REPRINT

R&C risk & compliance

THE NEW US ANTI-MONEY LAUNDERING ACT

REPRINTED FROM:
RISK & COMPLIANCE MAGAZINE
JUL-SEP 2021 ISSUE

www.riskandcompliancemagazine.com

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Guidehouse

Published by Financier Worldwide Ltd
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www.riskandcompliancemagazine.com

EXPERT FORUM

THE NEW US ANTI-MONEY LAUNDERING ACT

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R&C: How would you characterise the problem of money laundering in the US? What affect does it have on companies, the financial system, government and society in general?

Zimiles: Money laundering is both a domestic and global issue for the US. Globally, the United Nations estimates the amount of money laundered in one year is between 2 and 5 percent of global GDP, or $800bn to $2 trillion. In the US alone, domestic financial crime, excluding tax evasion, generates approximately $300bn of proceeds for potential laundering. Money laundering is not a victimless crime, and often involves the proceeds of drug trafficking, human trafficking and fraud, among other illicit activities, resulting in a significant social impact. In 2019, there were nearly 50,000 overdose deaths involving any opioid, and the US State Department estimates that 14,500 to 17,500 people are trafficked into the US each year.

Vasi: Money laundering is one of the greatest concerns for companies, the financial system and government in the US. It can hamper economic growth and, of course, is a source of criminal activity. The cost of compliance with anti-money laundering (AML) requirements, procedures and systems for financial services firms is significant. Fines for failures to comply with AML requirements are, year-over-year, the highest category of regulatory fines. Government and law enforcement also expend a lot of resources combatting money laundering. Criminals continue to find new and different ways to launder money and it appears the regulators, financial services firms, lawmakers and advocates believe that updating and adding to AML requirements and regulation will improve general AML efforts and reduce money laundering.

Yoskowitz: The problem of money laundering in the US is widespread. It is used by terrorist groups, drug cartels, human traffickers and other criminal organisations to fund their illegal activities. While it is hard to ascertain an exact amount, reports have money laundering levels of at least hundreds of billions of dollars. Its use and authorities' inability to detect it has become exacerbated by cryptocurrencies and the pace of technological change. Money launderers' ability to raise such huge sums of money affects society in general and governments which are forced not only to deal with the direct consequences of the assault on financial systems, but the very real secondary impacts of increased violence and fraud. For companies and financial institutions (FIs), it means they must keep an ever-watchful eye on transactions and relationships and not become complacent.

Angotti: We have seen US FIs engage in 'de-risking', by exiting higher risk businesses and customers, such as correspondent banking, charities

and money service businesses to avoid unnecessary regulatory attention. The practice of de-risking has displaced certain types of entities from the financial system, requiring them to engage in less formal and less transparent financial practices. This exclusion from the US financial system can paradoxically make it more difficult for law enforcement to conduct investigations, because these types of financial systems may not have the books, records and audit trails that regulated FIs must keep.

R&C: The Anti-Money Laundering Act of 2020 (AMLA) is the first major overhaul of US AML laws in decades. What are the key drivers for such substantial, sweeping legislative reforms being taken now?

Vasi: The 2018 customer due diligence (CDD) rule that amended the Bank Secrecy Act (BSA) was considered a major change to regulation by some and caused some waves for the covered FIs that must comply with it. The CDD requires these covered FIs to identify and verify natural persons – beneficial owners – of legal entity customers who own 25 percent or more of an FI's customers' business or control the business. The most important part of the Anti-Money Laundering Act (AMLA) is its establishment of a beneficial ownership registration database that will be implemented and operated by the Financial Crimes Enforcement Network (FinCEN). Registration is required of 'reporting companies' that excludes certain FIs, including banks, credit unions, registered issuers of securities, bank holding companies, brokers, dealers, money transmitters and exchanges. Companies are also exempt if they have a physical office located in the US, employ more than 20 full-time employees, and have over $5m in gross receipts or sales over the past year. The idea is to throw a wide net to prevent money laundering through small shell companies, which should help prevent and detect money laundering. However, implementation will likely be a challenge and companies are going to be reluctant to provide sensitive personal information to a government entity. Cyber security risk issues will be raised. Another interesting change is that AML requirements will now apply to the art market, specifically antiques and art dealers. Art dealing is certainly used for money laundering.

