



Rising to the Challenge — Staying Ahead of the AML Curve

How to Survive a Merger – The AML Perspective

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The views and opinions expressed here are those of the speaker. They do not represent an official position of the Federal Reserve Bank of Richmond or the Federal Reserve System.



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Panel Objectives:

- Understanding the legal requirements to enter into a merger or acquisition
- Importance of the BSA Officer's role early on in the due diligence process
- Considerations for consolidating core data into AML monitoring systems

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The Impact of BSA/AML Compliance on Mergers and Acquisitions



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Why BSA/AML Compliance Matters

- Regulatory Obligations
 - Policies and Procedures
 - Training
 - Monitoring
- Examination & Audit Obligations
- Fines and Penalties for Non-Compliance
- **The Least Known but Sometimes Most Important: Determines approval for mergers and acquisitions**



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Why it Matters

- Section 327 of USA PATRIOT Act
- Regulators "*shall take into account*" BSA/AML Compliance
 - "11. MONEY LAUNDERING- In every case, the responsible agency, shall take into consideration the effectiveness of any insured depository institution involved in the proposed merger transaction in combating money laundering activities, including in overseas branches." (USA PATRIOT Act 2001, § 327).



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BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM
WASHINGTON, D. C. 20551

DIVISION OF BANKING
SUPERVISION AND REGULATION
DIVISION OF CONSUMER
AND COMMUNITY AFFAIRS
SR 14-2
CA 14-1
February 24, 2014

Why it Matters

TO THE OFFICER IN CHARGE OF SUPERVISION AT EACH FEDERAL RESERVE
BANK AND TO FINANCIAL INSTITUTIONS SUPERVISED BY THE FEDERAL
RESERVE

SUBJECT: Enhancing Transparency in the Federal Reserve's Applications Process

Compliance with the Bank Secrecy Act

As discussed in SR letter 02-8, "Implementation of Section 327 of the USA Patriot Act in the Applications Process," the Federal Reserve is required to consider an organization's effectiveness in combatting money laundering activities in its evaluation of certain applications and notices. As part of the application review process, Federal Reserve staff considers the primary supervisor's assessment of the organization's compliance with the Bank Secrecy Act and its anti-money laundering program. Bank Secrecy Act compliance and anti-money laundering programs with significant program violations and/or deficiencies that have resulted in the issuance of a formal or informal enforcement action generally are considered to be less than satisfactory. Proposals from financial institutions with less than satisfactory Bank Secrecy Act and anti-money laundering compliance programs face substantial barriers to approval and generally have not received favorable consideration.



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The Federal Reserve Board

Testimony of Herbert A. Biern

Senior Associate Director, Division of Banking Supervision and Regulation
The Bank Secrecy Act and the USA Patriot Act
Before the Committee on International Relations, U.S. House of Representatives
November 17, 2004

The Federal Reserve Board's Position

- "The Federal Reserve has had a longstanding practice of considering an applicant's compliance with federal law, including anti-money laundering laws and regulations, in evaluating various applications, including applications for bank mergers and acquisitions of insured depositories [...]. The Patriot Act memorialized our practice in the application area and required the Board to take into account the effectiveness of an applicant's anti-money laundering compliance program when it considers applications under various laws."
- "Board staff has on some recent occasions **advised banking organizations considering expansion or other activities requiring the filing of applications with the Federal Reserve to concentrate instead of enhancing their anti-money laundering or other federal law compliance programs.**"



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Effects on Banks

- **Case Study: M&T Bank**
 - In 2012, M & T Bank proposed a merger with Hudson City Bank. In April 2013, however, "the Federal Reserve detected loopholes in M&T Bank's efforts to fight money laundering and put the acquisition on hold." (Zacks 2015) The issues identified by the Federal Reserve were discrepancies with the procedures and processes regarding the Bank Secrecy Act. The merger was delayed several times. The Federal Reserve "issued a written agreement to M&T, requiring adoption of a 'firm-wide compliance risk management program'." (The Capital Forum 2015)
 - Eventually, M&T's compliance with BSA/AML was deemed satisfactory, and the merger was approved in late 2015 (a 2-year delay). To the Federal Reserve, the most important aspect of a merger is that "it will result in a solid institution." (The Capital Forum 2015)



