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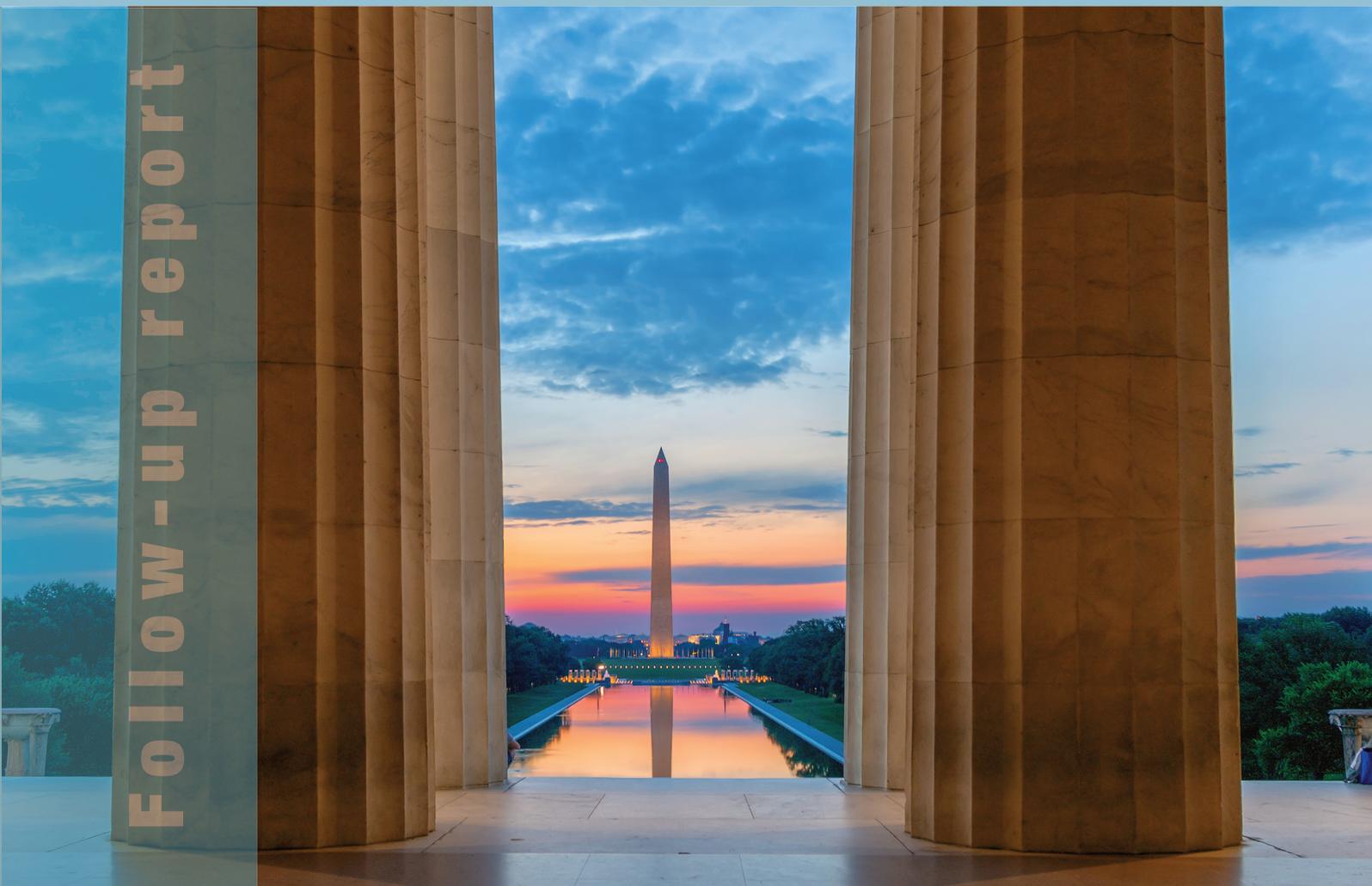


Anti-money laundering and
counter-terrorist financing
measures

United States

3rd Enhanced Follow-up Report &
Technical Compliance Re-Rating

Follow-up report





The Financial Action Task Force (FATF) is an independent inter-governmental body that develops and promotes policies to protect the global financial system against money laundering, terrorist financing and the financing of proliferation of weapons of mass destruction. The FATF Recommendations are recognised as the global anti-money laundering (AML) and counter-terrorist financing (CTF) standard.

