

Fiscal Year  
2019

# ANTI-MONEY LAUNDERING PROGRAM TESTING AND AUDIT KCD FINANCIAL, INC.

*Each FINRA member shall develop and implement a written anti-money laundering program reasonably designed to achieve and monitor the member's compliance with the requirements of the Bank Secrecy Act (31 U.S.C. 5311, et seq.), and the implementing regulations promulgated thereunder by the Department of the Treasury.*

## **INTRODUCTION**

As a FINRA member, per FINRA Rule 3310, KCD Financial, Inc. (hereinafter also referred to as “The Firm” or “Firm”) is required to develop and implement a written anti-money laundering program reasonably designed to achieve and monitor its compliance with the requirements of the Bank Secrecy Act (31 U.S.C. 5311, et seq.), and the implementing regulations promulgated thereunder by the Department of the Treasury. The firm’s anti-money laundering program must be approved, in writing, by a member of senior management and shall, at a minimum:

- Establish and implement policies and procedures that can be reasonably expected to detect and cause the reporting of transactions required by Section 352 of the Patriot Act and under Section 5318(h) of title 31, United States Code and the implementing regulations thereunder;
- Establish and implement policies, procedures, and internal controls reasonably designed to achieve compliance with the Bank Secrecy Act and the implementing regulations thereunder;
- Provide for annual (on a calendar-year basis) independent testing for compliance to be conducted by member personnel or by a qualified outside party, unless the member does not execute transactions for customers or otherwise hold customer accounts or act as an introducing broker with respect to customer accounts, in which case such "independent testing" is required every two years (on a calendar-year basis);
- Designate and identify to FINRA an associated person or persons of the Firm responsible for implementing and monitoring the daily operations and internal controls of the program and provide prompt notification to FINRA regarding any change in such designation(s); and;
- Provide ongoing training for appropriate personnel.

## **OVERVIEW**

This report is a result of a test of KCD Financial, Inc. Anti-Money Laundering Program. The report covers fiscal year 2019 and is a product of interviews/interactions with key personnel and review of available documentation. Mr. Leslie has a working knowledge of applicable requirements under the Bank Secrecy Act, FINRA Rule 3310 and Section 352 of the Patriot Act as relates to anti-money laundering. Mr. Leslie has years of experience in the compliance field, and has been through AML training courses. He has developed AML Programs for broker-dealer firms as well as conducted Broker/Dealer AML Program independent tests and audits with other FINRA member broker/dealer firms. While Mr. Leslie is not affiliated with KCD Financial, INC., he has no involvement in any of the firm’s revenue generation, client/customer acquisition or associated person hiring decisions is considered “independent” for the sake of addressing this need; and given the current state of finances the firm is in.

## **TEST PROCESS**

The test process was approached from a risk perspective that included discussions with the firm’s Principals, key officers, and review of relevant documents. Areas covered were as follows:

- AML Program and Implementation
- Risks: Client Risk, Business Risk and Geographic Risk
- Suspicious Activity Monitoring
- Reporting Requirements and Implementation

Documents that were reviewed include:

- 2018 AML Program and Training / Test Records
- Customer Identification Program (CIP) Documentation
- NAF 12-17
- NAF 3-28-16
- Clearing Agreement
- Account Verification
- aml audit 2017
- aml audit-2018
- Transactions xls 2019, and MF & VA placements
- Branch Information
- Firm's General Information
- KCD Written Supervisory Procedures updated 10/02/19
- KCD WSP effective 10-02-19
- Part III AML Program 2018

- Part III AML Program 2017
- Client Account Files as well as New Account Forms

**RISK PERSPECTIVE**

Observations regarding the named risk areas were as follows:

- Client Risk – The firm recognizes that conducting comprehensive due diligence on investors is critical to accomplishing a respectable and effective AML Program.
- Business Risk – Business scope has remained the same—no Continuing Membership Application (1017 filing) occurred in 2016-17-18 and 19.
- Geographic Risk – Client base is domestic (*Incorporated within United States Jurisdiction*) and so risk is relatively minimized.

**RESULT**

The firm’s account opening process involves data collection efforts through the use of forms and personal assessments by associated persons. The interaction between client and associated person also serves as an effective means of assessing the risk involved in every account and the impact that it may have on the firm’s AML Program.

