WILMERHALE

2021 AML Trends and Developments

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Anti-money laundering ("AML") issues have been a focus of regulators and law enforcement for the past decade and will likely continue to be a priority issue area for the Biden Administration. The AML landscape is shifting considerably as a series of regulatory actions in the last months of 2020 and the January 1, 2021 passage of the National Defense Authorization Act for Fiscal Year 2021 ("NDAA")[1]— adopted with bipartisan support overriding President Trump's veto—bring real change to the regulatory environment at the start of the new administration. Indeed, the NDAA is the most significant amendment to the AML landscape in a generation, since the adoption of the USA PATRIOT Act, and will require extensive implementation by the Treasury Department. The regulatory and legislative changes together have two principal themes: (i) a conscious effort to evolve AML compliance and the Bank Secrecy Act and its implementing regulations (collectively, the "BSA") to make the system more efficient and effective; and (ii) adapting the BSA to a new generation of threats.

Although the NDAA may be perceived as a win for the industry, particularly to the extent it may lessen institutions' burden with respect to obtaining beneficial ownership information, the law's bipartisan support makes it likely that implementing agencies will move to implement it as intended (as indeed they are required by law to do), even with the expected appointment of new leadership at some of the implementing agencies. Further, the NDAA's promise to facilitate the adaptation of advanced technology in BSA compliance and to help financial institutions focus AML resources on priorities identified by the government may also yield substantial dividends, though the devil will come in the details of implementation. It is worth noting that similar rulemakings, such as the Financial Crimes Enforcement Network's ("FinCEN") Customer Due Diligence Rule ("CDD Rule"), took years to be completed. It may therefore be some time before the industry sees benefits from the rulemaking, statutory deadlines for the rulemakings notwithstanding. Nevertheless, the industry should think through a strategy for proactively engaging with the government to inform those implementation efforts.

This alert primarily focuses on regulatory changes, specifically with respect to three key areas: (i) the creation of a national beneficial ownership registry; (ii) innovation and reforms to the suspicious

[1] The William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, H.R. 6395, 116th Cong. (2020).

activity reporting regime; and (iii) changes aimed at new aspects of the risk environment. But financial institutions should also brace themselves for a more aggressive enforcement environment across the board in the Biden Administration, and on AML issues in particular. Attention to AML and sanctions issues in the banking space has increased significantly in the past decade since the last round of major AML and sanctions enforcement actions. However, in response to those changes, regulatory expectations—and the risk environment—have clearly evolved as well, and we expect AML and sanctions to remain a top regulatory and law enforcement priority. While this piece focuses on regulatory and compliance issues, financial institutions should pay careful attention to recent trends—including individual liability for compliance officers—as the Biden Administration seeks to flex its muscle on the enforcement front. Now is the time to identify and proactively mitigate risk to best position your institution in the event of future inquiries.

I. Beneficial Ownership Information Collection

The most salient aspect of the NDAA relevant to AML issues is the Corporate Transparency Act ("CTA"),[2] mandating that FinCEN create and maintain a registry of beneficial ownership information for a wide swath of "reporting companies." The CTA registry is intended to help prevent money laundering, tax fraud, human and drug trafficking, foreign corruption, and other crimes by identifying beneficial owners of anonymous shell companies to cut down on the use of such companies to acquire and move illicit assets.[3] In many ways, the goal is similar to that of geographic targeting orders, which seek to prevent illicit activity by requiring identification of beneficial owners in certain high-value real estate transactions.[4] The CTA closes a significant gap as most states do not collect and make available to the industry information about beneficial owners of legal entities.[5]

Particularly relevant for financial institutions, the CTA requires the Secretary of the Treasury to revise the CDD Rule[6]—which requires certain covered financial institutions to identify and verify beneficial owners of legal entity customers at account opening—to be consistent with the CTA and remove unnecessary or duplicative requirements.[7] Once in place, modifications will likely have a significant impact on covered financial institutions' customer due diligence programs. Financial institutions must pay close attention to these changes and consider how to adapt their existing compliance programs to be consistent.

A. CTA Overview

Reporting Companies. "Reporting companies" will be required to provide FinCEN with beneficial ownership information under the CTA. "Reporting company" is defined as "a corporation, limited

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[2] NDAA §§ 6401-6403.
[3] *Id.* § 6402(3).
[4] Press Release, FinCEN, *FinCEN Reissues Real Estate Geographic Targeting Orders for 12 Metropolitan Areas* (Nov. 5, 2020), https://www.fincen.gov/news/news-releases/fincen-reissues-real-estate-geographic-targeting-orders-12-metropolitan-areas-2.
[5] NDAA § 6402(2).
[6] *See* 81 Fed. Reg. 29,398 (May 11, 2016), https://www.govinfo.gov/content/pkg/FR-2016-05-11/pdf/2016-10567.pdf.
[7] NDAA § 6403(d)(1).

liability company, or other similar entity" that is either "created by the filing of a document" with a state or created in a foreign jurisdiction but "registered to do business" in the United States by the filing of a document with a state.[8]

Notably, the CTA excludes various categories of entities, including many publicly traded, regulated, and tax-exempt companies; investment funds; registered broker-dealers; securities exchanges; clearing organizations; investment companies and advisers; banks and bank holding companies; credit unions; and companies owned or controlled by many of these exempted entities.[9] These exemptions largely track the exemptions currently found in the CDD Rule.[10] The CTA also excludes two types of entities from the reporting requirement based on specific identified qualities of the entity rather than their regulatory status:

- an entity that: (i) employs more than 20 full-time employees in the United States; (ii) filed, in the previous year, a U.S. federal income tax return demonstrating more than $5 million in gross receipts or sales in the aggregate, including the receipts or sales of affiliates; and (iii) operates at a physical office within the United States;[11] and
- an entity that (i) is in existence for over one year; (ii) is not engaged in an active business; (iii) is not owned, directly or indirectly, by a foreign person; (iv) has not, in the preceding 12-month period, experienced a change in ownership or sent or received funds in an amount greater than $1,000; and (v) does not otherwise hold any assets.[12]

These exemptions are intended to avoid imposing redundant reporting requirements on entities that already report similar information to other government agencies and to avoid unnecessary reporting requirements for entities at low risk of engaging in money laundering or other financial crime. To that end, the CTA also grants the Secretary of the Treasury, in consultation with the Attorney General and Secretary of Homeland Security, the ability to add to these categories of exempted entities by regulation where such reporting would not serve the public interest and would not be highly useful in national security, intelligence, and law enforcement agency efforts to detect, prevent, or prosecute money laundering, the financing of terrorism, proliferation finance, serious tax fraud, or other crimes.[13]

Beneficial Owners. Similar to the CDD Rule, a "beneficial owner" of a reporting company is one who, directly or indirectly, "exercises substantial control over the entity" or "owns or controls not less than 25 percent of the ownership interests of the entity."[14] Intermediate entities, no matter how many or where organized, are transparent for this purpose; that is, the ultimate individual beneficial owners will still need to be reported under the CTA. Certain individuals are exempted from the definition of beneficial owners, including agents, intermediaries, or custodians (though their

[8] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(a)(11)).
[9] *Id.*
[10] *See* 31 C.F.R. § 1010.230(e)(2).
[11] NDAA § 6403(a) (adding 31 U.S.C. § 5336(a)(11)(B)(xxi)).
[12] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(a)(11)(B)(xxiii)).
[13] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(a)(11)(B)(xxiv)).
[14] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(a)(3)(A)).

principals may not be excluded); employees of a reporting company whose interest in, or control of, the entity is attributable solely to their employment; and most creditors of the reporting company.[15]

Required Disclosures. The disclosure requirement is relatively straightforward. When the regulations under the CTA become effective, reporting companies must provide, for each beneficial owner, a name, address, date of birth, and driver's license or other form of identification number prescribed by the statute.[16] Reporting companies will not be expected to provide details about a company's purpose or operation, or the owners' own functions within the company.

Reporting Timing. By the terms of the legislation, implementing regulations are to be issued by the Treasury Department by 2022. There is no "grandfathering" exemption for compliance; entities formed prior to the effective date of the CTA are still fully subject to its provisions. Reporting companies in existence on the effective date of the FinCEN implementing regulations will have two years from that date to report beneficial ownership information. Companies formed after the effective date of the regulations will be expected to report at the time of formation. Reporting companies will also be required to update beneficial ownership information within one year of any change.

Penalties. An unexcused failure to report correct beneficial ownership information is subject to a $500 daily penalty and, potentially, a $10,000 penalty and imprisonment for up to two years.[17] The CTA excuses liability for incorrect submissions upon a voluntary correction furnished within 90 days after the filing of the original report.[18]

B. Use of Information

Federal and state law enforcement agencies will have access to data collected pursuant to the CTA, but the registry will not be available to the public. Federal agencies will have access to the information upon request, and state law enforcement may gain access to information with court approval.[19] Treasury Department employees will have broad authorization to use the information,[20] and the CTA specifically provides that information may be used for tax administration purposes.[21]

Information in the registry may be disclosed to financial institutions upon request—and only with the consent of the reporting company—to assist with customer due diligence.[22] The statutory text says that the form and manner of disclosure to financial institutions is to be determined by the Secretary of the Treasury by regulation.[23] Financial institution access is intended, in part, to help "confirm

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[15] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(a)(3)(B)).
[16] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(b)(2)).
[17] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(h)(3)(A)).
[18] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(h)(3)(C)(i)(I)(bb)).
[19] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(2)(B)(i)).
[20] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(5)(A)).
[21] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(5)(B)).
[22] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(2)(B)(iii) (FinCEN may disclose beneficial ownership information upon "(iii) a request made by a financial institution subject to customer due diligence requirements, with the consent of the reporting company, to facilitate the compliance of the financial institution with customer due diligence requirements under applicable law;").
[23] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(2)(C)).

beneficial ownership information provided to financial institutions to facilitate the compliance of the financial institutions" with AML, countering the financing of terrorism, and customer due diligence requirements.[24] The CTA also requires that such information provided to a financial institution be available to the federal regulators who assess the financial institution's compliance with customer due diligence requirements.[25]

C. Relevance to Financial Institutions

The BSA requires certain covered financial institutions to develop and maintain effective AML programs, including by identifying beneficial owners of companies. In 2016, FinCEN issued the CDD Rule, requiring financial institutions to obtain and verify beneficial ownership information for customers at the time an account is opened.[26] The CTA recognizes that there will now be overlap between information collected pursuant to the CDD Rule's requirements and what FinCEN collects directly from reporting companies.[27]

