

**UNITED STATES OF AMERICA
DEPARTMENT OF THE TREASURY
FINANCIAL CRIMES ENFORCEMENT NETWORK**

IN THE MATTER OF:

**ISRAEL DISCOUNT BANK OF NEW YORK
NEW YORK, NEW YORK**

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) **Number 2006 – 7**
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ASSESSMENT OF CIVIL MONEY PENALTY

I. INTRODUCTION

Under the authority of the Bank Secrecy Act and regulations issued pursuant to that Act,¹ the Financial Crimes Enforcement Network has determined that grounds exist to assess a civil money penalty against Israel Discount Bank of New York (“Israel Discount Bank” or “the Bank”). To resolve this matter, and only for that purpose, Israel Discount Bank has entered into a CONSENT TO THE ASSESSMENT OF CIVIL MONEY PENALTY (“CONSENT”), without admitting or denying the determinations by the Financial Crimes Enforcement Network, as described in Sections III and IV below, except as to jurisdiction in Section II below, which is admitted.

The CONSENT is incorporated into this ASSESSMENT OF CIVIL MONEY PENALTY (“ASSESSMENT”) by this reference.

II. JURISDICTION

Israel Discount Bank is an insured state chartered nonmember bank that is the U.S. subsidiary of Israel Discount Bank Ltd., a financial institution based in Israel. Israel Discount Bank has seven locations in New York, California, and Florida; an office in the Cayman Islands; representative offices in Latin American countries including Uruguay, Brazil, and Chile; and a wholly owned subsidiary in Uruguay, Discount Bank (Latin America) (“DBLA”). Israel Discount Bank offers a variety of banking services, including private banking, time deposits, lending, and wire transfer services to a client base comprised largely of nationals of Latin American countries. As of June 30, 2006, Israel Discount Bank had assets of approximately \$9.7 billion. The Federal Deposit Insurance Corporation is Israel Discount Bank’s Federal functional regulator and examines Israel Discount Bank for compliance with the Bank Secrecy Act, its implementing regulations and similar rules under Title 12 of the United States Code. The New York State Banking Department examines Israel Discount Bank for compliance with requirements under banking laws of the State of New York comparable to those of the Bank Secrecy Act and its implementing regulations.

¹ 31 U.S.C. § 5311 *et seq.* and 31 C.F.R. Part 103.

At all relevant times, Israel Discount Bank was a “financial institution” and a “bank” within the meaning of the Bank Secrecy Act and the regulations issued pursuant to that Act.²

III. DETERMINATIONS

A. Summary

Examinations of Israel Discount Bank by the Federal Deposit Insurance Corporation and the New York State Banking Department found deficiencies in Israel Discount Bank’s anti-money laundering program, revealing that Israel Discount Bank failed to implement an adequate system of internal controls to ensure compliance with the Bank Secrecy Act and manage the risks of money laundering. The examinations also revealed that Israel Discount Bank failed to conduct adequate independent testing to allow for the timely identification and correction of Bank Secrecy Act compliance failures, or adequately staff the compliance function with individuals responsible for coordinating and monitoring day-to-day compliance with the Bank Secrecy Act. These failures in internal controls, independent testing, and designated personnel led, in turn, to failures to timely file numerous suspicious activity reports involving, in the aggregate, hundreds of millions of dollars in suspicious transactions. The failures by Israel Discount Bank to comply with the Bank Secrecy Act and the regulations issued pursuant to that Act were significant.

B. Violations of the Requirement to Implement an Anti-Money Laundering Program

The Financial Crimes Enforcement Network has determined that Israel Discount Bank violated the requirement to establish and implement an adequate anti-money laundering program. Since April 24, 2002, the Bank Secrecy Act and its implementing regulations have required banks to establish and implement anti-money laundering programs.³ A bank is deemed to have satisfied the requirements of 31 U.S.C. § 5318(h)(1) if it implements and maintains an anti-money laundering program that complies with the regulations of its Federal functional regulator governing such programs. The Federal Deposit Insurance Corporation requires each bank under its supervision to establish and maintain an anti-money laundering program that, at a minimum: (a) provides for a system of internal controls to assure ongoing compliance; (b) provides for independent testing for compliance conducted by bank personnel or by an outside party; (c) designates an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and (d) provides training for appropriate personnel.⁴ Israel Discount Bank failed to implement adequate internal controls, provide for independent testing for compliance, or designate adequate individuals responsible for coordinating and monitoring day-to-day compliance. Furthermore, Israel Discount Bank’s internal controls failed to reasonably comply with the due diligence requirements with respect to correspondent accounts for non-U.S. persons established by Section 312 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (“USA PATRIOT Act”).⁵

² 31 U.S.C. § 5312(a)(2) and 31 C.F.R. § 103.11.

