PUBLIC HEARING:
ADVANCE NOTICE OF PROPOSED RULEMAKING ON CUSTOMER DUE DILIGENCE

U.S. DEPARTMENT OF THE TREASURY
WASHINGTON, DC
JULY 31, 2012
9:30AM - 4:30PM

SUMMARY OF PUBLIC HEARING

On March 5, 2012, the Financial Crimes Enforcement Network (FinCEN) issued an Advance Notice of Proposed Rulemaking (ANPRM) to solicit public comment on the potential development of an explicit customer due diligence obligation for financial institutions, including a requirement to collect beneficial ownership information of their customers.[1] The comment period closed on June 11, 2012. On July 31, 2012, officials from the U.S. Department of the Treasury (Treasury), including from FinCEN, hosted a public hearing to invite additional comment on specific issues raised during the comment period. Approximately 100 persons attended the public hearing, including representatives from various financial services industries and non-governmental organizations, as well as members of the law enforcement, regulatory and legislative communities.

Set forth below is the agenda from the public hearing and a general summary of the primary issues discussed, as understood by Treasury officials in attendance. It is not intended to be a transcript, and does not purport to include every comment or issue raised during the hearing. The morning session, which included prepared remarks from members of the public and senior officials from the Departments of Treasury and Justice, was recorded and is available online.[2]

Public Hearing Agenda and Summary[3]

9:30 am: *Welcome and introductory remarks by Jamal El-Hindi, Associate Director, Regulatory Policy and Programs Division, Financial Crimes Enforcement Network* (Exhibit A)

9:45 am: *Address by David S. Cohen, Under Secretary for Terrorism and Financial Intelligence, U.S. Department of the Treasury* (Exhibit B)

10:00 am: *Address by Lanny A. Breuer, Assistant Attorney General for the Criminal Division, U.S. Department of Justice* (Exhibit C)

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[1] Financial Crimes Enforcement Network, "Customer Due Diligence Requirements for Financial Institutions," 77 FR 13046 (March 5, 2012), available at: http://www.regulations.gov/#!docketDetail;D=FINCEN-2012-0001;dct=FR%252BPR%252BN%252BO%252BSR

[2] The recorded webcast can be found at: http://treas.yorkcast.com/webcast/Viewer/?peid=9012292836854735913 94a38c053e0c71d

[3] All times included in the agenda are approximate.

10:15am: *Overview of agenda and procedural matters by Jamal El-Hindi and Chip Poncy, Director, Office of Strategic Policy for Terrorist Financing and Financial Crimes, U.S. Department of the Treasury*

10:30 am: *Remarks from the following members of the public*

- Laura Stuber, Office of Senator Carl Levin (Exhibit D)
- John Moscow, Former Prosecutor (Exhibit E)
- David Landsman, National Money Transmitters Association, Inc. (Exhibit F)
- Stefanie Ostfeld, Global Witness (Exhibit G)
- Raymond Baker, Global Financial Integrity (Exhibit H)
- Joseph Alexander, The Clearing House Association LLC (Exhibit I)
- Thomas Bogle, Investment Company Institute (Exhibit J)
- Betty Santangelo, Securities Industry and Financial Markets Association (Exhibit K)

Following their remarks, each panelist responded to questions from Messrs. El-Hindi and Poncy. The panelists' remarks, as well as the subsequent question and answer session, may be accessed via the recorded webcast.

12:30 pm: *Break*

1:30 pm: *Open Forum Discussion*

Messrs. El-Hindi and Poncy co-chaired an open forum with all attendees to discuss key issues raised during the ANPRM comment period. As part of this open forum, Jennifer Shasky, the Chief of the Asset Forfeiture and Money Laundering Section of the Department of Justice, noted that (i) obtaining beneficial ownership information enhances the accuracy of a financial institution's risk assessment, (ii) self-declarations regarding beneficial ownership have investigative and prosecutorial value, even if a customer misleads a financial institution, and (iii) obtaining beneficial ownership information would assist law enforcement investigations involving a wide array of account relationships, including, but not limited to, shell companies. The co-chairs then engaged the attendees in a discussion of the key issues outlined below. The following is a general summary of the discussion:

- Definition of Beneficial Ownership

  - To address some confusion expressed by commenters in the earlier hearing sessions, Treasury officials clarified that the ANPRM definition of "beneficial owner" with respect to a legal entity customer includes both concepts of ownership and control. Including both concepts in the definition may be necessary to accommodate the vast array of complex ownership structures of legal entities that may become customers of financial institutions. The co-chairs asked participants to comment on the definition set forth in the ANPRM.

