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New Bank Secrecy Act Beneficial Owners Rule May 2017

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Overview

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- Background & Summary
- Beneficial Ownership Identification and Verification
- Beneficial Ownership Exclusions
- “Entities” and “Accounts”
- Account Exemptions
- Due Diligence Requirements
- Steps to Prepare for Final Rule

Background

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U.S. Department of State's Bureau of International Narcotics and Law Enforcement Affairs:

“A checklist of factors that contribute to making a country or jurisdiction particularly vulnerable to money laundering or other illicit financial activity...includes: ...

No requirement to disclose the beneficial owner of an account or the true beneficiary of a transaction”

Background

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- Drug Enforcement Agency (DEA)
 - Drug case trails often end in Delaware
 - No beneficial ownership disclosure requirement
 - Estimated \$65 billion of illicit money moved in U.S.
 - More public filings in Delaware than people
- “Panama Papers”
 - U.S. companies registered in another country or state with lower taxes
 - Registered agent dealt with intermediaries

Background

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- Los Zetas (Mexican drug cartel)
 - Used American companies to launder its profits
 - Bought racehorses
- Cali (Columbian drug cartel)
 - Used at least 105 American companies that accepted drug money for electronics, auto parts and other goods
 - Businesses were fronts for cartel
- Iranian government used American companies to evade sanctions

Background

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- Real estate purchased by foreign entities with money funneled through shell companies
 - Approximately \$104 billion from April 2014-March 2015
 - FinCEN Geographic Targeting Orders (GTO)
 - U.S. real estate title insurance companies must identify the natural persons behind shell companies used to pay all cash for high-end real estate in 6 major metro areas
- Real estate professionals exempt from suspicious activity reporting

Background

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- Global Witness investigation
 - Not-for-profit entity exposing corruption
 - 13 New York law firms approached about getting foreign money into the U.S. without detection
 - 12 of 13 provided advice (but no representation)
 - Anonymous trusts, using the law firm bank account, using the attorney to act as trustee of an offshore trust, using an American company

Background

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- Proposed HB 450: Incorporation Transparency and Law Enforcement Assistance Act of 2016
 - Would direct the U.S. Treasury to issue regulations requiring LLCs to file information about their beneficial ownership
 - Would provide minimal state disclosure requirements
 - Would impose civil penalties for those who lie
 - Most corporations would be exempt
 - Already regulated and those with more than 20 employees

Beneficial Ownership Rule

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- Purposes
 - Seeks to address weaknesses in financial system
 - Aids law enforcement investigations
 - Complies with international standards
- Compliance effective date: ***May 11, 2018***
- Two changes to the BSA:
 - Beneficial ownership identification and verification
 - Places due diligence expectations into the BSA/AML Compliance Program

Beneficial Ownership Identification & Verification

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- **General Rule:**

Written procedures reasonably designed to identify and verify the ***beneficial owner(s)*** of all legal ***entity*** members when they open an ***account...***

unless the member is excluded or the account is
exempted

Beneficial Ownership Identification & Verification

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- Included in BSA/AML Compliance Program
- Begins for new members on effective date
 - As well as during the course of monitoring
- Certification Form can be used to collect info, or by any other means that meet the requirement

Beneficial Ownership Identification & Verification

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- Members certify the accuracy of the information “to the best of their knowledge”
- CUs can rely on the information provided by the member – if the CU has no knowledge of facts to the contrary
- Signature notarization not required
 - FinCEN recognizes this may be appropriate for when docs are not delivered to the CU

Beneficial Ownership Identification & Verification

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- Verification procedures *similar to* your existing Member Identification Program
 - Can rely on copies of identity documents
 - Policies/procedures & communications should outline the types of copies that will/will not be accepted
- Verification – identity, **not** status as beneficial owner

Beneficial Ownership Identification & Verification

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- OFAC Requirements
 - Check names of beneficial owners against SDN List
 - Block or reject transactions conducted by one or more blocked persons who own more than 50% of the entity
 - Do not open accounts for an entity that is 50% or more owned by those on the List (even if the entity is not on the List)

What is a “Beneficial Owner”?