³ 31 U.S.C. § 5318(h)(1) and 31 C.F.R. § 103.120.

⁴ 12 C.F.R. § 326.8(c).

⁵ USA PATRIOT Act Section 312(a); 31 U.S.C. § 5318(i); 31 C.F.R. § 103.181.

1. Internal Policies, Procedures and Controls

Israel Discount Bank failed to implement an adequate system of internal controls to ensure compliance with the Bank Secrecy Act and manage the risks of potential money laundering. Israel Discount Bank lacked adequate written policies, procedures and controls reasonably designed to assess the risks of potential money laundering and ensure the detection and reporting of suspicious transactions, and failed to adequately implement aspects of its written policies, procedures and controls.

Israel Discount Bank's policies and procedures failed to ensure that the Bank gathered and reviewed sufficient information on customers, on a risk graded basis, to adequately assess risk and potential for money laundering. There were significant deficiencies in the Bank's documentation of specific customer information, including important information on the nature of customers' businesses, verification of legal existence, and anticipated account activity. Documentation of customer information was not subject to quality controls to ensure the accuracy of information, or a system for periodically updating customer information. The Bank also lacked the capability to link accounts evidencing common ownership to facilitate the detection of potential suspicious activity. Furthermore, the Bank's account opening procedures did not require review of all due diligence documentation for high-risk foreign accounts, such as accounts for non-bank financial institutions in Latin America, before the Bank opened such accounts. In addition, the Bank failed to implement a risk rating methodology that evaluated customers based on specific customer information and gave balanced consideration to all relevant factors, including country/jurisdictional risk, products and services provided, and nature of the customer. The Bank did not use its customer risk ratings to focus attention on accounts exhibiting high risk characteristics for money laundering. These deficiencies prevented the Bank from performing adequate analysis of the risks associated with particular customers and determining whether transactions lacked any apparent business or lawful purpose, or were within the particular customer's normal or expected range of conduct.

Israel Discount Bank lacked adequate systems and controls to monitor transactions for potential money laundering or other suspicious activity. Israel Discount Bank processed approximately 181,000 third-party wire transfers totaling \$35.4 billion in a one-year period from March 2004 to March 2005. A substantial amount of these funds transfers processed by Israel Discount Bank were for originators and beneficiaries that exhibited characteristics and patterns commonly associated with money laundering, including the nature of the business, high-risk geographic locations of the originator and/or beneficiary, and transaction activity that was inconsistent with the normal and expected transactions for similar customers. The Bank's automated transaction monitoring systems were inadequate to support the volume and types of funds transfer transactions conducted by the Bank. The Bank also failed to develop satisfactory procedures for reviewing even those alerts generated by the automated transaction monitoring system. There was no case management system for tracking system-generated alerts from initial recognition to final resolution, and no prescribed timeframes for addressing alerts, determining whether an investigation was warranted, or ensuring the timely filing of suspicious activity reports where appropriate. Furthermore, because of the deficiencies in the Bank's documentation of customer information, the Bank often lacked information necessary to assess the risk of potential money laundering and other illicit activity posed by certain customers upon detection of transaction anomalies.

2. Correspondent Accounts for Non-U.S. Persons

As amended by Section 312 of the USA PATRIOT Act, the Bank Secrecy Act requires that:

Each financial institution that establishes, maintains, administers, or manages a private banking account or a correspondent account in the United States for a non-United States person, including a foreign individual visiting the United States, or a representative of a non-United States person shall establish appropriate, specific, and, where necessary, enhanced, due diligence policies, procedures, and controls that are reasonably designed to detect and report instances of money laundering through those accounts.⁶

Guidance issued with the interim final rule implementing Section 312 stated that compliance with the due diligence requirements with respect to correspondent accounts for non-U.S. persons would be reasonable if "... it focuses compliance efforts on the correspondent accounts that pose a high risk of money laundering based on an overall assessment of the money laundering risks posed by the foreign correspondent institution. Treasury expects that a bank will accord priority to conducting due diligence on high-risk foreign banks for which it maintains correspondent deposit accounts or their equivalents, and will focus foremost on correspondent accounts used to provide services to third parties. Treasury also expects banks to give priority to conducting due diligence on high-risk correspondent accounts maintained for foreign financial institutions other than foreign banks, such as money transmitters."⁷

