



Rising to the Challenge — Staying Ahead of the AML Curve

WELCOME

BSA Coalition Webinar
March 14, 2017



Rising to the Challenge — Staying Ahead of the AML Curve

Beneficial Ownership – Preparing Your Front Line

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



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Opening Remarks:

Joe Soniat,
BSA Coalition Co-Sponsor
Vice President & BSA Officer
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Christi Burge, Moderator

*Assistant Vice President, Corporate BSA Officer
C&F Bank*

Jason Chorlins, Speaker

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Kaufman, Rossin & Company*

Kelly Gentenaar, Speaker

*Vice President/Deputy AML Officer
E*Trade Financial Corporation*



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Webinar Objectives

At the end of this webinar, participants will be able to:

- Explain the requirements of FinCEN's rule on customer due diligence/beneficial ownership; and
- List best practices for training your front line staff on the requirements of FinCEN's customer due diligence/beneficial ownership rule.



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Background on the CDD Rule and the Definition of a Legal Entity



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Background

The rule was designed to enhance financial transparency and safeguard the financial system against illicit use.

Key Precipitating Factors

- 2006 - FATF Rating – Partially Compliant with CDD standards related to beneficial ownership
- 2010 - Guidance Issued by FinCEN, the SEC and CFTC
- 2013 - US presented G-8 its Action Plan for Transparency of Company Ownership and Control
- Feb. 2015 – The Lagarde list was published which exposed suspected tax evaders
- April 2016 - Panama Papers list was published which exposed suspected tax evaders



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Definition of a Legal Entity

- The Rule defines a legal entity customer as:
 - A corporation
 - An LLC
 - A general partnership

Any other entity created by the filing of public document with a secretary of State or similar office

- The rule does not include:
 - Sole proprietorships
 - Unincorporated associations
 - Naturalized persons

*Note that general trusts are not included in the definition of a legal entity unless public filings are made.



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Description of the Beneficial Ownership Rule



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Beneficial Ownership Legislation

On May 5, 2016, FinCEN announced a Customer Due Diligence (CDD) Final Rule, proposed Beneficial Ownership legislation, and proposed regulations related to foreign-owned, single-member limited liability companies (LLCs). Rule becomes mandatory on May 11, 2018

Key Premises:

- The CDD Final Rule adds a new requirement that financial institutions – including banks, brokers or dealers in securities, mutual funds, futures commission merchants, and introducing brokers in commodities – **collect and verify the personal information of the real people** (also known as beneficial owners) **who own, control, and profit** from companies when those companies open accounts.
- Companies formed within the U.S. would be required to file beneficial ownership information with the US Treasury Department.



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Summary of Beneficial Ownership Legislation

Important Provisions and Comments:

- **Identify and verify the identity** of the beneficial owners or controllers of all legal entity customers (other than those that are excluded) **at the time a new account is opened**. It is **not required that verification** of the individual's **status** as a beneficial owner be obtained.
- The financial institution **may rely on the information provided** and is not required to investigate the items assuming there are no obvious signs of fraud and that the institution has no knowledge of facts that would reasonably call into question the reliability of information.
- Financial Institutions **are not required to obtain information directly from the beneficial owners** of a legal entity.
- In the case of documentary verification, the financial institution **may use photocopies** or other reproductions of the documents listed in the applicable CIP rule.



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Beneficial Ownership Legislation

What is collected:

- Name
- Address
- Date of Birth
- Social Security Number (or passport number/similar numerical identifier in the case of foreign persons)

Who it is collected from:

- Each individual, if any, who owns, directly or indirectly, 25 percent or more of the equity interests of the legal entity customer (e.g., each natural person that owns 25 percent or more of the shares of a corporation); and
- At least **one (1) or more individuals** with significant responsibility for managing the legal entity customer (e.g., a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer)



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Summary of Beneficial Ownership Legislation

Important Provisions and Comments:(continued)

- Financial institutions should **use beneficial ownership information as they use other information** they gather regarding customers (e.g., through compliance with CIP requirements), including for compliance with the Office of Foreign Assets Control (OFAC) regulations, and the currency transaction reporting (CTR) aggregation requirements.
- Information can be obtained via the **Certification Form** found in the published guidance or via a document created by the Financial Institution which obtains substantially the same information.



