOX. Senator, I am very pleased with the level of communication we have had with Commissioner Brown and his team. My team and his team are working quite closely on this issue. As I mentioned, we recognize that we are in this together, and we at FinCEN do not have the resources to be able to go and perform the examination function. The people at the IRS need to be able to utilize the resources that we have to help develop a risk-based examination program and I think this is a better and smarter way.

So, I must tell you, I am very pleased with the level of communication that has occurred between Commissioner Brown and his staff and my staff, and we are planning to continue that level.

Senator ALLARD. Mr. Brown.

Mr. BROWN. Likewise, we are quite pleased with the relationship we have with FinCEN. We work very closely together, and it is absolutely critical that we work well together. This is not going to function the way you want it to function unless we do this together and well.

Senator ALLARD. Ms. Taylor, can you communicate with the Federal agencies?

Ms. TAYLOR. I will tell you after I see the MOU.

Senator ALLARD. What is your practical experience?

Ms. TAYLOR. Our practical experience has been less than ideal, but I think it is getting better. I have had several conversations with Director Fox on this issue, and I think that things are improving.

Senator ALLARD. Could you elaborate on some of those for us?

Ms. TAYLOR. We have had a couple of incidents where we have found some breaches and where it has taken a little time to get people to concentrate on it, but I think that it will get better. For instance, with the Western Union incident, which I think you are all familiar with, our examiners found some breaches and it took a little while for us to get an opinion from FinCEN which we needed to actually conclude that investigation which had to do with what the exact interpretation of the law was, as far as aggregating transactions.

Senator ALLARD. So the States go ahead and file suspicious activity reports, do they do any of those?

Ms. TAYLOR. Well, we do not file them, but the institutions that we regulate file them, and then we send them on.

Senator ALLARD. I see. So you found, in some of the SAR's, some issues?

Ms. TAYLOR. Actually, no, it was the fact that SAR's had not been filed. That is the first thing you have to—people do not file SAR's unless they know that they are supposed to file them.

Senator ALLARD. How and when do each of the entities determine when to file a referral to you or to FinCEN on these SAR's?

Ms. TAYLOR. Let me just make sure I understand the question. How do our regulated entities know when to file an SAR? That is

a very good question. Their guidance has, in many cases, been put out by a regulatory agency such as FinCEN as to when SAR's should be filed, but there is some ambiguity in some cases as to when SAR's should be filed and when they should not be filed.

Senator ALLARD. Could you elaborate on that ambiguity.

Ms. TAYLOR. Well, in the case of Western Union, Western Union did not think that it needed to file SAR's in this particular case. Their interpretation of the law was that they did not need to aggregate these transactions. Our interpretation of it was that they did need to aggregate the transactions. Our bank examiner went in and aggregated the transactions and found some breaches of the law, and we alerted FinCEN that this was the case, and we worked together to solve that case.

So there was some real ambiguity in what the law said, and FinCEN, several months later, came out with a guidance or an opinion saying that, yes, SAR's did need to be filed in those circumstances.

Senator ALLARD. Now, I am assuming your regulatory purview is State banks and State financial institutions.

Ms. TAYLOR. Yes.

Senator ALLARD. Now, Mr. Fox, at the Federal level, I would ask you the same question. How and when do these SAR's get filed?

Mr. FOX. Generally, sir, what we require is that financial institutions file a report of suspicious activity when they know, I mean to put it in layman's terms, when they note something that is out of the ordinary that causes them to be suspicious about a particular financial transaction.

Senator ALLARD. Is there confusion that you get from them? I mean, she said in the State, they have some confusion there.

Mr. FOX. Sure. In this particular issue, it related to the aggregation of certain currency transaction reports and whether or not that activity could constitute structuring, if you are familiar with that term, which is structuring financial transactions to avoid a reporting requirement.

Senator ALLARD. So it would be less than \$10,000.

Mr. FOX. Yes, sir. For example, someone comes in and does an \$8,000 transaction.

Senator ALLARD. And you have a series of them.

Mr. FOX. Yes, sir.

Senator ALLARD. Yes. In reality, it is much more than—

Mr. FOX. Yes, sir. So there was some confusion about whether or not this particular money services business could aggregate or they were aggregating these reports. I believe, I was not at FinCEN at the time, but I believe that FinCEN came and ruled that aggregation was, in fact, impermissible and, therefore, suspicious activity reports should have been filed as a result of some of the transactions.

Senator ALLARD. So these are done on a case-by-case basis?

Mr. FOX. This type of action, sir, yes. In this case, I believe the New York State Banking Authority found this issue and asked whether or not this constituted a violation of the Bank Secrecy Act. That does not happen every time, but when there is an issue like that, generally, we are the agency that deals with those issues.

Senator ALLARD. The question that comes up then is, you know, we have had some discussion about whether the \$10,000-limit is adequate, should be increased because of inflation. In view of some of the problems that you are having here, how do you feel about increasing that \$10,000 limit?

Mr. FOX. Actually, sir, our Bank Secrecy Act Advisory Group, which is a gift from this Committee and the rest of the Congress, is working very hard on a recommendation to the Secretary about currency transaction reporting. Because that recommendation is going to contain the wisdom of the industry, law enforcement, and the regulators collectively, I would ask that you allow me to wait for that to come out. I think we are going to have that report by the end of the year, and we would be happy to share it with this Committee.

Senator ALLARD. I think it is imperative that this Committee get that report.

Mr. FOX. Yes, sir.

Senator ALLARD. And I would ask that it be provided to the staff.

Mr. FOX. You have my commitment to do so, sir.

Senator ALLARD. I do not have any further questions.

Thank you, Mr. Chairman.

Chairman SHELBY. Thank you, Senator.

I have a number of questions, and I am going to submit them for the record, but they touch on banks versus wire transfers, and we have alluded to this. One of the implications of increased global use of ATM's for money laundering and for the movement of terrorist funds, regulating casinos, which we have gotten into already. Why it took so long for you to get involved after they were legally made subject to anti-money laundering statutes 10 years ago? Why a delay of almost 10 years before the requisite rules were adopted concerning the filing of SAR's or suspicious activity reports.

Ms. Taylor, a question we are interested in for you concerns what role the State should they play if it had enabling legislation?

Ms. TAYLOR. I am sorry. I missed the first part of your question. What role should what play?

Chairman SHELBY. Yes, what role is the State playing now and what more could the State contribute, in your thinking?

Ms. TAYLOR. Our role right now?

Chairman SHELBY. Yes.

Ms. TAYLOR. The role that we play right now is I think a very important one in that we license, and regulate, and supervise these institutions.

Chairman SHELBY. Sure.

Ms. TAYLOR. All the way from licensing them in the first place, which means that they have to reach certain criteria even to do business in the State, to examining them each year or on a regular basis to make sure that they are following all of the requirements and to enforcement actions if they are not following the requirements. And we are on the ground, and we have 560 people devoted to this, to the institutions in the State of New York.

Chairman SHELBY. Good.

Lady and gentlemen, we thank all of you for your appearance today. You know we have another panel, and we are trying to move

on, but we will continue to do oversight in this area with you and work with you.

Mr. FOX. Thank you very much, Mr. Chairman.

Mr. BROWN. Thank you, Senator.

Chairman SHELBY. We are going to go to our second panel, which is composed of the following: Joseph Cachey, Vice President of Global Compliance, Western Union; Frank Fahrenkopf, President and CEO, American Gaming Association; and Ezra Levine, Partner, Howrey Simon Arnold & White, a law firm.

We welcome all of you here. Your written testimony will be made part of the records.

Frank, we will start with you. Mr. Fahrenkopf.

**STATEMENT OF FRANK J. FAHRENKOPF, JR.
PRESIDENT AND CHIEF EXECUTIVE OFFICER,
AMERICAN GAMING ASSOCIATION**

Mr. FAHRENKOPF. Thank you, Mr. Chairman, Senator Bunning and Members of the Committee.

I am pleased to be here this morning to testify on what is clear is a very important matter to our country. For the last 19 years, the commercial casino industry has spent millions of dollars and has devoted untold hours of effort to ensure the strictest possible compliance with the requirements of the Bank Secrecy Act and to prevent use of our facilities by money launderers.

The industry takes very seriously these obligations to our Nation, our customers, our employees, and the communities in which we operate. Our industry has always been, and always will be, highly regulated by our host States, and we have always recognized our duty to ensure maximum possible legal compliance.

Since the AGA, the American Gaming Association, was founded in 1995, we have helped the industry and the Department of the Treasury form an effective partnership in meeting these obligations. The AGA—my organization—represents the commercial casino industry, consisting primarily of publicly held hotel casinos listed on the New York and Nasdaq stock exchanges, including most of the names familiar to consumers in the country, companies like Harrah's Entertainment, MGM MIRAGE, Caesars Entertainment, et cetera.

Commercial casinos currently operate in 11 States and directly employ more than 350,000 people who earned more than \$11 billion in 2003. State regulations control the industry's financial and business practices to exacting conditions of licensing. Board members and senior executives of our companies are subject to exhaustive background investigation and must be found suitable for a gaming license. Our gaming employees and, in many cases, our vendors also must have background checks by State regulators before they can work in the industry.

Beginning in 1985, our casinos have been subject to currency reporting obligations under the BSA. And in the nearly two decades since then, commercial casinos have filed millions of CTRC's and currently submit them at the rate of several hundred thousand per year. The industry itself has expanded substantially. In 1985, commercial casinos operated only in Nevada and New Jersey.

When the Department of Transportation first applied currency obligations to casinos, the Department exercised its powers under the BSA to enter into a Memorandum of Understanding with Nevada gaming regulators, under which Nevada casinos reported currency transactions exceeding \$10,000 through a State administrative program that was supervised and approved by Treasury.

This Memorandum has been revised since 1985 to the point where the Nevada requirements closely track the Federal program. All non-Nevada casinos have always been subject to direct Federal supervision for CTRC compliance.

A major challenge for Federal and State regulators, and for our industry, has been adapting BSA requirements to an entertainment venue like a casino floor. The BSA was clearly designed to apply to business settings, like banks and brokerage offices, where customers expect to have to document their activities. A casino offers a very different environment. For example, rarely, if ever, will a visit to a bank or a stock brokerage include a Mardi Gras parade or a Cirque du Soleil performance or food and beverage services.

We provide cash services 24 hours a day, 7 days a week, well more than any other business regulated under the BSA. In the fast-paced atmosphere of a casino, at all times of day and night, our members have to acquire good identification documentation from our customers so we can report both cash transactions and suspicious activity. We also have to effectively track the activity of customers who play a number of different casino games during a visit to a casino or who play at different tables throughout an evening.

Now, although these are difficult tasks to perform, we think, on balance, we are meeting that challenge. That is not to say, as you have already heard, that individual companies have sometimes not missed filing currency reports that they should have filed. Any such violation, in our view, is one violation too many. Still, the banks and brokerage houses, and money businesses, the gaming industry has found that its systems and its people occasionally have failed to meet the daunting technological and administrative challenges posed by anti-money laundering requirements.

I would add that the case that you were talking about, both first raised by Senator Bunning and you, Mr. Chairman, and others Members of the Committee, was a case where the actual CTRC's were filled out. They had been completed. They had not been mailed. One individual did not mail the documents that were fully completed.

I want to stress that none of these violations has found to be intentional or to involve some forms of collusion with money laundering enterprises. Indeed, the more recent situations of this type largely have been discovered by the gaming companies themselves and self-reported to regulators, and that is what happened in the Mirage case. It was the Mirage Hotel that found out the work was not being done, it had not been mailed, and they reported it to regulators. Regulators did not find it.

Like the other financial institutions, we have to learn from these failures and make sure we do a better job every day, and that is exactly what we are committed to do. Seven years ago, the anti-money laundering effort in the industry moved to a new level when

Nevada required that its casinos file suspicious activity reports concerning customer activity that might constitute money laundering or illegal activities. Seven months after Nevada acted, Treasury proposed such an obligation for the rest of the industry.

At that time, a number of our members began filing suspicious activity reports for non-Nevada casinos on a purely voluntary basis. New Jersey imposed mandatory suspicious activity reporting on casinos in the State in October 2000 and Treasury's Suspicious Activity Rules for Casinos took effect some 30 months later, on March 25, 2003.

The AGA applauds this move toward suspicious activity reporting and away from the previous reliance on CTRC's. That move places the knowledge and observations of we believe our experienced employees in the service of the Government's anti-money laundering efforts. I would like to note just a few statistics related to suspicious activity reporting by casinos.

Between August 1, 1996 and December 31, 2003, casinos filed 9,866 SAR's, with over half of those being filed in 2003, when Treasury's mandatory rule took effect. Almost 90 percent of the SAR's filed by casinos and card clubs have been filed by the commercial casino industry as opposed to the other parts of legalized gaming in this country.

About one-third of the suspicious activity reports have concerned possible structuring activity by customers Senator Allard asked about, while 15 percent concerned large cash transactions where there has been minimal gaming, which could be a sign of money laundering. By way of comparison, roughly half of the SAR's filed by U.S. banks, through June 2003, concerned suspected money laundering and structuring.

As Mr. Fox said, we have also worked with Treasury very closely and our State gaming regulators in the fight against money laundering. For over 10 years, a representative of our commercial casino industry has participated in the efforts of the Bank Secrecy Act Advisory Group. On two recent occasions, we have organized a series of Government industry conferences across the country on money laundering issues.

The first round of conferences was designed to help Treasury gather information about anti-money laundering efforts that now exist at the casinos.

The second round involved a series of workshops on Treasury's new Suspicious Activity Regulations for casinos.

We have also organized, for Members of Congress, as well as Treasury and FinCEN what we call back-of-the-house tours of casino facilities, as well as other meetings with industry participants to help Treasury evaluate anti-money laundering programs in our industry.

We will continue to do our part in this heightened security environment. Because we handle many cash transactions and must comply with comprehensive State regulations our properties already have extensive security measures in place. It is part of our business. It is the nature of our business. And although new legal duties will often present challenges, we have confidence that we will be able to work with our Federal and State regulators to develop effective implementation plans. We seriously recognize the

importance of taking the meaningful steps to ensure the safety of our employees, our customers, our communities, our country, and to minimize any potential for terrorist or criminal activity involving our business, and we look forward to further cooperation with this Committee and with our Federal regulators.

**STATEMENT OF JOSEPH CACHEY, III
DEPUTY CHIEF COMPLIANCE OFFICER AND
COUNSEL, AML GLOBAL COMPLIANCE,
WESTERN UNION FINANCIAL SERVICES, INC.**

Mr. CACHEY. Good morning. My name is Joe Cachey. I am Deputy Chief Compliance Officer for Western Union Financial Services, and I would like to thank you, Mr. Chairman, and the Committee, for allowing us the opportunity to address this issue with you today.

Western Union is a leader in worldwide money transfer. We offer our services in over 195 countries, through some 200,000 agent locations. Western Union is part of First Data Corporation, which is a *Fortune* 300 company, publicly traded on the New York Stock Exchange, and which employs over 30,000 employees around the world.

Both First Data and Western Union are regulated on the State, Federal, and also international level through a series of regulations which ensure that our services are provided in a safe and secure method for our customers.

Since the anti-money laundering provisions of the USA PATRIOT Act went into effect a little more than 2 years ago, Western Union has created an industry-leading compliance program in a relatively short period of time. We continue these efforts today, and I will try to walk you through very briefly some of the enhancements and programs we have been putting in place since July 2002.

I am going to focus on three areas. The first is experienced people, the second is data analysis and reporting, I think which came up a little bit when you were speaking with the prior panel, and the third is regulatory outreach.

The most important aspect of any compliance program, whether it is for an MSB, a bank or a casino, is experienced people. Experienced people show you where the risk is. We have increased our anti-money laundering expertise within the company by hiring, and we continue to recruit, seasoned compliance officers from global banks, other regional-sized financial institutions, Government, and also other aspects of the financial services industry, such as insurance companies, mutual funds, and other non-MSB companies. This experience continues to help the company identify risk, enhance our programs and be able to address those risks in a broader fashion.

Currently, Western Union has over 150 employees that work on nothing but anti-money laundering compliance. Further, Western Union has significantly enhanced its transaction monitoring capabilities to better detect and report suspicious activity and large currency transactions to the Financial Crimes Enforcement Network.

We have developed our own proprietary software system to work with our own unique money transfer system. We believe that get-

ting the right information in a timely manner to law enforcement is our primary mission of our programs. Unlike other financial institutions, Western Union's money transfer services are offered through what I like to call a "closed-loop system." We have direct relationships with both the agent initiating the money transfer or receiving money from the customer and the agent paying out the money transfer or expending the funds to the receiving customer.

We collect information on both the sending customer and the receiving customer. The data never leaves our system because it is a closed-loop system. We control it from beginning to end. We are in a unique position to monitor the entire transaction and provide that complete picture of that transaction to law enforcement when need be. Now, with a little over 2 years' experience in filing SAR's and in developing anti-money laundering programs under the USA PATRIOT Act, we are continuously improving those reporting processes.

Additionally, we believe that communication and cooperation between industry and regulators is essential to a winning strategy. This year alone, my compliance officers and I have visited with the central banks or financial intelligence units of over 30 other countries to facilitate an exchange of information on these issues. We strive to partner with all Government stakeholders to facilitate an ongoing dialogue in an area where risk and money laundering trends may change on a day-to-day basis.

As an industry with just over 2 years' experience with the USA PATRIOT Act, we still need guidance and continued open dialogue. Western Union and the agent locations that we support really have 49 different regulators in the United States alone. There are 47 States and territories which issue licenses to us and regulate us, one of them being New York, with Superintendent Taylor, FinCEN, and the IRS.