Israel Discount Bank failed to establish appropriate, specific due diligence policies, procedures and controls reasonably designed to detect and report instances of money laundering through its correspondent accounts for non-U.S. persons. Because of the deficiencies in its gathering and documentation of customer information and risk assessments of customers, the Bank failed to focus its compliance efforts on correspondent accounts that posed a high risk of money laundering. The Bank maintained direct correspondent account relationships with customers that were high-risk foreign non-bank financial institutions, including unlicensed money transmitters and licensed currency exchanges in Latin America that were not authorized to engage in international funds transfers under host country laws. In response to Cease and Desist Orders by the New York State Banking Department and the Federal Deposit Insurance Corporation dated December 15, 2005 ("Cease and Desist Orders"), the Bank filed a substantial number of suspicious activity reports on cross-border funds transfers through the accounts of these foreign non-bank financial institutions. Adequate due diligence policies, procedures and controls would have enabled Israel Discount Bank to detect and report suspicious transactions through these accounts in a timely manner.

In addition, Israel Discount Bank failed to implement adequate due diligence policies, procedures and controls with respect to the correspondent account of its subsidiary, DBLA.

⁶ 31 U.S.C. § 5318(i)(1).

⁷ Anti-Money Laundering Programs; Special Due Diligence Programs for Certain Foreign Accounts, 67 FR 48348, 48350 (July 23, 2002).

Israel Discount Bank failed to implement such policies, procedures and controls although the correspondent account of DBLA posed a high risk of money laundering. Customers of DBLA conducted a large volume of dollar clearing transactions at Israel Discount Bank through this correspondent account, including a significant volume of transactions that warranted elevated monitoring in view of the risk of potential money laundering. A number of these transactions involved customers of DBLA that also had direct account relationships with Israel Discount Bank, including foreign non-bank financial institutions and private banking accounts held under code names or pseudonyms. Israel Discount Bank relied solely on DBLA for due diligence purposes and did not apply independent due diligence, as appropriate and practical, towards these transactions and transactors. Implementing adequate policies, procedures and controls with respect to the correspondent account of its wholly owned subsidiary would have enabled Israel Discount Bank to determine whether transactions related to that account conducted in the United States were commensurate with the normal or expected range of conduct of customers of the subsidiary, or lacked any apparent business or lawful purpose.

3. Independent Testing

Israel Discount Bank's program for independent testing was inadequate to assure compliance with the requirements of the Bank Secrecy Act. The internal audit function did not adequately evaluate and test Israel Discount Bank's suspicious activity monitoring system and related reporting procedures in either 2004 or 2005. The internal audit function also did not track adverse Bank Secrecy Act compliance findings by supervisory authorities to better enable management to respond in a timely manner. In addition, while Israel Discount Bank's internal auditors conducted periodic reviews of DBLA, the scope was too limited. Specifically, the reviews did not assess the overall adequacy of the anti-money laundering regime at DBLA, including practical and legal methods of acquiring due diligence information on persons and entities that conducted transactions at, by or through Israel Discount Bank. This information would have better enabled Israel Discount Bank to manage the risk of potential money laundering and comply with the Bank Secrecy Act.

4. Designation of Compliance Officer

Israel Discount Bank failed to adequately staff the compliance function at the Bank with individuals responsible for coordinating and monitoring day-to-day compliance with the Bank Secrecy Act. The BSA/AML Compliance Unit was understaffed, and its personnel lacked the requisite training to adequately perform their duties. The Bank's failure to provide adequate designated personnel and training limited its ability to initiate and complete investigations and file suspicious activity reports in a timely manner.

C. Violations of the Requirement to Report Suspicious Transactions

The Financial Crimes Enforcement Network has determined that Israel Discount Bank violated the suspicious transaction reporting requirements of the Bank Secrecy Act and regulations issued pursuant to that Act.⁸ These reporting requirements impose an obligation on banks to report transactions that involve or aggregate to at least \$5,000, are conducted by, at, or

⁸ 31 U.S.C. § 5318(g) and 31 C.F.R. § 103.18.

through the bank and that the bank “knows, suspects or has reason to suspect” are suspicious.⁹ A transaction is “suspicious” if the transaction: (1) involves funds derived from illegal activities, or is conducted to disguise funds derived from illegal activities; (2) is designed to evade reporting or record keeping requirements under the Bank Secrecy Act; or (3) has no business or apparent lawful purpose or is not the sort in which the customer would normally be expected to engage, and the bank knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction.¹⁰

Banks must report suspicious transactions by filing suspicious activity reports.¹¹ In general, a bank must file a suspicious activity report no later than thirty calendar days after detecting facts that may constitute a basis for filing a suspicious activity report. If no suspect was identified on the date of detection, a bank may delay the filing for an additional thirty calendar days to identify a suspect. However, in no event may the bank file a suspicious activity report more than sixty calendar days after the date of detection.¹²

Israel Discount Bank violated the suspicious activity reporting requirements of 31 U.S.C. § 5318(g) and 31 C.F.R. § 103.18 by failing to file a substantial number of suspicious activity reports in a timely manner. Through the first quarter of 2006, the Bank delinquently filed approximately one hundred suspicious activity reports, which reported transactions totaling \$1.4 billion. These suspicious activity reports involved prolonged transaction activity dating back as much as several years. An adequate anti-money laundering program would have allowed the Bank to file suspicious activity reports in a timely manner.

