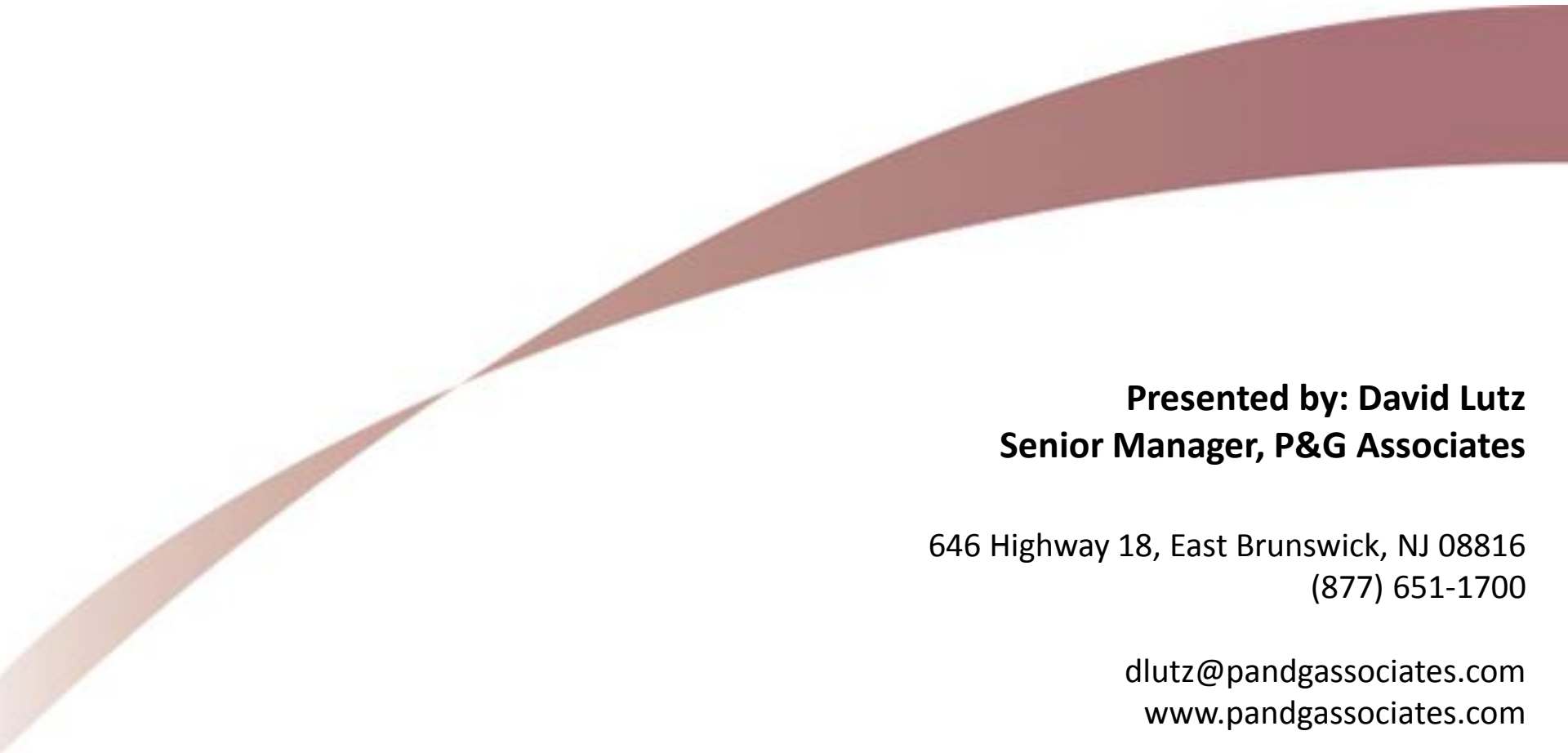


BSA/AML Updates

Key Trends in BSA/AML compliance



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Agenda

- SAR and Money Laundering Statistics
- Heightened Regulatory Expectations
- Key Areas of Examination Focus
- Common MRA's and Cited Deficiencies
- Beneficial Ownership
- BSA System Validation vs. Calibration

