Ballard Spahr LLP

2016 YEAR IN REVIEW

Money Laundering

PART ONE

INTRODUCING MONEY LAUNDERING WATCH

Financial institutions are facing an unprecedented level of scrutiny and enforcement in the area of money laundering. To keep you informed of the latest developments, we have launched a new blog focused exclusively on money laundering issues. Money Laundering Watch provides news, analysis, and insight from lawyers who advise many of the world's leading financial institutions and have first-hand experience in business and government. Please visit us at www.moneylaunderingwatchblog.com.

2016 was a busy year for developments in Anti-Money Laundering (AML), the Bank Secrecy Act (BSA), the criminal money laundering statutes, forfeiture, and related issues. In part one of our year-in-review, we discuss six key topics:

- The Panama Papers and its spotlight on the United States as a potential money laundering haven
- New Customer Due Diligence rules for financial institutions from the Financial Crimes Enforcement Network (FinCEN)
- New AML regulations from the New York Department of Financial Services (NYDFS) and related NYDFS enforcement
- FinCEN's and the Financial Action Task Force's (FATF) focus on the high-end real estate industry to combat money laundering
- FinCEN enforcement actions against banks and other lenders
- The gaming industry: enforcement actions and FATF recommendations

THE PANAMA PAPERS SPOTLIGHT THE ROLE OF THE UNITED STATES IN POSSIBLE GLOBAL MONEY LAUNDERING

As the world knows, the Panamanian law firm Mossack Fonseca was the subject of a stunning data breach of approximately 11.5 million financial and legal documents in April 2016. These leaked documents, the so-called "Panama Papers," have been publicized primarily by the International Consortium of Investigative Journalists and allegedly reveal a global system of undisclosed offshore accounts, money laundering, and other illegal activity. The effect of the Panama Papers has been explosive—the documents allegedly implicate world leaders, financiers, celebrities, and other prominent individuals from across the world in the use of shell companies to conceal assets and possible illegal activity from their home governments. The Office of the U.S. Attorney for the Southern District of New York has indicated that it is launching an investigation into these matters, as have enforcement agencies in many other countries.

To date, reports have suggested that relatively few U.S. citizens have employed the services—legitimate or otherwise—of Mossack Fonseca. However, and even before the Panama Papers came to light, reports also have suggested that individuals from across the globe have perceived that the United States is a secure place to hide assets. The states of Nevada, Wyoming, and Delaware—which allow for the quick creation of limited liability companies without identifying the true beneficial owners—have been criticized in particular. The Panama Papers have sharpened the national and global focus on the risks associated with money laundering, tax evasion, terrorist financing, and other illicit activity arising from the creation and use of U.S. entities whose true owners are obscured through corporate forms, as well as the need to identify the people behind these entities. The Panama Papers also illustrate how the growing possibility and ease of massive data breaches upends any notion that even the most powerful can count on privacy.

Although stated efforts at regulatory reform have been ongoing for years, the Panama Papers scandal clearly motivated the U.S. government to act in 2016 to address the alleged attempts by non-U.S. individuals to launder their proceeds of illegal activities through U.S. financial transactions. As discussed below, a key focus of the U.S. government's recent regulatory campaign—and of international enforcement efforts—is on identifying the true beneficial owners involved in financial transactions. This trend of expanding duties increases the potential risks—simply due to the expanding universe of required government scrutiny and filings—for entities and individuals accepting money from, or making representations on behalf of, possible bad actors from abroad or in the United States.

SPOTLIGHT ON BENEFICIAL OWNERSHIP:

FinCEN Finalizes Regulations Regarding Customer Due Diligence

As part of the U.S. Treasury Department's ongoing efforts to prevent possible bad actors from using U.S. companies to conceal money laundering, tax evasion, and other illicit financial activities, FinCEN issued, on May 11, 2016, a final rule to strengthen the customer due diligence (CDD) efforts of "covered financial institutions." This was one of the most important, if not the most important, AML developments in 2016. Covered institutions have until May 11, 2018, to comply with the new rule.

