Anti-Money Laundering

2015 Edition

Sources of funds
- Tax crimes, fraud, embezzlement, drugs, theft, bribery, corruption

Placement
Goal: To deposit criminal proceeds into the financial system
Common Methods:
- Change of currency
- Change of denomination
- Transportation of cash
- Cash deposits

Layering
Goal: Conceal the criminal origin of proceeds
Common Methods:
- Wire transfers
- Withdrawals in cash
- Cash deposits in multiple bank accounts
- Split and merge of various bank accounts

Integration
Goal: Create an apparent legal origin for criminal processes
Common Methods:
- Creating fictitious loans, turnover, capital gains, contracts, financial statements etc.
- Disguise ownership of assets
- Use of criminal proceeds in transactions with third parties

Use of proceeds for personal benefit

Figure 1: stages of money laundering

Continuing Education Course
for Insurance Agents and Brokers

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Anti-Money Laundering

Continuing Education Course for Insurance Agents

Introduction

The September 11 attacks showed the terrible destruction and loss of life that money laundering could make possible. As a result, Congress passed the USA PATRIOT Act, which greatly strengthens anti-money laundering laws and places increased responsibility on financial institutions to detect and report signs of money laundering.

This course is intended to provide agents and brokers with knowledge of money laundering and terrorist financing and the ways in which the insurance industry might be used to engage in such activities. In addition, it provides an in-depth look at the requirements imposed by the Treasury Department regulations, as well as the means by which brokers and agents may be integrated into insurers’ AML programs.

What Insurance Agents and Brokers Should Expect under the New Anti-Money Laundering Regulations for Insurance Companies

Insurers and agents now have additional responsibilities related to anti-money laundering and terrorist activities as a result of changes in the Bank Secrecy Act and the passing of the USA PATRIOT Act. This will be a new experience for the majority of those associated with the insurance industry. Agents and insurers have traditionally felt that they were immune from such activity. Today we realize that cash value life insurance and annuities products offer an excellent method of money laundering.

Financial Crimes Enforcement Network (FinCEN), the U. S. Treasury’s chief anti-money laundering watchdog, in October 2005 announced that insurance companies would have to comply with the same laws already on the books for banks and broker dealers.

While banks and broker dealers have long been subject to such regulations, insurance companies and other parts of the financial industry have remained relatively immune, until now.

The USA PATRIOT Act includes provisions intended to prevent the financial services industry, including the insurance industry, from being used for money laundering and terrorist financing by criminals and terrorists.

Under two final rules announced by the Financial Crimes Enforcement Network (FinCEN), certain U.S. insurance companies are required to both establish anti-money laundering (AML) programs and file Suspicious Activity Reports (SARS) on clients who exhibit behavior that warrants concern and government investigation. Insurance companies subject to these rules must establish an anti-money laundering program and start filing Suspicious Activity Reports 180 days after the date of the publication of the final rules in the Federal Register May 2, 2006.

The final rules apply to insurance companies that issue or underwrite certain products that present a high degree of risk for money laundering or the financing of terrorism or other illicit
activity. The types of contracts most vulnerable have cash values that can be easily accessed. The insurance products subject to these rules include:

- Permanent life insurance policies, other than group life insurance policies;
- Annuity contracts, other than group annuity contracts;
- Any other insurance products with features of cash value or investment features.

At minimum, insurance companies subject to the rule requiring an anti-money laundering program must establish a program that comprises four basic elements:

- A compliance officer who is responsible for ensuring that the program is implemented effectively;
- Written policies, procedures, and internal controls reasonably designed to control the risks of money laundering, terrorist financing, and other financial crime associated with its business;
- Ongoing training of appropriate persons concerning their responsibilities under the program; and
- Independent testing to monitor and maintain an adequate program.

“These rules represent key steps in ensuring that the Bank Secrecy Act is applied appropriately to these businesses and in protecting the insurance industry from potential abuse by those seeking to launder money or finance terrorism or other illicit activity, said William J. Fox, Director of the Financial Crimes Enforcement Network. “The rules enhance the protection of the U.S. financial system generally, given that the characteristics of financial products, including certain insurance products, can make those products vulnerable to those seeking to launder money or finance terrorism or other illicit activity.”

Although insurance agents and brokers are not required to have their own anti-money laundering programs, the Treasury Department and FinCEN have stated that insurance agents and brokers are expected to play an important role in implementation of these programs by insurers. The ultimate responsibility for preventing money laundering falls on insurers, but they will need to rely on their intermediaries to some degree since they are in the best position to recognize unusual or suspicious behavior.

The insurance industry includes insurers, reinsurance companies, and their intermediaries. Intermediaries relates to agents, brokers or others who would be performing services on behalf of an insurer. Agents and brokers have not previously received education in such matters but must now do so. Agents and brokers are likely to be the first individuals to have contact with criminals or members of terrorist groups wishing to launder money or conceal the origins of their funds. Those who wish to launder illicit funds will seek out agents and brokers who are unaware of, or are not concerned with anti-money laundering procedures.

**Terrorism and Criminal Activity**

Criminals look for ways of concealing the origins of illegitimate funds since knowledge of their illegal activities would bring about legal consequences. Those involved in terrorist activities look for ways to finance their acts of violence while concealing their intent. Insurance products and transactions provide an opportunity to launder money and to finance terrorism.
Insurers were not always recognized as having money-laundering risk. Some still feel the insurance industry is not at as great a risk as some other industries, however risk does exist. Insurers and agents can knowingly or unknowingly aid in money laundering and the financing of terrorism.

**What is Money Laundering and Terrorist Financing?**

**Money laundering**

Money laundering is a varied and often complicated process that can, but does not always, involve cash transactions. It is the process by which a person conceals (or attempts to conceal) the existence, illegal source or illegal application of income, or disguises the income to make it appear legitimate. For example, it can involve:

- Evading or falsifying certain reports required by the U.S. and certain state governments;
- Participating in a transaction that someone knows involves criminally derived proceeds valued at more than $10,000;
- Transporting, or helping transport, money or property that someone believes is criminally derived with the intent to hide its source or ownership or evade the payment of taxes;
- Engaging in a financial transaction involving criminally derived property while intending to promote illegal activity; or
- Attempting to do any of the activities listed above.

Those involved in criminal or terrorist activities want to avoid the attention that sudden wealth would bring. Therefore, they look for means of merging their illegal funds with legitimate business funds, such as insurance proceeds. The process of money laundering usually involves three stages. First, the money is placed with an unsuspecting financial institution or business. Next, the money is moved through “layers” of financial instruments until the original source of the money becomes obscured or impossible to ascertain. Finally, the money is “integrated into legitimate investments or businesses. The goal is to make it difficult or impossible to determine where the funds came from.

**Terrorist financing**

Terrorist financing involves the use of money, which may be lawfully obtained, to fund illegal activities. Because the transactions often have a legitimate origin and can often involve small amounts of money, terrorist financing can be more difficult to identify than money-laundering activities.

The final anti-money laundering rules apply to insurance companies selling covered products, as defined in the rule. The final rule focuses on insurance products possessing features that make them susceptible to being used for money laundering or the financing of terrorism. This typically includes life insurance policies with cash surrender value features and annuity products. Cash values can be redeemed by a money launderer or can be used as a source of further investment of tainted funds. By taking out policy loans against the cash values, these individuals have received legitimate funds in place of their tainted funds. Similarly, annuity contracts offer an ideal financial vehicle for laundering illicit funds or funds whose origins must be kept secret. Annuity products allow the policyowner to exchange illicit funds for an immediate or deferred income stream or clean funds upon redemption. Products without cash
values, such as term life insurance products or group policies do not pose the same opportunities to money launderers.

A Global Problem

The estimated amount of money laundered globally in one year is 2 - 5% of global GDP, or $800 billion - $2 trillion in current US dollars. Though the margin between those figures is huge, even the lower estimate underlines the seriousness of the problem governments have pledged to address.”

As the international community recognized the role insurers could play in money laundering activities they focused on creating corrective measures. The Financial Action Task Force (FATF) was established in 1989 at the G-7 Summit in Paris as a result of international concern. Starting with 16 members, today membership has grown to 31 countries and two international organizations. The Financial Action Task Force developed recommendations for insurers focusing on businesses involving the underwriting and placement of life insurance and other investment related insurance having cash values or surrender values.

The Financial Action Task Force (FATF) made specific recommendations regarding the steps insurers and their employees and intermediaries could take to reduce the risk terrorist activities presented:

1. Identify their clients and potential clients using reliable, independent source documents, data and information.
2. Determine whether the client is acting on behalf of another person. Take reasonable steps to obtain sufficient identification data to verify the identity of that other person.
3. Identify the ultimate beneficial owner, and take reasonable measures to verify the identity of that beneficial owner so that the insurer is satisfied that it knows whom the person or entity is.
4. Obtain information on the purpose and intended nature of the business relationship and any other relevant factors.
5. Conduct ongoing due diligence on the business relationship and scrutiny of transactions undertaken throughout the course of that relationship to ensure that the transactions being conducted are consistent with the insurer’s knowledge of the customer/client and the beneficial owner, where applicable. This would include knowledge of their business and risk profile including the source of funds to the extent that is reasonable and practical.

In the fight against money laundering, federal efforts have focused primarily in three areas: criminalizing certain types of activity, imposing reporting requirements on financial institutions and targeting nations or specific geographical locations thought to be “havens” for money launderers.

Legal Requirements Adopted

Since 1970 most financial institutions have had anti-money laundering (AML) laws, requiring reporting and record keeping procedures. Both the Bank Secrecy Act (BSA) and various NASD and SEC requirements have sought to prevent money laundering.
The U.S. Treasury Department, the SEC, and other governmental agencies have developed new and extensive anti-money laundering policies and regulations. These regulations cover virtually all financial institutions which receive or send potentially large amounts of money to retail clients, business entities or trust accounts. The term “financial institutions” now includes banks, securities broker/dealers, mutual fund companies, commodity futures merchants, credit unions, trust companies, insurance companies, as well as casinos, dealers in precious metals, stones or jewels, pawnbrokers, travel agencies, sellers of automobiles, airplanes and boats, and more.

Over the years, several laws have been passed and other actions taken to curb money laundering, including:

**Bank Secrecy Act of 1970**

Under the Bank Secrecy Act of 1970 financial institutions are prohibited from selling, using or accepting money orders, bank checks, cashier’s checks or traveler’s checks for more than $3,000 in currency. Larger amounts may only be accepted if the cash or cash equivalent and the purchaser’s identity is verified and recorded. Even when a financial institution does not sell these items, the rules still apply.

The final rule of the BSA requires insurers to implement procedures for obtaining customer identity information and to file suspicious activity reports when applicable. The Money Laundering Control Act (MLCA) prohibits any person from *knowingly* engaging in any monetary transaction in criminally derived property valued at $10,000 or more. It is only necessary to know that money was somehow involved in criminal activity, not that these particular funds were involved or derived from a specific illegal act.

**Money Laundering Control Act of 1985**

This law makes it a federal crime to engage in money laundering or to attempt to structure transactions. The Money Laundering Control Act added provisions to the Bank Secrecy Act (BSA) including a prohibition against structuring transactions, which means making multiple small transactions from one lump sum, the point of which is to conceal the origins of the money. By making smaller multiple transactions the depositor hopes to avoid the BSA’s reporting threshold, which would alert authorities. The multiple smaller deposits may be made in the names of multiple people, using the money launderer’s family and friends to open accounts. They might also use a single account, making multiple small deposits, each of which are under the reporting limits.

**Additional Legislation**

- Creation of the **Financial Crimes Enforcement Network (FinCEN)** as a bureau of the Treasury Department
- **Annunzio Wylie Anti-Money Laundering Act of 1992** expanding reporting obligations of banks to include filing of Suspicious Activity Reports.
The USA PATRIOT Act

By far the most comprehensive and all-inclusive legislation was passed in October of 2001, officially titled “Uniting and Strengthening America by Providing Appropriate Tools required to Intercept and Obstruct Terrorism.” This law is generally referred to as the USA PATRIOT Act.

