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**Memorandum for the Record**

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Memorandum prepared by: John Roth

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Commission Participants: Doug Greenburg, Serena Wille, John Roth

Non-commission participants: Richard Small

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On September 2, 2003, we interviewed on the record Richard Small, who is the managing director for global anti-money laundering for Citigroup, which includes Citibank, Smith-Barney, Primerica and a number of other financial services companies. He has been at that position for two years, since July of 2001. Prior to that, he worked at the federal reserve for 12 years ending up as the head of enforcement and investigations for the Federal Reserve. Prior to that, he was in the Treasury General counsel's office as Senior counsel for Law Enforcement for two years, and then as a lawyer for DOJ in anti-trust and then organized crimes.

Small was in London at the time of the attacks. The next day, he had reached out to his contacts in law enforcement and offered assistance in searching the names. He said that no one was worried about process – that the bank would search for the names, and then worried about getting legal process to cover the search. He stated that Citi group was not alone in this attitude.

A difficulty soon arose in that there were a number of lists of names that the government wished to search. Each individual law enforcement and regulatory entity put out a list. This was very confusing to the financial community, as there was a great deal of overlap in the names – some lists would have some names but not others, and names would be spelled differently depending on the list. He said there were lists from Customs, lists from the Secret Service, lists from the FBI, lists for foreign governments, and even lists from specific investigative agency field offices. Additionally, there was no guidance on what to do with each of these lists. No protocols had been developed, and there was no instruction as to what to do with the lists. This made it difficult to manage internally, and at one time he had 1,500 names to search for to determine whether they had accounts somewhere in Citigroup. Small stated that he had about 20 employees tasked to running the names of people, managing the work flow, building a database and making spreadsheets.

The biggest problem with the early lists was the fact that there were no identifiers, such as dates of birth, addresses or Social Security/TIN numbers. This made the task of identifying and potentially freezing money extremely difficult. For example, Small stated that there were 85 Mohammed Attas in New York City alone. Without some way

of narrowing down the list, it proved to be a very difficult task. He said the process improved over time, but it still “comes and goes”

Ultimately, in late September or early October, a meeting was held by the New York federal reserve, which suggested a unitary “control list,” and brought all federal law enforcement to the table. The FBI was tasked to compile the list, and Joe Ford from the FBI was in charge of it. It was issued by the functional federal regulators to the banks.

With regard to other public/private partnerships, Small mentioned the NY Clearinghouse, which hosted a meeting of the CEOs of 10 banks, who desired to do something proactive in the area of terrorist financing. As a result, a number of working groups were formed. One was tasked with developing a potential hijacker financial profile (an effort that ultimately was unsuccessful), another task force attempted to resolve some of the legal issues involved, and a third task force attempted to streamline and expedite the data flow between industry and government. The NY Clearinghouse effort lasted almost two years.

Ultimately, the “control list” process evolved into a process institutionalized by Section 314(a) of the USA PATRIOT Act. Initially, this section came as a result of an industry request to be able to get better information sharing from the government, consistent with their belief that they needed more information to properly examine their own transaction to identify and block transactions. Prior to section 314(a), the government could not share law enforcement information with banks. Small had suggested this to David Aufhauser, the Treasury General Counsel, as sort of a “reverse SAR.” Small stated that he would have been happy to get a few bank employees cleared to have access to classified information, similar to defense industry contractors, who could then receive sensitive law enforcement information and conduct searches of the databases. Aufhauser rejected the suggestion, and nothing came of it.

As 314(a) is currently constituted through rules put out by FinCEN, a request will go out from FinCEN, and banks have 14 days to get back and say whether there was a hit or not. Law enforcement will then be able to subpoena those records. Initially, there were a number of problems in the 314 process, centering around the lack of vetting and the volume of requests. With regard to the volume of requests, Small stated that he was getting a steady, non-stop stream of e-mail requests from FinCEN. He stated that he had around 200 names total in the initial time period that the 314 requests were in operation. He had contemplated that the system would be used only for those significant, high priority cases. Instead, it was clear to him that there had been no vetting of the lists regarding priorities. He was getting requests from analysts, and requests in which there was no identifying information. Moreover, there were misspellings in the names (for example, the word “charity”), leaving an impression that there was no review of the requests before the banks saw them. In response to an inquiry, FinCEN said it had no ability to vet the lists for priorities.