Western Union is routinely examined by up to 15 different State banking departments in any given year. This framework can make regulatory consistency a challenge, as you can imagine. It is our opinion that FinCEN, as the policymaker of our industry, is in the best position to provide the necessary guidance on the issues that arise on a day-to-day basis. A single guiding voice is becoming increasingly important in light of the fact that the entire industry of MSB's operate under multiple licenses.

For a risk-based approach to anti-money laundering compliance to have the desired effect, the regulator—in our opinion, FinCEN—must provide ongoing communication to industry about emerging risks and money laundering patterns so the industry can direct its compliance efforts toward the most critical areas of risk. And this is particularly important in light of Director Fox's comment of money laundering really being distinct from terrorist financing and how those patterns and the amounts needed are different. That is where we need more guidance.

Finally, we believe that more resources and more meaningful dialogue, not more regulations, are what is needed to further protect the country and its financial sector. In the State of New York, there are over 67 licensed money transmitters. On the other coast, in California, there are 58.

FinCEN, the IRS and the 47 States that license this activity need more resources to enforce the existing rules across the industry among both large and small money transmitters, as well as both the licensed and the unlicensed. By raising the level of compliance across the entire industry, we can all achieve the goal of a safer America.

Thank you, and I would be happy to answer any questions you may have later on.

Chairman SHELBY. Mr. Levine.

**STATEMENT OF EZRA C. LEVINE
COUNSEL, THE NON-BANK FUNDS TRANSMITTERS GROUP
AND PARTNER, HOWREY SIMON ARNOLD & WHITE, LLP**

Mr. LEVINE. Thank you, Mr. Chairman. My name is Ezra Levine. I am the Counsel to the—it is a long mouthful—Non-Bank Funds Transmitters Group. It has been in existence since 1987. It is the organization of the large national money transmitters, including Western Union, MoneyGram, American Express, RIA Financial Services, Comdata Network, and Travelex.

On behalf of the Group, we obviously appreciate the opportunity to testify today and to work with the Committee on important issues relating to MSB compliance with, and reaction to, USA PATRIOT Act rules enacted after the horrific events of September 11.

But it is important to set the stage, as even the earlier panel did, to discuss what this industry is. This industry, unlike the banking industry, essentially deals with individual consumers, many of whom are recent immigrants to the United States who are often sending very small amounts of money, typically well under \$400—it will vary company by company—but well under \$400 home.

Now, I was this morning preparing for this hearing and I came across the OCC report from September on the remittance industry; it is guidance to banks. It characterized, I think, beautifully the MSB industry, and these are the words—I wrote it down—“ubiquitous and convenient.” And I would add to that ubiquitous, convenient, safe, and secure.

Now, we heard before about State licensing, and I will digress from my prepared testimony. The State licensing that Commissioner Taylor talked about is in, as Mr. Cachey just testified, approximately 47 States, including Puerto Rico and the District of Columbia. It is safety and soundness regulation, much like bank regulation, to ensure that consumers are protected to the maximum extent practicable, so that MSB’s, which is a Federal term, not a State term, are safe and sound. Do they have the assets to match obligations?

Now, there has been an overlay recently of BSA compliance by the States. Part of that is good. Part of that, in our view, is bad because there has been a knee-jerk reaction over time among some of the State legislators to go well beyond what is in the BSA: To promulgate new and different recordkeeping and reporting thresholds, which may be well-meaning, but which, in fact, confuse and hinder the ultimate goal of compliance and education. When you have, for example, a Wal-Mart—I will pick a company—that operates in a number of States and provides as an agent certain MSB services this is a major issue.

Now, if you have to perform training, if you are Western Union, MoneyGram, or any of the large national or perhaps regional companies, you have an issue when the reporting threshold differs. You have other issues, for example, now as States jump in and say we want a copy of the SAR or a CTR, a hard copy, when, in fact, it is available to them through FinCEN's operation Gateway online immediately.

In fact, recently I was in a State in the Southeast; it was not your State, Mr. Chairman.

Chairman SHELBY. Not my State.

Mr. LEVINE. No, sir. We are working on the model legislation in that State for safety and soundness, and I said why do you want duplicate filings when you can get it from FinCEN? And they looked at me and said, we can? And I said, yes, you can. They will sign a MOU. You can get them. You do not need this. You do not want the paper.

I have talked to Committee staff about this. One of the things that is particularly infuriating, because you end up spending a lot of money to try to stop bad legislation in the States, such as a bill that is in New Jersey right now which would make it an absolute felony for any MSB to consummate a transaction at \$10,000 or more even if a CTR is filed.

However, the next sentence—and I could not make this up—the next sentence, Mr. Chairman, says, “However, it is permissible to do multiple transactions equal to or in excess of \$10,000,” which is the flip of the Federal rule.

Chairman SHELBY. I take it you did not write that, did you?

Mr. LEVINE. No, sir, I did not write that. I am opposing it, and it is costing us lots of money to oppose it and I hope we have it stopped. But there are a lot of things like this that are happening.

One of the recommendations—and I am glad that Superintendent Taylor is not in the room—that I have in my prepared testimony is that there really should be, at least in terms of the recordkeeping and reporting rules, as well as the Section 352 compliance programs, Federal preemption to the extent that these are the national rules. Whatever they are, good, bad, or indifferent, those should be the rules because once the States start jiggering around with this, when you have essentially an interstate industry—and let us not even get into the whole Internet issue—it makes it almost impossible for companies that are really spending the money and trying to do the job they are doing, like Western Union and MoneyGram, to effectively train people. We make the point that it is really a difficult challenge right now.

I would second those who have said that FinCEN needs to be strengthened. FinCEN, I will say, under Director Fox, has just become marvelously responsive. Director Fox has implemented a study now, and I think soon they are going to come up with a proposal for a one-page SAR.

The Senator indicated before that many of these entities are small businesses. If they are small businesses, let us give them something simple they can read. Let us put it in Spanish, too, so they can understand it, so filing can be effective.

Finally, enforcement. We have all been talking about enforcement, and then I will finish. Years and years ago, I had the good

fortune of working with Senator D'Amato when he had your position, Mr. Chairman, on the promulgation of 18 U.S. Code 1960, which makes it an automatic Federal felony to be an unlicensed money transmitter in a State.

The States do not have the resources to enforce their own State laws; they just do not, because they have to rely on county attorneys and district attorneys who quite frankly do not find violations of the licensing laws a sexy prosecution. The only way this can be done is to have the U.S. Attorneys prosecute under 1960, and that is beginning to happen. Again, it requires close cooperation between the Federal Government, the States, DOJ, FinCEN, and IRS.

And one plug for the IRS-CID. I believe they are doing a marvelous job both in outreach and enforcement. They are the only part of IRS that is continually doing outreach with the industry and with State banking departments and the U.S. Attorney and the FBI to get out to the small ma-and-pas and say, look, we need your help; please do it right.

Thank you, Mr. Chairman.

Chairman SHELBY. I thank all of you. First, I will ask each of you, what is the level of financial commitment to combat money laundering made in your businesses, just briefly?

Mr. FAHRENKOPF. That is a hard question for me to answer. I am not sure I have the answer. I think it would differ from company-to-company as to what the commitment is. But, you know, fundamentally, the integrity of our business depends on tough regulation, with law enforcement oversight. Without that, our business cannot exist.

So whatever is necessary to get the job done our companies will commit to. It is going to vary from company-to-company right now, but it is a significant sum, in the millions of dollars.

Chairman SHELBY. What about Western Union? You are all over the world, right?

Mr. CACHEY. Yes, sir, and, clearly, because we do business around the world, and also with the implementation of the USA PATRIOT Act 2 years ago, our compliance budgets, if you will, have been significantly increased hundreds and hundreds of percent over the last 2 to 3 years.

I think the important point, though, is that they will continue to increase. Banks have had 30 years, since 1970, to deal with the BSA and other types of anti-money laundering regulations, while this is new for the MSB businesses, if you will.

I think we have been in this for 2, 2½, maybe 3 years now and I think it is going to take several more years of continuous enhancing and building of these programs across the industry to really figure out what is the total financial commitment in the long-run.

Chairman SHELBY. If I wanted to wire \$9,000 to Bogota, Colombia, and I came to one of your offices, is that an average transaction or is that an unusual transaction?

Mr. CACHEY. No. As Mr. Levine indicated, our average transactions are well below \$500.

Chairman SHELBY. But, if I came in, you could make that \$9,000 transaction?

Mr. CACHEY. Yes, sir.

Chairman SHELBY. What would you ask me for in terms of information on that? Say I brought \$9,000 cash in and I wanted to send it to somebody in Bogota. They have a place to pick it up, do they not?

Mr. CACHEY. Yes, we do, sir, and that is the beauty of our system. We have locations all around the world.

First, we would obtain all the Bank Secrecy Act-required record-keeping information, which would be name, address, Social Security number; get a photo I.D., all the information under the BSA. Western Union, though, because the transaction is over a predetermined threshold which I would rather not disclose—

Chairman SHELBY. That is okay.

Mr. CACHEY. —would also require you to have a conversation with a specially trained customer service representative, where we would interview you, and this would happen out of our call center. We would get you on the phone and interview you and ask you questions like where did the cash come from, what is your relationship with the person you are sending money, what aren't you using a bank. That is a lot of money and it is really an exception to our process. Then if we felt we were comfortable with the answers we got, we would then allow the transaction to proceed.

Chairman SHELBY. What is your average money transfer?

Mr. CACHEY. Roughly, around between \$350 and \$400.

Chairman SHELBY. So anything that got up to \$5,000 would be kind of suspicious to you?

Mr. CACHEY. Not necessarily. For example, approximately half of our transactions in the United States alone are for bill payments to mortgage companies, car companies, or credit card companies. So the amount is really not a good indicator alone of what is suspicious.

Chairman SHELBY. If I went to a Western Union anywhere in the world and said, look, I have to pay my credit card bill, I owe American Express \$8,842.10, you could do that for me?

Mr. CACHEY. Assuming you were in the United States, because that is really where we offer most of these services. But if you are in the right place and we had a relationship with the credit card company where they said we want people to be able to send us money through your system, then you would be able to do that, yes, sir.

Chairman SHELBY. Okay.

Mr. CACHEY. And millions of people do it every month for house payments, credit card payments and car payments.

Chairman SHELBY. Mr. Levine, do you have a comment on that?

Mr. LEVINE. I was going to say, Mr. Chairman, that you were touching upon SAR's. When I do speak at the request of the IRS-CID often—and there is one coming, good travel, San Diego and Los Angeles next week. But when I testify there and I talk to small transmitters, the big issue that always comes up is what is suspicious, and what am I looking for?

Chairman SHELBY. How do you define it?

Mr. LEVINE. How do you define it? You know, what am I supposed to do? When do I do it? It is a perplexing issue, and I think in terms of MSB's, because they are, as the Senator indicated, often very small businesses who are trying to do it right, but they are

saying what is this, what am I supposed to be doing—but yet they are the ones who deal face-to-face with the customer.

Chairman SHELBY. Do the level of fines in your industry have any effect, Mr. Fahrenkopf?

Mr. FAHRENKOPF. They are significant. As you know, in the case that you were discussing earlier in the question, there was a \$5 million fine levied on that company. That is a significant fine. The regulators in Nevada are extremely tough and it certainly gets the attention of the companies.

Chairman SHELBY. Mr. Fahrenkopf, what, in your opinion, is needed now to ensure adequate governmental oversight of casinos, considering how they have grown in the last 10 or 15 years?

Mr. FAHRENKOPF. If I had to name an area where there should be some development, it would be more reliance on SAR's, less on CTRC's. As you know, I think there is a giant building in Detroit that is full of millions and millions of CTR's. I am not sure anyone has looked at them or will ever look at them.

The suspicious activity reporting requirements, I think, get more to the area where we can do a better job of making sure that money laundering, whether terrorism is involved or not—I think it is a more profitable area. In fact, we are working very closely with Mr. Fox and FinCEN people to try to develop a way to improve that system. I would say that would be the one area that I would see it.

Chairman SHELBY. Senator Bunning.

Senator BUNNING. Thank you, Mr. Chairman.

Mr. Fahrenkopf, are there any relatively quick and simple things that the Federal Government and the gaming industry can do to fight illegal money laundering that have not been mentioned here?

Mr. FAHRENKOPF. Senator, to my knowledge, there really have not been at this point in time any significant terrorism-related money laundering cases that have come down. But I think if there was one thing that would help, it is what I have just mentioned to the Senator, to increase the training of our people, which we are very concerned about.

I think the same question that Mr. Levine raised: How do you teach an employee what is suspicious and what is not, and that is why we have been holding these dialogues and conferences with FinCEN employees to work with our people. So education, I think, is probably the most important thing that perhaps is not what it should be.

Senator BUNNING. You realize the opportunity and the level of deception that the other side can use. Your facilities offer an unusual opportunity to do just that because of the amount of cash that is handled by many members in your group.

You are keenly aware of this, I know, and there are plenty of regulations, but I think it is up to the individual corporation or company to do a red-flag alert; if somebody comes back and sends some new people back and back, that you are keenly aware that this might not be normal procedure.

Mr. FAHRENKOPF. I think if you were to ask Mr. Fox and the FinCEN people, and ask State regulators in the States where we operate, that is very much what we focus on. We are concerned about structuring. We are concerned about people who come in par-

ticularly, Senator Bunning, and exchange a large amount of cash and we notice that they are doing very little gaming.

Senator BUNNING. In other words, they are trading the dollars for—

Mr. FAHRENKOPF. Exactly right.

Senator BUNNING. Okay.

Mr. FAHRENKOPF. So we are very, very cognizant of that, and I think we have been quite successful to this point, not perfect, and we continue to work on it.

Senator BUNNING. I know that you realize the biggest thing that the Fed and you can do today is to educate those that are handling those monies. I hope that the Western Union people are likewise being informed because I can send 20 people in with an \$8,000 transaction if I want to launder \$8,000 times 20, which would be about \$160,000. I can do that in many of your offices around this country and I can get an awful lot of money laundered if I choose to do so, if you are not alerted to the fact that this might be occurring, which is the big secret under the new laws that we have passed because you have not been governed before by any other transactions. You are not a bank.

Mr. CACHEY. Absolutely, but a couple of comments, Senator. First, Western Union was one of the money services businesses before we were defined as that by the USA PATRIOT Act that was actually filing suspicious activity reports on the bank form voluntarily for a number of years. So we have been fortunate to have a little bit of experience of already having a rudimentary program in place.

We have significantly enhanced that program since SAR filings became a required activity on January 1, 2002, for our industry. So, fortunately, my answer to you would be if you went to several different locations in the Washington, DC area and tried to either structure below the \$10,000 level or send what I would call an unusual amount of money—maybe not \$8,000, but some amount above that—we would have all that information.

Our system would have prompted our agents to automatically acquire the data that we are required to get from you. That would be aggregated in a central computer because all of our transactions go to one computer around the world, whether you are in the United States, France, Brazil, or China. We would be able to see in Washington, DC, what you were doing, fill out the SAR. And, again, if we thought you were a terrorist, we would be able to report that very promptly to FinCEN and other contacts in law enforcement.

Senator BUNNING. Thank you, Mr. Chairman.

Chairman SHELBY. Thank you.

Mr. Levine, in your testimony you were critical of State legislation directed at enforcing standards similar to BSA rules and MSB's. You have alluded to that. What are your views on allowing State examiners to examine for BSA compliance?

Mr. LEVINE. I have mixed views about it based on what we have seen. It is interesting because the States have been attempting through the Money Transmitter Regulators Association, which is the association of State bank superintendents, basically—it is akin to the CSBS, but they focus only on nonbank MSB's. They have

been trying for years to do one simple thing in their menu of activities, which is to take the 15 exams that Western Union or American Express undergoes now and have one.

The problem is really one of training, education, and cooperation. If you could have one and if they were trained by FinCEN and if there was close harmony so that you would know that the interpretation you were getting from the State regulator was the same interpretation that either the IRS or FinCEN would give, it might work. But it is not clear at this point that there is such a degree of training.

And also, because of State budget constraints—and you know all this, but because of State budget constraints, there is a huge turnover. People have been laid off in the various banking departments. The level of expertise is not always where it should be. Some States are good, other States are frankly abysmal.

Chairman SHELBY. But you could still balkanize the whole process, could you not?

Mr. LEVINE. Yes, and that is the way it is now. It is balkanized.

Chairman SHELBY. Mr. Cachey, Ms. Taylor's statement indicated that Western Union did not believe that it was subject to Federal statutes that prohibit the structuring of financial transactions for the purpose of evading currency transaction reporting requirements.

My question to you in light of that is what is your understanding of First Data Corporation and Western Union's responsibilities under the law with respect to currency transaction reports and the filing of suspicious activity reports?

Mr. CACHEY. Clearly, those laws apply to us.

Chairman SHELBY. You were fined \$11 million by the State of New York and FinCEN.

Mr. CACHEY. Correct.

Chairman SHELBY. What have you done since then?

Mr. CACHEY. Even before the fine actions took place, I can tell you, because I was involved in those negotiations, that—the New York fine occurred in December of that year.

Chairman SHELBY. Okay.

Mr. CACHEY. We changed our policies and our operations to comply with New York's guidance even before FinCEN opined with their guidance. The day after, we had a meeting with them at the beginning of October. We felt that this was just a question—and my understanding of the issue was that we just had a difference of interpretation for a very specific scenario for filing currency transaction reports, and that was do we treat our agents as separate financial institutions, as they are treated under the USA PATRIOT Act and the MSB? Or as a licensee, do we need to aggregate activity not for suspicious activity, but for currency transaction reporting? Clearly, now, after those fines and after being educated by FinCEN as to what their interpretation of the rule is, we have done that, and we have done that very proactively.