Money Laundering Vulnerabilities

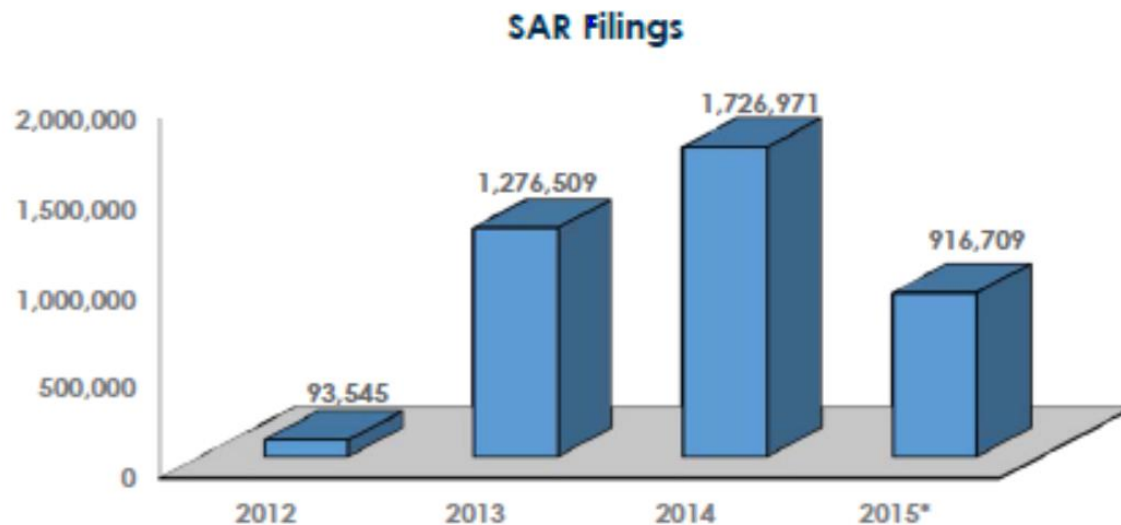
According to the 2015 National Money Laundering and Terrorist Financing Risk Assessment, top vulnerabilities include the following:

- Cash and Cash Structuring
- Disguise the identity of the individuals who control the accounts;
- Creating legal entities without accurate information about the identity of the beneficial owner;
- Misuse of products and services
- Financial institutions wittingly facilitating illicit activity.



SAR Statistics

The overall 3,097,025 SARs analyzed for this report are organized and presented by industry. Illustrated below is the total volume of filings since 1 March 2012 through 30 June 2015. Overall, SAR filings have been increasing steadily since 2012



* Represents filings through June 30, 2015

SAR Statistics at a Glance

Depository Institutions				
Suspicious Activity Category	Trending Now	2014	2012-2013 ¹⁵	Change ¹⁶
FRAUD	Tax Fraud	6,148	6,638	↓ -7%
	Prepaid Card Fraud	2,705	3,999	↓ -32%
	Deposit Fraud	2,435	2,188	↑ 11%
	Counterfeit Check	2,069	3,041	↓ -32%
	Kiting (Unspecified)	1,704	1,705	Unch
	Check Kiting	1,554	1,536	↑ 1%
	Emerging Online Banking	1,460	1,355	↑ 8%
	Credit Card Kiting	1,128	919	↑ 23%
	Emerging Due Diligence	1,064	643	↑ 65%
IDENTIFICATION DOCUMENTATION	Social Security Number Fraud ¹⁷	48,851	21,399	↑ 128%
	Insufficient Documentation Provided	1,010	869	↑ 16%
MONEY LAUNDERING	Emerging Funnel Account Activity	9,999	123	↑ 8,000%
	Suspicion Concerning Use of Funds	4,370	2,077	↑ 110%
	Suspicious/Rapid Movement of Funds	2,208	1,489	↑ 48%
	Emerging Cash Between Two Parties Multiple Locations ¹⁸	1,906	0	↑ NA
	Excessive Cash/Cash Activity	1,534	1,979	↓ -22%
	Tax Fraud	1,040	802	↑ 30%
Mortgage Fraud	Origination Fraud (Unspecified)	7,554	18,913	↓ -60%
	Emerging Application Misrepresentation	2,118	2,681	↓ -21%
	Emerging Occupancy Misrepresentation/Fraud	1,688	1,876	↓ -10%
	False Identity Theft Claim	1,587	84	↑ 1,800%
	Loan Origination Fraud	1,532	2,040	↓ -25%
	Short Sale Fraud/Collusion	1,176	1,787	↓ -34%
OTHER SUSPICIOUS ACTIVITIES	Income Discrepancy	20,352	7,021	↑ 190%
	Identity Fraud	9,755	2,229	↑ 338%
	Tax Fraud	6,841	6,663	↑ 3%
	Employment Discrepancy	2,577	1,017	↑ 153%
	Fraud Ring	2,376	3,066	↓ -22%
	Emerging False Statement	1,850	835	↑ 122%
	Check Kiting	1,794	2,267	↓ -21%
	Emerging Bust Out Scheme	1,074	936	↑ 15%
	Kiting (Unspecified)	1,028	1,202	↓ -14%
	Emerging Suspicious Financial Activity	968	517	↑ 88%
	Excessive Cash Payments	964	1,575	↓ -39%
	Rapid Utilization/Movement of Funds	890	1,434	↓ -38%
STRUCTURING	Single Transaction Below CTR Threshold	1,047	656	↑ 60%
	Emerging Excessive Cash Payments	603	1,638	↓ -63%
	Circumventing Chinese Currency Regulations ¹⁹	567	267	↑ 112%