Yoskowitz: The key drivers behind the AMLA were modernising existing systems and improving interagency cooperation and expanding the reach of certain prior provisions. It was clear to the bill's sponsors that more work needed to be done in these areas. In the US, they thought it too easy to set up shell companies that hid true ownership. Now, reporting companies, as further defined in the AMLA, will have to report their beneficial ownership, which will be stored in a non-public database. It also expands civil and criminal penalties in these areas. Importantly, it modifies the definition of FIs to include

the use of art, antiquities and cryptocurrencies to reflect the use of these non-cash items in the illicit business of money laundering.

Zimiles: The last significant enhancement to AML laws was the USA Patriot Act of 2001. Since then, we have seen changes in domestic and international financial crimes, changes in financial products and services, and the emergence of new technologies, including cryptocurrency, machine learning (ML) and artificial intelligence (AI). As a result, the AML regime was ripe for modernisation. Part of the statute requires a complete review of the BSA. In addition, the AMLA commissioned several studies that focus on how financial services and money laundering have changed since its initial passage, such as whether to amend currency transaction report (CTR) and suspicious activity report (SAR) thresholds, the impact of financial technology on financial crimes compliance and financial services de-risking. In addition, the private sector spends significant resources on AML and sanctions. As a result, it has lobbied for relief to reduce compliance obligations and to focus more on real risk. That said, the AMLA does not provide immediate relief to the private sector and will largely depend on the results of these studies.

Angotti: The ability to form anonymous shell companies in the US is a significant risk factor for money laundering and has been a subject of proposed legislation for decades. US government reports and the '2016 Financial Action Task Force Mutual Evaluation Report' identified the ability to form legal entities in the US without disclosing beneficial ownership as a key vulnerability to the US financial system. The implementation of the CDD rule helped narrow this gap, but it did not close it entirely. This was likely a driver for the passage of the Corporate Transparency Act (CTA) provisions of the AMLA. The CTA will require certain entities to register their beneficial ownership information with the FinCEN. Similar registries exist in other countries, such as Companies House in the UK, albeit that is a public registrar, whereas the CTA beneficial ownership registry will be nonpublic.

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R&C: What have been the major immediate impacts of the AMLA? What is supposed to occur in the future?

Yoskowitz: The AMLA is still very new and, therefore, companies and their consultants are still assessing its far-reaching aspects. Regardless, companies will have to update their compliance policies to reflect the new requirements. The FinCEN has recently issued an Advance Notice of Proposed Rulemaking to request comments from the public on the implementation of the reporting and beneficial ownership provisions of the AMLA. Other regulators like the Treasury Department and Department of Justice (DOJ) are probably also going through internal review processes to determine what they need to do to make use of the new provisions. Entities inside and outside government will have to establish 'best practices' for reporting, information sharing and compliance in general.

Angotti: Of the AMLA provisions that are effective immediately, the expanded subpoena power may have the most significant impact. Under section 6308, the secretary of the US Treasury or the attorney general may issue a subpoena to any foreign bank that maintains a US correspondent account to request records on any account at the foreign bank, including records maintained outside of the US. Importantly, if the foreign bank does not comply with the subpoena, then the US FI may be required to close the correspondent account of the foreign bank. It is doubtful that this authority will be used in routine investigations, but it is another powerful tool in the US government's AML arsenal. In addition, AMLA provisions for increased penalties for repeat BSA violators, the barring of certain BSA violators from serving on the board of an FI, and increased incentives and protections for whistleblowers were effective immediately. Accordingly, FIs should ensure employees throughout the organisation are aware of these provisions and update training materials where necessary.

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Zimiles: Most AMLA provisions require the US Treasury to issue implementing regulations. As part

of the AMLA, for example, reporting companies will be required to report beneficial ownership information directly to the FinCEN. The FinCEN, however, is responsible for not only developing and maintaining the registry, but also implementing rules that govern access to the information, and the specific information that reporting companies need to provide and how often. Another important future development is that the US Treasury will specify standards for testing FIs' compliance technology. FIs often apply existing model risk management guidance to AML systems, which may not be appropriate for less sophisticated AML systems or those that do not meet the definition of a model.

