Anti-Money Laundering Plans

By ADR Staff

Indirect Lenders as Enforcement Agencies

The CFPB's intention to impose controls on dealer markups through indirect lenders in order to ensure compliance with the Equal Credit Opportunity Act has been well reported in industry news. A similar technique is now being used by the Treasury Department to enforce Anti-Money-Laundering regulations on dealers. One component of Bank Secrecy Act and Anti-Money Laundering (AML) measures is the requirement for certain financial institutions to develop a written Customer Identification Plan (CIP). Auto dealers and their related finance companies have traditionally been tasked with the requirement to confidently identify their customers prior to entering into a financial transaction, but they are not required by regulation to develop a formal written plan specifically outlining their identification procedures. Nevertheless, even without a regulatory requirement at the current time, dealers with indirect lending agreements may be asked by their lending institution to provide a written CIP.

Regulatory Background

In an effort to restrict terrorist and drug trade access to the financial system, the USA Patriot Act of 2001 requires financial institutions - including banks, loan and finance companies, and vehicle dealers – to develop written CIPs. *However, vehicle dealers were exempted from the CIP regulatory requirement in 2002*. Until 2012, all non-bank loan and finance companies (including dealer related finance companies) were also exempt. In 2012, loan and finance companies as a category were removed from the exemption list. At that time, rules were published defining "loan and finance companies" to be limited to residential mortgage lenders and originators for purposes of CIP requirements, effectively retaining the exemption for dealer related finance companies. (It is worth noting that regulators have stated their intention to periodically add other segments of the finance industry to the definition and have specifically mentioned entities that provide credit for the purchase of equipment and motor vehicles as potentially being subject to AML regulations under future rules.) The requirement for dealers to develop a written CIP is arising from auditor and regulator pressure on banks and other indirect lending institutions. The indirect lender's regulatory obligation is essentially being extended out to dealers and related finance companies through indirect lending agreements.

Content of the CIP

The written CIP formally documents a dealership's policies and procedures involved in identifying a customer and forming a reasonable belief that it knows the customer's true identity. Development of those procedures begins with a risk assessment of the dealership's vulnerability to money-laundering activities, paying particular attention to the methods of opening accounts and to their geographic locations. For instance, accounts opened online generate a higher risk level than those opened in person. And Oklahoma dealerships located in the following counties –

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which are designated "High Intensity Drug Trafficking Areas" (HIDTAs) – are at higher risk for encountering money-laundering activities than those located elsewhere.

- Cleveland
- Comanche
- Muskogee
- Oklahoma
- Sequoyah
- Tulsa

The CIP must detail the identifying information that will be required from each customer prior to opening an account. At a minimum, the dealership must collect the customer's name, date of birth, physical address, and tax-identification number. If the risk assessment warrants, the dealership may require additional identifying documentation. The CIP must contain risk-based procedures for verifying the identity of the customer within a reasonable period of time after the account is opened, and must contain procedures for circumstances in which the bank cannot form a reasonable belief that it knows the true identity of the customer. Further, the CIP must include recordkeeping procedures. At a minimum, the dealership must retain the identifying information obtained at account opening for a period of five years after the account is closed.

Checking Government Lists

According to the Bank Secrecy Act CIP regulations, the written plan should include procedures for determining whether the customer appears on any federal government list of known or suspected terrorists or terrorist organizations. At the current time, no specific government lists have been identified for CIP purposes (FFIEC BSA/AML Examination Manual, footnote 50). However, the Office of Foreign Assets Control (OFAC) maintains a list of Specially Designated National (SDN) foreign entities with whom all U.S. persons are prohibited from engaging in business activities. When buying or selling a vehicle, or otherwise opening a customer account, dealers are obliged to check the SDN and ensure that the other party to the transaction is not a targeted entity. Dealers may wish to consider incorporating OFAC compliance procedures in the CIP.

Notice to the Customer

The CIP must include procedures for providing customers with adequate notice that the dealership is requesting information to verify their identities. Notice may be provided in a number of ways, including posting in the lobby, posting on a web site, or incorporating within transaction documents. Sample language is provided by the regulation:

> IMPORTANT INFORMATION ABOUT PROCEDURES FOR OPENING A NEW ACCOUNT – To help the government fight the funding of terrorism and money laundering activities, federal law requires all financial institutions to obtain, verify, and record information that identifies each person who opens an account. What this means for you: When you open an account, we will ask for your name,

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address, date of birth, and other information that will allow us to identify you. We may also ask to see your driver's license or other identifying documents.

Relationship to Other Regulations

As mentioned, the written CIP requirement is an anti-terrorism and money-laundering tool instituted by the USA Patriot Act that is incorporated in the Bank Secrecy Act section of the US Code. The CIP requirement does not derive from consumer financial protection regulations but, because of the nature of the personal consumer data involved, it interacts with them in various ways. For instance, the Red Flags Rule, a consumer protection rule, requires covered institutions to develop a written identity theft prevention plan. The Red Flags Rule also requires collection of personal identifying data and an institution's CIP can be incorporated into their written Red Flags plan to satisfy those customer identification requirements. Once collected, the personal information then becomes subject to consumer financial privacy regulations. The Safeguards Rule requires covered institutions to develop a written plan outlining their procedures to physically protect consumers' private financial information, including that collected as a product of the CIP. The Disposal Rule dictates that consumer personal private financial information that has been collected must be disposed of in a particular fashion. Procedures for complying with the Disposal Rule should be incorporated into the written Safeguards plan. Finally, the Privacy Rule requires covered institutions to provide consumers with a notice that summarizes the institution's activities involving the collection, protection, and sharing of consumers' personal financial information. The claims and statements made in the Privacy Notice should comport with the policies and procedures outlined in each of the above referenced written plans including the CIP. *And all of the claims and statements made in all of the written plans and the Privacy Notice should comport with the actual practices of the institution.*

Summary

Dealers and their related finance companies should plan to develop a written Customer Identification Plan if they do not already have one. Even though dealers and their related finance companies are not currently under a direct regulatory requirement to develop a written plan, their indirect lender is. Bank auditors and regulators are extending the indirect lender's regulatory obligation out to the dealer through the indirect lending agreement. Also, dealer related finance companies might keep in mind that their current regulatory exemption is temporary. They will, in all likelihood, at some point be included in the definition of "loan and finance companies" that are subject to the regulatory requirement to develop a written Anti-Money Laundering Program that incorporates strong customer identification procedures.

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