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CERTIFICATION OF BENEFICIAL OWNER(S)

Persons opening an account on behalf of a legal entity must provide the following information:

a. Name and Title of Natural Person Opening Account: _____

b. Name and Address of Legal Entity for Which the Account is Being Opened: _____

c. The following information for each individual, if any, who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, owns 25 percent or more of the equity interests of the legal entity listed above

Name	Date of Birth	Address (Residential or Business Street)	For U.S. Person: Social Security Number	For Foreign Persons: Passport No. and Country of Issuance or Other Similar ID No. ²

d. The following information for one individual with significant responsibility for managing the legal entity listed above, such as:

An executive officer or senior manager (e.g. Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, Treasurer, etc.); or

Any other individual who regularly performs similar functions.

(if appropriate, an individual listed under section (c) above may also be listed in this section (d))

Name/Title	Date of Birth	Address (Residential or Business Street)	For U.S. Person: Social Security Number	For Foreign Persons: Passport No. and Country of Issuance or Other Similar ID No.

I, _____ (name of natural person opening account), hereby certify, to the best of my knowledge, that the information provided above is complete and correct.

Signature: _____ Date: _____

² In lieu of a passport number, foreign persons may also provide an alien identification card number, or number and country of issuance of any other government issued document evidencing nationality or residence and bearing a photograph of similar safeguard.



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Assessing The Risk and Conducting Ongoing CDD



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The Risk and Ongoing CDD

- The CDD Rule amends the AML program requirements for each covered financial institution to explicitly require covered institutions to implement and maintain appropriate risk-based procedures for conducting ongoing customer due diligence, to include:
 - **Understanding the nature and purpose** of the customer relationships; and
 - **Conducting ongoing monitoring** to identify and report suspicious transactions and, **on a risk basis**, to maintain and **update customer information**.
- The **procedures must establish risk-based practices** for verifying the identity of each beneficial owner identified to the covered financial institution, **to the extent reasonable and practicable**.



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The Risk and Ongoing CDD

The Nature and Purpose:

- A customer risk profile refers to the information gathered about a customer at account opening used to develop a baseline against which customer activity is assessed for suspicious activity reporting.
- Information may be integrated into the financial institution's automated monitoring system and may be used after potentially suspicious transactions have been identified, as one means of determining whether or not the identified activity is suspicious.



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The Risk and Ongoing CDD

Ongoing Monitoring:

- When a financial institution detects information (including a change in beneficial ownership information) about the customer in the course of its normal monitoring that is relevant to assessing or reevaluating the risk posed by the customer, it must **update the customer information, including beneficial ownership information.**
- This provision **does not impose a categorical requirement** that financial institutions must update customer information, including beneficial ownership information, on a continuous or periodic basis. Rather, the updating requirement is event-driven and occurs as a result of normal monitoring.
- These requirements **represent a floor, not a ceiling**, and, consistent with the risk-based approach, financial institutions may do more in circumstances of heightened risk, as well as to mitigate risks generally.

