

**FEDERAL DEPOSIT INSURANCE CORPORATION
WASHINGTON, D.C.**

In the Matter of)	
)	
CALIFORNIA PACIFIC BANK)	DECISION AND ORDER
SAN FRANCISCO, CALIFORNIA)	TO CEASE AND DESIST
)	
)	
(Insured State Nonmember Bank))	FDIC-13-094b
)	
)	

I. INTRODUCTION

This matter is before the Board of Directors (“Board”) of the Federal Deposit Insurance Corporation (“FDIC”) following the issuance on September 8, 2015, of a Recommended Decision (“Recommended Decision” or “R.D.”) by Administrative Law Judge C. Richard Miserendino (“ALJ”). The ALJ recommended that California Pacific Bank, San Francisco, California (“Bank”) be subject to an order to cease and desist and corrective action plan pursuant to sections 8(b) and 8(s) of the Federal Deposit Insurance Act (“FDI Act”).¹

The Board has reviewed the record, including the parties’ pre- and post-hearing submissions, the Recommended Decision, and the Bank’s Exceptions to the Recommended Decision (“Bank’s Exceptions”) along with its supporting brief. The Board agrees with the ALJ’s findings that the Bank violated the Bank Secrecy Act (“BSA”) and the FDIC’s implementing regulations by failing to establish and maintain procedures reasonably designed to assure and monitor compliance with BSA recordkeeping and reporting requirements.² Therefore, the Board adopts in full and affirms the Recommended Decision.

¹ 12 U.S.C. § 1818(b)(1); 12 U.S.C. § 1818(s).

² See 31 U.S.C. § 5311 *et seq.* and 12 C.F.R. § 326.8(b).

II. STATEMENT OF THE CASE

The FDIC initiated this action on July 18, 2013, when it issued a Notice of Charges and of Hearing (“Notice”) alleging that the Bank, a federally insured State nonmember bank subject to the FDI Act³ and Part 353 of the FDIC Rules and Regulations⁴ (“FDIC Rules”), had violated the BSA and its implementing regulations. The federal law now referred to as the BSA was enacted in 1970 as part of the Bank Records and Foreign Transaction Act (“BRFTA”).⁵ As explained in its declaration of purpose,⁶ the BRFTA was a response to rising Congressional concern over the use of foreign banks to ‘launder’ the proceeds of illegal activity and to evade federal income taxes.⁷ The provisions of Title II of BRFTA now are commonly referred to as the BSA. Consistent with its purpose, the BSA imposed recordkeeping requirements on financial institutions.⁸ Among other things, section 8(s) of the FDI Act obligates the FDIC to issue regulations to banks requiring banks to maintain procedures to assure compliance with BSA and further requires the FDIC to examine a bank’s compliance with the BSA and describe any problems with a bank’s BSA compliance in a report of examination.⁹ The Notice was prompted by information obtained during the FDIC’s 2012 examination of the Bank’s BSA compliance program (“2012 Examination”).

The FDI Act and FDIC’s Risk Management Manual of Examination Policies requires FDIC to conduct an examination of the BSA compliance programs of financial institutions. To

³ 12 U.S.C. §§ 1811-46(a).

⁴ 12 C.F.R. § 353.

⁵ Pub. L. No. 91-508, 84 Stat. 1114 (1970)(codified as amended in various sections of 12 U.S.C, 15 U.S.C., and 31 U.S.C.).

⁶ 31 U.S.C § 5311 (2001).

⁷ See H.R. REP. NO. 975, 91st Cong., 2d Sess. 12-13, *reprinted in* 1970 U.S. Code CONG. & ADMIN. NEWS 4394, 4397-98.

⁸ *The Currency and Foreign Transactions Reporting Act* (“BSA”) 31 U.S.C. §5311 *et seq.*, 12 U.S.C. § 1829(b), and 1951-1959.

⁹ 12 U.S.C. § 1818(s).

determine BSA compliance, FDIC examines what are commonly referred to as the “four pillars” of a bank’s BSA compliance program. Specifically, pursuant to FDIC Rule 326.8, the BSA requires that banks develop and implement a board-approved BSA compliance program¹⁰ that, at a minimum: 1) provides for a system of internal controls to assure ongoing compliance; 2) provides for independent testing for compliance to be conducted by bank personnel or by an outside party; 3) designates an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and 4) provides training for appropriate personnel.¹¹

In part, the Notice charged that the Bank failed to provide for the continued administration of a BSA compliance program that was reasonably designed to assure and monitor compliance with recordkeeping and reporting requirements under the BSA.¹² The Notice also alleged that the Bank failed to file a Suspicious Activity Report (“SAR”) under circumstances where it was required by the BSA.¹³ In the Notice, FDIC sought imposition of an order to cease and desist from violations of laws and/or regulations as pled in the Notice and also sought an order requiring the Bank to take affirmative action to correct the conditions resulting from such violations.

The Bank filed its Answer to the Notice on August 12, 2013. In the months leading up to the hearing, the parties engaged in discovery and filed a series of pre-hearing motions *in limine*. The ALJ conducted a hearing on the merits in San Francisco from March 10 through March 13, 2014. At the hearing, the ALJ received sworn testimony from FDIC officials, each of whom was accepted as an expert without objection from the Bank, including FDIC Examiner-in-Charge

¹⁰12 C.F.R. § 326.8(b).

¹¹ 12 C.F.R. § 326.8(c)(1)-(4).

¹² See 12 C.F.R. § 326.8(b).

¹³ See 31 U.S.C. §§ 5318(g)(2), 5321, and 5322; 12 C.F.R. § 353.

Heather Rawlins (“EIC Rawlins” or the “EIC”).¹⁴ The ALJ also heard from the Bank’s auditor and outside consultant, Joan Vivaldo (“Vivaldo”), and its BSA Officer Alan Chi (“Chi”), who also was the Bank’s Senior Credit Officer, Internal Auditor, Chief Financial Officer, Operations Compliance Officer, and a loan committee member.

On September 8, 2015, the ALJ issued his Recommended Decision finding that the Bank violated the BSA by failing to provide for the continued administration of a BSA compliance program reasonably designed to assure and monitor compliance with FDIC Rules and for failing to file a SAR as required by FDIC Rule 353.3(a)(4)(iii).¹⁵ On October 29, 2015, the Bank filed written exceptions to the Recommended Decision, together with a supporting brief. On November 30, 2015, pursuant to FDIC Rule 308.40(c)(2), the FDIC Assistant Executive Secretary transmitted the record in the case to the Board for final decision.¹⁶

¹⁴ “Rawlins joined the FDIC in 2009 as a mid-career examiner. Between 2006-2009, she was employed by the Florida Office of Financial Regulation, where she conducted approximately 10 BSA exams. In 2009, she joined the FDIC and was designated a BSA subject matter expert. She became an FDIC-Commissioned Examiner in December 2010 and was promoted to Senior Examiner in December 2012. At the time of the hearing, Rawlins had conducted approximately 38 BSA exams. During the hearing, and without objection or challenge by . . . [Bank’s] counsel, Rawlins was qualified as an expert in FDIC Bank examinations and supervision, the Bank Secrecy Act, matters regarding suspicious activity reporting, and in connection with FDIC corrective actions and recommendations for corrective actions.” (citations omitted) R.D. at 3, n. 2.

¹⁵ Pursuant to federal law, SARs and related information may not be disclosed. See 31 U.S.C. §§ 5318(g)(2), 5319, 5321, and 5322 and 12 C.F.R. § 353.; see also *Union Bank of California, N.A. v. Super. Ct.*, 29 Cal. Rptr. 3d 894, 901-03 (Cal. App. 1st Dist. 2005)(citing with approval *Cotton v. Private Bank and Trust Co.*, 235 F. Supp. 2d 809, 815 (N.D. Ill. 2002)) (internal deliberations and certain documents prepared as part of investigation of whether to file SAR privileged from disclosure under BSA). Accordingly, where appropriate, this Decision and Order refers to and adopts the factual and legal analysis of the ALJ’s Recommended Decision regarding such issues. The Board carefully considered all such matters in adopting the Recommended Decision, but it will not here recite the facts and analysis undertaken, in order that the Board’s Decision not reveal information prohibited from disclosure by federal law. The parties hereto have access to the entirety of the ALJ’s Recommended Decision.

¹⁶ 12 C.F.R. § 308.40(c)(2).

III. FACTUAL OVERVIEW

Because the ALJ provided a lengthy, detailed, and well-reasoned opinion with extensive citations to the record in support of his conclusions, the Board finds it unnecessary to reiterate in full the contents of the Recommended Decision. The discussion below, however, provides a brief overview of the inadequacy of the Bank's BSA compliance program as alleged in the Notice, corroborated by supporting testimonial and documentary evidence, and recounted in the Recommended Decision.¹⁷

The Bank is a community bank with two offices – one in San Francisco California, the other in Fremont, California – and in 2012 it had fewer than 15 employees and approximately 200 customers with approximately 500 active deposit accounts. R.D. at 3. The Bank's customer base reflects a "high" BSA risk profile. *Id.* Although the FDIC's 2010 Report of Examination ("2010 ROE") found the Bank's BSA compliance program generally acceptable, it did identify several "must correct" items, including: training, customer risk ratings, account monitoring, risk assessment, and information sharing. R.D. at 3-4. The 2010 ROE reflects that Bank management "agreed to the . . . recommendations," R.D. at 4, however, during the 2012 Examination, FDIC observed that items on the "must correct" list were not adequately addressed, and noted further deterioration in the Bank's BSA compliance program.

In anticipation of the 2012 Examination, FDIC examiners received from the Bank materials regarding the Bank's BSA compliance program. The onsite portion of the 2012 Examination commenced on December 3, 2012. R.D. at 11. As with the 2010 Examination, the BSA portion of the 2012 Examination was largely managed by EIC Rawlins. *Id.* She and her

¹⁷ The Findings of Fact in the Recommend Decision include detailed citations to the voluminous record which includes pleadings, briefs, trial transcripts, and exhibits. R.D. at 3-28. In the interest of efficiency and, except where otherwise noted, the Board cites only to the numbered pages in the Recommended Decision rather than to the underlying supporting evidentiary documents or transcripts.

colleagues undertook a review of the four pillars of the Bank's BSA compliance program. With respect to the first pillar – internal control system – EIC Rawlins randomly selected 24 deposit accounts, including accounts that were newly opened since the 2010 Examination. *Id.* For those accounts, she requested that the Bank provide to her all account opening documentation as well as six months of account activity. *Id.* During the 2012 Examination, the EIC determined that eight of the 24 deposit accounts were BSA compliant but that the other 16 accounts were either improperly risk rated and/or were missing one or more types of information. R.D. at 12. For example, although ten of the 16 deposit accounts reviewed were in a “high risk” import export business, only one was rated “high risk” by BSA Officer Chi and the Bank. R.D. at 13. In addition, EIC Rawlins determined that the Bank – contrary to the recommendation in the 2010 ROE – was reviewing daily batch reports regarding accounts, rather than analyzing aggregate activity for a period of time. R.D. at 13-14. Moreover, while Chi made visits to several of his clients, the Bank did not make or document site visits specifically for BSA purposes. According to 2012 Examination notes, Chi informed Rawlins that notes regarding any site visits to the Bank were kept “in [his] head, as well as [the heads of] the other officers that went with [him].”¹⁸ R.D. at 15. The Board notes that other pertinent factual issues regarding the Bank's noncompliance with Pillar 1 relate to its failure to file SARs under appropriate circumstances. The Board refers to Recommended Decision at 15-16 regarding SARs, and, after careful consideration, approves, adopts and incorporates that portion of the Recommended Decision here by reference.¹⁹

¹⁸ During the hearing before the ALJ, the Bank did introduce some cryptic notes about site visits.

¹⁹ Because applicable provisions of the BSA and the FDIC Rule 353 prohibit disclosure of SARs or the acknowledgment that a SAR was filed, portions of the Recommended Decision remain under seal and are not publicly available. *See* 31 U.S.C. § 5318(g)(2), 5319, 5321, and 5322; 12 C.F.R. § 353.

With respect to independent testing – the second pillar of the Bank’s BSA compliance program reviewed during the 2012 Examination – FDIC examiners requested the Bank to produce any internal or external BSA audits performed since the 2010 ROE was issued. During the pendency of the 2012 Examination, the Bank produced to the FDIC an audit report performed by Vivaldo that covered the first two quarters of 2012 (“2012 Quarterly Report”). R.D. at 16. The FDIC examiners determined the 2012 Quarterly Report was inadequate because, among other things, it lacked an overall assessment of the BSA compliance program; did not point out to the Bank’s board BSA deficiencies that Rawlins had found, and lacked information sufficient to permit the independent assessment of the quality of the Bank’s BSA program. R.D. at 17. Moreover, the 2012 Quarterly Report did not inform the Bank’s board of the various negative changes Chi had implemented with respect to the Bank’s BSA program. More specifically, among the observations made by the FDIC during the 2012 Examination was that, under the auspices of Chi, the Bank’s customer new account form was improperly changed such that nearly all of the Bank’s new accounts fell into the “low risk” rating range. R.D. at 6. The changes implemented by Chi to the customer account form contravened the recommendation in the 2010 ROE, which instructed that the Bank’s risk rating worksheets should be prepared to more accurately permit risk rating of the Bank’s customers. R.D. at 6. Vivaldo informed Chi of the negative consequences of those changes, but Chi rejected her advice. R.D. at 7-9. Also problematic, and at odds with the BSA recommendation in the 2010 ROE, were inappropriate changes that Chi made to the Bank’s self-assessment risk rating, which resulted in changing the Bank’s own overall risk rating from “medium to high” to “low.” R.D. at 9.

The 2012 BSA exam also found deficiencies pertaining to the third and fourth pillars of an effective BSA compliance program – BSA officer qualification and BSA training. These two

factors are related because Chi, who had limited BSA education and training, also prepared the Bank's training materials and claimed to have trained the Bank's employees. Chi's lack of experience, knowledge, and education in BSA matters translated to poor, inaccurate training materials, and less than adequate training for Bank staff. R.D. 19-20. As explained in the Recommended Decision, these deficits also negatively affected the Bank's obligations with respect to filing SARs. The Board refers to Recommended Decision at 20-21 regarding SARs and, after careful consideration, approves, adopts and incorporates that portion of the Recommended Decision by reference.

After concluding the 2012 Examination, on December 19, 2012, EIC Rawlins held an exit meeting with the Bank's board and executive management to review her findings. R.D. at 22. The Bank's board agreed to review the FDIC's regulatory guidance related to BSA, and two members of the Board agreed to implement a satisfactory BSA program. R.D. at 22. A list of written recommendations regarding the Bank's BSA compliance program was presented to Chi on December 31, 2012. R.D. at 22-23. The Board refers to Recommended Decision at 23-26 regarding issues pertaining to SARs, and, after careful consideration, approves, adopts, and incorporates that portion of the Recommended Decision here by reference.

On or about March 8, 2013, the FDIC issued the 2012 ROE. R.D. at 26. Although certain aspects of the Bank's BSA compliance program were deemed sufficient, other aspects were determined to be inadequate, and deficiencies were found to exist under each of the four compliance pillars established under FDIC Rule 326.8(c). R.D. at 26-27. The 2012 ROE also concluded that various recommendations made in the 2010 ROE were not implemented by the Bank. For these and other reasons discussed with specificity in the ALJ's Recommended Decision, the FDIC requested the Bank to execute a BSA Consent Order. R.D. at 27. The Bank

declined, and in its response dated April 26, 2013, argued that it already had implemented several of the recommendations from the 2012 ROE. *Id.* The Bank also suggested that FDIC should – instead of imposing a Consent Order or Memorandum of Understanding – conduct another BSA review “in the latter half of 2013 to review the corrective action” already taken by the Bank. R.D. at 27-28. The Bank’s suggestion was a less than satisfactory response to the findings of the 2012 ROE and the FDIC’s request for a Consent Order. On July 18, 2013, the FDIC issued the Notice of Charges alleging that the Bank violated the BSA and seeking to impose a Cease and Desist Order against the Bank. R.D. at 1.

III. ANALYSIS

A. The ALJ’s Factual and Legal Findings are Fully Supported by the Record

The Recommended Decision offers extensive evidentiary support for the conclusion that the Bank failed to correct BSA compliance issues that were brought to its attention by the 2010 ROE, that the Bank’s BSA compliance program was inadequate as thoroughly explored in the 2012 ROE, and that the Bank failed to file a SAR in circumstances that required such a filing. R.D. at 28-64. The Board summarizes below various examples of the cited deficiencies with respect to each of the four BSA compliance pillars.

1. Lack of Internal Controls

In this case, the ALJ found significant failings with respect to the Bank’s internal controls – the first pillar required for an effective BSA compliance program. For example, after carefully reviewing the evidence regarding 16 combined deposit/loan files, the ALJ determined that the Bank failed to: 1) collect, document and update important BSA information in its deposit account files; 2) properly risk rate the accounts – for example categorizing as “low” risk certain import/export businesses with letters of credit that properly should have been categorized as

“high” risk; and 3) monitor the accounts for a period of six months. In this regard, the ALJ concluded that the Bank disregarded the BSA, FDIC Regulations, the 2010 ROE’s BSA recommendations and its own BSA Policy manual. R.D. at 37-42.

In addition, the Bank’s BSA compliance falls short of the first pillar because the Bank failed to document BSA site visits to its clients. The undisputed evidence establishes that during the 2012 Examination, and in connection with her review of 24 sample account files, EIC Rawlins found no documentation of any BSA site visits. R.D. at 42. Although BSA Officer Chi testified that he had visited some customer sites, the ALJ found, after careful analysis, that the evidence showed the Bank failed to perform documented BSA site visits. R.D. at 43-45. Finally, in contravention of the recommendations in the 2010 ROE, the ALJ determined that the Bank failed to monitor and aggregate activity in high risk accounts, and that the Bank improperly decreased, rather than increased, its self-assessed risk. R.D. 45-47. The ALJ also found that the Bank’s internal control deficits precluded it from detecting activity that might trigger the obligation to file a SAR. The Board refers to Recommended Decision at 47-53 regarding issues pertaining to SARs, and, after careful consideration, approves, adopts, and incorporates that portion of the Recommended Decision here by reference.

2. Lack of Independent Testing for BSA Compliance

With respect to the second pillar required for effective BSA compliance, the ALJ found, among other things, that the audit by Vivaldo was inadequate. After careful consideration of the facts and hearing testimony, the ALJ found that the audit failed to identify weaknesses that were discovered during the 2012 Examination; failed to evaluate overall effectiveness of the Bank’s

BSA program, and lacked sufficient information to permit FDIC to reach a conclusion about the overall quality of the Bank's BSA compliance program.²⁰

3. Unqualified BSA Officer

Likewise, the record supports the ALJ's findings that the Bank's BSA compliance failed with respect to the third BSA compliance pillar because, among other things, Chi, the Bank's BSA Officer, was not qualified to hold the position. R.D. at 43-51. In the Recommended Decision, the ALJ carefully explained why Chi was not qualified to serve as the person responsible for monitoring the Bank's day-to-day compliance with BSA. As the ALJ pointed out, the Federal Financial Institutions Examination Council's Bank Secrecy Act/Anti-Money Laundering Examination Manual ("FFIEC Manual")²¹ and the Bank's 2012 "Bank Secrecy Act/Anti-Money Laundering Program Risk Assessment" Policy Manual both required the BSA compliance officer to have the qualifications, experience, and expertise necessary to undertake the job. R.D. at 57. Chi's on the job training and BSA studies clearly were insufficient, as evidenced by the findings that Chi changed the methodology used by the Bank to self-assess its risk in contravention of the 2010 ROE, and then rejected Vivaldo's criticism in that regard. R.D. at 58. Chi's inadequacy as a BSA compliance officer also was reflected by his failure to monitor and analyze account activity over time. Instead, Chi and the Bank reviewed daily batch reports,

²⁰ The ALJ also determined that Vivaldo had a conflict of interest – auditing Bank compliance with its BSA program, while also providing advice to the Bank on its BSA program. R.D. at 56. The FDIC Board finds the evidence in this regard to be thin, and notes that, for example, FDIC regulations permit "independent" testing to be performed by bank personnel. 12 C.F.R. § 326.8(c)(2). Regardless, the Board does not need to reach this issue to find the Bank noncompliant as to the second pillar because the Board separately credits the ALJ's findings that the independent testing performed by Vivaldo was inadequate and also adopts the various other reasons articulated by the ALJ. R.D. at 53-56.

²¹ The FFIEC Manual was created in 2005 by Federal Financial Institutions Examination Council, which was comprised of the Board of Governors of the Federal Reserve System, FDIC, National Credit Union Administration, Office of the Comptroller of the Currency, Office of Thrift supervision, and State Liaison Committee. The purpose of the FFIEC Manual was to provide guidelines for complying with the four pillars of BSA. R.D. at 31-32.

which was insufficient. *Id.* Further, Chi failed to keep the BSA account files updated with appropriate information, and did not provide to Rawlins and her team the files that they needed during the 2012 Examination in order to assess whether the Bank's files were BSA compliant. R.D. at 59. Based on his findings, accompanied by thoughtful analysis, the ALJ concluded that Chi lacked the experience, training, and time to adequately monitor and coordinate the Bank's BSA compliance program.²² R.D. at 43-49.

4. Inadequate BSA Training

Finally, the record supports the ALJ's findings that the Bank's BSA program was not in compliance with training requirements under the fourth pillar. R.D. at 60-64. Specifically, the ALJ observed that BSA Officer Chi was not qualified for his position and, therefore, he was unable to provide adequate training. R.D. at 61. A further deficiency under the fourth pillar admitted as evidence at the hearing and identified by the ALJ was the lack of tailored training required by both the Bank BSA manual and the FFIEC Manual. Although the Bank argued that its small workforce did not require such specialized, targeted training, the Bank's own BSA Policy Manual – as well as the FFIEC Manual – undermined that argument. R.D. at 62. Finally, the ALJ reviewed the Bank's BSA training materials, and determined that they were inaccurate and inadequate to satisfy the BSA and FDIC Rule 326.8(c)(4) requirement that the Bank provide training for appropriate personnel. R.D. at 64. In the final analysis, after careful consideration, the ALJ determined that even if mistakes in the training materials were minor, considering the evidence as a whole, Chi was not qualified to train the Bank personnel, and the training that was undertaken was inadequate. *Id.*

²² The ALJ also determined that the Bank failed to appoint a back-up BSA officer. R.D. at 60. The Board found the ALJ's reasoning was sound as to this issue, but the lack of a back-up was not central to the Board's determination that the Bank's BSA compliance program was lacking under the third pillar.

In sum, in light of the ALJ's detailed findings as well as the statutory threshold, the Bank cannot credibly assert that the deficiencies cited do not reflect violation of the BSA warranting a cease and desist order.

B. The Requirements in the Proposed C&D Order are Reasonable

Congress has empowered the FDIC with broad discretionary authority under Section 8 of the FDI Act to initiate various types of enforcement actions and to fashion remedies appropriate to the nature of such actions. In the case of a cease and desist action, Sections 8(b) and 8(s) of the FDI Act empower the FDIC to craft a remedy requiring that affirmative action be taken to correct the conditions resulting from cited BSA violations.²³ Further, it is clear that a reviewing court will extend substantial deference to the expertise of administrative agencies in designing an appropriate remedy, and the only basis upon which the courts will overturn the agency's remedy is where the terms of the order are not reasonably related to the legislative purpose of the statute under which the action was initiated.²⁴ Thus, the appropriate inquiry here is whether the remedy proposed by the ALJ is reasonably related to and in accordance with the legislative purpose of FDI Act sections 8(b) and 8(s).