Title III of the USA PATRIOT Act, referred to as the International Money Laundering Abatement and Anti-terrorist Financing Act of 2001, requires financial institutions to address anti-money laundering (AML) provisions and amendments that were added to the Bank Secrecy Act. It is this act that extends the requirements to insurers. This Act requires government-institution information sharing, including voluntary information among financial institutions. Customer identification verification and related due diligence is required as well as anti-money laundering programs in the financial services industry.

The USA PATRIOT Act greatly strengthens anti-money laundering laws, enhances civil and criminal penalties for violations, and grants new law enforcement powers and surveillance capabilities. It also significantly strengthens earlier anti-money laundering laws by imposing new obligations on financial institutions, including insurance companies. The Act also amends the original Bank Secrecy Act and existing criminal statutes covering money laundering.

Not all insurers are considered at risk for money laundering, so this affects some insurers to a greater degree than others. Only those dealing in specific products are included. Broker-dealers, involved with securities, already have AML requirements and are not required to duplicate those already in place by the newer insurance company requirements.

Currency and Monetary Instrument Transportation Report (CMIR)

This report is required when a person transports, mails, or ships currency or other monetary instruments into or out of the United States, and the aggregate amount exceeds $10,000. For this reporting requirement, the term “monetary instrument” includes cash, cash equivalents, money orders, traveler’s checks, personal checks, business checks, third-party checks, and securities issued in bearer forms.

Report of Foreign Bank and Financial Accounts (FBAR)

This report is required if an individual has an interest in, or signature or other authority over a financial account in a foreign country where the aggregate value of the accounts exceeds $10,000.

Funds Transfers and Transmittals

Whenever broker/dealers, mutual fund companies or insurance carriers complete transmittals or transfers of funds, including wire fund transfers of $3,000 or more, they must collect, retain and record certain information on the transmittal order including the name and address of the transmitter and recipient, the amount of the transmittal order, the identity of the recipient’s financial institution, and the recipient’s account number.
Broker/dealers are required to file form SAR-SF with FinCEN. Broker/dealers must report known or suspected federal criminal offenses at certain dollar levels, or suspicious transactions involving $5,000 or more that they believe:

- Involve funds derived from illegal activity or an attempt to hide or disguise funds or assets derived from illegal activity;
- Are designed to evade the requirements of the BSA or the Patriot Act;
- Have no apparent lawful or business purpose; or
- Vary substantially from normal practice.

Using the OFAC List

The Office of Foreign Assets Control (OFAC) is part of the Treasury that administers and enforces certain economic and trade sanctions. In particular, OFAC prohibits transactions with and requires the freezing of assets with certain countries, organizations, and individuals in order to further U.S. foreign policy and national security goals. OFAC requires financial institutions to “block” transactions before they are executed, rather than subjecting violators to penalties after the fact.

These provisions prohibit doing business with identified enemies of the United States or with Specially Designated Nationals (SDN), as determined by OFAC and other government agencies. Many financial institutions routinely check their customers against this list. Should a professional encounter such a person (SDN), they must contact OFAC within ten days. If a Specially Designated National is discovered to already hold an open account, it must be frozen, including any pending transfers.

The Office of Foreign Asset Control prohibits working with identified money launderers, which includes companies and countries as well as individuals. Sanctions are currently in place against the Balkans, Burma, Cuba, Iran, Iraq, the Ivory Coast, Liberia, North Korea, Sudan, Syria, and Zimbabwe. Members of drug organizations, such as Columbian drug cartels have also been identified as money launderers under the Foreign Narcotics Kingpin Designation Act. These lists are updated continually, so there may be changes or additions to the previous list.

OFAC maintains a website (www.treas.gov/ofac) listing entities, organizations, and individuals with whom transactions are prohibited. This list should be consulted whenever a new account is opened, and checked frequently against customer lists to ensure that there are no transactions occurring with “blocked” individuals or entities.

If a customer is on the OFAC list, the broker/dealer must “block” the transaction and immediately report the findings to OFAC.

Penalties

Severe penalties can be imposed on both individuals and firms that violate the anti-money laundering laws. For example, criminal penalties include fines of up to $500,000 or twice the value of the property involved, whichever is greater. Prison sentences of up to 20 years can also be imposed. Civil penalties include fines of up to $10,000 or the value of the funds involved in the transaction, whichever is greater.
Additional criminal and civil penalties can be imposed under the Bank Secrecy Act, including up to 5 years imprisonment, a criminal fine of up to $250,000, or both. If the individual is violating the BSA along with any other laws, or engaging in a pattern of illegal activity, a criminal fine of up to $500,000 can be imposed along with up to 10 years imprisonment, or both.

The USA PATRIOT Act increased both the civil and criminal penalties that can be imposed for violating anti-money laundering laws including criminal and civil penalties for violations of certain BSA provision, including up to two times the amount of the transaction, or $1,000,000.

**Broker-Dealer Requirements**

Some insurance products or insurers are affiliated with broker-dealer firms. As a result, they may be subject to National Association of Securities Dealers (NASD) requirements. NASD has specific rules for companies offering certain products, such as variable annuities. Applicants must provide certain information when opening accounts, which includes:

1. Their legal name.
2. Place of residence.
3. Whether of legal age (usually 18 years old in most states).
4. Signature of registered representative who introduces the account and the signature of the member, partner, or officer/manager who accepts the account.
5. If the customer is a corporation, partnership, or other legal entity, the names of any persons authorized to transact business on behalf of the entity must be obtained.
6. NASD Rules 2110 and 2310 require additional information.
   (a) 2110 requires the firm to maintain just standards of trade, and
   (b) 2310 requires the firm to gather, as much as possible, information to help determine the suitability when making recommendations. Suitability information includes the client’s financial status, tax status, and investment objectives.

**Customer Identification Programs (CIP)**

**Know Your Customer (KYC)**

A program regulated by the PATRIOT Act, **Know Your Customer (KYC)**, requires verification of the client’s identity to the extent that is reasonable and practicable of any person seeking to open an account or place an application. The Act requires firms to maintain records of the information used to verify an individual’s identity and check the names against a government list of suspected terrorists. KYC requires risk-based determinations about:

- Their customers,
- Their customer’s sources of income, and
- Their customer’s expected transactions.

Customer Identification Programs (CIP) that broker-dealers adhere to must be appropriate for the size of their business. It should be regularly reviewed to ensure methods of verification are accurate and current. Additionally, there should be procedures to check a client’s name against the government’s list of known terrorists.
Customer Identification Programs may use non-documentary means of identification if necessary or desirable. Companies might use reporting agencies, references, checking account information, or other public sources when the identification used by their client has expired or when the client reports that their identification has been stolen or is otherwise unavailable.

Broker-dealers should notify their customers that such identity verification procedures exist. While suspicious activity reports are made without notifying the client, identity verification is not kept secret. Government issued identifications, usually a driver’s license or passport, are typically required as part of the process. For businesses, a certificate of incorporation or a business license is used. Personnel are not required to verify whether or not the identification is genuine; they must merely record the information.

The Financial Modernization Act of 1999 (Gramm-Leach-Bliley Act) protects personal financial information that might be shared by financial institutions. Prior to this Act it was common for the information gathered to be sold to other institutions. It is not permissible to obtain client information from financial institutions under false pretenses. Institutions must give clients clear notice of how and when information will be shared.

If any identification does not seem genuine the agent must be suspicious. While the agent is not legally required to investigate the authenticity of produced identification material, if it seems to be false, it is necessary to note this with the application sent to the insurer. In fact, any indication the agent has of potential money laundering activities must be reported to the insurer.

**Customer Due Diligence (CDD)**

There is little doubt that customer due diligence (CDD) is required on all levels of the insurance industry if money laundering activities are to be minimized. The quality of customer identification is pivotal to preventing the use of insurance products for terrorism purposes. Under the USA PATRIOT Act, verification of new accountholders will be focused on. The Treasury Secretary issued regulations establishing standards for customer identification that must be applied to all new account applicants. Insurers must:

1. Verify the identities of the new account holders.
2. Maintain records of the information used to verify a person’s identity.
3. Consult government lists of known or suspected terrorists and associated terrorist groups prior to issuing policies.

Failure to identify potential terrorists and criminals will allow money laundering to continue unchecked. CDD should be considered as a specific feature of financial intermediaries’ risk management. Therefore, failure to adequately identify an applicant early in the application process merely magnifies the problem later in the business relationship if the agent must correct the omissions. Why would an agent not properly identify a new applicant? The Financial Action Task Force stated in their 2004-2005 report that the most likely reasons include lack of expertise, time pressures, and lack of appropriate insurer requirements. Intermediaries are not directly accountable for customer due diligence but they are accountable for following insurer requirements.
Insurance companies should be concerned because in addition to having to comply with new federal regulations, insurance providers face potential damage to reputation and heavy financial penalties should they be found to have ineffective AML policies and procedures in place. In many of such cases, the negative impact can be difficult to recover from.

Reputation and integrity are the cornerstones of any financial institution’s long-term viability. If American consumers even suspect that an insurer (whether rightfully or wrongfully concluded) is aiding terrorist activity or even criminal activity, it would mean severe financial problems for the insurer and their intermediaries.

Today’s insurance agents and other intermediaries offer more products than ever before. Some agents have multiple license types enabling them to sell many types of financial and insurance products, including investments and mortgages. With their face-to-face contacts they are the individuals most likely to recognize suspicious behavior from new or even existing clients.

However, agents’ and brokers’ focus is not on terrorist activities or money laundering. Their primary focus is on earning a living through the commissions they earn. Like other professionals, agents have no expectation of ever personally being involved with terrorists who have money laundering as their goal. Because of this, their vigilance may be poor.

Some insurance companies have been reluctant to push agents for more compliance because of their dependency on them for new business in a competitive marketplace. They also had a perception that the risk of money laundering through insurance products was low. Those who need to launder their money recognized this lack of awareness and oversight by both intermediaries and insurers.

Agents and brokers are those most likely to initially notice suspicious activity. During face-to-face encounters, the agent should be able to recognize strange client behavior or an economic profile that may justify filing of a Suspicious Transaction Report (STR). Agents and brokers must comply with anti-money laundering procedures that enable their insurers to prevent the activity.

One of the concerns regarding placing too much responsibility on the field staff that meet face-to-face with their clients is the intermediary’s possible reluctance to ask the necessary questions of new applicants. Agents have an incentive to make the sale, not discourage it. That is why education is necessary. Agents should not refuse to write the policy; instead they should complete the application, attach notes regarding the facts, and forward it to the insurer with the application.

Some intermediaries may suspect illegal activity but say nothing since they are receiving commissions on the applications they accept. A number of case studies have found instances of collusion between criminals and intermediaries. In some instances, businesses placing insurance products were reportedly set up for the primary purpose of money laundering. This activity can be curtailed where there by an effective system of licensing checks at the point of establishment of new companies.

It is not always easy to uncover suspicious activity. Agents who are not trained in money laundering activity may not recognize the signs. Surveys have revealed that agents typically believe the insurance business is not at risk for money laundering activities. This false sense of security that agents and brokers have originates from their lack of recognition of the potential...
use of cash value products and generally poor understanding of the money laundering business.

Seldom would an honest client be reluctant to state where premium dollars or a deposit originates. In fact, most clients are proud of their ability to earn and save money. A new applicant that is reluctant to disclose the origins of premium dollars would be suspicious.

It is generally felt that insurers have not done an adequate job of monitoring and training their intermediaries. It is very difficult to monitor a group of mostly self-employed independent contractors. It is also very difficult for regulating agencies to monitor an international industry, especially one that is growing as fast as the insurance industry is.