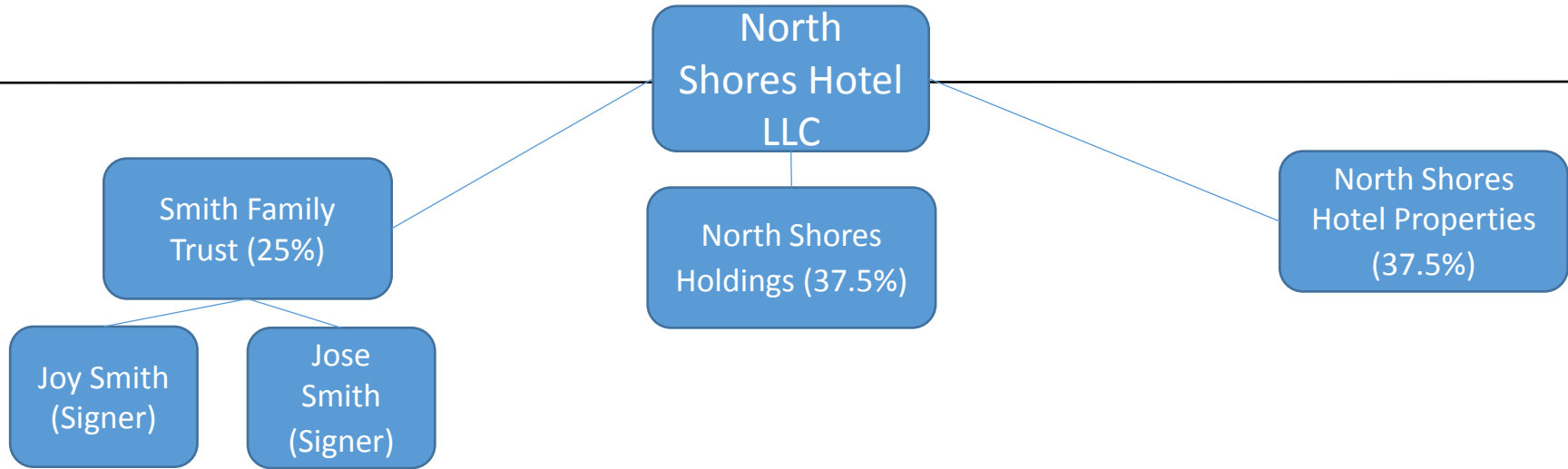


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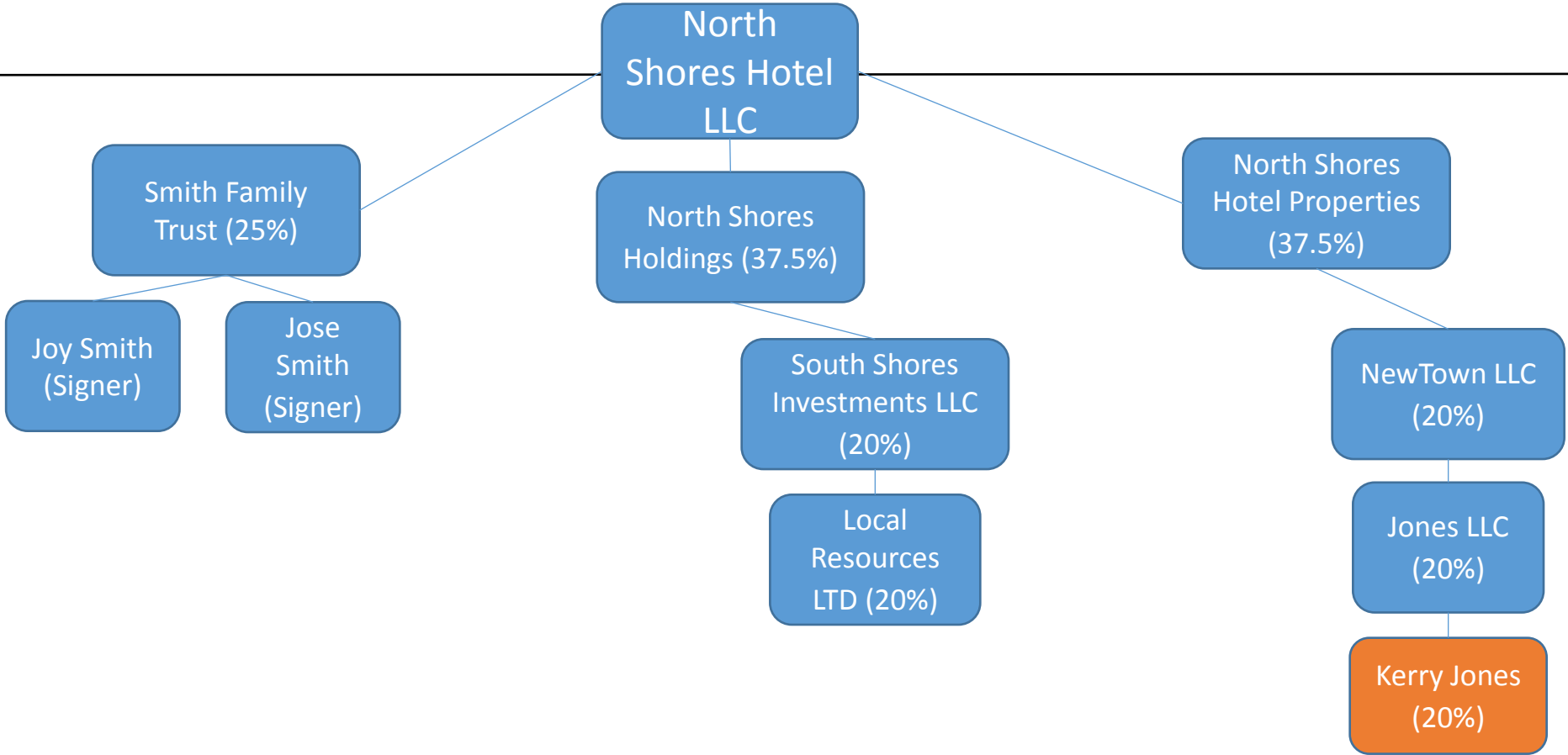
The Complexities of Beneficial Ownership