I would say, Mr. Chairman, that during that same year I had conversations with at least one other State banking department that, for lack of a better term, agreed with our interpretation of the law at the time. Again, I think this goes to Mr. Levine's statements that we really need to have one voice on how these rules should

be interpreted because, again, I was in a position where I had two different States saying to me you should be applying two different rules.

One agreed with me, one did not. The one I did not agree with is the one that fined me. We learn from our mistakes and we move forward. We are happy to do that, but really this is the reason why FinCEN really needs to give a lot more guidance out there on how the BSA should work in our industry.

Chairman SHELBY. First Data Corporation has experimented over the years with integrating its money transfer business with the use of ATM's.

Mr. CACHEY. Yes, sir.

Chairman SHELBY. I believe that another First Data Corporation subsidiary, Global Cash Access—is that it?

Mr. CACHEY. Yes. They are no longer a subsidiary of ours, but we did own a share of them at one point.

Chairman SHELBY. It allowed ATM's to be used to transfer funds through Western Union. What is the status of that program?

Mr. CACHEY. First, just to correct the record, I think the Global Cash Access product was one of issuing a money order to a customer to be cashed at the casino cage.

Chairman SHELBY. Okay.

Mr. CACHEY. But there are many pilots not just with Western Union, but a number of money transmitters and, quite frankly, banks are trying to crack the code on how do we use ATM's to facilitate money transfers around the world.

We currently have a pilot program in place which we spend a lot—

Chairman SHELBY. It is technically possible. That is, just the software, is not it?

Mr. CACHEY. Well, it is the software. I mean, from a technological standpoint, it is very easy to do. But from my standpoint as a compliance officer, you start to say what information are we collecting, how do we make sure that who is using the ATM is the person that should be using it, who is receiving the money. There are a lot of compliance questions.

I think, to me, the biggest pressing issue for the industry and for the regulators, particularly FinCEN, is ATM's and stored value cards, because they allow for a certain amount of anonymity with the customer. And trying to crack that code as to what guidance we can get from the Federal and State governments on how to do this, and then among the industry itself of how do we make sure that this system is going to be as safe and secure as somebody walking into an agent location and actually interacting with a human being who might be able to identify some type of suspicious activity—that is a real challenge right now.

Chairman SHELBY. What is the status of your partnership with 7-Eleven Corporation, where customers could purchase money orders, make money transfers, and cash checks through a system located in convenience stores everywhere?

Mr. CACHEY. Yes. That is a little bit different from an ATM product. It is what we call a kiosk product, and with that product you do not just sit at an ATM. Somebody actually has to pick up a dedicated phone.

Chairman SHELBY. I could go to a 7-Eleven, though, and buy a money order, could I not?

Mr. CACHEY. Yes, you could, absolutely.

Chairman SHELBY. Transfer money, whatever?

Mr. CACHEY. You could go to a 7-Eleven and buy a money order from their clerk.

Chairman SHELBY. Okay.

Mr. CACHEY. In a number of stores, we do have a kiosk product, which is what I think you are referring to, where you have to pick up a dedicated phone line and talk to one of our operators and say here is who I am, here is my information.

Again, these are pilot projects. These are not things that are thrown out there, though, and we do not just push the boat out into the lake and say let us see if it swims. We are monitoring all those transactions. We do file suspicious activity reports based on what we are seeing because not only is the business learning about how customers will interact with those new technologies, but also as a compliance department we are learning how could people potentially abuse these new technologies and what systems do we have in place to protect the systems.

Chairman SHELBY. Well, that is what we are after, assuming that most transactions are legitimate, and so forth, and what we must do is filter the system to get to the others. Isn't this what we are talking about?

Mr. CACHEY. Yes, sir.

Chairman SHELBY. I would assume that most gambling is gambling, but sometimes, Mr. Fahrenkopf, you would see somebody that gambled a little to get a little cash and move it?

Mr. FAHRENKOPF. I think so, sir.

Chairman SHELBY. And so how do you filter that?

Mr. FAHRENKOPF. That is the challenge.

Mr. CACHEY. The real challenge is finding—and I am just going to throw a number out—the 1 percent of the bad people, without impeding safe and convenient and quick services for everybody else that is doing stuff for legitimate purposes. It is that focusing on the 1 percent where I think we can all do better in communicating with each other on what we think we should be looking at.

Chairman SHELBY. Mr. Levine, do you have a comment?

Mr. LEVINE. Yes, Mr. Chairman. Then there is that “x” percent, the “x” percent of people that are using underground money transmitters who are avoiding licensing. We do not know how big that “x” percent is. So the Western Unions and the MoneyGrams of the world and the casinos of the world can do just a marvelous job, but there is an intricate balance.

Treasury always talks about this, and I think they are dead right, that if we set the standards too low, we end up driving customers, particularly some recent immigrants, to these underground hawalahs and others.

Chairman SHELBY. We have had hearings on that. We do not want to do that.

Mr. LEVINE. Exactly. That is a real problem because if the transactions are going through the licensed money transmitters, there is cooperation with law enforcement, there is a money trail, there are

records. You know who is doing it when you are in law enforcement.

Chairman SHELBY. Mr. Fahrenkopf, could you provide the Committee with some sense of how casinos, especially the larger ones, routinely process the paperwork associated with BSA requirements? How many CTR's and SAR's are filed annually by the industry that you represent? You can submit that for the record if you want to.

Mr. FAHRENKOPF. We will submit that to you, Mr. Chairman.

Chairman SHELBY. Can any of you think of any particular case where you have worked with law enforcement to stop the flow of laundered funds or funds to terrorist groups?

Mr. CACHEY. That is a challenge we have as an industry, and let us disregard the terrorism point of view. We file CTR's or SAR's, and rarely do we hear back from law enforcement, hey, great job; that piece of paper that you filed actually helped us catch a bad guy.

Typically, the only time I get any feedback like that is if I read something in the newspaper and I just knew that we were cooperating with law enforcement on a particular action. One of my officers was just down in Florida for a money laundering case where there were convictions for four individuals that were participating in a money laundering scheme.

We know we have a positive effect, but rarely do we get specific information back saying, good job, you did this, it led to this, keep it up. Particularly, I think, because of the national security issues on terrorist financing, rarely do I get feedback on that.

Chairman SHELBY. It would be good to know, though. That helps you and gives you courage to move forward to the next one, doesn't it?

Mr. CACHEY. Absolutely. We would love to have that feedback.

Chairman SHELBY. It would improve the working relationship between your industry and the Treasury.

Mr. Levine, do you have a comment?

Mr. LEVINE. I was just going to say, Senator, that the SAR review, the periodic review that FinCEN has been publishing now which is an attempt—and I think semi-successful—to give feedback to the industry, particularly banks, but also the MSB industry on how SAR's are helping in the war against terrorism, as well as the fight against money laundering—I think those efforts really need to be expanded. I think it is what you were suggesting.

Chairman SHELBY. How do you measure what you are doing, what you are accomplishing, if you do not have feedback, if you do not have examples? Isn't that correct?

Mr. LEVINE. Yes, sir.

Chairman SHELBY. Gentlemen, we thank you for your attention here and your participation.

The hearing is adjourned.

Mr. FAHRENKOPF. Thank you, Mr. Chairman.

Mr. CACHEY. Thank you, Mr. Chairman.

Mr. LEVINE. Thank you, Mr. Chairman.

[Whereupon, at 12:06 p.m., the hearing was adjourned.]

[Prepared statements, response to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF WILLIAM J. FOX
DIRECTOR, FINANCIAL CRIMES ENFORCEMENT NETWORK
U.S. DEPARTMENT OF THE TREASURY

SEPTEMBER 28, 2004

Chairman Shelby, Senator Sarbanes, and distinguished Members of the Committee, I appreciate the opportunity to appear before you to discuss the issues and challenges before us as we attempt to establish an effective and comprehensive anti-money laundering regulatory regime for two diverse and important sectors in the financial industry—money services businesses and casinos. Again, we applaud your leadership Mr. Chairman and the leadership of Senator Sarbanes and the other Members of this Committee on these issues. These issues are critically important to the health of our Nation's financial system and, indeed, our national security.

It is a pleasure for me to be here today with Superintendent Diana Taylor of the New York Banking Department and Commissioner Kevin Brown of the Internal Revenue Service's Small Business/Self-Employed Division. Superintendent Taylor and I have begun what I believe to be a good dialogue between our two agencies. We have high hopes that this dialogue will lead to a closer and deeper relationship with the New York Banking Department that will prove to be mutually beneficial.

As you know, the Secretary of the Treasury has delegated Bank Secrecy Act examination authority to the Internal Revenue Service for a variety of nonbank financial institutions including money services businesses and casinos. Commissioner Brown's division is responsible for this program. In the short time I have worked with him, I can state unequivocally that he and the people he has dedicated to this effort are taking their responsibilities under the Bank Secrecy Act quite seriously. We are all fortunate to have Commissioner Brown and his team in place.

When I appeared before you last June, I outlined a plan for establishing more aggressive and coordinated administration of the regulatory implementation of the Bank Secrecy Act. Since that time, we have made progress.

- We have created, within the Financial Crimes Enforcement Network's Regulatory Division, a new Office of Compliance devoted solely to overseeing the implementation of the Bank Secrecy Act regulatory regime by those agencies with delegated examination authority.
- We have created a new Office of Regulatory Support in our Analytics Division, thereby devoting, for the first time in the history of the Financial Crimes Enforcement Network, a significant part of our analytic muscle to our regulatory programs. These analysts will be used to identify regulatory weak points and common compliance deficiencies. The analysts will assist our Office of Compliance and the other delegated examiners to be smarter about their programs for Bank Secrecy Act compliance.
- We are very close to finalizing a Memorandum of Understanding with the five Federal bank regulators to provide information to us, in both specific and aggregate fashion, to prevent another situation such as the Riggs matter earlier this year and to give us a better understanding of the overall health of the Bank Secrecy Act regulatory regime. In those agreements, we have committed our direct involvement and support to those regulators in helping them discharge their regulatory plans.
- Finally, we are working to obtain similar agreements with the Internal Revenue Service, the Securities and Exchange Commission, and the Commodities Futures Trading Commission, which will enhance our collective ability to oversee Bank Secrecy Act compliance in the nonbank financial sectors.

Mr. Chairman, the importance of the personal and direct support that you and your colleagues on the Committee have provided to these efforts cannot be understated. That support will enable us to implement this plan in a much faster and more efficient manner. We believe that is critical and important, and we wish to thank you for that support.

I would do this Committee and my Agency a disservice if I did not tell you that we believe that the challenges associated with establishing and implementing an effective and comprehensive regulatory regime for nonbank financial institutions have been and continue to be extraordinary. In the money services business industry alone, we continue to face innumerable challenges. Beyond that, the USA PATRIOT Act directed FinCEN to extend the regulatory landscape to an even broader range of financial institutions, including such varied entities as unregistered investment companies, operators of credit cards systems, insurance companies and dealers in precious metals, stones and jewels. While we are firmly committed to expanding the Bank Secrecy Act regulatory regime to those financial service providers posing risks

for abuse by money launders and terrorists, it is essential that everyone understand the challenges we are facing when it comes to ensuring compliance with those regimes.

That said, it is our view that the nonbank financial services industry generally, and money services businesses and casinos in particular, understand the important link between the Bank Secrecy Act and our national security, and seek to comply with our regulations. There will always be outliers who seek to avoid regulation for the purpose of carrying out illegal acts. There will also always be those industries, such as the money services business industry, where we find a significant number of persons who do not understand their compliance obligations. Our task is to maximize compliance from all by utilizing the skills, resources, and expertise of our Federal and State-based regulatory partners.

Money Services Businesses

OVERVIEW OF THE MONEY SERVICES BUSINESS INDUSTRY

The term "money services business" refers to five distinct types of financial services providers: Currency dealers or exchangers; check cashers; issuers of traveler's checks, money orders, or stored value; sellers or redeemers of traveler's checks, money orders, or stored value; and money transmitters. The five types of financial services are complementary and are often provided together at a common location. Money services businesses have grown to provide a set of financial products that one would traditionally look to banks to provide. For example, a money services business customer who receives a paycheck can take the check to a check casher to have it converted to cash. The customer can then purchase money orders to pay bills. Finally, the customer may choose to send funds to relatives abroad, using the services of a money transmitter. All of these services are available without the customer needing to establish an account relationship with a bank or credit union. These businesses perform valuable services to a wide array of individuals.

In 1997, FinCEN commissioned Coopers & Lybrand to conduct a study of the industry prior to its rulemaking process. Based on this study, we had estimated the number of money services businesses nationwide to be in excess of 200,000.¹ Of these, approximately 40,000 were outlets of the U.S. Postal Service, which sells money orders. The study estimated that eight business enterprises accounted for the bulk of money services business financial products (that is, money transmissions, money orders, traveler's checks, and check cashing and currency exchange availability) sold within the United States, and accounted, through systems of agents, for the bulk of locations at which these financial products were sold. Members of this first group include large firms, with significant capitalization, that are publicly traded on major securities exchanges. We are commissioning another survey to update the information in the Coopers & Lybrand Study to get a better sense of the current size, composition, and nature of the industry, as well as of the potential for growth in the industry's component segments.

A larger group of (on average) far smaller enterprises competes with the largest firms in a highly bifurcated market for money services. In some cases, these small enterprises are based in one location with two to four employees. Moreover, the members of this second group may provide both financial services and unrelated products or services to the same sets of customers.² Far less is known about this second tier of firms than about the major providers of money services products.³

¹See Coopers & Lybrand L.L.P., "Non-Bank Financial Institutions: A Study of Five Sectors for the Financial Crimes Enforcement Network" (Feb. 28, 1997). This study estimated that there were approximately 158,000 money services business outlets or selling locations (not including Post Offices, which sell money orders and other money services business financial products, participants in stored value products trials, or sellers of various stored value or smart cards in use in for example, public transportation systems); and provided financial services involving approximately \$200 billion annually. This study estimated that, given trends current at the time, each money services business sector would grow at the following rates: Check cashers: 11 percent per year; Money Transmitters: 15 percent per year; Money Orders and Traveler's Checks: 5 percent or less per year.

²Members of the second group may include, for example, a travel agency, courier service, convenience store, grocery or liquor store.

³For example, at the time of the study, two money transmitters and two traveler's check issuers made up approximately 97 percent of their respective known markets for nonbank money services. Three enterprises made up approximately 88 percent of the \$100 billion in money orders sold annually (through approximately 146,000 locations). The retail foreign currency exchange sector was found by Coopers & Lybrand to be somewhat less concentrated, with the top two nonbank market participants accounting for 40 percent of a known market that accounts for \$10 billion. Check cashing is the least concentrated of the business sectors; the two

Continued

THE GROWTH OF THE LEGAL AND REGULATORY FRAMEWORK

Money services businesses have been subject to currency transaction reporting rules since the inception of the Bank Secrecy Act, and additional regulatory obligations have been added subsequently. In 1988, Congress enacted Section 5324 of the Bank Secrecy Act, requiring sellers of monetary instruments for \$3,000 or more in currency to verify the identity of the purchasers. The Money Laundering Suppression Act of 1994 mandated a system of registration for money services businesses. This was considered to be a necessary first step toward identifying a universe of financial service providers that was largely unregulated at the Federal level, extremely diverse both culturally and in size, and generally unknown to Federal regulators beyond the handful of large corporate entities such as Western Union and American Express. FinCEN proposed implementing registration regulations in 1997 along with a proposal to require the filing of suspicious activity reports. FinCEN finalized the rules in 1999, with a phased-in implementation period so that all initial registrations for existing money services businesses were required to be filed by December 31, 2001. In addition, money services businesses were required to begin filing suspicious activity reports in January 2002. In April 2002, in response to the mandate of Section 352 of the USA PATRIOT Act that financial institutions institute anti-money laundering programs, FinCEN issued a final rule requiring money services businesses to establish anti-money laundering programs reasonably designed to prevent such businesses from being used to facilitate money laundering and the financing of terrorism.

ADDRESSING THE CHALLENGES

The challenges we face in regulating the whole of the money services business industry are significant. We believe that a multifaceted approach—a combination of aggressive outreach and education to domestic industry, targeted examinations, fostering and development of similar international standards and approaches, and appropriate civil and criminal enforcement—with close coordination among FinCEN, the Internal Revenue Service, State regulatory authorities, and law enforcement, is the only way that we can maximize industry compliance.

Identifying the Universe of Money Services Businesses

Identifying the universe of businesses subject to our money services businesses anti-money laundering regulatory regime is a basic yet challenging initial step. Many of these businesses are small, one- or two-person operations. Additionally, the proprietors may not speak English as a first or even a second language. The challenge of merely identifying these businesses cannot be understated.

Our regulations require most money services businesses to register with the Department of the Treasury every 2 years. Certain money services businesses are exempt from that registration requirement, including:

- U.S. Postal Service outlets;
- Businesses that are considered money services businesses solely as issuers, sellers, or redeemers of stored value; and
- Branch offices and agents of a money services business.⁴

As of September 27, 2004, there are 21,058 money services businesses registered with FinCEN. This number is a raw number and does not account for filing errors, duplications, etc. While not all money services businesses are required to register, we believe there are a significant number of money services businesses required to register that have failed to do so.

Finding ways to enhance compliance with the registration requirement has been a focus of FinCEN since the inception of the registration concept. Initially, we hired a public relations contractor to engage in a multiyear outreach campaign (2000–2003) designed to educate money services businesses about the new registration and reporting requirements. The campaign employed a variety of techniques. The constituency relations portion of the campaign informed key third-party organizations and corporate entities, and their members and employees, respectively, about the new regulations. Media outreach consisted of issuing press releases, placement of stories and advertisements in targeted media, and arranging interviews with select reporters. Also, four ethnic subcontractors were engaged to conduct ethnic media

largest nonbank check cashing businesses make up approximately 20 percent of the market, with a large number of competitors.

