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Sanctuary or Tempest? Navigating Moves to the U.S. Financial System

The health effects of Covid-19 have created personal tragedies that seemed unimaginable a few short months ago. Despite the efforts of governments, the virus has shown that the world is inextricably interconnected. How we respond will dictate whether that interconnectedness is a positive or negative force as we try to recover from the economic crisis that has arisen in the wake of the pandemic. In Latin America, individuals and companies have either begun to see, or fear, the return of currency controls, defaults and chaos as the governments of the region confront historic challenges. Many have once again sought refuge in the perceived relative safety of the U.S. financial system. However, investors may find that their sudden search for a safe haven may bring on a series of unanticipated problems.

As we have seen in the wake of so many financial crises, fraudsters often take advantage of the very people who seek a safe haven from the financial collapse in their home countries. Unscrupulous "wealth managers" prey on people anxious to have money in the U.S. financial system. These criminals then rely on the fact that the depositor/investor may not want the fact of their investment in the U.S. to come to light for fear of consequences in their own country. When the incentive to preserve capital offshore is great, but the government criminalizes rational economic conduct, these so-called advisors count on the veiled or not-so-veiled threat to expose those who try to preserve their capital to local authorities. Whatever one may argue about the ethics of preserving capital offshore from possible emergency expropriation measures, this should not provide a license to steal to advisors who make a business of siphoning flight capital from frightened investors.

The U.S. financial system offers relatively little protection against fraud. Only a few types of accounts (e.g., accounts that are roughly equivalent to cash such as checking or savings accounts) held at U.S. banks physically in the U.S. are insured by the federal government. These types of accounts are insured by the federal government, even if the account holder is a foreigner, up to $250,000 per depositor per bank. In other words, if a foreigner deposits $250,000 in three different FDIC-insured banks, he will have $750,000 worth of insurance provided by the federal government.

Many investors, however, will seek better returns than the near-zero interest rates paid by U.S. banks (although the current state of markets may make zero return seem attractive). While funds invested in securities in the United States may not be insured by the FDIC, they may be covered by SIPC. SIPC is a nonprofit corporation created by the Securities Investor Protection Act and funded by securities brokers who are SIPC members. Foreign investors are covered if defrauded but only if the securities were held with a SIPC member. A list of SIPC members is available on the SIPC website. It is critical for investors to know who is managing their funds, how they are licensed and whether they have SIPC protection. Advisors also are required to post annual Form ADV's, which record performance metrics and list any complaints or lawsuits.

One common fraud committed on foreign investors is the assurance that the funds are deposited in an FDIC insured account or with a SIPC-member broker when in reality they are in a far riskier, uninsured investment or the advisors have converted the funds. It is the foreign investor who must do their own due diligence or risk losing the very funds used for which they wanted a financial safe haven. Confirming directly with third party custodians that the funds are held in the way the asset manager is saying and preventing unapproved movements in capital are the best ways to protect an investment. Customers should insist that the custodian is separate from the investment advisor and that statements are prepared and sent by the custodian, not the advisor. We have had more than one client who has received spreadsheets that were fictitious. Customers should make sure that they personally receive the statements; many advisors suggest that customers should allow the statements to be sent to the advisor to avoid detection in their home country. That is a red flag for fraud.

The foreign investor moving assets to the United States is at risk not only when the assets arrive but also while in transit. Because of increased currency controls, foreign investors may be tempted to use non-traditional banking services to move their funds to the United States. In so doing, they may be using the very same channels used by drug traffickers and money launderers and by unwittingly "mixing" their funds with those of criminals they may be subjecting their funds to seizure by the government. This unintended "mixing" and resulting seizure can also occur if the funds are placed with a wealth manager who is dealing with the funds of criminals. While the innocent foreign investor has recourse to retrieve her funds, it can often take years for this to occur and this makes investing with reputable, government-regulated wealth managers is all the more important.

When frauds do occur, the American judicial system does provide recourse, but it is vital to act quickly in order to increase the likelihood that funds will be available to satisfy the harm caused by the fraudster. U.S. litigation offers the aggrieved access to a wide-ranging set of tools to find and secure misappropriated assets. Foreign investors must be careful and commit to performing their own diligence but if they suffer harm there are avenues for recovery. Here again, fraudsters may threaten to expose that these assets were in breach of foreign tax or currency restrictions. U.S. courts will not be interested and investors should not permit extortionate threats to deprive them of their assets.

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