

## **DEALERSHIP'S COMPLIANCE WITH THE USA PATRIOT ACT, ITS IMPLEMENTING REGULATIONS AND OTHER ANTI-TERRORISM MEASURES**

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On September 11, 2001, terrorists launched an unprecedented attack on the United States. Since then, the Government has taken action to develop strategies to identify and freeze the assets of terrorists. Just two weeks after the attacks, President Bush issued an Executive Order pursuant to the International Emergency Economic Powers Act prohibiting U.S. citizens from entering into "any transaction or dealing" with individuals or entities identified by Federal and State Departments. On October 26, 2001, following a flurry of legislative activity, the President signed into law the USA Patriot Act making a number of amendments to the anti-money laundering provisions of the Bank Secrecy Act and the Money Laundering Control Act of 1986. The amendments were intended to make it easier to detect, prevent, and prosecute international money laundering activities and the financing of terrorism. The following is a summary of the requirements under the Executive Order issued by the President, the USA Patriot Act, emerging implementing regulations and the effects all of this will have on your Dealership's policies, practices and overall operations.

### **Executive Order 13224- Prohibiting Transactions with Terrorists**

Motor vehicle dealerships must comply with the reporting requirements mandated pursuant to the International Emergency Economic Powers Act and Executive Order 13224. The Executive Order prohibits U.S. citizens from entering into "any transaction or dealing" with individuals or entities identified either in the Executive Order, by the Department of Treasury or by the Secretaries of State as posing a significant risk of committing terrorist acts or providing support to these organizations or individuals. All property and interests in property of the individual or entity in the United States or in the possession or control of U.S. persons are blocked.

An alphabetical master list of Specially Designated Nationals and Blocked Persons is maintained by the Office of Foreign Asset Control (OFAC) and can be found in various formats at <http://www.ustreas.gov/offices/enforcement/ofac/sdn/index.html>. According to a Report issued by the Department of the Treasury in September of 2002, 236 individuals, entities and organizations were designated under the Executive Order as supporters of terrorism. This includes 112 individuals, 34 U.S. designated Foreign Terrorist Organizations, 15 other terrorist organizations and 74 companies, charitable organizations or entities who support and/or finance terrorism, and this list is updated regularly. The penalties for noncompliance with the Order can be severe. Individuals who violate the Order can be fined up to \$250,000 and serve up to 10 years in prison, while companies can be fined up to \$500,000. A U.S. based company that enters into a franchise, joint venture or other agreement with an individual or entity that appears on the list faces possible fines, and seizure of assets. Information about the OFAC's most recent actions and forms for reporting blocked and rejected transactions can be obtained at <http://www.ustreas.gov/offices/enforcement/ofac/forms/index.html>.

### **Introduction to the USA Patriot Act**

Title III of the USA Patriot Act is comprised of ten titles aimed at providing stronger surveillance powers, strengthening criminal laws against terrorism, improving intelligence, and combating money laundering. Title III of the USA Patriot Act applies to all “financial institutions,” regardless of size, and expands the scope of the Bank Secrecy Act to include organizations not formerly covered. The Rules adopted by the Financial Crimes Enforcement Network (FinCEN), a Bureau under the Department of Treasury, clarify that the Act expanded the scope of the Bank Secrecy Act to include insurance companies, loan or finance companies, and businesses engaged in motor vehicle sales. In many instances, the USA Patriot Act requires the Department of Treasury and/or other Federal Departments or Agencies to enact rules and regulations to implement the Act’s various requirements. Many of the Rules required by the Act are currently in effect or will be soon.

### **Cash Reporting Requirements**

One of the requirements under the USA Patriot Act that is already in effect for motor vehicle dealers is the reporting requirement adopted pursuant to Section 365 of the Act. Pre-existing laws required financial institutions to file a Currency Transaction Report (CTR) with FinCEN whenever they received large sums of money in one or a series of related transactions. Section 365 of the USA Patriot Act expanded the scope of entities required to file reports to include “anyone” engaged in a trade or business that receives more than \$10,000 in cash in one transaction (or two or more related transactions). Section 365 also prohibits anyone from structuring a transaction to avoid the cash reporting requirements. The Form, titled “IRS Form 8300/FinCEN Form 8300,” is virtually identical to the IRS Form 8300 that motor vehicle dealers are required to complete pursuant to a similar provision under the Internal Revenue Code. Now they are required to report to FinCEN as well as the IRS. In fact, the IRS issued a Rule amending its regulations to clarify that the information reported to the IRS on cash transactions is also required to be reported to FinCEN. Motor vehicle dealers were required to begin using the new Form on January 1, 2002. A copy of the Form is included with these materials and is also available at <http://www.treas.gov/fincen/form8300dec2001.pdf>. The penalties for failing to file the Form 8300 with FinCEN or otherwise evading the filing requirements are substantial, including fines, seizure of assets and, in some cases, imprisonment.

