

DEPARTMENT OF THE TREASURY

Notice of Finding That Liberty Reserve S.A. Is a Financial Institution of Primary Money Laundering Concern

AGENCY: Financial Crimes Enforcement Network, Treasury (FinCEN).

ACTION: Notice of finding.

SUMMARY: This document provides notice that, pursuant to the authority contained in 31 U.S.C. 5318A, the Director of FinCEN found on May 28, 2013, that Liberty Reserve S.A. (Liberty Reserve) is a financial institution operating outside the United States that is of primary money laundering concern.

DATES: The finding referred to in this notice was effective as of May 28, 2013.

FOR FURTHER INFORMATION CONTACT: FinCEN, (800) 949-2732.

SUPPLEMENTARY INFORMATION:

I. Statutory Provisions

On October 26, 2001, the President signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (the USA PATRIOT Act), Public Law 107-56. Title III of the USA PATRIOT Act amends the anti-money laundering provisions of the Bank Secrecy Act (BSA), codified at 12 U.S.C. 1829b, 12 U.S.C 1951-1959, and 31 U.S.C. 5311-5314, 5316-5332, to promote the prevention, detection, and prosecution of international money laundering and the financing of terrorism. Regulations implementing the BSA appear at 31 CFR Chapter X. The authority of the Secretary of the Treasury (the Secretary) to

administer the BSA and its implementing regulations has been delegated to the Director of FinCEN.

Section 311 of the USA PATRIOT Act (Section 311), codified at 31 U.S.C. 5318A, grants the Secretary the authority, upon finding that reasonable grounds exist for concluding that a foreign jurisdiction, financial institution, class of transaction, or type of account is of “primary money laundering concern,” to require domestic financial institutions and financial agencies to take certain “special measures” to address the primary money laundering concern. The Secretary has delegated this authority under Section 311 to the Director of FinCEN.

On May 28, 2013, the Director of FinCEN found that Liberty Reserve S.A. (Liberty Reserve) is a financial institution operating outside the United States that is of primary money laundering concern. The Director considered the factors discussed below in making this determination.

II. The Extent to Which Liberty Reserve Has Been Used to Facilitate or Promote Money Laundering in or Through Costa Rica and Internationally.

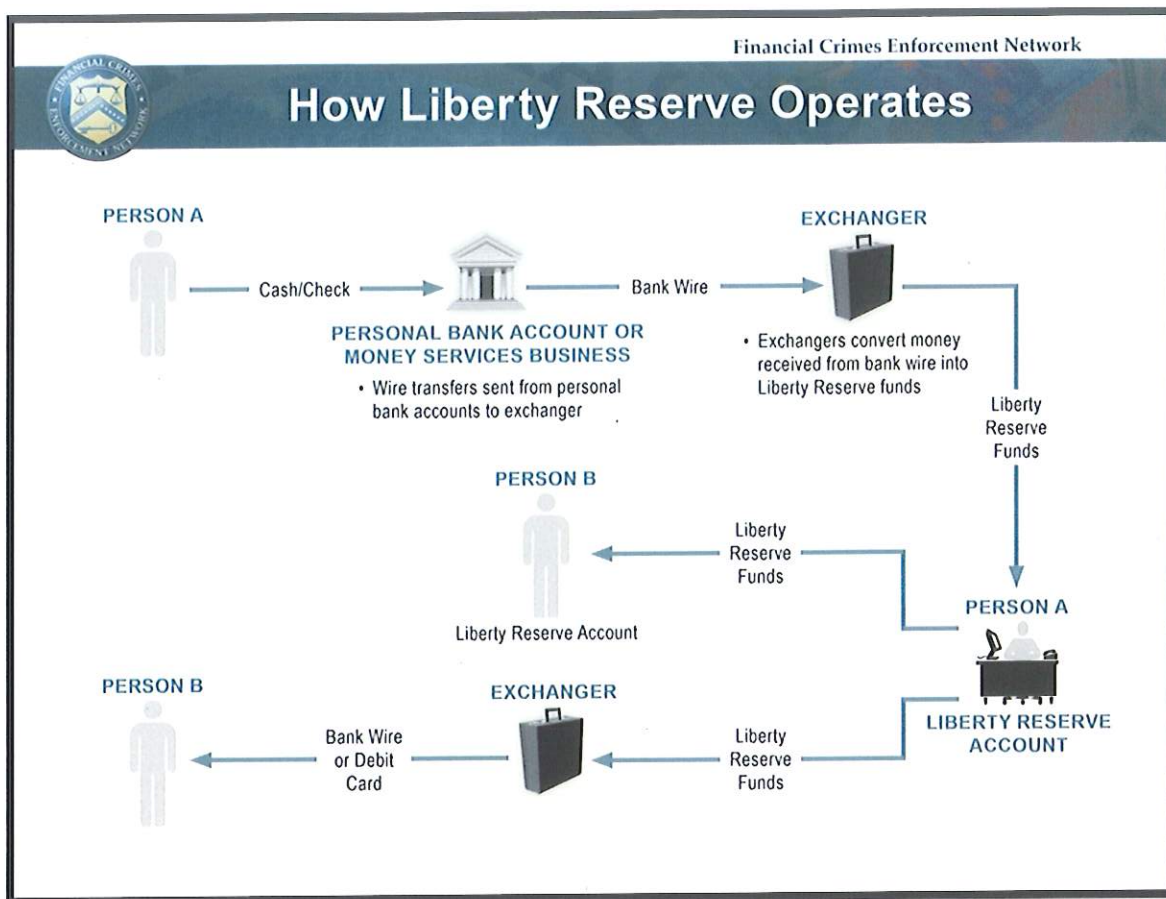
Liberty Reserve is a web-based money transfer system, or “virtual currency.” It is a financial institution currently registered in Costa Rica and has been operating since 2001. Liberty Reserve’s system is structured so as to facilitate money laundering and other criminal activity, while making any legitimate use economically unreasonable. The Department of Justice is taking criminal action against Liberty Reserve and related individuals.

