



August 28, 2006

Mary F. Rupp  
Secretary of the Board  
National Credit Union Administration  
1775 Duke Street  
Alexandria, VA 22314

RE: Comments on Notice of Proposed Rulemaking (Suspicious Activity Reports)

Dear Ms. Rupp:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents the interests of our nation's federal credit unions (FCUs), I am responding to the National Credit Union Administration's (NCUA) proposed rulemaking and request for comments concerning the requirements for reporting and filing a Suspicious Activity Report (SAR). Specifically, the proposal amends 12 CFR Part 748 to include greater detail about the requirements for reporting and filing a SAR, and to provide fundamental information about the process in a single location. The proposed changes would also provide consistency with the SAR regulations established by the other Federal Financial Institutions Examination Council (FFIEC) regulators and would extend to credit unions the banks' practice of notifying boards of directors of SAR filings.

NAFCU commends the agency's effort to increase clarity and consistency in its SAR regulations. Greater uniformity with the other SAR regulations would increase efficiency and help foster compliance; as such, NAFCU generally supports the proposed changes. We are not convinced, however, that notification of the board of directors should be required by regulation at this time. Relative to this, NAFCU would like to submit the following specific comments.

#### **Notification to the Board of Directors**

Section 748.1(c)(4)(i) of the proposal would impose on credit unions a new internal control requirement by requiring notification of the board of directors of SAR filings. This provision is purportedly meant to formalize a practice that is common

among banks, and to bring NCUA's regulation in line with the other FFIEC regulators' regulations.

Notification of the board is not statutorily required by the Bank Secrecy Act (BSA), nor is it imposed by regulation under Treasury's BSA rule, 31 CFR 103.18. As such, NAFCU does not believe that board notification for credit unions should be required by formal regulation at this time. Because the board of directors is charged with oversight over the credit union's BSA compliance, most credit unions are already voluntarily informing their boards of directors of SAR filings. NAFCU does not believe that it is necessary to formalize this already common practice through regulation.

If however, NCUA concludes that the board notification provision should be retained in the final rule, NAFCU suggests that further clarification is necessary. Proposed § 748.1(c)(4)(i) requires "prompt notification" of the board of directors (or appropriate board committee) of "any SAR filed." The proposed rule, however, does not define either of these terms, nor does it mandate any specific format for the board notification. Thus, it is unclear whether periodic aggregate reporting would be sufficiently "prompt", or whether the notification of "any SAR filed" would require actual copies of each SAR to be furnished to the Board.

The 2006 FFIEC BSA/AML Examination Manual notes that because the banking regulations do not mandate a particular notification format, banks should have flexibility in structuring their format. Indeed, under the guidance, banks are permitted (but not required) to provide actual copies of SARs, or to provide summaries, tables of SARs filed for specific violation types, or any other form of notification that would provide the board with adequate information to fulfill its fiduciary duties.

NAFCU believes that the same standard applies to credit unions and recommends that the final rule clarify that credit unions have flexibility in meeting the board notification requirement.

### **Suspect is a Director or Committee Member**

The proposed rule also prescribes specific requirements for SARs involving a board or board committee member. *See* proposed 12 CFR 748.1(c)(4)(ii).

As discussed above, NAFCU does not believe that board notification should be required by formal regulation. If however, the agency decides to retain this provision in the final rule, NAFCU recommends that, at minimum, subsection (ii) be removed. NAFCU member credit unions indicate that in only exceedingly rare circumstances would it be necessary to file a SAR in connection with activity involving a board member. In fact, based on anecdotal evidence, NAFCU is wholly unaware of any such occurrence.

Requiring board notification of a SAR where the suspect is a board or committee member could also have a potentially adverse affect on board governance. Activity that warrants the filing of a SAR is suspicious, but not necessary unlawful. Oftentimes, the activity is in reality innocuous but a SAR is nonetheless warranted. Informing directors of a SAR involving a fellow board member could nevertheless lead to mistrust, uncertainty, and skepticism within the board, thereby disrupting board relations and possibly interfering with the discharge of the board's fiduciary duties.

Further, only two of the four other FFIEC regulators' regulations include a specific provision for board notification of SARs involving a director or committee member. *See* 12 CFR 21.11(h) (OCC); 12 CFR 563.180(d)(9) (OTS). Neither the Federal Reserve Board's regulation, 12 CFR 208.62, nor the Federal Deposit Insurance Corporation's regulation, 12 CFR 353.3(f), contains a parallel provision. Accordingly, NAFCU does not believe that proposed subsection (ii) is necessary and recommends that it be excluded from the final rule.

Should subsection (ii) be retained in the final regulation, NAFCU suggests that further clarification be provided by the agency. Under the proposal, no specific format is mandated for notification of the board of directors where the credit union files a SAR and the suspect is a director or committee member. In these circumstances, the proposal simply states that the credit union may not notify the suspect, but must notify "all directors who are not suspects."

NAFCU believes that this provision lacks sufficient clarity. Read plainly, the proposed provision requires that each member of the board, other than the suspect-director, must be notified of the SAR involving the board member. However, it is unclear whether, for example, an actual copy of the SAR must be provided to the other board members, or whether a SAR involving a board member could merely be included as part of a summary, table, or other type of aggregated report. Like proposed § 748.1(c)(4)(i), greater detail about the required format for the notification is necessary.

The manner in which the other board members should receive such notification is also unclear. Because the credit union would be prohibited from notifying the suspect-director of the SAR, notification of the other directors could be very difficult. Indeed, even if steps are taken to avoid disclosure to the suspect, the procedure itself could alert the unscrupulous director of the existence of the SAR. Because the suspect-director would presumably be well aware of the notification procedure, any deviation from that procedure could itself alert the suspect to the report.

Furthermore, proposed § 748.1(c)(4)(ii) is somewhat inconsistent with guidance contained in the 2006 FFIEC BSA/AML Examination Manual. In a footnote, page 68 of the guidance states:

As noted in the Bank Secrecy Act Advisory Group's *The SAR Activity Review – Trends, Tips & Issues*, Issue 2, June 2001, "In the rare instance

when suspicious activity is related to an individual in the organization, such as the president or one of the members of the board of directors, the established policy that would require notification of a SAR filing to such an individual should not be followed. Deviations to established policies and procedures so as to avoid notification of a SAR filing to a subject of the SAR should be documented and appropriate uninformed senior organizational personnel should be so advised.”

The guidance directs financial institutions filing SARs involving a board member to “deviate” from “established policies and procedures,” and to advise “appropriate uninformed senior organizational personnel” of these deviations. Yet the proposed regulation expressly requires notification to “all directors who are not suspects.” Thus, it is unclear whether, in the event that a SAR involves a director or committee member, notification should be made through senior management personnel. It is also unclear whether credit unions should have an established set of procedures for suspicious activity involving a director (which, again, the suspect-director would be aware of and could therefore signal the suspect to the existence of a SAR) or whether a credit union should, on a case-by-case basis, simply “deviate” from its established notification policy in any way that would avoid notification to the suspect. NAFCU believes that if subsection (ii) is retained in the final rule, greater detail about the method of providing this notice should be included in the final regulation.

NAFCU would like to thank you for this opportunity to share its comments on this proposed rulemaking. Should you have any questions or require additional information please call me or Pamela Yu, NAFCU’s Associate Director of Regulatory Affairs, at (703) 522-4770 or (800) 336-4644 ext. 218.

Sincerely,



B. Dan Berger  
Senior Vice President of Government Affairs

BDB/pwy