As a result of complaints from numerous banks, FinCEN met with the American bankers association to rework the system. There was a moratorium on requests until the new procedures had been worked out. The modified process results in a request being

sent out every two weeks, with the names vetted for identifying detail. The banks have two weeks to respond, absent an emergency that would require a shorter turn-around time. Small says the list is better managed now. He still has problems with the prioritization, and doesn't know what internal government procedures have been put in place to ensure only the most serious cases use this process. He gets about 25 names every two weeks, and thinks that such a volume is too great. He has spoken to former IRS agents who say that they couldn't be that many major money laundering cases in the country. Moreover, he used the example of an individual who was caught trying to board an aircraft with piano wire. That request received a 48 turnaround time, purportedly because of its exigency. Citibank had a specific match on the name, and when Small reached out to his law enforcement contacts to report this, was told just to send it through the normal channels. This made Small wonder why there was a 48 hour turnaround time.

Another issue is FinCEN's directive that banks can not keep the lists that are sent. Small thinks that the fact that law enforcement is querying a name would be valuable information to have in doing customer due diligence.

Small's view is that the 319 process is not real information sharing; it is simply another administrative burden on banks. Small stated that for this process to work, there needs to be better filtering of the requests – better specificity and a large number of identifiers, as well as a policy-level decision regarding the frequency of use of these requests.

In Small's view, the best process is to develop good informal contacts with law enforcement. Small has good, informal contacts with the new York JTTF as well as ICE and the Secret Service and will receive calls from them about twice a month requesting information on an expedited basis. He thinks that most of the money-center banks have good, informal relationships with law enforcement. Another good idea was to have each JTTF designate a senior agent as the terrorist finance coordinator, who would be the central point of contact for the banks.

Small says that no good financial profile exists for terrorism, and none can be developed. The existing typologies issued by FinCEN and fatf are similar in that the suspicious activity reporting was done as a result of other crimes committed, such as credit card fraud. Only when this suspicious activity is married with the law enforcement information does a clearer picture emerge as to the terrorist activity. Small states that the data systems and filters banks have will be able to catch money launderers, but will not be able to detect terrorist financing. The 9/11 hijackers are a case in point – none of their transactions were suspicious; they were students, and fit the profile of students – similar addresses, no employment, large deposits followed by significant ATM activity, etc. there is nothing that would distinguish the 19 hijackers from typical students. This was ultimately the conclusion of the NY Clearinghouse effort on this activity. This is also reflected in the kinds of SARs filed on terrorism. Almost always, it is a matter of a name matching with an OFAC or control list, rather than some independent analysis of the financial transactions.

When asked, Small stated that not everyone in the government shares that conclusion. He pointed to public statements by Aufhauser, in which he talks about greater due diligence and better efforts on the part of banks.

With regard to profiles for terrorist fundraising, as opposed to funding for operations, Small stated that it was very difficult to do due diligence on charities absent the lists they receive from OFAC. They will investigate whether the beneficiaries exist, and do name searches on the officers and directors to determine whether they are on OFAC lists or there is any negative public information about them. This is complicated in many parts of the world by the fact that there are no databases for names in many parts of the world, such as East Asia, in order to check on the directors. Moreover, after an account is started, they will conduct transaction monitoring to determine whether there are inconsistent transactions with the stated purpose and beneficiaries of the charity.

With regard to OFAC, Small gives them generally high marks, and stated that they have made significant changes for the better over time. If the banks gets a "soft hit" – meaning there is a name match but it is unclear whether it is the same person as the OFAC blocking – they are able to get resolution of the issue fairly quickly. Additionally, OFAC has worked pretty hard to ensure that they have sufficient identifiers.