Thus, the CTA directs the Secretary of the Treasury to revise the CDD Rule—no later than one year after the effective date of the CTA's implementing regulations—to conform it with the CTA, account for the access of financial institutions to beneficial ownership information, and reduce "unnecessary or duplicative" burdens on financial institutions and customers.[28] Essentially, while the CTA directs the Treasury Department to leave in place the requirement that financial institutions identify and verify beneficial owners, it mandates the reconsideration and replacement of the accompanying mechanisms by which such identification is effectuated.[29] In revising the CDD Rule, the Secretary of the Treasury is directed to consider: (i) the use of risk-based principles for requiring reports of beneficial ownership information; (ii) "the degree of reliance by financial institutions on information provided by FinCEN for purposes of obtaining and updating beneficial ownership information;" (iii) strategies for more timely, accurate, complete information reporting to the Secretary; and (iv) any other matter deemed important by the Secretary.[30]

The effects of these changes on financial institutions will thus depend substantially on the specific regulations promulgated by the Secretary of the Treasury, but, depending on the rules that are ultimately published, the statute could result in making the customer onboarding process substantially more efficient. For example, beneficial ownership information may be provided to financial institutions merely as a verification tool, but alternatively, it could be provided as a resource for fulfilling customer information *collection* obligations.[31] To the extent financial

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[24] *Id.* § 6402(6)(B).
[25] *Id.* § 6403(a) (adding 31 U.S.C. § 5336(c)(2)(C)).
[26] *See* 81 Fed. Reg. 29,398 (May 11, 2016), https://www.govinfo.gov/content/pkg/FR-2016-05-11/pdf/2016-10567.pdf.
[27] NDAA § 6403(d).
[28] *Id.* § 6403(d)(1).
[29] *Id.* § 6403(d)(2).
[30] *Id.* § 6403(d)(3).
[31] *Compare id.* §§ 6402(6) (It is the sense of Congress that "beneficial ownership information collected under the amendments . . . will be directly available only to authorized government authorities . . . [to] . . . **confirm beneficial ownership information provided to financial institutions** to facilitate the compliance of the financial institutions with anti-money laundering, countering the financing of terrorism, and customer due

institutions are permitted to use the FinCEN registry as a primary source for customer due diligence, it is not clear whether the Secretary will afford a safe harbor from liability for reliance on such data. Likewise, because financial institutions' regulators will be able to access registry information, financial institutions may bear responsibility to verify against the registry information they have collected.[32]

Financial institutions should consider how to engage with Treasury as it considers these regulations, as the degree to which the CTA alleviates burdens on financial institutions will depend on the regulations that are ultimately published.

Until FinCEN revises the CDD Rule in light of the CTA, financial institutions' customer due diligence procedures should remain in place. Financial institutions covered by the CDD Rule must still obtain and verify beneficial ownership information of legal entity customers subject to the rule, along with other AML program requirements. However, covered financial institutions should be prepared to update policies and procedures when the CDD Rule is revised.

Financial institutions will face a host of potential implementation challenges as they update their policies and procedures in light of the new requirements. They will also need to consider novel questions, such as whether to file a Suspicious Activity Report ("SAR") to the extent beneficial ownership information in the national registry is inconsistent with information previously obtained from a customer.

Proactive financial institutions may wish to consider CTA preparedness initiatives. There is a significant likelihood that financial institutions will be drafted into a *de facto* role of identifying customers that should register and educating such companies about their registration requirements. To see why this is likely, imagine the scenario where a financial institution conducts a periodic refresh of customer due diligence and discovers that the customer is not registered. It is likely that the financial institution would then communicate with the customer, inform it of the requirements, and educate the customer on the requirements. If the customer does not then register, the financial institution would face questions about whether to file a SAR and/or exit the customer.

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diligence requirements under applicable law;") (emphasis added) and 6403(d)(1)(B) (The Department of Treasury is to revise the CDD Rule, in part, to "account for the access of financial institutions to beneficial ownership information filed by reporting companies under section 5336 . . . **in order to confirm the beneficial ownership information provided directly to the financial institutions** to facilitate the compliance of those financial institutions with anti-money laundering, countering the financing of terrorism, and customer due diligence requirements under applicable law;"), *with id.* § 6403(d)(3)(B) (In revising the CDD Rule, the sSecretary shall consider "the degree of reliance by financial institutions on information provided by FinCEN for purposes of **obtaining and updating beneficial ownership information**;") (emphasis added).

[32] CDD Rule revisions should "account for the access of financial institutions to beneficial ownership information filed by reporting companies under [the CTA] . . . to confirm the beneficial ownership information provided directly to the financial institutions to facilitate the compliance of those financial institutions with anti-money laundering, countering the financing of terrorism, and customer due diligence requirements." *Id*. § 6403(d)(1)(B).

II. Innovation and SAR Reform

Over the past few years, FinCEN and federal banking agencies have expressed general support for more effective, efficient, and innovative AML compliance programs, and both the letter and spirit of the NDAA represent another step in that direction.[33] Recent statutory and regulatory efforts have paved the way for concrete shifts in the compliance regime. In December, the Federal Deposit Insurance Corporation ("FDIC") and Office of the Comptroller of the Currency ("OCC") finalized parallel Notices of Proposed Rulemaking ("NPRMs") entitled *Exemptions to Suspicious Activity Report Requirements*. The regulators proposed modified regulations that, if finalized, would enable them to grant financial institutions broader exemptions to the SAR filing requirements in connection with innovative compliance approaches.[34]

Although FinCEN and the federal banking agencies have articulated support for innovation over the past several years, prior action did not result in concrete regulatory change to effectuate these goals. The NDAA and NPRMs provide a pathway toward a clear regime that would give financial institutions confidence that good faith efforts to experiment and to advance the use of technology in the financial crimes compliance space will not themselves generate adverse regulatory consequences. While the NDAA and NPRMs are promising steps forward, change will take more time as regulators continue to review the issues, absorb feedback, evaluate implementation, and issue additional guidance. In the meantime, to the extent a financial institution is contemplating adopting an innovative approach that would represent a material deviation from its standard process, it should take, at a minimum, two vital steps: (i) conduct a formal risk assessment in connection with the change; and (ii) thoroughly document the change, including why the financial institution has a good faith belief that the change supports financial crimes compliance and ensuring that the financial institution is able to explain clearly to its regulators what the technical tool does. Financial institutions that band together and collectively propose changes to the SAR regime that will assist law enforcement and regularize the compliance burden on companies may have more impact with the new Biden Administration.