⁴Businesses that are considered money services businesses solely because they serve as agents of another money services business are not required to register under current regulations; instead, the principal money services business must register and maintain a current list of its agents, which it must provide to the Financial Crimes Enforcement Network or the Internal Revenue Service upon request.

outreach to the African-American, Arab-American, Asian American, and Latino/Hispanic American communities. In addition, we created a website (www.msb.gov) dedicated to money services business regulations and guidance.

As part of FinCEN's outreach campaign, we developed free, easy-to-understand educational materials to help inform money services businesses about their obligations under the Bank Secrecy Act. These materials can be ordered or downloaded directly from the www.msb.gov website. These materials include a "Quick Reference Guide to Bank Secrecy Act Requirements for Money Services Businesses;" a more detailed guide to money laundering prevention; Posters and "Take One" cards, available in multiple languages and bilingual versions, to inform money services business customers about Bank Secrecy Act requirements and help customers understand why the business must ask for personal information; and videos and CD-ROM's, in English and Spanish, with case studies designed to educate money services business employees about the Bank Secrecy Act requirements.

This year, we posted the list of registered money services businesses on our website. By identifying registered money services businesses, we are assisting banks and other financial services providers in their own due diligence and publicizing further those businesses that comply with the registration requirement. We updated the list in July of this year, and intend to do such updates at regular intervals going forward.

Most recently, we solicited bids from contractors to update the money services businesses industry study originally conducted in 1997. This information, when coupled with the evolving information being obtained by the Internal Revenue Service as it conducts its examination activities, will further guide us in our outreach efforts and help us to target our examination and enforcement resources.

Unearthing the Underground Businesses

Perhaps the greatest challenge to regulating effectively the whole of the money services business industry lies in identifying and compelling the compliance of underground money transmitters or other informal value transfer systems. Steeped in history and clouded by secrecy, informal value transfer systems have existed for centuries and they continue to thrive in countries throughout the world, including the United States. Legitimate informal value transfer systems are utilized by a variety of individuals, businesses, and even governments to remit funds domestically and abroad in circumstances where a formal banking system does not exist. However, because such systems provide security, anonymity, and versatility to the user, the systems can be very attractive for misuse by terrorists and criminals. The vulnerability of informal value transfer systems in moving money on behalf of criminal organizations, and their potential misuse by terrorist organizations, poses a substantial investigative challenge to the U.S. law enforcement community, and certainly to us as regulators. These challenges include: (1) nonstandardized or non-existent recordkeeping and customer due diligence practices; (2) frequent commingling of informal systems with other business activities, including commodity trading or smuggling; (3) language and cultural barriers; and, (4) inconsistent laws and regulations at the international and domestic levels.

The challenge is further complicated by the recognition that informal value transfer systems often provide invaluable financial services to categories of individuals historically underserved or left out of the formal banking system. Our goal must be clear—to enhance the transparency of such systems through compliance with our regulatory requirements, without eliminating the ability of the unbanked to move legitimate funds to family members in other countries.

From a regulatory perspective, there are few things more challenging than identifying businesses that are deliberately seeking to avoid detection for unlawful purposes. However, in some instances, informal value transfer systems may be ignorant of the regulatory requirements, or they may be avoiding regulation because of a misperception of why we insist on transparency. While persuasion and outreach will never be effective in reaching the former, we are targeting our efforts toward the latter, both domestically and internationally.

In addition to the outreach efforts described above to educate these businesses about the requirements, FinCEN is working with the Department, the Internal Revenue Service and, increasingly, State regulators and law enforcement to better identify money services businesses operating underground, whether intentionally or ignorantly. For example, we are working with the Internal Revenue Service and law enforcement to develop "red flags" for legitimate financial institutions to help us identify money services businesses that choose to operate outside the regulatory regime. This builds on the prior work of FinCEN to educate the financial community about informal value transfer systems in Advisory 33, issued in March 2003. While it is theoretically possible for informal value transfer systems to operate wholly out-

side of the banking system, it is not the most likely scenario. Instead, most such systems will utilize an account to clear and settle transactions internationally. By providing our banks and other financial institutions with red flags and other indicia of such clearing accounts, they will be better able to assist us in identifying systems operating outside of our regulations. In our *SAR Activity Review* (Vol. 6) in November 2003, we highlighted informal value transfer systems and gave examples of the types of activities reported on suspicious activity reports by financial institutions that referenced such operations.

We are continuing our work with the Department of the Treasury on a variety of international initiatives not only to educate other jurisdictions about the need for a comprehensive regulatory regime, but also to learn from the experience of other jurisdictions as they attempt to address the problem of underground value transfer.

We also look forward to working even more closely with law enforcement as they target unlicensed and unregistered money transmitters. It is vital that we strike the appropriate balance between aggressive criminal enforcement and less invasive forms of education and outreach to those operating underground systems. As when we try to bring a school of fish to the surface, the splash spearing the one at the top may cause the others to scatter to the depths of the pond and actually make our job more difficult.

Finally, we will continue to analyze Bank Secrecy Act data, particularly to review suspicious activity reports filed by depository institutions to identify unregistered and/or unlicensed money transmitter businesses, and to perform independent research to unearth underground financial services providers.

Achieving better Compliance within the Money Services Sector

Since January 2002, money services businesses have filed more than 450,000 suspicious activity reports. These reports are providing useful information to law enforcement, but we are also seeing common deficiencies that need to be addressed through examination and guidance. This is to be expected from an industry with less experience in filing suspicious activity reports, especially given the wide diversity of businesses with varying levels of sophistication. That said, we are taking steps now to enhance the quality of data received. We have issued guidance to financial institutions on filing complete and accurate suspicious activity reports. Added emphasis is being placed on the quality of suspicious activity report data in all of our training seminars and presentations to the money services business industry. Finally, we will be monitoring reports filed to identify and ultimately minimize the occurrence of blank data fields.

We are seeing positive results. For example, we recently used suspicious activity reports filed by money services businesses to develop a case involving the remittance of U.S. dollars by U.S. citizens in circumstances indicating the potential for the funds to be diverted for terrorist funding purposes. This case has been referred to law enforcement.

Casinos

OVERVIEW OF THE INDUSTRY

Casinos in the United States are subject to a decentralized regulatory structure and are primarily regulated by the States and by tribal regulatory authorities. All casinos, including tribal casinos, with gross annual gaming revenue in excess of \$1,000,000 also are subject to the Bank Secrecy Act. There are approximately 800 casinos and card clubs operating in at least 30 jurisdictions in the United States (including Puerto Rico, the U.S. Virgin Islands, and Tinian) that are subject to the requirements of the Bank Secrecy Act. In particular, there has been a rapid growth in riverboat and tribal casino gaming as well as card room gaming over the last 10 years. More than \$800 billion was wagered at casinos and card clubs in the United States in 2003, accounting for approximately 85 percent of the total amount of money wagered for all legal gaming activities throughout the United States.

THE GROWTH OF THE LEGAL AND REGULATORY FRAMEWORK

State licensed gambling casinos were generally made subject to the recordkeeping and currency reporting requirements of the Bank Secrecy Act by regulation in 1985. Casinos were also, by regulations adopted in their current form in 1993 and amended in 1995 (there was a version in 1993), the first nonbank financial institutions required to develop anti-money laundering programs, prior to enactment of the USA PATRIOT Act. Gambling casinos authorized to do business under the Indian Gaming Regulatory Act similarly were made subject to the Bank Secrecy Act by regulation in 1996. The Department of the Treasury adopted Bank Secrecy Act regulations for casinos because it determined that:

- Casinos, as high cash volume businesses, are vulnerable to manipulation by money launderers, tax evaders, and other financial criminals; and
- In addition to gaming, casinos offer their customers a broad array of financial services, such as deposit or credit accounts, funds transfers, check cashing and currency exchange services, that are similar to those offered by other financial institutions and other financial firms.

In recognition of the importance of the application of the Bank Secrecy Act to the gaming industry, the Money Laundering Suppression Act of 1994 added casinos and other gaming establishments to the list of financial institutions specified in the Bank Secrecy Act. Specifically, the definition of casino includes a casino, gambling casino, or gaming establishment that is duly licensed or authorized to do business as such, and has gross annual gaming revenue in excess of \$1 million, or that is an Indian gaming operations conducted under or pursuant to the Indian Gaming Regulatory Act other than a Class I gaming operation.⁵

In 2002, FinCEN adopted rules requiring casinos, effective April 1, 2003, to file suspicious activity reports.

CURRENT CHALLENGES

Historically, casinos are no strangers to comprehensive regulation, and, as a result, simply do not pose the same types of risks as do money services businesses. Casinos have remained important partners in the fight against money laundering and financial crime. The challenge for FinCEN and the Internal Revenue Service is to determine how best to target casino examinations to deal with new issues, new products, and, importantly, new entrants to the industry. Providing outreach and guidance to the industry also will continue to be critical in assuring quality reporting and consistent compliance.

One facet of our efforts to coordinate with other Federal regulators and law enforcement to identify issues and target our examination efforts is FinCEN's participation on the Indian Gaming Working Group. The Federal Bureau of Investigation's Indian Country Unit established the Indian Gaming Working Group in February 2003 in an effort to identify and direct resources to Indian gaming matters and to focus on "national impact" cases. Indian Gaming Working Group's members include, in addition to FinCEN, representatives from the FBI, the Department of Interior-Office of Inspector General, the National Indian Gaming Commission, the Internal Revenue Service Tribal Government Section, the U.S. Department of Justice, and the Bureau of Indian Affairs. The purpose of the Group is to identify, through a monthly review of Indian gaming cases deemed to have a significant impact on the Indian gaming industry, resources to address the most pressing criminal violations in the area of Indian gaming. FinCEN provides regulatory guidance pertaining to the Bank Secrecy Act and case support to law enforcement as appropriate.

In an effort to help casinos understand the importance of reporting requirements under the Bank Secrecy Act, we are stepping up our outreach programs. Last year, we published Suspicious Activity Reporting Guidance for Casinos. We are now instituting programs at FinCEN to better monitor reporting under the Bank Secrecy Act to detect anomalies. Our new Office of Compliance will also be focusing on the casino industry as part of our efforts to enhance Bank Secrecy Act compliance. We are developing technological tools both in-house and in conjunction with the Internal Revenue Service that will enable us to develop sophisticated profiles of all financial institutions subject to regulation under the Bank Secrecy Act, not just casinos. This is our BSA Direct project about which I have spoken with you previously.

While BSA Direct is being developed, FinCEN has worked with the Detroit Computing Center to develop a monthly query to identify casinos with significant variances in their Bank Secrecy Act filings. The query compares the volume of casino currency transaction reports filed for the current month with the volume of currency transaction reports filed during the same month in the prior year. Based on the query, a report is produced which lists casinos whose currency transaction report filing volume has decreased by 30 percent or more. FinCEN has received and is analyzing the first report from the Detroit Computing Center, which compares data from January through August 2004 with data from January through August 2003. While this tool is not able to conduct the sophisticated monitoring that will be available through BSA Direct, this interim step should provide a rudimentary "early warning system" in the event of a catastrophic failure to file forms, as was

⁵ The Indian Gaming Regulatory Act, 25 U.S.C. 2701, establishes the jurisdictional framework that governs Indian gaming. The Act establishes three classes of games with a different regulatory scheme for each. Class I gaming is defined as traditional Indian gaming and social gaming for minimal prizes. Regulatory authority over Class I gaming is vested exclusively in tribal governments.

experienced in the Mirage case. We believe such tools will enhance our capabilities to identify and address potential compliance programs.

Finally, we will continue to work closely with the industry and industry leaders such as the American Gaming Association, who you will hear from shortly.

Further Examination and Regulatory Implementation

Today, our focus has been on money services businesses and casinos, yet the challenge of regulating all nonbank financial institutions is much larger. We will shortly issue final regulations requiring certain insurance companies and dealers in precious stones, metals, and jewels to establish anti-money laundering programs. There will be more industries that follow. Each new industry poses unique difficulties not only to FinCEN as the administrator of the Bank Secrecy Act, but also to the Internal Revenue Service as the examiner. We believe we are both doing all we can with present resource levels to attempt to achieve proper implementation of this regulatory regime, but the challenges are significant.

I would like to emphasize how we are working closely with the Internal Revenue Service on the issues associated with Bank Secrecy Act compliance in the nonbank financial sector. We believe that we are in this together and that we can only succeed if we work in close consultation. We meet monthly with the Internal Revenue Service to discuss examination issues, share information, and set priorities in a collaborative environment. FinCEN and the Internal Revenue Service also work together to train examiners, prepare education and outreach materials, participate in conferences and seminars, and prioritize and target examinations. FinCEN has conducted a comprehensive review of the Internal Revenue Service's Bank Secrecy Act examination manual and offered our suggestions for improving processes based on our experience in the other financial services sectors. FinCEN also provides analytical, regulatory and interpretive support for Internal Revenue Service examiners. Recently, FinCEN has supported and facilitated the development of a Memorandum of Understanding that would permit sharing of Bank Secrecy Act examination information between the Internal Revenue Service and State regulators.

Finally, our discussion of Bank Secrecy Act examination and enforcement, especially in the nonbank context, would be incomplete without acknowledging the vital role played by the State-based regulatory authorities. While we do not delegate Federal Bank Secrecy Act examination duties to the States, through their own authority and through similar regulatory regimes, the States apply their resources to these important duties. We have enjoyed a strong working relationship with our State regulatory partners and intend to enhance and supplement that relationship going forward to maximize the utility of scarce resources and to ensure the uniform application of our regulations.

Conclusion

In conclusion, Mr. Chairman, I hope my testimony today conveys the sense of urgency, energy, and commitment with which all of us at the Financial Crimes Enforcement Network are trying to tackle these challenging issues. Notwithstanding all of that good work, a robust and properly resourced examination function is the keystone to the success of our effort. We must avoid at all costs the cynicism created by a regulatory paper tiger. We are keenly aware of the importance of this task—we know that it is critical to our national security. We are committed to all we can with the resources we have been give to implement this regulatory regime in the best way possible. Again, we appreciate your leadership, support and willingness to address these issues. Thank you.

PREPARED STATEMENT OF KEVIN BROWN
COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED DIVISION
INTERNAL REVENUE SERVICE

SEPTEMBER 28, 2004

Good morning, Mr. Chairman and distinguished Members of the Committee.

I appreciate the opportunity to be here today to discuss the Internal Revenue Service's (IRS) efforts involving the Bank Secrecy Act (BSA). I would also like to thank your Committee staff members who assisted us during the preparation for this hearing.

IRS Enforcement

Under the leadership of Commissioner Everson, we are strengthening the focus on enforcement at the IRS, while maintaining appropriate service to taxpayers. We have four enforcement priorities. We will:

- Discourage and deter noncompliance, with emphasis on corrosive activity by corporations, high-income individual taxpayers, and other contributors to the tax gap;
- Assure that attorneys, accountants, and other tax practitioners adhere to professional standards and follow the law;
- Detect and deter domestic and offshore-based tax and financial criminal activity; and
- Discourage and deter noncompliance within tax-exempt and government entities and misuse of such entities by third parties for tax avoidance and other unintended purposes.

Detecting and investigating money laundering activity is an important part of tax compliance for the IRS. In addition, the failure to file Forms 8300 and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, often have a direct link to both tax evasion and money laundering. In some cases, because the schemes are sophisticated and because we may not be able to obtain evidence from some foreign countries, it is almost impossible to conduct traditional tax investigations. In these circumstances, money-laundering violations frequently are the only possible means to detect tax evaders.

Money laundering not only is used by domestic and international criminal enterprises to conceal the illegal, untaxed proceeds of narcotics trafficking, arms trafficking, extortion, public corruption, terrorist financing, and other criminal activities; but it is also an essential element of many tax evasion schemes. With the globalization of the world economy and financial systems, many tax evaders exploit domestic and international funds transfer methods to hide untaxed income. These schemes often involve the same methods to hide money from illegal sources and to hide unreported income. Both activities generally use nominees, currency, wire transfers, multiple bank accounts, and international “tax havens” to avoid detection.

Money laundering is the financial side of virtually all crime for profit. To enjoy the fruits of their crime, criminals must find a way to insert the illicit proceeds of that activity into the stream of legitimate commerce in order to provide the resources necessary for criminal organizations to conduct their ongoing affairs.

As part of its core tax administration mission, the IRS addresses both the civil and criminal aspects of money laundering. On the civil side, the Department of the Treasury has delegated to the IRS responsibility for ensuring compliance with the BSA for all nonbanking and financial institutions not otherwise subject to examination by another Federal functional regulator, including Money Service Businesses (MSB's), casinos, and credit unions. Under this delegation, the IRS is responsible for three elements of compliance—(i) the identification of MSB's, (ii) educational outreach to all these types of organizations, and (iii) the examination of those entities suspected of noncompliance.

The IRS' Criminal Investigation (CI) Division is responsible for the criminal enforcement of BSA violations and money laundering statutes related to tax crimes. CI uses the BSA and money laundering statutes to detect, investigate, and prosecute criminal conduct related to tax administration, such as abusive schemes, offshore tax evasion, and corporate fraud. CI also investigates the nonfiling of Forms 8300 and criminal violations of the BSA, including the structuring of deposits to avoid currency transaction reporting requirements, which frequently have a direct link to both tax evasion and money laundering.

Recently, the IRS created a new position with responsibility for the coordination of all IRS terrorist financing-related issues which will report directly to the Deputy Commissioner for Services and Enforcement.

BSA Program in IRS' Small Business/Self-Employed (SB/SE) Division

In further recognition of the importance of the IRS's role in the fight against terror and money laundering, SB/SE has just established a new organization, the Office of Fraud/BSA, which reports directly to the Commissioner of SB/SE. The director, an IRS executive, will have end-to-end accountability for compliance with BSA including policy formation, operations, and BSA data management. The director's operational responsibility will include line authority over all field activities, as well as the data management.

