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The Beef With Cattle Fraud

JULY 1, 2020

Everyone knows fraud and money laundering are two sides of the same coin. Fraudsters do what they do for one reason only—the money. Thus, fraud inherently leads to money laundering as conmen deposit, move or withdraw funds from their illicit activities. Unbeknownst to many anti-money laundering (AML) professionals, cattle fraud is a global threat with bigger and broader swindles identified in recent years. Law enforcement officials say it will continue to grow exponentially in the current unstable economic climate.

> *Cattle fraud is a viable criminal pursuit worldwide because of the sheer number of cattle as well as the proceeds that can be generated through the sale and processing of cattle and cattle products*

Scott Williamson, executive director of law enforcement, brand and inspection services for Texas and Southwestern Cattle Raisers Association, notes that thefts and scams targeting cattlemen are increasing during this period of economic and industry distress. People are more likely to initiate scams and conduct illicit activities when they are financially and emotionally anxious, or willing to take advantage of others who feel this way. In addition, those buying or selling cattle may be less likely to verify the validity of the transaction and the identity of whom they are conducting business with because they feel rushed to complete the deal. Williamson cautions buyers, sellers and investors to be especially wary of working with people they do not already know or conducting transactions they cannot verify in person.

Global Applicability

Cattle represent a global economic asset. In the top five cattle-producing countries (Uruguay, New Zealand, Argentina, Australia and Brazil) there are more cattle than people. In 2018, the top five U.S. cattle-producing states (Texas, Nebraska, Kansas, California and Oklahoma) were home to almost 36 million head of cattle—about 38% of the U.S. total cattle population.[1] Cattle fraud is a viable criminal pursuit worldwide because of the sheer number of cattle as well as the proceeds that can be generated through the sale and processing of cattle and cattle products (beef, dairy, leather, etc.) In 2018, cattle production in the U.S. alone accounted for $67.1 billion in annual cash receipts.[2]

Cattle fraud has "cradle to grave" potential, affecting a vast number of businesses. In addition to farms, dairies and ranching operations, other businesses impacted by cattle fraud include cattle brokers, sale and auction barns, transport companies, feedlots and feed vendors, slaughterhouses and meatpacking facilities. Moreover, financial institutions (FIs) that bank, process transactions for, lend to and facilitate investments for cattle operations are also significantly affected by cattle fraud. Given the global potential for cattle fraud, the money involved and the fundamental link between fraud and money laundering, it is prudent for AML professionals to consider the impact cattle fraud can have upon their institution.

Examples of Recent Cattle Fraud Cases

In March 2020, the U.S. Department of Justice (DOJ) filed an indictment against Robert Blom, alleging he was involved in a five-year, $20 million Ponzi scheme.[3] Blom reportedly billed investors for the purchase, feeding, care and sale of cattle to processing plants. However, according to the DOJ, it appeared that he repeatedly used the same herds of cattle to solicit funds from multiple investor groups. Funds derived from this activity were labeled as profits from ongoing sales and used to pay back prior investors.

In October 2019, Timothy Cosman was sentenced to 36 months in jail and ordered to pay just under $3 million in restitution to Busey Bank for fraud related to cattle loans.[4] Cosman overstated his assets and provided the bank with fabricated documents to be used as loan collateral, including a falsified promissory note secured by nonexistent cattle.

In September 2019, the Securities and Exchange Commission (SEC) sued Mark Ray for a massive cattle-flipping scheme that diverted investors' funds—originally collected to purchase and resell cattle—into personal interests and other businesses, including a marijuana business.[5] The SEC said that more than $140 million per month moved through accounts held in the names of Ray, various related businesses and two associates. Much of the money was apparently unaccounted for and untraceable. The SEC stated "Ray had no records of the various cattle transactions he purportedly engaged in, and he does not have sufficient records from which to reconstruct the investors' flow of funds, particularly given that a significant amount of investor funds went directly from one victim to another." The SEC also noted that Ray was previously barred from offering securities in the state of Illinois for similar activities.