In this case, the ALJ found, based on FDIC testimony and supporting documents, that the Bank failed to maintain an effective BSA compliance program consistent with each of the four pillars established under FDIC Rule 326.8(c). The ALJ also found that the Bank failed to file a SAR and that it did not implement various recommendations for BSA compliance brought to its attention by the 2010 ROE. In light of these findings, the Recommended Decision included affirmative provisions requiring that the Bank implement policies and procedures designed to

²³ 12 U.S.C. § 1818(b)(6); 12 U.S.C. § 1818(s).

²⁴ *In the Matter of Mansfield Bank & Trust Company Mansfield, Louisiana*, FDIC-90-44b, 1990 WL 711265 at *20 (November 16, 1990) (internal citations omitted); *see also In The Matter Of Marine Bank & Trust Company Vero Beach, Florida*, FDIC-10-825b, 2013 WL 2456822, at *8 (March 19, 2013).

bring the Banks' BSA program into compliance. Enforcement Counsel submitted evidence – including documents, opinions from the 2012 ROE and sworn testimony from experienced FDIC officials – establishing that the affirmative action plan in the Recommended Decision was appropriate. In sum, the Board finds that the affirmative provisions in the ALJ's Recommended Decision are reasonably crafted to address the areas of BSA non-compliance identified in the Recommended Decision.

IV. THE BANK'S EXCEPTIONS TO THE RECOMMENDED DECISION

The Bank's 29 exceptions can be broadly categorized as either: (1) objections to specific findings, or (2) challenges to various aspects of the proceedings including the ALJ's legal conclusions, and evidentiary rulings. The Bank's brief supporting its Exceptions discusses in depth its disagreement with several of the ALJ's evidentiary determinations. Specifically, the Bank asserts that the ALJ made erroneous findings with respect to the Bank's BSA compliance program, the Bank's compliance with the recommendations made by FDIC in the 2010 ROE, and the applicability of various BSA regulations and manuals to the Bank, which, it stresses, is a small community bank with approximately 200 customers. In addition, the Bank raised broad general exceptions that challenged many of the ALJ's evidentiary rulings and credibility assessments with respect to the FDIC and Bank witnesses. As discussed below, the Board is not persuaded by the Bank's arguments on any of these issues.

The Board further finds that the Bank's exceptions are, by and large, unconvincing, repetitious, and, in some instances, merely reargue issues raised below and adequately disposed of by the ALJ. As such, most do not justify further analysis. Although the Board finds that none of the exceptions raised by the Bank are compelling, we discuss below the exceptions that might, at first glance, prompt a closer look. In addition, the exceptions addressed – by applicable

BSA compliance pillar – are representative of the nature of the Bank’s challenges to the proceedings and the Recommended Decision.²⁵ Any exceptions not specifically discussed are denied and matters not raised at the hearing need not be considered.²⁶

First Pillar Exceptions

First, contrary to the ALJ’s findings, the Bank claims that: 1) its system of internal BSA controls were adequate, 2) its practices and forms for assessing risk were BSA compliant, particularly given the size the Bank and its relationships with its customers, and 3) that the ALJ failed to appreciate the extent to which the Bank had addressed and met the recommendations of the 2010 ROE. Bank’s Exceptions 1-3, 6, 8, 10-12. However, the Recommended Decision cites ample evidence from the record demonstrating that the Bank failed in myriad ways to comply with the first pillar of the BSA compliance requirements. R.D. at 36-53. For example, as found by the ALJ, the Bank failed to collect and document required information in 16 of 24 deposit account files analyzed by EIC Rawlins and her team and as a result, the files contained incorrect information or were improperly risk rated. R.D. at 37-38. The ALJ also carefully considered the evidence and testimony from the hearing and found the Bank’s failure to collect required

²⁵ With respect to Exception 13, which addresses SARs, the Board refers to Recommended Decision at 47-53 regarding issues pertaining to SARs and, after careful consideration, approves, adopts, and incorporates that portion of the Recommended Decision here by reference.

²⁶ “Exceptions” numbered 9, 14, 17, and 21 are so vague and overbroad as not to be considered exceptions at all. In addition, the Bank filed exceptions that included arguments and facts not presented to the ALJ at the hearing or that raise matters that take place after the issuance of the 2012 ROE. Objections, issues, and argument not raised before the ALJ need not be considered by the Board. 12 C.F.R. §308.39(b)(2). This would include, for example, Bank Exception 39, regarding BSA compliance steps the Bank purports to have taken after the issuance of the 2012 ROE. *See In the Matter of American Bank of the South, Merritt Island, Florida* FDIC-92-17b, 1992 WL 813377, at *15 (November 24, 1992)(“evidence of a bank’s condition and practices arising after the issuance of a notice in an administrative proceeding is irrelevant and immaterial as to any issue presented for adjudication”). By way of further example, and without citation in its briefing to any legal authority, the Bank’s argument in Exception 26 that the BSA is unconstitutionally vague was not asserted at the hearing; without addressing this issue, because it need not do so under 12 C.F.R. §308.39(b)(2), the Board notes that various grounds for constitutional challenges to the BSA have been raised in other contexts, and rebuffed by the courts. *See, e.g., California Bankers Association v. Schultz*, 416, U.S. 21, 71-78 (1974)(Plaintiffs unsuccessfully argued BSA unconstitutional on Fourth Amendments grounds, among other reasons).

information and risk rate its customers fell short of both the 2010 ROE recommendations, and the Bank's own BSA Policy Manual. R.D. at 38.

Although the Bank admits that it did not comply with all recommendations in the 2010 ROE, it argues that the 2010 ROE directive to "monitor and analyze aggregate activity over three month or more to establish patterns of activity" was minor and not substantive. R.D. at 45. The ALJ addressed this point directly when he determined that the undisputed evidence at trial established that analyzing aggregate account information was among the requirements for the Bank to be BSA Compliant. R.D. at 45-46. EIC Rawlins testified that although the Bank's review of daily batch reports was important, alone such a review is inadequate because it does not permit "longitudinal review" that would help compare the expectation of the Bank regarding client activity and actual activity over time. R.D. at 45. Further Rawlins pointed out that reviewing daily account activity "is not the same as aggregating results to look for trends, patterns or significant changes in activity." *Id.* The Board also notes that the Bank's relative size does not excuse it from its BSA compliance obligations.²⁷ Notably, the ALJ correctly points out that as a result of the Bank's failure to correct internal controls criticized in 2010 ROE, the FDIC was required, under the FDI Act, to seek a cease and desist order.²⁸ R.D. at 67.

²⁷ See, e.g., *In the Matter of First Bank of Jacksonville, Jacksonville, Florida* FDIC-96-155b, 1998 WL 363852, *13 (May 26, 1998), *aff'd mem.*, *First Bank of Jacksonville v. FDIC*, 180 F.3d 269 (11th Cir. 1999) ("The Board does not disagree with Respondent's assertion that smaller institutions cannot be expected to maintain the same level of segregation of responsibilities as their larger counterparts . . . Nonetheless, it is self-evident that all institutions, regardless of size, must operate in a safe and sound manner. . . Although small, Respondent's size is not unique. Rather, it is the magnitude of the Bank's management deficiencies that is exceptional.").

²⁸ "If the appropriate Federal banking agency determines that an insured depository institution . . . (B) has failed to correct any problem . . . [with its BSA compliance] which was previously reported to the depository institution by such agency, the agency shall issue an order . . . requiring such depository institution to cease and desist from its violation." 12 U.S.C. § 1818(s)(3)(B).

Second Pillar Exceptions

Similarly, the Board is not persuaded by the Bank's claim that the ALJ provided insufficient support for his findings that the Bank failed to conduct adequate independent testing of its BSA compliance program. Bank's Exceptions 15, 16. The ALJ observed that the report prepared by Vivaldo, the bank's auditor, neglected to identify several weaknesses that were identified in the 2012 ROE, failed to evaluate the overall sufficiency of the Bank's BSA compliance program, and failed to identify information sufficient to permit a third party to reach a conclusion about the adequacy of the Bank's BSA compliance program. R.D. at 53. By way of further example, Vivaldo's report failed to document to the Bank's board that the Bank was not monitoring and analyzing Bank account activity over a sufficient period of time to establish a pattern of activity. This omission also is significant because it was flagged in the 2010 ROE. R.D. at 54. In partial response, the Bank argues that the ALJ's findings regarding its BSA testing for compliance is "form over substance" because Chi monitored activity on a daily basis and was personally familiar with all his customer accounts and, therefore, would have noted any unusual activity. Bank's Exceptions 2, 12.

However, the Board finds that the ALJ accorded appropriate deference to the FDIC examiners' views on this topic. Courts have long recognized that bank examiners' unique experience leads to the conclusion that their determinations are entitled to great deference and cannot be overturned unless shown to be arbitrary and capricious or outside a "zone of reasonableness."²⁹ The Board too has repeatedly recognized the great deference due to the opinions and conclusions of FDIC examiners.³⁰ In this case, Enforcement Counsel presented

²⁹ *Sunshine State Bank v. FDIC*, 783 F.2d 1580, 1581-84 (11th Cir. 1986).

³⁰ See, e.g., *In the Matter of First Bank of Jacksonville*, FDIC-96-155b, 1998 WL 363852 at *11 (May 26, 1998); *In the Matter of Bank 1st, Albuquerque, New Mexico*, FDIC-09-025b, 2010 WL 1936984, at *3

expert testimony by EIC Rawlins, a highly experienced bank examiner, who testified that the Bank's BSA 2012 Quarterly Report was deficient because, among other things, it lacked an overall assessment of the Bank's BSA compliance program, did not identify deficiencies that Rawlins cited in the 2012 ROE, and lacked information sufficient for FDIC examiners to assess the Bank's BSA compliance program. R.D. at 17. Under the standard described above, the findings, conclusions and predictive judgments of the FDIC's expert witnesses are entitled to considerable deference both in determining whether the Bank's BSA compliance program met the requisites of the second pillar and in what specific corrective action is appropriate. Thus, the ALJ properly relied on the testimony of FDIC examiners, and other documentary evidence in the record in finding the Bank's BSA compliance testing inadequate. Moreover, the ALJ found the Bank's own BSA's audit lacking because:

Vivaldo's 2012 Quarterly Report did not inform the Board that (1) against her advice, Alan Chi changed the methodology used to risk rate customer deposit accounts which caused the new deposit accounts to fall into the "low-risk" range; (2) that against her advice, and contrary to the 2012 ROE BSA recommendations, Alan Chi altered the methodology used by the Bank to self-assess its overall risk, thereby resulting in a "low" rather than "medium or high" overall self-assessed risk; and (3) that contrary to the 2012 ROE BSA recommendations, the Bank failed to monitor and analyze aggregate activity over three months.

R.D. at 17. Likewise, the Board will not, in this regard, overlook Bank management's failure to address problems and comply with various recommendations in the 2010 ROE. For all of these reasons, the Board finds that the Bank failed to establish adequate independent testing and that the affirmative requirements in the ALJ's recommended action plan are reasonable.³¹

(March 16, 2010); *In the Matter of American Bank of the South, Merritt Island, Florida*, FDIC-92-17b, 1992 WL 813377, at *12-13 (November 24, 1992).

³¹ See, R.D. Appendix "A" p. 3 - 4 at ¶ (2)(b).

Third Pillar Exceptions

The Board rejects the Bank's claim of insufficient record evidence establishing that the Bank's BSA compliance officer lacked the knowledge, expertise, and training to serve as the Bank's BSA Officer. Bank's Exceptions 18-20. Before arriving at the remedy sought in the ALJ's proposed Order to Cease and Desist – that the Bank must assure its BSA compliance program is managed by a qualified officer³² – the ALJ carefully considered significant, available evidence. For example the ALJ observed that the Bank's BSA Policy Manual and the FFIEC Manual require the appointment of a "bank officer with appropriate qualifications and experience as the BSA Administrator." Then, after carefully considering the hearing testimony and documentary evidence, the ALJ found that Chi's education and experience as the Bank's credit officer were insufficient. R.D. at 57. As another example, a preponderance of evidence demonstrated that Chi, against the advice of Bank auditor Vivaldo, improperly altered the Bank's methodology for risk rating the Bank and its accounts and that he also failed to appropriately update the Bank's BSA accounts and appreciate the significance of doing so. R.D. at 57-58. The ALJ points to substantial evidence establishing that the Bank's BSA compliance officer was inadequate and that no backup officer was officially appointed. R.D. at 59-60. The record also shows that Vivaldo, the Bank's witness and BSA consultant, complained to Chi about the Bank's failure to promptly update its BSA files with complete and current information. R.D. at 58. The ALJ also correctly credited the testimony of EIC Rawlins, who highlighted the deficiencies in the Bank's BSA files. R.D. at 12-13. In light of the 2012 ROE and the informed judgment and analyses of the FDIC officials that Chi was an inadequate BSA compliance officer, the Board

³² See, R.D. Appendix "A" p. 4 at ¶ (2)(d).

sees no reason to second guess the ALJ's conclusion that the Bank failed to meet the requirements of the third pillar of BSA compliance. *See generally* R.D. at 56-60.³³

Fourth Pillar Exceptions

The Board is not persuaded by the Bank's claim that the ALJ had insufficient bases for finding that the Bank failed to provide adequate BSA training to its personnel as required under the fourth pillar of a compliant BSA program. Bank Exceptions 22-24. The Bank asserts that Chi did in fact prepare and train his employees on the BSA in satisfaction of the fourth pillar requirement. Although there may have been minor errors in the training materials, the Bank argues, the BSA training materials as a whole and the on the job training afforded to the Bank employees was appropriate. The ALJ found, however, that the BSA training materials prepared were not only in some respects inaccurate, but also failed to cover the Bank's own BSA policies, procedures, and processes as required by its BSA Policy Manual and the FFIEC Manual. R.D. at 62-64. Based on the evidence presented, it is reasonable for the ALJ to have found that a poorly trained, ill-qualified BSA officer could not provide adequate training, and that leaving copies of manuals around the Bank was not an adequate substitute for the formal BSA training required by FDIC Rule 326.8(c)(4). R.D. at 60-64. For all of these reasons, the Board finds the Bank failed to implement a BSA program that complied with the fourth pillar and that, therefore, the provisions regarding BSA training in the Order to Cease and Desist are reasonable.³⁴

³³ *See In the Matter of Marsha Yessick*, FDIC-00-050k, 2003 WL 22019840 (July 30, 2003); *In the Matter of Anderson County Bank, Clinton, Tennessee*, FDIC-89-235a, 1991 WL 789341 at *5-6 (May 21, 1991) (considerable deference and weight should be given to the opinions and conclusions of FDIC examiners); *accord Sunshine State Bank v. FDIC*, 783 F.2d at 1582-83; *Independent Bankers Ass'n of America v. Heimann*, 613 F. 2d 1164, 1169 (D.C. Cir. 1979).

³⁴ *See*, R.D. Appendix "A" p. 4-5 at ¶ (2)(e).

The Bank's General Exceptions

Finally, the Board rejects the Bank's general arguments (Bank's Exceptions 7, 25 and 27) which challenge, among other things, the ALJ's reliance on "biased" FDIC witness testimony as well as his citation to the FFIEC Manual, in purported contravention of the ALJ's February 27, 2014 Order Granting in Part and Denying in Part California Pacific Bank's Motions *In Limine* No. 1 & 2 ("February 27 Order").³⁵ First, although the February 27 Order sustained the Bank's position that the FFIEC Manual was not entitled to deference under *Chevron*³⁶, the ALJ also found that the FFIEC Manual was relevant and material to the proceedings and would assist the ALJ in understanding and analyzing evidence regarding the Bank's BSA compliance program. February 27 Order at 2–3. Importantly, the ALJ squarely addressed this issue in the Recommended Decision, when he found after careful consideration that although the FFIEC Manual may not have the force of law, the FFIEC Manual was: according to Rawlins and others, an industry-wide guide for compliance with BSA; incorporated in the Bank's own BSA Policy Manual; "scattered all over the Bank"; used by the Bank's own BSA consultant, and is the "foremost guide to bank examiners and banks on identifying and controlling risks associated with money laundering and terrorist financing, and for carrying out the BSA." R.D. at 66. The Board also notes that FDIC Rule 308.5 confers upon the ALJ broad powers to conduct hearings in a fair, impartial and efficient manner.³⁷ Accordingly, it is well within the ALJ's discretion to make evidentiary rulings regarding the admission of evidence and the credibility of testimony. Moreover, under the standard discussed above, the findings, conclusions and predictive

³⁵ The questions as to what, if any, weight should be afforded the FFIEC Manual was the subject of the Bank's Motion *in limine* No. 1; Motion *in limine* No. 2 related to FDIC expert witnesses and their expert reports.

³⁶ *Chevron, U.S.A., Inc. v. Natural Resource Defense Counsel, Inc.*, 467 U.S. 837 (1984).

³⁷ 12 C.F.R. § 308.5.

judgments of the FDIC's expert witnesses are entitled to considerable weight and deference in determining whether the Bank's BSA program complied with FDIC Rule 326.8(c).³⁸

V. CONCLUSION

Based upon its review of the record, the Board finds a preponderance of evidence supporting findings and conclusions that the Bank failed to comply with the BSA and FDIC Rules. Because all of the elements of sections 8(b) and 8(s) were proven, the Board concludes that a formal cease and desist order with affirmative action is justified. Although the FDIC has clear authority to issue a cease and desist order based on failure to comply with just one pillar of the BSA, in this case the Bank failed in its compliance obligations with respect to each of the four pillars. In addition, the Board notes that the BSA recommendations cited in the 2010 ROE persisted over a period of years despite ongoing regulatory efforts to correct them and assurances from Bank management that it would comply. Finally, the Board observes that there is ample evidence in the record warranting the imposition of a cease and desist order based on the Bank's failures with respect to any one of the four pillars of BSA compliance.

The present circumstances illustrate a compelling need for both an order citing BSA noncompliance and a corresponding plan to bring the Bank into compliance. The affirmative provisions in the Recommended Decision were clearly designed to address cited deficiencies in the Bank's BSA compliance program. The Board endorses the plan proposed by the ALJ because it aptly targets the Bank's BSA compliance deficiencies and provides what appears to be a reasonable, workable plan for corrective action. The Board further observes that the order and affirmative action plan are necessary because the record amply demonstrates that Bank management failed to address the BSA compliance issues raised in the 2010 ROE or to

³⁸ See e.g., *Sunshine State Bank*, 783 F.2d at 1582-1583; *In the Matter of Bank 1st of Albuquerque*, 2010 WL 1936984, at *3.

meaningfully respond to subsequent regulatory criticism, and that the finding of an inadequate BSA compliance program was well supported in the 2012 ROE and the evidence admitted in the hearing in this regard.

Based on the foregoing, the Board affirms the Recommended Decision and adopts in full the findings of fact and conclusions of law therein; and issues the following Order implementing its Decision.

ORDER TO CEASE AND DESIST

The Board of Directors of the FDIC (“Board”), having considered the entire record of this proceeding hereby ORDERS and DECREES that the Bank, its directors, officers, employees, agents, or other institution-affiliated parties of the Bank (as that term is defined in Section 3(u) of the Federal Deposit Insurance Act, 12 U.S.C. § 1813(u)), and its successors and assigns, cease and desist from the following violations of the Bank Secrecy Act, 31 U.S.C. §§ 5311-5314, 5316-5332, 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959 and 12 U.S.C. § 1818(s), and its implementing regulations, 31 C.F.R. Chapter X (effective March 1, 2011), section 326.8 and 12 C.F.R. Part 353 of the Rules and Regulations of the FDIC, 12 C.F.R. § 326.8 and 12 C.F.R. Part 353 (collectively the “BSA”):

- (a) Operating in violation of section 326.8 of the Rules and Regulations of the FDIC, 12 C.F.R. § 326.8, by failing to provide for the continued administration of a written, board-approved BSA compliance program in connection with the following:
- (1) Failure to establish a system of internal controls to assure ongoing compliance;
 - (2) Failure to provide for independent testing for compliance conducted by Bank personnel or by an outside party;
 - (3) Failure to designate an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and
 - (4) Failure to provide training for appropriate personnel.

(b) Operating in violation of Part 353 of the Rules and Regulations of the FDIC, 12 C.F.R. Part 353, in connection with the failure to file a Suspicious Activity Report (“SAR”).

1. Within 60 days of the effective date of this ORDER, the Bank shall comply in all material respects with the BSA and its rules and regulations.

2. Within 60 days of the effective date of this ORDER, the Bank shall develop, adopt, and implement a written compliance program, as required by the applicable provisions of section 326.8 of the FDIC’s Rules and Regulations, 12 C.F.R. § 326.8, designed to, among other things, ensure and maintain compliance by the Bank with the BSA and the rules and regulations issued pursuant thereto. The program shall ensure that clear and comprehensive BSA compliance reports are provided to the Bank’s Board of Directors (“Bank’s Board”) on a monthly basis. Such program and its implementation shall be in a manner acceptable to the Regional Director of the FDIC’s San Francisco Regional Office (“Regional Director”) as determined at subsequent examinations and/or visitations of the Bank. At a minimum, the program shall:

(a) Establish a system of internal controls to ensure compliance with the BSA and the rules and regulations issued pursuant thereto, including policies and procedures to detect and monitor all transactions to ensure that they are not being conducted for illegitimate purposes and that there is full compliance with all applicable laws and regulations.

(b) Provide for independent testing of compliance with the BSA, all applicable rules and regulations related to the BSA, and the reporting of suspicious transactions required to be reported pursuant to Part 353 of the FDIC’s Rules and Regulations, 12 C.F.R. Part 353. The independent testing shall be conducted on an annual basis and in accordance

with the procedures described in the current/applicable Federal Financial Institutions Examination Council (“FFIEC”) BSA/AML Examination Manual. The independent testing, at a minimum, should address the following:

- (i) overall integrity and effectiveness of the BSA/AML compliance program, including policies, procedures, and processes;
- (ii) BSA/AML risk assessment;
- (iii) BSA reporting and recordkeeping requirements;
- (iv) Customer Identification Program implementation;
- (v) adequacy of customer due diligence policies, procedure, and processes and whether they comply with internal requirements;
- (vi) personnel adherence to the Bank’s BSA/AML policies, procedures, and processes;
- (vii) appropriate transaction testing, with particular emphasis on high- risk operations (products, service, customers, and geographic locations);
- (viii) training adequacy, including its comprehensiveness, accuracy of materials, the training schedule, and attendance tracking;
- (ix) integrity and accuracy of management information systems used in the BSA/AML compliance program;
- (x) an evaluation of management’s efforts to resolve violations and deficiencies noted in the previous tests or audits and regulatory examinations;
- (xi) an assessment of the overall process for identifying and reporting suspicious activity, including a review of filed or prepared SARs to determine their accuracy, timeliness, completeness, and effectiveness of the Bank’s policy; and

(xii) a review of the methodology used to risk rate accounts.

(c) Written reports shall be prepared which document the testing results and provide recommendations for improvement. Such reports shall be presented to the Bank's Board.

(d) Ensure that the Bank's BSA compliance program is managed by a qualified officer who has the required authority, responsibility, training, resources, and management reporting structure to ensure compliance with the Bank's BSA program requirements and BSA-related regulations, including without limitation:

(i) the identification of timely, accurate and complete reporting to law enforcement and supervisory authorities of unusual or suspicious activity or known or suspected criminal activity perpetrated against or involving the Bank; and

(ii) monitoring the Bank's compliance and ensuring that full and complete corrective action is taken with respect to previously identified violations and deficiencies.

