

SENATE CAUCUS ON INTERNATIONAL NARCOTICS CONTROL

HEARING ON “MONEY LAUNDERING AND BULK CASH SMUGGLING ACROSS THE SOUTHWEST BORDER” – MARCH 9, 2011

QUESTIONS FOR THE RECORD FROM

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Questions for Jamal El-Hindi, Associate Director Regulatory Policy, Financial Crimes Enforcement Network

1. Regulations for Prepaid Access Cards

Prepaid access cards are useful tools that can be used for a number of applications such as fare cards, employee payroll cards or as gift cards. Unfortunately, criminals use prepaid access cards to facilitate money laundering. Moreover, prepaid access cards are not federally regulated which makes it easier for criminals to perpetuate crime. The Financial Crimes Enforcement Network (FinCEN), a component within the Department of Treasury, has developed their Notice of Proposed Rule Making (NPRM) for prepaid access cards. The proposal would address issues such as establishing requirements for sellers of prepaid access cards and holding “providers” of prepaid access cards responsible to regulations. However, to date, these rules have not been enacted and criminals continue to take advantage of this legal and regulatory vacuum.

According to the GAO’s testimony, regulatory gaps exist for dealing with prepaid access devices, such as stored value. We have heard from GAO that this gap in regulatory authority has allowed criminals to circumvent laws and facilitate money laundering via these devices.

Questions:

- Do you believe prepaid access cards should be subject to the Bank Secrecy Act regulations and if so, why has it taken so long for the Department of Treasury and/or FinCEN to issue these regulations?

Prepaid access cards currently are subject to Bank Secrecy Act (BSA) regulations in two principal respects. First, U.S. depository institutions involved in the issuance or use of prepaid access are subject to comprehensive BSA regulation, and have been for many years.¹ Second,

¹ The FFIEC Bank Secrecy Act/Anti-Money Laundering Examination Manual states (2010 edition at page 235): "Each relationship that a U.S. bank has with another financial institution or third party as part of a prepaid card program should be governed by an agreement or a contract describing each party’s responsibilities and other relationship details, such as the products and services provided. The agreement or contract should also consider each party’s BSA/AML and OFAC compliance requirements, customer base, due diligence procedures, and any payment

with respect to *non-bank* prepaid access products, however, BSA implementing regulations currently impose more limited regulatory requirements as part of money services business regulations applicable to issuers, sellers, and redeemers of stored value.

In June 2010, as part of a planned regulatory update and in response to the statutory requirement in Section 503 of the Credit Card Accountability Responsibility and Disclosure (CARD) Act of 2009, FinCEN proposed a more comprehensive regulatory framework for non-bank prepaid access.

FinCEN's proposed regulations would make providers and sellers of prepaid access subject to a broad range of BSA regulations including, implementation of an anti-money laundering program, suspicious activity reporting, customer identification recordkeeping, transactional recordkeeping requirements, and registration by providers. FinCEN is working urgently to finalize these regulations, after careful consideration of more than 75 public comment letters.

The number and extent of public comments received in response to FinCEN's June 2010 Notice of Proposed Rulemaking NPRM underscores that prepaid access is a complex issue, with particular implications for financial inclusion and small businesses. In this rapidly developing field, we believe it is especially important that we strike the right balance between the government's efforts to encourage financial inclusion of the unbanked and the need for increased transparency for law enforcement. On these complex issues, we have been consulting with the Department of Homeland Security (DHS) and other law enforcement stakeholders, the regulatory community, and other administration stakeholders with intersecting authorities.

network obligations. The issuing bank maintains ultimate responsibility for BSA/AML compliance whether or not a contractual agreement has been established."

- Do you define prepaid access cards as monetary instruments even though they do not meet that standard as defined by Title 18 U.S.C. § 1956?

The definition of monetary instrument under Title 18 is not applicable to the term as it is used in the BSA. Monetary instrument is, however, specifically defined in 31 U.S.C. § 5312(a)(3) for purposes of the BSA.² In this regard, while prepaid access devices are not currently defined as monetary instruments in FinCEN regulations under 31 CFR Chapter X,³ we believe there is sufficient statutory authority under the BSA to include them within the regulatory definition of monetary instruments as appropriate.

- Do you believe that traditional gift cards are a risk for use in money laundering schemes and evading financial transparency given that criminals often purchase them with stolen credit cards?

FinCEN believes that gift cards can present money laundering risks. FinCEN's June 2010 NPRM proposes requirements designed to mitigate the risks presented by both closed loop prepaid access products (for example, a card that can be used only at a specific merchant) and open loop prepaid access products (for example, a card that can be widely accepted in payment networks).