- To avoid confusion, some participants recommended that any proposed definition of "beneficial owner" in connection with a customer due diligence regulation be consistent with similar definitions applicable in other contexts, such as the Foreign Account Tax Compliance Act (FATCA)[4] or the regulations promulgated under Section 312 of the USA PATRIOT Act.[5] Other commenters suggested that additional sources may also provide helpful guidance with respect to the definition of "beneficial owner," such as the Glossary of the Financial Action Task Force (FATF) Recommendations,[6] the Wolfsberg FAQ's on Beneficial Ownership[7] and the Incorporation Transparency and Law Enforcement Assistance Act, a legislative bill proposed by Senator Carl Levin.[8]

- Other participants indicated that any definition intended to cover the wide variety of customers opening accounts, types of accounts opened, and products and services offered must be practical such that financial institutions, their line employees and their customers could understand and apply the definition with certainty. The current proposed definition and many of the alternatives identified above are unclear and do not satisfy this interest.

- Obtaining Beneficial Ownership Information – Current Practices

  - Treasury officials asked participants to provide examples of the circumstances in which financial institutions currently obtain beneficial ownership information, and how financial institutions define "beneficial owner" in such circumstances.

  - Participants expressed varied views as to whether, and in what circumstances, financial institutions obtain beneficial ownership information. In determining whether to obtain beneficial ownership under a risk-based approach, some financial institutions consider a customer's size, type of account, relationship history and applicable regulatory framework. For example, some financial institutions may obtain beneficial ownership information for certain non-operating entities formed under the laws of foreign jurisdictions, or after a financial institution observes suspicious activity related to a specific legal entity customer.

  - Some commenters indicated that beneficial ownership information should be viewed as only one component of a customer's broader risk profile, and that transaction monitoring

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[4] FATCA provisions are part of the Hiring Incentives to Restore Employment (HIRE) Act, Pub. L. No. 111-147, 124 Stat. 71 (2010).
[5] 31 CFR §1010.605(a).
[6] FATF Recommendations, General Glossary, p. 110.
[7] Wolfsberg FAQ's on Beneficial Ownership, available at http://www.wolfsberg-principles.com/pdf/Wolfsberg-FAQs-on-Beneficial-Ownership-May-2012.pdf.
[8] Incorporation Transparency and Law Enforcement Assistance Act, S. 1483, 112th Cong., 1st Sess. (2011).

may be more relevant in detecting illicit activity than information collected from the customer during the onboarding process.

- Some commenters acknowledged that simply identifying the beneficial owner by relying on a customer's declaration (without verification) could be workable as a broad-based requirement, but questioned the utility of such a requirement, given that persons could misrepresent the answer. A Department of Justice official stated that such misinformation could be significant to law enforcement, including with respect to proving criminal intent.

- Verification of Beneficial Ownership – Identity and/or Status

  - Treasury asked participants to comment on a potential obligation for financial institutions to verify a beneficial owner's (i) identity and (ii) status as beneficial owner, as described in the ANPRM.

  - Many commenters noted that verifying a beneficial owner's status as the beneficial owner would impose a substantial burden on financial institutions, and may not be possible in certain circumstances. Some commenters suggested that compliance with any such obligation requires the ability to corroborate information provided by a customer with an independent source of beneficial ownership information, such as a state registry. Other commenters noted that the FATF standards do not require verification of status. No one responded to Treasury's question of whether any financial institution currently had a policy of collecting beneficial ownership information from foreign state registries with respect to foreign entity customers.