Vasi: We do not believe that the impact of the AMLA has yet been felt, but art dealers and the new reporting companies must begin to understand their AML requirements and build policies and procedures to meet those requirements. We do believe that many auction houses and art dealers already have some type of AML policy in place.

R&C: To what extent does the AMLA strengthen the AML apparatus? How does it differ from previous provisions under the Bank Secrecy Act (BSA) and the Patriot Act, for example?

Angotti: The AMLA appears to strengthen the US AML apparatus, but by how much is hard to say. There is clear emphasis on information sharing, through the establishment of the FinCEN Exchange, semiannual report on threat patterns and trends, feedback on SARs and sharing of national AML priorities. In addition, expanded subpoena power and the establishment of the beneficial ownership registry should help law enforcement investigate and prosecute financial crime. The extent to which these measures strengthen the US AML apparatus will depend on factors such as the resulting protocols and implementing regulations promulgated to implement AMLA provisions, the outcomes, recommendations and proposed rulemakings resulting from the mandated AMLA studies, and how effectively FIs can incorporate the information that the government provides into their AML programmes.

Vasi: Subpoena power was expanded regarding foreign banks. New crimes for money laundering in art and businesses engaged in cryptocurrency were added, and penalties for violations were increased. We believe there will be coordination and information sharing among agencies and technological innovation will increase.

Zimiles: I see two key differences in the AMLA when comparing it to the USA Patriot Act. First, the AMLA requires the government to share information with FIs, while the existing AML regime generally requires FIs to provide information to law enforcement upon request. Second, the AMLA

requires reporting entities to provide beneficial ownership information directly to law enforcement. Previous legislation, such as section 312 and the CDD Rule, require covered FIs to collect beneficial ownership information on certain types of customers. Specifically, section 312 requires covered FIs to obtain beneficial ownership information on certain foreign banks, and the CDD Rule requires covered FIs to identify and verify beneficial ownership information of legal entity customers. Criminals can effectively circumvent these due diligence requirements by opening shell companies to acquire US-based assets. In other words, the FinCEN is going straight to the source of the information.

Yoskowitz: The AMLA adds many provisions to the structures that hunt down money laundering. It also improves coordination with the BSA and Patriot Act. It widens the definitions of reporting companies and requires the FinCEN to establish a non-public registry. It adds civil and criminal penalties to give its provisions teeth. It requires the Treasury to conduct a study about whether current dollar thresholds for CTR and SAR filings should be adjusted upward and to establish a pilot programme to allow FIs to share SAR information with their foreign branches, subsidiaries and affiliates. It further expands the scope of the DOJ's authority to seek and enforce correspondent account subpoenas. Finally, the AMLA updates the whistleblower reward programme to improve incentives for reporting of potential AML violations.

