



Complying with the CDD Rule

Presented by

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Roadmap

**Understanding the 4
Elements of Customer Due
Diligence (CDD)**

**Examiner's Expectations &
Guidance**



Customer Due Diligence Rule

- The CDD rule requires risk-based procedures for:
 1. Identifying and verifying the identity of members;
 2. Identifying and verifying the identity of **beneficial owners of legal entity members**;
 3. Understanding the nature and purpose of the member relationship to develop a member risk profile;
 4. Conducting ongoing monitoring to identify and report **suspicious activity**; and *on a risk-basis*, to maintain and update member(s)' and beneficial owner(s)' information



Identification and Verification of Members





Identity Verification

- The BSA requires credit unions to verify enough information to form a reasonable belief it knows the true identity of the member
- A credit union's CIP will explain which methods and documents will be required to be obtained and verified
 - For example, credit unions may apply **documentary** and/or **nondocumentary** methods to verify the identity of members
- A credit union's CIP must address situations where the identity of a member is not verifiable



Customer Identification Program

- At minimum, credit unions must collect the following information:
 - Name
 - Address
 - For individuals: a residential/business street address, an Army Post Office of Fleet Post Office box number, the address of next of kin or description of physical location.
 - For business: principal place of business/local office/other physical location.
 - Date of Birth for Individuals
 - TIN/Other for Non-US person



Identification and Verification of Beneficial Owners of Legal Entity Members



Defined Terms

- **Legal Entity Customer:** a corporation, limited liability company, other entity created by the filing of a public document with a Secretary of State/similar office, a general partnership, limited partnership and any similar entity formed under the laws of a foreign jurisdiction, business trusts that are created by a filing with a state office.
- Excluded: sole proprietorships, unincorporated associations or natural persons opening accounts on their own behalf, regulated financial institutions among others



Legal Entity Member Determination

- A credit union may rely on information provided by member to determine whether entity is excluded from the definition of a legal entity
- BUT CU must not have knowledge of facts that would reasonably call into question the reliability of such information



Defined Terms

- Definition of Beneficial Ownership has 2 prongs:
 - a) **Ownership:** each individual who, directly or indirectly, owns 25% or more of the equity interests of a legal entity member
 - b) **Control:** An individual with significant responsibility to control, manage, or direct the legal entity (e.g., CEO, CFO, COO, Managing Member, General Partner, President, VP, or Treasurer)



No. of Beneficial Owners

- Total number of beneficial owners is always between 1 – 5 individuals
 - Most legal entity accounts will have 0 to 4 individuals for the ownership prong +
 - At least 1 individual for the control prong
- For charities and non-profits that are not excluded from the definition of a legal entity, the CU is only required to obtain control prong information = 1



Examples of Ownership Prong

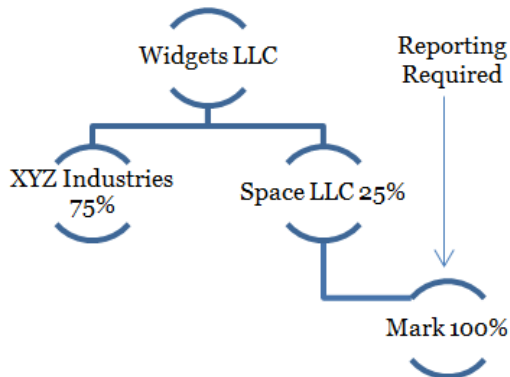


Image #1

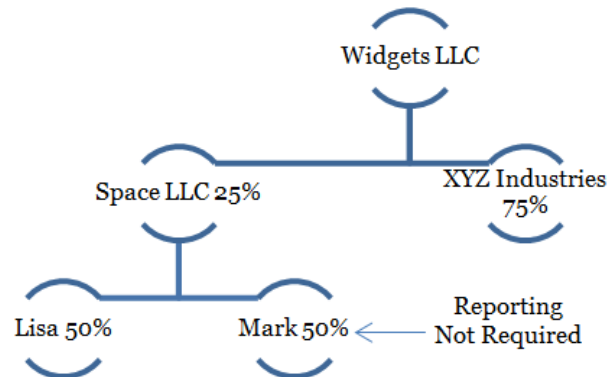


Image #2



New Accounts

- CUs must identify and verify BO information for each new or subaccount account opened
- If the CU has already obtained BO information, the CU may rely on this information for subsequent accounts opened provided the legal entity member certifies the information is up-to-date and accurate at the time of each account opening.
 - CU must maintain record of such certification