(e) Provide and document training by competent staff and/or independent contractors of all Bank's Board members and all appropriate personnel, including, without limitation, senior management, tellers, customer service representatives, lending officers, and all other customer contact personnel, in all aspects of regulatory and internal policies and procedures related to the BSA, with a specific concentration on accurate recordkeeping, form completion and the detection and reporting of known and/or suspected criminal activity. Training shall be updated on a regular basis to ensure that all personnel are provided with the most current and up to date information.

3. Within 60 days of the effective date of this ORDER, the Bank shall develop, adopt, and implement a written customer due diligence program, which shall include employees and directors at the Bank. Such program and its implementation shall be in a manner acceptable to the Regional Director as determined at subsequent examinations and/or visitations of the Bank. At a minimum, the customer due diligence program shall provide for the following:

(a) A risk focused assessment of the customer base of the Bank, including employees and directors at the Bank, to determine the appropriate level of enhanced due diligence necessary for those categories of customers, employees and directors that the Bank has reason to believe pose a heightened risk of illicit activities at or through the Bank.

(b) For those customers, employees and directors whose transactions require enhanced due diligence, procedures to:

(i) determine the appropriate documentation necessary to confirm the identity and business activities of the customer, employee and director;

(ii) understand the normal and expected transactions of the customer, employee, and director; and

(iii) reasonably ensure the identification and timely, accurate and complete reporting of known or suspected criminal activity against or involving the Bank to law enforcement and supervisory authorities, as required by the suspicious activity reporting provisions of Part 353 of the FDIC's Rules and Regulations, 12 C.F.R. Part 353.

4. (a) Within 60 days of the effective date of this ORDER, the Bank shall establish and implement policies and procedures to advise the Bank's Board of SARs. At a minimum, the Bank's Board shall be advised in detail of all SARs involving employees,

contractors, officers, and directors. The policies and procedures shall also include guidelines to determine what SARs are significant.

(b) The Bank shall establish and implement policies and procedures to ensure that SARs are filed within 30 days of identifying a suspect or unusual and suspicious activity (or a total of 60 days if a suspect is unknown or once per quarter for ongoing transactions). Such a program must also ensure that timely identification of suspicious activity occurs; that timely investigation into unusual activity is undertaken; that related accounts are considered and discussed in the SARs filing; that a detailed, accurate, comprehensive, and readable narrative description of the activity is included in the SARs filing; and that Bank management maintain adequate written information to support a decision not to file a SAR as a result of any investigation of a suspect or unusual and suspicious activity.

5. (a) Within 60 days of the effective date of this ORDER, the Bank's Board audit committee shall oversee the Bank's compliance with the BSA and Parts 326 and 353 of the FDIC's Rules and Regulations. The committee shall receive reports from the qualified officer appointed in Paragraph 2(d) regarding compliance with the BSA and Parts 326 and 353, at least monthly, and shall report to the Bank's Board at every meeting.

(b) Following the effective date of this ORDER, the Bank's Board shall monitor and confirm the completion of actions taken by management to comply with the terms of this ORDER. The Bank's Board shall certify in writing to the Regional Director when all of the above actions have been accomplished. All actions taken by the Bank's Board pursuant to this ORDER shall be duly noted in the minutes of its meetings. The committee shall receive reports from the qualified officer appointed in Paragraph 2(d) regarding

compliance with the BSA and Parts 326 and 353, at least monthly, and shall report to the Bank's Board at every meeting.

6. Within 150 days from the effective date of this ORDER, the Bank's Board shall develop and implement a plan to review all high-risk accounts and high-risk transactions ("Transaction Review"), including but not limited to the Bank's large currency transaction reports ("CTRs"), cash purchases of monetary instruments, wire transfer activity, and foreign exchange services for the six-month period immediately preceding the effective date of this Order (the "Transaction Review Period"), and shall prepare and file any additional CTRs and SARs necessary based upon the review. Based upon the results of the review, the Regional Director may extend the Transaction Review Period if necessary.

(a) Within 60 days of preparing a plan for the Transaction Review, but prior to commencement of the Transaction Review, the Bank shall submit to the Regional Director a written plan for approval that sets forth:

- (i) the scope of the Transaction Review, including the types of accounts and transactions to be reviewed;
 - (ii) the methodology for conducting the Transaction Review, including any sampling procedures to be followed;
 - (iii) the expertise and resources to be dedicated to the Transaction Review;
 - (iv) the anticipated date of completion of the Transaction Review;
- and
- (v) a commitment that any interim reports, draft reports or workpapers associated with the Transaction Review will be made available to the Regional Director upon request.

(b) On completion of the reviews required pursuant to the paragraphs above, the Bank shall submit the written findings of the review and copies of any additional SARs and CTRs filed to the Regional Director.

(c) Throughout the Transaction Review, the Bank shall ensure that all matters or transactions required to be reported that have not previously been reported are reported in accordance with applicable rules and regulations.

(d) Documentation supporting any determination made pursuant to the paragraphs above shall be retained in the Bank's records for such period of time as may be required by any applicable rules or regulations.

7. Within 30 days of the end of the first quarter, following the effective date of this ORDER, and within 30 days of the end of each quarter thereafter, the Bank shall furnish written progress reports to the Regional Director detailing the form and manner of any actions taken to secure compliance with this ORDER and the results thereof. Such reports may be discontinued when the corrections required by this ORDER have been accomplished and the Regional Director has released the Bank in writing from making further reports.

8. Following the effective date of this ORDER, the Bank shall send to its shareholder(s) or otherwise furnish a description of this ORDER in conjunction with the Bank's next shareholder communication and also in conjunction with its notice or proxy statement preceding the Bank's next shareholder meeting. The description shall fully describe the ORDER in all material respects. The description and any accompanying communication, statement, or notice shall be sent to the FDIC, Accounting and Securities Section, Washington, D.C. 20429, at least 15 days prior to dissemination to shareholders. Any changes requested to

be made by the FDIC shall be made prior to dissemination of the description, communication, notice, or statement.

This ORDER shall not bar, estop, or otherwise prevent the FDIC, or any other federal or state agency or department from taking any other action against the Bank, the Bank's current or former institution-affiliated parties, and/or any of their respective directors, officers, employees, and agents, including, but not limited to, the imposition of civil money penalties.

This ORDER shall be effective on the date of issuance.

The provisions of this ORDER shall be binding upon the Bank, its institution-affiliated parties, and any successors and assigns thereof.

The provisions of this ORDER shall remain effective and enforceable except to the extent that, and until such time as, any provisions of this ORDER shall have been modified, terminated, suspended, or set aside in writing.

By direction of the Board of Directors.

Dated at Washington, D.C. this 17th day of February 2016.

/s/

Valerie J. Best
Assistant Executive Secretary

(SEAL)

083235

ORDER DELAYING PUBLICATION AND DIRECTING REDACTION OF
REFERENCES TO CONFIDENTIAL BSA INFORMATION

The Board of Directors of the FDIC (“Board”), having reviewed the Administrative Record in this regard, including the Administrative Law Judge’s September 8, 2015 Recommended Decision (“Recommended Decision”) that is adopted by reference in the final Decision and Order to Cease and Desist (“Decision and Order”), finds that various discussion, documents, exhibits, and legal analyses of the parties and the Administrative Law Judge are precluded from disclosure to the public pursuant to the Bank Secrecy Act (“BSA Information”). *See*, 31 U.S.C. §§ 5318(g)(2), 5319, 5321, and 5322; 12 C.F.R. § 353. The Board further finds that under exceptional circumstances, such as those presented here where the Board determines that publication would seriously threaten the safety and soundness of an insured depository institution, the FDIC may delay publication of a final Decision for a reasonable time. 12 U.S.C. § 1818 (u)(4). NOW THEREFORE,

The Board ORDERS and DECREES that:

1) Although the final Decision and Order shall be provided without delay to the parties upon issuance by the Board, the final Decision and Order and Recommended Decision shall not be published or made available to the public, except as provided in Paragraph 2, below, to protect against disclosure of any BSA Information; and

2) Within 10 business days of issuance by the Board of the final Decision and Order, Enforcement Counsel shall provide to the Executive Secretary a proposed redacted version of the Recommended Decision, which redacts from the Recommended Decision any and all BSA Information. Enforcement Counsel shall consult with Bank counsel regarding redactions prior to submitting the final Decision and Order and redacted Recommended Decision to the Executive Secretary, and in its sole discretion, Enforcement Counsel may modify its redactions to the

Recommended Decision consistent with such consultation. Upon receipt and approval by the Executive Secretary, the Executive Secretary shall promptly publish the final Decision and Order, which attaches and incorporates by reference the redacted Recommended Decision.

Nothing in this Order shall be construed to require, authorize or permit any party to modify, change, amend or alter in any way any provision of the final Decision and Order or Recommended Decision; this Order requires and permits the redaction of BSA Information and nothing more.

This Order shall not alter, delay, or otherwise modify the effective date of the Board's final Order to Cease and Desist.

By direction of the Board of Directors.

Dated at Washington, D.C. this 17th day of February 2016.

/s/

Valerie J. Best
Assistant Executive Secretary

(SEAL)

083251

FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, D.C.

In the Matter of)

CALIFORNIA PACIFIC BANK)
SAN FRANCISCO, CALIFORNIA)

(INSURED STATE NONMEMBER BANK))
_____)

FDIC 13-094b

RECOMMENDED DECISION

Dated: September 8, 2015

C. Richard Miserendino
Administrative Law Judge

FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, D.C.

_____))
In the Matter of))
CALIFORNIA PACIFIC BANK) FDIC 13-094b
SAN FRANCISCO, CALIFORNIA))
(INSURED STATE NONMEMBER BANK)))
_____)

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FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, D.C.

In the Matter of)
)
) FDIC 13-094b
CALIFORNIA PACIFIC BANK)
SAN FRANCISCO, CALIFORNIA)
)
(INSURED STATE NONMEMBER BANK))

RECOMMENDED DECISION

Statement of the Case

C. RICHARD MISERENDINO, Administrative Law Judge. On December 3, 2012, the Federal Deposit Insurance Corporation (“FDIC”) commenced a safety and soundness examination of California Pacific Bank (“CPB” or “Bank”), using Bank information as of September 30, 2012. Based on this examination, the FDIC concluded that the Bank failed to provide for the continued administration of a Bank Secrecy Act (“BSA”)¹ compliance program reasonably designed to assure and monitor compliance with sections 326.8 (a), 326.8(b)(1) and 326.8(c)(1)-(4) of the FDIC Rules and Regulations, and failed to file a Suspicious Activity Report (“SAR”) as required by section 353.3(a)(4)(iii). 12 C.F.R. §§ 326.8(a), 326.8(b)(1), 326.8(c)(1)-(4), 353.3(a)(4)(iii). The FDIC requested the Bank to voluntarily agree to a Consent Order stipulating certain time frames for compliance with the BSA. The Bank declined to do so.

On July 18, 2013, the FDIC issued a Notice of Charges (“Notice”) seeking to impose a Cease & Desist Order against the Bank pursuant to 12 U.S.C. §§ 1818(b)(1) & (s). The Notice of Charges alleges that the Bank violated the Bank Secrecy Act, 31 U.S.C. §§ 5311-5314, 5316-5332, 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959 and 12 U.S.C. § 1818(s), and its implementing regulations, 31 C.F.R. Chapter X (effective March 1, 2011), section 326.8 and 12 C.F.R. Part 353 of the FDIC Rules and Regulations, 12 C.F.R. § 326.8 & 12 C.F.R. Part 353 (collectively “the BSA”).

¹ 31 U.S.C. §§ 5311 et seq., 12 U.S.C. § 1829b and 1951-1959e.

On August 13, 2013, the Respondent filed an Answer denying the material allegations of the Notice. A hearing in this matter was held from March 10-13, 2014, in San Francisco, California. The parties have been afforded a full opportunity to appear, present evidence, examine and cross-examine witnesses, and file proposed findings of fact and conclusions of law, post-hearing and reply briefs.

On the entire record, including my credibility determinations based on the weight of the evidence, established or admitted facts, inherent probabilities, and reasonable inferences drawn from the record as a whole, and after considering the parties' proposed findings and conclusions, post-hearing briefs, and reply briefs, I make the following findings of fact, conclusions of law, and recommended orders.

I. Jurisdiction

California Pacific Bank is, and at all times relevant to this proceeding has been, a corporation organized, existing, and doing business under the laws of the State of California with its principal place of business in San Francisco, California. (Answer ¶ 1.) The Bank is, and at all times relevant to this proceeding has been, a "State non-member bank" within the meaning of section 3(e)(2) of the Federal Deposit Insurance Act ("Act"), 12 U.S.C. § 1813(e)(2), and an "insured depository institution" within the meaning of section 3(c)(2) of the Act, 12 U.S.C. § 1813(c)(2). (Answer ¶ 2; CPB Prop. FOF ¶2.) Accordingly, the Bank is subject to the Act, 12 U.S.C. §§ 1811-1835(a), the Rules and Regulations of the FDIC, 12 C.F.R. Chapter III, 12 C.F.R. Parts 326 and 353, and the laws of the State of California. (CPB Prop. FOF ¶2.) Because the Bank is a "State non-member bank" and an "insured depository institution," the FDIC is the "appropriate Federal banking agency" with respect to the Bank within the meaning of section 3(q)(2) of the Act. 12 U.S.C. § 1813(q)(2). Based on the foregoing, I find that the FDIC has jurisdiction over the Bank, the "institution-affiliated parties" of the Bank as defined in section 3(u) of the Act, 12 U.S.C. § 1813(u), and the subject matter of this proceeding. *See* 12 U.S.C. § 1818(b); (CPB Prop. FOF ¶3).

II. Facts

A. The Bank

California Pacific Bank is a community bank and minority depository institution with one office in San Francisco, California and a second office in Fremont, California. (Tr. 595-96, 674.) Mr. Richard Chi (“CEO Chi”) is, and has been, the Bank’s only Chief Executive Officer since it opened. (Tr. 594.) In 2012, the Bank employed fewer than 15 people: two in the Fremont office and the remainder in the San Francisco office. (Tr. 674.)

The Bank primarily generates new business through referrals. (Tr. 596, 604.) All of its borrowers are required to open deposit accounts. (Tr. 719-20.) In 2012, it had approximately 200 customers with approximately 500 active deposit accounts. (Tr. 601-02.) Significantly, the Bank’s customer base reflects a “high” BSA risk profile. (R. Exh. 10/5, 11.) It has a significant number of import-export customers, including some with trade financing letters of credit. It has a significant number of non-resident alien accounts. It has a large number of accounts with international transactions, including wire transfers and other high volume activity. (Tr. 129, 173.)

B. The 2010 Report of Examination

In July 2010, the FDIC conducted a full safety and soundness examination of the Bank, including its BSA activities. (FDIC Exh. 136.) At that time, Henry Kuang was the Bank’s BSA Administrator. (Tr. 275, 671-72; R. Exhs. 30/1, 31/1, 37/1.) The BSA portion of the 2010 exam was conducted by Heather Rawlins.² (Tr. 35, 272-74.) Rawlins testified that, while the Bank’s BSA program in 2010 was deemed generally satisfactory, there were a number of areas that needed improvement, particularly given the

² Rawlins joined the FDIC in 2009 as a mid-career examiner. (Tr. 25.) Between 2006 - 2009, she was employed by the Florida Office of Financial Regulation, where she conducted approximately 10 BSA exams. (Tr. 23-25.) In 2009, she joined the FDIC and was designated a BSA subject matter expert. (Tr. 25-27.) She became an FDIC-Commissioned Examiner in December 2010 and was promoted to Senior Examiner in December 2012. (Tr. 27-29.) At the time of the hearing, Rawlins had conducted approximately 38 BSA exams. (Tr. 32.) During the hearing, and without objection or challenge by Respondent’s counsel, Rawlins was qualified as an expert in FDIC Bank examinations and supervision, the Bank Secrecy Act, matters regarding suspicious activity reporting, and in connection with FDIC corrective actions and recommendations for corrective actions. (Tr. 34.)

Bank's risk profile.³ (Tr. 275-76; FDIC Exh. 136/11-12.) Specifically, the BSA findings for the 2010 Report of Examination ("2010 ROE") were as follows:

Bank Secrecy Act

Compliance with BSA is generally adequate; however, the following findings must be corrected in order to maintain a satisfactory BSA program.

Training

- Send BSA Officer and supportive staff to outside training and conferences to enhance their understanding of BSA and current trends.
- Document director training and ensure that all directors receive annual training (Sylvia Chi was absent for 2010 annual training).
- Incorporate a method of testing employees' knowledge of training given.

Customer Risk Ratings

- Incorporate the types and levels of activities expected into the risk rating worksheet in order to more accurately risk rate the customer.
- Designate new customers with high levels of activity (such as gas stations) as high risk for at least six months and perform the required enhanced due diligence.

Account Monitoring

Monitor and analyze aggregate activity over three months or more to establish patterns of activity.

Risk Assessment

- Increase the risk rating for the customer base to medium or high risk in order to account for the high number of nonresident aliens and high risk business customers.
- Increase the risk rating for electronic banking in order to account for the 24 remote deposit capture customers.

Information Sharing

Enhance the search log to include the tracking number from the FinCEN request, the date the search was performed, and the signature of the employee who conducted the search.

W-8BEN

Ensure that future W-8BEN forms include the customer's foreign address instead of the U.S. address used by the power of attorney.

Currency Transaction Reports

- Include the number of CTRs filed on a monthly basis in reports to the Board.
- Ensure Section B of the CTRs are filled out properly (35 out of 67 CTRs reviewed had the box indicating "conducted on own behalf" incorrectly marked).

Management Response: Management agreed to the above recommendations and provided a revised log during the examination. Management stated that the customer risk rating worksheet was in process of revision, and a worksheet would be created to track the appropriate activities. CEO Chi emphasized that he understands the importance of training.

³ Contrary to the Respondent's repeated assertion, the un rebutted evidence shows during the 2010 examination the FDIC identified several areas of the Bank's BSA/AML program that required corrective action.

(FDIC Exh. 136/11-12.) (Emphasis added.)

According to Rawlins' unrebutted testimony, at the conclusion of the 2010 examination, she "sat down with [CEO] Chi as well as Joan Vivaldo [the Bank's outside consultant/auditor] ... and really walked them through a BSA program and what was expected of them to help them better understand, again, what regulator expectations were at a bank of their size and their complexity with their risk profile."⁴ (Tr. 276.) Rawlins recalled that CEO Chi, Henry Kuang, and Vivaldo were "extremely receptive, grateful for the time that [Rawlins] was taking to really walk them through the program, the recommendations that [Rawlins] had." (*Id.*) Rawlins was left with the impression that they were "absolutely committed to having a satisfactory BSA program." (*Id.*)

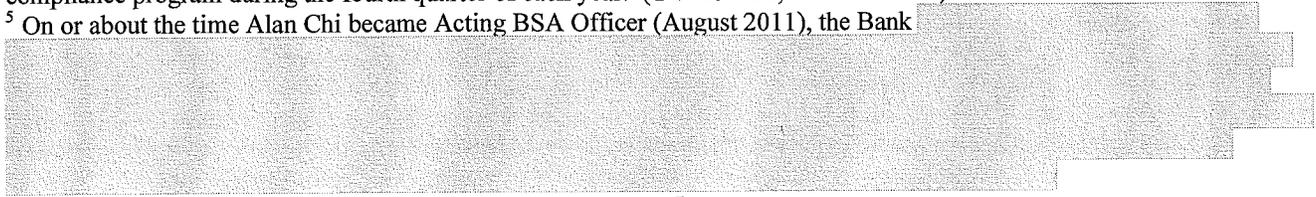
C. Alan Chi Becomes the Bank's Acting BSA Officer

The following year, 2011, not less than four individuals served as the Bank's BSA Officer. Henry Kuang left the Bank in 2011 and was replaced by Wenni Chung. (Tr. 275, 671-72; R. Exh. 36/1.) In mid-2011, Chung took a medical leave of absence and did not return. (Tr. 671-72.) She was temporarily replaced by Robert Zhao, who was appointed as interim BSA Officer. (Tr. 1033-34.) Soon thereafter, Alan Chi, son of CEO Richard Chi, became the Acting BSA Officer.⁵ At the time, Alan Chi was also serving as the Bank's Senior Credit Officer. (Tr. 646, 877-78, 1033-34.)

Sometime before the end of 2011, Alan Chi made two significant changes to the Bank's BSA compliance program : (1) he revised the Bank's customer new deposit account Risk Assessment

⁴ From 2006-2012, the Bank contracted with Consultant Joan Vivaldo to audit its BSA/AML program. (Tr. 918-919.) Her contract called for risk-based transaction testing on a quarterly basis, with evaluations of (1) the overall integrity of the Bank's risk assessment, (2) management's efforts to resolve violations and deficiencies noted in previous audits and regulatory exams, (3) the effectiveness of the suspicious activity monitoring system, and (4) the effectiveness of the Bank's BSA/AML compliance program during the fourth quarter of each year. (Tr. 919-921; Jt. Exh. 2/1-2.)

⁵ On or about the time Alan Chi became Acting BSA Officer (August 2011), the Bank



form⁶ and (2) he revised the risk assessment form used by the Bank to “self-assess” its own risk-rating. (Tr. 659, 661- 662, 1032-34, 1045; FDIC Exhs. 125, 5/632-633; R. Exh. 28/4-5.)

1. The Customer New Deposit Account Form Is Changed

What began as an attempt to “automate” the risk-rating process for new deposit accounts, eventually lead to a change in the risk assessment methodology used for rating those accounts as “high risk, medium risk or low risk.” The changed methodology resulted in an automatic deduction of 12 points from some customer’s overall risk rating score if, for example, the entity or individual opening the deposit account was already a customer of the Bank. (Tr. 1040; R. Exh. 27/5.) Consequently, nearly all of the Bank’s new deposit accounts that opened thereafter fell into the “low-risk” range and three new “high risk” deposit accounts were not properly identified. (Tr. 1035, 1064-65, 1065.)

In addition, the original new deposit account “Risk Assessment” form specifically contained cautionary language stating “all business (sic) listed below are ‘3’ (HIGH RISK) AND WILL BE RATED ‘HIGH RISK.’” The list included, among others, import/export, out of area residents, and gas stations. The purpose of the language was to alert the bank personnel who opened the new deposit account that these types of businesses are a “high-risk” designation. (Tr. 1034.) For unexplained reasons, Alan Chi deleted this cautionary language from his new form. (Compare R. Exh. 28/138 and 362.)

Significantly, these changes made by Alan Chi contravened the 2010 ROE’s BSA Customer Risk Ratings recommendation to:

Incorporate the types and levels of activities expected into the risk rating worksheet in order to more accurately risk rate the customer.”

Designate new customers with high levels of activity (such as gas stations) as high risk for at least six months and perform the required enhanced due diligence.

⁶ Before Alan Chi modified this form it was entitled, “Risk Assessment.” (R. Exh. 28/ 362, FDIC Exh. 14/1.) After he made changes, the form was entitled, “New Account BSA/AML/OFAC Risk Assessment.” (R.Exh. 28/138, FDIC Exh. 125.) Neither version of this customer risk rating form should be confused with the Bank’s self-assessed overall risk rating form entitled, “BSA/AML/OFAC Risk Assessment as of ____.” (R. Exh. 28/4, FDIC Exh. 5/632.) Throughout the hearing, all three of these documents were inadvertently referenced at various times as the “risk assessment” form, which created some confusion.