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Effects on Banks

- **What we learn from M&T Bank**
 - BSA/AML compliance will be closely reviewed by regulators
 - If it is not addressed before the merger, you will face significant delays while the issues are resolved
 - Banks contemplating mergers or acquisitions need to understand this risk and address shortcomings proactively. No one wants a two-year delay in a merger
 - If this is an issue, it is not the end. It can be fixed through close cooperation with the bank's regulator

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Mergers and Acquisitions – Why is it important that the BSA Officer have a seat at the table?

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2014 FDIC Atlanta Region Conference Call:

- Evaluate BSA/AML/Fraud risks of the target institution when considering a merger or acquisition
- **BSA review should be part of your due diligence process, similar to loan review**
- Develop a plan and timeline to incorporate the other bank's BSA Program into your own program
- Acknowledge and plan for additional customer due diligence and enhanced due diligence after the acquisition (i.e. CIP – how to handle going forward, what information will be updated within the customer records and when)

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Knowing what to review during the due diligence phase

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- Use Risk Assessment as the guide
- Create a tracking method to determine what's needed (i.e. Excel doc) and determine criticality – at what stage is it most important to know which information (i.e. Regulatory Exam and/or Audit results)
- Document the review indicating any points of concern

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What information should be shared?

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- Signing of NDAs are normally the first step during the initiation of a due diligence phase. Once signed, the banks share information as appropriate.
- The following information is essential to performing a risk assessment and should be reviewed.
 - # and types of High risk customers – names aren't always provided during the due diligence phase.
 - Volume of CTRs and SARs (customer names for each are not normally shared until an agreement has been signed; however this is where it's extremely important to include information in the agreement, if possible, whether or not the bank will accept the problem accounts/customers.)
 - Review of Programs, policies as applicable, which will initiate questions
 - Copies of internal/external audits and regulatory exam reports



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Vendor Considerations Regarding Mergers/Acquisitions

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Core System Compatibility



Target FI Systems

- Which Core/Teller systems? Compatibility?
- What other systems feed into their monitoring solutions?
- Customizations?



Converting Target to your Core

Merge to 'single institution' or maintain separately?

- If single, strategy for handling duplicates?
- How do they collect/tag data for monitoring?
- Beneficial Ownership?

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Monitoring/Reporting Systems



Target FI Systems

BSA/Fraud monitoring and/or Reporting?

- Do current solutions provide adequate coverage or are there holes you need to fill?
- Fill now or after consolidation?

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Pre Consolidation

How will you accomplish monitoring/reporting on ***common customers*** before core/vendor integration?

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Program Consolidation/Tuning



Target Assessment

Holes in their current program?

- Prior exam findings
- Based on your current program
- Based on your knowledge of their risk

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Covering the Gap

How do you identify customer, account, activity differences going forward on your system to cover their monitoring needs?

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Meeting Standard Needs

Do you need to tune existing parameters when you incorporate their customers' activity?

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Independent Assessment

Does the assessment of their risk identify any holes in your own program?

- Does your vendor offer solutions?

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Vendor Migration Considerations

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In House or Data Center

- Hardware/Capacity
- Duplicate Test Environment
- Single/Multi-Institution Environment
- User Security Needs

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Historical Mapping

- Customer, Institution, Branch #s
- Product Codes/Account Types/Codes/Tags...

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Historical Migration

- Historical CTR/SAR Filings
- Options for migrating prior investigations/notes...

Takeaways:

- **Proactivity is KEY! You don't want AML surprises halfway through a merger or acquisition**
- **Ensure the BSA Officer is a part of the Due Diligence team and effort**
- **Be proactive to ensure key pieces aren't being lost or missed during consolidation and conversion!**



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QUESTIONS????