This new Office of Fraud/BSA consists of four territories, with about 310 field examiners reporting to managers located in 33 field offices nationwide. These exam-

iners and their managers are fully trained and are dedicated full-time to the BSA program. Additional support personnel provide assistance to the examiners, including workload identification. Working in close collaboration with Treasury's Financial Crimes Enforcement Network (FinCEN), the IRS also conducts community outreach to ensure that MSB's are aware of their requirements under the BSA.

Bank Secrecy Act Data

The IRS has responsibility for processing and warehousing all BSA documents into the Currency Banking and Retrieval System (CBRS), including Foreign Bank & Financial Account Reports (FBAR's), Currency Transaction Reports (CTR's),¹ Forms 8300 (Report of Cash Payments Over \$10,000 Received in a Trade or Business), and Suspicious Activity Reports (SAR's).² All BSA forms are processed at the IRS Detroit Computing Center (DCC). Managing the BSA data involves three separate but related functions that include: (i) collecting and inputting BSA data from reporting institutions; (ii) housing and controlling access to the BSA data after it is entered into the central database; and (iii) supporting the IRS and other law enforcement query systems to mine BSA data in support of law enforcement investigations.

Currently, CBRS has approximately 173 million BSA documents on file. These documents are comprised of CTR's, SAR's, Forms 8300, CMIR's,³ FBAR's, and various other BSA documents. All documents entered into the CBRS (approximately 14 million annually) are made available, at FinCEN's direction, to other law enforcement agencies (Federal, State, local, and international) and regulatory agencies, in addition to the IRS. However, the IRS is the largest user of the CBRS.

Usefulness of Bank Secrecy Act Data

The combined currency information in CBRS is extremely important for tax administration and law enforcement. The information provides a paper trail or roadmap for investigations of financial crimes and illegal activities, including tax evasion, embezzlement, and money laundering. The detailed information in these currency reports routinely is used by IRS CI special agents and Assistant U.S. Attorneys to successfully pursue investigations and prosecutions.

In civil matters, the IRS uses the CBRS database to identify cases for potential examination. For example, in many of our offshore trust schemes a search of CTR's can produce a wealth of information. IRS field examiners also access BSA documents to assist in on-going examinations. The CBRS database is used to assist in case building prior to beginning an examination.

Federal and State law enforcement agencies also find the CBRS data useful as evidenced by their participation in each of the 41 IRS hosted Suspicious Activity Report Review Teams (SAR-RT's) located throughout the country in our 34 Criminal Investigation field offices. Nationwide, approximately 345 law enforcement personnel are assigned, either full or part-time, to the SAR-RT's. These teams evaluate and analyze the SAR's for case development and field office support. Each month, these SAR-RT's review approximately 12,000 to 15,000 SAR's.

IRS Coordination with FinCEN

In carrying out our responsibilities under the Bank Secrecy Act, we are engaged in a close partnership with FinCEN. Currently, the IRS assigns senior analysts to act as the liaisons to FinCEN in both the civil and criminal matters. These individuals address issues ranging from the case support supplied by FinCEN to strategic implementation and interpretation issues pertaining to the Bank Secrecy and USA PATRIOT Act.

Beginning in fiscal year 2003, funding from FinCEN has allowed the IRS to add 82 additional full-time employees (FTE's) to its BSA program. Key areas of coordination include:

- Improving the quality of referrals for enforcement;
- Using data-driven analysis to assist in the risk-based identification of cases as well as to identify geographic locations of potential noncompliance;
- Conducting joint monthly meetings to discuss BSA issues, trends, and examination results;
- Establishing examination priorities;
- Having FinCEN participate in IRS BSA training classes and managers' meetings;
- Incorporating feedback from FinCEN on IRS outreach materials; and
- Establishing production schedules at DCC for new forms and form revisions.

¹ CTR's include FinCEN Form 104 and FinCEN Form 103 (filed by casinos).

² SAR's are filed by financial institutions to report suspicious activity.

³ Report of International Transportation of Currency or Monetary Instruments.

Strategies and Initiatives

We are undertaking several initiatives to enhance the BSA Program:

MSB Audits—We are piloting the examination of MSB's at the entity's corporate headquarters level. Three such examinations are currently underway. Working with the businesses, we are identifying their agents with the highest risk of noncompliance. This is a new approach for the program that was advocated by FinCEN, which we believe will provide better customer service for the MSB's and maximize our use of resources.

Increased Coordination with the States—We have completed a model Federal/State Memorandum of Understanding (MOU), which provides both the IRS and the participating State the opportunity to leverage resources for examinations, outreach, and training. We expect this MOU, developed jointly with FinCEN, to be available for sharing with the States in the near future.

Improved BSA Training—We have undertaken a major training initiative, including revising the Basic BSA Course to reflect the changes resulting from the USA PATRIOT Act. All personnel are:

- Instructed on how to access OFAC's (Office of Foreign Asset Control) website to identify individuals and countries which have been placed on OFAC's SDN (Specifically Designated National or Blocked Person) list.
- Trained to look for transactions going to OFAC blocked countries. Identification of these transactions has resulted in several referrals to IRS' CI organization and one contact to the Terrorist Hotline.
- Trained to identify unlicensed money transmitters. This year, four continuing professional education (CPE) training classes were provided to IRS field examiners: (i) Suspicious Activity Reports; (ii) Structuring, (iii) Informal Value Transfer Systems, and (iv) Section 352 of the USA PATRIOT Act.
- Trained in audit procedures to detect structuring.

More Effective Case Selection—We have increased BSA program oversight to ensure the compliance risk case selection tools provided to our field examiners are being used to identify cases. The centralization of case identification that will incorporate leads from the field and CI, as well as CBRS analysis, is scheduled to be in place by the end of the year. This approach will ensure consistency in risk-based case selection.

Better Education and Outreach—Historically, most of our field examiners spent a portion of their time conducting individual outreach visits. Education and outreach now is performed by SB/SE's Taxpayer Education and Communication (TEC) Division, which leverages resources to reach a larger number of covered businesses. We provide keynote speakers, conduct seminars, and provide educational programs relating to check cashers, bankers, tax practitioners, fraud examiners, corporate security personnel, and bank security officers. This outreach and our efforts to contact money service businesses are significant parts of our program to identify and educate MSB's regarding their requirements to register their business with both the State and Federal Government. The National TEC AML strategy was designed in conjunction with FinCEN, SB/SE, and CI to increase compliance of MSB's and casinos with the BSA.

Streamlined Quality Review—Quality performance measures have been developed, including a centralized review process. The centralized closed case review process will provide headquarters with the ability to identify trends and training needs. Including BSA in our quality review process will ensure a systemic method for making proper use of managerial feedback.

Anticipating Expanded Examination Scope—In anticipation of the requirement for the insurance industry to come under Section 352 of the USA PATRIOT Act, the IRS is working with the industry and FinCEN to develop an examination plan and a training program for field examiners.

IRS Resources Devoted to BSA

In fiscal year 2004, the IRS devoted 1,112 FTE's to the BSA Program for enforcement, compliance, and data management activities. In particular, CI devoted 486 FTE's to BSA enforcement, including 457 FTE's directly related to investigations. The SB/SE Division devoted 414 FTE's for BSA compliance activity, including examinations and outreach/education efforts, and 212 FTE for managing information related to BSA (179 FTE for CTR processing and 33 FTE for program maintenance). Of the above amounts, 82 FTE's were funded by FinCEN, including 64 FTE's for compliance activities, 6 FTE's for outreach and 12 FTE's for managing information related to BSA.

The IRS' total fiscal year 2004 BSA costs will be approximately \$131 million, including direct and indirect costs such as human resources, training, space, and com-

puter support. In fiscal year 2004, CI expects to spend about \$71 million on BSA compliance, including \$67 million directly related to primary and secondary investigations. The SB/SE Division expects to spend \$36 million for BSA compliance activity, including examinations and outreach/education efforts. The IRS expects to spend \$24 million for managing information related to BSA, including \$2.5 million for data services.

Conclusion

As I stated earlier in this testimony, the war on terrorism and the fight against money laundering are top priorities for the Internal Revenue Service. We are prepared to increase our commitment to the BSA Program, and we will continue to coordinate our efforts closely with FinCEN.

Mr. Chairman, I thank you for this opportunity to appear before this distinguished Committee and I will be happy to answer any questions you and the other Members of the Committee may have.

PREPARED STATEMENT OF DIANA L. TAYLOR

SUPERINTENDENT OF BANKS, STATE OF NEW YORK

SEPTEMBER 28, 2004

Good morning and thank you Mr. Chairman for holding this hearing on this very important and very problematic issue.

I am Diana Taylor, Superintendent of Banks for the State of New York. My Department is the regulator for over 3,400 financial institutions in New York State, including State-chartered banking institutions, the vast majority of the United States offices of international banking institutions, all of New York State's money transmitters, check cashers, mortgage brokers, mortgage bankers, and budget planners. The aggregate assets of the companies and institutions supervised by the Banking Department are nearly \$2 trillion.

I am honored to testify before you today on the issues that we confront as a State regulator with regard to enforcing the Bank Secrecy Act (BSA) and anti-money laundering (AML) programs in the nonbank sector, the MSB's.

The New York State Banking Department is responsible for licensing, supervising, examining, and regulating the check cashing and money transmitting businesses. We currently license 213 check cashers with 964 locations, employing 4,000 people. In 2003, in New York State alone, licensed check cashers cashed more than 36.4 million checks with an aggregate face value of some \$16.5 billion. Put another way, on average, New Yorkers cash nearly 100,000 checks worth more than \$45 million every day using these nonbank entities.

There are 72 licensed money transmitters operating in New York through approximately 28,000 agents in New York State, employing more than 63,000 people. In 2003, these licensed money transmitters processed more than 95 million travelers checks, money orders, official checks issued on behalf of banks and remittances with an aggregate face value of over \$85.9 billion in New York alone. Total nationwide figures for New York State money transmitters exceeded one billion transactions with an aggregate face value of over \$1 trillion.

These MSB's are a portal into our Nation's banks and, through them, into our financial system.

There are two major problems. The first is that supervision and regulation of this industry is very uneven. For a number of reasons, where MSB's are concerned, Federal laws that have been passed to prevent banks from unwittingly serving as a conduit for money laundering are not being enforced to the same level from State-to-State.

The second problem is that there has been a complete lack of co-ordination between the Federal designee for examination and enforcement authority, the IRS, and the State regulators. We do not share information as we should. I would go further and ask if the IRS is the appropriate Federal agency to spearhead these efforts.

We need to meet in the middle.

What is clear and undeniable is that the State regulators of MSB's can be a powerful tool for enforcing these Federal laws, but there is much that needs to be done before we reach that goal.

I suggest that there are three actions that need to be taken to put us on the right track.

First, we need formalized, set-in-stone procedures for two-way communication and coordinated exams between the State banking supervisors, which are the licensers, regulators, supervisors, and examiners of MSB's, and the Federal Government. I un-

derstand that the IRS is developing an MOU that would have them sharing information on these issues with State tax collection entities. For AML and BSA purposes this makes little sense, because it does not go far enough.

The regulators of MSB's are left out! These are the entities which are on the ground, dealing on a day-to-day basis with these 50,000 (and growing) institutions. I urge FinCEN and the IRS to work with existing channels such as the State Financial Regulators Roundtable (SFRR) to draft an MOU that the State MSB regulators can embrace to make sure that the BSA is effectively enforced with respect these entities nationwide.

Second, the States need Federal funds to train State examiners to do AML and BSA exams with respect to MSB's.

Third and just as important, Congress should make it clear that State banking regulators have the authority to enforce the BSA/AML laws for MSB's in their States. Absent that unambiguous message, you have a hodgepodge of activity on the States' parts that runs the gamut from aggressive to anxious anticipation.

For example, 39 States currently require money transmitters to be licensed. Imagine if every State understood that they are also federally empowered to enforce the BSA and the USA PATRIOT Act! The State regulators will be a powerful tool and partner for enforcement when they are explicitly authorized to do so.

While banks are bound by the law to report suspicious activities and we, along with our Federal counterparts, consider it to be our mission to ensure that banks know exactly what is expected of them in this regard, it remains a fact that bad money can pass, via a money transmitter, through a bank and to an unsavory entity without the bank even having a chance to know the customer.

And these businesses move a lot of money through our banks.

As tough as we are on banks in terms of ensuring that they know what is required of them under our laws, we are not doing enough to guard the nonbank portals into our banking system. That puts the banks, and all of us, at risk.

Despite the fact that current Federal law does not empower States to enforce the BSA/AML standards on MSB's, a recent CSBS survey shows that 19 States are already conducting BSA/AML exams of money service businesses and more are actively exploring how they can proceed. The survey also demonstrates clearly that there is a crying need for better communication among the States and the IRS.

Based on our own experience, even though we license, examine and supervise MSB's, other than at the criminal investigation level, interaction and coordination with the IRS on examinations or enforcement is de minimus.

In New York in particular, we depend on the protections that the BSA and AML statutes provide, as we have been designated a high intensity financial crime area (HIFCA) and a high intensity drug crime area (HIDCA), we are constantly at a heightened level of risk for crimes involving money laundering, drug trafficking, and terrorism.

Obviously, we have good reason to care about effective BSA enforcement.

There is a solid wall of law enforcement entities and groups that work to detect these HIFCA and HIDCA activities and enforce the BSA laws. What is needed to police the MSB's, which, as largely unregulated entities nationwide, could be perceived as a conduit for criminal activity, is a strong State regulatory base to function alongside the criminal investigators, as a partner.

What we, the regulators of MSB's can contribute is parallel to what we, with our Federal banking regulator partners, provide on the bank side of the BSA.

It is the regulators that can require these entities to have effective BSA compliance programs in place; examine and detect noncompliance with BSA laws; issue enforcement actions to correct and penalize violations; and oversee compliance with corrective actions.

But in order to do that, we must have clear channels of communication.

Two years ago, SFRR, which is the umbrella organization for all State financial regulators, invited the Treasury Department and the IRS to a meeting to begin discussions on instituting a formal agreement to cooperate, coordinate, and share information in an effort to enforce AML and BSA laws with regard to money transmitters and check cashers.

To date, overtures from SFRR have not been successful in achieving such cooperation, much less a productive meeting.

How much more effective could we all be if we worked together? In New York, for example, the BSA/AML concerns with regard to all the entities we supervise or regulate are met through the application, examination, and supervisory processes.

During the application process, applicants must provide an Anti-Money Laundering Compliance Manual, and an affidavit indicating compliance with the USA PATRIOT Act, inclusive of the four requirements for an effective anti-money laundering compliance program:

- First, policies, procedures, and internal controls designed to ensure compliance with the BSA.
- Second, designating a compliance officer responsible for day-to-day compliance with the BSA and the compliance program.
- Third, education and/or training of appropriate personnel; and
- Fourth, independent review to monitor and maintain an adequate program.

At a minimum, the first three points must be checked off prior to the issuance of the license. This allows the Department to assess the BSA/AML knowledge base of the applicant and ensure—from the very beginning—that the compliance program is adequate.

The examination process applied approximately 9–12 months after licensing allows the Department to test the implementation of the compliance program presented during the application process.

After the initial examination a licensee is subjected to either an annual (money transmitter) or bi-annual (check casher) examination cycle. Needless to say, to examine every licensee outlet would not be possible. The examination process is conducted on the consolidated licensee level.

For consistency, the core BSA/AML examination program that we use is the same as that used by the Federal agencies. Although a standardized examination program is available, it is a flexible format that may be tailored to the risk profile of a given licensee. In addition, all sources of information available are used to determine a licensee risk profile, for example CTR's and SAR's filed with FinCEN. In the field, transaction testing is performed using a variety of sampling techniques, that is identified high-risk transactions. In addition, a visitation program is executed on selected agent locations.

A mix of examination resources is used. The Department's Criminal Investigation Bureau (CIB) has trained specialists dedicated to the BSA/AML. These resources are used for all money transmitter examinations and are available for any other targeted reviews as may be necessary.

Our regular examiners also conduct BSA/AML examinations. During the examination of every money transmitter and check casher, a BSA/AML review is conducted. Because it is recognized that specialization in BSA/AML reviews is required, the Department is continuing its efforts to strengthen a dedicated team of BSA/AML examiners within CIB. However, because resources continue to be scarce, continued training of the general examination staff remains critical. For example, in August, a training class in examining money transmitters included a segment dedicated to BSA/AML.

And what happens if something is amiss? We have the power to punish, either publicly or privately. In New York, we interpret our banking law to give us the authority to apply and enforce the BSA/AML standards under our safety and soundness rules.

Licensees found to be deficient and in violation of the BSA/AML standard face supervisory action or suspension of operations, or both. Serious deficiencies and violations represent unsafe and unsound practices that in the most severe case could result in revocation of a license.

Fines levied by my Department in these cases have ranged from \$15,000 to \$8 million.

As recently as last March, the result of on-site examinations culminated in the money transmitters Transworld Transmitting Corp's and Rupauli Exchange, Inc's operations being suspended until their BSA/AML compliance programs were developed to our satisfaction along with an independent audit of the program. Both businesses were fined \$15,000.

The \$8 million case involved Western Union and is perhaps the best known. And, better yet, for the purpose of this hearing is a perfect cautionary tale.

Because we are the regulator for Western Union, we supervise and examine it. And unlike some of our counterparts in other States, we do have the capacity and expertise to conduct BSA/AML exams for these entities.

In the course of a regular examination, our examiner noticed that Western Union did not aggregate transactions for each customer across all of their locations. Under the USA PATRIOT Act, the IRS has been given the examination and enforcement authority over MSB businesses. But it was my Department that was in Western Union and able to spot the problem, not the IRS.