The CDD rule requires covered financial institutions, including banks, federally insured credit unions, broker-dealers, mutual funds, futures commission merchants, and introducing brokers in commodities, to identify the natural persons that own and control legal entity customers—the entities' "beneficial owners." The CDD rule was almost four years in the making; the process began with an Advanced Notice of Proposed Rulemaking in March 2012. The final release of this long-delayed rule appears to have been motivated in part by the April 2016 disclosure of the Panama Papers. Despite the issuance of this new rule, the Financial Action Task Force (FATF) still stated in its December 2016 *Mutual Evaluation Report on the Unites States' Measures to Combat Money Laundering and Terrorist Financing* that a continued lack of timely access to adequate, accurate, and current information on the beneficial owners of entities represented a "fundamental gap" in the U.S. AML regulatory regime.

The new CDD rule imposes several new obligations on covered financial institutions with respect to their "legal entity customers." These include corporations, limited liability companies, general partnerships, and other entities created by filing a public document or formed under the laws of a foreign jurisdiction. Certain types of entities are excluded from the definition of "legal entity customer," including financial institutions, investment advisers and other entities registered with the Securities and Exchange Commission, insurance companies, and foreign governmental entities that engage only in governmental, non-commercial activities.

For each such customer that opens an account, including an existing customer opening a new account, the covered financial institution must identify the customer's "beneficial owners." The CDD adopts a two-part definition of "beneficial owner," with an ownership prong and a control prong. Under this approach, each covered financial institution must identify:

- each individual who owns 25 percent or more of the equity interests in the legal entity customer; and
- at least one individual who exercises significant managerial control over the customer.

The same individual(s) may be identified under both prongs. If no single individual owns 25 percent or more, the covered financial institution may identify a beneficial owner under only the control prong. The same approach is used for nonprofit entities, which do not have "owners."

The covered financial institution must verify the identity of each beneficial owner identified by the customer. Importantly, the covered financial institution is entitled to rely on the customer's certification regarding each individual's *status* as a beneficial owner. However, the covered financial institution must obtain personally identifying information about each beneficial owner. This information must be documented and maintained by the financial institution.

The rule references a sample certified form, a copy of which is attached to the rule; the form is optional and the rule permits the covered financial institution to obtain and record the necessary information "by any other means that satisfy" its verification and identification obligations. Nonetheless, it is likely that many financial institutions will use the proposed certified form, or a variant, particularly because the rule allows a financial institution to rely on the representations made in the form in the absence of information that such reliance would be unreasonable. On the proposed form, the signatory—designated as the person opening the account—purports to identify the beneficial owners of the entity opening the account. Thus, although the CDD rule directly imposes new obligations on financial institutions, it is the certification form that may represent the greatest legal risk for individuals. If the person signing the form, or causing the form to be signed, knows or has reason to believe that the beneficial owners listed on the form are mere nominees intended to disguise the true beneficial owner, that person could be directly responsible for a fraud-related offense.

In response to industry concerns that the beneficial ownership identification obligation would require covered financial institutions to continually monitor the allocation of its customers' equity interests and the composition of its management team to update its beneficial ownership information, FinCEN made clear that the CDD rule does not require covered financial institutions to continuously update each customer's beneficial ownership information. Rather, the CDD calls for a "snapshot" of the customer's beneficial owners at the time of account creation. However, FinCEN does expect covered financial institutions to update beneficial ownership information when it detects relevant information about the customer during regular monitoring.

At the same time that FinCEN issued its final CDD rule, the Treasury Department also issued a related Notice of Proposed Rulemaking (NPR) aimed at identifying the beneficial owners of foreign-owned, single-member LLCs. The NPR became a final regulation on December 13, 2016. The rule imposes additional reporting and recordkeeping requirements on foreign-owned single-member LLCs by treating them as domestic corporations separate from their owners "for the limited purposes of the reporting and record maintenance requirements" imposed by the Internal Revenue Code. Now, each foreign-owned, single-member LLC is required to:

- obtain entity identification numbers from the IRS, which requires identification of a responsible party—a natural person;
- annually file IRS Form 5472, an informational return identifying "reportable transactions" that the LLC engaged in with respect to any related parties, such as the entity's foreign owner; and
- maintain supporting books and records.