  - Some commenters referenced the discussion earlier in the day regarding the definition of beneficial ownership and federal legislation as a potential solution to concerns related to the verification of beneficial ownership. The commenters stated that the verification of beneficial ownership would have more uniformity and be more efficient if federal legislation was enacted that would require beneficial ownership information be provided through the legal entity formation process.

  - Some commenters suggested that Treasury publish a standardized self-declaration form that financial institutions could use to obtain the beneficial ownership information of their customers. According to the commenters, such a form could facilitate financial institutions' reliance on their customer's declaration of beneficial ownership information, and would provide investigative and prosecutorial value to law enforcement.

- Some commenters discussed earlier remarks from the Department of Justice official who stated there is value to law enforcement when a customer lies about beneficial ownership identity and/or status, noting this may be an indicia of criminal intent, or could represent fraudulent activity. One industry attendee acknowledged, understanding the value of collecting beneficial ownership information, that it would not be complicated to collect beneficial ownership information, but at a cost. Commenters strongly suggested it should be understood by regulators that in many instances they will not be able to verify the information they obtain.

- Challenges Associated with Obtaining Beneficial Ownership on Certain Products, Services, and Relationships

  - Treasury officials sought comment on the challenges associated with obtaining beneficial ownership in specific contexts, such as intermediated relationships, trust accounts and other unique circumstances.

  - Several commenters noted that intermediated relationships pose unique due diligence challenges when a financial institution interacts with its intermediary customer only, and not that customer's underlying clients. According to the commenters, obtaining beneficial ownership information on such underlying clients would be particularly burdensome, and would result in a diversion of limited resources. Furthermore, if law enforcement is concerned about activity associated with the underlying clients of an intermediary customer of a financial institution, the commenters suggested that the intermediary customer is better situated than the financial institution to assist law enforcement. However, commenters acknowledged that law enforcement face a number of additional challenges when dealing with intermediary customers outside of the United States.

  - Several commenters also noted that many financial institutions conduct extensive diligence on their intermediary customers. Such diligence includes, among other things, a review of the customer's anti-money laundering procedures and practices, its customer base and the applicable regulatory framework. Financial institutions also typically monitor their intermediary customer's activity, which may include activity associated with an underlying client. Some commenters acknowledged that a primary risk in intermediated relationships may be with respect to the underlying customer in a transaction. Commenters noted that customer due diligence monitoring obligations or specific due diligence requirements for correspondent accounts as mandated under Section 312 of the USA PATRIOT Act may be a more clear and effective way to address such risk.

- With respect to trust accounts, several commenters suggested that applying the same definition of "beneficial owner" to trusts as to legal entities (i.e., corporations, limited liability companies, etc.) would be unworkable. Accordingly, commenters recommended that Treasury issue guidance to specify the information financial institutions would be required to obtain from their trust account customers.

- Other Issues Pertaining to the Advance Notice of Proposed Rulemaking

  - Treasury officials encouraged participants to discuss other issues related to the ANPRM that may not have previously been addressed during the public hearing.

  - Some commenters reiterated the need for certain exemptions from a categorical requirement to obtain beneficial ownership information. These commenters indicated that such exemptions should include, at a minimum, those customers currently exempt from the customer identification program rule,[9] as well as other customers that may be considered lower risk or whose beneficial ownership information may not be relevant to a financial institution's risk assessment or a law enforcement investigation.

  - Some commenters suggested that any customer due diligence regulation should also incorporate the same concepts of reliance applicable to the customer identification program rules.[10]

  - Several commenters requested that Treasury provide sufficient time for financial institutions to plan and budget for a cost-effective and efficient implementation process.

4:30 pm: *Conclusion of Public Hearing:* The co-chairs thanked all participants for attending and described the ongoing outreach process with respect to the ANPRM. In particular, Treasury intends to continue direct engagement with financial institutions, industry associations and other relevant stakeholders through a variety of regional and industry-specific outreach events.