This goes to my point that State regulators are the ones performing regular examinations of MSB's—it is in our mandate. FinCEN and the IRS should take advantage of this on-the-ground force. The IRS simply does not have the resources to perform BSA compliance examinations of the tens of thousands of MSB's, nor does

doing this have any relation to the core mission of the IRS. For us, it is our core mission.

The Department held that Western Union had an obligation to ensure that transactions by the same party conducted at different agents of the money transmitter were being aggregated for the purpose of filing CTR's and detecting suspicious activities. Since Western Union would not, our examiners did conduct the aggregations and, lo and behold, suspicious activities became clearly apparent.

Still Western Union continued to maintain that they were not required to aggregate under the law.

Let me make it clear that we believe that under N.Y. Banking Law, the Department has the authority to make sure that its licensees are in compliance with all State and Federal laws, including the BSA.

While we take this position, some other States do not. If the authority of the State regulators of MSB's to enforce this law were made explicit in the BSA, we believe more State enforcement resources nationwide immediately would be turned to this critical task.

Even though my Department holds that it has the authority to enforce the BSA, it is important that the BSA be interpreted by the proper Federal authority, FinCEN.

On the Western Union case, we worked with FinCEN to get a ruling as to the correct interpretation of the BSA and they backed our position on this matter in an Advisory Opinion which appears on their website today.

It is important to note here that as closely as we work with them, getting a response from FinCEN took months. It is clear to me that they lack the resources to deal with the many responsibilities given them by Congress. FinCEN must be able to perform its critical role in producing and disseminating interpretations, advisories, regulations, and examination guidance, so that the rest of us can get on with the job of ensuring compliance with the BSA.

FinCEN must be given sufficient resources to dedicate to this fundamentally important task; otherwise financial institutions, both bank and nonbank, and State and Federal regulators who have the will to comply with and enforce the BSA are operating without sufficient direction on how to do so.

We have followed up with Western Union, monitoring its compliance with the Department's enforcement order. The role of supervisory follow-up is critical to ensure that the corrective steps that have been ordered are taken and a proper control environment is established and maintained, so that BSA compliance gets on track at the licensee. This function is played by regulators of MSB's and is an important component to ensure BSA compliance. The IRS is not set up to provide this type of continuing oversight.

Following the imposition of the enforcement order, Western Union has devoted extensive managerial and financial resources to becoming a leader among MSB's in compliance with the BSA.

I know you look forward to hearing from them in the next panel.

In addition to the \$8 million fine imposed by my Department—the largest enforcement action to date against an MSB—FinCEN imposed a nationwide \$5 million penalty against the company.

The point here is that many MSB's operate across State lines. The efforts of a single State MSB regulator can alert FinCEN and IRS to multi-State noncompliance which they can then use to further enforcement and compliance efforts nationwide.

In order to build this more perfect world, we must repair the disconnect evidenced by the status quo—a total lack of coordination between the State and Federal Governments when it comes to enforcing the BSA/AML statutes for MSB's.

In closing, a recent KPMG study has made the sober point that many banks are still unable to monitor financial transactions across international borders, despite all of the money they have spent on technology designed to help them spot trends and suspicious activity.

If banks continue to have trouble in this area, how are the MSB's to deal with their customers—a massive population that, for whatever the reason, does not use banks directly to move money around? No matter how minuscule the percentage of bad actors using MSB's for illicit purposes, there is the potential for massive damage.

We have the responsibility to protect our people, our businesses and our financial system. We also have the responsibility for keeping legitimate money flowing, unimpeded, to where it needs to go, but we must put a ring of protection around the portal.

We cannot afford to do less.

PREPARED STATEMENT OF FRANK J. FAHRENKOPF, JR.

PRESIDENT AND CEO, AMERICAN GAMING ASSOCIATION

SEPTEMBER 28, 2004

Mr. Chairman, I am very pleased to be able to appear before this Committee on the important subject of anti-money laundering programs. For the last 19 years, the commercial casino industry has spent millions of dollars and has devoted untold hours of effort to ensure the strictest possible compliance with the requirements of the Bank Secrecy Act, and to prevent the use of our facilities by money launderers. This industry takes very seriously these obligations to our Nation, our customers, our employees, and the communities in which we operate. Our industry has always been—and always will be—highly regulated by our host States, and we have always recognized our duty to ensure maximum possible legal compliance. Since the American Gaming Association was founded in 1995, we have helped our industry and the Department of the Treasury form an effective partnership in meeting these obligations.

The American Gaming Association represents the commercial casino industry, consisting primarily of publicly held hotel-casinos listed on the New York and Nasdaq stock exchanges, including most of the names consumers are most familiar with in our industry: Harrah's Entertainment, MGM MIRAGE, and Caesars Entertainment. Commercial casinos currently operate in 11 States and directly employ more than 350,000 people, who earned more than \$11 billion in 2003. Our segment of the industry generated at least an equal number of additional jobs in construction and related businesses. State regulations control the industry's financial and business practices through exacting conditions of licensing. Board members and senior executives are subject to exhaustive background investigations and must be found suitable for a gaming license. Our gaming employees, and in many cases our vendors, also must have background checks by State regulators before they can work in the industry.

Beginning in 1985, our casinos have been subject to currency reporting obligations under the Bank Secrecy Act (BSA). In the nearly two decades since then, commercial casinos have filed millions of CTRC's (Currency Transaction Reports for Casinos), and currently submit them at a rate of several hundred thousand per year. The industry itself has expanded substantially over the same period. In 1985, commercial casinos operated only in Nevada and New Jersey. When the Department of the Treasury first applied currency-reporting obligations to casinos, the department exercised its powers under the BSA to enter into a memorandum of understanding with Nevada gaming regulators under which Nevada casinos reported currency transactions exceeding \$10,000 through a State-administered program that was supervised and approved by the Treasury. That memorandum has been revised since 1985, to the point where the Nevada requirements closely track the Federal program. All non-Nevada casinos have always been subject to direct Federal supervision for CTRC compliance.

A major challenge for Federal and State regulators, and for the casino industry, has been adapting BSA requirements to an entertainment venue like a casino floor. The BSA was designed to apply to business settings like banks and brokerage offices, where customers expect to have to document their activities. A casino offers a very different environment. For example, rarely (if ever) will a visit to a bank or stock brokerage include a Mardi Gras parade, a Cirque du Soleil performance, or food and beverage service. Similarly, we provide cash services 24 hours a day, 7 days a week—well more than any other business regulated under the BSA. In the fast-paced atmosphere of a casino, at all times of the day or night, our members have to acquire good identification documentation from customers so we can report both cash transactions and suspicious activity. We also have to effectively track the activity of customers who play a number of different casino games during a visit or who play at different tables throughout an evening. Although these are difficult tasks to perform, we think, on balance, we are meeting these challenges.

That is not to say that individual companies have not sometimes missed filing currency reports that they should have filed. Any such violation is one violation too many. Still, like banks and brokerage houses and money businesses, the gaming industry has found that its systems and its people occasionally have failed to meet the daunting technological and administrative challenges posed by anti-money laundering requirements. I want to stress that none of these violations has been found to be intentional, or to involve some form of collusion with a money laundering enterprise. Indeed, the more recent situations of this type largely have been discovered by the gaming companies themselves and self-reported to regulators. Like the other

financial institutions, we have to learn from these failures and make sure we do a better job every day, and that is exactly what we are committed to doing.

Seven years ago, the anti-money laundering effort in the industry moved to a new level when Nevada required that its casinos file "suspicious activity reports" concerning customer activity that might constitute money laundering or other illegal activity. Seven months after Nevada acted, Treasury proposed such an obligation for the rest of the industry. At that time, a number of our members began filing suspicious activity reports for non-Nevada casinos on a purely voluntary basis. New Jersey imposed mandatory suspicious activity reporting on casinos in that State in October 2000, and Treasury's suspicious activity rule for casinos took effect some 30 months later, on March 25, 2003.

The AGA applauds this move toward suspicious activity reporting, and away from the previous reliance on CTRC's. That move places the knowledge and observations of our experienced employees in the service of the Government's anti-money laundering efforts. I would like to note a few statistics relating to suspicious activity reporting by casinos:

- Between August 1, 1996 and December 31, 2003, casinos filed 9,866 suspicious activity reports (SAR's), with over half of those being filed in 2003, when Treasury's mandatory rule took effect.
- Almost 90 percent of the suspicious activity reports filed by casinos and card clubs have been filed by the commercial casino industry.
- About one-third of the suspicious activity reports have concerned possible "structuring" activity by customers, while 15 percent concerned large cash transactions with "minimal gaming," which could be a sign of money laundering. By way of comparison, roughly half of the SAR's filed by U.S. banks through June 2003 concerned suspected money laundering and structuring.

We also have worked with Treasury, and our State gaming regulators, in the fight against money laundering. For over 10 years, a representative of the commercial casino industry has participated in the efforts of the Bank Secrecy Act Advisory Group. On two recent occasions, we have organized a series of government-industry conferences across the country on money laundering issues. The first round of conferences was designed to help Treasury gather information about anti-money laundering efforts at casinos. The second round involved a series of workshops on Treasury's new suspicious activity regulations for casinos. We also have organized numerous "back of the house" tours of casino facilities, as well as other meetings with industry participants, to help Treasury officials evaluate anti-money laundering programs in our industry.

The gaming industry will continue to do its part in this heightened security environment. Because we handle many cash transactions and must comply with comprehensive State regulations, our properties already have extensive security measures in place. The nature of our business demands that we meet a safety standard that other industries now strive to reach.

Although new legal duties will often present challenges, we have confidence that we will be able to work with our Federal and State regulators to develop effective implementation plans. We recognize the paramount importance of taking meaningful steps to ensure the safety of our employees, our customers, and our communities, and to minimize any potential for terrorist or criminal activity involving our businesses.

PREPARED STATEMENT OF JOSEPH CACHEY III

DEPUTY CHIEF COMPLIANCE OFFICER AND
COUNSEL, AML GLOBAL COMPLIANCE
WESTERN UNION FINANCIAL SERVICES, INC.

SEPTEMBER 28, 2004

Good morning. I would like to thank you on behalf of Western Union for the opportunity to address the Committee on the important topic of the effectiveness of our Nation's anti-money laundering efforts and the compliance measures undertaken by Western Union under the Bank Secrecy Act and USA PATRIOT Act.

Western Union is a leader in worldwide money transfer. Our services are available in over 195 countries through some 200,000 agent locations. Western Union is a part of first data corporation, a publicly traded *Fortune* 300 company with over 30,000 employees worldwide. First data provides credit card and payment processing solutions to a wide range of clients including over 1,400 banks, millions of

merchant locations, and even Government agencies, such as the Internal Revenue Service. First Data and Western Union are subject to a broad array of State and Federal regulations that ensure safe and sound services to our customers.

Since the anti-money laundering regulations implementing the USA PATRIOT Act took effect in July 2002, Western Union has created an industry leading compliance program in a relatively short period of time and we continue in these efforts. I am here today to discuss the most important aspects of our anti-money laundering compliance program: Experienced people; data collection, monitoring; analysis and reporting; OFAC compliance measures; regulatory and law enforcement outreach; and our agent compliance support program.

The most important aspect of any compliance program is experienced people. We have increased anti-money laundering expertise within Western Union's compliance department by hiring, and we continue to recruit seasoned compliance officers from global banks, regional financial institutions, Government and other segments of the financial services industry. This expertise continues to help the company enhance its overall compliance effort and identify and address potential risk. This leadership team is working toward providing more sophisticated risk assessments, developing ongoing training, and support programs for our agents and enhancing our anti-money laundering programs across the company. They also assist in the development and management of the over 150 employees within the department.

Further, Western Union has significantly enhanced its own transaction monitoring capabilities to better detect and report suspicious activity and large currency transactions to the Financial Crimes Enforcement Network (FinCEN). We developed our own proprietary software for our unique money transfer system. We believe that getting the right information into the hands of law enforcement is our primary mission. Unlike other financial services, Western Union's money transfer services are offered through a "closed loop" system. We have direct relationships with both the agent initiating the money transfer and the agent paying out the money transfer. We collect information from both the sending consumer and receiving consumer. The data never leaves the Western Union system. We are in a unique position to monitor the entire transaction and provide that complete picture to law enforcement. Now with over 2 years of experience, we continue to improve on our reporting processes.

In addition to our standard monitoring programs, we are currently developing an internal financial intelligence unit (FIU) to better identify possible money laundering trends early on and be more proactive in reporting such activity to law enforcement. This FIU is modeled after those created by central banks and global banks and evidences a multi-layered approach to addressing anti-money laundering risk, which includes agent reporting under the Bank Secrecy Act, and our standard, as well as specialized, monitoring.

Additionally, Western Union maintains a worldwide OFAC/Government interdiction program that examines the names of every sender and receiver that enters our system, whether or not the money transfer touches the United States.

Finally, we believe that communication and cooperation between industry and regulators is essential to a winning strategy. This year alone, my compliance officers and I have visited with the central banks and FIU's of over 30 other countries to facilitate an exchange of information on these issues. We strive to partner with all Government stakeholders to facilitate an ongoing dialogue in an area where risk and trends can shift on a daily basis.

As you can see, Western Union is totally committed to getting this right. But it is also important that our agents get it right.

Outside the United States, the majority of our agents are banks or postal service systems. These entities are very familiar with doing business under a regulatory framework and have experience in combating money laundering. In the United States, our services are offered through retail businesses like grocery store chains, local convenience stores, and check cashers.

Under the USA PATRIOT Act and its implementing regulations, both Western Union and its domestic agents representing 45,000 independently owned locations have a separate and independent obligation to implement and maintain an anti-money laundering compliance program. Western Union takes this responsibility seriously, as do our agents. Our agents are the "front line" defense against money-laundering. Many of our U.S. agents belong to large, publicly traded entities and have controls and programs in place like any large U.S.-based company.

Effective compliance starts when we are selecting our agent partners. Western Union wants to make sure we have the best available businesses offering our services. Our due diligence on prospective agents can include both financial and third-party verifications and criminal background checks. Agents receive initial training, monthly compliance information, and ongoing training opportunities.

Our initial challenge with the USA PATRIOT Act was that the requirement of having a formal compliance program was new for many of our U.S. agents. Our agents faced a steep learning curve. To meet this challenge, Western Union initially distributed a “turn-key” compliance guide to the entire agent base. This guide explained what a compliance officer does, and provided sample policies and procedures, employee training materials, and an independent review guideline. Our goal was two-fold, first, educate the agent and second, make compliance affordable. We did not want each agent to have to hire a lawyer or consultant to understand the law and create its program.

We continue to enhance these efforts. We offer our agents training opportunities to assist them in understanding anti-money laundering issues and how to build a better compliance program. We have developed additional materials, in a variety of languages, to assist in the drafting of more in-depth policies and procedures. We also offer agents software that allows them, if appropriate, to monitor weekly transaction activity for suspicious activity at their locations. We continue to expand the compliance tools we offer our agents. We have been implementing a compliance review program and will suspend or terminate any agent who does not meet our compliance standards.

However, as an industry with just over 2 years experience in developing USA PATRIOT Act anti-money laundering programs, we still are in need of guidance and continued open dialogue.

Western Union and the agent locations we support really have 49 regulators in the United States: 47 States, FinCEN, and the IRS. Western Union is routinely examined by up to 15 different State banking departments in any given year. This framework can make regulatory consistency a challenge. It is our opinion that FinCEN, as the policymaker for our industry, is in the best position to provide the necessary guidance on these issues. A single guiding voice is becoming increasingly important in light of the fact that money services businesses operate under multiple licenses.

The regulations call for a risk-based program meaning that a one-size-fits-all approach is neither required nor appropriate. This approach allows the money services business to determine the risk areas and apply resources appropriately—efficiencies are created and in this manner actually more risk can be addressed, more effectively.

However, risk may shift as more information can be obtained and analyzed, and so must our focus. For this approach to have the desired effect, the regulator, in this case FinCEN, must provide ongoing communication to industry about emerging risks and money laundering patterns so that the industry can direct its compliance efforts toward the most critical risk areas. This type of ongoing communication should not only result in more meaningful reporting of suspicious activity to law enforcement but allow the industry to reduce the filing of non-useful reports which may create “noise” and undermine the efforts of law enforcement.

One primary example is the reporting of simple structuring. Currently, the suspicious activity reporting (SAR) threshold is at \$2,000 and structuring may occur just below the \$3,000 recordkeeping requirement. Together, we need to question whether financial institutions reporting activity at this level is helpful to law enforcement. We would encourage FinCEN to analyze its SAR data across the financial services community and provide more guidance on what type and level of activity presents the best intelligence to law enforcement. It is possible that by focusing on higher levels of activity we can reduce the number of non-useful reports, assist law enforcement in more rapidly identifying money laundering schemes and drive our collective resources to where the risk really lies.

We believe that more resources and more meaningful dialogue, not more regulations, are what is needed to further protect the financial sector. In the State of New York, there are over 67 licensed money transmitters; on the other coast in California there are 58. FinCEN, the IRS, and the 47 States that license this activity need more resources to enforce the existing rules across the industry, among both large and small money transmitters, as well as both the licensed and unlicensed.

Finally, a few words on combating terrorist financing. We believe, particularly in the fight against terrorism, that there is no foreseeable finish line, and Western Union, as a global company, is committed to applying resources commensurate with this great risk we are all facing. The September 11 Commission states “while the hijackers were not experts on the use of the U.S. financial system, nothing they did would have led the banks to suspect criminal behavior, let alone a terrorist plot to commit mass murder.” (The September 11 Commission Report, Norton Ed., p. 237.) Terrorist cells obtain legitimate Government-issued identification, they open bank accounts and they have debit and credit cards. Their financial needs and transactions, moreover, may also be surprisingly small and consequently not easily de-

tected or prevented. In fact, their funding may be generated internally without the need for regulated financial services. All these factors make it extremely difficult for a money services business to find that needle in the haystack without better information from the Government. If a name is identified by the Office of Foreign Assets Control as a specially designated person, we will stop that transaction. But, I ask, how can we work better together to identify and report on money transfers before the name gets on a publicly available list?