The characteristics of certain insurance products make them potentially vulnerable to those seeking to launder money. This regulation is a key step in ensuring that the Bank Secrecy Act is applied appropriately to insurers. An insurance company is defined as a “financial institution” under the Bank Secrecy Act. The USA PATRIOT Act further directs the Secretary of the Treasury to prescribe through regulation minimum standards for such programs.

Money Laundering Indicators - Policyholder Characteristics and Behavior

Most insurance applicants are not terrorists and are not attempting to launder money, but how can an agent or broker tell the difference?

A customer’s profile is the most likely way to differentiate between the typical client and one who has a different agenda. The profile should include both the individual’s financial and personal data as it relates to the products they are interested in purchasing. The agent must remember that these policyholder characteristics do not necessarily signify illegal behavior. When a policyholder raises suspicions it is necessary for either the insurer or the agent/broker to verify the reasons for the activity or characteristics.

Some clients would automatically be considered high risk, including citizens of uncooperative jurisdictions that have been identified by FATF as money laundering havens. While coming from such a jurisdiction does not automatically make the individual or company a criminal it should alert the agent to the possibility.

Companies or clients whose funds come from offshore banks or uncooperative jurisdictions must also be considered questionable. Senior foreign officials and their family members or political figures whose transactions of funds could be the result from embezzlement or misuse of public funds must be considered as potentially suspicious. Even when these individuals are not on OFAC or SEC lists, they have a higher potential risk so agents must use caution when doing business with them.

Money laundering through insurers is most evident in international transactions, where risk of money laundering appears very high. It is likely that more stringent controls will be placed on transactions between companies in different countries.

Generally, the types of “red flags” warranting concern are transactions that are outside the norm of a customer’s behavior or actions where the economic benefit is not immediately clear. For
example, the purchase of an insurance product inconsistent with the customer’s needs or unusual payment methods, such as cash, cash equivalents (when usage of cash or cash equivalents is, in fact, unusual). Early termination of a product (especially during the “free look” period), especially at a cost to the customer, or where payment is made by, or the refund check is sent to, an apparently unrelated third party.

Indicators of suspicious customer behavior include:

- Any lack of information or delay in providing information
- Unusual concern for secrecy
- Documents that appear to be false or altered
- Paying in cash, money orders or travelers’ checks
- Any transaction involving an undisclosed party.

**Cash Premium Payments**

Most people pay major bills by check or some other method that can be proven if necessary. Cash is not the normal method used to purchase a life or annuity product, especially if the premium was a large amount.

In the past when policyholders paid with cash, their agent merely deposited it into their own account and wrote a check to be submitted to the insurer. This method works quite well for money laundering. It is also illegal in most states and should be avoided even when the amount of the premium is small.

**Single Premium Life Insurance Contracts**

Single premium products of all kinds enable the money launderer to purchase a policy with a lump sum payment. This product is ideal because the purchaser can deposit a significant amount of money at one time.

**Early Policy Redemption**

A policyholder who surrendered his or her policy early despite penalties should be considered a potential money launderer, including clients who opted for early redemption even when it seemed very financially disadvantageous to do so. Some of these policies experienced unusually high penalties (as much as 40 percent in some cases). An agent must be suspicious when the policyowner shows little regard for the loss he or she will experience.

**“Free Look” Periods for Newly Issued Policies**

Insurance policies allow a specific period of time (usually 10-30 days) following issuance for the new policyholder to review the policy and decide if he or she is satisfied with the contract terms. A few clients will choose not to keep their policy after delivery.

When money laundering is the objective, individuals purchase policies with illicit cash that they never intend to keep. The individual may buy one very large policy or a number of smaller policies through various agents. When the policy or policies arrive the buyer cancels them and
receives a refund in the form of a check from the insurer. This has allowed the money launderer to exchange his or her illicit funds for legitimate insurer funds.

The policy selected will be one that produces a significant premium amount. The individual may buy the same type of policy from several different insurers, canceling all of them upon issuance and delivery. The most likely type of policy would be an annuity or cash value life policy.

**Collusion of Customer Intermediary and/or Insurer Employee**

Most agents and employees of insurance companies are honest people, but people who launder illicit funds are keen observers who often recognize individuals who are unknowledgeable or can be manipulated. There are also dishonest agents who need no manipulation at all – just the promise of wealth.

**High Commissions**

Studies have shown that policies paying unusually high commissions are often selected by money laundering groups or individuals. In some cases, the intermediary (agent or broker) was directly or indirectly involved in a money laundering operation. In other cases, the intermediary sensed the transactions were shady and therefore selected a higher commission for him or herself.

**Third Party Premium Payments**

This involves paying the premiums on policies through third parties. A third party is a person who is not the policyholder and who has not been subject to identification by the writing agent or issuing company. Therefore, neither the agent nor the insurer can verify the person or the relationship to the policyholder.

**Risks Involved in International Transactions**

International transactions exist in a variety of ways. When money laundering is the goal, it may involve foreign customers and customers domiciled abroad who seek insurance policies through domestic or foreign intermediaries. The policy payout is usually to a foreign jurisdiction.

**Fraudulent Customers, Insurers, or Reinsurance Companies**

FATF noticed that criminals established or took over complex corporate structures and then entered into business relationships with insurers to get coverage. The purpose of the various commercial insurance contracts was to invest illicit funds. In some cases this was facilitated by the fraudulent setting-up of insurance or reinsurance companies for the purpose of laundering money. The criminals were able to invest proceeds of crimes into legal business entities and initiate transfers of money behind the veil of an insurance company or reinsurance company.
**A Known Criminal or Criminal Associate or Relative**

Having relatives or past associates that are involved in illicit activities does not automatically make someone a terrorist or criminal. However, suspicious activity combined with criminal association should raise suspicions that must be either confirmed or denied.

Usually suspicion is raised because of the way they purchase or use policies. That suspicion would then be cause for effective customer due diligence procedures and other procedures to prevent money-laundering activity.

**Erratic or Abnormal Use of Policies**

Most policyholders purchase a policy for a specific reason. A person who buys a policy for money laundering purposes generally does not use them in a typical manner. Those who are using insurance contracts to launder money may deposit funds that do not seem consistent with their income or lifestyle, make abrupt withdrawals, or have unjustified intervention of third parties who make deposits or withdrawals on the policyholder’s behalf. There may be an unacceptable refusal to provide information about him or herself or pertaining to intervening third parties. The agent should know their customers well enough to recognize abnormal behavior and report such incidents when prudent.

**High Premiums Compared to Verifiable Income**

Agents are now required to obtain reasonable information regarding their client’s incomes and finances. When there is inconsistency between a customer’s verifiable economic profile and the scale of investment in insurance products, it is a significant indicator of possible money laundering, which requires further investigation.

**Lack of Concern over Charges or Costs**

The typical policyholder is concerned about surrender penalties or other costs that might erode part of their policy values. If the policyholder shows little or no concern about terminating a contract prior to maturity and triggering a significant penalty it is a sign of money laundering risk. Money launderers consider policy costs and penalties a valid cost of doing business.

**Undue Interest in Payout Options**

When a new policyholder is less concerned with policy benefits and more concerned with potential payout options, agents must recognize that this may signify money laundering.

**Change of Beneficiary**

While it is not unusual for a legitimate client to change their beneficiary, a widely observed and effective indicator of risk relates to repeated changes in the beneficiary designation of a policy. Such events are more significant in cases when the relationship between policyholder and beneficiary is not clearly established.
High Profile Money-Laundering Cases

Experts have long viewed the insurance industry as vulnerable due to the size of the industry, the easy availability and diversity of products and the structure of the business. This is particularly important since much of the distribution of insurance products are handled by brokers and intermediaries who are often outside of the control of the company that issues such products.

Criminals have considered insurance products a good avenue for laundering illicit funds for some time. A 2002 federal grand jury indictment against five Colombian nationals laundering cocaine money using life insurance policies demonstrated how easily it could be accomplished. Called Operation Capstone, the investigation revealed approximately $80 million had been laundered through insurance products. Although there had already been concern regarding the use of insurance products for money laundering, Operation Capstone illustrated the ease with which it could be accomplished.

U.S. Customs Case: “Operation Capstone”

One of the most high-profile cases in recent years developed when U.S. Customs agents in Miami uncovered a sophisticated scheme by which Colombian drug trafficking organizations exploited investment-grade life insurance companies in the United States, the Isle of Man, and other locations to launder roughly $80 million worth of drug proceeds over several years.

Called “Operation Capstone,” the multi-national investigation marked the first time that massive drug money laundering through the international life insurance industry had been exposed and prosecuted. The two-year probe was spearheaded by U.S. Customs, the Isle of Man Customs & Excise Service, and Colombia’s Departamento Administrativo de Seguridad (DAS). Authorities in the United Kingdom, Panama, and South Florida also assisted in the investigation.

The investigation revealed that Colombian cartels, through a small number of insurance brokers, were purchasing life insurance policies in the U.S., the Isle of Man, and other locations, with cartel associates as the beneficiaries. These policies were funded with millions in drug proceeds sent via wire transfers and checks from third parties.

The probe disclosed that cartels were routinely liquidating their drug-financed life insurance policies early, despite the stiff financial penalties for early liquidation. Despite the early withdrawal fees, the cartel beneficiaries would then receive funds from the insurance company that appeared to be legitimate insurance/investment proceeds. The cartels could then use these “clean” funds unquestioned.


The Colombian drug cartel did not purchase only US insurance policies. Policies were bought in continental Europe, the United Kingdom and in smaller jurisdictions, such as the Isle of Man. Using narcotics proceeds from the United States and Mexico, the traffickers bought approximately 250 life insurance policies in the Isle of Man alone. The insurance policies had values ranging up to $1.9 million each. They were taken out in the names of cartel associates and members of their families. Usually they would cash out part or all of the policies prematurely, even though there were penalties of as much as 25 percent or more. While a
legitimate policyholder would try to avoid such penalties, these individuals considered them a business expense in the process of laundering the illicit narcotics proceeds.

Inconsistent regulation and supervision across the industry also provides unique opportunities that were likely to be recognized by money launderers. If insurers and their agents had been properly trained in anti-money laundering techniques it is likely that the cartels would not have found it so easy to cleanse their money in this way.

Worldwide the insurance industry generates premiums of some USD 2.941 trillion per annum so the potential for abuse is obvious. In some product areas, premium dollars have doubled in the last ten years. The insurance industry gathers most of their premium through agents and independent brokers so that the insurer itself has limited control. An increasing share of the market is being sold by financial service industries, such as banks. While the individuals selling these products must still hold an insurance license in most cases, the fact that they work within another industry may affect how they understand insurance money-laundering schemes.
Anti-Money Laundering Program and Suspicious Activity Reporting Requirements for Insurance Companies

Each insurance company, like other financial institutions subject to anti-money laundering program requirements, must develop a risk-based anti-money laundering program that identifies, assesses, and mitigates any risks of money laundering, terrorist financing, and other financial crime associated with their particular business. Not all insurance companies will have the same risk profile or resources; companies will differ in the number of associated agents and brokers and in the complexity of distribution structures; and some companies may be in a better position than others to provide anti-money laundering program training for their agents and brokers by the rule’s applicability date of May 2, 2006.

The Financial Crimes Enforcement Network intends to administer and interpret the insurance anti-money laundering program regulations in a manner that takes into account these differences in risk profiles and resources. Some insurance companies may require additional time to provide anti-money laundering program training to all of their agents and brokers. Nonetheless, it is expected that by May 2, 2006, all insurance companies that are subject to the anti-money laundering regulations will have formally adopted written anti-money laundering policies and procedures that include reasonable plans for training of all appropriate agents and brokers.