Rising Regulatory Expectations

- *“The Federal Reserve places great importance on ensuring that the institutions we supervise comply with the BSA and U.S. economic sanctions. When we find problems at a supervised institution, we demand specific corrective measures, by specific dates, and we take strong enforcement actions when necessary” - Governor Jerome H. Powell*
- *“Without a commitment from the highest levels of bank management to maintain strong programs, ensure a culture of compliance, and support the BSA/AML officers...its more than likely that BSA/AML programs will not be effective and will result in an enforcement action.” – Thomas J. Curry, Comptroller of the Currency*



Feedback from Regulators

“The overwhelming majority of banks in the New York Region are doing a good job overseeing BSA/AML compliance; however, there have been some institutions with high profile BSA/AML deficiencies that have triggered recent civil and criminal enforcement actions. ” – John Conneely, Deputy Regional Director FDIC

Here are some statistics taken from the March 3, 2015 FDIC New York Region Regulatory Teleconference:

- As of year end 2014, only 9 out of 500 state non-member banks are under BSA related consent orders (less than 2%)
- Out of 4,100 state non-member banks nationwide, only 43 are under BSA related consent orders (less than 1%)

What's driving heightened regulatory expectations?

- Fallout from financial crisis
- Emergence of complex products, services, and markets
- Misuse of transaction monitoring systems
- Insufficient resources allocated to risk management and BSA/AML compliance

Key Areas of Examinations

- Customer Due Diligence/Enhanced Due Diligence
- Suspicious Activity Monitoring
- Transaction Monitoring
- Department Resources
- Independent Testing



Common Internal Control and Related Weaknesses

- The BSA program has not kept pace with the bank's growth and risk profile
- The bank's leadership is not fully engaged
- Retaining qualified BSA Officers and support staff
- Insufficient resources/training dedicated to BSA compliance
- Inadequate customer due diligence (CDD) and enhanced due diligence (EDD)
- Failure to identify, monitor, and/or report suspicious activity
- Inadequate independent BSA/AML audit scope



Common MRA's and Cited Deficiencies

- Insufficient Staff
- Independent Testing Inadequate
- Transaction monitoring system not properly calibrated
- Transaction monitoring alerts capped to accommodate staffing
- Inadequate assessment of BSA/AML and OFAC risks



Emerging Trends

- Increased Focus on MSBs, Including Cryptocurrency Companies
- Innovative Payment Technologies Present a Challenge
- Oversight of Third Party Vendors
- Cybersecurity
- Focus on Individual Accountability



Money Service Businesses

The allure of the Money Service Business (MSB)

- Increasing risk complexity is putting many MSB accounts “on the street” for banks to service
 - MSB are generally viewed as very high risk customers
 - Concept of de-risking
- MSBs are used to paying service fees in excess of several thousand dollars per month
 - Non-interest fee income becomes attractive to many Banks
- Money isn’t everything
 - Fee income still doesn’t offset actual BSA risk

PrePaid Access Programs

- The growth of prepaid access as a financial tool continues to flourish.
- Money laundering, terrorist financing, and other criminal activity may occur through prepaid access and prepaid card programs if effective controls are not in place.



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- A close-up photograph of a person's hands holding a blue credit card. The card is held between the thumb and index finger of the right hand, with the left hand supporting it from underneath. The card is blue with a silver chip and embossed text. The background is blurred, showing a person in a blue shirt.