Following is a tabular presentation of the test result. Each section on this report is cross-referenced against the corresponding section on the Firm’s AML Program and individually presented with the findings and recommendations:

Firm Policy	
<p><b>Findings:</b></p> <p>The firm has a working AML program. The firm mindfully acknowledges business, client and geographic risks associated with its business scope and has demonstrated willingness to keep its AML Program current and updated. The firm’s Designated Principal acknowledges the relevance of disseminating the AML Program and any subsequent updates to its associated persons.</p> <p><b>Result:</b></p> <p>Tested for adequacy of procedures covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The firm is advised to carefully review the result of this testing and implement updates to the AML Program where applicable.</p> <p>This includes maintaining appropriate records concerning Form I-9 with regard to new employees. Employers must complete Form I-9 for all newly hired employees to verify their identity and authorization to work in the U.S. To learn more about Form I-9 visit <a href="#">I-9 Central</a>.</p>
AML Compliance Person Designation and Duties	
<p><b>Findings:</b></p> <p>Mr. David S. Wilson has been designated the Firm’s AML Compliance Officer. The AML Primary is Robert Rivera. This role is accordingly reflected in the FINRA Contact System.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>As the AML Compliance Officer, David Wilson is encouraged to continue monitoring FINRA’s guidelines pertaining to AML as well as its AML E-Learning Courses. Mr. Wilson designation was duly reflected in the firm’s AML Program and the FINRA Contact System; so in that regard, no further recommendation is necessary.</p>
Giving AML Information to Federal Law Enforcement Agencies and Other Financial Institutions	
<p><b>Findings:</b></p> <p>The firm receives 314(a) notice emails. Procedures are in place regarding what needs to be done when voluntary sharing of information with other financial</p>	<p><b>Recommendation:</b></p> <p>The firm is encouraged to continue participation in FinCEN’s 314(a) Secure Information Sharing System and to document</p>

<p>institutions takes place. FinCEN reviews have been documented.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p>such participation.</p>
<p><b>Checking the Office of the Foreign Assets Control (“OFAC”) List</b></p>	
<p><b>Findings:</b></p> <p>The firm conducts OFAC List checks using the OFAC search tool. The review process involves checking of the firm name, its key officers/representatives and keeping the search result in each client/customer file.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The review process in place is adequate. The firm is reminded of the filing requirement pertaining to blocked assets and/or transaction; and that it must be done within 10 days. The OFAC hotline is (800) 540-6322 and must be called immediately upon discovery.</p>
<p><b>Customer Identification Program</b></p>	
<p><b>Findings:</b></p> <p>Procedures are in place regarding customer identification or verification via documentary means. Such procedures appear to be properly implemented. The firm’s CIP complements with its due diligence process.</p> <p><b>Result:</b></p> <p>Reviewed for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The firm’s Customer Identification Program is deemed to have been appropriately addressed. The only recommendation at this time is to ensure that any updates that affect the CIP process be monitored accordingly—be that from the BSA, SEC, FINRA, NIAC or any other applicable regulatory entity. The use of a checklist may be useful to the Firm.</p>
<p><b>General Customer Due Diligence</b></p>	
<p><b>Findings:</b></p> <p>The Firm’s procedures are well in place and properly executed: Prior to starting a new customer relationship, a registered representative must complete due diligence sufficient to “know the customer.” Reviewed documentation revealed implementation of the due diligence process.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>Continue to monitor new accounts.</p>
<p><b>Correspondent Accounts for Foreign Shell Banks</b></p>	
<p><b>Findings:</b></p> <p>The firm’s AML Program is clear in stating that, “the Firm does not include in its operations any correspondent accounts for foreign shell banks.” No infraction against this mandate was found as of the time of the audit. The firm has established procedures to address this concern if it must arise.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>Maintain current procedure and process.</p>