Israel Discount Bank also failed to monitor transactions by entities that it had already identified as suspects in suspicious activity reports. In 2003 and 2004, the Bank filed a number of suspicious activity reports on funds transfers involving “shell companies” – business entities lacking a physical presence – organized in the United States as limited liability companies. The shell companies served as originators or beneficiaries, and financial institutions in Russia and other former Republics of the Soviet Union served as originator’s or beneficiary’s institutions.¹³ After filing these suspicious activity reports, the Bank continued to process transactions involving the same shell companies, without continued review and the filing of additional or corrected suspicious activity reports. In some instances, the Bank continued to allow wire activity through accounts after the state government had dissolved the account holder, even after the Bank had knowledge of the dissolution.

In addition, Israel Discount Bank filed suspicious activity reports that were incomplete or inaccurate. The Bank filed suspicious activity reports with incorrect or missing identification numbers for suspects or for the Bank itself. Numerous suspicious activity reports failed to identify suspects, provide adequate narrative descriptions, or provide information such as activity dates and dollar amounts, in contradiction to the instructions on the form.

⁹ 31 C.F.R. §103.18(a)(2).

¹⁰ 31 C.F.R. § 103.18(a)(2)(i)-(iii).

¹¹ 31 C.F.R. § 103.18(b)(2).

¹² 31 C.F.R. § 103.18(b)(3).

¹³ In October 2000, the Government Accounting Office published a report detailing the risk that criminals in Russia could use “shell companies” organized in the United States as a means of concealing identity.

IV. CIVIL MONEY PENALTY

Under the authority of the Bank Secrecy Act and the regulations issued pursuant to that Act,¹⁴ the Financial Crimes Enforcement Network has determined that a civil money penalty is due for the violations the Bank Secrecy Act and the regulations issued pursuant to that Act and described in this ASSESSMENT.

Based on the seriousness of the violations at issue in this matter, and the financial resources available to Israel Discount Bank, the Financial Crimes Enforcement Network has determined that the appropriate penalty in this matter is \$12,000,000.

V. CONSENT TO ASSESSMENT

To resolve this matter, and only for that purpose, Israel Discount Bank, without admitting or denying either the facts or determinations described in Sections III and IV above, except as to jurisdiction in Section II, which is admitted, consents to the assessment of a civil money penalty against it in the sum of \$12,000,000. The assessment shall be concurrent with the \$12,000,000 penalty assessed against Israel Discount Bank by the Federal Deposit Insurance Corporation and the New York State Banking Department, and shall be satisfied by one payment of \$6,000,000 to the Department of the Treasury and one payment of \$6,000,000 to the New York State Banking Department.

Israel Discount Bank recognizes and states that it enters into the CONSENT freely and voluntarily and that no offers, promises, or inducements of any nature whatsoever have been made by the Financial Crimes Enforcement Network or any employee, agent, or representative of the Financial Crimes Enforcement Network to induce Israel Discount Bank to enter into the CONSENT, except for those specified in the CONSENT.

Israel Discount Bank understands and agrees that the CONSENT embodies the entire agreement between Israel Discount Bank and the Financial Crimes Enforcement Network relating to this enforcement matter only, as described in Section III above. Israel Discount Bank further understands and agrees that there are no express or implied promises, representations, or agreements between Israel Discount Bank and the Financial Crimes Enforcement Network other than those expressly set forth or referred to in this document and that nothing in the CONSENT or this ASSESSMENT is binding on any other agency of government, whether federal, state, or local.

VI. RELEASE

Israel Discount Bank understands that its execution of the CONSENT, and compliance with the terms of this ASSESSMENT and the CONSENT, constitute a complete settlement with the Financial Crimes Enforcement Network of civil liability for the violations of the Bank Secrecy Act and regulations issued pursuant to that Act as described in the CONSENT and this ASSESSMENT.

¹⁴ 31 U.S.C. § 5321 and 31 C.F.R. § 103.57.

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