Cattle fraud even appears to have played a role in a murder case. In October 2019, Garland "Joey" Nelson was accused of murdering Nicholas and Justin Diemel. The Diemels, who co-owned a livestock business, were last known to be visiting Nelson in July 2019. Authorities later identified the human remains found on Nelson's farm as those of the Diemel brothers. The Diemels boarded cattle with Nelson, and appear to have been visiting him in conjunction with a $250,000 debt Nelson owed them.[6] In 2015, Nelson was also found guilty of a $300,000 cattle fraud that resulted in jail time.[7] At the time of writing, Nelson is in jail and the murder trial has been delayed due to COVID-19 restrictions.

Prevention

The cheapest, easiest and most informative tool to identify and prevent cattle fraud and associated money laundering from occurring within FIs is one many already have in their arsenal: boots on the ground. That is, actually getting out and visiting local cattle ranchers, feedlots, brokers, auction houses and farmers who bank with the institution. Whenever possible, plan impromptu visits as well as follow-up visits to verify the collected information.

While gathering information, it is important to consider the following:

- Visit their place of business (this can be done via an online mapping search first). How large is their operation and are all cattle housed on-site? If they are a cattle broker, where are the cattle housed? If their business address is a suburban home or a mail drop, then that may be a red flag that they are not running the operation they claim to be.
- Map and verify the locations of pastures, barns and other operations. Another recommended practice is to note and record GPS coordinates where possible, including entry points such as gates. Verify whether the rancher owns or leases the properties shown. Note ease of access to the highway or busy roads, as this can present temptation for theft or tampering with the cattle.
- Check out the size of herd and type of cattle. What breeds of cattle do they have? How many bulls, cows, steers and calves? Where are they pastured? This information should match all files, especially if liens exist on any of the

cattle to secure loans or if owners are soliciting investors to back purchases and sales.

- Verify the type of cattle identification system used. Most cattlemen use branding, ear tags or a combination thereof on their herds. Take photos of each type of identification used and file them. Compare brands and information on ear tags to the state and local requirements—if there is a brand registered to a local operator, make sure that brand is actually being used on current herds or that there is a clear reason why it is not. In addition, remember that brands are state- and region-specific, so there may be multiple brands in use depending on where the herd originated.
- Review the scope of the operation, number of employees, level of activity in the yard, and suppliers going in and out. Then compare that to what is known about the operation, or review their accounts to clarify. The information on hand should tie to what is seen in the field.
- Consider how and whether various cattle accounts and personnel overlap and are interrelated. In most communities, like industries tend to interact and use the same group of vendors. If the FI works with a cattle business that appears to be doing business with completely different partners and vendors than the others in the area, that may indicate unusual activity.

Looking Down the Road

As with all facets of modern life, new technology is being developed to assist in cattle ranching that will have practical applications for anti-fraud and AML measures. A company called MoooFarm is developing facial recognition programs for cattle.[8] The company took numerous photos of the faces of cattle in all kinds of lighting, angles and backgrounds. The algorithm in their technology recognizes that cattle have unique features, markings and coloration; MoooFarm says its model identifies the correct animal 96% of the time. Using facial recognition software would reduce the reliance on branding, radio-frequency identification (RFID) tags and other potentially variable and removable technology. In addition, MoooFarm's technology is developed for smartphones, eliminating the need for special scanners, drones or other expensive equipment that can exclude small cattle operations.

Closer to home, blockchain technology is becoming more widespread among larger cattle operations.[9] Blockchain technology is used at birth as calves receive an RFID tag that is scanned into an online database. Calves continue to be scanned at various points in their life cycle, including when they are weaned and sold. Data is unalterable once it has entered into the blockchain, giving confidence that the buyer and seller know exactly where a particular calf or herd originated and where they have been since. Blockchain also allows sellers to ensure they have a verified buyer and that there are confirmed funds to cover the transaction.

Conclusion

Cattle fraud is a preventable crime, provided that one is willing to invest some time and energy into guarding against it. Taking proactive steps to become familiar with operations in one's business line may save the institution and its customers millions down the road.[10]

*Brigette K. Miller, CAMS-FCI, CRCM, senior risk specialist (BSA/AML), Federal Reserve Bank of Dallas, Dallas, TX, USA, **Brigette.K.Miller@dal.frb.org (Brigette.K.Miller@dal.frb.org)***

The views and opinions expressed herein are those of the author and do not represent an official position of the Federal Reserve Bank of Dallas or the Federal Reserve System.

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