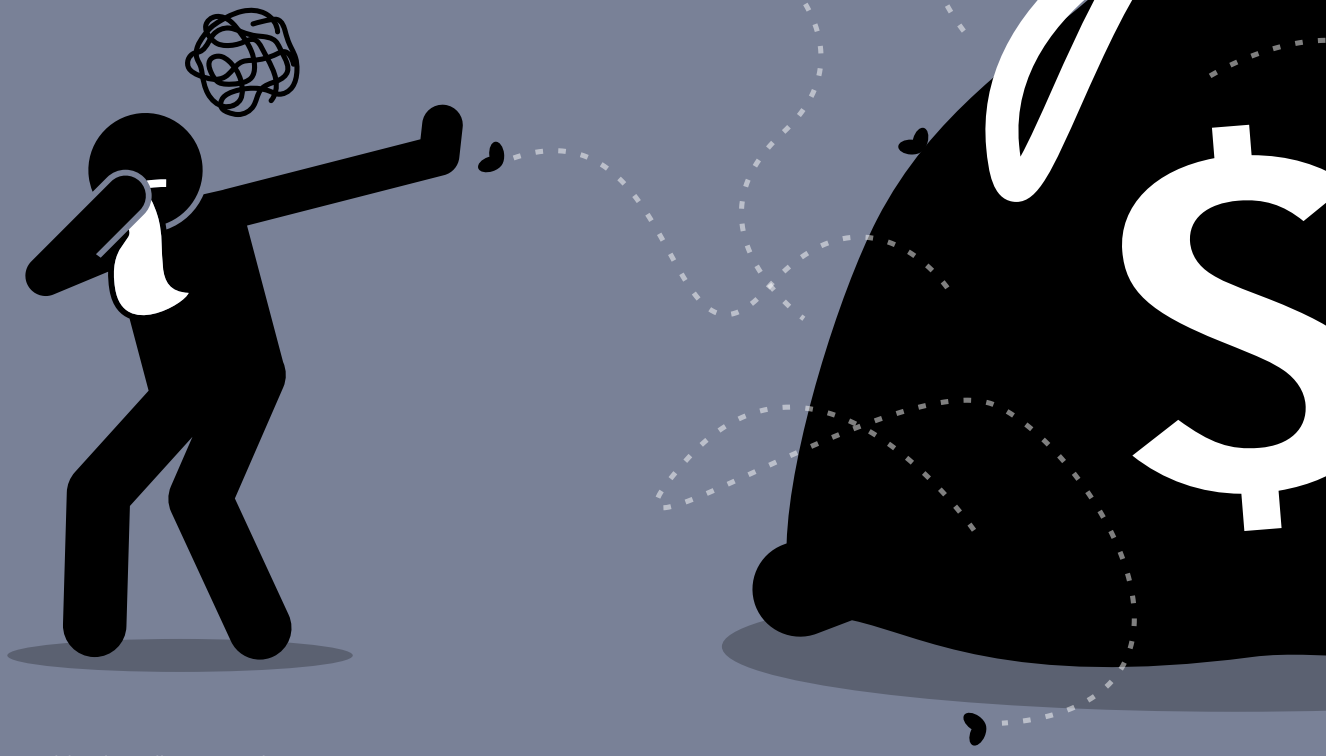
R&C: Could you explain how the AMLA will help strengthen communication channels between law enforcement, bank supervisors and banks, and shape their AML policies?

Vasi: It is likely that the Treasury Department and the attorney general will work closely to implement the changes and work more closely with state governments and authorities. One of the stated goals of the AMLA is to "improve coordination and information sharing among agencies fighting money laundering and the financing of terrorism".

Angotti: Although section 314a of the AMLA was supposed to be a mechanism for information sharing between the government and FIs, in practice it became a method for the government to request information from FIs. The AMLA establishes several communication channels between the government and FIs, with the focus on the government providing information and feedback to FIs. For example, the AMLA requires the FinCEN to issue semi-annual reports on threat patterns and trends, share feedback on SARs and regulators must share their exam priorities with FIs. If the government arms FIs with the right information, hopefully FI AML programmes

become more effective in detecting and reporting financial crime.

Yoskowitz: Enhanced communication is at the heart of the new AMLA. For example, the AMLA empowers the Treasury Department to issue rules to create a pilot programme to allow FIs to share information related to SARs with their foreign branches, subsidiaries and affiliates. The Act also formalises the FinCEN Exchange, originally created in 2017, which is designed to enhance the sharing of information among institutions. The Secretary of the Treasury will also convene a team



of stakeholders from the both the public and private sector to examine strategies to increase cooperation. Companies will have to come up with strict policies on this type of information sharing.

Zimiles: AML 'red flags' are too often outdated. As we know, criminals modernise their methods, which is why access to current trend and threat information is so valuable. FIs, however, will have to do their part and use the information that the government provides. It will be incumbent upon them to incorporate it, as appropriate, into their risk assessment and programme. If the government goes through the trouble of producing these reports and providing feedback, but the FI does not use it, then they will miss opportunities to increase effectiveness. The AMLA also includes provisions to strengthen communication with international partners. The attaché programme, for example, seeks to build relationships with the Treasury's foreign counterparts and conduct outreach with foreign FIs. The AMLA also establishes foreign financial intelligence unit liaisons, which will focus on public and private sector outreach abroad.

R&C: In your opinion, do companies need to review their existing AML controls, policies and procedures in light of the AMLA?

