

New York State Department of Financial Services Releases Final Regulations to Enhance Anti-Money Laundering and Sanctions Compliance for Financial Institutions

Final regulations impose certification requirements on a financial institution's Board of Directors or Senior Officer(s) relating to BSA/AML and OFAC compliance.

The New York State Register today published the final regulations issued by the New York State Department of Financial Services (NYSDFS) that require financial institutions, including banks and other financial firms, to maintain enhanced Bank Secrecy Act¹/Anti-Money Laundering (BSA/AML) and Office of Foreign Asset Control (OFAC) monitoring and reporting programs (the Final Rule). The NYSDFS had released the final regulations on June 30, 2016. The Final Rule requires the board of directors or senior officer(s), as applicable, of such institutions to make an annual Board Resolution or Senior Officer(s) Compliance Finding certifying to their institution's full compliance with the BSA/AML and OFAC monitoring and filtering programs set forth in the Final Rule. The Final Rule will become effective on January 1, 2017.²

The Final Rule is largely similar to the proposed regulations the NYSDFS issued on December 1, 2015 (the Proposed Rule), which we described in our prior [Client Alert](#). However, in a significant departure from the Proposed Rule, the Final Rule removes the most controversial aspect of the proposal, which would have required an institution's chief compliance officer (or functional equivalent) to make an annual certification attesting to full compliance with the proposed rule's BSA/AML and OFAC monitoring and filtering programs. That requirement could have resulted in potential criminal penalties targeted at such certifying officer for filing an incorrect or false annual certification.

Background

In a speech announcing the Final Rule, NYSDFS Superintendent Maria T. Vullo noted that the final regulations aim to "close the compliance gaps in our financial regulatory framework to shut down money laundering operations and eliminate potential channels that can be exploited by global terrorist networks and other criminal enterprises."³ Superintendent Vullo further commented that financial institutions doing business in New York are responsible for doing "everything they can to stem the tide of illegal financial transactions that fund terrorist activity."⁴

The Proposed Rule was subject to an extended comment period that ended on March 31, 2016, and as the NYSDFS noted, the Final Rule has been amended to take into consideration comments which the financial services industry and other market participants submitted.

Overview of Final Rule

Scope of the Final Rule

Consistent with the Proposed Rule, the Final Rule applies to “Regulated Institutions,” which include:

- All banks, trust companies, private bankers, savings banks and savings and loan associations chartered pursuant to New York Banking Law (NYBL), and all branches and agencies of foreign banking corporations licensed pursuant to NYBL to conduct banking operations in New York
- All check cashers and money transmitters licensed pursuant to NYBL

In order to address shortcomings identified by the NYSDFS in the transaction monitoring and filtering programs of Regulated Institutions, such institutions are required to maintain a Transaction Monitoring and Filtering Program that meets the requirements set forth in the Final Rule and that is reviewed by senior management. The requirements applicable to the Transaction Monitoring and Filtering Program as well as the scope of senior management’s review of such programs are discussed in more detail below.

Transaction Monitoring and Filtering Program Requirements

In connection with the Transaction Monitoring and Filtering Program, the Final Rule adopts many of the same technical and mapping requirements imposed on Regulated Institutions that were introduced in the Proposed Rule, with a few revisions. Such revisions include, but are not limited to, the following:

- Eliminating the minimum requirement standard for each of the programs and instead including an exhaustive list of requirements to be applied only if applicable to each Regulated Institution
- Incorporating additional language into some of the requirements to emphasize the risk-based nature of the programs
- Replacing many of the references to “watch lists” with the “OFAC sanctions list” and changing the name of the Watch List Filtering Program to the Filtering Program

Pursuant to the Final Rule, each Regulated Institution must maintain a:

- Transaction Monitoring Program that is reasonably designed to monitor transactions that have already been executed for potential BSA/AML violations and Suspicious Activity Reporting. The system used to implement the program may be manual or automated and must meet the requirements set forth in the table below, to the extent they are applicable.
- Filtering Program that is reasonably designed to prevent the occurrence of transactions prohibited by OFAC. The system used to implement the program may be manual or automated, and should meet the requirements described in the table below, to the extent they are applicable.

Requirements Specific to the Transaction Monitoring Program, as Applicable	Requirements Specific to the Filtering Program, as Applicable
<ol style="list-style-type: none"> 1. Be based on the institution's on-going comprehensive risk assessment, including an enterprise-wide BSA/AML risk assessment, that takes into account the institution's size, staffing, governance, businesses, services, products, operations, customers, counterparties, other relations and their locations, as well as the geographies and locations of its operations and business relations (Risk Assessment); 2. Be reviewed and periodically updated at risk-based intervals to take into account and reflect changes to applicable BSA/AML laws, regulations and regulatory warnings, as well as any other information determined by the institution to be relevant from the institution's related programs and initiatives; 3. Appropriately match BSA/AML risks to the institution's businesses, products, services, and customers/counterparties; 4. BSA/AML detection scenarios with threshold values and amounts designed to detect potential money laundering or other suspicious or illegal activities; 5. End-to-end, pre-and post-implementation testing of the Transaction Monitoring Program, including, as relevant, a review of governance, data mapping, transaction coding, detection scenario logic, model validation, data input and Program output; 6. Documentation that articulates the institution's current detection scenarios and the underlying assumptions, parameters and thresholds; 7. Protocols setting forth how alerts generated by the Transaction Monitoring Program will be investigated, the process for deciding which alerts will result in a filing or other action, the operating areas and individuals responsible for making such a decision, and how the investigative and decision-making process will be documented; and 8. Be subject to an on-going analysis to assess the continued relevancy of the detection scenarios, the underlying rules, threshold values, parameters and assumptions. 	<ol style="list-style-type: none"> 1. Be based on the Risk Assessment of the institution; 2. Be based on technology, processes or tools for matching names and accounts, in each case based on the institution's particular risks, transaction and product profiles; 3. End-to-end, pre-and post-implementation testing of the Filtering Program, including, as relevant, a review of data matching, an evaluation of whether the OFAC sanctions list and threshold settings map to the risks of the institution, the logic of matching technology or tools, model validation, and data input and Filtering Program output; 4. Be subject to on-going analysis to assess the logic and performance of the technology or tools for matching names and accounts, as well as the OFAC sanctions list and the threshold settings to see if they continue to map to the risks of the institution; and 5. Documentation that articulates the intent and design of the Filtering Program tools, processes or technology.