A. The Progression of Regulatory Efforts to Modernize SAR Requirements

Background: The Joint Statement. On December 3, 2018, FinCEN issued a joint statement with the Federal Reserve Board, FDIC, National Credit Union Administration, and OCC to encourage financial institutions to consider and implement "innovative efforts to combat money

[33] The NDAA significantly amends the BSA and other AML laws. The NDAA imposes multiple requirements on regulators which that are aimed at advancing the use of technology in this space. These include requirements that regulators conduct reviews, provide reports and briefings to Congress, implement new guidance, and make institutional changes, including the establishment of "Innovation Officer" positions to provide resources to financial institutions.

[34] *See* Press Release, FDIC, *FDIC Board Approves Proposed Rule to Amend Suspicious Activity Report Requirements* (Dec. 15, 2020), https://www.fdic.gov/news/press-releases/2020/pr20138.html; Press Release, OCC, *OCC Proposes Rule Regarding Exemptions to Suspicious Activity Report Requirements* (Dec. 17, 2020), https://www.occ.gov/news-issuances/news-releases/2020/nr-occ-2020-174.html.

laundering and terrorist financing" through the deployment of novel technologies.[35] The regulators noted that as money launderers' tactics evolve, compliance mechanisms must keep pace, and new technologies such as artificial intelligence and machine learning can help manage risks. They also acknowledged that innovative pilot programs should be encouraged, even when such programs prove ultimately unsuccessful or uncover compliance gaps. FinCEN announced a new innovation initiative that would include outreach efforts. The other agencies committed to establish or continue to support their respective offices focused on advancing innovation.

While this guidance signaled openness to innovation in theory, it was heavily caveated and did not offer concrete regulatory relief. Banks were cautioned to "prudently evaluate whether, and at what point, innovative approaches may be considered sufficiently developed to replace or augment existing BSA/AML processes."[36] As a result, relying on innovative approaches carried nontrivial risks for financial institutions, and the opportunities for change were limited. Although FinCEN has taken subsequent steps to promote innovation—including the BSA Value Project,[37] "Innovation Hours,"[38] and COVID-19 accommodations[39]—these risks remain.

FinCEN's Advance Notice of Proposed Rulemaking. In 2019, the Bank Secrecy Act Advisory Group ("BSAAG")—a forum for industry, regulators, and law enforcement—created an Anti-Money-Laundering Effectiveness Working Group to develop recommendations for strengthening the national AML regime by increasing its efficiency and effectiveness. This working group offered recommendations, culminating in FinCEN's September 17, 2020 publication of an Advance Notice of Proposed Rulemaking ("ANPRM"). The ANPRM is aimed at ensuring an "effective and reasonably designed" AML program that provides a "high degree of usefulness to government authorities."[40] Among other things, the ANPRM addresses the need "to facilitate the

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[35] FRB, FDIC, FinCEN, NCUA, OCC, Joint Statement on Innovative Efforts to Combat Money Laundering and Terrorist Financing (Dec. 3, 2018), https://www.fincen.gov/sites/default/files/2018-12/Joint Statement on Innovation Statement (Final 11-30-18)_508.pdf.

[36] *Id.* at 2.

[37] In 2019, FinCEN launched the BSA Value Project to analyze the value of the BSA information it receives in order to improve processes. Press Release, FinCEN, *Prepared Remarks of FinCEN Director Kenneth A. Blanco, delivered at the American Bankers Association/American Bar Association Financial Crimes Enforcement Conference* (Dec. 10, 2019), https://www.fincen.gov/news/speeches/prepared-remarks-fincen-director-kenneth-blanco-delivered-american-bankers.

[38] This program provides opportunities for financial institutions and technology companies to present innovative products and services to FinCEN during monthly virtual meetings. Press Release, FinCEN, *FinCEN Announces Its Innovation Hours Program* (May 24, 2019), https://www.fincen.gov/news/news-releases/fincen-announces-its-innovation-hours-program; FinCEN, FinCEN's Innovation Hours Program, https://www.fincen.gov/resources/fincens-innovation-hours-program (last visited Jan. 14, 2021).

[39] FinCEN acknowledged that financial institutions might experience difficulties or delays in meeting their BSA obligations due to the demands of disbursing COVID-19 relief funds. FinCEN guidance highlights innovation as a potential solution to this problem. For more information, *see* David S. Cohen, Michael J. Leotta, Zachary Goldman & Michael Romais, *COVID-19: Federal Regulators Provide Limited AML Relief in Coronavirus Response, and Limited Support for the Use of Technology in Financial Crime Compliance Activities*, WilmerHale (Apr. 24, 2020), https://www.wilmerhale.com/en/insights/client-alerts/20200424-federal-regulators-provide-limited-aml-relief-in-coronavirus-response.