Liberty Reserve uses a system of internal accounts and a network of virtual currency exchangers to move funds. Operating under the domain name www.libertyreserve.com, it maintains accounts for registered users. Users fund their

accounts by ordering a bank wire or money services business (MSB) transfer to the bank of a Liberty Reserve exchanger. Users can also fund Liberty Reserve accounts by depositing cash, postal money orders, or checks directly into the exchanger's bank account. The exchanger then credits a corresponding value to the user's Liberty Reserve account, denominated in "Liberty Reserve Dollars" or "Liberty Reserve Euros." Liberty Reserve claims to maintain Dollar for Dollar and Euro for Euro reserves to back their virtual currencies.

To withdraw funds, the user instructs Liberty Reserve to send funds from the user's Liberty Reserve account to a Liberty Reserve exchanger, which then sends a bank wire, MSB transfer, or other transfer method to the user's or recipient's bank account in U.S. dollars or other major currencies. The exchangers are independent MSBs operating around the world. They charge a commission on each transfer to and from the Liberty Reserve system.

Once funded, the Liberty Reserve virtual currency can be transferred among accounts within the Liberty Reserve system. The transfers are anonymous, and the recipient only sees the account number from which the funds were transferred. For an additional fee, even that information can be eliminated for greater anonymity.



A. History and Ownership

According to reporting of a Planetgold.com interview in 2003 with Arthur Budovsky, who founded the company, Liberty Reserve was then based in Nevis and began as a private exchange system for import/export businesses. In 2002, Budovsky and another individual, Vladimir Kats, set up several other companies, including GoldAge Inc., according to the New York County District Attorney's Office. GoldAge served as a prominent exchanger for E-Gold, a gold-based virtual currency system. E-Gold was charged with money laundering and operating an illegal MSB, and pled guilty in 2008. Similar to how Liberty Reserve operates, customers opened online GoldAge accounts with only limited identification documentation and then could choose their method of

payment, including wire transfers, cash deposits, postal money orders, or checks, to GoldAge to buy digital gold-based currency. GoldAge customers could withdraw their funds by wire transfers to anywhere in the world or by having checks sent to an individual.

In March 2004, Liberty Reserve's website indicated that it was operating out of Brooklyn, New York. In May 2006, Liberty Reserve was re-registered in Costa Rica. In July 2006, Budovsky and Kats were indicted by the state of New York for operating an illegal money transmitting business, GoldAge, out of their Brooklyn apartments. By that date, the defendants had transmitted at least \$30 million through GoldAge to digital currency accounts globally since 2002. Budovsky pled guilty and was sentenced to five years of probation.