(FDIC Exh. 136/11-12.)

They also caught the attention of the Bank's outside consultant/auditor, Joan Vivaldo, who counseled Alan Chi against making them.

In a series of email exchanges, Vivaldo bluntly informed Alan Chi in December 2011 that his revised new deposit account risk assessment form failed to correctly identify three new high-risk deposit accounts. (Tr. 1035; FDIC Exh. 118.) She also pointed out that “[h]igh risk accounts are listed in the FFIEC Exam Manual, CPB Bank policy and on the [Bank's] Risk Assessment by the type of industry. Before it was modified in July 2011, the Risk Assessment indicated that if an account was one of the identified high risk, it should be graded high risk. That caveat disappeared with the revision.” (FDIC Exh. 118.)

In addition, Vivaldo told Alan Chi that instead of an automatic 12 point reduction, the Bank should “correctly identify high risk accounts,” and then, in the comments section of the form, explain why, in the opinion of Bank management, the specific account actually posed a lower risk based on its individual facts and circumstances. (*Id.*) Specifically, she wrote: “If CPB can document why these are not really high risk, then do so on the Risk Assessment with the reason and the revised score under Comments. You or Mr. Richard Chi should approve it. If CPB cannot document why these are not high risk, then the monthly monitoring for high risk accounts should begin and continue for 6 months.” (*Id.*) Vivaldo opined that by using an automatic 12 point reduction the Bank would be taking an unnecessary risk that “could turn around and bite them someday.” (Tr. 1037.)

Alan Chi rejected Vivaldo's recommendations. (Tr. 1036.) He told her that he believed the assessments had been done correctly and that he did not want to change the risk assessment process per her suggestions. (Tr. 1038-1039; FDIC Exh. 121/1.) Vivaldo pushed back – telling Alan Chi “I'm afraid you are wrong on both counts. I've explained what's wrong with the risk scoring and suggested a way around it.” (*Id.*) Again she stated that, pursuant to the FFIEC BSA Manual, certain types of accounts are considered high risk and should be treated as such. (*Id.*) She also warned Alan Chi “[i]f you choose to

ignore my advise (sic), I must leave you to the tender mercies of the FDIC.” (*Id.*) Unpersuaded, Alan Chi replied: “if we personally know them then they are not high risk. I do not feel we need to do monitoring for people we have known for 5+ years and some even longer than that.”⁷ (FDIC Exh. 122/1.) He did however make some unspecified modifications to the form.

After reviewing what Alan Chi had modified, Vivaldo told him that the scores were still “too generous.” She reiterated that the Bank would be “better off showing a high risk as high risk initially and then in ‘comments’ explaining why the risk rating has been knocked down to a low or medium risk and the compensating factors that were responsible for the mediation.” (Tr. 1051; FDIC Exh. 126/1.) Notably, Vivaldo also opined that “[t]he BOD should be informed with the monthly report of high risk accounts of those that were scored high risk but were reduced because of compensating factors, like referral by a well known customer or CPB employees.” (*Id.*) She ended by opining “[w]e are pushing the envelope with ‘referral by a well-known customer.’” (Tr. 1052-1053.)

Alan Chi again rejected Vivaldo’s advice. He did not want the Bank to use a comments section to explain the mitigating factors, and he did not want to report to the Board which accounts had been downgraded based on mitigating factors.⁸ (Tr. 1044, 1054; FDIC Exh. 127/1.) He wanted to stress “automation as much as possible for compliance.” (*Id.*) He agreed, however, to make some other adjustments to the risk assessment form that were recommended by Vivaldo.

Vivaldo persisted. She wrote back stating, “I have seen many FDIC reports where they criticism (sic) the bank for not reporting high risk accounts to the board and not reporting high risk accounts downgraded to the board.” (FDIC Exh. 128.) “My aim is to keep you out of trouble with the FDIC. I strongly advise you to do what I have said a couple of times already to handle the high risk accounts.”

⁷ In contrast to her contemporaneous writings, Vivaldo testified at the hearing that if the Bank could document in writing that it had known the customer for “five years” or so, she saw no need for monitoring a new deposit account. (Tr. 1041-1042.) She then conceded that she had never seen such a writing when auditing the Bank. (Tr. 1043.) Eventually she reverted to her original position that Alan Chi would be “better off substantiating with words the reason a risk rating is modified, substantiating the methodology,” rather than automatically downgrading the numerical risk rating. (Tr. 1048.)

⁸ Alan Chi also rejected Vivaldo’s recommendation to file a report with the Bank Board when high-risk customers were downgraded to low-risk as required by the Bank’s Policy Manual. (FDIC Exh. 128.)

(*Id.*)

Alan Chi sent Vivaldo a revised form which changed the criteria used to automatically downgrade a customer from high to low risk. (FDIC Exhs. 129, 130.) Whereas, under his initial revision, the account would be downgraded if the customer had been referred to the Bank by an employee or well-known customer (FDIC Exh. 125), in the later revision, the account would be downgraded only if it was directly related to any loan or existing deposit account. (FDIC Exh. 130.) After reviewing the latest revisions, Vivaldo had the same comments for Chi: “Again, I suggest you lower the score tiers to pre July 2011 levels. With the proposed ranges, almost no account will be medium risk or high risk. An unnatural system. The FDIC recommended the pre July 2011 scoring tiers.”⁹ (Tr. 1044, 1061-62; FDIC Exh. 131/1.) Despite her repeated best efforts, and the BSA recommendations of the 2010 ROE, Vivaldo was unsuccessful in persuading Alan Chi to change his new deposit account risk rating system.

2. The Bank’s Self-Assessment Risk Rating Form Is Changed

The Bank also had a BSA/AML/OFAC Risk Assessment form that it used to “self-assess” its overall risk rating. (R. Exh. 28/5.) In the 2010 ROE, it was recommended that the Bank “[i]ncrease [its self-assessed] risk rating for the customer base to medium or high risk in order to account for the high number of nonresident aliens and high risk business customers.” (FDIC Exh. 136/11.) Alan Chi, however, changed the Bank’s “BSA/AML/OFAC Risk Assessment,” by altering the methodology used by the Bank to self-assess its overall risk, which resulted in a “low,” rather than “medium to high,” self-assessed risk rating. (Tr. 172; FDIC Exh. 5/632-633.) More than once, Consultant Vivaldo told Alan Chi that she disagreed with the “low” self-rating and the methodology that he used. (Tr. 1119-1123; FDIC Exhs. 132, 133.) Alan Chi was unpersuaded.

⁹ In her testimony, Vivaldo clarified that when she advised Alan Chi to return to the pre-July 2011 system, she was referring to “a system that allows medium risk and high risk to appear as they are, not to ... not to arrange a system so that almost everything is low risk.” (Tr. 1065.)

D. Alan Chi Is Officially Appointed BSA Administrator

In January 2012, Alan Chi officially became the Bank's BSA/AML Administrator. (Tr. 646, 878; FDIC Exh. 34/2.) At the same time, the Bank Board elected him to be Senior Vice President, Senior Credit Officer, Chief Financial Officer, Internal Auditor, and Operations Compliance Officer. (FDIC Exh. 34/2.) He also became the Management Information Systems Supervisor and a member of the Directors and Officers Loan Committee. (FDIC Exh. 1/5.) In other words in addition to his new BSA duties, Alan Chi simultaneously assumed the responsibilities of six other high level Bank positions.

E. The 2012 Examination

A full-scope safety and soundness examination was scheduled for early December 2012. Heather Rawlins—the BSA examiner for the 2010 examination—was the Examiner-In-Charge (“EIC”) of the 2012 examination. (Tr. 34-36, 272-74.) FDIC Senior Examiner Bradley Forgang, a BSA subject matter specialist, was assigned to work with Rawlins on the BSA section of the exam. (Tr. 50-51.) On November 9, 2012, in preparation for the exam, Rawlins sent CEO Chi a written request for documentation to be provided to the FDIC prior to the beginning of the on-site review. (Tr. 38-42; FDIC Exh. 3.) The BSA-related items were set forth in numbered paragraphs 91 through 168 of the request. (Tr. 41-42; FDIC Exh. 3/10-15.)

Based on her preliminary review of the items provided to the FDIC, Rawlins had several concerns regarding the BSA portion of the exam. She noted that although the Bank's customer base had several high risk characteristics, there was only one customer on its high-risk list. (Tr. 173.) She was surprised that as of January 2012 the Bank had self-assessed its overall risk level as “low,” even though the 2010 ROE recommended that the Bank “increase the risk rating for the customer base to medium or high risk in order to account for the high number of nonresident aliens and high risk business customers.” (Tr. 48-49, 170-175; FDIC Exhs. 5/632; 136/11-12.) She observed that the Bank had appointed a new BSA Officer after experiencing a significant turnover of BSA Officers since the 2010 exam.

Given her background as a Subject Matter Expert in BSA, her familiarity with the Bank's BSA program, and the BSA findings in the 2010 ROE, Rawlins decided to become directly involved in the BSA review of the Bank. She assumed responsibility for assessing the first pillar of the BSA – the Bank's system of internal controls – to assure ongoing compliance, and in particular compliance with the 2010 ROE BSA findings. (Tr. 49-51, 63-64.)

1. Internal Control System

The onsite examination commenced on December 3, 2012. (Tr. 35; FDIC Exh. 1.) During the first week, Rawlins randomly selected 24 deposit accounts from different lists provided by the Bank during the FDIC's Pre-Examination Planning period, to wit: new accounts opened since the FDIC's 2010 examination; high risk/cash intensive businesses; non-governmental organizations and charities; and the Bank's subpoena log.¹⁰ (Tr. 71.) For each of the 24 accounts, Rawlins asked the Bank to provide "all account opening documentation, including CIP, CDD, EDD and any [BSA] reviews that have been performed on the accounts," as well as six months of account activity.¹¹ (Tr. 64-66, 74-76; FDIC Exh. 8, 9.) As she reviewed the information, Rawlins made notes of her findings on each account, which became part of the FDIC's examination work papers. (Tr. 77-78; FDIC Exh. 10.) As the examination proceeded, Rawlins' notes also reflected discussions that she had with Alan Chi and his responses to questions she asked of him.

Every deposit account opened by the Bank was required to have a completed "New Account Application Form," and a "BSA/AML/OFAC Risk Assessment" form. (Tr. 91-93; FDIC Exh. 5/635-637 and R. Exh. 10/28.) The former contained CIP and CDD to help the Bank verify the customer's identity

¹⁰ Two of the accounts that Rawlins originally requested were not available at the Bank's San Francisco location, so Rawlins replaced them with two other accounts selected from the same pool. (Tr. 72.)

¹¹ "CIP" or "customer identification program," includes four pieces of basic information: the customer's name, date of birth (for an individual), address, and identification number. *See* 12 C.F.R. § 326.8(b)(2) & 31 C.F.R. § 1020.220. CIP is collected to help the Bank verify the customer's true identity. "CDD" or "customer due diligence" includes information concerning the purpose of the business, the purpose of the account, the source of funds for the account opening deposit, and other information which would help the Bank to understand the customer. (Tr. 66.) For high risk customers, additional information beyond CDD, called "EDD" or "enhanced due diligence" is collected. Both CDD and EDD are recorded and monitored to enable the Bank to predict with relative certainty the types of transactions in which a customer may engage and to determine when transactions are potentially dangerous. (FDIC Exh. 103/64-66.)

and to understand and predict the customer's normal transactional activity. The latter form, as explained above, contained a numerical rating system which would allow the Bank to gauge the appropriate customer risk rating, e.g., low, medium or high.

a. Missing CDD/EDD

After reviewing the selected deposit account files, Rawlins determined that 8 of the 24 deposit accounts were BSA compliant. (Tr. 82-83.) The other 16 accounts, however, were either missing one or more types of CDD information and/or were improperly risk rated. (Tr. 83; FDIC Exhs. 11-26.) Eight of the 16 were missing information regarding the source of information and three failed to disclose the purpose of the account. (FDIC Exh. 10.) Four of the 16 were missing information regarding expected activity and eight had account activity that was significantly higher than what was expected by the Bank or had some other combination of all of the above. (*Id.*)

For example, the account files for USA Performance Technology Inc., Wantech International Corp. and Dynasty Customs Broker, Inc., which were opened in 2012, were missing a New Account BSA/AML/OFAC Risk Assessment form. (FDIC Exh. 10/1-3, 11, 16, 20.) The deposit account file for Creative Multi-Commodities International Corp. contained a blank IRS Form W-8BEN.¹² (FDIC Exh. 18/2.) In addition, there was no "expected activity" reflected on the New Account Application Form of Happy D Corporation. (FDIC Exh. 22/1.) The New Account Application Form for New CNB LTD LP/Richard K CHI GEN PTR was missing information pertaining to the nature of business, source of income, purpose of account and expected activity. (FDIC Exh. 12/1.) The account file for Pioneer International Customhouse Brokerage Inc. was missing a Risk Assessment and the business description was inadequate. (Tr. 117; FDIC Exh. 24/1.) The New Account Application Form for New Bridge Group indicated that it was an "import/export" business of food products, but discussion with Alan Chi revealed that the customer was actually exporting cars. (Tr. 103-104, 731; FDIC Exh. 13/3.) The New Bridge

¹² Form W-8BEN: "Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding" is used by foreign persons (including corporations) to certify their non-U.S. status for federal income tax withholding purposes.

Group account file also disclosed that it had an international line of credit, that it was receiving wires from foreign individuals and that its actual account activity was significantly higher than the expected activity.¹³ (FDIC Exh. 10/1 and 13.)

In addition to missing CDD in several deposit accounts, Rawlins specifically noted that the New Account BSA/AML/OFAC Risk Assessment for a gas station that opened a deposit account on July 17, 2012, was incorrectly rated as “low risk,” even though “gas stations” are considered as high-risk accounts because they are cash intensive businesses. (Tr. 125; FDIC Exh. 26/2; R. Exh. 10/5-6.) She also noted that although 10 of the 16 deposit accounts reviewed were “high risk” import/export businesses, only one, Colinda International, was rated “high risk” by Alan Chi. (Tr. 128-129, 133-135, 137.) The Colinda account, however, was promptly removed from the high risk list in August 2012, six months after it was opened, which caused Rawlins to question whether the account had been properly monitored for suspicious activity while on the “high risk” list as per the BSA recommendations in the 2010 ROE. (Tr. 128, 137; FDIC Exh. 136/11 (Customer Risk Ratings.)) When Rawlins asked for documentation showing that the Colinda International account was monitored for suspicious activity, none was provided.¹⁴ (Tr. 137.)

b. Lack of Monitoring

The lack of documentation lead Rawlins to question whether the Bank was actually monitoring and aggregating the new deposit account data for any of its new deposit accounts over three months or more to detect suspicious activity as per another specific 2010 ROE BSA recommendation. (Tr. 164;

¹³ Throughout the 2012 exam, Rawlins and Forgang discussed certain BSA concerns with Alan Chi, including, but not limited to, the CDD that was missing from the deposit account files. (Tr. 79-82, 104, 125, 128, 132, 149-150, 166-168, 190, 215, 243-244; FDIC Exh. 10.) Although no one disputes that the deposit account files did not contain this information, Alan Chi testified at the hearing that at one point during the exam he told Rawlins that “there were documents relating to these depositors ... in the loan files,” the implication being that the CDD information was available for review. (Tr. 707.) Other than this oblique reference to documents in the loan files, there is no evidence or argument that Alan Chi or anyone else at the Bank provided these other documents to the FDIC examiners during the exam. Nor did anyone give Rawlins or Forgang a loan file containing the missing BSA information that correlated to a deposit account. Finally, Alan Chi did not explain why these “other documents” were not copied into the respective deposit account files as required by the Bank’s BSA Policy Manual. (R. Exh. 10/29.)

¹⁴ The documentation would have been used to determine whether the new deposit account should remain on the “high risk” list to be monitored indefinitely for suspicious activity on at least an annual basis. (Tr. 140-141.)

FDIC Exh. 136/11 (Account Monitoring.)) When she asked Alan Chi for clarification, her suspicion was confirmed. Alan Chi told Rawlins that the Bank did not aggregate activity for any period of time to establish patterns. (Tr. 167.) Instead, he and the Bank staff manually reviewed various Bank batch reports on a daily basis, e.g., wire reports, large transactions, currency transactions, etc., to detect suspicious activity. (Tr. 164-165, 169.) They did not, however, record or aggregate the daily snap shots over a period of time in order to discern patterns of suspicious activity. (Tr. 168.) While Rawlins acknowledged that the daily review of account activity was important, she opined that it alone was inadequate because it failed to provide a longitudinal review that would help determine, among other things, whether the customer's actual activity, volume and services rendered were consistent with its expected activity, volume, and services as reported by the deposit account holder at the time the account was opened.¹⁵ (Tr. 137, 167-169, 1072.)

To Rawlins all of these deficiencies were particularly disconcerting. Many of them ran counter to specific BSA recommendations made in the 2010 ROE, which specified that the Bank had to take certain corrective actions in order to maintain a satisfactory BSA program. (FDIC Exh. 136/11-12.) The CDD information missing from the deposit account files, coupled with the omission of the aggregated account data, and the fact that only one of 24 deposit accounts reviewed was rated high risk during the entire 2012 examination period, lead her to conclude that the Bank was not actually performing the appropriate level of customer due diligence and enhanced due diligence. (Tr. 126, 129-130.)

c. No Documented BSA Site Visits

In addition, none of the deposit account files reviewed by Rawlins contained documentation showing that a BSA site visit had occurred, particularly among "high risk" customers with deposit

¹⁵ In addition, a daily batch report, which often exceeds 600 pages, does not provide a separate report for each individual customer. Rather, it is list of all customers for a particular date without an analysis of any transactions. (Tr. 618; R. Exh. 116.) It therefore has extremely limited utility in detecting suspicious activity. (Tr. 882-883.)

accounts.¹⁶ (Tr. 148-149.) During the exam, Alan Chi told Rawlins that he occasionally visited customer businesses, but did not document any of these visits in the deposit account files. (Tr. 149-150, 152.) Instead, he kept note of these visits “in [his] head, as well as [the heads of] the other officers that went with [him].”¹⁷ (Tr. 898, 896-899.) At the hearing, however, Alan Chi testified that he occasionally made “loan” site visits, which also served as BSA site visits.¹⁸ He identified some of the notations that he made in a few loan files reflecting that a customer was visited.¹⁹ (Tr. 739-740, 751-752, 784-86; R. Exh. 97/100, 99/71 and 108/52.)

d. Lack of SAR Filings

As part of her review of the Bank’s system of internal controls, Rawlins also sought to determine whether the Bank filed any suspicious activity reports during the relevant time period.²⁰ (Tr. 231-232.) A pre-exam search of the FDIC’s electronic filing system for information concerning the Bank revealed that

[REDACTED]

21 [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

¹⁶ A BSA site visit is a form of EDD that allows the BSA Officer to observe first-hand the customer’s business operation, as well as any irregularities, that may reflect suspicious activity. (Tr. 148-149.)

¹⁷ At the hearing, Vivaldo lamented that she often had to “drag the information out of [Alan Chi’s] head” in order to document it in her own work notes for BSA purposes. (Tr. 1029-1030.)

¹⁸ Rawlins testified that a “BSA site” visit differs from a “loan site” visit. She opined that a BSA site visit is primarily focused on the legitimacy of the business and the transactions that are flowing from that business through the bank, e.g., whether the business had an ATM on site, the extent to which it engaged in cash transactions, and whether the nature of the business has changed. (Tr. 150-151.) In contrast, a loan site visit is primarily focused on assessing the credit risk to the bank, e.g., whether sufficient collateral exists for the loan, and whether the condition of that collateral is acceptable.

¹⁹ The notations do not reflect much in the way of addressing any BSA issues. Also, there is no evidence that Alan Chi showed any of these notations to Rawlins during the exam. Nor did he explain at the hearing why these notations were not copied into the deposit account file as per Bank policy, if indeed they reflected BSA compliance.

20 [REDACTED]

21 [REDACTED]

After the onsite exam began, Rawlins asked for documentation pertaining to the business accounts of the customers [REDACTED] A review of the documentation that was provided lead Rawlins to conclude that the Bank should have filed a SAR and that the Bank had not done a careful review of the customer accounts for suspicious activity, [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

2. Independent Testing

In addition to the Bank’s internal controls system, Rawlins, with the help of BSA Specialist Forgang, assessed the other three BSA pillars: independent testing for BSA compliance; the BSA Officer qualifications; and BSA/AML training. (Tr. 51.)

As part of its pre-examination document request, the FDIC had asked for “[a] copy of the results of any internally or externally sourced independent audits or tests performed since the previous examination for BSA/AML, including the scope or engagement letter, management’s responses, and access to work papers.” (FDIC Exh. 3/10.) In response, the Bank provided the FDIC with one audit report prepared by Vivaldo that covered only the first two quarters of 2012 (2012 Quarterly Report). (Tr. 190; Jt. Exh. 3.) Rawlins thought it was odd that the Bank did not have an annual audit report. The undisputed evidence shows that when Rawlins specifically asked Alan Chi during the exam if the Bank had any

[REDACTED]

reports, other than the lone 2012 Quarterly Report, none was provided. (Tr. 190-191.) Unbeknown to the examiners, Vivaldo had submitted an “Annual Report for 2011” to the Bank board on March 31, 2012. (Tr. 1089-1090; R. Exh. 27/9-14.)

a. Inadequate 2012 Quarterly Report

After reviewing the 2012 Quarterly Report, Rawlins and Forgang concluded that it was inadequate for several reasons. It lacked an overall assessment of the BSA/AML compliance program (that is, it did not specifically state whether or not certain BSA components were satisfactory.) (Tr. 193-195; Jt. Exh. 3/1.)²³ It did not identify for the Board many of the BSA deficiencies that Rawlins’ found with the customer deposit accounts. (Tr. 196-198; Jt. Exh. 3.) It generally lacked information sufficient to enable the examiners or anyone else to independently assess the quality of the Bank’s BSA program. (Tr. 198.) Notably, Vivaldo’s 2012 Quarterly Report did not inform the Board that (1) against her advice, Alan Chi changed the methodology used to risk rate customer deposit accounts which caused the new deposit accounts to fall into the “low-risk” range; (2) that against her advice, and contrary to the 2012 ROE BSA recommendations, Alan Chi altered the methodology used by the Bank to self-assess its overall risk, thereby resulting in a “low” rather than “medium or high” overall self-assessed risk; and (3) that contrary to the 2012 ROE BSA recommendations, the Bank failed to monitor and analyze aggregate activity over three months. (Jt. Exh. 3.)

b. Vivaldo’s Conflicting Roles

Rawlins and Forgang also had concerns about various tasks performed by Vivaldo for the Bank that exceeded the scope of her “auditing” agreement. For example, in 2006, she wrote the Bank’s BSA Policy Manual. (Tr. 1100-1101.) Thereafter, she annually updated the manual and proposed changes to the Bank’s BSA Officer. (Tr. 1101- 1105.) At the conclusion of the 2010 examination, Vivaldo was present when Bank President Richard Chi met with Rawlins to go over the FDIC’s BSA findings and

²³ In contrast to the 2012 Quarterly Report, several reports Vivaldo prepared for the Bank in 2010 and 2011 specifically stated that the Bank’s BSA program was satisfactory. (R. Exhs. 30/1 at ¶ 2, 31/1 at ¶ 2, 36/1 at ¶ 2.)

subsequently assisted the Bank in addressing some of the findings. (Tr. 179, 1115.) When Alan Chi made changes to the customer risk assessment form and the Bank's self-assessed risk assessment form, which contravened the 2010 ROE BSA findings, Vivaldo advised him against doing so, explained to him why, and recommended other alternatives. At the conclusion of the 2012 examination, she participated by phone in an exit examination meeting between the FDIC and senior Bank management. (Tr. 1082-1083.) For these reasons, Rawlins and Forgang concluded that Vivaldo was acting as both a consultant and an auditor.