Due Diligence and Enhanced Due Diligence Requirements for Correspondent Accounts of Foreign Financial Institutions	
<p><b>Findings:</b></p> <p>While this does not apply to the firm, the firm's AML Program has established procedures to address this concern if it must arise. There was no known correspondent account of foreign financial institutions during the audit.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>None at this time.</p>
Due Diligence and Enhanced Due Diligence Requirements for Private Banking Accounts/Senior Foreign Political Figures	
<p><b>Findings:</b></p> <p>The Firm does not anticipate opening, maintaining, or administering private banking accounts or offer securities for senior foreign political figures. Current procedures include this area of concern for documentary purposes and to acknowledge awareness of the steps to take if a situation must arise.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>None at this time.</p>
Compliance with FinCEN's Issuance of Special Measures against Foreign Jurisdictions, Financial Institutions or International Transactions of Primary Money Laundering Concern	
<p><b>Findings:</b></p> <p>The firm's procedures pertaining to "special measures" if FinCEN determines that reasonable grounds exist for concluding that a "primary laundering concern" exists are in place. Moreover, the firm participates in FinCEN checks.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The AML Compliance Officer, Mr. Wilson, is advised to continue monitoring any new information under Section 311 of the Patriot Act and by checking the Special Measures list and FinCEN guidance on Section 311 entities.</p> <p><a href="https://www.fincen.gov/statutes_regs/patriot/section311.html">https://www.fincen.gov/statutes_regs/patriot/section311.html</a></p>
Monitoring Accounts for Suspicious Activity	

<p><b>Findings:</b></p> <p>The firm's procedures for "<i>Monitoring Accounts for Suspicious Activity</i>," appears to be adequate.</p> <p>The firm evaluates its potential customers from the onset even before any formal relationship is established between the customer and the Firm. If there is any element of doubt with regard to the potential customer/client's identity and ability to provide documentation pertaining to legitimate fund source, the relationship is not pursued.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The firm is reminded that in the event that a suspicious activity is discovered requiring form SAR-SF to be filed, this filing should be done within 30 days of becoming aware of the suspicious transaction.</p> <p>Associated persons of the firm are advised to review the "The SAR Activity Review"-Trends, Tips &amp; Issues."</p> <p>The firm's associated persons are further reminded of the emergency notification to the government by telephone:</p> <ul style="list-style-type: none"> <li>• OFAC Hotline: 1 (800) 540-6322</li> <li>• Financial Institutions Hotline: 1 (866) 556-3974</li> <li>• Mr. Wilson should also be involved in decisions.</li> </ul>
<p><b>Suspicious Transactions and BSA Reporting</b></p>	
<p><b>Findings:</b></p> <p>The procedure for Suspicious Transactions and BSA Reporting is adequate. The firm has not had an occasion when it deemed that it knew, suspected, or had reason to suspect that certain transactions, either securities / insurance products, have been involved in suspicious activities.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>In addition to the review process that occurs during account opening, the firm must ensure that monitoring for suspicious activity continues as a day-to-day responsibility. Associated Persons are reminded to be cognizant of the types of activities that must be reported that may include (though not by any means exhaustive):</p> <ul style="list-style-type: none"> <li>▪ Wire transfers or cash transactions that have no apparent investment purpose;</li> <li>▪ Significant deposit supposedly intended for investment / insurance products followed by an abrupt request for withdrawal;</li> <li>▪ Multiple accounts for the same individual with no clear reason as to why the account should be separated;</li> <li>▪ Customer activity that are focused on investment vehicles often associated with fraudulent schemes such as "Reg S" stocks, bearer bonds, penny stocks, etc.;</li> <li>▪ A bearer bond / annuity / life insurance deposit that is followed by an abrupt request for liquidation;</li> <li>▪ Supposed investment / insurance activity without any regard for CDSC, fees, risk, return or other performance criteria;</li> <li>▪ Dramatic change in the account's activity level especially when such an account has been dormant.</li> </ul>
<p><b>AML Record Keeping</b></p>	
<p><b>Findings:</b></p> <p>In terms of AML recordkeeping and confidentiality, the firm has adequate procedures in place to address these concerns. Associated Persons are aware of this responsibility.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>Maintain the confidentiality procedures and continue representatives' training annually.</p>