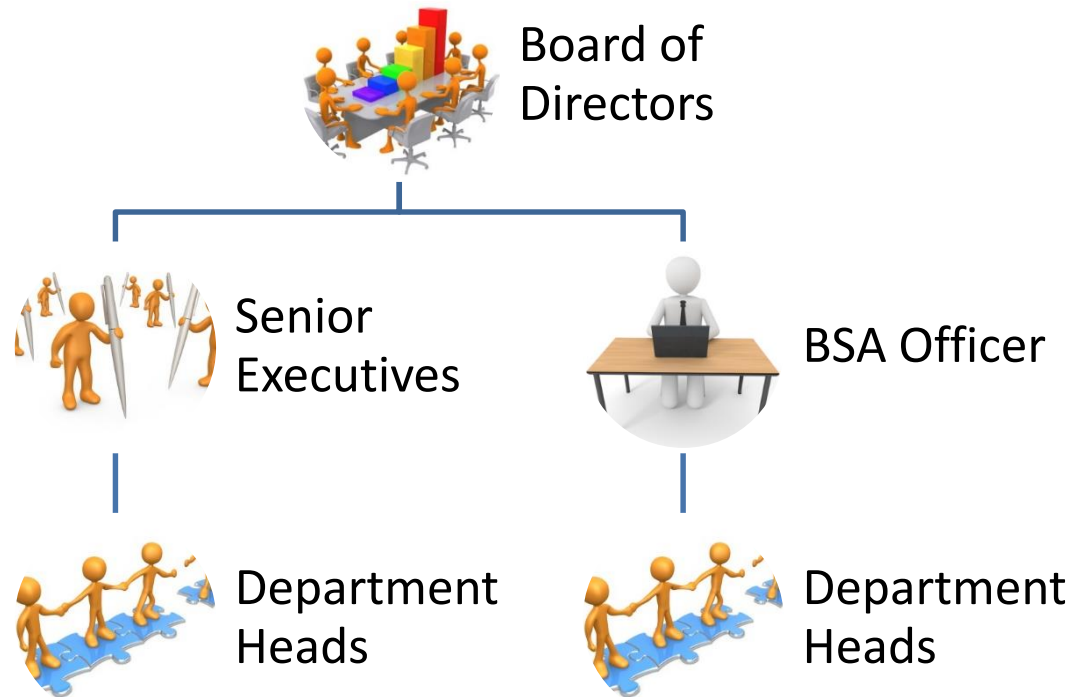
BSA Governance, Administration and Staffing



- A matter of roles and responsibility
 - BSA Officer
 - Day to day administration of the program unfettered from “corporate” politics and hierarchy
 - Senior Executives
 - Promoting a culture of compliance which allows the BSA officer to administer the program without road blocks
 - Board of Directors
 - General oversight to ensure that Senior Executives and the BSA Officer are working in coordination to promote the goals of the Bank’s BSA program, including the allocation of appropriate resources



BSA Governance, Administration and Staffing



Importance of Due Diligence

- Customer Due Diligence/Enhance Due Diligence
 - Help the Bank know the customer and their unique risks
 - Makes identifying suspicious activity more effective
- Beneficial Ownership
 - Final rules coming soon
 - 25% natural owner must be identified
 - Goal is to prevent someone creating layers upon layers of corporate structure to make perpetrating financial crimes easier

Beneficial Ownership on the Rise

- Beneficial Ownership is one example where FinCEN is addressing customer risk
 - “Heightened risks can arise with respect to beneficial owners of accounts because nominal account holders can enable individuals and business entities to conceal the identity of the true owner of assets or property derived from or associated with criminal activity.”
 - FIN-2010-G001

Beneficial Ownership

- Beneficial Owner defined:
 - A natural person
 - Directly or indirectly owning 25% or more equity interests (Ownership prong)
 - Directly or indirectly means... owners of other legal entities
 - With significant responsibility to control, manage or direct a legal entity (Control prong)

Beneficial Ownership

- Identification Methods
 - Two Prong Concept:
 - Ownership Prong – Each individual, up to four, who owns, directly or indirectly, 25 percent or more of the equity interest in the legal entity customer
 - Control Prong – At least one individual who exercises significant managerial control over the legal entity (e.g. C-level executive)