For more information about the FATF, please visit the website: www.fatf-gafi.org

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UNITED STATES: 3rd ENHANCED FOLLOW-UP REPORT

1. INTRODUCTION

The mutual evaluation report (MER) of the U.S. was adopted in October 2016. The U.S. did not request technical compliance re-ratings during its 1st or 2nd follow-up reports. This follow-up report analyses the U.S.' progress in addressing certain technical compliance deficiencies which were identified in its MER. Re-rating is given where sufficient progress has been made (Recommendation 10). This report also analyses the U.S.' progress in implementing new requirements relating to the Financial Action Task Force (FATF) Recommendations which have changed since the end of the on-site visit to the U.S. in February 2016: Recommendations 2, 5, 7, 8, 15, 18 and 21. This report does not address what progress the U.S. has made to improve its effectiveness. A later follow-up assessment will analyse progress on improving effectiveness which may result in re-ratings of Immediate Outcomes at that time.

2. FINDINGS OF THE MUTUAL EVALUATION REPORT

The MER rated the U.S. as follows for technical compliance:

Table 1. Technical compliance ratings, October 2016

R 1	R 2	R 3	R 4	R 5	R 6	R 7	R 8	R 9	R 10
PC	C	LC	LC	C	LC	LC	LC	C	PC
R 11	R 12	R 13	R 14	R 15	R 16	R 17	R 18	R 19	R 20
LC	PC	LC	LC	LC	PC	LC	LC	LC	PC
R 21	R 22	R 23	R 24	R 25	R 26	R 27	R 28	R 29	R 30
C	NC	NC	NC	PC	LC	C	NC	C	C
R 31	R 32	R 33	R 34	R 35	R 36	R 37	R 38	R 39	R 40
LC	C	LC	C						

Note: There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

Source: United States Mutual Evaluation Report, December 2016, <https://www.fatf-gafi.org/media/fatf/documents/reports/mer4/MER-United-States-2016.pdf>

Given these results, the FATF placed the U.S. in enhanced follow-up¹. The following experts assessed the U.S.' request for technical compliance re-ratings:

- Mr. Alvin Koh, Deputy Director & Specialist Leader, Monetary Authority of Singapore, Singapore, and
- Mr. Bill Peoples, Legal Services, New Zealand Police, New Zealand.

¹ Enhanced follow-up is based on the FATF's traditional policy that deals with members with significant deficiencies (for technical compliance or effectiveness) in their AML/CFT systems, and involves a more intensive process of follow-up.

Section 3 of this report summarises the U.S.' progress made in improving technical compliance. Section 4 sets out the conclusion and a table showing which Recommendation has been re-rated.

3. OVERVIEW OF PROGRESS TO IMPROVE TECHNICAL COMPLIANCE

This section summarises the U.S.' progress to improve its technical compliance by:

- a) Addressing certain technical compliance deficiencies identified in the MER, and
- b) Implementing new requirements where the FATF Recommendations have changed since the on-site visit to the US (Recommendations 2, 5, 7, 8, 15², 18 and 21).

3.1. Progress to address technical compliance deficiencies identified in the MER

The U.S. has made progress to address the technical compliance deficiencies identified in the MER in relation to Recommendation 10. As a result of this progress, the U.S. has been re-rated on this Recommendation.

Recommendation 10 (originally rated PC)

In its 4th round MER, the U.S. was rated PC with R.10 based on the following deficiencies: lack of customer due diligence (CDD) requirements to ascertain and verify the identity of beneficial owners (BO), which was a significant shortcoming; investment advisers (IAs) were not directly covered by *Bank Secrecy Act* (BSA) obligations (some IAs were indirectly covered through affiliations with banks, bank holding companies and broker-dealers); financial institutions other than in the securities and derivatives sectors were not explicitly required to identify and verify the identity of persons authorised to act on behalf of customers, and some FIs were not explicitly required to understand and obtain information on the purpose and intended nature of the business relationship. FIs were not required to understand the ownership and control structure of customers that are legal persons/arrangements.

