

Focus on Anti-Money Laundering Enforcement at the SEC and FINRA

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Anti-Money Laundering Overview

- Bank Secrecy Act (“BSA”) / USA PATRIOT Act
- Financial Crime Enforcement Network (“FinCEN”) at the U.S. Treasury Department
- **Five Pillars of a Successful AML Program**
 - Policies, Procedures, and Controls
 - AML Compliance Officer
 - Independent Audit
 - Training
 - Customer Due Diligence



SEC and FINRA

- **The U.S. Securities and Exchange Commission (SEC) is responsible for examinations of registered broker-dealers with AML laws and regulations.**
 - Federal regulator of the securities markets and administers the federal securities laws
 - SEC Office of Compliance Inspections and Examinations (“OCIE”)
- **Financial Industry Regulatory Authority (FINRA) is the self-regulatory organization (SRO) for broker-dealers and has been delegated authority by the SEC to enforce AML laws and regulations for registered entities.**
 - A SRO is a nongovernment organization that has the power to create and enforce industry regulations and standards under the supervision of a federal agency.
 - Oversight and exams may be conducted by SROs. The responsible SRO is based upon where the broker-dealer is registered and/or listed.

Enforcement – U.S. Securities and Exchange Commission

- SEC OCIE deemed AML as an examination priority in 2018
- **Section 17(a) of the Exchange Act**
 - Generally prohibits fraud and misrepresentations in the offer or sale of securities
- **SEC Rule 17a-8 Financial recordkeeping and reporting of currency and foreign transactions.**
 - Specifically requires broker-dealers to comply with recordkeeping, retention, and reporting obligations of the BSA, including Suspicious Activity Reports (SARs)



Enforcement – Financial Industry Regulatory Authority

- **In April 2002, the National Association of Security Dealers adopted Rule 3011 (now FINRA Rule 3310) in response to the 2001 PATRIOT Act:**
 - Broker-dealers required to develop AML programs that must, at a minimum:
 - Must be approved by a member of senior management
 - Establish and implement policies and procedures reasonably expected to detect and cause the reporting of “suspicious transactions”
 - Establish and implement policies, procedures, and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act and implementing regulations
 - Provide for annual independent testing of the AML program
 - Designate and identify to FINRA an individual or individuals responsible for implementing and monitoring the AML program
 - Provide ongoing training for appropriate personnel



Enforcement Focus

- AML Program Tailored to a Firm's Business
- Adequate Resources to Address AML Risk
- Filing of Suspicious Activity Reports ("SARs")
- Wire Transfers and Correspondent Accounts
- Individual Liability



Filing of Suspicious Activity Reports

- Broker-dealers are required to file SARs if it involves or aggregates funds or other assets of at least \$5,000, and the broker-dealer knows, suspects, or has reason to suspect that the transaction:
 - Involves funds derived from illegal activity or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity as part of a plan to violation or evade any federal law or regulation;
 - Is designed to evade any requirement of the Bank Secrecy Act;
 - Has no apparent business or lawful purpose or is not the sort of activity in which the particular customer would normally be expected to engaged; or
 - Involves the use of the firm to facilitate criminal activity (31 C.F.R. § 1023.320)
- **Common Issues**
 - Quantity of SARs filed by a broker-dealer do not match the size and type of business
 - Insufficient information and analysis provided in the SAR
 - Adequate consideration of whether to file a SAR

Filing of Suspicious Activity Reports

- **SEC - Wilson-Davis & Co. Inc (\$300,000) (May 2019)**
 - Transactions involved the deposit of physical certificates, liquidation of securities, and immediate wiring of funds out of customers' accounts
 - In several instances, the customer conduct reached such a level that Wilson froze or closed certain customer accounts, but still did not file a SAR
 - Failed to file SARs while ignoring numerous red flags, even when it has reason to suspect that penny stock transactions it executed on behalf of customers were fraudulent
- **SEC - COR Clearing Inc. (\$800,000) (September 2018)**
 - Cleared shares of low-priced securities on behalf of customers where the customers deposited large blocks of low-priced securities, sold the securities into market shortly thereafter, and then withdrew the proceeds of the sales
 - SAR detection software failed to flag these deposit, sale, and withdrawal transactions, and as a result, failed to file SARs

Wire Transfers and Correspondent Accounts

- FinCEN's regulations require the establishment of a risk-based AML program for correspondent accounts established, maintained, administered or managed by U.S. broker-dealers for non-U.S. broker-dealers.
- A correspondent account for broker-dealers is defined as “any formal relationship established for a foreign financial institution to provide regular services to effect transactions in securities.”
 - Accounts to purchase, sell, or lend securities
 - Prime brokerage accounts
 - Accounts trading foreign currency
 - Custody accounts holding settled securities as collateral

Wire Transfers and Correspondent Accounts

- **Risk factors that should be considered include:**
 - Nature of the foreign financial institution's business and markets it serves;
 - Type, purpose, and anticipated activity;
 - Nature and duration of the relationship with the non-U.S. financial institution
 - AML supervisory regime of the jurisdiction where the non-U.S. financial institution operates
 - Information known or reasonably available to the broker-dealer about the non-U.S. financial institution's AML record (31 C.F.R. § 1010.610)

- **The U.S. broker-dealer should also be prepared to conduct periodic audits on the correspondent account activity to**
 - (1) ensure current account activity is consistent with information initially obtained and
 - (2) that suspicious transactions can still be identified given the volume and activity of the account.

