Global Transaction Services

Cash Management  Trade Services and Finance  Securities Services  Fund Services

Regulatory Compliance and Trade 2007
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Objectives

- Provide an overview of some U.S. Government regulations related to international trade impacting bank transactions
During this presentation, we will provide information on the following topics:

- U.S. Regulations
  - U.S. Sanctions
  - Anti-Boycott
  - Anti-Money Laundering
  - USA PATRIOT Act
  - Export Controls
What is Compliance?

“Compliance” means adherence to a regulatory framework that include laws, rules, regulations, internal policies and procedures, codes, guidelines, and best practices

Regulators

- Office of the Comptroller of the Currency
- Federal Reserve
- Securities Exchange Commission
- Self regulatory organizations (i.e., National Association of Securities Dealers, New York Stock Exchange)
Why is Compliance Important?

- A bank expects that its employees will do their best to ensure compliance and protect the firm

- Failure to do so may result in potential problems for banks, including
  - Reputational damage
  - Regulatory sanctions
  - Litigation
  - Fines
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U.S. Sanctions
U.S. Sanctions

- These laws are administered by the Office of Foreign Assets Control (OFAC) within the U.S. Department of the Treasury

- U.S. law prohibits or restricts U.S. persons from doing business with certain countries and individuals as a tool of U.S. foreign policy objectives
  - Applies to U.S. persons (regardless of employer) and U.S. businesses anywhere in the world

- Depending on the country or entity involved
  - Accounts/assets of sanctioned parties must be blocked
  - Transactions involving sanctioned parties may be rejected or blocked
  - Blocked funds must be held in an interest-bearing account

- All blocked accounts are reported to the U.S. Government annually
At the present time, the U.S. Government has in force various types of sanctions against the following countries:

- Burma, Cuba, Iran, Sudan, and Syria
- Limited sanctions also exist with respect to North Korea and Iraq

OFAC has designated individuals and other entities as Specially Designated Nationals (SDN) of target countries, subjecting them to the same sanctions as the country itself

- Detailed information is available on the OFAC website (http://www.ustreas.gov/offices/enforcement/ofac/)
- The SDN and Blocked Persons list is frequently updated
Other OFAC programs include:

- Anti-terrorism sanctions
- Non-proliferation sanctions
- Narcotics trafficking sanctions
- Diamond trading sanctions
- Belarus
- Democratic Republic of Congo
- Ivory Coast
- Western Balkans
- Zimbabwe
U.S. Sanctions (continued)

- Banks cannot provide economic support to blocked persons and entities that appear on the SDN list or to sanctioned countries.
- Banks cannot accept instructions from an individual or entity that appears on the SDN list.
- To comply with the sanctions screening policy compare names, addresses, SWIFT codes, and countries found in transactions to the SDN list and the sanctioned countries list.
Questions to ask when reviewing a transaction for sanctions

- Does the account party, beneficiary, issuing bank, paying bank, or other third party named in a transaction or documents match to a name on the SDN list?
- Is the underlying trade transaction prohibited?
- Does the bill of lading indicate that the goods were shipped by a blocked shipping company or aboard a merchant vessel appearing on the SDN list?
- Does the certificate of origin reveal that the goods originated from a targeted country?
- Does the invoice indicate that a blocked company supplied goods to the seller?
- Does the letter of credit state shipment/transshipment to or from a sanctioned country?
U.S. Anti-Boycott
U.S. Anti-Boycott

- Two U.S. laws that seek to counteract the participation of US citizens in other nations’ economic boycotts or embargoes:
  - The 1977 amendment to the Export Administration Act (EAA) administered US Commerce Department
  - The Ribicoff Amendment to the 1976 Tax Reform Act (TRA) administered by US Treasury Department
Anti-Boycott Laws

- The U.S. anti-boycott laws limit the extent to which U.S. banks, their subsidiaries, branches, and controlled affiliates worldwide may honor economic boycotts or embargoes imposed by other nations
Prohibits participation in boycott requests by “U.S. persons” and applies tax penalties and or fines to those “U.S. persons” who agree to participate in boycotts of countries friendly to the U.S.

“U.S. person” is defined in the Export Administration Regulations to include individuals and companies located in the U.S. and their foreign affiliates (e.g., non-U.S. branches)

“U.S. person” is defined in the Tax Reform Act to include all U.S. taxpayers and their related companies
These laws may require that a bank’s personnel:

1. Refuse to participate in a business transaction;
   or
2. Participate in a business transaction ONLY if certain conditions are met – e.g., amendments to offending clauses

These laws also require that certain “requests” to participate in or comply with foreign boycotts be reported to U.S. government agencies, whether or not a bank implemented the request.
What to Look for in Letters of Credit?

- Certifications concerning:
  - Agreements to blacklisted status
  - Substantive business relationships with certain countries that are not of a purely commercial nature
  - Request to participate in a boycott
  - Eligibility of carrier vessel to enter the ports of a particular country or group of countries
  - Agreements to abide by rules or regulations of a boycotting country
How do Sanctions and Anti-Boycott differ?