Again emphasizing the focus on identifying beneficial ownership, former Treasury Secretary Jacob Lew explained in a letter to Congress that the new tax regulations are designed specifically "to close a current loophole in our system" that allows foreign persons to use U.S. LLCs to hide assets both in and outside of the United States. Highlighting the increasingly international aspect of AML and anti-tax evasion efforts, the NPR explained that the information obtained will be shared with other governments.

NEW AML REGULATIONS AND ENFORCEMENT FROM THE NYDFS

The New York State Department of Financial Services (NYDFS) emerged in 2016 as a leader in AML enforcement by issuing new and detailed AML regulations with the unique requirement of an individual certification of compliance, and by announcing significant settlements with foreign banks involving alleged AML violations.

NYDFS Finalizes Broad AML Regulations

On June 30, 2016, the NYDFS finalized a new regulation setting forth rigorous standards for monitoring and filtering programs to monitor transactions for potential AML violations and block transactions prohibited by the Office of Foreign Assets Control (OFAC). The regulation, which became effective on January 1, 2017, applies to all banks, trust companies, private bankers, savings banks, and savings and loan associations chartered under the New York Banking Law (NYBL); branches and agencies of foreign banking corporations licensed under the NYBL to conduct banking operations in New York; and check cashers and money transmitters licensed under the NYBL (collectively, the Regulated Institutions). The NYDFS regulation is instructive to all financial institutions as a benchmark for future standards potentially to be issued by other states and/or federal regulators.

The most notable provisions of the new regulation require each Regulated Institution to submit to NYDFS by April 15 of each year either a "Senior Officer Compliance Finding" or a resolution of its "Board of Directors" to certify compliance with the regulation. A "Senior Officer" is "the senior individual or individuals responsible for the management, operations, compliance and/or risk" of a Regulated Institution. The "Board of Directors" is the "governing board of every Regulated Institution or the functional equivalent if the Regulated Institution does not have a Board of Directors." The resolution or finding must state that the Senior Officer or Board of Directors has reviewed documents, reports, certifications, and opinions of officers, employees, outside vendors, and other parties as necessary to adopt the resolution or compliance finding. A Regulated Institution must maintain for NYDFS examination, for a period of five years, all records, schedules, and data supporting adoption of the board resolution or Senior Officer Compliance Finding.

This requirement is currently unique in the AML space, and resembles executive attestations required under Sarbanes-Oxley. It may encourage similar AML requirements under federal law or the laws of other states in the future. It also is consistent with the trend of increasing emphasis on individual executive liability in corporate enforcement cases, and may create practical tensions between an institution's board and its compliance department, because one or the other must submit the required form.

The final regulation also requires a Regulated Institution to maintain a manual or automated "Transaction Monitoring Program" and "Filtering Program" that are reasonably designed to, respectively, monitor transactions after their execution for potential AML violations and suspicious activity reporting, and interdict OFAC-prohibited transactions. The regulation lists eight attributes a Transaction Monitoring Program must have and five attributes a Filtering Program must have, to the extent applicable.

The final regulation lists eight additional requirements that must be part of both a Transaction Monitoring and Filtering Program, to the extent applicable. Among the areas covered by such requirements are data identification, validation of data integrity, accuracy and quality, data extraction and loading processes, governance and management oversight, vendor selection, and training.

NYDFS Fines Intesa Sanpaolo $325 Million for Alleged Repeated AML Violations

Capitalizing on its new AML regulations and perhaps attempting to seize the mantle of leading AML enforcement, the NYDFS announced several high-dollar value enforcement actions in 2016, all against foreign banks. The summary below provides an example.

On December 15, 2016, the NYDFS filed a consent order requiring Intesa Sanpaolo, S.p.A. to pay a $235 million civil monetary fine and extend the term of engagement with a NYDFS-appointed consultant for violations of the New York AML regulations. The consent order addressed the bank's alleged compliance failures spanning several years and arising from deficiencies in the implementation and oversight of its transaction monitoring system. These alleged compliance failures were discovered by a NYDFS-appointed consultant who was installed at the bank due to ongoing issues with the bank's AML compliance program.

