



## Newsletter Article

April, 2017

### SERVING MONEY SERVICES BUSINESSES AND/OR THIRD PARTY PAYMENT PROCESSORS

By Jay Postma and Doug Dwyer

#### ABOUT THE AUTHOR(S)

**Jay Postma**, President of MSB Compliance, is Certified Anti-Money Laundering Specialist (CAMS), with over 25 years experience in the Banking, Financial Services, and Software Development industries. **Doug Dwyer**, Director of Bank Consulting at MSB Compliance, is a results-driven professional with a 30 plus year track record of successful financial institution management consulting. **MSB Compliance, Inc.** is dedicated to helping money services businesses (MSBs) meet their Bank Secrecy Act compliance obligations, protect their communities, and maintain their vital banking relationships. <http://www.msbcomplianceinc.com>



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#### Board of Directors

1. In August 2014 FinCEN issued an important advisory, FIN-20140A007, Advisory to U.S. Financial Institutions on Promoting a Culture of Compliance. In recognizing the importance of culture, FinCEN shared key learnings from various enforcement actions so that financial institutions might better ensure maintenance of effective BSA/AML programs. Each bank's Board of Directors typically has had BSA training annually in compliance with regulatory guidance. However, some bank Boards may not have had training and discussion specifically covering "culture of compliance." Or perhaps training was given when the advisory was released but has not been incorporated into subsequent training. When expanding services to areas of potentially higher risk such as MSBs and TPPPs we recommend that the subject be revisited. We recommend that a training presentation to the Board be made covering this "Culture of Compliance" and that the Advisory be shared with the Board for discussion.

2. As a bank grows through serving potentially higher risk customers such as MSBs and TPPPs, regulators will have reasonable concerns to be addressed as to whether the Board, Management, staff and systems are adequate to the increasing potential risks. As the profile of the bank changes, it becomes more important that Board members ensure they have adequate training appropriate to the higher risk profile enabling them to best fulfill their responsibilities. The OCC and other bank regulators typically conduct various Community Bank Director workshops each year. If bank directors have not already attended regulator sponsored training, it would likely be beneficial for the bank's directors to attend the regulator sponsored training.



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3. Governance practices are important to a sound compliance program regardless of whether a bank serves MSBs, payment processors or other potentially high risk entities. When expanding services, it is wise to review the corporate governance practices to evaluate whether improvements are warranted. The BSA Officer should maintain reporting of any open items of importance indicating whether self-identified, identified through the independent review or through engagements with contracted consultants, or through regulatory examination. The current list showing status of efforts to address, anticipated completion, and any issues closed since the prior Board meeting should be provided at each Board meeting or meeting of its compliance/audit committee.

4. As a bank moves to service potentially higher risk customers such as MSBs and TPPPs, the knowledge, experience and ability of the company and its personnel performing independent review should be further examined. Parties that may have been adequately prepared to perform reviews of lower potential risk banks may no longer be appropriate as the bank's risks increase. Likewise, if an internal audit function performs reviews it is possible they may need additional training, outside assistance, or to be replaced by outside examiners with deeper knowledge and experience.

## **Staffing**

1. As a bank begins serving MSBs and/or TPPPs, it is important to consider ahead of time when it is likely that staff level needs to be increased in order to ensure adequate, timely coverage of all responsibilities and to provide for effective backup and for BSA program continuity. The bank and BSA Officer should recognize as part of its planning and budgeting that it may take time to identify, move and train a strong internal candidate or to identify, hire and train an effective external candidate.

2. As a rough rule of thumb, consider that the bank's first additional BSA employee (if not needed before taking on any new potentially higher risk customers) may be needed after taking on 12 to 15 lower potential risk MSBs. Plan ahead for continuing success! A bank should not place itself in the position of having to explain to its regulators why it took on 15, 30, 50 or more MSBs and is making hundreds of thousands of dollars in net profit on MSB relationships but has not increased staff. Significant revenue growth in an area of higher potential risk without corresponding investment in expanding or improving staffing, systems, independent review, etc. would be indicative of problems with Board and management oversight, culture of compliance, training, etc.

## **Risk Based BSA/AML and OFAC Policies, Procedures and Controls**

1. Updated policies, procedures and controls need to be developed, presented to and approved by the Board, and then implemented with training. Key areas to address include: application process; valuation of potential customer risks including both compliance and credit risk implications; pricing; transaction monitoring; site visitation; evaluation of MSB compliance program and scope/quality of independent review; when and under what circumstances a third party review contracted by the bank is warranted; customer disciplinary and termination practices. If the bank does not employ a committee structure for review of potentially higher risk customer relationships, one should be implemented to help ensure potential revenue interests do not outweigh compliance interests, that there is no hint of impropriety in decision making, and that no person be placed into a position where his or her integrity might be questioned.

