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To SAR or Not to SAR

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Moderator:
Michelle Neufeld
Managing Director & Chief Financial Crimes Compliance Executive,
Global AML and Economic Sanctions
Bank of America

Panelists:
Lisa Belle
Head of AML, Markets and International Banking
Royal Bank of Scotland

Julie Copeland
Managing Director
Head of AML & Sanctions for the Americas
Societe Generale

Mike McNally
Vice President External Investigations
Fidelity Investments

Lourdes Paredes
Director
Head of Americas AML/AML Risk & Controls
Credit Suisse

1. Introduction – Michelle
2. Foundation – Mike
   a. Best practices
   b. What does By, at or through mean
   c. New SAR database
      i. Key issues to be aware of
3. When you decide not to file a SAR - Lourdes
   a. What are the factors to consider when making this decision
   b. How to document the decision
   c. Examination focus – holistic view of the customer
4. Defensive filing - Lisa
   a. Issues with defensive filing pros/cons
   b. Enforcement actions
5. Good faith requirement – does it exist? - Julie
   a. Indicia to be considered
   b. Review of Cummings case as an example

SAR Foundation Concepts

The USA Patriot Act requires financial institutions to report to Treasury any transactions conducted by, at or through it, where the firm knows, suspects or has reason to suspect the transaction:

- Involves assets related to illegal activity and was conducted to conceal the origin of the funds;
- Is designed to evade federal reporting regulations;
- Appears to serve no business or lawful purpose or is not the sort in which the particular customer is expected to engage; or
- Facilitates criminal activity.

- A SAR must be filed within 30 days of initial detection of facts that may constitute a basis for filing the SAR
- It is a felony to make a customer aware SAR has been filed
- Confidentiality considerations

New SAR Form Considerations

- Formatting for Law Enforcement and Regulators
- Clarity of terms / Consistency in approach
- Key word advisories
- Internal reporting challenges
- Current and future impact

SAR Decision-Making

- The decision to file a SAR is an inherently **subjective judgment.**
- It is at the discretion of a financial institution to make a **reasonable**, **risk-based** decision, in **good faith**, to file or not file a SAR.
- If a financial institution decides to **not** file a SAR, then that institution:
  - **Must**[1] **document** the specific reason(s) for that decision, and
  - **May** continually **monitor** subjects of a SAR for future reporting.

[1] Best practice and regulatory expectation, but not law or regulation.

SAR Decision-Making

- Financial institutions should have **policies and procedures** for:
  - **Referring unusual activity** from business lines to personnel responsible for evaluating unusual activity, and
  - **Escalation process** from point of initial detection to disposition of the investigation.
- Possible suspicious activity findings should be forwarded to a **final decision-maker** (individual or committee).
  - Final decision-maker should have proper **background and expertise**.
  - Decision-maker should have **authority** to make final SAR **filing decision**.

Source: FFIEC's BSA/AML Examination Manual

SAR Decision Documentation

- Financial institutions should **document SAR decisions**, including the **specific reason(s)** for filing or not filing a SAR.
  - Documentation should be **thorough**.
  - **No single form** of documentation is required based on variety of available systems.
- Documentation can provide **internal MI** as well as assist internal and external auditors in **assessment of** effectiveness of SAR **monitoring** system.

Source: FFIEC's BSA/AML Examination Manual

Examiners' Expectations

- Examiners focus on **effectiveness of** SAR decision-making **process**, **not individual** SAR **decisions**.
  - Review of individual SAR decisions test effectiveness of SAR monitoring systems, reporting and decision-making process, holistically.
  - Do **not expect penalties** for **individual** SAR **decisions** except if decision represents ineffective SAR decision-making process.
- Example:
  - Firm's records showed excessive wire activity and penny stock transactions suggesting market manipulation. Decision-maker did not review red flags and did not file a SAR.
  - FINRA likely will cite firm for failure to implement SAR filing procedures, *rather* than failure to file SAR.

Source: FinCEN: The SAR Activity Review: Trends, Tips & Issues, Issue 1, p. 27 (May 2006)

Continued Monitoring and Activity

- **No** specific **requirements to monitor** the activity of names mentioned on **non-filed SARs**, or to classify these names as higher-risk.
- Decision to monitor names mentioned on non-filed SARs is at the **discretion of a financial institution**.
- FinCEN's guidelines suggest:
  - Reporting continuous suspicious activity every 90 days, and
  - Continue to review suspicious activity to determine whether other, non-SAR, actions are appropriate.
    - Actions may include **watch lists** or termination of customer relationship.

Source: FinCEN: The SAR Activity Review: Trends, Tips & Issues, Issue 1, p. 27 (October 2009)

Defensive filing – What is it, exactly?

2009 GAO Report; GAO-09-226 "Bank Secrecy Act-Suspicious Activity Reports" says "SARs filed as a result of the [bank's] effort to comply with the 30-day requirement could be considered defensive if, to meet the deadline, [depository institutions] filed SARs before fully investigating anomalous transactions."

"When in doubt, file."

1. Issues with defensive filing pros/cons:
   - An effective SAR program is appropriate to the size and complexity of the institution.
   - Examiners use SARs in their supervision of broker dealers.
   - Con: defensive SAR filing allows a regulator or internal auditor to criticize the SAR program as ineffective because it is not appropriately tailored to the institution's risks.
     - Example: a firm that files SARs indiscriminately based only on one element, e.g. cross border transfers to a high risk jurisdiction.
     - Why would an institution do this? There can be legitimate reasons.
     - It may be an appropriate filing based on a client's KYC profile if the client is a domestic low risk client with no history of cross border business.
     - It may not be an appropriate filing if the institution does not make an adequate determination of the nature of the behavior and instead files on any cross border wire to a high risk jurisdiction.
     - Document the rationale.

Defensive filing – Pros and Cons

Issues with defensive filing pros/cons continued:

- Pro: the decision to file fulfills the obligation to report suspicious activity.
  - Erring on the side of caution is a fine line.
  - The number of SAR filings does not determine the adequacy of a SAR program, but the lack of filings may flag a review.

Additional Cons:

- Additional monitoring of SAR suspects.
- Additional filtering or watch list "crowding"
- Additional head count to support program
- Validity of any analysis or trend monitoring done from SAR reporting data

2. The decision to file a SAR is inherently subjective.

   Examiner's focus should be on whether the institution has an Effective SAR decision making process, rather than on individual SAR decisions.

Enforcement Actions with notable SAR program findings

- AMSouth Bank, 2004:
  - Inability to identify or monitor high risk customers/transactions, therefore could not identify all transactions meriting the filing of a suspicious activity report.
  - Notable because of Deferred Prosecution Agreement for failing to file SARs in a "timely, complete and accurate manner."
- Arab Bank PLC, New York Branch, 2005:
  - Failure to adequately obtain information on funds transfers sufficient to determine whether it was required to file SARs.
- Union Bank, 2007
- HSBC, 2012:
  - Violated BSA SAR requirements by filing both untimely and incomplete SARs.
  - Failure to obtain necessary due diligence from Mexican affiliate to determine if activity was suspicious.
- JP Morgan Chase, 2013:
  - Significant shortcomings in SAR decision-making protocols.