B. Liberty Reserve Seeks Out Jurisdictions With Weak Regulatory Environments.

According to the 2012 International Narcotics Control Strategy Report (INCSR) prepared by the U.S. Department of State, money laundering in Costa Rica occurs across the formal and non-formal financial sectors, especially via both licensed and unlicensed money remitters. According to the 2013 INCSR, although Costa Rica continues to take steps to enforce its financial and non-financial regulatory regimes to prevent and detect money laundering, money remittance services remain a sector of particular concern. The INCSR notes that "Costa Rica is primarily used by foreign organizations as a bridge to send funds to and from other jurisdictions using bulk cash shipments and companies or financial institutions located offshore."

The 2007 INCSR noted that "[r]eforms in 2002 to the Costa Rican counternarcotics law expand the scope of anti-money laundering regulations, but also

create an invitation to launder funds by eliminating the government's licensing and supervision of casinos, jewelers, realtors, attorneys, and other nonbank financial institutions." While some progress has been made since that time, regulation of this sector remains a concern. Thus, when Liberty Reserve moved its registration to Costa Rica in 2006, Costa Rica was commonly known to have inadequate regulation of non-bank financial institutions, including MSBs and internet businesses.

In October 2007, Liberty Reserve's official blog explained that registering in Costa Rica allowed the company to avoid U.S. authorities because Costa Rica does not have a mutual legal assistance treaty with the United States. Taken together, these facts suggest that Liberty Reserve has specifically sought out jurisdictions with weak anti-money laundering controls and apparent immunity from U.S. prosecution.

C. Liberty Reserve Is Designed to Facilitate Money Laundering and Illicit Finance.

To open an account through the Liberty Reserve website, a user is asked to enter basic identifying information, such as name, e-mail address, and date of birth. Liberty Reserve does not require users to validate any of that information. Users are also able to open as many accounts as they want. Liberty Reserve requires only a working, even if anonymous, email address. Once a user has an account with Liberty Reserve, its anti-money laundering policy (AML policy) does not suggest that it either requires or verifies any information associated with any transaction.

This lack of customer due diligence means that the accounts can be entirely anonymous and thus that account holders can transfer funds to or from anywhere with anyone with anonymity. Indeed, Liberty Reserve advertises this fact as a virtue of the service. The deliberate lack of verification makes Liberty Reserve a particularly

attractive money transfer system for criminal clientele seeking to launder their criminal proceeds, to move funds to or from sanctioned jurisdictions and entities, or to finance terrorism internationally. Forcing users to deposit or withdraw funds through exchangers creates another layer of anonymity in the system. To offer even more anonymity, Liberty Reserve provides an option, for an additional fee, to conceal the sole identifier of origin, the originator's account number, in transactions.

Liberty Reserve's AML policy, issued in 2010, states that it is illegal for Liberty Reserve, "its employees, agents or exchangers to knowingly engage, or attempt to engage in a monetary transaction in criminally derived property." It also states that it is illegal to "transport, transmit or transfer, or attempt to transport, transmit or transfer a monetary instrument or funds in excess of \$10,000 . . . either into or out of Costa Rica and/or any other countries with similar legislation if the purpose is to carry out an illegal activity, or to avoid reporting requirements." Its citation to these requirements demonstrates that Liberty Reserve is well aware of anti-money laundering laws. However, even having acknowledged that these activities are illegal in many jurisdictions in which they operate, and that they are aware of applicable laws and regulations in multiple jurisdictions, Liberty Reserve has structured its business to separate itself from knowledge that would allow it to detect money laundering. Indeed, the fact that Liberty Reserve has only a statement in its policy, with no implementation to address anti-money laundering concerns or requirements, is so deficient that it would not comply with any implementation of internationally accepted anti-money laundering requirements, such as the standards recommended by the Financial Action Task Force.

Liberty Reserve's AML policy provides less than one page regarding what Liberty Reserve considers a sufficient response to its risk for money laundering activity and its legal requirements. The only component of the policy that addresses any due diligence requirement indicates that the obligation is transferred entirely to the exchangers. The AML policy states that Liberty Reserve will verify the identity of the exchangers and request from them "a compromise to verify the identity of their direct clients." Whatever this is intended to mean, there is no evidence that Liberty Reserve requires the accredited exchangers to engage in any such customer verification. To the contrary, exchangers with which Liberty Reserve continues to work appear to have no or minimal verification or monitoring of clients; for example, some have no anti-money laundering policy, and others affirmatively advertise that they conduct no verification. Many of them are located in countries with lax money laundering enforcement. As of 2009, Liberty Reserve had outsourced its own verification process for new exchangers to a non-affiliated company for which at least two U.S. banks have rejected wires due to money laundering concerns.