AML Monitoring Systems



AML Monitoring Systems

- Powerful and sophisticated tools in the fight against financial crime
 - Do more to detect financial crime
 - See more evidence of financial crime
- Sophistication requires an understanding of the monitoring system
 - How it works
 - Why it works
 - What the results mean

Common AML System Issues

The grass isn't always greener as they say. These are some common issues Bank's are having with AML systems:

- Incomplete/inaccurate customer or transactional data
- Data mapping errors/irregularities
- Design of rules and/or configurations inconsistent with regulatory expectations and the Bank's exposure to related risks
- Abundantly high volume of alerts due too many alert types, incorrect parameter settings
- Lack of change management and/or adaptation to changes in products/services
- Underutilization of feature functionality

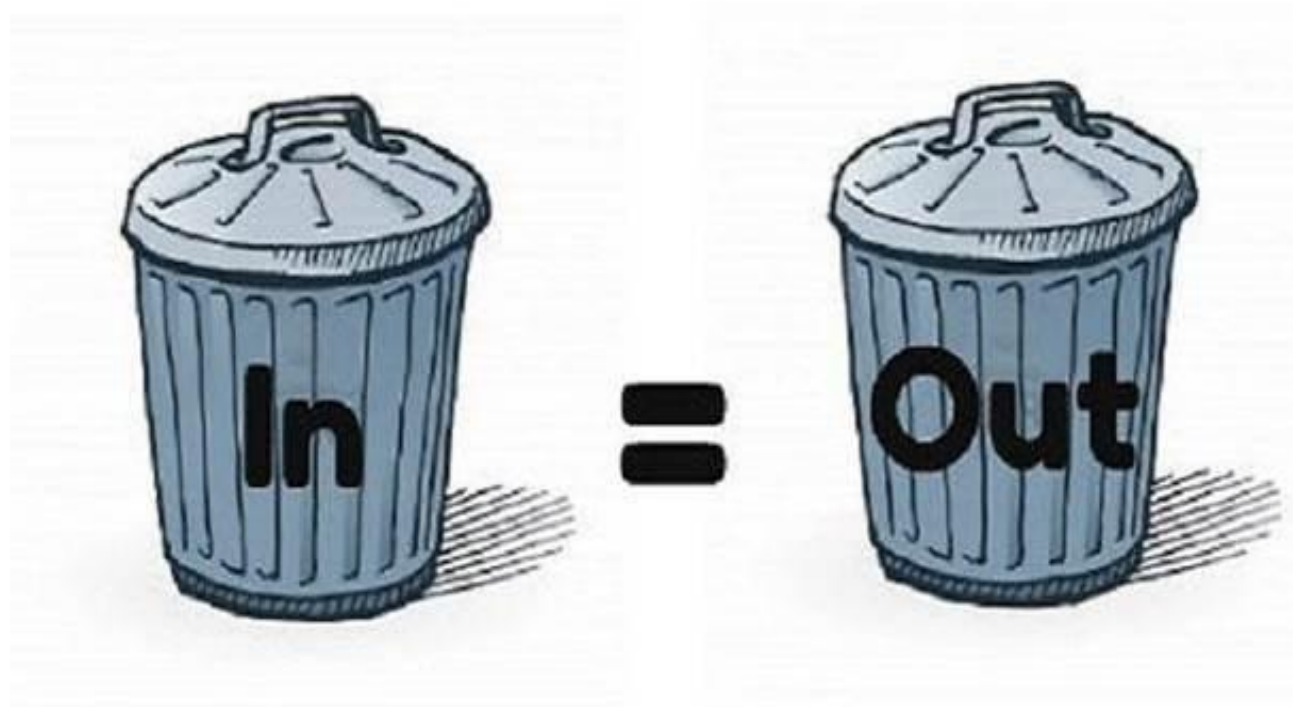
Recent Focal Point of Examination

“Transaction monitoring works by running transactions through various detection scenarios that are designed to create alerts that show patterns of money laundering or red flags, such as high-volume transaction activities. But – and this is a truly frightening question to ask – what if those monitoring and filtering systems are flawed or ineffective?” – Benjamin Lawsky, Superintendent of Financial Services

- Increased examiner focus on AML models when assessing soundness of BSA/AML program
- Emphasis on implementation and design of transaction monitoring systems in alignment with BSA/AML risk
- Expectation on an independent assessment of an institutions utility of a BSA/AML Model