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[9] *See, e.g.*, 31 CFR §1020.100(c)(2).
[10] *See, e.g.*, 31 CFR §1020.220(a)(6).

Remarks by Under Secretary David Cohen

July 31, 2012

Thank you, Jamal.

Good morning, ladies and gentlemen, it is a pleasure to be here with you. It has been a long time since Treasury has hosted a public hearing such as this, so I would like to begin by welcoming you all to the Treasury Cash Room. We believe public engagement is essential to the development of effective rules; rules that help protect our financial system but also make sense for industry. We want to promote transparency in the regulatory process, as well as in the financial system. So, I am delighted to see so much interest in both the process and the topic of customer due diligence, something we believe is of the utmost importance.

Before I turn the podium over to my good friend Assistant Attorney General Lanny Breuer I'd like to touch briefly upon a few things.

At the outset, it is important to acknowledge that the U.S. anti-money laundering regime is one of the strongest and most effective in the world, anchored by strong preventive measures, effective implementation by financial institutions, and thorough investigations by law enforcement. But despite the strength of our regime, the scale, efficiency and sophistication of the U.S. financial system will always make it a target for those who wish to move illicit money.

Recent enforcement actions against financial institutions highlight the continued misuse of the financial system as well as the importance of compliance with legal obligations. The way I see it, the strength of our regime rests squarely on three things: (1) clear and sufficient AML requirements; (2) vigorous implementation by industry; and (3) thorough and effective financial investigations by regulators and law enforcement. So we're working with our interagency

partners, including the regulators, to take a step back and look at the AML regulatory framework and take stock of what's working and what's not. We're also engaging with industry, including through forums such as this, to gain a better understanding of implementation practices to see if there's more we can do to facilitate compliance.

And while we're looking at how best to strengthen and clarify our regulatory regime, simultaneously we're looking at ways to improve our use of BSA data to more effectively combat financial crime. We are collaborating with the Department of Justice and the law enforcement community more broadly to identify ways that we could more consistently and effectively take advantage of BSA and other data to proactively identify and advance investigations of money laundering and other financial crimes.

To meet the challenges of a complex and ever-evolving financial system, we must work together to ensure that our anti-money laundering requirements for financial institutions continue to be clear, strong, and effective in protecting the financial system, including by facilitating financial transparency.

Financial transparency, of course, has long been recognized as paramount to protecting the U.S. and global financial systems from all manner of illicit financial activity, from proliferation financing to terrorist financing to more traditional forms of financial crime like money laundering, tax evasion, and securities fraud. Key to financial transparency, we believe, is understanding beneficial ownership.

Over the past several years, we have worked extensively with industry stakeholders, government colleagues, and international counterparts to address the challenges to financial transparency and facilitate access to beneficial ownership information. We believe the solution lies in an approach that includes the revised international standards, issued earlier this year by the

Financial Action Task Force, that clarify the global standards related to customer due diligence and the transparency of legal entities and trusts; legislation that would enhance law enforcement's access to meaningful beneficial ownership information for legal entities formed in the United States; and a clearer customer due diligence regulatory requirement, including the possibility of an express obligation to collect beneficial ownership information.

While we will maintain our call for legislation that will require beneficial ownership information at the time of legal entity formation, and we will continue to work with international counterparts to promote global implementation of clear and effective international AML standards, today's conversation centers on the third prong of this strategy: the development of a regulation to clarify and strengthen customer due diligence.

As I'm sure you're all well aware, by CDD I mean identifying and understanding your customer and monitoring the relationship for suspicious activity; but in order to do this effectively you also must know the beneficial owner of the customer. So a financial institution must do more than just know its immediate customer, the account holder. To effectively conduct CDD, an institution must know and understand the beneficial owner of its customer.

Despite the common understanding that CDD is necessary to comply with U.S. law, our regulations do not now have an explicit and clear CDD rule. We understand that financial institutions generally are expected to perform some sort of CDD to meet their BSA obligations; however, the obligation to collect beneficial ownership information currently is only explicitly required in very limited circumstances, or as a potential risk mitigant for higher-risk scenarios.