In conclusion, the USA PATRIOT Act has strengthened our country's anti-money laundering efforts significantly and our industry has been there every step of the way. But to move to the next level, to become more sophisticated in detecting and reporting meaningful suspicious activity, will require all of us to do a better job in proactively communicating and cooperating. Thank you. I will be happy to address any questions you may have.

PREPARED STATEMENT OF EZRA C. LEVINE
COUNSEL, THE NON-BANK FUNDS TRANSMITTERS GROUP AND
PARTNER, HOWERY, SIMON, ARNOLD & WHITE, LLP

SEPTEMBER 28, 2004

Mr. Chairman and Members of the Committee, I am Ezra Levine, Counsel to the Non-Bank Funds Transmitters Group (Group)—the organization of the national money transmitters—Western Union Financial Services, Inc., MoneyGram International, Travelex Americas, American Express Travel Related Services, RIA Financial Services, and Comdata Network, Inc. Each company is licensed under State money transmission laws and each is registered as a Money Services Business (MSB) with the Treasury Department. The Group is a participant in the Treasury's Bank Secrecy Act Advisory Group. On behalf of the Group, we appreciate the opportunity to appear before you today to discuss the role of money transmitters, including issuers of payment instruments such as money orders and travelers checks, in the fight against money laundering and terrorist financing.

As you are aware, even before the horrific events of September 11, nonbank money transmitters as "financial institutions" under the Bank Secrecy Act (BSA) were subject to essentially the same recordkeeping and reporting rules applicable to other financial institutions such as banks. Unlike banks, however, nonbank money transmitters do not accept deposits.

Rather, the vast majority of transactions are retail transactions at relatively small dollar amounts—less than \$400. In fact, while it is imperative that United States financial institutions as a whole not be utilized as conduits for illicit sums, the nonbank money transmitter industry is a relatively small player in the overall volume of funds transfers conducted in the United States. Since 1994, Fedwire, used only by banks, has transferred on average more than \$800 billion *per day* while the daily dollar volume processed through CHIPS, the main U.S. wire transfer system for banks to process international wire transfers, was well over \$1 trillion. By contrast, it is estimated that in the aggregate, the nonbank funds transfer companies move significantly less than 1 percent of that amount yearly.

In short, the nonbank funds transfer industry caters to individual consumers, including recent immigrants who find that the safe, secure, services offered at reasonable prices at locations throughout the United States suit their needs. Many of these locations are in inner cities where there are no banks and funds can be transmitted to over 140 countries. The business provides a critical service for many who rely on these companies to provide basic financial services. The vast majority of funds transmitters are licensed for safety and soundness by the States, Puerto Rico, and the District of Columbia.

Since September 11, the funds transfer industry has responded to the new challenges created by the war on terrorism. Soon after these events, the industry volunteered to work with the FBI and other law enforcement agencies to provide case specific information and targeted transactional reviews as requested. In addition, the Group met with FBI headquarters representatives to intensify the dialogue on terrorist financing issues and provide information on industry procedures, systems, and operations. Compliance staffing was increased and new programs were implemented to enhance compliance training and monitoring, consistent with the letter and spirit of the USA PATRIOT Act. For example, under Section 352 of the USA PATRIOT Act, the Treasury Department was directed to promulgate anti-money laundering compliance program requirements for all financial institutions including MSB's. Treasury did a good job. The compliance program regulations embody a risk-

based approach which can be tailored by large and small businesses to suit the unique nature of those businesses. Group members enhanced existing compliance plans and disseminated revised model plans to their sales outlets. This is a major task which the industry agrees is necessary in these perilous times.

In addition, the Financial Crimes Enforcement Network (FinCEN), in a positive, proactive outreach development, has issued a variety of MSB guidance materials, written in “plain speak” and aimed at the 150,000 or more money services sales outlets. Group members use these materials to assist in educating sales outlets on their responsibilities under the law. The Group has urged FinCEN to increase MSB compliance outreach activities, perhaps with periodic regional MSB conferences since many MSB’s are small businesses.

The MSB sales outlets, often “mom-and-pop” operations such as grocery stores, convenience stores, travel agencies, etc. which sell the wire transfer services, as well as money orders and travelers checks, as an ancillary part of their business are also subject to the recordkeeping and reporting rules of the BSA. Money transmitters, such as the Group members, provide to the sales outlet—“agents,” BSA compliance training materials and procedural guidelines to ensure, to the maximum extent practicable, that the sales outlets which have the face-to-face contact with consumers, are conversant with BSA recordkeeping and reporting requirements, including but not limited to the filing of Suspicious Activity Reports (SAR). Group members evaluate sales outlets based on a risk analysis approach. Also, Group members perform “back office” transaction analyses in an attempt to spot suspicious activity and to review sales outlet compliance.

With the increased focus on terrorist financing, the Suspicious Activity Report (SAR) has become, in the view of the Group, one of the most promising tools to identify matters of interest to law enforcement. The Group has actively supported and participated in efforts such as the California regional outreach programs of the IRS Criminal Investigation Division to emphasize to money transmitter outlets the importance of reporting suspicious activities with clear and accurate SAR’s. It should be noted that FinCEN, reacting to industry comments, has been working on a short form SAR which can be more easily utilized by retail businesses. The goal, of course, is to provide to the Government timely and accurate information about suspicious activity. The industry is committed to assist in this critical effort. In turn, the Government should continue to enhance its efforts to provide guidance to the industry on types, categories and examples of “suspicious activity.”

In sum, the Group believes that the Treasury Department got it right in November 2002 when it reported to Congress pursuant to Section 359 of the USA PATRIOT Act that as to MSB’s “it would be premature at this time to call for new legislation” in the fight against money laundering and terrorist financing. As Treasury emphasized, “based on what we know so far, we appear to have the legislative and regulatory tools we need. *The primary problems are those of compliance, enforcement, education, and cooperation.* These are the correct priorities. To achieve these priorities, the following measures would be of help:

- If there is a failing in the system for MSB’s, it is the lack of uniformity in national recordkeeping and reporting standards. For example, in the rush to jump on the antiterrorism bandwagon, some State legislators and State regulatory agencies have enacted recordkeeping and reporting rules which are at odds with or different than those promulgated under the BSA—including but not limited to differing reporting thresholds and duplicate filing of SAR’s. Such measures hinder the efforts of regional and national money transmitters to achieve compliance by creating confusion and ambiguity. Multi-State MSB sales outlets such as convenience store chains and the like have an especially difficult time coping with the increasing patchwork quilt of divergent requirements. These state-specific efforts are counter productive and do not enhance the difficult task of maintaining constant vigilance. Therefore, the Group suggests that whatever the scope and character of anti-money laundering regulation under the BSA, inconsistent State mandates should be preempted.
- On a related topic, a more robust Federal compliance and enforcement program for money transmitters could be achieved by affording FinCEN the leadership role in this effort.
- Finally, there is a need to emphasize to law enforcement the need to prosecute unlicensed money transmitters under both State law and the Federal felony provision of 18 U.S.C. §1960 which was recently strengthened in the USA PATRIOT Act. However, State enforcement officials have been reluctant, in many cases, to undertake prosecution of the unlicensed under State law provisions. The only remedy then is prosecution under 18 U.S.C. §1960. As the Congress pointed out in the Money Laundering Suppression Act, an entity which knowingly ignores licensing also is likely to be ignoring the BSA requirements and could be facili-

tating terrorist financing. There is no excuse for willfully ignoring the State licensing laws.

In closing, it is worth noting that notwithstanding unsubstantiated anecdotal tales, no credible evidence has been produced which demonstrates that nonbank money transmitters are disproportionately used, or susceptible to being used, as conduits for illicit sums. Dedicated compliance with the existing BSA requirements is the best way to ensure that MSB's remain a vital component in the U.S. financial system. On the other hand, promulgation of increasingly stringent identification and other regulations will only drive transactions to the underground world of the unregulated—further frustrating enforcement goals.

Mr. Chairman and Members of the Committee, thank you again for this opportunity to comment on these issues of national importance. I look forward to responding to any questions you may have.

**RESPONSE TO WRITTEN QUESTIONS OF SENATOR SHELBY
FROM WILLIAM J. FOX**

Q.1. Increasingly, banks seeking to attract business from both the legal and illegal alien communities have done so through the provision of services historically left to companies in the wire transfer and other nonbank money services businesses. With more and more banks seeking to enter the realm of financial services that extend beyond traditional banking activities, it would be instructive to hear from the witnesses their views on whether this trend has any implications, for good or bad, on the Government's ability to regulate the kinds of financial transactions that are of issue in today's hearing.

For example, what are the implications of increased global use of ATM's for money laundering and for the movement of terrorist funds?

A.1. It is important to note that, regardless of whether financial services are provided by a depository institution or by a money services business, the requirements under the Bank Secrecy Act are the same:

- to establish a written, risk-based anti-money laundering program;
- to implement policies, procedures, and internal controls reasonably designed to ensure that the business is not subject to abuse by financial criminals and terrorists;
- to designate a compliance officer;
- to provide ongoing training and education to appropriate personnel;
- to provide for independent testing to monitor the program;
- to comply with recordkeeping and reporting requirements; and
- to file suspicious activity reports.

As a result, FinCEN fully expects both depository institutions and money services businesses to comply with all the requirements of the Bank Secrecy Act, including the program requirements, the recordkeeping and reporting requirements, and the requirements to timely file suspicious activity reports.

FinCEN understands the need to provide banking services to both resident and nonresident aliens in the United States. Providing financial services to all sectors of the population, and encouraging traditionally unbanked populations to participate in the formal financial institution system are goals that are both economically sound and achieve the Department of the Treasury's goal of enhancing the transparency of the conduct of financial services. However, FinCEN also understands that conducting financial transactions can, depending on the nature of the customer and the services provided, involve varying degrees of risk. FinCEN expects both depository institutions and money services businesses to assess the risks involved in any such relationships, and to take steps to ensure both that such risks are appropriately managed and that the institution can do so in full compliance with its obligations under the Bank Secrecy Act and the regulations promulgated there under. As in any case where higher risks are presented, both depository institutions and money services businesses should expect an increased level of review by examiners to ensure that the insti-

tution has in place controls and compliance oversight systems adequate to monitor and manage such risks, as well as personnel trained in the management of such risks and in the requirements of applicable laws and regulations.

As new financial service providers and new financial products, services, and instruments emerge and develop, FinCEN will continue to evaluate their vulnerabilities toward terrorist financing and money laundering and respond with appropriate guidance and, where appropriate, regulations to refine definitions, expand Bank Secrecy Act requirements to additional financial services or service providers, or alter existing requirements or thresholds to accommodate the risk. The example cited in your question, specifically the use of automated teller machines, as well as other products and services are being analyzed and reviewed by FinCEN for these very reasons.

Our research concerning the use of automated teller machines and other product services indicates a number of common scenarios have been identified including:

- Use of multiple accounts at a single financial institution to deposit bulk case via automated teller machine transactions domestically followed by cash withdrawal of funds in foreign countries.
- Multiple cash deposits and/or withdrawals on the same day at different or single automated teller machine locations followed by withdrawals using a combination of same day counter and automated teller activity.
- Wire transfers into domestic accounts followed by withdrawals in a foreign location via automated teller machines or checks.
- Passing insufficiently funded checks through an automated teller machine to provide a greater degree of anonymity.
- Deposit of fraudulent or worthless¹ checks followed by depletion of the account balance using checks, point of sale debits or cash withdrawals at automated teller machines before the checks were returned an unpaid.

Anyone of these scenarios could be employed by money launderers or terrorist financiers.

Q.2. Mr. Fox, I understand that casinos, which exist to facilitate the expeditious transfer of large amounts of cash while providing a modicum of confidentiality for their customers, present a somewhat unique challenge. And I appreciate that this challenge has grown by exponential proportions just over the last 10 years. The appearance in more and more States of legalized gambling, especially on tribal lands, has created a problem that FinCEN in particular must find difficult to grasp. Your prepared statement summarized the scale of the challenge confronting your organization very well.

As you noted in your statement, casinos have fallen under the anti-money laundering statues for 10 years, longer if you consider the casinos' obligation to file currency transaction reports under the Bank Secrecy Act. I am troubled, however, by the Government's

¹“Worthless” is a term used in the suspicious activity report narratives to describe, among other things, checks that are drawn on insufficient funds or closed accounts; stolen, forged, or counterfeit checks (identity theft); or checks on which payment has been stopped.

record of oversight with respect to the gambling industry. For example, your statement notes that casinos were more formally incorporated into the anti-money laundering statutory regime with passage of the Money Laundering Suppression Act of 1994. Yet, as your statement indicates, FinCEN did not adopt rules requiring casinos to file suspicious activity reports until 2002.

Q.2.a. If casinos were made legally subject to anti-money laundering statutes 10 years ago, why a delay of almost a decade before the requisite rules were adopted requiring the filing of SAR's?

A.2.a. As I indicated in my written testimony, casinos were actually designated as financial institutions by the Department of the Treasury for purposes of the Bank Secrecy Act in 1985, 9 years before Congress amended the Bank Secrecy Act to include casinos explicitly. Casinos were also, by regulations adopted in 1994,² the first nonbank financial institution required to develop an anti-money laundering program. The Department of the Treasury adopted Bank Secrecy Act regulations for casinos because it determined that:

- Casinos, as high cash volume businesses, are vulnerable to manipulation by money launderers, tax evaders, and other financial criminals; and,
- In addition to gaming, casinos offer their customers a broad array of financial services, such as deposit or credit accounts, funds transfers, check cashing, and currency exchange services, that are similar to those offered by other financial institutions and other financial firms.

In 1994, Congress amended the Bank Secrecy Act to add casinos and other gaming establishments to the list of financial institutions specified in the Bank Secrecy Act, and FinCEN began the rule-making process to require casinos to file suspicious activity reports. However, a notice of proposed rulemaking was not published until 1998, and I do not know the reason for the delay. In my view, certainly judged by today's standards, the suspicious activity reporting requirement for casinos should have closely accompanied the implementation of suspicious activity reporting for banks in 1996.

Subsequent to issuing the notice of proposed rulemaking in 1998, FinCEN held four public meetings to provide interested parties with the opportunity to present their views, as well as to provide FinCEN with additional information and feedback.³ Because of controversy surrounding certain provisions of the proposed rule, FinCEN issued a Request for Additional Comments in 2002, see 67 Fed. Reg. 15138 (March 29, 2002), and a final rule several months later, see 67 Fed. Reg. 60722 (Sept. 26, 2002).

FinCEN did encourage casinos voluntarily to file suspicious activity reports well before the final rule became effective in March 2003, and in 1998 issued guidance on suspicious activity reporting for casinos. Between October 1997 and March 2003, casinos filed over 5,000 suspicious activity reports.

²See 59 FR 61660 (Dec. 1, 1994) (mandatory compliance required by June 1, 1995).

³Meetings were held in New Orleans, Louisiana, Chicago, Illinois, Scottsdale, Arizona, and New York City.

Q.2.b. As it has been well over a year now since the SAR requirement took effect, how would you rate implementation by the casinos of this requirement? How many SAR's have been filed since the rule took effect?

A.2.b. FinCEN believes that the casino industry, taken as a whole, has implemented and responded positively to the suspicious activity reporting requirement. As with other suspicious activity reports, these forms have been used by law enforcement to identify and trace the flow of illicit proceeds.

Since the implementation of the rule in 2003, 308 casinos and card clubs filed 5,415 casino suspicious activity reporting forms. The total dollar value of casino suspicious activity reported on these forms was \$300,797,862 in 2003.

FinCEN's latest *SAR Activity Review: By the Numbers* publication (Issue 2, May 2004) includes the following statistics relating to suspicious activity reports filed by casinos for the period August 1, 1996 through December 31, 2003:

Number of SAR-C Filings by Characterization of Suspicious Activity in Descending Order

For the Period August 1, 1996 through December 31, 2003

Rank	Violation	Filings (Overall)	Percentage (Overall)
1	Structuring	4,020	33.39%
2	Other	3,201	26.59%
3	Minimal Gaming with Large Transactions	1,838	15.27%
4	No Apparent Business or Lawful Purpose	612	5.08%
5	Money Laundering	552	4.59%
6	Large Currency Exchange(s)	444	3.69%
7	Unknown/Blank	330	2.74%
8	False or Conflicting (IDs)	246	2.04%
9	Unusual Use of Counter Checks or Markers	221	1.84%
10	Check Fraud (includes Counterfeit)	173	1.44%
11	Unusual Use of Negotiable Instruments (Checks)	112	less than 1%
12	Unusual Use of Wire Transfers	90	less than 1%
13	Credit/Debit Card Fraud (Includes Counterfeit)	77	less than 1%
14	Embezzlement/Theft	41	less than 1%
15	Bribery/Gratuity	27	less than 1%
16	Misuse of Position	26	less than 1%
17	Use of Multiple Credit or Deposit Accounts	16	less than 1%
18	Terrorist Financing	12	less than 1%

Number of SAR-C Filings by Characterization of Suspicious Activity*

For the Period August 1, 1996 through December 31, 2003

Violation	1996	1997	1998	1999	2000	2001	2002	2003
Bribery/Gratuity	-	1	5	5	1	4	1	10
Check Fraud (Includes Counterfeit)	-	-	9	7	9	18	18	112
Credit/Debit Card Fraud (Includes Counterfeit)	-	-	1	9	3	9	2	53
Embezzlement/Theft	-	-	1	3	1	10	3	23
False or Conflicting (IDs)	-	-	-	-	-	-	-	246
Large Currency Exchange(s)	-	-	18	26	28	56	45	271
Minimal Gaming with Large Transactions	-	-	85	71	89	333	436	824
Misuse of Position	-	-	1	3	-	8	7	7
Money Laundering	-	19	89	29	36	83	79	217
No Apparent Business or Lawful Purpose	-	3	17	11	19	61	158	343
Other**	77	9	152	150	158	428	714	1,513
Structuring	-	14	165	165	186	558	636	2,296
Terrorist Financing	-	-	-	-	-	-	-	12
Unknown/Blank	8	2	86	55	28	63	35	53
Unusual Use of Counter Checks or Markers**	-	-	-	-	-	-	-	221
Unusual Use of Negotiable Instruments (Checks)	-	-	3	5	-	18	7	79
Unusual Use of Wire Transfers	-	-	3	9	4	9	11	54
Use of Multiple Credit or Deposit Accounts	-	-	1	-	1	3	7	4

* Some SAR-Cs may list multiple violations.

