FinCen’s Final Rule: “Customer Due Diligence Requirements for Financial Institutions”

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Welcome and Introductory Remarks

Laurie Kelly, CAMS
Compliance Officer, CoBank

Andrew Jacob, CFP
Chief Reg., Legislative & Compliance Officer CoBank
Regulatory Panel

Considerations for Implementing New Customer Due Diligence Requirements

Moderator: Micah Schwalb, Esq., Partner, Roenbaugh Schwalb

Panelists:
Cynthia Santiago, CFE, CAMS
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- **FinCEN’s** Final Rule on *minimum* CDD requirements and *existing* CDD requirements
- Observed practices for initiating the *design and implementation of solutions* to meet heightened CDD requirements
- FDIC’s observations regarding *sound practices* for identifying Beneficial Owners
• FDIC’s **expectations** regarding BSA/AML compliance reviews for 2016 and 2017
• Where to look for **evolving CDD guidance**
• FDIC’s **preferred point-of-contact** for CDD queries during the Implementation Period: Case Manager
Securities-Related Items
SEC Guidance:

- **SEC Policy Statement on Obtaining and Retaining Beneficial Ownership Information for AML Purposes** (issued in 2010 jointly with FinCEN, CFTC, and federal bank regulators)  

- **SEC’s AML Source Tool for Broker Dealers**  
  www.sec.gov/about/offices/ocie/amlsource-tool.htm

- **SEC’s AML Source Tool for Mutual Funds**  
  www.sec.gov/about/offices/ocie/amlmfsource-tool.htm

- **Andrew Ceresney’s 2015 speech on AML and SARs**  

- **Kevin Goodman’s 2015 speech on AML compliance**  
Recent SEC Enforcement Actions:

• Albert Fried & Co: *Failure to file SARS*

• E.S. Financial Services: *Failure to comply with CIP rules*
  www.sec.gov/litigation/admin/2016/34-77056.pdf
FINRA Guidance:

FINRA’s AML page:  www.finra.org/industry/aml

Recent FINRA Enforcement Actions:

• Raymond James: *Failure of firm and AMLCO to implement adequate AML procedures*

• Aegis Capital: *Failure to investigate red flags and file SARs*
Q & A

Regulatory Panel
Law Enforcement Panel

The Customer Due Diligence Context and Schemes for Hiding Beneficial Owners

**Moderator:** Robert L. Goecks, CAMS, CPA, MBA
Co-Chair, ACAMS Colorado Chapter

**Panelists:**
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Special Agent-in-Charge
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Internal Revenue Service, Criminal Investigations
David A. Thompson, CAMS
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The Customer Due Diligence Context
Financial Action Task Force (FATF)

• FATF is an inter-governmental policy-making body that sets standards and promotes effective implementation of legal, regulatory and operational measures for combating money laundering, terrorist financing and other related threats to the integrity of the international financial system.

• FATF’s “Recommendations” are the accepted international anti-money laundering and counter-terrorist financing (AML/CFT) standards

• Recommendation 10, Customer Due Diligence, states in part that CDD measures to be taken include: “Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the financial institution is satisfied that it knows who the beneficial owner is.”

• To ensure effective implementation of its Recommendations, FATF conducts Mutual Evaluations of its member nations every ten years

• The third FATF Mutual Evaluation of the United States was conducted in 2006
The 2006 FATF Mutual Evaluation evaluated **two items related to beneficial ownership:**

- Item 33. Legal persons – Beneficial Owners
- Item 34. Legal arrangements – Beneficial Owners

The 2006 FATF Mutual Evaluation Report assigned a final rating of **non-compliant (“NC”)** for both items related to beneficial owners.

**FATF comments** included in part: "Company formation procedures and reporting requirements are such that the information on beneficial ownership of legal persons may not, in most instances, be adequate, accurate or available on a timely basis.”
The Customer Due Diligence Context
Financial Action Task Force (FATF) – cont’d

• A contributing complication for the U.S. is that FATF’s Mutual Evaluations focus on the national level while U.S. entity creation (LLC’s etc.) occurs at the state level

• The federal government does not have the authority to force states to tighten their company formation laws and processes

• To address this issue the federal government is using its authority to regulate financial institutions in order to implement FATF’s CDD Recommendations related to identification of beneficial owners

• FATF’s 2016 Mutual Evaluation of the United States has just concluded and their report is expected to be finalized at the Plenary session in October 2016
Cindy Hearn
Special Agent
Internal Revenue Service
Criminal Investigations
The Customer Due Diligence Context
U.S. Treasury Department’s Proposed Legislation

Beneficial Owner Legislation - companies formed within the United States would be required to file beneficial ownership information with the Treasury Department, and face penalties for failure to comply.