In a first step towards addressing this issue, earlier this year FinCEN issued an ANPRM designed to solicit your comments on a wide range of questions relating to the development of a possible CDD rule. The ANPRM specifically requests input related to the identification and

verification of the beneficial owners of a financial institution's customers. While many issues for comment center around the topic of beneficial ownership, we know there are a number of other issues weighing on the minds of both industry and the public sector.

Your responses to these and the other questions posed in the ANPRM have been instrumental as we move forward to consider whether and how to implement a customer due diligence rule with a specific beneficial ownership component. Regardless of precisely how we resolve this regulatory issue, we remain convinced that we can – and, indeed, must – improve financial transparency so that, together, we do an even better job of combating illicit financial activity.

We understand that different financial sectors present unique complexities and nuances that make a 'one-size-fits-all' approach potentially problematic. So, while we seek to promote consistency across sectors, we will look closely at sectoral differences as we work to determine what makes the most sense, carefully balancing costs and benefits.

As we move forward, we are committed to doing so together, in a manner that is both sensitive to regulatory burden and calculated to improve the quality of the U.S. AML regime. If we are going to develop regulation that meets our objectives, assists you and your institutions in identifying and managing risk, and accomplishes all this in a manner as simple and clear as possible, then public engagement is a must. Today's public hearing is an important step in this process. Your input is essential to the development of a clear and effective CDD rule.

So thank you all for coming today. I'm sure it will be a useful and enlightening event. I encourage everyone to think of this ANPRM as an opportunity to begin thinking about how to improve our framework. I hope you all use today's discussions to plot a path forward. And I am

confident that, collectively, we will seize this opportunity to strengthen our regulatory framework and further protect our financial system from illicit abuse.

GLOBAL FINANCIAL INTEGRITY

Out of Testimony by Raymond Baker
Director, Global Financial Integrity
For the Customer Due Diligence Public Hearing
Department of Treasury, July 31, 2012

I. The problem of accounts without known beneficial owners.

a. Corporations, trusts, and accounts without known beneficial owners are one of the most commonly used tools by money launderers and criminals to hide money and transactions.
b. Recent examples of abusers include: the Zeta drug cartel, Al Qaeda, rhinoceros poachers in Africa, arms dealer Viktor Bout, and the son of the corrupt dictator of Equatorial Guinea.
c. Closing the beneficial ownership loophole would be the single most important step toward stemming the flow of illicit money.

II. Why banks should be required to identify the beneficial owner of their accounts.

a. Our research estimates that about $1 trillion in illicit financial flows leaves the developing world every year. Of this, about $500 billion a year winds up in western bank accounts, including in the United States.
b. Modern-day globalized, billion-dollar transnational organized criminal organizations would not be able to function on the scale that they do without access to bank accounts.
c. Criminals use corporations to hide their connection with bank accounts. Unless a bank is required to look beyond the corporate vehicle, it is very difficult to know if it is doing business with a criminal or high risk client.

III. Definition of beneficial ownership

a. Must be clearly defined and include the concept of control.
b. Taking into account the current international standard for customer due diligence as established by Congress via FATCA, beneficial ownership should be defined as at least:
    i. Each of the natural persons who, directly or indirectly, through any contract, arrangement, relationship, intermediary, tiered entity or otherwise, owns more than 10 percent of the equity interests in the entity; or
    ii. If there is no natural person who satisfies (a), then the individual(s) who, directly or indirectly, through any contract, arrangement, relationship, intermediary, tiered entity or otherwise, has at least as great an equity interest in the entity as any other individual; **and**
    iii. The individual(s) who, directly or indirectly, exercises control of the legal entity by any other means (if any).
c. If it is not possible to identity any natural persons meeting criteria set forth in (b.i) or (b.ii), the covered entity has failed to identify the beneficial owner. If this is the case, the covered entity should treat the account as a high-risk account and be

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required to justify any decision to open an account for such potential client to the head of compliance.