As of May 2018, *31 Code of Federal Regulations (CFR) § 1010.230 (Beneficial ownership requirements for legal entity customers)* requires covered financial institutions³ to establish and maintain written procedures that are reasonably designed to identify and verify beneficial owners of legal entity customers and to include such procedures in their anti-money laundering (AML) compliance program. The requirements to identify and verify BO, as applied to legal persons (such as corporations and limited liability companies), is clear with respect to both its ownership threshold and its control element. It is however not explicit as regard all type of legal arrangements, but would cover legal arrangements (such

² The U.S. volunteered to be reassessed on R.15 based on the revised FATF Methodology (adopted at October 2019 plenary).

³ As noted in footnote 91 (page 197) of its 4th round MER, covered financial institutions include insured banks, commercial banks, agencies or branches of a foreign bank in the U.S., credit unions, savings associations, corporations acting under section 25A of the *Federal Reserve Act 12 USC 611*, trust companies, securities broker-dealers, futures commission merchants (FCMs), introducing brokers in commodities (IBs), and mutual funds.

as trust) which are required to be registered by certain state authorities – such legal arrangements are considered legal entities and hence covered.

In addition, the U.S. has introduced ongoing CDD requirements for FIs, which included the need to have appropriate risk-based procedures on understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile, and ongoing monitoring of the customer relationship to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

However, a few minor technical gaps remain, including the lack of explicit BO requirements, mainly in relation to other trust relevant parties for legal arrangements. Limited measures have been taken to improve the occasional transaction threshold of USD 3 000 for Money Services Business (MSBs)⁴ and to improve gaps with regard to life insurance companies.⁵ In addition, IAs are still not directly covered by BSA obligations.⁶

Overall, the U.S. has addressed a number of the key identified deficiencies, but deficiencies (especially in relation to all types of legal arrangements) still remain. **The U.S. is therefore re-rated as Largely Compliant with R.10.**

3.2. Progress on Recommendations which have changed since the adoption of the MER

Since the U.S. 4th round MER on-site visit, the FATF has amended Recommendations 2, 5, 7, 8, 15, 18 and 21. This section considers the U.S.' compliance with the new requirements, and its progress to address the technical compliance deficiencies identified in the MER in relation to these Recommendations.

Recommendation 2 (originally rated C)

In October 2018, R.2 was amended to require countries to have cooperation and coordination between relevant authorities to ensure compatibility of AML and counter-terrorist financing (AML/CFT) requirements with Data Protection and Privacy rules. The amended Recommendation further requires a domestic mechanism for exchange of information. In its 4th round MER, the U.S. was rated C with R.2.

The U.S. complies with the revised requirements of R.2. Domestic coordination and cooperation, including exchange of information domestically concerning the development and implementation of AML/CFT policies and activities, were considered in the U.S. 4th round MER to be an overall strength of the U.S. system. In addition, the publication of the first *National Strategy for Combating Terrorist and Other Illicit Financing* in 2018 further affirms the ability of various agencies in the U.S. to coordinate and exchange information.

⁴ In practice, MSBs have also filed suspicious activity reports (SARs) under the thresholds and hence it would suggest that there is a certain level of checks and controls present. Hence, the deficiency is given lesser weight in the U.S.' context.

⁵ This is given less weight in light of the lower ML/TF risk of the sector, which is also consistent with the FATF Risk-based Approach Guidance for the Life Insurance Sector and U.S.' risk assessment.

⁶ While additional measures should continue to be taken for IAs, the IA sector is assessed to be relatively lower risks in light that there are few (if any) ML-related typologies, and in practice, a large percentage (over 54%) of IAs currently undertake AML/CFT obligations via affiliations with FIs that are subject to AML/CFT requirements, and with over 75% of IAs having some form of AML/CFT policies. Hence, from technical compliance perspective, this deficiency is given less weight in the US' context.

The U.S. does not have a central data protection authority, nor a privacy regime that conceives the protection of privacy as a fundamental right in all circumstances. While there are various statutes that protect financial data, these do not inhibit the implementation of AML/CFT measures or requirements (see criterion 9.1 of the U.S. 4th round MER). In addition, the U.S. Department of the Treasury's Office of Terrorist Financing and Financial Crimes (TFFC) coordinates with a number of authorities to ensure privacy and other restrictions do not unduly hinder the dissemination of information for AML/CFT purposes.