The order enumerated several alleged AML and BSA violations including:

- A deficient transaction monitoring system at the bank's New York branch including:
    - Failing to maintain an effective and compliant AML program and OFAC compliance program, such as unauthorized clearing practices that were being cleared outside of the bank's prescribed written procedures;
    - Failing to maintain and make available true and accurate books, accounts, and records reflecting all transactions and actions, such as failing to track thousands of alerts generated by the bank's automated system that may have identified suspicious transactions; and
    - Failing to submit a report to the Superintendent upon discovering omissions of true entries.
- Shell company activity indicative of potentially suspicious transactions such as clearing thousands of transactions through the New York branch totaling hundreds of millions of dollars that bore indicia of potentially suspicious activity in relation to shell companies; and
- Non-transparent payment processing, such as:
    - Training employees to handle transactions involving Iran to conceal money-processing activities so they could not be readily flagged as transactions tied to a sanctioned entity;
    - Using non-transparent protocol to conduct more than 2,700 U.S. dollar clearing transactions worth more than $11 billion on behalf of Iranian clients and other entities possibly subject to U.S. economic sanctions; and
    - Failing to fully comply with a 2007 agreement, which required the bank to implement and maintain an effective AML compliance program.

In addition to the $235 million penalty, the consent order compels the bank to extend the engagement of its independent consultant for up to two years to further analyze and test the bank's efforts to remediate its violations. Within 60 days of the consultant's report, the bank must submit a revised AML and BSA compliance program and internal audit program; a plan to enhance oversight of the bank's compliance program by bank management; an enhanced customer due diligence program; and a program ensuring identification and timely reporting of all known or suspected violations of law or suspicious transactions to authorities.

THE HIGH-END REAL ESTATE INDUSTRY COMES UNDER AML SCRUTINY

Addressing money laundering vulnerabilities in the high-end real estate industry became a major FinCEN initiative in 2016. Reinforcing these efforts, the Financial Action Task Force (FATF) report on U.S. anti-money laundering efforts stressed that U.S. regulators and the real estate industry should do more to address money laundering and terrorist financing risks. These developments will have ongoing consequences for nonbank mortgage lenders, title insurance companies, and other real estate professionals.

Real Estate Risks and Mortgage Lender Compliance: FinCEN's Increasing Focus on AML Risks in Real Estate

In January 2016, FinCEN issued two geographic targeting orders (GTOs) aimed at combating money laundering in all-cash real estate transactions in the Borough of Manhattan, New York, and Miami-Dade County, Florida—two areas identified by FinCEN as having "a higher than average percentage of all-cash transactions." The GTOs, which took effect in March 2016, required certain title insurance companies to identify the natural persons behind entities using cash to purchase high-end real estate—properties with a sales price of more than $1 million in Miami-Dade County and more than $3 million in Manhattan.

In an April 12, 2016, speech, former FinCEN Director Jennifer Shasky Calvery highlighted the risks in the industry. She noted that although most real estate transactions already are subject to AML scrutiny through the AML programs and controls of banks and residential mortgage lenders and originators, "none of the parties involved in the transaction are subject to AML program requirements" in the case of an all-cash purchase made "without a mortgage issued by a bank or mortgage broker." According to former Director Shasky Calvery, the beneficial ownership identification requirement is key to AML risk assessment and enforcement in this area because the use of shell company purchasers "is often enough to dramatically increase the difficulty of tracking the true owner of a property in a transaction."

In August 2016, FinCEN implemented a major expansion of its GTOs aimed at high-end cash buyers of real estate to a total of six separate metropolitan areas. The August GTOs covered all title insurance companies, rather than the handful of insurers subject to the initial orders issued in January 2016 that expired on August 27, 2016.

In the expanded GTOs, the two narrowly drawn areas in the initial GTOs were expanded to include all five boroughs of New York City as well as Broward County and Palm Beach County in Florida. Four other markets were added: Los Angeles County, California; San Diego County, California; the three California Bay Area counties of San Francisco, San Mateo, and Santa Clara; and Bexar County, Texas, which includes San Antonio. Similar to the initial GTOs, each county has a separate dollar threshold for covered transactions. The new GTOs are in effect from August 28, 2016, until February 23, 2017.

The scope of "covered transactions" that must be reported on a Form 8300 also was significantly expanded in the August 2016 GTOs by the addition of personal checks and business checks to the types of monetary instruments that trigger reporting.

