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FinCEN Issues Joint Release Providing Guidance on Obtaining and Retaining Beneficial Ownership Information

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The author explains the Financial Crimes Enforcement Network's joint release issued to clarify existing regulatory expectations for obtaining beneficial ownership information for certain customer accounts and relationships.

On March 5, 2010, the Financial Crimes Enforcement Network ("FinCEN"), along with other regulators, issued guidance to clarify existing regulatory expectations for obtaining beneficial ownership information for certain customer accounts and relationships (the "Joint Release"). As noted in the Joint Release, the requirement that a financial institution know its customers, and the risks presented by its customers, is basic and fundamental to the development and implementation of an effective Bank Secrecy Act ("BSA") and anti-money laundering ("AML") compliance program. Indeed, it is this knowledge that may assist the institution in identifying, detecting and reporting suspicious activity.

Most notably, the Joint Release clarifies that based upon the financial institution's evaluation of risk related to an account, financial institutions may need to identify the beneficial owners of an account. In an effort to encourage cost effectiveness, enhance efficiency and increase available relevant information to identify beneficial owners, the Joint Release

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also supports a financial institution's enterprise-wide efforts to identify and verify beneficial owners in accounts where appropriate. Therefore, the Joint Release serves as a reminder to financial institutions to revisit their BSA/AML compliance programs. Specifically, financial institutions should evaluate whether their processes for identifying customers who pose heightened money laundering or terrorist financing risks are appropriate and whether the financial institution's assessment of those risks should be enhanced.

Of course, the ability to ascertain the identity of beneficial owners of certain legal entities is no easy task. Indeed, the guidance provided in the Joint Release will not change those challenges. Certain individuals and business entities will continue to attempt to conceal the identity of the true owner of the asset or property. As noted in the Joint Release, this is especially apparent in situations where a financial institution deals with certain business entities, such as shell companies or other vehicles designed to conceal the nature and purpose of the illicit transactions and identities of individuals. The Joint Release provides financial institutions with basic guidance on the types of documents and information that they may want to obtain in order to identify and verify certain customer accounts and relationships. Yet, depending upon the financial institution's risk assessment of certain customer accounts and relationships, they may have to conduct enhanced due diligence. The Joint Release, however, provides minimal guidance to financial institutions in assessing what is adequate or appropriate enhanced due diligence. As a result, financial institutions are likely to continue to struggle in their assessments of what constitutes adequate and appropriate enhanced due diligence for certain customer accounts and/or relationships. Despite these challenges, the Joint Release reminds financial institutions that this information is not only valuable to the institution's ability to detect suspicious activity, but also may provide useful information to law enforcement.

CUSTOMER DUE DILIGENCE PROCEDURES

Financial institution BSA/AML compliance programs should have customer due diligence procedures that are reasonably designed to iden-

tify and verify the identity of beneficial owners of an account based on the financial institution's evaluation of the risk pertaining to an account. In particular, the Joint Release states that customer due diligence procedures should include such things as:

- Determining whether the customer is acting as an agent for or on behalf of another, and if so, obtaining information regarding the capacity in which and on whose behalf the customer is acting.
- Where the customer is a legal entity that is not publicly traded in the United States, such as an unincorporated association, a private investment company ("PIC"), trust or foundation, obtaining information about the structure or ownership of the entity so as to allow the institution to determine whether the account poses heightened risk.
- Where the customer is a trustee, obtaining information about the trust structure to allow the institution to establish a reasonable understanding of the trust structure and to determine who is the provider of funds and whether that provider has the power to remove the trustees.

When such heightened risk accounts are identified, financial institution procedures should subject the accounts to enhanced due diligence and the procedures should be reasonably designed to enable the financial institution to be in compliance with BSA requirements.

Private banking and foreign correspondent accounts are already subject to particular due diligence requirements relating to beneficial owners. The Joint Release, however, notes that certain trusts, corporate and shell entities, and PICs are further examples of customers that may pose heightened risk. In those latter instances, depending upon the risk level, the financial institution may need to take additional steps. In particular, the financial institution may have to identify and verify beneficial owners and reasonably understand the sources/uses of funds and relationship between the customer and its beneficial owner. Therefore, financial institutions that allow for these types of accounts should review their procedures to ensure that they are taking at least the steps identified in the Joint Release.

