

Managing High Risk Customers

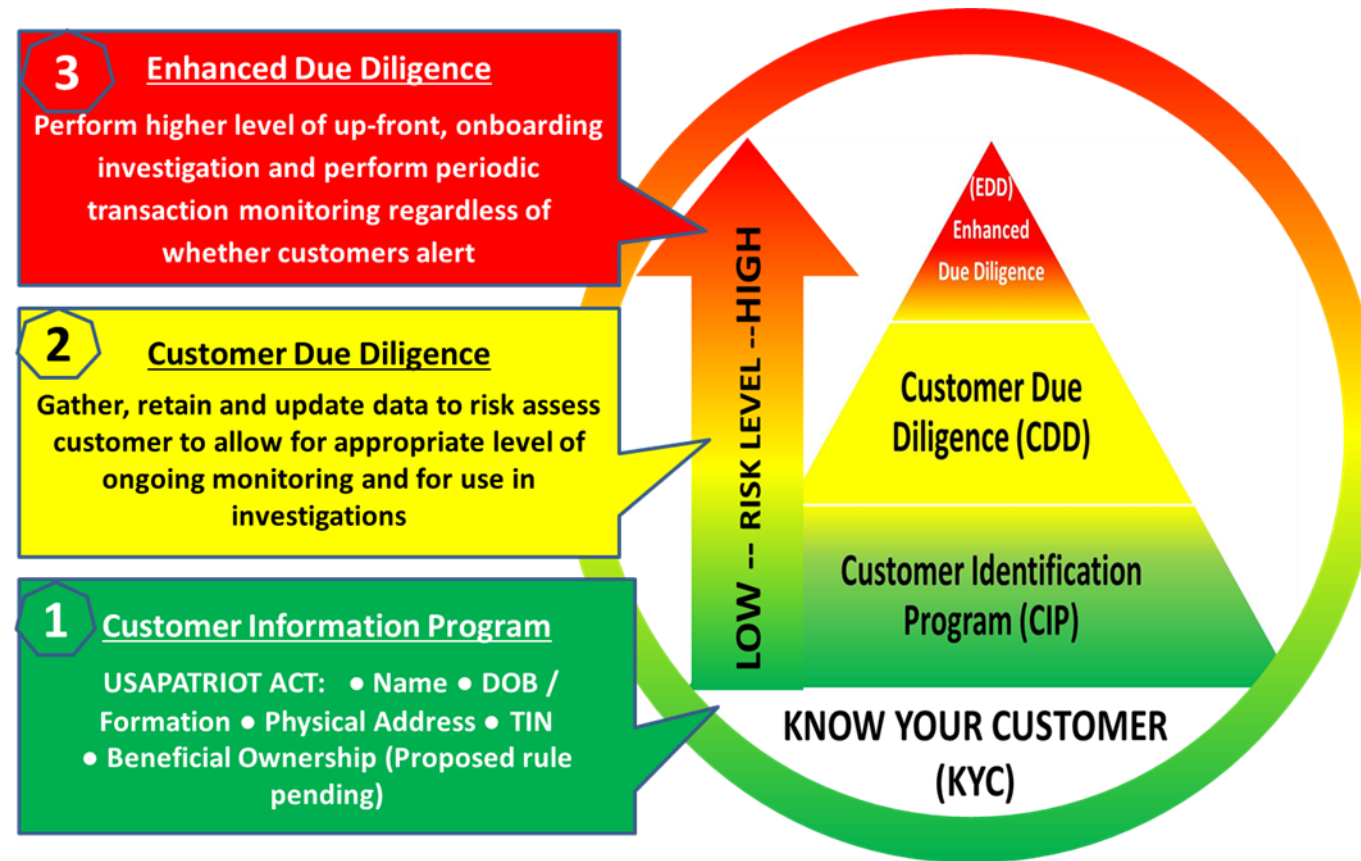
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Agenda

- Requirements of Managing HRCs
- Spotlight on ISIS/ISIL
- De-Risking MSBs
- Proposed Customer Due Diligence/Beneficial Owner

Managing HRCs at a Financial Institution



Requirements – Customer Identification Program (CIP)

- The CIP rule is designed to enable banks to form a reasonable belief that it knows the true identity of each customer.
- Banks must develop a program that includes a risk-assessment of their customer base and product offerings.
- Minimum required account opening identification includes:
 - Name
 - Date of birth for individuals
 - Address
 - Identification number

Requirements – Customer Due Diligence (CDD)

- CDD should be to enable the bank to predict with relative certainty the types of transactions in which a customer will engage.
- CDD starts with verifying the customer's identity and assessing the risks associated with the customer.
- For customers that pose an increased risk to the bank, due diligence should be enhanced.

Requirements – Enhanced Due Diligence (EDD)

- EDD for higher risk customer is especially critical in understanding anticipated transactions and implementing a suspicious activity monitoring system
- The bank should consider the following information on the customers:
 - Purpose of the account
 - Sources of funds/wealth
 - Beneficial ownership
 - Occupation/type of business
 - Banking references/financial statements
 - Geographical footprint
 - Description of operations

911 Hijackers – 911 Congressional Commission

- All opened branches one after the other at a busy branch. DDAs
- Shared same addresses and phone numbers, moved at same time.
- Activity included:
 - Wire transfers into the accounts from HR jurisdictions
 - Withdrawals were cash only – under any thresholds
 - Money was withdrawn from ATMs, one right after the other
- It cost only a few thousand dollars to buy plane tickets and box cutters.