FinCEN has cited the diverse approaches to real estate transactions and closings in different states (and even municipalities) as an impediment to expanding compliance requirements in the real estate industry. The title insurance industry was a convenient first step for FinCEN to expand its efforts because of the percentage of all-cash transactions that involve title insurance and because title insurers are regulated at the state level. Now that FinCEN has taken this step, we expect the agency to use the experience and data from the GTOs to extend its reach to more participants and transactions in the real estate industry.

FATF Report Highlights Real Estate Risks and Mortgage Lender Compliance Shortcomings

The December 2016 FATF *Mutual Evaluation Report on the United States' Measures to Combat Money Laundering and Terrorist Financing* repeatedly highlighted the need for U.S.

regulators and the real estate industry to do more to address money laundering and terrorist financing risks.

The FATF report identified “high-end real estate” transactions as an area needing priority action. In the report, the FATF assessors recommend that FinCEN take further action after analyzing the outcomes from FinCEN’s 2016 GTOs for high-end cash transactions in several U.S. real markets.

The FATF assessors noted that 25 percent of the market in real estate does not involve financing—particularly in high-end transactions. Accordingly, they concluded that the U.S. regulatory “strategy of addressing [money laundering and terrorist financing] risk in the real estate sector through the financial sector has been of only limited value as it focused attention mostly on lower risk (the mass market) rather than the high-end market.”

The FATF report’s executive summary also noted that “Residential Mortgage Lenders and Originators [RMLOs]… do not seem to have a good understanding of [money laundering] vulnerabilities in their sector or the importance of their role in addressing them.” In the body of the report, the assessors elaborated that, “although banks have reasonably good AML/CFT [Combating the Financing of Terrorism] programs overall, the same cannot be said of RMLOs, whose programs are still in the early implementation stage…” The assessors further noted that RMLOs’ “low understanding of risks is reflected in the very low number of SARs [Suspicious Activity Reports] being reported by them, most of which were related to mortgage fraud.”

The FATF evaluation also looked closely at the role of real estate agents and other parties (including condominium associations and cooperative boards) in the high-end market. Although acknowledging the limited role of real estate agents, the report notes that “neither the real estate agents nor the RMLO sector appeared to understand what the [money laundering] risks in relation to high-end real estate are or what the appropriate mitigation measures would be.”

These finding about risks as well as the current compliance shortcomings point to continued and expanded focus by FinCEN on the real estate industry. Continued outreach and further rulemakings seem likely. We will have to wait and see whether enforcement actions are forthcoming as well. In the meantime, nonbank mortgage lenders should reassess their AML/CFT programs, including their SAR reporting policies and procedures, given the shortcomings cited in the FATF report.

AML/BSA ENFORCEMENT INVOLVING BANKS AND OTHER LENDERS

FinCEN continued in 2016 to obtain penalties against banks and other lenders based on alleged AML failures. However, FinCEN encountered determined resistance in the ongoing fight with a foreign bank over the bank’s ability to maintain correspondent accounts in the United States.

District of Columbia District Court Again Stays Section 311 Action Against FBME Bank

Pursuant to Section 311 of the of the USA Patriot Act, FinCEN is authorized to designate foreign financial institutions as being “of primary money laundering concern” and to take any of five “special measures” against institutions so designated. FinCEN can impose the most severe, fifth special measure—allowing it to prohibit or restrict domestic financial institutions from opening or maintaining correspondent accounts for designated foreign financial institutions—only by issuing a regulation under the Administrative Procedure Act (APA). Ongoing litigation surrounding a Section 311 designation implicates the important question of how much FinCEN must explain itself under the APA, and the extent to which FinCEN must provide objective comparative benchmarks—such as the practices of other financial institutions—when it concludes that an institution has engaged in an unacceptably high degree of suspicious transactions.

On July 22, 2014, FinCEN issued a Notice of Finding designating FBME Bank Ltd., a Tanzanian-chartered bank operating primarily out of Cyprus, as an institution of primary money laundering concern based on its alleged involvement in money laundering and other illicit activity. FinCEN later promulgated a final rule imposing the special measure. Before the rule took effect, FBME brought suit against FinCEN seeking an order declaring the final rule unlawful and permanently enjoining its enforcement. FBME alleged, *inter alia*, that FinCEN violated the APA by failing to give FBME sufficient notice of the rule’s factual and legal basis and had acted arbitrarily and capriciously by failing to properly consider alternative measures against FBME. On August 27, 2015, the District Court for the District of Columbia granted FBME’s preliminary injunction. The court ruled that FBME likely would be able to show that FinCEN failed to disclose to FBME the information that led to the designation, preventing FBME from responding. The court also ruled that FBME likely could show that FinCEN erred by failing to consider alternative, less onerous sanctions.