Resources Available to help an Insurance Company to establish an Adequate Program

FinCEN has issued a series of Frequently Asked Questions that are designed to assist insurance companies in establishing their anti-money laundering and suspicious activity reporting programs. FinCEN will continue to issue additional guidance for this industry and will provide outreach and training about these and related issues. Financial institutions may also call the FinCEN Regulatory Helpline at 800-949-2732 for assistance. Their website is located at www.fincen.gov.

FinCEN Final Rules

On Monday, October 31, 2005, the Director of the Financial Crimes Enforcement Network (FinCEN), an agency of the U.S. Treasury Department, published two long-awaited final rules. These two new regulations require collaboration between insurance companies and their agents or brokers to be certain that insurance companies:

- Establish an Anti-Money Laundering (AML) Program, and
- Report Suspicious Activity Through the Filing of a Suspicious Activity Report (SAR)

Anti-Money Laundering Program Requirement for Certain U.S. Insurance Companies

This is the application of Section 352 of the USA PATRIOT Act (the Act), amending Section 31 U.S.C. 5318(h) of the Bank Secrecy Act (BSA), referred to as the AML final rule.
Under the USA PATRIOT Act, financial institutions that have an obligation to establish anti-money laundering programs are able to participate in the sharing of information between financial institutions concerning terrorist financing and/or money laundering. Once an insurance company subject to the final insurance company anti-money laundering program rule has established its anti-money laundering program, it may file a certification for purposes of Section 314(b) of the USA PATRIOT Act.

**AML Program Requirements**

Insurers who are required to meet the new regulations must have an AML program that meets the following criteria:

- The program must be in writing.
- The program must be approved by senior management.
- The program must be made available to FinCEN upon request.

In addition, the AML program must:

- Include risk-based policies, procedures and controls that, among other things, “integrate[e]” the company’s insurance agents and insurance brokers into its anti-money laundering program,
- Be tailored to meet each company’s assessment of the money laundering and terrorist financing risks of its products.
- Designate a compliance officer responsible for ensuring that the program is implemented effectively and is updated as necessary.
- Provide for ongoing training of individuals, including agents and brokers, with responsibilities under the program, and
- Provide for independent testing of the program, including testing with respect to compliance of agents and brokers.

The new rules cover insurance companies that issue or underwrite permanent life, annuities or any other product with a cash value or an investment feature. Excluded are term life, group, property and casualty, reinsurance and health insurance products.

**Responsibilities of Agents and Brokers under the New Rules**

The new insurance regulations do not require insurance agents and brokers to establish anti-money laundering programs or to report suspicious transactions themselves. To assure that insurance companies and their distribution partners collaborate in preventing money laundering, the new rules require life insurance companies to integrate agents and brokers into their anti-money laundering programs and to monitor the agents’ compliance with the programs. The preamble to the rules states that if efforts to integrate agents into insurance company programs are ineffective, FinCEN may reconsider its decision not to require agents and brokers to establish their own programs.

Minimum requirements that must be followed by agents and their insurers, pursuant to provisions in the Bank Secrecy Act (BSA), require financial institutions to establish anti-money laundering programs and to define the companies and insurance products that are subject to
this requirement. The Bank Secrecy Act (Public Law 91-508) authorizes the Secretary of the Treasury to issue regulations requiring financial institutions to keep records and file reports that are determined to have a high degree of usefulness in criminal, tax, and regulatory matters, including the conduct of intelligence or counter-intelligence such as analysis of terrorism activity.

- It is the insurance company’s obligation to report suspicious activity that may have been transacted through the agent or broker.
- Policies and procedures must include a means for obtaining customer-related information from the agent or broker to detect suspicious activity.

**Customer Information**

The new rules require insurance companies to collect customer information from agents and brokers, among other sources, to support their anti-money laundering programs and to detect and report suspicious transactions. FinCEN has made clear that insurance agents and brokers have a crucial role to play in this area:

Insurance agents and brokers are an integral part of the insurance industry due to their contact with customers. Insurance agents and brokers typically are involved in sales operations and are therefore in direct contact with customers. As a result, the agent or broker will often be in a critical position of knowledge as to the source of investment assets, the nature of the client, and the objectives for which the insurance products are being purchased.

Because each company’s program must be risk-based, agents and brokers should expect to collect and retain information needed to assess the risk associated with particular business – in particular, to identify customers in high-risk businesses or high-risk geographic locations, or those using products or services that may be more susceptible to abuse in money laundering activity.

In addition to the above, insurance companies must develop procedures for ensuring that appropriate customer information is obtained by agents and brokers and communicated to the insurance company for purposes of detecting and reporting suspicious activity (Section 103.16(b)(3)(i)). It is not inconceivable that new account opening forms such as applications, customer profiles, fact finders and suitability assessment tools will need to be developed so that necessary customer information is captured and provided to the insurance company.

**Customer Identification Program**

Currently insurance companies are not required to implement a Customer Identification Program (CIP) and obtain minimum mandatory information verifying the identity of a customer. Even so, other applicable Bank Secrecy Act regulations require insurance companies to obtain and retain identifying information from customers in specific circumstances. Insurance companies must obtain all relevant and appropriate customer-related information necessary to administer an effective anti-money laundering program.

Insurance companies that are subsidiaries of banking organizations should consult with their parent bank’s primary Federal regulator.
Anti-Money Laundering General Requirements

Language of AML final rule:

Section 103.137(b): AML Program – General Requirements

(b) Anti-money laundering program requirements for insurance companies.

Not later than May 6, 2006, each insurance company shall develop and implement a written anti-money laundering program applicable to its covered products that is reasonably designed to prevent the insurance company from being used to facilitate money laundering or the financing of terrorist activities.

The program must be approved by senior management.

An insurance company shall make a copy of its anti-money laundering program available to the Department of the Treasury, the Financial Crimes Enforcement Network, or their designee upon request.

FinCEN comments:

- Both the regulatory text and the comments clarify that a company’s AML program is only required with respect to covered products.
- “Beyond these minimum requirements, the final rule is intended to give insurance companies the flexibility to design their programs to meet the specific risks associate with their particular business.”

Insurance companies required to perform a risk assessment

Similar to the banking and securities industry insurance providers must adopt a risk-based approach to meet the new AML requirements.

The AML final rule specifies that an insurance company shall “incorporate policies, procedures, and internal controls based upon the insurance company’s assessment of the money laundering and terrorist financing risks associate with its covered products.” (Section 103.137(b)(1))

Based on FinCEN comments and regulations, as well as industry activity, it is clear that regulators expect insurance companies to perform a comprehensive risk assessment as the basis for the design of AML compliance controls.

As with all anti-money laundering program rules; insurance companies must develop a risk-based program. Under the Bank Secrecy Act, financial institutions are required to identify, assess, and mitigate the risk that their business will be abused by criminals. Risks can be jurisdictional, product-related, service-related, or client-related. Regardless of where those risks arise, financial institutions covered by the regulations must take reasonable steps to mitigate them. Compliance is risk-based, meaning that a financial institution must devote more compliance resources to the areas of its business that pose the greatest risk. Businesses of
different sizes and circumstances will not necessarily have the same types of anti-money laundering programs.

Effective implementation must be predicated upon the insurer’s knowledge of their business, a careful assessment of the vulnerabilities of their business to money laundering, and adoption of controls appropriate to that risk.

**Risk-based compliance: Each institution is different**

No two institutions are identical in terms of the way they conduct business, whether in terms of their client base, geographical reach, sales and distribution channels or products offered. Therefore, each company will have its own unique profile which should allow for a determination of which parts of the business are more at risk than others.

The development of risk-based controls requires that each company assess the risk factors evident in the manufacture and sale of its products, and design and implement tailored controls commensurate with these risks. Risk factors must include an assessment of the company’s products, customers, distribution methods, geographies being served, payment options and administrative operations.

**Methods of Payment**

Certain forms of payment – including cash, money orders, traveler’s checks, and bank checks – can be used in the placement phase of a money laundering scheme. To manage this risk, companies may set limits on the forms of payments that will be accepted and the amounts acceptable for some of them. The goal is to reduce the chances that the insurance business will be involved in money laundering, without excluding forms of payment with a legitimate business purpose.

The Department of the Treasury has instituted procedures that must be followed when an agent, broker, or insurer suspects money laundering is taking place or could take place using insurance products.

The AML program must include policies, procedures and internal controls that detect suspicious activity and provide for reporting of this detected activity to FinCEN in accordance with regulatory requirements.

At a minimum, insurance companies must establish an anti-money laundering program that comprises the four elements set forth below. This program is not expected to prevent all potential money laundering. The insurer is expected to take prudent steps, with the same kind of thought and care taken to guard against other crimes, such as theft or fraud.

The required components are minimum requirements. Insurance companies that offer a diversity of insurance products may decide to adopt institution-wide anti-money laundering programs regardless of the types of products offered. However, the final rule requirement applies only to covered products offered by the company.
(1) A compliance officer who is responsible for ensuring that the program is implemented effectively.

Language of AML final rule:

Sec. 103.137(c)(2)AML Program – Minimal Requirement: Designation of a Compliance Officer

(2) Designate a compliance officer who will be responsible for ensuring that:

(i) The anti-money laundering program is implemented effectively, including monitoring compliance by the company’s insurance agents and insurance brokers with their obligations under the program;

(ii) The anti-money laundering program is updated as necessary; and

(iii) Appropriate persons are educated and trained in accordance with paragraph (c)(3) of this section.

FinCEN comments:

- An insurance company “may designate an individual person or a committee to be responsible for administering the anti-money laundering program.”
- Responsible person(s) must be “competent and knowledgeable” regarding all requirements, issues and risks.
- These individuals should be “empowered with full responsibility and authority to develop and enforce appropriate policies and procedures.”
- Of note, it is the express role of the compliance officer to ensure that the AML program is being implemented effectively by the company’s agents and brokers.

Insight and recommendations

- A company should clearly define the reporting structure for individuals with compliance responsibilities. This is particularly important for the designated AML compliance officer. This individual, or committee, should be reporting to the highest levels of senior management to help set the appropriate tone for compliance and to help ensure that recommendations are appropriately considered.
- It is very important that companies establish and define the appropriate roles and responsibilities for all individuals who will have a significant role in implementing the AML program and include these roles and responsibilities into the performance evaluation along with an appropriate incentive structure to help alleviate concerns over the added responsibilities that individuals may incur as a part of the AML program’s implementation.

Each insurer will designate a compliance officer who will be responsible for ensuring that the anti-money laundering program is implemented effectively. This includes monitoring the agents and brokers to be sure they have complied with all requirements. It will be necessary to update the program as changes or additional knowledge requires it. Appropriate persons must be educated and trained so that they can adequately meet the requirements mandated.
The compliance officer is an employee or group of employees who will be responsible for the day-to-day operation of an anti-money laundering program. In particular, this person (or persons) will be responsible for ensuring that the steps within the program are fully implemented. As such, this person should be someone with enough authority to achieve this important task. The amount of time devoted to these duties will depend on the level of risk. An insurance company is not required to designate a person to serve on a full-time basis as a compliance officer for purposes of the final rule unless the level of risk or volume of transactions warrants. If the business faces a very high level of risk for money laundering, then a great deal will be required of this person. If the exposure to these risks is more moderate, then the level of effort will be commensurate with that risk.

In all cases, however, the compliance officer should be thoroughly familiar with the operations of the business itself and with all aspects of the anti-money laundering program, as well as with the requirements of the Bank Secrecy Act and applicable Financial Crimes Enforcement Network forms, and should have read carefully all applicable documents issued or posted on the web page (www.fincen.gov).

(2) Policies, procedures, and internal controls.

Language of AML final rule:

Sec. 103.137(c)(1) AML Program – Minimal Requirement: Performing a Risk Assessment and Integrating Agents and Brokers

At a minimum, the program required by paragraph (b) of this section shall:

(1) Incorporate policies, procedures, and internal controls based upon the insurance company's assessment of the money laundering and terrorist financing risks associated with its covered products. Policies, procedures, and internal controls developed and implemented by an insurance company under this section shall include provisions . . . integrating the company’s insurance agents and insurance brokers into its anti-money laundering program, obtaining all relevant customer-related information necessary for an effective anti-money laundering program.