PRIVATE BANKING

The Joint Release also reminds "covered financial institutions" that, under FinCEN regulations, they are required to establish and maintain due diligence programs that include policies, procedures and controls reasonably designed to detect and report suspicious activity and money laundering conducted through or involving private banking accounts established, maintained, administered or managed in the United States. The failure of a covered institution to take reasonable steps to identify nominal and beneficial owners of a private banking account generally would be viewed as a violation of the requirements of 31 CFR 103.178.

The Joint Release provides that under FinCEN's regulations, a "covered financial institution" that offers private banking services must take reasonable steps to ascertain the source of the customer's wealth and anticipated activity of the account, the geographic location of the account, the customer's corporate structure, and public information about the customer. Furthermore, reasonable steps must be taken to identify nominal and beneficial owners of private banking accounts. Obtaining this beneficial ownership information in these accounts may require the financial institution to apply enhanced due diligence procedures to those accounts. The Joint Release, however, does not address the steps a financial institution may take when applying enhanced due diligence in these circumstances. One reason to review a private banking account relationship is to determine whether the nominal or beneficial owners are senior foreign political figures ("SFPF") for which special rules apply. Indeed, FinCEN regulations require that the covered financial institutions establish policies, procedures and controls that include reasonable steps to ascertain the status of a nominal or beneficial owner as a SFPF. In so doing, the Joint Release notes that procedures should include such things as obtaining information on employment status and sources of income, as well as consulting news sources and checking references where appropriate. Moreover, all SFPF accounts require enhanced due diligence reasonably designed to detect and report transactions that may involve the proceeds of foreign corruption.

FOREIGN CORRESPONDENT ACCOUNTS

The Joint Release also provides that covered financial institutions must establish appropriate, risk based, and where appropriate, enhanced due diligence procedures and controls that are reasonably designed to detect and report, any known or suspected money laundering activity conducted through or involving any correspondent account established, maintained, administered or managed in the United States for a foreign financial institution. The regulations also require enhanced due diligence for correspondent accounts established, maintained, administered or managed in the United States, for certain foreign banks.

As stated in the Joint Release, enhanced due diligence for correspondent accounts for such foreign banks should be risk based. There also should be a procedure for obtaining information from the foreign bank about the identity of the person with authority to direct transactions through any correspondent account that is a payable-through account and the source and beneficial owner of funds or other assets in a payable-through account. The Joint Release informs covered financial institutions that they may want to consider using a questionnaire or conducting a review of the transaction history for the respondent bank in collecting the required information.

FinCEN regulations also prohibit covered financial institutions from opening and maintaining correspondent accounts for foreign shell banks. In order to ensure that the account is not being used to indirectly provide services to foreign shell banks, covered financial institutions must identify the owners of foreign banks whose shares are not publicly traded. In addition, they have to record the name and address of a person in the United States that is authorized to be an agent to accept service of legal process. Notably, the Joint Release informs covered financial institutions that their failure to maintain records identifying the owners of non-publicly traded foreign banks could be viewed as violating the requirements of 31 CFR 103.177.

CONCLUSION

The Joint Release does clarify certain steps financial institutions must take to ensure that they meet their BSA/AML regulatory requirements when

obtaining and retaining beneficial ownership information for certain customer accounts and relationships. However, with respect to enhanced due diligence that financial institutions may have to address for certain customer accounts or relationships, the Joint Release provides only minimal guidance. Given that criminals, money launderers and terrorists will continue to exploit the privacy and confidentiality surrounding some business entities, financial institutions will continue to struggle with identifying and verifying beneficial ownership information for certain customer accounts and relationships. The Joint Release, however, presents a good opportunity for financial institutions to review and assess their risk based BSA/AML compliance programs relating to certain types of heightened risk customer accounts, private banking and foreign correspondent accounts.