White Paper

How Money Launderers Use Life Insurance Products

Why It’s a Real Risk to the Industry

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Redeemable cash products make the life insurance industry an easy target for money launderers.

It's easy to underestimate the magnitude of the money laundering problem worldwide and the risk it poses to the life insurance industry. While life insurance is regulated like the rest of the financial services industry, the enforcement of those regulations is inconsistent. As a result, life insurance companies often don't employ sophisticated anti-money laundering (AML) solutions to help uncover potential money laundering activity. That makes them increasingly vulnerable to money laundering schemes by savvy criminals.

How Criminals Attack

The life insurance sector is attractive to launderers seeking to place money into a financial product that will provide them with a reliable, clean return on their investment. In the case of life insurance and annuity contracts, money goes into the policy or contract mainly through premium payments and normally comes out through maturity, the policyholder's death or a predefined payment schedule.

However, some financial products have redeemable cash values that make them vulnerable to money laundering. For instance, "dirty money" could be used to buy a policy, which then could be surrendered for a cash payment. That payment would be "clean." Premium overpayments also can be used to launder money, with launderers significantly overpaying their premiums and then requesting refunds.

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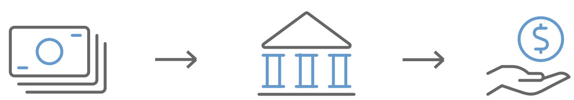

What Makes Life Insurance Susceptible

There are three main factors that make the insurance industry vulnerable to money laundering: inconsistent enforcement of government regulations, certain features of life insurance products and the use of intermediaries. Risks inherent in all three can be decreased with a comprehensive AML program.

1. Inconsistent Enforcement of Government Regulations

Criminals are always looking for new ways to launder the proceeds of crime through the financial system. Life and annuity products are susceptible to being used as part of the layering stage of money laundering. However, because there is inconsistent enforcement of government regulations, life insurers often become complacent about updating their AML solutions, leaving themselves open to criminal activity. With the proper detection processes and tools in place, life insurers would be better protected against schemes.

2. Life Insurance Policy Features

Life insurance policies with cash-surrender values are potential money laundering vehicles. Launderers can redeem the cash value or use it to invest additional tainted money, such as taking out loans against the cash value. Similarly, annuity contracts can offer an immediate or deferred income stream.

In addition, there may be procedures in place that make it easier for the money launderer, including:

- Allowing premium overpayments, which then must be reimbursed
- Letting excess premiums or policy cash-outs be paid to a third party
- Permitting premiums to be paid in cash, cashier's check or money order
- Allowing withdrawals at any time with limited fees

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3. Use of Intermediaries

Another susceptible target involves inconsistencies in the oversight of intermediaries. The insurance company generally gives brokers or independent agents a great deal of freedom regarding policies.

The intermediaries focus on selling the insurance products and often overlook money laundering signs, such as presigned forms, lack of explanation for wealth or unusual methods for paying premiums. A lack of AML controls with intermediaries can result in the independent financial advisor, agent or broker essentially becoming the launderer. The intermediary may knowingly go along with the scheme or simply be unwilling to question or confront a customer who is profitable to the company.

A new wrinkle comes from distribution channels with direct-to-consumer sales programs that require insurers leverage know your customer (KYC) data to ensure compliance.

Why It Matters

There are multiple reasons to take steps to fight money laundering schemes, including:

Reputational Risk

Fines for noncompliance with AML regulations are the first of several problems for companies. It gets worse when news stories expose the business as having allowed itself to be abused by launderers. How can customers trust a life insurance provider that, knowingly or not, did business with criminals?

Business Integrity

Preventing money laundering is simply the right thing to do. It sets apart the professional businesses seeking to provide high-quality products to real customers from the underhanded companies willing to look the other way for profits.

Regulatory Compliance

While global regulations vary, all financial services businesses in the U.S. that have products with a cash value, investment or annuity must implement an AML program, train employees and report suspicious activity.