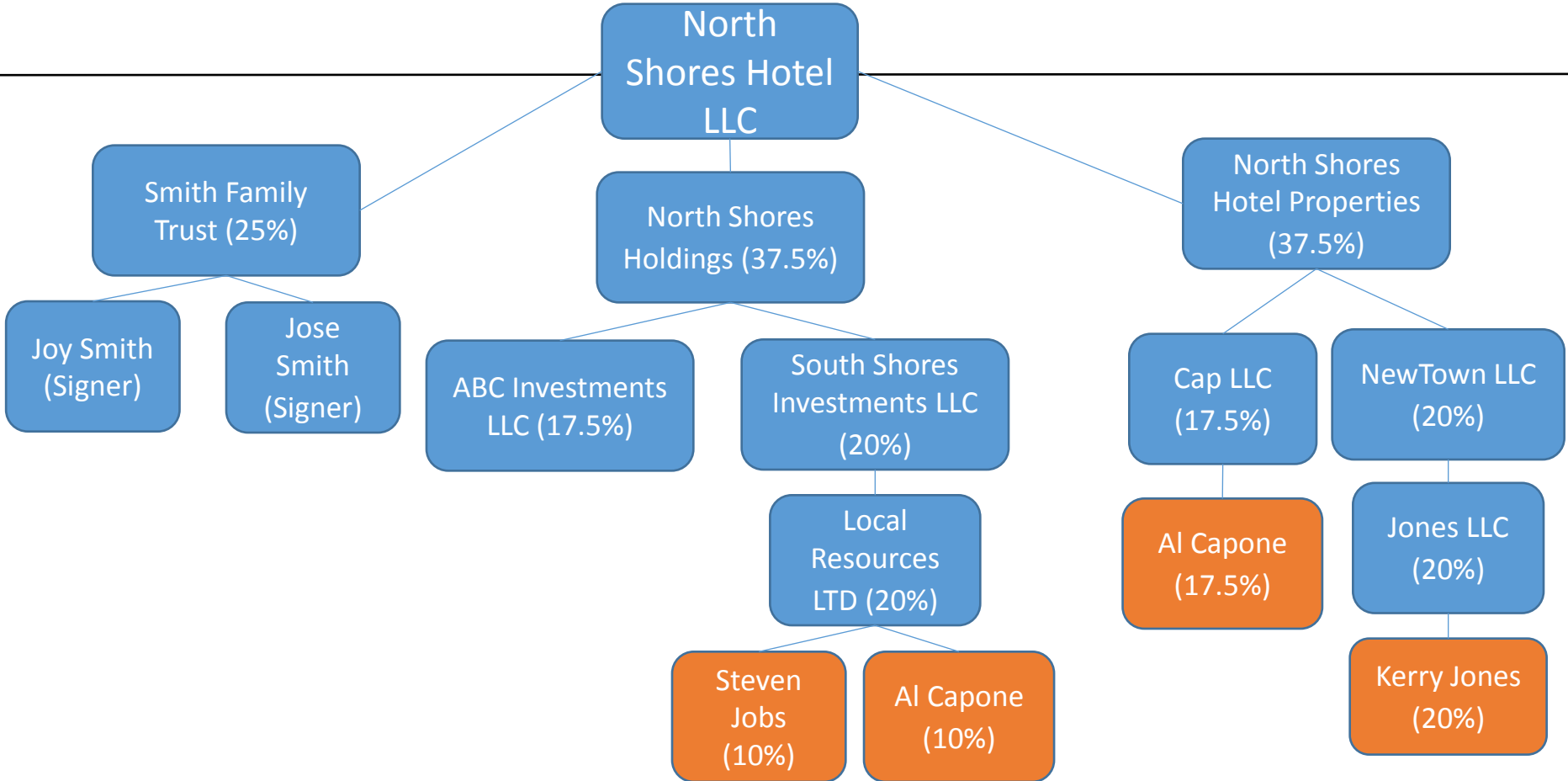
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