With regard to the SAR process, it is far more important for banks to have a process in place to screen for and then resolve suspicious activity than it is to actually file SARs. To Small, what happens to the specific SAR is less important than the fact that banks see suspicious activity and then resolve it, either by clearing up the suspicious or closing the accounts. His only complaint with the SAR process is that there is not a lot of feedback regarding what happens to the SAR. FinCEN publishes a quarterly review of SAR activity, and reports on trends and case studies, but what is needed is a way for law enforcement to tell what has happened to specific suspicious activity reports. Citibank files something like 10,000 SARs per year, and it is better for morale for the bank compliance officers to know that their work has some effect. Moreover, it is better to have feedback so the bank knows whether it should close that account as a result of the activity described in the SAR. When asked, Small stated that he thought the electronic filing that takes place in the PACS system seems to be working fine and he had no comment on it. The CTR filing requirement was useful, Small said, because of its deterrent effect.

With regarding the other patriot act provisions affecting banks, Small thought that the 326 rule regarding customer identification has not been thought through. He said that there were a number of internal contradictions within the rule that show that, although the revisions between the proposed rule and the final rule have made it considerably better, particularly the original requirement that the banks would have to verify the information, such as address, etc., within the documents used for identification. He considers this the most costly and burdensome part of the USA PATRIOT Act, mostly because all of the data systems will have to be modified to capture this information. To Small, customer identification is a subset and subsumed in some respects by the risk-based procedures used of AML programs. For example, the identification requirements necessary for an

entity like general motors will be considerably different than a limited partnership or mutual fund from the Cayman Islands. In the former the “identity” of the signatories is irrelevant, in the latter, it is critically important. This is not about customer identification – rather, it is about assessing the risk of money laundering.

Small believes that the Social Security Administration should have a program whereby a bank could give them a name and SSN and get instant feedback on whether the number is valid. Currently the government cannot do that, although they are investigating the possibility. Private vendors can do it, but there are costs associated with it.

With regard to non US persons, the problem is considerably more difficult. Citi uses an official identification such as a passport or national identity card, along with some other secondary form of identification showing local evidence, such as a utility bill. They are simply trying to verify identity, not authenticate documents, so unless there is an obvious alteration, there is no attempt to go behind the documents. Small says that they will use a Mexican consular identification as an official ID, and that much of the criticism behind them is based on the old procedures used to issue them, rather than the new security procedures in place.

Considerably more problematic are those foreign accounts that are opened without the account holder being present. Approximately 15 to 20 of their foreign account openings are not done face-to-face. Currently, most documents are transmitted by fax – including the identity documents and the account opening documents. Comparing faxed signatures is difficult, and it is easy for anyone to falsify a document that is to be faxed.

With regard to rule 312, the correspondent banking provisions, the rule has been delayed, and Small does not see it coming out in the foreseeable future. Of note in that rule is whether there will be a requirement to know your customer’s customer, or whether you can rely on your customer’s ID and AML programs as sufficient due diligence. Small’s view is that having to do an independent due diligence on each downstream customer will put a sever burden on smaller businesses, and thinks it will be sufficient to simply ensure that your first tier customer does appropriate due diligence.

With regard to the ability of banks to engage in real time transaction monitoring, small says that truly “real time” is extraordinarily difficult due to the volume involved, particularly if you are talking about monitoring the funds transfer issue. Real time credit card monitoring is possible, and Citi did some of that post-9/11. Small stated, however, that in emergency situations it was possible to get very fast turnaround – easily less than 24 hours. I could be done on nights and weekends as well. Citi’s process is somewhat more difficult because as they buy banks and inherit the data systems that go along with it, so Small must contact a number of individuals and have them run it. Smaller banks have an easier time conducting transaction monitoring. Small stressed that the informal relationships are the ones that bear the most fruit, and that those relationships have expanded after 9/11.

With regard to the 9/11 hijackers, two of the hijackers had credit cards with Citi, in Dubai and Germany. Small said that there was nothing unusual about that activity. The \$105,000 that was transferred to the SunTrust accounts moved through the UEA exchange account in Citibank in NY. Small stated that there was nothing unusual about that transaction that should have aroused suspicion. Citi looked at the due diligence conducted by UAE Exchange and concluded that, at the time of the transaction, it conducted a typical amount of due diligence. Small also said that it is getting out of the business of services money exchangers and other MSBs.

Others we could talk to include John Bryne from the American Bankers Association, Dan Soto from Bank of America, Mark Mathews from DB, David Laurence from Goldman, Cort Golumbic from Bear Stearns, David Whittman from Western Union, and Ezra Levine, a lawyer who represents the MSB industry.