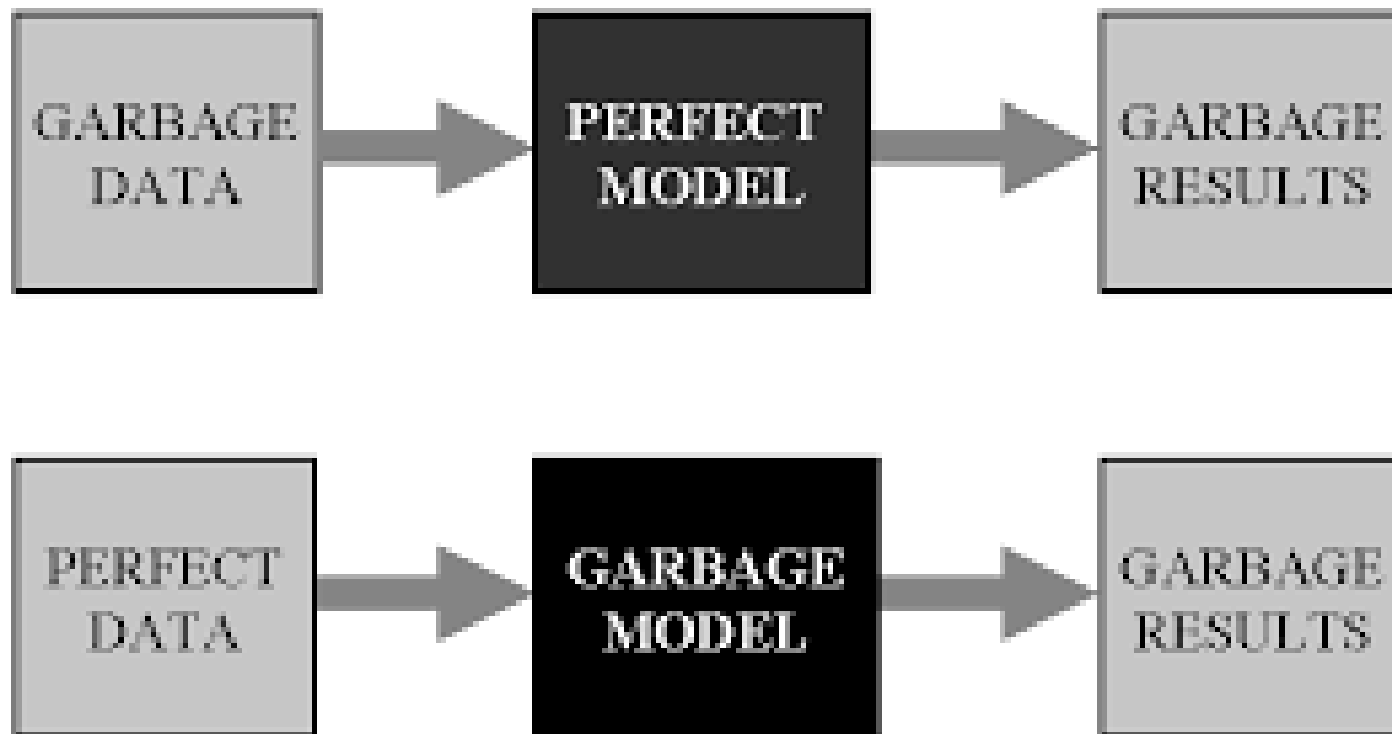


BSA System Validation



MODEL CALCULATIONS

"Garbage In-garbage Out" Paradigm



BSA System Validation vs. Calibration

BSA System Validation

- Analyze transaction codes and mapping between the Core system to the BSA/AML system
- Verifies transactions are accurately reflected and reconciled to the AML system
- Analyzes transactions to ensure accurate identification, proper categorization and mapping between the Core to the BSA/AML system

BSA Calibration

- Confirms alerts cover BSA/AML related risks
- Reviews the alert-to-case ratio for each detection scenario to identify parameters that could be adjusted to reduce the volume of “false-positives”.
- The Calibration determines that the thresholds and detection scenarios are properly configured so that the Bank can make sound decisions regarding whether further action is required

Action Plan for Community Banks

- Ensure a Strong Top-Down Compliance Culture.
- Committing Sufficient Personnel and Technological Resources, While Avoiding Excessive Overhead Costs.
- Focus on Cybersecurity
- Risk Management
- Effective Detection and Reporting

Questions?

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