Closed-loop prepaid access, the use of which is limited to the purchase of goods or services, generally falls outside the parameters of the rulemaking proposal. As stated in the NPRM, the

² Section 5312(a)(3) defines "monetary instrument" to mean:

(A) United States coins and currency;

(B) as the Secretary may prescribe by regulation, coins and currency of a foreign country, travelers' checks, bearer negotiable instruments, bearer investment securities, bearer securities, stock on which title is passed on delivery, and similar material; and

(C) as the Secretary of the Treasury shall provide by regulation for purposes of [sections 5316](#) and [5331](#), checks, drafts, notes, money orders, and other similar instruments which are drawn on or by a foreign financial institution and are not in bearer form.

³ 31 CFR 1010.100(dd) defines "monetary instruments" to include:

- Currency;
- Traveler's checks in any form;
- All negotiable instruments (including personal checks, business checks, official bank checks, cashier's checks, third-party checks, promissory notes (as that term is defined in the Uniform Commercial Code), and money orders) that are either in bearer form, endorsed without restriction, made out to a fictitious payee (for the purposes of §1010.340), or otherwise in such form that title thereto passes upon delivery;
- Incomplete instruments (including personal checks, business checks, official bank checks, cashier's checks, third-party checks, promissory notes (as that term is defined in the Uniform Commercial Code), and money orders) signed but with the payee's name omitted; and
- Securities or stock in bearer form or otherwise in such form that title thereto passes upon delivery.

effort required to use closed-loop products for the placement, layering or integration of funds makes them unattractive and unlikely vehicles for moving large sums of money efficiently. However, the NPRM also sets forth that closed-loop providers could be subject to the BSA implementing rules under the proposal where risk factors warrant. FinCEN received a number of comment letters strongly advocating for more limited regulation of closed loop providers, notwithstanding continuing concerns expressed by the law enforcement community with respect to these products. The final rule will address these comments and concerns.

Open loop prepaid access generally falls within the parameters of the rulemaking proposals. The proposal included limited exemptions for open loop prepaid access meeting certain threshold and use restrictions based on the reduced money laundering/illicit finance risks posed by low-dollar-value open loop prepaid access products.

- These closed end gift cards are often used to purchase items for sale in other locations to integrate unlawfully obtained proceeds into legitimate businesses. So in your view, these cards don't represent a potential problem for money laundering?

As stated in the June 2010 NPRM, and in the preceding answer, FinCEN believes that closed loop prepaid access can present money laundering risks, and the potential risk of money laundering varies based on the characteristics of the closed loop prepaid access. In cases where closed-loop prepaid access is limited in usability (for example, prepaid access whose use is restricted to a particular merchant, such as a coffee chain), the risk is lower. Our attempts to achieve a balanced approach on closed loop led us to propose rules that would be triggered if the prepaid access product could be used internationally or if other persons and non-depository sources had access to and could transfer the value of the funds. These triggers generated substantial comment. Other options for regulatory triggers include size limits on individual closed loop accounts.

- Associate Director El-Hindi, do you support requiring providers of prepaid access cards to register as Money Services Businesses (MSB)? If so, do you also support requiring providers of prepaid access cards to maintain records for subpoena requirements as well as requiring providers to file currency transaction reports (CTRs) to FinCEN for transactions in currency greater than \$5,000?

FinCEN supports registration, recordkeeping, and currency transaction reporting requirements for providers of prepaid access. The June 2010 NPRM proposes requirements associated with all of these provisions as detailed below:

- Registration: The June 2010 NPRM proposes to require non-bank providers of prepaid access to register with FinCEN as money services businesses, and to identify each prepaid program for which they are the providers of prepaid access.

- Recordkeeping: The June 2010 NPRM proposes to require providers of prepaid access to maintain transactional records and customer identifying information for a period of five years.
 - Currency Transaction Reporting: The June 2010 NPRM proposes to define providers of prepaid access as both “money services businesses” and “financial institutions,” which would subject providers of prepaid access to FinCEN’s currency transaction requirements for transactions in currency exceeding \$10,000 in one day – which is the current threshold for all financial institutions that file CTRs. However, FinCEN has not proposed a lower currency transaction reporting threshold of \$5,000 for providers of prepaid access.
- Your agency was required by the CARD Act to issue regulations no later than 270 days after the Act was signed into law. That means regulations should have been published by February of last year. How much of a factor have the objections from industry been in the delay of the regulation?

As FinCEN works to finalize its proposed regulation related to prepaid access, we are balancing a variety of interests that have been brought to our attention by stakeholders, including industry, regulators, and law enforcement, though we would not characterize all comments received from industry as expressing objection to the proposed regulation. In fact, industry comments presented diverging views on the best way to proceed. In total, FinCEN received more than 75 comments representing viewpoints from depository institutions, prepaid access program managers, service providers, industry trade associations, retailers, state and federal governments, private individuals and others. As varied were the sources, so were the opinions offered. We have carefully read, catalogued and analyzed the information provided to us and have used it to inform our efforts to finalize the regulation.