Angotti: Most AMLA provisions require implementing regulations before they become effective for covered FIs. That said, there are a few provisions that are effective immediately, such as the new long-arm subpoena power under section 6308, which allows the US government to issue subpoenas to a foreign bank with US correspondent accounts about any information, including records maintained outside the US. As such, US FIs with foreign correspondent relationships may need to update their terms and conditions with these relationships to comply with this AMLA provision. Covered FIs that operate globally should also consider assessing whether they are identifying foreign correspondent accounts properly. Even if an FI does not offer US dollar clearing services, it may still have foreign correspondent relationships with foreign banks subject to this provision.

Yoskowitz: The AMLA is wide-reaching. Companies that already have robust AML policies and procedures will need to examine those policies to determine how they need to be updated. For example, the pilot programme on information sharing by FIs will have to be rigorously examined. Record keeping will be even more essential going forward. The law may have unintended consequences. For example, internal whistleblowing policies may need to be updated. Companies that previously may not have met the definition of reporting companies will now need procedures and policies, so they are

prepared to disclose beneficial ownership to the FinCEN. And foreign institutions with a presence in the US should expect enhanced supervision from the various agencies.

Zimiles: Other provisions that are effective immediately are increased penalties for repeat BSA violators, greater incentives and protections for whistleblowers, and barring certain individuals from serving on boards of FIs. As such, covered FIs should review their policies and procedures affected by these currently effective AMLA provisions. FIs should also closely monitor regulatory communications regarding new rules and reports, such as rules for testing compliance technology and semi-annual reports on threat patterns and trends, to determine the extent to which these communications and proposed rules impact their programme. I do not believe the AMLA significantly changes the current BSA obligations of covered FIs. Therefore, a full programme review focused on AMLA provisions does not seem practical at this point.

Vasi: AML controls, policies and procedures should be reviewed at least annually, and companies should look at the AMLA to see if they need change or edit those policies.

R&C: What advice would you offer to companies on implementing a framework that ensures compliance with the AMLA? In what ways can technology help companies to meet their obligations?

Yoskowitz: Companies should engage in a comprehensive review of their current policies and procedures. Over the next few years, best practices will undoubtedly develop for a comprehensive and cost-effective AML compliance system. It will likely rely on technology to capture and protect information and to share that information as appropriate with affiliates or government agencies. There will hopefully be various tiers of these programmes so that smaller companies will not be overburdened with a compliance structure. Companies should reach out to consultants and counsel knowledgeable in

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these areas, especially as the framework develops over time and enforcement actions are taken that highlight where the deficiencies may lie.

Zimiles: The AMLA does not materially change the current BSA obligations of covered FIs, except in limited circumstances. Even businesses "engaged in the exchange of value that substitutes for currency or funds" and antiquities dealers, which are now covered FIs under the BSA, require the Treasury to promulgate implementing regulations before their BSA obligations are enforceable. "Businesses engaged in the exchange of value" may allow the FinCEN to issue regulations to cover not only cryptocurrency exchanges but also decentralised finance and non-fungible tokens. Treasury will have to request public comment on how to implement these provisions. This process has already started in certain areas, such as the advance notice of proposed rulemaking on beneficial ownership registry requirements and interagency statements on model risk management guidance. Companies should closely monitor and participate, as appropriate, in regulatory communications that request comment on implementing AMLA provisions.

Vasi: FIs need to review the AMLA, be sure they comply with the AMLA, and get started on the implementation of policies, procedures and controls to manage their requirements.

Angotti: The statute requires the government to conduct studies and issue findings for a broad spectrum of issues. The FinCEN and the banking regulators will issue exam priorities and information about threats and financial crime typologies. The one thing we know is that if the government provides you with information, you must use it. FIs should closely monitor these studies and reports to determine how they can use this information to increase the effectiveness of their AML programme, and should have a governance process to incorporate the information, as appropriate, into their risk assessments and transaction monitoring scenarios, or investigations. Covered FIs should consider using technologies such as AI, ML and robotics to meet

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their BSA obligations. It is, however, important that FIs should not only focus on gaining efficiencies with these technologies, but also on effectiveness. FIs should also be transparent about how their AML systems operate and clearly document their rationale.

R&C: What penalties and other consequences might companies face if they fail to take the necessary steps to enhance their AML frameworks? How do you expect such frameworks to develop and improve?