Rather than appealing the injunction, FinCEN successfully sought a voluntary remand to permit it to revise its rulemaking regarding FBME. FinCEN published its second final rule on March 31, 2016, again concluding that FBME is of primary money laundering concern and that the fifth special measure is appropriate. The parties filed cross-motions for summary judgment. On September 20, 2016, the district court issued a detailed opinion and again remanded, finding that FinCEN had not meaningfully responded to FBME's criticism of FinCEN's treatment of aggregate Suspicious Activity Report (SAR) data, including the bank's critique that FinCEN provided no comparative benchmarks referencing other similarly situated banks to support its claim that FBME-facilitated transactions were the subject of an unusually high number of SAR filings.

On December 1, 2016, FinCEN published a supplement to its final rule that attempted to respond to FBME's comments, and the bank has filed additional pleadings. The district court has not yet ruled to resolve the issue. The outcome may provide valuable insight into the degree to which FinCEN may be compelled under Section 311—and perhaps in other enforcement contexts—to explain, under the guise of a procedural challenge, the substantive and objective merits of its decision that a particular institution has engaged in an unacceptable number of suspicious transactions.

As the district court explained in its September 2016 opinion, "FinCEN provides no comparative benchmarks referencing other banks to support its assertions that FBME has a 'large number' of shell company customers or that the Bank has facilitated a 'high volume' of U.S. dollar transactions by such shell companies. . . . Nor does the agency attempt to explain why such benchmarks may be unnecessary, or infeasible to provide, or how else the agency may have applied its expertise and regulatory experience in the absence of specific benchmarks." Whether FinCEN can provide such benchmarks, or compellingly argue that such benchmarks are not necessary to evaluate adequately its decisions, is an issue that should be closely watched.

Other Enforcement Actions Involving Banks and Credit Unions

FinCEN assessed two significant AML-related civil money penalties in 2016 against a bank and credit union. First, FinCEN and the Office of the Comptroller of the Currency announced a combined $4 million civil money penalty against Gibraltar Private Bank and Trust Company for allegedly willfully violating the AML requirements of the BSA. According to FinCEN, Gibraltar's AML program deficiencies ultimately caused the bank to fail to timely file at least 120 SARs involving nearly $558 million in transactions from 2009 to 2013. These deficiencies also unreasonably delayed Gibraltar's SAR reporting on accounts related to a $1.2 billion Ponzi scheme led by Florida attorney Scott Rothstein.

Second, FinCEN assessed a $500,000 civil money penalty against Bethex Federal Credit Union for alleged AML violations. Bethex was a federally chartered, low-income designated, community development credit union. In December 2015, the National Credit Union Administration liquidated Bethex, determining that it was insolvent with no prospect of returning to viable operations. According to FinCEN, Bethex failed to detect and report suspicious activity in a timely manner to FinCEN and did not file any SARs from 2008 to 2011. In 2013, due to a mandated review of prior transactions, Bethex late-filed 28 SARs. The majority of the suspicious activity involved high-volume, high-dollar transfers outside of Bethex's expected customer base by Money Services Businesses allegedly capable of exploiting Bethex's AML weaknesses. Most of those SARs were allegedly inadequate and contained short, vague narratives encompassing a broad summary of multiple and unrelated instances of suspicious activity.

THE GAMING INDUSTRY: ENFORCEMENT ACTIONS AND FATF RECOMMENDATIONS

Because the gaming industry has been known to attract some bad actors who attempt to use its financial services to conceal or transfer illicit wealth, AML compliance remains a key concern in this growing business sector.

FinCEN Enforcement Actions in Gaming Focus on Culture of Compliance

Three significant 2016 enforcement actions emphasized that the gaming industry is particularly relevant to FinCEN's focus on the importance of cultivating a culture of robust AML/BSA compliance within financial institutions. These enforcement actions also suggest that some segments of the gaming industry are still in the process of attaining a fully mature AML compliance culture.