Training	
<p><b>Findings:</b></p> <p>Training is deemed as a dynamic and interactive process (with personal reminders from the AML Compliance Officer during interactions throughout the year) and procedures are in place.</p> <p><b>Result:</b></p> <p>Tested for adequacy of procedures during the review period. More structured implementation and documentation of training initiatives would be ideal.</p>	<p><b>Recommendation:</b></p> <p>The Firm is encouraged to participate in FINRA's Online Programs/E-learning courses as several AML topics are on the list of available courses.</p> <p>While not endorsing the FINRA E-learning courses, such a program offers a cost-effective solution to a FINRA member firm's AML training needs.</p> <p>Each Associated Person may have specific training needs. As such the firm is advised to be proactive in identifying relevant training needs for each Associated Person and the Firm as a whole. FINRA's website has ample reference materials and/or links that can be conveniently availed by the firm. More structured implementation and documentation of training initiatives would be ideal.</p> <p>Insurance licensed associates should maintain CE's as required per their resident State specific requirements.</p>
Program to Independently Test AML Program	
<p><b>Findings:</b></p> <p>Due to the firm's limited financial wherewithal, it requested its FINOP to conduct the testing and audit of its AML program. As the FINOP does not participate in any account opening process or interact with clients, it was deemed that the FINOP is the most "independent" person within KCD FINANCIAL, INC..</p> <p><b>Result:</b></p> <p>Tested for adequacy of procedures covering the review period.</p>	<p><b>Recommendation:</b></p> <p>The firm has hired an external consultant to conduct the AML Program Testing and Audit under both securities and/or insurance product transactions.</p>
Monitoring Employee Conduct and Accounts	
<p><b>Findings:</b></p> <p>Mr. Wilson, Chief Compliance Officer, is aware of his obligations to monitor employee conduct and accounts. He coordinates with AML Primary Robert Rivera who monitors associated persons' brokerage accounts activity (as applicable) as well as their involvement in outside business activities. Responsibilities are designated in the firm's WSP effective 10/02/2019.</p> <p><b>Result:</b></p> <p>Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b></p> <p>KCD has designated a AML primary, Mr. Robert Rivera, who is listed on the Designation Of Supervisors chart and Schedule A of Form BD which is filed with regulators. Mr. Rivera documents day-to-day customer account activity conducted by office managers, sales managers, regional or district managers or other supervisors subject to review and supervision by someone senior to or independent of the supervised person. The Firm has an obligation, and should continue, to effectively administer its responsibility to mitigate potential conflicts of interest and put the customer's interest before its own.</p>
Confidential Reporting of AML Non-Compliance	
<p><b>Findings:</b></p> <p>There has not been any report by an Associated</p>	<p><b>Recommendation:</b></p> <p>The firm should ideally continue reminding its Associated</p>

<p>Person regarding another Associated Person's non-AML compliance. The Firm's AML Program has been updated to reflect clear and specific procedures regarding confidential reporting in the event that an Associated Person discovers another Associated Person's AML non-compliance.</p> <p><b>Result:</b> Tested for adequacy covering the review period.</p>	<p>Persons about their responsibility to confidentially report any known AML non-compliance by another Associated Person.</p>
<p><b>Senior Manager Approval (Section 3.17 of the AML Program/WSP)</b></p>	
<p><b>Findings:</b> The firm's AML program has been properly approved by a senior manager of the firm.</p> <p><b>Result:</b> Tested for adequacy covering the review period.</p>	<p><b>Recommendation:</b> The AML Compliance Officer and AML Primary are advised to thoroughly review the findings and recommendations identified in this AML Independent Test Result then integrate the relevant portions as part of the AML Program updating process. Subsequently, the updated AML program should be approved by a senior manager of the firm. Upon approval, the updated AML Program should be properly disseminated to all Associated Persons of the firm.</p>

*Notes to Findings and Recommendations:*

*The findings and recommendations in this testing process are not to be interpreted as outright violations or failure to implement applicable AML related rules and regulations for a FINRA member organization.*

**FOCUS AREAS**

It is highly recommended that the Principals consider action points to address these focus areas:

- **Firm Risk Assessment**
  - The firm is advised to be proactive in re-evaluating its risk profile. While risks may already be "comfortably" known, changes in risks may quietly occur without the firm noticing them.
- **AML Training**
  - The firm may want to invest time and effort to evaluate the individual training needs of its Associated Persons. FINRA and insurance E-learning courses are good and cost-effective resource materials.
- **Suspicious Activity Reporting and Other Reporting Requirements**
  - The Firm should try to ascertain that each Associated Person is familiar with the AML reporting requirements: What forms to use; how forms should be filled out; when forms/reports must be filed; what other concerns they need to be aware of when reporting is imminent.

**CONCLUSION**

The firm has a working AML Program and it continues to try to implement it appropriately. Revised procedures were updated 10/19. As indicated above, the firm is advised to remain mindful of any changes to its risk profile. As the firm has limited business scope, risk may also correspondingly be limited. The firm has to constantly be cognizant of the fact that the threat of becoming an investment vehicle for money laundering purposes will always be present. Thus, firm vigilance will have to remain a continuing concern.

The new account form may need to be changed due to regulation alterations in the future.

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Date 12/23/2019