**Requirements Relating to Both the
Transaction Monitoring and Filtering Programs, as Applicable**

1. Identification of all data sources that contain relevant data;
2. Validation of the integrity, accuracy and quality of data to ensure that accurate and complete data flows through the Transaction Monitoring and Filtering Program;
3. Data extraction and loading processes to ensure a complete and accurate transfer of data from its source to automated monitoring and filtering systems, if automated systems are used;
4. Governance and management oversight, including policies and procedures governing changes to the Transaction Monitoring and Filtering Program to ensure that changes are defined, managed, controlled, reported and audited;
5. Vendor selection process if a third party vendor is used to acquire, install, implement or test the Transaction Monitoring and Filtering Program or any aspect of it;
6. Funding to design, implement and maintain the Transaction Monitoring and Filtering Program that complies with the requirements of the Proposed Rule;
7. Qualified personnel or outside consultant(s) responsible for the design, planning, implementation, operation, testing, validation and on-going analysis of the Transaction Monitoring and Filtering Program, including automated systems if applicable, as well as case management, review and decision-making with respect to generated alerts and potential filings; and
8. Periodic training of all stakeholders with respect to the Transaction Monitoring and Filtering Program.

Annual Certification Requirement

As noted above, the Final Rule dispenses with the chief compliance officer certification and instead requires a certification from a Regulated Institution's governing board or functional equivalent if such institution does not have a board of directors (Board of Directors) or the senior individual(s) responsible for the management, operations, compliance and/or risk of a Regulated Institution, including a branch or agency of a foreign banking organization that is subject to the Final Rule (Senior Officer(s)), as applicable. Notably, the Final Rule also does not provide for potential criminal penalties to be imposed on the Board of Directors or Senior Officer(s) in the event of the filing of an incorrect or false annual certification. The Final Rule does, however, clarify that the requirements set forth in the final regulations will be enforced pursuant to the Superintendent's authority under any applicable laws.

The Final Rule requires that a Regulated Institution's Board of Directors or Senior Officer(s) adopt and submit a Board Resolution or Senior Officer(s) Compliance Finding, as applicable, certifying to compliance with the requirements set forth in the Final Rule. Such Board Resolution or Senior Officer(s) Compliance Finding must be submitted by April 15 of each year, commencing on April 15, 2018. In addition, each Regulated Institution is required to maintain — for a period of five years — all records, schedules and data supporting the adoption of the Board Resolution or Senior Officer(s) Compliance Finding.

While the removal of any references to criminal penalties and the insertion of a knowledge qualifier in the annual certification to be submitted by an institution's Board of Directors or Senior Officer(s) should eliminate the potential chilling effect of that component of the Proposed Rule on the ability to recruit, hire and retain qualified compliance officers, the Final Rule remains highly technical in nature. As a consequence, Regulated Institutions will need to ensure that persons with the requisite qualifications will be carrying out the requirements set forth in the Transaction Monitoring and Filtering Program effectively and on an enterprise-wide basis. Furthermore, New York branches or agencies of foreign banks may find compliance with the Final Rule to be particularly challenging considering that foreign banks are subject to

home country anti-money laundering and sanctions regimes that are different from those to which their New York branches and agencies are subject.

Conclusion

The issuance of the Final Rule is a decisive step on the part of the NYSDFS to take affirmative action to address the many anti-money laundering and sanctions violations that have plagued New York's financial institutions in recent years, the perceived gaps in Federal regulation relating to BSA/AML and OFAC programs and system requirements, and a global terrorist network that is becoming increasingly sophisticated at infiltrating the systems of financial institutions. While the Final Rule does attempt to address the shortcomings in the transaction monitoring and filtering programs maintained at New York's financial institutions, the complexity of the Transaction Monitoring and Filtering Program, which requires a high degree of technical knowledge to implement, will likely present significant challenges to affected financial institutions as they work towards amending their internal systems by the January 1, 2017 conformance deadline.

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Endnotes

¹ 31 USC 5311 *et seq.*

² NY Reg, July 20, 2016 at 13-16, available at <http://docs.dos.ny.gov/info/register/2016/july20/pdf/rulemaking.pdf>.

³ DFS Issues Final Anti-Terrorism Transaction Monitoring and Filtering Program Regulation, NYSDFS Press Release, June 30, 2016, available at <http://www.dfs.ny.gov/about/press/pr1606301.htm>.

⁴ *Id.*