- **Cantor Gaming:** On October 3, 2016, FinCEN assessed a $12 million civil penalty against Cantor Gaming for alleged "egregious and systemic" violations of the program, reporting, and recordkeeping requirements of the BSA. In particular, FinCEN alleged that Cantor failed to: provide sufficient AML training for its officers and employees; use all available information to detect and report suspicious transactions; and maintain sufficient internal controls to detect ongoing criminal activity by its Director of Risk Management and Vice President and his co-conspirators.

"When greed clouds judgment within the leadership of an organization, and when even explicit warnings are ignored, it is a sign that the organization's compliance culture is damaged or nonexistent," FinCEN Acting Director Jamal El-Hindi remarked in a press release about the settlement.

- **Hawaiian Gardens Casino:** On July 15, 2016, FinCEN assessed a $2.8 million civil penalty against card club Hawaiian Gardens Casino for repeated alleged BSA violations, including failure to implement and maintain an effective AML program and failure to comply with BSA reporting and recordkeeping requirements. FinCEN specifically attributed these failures to Hawaiian Gardens' lack of compliance culture, stating that "leadership at [the card club] did not take an active role as it should have in promoting a strong culture of compliance." FinCEN noted that: the club's BSA committee, which included casino management, failed to meet as required by its charter; its leadership did not review and approve its risk assessment; and its management failed to establish policies and procedures regarding customer identification. FinCEN also criticized Hawaiian Gardens' failure to take corrective action in response to findings of significant BSA violations by both the IRS and the card club's own independent consultant, allowing violations to go uncorrected for years.

- **Sparks Nugget:** On April 5, 2016, FinCEN assessed a $1 million civil penalty against Sparks Nugget, Inc., relating to its alleged willful and repeated violations of the program, reporting, and recordkeeping requirements of the BSA. In particular, FinCEN alleged that Sparks Nugget had systemic compliance failures, a poor compliance culture, and "a blatant disregard for AML compliance that permeated all levels of [the casino]." FinCEN said Sparks Nugget: "chose not to file rightfully prepared [SARs];" had a committee to determine whether to file SARs that never met and several of whose putative members did not know that they were on the committee; and ordered its compliance manager not to interact with BSA examiners. FinCEN also criticized the casino for failing to use the information it gathered about customers to ensure BSA compliance, and instead only used it to further business interests.

FATF Report Recommends Expanding Gaming Examinations and Section 314 Efforts; Praises Progress in Gaming Industry Compliance

The Financial Action Task Force (FATF) highlighted in its December 2016 *Mutual Evaluation Report on the United States' Measures to Combat Money Laundering and Terrorist Financing* the "excellent results" in compliance and supervision in the U.S. gaming industry during the period of 2007 to 2016. The report noted that efforts by regulators and the gaming industry have led to enhanced AML and CFT compliance. The assessors specifically mentioned the efforts of the American Gaming Association (AGA), including its study, *Investing in America's Financial Security: Casinos' Commitment to AML Compliance*. The FATF report also included several recommended actions related to gaming.

The FATF report recommended that FinCEN, the IRS, and state regulators "should continue their focus on casinos, including [IRS] examination work, and expand it to include some of the smaller and less sophisticated players." Given the progress made and significant engagement of FinCEN with the industry over the past several years, we believe the bar has been raised for AML/CFT programs. Accordingly, we recommend that all gaming companies, especially those with less mature AML/CFT programs, evaluate their programs against FinCEN guidance and the *AGA Best Practices for AML Compliance*. This should be a priority because we expect further enforcement activity in 2017.

The FATF report also focused on information sharing. The report includes a recommended action to "operationalise casinos' participation in information sharing" under section 314(a) of the USA Patriot Act and "further encourage" use of section 314(b). All gaming companies should examine their readiness for handling section 314(a) requests. Those companies with more mature AML/CFT programs also should consider whether to participate in voluntary information sharing under section 314(b).

Finally, we believe that the approach taken by FinCEN and the gaming industry over the past several years may provide a useful model for other industries, such as real estate, for how to partner with FinCEN to develop AML/CFT compliance requirements that effectively address money laundering risks in a manner that reflects the operating environment of the industry.

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