[40] Press Release, FinCEN, *FinCEN Seeks Comments on Enhancing the Effectiveness of Anti-Money Laundering Programs* (Sept. 16, 2020), https://www.fincen.gov/news/news-releases/fincen-seeks-comments-enhancing-effectiveness-anti-money-laundering-programs.

ability of the financial industry and corresponding supervisory authorities to leverage new technologies and risk-management techniques."[41] The ANPRM specifically includes FinCEN's recommendations to "support[] potential automation opportunities for high-frequency/low-complexity SARs and currency transaction reports ('CTRs'), and explor[e] the possibility of streamlined SARs on continuing activity."[42]

It is worth monitoring developments on this front to consider how FinCEN may approach the continued evolution of the BSA, particularly with new leadership at the Treasury and, we anticipate, FinCEN. However, proactive financial institutions should consider conducting annual effectiveness reviews of their AML compliance programs, with the expectation that examiners will increasingly look at their programs through this lens, even as the rulemaking progresses or, indeed, even if the rulemaking is abandoned. An effectiveness review could be done by enhancing the "control effectiveness" portion of a financial institution's existing enterprise risk assessment. For example, assessment of the control effectiveness of a financial institution's SAR reporting process could be expanded to include information sharing with law enforcement. The results of the annual effectiveness review should be fed back into the financial institution's plan for continuous improvement of its AML compliance program.

B. Recent Actions: Proposed SAR Exemptions and the NDAA

1. Proposed SAR Exemptions

The recent FDIC and OCC NPRMs are intended to alleviate burdens for financial institutions that adopt innovative approaches to SAR filing. These NPRMs reinforce the general statements that FinCEN and the banking agencies have been making since their 2018 joint statement, and take the important step further by proposing concrete regulatory change that incentivizes innovation and efficiency in BSA compliance activities.

The proposed changes are designed to accomplish two primary goals: (i) enable the banking agencies to reduce regulatory burdens by coordinating with FinCEN to provide one unified requirement; and (ii) encourage financial institutions to embrace technology to meet BSA requirements.

With respect to the first objective, the NPRMs enable the banking agencies to allow broader SAR exemptions for certain kinds of activity that are consistent with safe and sound banking practices. The current regime only relieves SAR filing obligations in circumstances involving physical crimes (*e.g.*, robberies) and lost, missing, counterfeit, or stolen securities. FinCEN has broader discretion to grant exemptions from BSA requirements, meaning FinCEN may issue a SAR filing exemption

[41] Anti-Money Laundering Program Effectiveness, 81 Fed. Reg. 58,023, 58,024 (Sept. 17, 2020), https://www.govinfo.gov/content/pkg/FR-2020-09-17/pdf/2020-20527.pdf.
[42] 81 Fed. Reg. at 58,025.

but an institution could still be required to file a SAR under the relevant banking agency's regulations. This proposed rule, if adopted, would harmonize these approaches.

On the innovation front, the banking agencies contemplate that financial institutions may adopt technologies to enhance monitoring tools, automate investigation processes, and automate the population of forms.[43] The FDIC anticipates that "supervised institutions will leverage existing or future technologies to report information concerning suspicious activity in a different manner or time frame or to share SAR-related information."[44] The OCC specifies that exemption requests from financial institutions may relate to, "among other things, expanded investigations and SAR timing issues, SAR disclosures and sharing, continued SAR filings for ongoing activity, outsourcing of SAR processes, the role of agents of national banks and federal savings associations, the use of shared utilities and shared data, and the use and sharing of de-identified data."[45]

The proposed regulatory changes would enable more flexibility in granting exemptions and help synchronize requirements imposed by multiple federal regulators, notwithstanding some differences between the FDIC and OCC's proposed changes.[46]

2. The NDAA

Beyond the provisions identified above, the NDAA amends the BSA in several ways that support innovation, efficiency, and effectiveness related to SARs by conducting reviews, providing reports and briefings to Congress, implementing new guidance for financial institutions, and making institutional changes by designating innovation support roles (*e.g.*, Innovation Officers and a Subcommittee on Innovation and Technology).

Regulator Reviews and Reports to Congress. The NDAA requires the Treasury Department, the Justice Department, and other agencies to evaluate SAR reporting requirements and Currency Transaction Reports and consider options for streamlining compliance processes. Among other things, agencies must analyze options to integrate financial institution systems and the BSA e-filing system to permit, for example, "automatic population of report fields and the automatic submission of transaction data for suspicious transactions, without bypassing the obligation of each reporting financial institution to assess the specific risk of the transaction reported."[47] The agencies' review also must include an analysis of "whether financial institutions should be permitted to streamline or otherwise adjust, with respect to particular types of customers or transactions, the process for determining whether activity is suspicious or the information included in the narrative of a [SAR]."[48]

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[43] FDIC NPRM at 6–7, https://www.fdic.gov/news/board/2020/2020-12-15-notice-sum-d-fr.pdf; OCC NPRM at 8, https://www.occ.gov/news-issuances/federal-register/2020/nr-occ-2020-174a.pdf.
[44] FDIC NPRM at 3.
[45] OCC NPRM at 8–9.
[46] The FDIC proposal contemplates more deference to FinCEN as the administrator of the BSA. When both FinCEN and the banking agency require a SAR, the FDIC would seek FinCEN's determination whether the exemption is consistent with safe and sound banking principles under the BSA and FinCEN's exemption concurrence, whereas the OCC would make an independent determination and *may* notify the other banking agencies and consider their views. FDIC NPRM at 8; OCC NPRM at 10.
[47] NDAA § 6204(b)(2)(H).
[48] *Id.* § 6204(b)(2)(L).

