



## **How Broker Dealers AML Expectations have Been Clarified Through Revised Small Firm Templates**

*Featured in ACAMS Connection Newsletter*

Finra opened 2010 with notice that the small firm template had been updated<sup>1</sup> and followed with \$750,000 in fines lodged against two broker dealers, Penson Financial Services and Pinnacle Capital Markets.<sup>2</sup> Asked and answered...as in...the industry has been demanding clearer guidance and the regulators have responded.

The revised small firm template has almost doubled in size but doesn't really have any content or expectations that will appear new to the AML officer who has listened during their AML exam, read AML sanctions and followed industry discussions over the last five years.

In general, the revised small firm template indicates that firms are expected to be more specific in their descriptions of how they execute their duties. The guidance text specifically states in various places that firms are expected to include who, what, when, where and how as they describe what they will do to meet a regulation and how they will address failures or issues. While most firms will find that their desktop procedures can be cross referenced to the template, it would be wise to double check that all of the required content is easily identified. It is likely that regulators will measure programs against the revised template.

*Select areas and details have been noted below. Not all revisions to the template have been included. Firms are encouraged to review their programs carefully to ensure they identify necessary changes.*

### **Risk Assessments**

The revised template opens with an expanded discussion on risk-based programs. FINRA cites a formal written risk assessment as a good practice and notes that the risk assessment can be used to demonstrate why your program is reasonable for your firm.

To meet their expectations, make sure that you identify all key areas of business as well as methods employed to identify new or changed risks. For example, if your firm has a new business or new product committee, explain how AML is advised of potential new products. If your firm is engaged on a path to grow through acquisition, explain when and how AML participates in the acquisition and integration of newly acquired units. Review AML sanctions over the last few years and consider how the business of the sanctioned firm compares to your business. Look beyond AML sanctions to trends in all types of violations. The SAR-SF form cites many types of violations; understanding the risk of those violations and the controls that mitigate those risks is key to the success of your firm's AML program.

### **AML Compliance Person and Duties**

Be sure to update your designated AML compliance person within 30 days of a change.

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<sup>1</sup> <http://www.finra.org/Industry/Issues/AML/p006340>

<sup>2</sup> <http://www.finra.org/Newsroom/NewsReleases/2010/P120859>



## **Information Sharing**

### *Sharing with Parent Companies including non-U.S. Entities*

Although this section is new, the content referenced was originally published in January 2006.

## **Customer Identification Program**

### *Responsibility for completing CIP*

Make certain that your clearing firm agreement and your AML program consistently reflect whether the introducing firm or the clearing broker is executing customer identification program (CIP). Be certain that you clarify between receiving reports which you may use as part of your CIP and actual responsibility for the verification. If you are relying on your clearing firm to execute CIP, identify exactly where this is documented in the your clearing services agreement. Be prepared to discuss how you know the process used is adequate.

### *Required Customer Information*

Procedures for following up on a tax identification number applied for but not received must be described including who, what, when and how such follow-up will occur.

### *Higher Risk Accounts*

The revised template advises adequate customer due diligence is the foundation of a strong AML compliance program and suggests including specific thresholds for account value or types of accounts that will be subjected to additional customer due diligence. As with other sections, the customer due diligence includes text which suggests including procedures explaining how due diligence information will be maintained.

## **Correspondent Accounts for Foreign Banks**

The revised template notes that where firms have a policy prohibiting correspondent accounts for foreign banks, the firm should include the policy as well as a description of internal controls implemented to ensure that such accounts are not opened.

The easiest procedure to implement to meet this requirement is to subject all entity accounts opened without a TIN to a series of tests to determine if they would be considered a foreign financial institution. This will cover both the foreign banks issue and the foreign financial institutions in the next section.

## **Due Diligence and Enhanced due diligence requirements for correspondent accounts of Foreign Financial Institutions**

Based on the fact that the Pinnacle sanction was related to failure to adequately identify and monitor activity related to sub accounts of a foreign financial institution, firms should pay careful attention to their policies and procedures in this area if they service foreign broker dealers. This is especially true if the foreign broker dealer is active in products that can be high risk such as low priced securities.



*This section is updated for regulatory changes that have occurred since the original issuance of the small firm template.*

### **Special Measures/Section 311**

*This section is updated for regulatory changes that have occurred since the original issuance of the small firm template.*

### **Monitoring Accounts for Suspicious Activity**

The revised template recommends very specific information in this section including descriptions of the reports or documents that are used to monitor for suspicious activity and what firms will do to investigate information identified in the reports.

Red flags have been updated and grouped by activity or characteristic. Information related to insurance products, penny stock companies and securities transactions has been expanded. Pay careful attention to this section of your program. Failure to adequately develop policies, procedures and controls associated with these tasks could cause your written AML program to be deemed inadequate. Inclusion of activities that your firm does not have adequate resources to execute could be deemed failure to execute and/or supervise if you do not complete actions in a timely manner or follow-up on items identified in your reports.

If you do not designate specific methods to monitor suspicious activity and you fail to use or evidence use of any of the AML related reports offered by your clearing services provider, it could be considered failure to adequately implement controls.

### **AML Record Keeping**

The AML record keeping section has been expanded to include an entire section on additional brokerage records.

### **Clearing/Introducing Firm Relationships**

While there are no significant changes to content, this section now includes direction to identify reports provided by the clearing firm and the manner in which they will be used.

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