2. IF the bank has not registered with FinCEN to participate in voluntary information sharing under USA PATRIOT Act, section 314(b) it should do so and update its risk assessment and compliance program accordingly. Given the increased potential risk of a bank serving MSBs and/or TPPPs it would be beneficial to the bank to register. There are likely to be situations where it would be beneficial to contact another financial institution for information helpful in understanding whether observed activity is truly suspicious or

not. By registering the bank may also benefit from contact initiated by other financial institutions who would likely not call if the bank is not registered.

## Relationship Due Diligence and Monitoring

1. As part of understanding customers, evaluating and mitigating risks, it is important that site visits to MSBs occur AND that such visits be appropriately documented. Contemporaneous documentation should cover: the compliance and risk mitigation purposes of the visit; persons present; areas and scope of review, discussion and testing; and any findings/recommendations to share with either the customer and/or the bank's MSB review committee as may be applicable. Remember that from an examiner's viewpoint, if a site visit is not documented - it did not occur. And more importantly, if not documented the bank is less likely to identify and report potential problems and follow through to ensure the risk is adequately addressed.
2. Site visits for BSA/AML purposes need to be performed by BSA personnel who have received adequate training to perform such visits. A bank president or other executive (trained and alert for potential BSA/AML red flags) may visit an MSB or TPPP for relationship purposes in addition to the compliance visit but such visit should never take the place of visitation by the BSA Officer or compliance delegate. There are potential conflicts of interest in having a person with significant revenue responsibilities perform a site visit intended to mitigate compliance, credit and operating risks of an MSB or TPPP. As part of maintaining a strong culture of compliance it is important that the bank president or other executive not put himself or herself unnecessarily into a position that could create even a hint of impropriety. MSB site visits should generally be made by the BSA Officer or designee as agreed by the MSB review committee. Again, if beneficial for relationship purposes the President or other designee of the MSB committee might visit with the compliance visitation or separately from the compliance visitation.
3. Ideally, the bank will have the ability to monitor for negative news pertaining to higher potential risk customers, beneficial ownership and persons in significant management roles. As part of managing risk we recommend that all MSBs, TPPPs and their account signers and/or beneficial owners be subject to negative news monitoring.

## Transaction Monitoring

1. BSA and/or Operations staff typically review remote deposit capture deposit items from check cashing customers. In order to effectively carry out such review it is important for staff to be trained to understand the types of risks and compliance issues which may be identified by review of deposit items originating from check cashers, e.g. improper or inadequate endorsements, signs of kiting or structuring, unusual number of money orders from one customer, etc.
2. Check cashing is reversed from the normal flow of money laundering in that with the cashing of a check funds are being removed from the formal financial system. Money laundering is usually not something implicated by the cashing of checks although fraud may occur presenting credit risk to the MSB and to the servicing bank. The result of check fraud will then create money laundering which may thereafter be at another financial institution. The principal risk of money laundering with check cashers arises if there are unexplained sources of cash to the business. For the check casher, cash is a salable asset and unaccounted for signs of significant cash could indicate problems. The bank should periodically do a transaction analysis to evaluate whether cash orders are reasonable in light of checks cashed and cash generated through other sales, e.g. money transfer and money orders.
3. IF a bank begins to serve MSBs and as part of doing so establishes cash vaulting relationships with armored carriers, there are common risks which a bank may initially miss. Cash vaulting needs to be

covered within the risk assessment and compliance program. Implementation may involve new system transaction codes and, regardless of that may impact system transaction aggregation for CTR purposes. If the bank begins doing transactions both through bank and non-bank contracted carriers, there will also be ramifications to CTR reporting and the bank should carefully review FinCEN guidance and provide additional CTR training to staff, if applicable.

4. If a bank serves check cashers which cash checks payable to businesses (non-natural persons rather than sole proprietors), the bank should verify that the MSB has appropriate procedures to validate existence of the business and authority of the person presenting the check to negotiate the item. If the state of operation does not already require that licensees do this to ensure their holder in due course status, the bank should require such within the MSB's procedures. MSBs should be encouraged to ensure both an endorsement by the business owner/operator (or authorized party) in his/her capacity with the business and also an anomalous endorsement by the individual presenter as part of mitigating credit risk to both the MSB and also to the bank. Procedures should provide for reasonable additional due diligence by the MSB for businesses cashing significant dollar amounts of checks. Independent reviews should clearly cover these practices within the scope of the MSB's review.