The review will rely heavily on the BSA Value Project[49] and focus on identifying data that provide "the greatest value to, and that best support, investigative priorities of law enforcement and national security agencies."[50] In addition, the NDAA contemplates that the government must consult with "other relevant stakeholders" in connection with the review. Financial institutions and industry groups should consider whether and how to ensure this process accounts for their perspectives. The review will culminate with a report to Congress and appropriate proposed rulemakings within one year of enactment of the NDAA.[51]

Additionally, the Secretary of the Treasury must submit to relevant Senate and House Committees a report that must include legislative and administrative recommendations related to "the impact of financial technology on financial crimes compliance."[52] And the Director of FinCEN must "brief" relevant Senate and House Committees on the use of emerging technologies, including "artificial intelligence, digital identity technologies, [and] distributed ledger technologies."[53]

New Guidance. Regulators must update guidance for financial institutions on innovative compliance systems. The NDAA includes these requirements:

- Regulators shall "establish streamlined, including automated, processes to, as appropriate, permit the filing of noncomplex categories of reports."[54]
- FinCEN will provide financial institutions information about typologies (techniques to launder money or finance terrorism), "including data that can be adapted in algorithms if appropriate."[55]
- New regulations will define standards for testing technology, which may include "innovative approaches such as machine learning or other enhanced data analytics processes."[56]
- The Secretary of the Treasury, in coordination with FinCEN, will establish a pilot program permitting financial institutions to share SAR information with their "foreign branches,

[49] This project includes three core components: (1) assessing how potential regulatory and compliance changes will lead to more effective law enforcement outcomes, beyond the goal of industry efficiency; (2) providing detailed feedback to financial institutions so that they can assess the value of their automated tools and databases; and (3) identifying challenges that require action, particularly with respect to the development and communication of AML priorities. Through this project, FinCEN has developed over 500 metrics to quantitatively track and measure the value of the compliance information that financial institutions submit. Press Release, FinCEN, *Prepared Remarks of FinCEN Director Kenneth A. Blanco, delivered at the American Bankers Association/American Bar Association Financial Crimes Enforcement Conference* (Dec. 10, 2019), https://www.fincen.gov/news/speeches/prepared-remarks-fincen-director-kenneth-blanco-delivered-american-bankers.
[50] NDAA § 6204(b)(2)(D).
[51] *Id.* § 6204(c).
[52] *Id.* § 6210(a), (c).
[53] *Id.* § 6211(f).
[54] *Id.* § 6202 (adding 31 U.S.C. § 5318(g)(5)(D)(i)(I)).
[55] *Id.* § 6206 (adding 31 U.S.C. § 5318(g)(6)(C)).
[56] *Id.* § 6209(a) (adding 31 U.S.C. § 5318(o)(2)(A)).

subsidiaries, and affiliates" to facilitate more effective and efficient groupwide AML compliance.[57]

Designated Innovation Roles. To foster innovation and coordination with the private sector, the NDAA requires a BSAAG Subcommittee on Innovation and Technology. This Subcommittee will focus on reducing "obstacles to innovation" and will include "representatives of a cross-section of financial institutions subject to the [BSA]."[58] Additionally, FinCEN and each federal functional regulator must appoint an Innovation Officer who will work with financial institutions and technology providers to foster "innovative methods, processes, and new technologies that may assist in compliance with" BSA requirements.[59] Additionally, to advance outreach and collaboration further, the Secretary of the Treasury must convene an international financial crimes technology symposium that will include regulators, regulated firms, technology providers, and other experts.[60]

The NDAA requires FinCEN and banking agencies to launch initiatives that will take time. These requirements represent a critical step toward eventual important improvements to the BSA/AML compliance regime. However, proactive financial institutions may wish to consider establishing a financial crime innovation function. This office should ensure that efforts to apply new technologies to manage financial crime are well-conceived, well-documented, well-tested, and well-supported by data of sufficient quality. Such a proactive approach would help position financial institutions to both successfully apply new technologies to AML risk and successfully engage with their regulators about the application of new technologies.

III. Expanded Scope of BSA Coverage

The NDAA and recent regulatory action also broaden the scope of the BSA. Specifically, lawmakers and FinCEN are broadening the scope of the AML regulatory framework to account for convertible assets such as antiquities and cryptocurrencies—both of which can be misused for money laundering and other illicit purposes. These developments demonstrate the evolving nature of the AML landscape and indicate that financial institutions and other companies should remain up to date on their BSA/AML obligations with respect to different types of assets.

A. Antiquities

The NDAA amends the BSA to include antiquities dealers within the definition of "financial institution" subject to the act.[61] It also specifically directs the Secretary of the Treasury to issue proposed rules implementing the change within a year, taking into account factors such as the

[57] *Id.* § 6212(a) (adding 31 U.S.C. § 5318(g)(8)(B)(i)).
[58] *Id.* § 6207 (adding 31 U.S.C. § 5311(d)(2)(B), (3)(A)).
[59] *Id.* § 6208(a), (c)(1).
[60] *Id.* § 6211(b), (c).