3. BSA Officer Qualifications

Rawlins and Forgang also questioned whether Alan Chi possessed the BSA knowledge, experience and training to takeover as the Bank's BSA Officer, particularly given the high turnover of BSA Officers that preceded him. (Tr. 203-204; FDIC Exh. 35.) They were troubled by the fact that the Bank board officially appointed him to the position without recruiting or interviewing anyone else. (Tr. 203-204, 878.)

A review of Alan Chi's resume revealed that he had a bachelor degree in molecular cell biology. He had worked for the Bank for eight years, primarily as the senior credit officer making loan decisions and monitoring loan activity. (Tr. 877.) In February 2011, he and another employee were appointed co-backup BSA Administrators to Wenni Chung.²⁴ A few months after she left the Bank, Alan Chi was made "Acting" BSA Officer.²⁵

With respect to BSA education, in 2008, he completed a community bank compliance officer course given by the Independent Community Bankers of America ("ICBA"), which included a BSA overview. (R. Exh. 78.) In 2009, he completed an ICBA bank internal audit course. (R. Exh. 77.) In 2012,

²⁴ There is no evidence delineating Alan Chi's specific duties in that position. (R. Exh. 26/2.) Rather, he generally testified that prior to becoming the Acting BSA Officer, he helped others prepare responses to FDIC entry letters which, in part, contained information regarding BSA compliance. He also attended some examination exit interviews. (Tr. 648-650, 1153-1154.)

²⁵ When specifically asked why he was selected to become the Acting BSA Officer, Alan Chi testified that it was "because of [his] familiarity with the customers and also being able to implement other processes at the bank regarding compliance, especially loan compliance...." (Tr. 672.)

after he was officially appointed BSA Officer, he, along with several other Bank employees, took a webinar on regulatory compliance, which contained some BSA components covering customer identification and customer due diligence. (Tr. 205, 812, 1008-1009; FDIC Exh. 36.)

Against this background, Rawlins and Forgang believed that the combined responsibilities of all the other key Bank positions to which he was simultaneously appointed would hinder Alan Chi's ability to perform his BSA Officer duties. (Tr. 211; FDIC Exh. 34/2.) In particular, they saw a potential conflict between his role as Senior Credit Officer and his role as BSA Officer. (Tr. 211-213.) Adding to these concerns was the fact that the Bank had not appointed a back-up BSA Officer. (Tr. 214.)

4. BSA Training

In addition to his responsibilities as Senior Vice President, Senior Credit Officer, Chief Financial Officer, Internal Auditor, Operations Compliance Officer, Management Information Systems Supervisor, member of the Directors and Officers Loan Committee, and BSA Officer, Alan Chi had also undertaken responsibility for all BSA training at the Bank. (Tr. 214, 217, 798, 807.) At Board meetings, he provided the Bank Board with a brief BSA overview on customer identification, anti-money laundering and currency transaction reporting. (Tr. 799-805; R. Exhs. 11/8, 12/7, and 14/7.) He provided the Bank staff with BSA training on customer identification, currency transaction reporting, anti-money laundering, identity theft, and unlawful internet gambling. (Tr. 807-808, 811, 813-816, 820-824; R. Exh. 19, 20, 21, 23, 24 and 25.) Rawlins and Forgang reasoned that if Alan Chi lacked the knowledge, education, experience and time to undertake, administer and monitor the Bank's BSA compliance program, he more than likely also lacked the knowledge, experience, training and time to provide adequate BSA training to Bank personnel. (Tr. 230, 453.)

An analysis of the BSA training arranged by Alan Chi supported the inference that the training itself was inadequate.²⁶ According to Rawlins' unrebutted testimony, all Bank employees, including Alan

²⁶ Alan Chi's inability to identify and explain at the hearing the content of some of the training material that he provided to the Bank staff also raises a question about the depth of his understanding of the subjects he was teaching. (Tr. 812.)

(FDIC Exh. 52.)

The conciliatory tone of this letter was relatively short lived. Five days later, on December 19, 2012, Rawlins held an exit meeting with the Bank's executive management and Board to review the 2012 exam findings.³⁰ (Tr. 266.) As the findings were reported to the Bank's directors and officers, Rawlins perceived that CEO Chi and Alan Chi were less receptive to some of the FDIC's findings, particularly in areas administered by Alan Chi, i.e., credit administration and BSA. (Tr. 268-272.) The Board of Directors, however, agreed to review the regulatory guidance related to these areas. (Tr. 269-70; Jt. Exh. 1/10.) In addition, Board members Grisanti and Lauterbach agreed to implement a satisfactory BSA program. (Tr. 270; Jt. Exh. 1/18, 25.)

6. Post Exam Communications

On December 31, 2012, Rawlins gave Alan Chi a written list of recommendations for the Bank based on the results of the examination. (Tr. 263-64.) With respect to BSA Compliance, Rawlins recommended the following:

- Develop a complete and well-documented high-risk customer list, including information explaining the reason the customer is considered high risk.
- Ensure BSA risk ratings for customer accounts are current and appropriate. Changes in risk ratings should be supported and documented.
- Develop and implement a risk-based CDD and EDD program that ensures the collection and retention of sufficient document [*sic*] to assist effectively in determining lawful and customary transactions expected of each customer and especially for those customers determined to be high-risk. EDD should be documented on all HR customers. CDD and EDD should be updated throughout the life of the account.
- Develop and implement formal procedures for monitoring suspicious activity and HR accounts, focusing on whether a customer's activity, cash or otherwise, is usual and lawful business behavior considering the documentation maintained on the customer through the CDD/EDD process.

acknowledged that some of those recommended BSA changes were subsequently implemented, which shows that Bank management was actually aware of the recommended changes.

³⁰ Rawlins prepared two different agendas for the meeting. A nine page detailed agenda for the FDIC attendees and a one page abbreviated agenda for Bank management and directors. (Tr. 266-267; FDIC Exhs. 60, 61.)

- File Suspicious Activity Reports (SARs) on customers if not able to justify why customer activity is not suspicious based on documented CDD/EDD.
- File SARs on customers [REDACTED]
- Maintain PSARs (A/K/A No-SAR files) evidencing suspicious activities reviews where management determined that the account activity was not suspicious.
- Ensure the BSA Risk Assessment accurately reflects the bank's residual BSA risk profile, which is presently high given the high number of import/export customers and weak BSA internal controls.
- Incorporate and document site inspections of customer businesses within customer information files maintained for BSA purposes. Documented site inspections/visits are an important part of EDD.
- Appoint a back-up BSA officer and provide the individual with appropriate training.
- Ensure compliance with the BSA and all related regulations.

(FDIC Exh. 50/4-5.) Rawlins described this list as a way to help management begin the process of taking corrective action before they received the actual ROE several months later. (Tr. 264-65.) Rawlins did not, however, meet with Alan Chi to discuss the recommendations. (Tr. 265.)

7. The Draft 2012 ROE

Rawlins prepared a preliminary draft of the 2012 report of examination, which was internally circulated. She recommended that the Bank be cited with various alleged BSA violations, including apparent BSA pillar and program violations. In addition, she recommended two SAR violations. One for failing to file a SAR based on [REDACTED]

[REDACTED] 31 [REDACTED]

[REDACTED] She also recommended that an enforcement action be initiated against the Bank, which prompted a second layer of review by

³¹ Alan Chi testified that at no time prior to receiving the final 2012 ROE did anyone at the FDIC tell him that he should have filed a SAR [REDACTED]

Case Manager-Special Activities (“CMSA”) Edmund Wong in the FDIC San Francisco Regional Office.³² (Tr. 250-51, 271-72, 521-22; FDIC Exh. 51.)

Upon review of Rawlins’ findings and recommendations, Wong determined that additional information was needed to support some of the noted deficiencies, as well as the recommended violation for failing to file a SAR for [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

The very next day Rawlins provided detailed information concerning the deficiencies with the BSA/AML internal control structure, as well as the circumstances surrounding [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

CM Pinkard promptly responded:

Is this the support for the violation, as EIC, that you are proposing be included in the ROE?

[REDACTED]

The ROE needs information (report quality) as indicated by the following note:
There is not enough information to conclude a SAR should have been filed.

[REDACTED]

**Need to add more
more details on reason a SAR should have been filed and** [REDACTED]

³² During the hearing, and without any objection or challenge by the Respondent, Wong was designated as an expert in the Bank Secrecy Act, suspicious activity monitoring, FDIC enforcement matters, bank examination and bank supervision. (Tr. 419-20.)

[REDACTED]

A few days later, on March 1, 2013, CM Pinkard sent Rawlins a revised ROE, specifically calling her attention to the fact that “[o]ne of the most significant changes was on the Violations page where we changed [REDACTED]

[REDACTED]

Rawlins did not have complete account information for [REDACTED]

[REDACTED] She wrote to CM Pinkard that his suggested revision was inaccurate because:

We do not have information on [REDACTED]

[REDACTED]

[REDACTED]

In short, it was Rawlins’ position that if a SAR violation could not be supported based on the available information derived from the 2012 exam, then the SAR violation should be deleted.

When CMSA Wong read Rawlins’ email, he replied “[w]e can call the bank to get account activity or take out the violation.” (R. Exh. 75.) He also [REDACTED]

and an inadequate system to detect suspicious activity; an inadequate BSA/AML audit by an auditor who is also a consultant for the bank; an unqualified BSA officer; and an inadequate training program. The Board elected SCO Alan Chi as BSA administrator in January 2012, without regard for his lack of knowledge, experience, training, and the time necessary for proper supervision of the program. In addition, management failed to implement examiner recommendations from previous examinations. Due to the severity of the weaknesses, five apparent violations of Section 326.8 (BSA Compliance), including the entire program and all four program pillars, are cited. Examiners are also citing two apparent violations of Part 353 (Suspicious Activity Reports) for failure to file suspicious activity reports (SARs). The Board must take immediate action to correct the BSA weaknesses identified in this Report. Refer to the Bank Secrecy Act Assessment pages as well as the Violations of Laws and Regulations pages for further detail.

(Jt. Exh. 1/14.)

On this basis, the FDIC asked the Bank to sign a BSA Consent Order. (Tr. 529; FDIC Exh. 51.)

The Respondent opposed entering into a consent order. In its response, dated April 26, 2013, it pointed out several ways in which it already had sought to comply with the 2012 ROE, to wit:

1. Appointed a new BSA Administrator and a backup BSA Administrator. Both have already attended BSA coursework and are enrolled in the Independent Community Bankers of America BSA certification training program.
2. Contracted with core IT provider Jack Henry to install more than 50 new transaction codes. These transaction codes allow for the count and categorization of customer deposit transactions to form the basis for an automated and updated Customer Due Diligence (CDD) program. The count and categorization of transactions are inputs into an algorithm that quantitatively compares actual to expected values and based on a numerical score flags certain accounts as "High Risk" for BSA purposes.
3. Designed an Enhanced Due Diligence (EDD) work program that is able to compare the FDIC recommended 6-12 months worth of customer transactions thereby allowing a view of long term patterns and highlight any deviations from the customer average.
4. Designed a program to track subpoenas and ensure that customers whose information is being subpoenaed by law enforcement are being tracked by EDD.
5. Performed training for all staff to understand the BSA program in general, in addition, three staff have been trained [on] how to specifically review the CDD and EDD information.
6. AuditOne BSA review to be completed by the end of May 2013.

(FDIC Exh. 68/3.)

It further stated "[w]e believe that the 2012 ROE made some good recommendations regarding management (such as in BSA) that have already been implemented in the January 2013 Board Meeting.

We keep an open mind, and welcome all constructive recommendations. In light of the prompt corrective action especially towards BSA, as well as many of the recommendation of the 2012 ROE (see details), we request a FDIC checkup to occur in the latter half of 2013 to review the corrective action, and that no MOU or Consent Order be enforced.” (FDIC Exh. 68/4.) In essence, three findings were disputed by the Bank: (1) the independent testing by Joan Vivaldo; (2) whether Alan Chi erred by not filing two SARs;³⁴ and (3) whether the Bank failed to satisfy the recommendations of the 2010 ROE. (FDIC Exh.68/16 -18, 20-21, 22-23.)

III. Analysis and Findings

A. Section 8(b)

12 U.S.C. § 1818(b)(1) provides, in pertinent part:

If, in the opinion of the appropriate Federal banking agency, any insured depository institution, [or] depository institution which has insured deposits, ... is violating or has violated, ... or is about to violate, a law, rule, or regulation, ... the agency may issue and serve upon the depository institution ... a notice of charges ... [and] if upon the record made at any ... hearing, the agency shall find that any violation ... has been established, the agency may issue and serve upon the depository institution ... an order to cease-and-desist from any such violation....

See also, In the Matter of First Bank of Jacksonville (“Jacksonville”), Jacksonville, Florida,

FDIC-96-155b, FDIC Enf. Dec. 5248, 1998 WL 363852 (1998), *aff’d, First Bank of Jacksonville v.*

FDIC, 180 F.3d 269 (11th Cir. 1999) (affirmed without panel).

B. The Bank Secrecy Act

The Bank Secrecy Act (“BSA”) establishes the recordkeeping and reporting requirements for private individuals, banks, and other financial institutions.³⁵ It is designed to help identify the source, volume and movement of currency and other monetary instruments that are transported or transmitted into

³⁴

³⁵ The *Currency and Foreign Transactions Reporting Act* (“Bank Secrecy Act”) 31 U.S.C. § 5311 *et seq.*, 12 U.S.C. § 1829b, and 1951-1959.

or out of the United States or deposited in financial institutions. The statute requires individuals, banks and other financial institutions to file currency reports with the U.S. Department of the Treasury, properly identify persons conducting transactions, and maintain a paper trail by keeping appropriate records of financial transactions. These records enable law enforcement and regulatory agencies to pursue investigations of criminal, tax and regulatory violations, if warranted, and provide evidence useful in prosecuting money laundering and other financial crimes.³⁶ (FDIC Exh. 103/8.)

C. Section 8(s)

Section 8(s) of the Federal Deposit Insurance Act (“FDIA”)³⁷ directs the FDIC, the Board of Governors of the Federal Reserve System (“FRB”) and the Office of the Comptroller of the Currency (“OCC) to: (1) prescribe regulations requiring each insured bank to establish and maintain procedures reasonably designed to assure and monitor the institution’s compliance with the requirements of the BSA; (2) review as part of its examination the bank’s BSA compliance program; (3) describe in a report of examination any problem with a bank’s BSA compliance program; and (4) state in that report whether a bank has failed to correct any problem with its BSA compliance program that was previously brought to its attention.³⁸ In the event a bank fails to correct any problem with its BSA compliance that was previously brought to its attention, Section 8(s) directs the respective agency to issue a cease and desist order against the bank.³⁹

³⁶ In 2001, the BSA framework was augmented by the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (“USA PATRIOT ACT”) which, among other things, strengthened customer identification procedures; prohibited financial institutions from engaging in business with foreign shell banks; required financial institutions to have due diligence procedures and, in some cases, enhanced due diligence (EDD) procedures; and improved information sharing between financial institutions and the U.S. government. Pub. L. No. 107-56 (2001) (codified in various titles and sections of the U.S. Code, including 12 U.S.C. §§ 1813, 1828, 1829b, 1842, 1953, 248, 3101, 3412, 3414 & 3420, & 31 U.S.C. §§ 1304, 5311, 5312, 5313, 5314, 5317, 5318, 5319, 5321, 5322, 5324, 5326, 5330 & 5341 Chapters 3 & 53). *See specifically*, 31 U.S.C. §§ 5318 (g) and (h).

³⁷ 12 U.S.C. § 1818 (s).

³⁸ The same requirements are imposed upon the National Credit Union Administration by section 206(q) of the Federal Credit Union Act (“FCUA”). 12 U.S.C. § 1786 (q).

³⁹ 12 U.S.C. § 1818 (s)(3)(B).

D. The FDIC's BSA/AML Regulations

1. 12 C.F.R. §§ 326.8 (a) – (c)

Sections 326.8(a) – (c) of the FDIC's regulations ensure that all insured nonmember banks “establish and maintain procedures reasonably designed to assure and monitor their compliance with the requirements of” the BSA and its implementing regulations.⁴⁰ 12 C.F.R. § 326.8(a).

Specifically, section 326.8(b) and (c) state:

- (b) *Compliance procedures*—(1) *Program requirement*. Each bank shall develop and provide for the continued administration of a program reasonably designed to assure and monitor compliance with recordkeeping and reporting requirements set forth in subchapter II of chapter 53 of title 31, United States Code, and the implementing regulations issued by the Department of Treasury at 31 CFR Chapter X. The compliance program shall be written, approved by the bank's board of directors, and noted in the minutes.
- ...
- (c) *Contents of compliance program*. The compliance program shall, at a minimum:
- (1) Provide for a system of internal controls to assure ongoing compliance;
 - (2) Provide for independent testing for compliance to be conducted by bank personnel or by an outside party;
 - (3) Designate an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and
 - (4) Provide training for appropriate personnel.

12 C.F.R. § 326.8(b)(1) & (c).

In 2007, the FDIC issued a Financial Institution Letter, FIL-71-2007, to all federal financial institutions announcing that the federal banking agencies had released an Interagency Statement on Enforcement of BSA/AML Requirements. The Letter, among other things, explained the FDIC's current practices of enforcement regarding BSA/AML compliance in an effort to complement the guidance provided in the expansive Federal Financial Institutions Examination Council's BSA/AML Examination Manual (“FFIEC Manual”). (FDIC Exhs. 107/3.)

⁴⁰ The other federal banking agencies have issued similar regulations requiring banks to develop and maintain programs for BSA compliance. 12 C.F.R. §§ 21.21(OCC); 208.63 (FRB); 748.2 (NCUA).

2. 12 C.F.R. §§ 353.1 - 353.3

Sections 353.1 – 353.3 of the FDIC’s Rules and Regulations require an insured state nonmember banks to file a SAR whenever it suspects “a known or suspected criminal violation of federal law or a suspicious transaction related to a money laundering activity or a violation of the Bank Secrecy Act.” 12 C.F.R. § 353.1 – 353.3.

Of particular relevance to this case, section 353.3(a)(4) in pertinent part states:

§ 353.3 Reports and records.

- (a) *Suspicious activity reports required.* A bank shall file a suspicious activity report with the appropriate federal law enforcement agencies and the Department of the Treasury, in accordance with the form’s instructions, by sending a completed suspicious activity report to FinCEN in the following circumstances:

...

(4) *Transactions aggregating \$5,000 or more that involve potential money laundering or violations of the Bank Secrecy Act.* Any transaction (which for purposes of this paragraph (a)(4) means a deposit, withdrawal, transfer between accounts, exchange of currency, loan, extension of credit, purchase or sale of any stock, bond, certificate of deposit, or other monetary instrument or investment security, or any other payment, transfer, or delivery by, through, or to a financial institution, by whatever means effected) conducted or attempted by, at or through the bank and involving or aggregating \$5,000 or more in funds or other assets, if the bank knows, suspects, or has reason to suspect that:

- (i) The transaction involves funds derived from illegal activities or is intended or conducted in order to hide or disguise funds or assets derived from illegal activities (including, without limitation, the ownership, nature, source, location, or control of such funds or assets) as part of a plan to violate or evade any federal law or regulation or to avoid any transaction reporting requirement under federal law;

... or

- (iii) The transaction has no business or apparent lawful purpose or is not the sort of transaction in which the particular 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.

E. The FFIEC Manual

The 439 page FFIEC Manual is a uniformly recognized “authority” on BSA policies, procedures and processes. (Tr. 433, 1039; FDIC Exh. 103.) It provides guidance on identifying and controlling risk’s

associated with money laundering and terrorist financing. It contains an overview of BSA/AML compliance program requirements, BSA/AML risks and risk management expectations, industry sound practices, and examination procedures. (FDIC Exh. 103/6.) It is structured to allow examiners to tailor the BSA/AML examination scope and procedures to the specific risk profile of the particular bank.

The core and expanded overview sections provide narrative guidance and background information on each topic. Each section serves as a platform for the BSA/AML examination and, for the most part, addresses the legal and regulatory requirements of the BSA/AML compliance program. (FDIC Exh. 103/7.) The undisputed evidence shows that in the instant case the FFIEC Manual was heavily relied upon by the Bank's Consultant, Joan Vivaldo, as well as the FDIC examiners. It is also repeatedly referenced in the Bank's BSA Policy Manual as an authoritative resource and there were several copies of the Manual distributed throughout the Bank's premises.⁴¹ (Tr. 433, 1039; R. Exh. 10/38.)

Notably, the FFIEC Manual provides guidance on suspicious activity reporting, [REDACTED]

[REDACTED] According to the

FFIEC Manual, every bank, regardless of its size, should have an effective suspicious activity monitoring and reporting system involving four components: (1) identification or alert of unusual activity, [REDACTED]; (2) managing alerts; (3) SAR decision making; and (4) SAR completion and filing. (FDIC Exh. 103/69-70.) [REDACTED]

⁴¹ In Financial Institution Letter 17-2010, dated April 29, 2010, the FDIC announced the release of the 2010 version of the FFIEC Manual. (FDIC Exh. 109.) The revised manual reflected the ongoing commitment of federal and state banking agencies to provide current and consistent guidance on risk-based policies, procedures, and processes for banks to comply with the BSA and safeguard operations from money laundering and terrorist financing. It further clarified supervisory expectations subsequent to the 2007 update based upon feedback from the banking industry and examination staff. On the same date, an Interagency Transmittal Letter was issued by all federal banking regulators highlighting the updates in the revised 2010 FFIEC Manual. (FDIC Exh. 110.)

[REDACTED]

[REDACTED]

The bank should determine whether a SAR should be filed based on all customer information available. [REDACTED]

(FDIC Exh. 103/70-71 (emphasis added).)

The FFIEC Manual also lists the type of activity that might be suspicious or a “red flag” indicative of money laundering or terrorist financing. (FDIC Exh. 103/350-62.) [REDACTED]

- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]
- [REDACTED]

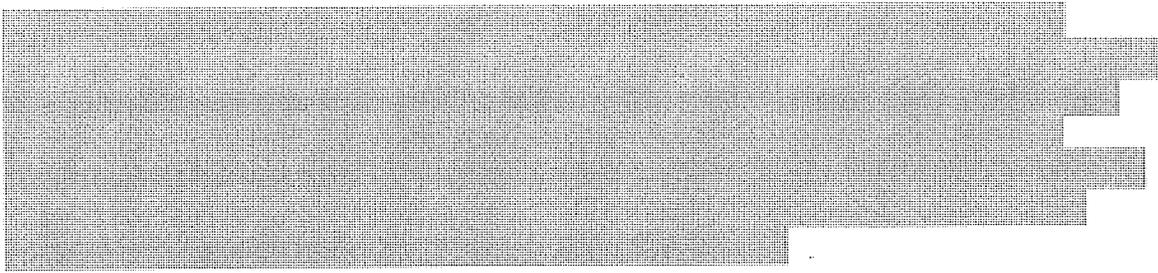
[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]



F. The Bank's BSA Policy Manual

In January 2012, the Bank issued a revised "Bank Secrecy Act/Anti-Money Laundering Program Risk Assessment" manual ("Bank BSA Policy Manual"). (FDIC Exh. 7/1, R. Exh. 10/1, FDIC Exh. 34/7.) It is a comprehensive manual which, among other things, explains the background and purpose of the BSA, acknowledges that it is the Bank's responsibility to establish and maintain procedures to assure and monitor compliance with the reporting and recordkeeping requirements of the BSA/AML regulations (including, but not limited to, internal controls and independent testing), delineates the responsibilities of the Bank's BSA Administrator, describes its overlapping systems to monitor suspicious activity, identifies examples of high-risk accounts, and specifically includes as Exhibit D, the FFIEC Manual's Appendix F: Money Laundering and Terrorist Financing "Red Flags," which describes examples of potentially suspicious activities for Bank officers, directors, managers and staff. (R. Exh. 10/66-76.)