- **U.S. Sanction Laws**
  - Inflexible and strictly enforced
  - Language cannot be altered or deleted to make the transaction [appear] permissible
  - Generally, assets must be blocked and reported to OFAC

- **U.S. Anti-Boycott Laws**
  - Transactions go forward provided the offensive language is altered or deleted
  - Offensive language must be reported to the Department of the Treasury, and/or the Department of Commerce
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Anti-Money Laundering (AML)
Money laundering is the disguising or concealing of the illicit nature or source of income or assets in order to make them appear legitimate

The phases of money laundering are:

- **Placement** – the initial point of entry for funds derived from criminal activities
- **Layering** – the creation of complex networks of transactions which attempt to obscure the link between the initial entry point and the end of the laundering cycle
- **Integrating** – the return of funds to the legitimate economy for later extraction

U.S. banks are committed to preventing the misuse of their personnel and facilities by persons who seek to launder money

*Under Bank Secrecy Act (BSA)* criminal and civil liability may result from the willful failure to act when action is required, including:

- Failing to report suspicious activity
- Failing to maintain required records
- Ignoring or failing to ascertain the source of a client’s assets or the nature of a client’s transactions
Anti-Money Laundering (continued)

- Employees at U.S. banks have a duty to safeguard their firm’s business and reputation
- They are responsible for
  - “Know your customer”
  - Documenting the bank’s due diligence efforts
  - Reporting suspicious transactions
    ... continues for the duration of the client relationship
- Concerns about potentially suspicious activity must be escalated
Anti-Money Laundering (continued)

- Employees should familiarize themselves with the “risk indicators”/“red flags” associated with questionable clients or potentially suspicious activity.

- This has received even greater emphasis in the past year:
  - Financial Action Task Force white paper on “Trade Based Money Laundering” (June 2006) identified key findings including trade based money laundering techniques as follows:
    - Over- and under-invoicing of goods and services
    - Multiple invoicing of goods and services
    - Over and under shipments
    - Falsely described goods and services
    - Black Market Peso Exchange

Anti-Money Laundering (continued)

**U.S.A. PATRIOT Act 2001 – Highlights**

- Enacted to combat money laundering and the financing of terrorist activity
- Places responsibility to “Know Your Customer” on Banks
- Prohibits the maintaining of correspondent accounts for foreign shell banks (i.e., banks without a physical presence in any country)
- Firm is required to apply special measures, maintain certain records and share information about our clients with government regulators and other financial institutions
- Requires a Client Identification Program (CIP)
Expands the scope of federal anti-money laundering laws

- Requires U.S. financial institutions to create enhanced procedures for detecting money laundering

- Requires a client identification program
  - Customer identification information must be obtained prior to account opening or the establishment of a formal relationship
  - This information must be verified within 30 days of account opening
  - These requirements are incorporated in the front-end of the account opening process
Anti-Money Laundering (continued)

U.S.A. PATRIOT Act 2001 – Highlights (Cont.)

- Prohibits the maintaining of correspondent accounts for foreign shell banks (i.e., banks without a physical presence in any country)
  - All foreign banks must submit a Foreign Bank Certification form stating that they are not a shell bank, nor that they indirectly provide banking services to one
  - Sub-accounts for foreign banks can be opened without a certification form, but they will be frozen if the form is not received within 30 days

- Includes provisions for the cooperation of financial institutions with regulators, law enforcement, and other U.S. financial institutions
Anti-Money Laundering (continued)

U.S.A. PATRIOT Act 2001 – Highlights (Cont.)

- Under Section 311, the Secretary of the Treasury may conclude that a jurisdiction or financial institution operating outside the U.S. is of “primary money laundering concern” and enact special measures, including prohibitions on maintaining or opening correspondent accounts.

- High Risk Jurisdictions
  - Be aware of jurisdictions that have been identified as high risk by the Financial Action Task Force (FATF) Non-Cooperative Countries and Territories (NCCT)
    - FATF NCCT: Myanmar (Nigeria recently removed)
Anti-Money Laundering (continued)

**U.S.A. PATRIOT Act Section 314(a)**

- Required regulations to encourage regulatory and law enforcement authorities to share information with financial institutions regarding individuals, entities & organizations engaged in, or reasonably suspected of engaging in terrorist acts or money laundering activities.

- Financial Crimes Enforcement Network (FinCEN) regulations enable federal law enforcement agencies to reach out to financial institutions to locate accounts and transactions.
U.S. Export Controls

What is Controlled?

- Commodities – tangible products or goods, vs. software/technology

- Software – programs, microprograms, tangible medium of expression

- Technology – information, tangible technical data, intangible technical assistance, development, production, use
U.S. Export Controls (continued)

Who Administers the U.S. Export Controls?

- Export Administration Regulations (EAR) are administered by U.S. Department of Commerce, Bureau of Export Administration
- International Traffic in Arms Regulations (ITAR) are administered by U.S. Department of State, Office of Defense Trade Controls
- ITAR is concerned with “military” related items
- What type of questions might be asked as due diligence for transactions involving military equipment?
  - End use of goods – military or civilian
  - Application of goods – lethal, non-lethal, dual use
  - Parties involved
U.S. Export Controls (continued)

- EAR and ITAR apply when goods, services, software, or technology are:
  - Exported from the U.S.
  - U.S. origin and re-exported from another country
  - Manufactured overseas for export with U.S. origin components (subject to de minimis rules)

*Screening against lists published by the Departments of Commerce and State Regs. apply to U.S. persons and non-U.S. persons involved in above activities*
Questions?
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