ISIS/ISIL

Operates in large areas of land in Iraq and Syria (5-6 million people)

- Best funded terrorist group in history
- Funding is derived from within the territory under which they operate, not external sources - demanding portion of economic resources in the area and calling it charity
 - Bank looting –
 - Cash at state owned banks is considered “property” (est. 5 billion – US Treasury)
 - Cash at private banks is ‘taxed’ by ISIL upon withdrawal
 - Almost exclusively dinars, which makes foreign movement of funds difficult
 - Bank robberies
 - Human Trafficking – used to meet fighters demands vs real revenue source
 - Publication Al Dabiq
 - Selling women as slaves for about 13 USD
 - Real money is in the ransom – one woman’s family paid 3000 USD
 - Extortion of oil fields and refineries – looking to operate vs destroy (like Saddam Hussein did)
 - Biggest area of revenue
 - Long history of smuggling in the area – uses middlemen and smugglers
 - Acts like the mob and extorts the revenue from local users of oil and petroleum – relying on families owning oil fields
 - Unable to extract crude to full extent due to lack of expertise and equipment – however are able to rebuild them after air attacks (10 days and 230,000 USD)
 - Extort agriculture
 - Confiscating machinery and then renting it back to the farmers

ISIS/ISIL – operates in large areas of land in Iraq and Syria

- Smuggling historical artifacts, there are over 4500 UNESCO sites in the areas taken over by ISIL
- Extort money from Government employees in the area
- Kidnapping for ransom
 - Has killed hundred of individuals – we've seen the horrific video clips
 - Raised substantial revenue through this – estimate – 20 – 45 million USD (Treasury)
- Donations from non-profits – mostly foreign donors
- Material support from foreign terrorist fighters
 - As of December 2014, estimated 19,000 FTF from 90 countries (Tunisia, Saudi Arabia and Jordan – US in the middle @130) have left their home countries to join ISIL – great deal of cash smuggling that happens
- Fundraising through social media and networks
 - Al Itisam Establishment and the Al Hayat Media Centre – focus on distribution of ISIL propaganda through the Internet and other means
 - Use of Twitter is prolific with the hashtag all eyes on ISIS
 - Crowdfunding

ISIS/ISIL Use of FIs

- Most western banks have severed ties with banks in Iraq and Syria.
- Both governments are trying to prevent wire transfers to and from ISIL areas
- Expenses of ISIL are substantial
 - Each fighter gets 350 -500 USD/month
 - Est 20,000 – 30,000 fighters
 - 10 million drain on ISIL/month
 - In addition there are stipends for each member of the family of fighters
 - Benefits paid to the families of fallen or captured fighters

Risk Based Approach

- FinCEN Statement on Providing Banking Services to MSBs- Nov. 10, 2014
 - -MSBs play an important role
 - Banks can serve MSB industry and meet their BSA obligations
 - Concern that banks are indiscriminately terminating the accounts of MSBs or refusing to open them.
 - MSBs present varying degrees of risk; not all are high risk.
 - Risk assessment should include whether customer risks can be managed appropriately

FinCEN MSB risks

- Bank's due diligence should be = to level of risk presented by MSB as identified in bank's risk assessment
- Bank needs to understand MSB's business model and general nature of MSB's own customers, but does not need to know the MSB's individual customers to comply with BSA
- Same requirements as other business customers

OCC Statement of Risk Management

- Nov. 2014
- OCC does not direct banks to open, close or maintain individual accounts
- OCC does not encourage banks to terminate entire categories of customers without regard to risks presented and the bank's ability to manage the risks
- Bank should assess risks and implement controls to manage the risks

Banking MSBs

- Where additional due diligence is appropriate, may include:
 - analyzing MSB's policies, procedures, independent reviews and audits
 - transaction monitoring, including but not limited to amounts, volume, balances, chargebacks
 - site visits
 - training, knowledge of employees
- Could be a significant source of income

Proposed FinCEN Rule: Customer Due Diligence

- Aug, 2014
- Banks; brokers or dealers in securities; mutual funds; future commission merchants and introducing brokers in commodities (“Covered Entities)
- FinCEN noted possible interest in expanding to others, such as MSBs
- Would require the identification of “beneficial owners” of “legal entity customers” and verification of their identity
- “Legal entity customers” are those formed in a filing with a secretary of state or other applicable government agency

Proposed Customer Due Diligence Rule

- “Beneficial ownership” of a “legal entity customer” is a 2 prong test:
 - “ownership prong” is met if individual has a 25% or more equity interest in the legal entity
 - “control prong” is met by individuals exercising significant responsibility to control, manage, or direct the legal entity.
- Either prong triggers identification and verification –FinCEN wants identity of natural persons as opposed to other legal entities who own or control “legal entity customers”

Proposed Customer Due Diligence Rule

- To verify identity of “beneficial owner” FinCEN proposed use of a standard form asking individuals opening such accounts to provide certain information and certify the veracity of the information
- No specific timing requirement on updating such information, but it should be kept as current as possible
- Can rely on information in standard form under certain conditions
- Some exceptions from “beneficial ownership”, such as customer already exempt from CIP under current rule, certain publicly traded companies and government agencies, etc.

Proposed Customer Due Diligence Rule

- In addition to requiring the collection of “beneficial ownership” identification information, must understand the nature and purpose of the account and conduct ongoing monitoring to maintain and update customer information and report suspicious activity
- Need to update as bank becomes aware or changes