Several parts of the Bank BSA Policy Manual are of notable interest to this case. For example, Part I of the manual acknowledges that the "Bank's Inherent Risk Assessment of BSA/AML is HIGH because the Bank is in both a High Intensity Drug Trafficking Area and a High Intensity Financial Crime Area." (R. Exh. 10/4 and 11.) It further states that "[b]ecause of strong controls, the aggregate risk from activity is **Moderate**. Please see the matrix in Exhibit A delineating and rating risk by Indicator and comments." (*Id.*) (Emphasis added.) The attached Exhibit A, however, is the new self-assessment risk form – "BSA/AML/OFAC Risk Assessment" created by Alan Chi, which resulted in a "**low**," rather than a "moderate" self-assessed risk rating for the Bank. (FDIC Exh. 5/632-633.) There is no evidence showing that this inconsistency was detected by the Bank Board or brought to its attention. Nor does the

evidence show that the changes made by Alan Chi which resulted in the “new self-assessment risk form” were ever specifically discussed with the Bank Board and/or approved by it.

Part II of the Bank’s BSA Policy Manual discusses, among other things, the risk rating of new accounts (deposit and loan accounts) and in particular “High Risk” accounts. (R. Exh. 10/5.) It states, in pertinent part:

For new accounts, please see the new account form “Risk Assessment” for the methodology of establishing risk for new accounts. If an account changes in some way, such as account title or signers, a regrading is required. Regrading is also required if unusual activity or activity inconsistent with the stated nature of the account or stated anticipated activity is detected. The reason for the regarding will be documented in the account documentation/legal file. All regradings will be approved by the BSA Administrator.

(Id.)

Part III also emphasizes that the Bank is committed to complying with the regulatory requirements for CIP and CDD by, among other things, using a New Account Application form for personal and business accounts, a signature card, and a Risk Assessment form for all deposit accounts that rates the customer’s risk from Low to High, i.e., from 1 to 3. (R. Exh. 10/28.) For business deposit accounts, it states that “[a]ll documents pertaining to the new [deposit] account will be filed in a file for that account. If there is a loan file for the depositors, the documents will copied from the loan file. For depositors opening deposits accounts after loan accounts have been established, [the Bank’s] account officers will provide information about the business operations, management, sales volume, territory, suppliers, etc.” (R. Exh. 10/29 (emphasis added).)

In addition, Part III of the manual in pertinent part states that the Bank “will designate a bank officer with appropriate qualifications and experience as the BSA Administrator.” (R. Exh. 10/8.) Among the many responsibilities assigned to the Bank BSA Administrator is the duty to “[p]repare and submit Suspicious Activity Reports to the SAR Committee as appropriate ... [and] [m]aintain Suspicious Activity ‘no File’ files.” (R. Exh. 10/8-9.) It further states:

SAR Filing Requirements:

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Finally, the Bank's BSA Policy requires that an account be re-graded from low to medium or high risk if the Bank receives a [REDACTED]

[REDACTED] Upon re-grading, the account would then be subjected to additional scrutiny and ongoing monitoring. (*Id.*)

G. Alleged Violations

1. First Pillar: Inadequate System of Internal Controls

The Notice alleges, and the FDIC argues, that the Bank failed to establish an adequate system of internal controls consisting of effective policies, procedures, and processes to ensure ongoing BSA compliance in violation of section 326.8(c)(1). 12 C.F.R. § 326.8(c)(1). Specifically, the FDIC asserts that the Bank failed, among other things: (1) to conduct and document adequate customer due diligence and enhanced due diligence in assessing the risk of illicit activities for certain customers; (2) to identify

⁴² Thus, both the FFIEC Manual and the Bank's BSA Policy Manual require the Bank to review account activity for [REDACTED]

certain customers as high risk at the time of opening their accounts, provide for an effective system to monitor those accounts for suspicious activity, and to accurately assess its own risk profile; and (3) to implement sufficient controls and monitoring systems to identify and report suspicious activity, including high risk account monitoring.

a. Failure to Collect and Document Adequate CDD and EDD

The un rebutted evidence shows that 16 of the 24 deposit account files reviewed by Rawlins were missing one or more types of CDD/EDD information, contained incorrect information, and/or were improperly risk rated. (Tr. 83; FDIC Exhs. 10-26.) Eight of the 16 deposit account files were missing information regarding the source of funds. Three failed to disclose the purpose of the account. Four were missing information regarding expected activity and eight had account activity that was significantly higher than what was expected by the Bank when the deposit account was opened. (FDIC Exh. 10/1-3, 11, 16, 20.) Eleven had incorrect, vague or missing information concerning the customer's business type. (Tr. 98-99, 102, 103-04, 107, 109, 111, 113-14, 116-18; FDIC Exhs. 10, 11/1, 12/1, 13/3, 15/3, 16/1, 19/1, 20/2, 21/3, 23/3, 24/7, 25/1, 27/12.)

The evidence also shows that at least eight deposit accounts reviewed by Rawlins were for import/export businesses, i.e., high risk activities.⁴³ (Tr. 134, 436-444.) Of those, at least two businesses also had trade financing letters of credit which alone are considered "high risk" because letters of credit can be used by money launderers to move money across borders. Four of these businesses opened deposit accounts in 2012 under Alan Chi's watch. Yet, only one, Colinda International, was rated "high risk." (Tr. 128-129, 133-135, 137.) The other three high risk businesses that opened deposit accounts in 2012 had no risk rating: Wantech International Corp.; Dynasty Customs Broker, Inc.; and Javier Pimenta. Another high risk business that opened a deposit account in 2012, a gas station, was rated "low risk." There is no

⁴³ In its post-hearing brief at page 33, the FDIC alternately claims that 9 or 10 of the 24 businesses were involved in import-export businesses. However, in the accompanying footnote, it identifies only 8 such businesses. (FDIC Br. p. 33, n.24.) Additionally, in the chart appended to the Notice of Charges, Rawlins identified "Bank Customers 3, 5, 6, 7, 8, 9, 11, and 13" as import-export businesses. (FDIC Exh. 27/12, n.1.) Thus, on balance, it is safe to say that "at least 8" of the 24 deposit accounts reviewed were involved in import-export businesses.

evidence that any of these deposit accounts were monitored for at least six months and/or were subject to enhanced due diligence.

Without complete and/or correct CDD/EDD, the Bank could not properly monitor the customer's deposit account for suspicious activity. Absent an accurate estimate of the expected activity, for example, the Bank lacked a baseline against which to measure the actual activity to determine whether it was suspicious. (Tr. 1135-1136.) Without the requisite CDD/EDD, the Bank could not properly risk rate the customer account.

In addition, the failure to collect, document and monitor these deposit accounts contravened the 2010 ROE recommendations, as well as the Bank's BSA Policy Manual. In the 2010 ROE, the Bank was directed to "designate new customers with high levels of activity (such as gas stations) as high risk for at least six months and perform required enhanced due diligence." (FDIC Exh. 136/11.) The Bank's BSA Policy Manual states:

20. Every High-Risk account, every account with an opening amount of \$10,000 or more (excluding time deposits, accounts opened with loan proceeds, escrow accounts and accounts referred by officers), and every account missing information will be placed on the High-Risk List and monitored for a sufficient time (e.g., 60 days) to determine if actual activity, volume and services used are consistent with the anticipated activity, volume and services projected by the account holder and consistent with the nature of the business as reported by the depositor.

(R. Exh. 10/31 (emphasis added).)

There is no question that Alan Chi knew, or should have known, that the Bank was not collecting and documenting CDD/EDD, that it was not monitoring the deposit accounts for suspicious activity, and that it was not properly risk rating the customer accounts. The un rebutted evidence shows that when Rawlins asked Alan Chi if the Bank had monitored and aggregated the deposit account information for the high-risk Colinda International account, he told her that the Bank did not aggregate any account activity for any period of time to establish patterns. (Tr. 167.) The evidence also shows that soon after he became Acting BSA Officer in 2011, Vivaldo told Alan Chi that she had identified three new deposit accounts

that were not properly identified as “high” risk accounts. (Tr. 1135-1136.) She also told him that his modified customer risk rating form would not withstand scrutiny of the FDIC.

The Bank does not dispute that CDD/EDD information was missing from its customer deposit account files. (R. Prop. FOF ¶¶ 60, 65, 67, 69 and 73.) Rather, it attempts to side-step the issue by arguing that the FDIC has a “fixation on the documentation in one form.” (R. Reply Br., p. 11.) However, that “one form” is required by the Bank’s BSA Policy Manual, and it is undisputed that it was missing from several deposit account files. Moreover, even Alan Chi conceded that the “high” risk deposit account files “could have been better documented” and the Bank’s risk assessment forms “needed some improvement.” (Tr. 696-97.)

The Bank also argues that through his involvement with the lending process, Alan Chi was “familiar” with each of the 16 customers whose deposit accounts were missing CDD/EDD and therefore he knew the customers and understood the risks, if any, associated with their deposit accounts. The argument is unpersuasive for two reasons.

First, the evidence shows that much of Alan Chi’s knowledge of the Bank’s customers was stored “in his head.” (Tr. 898, 980, 1029.) It is neither practical nor prudent for a bank to premise its business on knowledge stored in one individual’s memory. This is particularly true when the statute, regulations and the Bank’s Policy Manual require CDD/EDD to be properly documented so that Board members, other members of bank staff and bank management, inside and outside auditors, bank examiners, and law enforcement agencies can access and review it.

Second, relying on one’s memory, is contrary to the generally accepted industry practice - as demonstrated by the testimony of Rawlins and Vivaldo, as well as the FFIEC Manual, and the Bank’s BSA Policy Manual - which requires a BSA Officer to conduct and document an individualized, fact-based assessment of the risk level of the account at account opening for BSA purposes. (Tr. 88-90, 107, 145-46, 312-13, 979-81; FDIC Exh. 103/25-28; R. Exh. 10/5.) The preponderance of the evidence viewed as a whole reflects that this was not done.

The Bank also argues that Rawlins and Forgang could—and should—have reviewed the loan files of the 16 customers for which CDD/EDD information was missing, incomplete and/or incorrect. At the hearing the Respondent submitted, over the FDIC’s objection, 16 exhibits reflecting 16 combined customer deposit account/loan files that Alan Chi prepared specifically for the hearing. (Tr. 313-318, 702-709, 721; R. Exh. 94-109.) Much of Alan Chi’s testimony regarding the 16 combined files was dedicated to demonstrating that some—but not all—of the missing information was located in the loan files. The Bank’s argument pertaining to these loan files likewise fails for several reasons.

First, Alan Chi knew, or should have known, the nature of the information and the type of file that the examiners wanted to review. The evidence shows that at the outset Rawlins requested in writing “all account opening documentation, including CIP, CDD, EDD and any reviews that have been performed on the accounts.” (Tr. 64-66, 81-82, 299, 301-02, 307-08, 705-06, 709; FDIC Exh. 8.) According to her unrebutted testimony, she and Forgang also explained to Alan Chi what they were looking for. (Tr. 82.) It is no coincidence, therefore, that the 24 files that she was given to review were “deposit account” files and not “loan files.”

Second, the Bank’s BSA Policy Manual requires the Bank staff – not the FDIC examiners - to ensure that the Bank’s deposit account files are complete and up to date. Specifically, it states: “All documents pertaining to the new [deposit] account will be filed in a file for that account. If there is a loan file for the depositors, the documents will be copied from the loan file.” (R. Exh. 10/29.) There is no evidence or argument that the Bank staff copied any loan documents to the deposit account files or that those files were updated with BSA-related information from the loan files. To the contrary, Respondent concedes that it did not follow this policy, explaining: “Rather than updating the documentation in the account opening files, the Bank updated the documentation in the loan files every time the Bank’s customer received or renewed a letter of credit or a loan.” (R. Br., p. 12-13.) In its Reply Brief, the Bank attempts to shift the responsibility for its failure to comply with this section of its own BSA Policy Manual by arguing that in the 2010 ROE, the FDIC failed to “indicate that documentation regarding the

depositors located in the loan files needs to be incorporated in the account opening files.” (R. Reply Br., p. 9.) The suggestion that Alan Chi and other Bank staff are not required to follow their own BSA Policy Manual unless the FDIC specifically instructs them to do so is unavailing.

Third, the undisputed evidence shows that neither Alan Chi nor anyone else at the Bank actually gave Rawlins or Forgang any loan files to review, or any documents from the Bank’s loan files or any files other than the 24 deposit account files.⁴⁴ (Tr. 82, 705.) Rather, in response to a leading question from Respondent’s counsel, Alan Chi testified that unspecified loan files with documentation as it existed in December 2012 were “made available” to the FDIC examiners. (Tr. 705.) When asked to explain what he meant by was “made available,” Alan Chi stated, “If the FDIC examiners were aware of them and if they asked for it, it would be provided.”⁴⁵ (*Id.*) However, there is no evidence that Rawlins or Forgang were made aware that there were corresponding loan files containing the missing BSA information for the 16 customers. Rawlins credibly testified that Alan Chi did not specifically tell her or Forgang that there were loan files that contained BSA-related information. (Tr. 81-82.) The only testimony by Alan Chi on this subject comes in response to an ambiguous leading question from Respondent’s counsel, to wit:

Q. Mr. Chi, did you tell Ms. Rawlins that there were documents relating to these depositors that she had questions about the loan files?

A. Yes.

(Tr. 707.)

The sum and substance of Alan Chi’s sparse testimony casts doubt on what, if anything, he actually told Rawlins and Forgang about the 16 customer loan files. Stated otherwise, given the Bank’s reliance on its “loan file” argument, one would expect Alan Chi to delineate when, where, and what exactly he told

⁴⁴ It is disconcerting that Alan Chi took the time and made the effort to combine these 16 files for purposes of the hearing, but made no attempt during the exam to give Rawlins or Forgang a single loan file which purportedly contained CDD/EDD information.

⁴⁵ Alan Chi also added that to the best of his knowledge the FDIC examiners reviewed probably close to half the Bank’s loan portfolio which consisted of more than 200 loan files. (Tr. 601, 705.) There is no evidence in the record, however, showing that any of the loan files for the 16 customers whose deposit account files had missing/incomplete/incorrect CDD/EDD information were among the 200 or so loan files that were “made available” for review to the other FDIC examiners during the 2012 examination.

Rawlins and Forgang about a purported connection between the 16 customer deposit account files with missing, incomplete and/or incorrect CDD/EDD information and the information in their counterpart loan files.

If anything, a careful review of evidence concerning the 16 combined deposit/loan files prepared by Alan Chi specifically for the hearing: corroborates Rawlins' testimony that there was missing, incomplete and/or incorrect CDD/EDD information in the 16 customer deposit account files; confirms that the Bank did not comply with its own BSA Policy Manual or the 2010 ROE BSA findings; highlights that several of these customers were import/export businesses with letters of credits which would place them in a "high" risk category; and underscores that despite the high risk nature of these businesses, their customer risk ratings on the risk assessment forms as modified by Alan Chi, placed them in a "low" risk category in contravention of the 2010 ROE BSA findings. (Tr. 704-792; R. Exhs. 94-109)

Based on the evidence viewed as a whole, I find that the Bank failed to collect, document and update important BSA information in its deposit account files, failed to properly risk rate these deposit accounts and failed to properly monitor these accounts for suspicious activity for a minimum of six months. I further find that in doing so the Bank contravened the BSA, applicable regulatory requirements, the 2010 ROE BSA findings, and its own BSA Policy Manual.⁴⁶

b. Lack of Documented BSA Site Visits

The Notice also alleges, and the FDIC asserts, that the Bank failed to perform documented BSA site visits. Rawlins opined that as a part of enhanced due diligence, the Bank was required to site visit its customers to visually determine whether the customer's business operation comports with the BSA information in its deposit account file. (Tr. 148.) Although she expected the BSA site visits to be documented in the deposit account files, the undisputed evidence shows that none of the 24 deposit account files that she reviewed contained any documentation showing that a BSA site visit had occurred.

⁴⁶ It should be emphasized again that in the event a bank fails to correct any problem with its BSA compliance that was previously brought to its attention, section 8(s) of the FDIA directs the respective agency to issue a cease and desist order against the bank. 12 U.S.C. § 1818(s).

(Tr. 149.) Moreover, at no time during the examination did anyone at the Bank provide her with documentation regarding BSA site visits undertaken by the Bank. (Tr. 152.)

The Bank does not dispute that the deposit account files did not contain any BSA site visit documentation or that no documentation of BSA site visits was provided to Rawlins during the examination. Rather, it argues that Alan Chi occasionally visited customers on site, and that some of those site visits were documented in the loan files. At the hearing, Alan Chi pointed to documented site visits in four of the Bank's loan files, to wit: Metamining (Tr. 739-741; R. Exh. 97/100), USA Metals (Tr. 746-747; R. Exh. 98/88), Wantech (Tr. 751-752; R. Exh. 99/71), and M&S Central Warehouse (Tr. 785-786; R. Exh. 108/52).⁴⁷ The evidence shows:

October 10, 2011 - Alan Chi and his father, Richard Chi, visited the Metamining office in connection with a pending commercial credit application. (Tr. 737-739.) It further discloses that a company official discussed with them the cash flow sufficiency of the certain mines. When Alan Chi was asked at the hearing what he remembered about the site visit, he recalled "several people working in the office ... a large map – I think mountains near – heading down from Virginia ... maps of Oklahoma and all sorts of big, thick geological reports there." (Tr. 740.) However, he failed to explain how this site visit related to BSA compliance.

October 14, 2010 - Alan Chi and Richard Chi visited USA Metal LLC where they met with the husband and wife owners of the company to discuss and review fire damage to a warehouse. The evidence further shows that in the course of that visit, which culminated in dinner at "Peony's," the Messrs. Chi encouraged their customers to reconcile their marital difficulties, and discussed with them how their assets could be divided, in the event of a divorce. (Tr. 746-748; R. Exh. 98/88.) Again, Alan Chi failed to explain how this visit related to BSA compliance.

⁴⁷ Alan Chi also referenced at least one other site visit for which there was no documentation. (Tr. 897-899.) In an effort to explain away the omission, he testified that the "documentation" was "in [his] head, as well as the other officers that went with [him]." (Tr. 898.) But even Vivaldo, the Bank's consultant, expressed frustration with Alan Chi's failure to document his site visits, explaining that she frequently has to "drag the information out of [his] head." (Tr. 1029-30.)

August 13, 2009 - Alan Chi visited Wantech's warehouse in order to get a feel for its daily operations. (R. Exh. 99/71.) He observed that the warehouse is "very carefully operated so that Wantech is always well supplied with high quality goods ... [and that] it is more of a trafficking warehouse with goods going in and out as opposed to a hoarding warehouse where a large shipment comes in and trickles out." *Id.* His "overall impression of Wantech's facilities and management are strong and stable." Instead of asking Alan Chi to explain how that visit related to BSA compliance, Respondent's counsel had him fast forward to page 106 of the loan file to review four pages of "Aged Receivables As of Sep 30, 2012." Upon doing so, Alan Chi stated that this information helped him to confirm the source of funds that might run through Wantech's deposit account because he would expect to see checks from these customers. (Tr. 755.) His answer, however, does not explain how reviewing Wantech's balance sheet for a credit renewal in **September 2012**, relates to a warehouse visit in **August 2009**, which occurred three years before he became the Bank's BSA Officer. In fact, with the exception of the Metamining visit in 2011, the two other visits which the Bank chose to illustrate BSA site visit compliance, took place long before Alan Chi became "Acting" BSA Officer, during a time when his sole responsibility was the Bank's Senior Credit Officer.

The only site visit referenced in the record after Alan Chi officially became the Bank's BSA Officer occurred on May 11, 2012, when he visited M&S Central Warehouse. Although Alan Chi relates in detail what he learned about the warehouse operations, the evidence discloses that the visit was prompted by a loan application from a new customer, and not by the fact that the new customer opened a deposit account.

Moreover, there is no evidence of a follow up site visit of any kind to any of these four businesses. Rather, Alan Chi conceded that after making an initial visit, the Bank does not necessarily perform repeat

site visits. (Tr. 786-788.) Nor did the Bank point to any a site visit of any kind in connection to the other 12 deposit account customers.⁴⁸

Based on the evidence viewed as a whole, I find that the Bank failed to perform documented BSA site visits.

c. Failure to Comply With Other 2010 ROE BSA Recommendations

(1) Failure to Monitor and Aggregate Activity in High Risk Accounts

The 2010 ROE also directed the Bank to “monitor and analyze aggregate activity over three months or more to establish patterns of activity.” The Bank admits that it did not implement this directive. (R. Reply Br., p. 10.) The undisputed evidence shows that the Bank did not monitor high-risk accounts over any period of time. (Tr 167, 620.) Nor did it perform any documented trend analysis on its customer accounts. (Tr. 1072.) Rather, Alan Chi and Bank staff reviewed batch reports on a daily basis. (Tr. 620, 1072.) While Rawlins acknowledged that the daily review of account activity was important, she opined that it alone was inadequate because it failed to provide a longitudinal review that would help determine whether the customer’s actual activity, volume, services and nature of business were consistent with the expected activity, volume, services, and nature of business as reported by the account holder at the time the account was opened. (Tr. 137, 167-169, 1072.) Rawlins opined that looking at each account each day is not the same as aggregating results to look for trends, patterns or significant changes in activity. (Tr. 167-68.)

Rawlins also opined that the failure to aggregate activity precluded the Bank from detecting anomalies which might necessitate the filing of a SAR. (Tr. 167-169.) Alan Chi admitted on cross-examination that he had never filed a SAR as the result of his identification of suspicious activity during

⁴⁸ Rawlins’ testified that the M&S Central Warehouse visit, as well as the other three visits, were conducted solely for credit administration purposes, and that they differed in purpose and perspective from a BSA site visit. (Tr. 150-152, 752-753, 787.) Alan Chi disagreed. He testified, “[t]here’s no reason to be asking two sets of questions, thinking two separate way for something that should be considered aggregate.” (Tr. 753.) While it is unnecessary to conclude that a BSA and a loan administration site visit can never be made at the same time or by the same person, the absence of any documented BSA site visit in either file (deposit or loan) speaks for itself. The failure of the Bank to document BSA site visits is consistent with its overall failure to establish an adequate system of internal controls.

review of the daily batch reports. (Tr. 882-83.) Nor had there ever been an instance, as a result of his review of the daily batch reports, where he determined that there might be suspicious activity, but decided not to file a SAR. (*Id.*)

Respondent nevertheless argues that “the FDIC failed to present any evidence indicating that a change in the nature of the activity affecting a customer’s account over the course of time was somehow missed by the Bank.” (R. Br., p. 14.) To the contrary, the evidence shows that the Bank failed to properly review a deposit account file for [REDACTED]

[REDACTED]

[REDACTED] This is precisely the sort of information that the Bank would have gleaned by reviewing aggregate activity over time as opposed to simply reviewing daily batch reports.