FinCEN comments:

- According to FinCEN, risk-based AML programs must consider all relevant factors affecting the risks inherent in its covered products, including, but not limited to:
  - Whether the customer uses cash or cash equivalents;
  - Whether the product is issued to an individual in a non-cooperative jurisdiction;
  - Whether the agent or broker is required to establish an AML program pursuant to another requirement.

- As agents often obtain client information for the insurance company, FinCEN expects that the insurance company will arrange to have the agent perform certain aspects of the AML program.
- It is important to note that FinCEN also states, “Any insurance company that arranges for its agent to perform aspects of its anti-money laundering program, however, remains
responsible for the effectiveness of the program as well as for ensuring that the appropriate examiners have access to information and records relating to the anti-money laundering program and are able to inspect the agent or the third party for purposes of the program.”

**insight and recommendations:**

- A company should consider performing a formal risk assessment as an initial step in the design and development of its policies, procedures and internal controls. While not expressly required, it is clearly implied in numerous provisions and in the comments to the new rules.
- The risk assessment process should be documented and made available to examiners as support for the reasonableness of the implemented controls.
- A good source of cross-industry guidance from the banking industry on AML risk assessment is the Federal Financial Institutions Examination Council’s (FFIEC) Bank Secrecy Act/Anti-Money Laundering Examination Manual (June 2005).
- Where a company delegates information gathering and analysis functions to an independent agent or broker, the company will need to implement certain controls to help ensure that these agents and brokers are performing these functions in accordance with the program. Specifically, a company may want to consider the following:

  - Modify selling agreements and contractual arrangements to include provisions that specifically address the AML compliance responsibilities of the agent or broker;
  - Include provisions that permit appropriate inquiry, oversight and analysis of the agent’s performance as it relates to AML compliance;
  - Modify applications to include the documentation of appropriate client information that will permit the company to perform additional analysis of the individual;
  - Collect fact finding and suitability information to supplement the information provided in the application;
  - Require certain certifications from the agent or broker as part of the application process.

Policies, procedures, and internal controls must be designed to enable the insurance company to comply with the applicable requirements of the Bank Secrecy Act and to prevent the insurance company from being used by money launderers.

At minimum, the program is required to incorporate policies, procedures, and internal controls based upon the insurance company’s assessment of the money laundering and terrorist financing risks associated with its covered products. Policies, procedures, and internal controls developed and implemented by an insurer must include provisions for integrating the company’s insurance agents and brokers into its anti-money laundering program, and obtaining all relevant customer-related information necessary to ensure an effective program.

Insurers should assess the extent to which their particular business is susceptible to money laundering. Those companies dealing with covered products that pose a significantly higher risk require greater diligence for detecting transactions that may involve money laundering. Using customer and other information obtained through agents, brokers or otherwise, an insurance company can assess the money laundering risks presented by its business based on such
factors as the particular types and locations of customers served, distribution channels, and products offered.

(3) **Ongoing training of appropriate persons concerning their responsibilities under the program.**

Training for Agents and Brokers

Language of AML final rule:

Sec. 103.137(c)(3): AML Program – Minimal Requirement: Training

(3) Provide for on-going training of appropriate persons concerning their responsibilities under the program. An insurance company may satisfy this requirement with respect to its employees, insurance agents, and insurance brokers by directly training such persons or verifying that persons have received training by another insurance company or by a competent third party with respect to the covered products offered by the insurance company.

FinCEN comments:

- An insurance company can satisfy its training obligation regarding agents and brokers by “verifying that its agents and brokers have received the training required by the rule from another insurance company or a competent third party with respect to the covered products being offered.”
- For purposes of the rule, a “competent third party” can include:
  - A third-party vendor; or
  - Another financial institution that is subject to AML program requirements.
- While FinCEN will not establish a registry for purposes of tracking the training of agents and brokers, it would not object to the establishment of a privately maintained registry.
- Training must include the “requirements of the program and money laundering risks generally so that ‘red flags’ associated with covered products can be identified.”
- Training can be conducted by “outside or in-house seminars, and could include computer-based training.”
- Individuals with specific responsibilities should receive sufficient training to carry out these responsibilities.
- Individuals being trained “should receive periodic updates and refreshers regarding the anti-money laundering program.”

Insight and recommendations:

- Training should be tailored to the AML program responsibilities of the individual or group being trained. Also, given the responsibility of senior management and possibly the board of directors in reviewing and approving the AML program, it is important that meaningful training be provided to appropriate individuals at this level.
- The industry will need to determine the most effective way to provide AML training to independent agents and brokers in a manner that does not jeopardize the business relationship with these individuals.
The new regulations require companies to train their agents and brokers regarding their responsibilities under the company’s anti-money laundering program. These programs must be tailored to the needs of agents and brokers and to include training on identifying suspicious customer behavior and transactions as well as on procedures to report suspicious activities to the company.

Employees must receive appropriate education in order to understand and prevent money-laundering tactics using insurance companies and their products. This includes the company’s agents and brokers as well as other in-house employees.

An insurance company may satisfy the training requirement under its anti-money laundering program with respect to its employees, agents and brokers by directly training such persons or by verifying that those employees, agents and brokers have received adequate training by another insurance company or by a competent third party with respect to the covered products offered by the insurance company. For purposes of the rule, a competent third party can include, among others, another financial institution that is subject to an anti-money laundering program, such as a broker-dealer in securities or a bank.

An insurance company remains responsible for assuring compliance with the final rule and monitoring the effectiveness of its training program. The nature of the insurance company’s review of a training program performed by another entity depends upon the facts and circumstances of the particular situation. Mere certification of attendance at a program is insufficient; rather, evaluation of the substance of the training is essential.

Regardless of where the education is acquired, companies must develop an independent audit program to test whether it has been effective. Insurers must stress the requirements with their intermediaries and urge compliance with all aspects of AML procedures. Every employee should receive written copies of consequences of non-compliance including civil, criminal, and disciplinary penalties for money laundering activities.

Companies should first consider what training is appropriate for each individual employee. Some employees may require no training on the program, given their particular duties. Others may require a great deal of training. The training should be clearly understood by employees, agents, brokers, and others doing business with covered products. The compliance officer should be available to answer questions posed by employees which means that they should periodically retrain employees on the program to ensure that they understand and can fully implement the program.

Ongoing training is required under the USA PATRIOT Act. Insurers must inform their employees and intermediaries (agents and brokers) of where training can be obtained or provide training so that they may learn to detect unusual or suspicious transactions. Employees must also know how to comply with the federal rules, regulations, and reporting requirements. Relevant manuals should be available to new employees who may not have yet had such training.
(4) Independent testing to monitor and maintain an adequate program.

Testing the Effectiveness of the Anti-Money Laundering Program

Language of AML final rule:

Sec. 103.137(c)(4) AML Program – Minimal Requirement: Independent Testing

(4) Provide for independent testing to monitor and maintain an adequate program, including testing to determine compliance of the company's insurance agents and insurance brokers with their obligations under the program. The scope and frequency of the testing shall be commensurate with the risks posed by insurance company's covered products. Such testing may be conducted by a third party or by any officer or employee of the insurance company, other than the person designated in paragraph (c)(2) of this section.

FinCEN comments:

- Independent testing does not require the use of an outside consultant or accountant.
- Independent testing can be completed by an employee of the company “so long as the tester is not the compliance officer or otherwise involved in administering the program.”
- Where an insurance company relies on a third party to administer elements of the company’s AML program, independent testing must include more than the procurement of a simple certification.
- In a footnote, FinCEN provides the example of an agent or broker who is a registered representative of a broker-dealer. In this situation, the insurance company would not need to independently test the broker-dealer’s AML program but would need to confirm that such testing has been completed. The footnote further explains that the insurance company should review relevant portions of any independent testing report that is produced.
- There is no frequency requirement to the monitoring program. The frequency of the testing will “depend upon the insurance company’s assessment of the risks associated with its covered products.”
- “Recommendations that result from the testing should be implemented promptly or submitted to senior management for consideration.”

Insight and recommendations:

- Effective testing will require the development of an audit program that is comprehensive and addresses the unique aspects of the company’s AML program.
- The audit program should be based on clear control objectives that have been drawn from the regulations and the company’s policies and specific test steps that objectively measure the effectiveness of the company’s implementing procedures.
- All testing should be documented for purposes of any regulatory review.

An insurance company is required to conduct independent testing as to the effectiveness of its anti-money laundering program, including the compliance of its agents and brokers. The scope and frequency of the potential testing would be commensurate with the risks posed by the insurer’s products. The testing might be done in-house or by a third party. If performed in-house, the compliance officer may NOT be the person doing the testing.
Regarding independent agents and brokers, insurance companies will need significant guidance on how to implement effective monitoring without jeopardizing the independent contractor relationship.

Independent testers should carefully consider all of the decisions made by the compliance officer, such as the determination of the level of risk faced by the insurance company for money laundering, the frequency of training, etc. The independent testing is intended to confirm that the program complies with the requirements of the rule and that the program functions as designed.

For example, if the program requires that a particular employee be trained once every six months, then the independent testing should determine whether the training occurred and whether the training was adequate. Independent testing does not mean that an outside party must be hired, although outside parties may be utilized to conduct the independent review.

**Covered products**

**Language of AML final rule:**

Section 103.137(a) (4): Definition of a “Covered Product”

(4) **Covered product** means:

(i) A permanent life insurance policy, other than a group life insurance policy;

(ii) An annuity contract, other than a group annuity contract; and

(iii) Any other insurance product with features of cash value or investment.

**Language of SAR final rule:**

Sec. 103.16 (a) (4:) Definition of a “Covered Product”

(4) **Covered product** means:

(i) A permanent life insurance policy, other than a group life insurance policy;

(ii) An annuity contract, other than a group annuity contract; and

(iii) Any other insurance product with features of cash value or investment.

**FinCEN comments:**

- Permanent life insurance policies and annuity contracts possess feature “that make them susceptible to being used for money laundering or the financing of terrorism.” Specifically, this refers to products with cash value that can be redeemed at a future date.
- Notably, term life insurance is not a covered product as the above “risks do not exist to the same degree in term life.”
In addition, the definition does not include property and casualty insurance or health insurance but does include a “catch-all” definition that could encompass these products, in the event a company designs one of these products to include cash value or investment features.

The focus is on “covered products” or those that are perceived to present a high risk for money laundering.

The Department of the Treasury Financial Crimes Enforcement Network (FinCEN) definition of “covered products” includes:

1. A permanent life insurance policy, other than a group life insurance policy;
2. An annuity contract, other than a group annuity contract or charitable gift annuity; and
3. Any other insurance product with features of cash value or investment.

**Any Other Insurance Product with Features of Cash Value or Investment**

The purpose of including the language “any other insurance product with features of cash value or investment,” in the definition of “covered products” is to ensure that any newly developed products in the life insurance and annuity areas having these characteristics, and that are particularly vulnerable to money laundering, would be covered. It is not intended that group life insurance policies or group annuities, with or without these characteristics, would be covered because group policies are administered according to guidelines that make them generally less vulnerable to abuses by participants in the plan.

A request for an administrative ruling interpreting the application of this definition may be submitted in writing to FinCEN pursuant to 31 C.F.R. § 103.81.

**Insurance Products that are not “Covered Products” Pursuant to the Rule**

Because they pose a lower risk for money laundering, the following products are not defined as “covered products” in the final rule:

- Group insurance products
- Products offered by charitable organizations, e.g. charitable annuities
- Term (including credit) life, property, casualty, health, or title insurance
- Reinsurance and retrocession contracts.

