Finances - Affluence

Note: Unexplained affluence is one of the potentially disqualifying conditions in the Financial Considerations adjudicative guideline. Although unexplained affluence is not as common as debt, it is discussed here as a separate topic to show that unexplained affluence is equally important as a potential security concern.

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Relevance to Security

Unexplained affluence refers to a lifestyle or standard of living, a pattern of expenditures, sudden increase in net worth, or money transfers that cannot be explained by the subject's known sources of income. An individual with more money than can be logically explained by known sources of income is a security concern because that money may have come from financially profitable crimes.

Of recent American spies who betrayed their country for financial gain, about half were motivated by greed rather than need. In most cases, the amount of money earned from espionage was so small that it was not apparent as unexplained affluence. However, four of the most damaging and best-paid spies in recent American history, Robert Hanssen, Aldrich Ames, John Walker, and James Hall, risked their security by almost flaunting their ill-gotten affluence rather than hiding it. In other words, they showed unexplained affluence which, if it had been reported and thoroughly investigated, may have identified them as having income from some illegal activity.

- Robert Hanssen, a Soviet and then Russian spy in the FBI, used his illegal income to pay for private school education for his six children and to buy diamonds. After his arrest, Hanssen advised investigators that a thorough financial investigation would have shown that he was spending more money than he was earning. [1]

- Aldrich Ames was a Soviet spy in the CIA. Soon after paying a divorce settlement and marrying a woman with expensive tastes, he bought an expensive home without a mortgage. His expenditures were so high that his monthly credit card payment was greater than his monthly CIA salary. He had an A-1 credit rating, with no overdue debts, but the high monthly payments disproportionate to his monthly salary should have been recognized as suspicious.
- After his arrest, Navy Chief Petty Officer John Walker took pride in being described in the press as the most damaging spy in the history of the United States. Walker flaunted the money he received from the Soviets. He bought a house and gave his wife carte blanche to furnish and decorate it as she pleased. He bought a boat where he spent much time partying with other women, and eventually he purchased an airplane. He claimed the income came from a bar he had bought, which was actually losing money, and other "astute investments."
- Army Sgt. James Hall received about $300,000 from the Soviets during six years working as a spy in West Germany. His $25,000 cash purchase of a new Volvo attracted attention, as did his large down payment on a home after returning to the United States. He is said to have given his military colleagues at least six conflicting stories to explain his lavish life style, but no investigation was initiated until his espionage was reported by an Eastern Bloc defector. [2]

It is often asked why spies like those discussed above endanger their security by conspicuous expenditures beyond what they could afford with their salary. It is because, in many cases, hiding the money would defeat the purpose for which they committed the crime. In most crimes motivated by greed rather than financial need, the money is sought because of its symbolic value. Money is a means to achieve or to measure social prestige, power or control, or to buy affection or gain self-esteem. The same compelling emotional needs that drive an individual to commit a crime like espionage often drive that person to spend the illegal income rather than save it or hide it. When the amount is large, this spending is observable as unexplained affluence.

Potentially Disqualifying Conditions

Extract from the Guideline

(e) consistent spending beyond one's means, which may be indicated by excessive indebtedness, significant negative cash flow, high debt-to-income ratio, and/or other financial analysis;

(h) unexplained affluence, as shown by a lifestyle or standard of living, increase in net worth, or money transfers that cannot be explained by subject's known legal sources of income;

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One of the potentially disqualifying factors in the Financial Considerations guideline is unexplained affluence as "shown by a lifestyle or standard of living, increase in net worth, or money transfers that cannot be explained by subject's known legal sources of income." Another potentially disqualifying factor in the guideline is "consistent spending beyond one’s means." This usually means too much debt, but it can also show up in the credit report as an indicator of unexplained affluence. If someone has an unusually high level of nonmortgage debt but has no delinquent debt or any other indicator of financial stress, there may be an undisclosed flow of illegal income.

Obviously, there are many legal sources of income beyond one's own salary. Unusual affluence might come from inheritance, gifts from parents, a wealthy spouse, astute investments, a profitable hobby, or a second job. On the other hand, it may also be attributable to drug dealing, embezzlement, fraud, espionage, or other criminal activity. In most cases, the indications of affluence are the same regardless of whether it comes from a legal or illegal source.

It is not sufficient to know only the subject's explanation of the source and amount of these funds. It is easy for spies and other criminals who acquire large amounts of cash through illegal activities to make up plausible cover stories to explain their apparent wealth. In many cases, therefore, the affluence is not "explained" until it is corroborated by one or more independent interview sources or documented by copies of tax returns, canceled checks, or bank or brokerage account statements. The discussion under mitigating conditions cites several examples of cases where the affluence would need to be documented.