Existing Accounts

- If the BO has an account at the credit union, the CU may rely on CIP information already collected if it is:
 1. Up-to-date,
 2. Accurate, and
 3. The legal entity member's representative certifies/confirms (verbally or in writing) the accuracy of the pre-existing CIP information



Limited Relief

- FinCEN created a limited exemption from the requirement to collect BO information for certain financial products that present low risks for money laundering and terrorist financing
- At first the relief was set to expire in September, but it is now permanent for accounts opened before May 11, 2018
- The relief applies to certain renewals, rollovers, modifications and extensions



Covered Financial Products

- There are four types of accounts exempted:
 - 1. Certificates of Deposit Rollovers**
 - 2. Loan Renewals, Modifications and Extensions**
 - 3. Commercial Lines of Credit and Credit Cards**
 - 4. Safe Deposit Boxes Renewals**
- FinCEN defined and provided specific characteristics for each account type; if a credit union's products do not fit the descriptions, the credit union may need to collect beneficial ownership information



Obtaining BO Information

- BO information does not need to be collected directly from the beneficial owner, it can be collected from individual opening account on behalf of legal entity member
- Information that must be collected includes CIP information (e.g., name, date of birth, address, TIN or other government ID number)



Certification Form

- To make the collection of BO information easier, FinCEN created a [sample Certification Form](#)
- The use of this form is not mandatory, credit union can use its own form or other means to comply with the rule
- Make sure you are using the updated sample form as FinCEN released an amended form



Verification of BOs

- Verification of BOs must contain the same elements required for verifying the identity of individuals under the applicable CIP rule
- Differently from CIP for individuals, CUs may use photocopies or other reproductions of identification documents in the case of documentary verification
- Procedures must address situations in which the BO's identity cannot be verified



Understanding Member Relationship to Develop a Risk Profile; and on a Risk-Basis, Maintaining and Updating Member and Beneficial Owners' Information



Member Risk Profile

- Certain members/accounts may pose a higher risk for money laundering and terrorist financing than others
- CU must understand how the account will be used to better anticipate member's activity and report suspicious activity
- CDD rule is not prescriptive about how to "risk score" members and accounts, information gathered may include:
 - Self-evident information such as type of member or account, service or product; or
 - Basic information about the member such as annual income, net worth, principal occupation or business and the member's history of activity (for longstanding members)



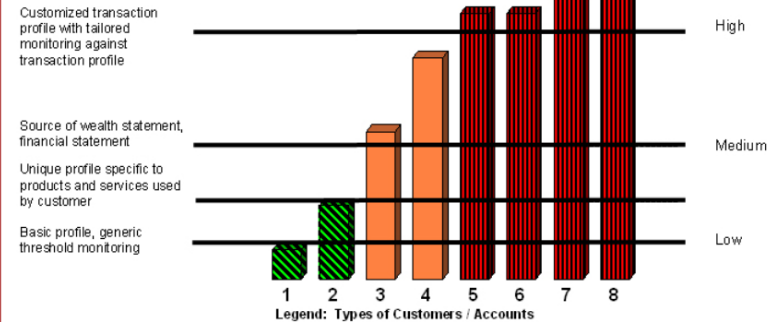
Example of Risk Rating

FOR ILLUSTRATION ONLY

Customer Risk versus Due Diligence and Suspicious Activity Monitoring

Certain customer relationships may pose a higher risk than others. This chart provides an example of how a bank may stratify the risk profile of its customers (see legend and risk levels). Because the nature of the customer is only one variable in assessing risk, this simplified chart is for illustration purposes only. The chart also illustrates the progressive methods of due diligence and suspicious activity monitoring systems that banks may deploy as the risk level rises. (See Observed Methods, below.)