Furthermore, the comments received from FinCEN’s June 2010 NPRM underscore the fact that prepaid access has implications on financial inclusion and small business, and it is important that we strike the right balance between the government’s efforts for financial inclusion of the unbanked and the need for increased transparency for law enforcement. On these complex issues, we have been consulting with DHS and other law enforcement stakeholders, the regulatory community, and other administration stakeholders with intersecting authorities.

- The proposed rule that was published kicks the can down the road on cross-border transport of prepaid access, why not address it now?

FinCEN’s top rulemaking priority is to finalize the NPRM on prepaid access as expeditiously as possible, making appropriate changes based on the comments received during the rulemaking process. By defining prepaid access and imposing BSA requirements on certain participants, the final rule will create the foundational definitions and impose the infrastructure necessary to

provide for effective future rulemaking related to prepaid access, including the international transport of prepaid access.

FinCEN's plan is to address the issue of requirements for prepaid access, including those established by the CARD Act, in phases. Specifically, in the June 2010 NPRM, we explained that we intend to engage in a rulemaking on reporting the international transport of prepaid access, and solicited comments from the public on any aspect of the international transport of prepaid access. We are working on a border declaration regulation, and intend to finalize as soon as possible.

- Your agency told GAO in October that it would update its plans and identify targeted dates of a phased rulemaking. What are those dates? When will your agency issue final regulations on cross-border transport of prepaid access, which was the clear intent of Congress in passing the amendment to the CARD Act?

FinCEN has identified prepaid access as the top rulemaking priority for Fiscal Year 2011, and the revised prepaid access management plan that FinCEN developed in response to the GAO's recommendation sets a target for finalizing FinCEN's June 2010 NPRM by the end of Fiscal Year 2011. FinCEN continues to give this rulemaking top priority, and although we are mindful of the challenges that can arise in the clearance of any significant rulemaking, such as prepaid access, we are accelerating our efforts and will finalize this important regulation as soon as possible..

With respect to the international transport of prepaid access, FinCEN understands and appreciates the importance of establishing a border reporting regime for the international transport of prepaid access. While FinCEN is expediting the process of preparing an NPRM, and has begun consulting with our law enforcement colleagues on a draft, it would be premature to project a specific date for issuing a final rule until a NPRM has been further developed. As noted above, however, it is our intention to issue an NPRM on a cross-border transport reporting requirement as contemporaneously as possible with the issuance of the final prepaid access rule.

- Do you believe the revolving door of employees leaving the Department of Treasury for the financial industry has played any factor in the delay in implementing this regulation?

FinCEN does not consider employee turnover to have played any factor in the timing of our rulemaking efforts related to prepaid access.

2. Global Efforts to Combat Money Laundering

Combating the global money laundering schemes that support the drug trade requires the cooperation of not just one nation or two nations that share a border, but of all nations.

This is an effort that requires constant vigilance and a true commitment from every nation.

However, some nations may not be able or willing to combat these drug trafficking organizations or their practices effectively. This may stem from corruption or a lack of desire to deal with this issue within the host nation. Further, some countries may go so far as to not share any intelligence or misuse intelligence we share with them for unauthorized purposes. For example, FinCEN had to suspend sharing sensitive information with Argentina in 2009 because of concerns that the information was being put to improper uses.

Money Laundering is a global problem and international organizations have estimated that as much as \$1 trillion in illicit proceeds is transferred globally annually. Corruption is probably the single greatest factor in allowing illegal activity to occur. Corruption isn't uncommon in our own country but it is especially prevalent in a number of countries that we call partners in combating drug trafficking, money laundering, and terrorism.

Questions:

- In your opinion, how big of a problem is corruption in Mexico? Particularly, among Mexican law enforcement agencies?

Within the last five years, FinCEN has developed a close working relationship with its Mexican counterpart and maintains a robust relationship with the Mexican government. FinCEN is fully aware of reports of corruption; however, corruption has not adversely affected our cooperative relationship with the Mexican government.

- How does it affect, or undermine, our country's efforts to combat money laundering and the drug trade when nations are not taking the necessary internal actions to support our shared effort?

Regarding the effect that corruption has on law enforcement investigations, we defer to law enforcement.

- How does not being able to share intelligence with uncooperative nations, impact the ability to work with foreign governments to combat the money laundering schemes that finance the drug trade?

FinCEN is a member of the Egmont Group of Financial Intelligence Units (FIUs). FIUs have unique authority under the laws of each jurisdiction that is represented in the Egmont Group to share financial and other information that may be sensitive or otherwise subject to a range of legal restrictions and protections, with a known counterpart, in furtherance of specific law enforcement investigations and under common understandings as to appropriate use, limits on

dissemination, and protection for this information. As such, FinCEN shares intelligence with countries that are part of the Egmont Group, including Mexico. Not being able to share intelligence with uncooperative nations impairs FinCEN's ability to obtain vital tactical information for U.S. law enforcement. Within the Egmont Group several countries (not including Mexico) are non-responsive and U.S. law enforcement has indicated their frustration with regard to the negative impact on investigations.