The revised and new criteria have both been met. **The U.S. therefore remains rated Compliant with R.2.**

Recommendation 5 (originally rated C)

In February 2016, a new obligation was added to R.5, requiring countries to criminalise the financing of foreign terrorist fighters.

The U.S. federal criminal terrorist financing (TF) offences are broad enough to cover this aspect, since the time of the U.S. 4th round MER. Operation Rhino, for example, described in paragraph 193 of the MER, provided an example of an enforcement action involving individuals travelling abroad and included an enforcement response against individuals who facilitated travel. Facilitation includes financing the travel of individuals to another country.

In addition, several cases were pursued against foreign terrorist fighters and attempted supporters subsequent to the MER, which confirm the existing TF offences are broad enough. **The U.S. therefore remains rated Compliant with R.5.**

Recommendation 7 (originally rated LC)

In November 2017, R.7 was amended to reflect changes to the United Nations Security Council Resolutions (UNSCRs) on proliferation financing since the FATF standards were issued in February 2012.

In its 4th round MER, the U.S. was rated LC with R.7. The deficiency was in relation to the fact that the U.S. had applied targeted financial sanctions (TFS) without delay to most, but not all persons designated by the UN pursuant to UNSCRs 1718 and 1737, which was a minor deficiency as the US implemented 90% (138 of the 154) of the UN Democratic People's Republic of Korea (DPRK)-related and Iran-related listings without delay (within a matter of hours).

The U.S. implements UN TFS through a combination of legal authorities that are codified in the regulations of Treasury's Office of Foreign Asset Control. These are: the *Weapons of Mass Destruction Proliferators Sanctions Regulations (31 C.F.R. Part 544)*, which implements *Executive Order 13382*, the *North Korea Sanctions Regulations (31 C.F.R. 510)*, the *Iranian Transactions and Sanctions Regulations (31 C.F.R. part 560)*, the *Iranian Financial Sanctions Regulations (31 C.F.R. part 561)*, and the *Iranian Human Rights Abuses Sanctions Regulations (31 C.F.R. part 562)*.

On DPRK, UNSCRs 1718 and 1874 have been implemented and the U.S. issued press releases relevant to the listings in UNSCRs 2087, 2094, 2270, and 2321. The press releases accompany most U.S. designations. Whenever a UN listing is not reflected in the press release, it is because that individual or entity was already listed by the authorities. On Iran, for the purposes of R.7, UNSCR 2231 terminated several previous UNSCRs relating to Iran and weapons of mass destruction proliferation, but no individual or entity that has been added to the UNSCR 2231 list since it was created (hence no specific release needed).

However, the deficiency in its 4th round MER has not been fully addressed. The U.S. has implemented around 93% (versus 90% at time of MER) of the total UN Proliferation Financing (PF)-related listings, but has still not covered all of the persons/entities designated by the PF-related UNSCRs.

On this basis, the U.S. remains rated Largely Compliant with R.7.

Recommendation 8 (originally rated LC)

In June 2016, R.8 and its Interpretive Note were substantially revised, and the assessment of R.8 in the MER therefore needed to be reviewed.

In its 4th round MER, the U.S. was rated LC with R.8, based on a minor deficiency in relation to the fact that houses of worships were exempt from the requirement of applying to the Internal Revenue Service (IRS) for recognition of their tax-exemption status.

The 2018 *National Terrorist Financing Risk Assessment* deals extensively with charitable organisations and the risk of TF abuse in line with the required by the revisions to R.8. The U.S. has regulatory and administrative mechanisms, described in its 4th round MER, that promote accountability and integrity in the management of non-profit organisations (NPOs). In addition, the IRS monitors compliance of NPOs with the U.S. tax laws and can conduct criminal investigations as necessary. Sanctions applied are proportionate and dissuasive in case of violation of requirements.

Moreover, there are mechanisms to ensure effective cooperation, coordination and information sharing on TF issues, including as regards NPOs. There are multiple mechanisms to promptly share information regarding suspected terrorist abuse.