IV. Conclusion

There is no persuasive argument to be made not to know with whom you are doing business. Financial institutions should not be allowed to be willfully blind to their role in the money laundering process. Without knowing the beneficial owner of a corporation, it is difficult to impossible for financial institutions to accurately assess money laundering vulnerabilities.

global witness

FinCEN's CDD Public Hearing – July 31, 2012

Outline of Testimony

Stefanie Ostfeld

Global Witness

I. How the financial system enables grand corruption and perpetuates poverty
   a. Banks are the first line of defense against corrupt funds, as well as terrorist finance and the proceeds of drug trafficking, organized crime and tax evasion.
   b. Shell companies, trusts and other corporate vehicles are easily used to disguise ownership in order to access the financial system.
   c. There are many examples of shell companies being used as vehicles for laundering the proceeds of state looting, corruption and other ill-gotten money.

II. Why financial institutions must be required to obtain and verify beneficial ownership information for all accounts
   a. There are loopholes in U.S. law.
      i. Financial institutions covered by U.S. anti-money laundering requirements, with few exceptions, are not required to identify the beneficial owner of all accounts in which the customer is not an individual. As noted in the Financial Action Task Force's (FATF) Third Mutual Evaluation Report on Anti-Money Laundering and Combating Financing of Terrorism: United State of America, the U.S. Customer Identification Program rules, "...do not require a financial institution to look through a customer that is an entity to its beneficial owners."
      ii. There is far too little beneficial ownership information available to covered institutions or in the public domain.
   b. If a bank does not know the identity of the beneficial owner of an account, it cannot meaningfully assess risk.

III. Defining beneficial ownership
   a. A beneficial owner is a person; it is not a company or other corporate vehicle or a nominee.
   b. In brief, the beneficial owner is the person who profits from and exerts control over the corporate vehicle.
   c. The term beneficial ownership must be clearly defined and must include the concept of control.
   d. The definition proposed by FinCEN in the ANPRM places too great an emphasis on percentage ownership as opposed to the concept of control.

e. Greater harmonization of the concept of beneficial owner would reduce confusion – financial institutions should use one definition in their CDD obligations for all non-individual accounts, including accounts that under the PATRIOT Act, have previously been reviewed under a different definition.
f. Taking into account the current international standard for customer due diligence as established by Congress via FATCA, beneficial ownership should be defined as at least:
    i. Each of the natural persons who, directly or indirectly, through any contract, arrangement, relationship, intermediary, tiered entity or otherwise, owns more than 10 percent of the equity interests in the entity; or
    ii. If there is no natural person who satisfies (a), then the individual(s) who, directly or indirectly, through any contract, arrangement, relationship, intermediary, tiered entity or otherwise, has at least as great an equity interest in the entity as any other individual; **and**
    iii. The individual(s) who, directly or indirectly, exercises control of the legal entity by any other means (if any).
g. If it is not possible to identity any natural persons meeting criteria set forth in (f.i) or (f.ii), the covered entity has failed to identify the beneficial owner. If this is the case, the covered entity should treat the account as a high-risk account and be required to justify any decision to open an account for such potential client to the head of compliance.

IV. What banks must do

a. FinCEN must require covered institutions to identify and verify both the identity of the real person who is the beneficial owner of each account, and that they are in fact the beneficial owner of the legal structure. This must include making a judgment on the reasonableness of the beneficial ownership information provided to them, including whether the corporate structure appears to be reasonable given the business activity of the client.
b. Banks must also be required to continue to monitor accounts to determine if there is any change in beneficial ownership.
c. If a bank is unable to identify the beneficial owner of an account, it should not accept the business, as laid out in the FATF standard.