### **Information Sharing Between Government Agencies and Financial Institutions**

The Treasury Department also issued a Final Rule implementing Section 314 of the Act, which establishes procedures that encourage information sharing between governmental authorities and financial institutions, and among financial institutions themselves. The first part of the Rule establishes a mechanism for law enforcement agencies to communicate the names of suspected terrorists and money launders to financial institutions in an effort to locate and secure accounts and transactions involving those suspects.

Effective as of September 26, 2002, any motor vehicle dealership that receives the name of a suspect must designate one person at the dealership to be the contact person regarding the request and any future requests that it receives. While all industries should be on notice that FinCEN may contact them for information, as a practical matter, not all financial institutions will receive requests for information because FinCEN does not currently regulate all of the covered financial institutions and it does not have contact information to reach a large number of them. In the event that FinCEN does submit such a request, however, the dealership must be prepared to provide it with the contact person’s name, title, mailing address, e-mail address, telephone number and facsimile number and to notify FinCEN promptly of any modifications with respect to that information.

The dealership's contact person must search the following account and transaction records for the names provided:

1. Any current accounts maintained by the dealership;
2. Any accounts maintained by the dealership during the past 12 months; and
3. Any transactions conducted during the past 6 months that the dealership is required by law or regulation to record or that the dealership has recorded and maintained.

If the dealership has entered into a transaction with an individual or entity on the list, the contact person must send a Report to FinCEN that contains:

1. The name of the individual, entity or organization;
2. The account numbers or, in the case of transactions, the date and type of each transaction; and
3. The social security number, taxpayer identification number, passport number, date of birth, address, or other identifying information provided by the individual or entity at the time of the transaction.

Questions about the scope or terms of a request should be directed to the Federal Law Enforcement Agency that sent the request for information to FinCEN. Remember, however, that if the dealership finds a match, it must send the Report to FinCEN, not the Federal Law Enforcement Agency that requested the search. Although the dealership may be disclosing nonpublic personal information about its customer(s), it is permitted to do so pursuant to the Gramm-Leach-Bliley Act and the Federal Trade Commission's (FTC) Privacy Rule. The Gramm-Leach-Bliley Act and the FTC's Privacy Rule permit the disclosure of nonpublic personal information without having to provide the customer with an opportunity to opt out of the disclosure if it is necessary to comply with federal, state and local laws. The information provided by FinCEN may only be used by the dealership to:

1. Provide FinCEN with the required Report;
2. Determine whether to establish or maintain an account or engage in a transaction; and
3. Assist the dealership in complying with the applicable anti-money laundering program requirements.

Except as necessary to process a request for information, dealerships are further prohibited from disclosing to any person or entity, other than FinCEN or the Federal Law Enforcement Agency for which FinCEN is requesting information, the fact that FinCEN has requested or obtained information from the dealership. In fact, the dealership must maintain adequate procedures to protect the security and confidentiality of information requested by FinCEN.

The requirement to maintain adequate security and confidentiality procedures to protect the information is met if the dealership applies the same procedures it has established to comply with the Gramm-Leach-Bliley Act and the FTC's Safeguards Rule. Motor vehicle dealerships must comply with the Safeguards Rule by May 23, 2003. In order to do so, they must develop, implement, and maintain an information security program that is appropriate to the dealership's size and complexity, the nature and scope of its activities and the sensitivity of the customer information it collects. Since most dealerships have not established procedures to comply with the FTC's Safeguards Rule, they must establish adequate procedures to protect the security and confidentiality of requests from FinCEN. The FTC recently issued Guidelines titled

“Financial Institutions and Customer Data: Complying with the Safeguards Rule,” which includes suggested policies and procedures for complying with the FTC’s Safeguards Rule. A copy of the Guidelines is included with these materials.