If the investigation finds that the subject is either unwilling or unable to document the source of the apparent affluence, the case should be referred for more detailed financial analysis and/or counterintelligence review. Whether this is done by the investigative element or the adjudicator, and the process for doing it, depends upon the circumstances and the capabilities of the agency involved.

Adjudicators are sometimes faced with an incomplete investigation that fails to adequately explain or verify a subject's explanation for additional income. The adjudicator then has a difficult choice -- accept the investigation and approve the clearance, or delay the investigation by requiring further investigation. Under these circumstances, the decision should be guided by a whole-person assessment of the subject's reliability and trustworthiness, developments in the subject's life that may cause financial stress or alienation (expensive divorce settlement, resentment after being passed over for promotion), and the opportunities for betrayal available to the subject (access to especially valuable information or a position dealing with money).

For example, long before CIA spy Aldrich Ames' arrest, coworkers reported that his standard of living far exceeded his income. This was initially "explained" by rumors that his new wife was from a wealthy Colombian family, but no investigation confirmed that his wife had significant income. In fact, one work colleague who knew Ames well and was concerned about his unexplained affluence reported specifically that his wife was not wealthy. Once the unexplained affluence issue was raised, the intensity and depth of investigation should have been guided by the following factors: Ames had a known drinking problem, he had had an expensive divorce and remarried a woman accustomed to a high standard of living, and he resented being passed over for promotion. Also, his job involved direct contact with Soviet intelligence officers, and he had access to the most sensitive information on CIA agents in the Soviet Union.

Noteworthy Indicators of Unexplained Affluence

The following indicators of unexplained affluence may be observed and reported by friends or coworkers:

- Subject's use of cash to buy expensive items normally paid for by check or credit card.
- Subject spends money on things that are well beyond the reach of others with similar incomes, such as: expensive home or home improvements, expensive vacations, luxury automobiles or collector cars, a boat or airplane, private schools for his or her children, domestic help, diamond jewelry, expensive collectibles (rare coins, stamps, art), and commodity holdings (gold, diamonds), and offshore investments.
- After a period of indebtedness or frugal living, the subject starts to act like a big spender, picking up the bar bill, buying new and expensive clothing, giving gifts to nonrelatives.
- Subject continues to spend money freely despite major new financial obligations, such as child support, support of relatives, or high medical expenses.
- Subject explains sudden influx of money by claiming large gambling wins, inheritance, or stock market dealings, but the explanation is vague, inconsistent, or seems uncharacteristic for that person.

The following indicators of unexplained affluence may be identified through the credit report or other investigative measures:

- Fast pay-down of debts. After a history of continuing indebtedness or recurring financial difficulties, the credit report shows that the subject has paid all overdue debts. The source of funds to pay the debts is unknown, i.e., there is no evidence in the credit report of a new debt consolidation loan or home equity loan and no information on sale of assets, inheritance, or other source of income. (Thomas Cavanaugh, a

Northrop employee who tried to sell information on the Stealth bomber to the Soviets, was motivated, in part, by a need to pay off his debts to protect his security clearance. He was having financial problems and thought he needed to get his debts paid off before his upcoming periodic background reinvestigation.) 4

- Subject has no overdue debt, but has unusually high revolving credit card debt, or auto loan or home mortgage payments for a person in the subject's position. In other words, large debts are being paid off successfully with a relatively low salary. This situation suggests either of two circumstances: (1) the subject has unexplained income the adjudicator needs to know about, or (2) the subject has maxed out his or her credit cards in order to avoid overdue debt, in which case the subject may be on the precipice of financial failure. Soviet spy Aldrich Ames is an example of the first type of case. His minimum monthly payment on credit accounts was greater than his monthly CIA salary.
- A Department of Treasury Financial Crimes Enforcement Network (FinCEN) check identifies large cash currency transactions not associated with work or civic activities. Large deposits are of greater security interest than withdrawals.
- An unexplained increase in net worth, as shown in the series of financial disclosure statements that are required to be filed by some individuals in very sensitive positions.
- Any credible report that the subject has attempted to hide income or assets.

Financial Analysis

There are two principal types of analysis for assessing a person's financial status -- cash flow analysis and net worth analysis. Both may be used to assess the possibility of unexplained affluence or the extent of financial hardship. The source of information for a cash flow analysis is the credit report plus a Personal Financial Statement prepared by the subject, usually with assistance from an investigator. The source of information for the net worth analysis is the annual Financial Disclosure form that is increasingly being required of designated personnel in especially sensitive positions. Cash flow analysis is discussed in the next paragraph, while net worth analysis is discussed in the following section on analysis of the Financial Disclosure Form.

