LAW OFFICE OF JAMES A. NOFI, LLC

WHITE PAPER

FOREIGN BANKS' CERTIFICATION FOR PURPOSES OF SECTIONS 313 AND 319(b) OF THE USA PATRIOT ACT, 31 U.S.C. 5318(j) and 5318(k)

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INTRODUCTION

In the aftermath of the September 11, 2001, terrorist attacks in New York and Washington, D.C., the United States government, in order to combat terrorism more effectively, stepped up its efforts against the international money laundering that finances much terrorist and other illegal activity. In October 2001, Congress enacted – and President Bush signed into law – the Uniting and Strengthening by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act ("the USA PATRIOT Act" or "the Act").

The Act was designed to prevent, detect, and prosecute both international money laundering and the terrorist activity it funded. The Act changed in fundamental ways how business in the United States – especially the financial service business – is conducted. Title III of the Act, the International Money Laundering Abatement and Anti-Terrorist Funding Act of 2001, amended the existing Bank Secrecy Act ("the BSA") to require certain due diligence and record keeping requirements of United States financial institutions that maintain correspondent accounts for foreign banks. The regulations promulgated under the Act include a safe harbor through a certification process for foreign banks to comply with Sections 313 and 319(b) of the Act.

As the eighth anniversary of the adoption of the Act approaches, this White Paper reviews the requirements relating to the safe harbor of the Certification by foreign banks in order for both the foreign banks and United States financial institutions to comply with Sections 313 and 319(b) of the Act and provides a "how to" guide for completing the Certification Form. This will serve as a refresher for those United States financial institutions and foreign banks that have been complying with these requirements and an introduction for those financial institutions, both domestic and foreign, that are new to this requirement.

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The Statutory Provisions and Rules

Section 313(a) of the Act prohibits a covered financial institution[1] from establishing, maintaining, administering, or managing a correspondent account[2] in the United States for,or on behalf of a foreign shell bank, *i.e.* a foreign bank that does not have a physical presence in any country.[3] Section 313(a) also requires covered financial institutions to take reasonable steps to ensure that correspondent accounts they provide to foreign banks are not being used to provide banking services indirectly to foreign shell banks.[4]

Section 319(b) of the Act requires any covered financial institutions that provides a correspondent account to a foreign bank to maintain records of the foreign bank's owners and to maintain the name and address of an agent in the United States designated to accept service of legal process for the foreign bank for records relating to the correspondent account.[5]

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1 A "covered financial institution" is defined as (1) an insured bank, as defined in Section 3(h) of the Federal Deposit Insurance Act; (2) a commercial bank or trust company; (3) a private banker ; (4) an agency or branch of a foreign bank in the United States; (5) any credit union, a thrift institution; and (6) a broker or dealer registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934.

2 A correspondent account is "an account established . . . for a foreign bank to receive deposits from, [or] to make payments or other disbursements on behalf of[,] a foreign bank, or to handle other financial transactions related to the foreign bank." 31 CFR 103.175(d). For covered financial institutions that are registered broker-dealers, the term would include "any account . . . that permits the foreign bank to engage in securities transactions, fund transfers, or other financial transactions through [the] account." *See,* 67 FR 60562. This definition clearly includes, among other accounts, any delivery-versus-payment (DVP) brokerage account established for a foreign bank. *In the Matter of Hartsfield Capital Securities, Inc.*, FINCEN No. 2003-05 at p. 2, fn 4.

3 31 U.S.C. 5318(j) (1).

4 31 U.S.C. 5318(j) provides

> A covered financial institution shall take reasonable steps to ensure that any correspondent accounts established, maintained, administered, or managed by that covered financial institution in the United States for a foreign bank is not being used by that foreign bank to indirectly provide banking services to another foreign bank that does not have a physical presence in any country.

5 31 U.S.C. 5318(k)(3)(B)(1).

Under the Act, the Secretary of the Treasury is authorized to interpret and administer these provisions. In September 2002, the Financial Crimes Enforcement Network ("FINCEN") of the Treasury Department issued final rules to implement the provisions of the Act discussed above. This rule provides that a covered financial institution could satisfy the requirements of Sections 313(a) and 319(b) by obtaining from the foreign bank a certification that contained the necessary information or by otherwise obtaining documentation of the required information.[6] The covered financial institutions can avail themselves of this safe harbor provision if it obtains the foreign banks' certification or re-certification at least once every three years or whenever the relevant information changes. Obviously, it is easier for both parties to use the certification process rather than for the foreign bank to produce – and the covered financial institutions to maintain – the records necessary to establish the information required by the Act.

The Certification

The Certification Form is relatively straightforward and consists of seven sections. It can be found as Appendix A to Subpart I of Part 103 – Certification Regarding Correspondent Accounts for Foreign Banks, OMB Control Number 1505-0184. Section A identifies the foreign financial institution. Under Section B of the Certification, the foreign bank chooses whether to apply the Certification to all of its United States correspondent accounts or only to the accounts in a particular financial institution.