Relying on exchangers to conduct what little due diligence Liberty Reserve purports to require enhances the gravity of Liberty Reserve's money laundering risk. A review of publicly available information on Liberty Reserve's exchangers indicates that many of them do not provide names of contact persons and obscure the country of their business registration or physical location. To further conceal their ownership, several of the exchangers registered their domain names through third-party hosting services, and some of them used a paid service through their registrars to hide registration information from the public. Website visitor traffic data on the exchangers' websites showed that

most exchangers appear to serve relatively few customers and produce little online attention.

Liberty Reserve's AML policy states that it will verify the identity of any direct client of Liberty Reserve "according to the guidelines of various jurisdictions."

However, Liberty Reserve appears to have no verification requirements in practice except for a working e-mail address. Similarly, its AML policy mentions requirements to "train staff continuously on anti-money laundering regulations" and to appoint a compliance officer responsible for monitoring and reporting "any and all suspicious activities."

Based on the information, or lack of information, collected by Liberty Reserve, it would be impossible for Liberty Reserve to operate an AML compliance program that complied with commonly required customer due diligence and suspicious activity reporting requirements.

Liberty Reserve's AML policy indicates an understanding of the key role suspicious activity reporting and responses play in anti-money laundering program requirements. The policy states "LIBERTY RESERVE is legally bound to report such misdemeanors to the relevant authorities and as such you may be the [sic] subject to a criminal investigation." Liberty Reserve has structured itself, however, to ensure that it never has the relevant information needed to comply with any stated obligation.

For all of these reasons, Liberty Reserve appears designed to facilitate money laundering and illicit finance. Funding a Liberty Reserve account, either through transfers from the owner of the account or from others, serves to place funds in the nominally legitimate stream of commerce. The anonymous nature of Liberty Reserve means such placement can be performed by anyone from anywhere using funds of any

origin. Transfers within Liberty Reserve's system, which can be made between any accounts without record or identification, serve to structure and layer movement of funds such that, even if the initial placement can be traced, subsequent movement cannot. The ease and anonymity of account opening means that such movement could easily occur among accounts owned by a single person or entity, completely obscuring the origin of funds that leave the system, creating a one-stop money laundering system.

D. Liberty Reserve Is Regularly Used to Store, Transfer, and Launder Illicit Proceeds.

Liberty Reserve is used extensively by criminals to store, transfer, and launder illicit proceeds, including through U.S. financial institutions. Information available to the U.S. government shows frequent wire transfer activity to or from Liberty Reserve that indicates money laundering, in that: 1) the legitimate business purpose, source of funds, and validity of the wire transactions could not be determined or verified; 2) little or no identifying information appeared in wire transaction records regarding the ultimate originators or beneficiaries such as addresses, telephone numbers, or identification numbers, with only Liberty Reserve in the "reference" field, suggesting an attempt to conceal the identities of the involved parties; 3) transactions involved unidentified entities located and/or banking in jurisdictions considered vulnerable or high-risk for money laundering activities; and 4) transactions involved large, round-dollar, repetitive international wire transfers sent to the same Liberty Reserve exchanger.

Information available to the U.S. government suggests frequent use of Liberty Reserve by criminals to receive, send, or launder funds. For example:

- A U.S. resident, on instructions from an individual allegedly involved in online fraud, sent over \$150,000 in possible stolen funds to the individual through a Liberty Reserve account set up in the resident's name.
- Several persons reportedly utilized a scheme involving identity theft to create multiple fraudulent corporate accounts with an online broker/dealer and funded the accounts with over \$250,000 in allegedly stolen funds. They then ordered over \$100,000 in an unspecified number of international wire transfers to be credited to a specified Liberty Reserve account number.
- A contact for an international company sent over \$1.3 million in dozens of large, round-dollar, repetitive international wire transfers to a Liberty Reserve account in mid- to late-2012. The individual was possibly using a personal bank account to conduct these business transactions, an indicator of potential money laundering.
- According to a news article in The Times of India, two individuals in Rajasthan, India were arrested in March 2013, for abducting and killing an individual they targeted through an online social networking site. The kidnappers demanded that ransom money be paid to their Liberty Reserve account. A cyber security expert cited in the news article stated that the kidnappers chose to use Liberty Reserve to execute their crimes because the system requires no proof of identification for the depositor or the recipient of funds, and Liberty Reserve will not disclose the internet protocol address of the recipient, which would aid law enforcement efforts.
- A facilitator of a foreign extremist group in 2013 held a Liberty Reserve account, which may have been used to collect funds for the group.