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- Reputational Risk
- Business Integrity
- Regulatory Compliance

> "If insurers aren't diligent in establishing effective AML programs, they risk regulatory noncompliance, reputational harm and disappointed customers."

Take a Risk-Based Approach

Regulators require insurers have an AML program that is "risk-based," meaning the insurer should focus its detection and control efforts where the company is most vulnerable to money laundering. The first step is to identify products with high, medium and low risk for money laundering and then identify customers who may be high risk. In general, the risk of products is determined by whether the product has a cash payout or allows large overpayments of premiums that can be reimbursed. The risk of customers is determined by certain factors such as PEP status, country of residency, unusual number of policies per customer or policy owners per address and so on.

Intermediaries can also be a source of money laundering, whether knowing or unknowing, and contracts and agreements with third parties conducting sales activities on behalf of the carrier should be reviewed with that in mind.

Insurers must not only have the ability to pick up on structuring, but also on more complicated laundering. For example, the policyholder, or purchaser of an insurance contract, may not be the beneficiary. The potential for multiple parties to be involved in a single contract makes it difficult to perform customer due diligence and identify suspicious patterns. Insurance companies will need to avail themselves of the latest in technology advances to stay ahead of the game.

How Solutions Can Mitigate Risk

Money launderers are in the business of avoiding suspicion and obscuring the money trail. However, hidden in the insurer's data are telltale signs that certain parties, policies or payments might be suspect. Finding those signs in thousands or even millions of life and annuity policies usually requires detection technology.

A compliance department cannot investigate every person involved with every policy or every payment made to or by the insurer. It needs a way to focus its investigative resources on the policies with the highest risk of being abused for money laundering or terrorist financing.

Here are just a few examples of what needs to be monitored:

- Track discrepancies/changes to sources of funds or source of wealth
- Track if/when a customer transfers ownership or designates a beneficiary
- Track discrepancies around static data such as address and Social Security number
- Monitor expected activity versus actual activity
- Monitor loan, surrender, cancellation, nonforfeiture option and withdrawal request activity
- Monitor changes made to methods of payment and unusual/suspicious loan repayment activity
- Monitor pace of refund premiums, surrenders, redemptions and withdrawals
- Track use of policy loans

An AML solution can sort through all the data to detect and report suspicious activity, helping the insurer meet regulatory requirements and minimize exposure to reputational harm. An effective AML system offers:

- Tools combining data such as KYC, risk scoring, and customer and enhanced due diligence to form a comprehensive view of policies, contracts, customers, agents, advisors and related parties
- Monitoring of transactions and events involving policies, parties and products based on known insurance money laundering scenarios, such as lump-sum payments, early withdrawals, frequent address changes or high-risk payment methods
- Checks on policyholders, beneficiaries and other parties against a variety of money launderer, sanctions and PEP watch lists
- A risk rating for each policy and policyholder based on a risk profile using characteristics such as the customer's PEP status, country, product type and policy value
- Prioritized alerts based on a combination of risk factors to minimize false positives and enable full investigations by drilling down to the details of policies, parties and payments involved
- Reports that are automatically generated based on defined suspicious activity criteria and can be configured based on the specific reporting requirements imposed by local authorities or regulatory bodies

Stop Laundering Before It Starts

Life insurance is increasingly vulnerable to money laundering activities. If insurers aren't diligent in establishing effective AML programs, they risk regulatory noncompliance, reputational harm and disappointed customers. Having a reputation for integrity is important to maintaining loyal customers and attracting new ones.

Constantly monitoring such large and complex data sets is almost impossible to do manually. A comprehensive AML solution can provide monitoring, alerting and reporting capabilities that let compliance departments focus their investigations on real threats.

Connect With Us

For more information about
AML Risk Manager from Fiserv:

800-872-7882

getsolutions@fiserv.com

fiserv.com

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Fiserv, Inc.
255 Fiserv Drive
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