Zimiles: The AMLA increases the fines for repeat BSA violators and bars individuals with significant historical BSA violations from serving on an FI's board. That said, these provisions are specific to individuals, not institutions. While the AMLA does not impose a significant number of new requirements on FIs, it does not relieve them of any BSA obligations. FIs should continue to update and enhance their AML and sanctions programmes as part of 'business as usual', especially in cases when there are changes to their business, products and customers. If FIs do not meet their current BSA obligations, they should expect similar enforcement actions and fines as we have seen over the past several years.

Angotti: In the short term, FIs should continue to focus on their current BSA obligations and make updates in response to the few provisions that are effective immediately, as applicable. In the long term, AML risk management may improve as FIs receive information from the government, such as the reports on patterns and emerging trends, and feedback on SARs. I also anticipate regulators will continue to expect the first line to own risk issues, including a strong tone at the top and culture of compliance. This is not directly tied to the AMLA, but increased penalties for repeat BSA violators, a focus on penalties for the board of directors, and increased incentives and penalties for whistleblowers, indicates an emphasis on compliance and ethics throughout all levels of the organisation.

Yoskowitz: The AMLA provides for new and enhanced penalties. For example, wilful failure to file beneficial ownership information can result in civil liability of $500 per day for every day the violation continues, and potential imprisonment up to a maximum of two years. Unauthorised disclosure can lead to up to five years in prison. There are new criminal violations under the BSA including making it a crime to misrepresent a fact to an FI concerning the ownership of assets where the person or entity who owns the asset is a senior foreign political figure and the value of assets is at least $1m. It is also a violation to mispresent a material fact to an FI about the sources of funds in a monetary transaction that involves an entity found by the Treasury to be a primary money laundering concern. This could result

in a fine of up to $1m and up to 10 years in prison. In addition, there will undoubtedly be penalties for not having adequate policies and procedures in place. Companies will need to demonstrate to regulators how they are complying with the new regulations with updated policies and internal reporting.

R&C: Looking ahead, what long-term impact do you believe the AMLA will have on money laundering activity in the US? To what extent do you consider the Act to be a game-changer for enforcement and compliance?

Angotti: It is hard to tell what the long-term impact will be, as many of the regulations required by the AMLA are still in development. Based on the tone of and the provisions in the AMLA, we anticipate more transparency from regulators and the FinCEN, which will hopefully mean more effective AML programmes, which should mean better information for law enforcement. We also anticipate more collaboration between private and public sectors, and more international cooperation, including helping to enhance AML regimes in other countries. The beneficial ownership registry is intended to be a 'game-changer', but there is still a lot unknown about how it will work in practice. The AMLA excludes several types of entities from the definition of a "reporting company", and it will be interesting to see if criminals begin to form those types of companies to avoid reporting beneficial ownership.

Zimiles: Money laundering is a global problem, which is why there is so much focus in the AMLA on domestic and foreign cooperation in both the public and private sector. The US cannot solve its money laundering problems without international cooperation. There are more questions than answers about the beneficial ownership registry at this point and we do not know whether the required studies will lead to any changes in AML laws. Certainly, the focus on innovation and technology is important, as we need to leverage new technologies, such as ML and AI, to help fight financial crime. Importantly, the AMLA requires the government to conduct a formal review of the regulations implementing the BSA and related guidance. The purpose of the review is to ensure provisions that produce highly useful information remain, and to identify regulations and guidance that may be outdated or redundant. This study will hopefully lead to a more effective US AML regime in the long term, but it may not result in significant changes. We will have to wait and see.

Yoskowitz: The AMLA is going to have a significant impact on the enforcement and compliance landscape. Its emphasis on information sharing and its focus on both expanded concepts for beneficial ownership reporting and cash alternatives in the money laundering universe are game-

changers. There will be increased enforcement and scrutiny at all levels and companies are going to have to race to keep up with best practices as they evolve and grow. No one can afford to be complacent, both in terms of compliance but also in terms of how the criminals find new ways to evade current systems. Constant vigilance and self-reflection will be key, and companies need to keep an eye on the regulators as they figure out what they will do with their new enforcement powers and information.

Vasi: Many more companies and businesses will now be subject to AML requirements, which will hopefully help reduce money laundering. It is a potential game-changer for enforcement and compliance. Enforcement has more weapons and compliance has more responsibility. R&C