

## **Despite Regulatory Clarity, AML Errors Persist in Mortgage Lending Six Years On** *by: Michael Barone, Esq.*

The U.S. Department of the Treasury, through the Financial Crimes Enforcement Network (FinCEN) issued a final rule in February 2012 requiring non-bank residential mortgage lenders and brokers to establish anti-money laundering (AML) programs and to report suspicious activities under the Bank Secrecy Act (BSA). The BSA is designed to alert law enforcement of criminal and terrorist activity. The BSA requires U.S. financial institutions (including non-bank residential mortgage lenders/brokers) to assist U.S. government agencies in detecting and preventing money laundering.

Despite the issuance of this final rule more than six years ago, many non-bank mortgage lenders/brokers are not complying with the requirements of the BSA, and as a result, regulators are beginning to take note in their examinations.

A compliant AML program for a residential mortgage lender/broker includes: (i) designating a competent individual to serve as the company's BSA/AML Compliance Officer; (ii) conducting an AML Risk Assessment; (iii) drafting and implementing written internal policies and procedures; (iv) establishing an ongoing training program; and (v) conducting an independent audit of the company's AML program every 12-18 months. An AML program must also include the maintenance of a "Red Flags" program and a Customer Identification Program, the filing of Suspicious Activity Reports (SARs), when required, and compliance with Section 314 of the U.S. Patriot Act and Office of Foreign Assets Control (OFAC) Regulations.

Most mortgage broker companies have designated a BSA/AML Compliance Officer and have an AML policy and procedure in place; however, many companies do not comply with one or more of the other AML requirements.

For example, more often than not, mortgage broker companies are not conducting an AML Risk Assessment. This needs to be completed at least every 12 to 18 months, and companies should be modifying identified activities based on their operations and growth. The Risk Assessment should consider the current and future state of items such as the company's size, products, customer base and geographic area of operation. The Conference for State Bank Supervisors (CSBS) has issued a tool to assist mortgage companies in completing such risk assessments. This tool can be found at: <https://www.csbs.org/bsa-aml-self-assessment-tool>. The New York State Department of Financial Services (DFS) is citing mortgage brokers on examinations for not having a Risk Assessment. AML should be one component of these risk assessments.

Another BSA requirement that is frequently lacking or unfulfilled is on-going training. Mortgage broker companies must train their personnel at least annually in all applicable aspects of AML regulations. A best practice is to provide AML training to all new employees within 30 days of hire.

All AML training needs to be adequately tailored to a company's operations. For example, mortgage companies should specifically train their personnel on the types of suspicious activity and "red flags" they are likely to come across, such as mortgage fraud related items.

Finally, companies must document their training programs by maintaining training and testing materials, the dates of training sessions and attendance records. Companies that are not conducting this annual training should immediately do so as examiners are consistently verifying that such training was completed.

Another aspect mortgage brokerage companies seem to be overlooking is independent testing/audits. While the specific nature of the testing will be somewhat dependent on the company's size and risk profile, the AML audit can be performed by an independent third party or an employee of the company, **provided** the employee has no role whatsoever in the AML functions being tested and possesses enough knowledge of BSA regulations to be qualified to perform the audit. Once again, the DFS is citing mortgage brokers on examination for not having completed such an audit.

By far, the area of most non-compliance by mortgage broker companies pertaining to AML requirements is with regard to the filing of SARs. FinCEN highlights the importance of SAR filing by indicating that mortgage companies are the, "primary providers of mortgage finance ... and are in a unique position to assess and identify money laundering risks and fraud."

A SAR requires basic company information, information about the individuals involved and information about the suspicious activity or transaction. FinCEN requires all filings to be submitted electronically through its website.

Many companies are of the view that transactions are only reportable if they involve currency. Not only is this view incorrect, it's also quite risky. While many of the requirements for the filing of a SAR involve currency, there is also a requirement for a transaction to be reported if a mortgage company knows, suspects or has reason to suspect that a transaction involves the use of the loan or company to facilitate criminal activity.

Given this, mortgage companies must file a SAR every time they suspect fraud – whether it is income, employment, occupancy or some other type of fraud. If a mortgage broker company has not filed any SARs in the past six years, it could be sign that the company does not have a compliant AML program or a weak one for that matter.

Given the substantial civil and criminal penalties set forth in the statute and the significant increase in state examination questions related to AML items, it is recommended that mortgage brokers take a long, hard look at their AML programs and ensure all requirements are properly satisfied.