Observed Methods of Due Diligence and Suspicious Activity Monitoring:



- Legend: Types of Customers / Accounts
- | | |
|---|--|
| 1 Resident Consumer Account (DDA, Savings, Time, CD) | 5 Nonresident Alien Offshore Investor |
| 2 Nonresident Alien Consumer Account (DDA, Savings, Time, CD) | 6 High Net Worth Individuals (Private Banking) |
| 3 Small Commercial and Franchise Businesses | 7 Multiple Tiered Accts (Money Managers, Financial Advisors, "Payable Through" Accounts) |
| 4 Consumer Wealth Creation (at a threshold appropriate to the bank's risk appetite) | 8 Offshore and Shell Companies |



Ongoing Monitoring to Identify and Report Suspicious Activity





Ongoing Monitoring

- Credit unions are expected to have internal controls to provide “sufficient controls and monitoring systems for timely detection and reporting of suspicious activity”
- All transactions going through, at or by the credit union should be subject to the monitoring
- Credit unions must file Suspicious Activity Reports for certain transactions



Risk-Based Updates





Triggering Events

- The rule does not impose a categorical requirement to update information, rather:
 - Credit unions must collect updated member/beneficial owner information if during the normal course of monitoring, there is a trigger that indicates a relevant change to the risk posed by the member or beneficial owner
 - Triggering events are not defined or prescribed
 - Credit union is expected to come up with its own list of triggering events



Examples of Triggers

- The rule does provide the following examples of events that could lead to a review of an account's beneficial ownership structure such as:
 - *"an unexpected transfer of all of the funds in a legal entity's account to a previously unknown individual... bank learns that the funds transfer was directly related to a change in the beneficial ownership of the legal entity...;*
 - *when a financial institution detects information (including a change in beneficial ownership information) about the customer in the course of its normal monitoring....; [and/or]*
 - *a significant and unexplained change in the customer's activity... for no apparent reason or a significant change in the volume of activity without explanation."*



Record Retention of Identification and Verification Documents



Record Retention Requirements

- CDD rule requires CU to retain all BO information collected about a legal entity member
- **Identifying information**, including the Certification Form or its equivalent, must be maintained for a period of 5 years after the legal entity's account is closed
- **All verification records** must be retained for a period of 5 years after the record is made



Examiner's Expectations



NCUA Examiner Expectations

- NCUA examines credit unions from a risk-focused approach
- [NCUA AIREs Questionnaire](#) details the items that will be examined for BSA compliance and notes the 3 areas of focus: (1) risk assessment; (2) independent testing; (3) monitoring for suspicious activity
- Additional examination priority for 2018: “...NCUA remains vigilant in ensuring the credit union system is not used to launder money or finance criminal or terrorist activity...Examiners will begin assessing compliance with [the CDD rule] in the second half of 2018.”

(emphasis added)



Examiner's Expectations

- NCUA recently published updated examination BSA Questionnaire and noted it would be examining CU's CDD processes for "good faith" through 2018
- In 2019, NCUA will be doing more in-depth reviews
- Of interest, the examination procedures mentioned policies and procedures for how BO information will be used for OFAC purposes



FinCEN Guidance

- FinCEN issued a couple of guidance documents pertaining to the CDD rule:
 - [FAQs # 1 \(7/16\)](#), [FAQ # 2 \(4/18\)](#), [FinCEN's Permanent Exemptive Relief \(9/07\)](#)
- Other helpful guidance includes the [FFIEC BSA/AML Examination Manual](#), which has sections on [Customer Identification](#), [CDD](#), [Suspicious Activity Reporting](#) and [Customer Risk Versus Due Diligence and Suspicious Activity Monitoring](#)



Questions?



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