Contracts of indemnity and structured settlements (including workers’ compensation payments) are not within the definition of “covered products” for purposes of the final rule.

**Definition of Insurance Company**

Language of AML final rule:

Section 103.137(a) (9): Definition of an “Insurance Company or Insurer”

(9) Insurance company or insurer.
(i) Except as provided in paragraph (a)(9)(ii) of this section, the term “insurance company” or “insurer” means any person engaged within the United States as a business in the issuing or underwriting of any covered product.

(ii) The term “insurance company” or “insurer” does not include an insurance agent or insurance broker.

Language of SAR final rule:

Sec. 103.16 (a) (9): Definition of an “Insurance Company or Insurer”

(9) Insurance company or insurer.

(i) Except as provided in paragraph (a)(9)(ii) of this section, the term “insurance company” or “insurer” means any person engaged within the United States as a business in the issuing or underwriting of any covered product.

(ii) The term “insurance company” or “insurer” does not include an insurance agent or insurance broker.

FinCEN comments:

- While the definition expressly excludes agents and brokers, FinCEN clearly states that agents and brokers will play an important role in the effective operation of an insurance company’s AML program.
- Should FinCEN determine that the effectiveness of the rule is being “undermined by the failure of agents and brokers to cooperate with their insurance company principals, [FinCEN] will consider proposing appropriate amendments to the rule.”
- FinCEN expects that an insurance company “faced with a non-compliance by an agent or broker, will take the necessary action to secure such compliance, including, when appropriate, terminating its business relationship with such agent or broker.”
- Companies can, and should, delegate certain AML functions to an agent or broker, but the company remains fully responsible for the program’s effectiveness.

The Final Rule Does Not Apply to All Insurance Companies

The term “insurance company” or “insurer” is defined in the final rule to describe any person engaged within the United States as a business in the issuing or underwriting of “covered products.” Covered products are those insurance products that have been determined to present a higher degree of risk for money laundering.

The phrase “as a business” in the definition of “insurance company” is intended to exclude those persons that offer annuities or other covered products as an incidental part of their business. For example, a tax-exempt organization that offers charitable gift annuities, as defined in section 501(m)(5) of the Internal Revenue Code, that would not ordinarily fall within the definition of an insurance company, would not be considered an insurance company for purposes of the final rule.
If an insurance company that is not presently issuing or underwriting a covered product should do so in the future, the insurance company would then become subject to the rule (but only to the extent of its business relating to covered products). Conversely, if an insurance company ceases issuing or underwriting covered products, the insurance company would no longer be subject to the rule.

An insurance company that is registered or is required to register with the Securities and Exchange Commission will be deemed to have satisfied the requirements of this rule for those activities regulated by the Securities and Exchange Commission to the extent that the company complies with the anti-money laundering program requirements applicable to such activities that are imposed by the Securities and Exchange Commission or by a self-regulatory organization registered with the Securities and Exchange Commission. However, the company should evaluate the extent (if any) to which its existing anti-money laundering program should be revised to appropriately address the risks of doing business in covered insurance products.

Agents and brokers not covered by final rules

Insurance agents and insurance brokers are specifically exempt from the definition of “insurance company” or “insurer,” which means they are not directly covered by the rules. An “insurance agent” is defined as a “sales and/or service representative of an insurance company.” Consequently, agents and brokers are not required to establish independently an anti-money laundering program or file suspicious activity reports. Agents and brokers are an integral part of the insurance industry; they are the ones most likely to be obtaining applicant information. This places agents in a critical position of knowledge regarding the source of investment assets, the nature of the clients, and the objectives and goals considered when purchasing insurance products.

While agents are exempt from the definition of insurance companies, the Rules require each insurance company to develop and implement policies, procedures, and internal controls that integrate the company’s agents and brokers into its anti-money laundering program. This places significant oversight responsibilities on insurers. It is difficult to oversee people working independently in the field. Education seems the only efficient way to integrate agents and brokers into the prevention of money laundering activities.

According to the Paris-based Financial Action Task Force (FATF), “money launderers have exploited the fact that insurance products are often sold by brokers…Thus, the launderer may seek an insurance broker who is not aware of or does not conform to necessary procedures, or else who simply fails to recognize or report information regarding possible cases of money laundering.”

In a more recent international survey of the industry, FATF concluded that the integral role played by intermediaries in driving new business might be a hindrance to compliance with AML requirements:

“One of the most important findings emerging from jurisdictions’ responses is an insufficient degree of compliance with AML requirements by intermediaries… A possible reason for the low compliance could be that intermediaries – especially if independent from the insurer – perceive the risk of ML (money laundering) as low and are focusing more on sales figures and their commission. Insurers, on the other hand, might be reluctant to push for more compliance by intermediaries because of their dependency on these organizations for new business.”
Observations and cases such as these help explain why FinCEN concluded that brokers and agents should be part of an insurance company’s overall compliance program, even though they are not typically employed by a provider.

**FinCEN’s View on Agents and Brokers**

“The agent or broker will often be in a critical position of knowledge as to the source of investment assets, the nature of the clients, and the objectives for which the insurance products are being purchased. Agents and brokers have an important role to play in assisting the insurance company to prevent money laundering. Therefore, the final rule requires each insurance company to integrate its agents and brokers into its anti-money laundering program and to monitor their compliance with its program. The final rule also requires an insurance company’s anti-money laundering program to include procedures for obtaining relevant customer-related information necessary for an effective program, either from its agents and brokers or otherwise.

The insurance company remains responsible for the conduct and effectiveness of its anti-money laundering program, which includes the activities of the agents and brokers that are involved with covered products. The insurance company must exercise due diligence, not only in the development of its anti-money laundering program and in the collection of appropriate customer and other information but also in monitoring the operations of its program, its employees, and its agents.”

*Source: FinCEN October 2005*

FinCEN offers three reasons for its decision to impose direct obligation only on the insurance company and not on a company’s agents or brokers:

1. As it is the company that bears the risks of its products, it should retain the responsibility of guarding against having those products used in an unlawful manner;
2. The company is in a better financial position to bear the cost of compliance; and
3. Many insurers can integrate the AML compliance requirements into existing fraud detection and other compliance programs.

**Contractual Arrangements with Agents and Brokers**

FinCEN contemplates that companies will be expected to use their contractual relationships to require agents and brokers to provide them with information that may be useful for identifying potential suspicious activity.

The contractual responsibilities of agents and brokers with respect to anti-money laundering programs will likely be similar the current responsibilities agents and brokers undertake in connection with company customer identification and anti-fraud procedures.

Insurers already have numerous compliance and best practices guidelines that both captive and independent agents and brokers follow in order to continue doing business with them. Insurers also require very extensive information-gathering by many of their agents and brokers for underwriting purposes. It is expected that many insurance companies will adopt the same structural model for their anti-money laundering programs.
Suspicious Activity Reports Filing Requirement for Certain U.S. Insurance Companies

This is the application of Section 356 of the Act, amending Section 31 U.S. C. 5318(g) of the BSA, referred to as the SAR final rule.

The requirement to identify and report suspicious transactions applies only to an insurance company, and not its agents or brokers. Insurance companies are required to obtain customer information from all relevant sources, including its agents and brokers, and to report suspicious activity based on such information.

In addition to filing a SAR, the agent would be required to contact the proper authorities immediately. Should an agent decide that suspicious activity is taking place, and especially if the agent is concerned that a terrorist act might occur, he or she must call the Financial Crimes Enforcement Network’s Financial Institution’s hotline: 1-866-556-3974.

All SAR reports are confidential

All SAR reports are confidential and it is not necessary or even advisable that the individual in question be told of the report’s filing. If an agent is subpoenaed in response to the filing of a suspicious activity report, the agent is not required to provide any information. He or she should immediately contact FinCEN. If an insurer receives a subpoena, it should not confirm or deny the report. The insurer should contact the Chief Council at the FinCEN office at 1-703-905-3590.

A new Suspicious Activity Report form for insurance companies (FinCEN Form 108 – Suspicious Activity Report by Insurance Companies) will replace the procedure of checking the suspicious transaction box on Form 8300 (Report of Cash Payments Over $10,000 Received in a Trade or Business). It may, however, be appropriate for an insurance company to file a Form 8300 as well as file FinCEN Form 108 when circumstances surrounding the receipt of cash are suspicious.

The threshold amount obligating an insurance company to report suspicious transactions that are conducted or attempted by, at, or through the institution is at least $5,000 (whether in an individual transaction or in aggregate) in funds or other assets. This threshold amount is not limited to insurance policies whose premiums meet or exceed $5,000; rather, it includes a policy in which the premium or potential payout meets the threshold. However, insurance companies are encouraged to voluntarily file Suspicious Activity Reports, if appropriate. An insurance company that files a Suspicious Activity Report voluntarily is protected from civil liability to the same extent as a company filing a Suspicious Activity Report that is required under this final rule.
Suspicious Activity Reporting (SARs) – General Requirements

Language of SAR final rule:

Sec. 103.16 (b) (1): SAR Filing – General Requirement

(b) General.

(1) Each insurance company shall file with the Financial Crimes Enforcement Network, to the extent and in the manner required by this section, a report of any suspicious transaction involving a covered product that is relevant to a possible violation of law or regulation.

An insurance company may also file with the Financial Crimes Enforcement Network by using the form specified in paragraph (c)(1) of this section or otherwise, a report of any suspicious transaction that it believes is relevant to the possible violation of any law or regulation but the reporting of which is not required by this section.

FinCEN comments:

- The reporting requirement extends only to transactions involving a “covered product” as those are the products that FinCEN believes pose a significant risk of being used to launder money or finance terrorism.
- FinCEN expressly encourages the filing of a SAR even where the transaction involves less than the threshold dollar amount of $5,000.
- The $5,000 threshold is not limited to an analysis of the premium alone but includes any covered policy in which either the premium or the potential payout meets the threshold.

The second rule requires insurance companies to report “suspicious activities” and to establish procedures to obtain information from agents and brokers, among others, necessary to detect and report those transactions.

The rule requiring insurance companies to report suspicious activity was effective date on May 2, 2006, and insurance companies must begin reporting suspicious activity on that date. A new suspicious activity reporting form was developed for insurance companies (FinCEN Form 108, SAR-IC).

Form 8300 – Report of Cash Payments over $10,000 Received in a Trade or Business

Insurance companies should continue to file Form 8300 in appropriate situations to report the receipt of cash over $10,000. There is no requirement at this time for insurance companies to file Currency Transaction Reports.

Form 8300 includes Box 1b for reporting of suspicious transactions. Because covered insurance companies are required to file Suspicious Activity Reports as part of their anti-money laundering program, the Suspicious Activity Report for Insurance Companies form will be the required medium for reporting suspicious activity. An insurance company is not precluded from also checking the “suspicious transaction” box, as appropriate, when filing a Form 8300; however,
checking the box on the Form 8300 is not required, and will not satisfy the insurance company’s obligation to file a Suspicious Activity Report in the appropriate circumstances.

It may be appropriate for an insurance company to file a Form 8300 for receipt of cash and other items over $10,000 as well as to file a Suspicious Activity Report when the circumstances surrounding the receipt of cash and other items are suspicious.

**SAR Filing Thresholds**

**Language of SAR final rule:**

Sec. 103.16 (b) (2): SAR Filing - Filing Thresholds

(2) A transaction requires reporting under this section if it is conducted or attempted by, at, or through an insurance company, and involves or aggregates at least $5,000 in funds or other assets, and the insurance company knows, suspects, or has reason to suspect that the transaction (or pattern of transaction of which the transaction is a part):

(i) Involves funds derived from illegal activity or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity (including without limitation, the ownership, nature, source, location, or control of such funds or assets) as part of a plan to violate or evade any federal law or regulation or to avoid any transaction reporting requirement under federal law or regulation;

(ii) Is designed, whether through structuring or other means, to evade any requirements of this part or any other regulation promulgated under the Bank Secrecy Act . . .;

(iii) Has no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage, and the insurance company knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction; or

(iv) Involves use of the insurance company to facilitate criminal activity.