- One cybercriminal forum, the contents of which were recently made public, has long served as a point of sale for cybercriminal wares, including exploit kits, spam services, ransom-ware programs, botnets, and key-logging services, payable via Liberty Reserve.
- One hacker, who only accepts Liberty Reserve as payment, offered to sell the source code to “Winlocker,” an application to secure a computer with a password.
- One hacker claimed to have access to and control over several top dot-gov, dot-mil and dot-edu Web sites. The hacker also purported to sell personally identifiable information from hacked sites, for \$20 per 1,000 records. These services were payable only via Liberty Reserve.
- As of February 2011, the source code for the latest version of the Zeus banking Trojan, the preeminent cybersecurity threat used to steal bank account information, was available on an online criminal forum for a reported \$100,000, payable only through Liberty Reserve.

E. Liberty Reserve Is Not Designed For Legitimate Use.

Transfers made through Liberty Reserve currency cost considerably more than transactions made through comparable services, providing a significant disincentive for legitimate users. For example, a \$10,000 transfer using Liberty Reserve would cost approximately \$248 to \$1,946 in fees. Transferring \$10,000 through a comparable direct bank wire or MSB transfer costs approximately \$40 to \$200. The below chart illustrates some costs involved with a Liberty Reserve transfer, where, for example, Person A has \$10,000 to move from a U.S. bank to Person B’s bank account in another country through Liberty Reserve:

	Process Step	Cost	Charges
1.	Person A wires money from a bank account to an exchanger	Varies. \$45 is an approximate average	\$45
2.	Exchanger charges fee to convert USD into Liberty Reserve funds and places funds in Person A's Liberty Reserve account	Ranges from 1%-10%, with possible flat fees associated with transaction	At 1%: \$99 charge At 5%: \$497 charge At 10%: \$995 charge
3.	Person A instructs Liberty Reserve to move funds from his account to Person B's Liberty Reserve account	1% of transfer to receive money, up to a maximum of \$2.99	\$2.99. Users can also pay an optional privacy fee to remove their account number from internal transfers
4.	Person B sends Liberty Reserve funds to exchanger to convert to USD and send to Person B's bank account	Ranges from 1%-10%, with possible flat fees associated with transaction	At 1%: \$98 charge At 5%: \$472 charge At 10%: \$896 charge
5.	Person B receives funds in his bank account		Total cost at 1%: \$248 Total cost at 5%: \$1020 Total cost at 10%: \$1946

Liberty Reserve also is a completely irrevocable payment system and digital currency. The fact that the transactions are irrevocable, meaning that they cannot be reversed or refunded in the event of fraud, makes it a highly desirable system for criminal use and a highly problematic one for any legitimate payment functions. Revocability protects merchants and users from fraud and is a common feature of legitimate payment systems. Despite the security precautions that make it secure for illicit use, funds reportedly have been stolen from user accounts, making it even less attractive to any potential licit users. The company has been unresponsive to these customer complaints.

III. The Extent to Which Liberty Reserve Is Used for Legitimate Business Purposes in Costa Rica

FinCEN has found no evidence that Liberty Reserve is used in Costa Rica for any business purpose, legitimate or otherwise. Costa Rican customers have no direct access

to Liberty Reserve's offices. The only access to the business, anywhere in the world, is through its website. As noted above, Liberty Reserve appears to have chosen to locate itself in Costa Rica because Costa Rica is commonly known to have inadequate regulation of MSBs and internet businesses, and because the location allowed the company to avoid U.S. authorities because Costa Rica does not have a mutual legal assistance treaty with the United States.

IV. The Extent to Which This Action Is Sufficient to Guard Against International Money Laundering and Other Financial Crimes

FinCEN's finding that Liberty Reserve is an institution of primary money laundering concern will guard against the international money laundering and other financial crimes described above directly by restricting the ability of Liberty Reserve to access the U.S. financial system to process transactions, and indirectly by public notification to the international financial community of the risks posed by dealing with Liberty Reserve.

Dated: 5/28/13

/s/

Jennifer Shasky Calvery
Director
Financial Crimes Enforcement Network