However, the minor deficiency identified in the 4th round MER remains, as houses of worships are still exempt from the requirements of applying to the IRS for recognition of their tax-exemption status.

On this basis, the U.S. remains rated Largely Compliant with R.8.

Recommendation 15 (originally rated LC)

In October 2019, revisions were made to methodology for assessing R.15, to reflect amendments to the FATF Standards incorporating virtual assets (VA) and virtual asset service providers (VASP).

In its 4th round MER, the U.S. was rated LC with R.15, based on minor deficiencies, including that not all IAs were covered and there were no explicit requirements for FIs to address the risks presented by new technologies.

The U.S. has met or mostly met most of the new criteria of R.15, through the following actions, although minor deficiencies, such as coverage of IAs, remain:

- U.S. authorities understand and are aware of the ML/TF risks emerging from virtual assets. Aside from various taskforce and working groups set up to consider the risks, their risk understanding is also reflected in their *2018 National Money Laundering Risk Assessment* and *National Terrorist Financing Risk Assessment*, as well as the *2018 National Strategy for Combating Terrorist and Other Illicit Financing*.
- The combination of the various U.S. legislation would cover the five classes of VASPs as defined by the FATF, but it does not explicitly include all VASPs that is solely incorporated the U.S. (i.e. a VASP which does not perform any activity relating to U.S. persons, or a U.S.' nexus).

- Most convertible virtual currencies (CVC) exchangers, administrators and other similar entities are regulated as money transmitters (or MSBs) under the BSA and have to implement AML/CFT programs as MSBs. Such MSBs have to develop, implement and maintain an effective AML program and the program shall be commensurate with the risks posed by the location, size, nature and volume of the financial services provided by the MSBs. Further, banks and persons registered with, and functionally regulated or examined by, the Securities and Exchange Commission (SEC) and Commodity Futures Trading Commission (CFTC), that engage in transactions denominated in value that substitutes for currency will be subject to BSA regulations according to the applicable section of *31 CFR* Chapter X. However, the CDD threshold for occasional transactions for MSBs is USD 3 000 (as opposed to USD 1 000 required in the FATF Standards) and this higher threshold is not clearly supported by low ML/TF risks.
- MSBs must register with FinCEN and renew every two years. MSBs have to be licensed at the state level, and background checks are conducted at the state level prior to the issuing of licenses. CVC providers examined by SEC or CFTC are also subject to fit and proper checks.
- In general, FinCEN, SEC, and CFTC are able to apply a range of proportionate and dissuasive sanctions for non-compliance, including for CVCs that are unlicensed or not-registered. The U.S. authorities have, even prior to the revisions made to R.15, also taken actions against CVCs providers for operating as an unlicensed money transmitting business (e.g. U.S. vs E-Gold and Liberty Reserve).
- Since 2014, IRS and FinCEN have conducted examinations of various CVC providers, including administrators, some of the largest exchangers by volume (a key vulnerability assessed by the U.S. authorities in this space), individual peer-to-peer exchangers, etc. The U.S.' strategy is to inspect all covered financial institutions but does not specifically identify higher risk VASPs, as they are largely covered under the broader MSB regime. Therefore, it is not entirely clear whether the current approach is sufficiently risk focused, especially since only 30% of all registered CVC providers have been inspected since 2014.
- FinCEN, SEC and CFTC have published a range of guidance over the years. In particular, FinCEN's Guidance issued in May 2019 provides a good overview of the existing regime and regulatory expectations with regard to CVC providers in the U.S.
- With regard to mutual legal assistance and international cooperation, the U.S. was rated LC for R.37, R.38, and R.39, and C for R.40 in its 4th round MER, due mainly to concerns relating to application of dual criminality requirements. Financial supervisors (such as SEC, CFTC and FinCEN) have a legal basis for providing co-operation with their foreign counterparts (regardless of their respective nature or status), in particular with respect to the exchange of supervisory information related to or relevant for AML/CFT purposes. However, given the overall treatment of U.S. authorities of CVC as a form of assets, which can be subject to seizure and confiscation, the gaps are the same with those identified in the 4th round MER.