Cash flow analysis examines how much money remains, if any, after deducting all of a person's monthly living expenses and debt payments from their total monthly income. The analysis is used to determine if a person with unpaid debts is living within his or her income, or, if a person with no unpaid debts but an unusually high credit balance is making such high mortgage, car loan, and/or credit card payments that he or she must have some undisclosed source of income. The latter circumstance would indicate unexplained affluence. The source of information for a cash flow analysis is the credit report plus a Personal Financial Statement prepared by the subject, usually with assistance from an investigator.

Financial Disclosure Form Analysis

Many individuals with access to extremely sensitive information are required to file an annual Financial Disclosure Form (FDF). This form is designed to help identify signs of unexplained affluence or unusual financial hardship.

Most offenders who engage in crimes for profit do so, at least in part, because they desire big ticket assets like houses, automobiles, boats and expensive jewelry. Offenders who have gained wealth from illegal sources will be faced with a dilemma. FDF filers who report all of their illegally obtained assets will risk identification and will look suspicious because their income does not justify such wealth. If filers attempt to hide large assets by not listing them on the FDF, the automated search of external databases is likely to identify at least one, if not all, of the unreported assets. Obviously this will call into question the honesty of the filer. The FDF should create a deterrent effect if filers believe that the information they are providing might make it more likely they will be caught.

Two main methods are used along with the Financial Disclosure Form to help identify income that has been obtained from an unknown and possibly illegal source. The methods are internal and external inconsistencies.

- Internal Inconsistencies: These appear when a filer lists two or more values on the FDF that are inconsistent. For example, if a filer lists a mortgage loan but does not report any real estate there is an inconsistency. If a filer lists interest received but does not list a bank or investment account, there is an inconsistency.
- External Inconsistencies: Reported values such as salary, vehicles and real estate owned can be compared and matched against government and or commercial databases. For example, if a filer fails to list an automobile, this can easily be discovered by computerized matching of data.

If either internal or external inconsistencies are observed, additional analysis is warranted. There are two types of assessments that can be utilized, but a subject has to provide additional financial information before they can be employed. The assessments are net worth and bank deposits.

Net Worth Assessment

Increases or decreases in a filer's net worth during a period of time, adjusted for living expenses, result in a determination of income. Net worth is the difference between a filer's assets and liabilities at a particular point in time. An asset is any item of value. A liability is a financial obligation with a promise to pay. Net worth is the difference between what is owned and what is owed. According to the Federal Reserve, in 2004 the median net worth in the U.S. was $93,100. A net worth assessment can only be done when there is financial information for two different years. First compute the net worth for year 1, then compute the net worth for year 2, and the difference between the two figures is the change in net worth:

Assets	$800,000	Net Worth (Year 2)	$750,000
- Liabilities	-$200,000	- Net Worth (Year 1)	-$600,000
Net Worth (Year 1)	= $600,000	Change in Net Worth	= $150,000

The change in net worth figure is added to the living expenses for year 2 and equals the total outlay. The known income figure is subtracted from the total outlay figure to determine the unknown income amount:

Change in Net Worth	$150,000	Total Outlay	$190,000
+ Living Expenses*	+$ 40,000	- Known Income	-$ 90,000
Total Outlay	=$190,000	Unknown Income	=$100,000

*Living expenses are expenditures which are not classified as assets or liabilities. They are payments for consumables. Living expenses include: household expenses; auto repairs; insurance premiums; contributions; medical expenses; entertainment expenses; gifts; taxes paid; etc.

Note that living expenses are not listed on the FDF and a subject would have to provide the amounts separately.

Bank Deposit Assessment

The bank deposit assessment computes income by showing what happened to a filer's funds. Income is proved through an analysis of bank deposits, canceled checks and currency transactions. Bank deposit information is not listed on an FDF and a subject would have to provide the amounts separately. For example:

Gross Deposits	$200,000
- Account Transfers	-$ 50,000
Net Deposits	$150,000
+ Expenditures	+$ 25,000
Total Available Funds	$175,000
- Known Source Funds	-$ 75,000
Unknown Source Funds	$100,000

FinCEN Database

The Financial Crimes Enforcement Network (FinCEN), managed by the Treasury Department, supports law enforcement, intelligence, and regulatory agencies through the sharing and analysis of financial intelligence to combat money laundering. Title 31 of the Bank Secrecy Act provides for maintenance by Customs and/or the Internal Revenue Service of databases that are relevant to detection of unexplained affluence.[5] These databases are accessed through a FinCEN check conducted by the government agency that requested or is supervising the investigation. The FinCEN check can turn up the records described below.