Foreign-Owned Single-Member LLC Proposed Regulations - would require foreign-owned “disregarded entities,” (i.e. entities that have no obligation to report information to the IRS or to get a tax identification number) - including foreign-owned single-member limited liability companies (LLCs) - to obtain an employer identification number (EIN).
The Customer Due Diligence Context
U.S. Treasury Department’s Proposed Legislation – cont’d

• U.S. Immigration and Customs Enforcement (ICE), Homeland Security Investigations (HSI), and Internal Revenue Service Criminal Investigations (IRS-CI) have long recognized the misuse of corporations, shell corporations and limited liability companies (LLCs) formed under State law as a serious threat to the ongoing effort to combat international criminal activities

• A handful of U.S. states offer company registrations with cloaking features, such as minimal information requirements and limited oversight, which rival those offered by offshore financial centers

• Delaware, Nevada, and Wyoming are often cited as the most accommodating jurisdictions in the United States for the organization of these legal entities
Case Studies

**Homeland Security Investigations** (HSI) received a request from an Eastern European country seeking information on two U.S. companies registered in Wyoming.

- The companies were suspected of undervaluing several shipments of canned seafood, allegedly shipped from the U.S.
- The request sought evidence of the companies’ existence, and for as much information as possible regarding corporate officers, business locations, business activities, and corporate formation documents.
The Customer Due Diligence Context
U.S. Treasury Department’s Proposed Legislation – cont’d

HSI discovered that both entities were “shell” companies, legally incorporated in the state of Wyoming.

• The addresses provided by both suspect companies on their import documents was that of the Wyoming incorporating agent.
• The Articles of Incorporation for the suspect U.S. companies indicated they were managed by a foreign firm in the Seychelles.
• The Articles of Incorporation for the Seychelles firm was signed by the Wyoming incorporation agent.

The investigation located no records for any additional business addresses, phone listings, or officers located in the United States. As a result, HSI was unable to comply with the foreign country’s request.

A Colorado HSI investigation involving international money laundering has identified dozens of corporations that have been established for the purpose of launder the proceeds of criminal activity – who are the beneficial owners?
The Customer Due Diligence Context
U.S. Treasury Department’s Proposed Legislation – cont’d

The Bank Secrecy Act states that its purpose is: “to require certain reports or records where they have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, [or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism]” (31 U.S.C. 5311)

Enhancements to Usefulness
• Lack of beneficial ownership information undermines law enforcement’s ability to link financial transactions to the underlying individuals engaged in the criminal activities and their network of money launderers and terrorist financiers
• Shell companies frequently have no physical presence other than a mailing address, employ no one, and produce nothing.
Enhancements to Usefulness cont’d

- In countless investigations, where the criminal targets utilize shell corporations, law enforcement’s inability to obtain beneficial ownership impedes the investigation
- Beneficial ownership information aids in identification of potential tax evasion
- Identifying beneficial owners facilitates compliance with Office of Foreign Assets Control (OFAC) regulations
Enhancements to Usefulness cont’d

• Special Agents trace the flow of assets through multiple layers and jurisdictions to those individuals that ultimately benefit from the crime using various investigative techniques to identify a beneficial owner.

IRS-CI uses the Form SS-4 “Application for Employer Identification Number” for evidentiary support in criminal investigations.

• January 2010: Form SS-4 is revised to require the name and social security number of the entity’s “responsible party”
• January 2014: Any entity with an EIN must now report a change in its “responsible party” by completing Form 8822-B within 60 days of the change
• The tax return information on the forms is protected by IRS Code Section 6103

IRS-CI also cooperates with foreign jurisdictions pursuing charges against non-US persons through our foreign attaches, tax treaties, Tax Information Exchange Agreements and Mutual Law Assistance Treaties
Example
A complex money laundering and tax investigation discovered a $685 million corporate Ponzi scheme. The CEO of this bottled water producer collapsed it in bankruptcy in late 2006. He then implemented an elaborate loan-fraud pyramid scheme to falsely inflate the sales and revenues of his company (which served as a front operation) to lenders and investors. The CEO’s wife and son also participated in the money laundering scheme, which involved the creation of numerous legal entities and arrangements to conceal the true ownership of these entities and illicit assets.

As a result of investigators’ access to adequate, accurate and current beneficial ownership information, the largest financial fraud scheme to take place in Western Pennsylvania was dismantled. The CEO pleaded guilty to one count of conspiracy to commit money laundering and was sentenced to 20 years’ imprisonment, to be served concurrently with the sentences imposed on him in related cases. In the related cases, he pleaded guilty to three counts of tax evasion and 24 counts of mail fraud. The wife and husband were sentenced to 4 years and 9 years, respectively, for their convictions on conspiracy to commit money laundering. Additionally, a criminal forfeiture proceeding was instituted against them in connection with conviction on the money laundering charges and approximately $2.8 million was forfeited to the United States.
Schemes for Hiding Beneficial Owners

• Current “friendly” jurisdictions may push back – Delaware, Nevada, Wyoming
• Wholesale clients – “correspondent accounts just got worse”
• OFAC tricks – “Everything old is new again”
• Existing client accounts that do not require identification of Beneficial Ownership will be in demand
• “If 25% ownership is the rule, then 24% ownership is the solution”
Audience Q & A

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Thank you for attending!

If you are not already an ACAMS Colorado Chapter Member: We invite YOU to join us!

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