On this basis, the U.S. remains rated as Largely Compliant with R.15.

Recommendation 18 (originally rated LC)

In February 2018, R.18 was amended to reflect the November 2017 amendments to the FATF Standards (interpretive note 18), which clarified the requirements on sharing of information and analyses related to unusual or suspicious transactions within financial groups, and the interaction of these requirements with tipping-off provisions.

In its 4th round MER, the U.S. was rated LC with R.18, based on minor deficiencies that not all IAs were covered and there was no explicit obligation to inform the home supervisors if the host country did not permit proper implementation of AML/CFT measures.

The revised standard is met. There are no specific prohibitions preventing covered financial institutions from sharing customer information within the financial group. In 2006, FinCEN issued guidance permitting banks, securities and futures firms to share SARs as well as information underlying SARs (subject to certain exceptions and qualifications) with parent entities, both within and outside of the U.S. In 2014, FinCEN also highlighted in an Advisory that information should be shared throughout the organization (which would include multiple affiliated institutions) and that there is information in various departments within a financial institution that may be useful and should be shared with the compliance staff. The *31 U.S.C. § 5318* also contains a general prohibition on tipping off.

However, the deficiencies identified in its 4th round MER relating to coverage of IAs and obligation to inform the home supervisors, if the host country does not permit proper implementation of AML/CFT measures, still remain.

On this basis, the U.S. remains rated as Largely Compliant with R.18.

Recommendation 21 (originally rated C)

In February 2018, R.21 was amended to clarify that anti-tipping-off provisions are not intended to inhibit information sharing under R.18. In its 4th round MER, the U.S. was rated C on R.21.

The revised standard remains met. Pursuant to *31 C.F.R. 1020.320(e)*, the provisions of prohibiting financial institutions and their directors, officers and employees from disclosing the fact that an SAR or related information is being filed shall not be construed as prohibiting the sharing of an SAR or any information related to the SAR.

The U.S. therefore remains rated as Compliant with R.21.

3.3. Brief overview on other Recommendations rated PC/NC

The U.S. has reported progress on other Recommendations rated PC/NC, such as R.1, R.12, R.16, R.20, R.24, R.25 and R.28. Actions underway include, among others, undertaking a systemic review of its AML/CFT system to more effectively address identified risks, including with respect to some sectors currently uncovered.

CONCLUSION

The U.S. has made progress to address the technical compliance deficiencies identified in the MER and has been upgraded on Recommendation 10. After the technical compliance re-rating, five Recommendations remain PC and four Recommendations remain NC.

Technical compliance with the FATF Recommendations has been re-rated as follows:

Table 2. Technical compliance with re-ratings, February 2020

R 1	R 2	R 3	R 4	R 5	R 6	R 7	R 8	R 9	R 10
PC	C	LC	LC	C	LC	LC	LC	C	LC
R 11	R 12	R 13	R 14	R 15	R 16	R 17	R 18	R 19	R 20
LC	PC	LC	LC	LC	PC	LC	LC	LC	PC
R 21	R 22	R 23	R 24	R 25	R 26	R 27	R 28	R 29	R 30
C	NC	NC	NC	PC	LC	C	NC	C	C
R 31	R 32	R 33	R 34	R 35	R 36	R 37	R 38	R 39	R 40
LC	C	LC	C						

Note: There are four possible levels of technical compliance: compliant (C), largely compliant (LC), partially compliant (PC), and non-compliant (NC).

The U.S. will remain in enhanced follow-up on the basis that it has nine Recommendations remaining rated PC/NC for technical compliance, and three Immediate Outcomes remaining rated ME/LE for effectiveness. In accordance with the FATF Procedures, the U.S. will report back to the FATF on progress to strengthen its implementation of AML/CFT measures.

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March 2020

Anti-money laundering and counter-terrorist financing measures in the United States

3rd Enhanced Follow-up Report & Technical Compliance Re-Rating

As a result of the United States' progress in strengthening their measures to fight money laundering and terrorist financing since the assessment of the country's framework, the FATF has re-rated the country on 1 of the 40 Recommendations.

The report also looks at whether the United States' measures meet the requirements of FATF Recommendations that have changed since their Mutual Evaluation in 2016.

Follow-up report