Part C requires the foreign bank to certify information dealing with its physical location to ensure that it is not a shell bank. The bank must certify whether it maintains a physical address in a country where it is authorized to conduct banking activities, employs one or more individuals on a full time basis, maintains operating records related to its banking activities, and is subject to inspection by the banking authority that issued its license. If the bank does not have such a physical presence, but is a "regulated affiliate," it must certify that it is an affiliate of a depository institution, credit union, or bank that meets the physical presence test set forth above. If the foreign bank does not have a physical presence and is not a regulated affiliate, it must so state in Part C, and it is deemed a foreign shell bank. In that case, the covered financial

6 31 CFR § 103.77(b).

institution must terminate the correspondent relationship.[7]

Under Part D, the foreign bank must certify that it does not use any correspondent accounts with a covered financial institution to indirectly provide banking services too a foreign shell bank, *i.e.*, a foreign shell bank that does not maintain a physical presence in any country and is not a regulated affiliate of a bank that does maintain such a physical presence.

Part E requires the foreign bank to provide its ownership information. If the foreign bank is publicly traded or has previously reported its ownership to the Federal Reserve Board on a Form FRY-7, it simply has to check the appropriate box. If the foreign bank does not fall under either of these categories, it must identify its owners in the next section of Part E.

For purposes of the Certification, "owner" is defined as any person who, directly or indirectly, either owns, controls, or has the power to vote 25 percent or more of any class of voting securities or other voting interests of the foreign bank or controls in any manner the election of a majority of the directors of the foreign bank. "Person" is defined as any individual, bank, corporation, partnership, limited liability company, or any other legal entity. "Voting securities or other voting interests" means securities or other interest that entitle the holder to vote for or select directors. Members of the same family[8] are considered one person. In determining the ownership interest of the same family, any voting interest of any family member must be taken into account.

Under Part F, the foreign bank must identify an individual or entity resident in the United States who is authorized to accept service of process on behalf of the foreign bank from the Secretary of the Treasury and/or the Attorney General of the United States pursuant to 31 U.S.C. 5318(k). As set forth more fully below, this process agent must be appointed in accordance with the laws and procedures relating to corporate governance of the foreign bank in its home jurisdiction.

Part G of the Certification contains an agreement by the foreign bank to notify the covered financial institution, in writing, of any changes in fact or circumstance of the Certification. The foreign bank also acknowledges that the covered financial

7 31 CFR § 104.40(d).

8 In a footnote, the Certification Form defines "same family" to means parents, spouses, children, siblings, uncles, aunts, grandparents, grandchildren, first cousins, stepchildren, step-siblings, parents-in-law, and spouses of any of the foregoing.

institution may provide a copy of the Certification to the Treasury Department and the Department of Justice. The foreign bank also acknowledges its understanding that the information contained in the Certification may be transmitted to other United States departments or agencies.

Recertification Process

Treasury Department regulations require that a foreign bank update its Certification at least once every three years.[9] Through the Re-Certification Form, the foreign bank certifies that the information contained in the Certification either remains true and correct or is revised by attaching a statement describing the information that is no longer correct and setting forth the current correct information. The Recertification Form must contain both the date of the execution of the prior Certification or Recertification and the date of its own execution. It can be found as Appendix B to Subpart I of Part 103 – Recertification Regarding Correspondent Accounts for Foreign Banks, OMB Control Number 1505-0184.

In February 2006, FINCEN issued guidance to clarify the date on which covered financial institutions must complete the recertification to comply with the regulations relating to correspondent accounts for foreign banks. FINCEN "determined that all recertifications must be obtained by covered financial institutions on or before the three-year anniversary of the *execution* of the initial or previous certification (emphasis in original).[10]

FINCEN further advised that it viewed all recertifications as essentially formal attestations of no material change to the previous certification. Since the recertification form contains both the execution date of the previous certification and the date of delivery of the recertification to the covered financial institution, compliance with the regulation can be confirmed directly from the face of the recertification form. As long as the gap between the two dates does not exceed three (3) years, the foreign bank is in compliance with the regulation.[11]

If inaccuracies in a certification are corrected by a revised certification, as set forth in more detail below, or if a certification is amended to reflect a material change in

9 31 CFR §105.7(b).
10 FIN-2006-G003 (February 3, 2006) at p. 2.
11 *Id.*

fact or circumstance, the recertification applies to the revised or amended certification and not the original certification. In these circumstances, a recertification should note the execution date of the revised or amended certification and should be delivered within three years of that date.[12]