If there is a FinCEN report on a subject of investigation, first ensure that it does in fact apply to the subject. To make this identification, compare as many parameters as possible, not just the name or Social Security number. Also check date of birth, address, identification document number, signature, occupation, and employer's name when any of these are available on the form. While not all the information needs to match (e.g., the person may list a different employer or occupation), there should be enough agreement to warrant a high degree of confidence that the document pertains to the subject of the investigation.

Currency Transaction Reports (CTRs): As part of a broad program to combat money laundering, banks and other financial institutions are required to report to the government cash transactions of $10,000 or more. If a person pays deposits more than $10,000 in currency at a bank, this transaction is supposed to be reported. The report then becomes available in a FinCEN check.

If a large bank deposit is made within two weeks after subject of investigation returns from a foreign trip, and there is no report on the international transportation of currency (which means the subject did not declare the money when going through Customs), the case should be referred for counterintelligence review.

Cash Transaction Reports by Casinos (CTRCs): This is similar to the Currency Transaction Report, except that this form must be filed by casinos, gambling casinos, and card clubs. The receipt or disbursement of cash totaling $10,000 or more during a single gaming day must be reported.

Report of Cash Payments Received in a Trade or Business: Any trade or business receiving a payment in cash of $10,000 or more is required to report this on IRS and FinCEN Form 8300. If you buy a car from an automobile dealer and pay $10,000 or more in cash, the dealer is required to report this.

Report of International Transportation of Currency or Monetary Instruments (CMIRs): This is a self-reporting form filed by individuals whenever currency or currency equivalents (cash or financial instruments such as bearer bonds -- but not checks) with a value of $10,000 or more are carried or otherwise transported or sent into or out of the United States.

Transporting currency or currency equivalents of this amount raises questions about foreign contacts and activities that must be covered during the investigation. If there is any reason to suspect that cash brought into this country may be related to illegal activity, the case should be referred to an appropriate office for counterintelligence review.

Report of Foreign Bank and Financial Accounts (FBAR): Anyone who has a financial interest in, signature authority, or other authority over one or more bank accounts, securities accounts, or other financial accounts in a foreign country must report this annually to the Department of Treasury if the total value exceeds $10,000 at any time during the calendar year. Any foreign bank account raises questions about foreign contacts and activities that must be covered during the investigation. Check what the subject has disclosed on the security form about residence or travel to that country.

Other Reports: FinCEN also maintains the following reports that are not currently available but may become available in the future: Bank Suspicious Activity Report (SAR), and Casino Suspicious Activity Report (CSAR).

Mitigating Conditions

Extract from the Guideline

(f) the affluence resulted from a legal source of income.

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Unexplained affluence is not an issue if investigation confirms that the unexplained affluence is from a legal source such as inheritance, legitimate business interests, or investments. As discussed under potentially disqualifying conditions, however, affluence is often not really "explained" until it is corroborated by one or more independent interview sources or documented by copies of tax returns, canceled checks, or bank or brokerage account statements. The following are obvious examples of circumstances where the subject should be required to document the source of funds.

- Security officer reported the subject had deposited $90,000 into his account at the company Credit Union.
- Subject reported approximately $300,000 in assets kept in German Banks. Subject stated that the money was from an inheritance from unspecified relatives in Germany.
- Credit reports 6 months apart show that $136,000 mortgage was paid off and personal debt was reduced from $54,000 to $30,000. 3

Footnotes

1. Ciccarello, N.J., & Thompson, T.J. (2003, March). *Money, the fear of failure, and espionage: Report of an interview with Robert Philip Hanssen.* Washington, DC: Personnel Security Managers' Research Program.

2. Engelberg, S. (1989, July 18). U.S., in detail, admits its spying in Europe as suspect's trial opens. *The New York Times*. Also Engelberg, S. (1989, July 21). Turk convicted in spy case called harmful to U.S. *The New York Times.*

3. Kramer, L.S., Jung, C.G., Gonzalez, J.L., & Richmond, D.A. (2006). *Behaviors and characteristics of counterintelligence concern exhibited by DoD security clearance applicants* (Draft). Monterey, CA: Defense Personnel Security Research Center.

4. National Counterintelligence Center. (1996, March). Through the looking glass. *CI News & Developments, I*.

5. P.L. 91-508, 84 Stat. 1114 (1970). Implementing regulations containing the reporting and recordkeeping requirements for financial institutions are promulgated by the Department of the Treasury at 31 C.F.R. part 103.