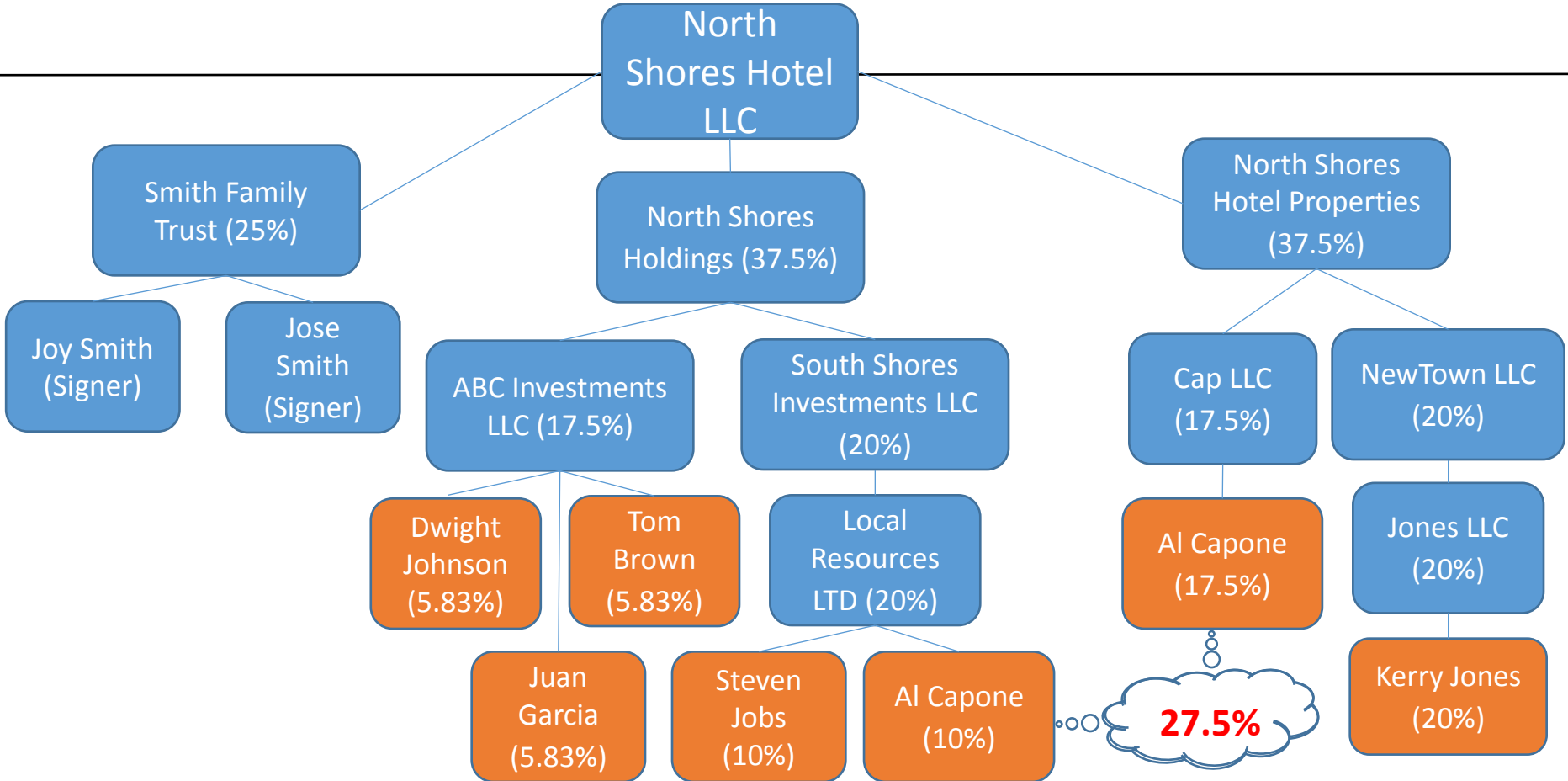
The Complexities of Beneficial Ownership