5. Banks may at times have MSBs, including check cashers, that they haven't identified via their current processes. One method to identify potential MSBs is to determine if your core processing system has a report identifying business entities have negative average collected balances. Review to determine if there are any businesses with negative or very low balances that may potentially be check cashers; review deposit images where necessary and helpful to make determination. A second method, depending on systems, involves making queries of ACH transaction data fields, e.g. are there any customers receiving ACH settlement debits from perhaps Western Union, MoneyGram, etc. 6. If a Bank is serving a principal money transmitter, it is prudent for the bank to request the MSB's due diligence files on any foreign or domestic correspondent to whom it may be requested to wire funds on behalf of the principal money transmitter. The bank may consider the strength of due diligence by the MSB and whether the MSB has reasonably met FinCEN requirements for due diligence including confirmation of licensure where required, examination of beneficial ownership, etc. The bank may reasonably wish to restrict wire activity only to endpoints reviewed and authorized by the compliance function.

7. The BSA Officer should review the Bank's transaction monitoring program to ensure that monitoring rules are effective and appropriate for MSBs; same or similar rules may potentially need to be established to be run only against MSBs but with different thresholds than used with other customers.

## Training

1. From a training and coaching standpoint, it would be beneficial for the BSA Officer to participate and observe during an independent review of an MSB and during one or more site visits of an MSB alongside a staff member of MSB Compliance Inc. A BSA Officer may better operationalize information shared during in-house discussion and training after observing and receiving coaching and direction at a customer location.

2. We recommend that the BSA Officer or designee attend quarterly ACAMS Chapter meetings, where local meetings are available and as able.

3. We recommend that bank personnel attending BSA training events identify key takeaways / learnings and then, where applicable and beneficial, present them briefly to other key personnel who would benefit from the knowledge and insight. Document by memo to file as part of contemporaneous records supporting proof of ongoing training.

4. The American Bar Association's and American Bankers Association's Money Laundering Enforcement Conference is an outstanding conference for bankers. We recommend the BSA Officer attend once every several years if possible. On a subsequent year it would be beneficial for the BSA Officer to attend either the annual ACAMS or ACFCS conference.

5. BSA Officer should strongly consider achieving CAMS or CFCS certification. 6. We recommend that banks consider obtaining and using the short award winning movie "Carl's Story" and related training materials available from TAMLO International for a staff wide BSA training. The Board would also benefit from the perspective obtained by viewing the video.

### **Risk Based Transaction Monitoring and Filtering Program (NY DFS Section 504)**

On June 30, 2016, the New York State Department of Financial Services ("NYDFS") adopted a final regulation imposing new anti-money laundering and economic sanctions requirements on financial institutions regulated by the NYDFS (the "Final Rule"). The Final Rule requires various entities chartered or licensed under New York law such as principal money transmitters (each, a "Regulated Institution") to maintain a "Transaction Monitoring Program" and a "Filtering Program" (collectively, a "Transaction Monitoring and Filtering Program") to detect potential violations of applicable AML laws and regulations and sanctions programs administered by the U.S. Department of the Treasury's Office of Foreign Assets Control ("OFAC").

The Final Rule formally extends the understanding of a "reasonably designed" program to an entities Transaction Monitoring and Filtering Program and provides guidance on determining if a program is in fact "reasonably designed." The Final Rule becomes effective January 1, 2017 with initial requirement of Annual Board of Directors Resolution or Senior Compliance Official Certification due by April 15, 2018.

The Final Rule will require: increased rigor by subject entities in more effectively documenting their understanding of risks; clearly tying such risks to the selection, implementation, and testing of transaction and sanction monitoring protocols; ensuring effective tailored training fully extended to monitoring; and other matters.

The new NY DFS Section 504 Final Rule represents a significant expansion in understanding of what constitutes a risk based BSA/AML program reasonably designed to prevent, deter, detect and report potential abuse of financial services for money laundering and/or terrorist financing. The Rule also seeks to more effectively establish liability to the Compliance Officer and Board for programs that are not reasonably designed.

MSB Compliance Inc. believes that other states as well as federal examiners are likely to follow New York's lead in this area of understanding and increased expectation. Other than the certification requirements, it is not clear that existing law and regulation required adjustment to move the financial industry to a new understanding of the risk based approach. It is important that the MSBs subject to the requirement and banks serving entities subject to the requirement understand them, recognize their impact, and ensure the compliance function has sufficient resources to meet the new heightened expectations as applicable.

Banks serving MSBs and TPPPs, especially any higher risk ones, would be well served to more formally document and implement a risk based Transaction Monitoring and Filtering Program meeting the requirements as outlined by NY DFS. A copy of the text of the Final Rule is available at [www.dfs.ny.gov/legal/regulations/adoptions/dfsp504t.pdf](http://www.dfs.ny.gov/legal/regulations/adoptions/dfsp504t.pdf) . A copy of the press release is available at [www.dfs.ny.gov/about/press/pr1606301.htm](http://www.dfs.ny.gov/about/press/pr1606301.htm).

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