The second part of the Final Rule implementing Section 314 of the Act outlines how financial institutions can share information concerning suspected terrorist and money laundering activities with other financial institutions under the protection of a safe harbor that protects them from liability. This portion of the Rule only applies to financial institutions that are required to establish and maintain an anti-money laundering program at this time. Since the regulations for motor vehicle dealerships have not taken effect as of yet, motor vehicle dealerships cannot avail themselves of the safe harbor provisions and are not subject to the certification requirements.

### **Implementation of Anti-Money Laundering Regulations**

Section 352 of the USA Patriot Act mandates that all covered industries establish anti-money laundering programs. Section 352(c) of the Act directs the Secretary of Treasury to prescribe regulations for anti-money laundering programs that are "commensurate with the size, location, and activities" of the financial institution. On April 29, 2002, the Department of Treasury released Interim Rules requiring banks and certain other financial institutions to establish their anti-money laundering programs. Separate Rules applicable to each industry were drafted to ensure that the programs would be appropriately tailored to address the risks posed by how the individual industries conduct business.

Under the Interim Rules issued in April and the subsequent Final Rules issued in September, covered financial institutions must, at a minimum: (1) Develop internal policies, procedures and controls; (2) appoint a compliance officer to oversee the program; (3) train employees to follow the program; and (4) conduct an independent audit to make sure the program is followed. Covered financial institutions include banks, which already had an anti-money laundering program requirement, securities brokers, futures commission merchants and introducing brokers, money services businesses and operators of credit card systems.

The Treasury Department also issued Proposed Rules on September 18, 2002, requiring insurance companies and investment companies not registered with the Securities and Exchange Commission to establish anti-money laundering programs. Insurance companies are defined as life insurance companies and any other insurance company that offers products with investment features or features of stored value and transferability. Under the applicable Rule, insurance and investment companies must establish and maintain written anti-money laundering programs that, at a minimum: (i) Incorporate internal policies, procedures, and controls based on the assessment of their money laundering risks; (ii) designate a compliance officer; (iii) include an ongoing employee training program; and (iv) establish an independent audit function.

As for the motor vehicle industry, the Department of Treasury exercised its authority to defer the application of the Interim Rules until October 24, 2002. Motor vehicle dealerships, and other specified industries, were temporarily exempted so that the Department of Treasury could conduct additional research on the potential risks of money laundering activities and “ensure the issuance of well-considered regulations tailored to the unique money laundering risks of the [se] remaining financial institutions.” The Department recognized that many of the remaining financial institutions are small businesses that have never been subject to anti-money laundering regulations and that the risks inherent in their operations will vary considerably. The Interim Rules issued in April provided that if the Department of Treasury did not publish industry

specific Rules or elect to exempt or further defer the application of the Interim Rules, the Interim Rules would become effective as of October 24th.

As we anticipated, the October 24th deadline was further extended for the motor vehicle industry. The Department of Treasury has indicated that it will not publish final anti-money laundering rules applicable to motor vehicle dealerships before the October 24th deadline and it intends to publish guidance again deferring the effective date. The Department of Treasury has further indicated that it will publish proposed rules in the near future and will provide the affected industries with an opportunity to comment.

Although rules requiring implementation of an anti-money laundering program have not been issued for the motor vehicle industry, based upon the Rules that have been issued to date for other financial institutions, motor vehicle dealerships can begin preparing to comply with the anticipated Rules by establishing written procedures on how the dealership will:

1. Verify the identity of customers.
2. Record identifying information provided by the customer, methods and results of any measures undertaken to verify identities, and the resolution of any discrepancies in identifying information obtained.
3. Determine whether a customer appears on any list of known or suspected terrorists or terrorist organizations provided by a Federal Government Agency, including the list of Specially Designated Nationals and Blocked Persons provided by OFAC.
4. Provide customers with adequate notice that the dealership is requesting information to verify their identity. Verifying customer identities, which is discussed in more detail in the next section, includes using third-party sources, such as consumer reporting agencies, verifying change-of-address requests, maintaining adequate security standards, and using encryption technology when storing or transmitting electronic information.