**FinCEN comments:**

- A “reason to suspect” infers a pattern of transactions that is, or should be, known by the insurance company.
- While the first three categories imply the laundering of money obtained from illegal activities, the fourth category implies the laundering of money to fund terrorist activities.
- FinCEN acknowledges that the identification of a suspicious transaction requires a determination based on all facts and circumstances and that different fact patterns require different judgments.
- FinCEN does provide examples of red flags that may indicate a transaction is suspicious. The provided examples include:
  - A purchase that appears to be inconsistent with a customer’s needs;
  - Any unusual method of payment, particularly by cash or cash equivalents or monetary instruments in structured amounts;
- The early termination of an insurance product, especially at a cost to the customer, or where cash was tendered and/or the refund check is directed to an apparently unrelated third party;
- The transfer of the benefit to an unrelated third party;
- Little or no concern for the investment performance but much concern about early termination features of the product;
- The reluctance to provide identifying information or the provision of minimal or seemingly fictitious information; and
- The borrowing of the maximum amount available soon after purchasing the product.

Under the SAR final rule, insurance companies are required to file a Suspicious Activity Report (SAR) of any suspicious transaction relating to a covered product that involves at least $5,000 in funds or other assets, whether the cash payment is for a single policy application or multiple applications that total that amount or more. Payments made by check would most likely not cause concern. This threshold amount is not limited to insurance policies whose premiums meet or exceed $5,000; it includes a policy in which the premium or potential payout meets the threshold. Insurance companies are encouraged to voluntarily file Suspicious Activity Reports any time they seem appropriate.

In addition to the dollar threshold, there are four categories of transactions that require the filing of a SAR. These are transactions in which the insurance company knows, suspects or has reason to suspect that the transaction:

1. Involves funds derived from illegal activity or is intended to hide the fact that the funds are derived from illegal activity;
2. Is designed to evade the reporting requirements of the Bank Secrecy Act (e.g., the reporting of $10,000 in cash or cash equivalents);
3. Has no legitimate business or lawful purpose and an inquiry does not reveal a reasonable explanation for the transaction;
4. Is intended to use the insurance company to facilitate future criminal activity (e.g., terrorist financing).

Some examples of "red flags" include, but are not limited to, the following: the purchase of an insurance product inconsistent with the customer's needs; unusual payment methods, such as cash, cash equivalents (when such a usage of cash or cash equivalents is, in fact, unusual), or structured monetary instruments; early termination of a product (including during the "free look" period), especially at a cost to the customer, or where payment is made by, or the refund check is directed to, an apparently unrelated third party; the transfer of the benefit of a product to an apparently unrelated third party; a customer who shows little concern for the investment performance of a product, but a great deal of concern about the early termination features of the product; a customer who is reluctant to provide identifying information when purchasing a product, or who provides minimal or seemingly fictitious information; and a customer who borrows the maximum amount available soon after purchasing the product.

Reportable transactions are not limited to a narrow definition of money laundering. They include any effort to involve an insurance company in illegal activity, and may even include lawful transactions that are atypical for the customer involved and for which there is no reasonable explanation.
Suspicious Transactions Conducted Through Agents or Brokers

Language of SAR final rule:

Sec. 103.16 (b) (3): Suspicious Transaction Conducted Through Agents and Brokers

(3) (i) An insurance company is responsible for reporting suspicious transactions conducted through its insurance agents and insurance brokers. Accordingly, an insurance company shall establish and implement policies and procedures reasonably designed to obtain customer-related information necessary to detect suspicious activity from all relevant sources, including from its insurance agents and insurance brokers, and shall report suspicious activity based on such information.

(ii) Certain insurance agents may have a separate obligation to report suspicious activity pursuant to other provisions of this part. In those instances, no more than one report is required to be filed by the financial institutions involved in the transaction, as long the words “joint filing” are in the narrative section, and both institutions maintain a copy of the report filed, along with any supporting documentation.

FinCEN comments:

- FinCEN acknowledges that “suspicious activity that occurs at the time of sale of the covered product is most likely to be observed by the agent or broker.”
- However, agents and brokers do not have an independent obligation to report this suspicious activity: that obligation rests with the insurance company. As such, the insurance company must have policies and procedures in place that are “reasonably designed to obtain customer-related information (which includes observations and assessment) from its insurance agents and brokers necessary to detect suspicious activity.”
- FinCEN further acknowledges that while it is up to the insurance company to determine the appropriate means for obtaining this information, “we anticipate that the insurance company may need to amend existing agreements with its agents and brokers to ensure that that company receives necessary customer information.
- Where an agent or broker is affiliated with an institution that has a separate obligation to file a SAR, it is permissible to file a joint SAR provided the narrative identifies the SAR as a “joint filing” with only one of the filing institutions being identified as the “filer”. The other institution should be identified in the narrative.
- The importance and implication of this provision cannot be overstated. There is now an express obligation on the part of an insurance company to identify and report suspicious activity that would only be known to it if communicated by its agent. The only way the insurance company will know about this is if the agent relates it to the insurance company. However, the insurance company is the entity obligated to file the SAR in this situation.
- While FinCEN acknowledges that certain agreements and contracts between the company and the agent may need to be modified, the extent of the documents that will require modification may not be significant.
- In addition to contracts and agreements, companies may need to modify applications, fact-finding tools and disclosures.
What to File

Language of SAR final rule:
Sec. 103.16 (c) (1): Filing Procedures – What to File

(1) What to file. A suspicious transaction shall be reported by completing a Suspicious Activity Report by Insurance Company (SAR-IC), and collecting and maintaining supporting documentation as required by paragraph (e) of this section.

FinCEN comments:

- FinCEN has released for comment proposed form SAR-IC, which resembles the SAR forms used by depository institutions.
- Until the SAR-IC form is adopted, insurance companies are directed to use FinCEN Form 101 - Suspicious Activity Reports by Securities and Futures Industries to report suspicious transactions.
- Companies issuing variable products should, at this time, also use FinCEN Form 101 to report suspicious activity. FinCEN is expected to clarify this requirement when it issues final rules for mutual funds in the future.
- While companies are still obligated to complete Form 8300 to report the receipt of certain cash and non-cash instruments totaling more than $10,000 in one transaction or in two or more related transactions, companies are not to use Form 8300 as the means for reporting suspicious activity. Companies can still check the appropriate box on the Form 8300 but the company must also file the required SAR-IC form.

Where to File SAR

Language of SAR final rule:
Sec. 103.16 (c) (2): Filing Procedures – Where to File

(2) Where to file. The SAR-IC shall be filed with the Financial Crimes Enforcement Network as indicated in the instructions to the SAR-IC.

When to File SAR

Language of SAR final rule:
Sec. 103.16 (c) (3): Filing Procedures – When to File

(3) When to file. A SAR-IC shall be filed no later than 30 calendar days after the date of the initial detection by the insurance company of facts that may constitute a basis for filing a SAR-IC under this section.

If no suspect is identified on the date of such initial detection, an insurance company may delay filing a SAR-IC for an additional 30 calendar days to identify a suspect, but in no case shall reporting be delayed more than 60 calendar days after the date of such initial detection.
In situations that require immediate attention, such as terrorist financing or ongoing money laundering schemes, the insurance company shall immediately notify by telephone an appropriate law enforcement authority in addition to filing a timely SAR-IC.

Insurance companies wishing voluntarily to report suspicious transactions that may relate to terrorist activity may call the Financial Crimes Enforcement Network’s Financial Institution Hotline at 1-866-556-3974 in addition to filing a timely SAR-IC if required by this section.

FinCEN comments:

- A SAR must be filed within 30 days after the insurance company becomes aware of the reportable suspicious activity.
- However, a delay of an additional 30 days is permissible if the insurance company has not identified the suspect. There is no delay permitted after 60 days.
- Companies will need to carefully document the process employed to demonstrate that a SAR was in fact filed in a timely manner.

A Suspicious Activity Report by an Insurance Company (SAR-IC) must be filed no later than 30 calendar days after the date of the initial detection of the suspicious transaction, with a permissible additional 30-day delay for the identification of the suspect. Section 103.16(c)(3).

Exceptions

Language of SAR final rule:

Sec. 103.16 (d): Exceptions

(d) Exception. An insurance company is not required to file a SAR-IC to report the submission to it of false or fraudulent information to obtain a policy or make a claim, unless the company has reason to believe that the false or fraudulent submission relates to money laundering or terrorist financing.

- Companies may want to clearly note in the files relating to a fraud inquiry that there is no reason to suspect the activity being investigated involves activity that would require the filing of a SAR.

Retention of Records

Language of SAR final rule:

Sec. 103.16 (e): Record Retention

(e) Retention of records. An insurance company shall maintain a copy of any SAR-IC filed and the original or business record equivalent of any supporting documentation for a period of five years from the date of filing the SAR-IC.

Supporting documentation shall be identified as such and maintained by the insurance company and shall be deemed to have been filed with the SAR-IC. When an insurance company has filed
or is identified as a filer in a joint Suspicious Activity Report, the insurance company shall maintain a copy of such joint report (together with copies of any supporting documentation) for a period of five years from the date of filing.

An insurance company shall make all supporting documentation available to the Financial Crimes Enforcement Network and any other appropriate law enforcement agencies or supervisory agencies upon request.

**FinCEN comments:**

- A copy of the filed SAR and all supporting documentation must be kept for a period of five years from the date of the filing.
- This includes all documentation provided to the insurance company by the agent or broker even where the filing is joint report.
- Companies should establish a clear policy and guidelines for the retention of documents required to be maintained under this rule.

An insurance company must keep a copy of the filed Suspicious Activity Report form for its records. The Suspicious Activity Report and the original or business record equivalent of any supporting documentation must be maintained in the insurance company’s records for a period of five years from the date of filing. An insurance company must also retain copies of reports (and supporting documentation) provided to it by its agents that are required to make reports when the agents and the company file a joint report regarding a transaction involving both companies.

**Insurance Brokers and Agents are not Required to File Suspicious Activity Reports**

The obligation to identify and report suspicious transactions applies only to an insurance company, and not to its agents or brokers. Although insurance agents and brokers are not independently required to report suspicious transactions, the regulation makes clear that agents and brokers are expected to work with insurance companies in identifying suspicious transactions that the company must report.

Not placing an independent reporting obligation on agents and brokers does not intend to minimize their role. FinCEN will assess the effectiveness of the rule on an ongoing basis. If it appears that the effectiveness of the rule is being undermined by the failure of agents and brokers to cooperate with their insurance company principals, they will consider proposing appropriate amendments to the rule. They also expect that an insurance company, when faced with a non-compliant agent or broker, will take necessary actions to secure such compliance, including, when appropriate, terminating its business relationship with such an agent or broker.
Confidentiality & Safe Harbor

Language of SAR final rule:

Sec. 103.16 (f): Confidentiality and Safe Harbor

(f) Confidentiality of reports; limitation of liability. No insurance company, and no director, officer, employee, agent, or broker of any insurance company, who reports a suspicious transaction under this part (whether such a report is required by this section or made voluntarily), may notify any person involved in the transaction that the transaction has been reported, except to the extent permitted by paragraph (b) (3) of this section.

Thus, any insurance company subpoenaed or otherwise requested to disclose a SAR-IC or the information contained in a SAR-IC (or copy of a joint Suspicious Activity Report filed with another financial institution involved in the same transaction, including an insurance agent), except where such disclosure is requested by the Financial Crimes Enforcement Network or another appropriate law enforcement or supervisory agency, shall decline to produce the Suspicious Activity Report or to provide any information that would disclose that a Suspicious Activity Report has been prepared or filed, citing as authority 31 CFR 103.16 and 31 U.S.C. 5318(g)(2), and shall notify the Financial Crimes Enforcement Network of any such request and its response thereto.