Continuing Obligation to Update Information

Both the Certification and the Recertification are not just forms that must be completed every three years and then ignored until the next deadline. If, at any time, a covered financial institution know, suspects, or just has a reason to suspect that any of the information contained in a Certification or Re-certification is no longer correct, it *must* ask the foreign bank to verify or correct such information. Failing that, the covered financial institution must take other appropriate measures to ascertain the accuracy of the information or to correct the information.[13] The covered financial institution has 90 days to receive verification or correction of the information from the foreign bank. If not received within that time period, the covered financial institution must close all correspondent accounts within a commercially reasonable time. It may not permit the foreign bank to establish any new positions or execute any transaction through any correspondent account, except for the transactions necessary to close the account.[14]

Record Keeping Requirements

The covered financial institution is required to retain the original of the Certification and Re-Certification Forms for at least five (5) years after the closing of all correspondent accounts for a foreign bank.[15] It is also required to retain for five (5) years the original or copy of any document it otherwise relied upon to comply with these sections of the Act. The Treasury Secretary is also given the power to order the covered financial institution to retain such documents for a longer period of time.

12 *Id.* at 3.
13 31 C.F.R. § 103.177(c).
14 31 C.F.R. § 103.177(D)(3).
15 31 C.F.R. § 103.177(e).

Considerations for Selecting a USA PATRIOT Act Process Agent

Most of the Certification form merely requires the foreign bank to provide information to the covered financial institution, in lieu of providing the actual documents evidencing that information. The one affirmative action required of the foreign bank is the appointment of a process agent in the United States.

Under Section 319(b) of the Act, 31 U.S.C. 5318(k), the Treasury Department and/or the United States Attorney General may issue a subpoena or a summons to any foreign bank with a correspondent account in the United States compelling the production of records relating to the correspondent account. Such a request could include records maintained outside of the United States relating to the deposit of funds into the foreign bank. In order to facilitate the service of such process on the foreign bank in the United States, a foreign bank must designate an agent for service of process in the United States.[16]

The process agent must be a person who resides in the United States and must be authorized to accept service of legal process on behalf of the foreign bank from the Secretary of the Treasury and/or the Attorney General of the United States. The purpose of this appointment is to give the United States government a direct method of asserting jurisdiction over a foreign bank that maintains a correspondent account at a financial institution in the United States in order to obtain documents from the foreign bank. A foreign bank can no longer seek to force the United States to serve process on it in its home jurisdiction in order to obtain the documents relating to the correspondent accounts, including deposits into the foreign bank.

The failure for a foreign bank to appoint and identify its process agent is a vital component of the Certification. In assessing a civil monetary penalty with undertakings against a broker-dealer, FINCEN noted that

> The failure to obtain information on agents for service of legal process is of particular concern, since the information is essential for perfecting legal process on foreign banks and for ensuring that domestic law enforcement agencies have access to foreign bank records. Foreign bank records could

16 The summons or subpoena "may be served on the foreign bank in the United States . . . if the foreign bank has a representative in the United States." 31 U.S.C. § 5318(k)(3)(A)(iii). Similar language is contained in 31 CFR § 103.185.

> be used to reconstruct deposits and other transactions between foreign banks and their customers, thereby assisting law enforcement in their investigation of money laundering and terrorist financing.[17]

What does a foreign bank need in a process agent? It needs someone who understand the importance of that function and can timely notify the foreign bank of the receipt of any such process. The Law Office of James A. Nofi, LLC is well suited to handle this function for a foreign bank. Mr. Nofi is an experienced litigator and regulatory attorney who spent more than a decade working for the New York Stock Exchange Division of Enforcement. He is experienced in dealing with regulators and self-regulatory organizations. Mr. Nofi is also experienced in dealing with international issues relating to broker-dealer compliance. He has been a speaker on securities regulatory matters at the Jamaica Stock Exchange's Investment & Capital Markets Conferences in 2008 and 2007. Mr. Nofi also lectured at the Jamaica Stock Exchange's Summer Workshop for Brokers in 2006.

The appointment of a process agent is a straightforward matter. The foreign bank must, in accordance with the law of its home jurisdiction adopt the necessary corporate resolution appointing the Law Office of James A. Nofi, LLC as process agent. (A sample copy of such a resolution can be provided to the foreign bank, but it must be adapted as necessary to comply with the legal requirements of the foreign bank's home jurisdiction.) The foreign bank must then complete its Certification Regarding Correspondent Accounts for Foreign Banks, OMB Control Number 1505-0184 and file it with the United States covered financial institution where it maintains its accounts. Section F of the Certification must be completed to report that the Law Office of James A. Nofi, LLC, residing at 3003 Summit Boulevard, Suite 1400, Atlanta, Georgia 30319, (404) 684-8844, (678) 303-9387 (fax), has been appointed as process agent pursuant to 31. U.S.C. 5318(k).

17 *Hartsfield Capital Securities, Inc.*, at 3-4.

For further information, including fees and contract terms, please contact the Law Office of James A. Nofi, LLC.

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