[61] *Id.* § 6110(a)(1) (amending 31 U.S.C. § 5312(a)(2)(Y)). The NDAA directs the Secretary of the Treasury to coordinate with the Director of the Federal Bureau of Investigation, the Attorney General, and the Secretary of Homeland Security in "perform[ing] a study of the facilitation of money laundering and the financing of terrorism through the trade in works of art." *Id.* § 6110(c). The NDAA specifies that the study should include consideration of potential regulations for the art market. *Id.*

specific persons who should be subject to the rule, the value of the antiquities whose trade should be subject to regulation, and other related matters.[62]

B. Cryptocurrencies

Over the past few years, FinCEN and other agencies have increased the specificity with which they apply existing regulations to cryptocurrencies and have increasingly promulgated new rules to cover this rapidly evolving space.[63] This trend continued throughout 2020, during which the agencies emphasized AML obligations relating to cryptocurrencies. While these developments largely do not create "new" obligations for financial institutions and other businesses, they do apply existing requirements to certain transactions or dealings in cryptocurrencies. Secretary of the Treasury Janet Yellen, who was confirmed on January 26, is expected to advocate further regulation of cryptocurrencies and other financial technologies. In her Senate confirmation hearing testimony, Secretary Yellen noted that the Treasury Department should consider regulations to "curtail[] [cryptocurrencies and other digital assets'] use for malign and illegal activities," such as financing of terrorism and money laundering. Such regulations would continue the recent trend focusing on misuse of cryptocurrencies.

1. OCC Enforcement Action

In January 2020, for example, the OCC brought its first known enforcement action against a bank for AML failures related to cryptocurrency customers.[64] And in May 2020, FinCEN Director Ken Blanco delivered remarks emphasizing the agency's focus on financial crimes involving cryptocurrencies. Director Blanco noted that the agency "expect[s] each financial institution to have appropriate controls in place based on the products or services it offers, consistent with the obligation to maintain a risk-based AML program," and that the agency is "taking a close look at the AML/CFT controls [regulated entities] put on the types of virtual currency [they] offer."[65]

2. FinCEN Regulatory Changes

In September 2020, FinCEN issued a final rule regarding the BSA requirements applicable to banks that lack a federal functional regulator, including state-chartered non-depository trust companies.[66] The rule sets minimum standards for those institutions' AML programs and requires them to

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[62] *Id.* § 6110(b).
[63] FinCEN has been publishing guidance regarding cryptocurrencies since at least 2013. *See, e.g.*, FIN-2013-G001, Application of FinCEN's Regulations to Persons Administering, Exchanging, or Using Virtual Currencies (Mar. 18, 2013), https://www.fincen.gov/sites/default/files/shared/FIN-2013-G001.pdf.
[64] *See* Franca Harris Gutierrez, David S. Cohen, Zachary Goldman & Alina Lindblom, *Recent OCC Actions Focus Attention on Financial Crime Controls for Cryptocurrency Custody Businesses*, WilmerHale (Aug. 6, 2020), https://www.wilmerhale.com/en/insights/client-alerts/20200806-recent-occ-actions-focus-attention-on-financial-crime-controls-for-cryptocurrency-custody-businesses.
[65] Press Release, FinCEN, *Prepared Remarks of FinCEN Director Kenneth A. Blanco, delivered at the Consensus Blockchain Conference* (May 13, 2020), https://www.fincen.gov/news/speeches/prepared-remarks-fincen-director-kenneth-blanco-delivered-consensus-blockchain.
[66] Press Release, FinCEN, *FinCEN Issues Final Rule to Require Customer Identification Program, Anti-Money Laundering Program, and Beneficial Ownership Requirements for Banks Lacking a Federal Functional Regulator* (Sept. 14, 2020), https://www.fincen.gov/news/news-releases/fincen-issues-final-rule-require-customer-identification-program-anti-money.

establish customer identification programs and fulfill beneficial ownership requirements.[67] This rule heightens the compliance expectations for certain cryptocurrency companies because many cryptocurrency custody businesses take the corporate form of state-chartered non-depository trust companies.

On December 23, 2020, FinCEN published a significant NPRM, "Requirements for Certain Transactions Involving Convertible Virtual Currency or Digital Assets."[68] If adopted, FinCEN's proposed rule would require banks and money service businesses "to submit reports, keep records, and verify the identity of customers" that participate in certain transactions involving cryptocurrencies held in unhosted wallets or held in wallets hosted in certain jurisdictions to be identified by FinCEN.[69] In its notice, FinCEN notes that its proposed rule is motivated, in part, by the government's finding that "malign actors are increasingly using [cryptocurrency] to facilitate international terrorist financing, weapons proliferation, sanctions evasion, and transnational money laundering," as well as for other nefarious purposes such as ransomware attacks.[70] Although the window for the submission of comments regarding the proposed rule initially closed on January 7, 2021, FinCEN has since reopened the window, and extended the time for submission of comments;[71] it is therefore unclear whether the rule will be adopted and, if so, in what format.

If FinCEN adopts a rule similar to the one for which it provided notice, the impact on cryptocurrency businesses would be significant. In order to comply with this regulation, U.S.-based cryptocurrency exchanges would be required to build and implement technical systems for capturing the identity of their customers' counterparties in transactions involving unhosted wallets, as well as systems for fulfilling the new reporting requirements. This type of requirement is novel for the BSA. Even if FinCEN promulgates an amended rule, however, its focus on regulating cryptocurrencies will remain.

A few days later, on December 31, 2020, FinCEN issued a succinct notice, "Report of Foreign Bank and Financial Accounts ("FBAR") Filing Requirement for Virtual Currency."[72] In its statement, FinCEN announced its intention to amend the BSA regulations "regarding reports of [FBAR] to include virtual currency as a type of reportable account under 31 CFR 1010.350." As with the NPRM described above, this proposed amendment would subject the holders of virtual currency in foreign accounts to greater reporting requirements.