Wire Transfers and Correspondent Accounts

- **FINRA – UBS Financial Services/UBS Securities LLC (\$5 million) (December 2018)**
 - Due to the size and complexity of its customers, UBS relied on automated surveillance systems that were not reasonably designed to monitor high-risk transactions like foreign currency wire transfers and penny stocks transactions
 - System did not capture sender/recipient information or country of origin, which could have helped determine whether suspicious
 - Did not appropriately monitor wire transfers of foreign currency to and from high money-laundering risk countries without sufficient AML oversight
 - Did not conduct required periodic risk-based due diligence reviews of correspondent accounts for certain non-U.S. financial institutions

AML Program Tailored to a Firm's Business

- Under FINRA Rule 3310, an AML program must be “reasonably designed” and “risk-based”.
 - “Out of the box” programs are typically not sufficient.
 - NASD Notice to Members 02-21 (April 2002), each broker-dealer should consider the following:
 - Size of entity
 - Location of customers
 - Business activities
 - Type of accounts it maintains
 - Type of transactions in which its customers engage
- FINRA provides a AML Template for Small Firms
 - “Following this template does not guarantee compliance with AML Program requirements or provide a safe harbor from regulatory responsibility.”

AML Program Tailored to a Firm's Business

- **FINRA – Tradition Securities and Derivatives, Inc. (\$100,000) (December 2018)**
 - Well known in the AML world at the time that sovereign bonds from these countries were being used to circumvent currency controls
 - Both Venezuela and Argentina were identified by the Financial Action Task Force as having strategic AML deficiencies during this time period, and the Department of State also identified Venezuela as a “major money laundering country”
 - Failed to tailor its AML program to accommodate for its facilitation of transactions involving Venezuelan and Argentinian bonds, which garnered more than \$8 million in revenue between 2014-2016 predominantly using “Delivery-Versus-Payment” accounts
 - Some of its customers were located in the Cayman Islands, Panama, and Uruguay, locations known for their money laundering risks
 - Neither the written policy and procedures, nor the red flags within its policies and procedures addressed the foreign bonds

Adequate Resources to Address AML Risk

- An AML program must have adequate resources commensurate with the size and sophistication of its business.
 - “Examiners assess the capacity of designated compliance officers, including their background and experience and whether they have the resources to perform their jobs adequately.” – Kevin W. Goodman, National Associate Director, Broker-Dealer Examination Program, Office of Compliance Inspections and Examinations (June 2015)

Adequate Resources to Address AML Risk

- **FINRA - Morgan Stanley Smith Barney (\$10 million) (December 2018)**
 - Internal systems that handled wire information failed to transmit the information to the automated AML surveillance system, which allowed tens of billions of wire and foreign currency transfers to be executed without monitoring
 - AML analysts determined to have “extraordinary workloads that likely contributed to their unreasonable reviews”
 - The firm failed to devote sufficient resources to review alerts generated by the firm’s automated AML system, and as a result, the firm’s AML analysts often closed alerts without an appropriate investigation or documentation of the suspicious wire transfers

Individual Liability

- Broker-dealers registered with FINRA are required to designate an AML compliance officer, and provide information on the individual to FINRA through the FINRA Contact System.
- **FINRA Rule 2010: Standards of Commercial Honor and Principles of Trade**
 - A member, in the conduct of its business, shall observe high standards of commercial honor and just and equitable principles of trade.
- ***U.S. Department of the Treasury v. Haider (D. Minn 2016)***
 - Federal district court held that individuals can be liable for violations of the BSA's AML program requirements
 - BSA's general civil penalty provision authorizes the imposition of money penalties against, among other individuals, "officer[s]" of financial institutions

Individual Liability

- **FINRA – Sebastian Jimenez, General Securities Representative for HSBC Securities (USA) Inc., and private banker/relationship manager for HSBC Private Bank International**
 - Violated FINRA Rule 2010 by knowingly providing inaccurate answers to questions regarding a \$100,000 and \$165,000 deposit into a customer's bank account in connection with an AML review conducted by the bank
 - Circumvented HSBC's written supervisory procedures in both cases to provide misleading answers regarding the source of funds
 - Barred from association with any FINRA member



Individual Liability

- **SEC – Jerard Basmagy, Former CCO and AML Officer of Chardan Capital Markets, LLC (\$15,000) (May 2018)**
 - Violated Section 17(a) of the Exchange Act and SEC Rule 17a-8 promulgated thereunder
 - Basmagy fined directly for willfully aiding and abetting and causing Chardan's AML violations by failing to investigate red flags, monitoring patterns of suspicious activity related to penny stock liquidations, and filing SARs
 - Chardan's clearing firm, Industrial and Commercial Bank of China Financial Services LLC, raised multiple concerns to the firm about certain customers
 - Basmagy prohibited from associating with any broker, dealer, or investment advisor and barred from participating in penny stock offering for three years

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Education

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JD, 2008

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Practice

Nomi Goheer is an associate in Willkie's Global Trade & Investment Practice Group in Washington. He provides advice and assistance to clients on government regulation of international trade, particularly with regard to export controls, economic sanctions, anti-money laundering, and foreign investment in the United States (CFIUS).

Mr. Goheer advises clients across a range of industries, including financial, technology, telecommunications, defense, manufacturing, and petroleum. He counsels clients on the development and implementation of regulatory compliance programs; internal investigations of potential violations; and advice regarding licensing and product classification under the Export Administration Regulations (EAR), and International Traffic in Arms Regulations (ITAR). He also assists clients with questions of international trade policy, trade remedies, and customs.

Bar Admissions

Mr. Goheer is a member of the District of Columbia and Georgia Bars.

Education

Mr. Goheer received a JD from the American University, Washington College of Law, where he served on the American University Law Review. He also received a MA from American University, School of International Service in International Politics and a BA from Emory University.