**Issue 1 of By the Numbers incorrectly reported the data for the period, 01/01/03 to 06/30/03, for these categories due to technical issues. (The numerical data was attributed to the wrong categories.)

In the first 6 months of 2004, 249 casinos and card clubs have filed 2,634 casino suspicious activity report forms. The total dollar value of casino suspicious activity reported on these reports was \$347,531,007 in 2004. While the number of casino suspicious activity reports filed stayed roughly in proportion to the number filed in 2003, the total dollar amount reported so far in 2004 exceeds the amount reported for all of 2003. This indicates a significant increase in amount of funds being reported on casino suspicious activity reporting forms. Over 23 percent of the casino suspicious activity reporting forms filed were for dollar amounts less than \$5,000.

While the above statistics are encouraging, FinCEN has detected a decrease in the number of casinos that are filing casino suspicious activity reporting forms that may not be fully explained by consolidation and vigilance on the part of the industry. Further, less than 50 percent of the approximately 800 casinos and card clubs operating in at least 30 jurisdictions in the United States and its territories subject to the Bank Secrecy Act are filing casino suspicious activity reporting forms, not all of which can be explained by wagering limitations or other exigencies related to State law or the nature of the establishments involved. FinCEN will continue to monitor the aforementioned anomalies and respond with measures

as appropriate, including outreach, guidance, education, and compliance examinations.

Q.2.c. What constitutes “suspicious activity” in a gambling house?

A.2.c. A casino must file a casino suspicious activity report when a transaction is both suspicious and involves \$5,000 or more (in a single event or when aggregated). The casino suspicious activity reporting rule provides that suspicious activity relates to a transaction or pattern of transactions that the casino knows, suspects, or has reason to suspect:

- involves funds derived from illegal activity or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity as part of a plan to violate or evade any Federal law or to avoid a Federal reporting requirement;
- is designed, whether through structure or other means, to evade any requirement under the Bank Secrecy Act;
- has no business or apparent lawful purpose or is not the transaction in which the particular customer would normally engage, and the casino has no reasonable explanation for the transaction after examining the available facts;
- or, involves use of the casino to facilitate criminal activity.

31 CFR 103.21(2)

It is fundamental to our regulatory approach that effective implementation of the Bank Secrecy Act must be predicated upon a financial institution’s careful assessment of its vulnerabilities to money laundering and other financial crime and building an anti-money laundering program that makes sense for that institution and its customers. We believe no one is better positioned to evaluate its business processes, including distribution channels and customer base, than the financial institution itself. The same is true for identifying transactions or activity that should be considered suspicious for purposes of any financial institution. The institution is in the very best position to determine what constitutes normal activity both generally and with respect to specific customers.

Structuring is by far the most reported characterization of suspicious activity by casinos. The following examples are illustrative of activities identified by casinos as suspicious on casinos suspicious activity reports.

- A customer furnishes an identification document that the casino believes is false or altered (for example, address changed, photograph substituted, etc.) in connection with the completion of a currency transaction report by the casino or the opening of a deposit, credit, or check cashing account by the customer.
- A customer seeks to cash out chips or tokens in excess of \$10,000, but when asked for identification reduces the amount of chips or tokens to be cashed out to less than \$10,000.
- A customer, who is a big winner, enlists another person, to cash out a portion of the chips or tokens won to avoid the filing of Bank Secrecy Act or tax forms.
- A customer exchanges large amounts small denomination bills for large denomination bills, which are easier to hide or transport.

- A customer makes large deposits or pays off large markers with multiple instruments (for example, cashier's checks, money orders, traveler's checks, or foreign drafts) in amounts of less than \$3,000 that appear to have been purchased in *structured* manner or issued by several different financial institutions.
- A customer requests the issuance of casino checks, each less than \$3,000, which are made out to third parties or checks without a specified payee.
- A customer purchases a large amount of chips with currency at a table, engages in minimal gaming, and then redeems the chips for a casino check.
- Two or more customers purchase chips with currency in amounts between \$3,000 and \$10,000, engage in minimal gaming, combine the chips and redeems them for a casino check.
- A customer makes a large deposit using small denomination bills, engages in minimal gaming and then withdraws the funds in large denomination bills, a casino check or a money transfer.
- A customer inserts currency in a bill validator on a slot machine or video lottery terminal, accumulates credits with minimal or no gaming activity, and then cashes out the tokens for large denomination bills or a casino check.
- A customer withdraws a large amount of funds (for example, \$30,000 or more) from a deposit account and requests that multiple casino checks be issued each of which is less than \$10,000.
- A customer, using a deposit or credit account, sends or receives money transfers to or from a high-risk country, wires funds derived from nongaming proceeds, to or through a bank and/or a nonbank financial institution(s) located in a country that is not his/her residence or place of business, or sends or receives frequent or large volumes of money transfers to or from persons located in foreign countries, especially high-risk countries.
- A customer requests a money transfer to a charity that is unfamiliar to a casino or located in a high-risk country.
- A first-time customer sends a large money transfer to a casino from a domestic bank. After engaging in minimal gaming, he goes to the cage and requests that the proceeds be transferred to a joint account in a high-risk country.
- A customer transfers funds to a casino for deposit into a front money/safekeeping account and after engaging in minimal or no gaming activity withdraws the funds in the form of a casino check.
- A customer offers a bribe in form of a tip or gratuity to a casino employee, or requests that a casino employee structure currency transactions to evade Bank Secrecy Act filing requirements.
- A customer asks for jewelry, airplane ticket vouchers, vacation vouchers, or other noncash gifts (that are easily converted to currency) to be provided as "comps" to a friend or unknown party.

We believe that we have an obligation to find ways to provide information to the regulated industries that is relevant to assessing the risks facing the financial system. This includes providing information about trends and patterns we are finding. FinCEN has provided guidance to assist the casino industry in identifying transactions that may be considered "suspicious" for purposes of the rule in a variety of forms, including through its biennial publication, the

SAR Activity Review. In December 2003, FinCEN issued “Suspicious Activity Reporting Guidance for Casinos,” a copy of which is attached for your reference.* These and other materials are available on FinCEN’s website at *www.fincen.gov*. We will continue to provide appropriate guidance to the industry to achieve the purposes of the Bank Secrecy Act.

**RESPONSE TO A WRITTEN QUESTION OF SENATOR SARBANES
FROM KEVIN BROWN**

Q.1. What percent of the casinos have not been examined at all?

A.1. Of the 564 casinos (excluding card clubs) currently in our database, 428 (75 percent) have not been examined. With the establishment of the new Office of Fraud/Bank Secrecy Act in the IRS’ Small Business/Self-Employed Division, we will be reviewing the criteria for selecting casinos for examination to ensure that our coverage of these entities is sufficient. In addition to our examination program, we conduct an educational program for casinos to make them aware of their responsibilities under the Bank Secrecy Act. In the past 4 years, we have made individual visits to 72 casinos and presented 111 seminars, which reached over 5,000 individuals in the casino industry.

**RESPONSE TO A WRITTEN QUESTION OF SENATOR CARPER
FROM KEVIN BROWN**

Q.1. What is going on that we are trying to prevent? Give me some examples of what is going on that we are trying to prevent in the casino or gaming industry.

A.1. As Government and industry programs have made it more difficult for customers to launder money at banks and other depository institutions, the interest of money launderers in moving funds into the financial system through nonbank financial services providers has increased. Gaming establishments have not been spared from this trend. The experience of law enforcement and regulatory officials suggests that the gambling environment can attract criminal elements involved in a variety of illicit activities, including fraud, narcotics trafficking, money laundering, and terrorist financing. With large volumes of currency being wagered by legitimate gaming customers from throughout the United States (and, indeed, from around the world), the fast-paced environment of casino gaming can create an especially valuable “cover” for money launderers. The explosive growth of casino gaming in the United States vastly increases the “targets of opportunity” for such criminals, as casino sites, amounts wagered, and casino attendance have multiplied.

Some examples of how casinos have been used include:

- individuals laundering drug proceeds by buying and cashing casino tokens;
- individuals using organized crime proceeds to open a casino on tribal lands; and,
- individuals structuring transactions to avoid reporting by cashing \$20,000, in increments of \$1,000, in casino chips.

* Held in Committee files.

**RESPONSE TO WRITTEN QUESTIONS OF SENATOR SHELBY
FROM EZRA C. LEVINE**

Q.1. Given your impressive experience in this area, could you provide the Committee your view of how you see the division of labor between respective Federal agencies and expand on your statement with regard to FinCEN? From your perspective, what roles do the various Federal departments and agencies play in regulating money services businesses? What capabilities would you recommend for FinCEN that it currently lacks that would make it more effective in overseeing compliance and enforcement?

A.1. As you indicated, I suggested in my opening statement, that FinCEN should be the lead agency for ensuring a more robust Federal compliance and enforcement program for money transmitters. The reason for this view is twofold. First, FinCEN, as the primary agency responsible for the promulgation and interpretation of the Bank Secrecy Act (BSA) recordkeeping and reporting rules, is best able to provide authoritative, uniform guidance on the application of those rules to money services businesses (MSB's). Second, the IRS has been buffeted by criticism from Congress over the years largely relating to tax enforcement issues and has been subject to budget restrictions and personnel limitations. Not surprisingly, therefore, it would appear, based on empirical evidence, that the principal focus of the IRS is with regard to improving its performance in the area of tax-related issues—not BSA compliance. Over the many years that MSB's (or "nonbank financial institutions" as they were previously known) have been subject to the BSA rules, the IRS civil examination staff has not received intensive training or the resources to conduct essential outreach and/or enforcement activities with respect to MSB's. The problem has been exacerbated by frequent personnel turnovers. The unfortunate consequence of this vacuum is that many State regulators have decided to fill the gap by attempting to enforce the BSA notwithstanding inadequate training, resources and lack of uniformity in the interpretation of the regulations at the State level.

Therefore, with these considerations in mind, it would appear that FinCEN, as the lead MSB regulator (unlike banks, MSB's do not have a Federal "bank" regulator such as the Fed, the OCC, the FDIC, etc.), is in the best position to exercise the leadership role in the regulation of MSB's for compliance with the BSA. Particularly under the revitalization of FinCEN by Director Fox, FinCEN could be empowered with the direct supervisory role over the enforcement efforts directed at MSB's. FinCEN could be given additional staff for this enforcement effort or, at the least, FinCEN should oversee, on a direct basis, the enforcement efforts conducted by the IRS. There is precedent for such an arrangement. During Phases I–IV of the Economic Stabilization Program (price controls) in the early 1970's, followed in 1974 by the Emergency Petroleum Price and Allocation Regulations administered by the Federal Energy Office (FEO) during the Arab oil embargo, the IRS under delegated authority from the Cost of Living Counsel (CLC) and the Federal Energy Office enforced the price regulations of those two national programs. Those agencies were able, to a greater degree, to monitor the quality of the enforcement efforts to ensure consistency, fairness, and effective targeting. While perhaps not ideal, a

similar arrangement could be employed to afford FinCEN a more direct role in the day-to-day supervision of the IRS BSA civil enforcement effort with regard to MSB's. It should be noted that the IRS-CID, on the criminal side, is very effective and in California, for example, has conducted extensive MSB outreach for a number of years.

Q.2. Do you believe States should be vested with primary authority for enforcing Federal anti-money laundering statutes? Can you expand on what FinCEN should do to improve or increase its level of interaction with State and local governments with regard to BSA compliance? Have the Federal regulatory agencies been responsive to State concerns?

A.2. I noted in my testimony on September 28 that, "if there is a failing in the system for MSB's, it is the lack of uniformity in national recordkeeping and reporting requirements" at the State level. You sought my comment on whether the States should be vested with the authority for enforcing Federal anti-money laundering statutes. My answer is an unequivocal *no*. The BSA program is a national program which is focused on transactions and activities which are largely interstate and international in nature. The BSA rules have been designed to deal with these financed transactions. Regulated entities attempting in good faith to comply with the rules need predictability and uniformity in order to achieve, through training and monitoring, a uniform national compliance program. The consequences of unpredictable State-by-State interpretation of the BSA Federal program are likely to be contradictory and confusing mandates which undercut compliance efforts. As one panelist pointed out in testimony before the Committee on September 28, 2004, the same conduct that triggered enforcement action in New York had been blessed by another State and the IRS. This is but one highly visible example. Since States possess the regulatory power to fine, suspend or revoke licenses of money transmitters in their states, the local purported BSA enforcement efforts, however well meaning, are fraught with peril.

Currently, in the absence of a Federal preemption provision in the BSA, States are free to enact laws and promulgate regulations which digress from national BSA recordkeeping and reporting requirements set forth in Title 31 of the CFR. The State statutory and regulatory initiatives have accelerated since September 11 as States do not want to appear to be lagging in the war against terrorism. For example, some States require reporting or recordkeeping at different thresholds. Other States require the recordation of different information than that specified under the BSA rules. At least 5 States now require or are contemplating requiring the useless duplicate filing of CTR's and SAR's by MSB's, notwithstanding that all States participate in FinCEN's BSA Direct program which permits real-time electronic access to all filed SAR's and CTR's. In short, these inconsistencies and duplications create confusion, extra cost, and lack of predictability for MSB's. They hamper nationwide training efforts and undercut effective nationwide BSA compliance by MSB's.

Moreover, the majority of State examiners are not adequately trained in BSA requirements. They often apply their own interpre-

tation of the rules. Since there is no coordination within the States with regard to BSA enforcement, it is axiomatic that there is no uniformity. In fact, the vast majority of State regulators do not examine MSB's. Likewise, the States have not taken the initiative in BSA outreach, training, or providing guidance of any sort to MSB's with regard to BSA requirements. The situation is particularly egregious because attempts by some States to enforce the BSA diverts resources from essential primary State programs. That is, most States, do not enforce the money transmission laws with regard to unlicensed entities. As technological innovation occurs, new money transmission methods are developed and more entities enter the business—yet State efforts to aggressively enforce the licensing laws of these new and/or nontraditional money transmission vehicles is deficient. That failure spurred the passage by Congress of 18 U.S.C. § 1960 some years ago and the further strengthening of that provision in the USA PATRIOT Act.

The emphasis of the State regulators should be on enforcing State laws and penalizing those entities which ignore licensing mandates. Federal programs such as the BSA should be enforced by the Federal Government. If the States are unable to cobble together the resources necessary to ensure that all money transmitters are licensed, it is abundantly clear that diversion of resources to perform BSA examination *of only the licensed entities in the State* makes little sense and is largely counterproductive.

FinCEN, under Director Fox, has made a major shift in focus by increasing the Agency's interaction with State agencies. Just last month, Director Fox was the first FinCEN Director in the 11-year history of the Money Transmitters Regulators Association to accept an invitation to speak at that organization's annual meeting. Director Fox has committed FinCEN to a proactive program of providing support and responsiveness to State and local governments about all aspects of the BSA. Moreover, FinCEN can be of assistance to State and local agencies that have information about potential money laundering and terrorist financing activities. In addition, Director Fox is committed to enhancing the technological capabilities of BSA Direct so that State agencies can better access and utilize the data contained in SAR's and CTR's filed by MSB's. In short, the focus of FinCEN's interaction with States should be in assisting the States with information and guidance to prosecute those charged with money laundering, terrorist financing, and related crimes which threaten the security of the United States. FinCEN, not the States, should be responsible for nationwide BSA enforcement.

I will be pleased to provide to you and the Committee such further information as may be required.



AMERICAN GAMING ASSOCIATION

FRANK J. FAHRENKOPF, JR.
President & CEO

October 20, 2004

The Honorable Richard Shelby
Chairman, Senate Committee on Banking, Housing and Urban Affairs
United States Senate
110 Hart Senate Office Building
Washington, DC 20510

Dear Dick:

I write to respond to certain questions you posed to me during the September 28, 2004 hearing of the Senate Committee on Banking, Housing and Urban Affairs, concerning Bank Secrecy Act enforcement for certain non-bank financial institutions, such as casinos. You asked for information concerning the level of reporting by the casino industry of both (i) Currency Transaction Reports for Casinos (CTRCs) and (ii) Suspicious Activity Reports for Casinos. The following statistics have been acquired from the Financial Crimes Enforcement Network at the Department of the Treasury:

CTRCs

2000 - 373,723
2001 - 385,555
2002 - 408,137
2003 - 472,400
2004 - 337,740 (through Aug. 31)

SARCs

2000 -- 464 (only Nevada had mandatory SARC reporting)
2001 -- 1,377 (New Jersey made SARC reporting mandatory)
2002 -- 1,827
2003 -- 5,095 (federal SARC rule became mandatory)

I hope this responds to your inquiry. Please contact me if we can provide any additional information.

Kindest personal regards,

Frank J. Fahrenkopf Jr.