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- Each individual, if any:
 - Directly or indirectly owns **at least 25%** of the entity (**ownership prong**); and
 - A single individual with significant responsibility to control, manage or direct the entity (**control prong**)
 - Executive officer or senior manager

Beneficial Owners

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- Identify up to 4 individuals for the ownership prong
 - Could be zero
- Identify one beneficial owner for the control prong
- When dealing with an intermediary (attorney escrow accounts, broker-dealers, mutual funds and futures), treat the intermediary as the member, and not the clients

Beneficial Owner Exclusions

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- Regulated financial institutions
- Departments or agencies of the federal or state government
- Entities established by federal or state govt. that exercise govt. authority
- Entities on the NYSE or NASDAQ
- Entities 51% controlled by parent companies on NYSE or NASDAQ

Beneficial Owner Exclusions (cont.)

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- Issuers of securities required to file with the Securities and Exchange Commission (SEC)
- Entities registered with the SEC
- Entities registered with the Commodities Futures Trading Commission
- Public accounting firms registered under the Sarbanes-Oxley Act
- Bank/savings and loan holding companies

Beneficial Owner Exclusions (cont.)

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- Insurance companies regulated by a state
- Financial market utilities by the Financial Stability Oversight Council
- Foreign financial institutions (where the jurisdiction maintains beneficial ownership information)
- Legal entities that open private accounts for non-U.S. persons under FinCEN's private banking account rule

Beneficial Owner Exclusions (cont.)

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- Pooled investment vehicles operated or advised by a financial institution
 - **Record control prong** in the case of non-U.S. managed mutual funds, hedge funds and private equity funds
- Charities and Nonprofit Entities
 - Must still **record control prong**
 - Do NOT have to verify tax exempt status

What is an “Entity”?

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- Corporations, limited liability companies, partnerships, business trusts, or any entity that is created by the filing of a public document with the Secretary of State (SoS) or similar entity
- Does **NOT** include:
 - Sole proprietorships
 - Unincorporated associations (e.g., PTAs, Boy Scouts)
 - Trusts (those not filed with the SoS)

What is an “Account”?

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- Same as BSA definition
- Excludes accounts opened for the purpose of participating in an employee benefit plan established under the Employee Retirement Income Security Act of 1974

What Accounts are Exempted?

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- Private label credit card accounts
 - Co-branded cards NOT exempted
- Accounts established for the purpose of purchasing postage
- Commercial accounts to finance insurance premiums
- Accounts to finance the purchase or lease of equipment

Requirements for Exemption

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- Payments must be made directly to the third party
- No possibility of any cash refund to anyone

Record Retention

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- Records of any other related identifying information reviewed or collected - **5 years after the account is closed**
- No need to keep all Certification Forms (or substitutes) when changes are made

Due Diligence Requirements

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- Final rule moved expectations to requirements*
- Will be *required* to:
 - Understand the nature and purpose of relationship (for risk profile)
 - Monitor accounts and update information (and identify and report suspicious activity)

*Continue to treat these as requirements

Due Diligence: Amending Beneficial Owners

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- Updating beneficial ownership information and risk ratings are event-driven
 - **Not** required on a scheduled basis
 - During the course of normal monitoring
 - Suspicious activity detected

Due Diligence: Monitoring Accounts

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- Currency Transaction Report (CTR) Aggregation
 - Understanding when a transaction is “by or on behalf” of the entity
- FinCEN 314(a) – No need to report beneficial ownership information

Steps to Prepare for Final Rule

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- Amend BSA policy and procedures
- Decide whether to use model form or create a substitute
 - Create online form
- Decide what types of identification documents will and will not be accepted (e.g., resolution quality, faxed documents, etc.)
- Review and update BSA risk assessment
- Train staff on new requirements to obtain additional information regarding entities under the rule

Thank You for Participating!

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