V. Impact of the U.S. strengthening its anti-money laundering framework on the rest of the world

PRELIMINARY OUTLINE FOR ORAL PRESENTATION
OF
THE CLEARING HOUSE ASSOCIATION L.L.C
BEFORE
FINANCIAL CRIMES ENFORCEMENT NETWORK
ON
CUSTOMER DUE DILIGENCE FOR FINANCIAL INSTITUTIONS

JULY 31, 2012

I. Introduction.

A. Brief description of The Clearing House and its involvement in AML issues.

B. Brief summary of The Clearing House's position on the general CDD proposal.

1. The Clearing House supports a clear CDD rule to clarify FIs' responsibilities regarding CDD.

2. The Clearing House supports a three-tiered CDD program for FIs.

a. Identification of all customers—the same as the current CIP requirement.

b. Basic due diligence applied to all customers to obtain sufficient information to allow the bank to categorize a customer's risk. Based on the risk characteristics of the customer, the FI may decide to obtain additional information from the customer.

c. Enhanced due diligence applied to customers that are high risk for money laundering or terrorist financing.

C. Our presentation will concentrate on the beneficial ownership proposals.

III. Beneficial ownership information.

A. FinCEN's proposal has three main components: (1) expanded requirement to obtain beneficial ownership information to all customers; (2) requirement to verify the beneficial ownership information in certain circumstances; and (3) expanded definition of beneficial owner.

B. The Clearing House supports a reasonable expansion of the requirement to obtain beneficial ownership information.

C. The definition of *beneficial owner* is crucial. If this isn't right, the information obtained will not be useful for banks or law enforcement.

1. There are multiple possible definitions of beneficial owner that are useful to financial institutions and law enforcement depending on the circumstances. FinCEN must be clear about the purpose of a beneficial owner identification rule in order to determine which of these various definitions is appropriate for a CDD rule.

2. What's crucial is the person who has control over the account rather than a passive owner or a person whose sole connection is an entitlement to the assets in the account, e.g., a trust beneficiary.

a. The current definition of *beneficial owner* found in FinCEN's regulations regarding private-banking accounts captures that concept well.

b. The proposed definition is confusing and may not identify the person law enforcement is interested in.

3. FinCEN's treatment of intermediaries causes particular issues:

a. Correspondent accounts.

i. A correspondent account is a debt that the FI owes to the correspondent banking customer. The customer's customer has no claim to the balance. Asset forfeiture does not depend on ownership of the balance in the account.

ii. U.S. banks generally do not open correspondent accounts unless they are comfortable with the customer's AML controls and the customer's home country.

iii. Use of risk-based transaction monitoring allows a US bank to detect unusual or suspicious behavior.

b. Private banking accounts.

i. The current definition, which emphasizes the person with control or entitlement to the balance of the account or other assets in the account, works well.

c. Nominee accounts.

i. Where the U.S. bank holds an account for a nominee, the nominee should be regarded as the customer.

ii. Where the bank is itself a nominee, it should have information on its principal.

D. Exemptions to the requirement to obtain beneficial ownership information.

E. Verification of beneficial ownership information.

1. Should be required only in certain high-risk circumstances.

2. Should focus on verifying the beneficial owner's identity, not status as beneficial owner.

a. Given the absence of ownership registries for non-personal entities, it is almost impossible to verify the fact of ownership.

sifma

Invested in America

PRESENTATION OF
BETTY SANTANGELO
PARTNER, SCHULTE ROTH & ZABEL LLP
COUNSEL FOR SIFMA AML COMMITTEE
ON BEHALF OF
SECURITIES INDUSTRY & FINANCIAL MARKETS ASSOCIATION (SIFMA)
BEFORE THE
FINANCIAL CRIMES ENFORCEMENT NETWORK
U.S. DEPARTMENT OF THE TREASURY
JULY 31, 2012

INTRODUCTION

Good morning. My name is Betty Santangelo and I serve as counsel to the Securities Industry & Financial Markets Association (SIFMA) Anti-Money Laundering and Financial Crimes Committee (AML Committee). SIFMA and its AML Committee very much appreciate the opportunity to appear before you today to provide comment on FinCEN's Advance Notice of Proposed Rulemaking pertaining to Customer Due Diligence (CDD) Requirements for Financial Institutions.