An insurance company, and any director, officer, employee, agent, or broker of such insurance company, that makes a report pursuant to this section, including a joint report (whether such report is required by this section or made voluntarily) shall be protected from liability for any disclosure contained in, or for failure to disclose the fact of, such report, or both, to the extent provided by 31 U.S.C. 5318(g)(3).

FinCEN comments:

- There is a statutory prohibition against the disclosure of information file in a SAR or even the disclosure that a SAR has been filed, regardless of whether the filing is required or is filed voluntarily. The exception is disclosures made to appropriate law enforcement and supervisory agencies.
- Insurance companies are not prohibited from obtaining customer information from agents or brokers or discussing with agents or brokers information necessary to detect and report suspicious activity.
- The SAR final rule provides a safe harbor from liability to any financial institution that makes a required or voluntary filing of a SAR.
- FinCEN states “If you are served with any subpoena requiring disclosure of the fact that a Suspicious Activity Report has been filed or of a copy of the Suspicious Activity Report itself, except to the extent that the subpoena is submitted by an appropriate law enforcement or supervisory agency, you should neither confirm nor deny the existence of the Suspicious Activity Report. You should immediately notify the Office of Chief Counsel at the Financial Crimes Enforcement Network (703-905-3590).”
- Companies must establish clear procedures and guidelines to protect the confidentiality of information related to the investigation and filing of a SAR. Most companies have significant experience establishing these protocols due to comparable requirements under such provisions as HIPAA for medical information.
Information Regarding a Suspicious Activity Report May Not Be Disclosed

Suspicious Activity Reports and the fact that they have been filed must be kept confidential. In particular, customers cannot be notified that a suspicious activity has been reported.

There are statutory and regulatory prohibitions against the disclosure of information filed in, or the fact of filing, a Suspicious Activity Report whether the report is required or is filed voluntarily. Thus, insurance companies filing the proposed Suspicious Activity Report by Insurance Companies (or receiving a copy of filed joint Suspicious Activity Reports from another financial institution involved in the same transaction) are specifically prohibited from disclosing that a Suspicious Activity Report has been filed or the information contained therein, except to appropriate law enforcement and regulatory agencies.

If someone is served with any subpoena requiring disclosure of the fact that a Suspicious Activity Report has been filed or of a copy of the Suspicious Activity Report itself, except to the extent that the subpoena is submitted by an appropriate law enforcement or supervisory agency, they should neither confirm nor deny the existence of the Suspicious Activity Report. They also should immediately notify the Office of Chief Counsel at the Financial Crimes Enforcement Network (703-905-3590).

Under federal law, insurance agents and brokers, as well as insurance companies, are protected from liability to customers for disclosing possible criminal activity to their insurance companies, law enforcement, and certain government supervisory agencies.

Consistent with requirements for other financial institutions, an insurance company and all relevant individuals associated with the company are prohibited from disclosing the filing of a SAR to any person involved in the reported transaction. The rule also includes a safe harbor for all individuals and companies who investigate or file a SAR as required by the rule.

An Insurance Company That Files a SAR Voluntarily Will Be Protected from Civil Liability

When an insurer voluntarily files a Suspicious Activity Report they are protected from civil liability to the same extent as a company filing a Suspicious Activity Report would be when required by law.

“Any financial institution that makes a voluntary disclosure of any possible violation of law or regulation to a government agency …shall not be liable to any person under any law or regulation of the United States… or regulation of any State…for such disclosure or for any failure to provide notice of such disclosure to the person who is the subject of such disclosure or any other person identified in the disclosure.”

It is the intent of this provision of the Bank Secrecy Act to provide the greatest possible protection to financial institutions, in the form of a “safe harbor,” to encourage the filing of Suspicious Activity Reports if appropriate.
Insurance Companies May Now Participate in Information Sharing Pursuant to the USA PATRIOT Act and Financial Crimes Enforcement Network Regulations

Information sharing between financial institutions concerning terrorist financing and/or money laundering is available to financial institutions that have an obligation to establish anti-money laundering programs. Once an insurance company subject to the insurance company anti-money laundering program rule has established its anti-money laundering program it may file a certification for purposes of section 314(b) of information sharing.

Joint Suspicious Activity Reports

In circumstances where two or more financial institutions subject to suspicious activity reporting requirements under the Bank Secrecy Act are involved in a common or related transaction, and each financial institution has information about the transaction, a joint Suspicious Activity Report may be filed. Neither the Bank Secrecy Act nor regulations promulgated by us prohibit financial institutions from sharing information relating to suspicious activities as long as no persons involved in the transaction are notified. A joint Suspicious Activity Report that is filed with us in the manner described above will be deemed to have been filed by each financial institution involved in the underlying transaction, thereby satisfying each financial institution's obligation to report suspicious activity. Financial institutions may share information pertaining to the transaction, as long as no persons involved in the transaction are notified. Such communications between financial institutions for the purpose of filing or determining whether to file a joint Suspicious Activity Report are protected by a safe harbor from civil liability pursuant to, as disclosures authorized under that section's implementing regulations and interpretative guidance.

In all such joint filings, only one of the filing institutions should be identified as the “filer” in the filer identification section of the form (unless the form accommodates multiple filers, as the Suspicious Activity Report for Insurance Companies will do). The Narrative section of the suspicious activity report must include the words “joint filing” and must identify the other financial institution or institutions on whose behalf the report is being filed (unless the form will accommodate multiple filers, in which case there is no need to include that information in the Narrative section).

Examining Authority & Compliance

Language of AML final rule:

Sec. 103.137(e):Examining Authority

(e) Compliance. Compliance with this section shall be examined by the Department of the Treasury, through the Financial Crimes Enforcement Network or its delegees, under the terms of the Bank Secrecy Act. Failure to comply with the requirements of this section may constitute a violation of the Bank Secrecy Act and of this part.

Language of SAR final rule:

Sec. 103.16 (g):Examining Authority

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(g) **Compliance.** Compliance with this section shall be examined by the Department of the Treasury, through the Financial Crimes Enforcement Network or its delegees, under terms of the Bank Secrecy Act. Failure to comply the requirements of this section may constitute a violation of the reporting rules of the Bank Secrecy Act and of this part.

**Compliance**

Compliance is mandatory. Compliance will be monitored by the Department of the Treasury, through the Financial Crimes Enforcement Network (FinCEN) or its delegees, under the terms of the Bank Secrecy Act. Failure to comply with the requirements could constitute a violation of the Bank Secrecy Act.

The Internal Revenue Service will examine insurance companies on the adequacy and effectiveness of their anti-money laundering programs.

The final rules specify that compliance with the rules “shall be examined by the Department of the Treasury, through the Financial Crimes Enforcement Network, or its delegees.” Based on comments provided by FinCEN at an industry conference, it is expected that the IRS will be the examining authority. It is not clear whether the examining authority will publish an examiner’s guide or provide the industry with insight into the examination process. However, in light of the recent publication of the Bank Secrecy Act/Anti-Money Laundering Examination Manual published by the Federal Financial Institutions Examination Council (FFIEC BSA/AML Examination Manual), the regulatory authority examining insurance companies for compliance with the final rules may be expected to produce relevant guidance for the industry to help ensure consistency and transparency in the examination process.

**Requirement for Companies Registered with the SEC**

**Language of AML final rule:**

Sec. 103.137(d): Requirement for Companies Registered with the SEC

(d) Anti-money laundering program requirements for insurance companies registered or required to register with the Securities and Exchange Commission as broker-dealers in securities. An insurance company that is registered or required to register with the Securities and Exchange Commission as a broker-dealer in securities shall be deemed to have satisfied the requirements of this section for its broker-dealer activities to the extent that the company is required to establish and has established an anti-money laundering program pursuant to §103.120 and complies with such program.

**Language of SAR final rule:**

Sec. 103.16 (h): Requirement for Companies Registered with the SEC

(h) Suspicious transaction reporting requirement for insurance companies registered or required to register with the Securities and Exchange Commission as broker-dealers in securities. An insurance company that is registered or required to register with the Securities and Exchange Commission as a broker-dealer in securities shall be deemed to have satisfied the requirements
of this section for its broker-dealer activities to the extent that the company complies with the reporting requirement applicable to such activities pursuant to § 103.19.

FinCEN comments:

- The intent of this provision is to help insurance companies avoid being subject to two different AML rules regarding the same activities.
- Requirements of the AML final rule falling outside of the covered broker-dealer activities would still be the responsibility of the insurance company.
- FinCEN does not extend the provision to apply to a broker-dealer that is distributing the insurance company’s products as an agent.

Certain insurance agents and insurance brokers may be broker-dealers in securities with an independent obligation to report suspicious activity under another Bank Secrecy Act regulation. Variable insurance products that are deemed securities under the Securities Exchange Act of 1934 must be sold by registered broker-dealers, which are themselves subject to a suspicious activity reporting obligation. Banks, which sell fixed annuities as agent for insurance companies, are also subject to suspicious activity reporting.

Efforts will be made to assure that agents and brokers who sell insurance products through broker-dealers that have their own anti-money laundering programs will not be subject to inconsistent insurance company programs. These registered representatives will likely experience little, if any, change to their current customer due diligence requirements with respect to sales of variable products.

**How Suspicious Activity Involving Variable Insurance Products Funded by Separate Accounts that Meet Definition of a “Mutual Fund” be Reported**

Some insurance companies issue variable insurance products funded by separate accounts, some of which meet the definition of a mutual fund. FinCEN is in the process of finalizing a rule that would require mutual funds to themselves file suspicious activity reports. When that final rule becomes effective, they will amend the insurance company suspicious activity reporting rule to ensure that such suspicious activity is reported under the mutual fund rule.

Until such time as a final rule requiring suspicious activity reporting by mutual funds is adopted, however, insurance companies that issue variable insurance products funded by separate accounts that meet the definition of a mutual fund may report suspicious activity on FinCEN Form 101 – Suspicious Activity Report by Securities and Futures Industries.

A mutual fund is an investment company (as defined in section 3 of the Investment Company Act of 1940 (15 U.S.C. 80a-3) that is an open-end company (as defined in section 5 of the Investment Company Act of 1940 (15 U.S.C. 80a-5)) that is registered, or required to register, with the Securities and Exchange Commission under section 8 of the Investment Company Act of 1940.
Unauthorized Entities

AN UNAUTHORIZED ENTITY IS AN INSURANCE COMPANY THAT IS NOT LICENSED BY THE FLORIDA DEPARTMENT OF FINANCIAL SERVICES. AGENTS AND BROKERS HAVE RESPONSIBILITY FOR CONDUCTING REASONABLE RESEARCH TO ENSURE THAT THEY ARE NOT WRITING POLICIES OR PLACING BUSINESS WITH UNAUTHORIZED ENTITIES. LACK OF CAREFUL SCREENING CAN RESULT IN SIGNIFICANT FINANCIAL LOSS TO FLORIDA RESIDENTS DUE TO UNPAID CLAIMS AND/OR THEFT OF PREMIUMS. AGENTS MAY BE HELD LIABLE WHEN REPRESENTING THESE UNAUTHORIZED ENTITIES. IT IS THE AGENTS AND BROKERS RESPONSIBILITY TO GIVE FAIR AND ACCURATE INFORMATION REGARDING THE COMPANIES THEY REPRESENT. ANY QUESTION ABOUT THE AUTHORIZED STATUS OF A COMPANY CAN BE CHECKED BY CALLING THE FLORIDA DEPARTMENT OF FINANCIAL SERVICES AT 1.800.342.2762. WE URGE ALL AGENTS AND BROKERS TO ADHERE TO THIS ADMONITION. THE STATE OF FLORIDA HAS TAKEN A VERY STRONG POSITION ON THE ISSUE OF UNAUTHORIZED ENTITIES.