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[67] 85 Fed. Reg. 57,129 (Sept. 15, 2020), https://www.govinfo.gov/content/pkg/FR-2020-09-15/pdf/2020-20325.pdf.
[68] 85 Fed. Reg. 83,840 (proposed Dec. 23, 2020), https://www.govinfo.gov/content/pkg/FR-2020-12-23/pdf/2020-28437.pdf.
[69] *Id.* at 83,840–41. Although this alert uses the term "cryptocurrency," the regulation covers "transactions involving convertible virtual currency ('CVC') or digital assets with legal tender status ('legal tender digital assets' or 'LTDA')." *Id.*
[70] *Id.* at 83,841.
[71] Press Release, FinCEN, *FinCEN Extends Reopened Comment Period for Proposed Rulemaking on Certain Convertible Virtual Currency and Digital Asset Transactions* (Jan. 26, 2021), https://www.fincen.gov/news/news-releases/fincen-extends-reopened-comment-period-proposed-rulemaking-certain-convertible.
[72] FinCEN Notice 2020-2, Report of Foreign Bank and Financial Accounts (FBAR) Filing Requirement for Virtual Currency (Dec. 31, 2020), https://www.fincen.gov/sites/default/files/shared/Notice-Virtual%20Currency%20Reporting%20on%20the%20FBAR%20123020.pdf.

3. OCC Interpretive Letter

Finally, on January 4, 2021, the OCC published an interpretive letter announcing that national banks and federal savings associations are authorized to use "independent node verification networks" (*i.e.,* blockchain technology) and stablecoins (*i.e.,* cryptocurrencies whose value are pegged to fiat currency, other stablecoins, or commodities such as gold) to conduct payment activities.[73] In addition to constituting further evidence of the federal banking agencies' interest in financial technologies, the OCC's letter implies that the agency views cryptocurrencies and the blockchain networks on which they operate as "new technological means of carrying out bank-permissible payment activities"[74]—that is, banks continue to play an intermediary role, "facilitating the flow of money and credit among different parts of the economy," but may leverage new technological developments to do so.[75]

As the OCC notes in its letter, however, the use of new technologies carries unique benefits as well as AML risks. While blockchain technology and cryptocurrencies can achieve efficiencies in payment activities, such as increased resiliency and speed, banks that choose to serve as nodes on blockchain networks or use blockchain networks or stablecoins to facilitate payment activities must be attuned to the risks inherent in those activities. As the OCC describes, these risks include money laundering by bad actors, cross-border transfers, and reporting and recordkeeping challenges.[76] Yet these risks are not insurmountable, and the OCC recognizes that "banks have significant experience with developing BSA/AML compliance programs to assure compliance with the reporting and recordkeeping requirements of the BSA and to prevent such usage of their systems by bad actors."[77]

IV. Conclusion

Financial institutions are well aware that this is an exciting, but uncertain, time in AML. We expect AML compliance to remain a top risk facing financial institutions and a top regulatory and law enforcement priority in the new Administration. Financial institutions should be sure to keep abreast of the significant changes occurring. And financial institutions, collectively or individually, should engage in the rulemaking and reform process to enhance compliance efficiencies and effectiveness for all stakeholders.

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[73] OCC Interpretive Letter 1174, OCC Chief Counsel's Interpretation on National Bank and Federal Savings Association Authority to Use Independent Node Verification Networks and Stablecoins for Payment Activities (Jan. 2021), https://www.occ.treas.gov/news-issuances/news-releases/2021/nr-occ-2021-2a.pdf. The OCC also published two significant interpretive rules regarding cryptocurrencies in 2020. *See* OCC Interpretive Letter 1170, Authority of a National Bank to Provide Cryptocurrency Custody Services for Customers (July 2020), https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2020/int1170.pdf; OCC Interpretive Letter 1172, OCC Chief Counsel's Interpretation on National Bank and Federal Savings Association Authority to Hold Stablecoin Reserves (Oct. 2020), https://www.occ.gov/topics/charters-and-licensing/interpretations-and-actions/2020/int1172.pdf.
[74] *Id.* at 4.
[75] *Id.* at 2, 3 ("Over time, banks' financial intermediation activities have evolved and adapted in response to changing economic conditions and customer needs. Banks have adopted new technologies to carry out bank-permissible activities, including payment activities.").
[76] *See id.* at 8–9.
[77] *Id.* at 9.

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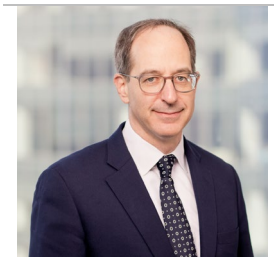

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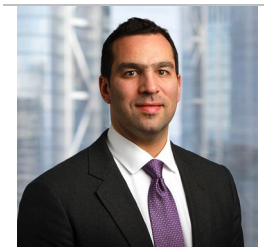

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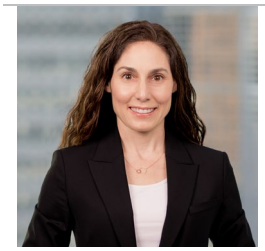

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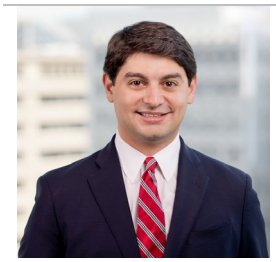

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