Thus, based on the evidence viewed as a whole, I find that the Bank failed to monitor and aggregate activity in high risk accounts in accordance with the 2010 ROE BSA findings.

(2) Improper Self-Assessed Risk Rating

The Bank has an overall BSA/AML/OFAC Risk Assessment form that it used to self-assess or self-score its own BSA risk. (Tr. 170-171.) According to Rawlins, the purpose of the Bank’s Risk Assessment form is to identify areas of higher BSA risk within the Bank given its geographic location, customer base, services and products offered in order to determine the level of resources required to mitigate these risks to the Bank. (Tr. 171-172.) It is not gainsaid that the Bank’s customer profile has many BSA “high” risk characteristics, including, but not limited to several import-export customers,

including some with trade financing letters of credit; numerous non-resident alien accounts; and significant international activity, including international wires and high volume activity. (Tr. 173.)

In the 2010 ROE, the Bank was also directed to “[i]ncrease the risk rating for the customer base to medium or high risk in order to account for the high number of nonresident aliens and high risk business customers.” (FDIC Exh. 136/12.) Soon after he became “acting” BSA Officer, Alan Chi altered the Bank’s risk assessment form by changing the methodology used to rate certain risk factors. As a result, as of January 2012 the Bank rated itself “low risk,” rather than “medium” or “high risk.” The Bank’s BSA Consultant/Auditor, Joan Vivaldo, criticized the methodology used by Alan Chi to reach the “low” risk rating, cautioned him that the rating was too low, and bluntly told him that her risk assessment of the Bank was much higher. Rawlins likewise disagreed with the Bank’s “low” risk self-assessment. (Tr. 172-174.) She opined that given the Bank’s overall profile, the controls in place at the Bank were insufficient to mitigate the high risks attributable to its customer base, etc. (Tr. 173-176.)

Thus, based on the preponderance of the evidence, I find that the Bank improperly decreased, rather than increased, its self-assessed risk as directed by the 2010 ROE BSA findings.

d. SAR Violations

(1) Failure to Document and Support a File/No File SAR Decision

[REDACTED]

Both the FFIEC Manual and the Bank's BSA Policy Manual require the Bank to review account activity [REDACTED] and to independently evaluate the need to file a SAR based on the Bank's own review of those materials.⁴⁹ The undisputed evidence shows that the Bank (or Alan Chi) did not [REDACTED]

[REDACTED]

Accordingly, by failing to properly investigate and document his review of the subject account files, and by failing to document his decision not to file a SAR, the Bank failed to implement, maintain and ensure an effective BSA compliance program.

⁴⁹ As Bank Consultant Vivaldo explained, [REDACTED]

(2) Failure to File a SAR

The undisputed evidence also shows that the neither the Bank nor Alan Chi filed a SAR with respect to [REDACTED]

[REDACTED]

In preparing a draft of the 2012 ROE, Rawlins concluded that the Bank should have filed a SAR pursuant to [REDACTED]

[REDACTED]

51

50 [REDACTED]

While conducting the second-level review of the 2012 ROE, CMSA Wong advised Rawlins that, in his opinion, [REDACTED]

[REDACTED] that [REDACTED]

[REDACTED] 52 [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

Wong testified extensively regarding his review [REDACTED]

While the parties spend significant energy trying to recreate the conversations between Alan Chi and Rawlins during the 2012 examination, the result has little bearing on the outcome of this proceeding.

53 [REDACTED]

[Redacted text block containing multiple lines of obscured content]

by both the FFIEC Manual and the Bank's BSA Policy Manual. Thus, I find that the Bank have filed a SAR [REDACTED].

2. Second Pillar: Failure to Conduct Adequate Independent Testing

The Notice alleges that the quarterly report of the Bank's external auditor, Joan Vivaldo, failed to identify several BSA weaknesses found during the 2012 examination; failed to evaluate the overall adequacy and effectiveness of the Bank's BSA compliance program; and lacked sufficient information to reach a conclusion about the overall quality of the BSA compliance programs. In further support of this position, FDIC asserts that the Vivaldo's independence was compromised because she served in a dual and conflicting role as a consultant to the Bank.

a. Inadequate Quarterly Review

The FDIC argues that the 2012 Quarterly Report prepared by Vivaldo was inadequate in several respects. First, the evidence shows, and Vivaldo acknowledged, that the Quarterly Report did not contain an overall evaluation of the adequacy and effectiveness of the Bank's BSA/AML compliance program.⁵⁴ (Tr. 1067-1068.) Unlike prior quarterly reviews, it also lacked the phrase "Conditions for BSA/AML/OFAC, Flood Disaster and Reg. B are satisfactory." (Tr. 1068-1069; R. Exh. 30/1, 31/1 and 36/1.) Vivaldo testified that at some point in time she stopped doing overall evaluations on a quarterly basis because she thought it was redundant. ((Tr. 1069-1071.) She never explained to the Bank Board or anyone else why she changed the process. If nothing else, the omission of an overall assessment on a quarterly basis deprived the Bank Board the opportunity to make corrections in a timely manner.⁵⁵

The FDIC also asserts that the 2012 Quarterly Report lacked sufficient information to enable the examiners or other readers to reach a conclusion about the overall quality of the BSA/AML compliance

⁵⁴ Vivaldo's contract with the Bank specified that she would use regulatory guidance, e.g., FFIEC BSA/AML Examination Manual, to assist in performing her quarterly reviews. (R. Exh. 26/2, Jt. Exh. 2/2.) According to the FFIEC Manual, "independent testing" includes, among other things, an evaluation of the overall adequacy and effectiveness of the BSA/AML compliance program and at the very least sufficient information to allow a reviewer to reach a conclusion about the overall quality of the program. (FDIC Exh. 103 at 36.)

⁵⁵ In lieu of quarterly evaluations, Vivaldo added an "Annual BSA et al Review" section at the end of the 2010 and 2011 fourth quarter reviews. (R. Exh. 36/7, 27/9.) The evidence shows, however, that in December 2012, Vivaldo withdrew as the Bank's consultant and therefore she did not prepare a 2012 fourth quarter review with an annual BSA assessment. (Tr. 919, 925.)

program. The evidence shows that in comparison to the review made by Rawlins and Forgang, the Quarterly Report by Vivaldo did not address many of the BSA deficits noted by the examiners. For example, based on her review of 22 deposit accounts, Vivaldo opined without explanation that the “[n]ew account documentation shows considerable improvement over prior results.” Her report, however, did not identify which new deposit accounts were reviewed, explain how many were actually opened in 2012, or provide any details about what her review disclosed.⁵⁶ Although Vivaldo knew that the Bank had not engaged in monitoring and analyzing this activity for three months or more to establish a pattern of activity, as recommended in FDIC’s 2010 ROE, she failed to note this deficiency in her Quarterly Report. (Tr. 1117-18; R. Exhs. 27/12-13, 36/9.) Finally, with respect to Alan Chi’s appointment as the BSA Officer, the Quarterly Report does not assess his qualifications or discuss why the Bank did not recruit and/or interview any other candidates for the position.⁵⁷

The Bank argues that Vivaldo’s review was actually more comprehensive than the FDIC’s review because she, unlike Rawlins, reviewed documentation in the loan files in addition to information in the deposit account files.⁵⁸ (R. Reply Br., p. 24.) However, Vivaldo testified that she it was part of her practice to ask for the loan files because she was looking for more than BSA information as part of her audit review. (Tr. 1026- 1028.) Although she found some BSA related information in the loan files that she reviewed, she conceded that the deposit account files did not necessarily correlate to the loan files that

⁵⁶ Notably, the report states although she requested the new account information when the review began on July 24, 2012, all of the information was not provided until the last day of the review, July 31, 2012. Vivaldo commented in the report that it took the Bank an excessive amount of time to provide this information. (FDIC Exh. 5/6.)

⁵⁷ Nor did Vivaldo assess Alan Chi’s BSA qualifications in 2011 fourth quarter review where she recommended that the “Board should appoint Mr. Alan Chi as BSA Administrator.” (R. Exh. 27/3.)

⁵⁸ In an effort to deflect criticism of the adequacy of the 2012 Quarterly Report, the Bank further argues that Rawlins and Forgang could have, and should, have reviewed the Annual Report that was included in the 2011 fourth quarterly review. It was the Bank’s responsibility to provide all the information requested in a timely fashion during the 2012 examination, particularly after the FDIC gave clear notice of the reports that where necessary. The fact that a 2011 Annual Report was first mentioned in a telephone conference call at the end of examination process underscores the fact that the Bank failed to meet its obligation to provide this information. In any event, a careful review of the 2011 Annual Report offers the Bank no solace because there Vivaldo likewise did not inform the Board that (1) against her advice, Alan Chi changed the methodology used to risk rate customer deposit accounts which caused most new deposit accounts to fall into the “low-risk” range; (2) that against her advice, and contrary to the 2010 ROE BSA recommendations, Alan Chi altered the methodology used by the Bank to self-assess its overall risk, thereby resulting in a “low” rather than “medium or high” overall self-assessed risk; and (3) that contrary to the 2010 ROE BSA recommendations, the Bank failed to monitor and analyze aggregate activity over three months.

she reviewed. (Tr. 968-970, 971-973, 973-976.) Finally, Vivaldo did not state that she reviewed any loan files for the purpose of supplementing missing, inaccurate or incomplete BSA information in any deposit account file.

b. Vivaldo's Conflicting Roles

The FDIC also argues that Vivaldo had a conflict of interest which compromised her independence because she advised the Bank on various BSA areas and, at the same time, was responsible for auditing them. In her contract with the Bank and her quarterly reviews, Vivaldo refers to herself as "Consultant." In discussions with Rawlins during the 2012 examination, Vivaldo repeatedly referred to the Bank as "we."⁵⁹ (Tr. 180-81, 185; FDIC Exh. 32/47-48.) While the use of these terms is not outcome determinative, they support a reasonable inference that Vivaldo thought of herself as something more than simply an auditor.

Although the FFIEC Manual states that the person performing independent testing need not be specifically designated as an "auditor," it also states that the person "must not be involved in any part of the bank's BSA/AML compliance program." (FDIC Exh. 103/17, n.17.) That being said, the undisputed evidence shows that in 2006 Vivaldo wrote the Bank's BSA Policy Manual. (Tr. 1100.) As she explained, while the Bank previously had a BSA policy in place, she "took the pieces [and] reorganized them." She also "supplemented them with parts they should have and [she] brought it all up to date." (Tr. 1101.) She further testified that she provided these revisions to the policy pursuant to substantially the same agreement by which the Bank retained her services for the audit of the Bank in 2012. Each year, following her annual review of the Bank's policy, she would provide recommendations for the inclusion of updates and new information in the Bank's policy. (Tr. 1101, 1102-04.)

The evidence also shows that Vivaldo assisted the Bank in making certain corrections to Bank

⁵⁹ Vivaldo explained that she uses the term "we" whenever she addresses a bank that she is working with, because she thinks it is offensive simply to tell the bank what it is doing wrong. (Tr. 1117-18.) Of course in the context of her discussions with Rawlins, she was not addressing the Bank, but was explaining to a third-party examiner what the Bank did or did not do and why, thus giving the impression that she was fulfilling an "agency" role, rather than an "auditor" role.

policy following the 2010 examination. (Tr. 179, 1115-19.) Rawlins testified that, in her experience, such assistance by an auditor was unusual. Serving as a consultant creating and remediating the Bank's policies and as an auditor evaluating the policies she helped to put in place at minimum gives the appearance of a conflict of interest.

Equally compelling is the evidence of a robust ongoing email exchange between Vivaldo and Alan Chi concerning the changes Alan Chi made to the Bank's Risk Assessment form. As one example, on December 15, 2011, Vivaldo wrote:

Hi Alan,

I'm afraid you are wrong on both counts. I've explained what's wrong with the risk scoring and suggested a way around it.

The FFIEC BSA Examination Manual lists certain high risk accounts among which are the subject three accounts (lawyer, retail, import export).

If you ignore my advise. I must leave you to the tender mercies of the FDIC.

Joan

(R. FDIC Exh. 122/1.)

Thus, the preponderance of the evidence shows that Vivaldo often modulated between giving assistance and advice concerning the Bank's BSA compliance program and cross-checking the same program for compliance, thereby calling into question her independent status as a "Consultant" to the Bank. Stated otherwise, the preponderance of the evidence supports a reasonable inference that her independent judgment was tainted by her dual roles.

Accordingly, based on the preponderance of the evidence viewed as a whole, I find that Vivaldo's 2012 Quarterly Report was deficient, that she did have a conflict of interest, and that the Bank's independent testing was not adequate.

3. Third Pillar: BSA Compliance Officer

The Notice alleges, and the FDIC argues, that the Bank's Board of Directors failed to appoint a qualified person as BSA Officer, who could coordinate and monitor day-to-day compliance with the BSA.

Specifically, the FDIC asserts that Alan Chi did not have the knowledge, experience and training to serve as the Bank's BSA Officer. It further asserts that given his other positions at the Bank, Alan Chi did not have adequate time to fulfill to his BSA responsibilities and that his duties as Senior Credit Officer conflicted with his BSA Officer duties. Finally, the FDIC asserts that the Bank failed to appoint a back-up BSA Officer with adequate training.

a. Lack of Knowledge, Experience and Training

The FFIEC Manual states that a bank should designate a BSA compliance officer that is:

... fully knowledgeable of the BSA and all related regulations. The BSA compliance officer should also understand the bank's products, services, customers, entities, and geographic locations, and the potential money laundering and terrorist financing risks associated with those activities. The appointment of a BSA compliance officer is not sufficient to meet the regulatory requirement if that person does not have the expertise, authority, or time to satisfactorily complete the job.

(FDIC Exh. 103/37 (emphasis added).) The Bank's BSA Policy Manual likewise states that the Bank will designate "a bank officer with appropriate qualifications and experience as the BSA Administrator." (R. Exh. 10/8.)

The undisputed evidence shows that prior to being appointed as the BSA Officer, Alan Chi worked at the Bank for eight years primarily as a senior credit officer making loan determinations. (Tr. 877.) During that time he completed a compliance course which included a BSA overview component. In February 2011, he and Robert Zhao were appointed as backup BSA Administrators to BSA Officer Wenni Chung. (R. Exh. 36/2.) Although he testified that he attended a few bank examination exit meetings and was accustomed to reviewing batch reports as part of his senior credit officer duties, Alan Chi did not explain what he did as a backup BSA Officer or otherwise explain what qualified him to take over as the Bank's BSA Officer. Nor did the Bank present any evidence showing why Alan Chi was appointed to the BSA Officer position in January 2012 or explain why no one else was interviewed for the position.

Alan Chi's lack of BSA knowledge, experience and training is illustrated by his conduct from the time he became the "Acting" BSA Officer to the end of the 2012 examination. For example, the evidence shows that soon after becoming the "Acting" BSA Officer, Alan Chi altered the methodology used by the Bank to self-assess its own risk rating which decreased the Bank's self-assessed risk rating rather than increase it, as required by the 2010 ROE BSA findings. In doing so, Alan Chi rejected the advice of the Joan Vivaldo, the Bank's BSA consultant, and brushed aside her repeated warnings that the changes he implemented would be scrutinized and criticized by the FDIC. The undisputed evidence also shows that while he was the Bank's BSA Officer, the Bank failed to monitor and analyze aggregate activity over three months or more to establish patterns of suspicious activity as required by the 2010 ROE BSA findings. Instead, Alan Chi chose to rely solely on reviewing batch reports – a practice he followed as senior credit officer, rather than one he adopted to ensure BSA compliance.⁶⁰ In light of the fact that Alan Chi was aware of the 2010 ROE BSA findings, it reasonably follows that his failure to comply was attributable to a lack of BSA knowledge and experience. (Tr. 727, 807-808.)

In addition, the evidence supports a reasonable inference that Alan Chi failed to grasp the importance of the deposit account files to a BSA compliance review. Vivaldo complained to Alan Chi about the "excessive" amount of time it took the Bank to provide new account information for the 22 deposit accounts that she reviewed as part of her Quarterly review. (FDIC Exh. 5/6.) She also pointed out that there was no indication that Alan Chi, as BSA Officer, had reviewed each new deposit account immediately upon opening as required by Bank policy. *Id.* Even though he was prodded by Vivaldo to pay more attention to the deposit account files, many of the new deposit account files opened in 2012 were still missing BSA information six months later when Rawlins commenced the 2012 examination. Alan Chi responded to the poor condition of the deposit account files with a vague reference that some information might be contained in the loan files. His response does not explain why – as required by Bank

⁶⁰ In his testimony, Alan Chi never identified the BSA markers that he was looking for as he reviewed the batch reports, or what he did if and when he found one, or how his review of the batch reports differed, if at all, after he became "Acting" BSA Officer.

policy - the deposit account files were not updated with whatever pertinent BSA information was contained in the loan files. Nor does it explain why Alan Chi did not show EIC Rawlins the actual loan file(s) during the exam. His failure to address these deficiencies and to promptly provide Rawlins with the loan files that he believed might supplement the deposit account files reflects his lack of BSA knowledge and experience.

Thus, Alan Chi's conduct after he took over the BSA Officer position underscores the fact that he lacked the training, knowledge and experience to adequately perform the BSA Officer job.

b. Conflicting Responsibilities and Interests

In addition, the undisputed evidence also shows that notwithstanding his lack of BSA training, knowledge and experience, Alan Chi simultaneously assumed several other senior officer positions which hindered his ability to adequately perform the BSA Officer duties. At the time he was made the Bank's BSA Officer, Alan Chi, already was the Bank's Senior Credit Officer, which he conceded took up the majority of his day. (Tr. 647.) To make matters worse, the Bank Board also appointed him as the Bank's Chief Financial Officer, Internal Auditor, Operations Compliance Officer and member of the Bank's Directors and Officers Loan Committee. It is hard to imagine that he would have any time on a daily basis to carry out his BSA duties,⁶¹ particularly given his lack of training, knowledge and experience. Even Joan Vivaldo thought that Alan Chi had too many competing responsibilities.⁶² (Tr. 1111-1114; FDIC Exh. 134.)

⁶¹ The responsibilities of the Bank's BSA Officer, as set forth in the Bank's BSA Policy Manual, include coordinating Bank-wide BSA operating procedures, developing a formal BSA training program for Bank personnel, daily monitoring of the Bank's BSA/AML system to determine compliance with reporting requirements and detection of suspicious activity, and preparing various BSA/AML reports to the Board. (R. Exh. 10/8-9.)

⁶² In addition, the FDIC asserts that Alan Chi's role as Senior Credit Officer conflicted with his responsibilities as BSA Officer. (Tr. 211-13, 449-52.) In response, the Bank asserts that Alan Chi had no economic incentive to disregard potential illegal activity in order to make a loan, and that serving as senior credit officer allowed him to obtain a more thorough understanding of his customer's business. In very general terms, Alan Chi explained that he believed his duties as senior credit officer overlapped with his duties as BSA Officer. (Tr. 592, 647.) His comparison, in my view, was vague and self-serving. Moreover, the FFIEC Manual recommends that, as part of its internal controls, a bank should "[p]rovide for dual controls and the segregation of duties to the extent possible. For example, employees that complete the reporting forms (such as SARs, CTRs, and CTR exemptions) generally should not also be responsible for the decision to file the reports or grant the exemptions." (FDIC Exh. 103/34-35.) I find based on the evidence viewed as a whole that the Senior Credit Officer and BSA Officer are potentially conflicting management positions.

Accordingly, I find, based on the preponderance of the evidence viewed as a whole, that Alan Chi lacked the knowledge, experience, training and time to adequately monitor and coordinate the BSA compliance program as required section 326.8(c)(3) of the FDIC Rules and Regulations. 12 C.F.R. § 326.8(c)(3).

c. Absence of a Back-up BSA Officer

Finally, the Notice alleges, and the FDIC argues, that the Bank failed to appoint a back-up BSA officer. According to Rawlins' unrebutted testimony a back-up BSA Officer is important in the event that the appointed BSA Officer is unavailable to oversee the Bank's BSA compliance. (Tr. 214.) The evidence shows that on February 25, 2011, Alan Chi and Robert Zhao were appointed as backup BSA Administrators. (R. Exh. 36.2.) However, there is no evidence that Robert Zhao continued in that role after Alan Chi was appointed as BSA Officer. In her 2012 Quarterly Report, Vivaldo does not identify Robert Zhao as part of the "BSA team, including Ms. Abbey Yang, Mr. Jimmy Phang and Fremont." (Jt. Exh. 3/1.) Although Alan Chi considered Jimmy Phang to be the back-up BSA Officer, there is no evidence that he or any one else was ever appointed to that position. (Tr. 214-215.) According, I find that the Bank failed to appoint a backup BSA Officer.

4. Fourth Pillar: Lack of Appropriate BSA Training

The Notice alleges, and the FDIC argues, that the Bank failed to provide its staff with adequate BSA training, as Alan Chi, the provider of the training, lacked sufficient qualifications to provide such training, the training was not tailored to employee positions of job functions, and the training materials for 2012 contained incorrect information and failed to incorporate the majority of the Bank's BSA and AML policy.

The FFIEC Manual provides the following guidance regarding training:

Banks must ensure that appropriate personnel are trained in applicable aspects of the BSA. Training should include regulatory requirements and the bank's internal BSA/AML policies, procedures, and processes. At a minimum, the bank's training program must provide training for all personnel whose duties require knowledge of the BSA. The training should be tailored to the person's specific responsibilities. ... The BSA compliance officer

should receive periodic training that is relevant and appropriate given changes to regulatory requirements as well as the activities and overall BSA/AML risk profile of the bank.

...

Training should be ongoing and incorporate current developments and changes to the BSA and any related regulations. Changes to internal policies, procedures, processes, and monitoring systems should also be covered during training. The training program should reinforce the importance that the board and senior management place on their bank's compliance with the BSA and ensure that all employees understand their role in maintaining an effective BSA/AML compliance program.

Examples of money laundering activity and suspicious activity monitoring and reporting can and should be tailored to each individual audience. For example, training for tellers should focus on examples involving large currency transactions or other suspicious activities; training for the loan department should provide examples involving money laundering through lending arrangements.

(FDIC Exh. 103/38 (emphasis added).)

The Bank's BSA Policy Manual likewise states that "training will be appropriate for the position and function of each person trained," and "[a]t a minimum, Bank policies and procedures will be covered as well as new governmental rules and regulations. Training will include coverage of different forms of money laundering and terrorist financing as it relates to identification and example of suspicious activity. Training will also include a discussion of the penalties for non-compliance with Bank policy and procedures and government rules and regulations, i.e. employee counseling or termination, government sanctions, fines or imprisonment." (R. Exh. 10/32.)

a. BSA Officer Qualifications

As BSA Officer, Alan Chi was responsible for providing training on the BSA to Bank staff and Board members. (Tr. 217, 798, 807.) Because he was not qualified to serve as the Bank's BSA Officer, it reasonably follows that Alan Chi lacked the qualifications to provide adequate BSA-related training for others. (Tr. 230, 453.)

b. Training Tailored to Job Functions

Contrary to the guidance of both the FFIEC Manual and the Bank's BSA Policy Manual, the evidence also shows that all Bank employees received the same training, regardless of their positions. (Tr.