### **Regulations Pertaining to Identifying and Verifying Customer Identities**

In July, the Department of Treasury, in conjunction with seven other Federal Regulatory Agencies, jointly issued Proposed Rules pursuant to Section 326 of the USA Patriot Act requiring certain financial institutions to develop procedures for identifying and verifying the identity of customers seeking to open accounts. Section 326 of the Act provides that the regulations must, at a minimum, require financial institutions to implement reasonable procedures for:

1. Verifying the identity of any person seeking to open an account, to the extent reasonable and practicable.
2. Maintaining records of the information used to verify the person's identity, including the person's name, address, and other identifying information.
3. Determining whether the person appears on any lists of known or suspected terrorists or terrorist organizations provided to the financial institution by a Government Agency.

The Proposed Rules are aimed at protecting the U.S. financial system from money laundering and terrorist financing, as well as protecting consumers against various forms of fraud, including

identity theft. They apply to banking institutions, securities brokers, mutual funds, futures commission merchants and introducing brokers, credit unions and private banks and trust companies that do not have a federal regulator. These institutions are required to incorporate a written Customer Identification Program into their anti-money laundering program that is appropriate given the entity's size, location and type of business no later than October 26, 2002. The Customer Identification Program must include:

1. Reasonable procedures for identifying any person, including businesses, seeking to open an account. The procedures must specify the type of identifying information the institution will require. At a minimum, for U.S. citizens, they must obtain the name, address, taxpayer identification number and, for individuals, date of birth. They have the discretion to decide what type of information they will request of a non-U.S. citizen in place of a taxpayer identification number. Options include a U.S. taxpayer identification number, passport number and country of issuance, an alien identification card, or the number and country of issuance of any other government-issued document evidencing nationality or residence and bearing a photograph or similar safeguard.
2. Procedures for providing customers with adequate notice that information is being required to verify their identity. This notice requirement may generally be satisfied by notifying customers about the procedures that the financial institution must comply with in order to verify their identities. For example, a sign may be posted in the lobby or the customer may be provided with written or oral notice. If an account is opened electronically, the financial institution may also provide notice electronically.
3. Procedures for verifying the identity of customers seeking to open an account within a reasonable period of time. The financial institutions must set forth in writing procedures describing how identifications will be verified, when documents will be used for this purpose, and when other methods will be used in lieu of or in addition to documents. While the Rule is flexible, it is clear that the financial institutions are ultimately responsible for exercising reasonable efforts to identify customers and their procedures must enable them to form a reasonable belief that they know a customer's true identity.
4. Maintenance of records of information used to verify a customer's name, address, and other identifying information. Such records must include the customer information, a copy of the documents reviewed, and a summary of the means and results of any other measures taken to identify the customer, including the resolution of any discrepancy in the identifying information obtained.
5. Procedures to determine whether customers appear on any lists of known or suspected terrorists issued by the Federal Government.

Development of procedures for determining when an account should not be opened, or when an existing account should be closed, as a result of an inability to verify the identity of a customer. Such procedures must include determining when an account may be opened while a customer's identity is being verified, and whether a Suspicious Activity Report (SAR) should be filed. To date, FinCEN has imposed filing requirements for SARs only with respect to banks, savings associations, credit unions, certain money services businesses and registered securities brokers, and casinos and card clubs. For example, the Department of Treasury issued a Final Rule requiring all casinos and card clubs located in the United States with gross annual gaming revenue of more than \$1 million to file a SAR with FinCEN on all transactions involving at least \$5,000 that the casino "knows, suspects, or has reason to suspect" fall into specific categories.

Motor vehicle dealerships are not required to file SARs, but may voluntarily file such Reports or report information concerning suspicious transactions that may be related to money laundering or terrorist activity by calling the Financial Institutions Hotline (1-866-556-3974). The purpose of the Financial Institutions Hotline is to facilitate the immediate transmittal of the information provided to law enforcement officials.

For motor vehicle dealerships, the identifying information obtained from customers would be essentially the same information currently obtained by most motor vehicle dealerships for individual customers, including the customer's name, address, date of birth and identification numbers (driver's license and social security number). Similarly, motor vehicle dealerships generally have procedures in place to verify the identity of customers within a reasonable period of time. Forms of identity verification utilized by motor vehicle dealerships include examining and making copies of customer driver's licenses and obtaining credit reports. Dealers should determine whether these policies have been reduced to writing in a procedures manual and what additional policies and procedures may be necessary to meet the remaining requirements.

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