The Complexities of Beneficial Ownership



The Complexities of Beneficial Ownership





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The Complexities of Beneficial Ownership

Beneficial ownership information can be obscured through the use of:

- Shell companies (which can be established with various forms of ownership structures), especially in cases where there is foreign ownership which is spread across jurisdictions,
- Bearer Shares,
- Formal nominee shareholders and directors where the identity of the nominator is undisclosed,
- Informal nominee shareholders and directors, such as close associates and family, and
- Trusts and other legal arrangements which enable a separation of legal ownership and beneficial ownership of assets.
- Use of intermediaries in forming legal persons, including professional intermediaries (ex. Lawyers)



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Red Flags for Identifying High-Risk Legal Entity Customers

Potential Red Flags to look out for:

- Entities incorporated in various high risk geographies. Especially when the business is not involved in that area
- Foreign individuals of high risk geographies that own shares in a domestic company
- The client or representative opening the account on behalf of the client is unable to/or is reluctant in providing ownership information
- The use of shell companies, private investment companies, or trusts
- The use of a registered agent appears to be a nominee incorporation service provider
- A customer provides an invalid phone number
- The customer's background differs from that which would be expected on the basis of their business activities



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Training for Front Line Employees



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Training: Who, What, When, How?

Who to Train

Front Line includes:

- Lenders – train lenders separately
- Account Opening Employees

Back-Office includes:

- Operations
- Training
- Audit

Senior Management and the board of directors



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Training: Who, What, When, How?

What to Train

- Definitions are really important
- Your organization's approach to collecting and documenting beneficial information is important too
- Try to anticipate "what if scenarios," like What if the person opening the account for the legal entity does not know ownership percentages or who all of the beneficial owners are?



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Training: Who, What, When, How?

When to Train

- Senior Management
 - You need their buy in **now** if you haven't already
 - You will need to keep them apprised of your state of compliance as you go along
- Lines of Business – Quarter 4, 2017 and Quarter 1, 2018



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Training: Who, What, When, How?

How to Train

- Workshops
 - Tailored to Line of business
- Webinars
- Workflow/Handouts/Definition cheat sheets
- If your bank is of a certain size, consider a “train the trainer” approach
- Use examples in your training; have employees apply the rule to different scenarios



Definitions

Clearly define in your policies and procedures and training materials the following so that front line can identify them up front:

- Legal Entity
 - Looking for that space in between a publicly traded company and sole proprietor
 - Use examples that show how an organization's ownership can be obscured by showing them the [Delaware Secretary of State website](#) to show them what little information is publicly available.
- Beneficial Ownership
 - Clearly define the difference between **beneficiary** and **beneficial owners**
- Control Person
 - Ensure they understand that a control person may or may not have ownership. The rule itself contains many examples of titles.



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Definition Cheat Sheets

- Legal Entity
 - Does the customer have a pulse? If yes, not a legal entity subject to the CDD rule
 - Is the customer a publicly traded? If yes, not a legal entity subject to the CDD rule.
 - Is the customer a trust? If yes, generally not a legal entity subject to the CDD rule, but you might want to double check with your AML department.
- Beneficial Ownership
 - Who owns this entity in terms of shares of stock or membership in a limited liability corporation or partnership?
- Control Person
 - President, Executive Officer, Senior Manager



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Referral Processes or Exemptions

Establish as part of your training an open communication/communications protocol with your department:

- Dedicate an inbox to questions or use existing communication lines for questions referrals
- No matter how inconsequential the question, it's best to get it answered up front
- Define in your training materials the best point to involve your AML department prior to the opening of the account and the points where gray areas may arise. Examples:
 - Trusts
 - An Entity owning an Entity
 - A customer unwilling to provide beneficial ownership information (unwillingness would also indicate a red flag)



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Training Best Practices



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Best Practices for Training your Front Line

- Use a Beneficial Ownership Certification form
- Train the front line staff responsible for opening accounts on the importance of gaining a true understanding of the entity and its owners
- Use definition cheat sheets and examples to illustrate application of the rule
- Establish a communication protocol between AML and lines of business so that you can answer questions efficiently
- Establish a standard timeline for periodic review of existing client relationships
- Ensure that once new beneficial ownership information is collected, all affected accounts are updated accordingly
- Conduct research on the registered agent of the company
- Conduct research on the basic information of the entity (address, EIN, website, phone number)

Ultimately, it is up to the financial institution's risk appetite in the areas of Compliance, Legal, Reputational, and Credit risks as to how far the due diligence on the beneficial owners will go.



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In Summary

- The new CDD rule requires the identification of ownership greater than 25% and at least one controlling party when new accounts are opened on or after May 11, 2018.
- Verification of the individual's status as a beneficial owner is not required.
- Financial institutions are not required to obtain information directly from the beneficial owners of a legal entity.
- In the case of documentary verification, the financial institution may use photocopies or other reproductions of the documents listed in paragraph in the applicable CIP rule.
- The financial institution may rely on the information provided and are not required to investigate the items assuming no concerns related to deception exist for the Bank.
- The financial institution is required to implement and maintain appropriate risk-based procedures for conducting ongoing customer due diligence to understand the nature and purpose of the customer relationship and for conducting ongoing monitoring to maintain and update customer information.



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