229, 807, 809-10, 813-817, 819-823; R. Exhs. 19/1, 20/1, 21/1, 23/1, 24/1 & 25/1.) EIC Rawlins

emphasized the importance of targeting training to the specific responsibilities of each employee:

[Y]ou should provide specific training based off the position so that the employee understands what's expected of them in their position to help the bank with their compliance with BSA as a whole. So, for instance, the types of suspicious behavior or suspicious activity that a teller may run across are going to be different than that [which] a loan officer runs across or can identify. So that should be brought out in BSA training so that they can differentiate and just better be able to comply with the BSA in their particular position that they hold.

(Tr. 229-30.) CSMA Wong concurred that the Bank's training should have been tailored to specific positions, but was not. (Tr. 453.)

In addition, in 2012, Alan Chi and other Bank employees attended an outside webinar entitled "Required Compliance Series: Regulatory Compliance for the Frontline." (Tr. 812, 1008-09; FDIC Exh. 36.) EIC Rawlins testified that this webinar provided only rudimentary BSA training to front-line Bank staff such as tellers. It did not take into account the specific positions and functions of Bank personnel in attendance, and in particular, it was not appropriate training for someone in Alan Chi's position as BSA Officer. (Tr. 204-06.)

The Bank argues that it has a very small workforce, whose responsibilities overlap and, therefore, targeted training was unnecessary.⁶³ (R. Reply Br., 35-36.) Both the FFIEC Manual and the Bank's BSA Policy Manual specify that training should be tailored to the position and function of the employee. (FDIC Exh. 103/38; R. Exh. 10/32.) Thus, the Bank itself, through its Board, has rejected the notion that all Bank employees should receive the same training. Because the Bank's BSA training was not targeted to each employees' role, the evidence shows that the training was inadequate in this respect.

c. Adequacy of Training Materials

According to the Bank's employee training schedule, Alan Chi provided the following BSA-related training in 2012: cash purchase and monetary instruments (February), anti-money laundering

⁶³ The evidence shows that the Bank had high workforce turnover, which heightens the underlying problem of failing to tailor training to specific positions. (Tr. 281 .)

(March), suspicious activity monitoring and suspicious activity (April), currency transaction reports, multiple currency transactions, and filing of OFAC policy and procedures (June), international department correspondent banking (July), wire procedures (September), CTR recordkeeping (October), customer due diligence and customer identification program (November). (Tr. 218-19; FDIC Exh. 5/13.)

As per the 2010 ROE BSA recommendations, Alan Chi prepared quizzes to go with each lesson. (Tr. 808; FDIC Exh. 136/11; R. Exhs. 19-21, 23-25.) A review of the training materials and accompanying quizzes reveal that they contained inaccurate or irrelevant information. For example, one of the questions in a multiple-choice quiz administered in April 2012 did not offer a correct answer. (Tr. 223-24, 1152.) In another lesson, Alan Chi distributed a quick reference guide for money-services businesses, even though the Bank is not a money-services business. (Tr. 224-26.)

In addition, the Bank's employee training did not cover the Bank's own BSA policies, procedures, and processes, as required the FFIEC Manual and the Bank's BSA Policy Manual. (Tr. 226-29, 230-31; FDIC Exh. 103/38; R. Exh. 10/32.) In an attempt to justify this important omission, Alan Chi testified that he provided the Bank's BSA Policy Manual to the employees in connection with some of the trainings and expected them to read the manual and pass the related test.⁶⁴ (Tr. 821-822; R. Exhs. 23/1, 24/1, 25/1.) There is no evidence, however, showing whether that approach was successful and more importantly whether any employee had a working knowledge of the Bank's BSA policies.

The Bank argues that the FDIC ignores the fact that the training conducted in 2012 reflected substantial improvement over the training conducted in 2010, and that by 2012, Alan Chi had implemented a number of the recommendations made by the FDIC, including providing training to the Board of Directors and creating written records of the courses provided to officers and employees of the Bank. (Tr. 655-56; R. Exh. 3/11.) The fact that the Bank improved certain aspects of its training is commendable, and will facilitate the continued improvement of the program. However, by adding training

⁶⁴ In reality the employee were given a copy of a "BSA AML OFAC Policy," which according to Alan Chi was the Bank's BSA Policy Manual. (Tr. 818, 821-22.)

components which are incorrect or inadequate, the Bank has not necessarily made a net improvement and will not be immune from further criticism in this regard.

The Bank also argues that employees received on the job training from Alan Chi. (R. Reply Br., p. 35; *see also* Tr. 648, 799, 1009-11.) Such training, while necessary, cannot be substituted for the formal, structured training program anticipated by the FFIEC and Bank's BSA Manuals. Finally, the Bank argues that its effectiveness in training its employees should not be measured by its lessons and quizzes, but by whether customers of the Bank were able to conduct illegal activities through the Bank. BSA regulations, however, require that the Bank "provide training for appropriate personnel," 12 C.F.R. § 326.8(c)(4), and the FFIEC Manual fleshes out what the training should consist of. There is no requirement that the FDIC demonstrate a raft of illegal activity conducted through the Bank in order to prove a violation of this pillar.

The evidence shows that Alan Chi was not qualified to provide the rest of the Bank staff with training, and that the training provided was not geared toward each employee's role in the organization. While the errors in the materials provided by the Bank alone might not be sufficient to demonstrate a violation of this pillar, the evidence taken as a whole demonstrates that the Bank did not provide its staff with adequate BSA training.

H. The Bank's Ancillary Defenses

Various ancillary defenses that are interlaced throughout the Respondent's post-hearing and reply briefs are addressed below.

1. Bias

The Bank argues that the FDIC's 2012 examination was biased from the beginning. In support of this contention, it points to a statement in the Pre-Examination Planning Report which originally read: "Examination resources will be directed towards assessing internal control deficiencies due to the presence of a dominant influence and ensuring the bank establishes mitigating controls." (R. Exh. 39/4 (emphasis added); Tr. 328-30.) Following her review of the Pre-Examination Planning Memo, Rawlins

promptly corrected the sentence to read: “Examination resources will be directed towards assessing internal control issues due to the presence of a dominant influence and ensuring management has established mitigating controls.” (*Id.*)

In addition, the Bank refers to two emails authored by Examiner Forgang. In one, he wrote: “I wouldn’t be surprised if I find some BSA issues and potential violations regarding their CDD/EDD and perhaps issues with their SAM.” (R. Exh. 38/1.) In another, Forgang disseminated quotes attributed to Richard and Alan Chi and one of the Bank’s Directors. (R. Exh. 41.) Other than these examples, the Bank points to no evidence that the FDIC examiners deviated from their normal examination procedures or manipulated the data.

The countervailing evidence shows that at the outset of the 2012 exam Rawlins accommodated the Bank by substituting deposit account folders; that throughout the onsite exam she and Forgang interacted with Alan Chi in an effort to obtain a better understanding of various transactions, to provide him an opportunity to put things in proper context, and to relate to him on an ongoing basis problematic issues, rather than waiting to disclose them at the end of the exam. The evidence also shows that in many respect the concerns articulated by the examiners were echoed previously and privately to Alan Chi (to no avail) which underscores the fact that these concerns were not “trumped up.” Most notably, when CMSA Wong advised Rawlins that her preliminary ROE findings that a SAR violation based on [REDACTED] was unsupported, she recommended that it be omitted from the final report stating, “we do not want to cite anything that we cannot support 1000%.” (R. Exh. 43/1.)

Accordingly, I find, based on preponderance of the evidence viewed as a whole, the Respondent’s bias defense lacks merit.

2. Lack of Fair Notice of Conduct Required

Respondent argues that the BSA and its applicable regulations fail to give adequate notice of the conduct required of a bank in violation of the Bank’s due process. The short response to this assertion is that the conduct required of the Bank to comply with the BSA and its applicable regulations is identified

in the Bank's own BSA Policy Manual, which repeatedly quotes and references the law, regulations, and FFIEC Manual reflecting that the Bank knew precisely the conduct that was required and expected by the federal regulator in order to comply with the BSA. Suffice it to say, if the Bank had read and complied with its own BSA Policy Manual, it is very unlikely that the instant case would have resulted. The Lack of Fair Notice defense is unavailing.

3. FFIEC BSA Manual Is Not a Law or Regulation

The Respondent argues that the FFIEC BSA/AML Examination Manual does not have the effect of law or regulation and therefore does not establish prescriptive standards or requirements. While that may be true, it is not gainsaid that the Manual is recognized throughout the industry as the foremost guide to bank examiners and banks on identifying and controlling risks associated with money laundering and terrorist financing, and for carrying out the BSA. It provides supervisory guidance to banks to help them develop and provide a compliance program that meets the requirements of the BSA.

Both Rawlins and Wong testified that it is an industry-wide practice for banks to use the FFIEC Manual as a guide for compliance with the BSA. (Tr. 59-60, 433.) The evidence discloses that at all times pertinent herein, the Bank was aware and relied heavily on the FFIEC Manual in structuring its BSA Compliance Program – at least in theory. The Bank's BSA Policy Manual incorporates numerous references to the FFIEC Manual, and even appends a section of the FFIEC BSA Manual to its BSA Policy Manual as an exhibit. (R. Exh. 10/38, 42, 51, 66-76.)

The Bank's engagement letter with its consultant/auditor Joan Vivaldo required her to "use regulatory, e.g., FFIEC BSA/AML Examination Manual" in conducting her review and assessment of the Bank's BSA/AML Compliance Program. (Jt. Exh. 2/2.) Furthermore, Vivaldo testified that the FFIEC Manual is "an authority for BSA" and that the Bank "had copies of the FFIEC BSA examination manual scattered all over the Bank." (Tr. 1003, 1039.) Additionally, Vivaldo's engagement letter incorporated sections of an earlier FDIC Financial Institution Letter, which contained the same points as the FFIEC Manual. She also based the request list for her compliance audit on items suggested in the FFIEC Manual.

(Tr. 923-24, 931.) Thus, the evidence reflects that the Bank's Board and its auditor/consultant considered the FFIEC Manual to be a roadmap for successful execution of its BSA Compliance Program.

Thus, the importance of the FFIEC BSA/AML Examination Manual cannot be understated or undermined.

4. Prior Examinations

The Bank asserts that most of its internal controls have been in place for a number of years, have been subject to review by the FDIC, and have not previously been found so deficient that they violated the BSA. (R. Prop. FOF ¶ 30; R. Br., p. 10; R. Reply Br., p. 5-6.) The argument is unconvincing for several reasons. First, the FDIC largely criticizes the Bank's application and implementation of its policies and procedures, or lack thereof, under Alan Chi's leadership, and not the policies and procedures themselves as written. Second, the FDIC is not the Bank's auditor. It conducts a limited review of the Bank's BSA policies and procedures as part of its overall safety and soundness examinations. The FDIC is not estopped nor will it be found to have "waived" claims against the Bank because they were not raised in prior examinations. *de la Fuente II v. FDIC*, 332 F.2d 1208, 1220 (9th Cir. 2003); *FDIC v. Baker*, 739 F. Supp. 1401 (C.D. Cal. 1990). Finally, to the extent any of the Bank's internal controls were criticized in the 2010 examination, and were not corrected, the FDIC is required by statute to seek a cease and desist order to correct those conditions. *See* 12 U.S.C. § 1818(s)(3)(B) (mandating that, if the FDIC determines that a depository institution "has failed to correct any problem with the procedures maintained by such depository institution which was previously reported to the depository institution by [the FDIC]," it "shall" issue a cease and desist order). Therefore, the fact that the Bank's policies and procedures had been in place prior to this proceeding does not mean that the Bank has not violated the BSA. The Respondent's reliance on this defense is misplaced.

Conclusion

The Bank is, and at all times relevant to this proceeding has been, a corporation organized, existing, and doing business under the laws of the State of California with its principal place of business

APPENDIX "A"

FEDERAL DEPOSIT INSURANCE CORPORATION

WASHINGTON, D.C.

_____)
)
 In the Matter of)
)
 CALIFORNIA PACIFIC BANK)
 SAN FRANCISCO, CALIFORNIA)
)
 (INSURED STATE NONMEMBER BANK))
)
 _____)

ORDER TO
CEASE AND DESIST

FDIC-13-094b

IT IS HEREBY ORDERED that California Pacific Bank, San Francisco, California ("Bank"), its directors, officers, employees, agents, or other institution-affiliated parties (as that term is defined in Section 3(u) of the Federal Deposit Insurance Act, 12 U.S.C. § 1813(u)), and its successors and assigns cease and desist from the following violations of the Bank Secrecy Act, 31 U.S.C. §§ 5311-5314, 5316-5332, 12 U.S.C. § 1829b, 12 U.S.C. §§ 1951-1959 and 12 U.S.C. § 1818(s), and its implementing regulations, 31 C.F.R. Chapter X (effective March 1, 2011), section 326.8 and 12 C.F.R. Part 353 of the Rules and Regulations of the FDIC, 12 C.F.R. § 326.8 and 12 C.F.R. Part 353 (collectively the "BSA"):

- (a) Operating in violation of section 326.8 of the Rules and Regulations of the FDIC, 12 C.F.R. § 326.8, by failing to provide for the continued administration of a written, board-approved BSA compliance program in connection with the following:

- (1) Failure to establish a system of internal controls to assure ongoing compliance;

- (2) Failure to provide for independent testing for compliance conducted by Bank personnel or by an outside party;
- (3) Failure to designate an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and
- (4) Failure to provide training for appropriate personnel.

(b) Operating in violation of Part 353 of the Rules and Regulations of the FDIC, 12 C.F.R. Part 353, in connection with the failure to file a Suspicious Activity Report ("SAR").

1. Within 60 days of the effective date of this ORDER, the Bank shall comply in all material respects with the BSA and its rules and regulations.

2. Within 60 days of the effective date of this ORDER, the Bank shall develop, adopt, and implement a written compliance program, as required by the applicable provisions of section 326.8 of the FDIC's Rules and Regulations, 12 C.F.R. § 326.8, designed to, among other things, ensure and maintain compliance by the Bank with the BSA and the rules and regulations issued pursuant thereto. The program shall ensure that clear and comprehensive BSA compliance reports are provided to the Bank's Board of Directors ("Board") on a monthly basis. Such program and its implementation shall be in a manner acceptable to the Regional Director of the FDIC's San Francisco Regional Office ("Regional Director") as determined at subsequent examinations and/or visitations of the Bank. At a minimum, the program shall:

(a) Establish a system of internal controls to ensure compliance with the BSA and the rules and regulations issued pursuant thereto, including policies and procedures to detect

and monitor all transactions to ensure that they are not being conducted for illegitimate purposes and that there is full compliance with all applicable laws and regulations.

(b) Provide for independent testing of compliance with the BSA, all applicable rules and regulations related to the BSA, and the reporting of suspicious transactions required to be reported pursuant to Part 353 of the FDIC's Rules and Regulations, 12 C.F.R. Part 353. The independent testing shall be conducted on an annual basis and in accordance with the procedures described in the current/applicable Federal Financial Institutions Examination Council ("FFIEC") BSA/AML Examination Manual. The independent testing, at a minimum, should address the following:

- (i) overall integrity and effectiveness of the BSA/AML compliance program, including policies, procedures, and processes;
- (ii) BSA/AML risk assessment;
- (iii) BSA reporting and recordkeeping requirements;
- (iv) Customer Identification Program implementation;
- (v) adequacy of customer due diligence policies, procedure, and processes and whether they comply with internal requirements;
- (vi) personnel adherence to the Bank's BSA/AML policies, procedures, and processes;
- (vii) appropriate transaction testing, with particular emphasis on high-risk operations (products, service, customers, and geographic locations);
- (viii) training adequacy, including its comprehensiveness, accuracy of materials, the training schedule, and attendance tracking;

(ix) integrity and accuracy of management information systems used in the BSA/AML compliance program;

(x) an evaluation of management's efforts to resolve violations and deficiencies noted in the previous tests or audits and regulatory examinations;

(xi) an assessment of the overall process for identifying and reporting suspicious activity, including a review of filed or prepared SARs to determine their accuracy, timeliness, completeness, and effectiveness of the Bank's policy; and

(xii) a review of the methodology used to risk rate accounts.

(c) Written reports shall be prepared which document the testing results and provide recommendations for improvement. Such reports shall be presented to the Bank's Board.

(d) Ensure that the Bank's BSA compliance program is managed by a qualified officer who has the required authority, responsibility, training, resources, and management reporting structure to ensure compliance with the Bank's BSA program requirements and BSA-related regulations, including without limitation:

(i) the identification of timely, accurate and complete reporting to law enforcement and supervisory authorities of unusual or suspicious activity or known or suspected criminal activity perpetrated against or involving the Bank; and

(ii) monitoring the Bank's compliance and ensuring that full and complete corrective action is taken with respect to previously identified violations and deficiencies.

(e) Provide and document training by competent staff and/or independent contractors of all Bank's Board members and all appropriate personnel, including, without

limitation, senior management, tellers, customer service representatives, lending officers, and all other customer contact personnel, in all aspects of regulatory and internal policies and procedures related to the BSA, with a specific concentration on accurate recordkeeping, form completion and the detection and reporting of known and/or suspected criminal activity. Training shall be updated on a regular basis to ensure that all personnel are provided with the most current and up to date information.

3. Within 60 days of the effective date of this ORDER, the Bank shall develop, adopt, and implement a written customer due diligence program, which shall include employees and directors at the Bank. Such program and its implementation shall be in a manner acceptable to the Regional Director as determined at subsequent examinations and/or visitations of the Bank. At a minimum, the customer due diligence program shall provide for the following:

(a) A risk focused assessment of the customer base of the Bank, including employees and directors at the Bank, to determine the appropriate level of enhanced due diligence necessary for those categories of customers, employees and directors that the Bank has reason to believe pose a heightened risk of illicit activities at or through the Bank.

(b) For those customers, employees and directors whose transactions require enhanced due diligence, procedures to:

(i) determine the appropriate documentation necessary to confirm the identity and business activities of the customer, employee and director;

(ii) understand the normal and expected transactions of the customer, employee, and director; and

(iii) reasonably ensure the identification and timely, accurate and complete reporting of known or suspected criminal activity against or involving the Bank to law

enforcement and supervisory authorities, as required by the suspicious activity reporting provisions of Part 353 of the FDIC's Rules and Regulations, 12 C.F.R. Part 353.

4. (a) Within 60 days of the effective date of this ORDER, the Bank shall establish and implement policies and procedures to advise the Bank's Board of SARs. At a minimum, the Bank's Board shall be advised in detail of all SARs involving employees, contractors, officers, and directors. The policies and procedures shall also include guidelines to determine what SARs are significant.

(b) The Bank shall establish and implement policies and procedures to ensure that SARs are filed within 30 days of identifying a suspect or unusual and suspicious activity (or a total of 60 days if a suspect is unknown or once per quarter for ongoing transactions). Such a program must also ensure that timely identification of suspicious activity occurs; that timely investigation into unusual activity is undertaken; that related accounts are considered and discussed in the SARs filing; that a detailed, accurate, comprehensive, and readable narrative description of the activity is included in the SARs filing; and that Bank management maintain adequate written information to support a decision not to file a SAR as a result of any investigation of a suspect or unusual and suspicious activity.

5. (a) Within 60 days of the effective date of this ORDER, the Bank's Board audit committee shall oversee the Bank's compliance with the BSA and Parts 326 and 353 of the FDIC's Rules and Regulations. The committee shall receive reports from the qualified officer appointed in Paragraph 2(d) regarding compliance with the BSA and Parts 326 and 353, at least monthly, and shall report to the Bank's Board at every meeting.

(b) Following the effective date of this ORDER, the Bank's Board shall monitor and confirm the completion of actions taken by management to comply with the terms

of this ORDER. The Bank's Board shall certify in writing to the Regional Director when all of the above actions have been accomplished. All actions taken by the Bank's Board pursuant to this ORDER shall be duly noted in the minutes of its meetings. The committee shall receive reports from the qualified officer appointed in Paragraph 2(d) regarding compliance with the BSA and Parts 326 and 353, at least monthly, and shall report to the Bank's Board at every meeting.

6. Within 150 days from the effective date of this ORDER, the Bank's Board shall develop and implement a plan to review all high-risk accounts and high-risk transactions ("Transaction Review"), including but not limited to the Bank's large currency transaction reports ("CTRs"), cash purchases of monetary instruments, wire transfer activity, and foreign exchange services for the six-month period immediately preceding the effective date of this Order (the "Transaction Review Period"), and shall prepare and file any additional CTRs and SARs necessary based upon the review. Based upon the results of the review, the Regional Director may extend the Transaction Review Period if necessary.

(a) Within 60 days of preparing a plan for the Transaction Review, but prior to commencement of the Transaction Review, the Bank shall submit to the Regional Director a written plan for approval that sets forth:

- (i) the scope of the Transaction Review, including the types of accounts and transactions to be reviewed;
- (ii) the methodology for conducting the Transaction Review, including any sampling procedures to be followed;
- (iii) the expertise and resources to be dedicated to the Transaction Review;

(iv) the anticipated date of completion of the Transaction Review;

and

(v) a commitment that any interim reports, draft reports or workpapers associated with the Transaction Review will be made available to the Regional Director upon request.

(b) On completion of the reviews required pursuant to the paragraphs above, the Bank shall submit the written findings of the review and copies of any additional SARs and CTRs filed to the Regional Director.

(c) Throughout the Transaction Review, the Bank shall ensure that all matters or transactions required to be reported that have not previously been reported are reported in accordance with applicable rules and regulations.

(d) Documentation supporting any determination made pursuant to the paragraphs above shall be retained in the Bank's records for such period of time as may be required by any applicable rules or regulations.

7. Within 30 days of the end of the first quarter, following the effective date of this ORDER, and within 30 days of the end of each quarter thereafter, the Bank shall furnish written progress reports to the Regional Director detailing the form and manner of any actions taken to secure compliance with this ORDER and the results thereof. Such reports may be discontinued when the corrections required by this ORDER have been accomplished and the Regional Director has released the Bank in writing from making further reports.

8. Following the effective date of this ORDER, the Bank shall send to its shareholder(s) or otherwise furnish a description of this ORDER in conjunction with the Bank's next shareholder communication and also in conjunction with its notice or proxy statement

preceding the Bank's next shareholder meeting. The description shall fully describe the ORDER in all material respects. The description and any accompanying communication, statement, or notice shall be sent to the FDIC, Accounting and Securities Section, Washington, D.C. 20429, at least 15 days prior to dissemination to shareholders. Any changes requested to be made by the FDIC shall be made prior to dissemination of the description, communication, notice, or statement.

This ORDER shall not bar, estop, or otherwise prevent the FDIC, or any other federal or state agency or department from taking any other action against the Bank, the Bank's current or former institution-affiliated parties, and/or any of their respective directors, officers, employees, and agents, including, but not limited to, the imposition of civil money penalties.

This ORDER shall be effective on the date of issuance.

The provisions of this ORDER shall be binding upon the Bank, its institution-affiliated parties, and any successors and assigns thereof.

The provisions of this ORDER shall remain effective and enforceable except to the extent that, and until such time as, any provisions of this ORDER shall have been modified, terminated, suspended, or set aside in writing.

By direction of the Board of Directors.

Dated this _____ day of _____, 2015
Washington DC

Executive Secretary
Federal Deposit Insurance Corporation