As you may know, SIFMA brings together the shared interests of hundreds of securities firms, banks and asset managers. SIFMA's mission is to support a strong financial industry, investor opportunity, capital formation, job creation and economic growth, while building trust and confidence in the financial markets. Since 2001, SIFMA's AML Committee has worked with both regulators and the securities industry to address AML regulatory and legislative issues, as well as to foster broker-dealers' compliance with their AML responsibilities in a way that is both effective and efficient.

SIFMA has long been a strong supporter of AML efforts. Both prior to and since the passage of the USA PATRIOT Act of 2001, SIFMA has worked with our members to develop and implement policies and procedures to detect and deter money laundering and other illicit activities. Since its inception, the AML Committee has undertaken a number of initiatives to assist its members in addressing their AML responsibilities. SIFMA also offers its members opportunities for AML education through conferences, seminars and meetings, and has submitted comment letters to regulators on various issues pertaining to the deterrence of financial crime.

SIFMA strongly supports the efforts of FinCEN in working with financial institutions to implement robust, risk-based anti-money laundering (AML) compliance programs. We also strongly support FinCEN's goal of creating greater transparency and harmonizing and clarifying expectations relating to CDD. We are especially appreciative of FinCEN's outreach to the securities industry and its willingness to engage in open and meaningful dialogue on this topic, including today's public hearing. We remain committed to continuing our dialogue with FinCEN and welcome this opportunity to provide input into the rulemaking process.

As you are aware, we have already submitted our comment letter on June 8th providing you with detailed comments on the ANPRM. We would like to highlight for you some of our key comments with respect to the proposed CDD rule and other concerns, which we addressed in our June 8th comment letter. In summary form, our comments are as follows, and are addressed more particularly to the questions raised in FinCEN's notice of the Public Hearing:

•*Complexities of the Securities Industry*. FinCEN should take into account the complexities and unique nature of the securities industry when crafting any proposed CDD rule to ensure that a final rule effectively mitigates potential money laundering risks. As FinCEN is aware, the industry is comprised of many types of firms (e.g., retail, institutional, clearing, and online) and offers various and numerous products (e.g., equity,

fixed income, options and derivatives). Customers are varied and include trusts, omnibus accounts, and pooled investment vehicles. Any proposed CDD rule needs to take into account the various types of firms involved and the products offered.

•*Risk-Based Requirements*. Consistent with the risk-based concept that is embedded in the AML regulations and with international standards, any CDD requirements should be risk-based. If the collection of beneficial ownership data is to be included in the CDD process, both the collection of the data and the verification requirement should be implemented on a risk-based basis, allowing for securities firms to make a meaningful assessment that is tailored to their business.

•*Beneficial Ownership Definition*. As presently crafted, the Proposed Definition of beneficial ownership is vague, difficult to implement from an operational perspective, may cause confusion because it conflicts with other beneficial ownership definitions (e.g., FATCA and Section 312 of the PATRIOT Act) and does not readily fit all types of customer relationships (e.g., trusts, omnibus relationships and pooled investment vehicles).

•*Verification.* Where identification and verification of beneficial ownership is deemed by the financial institution to be appropriate, given the difficulty in verifying beneficial ownership, verification of beneficial ownership should be limited to verifying the identity of the beneficial owner, and not verifying beneficial ownership status.

• *Existing Customers*. All four elements of any proposed CDD rule (unless Element Four pertains to compliance with the SAR Rule) should not apply to existing Customers, unless they are limited to event-driven situations.

•*Exemptions.* Existing exceptions from the CIP Rule should be applied to the proposed CDD rule and any beneficial ownership requirement. In addition, these exemptions should be expanded to include certain lower risk entities, such as those referenced in the Incorporation Transparency and Law Enforcement Assistance Act, or H.R. 6098, and

should be applied to the identification/verification of beneficial owners. Financial institutions should be allowed to use a risk-based approach in assessing what is a low-risk account/customer.

•*Proposed CDD Rule Timing.* Any proposed CDD rule should include 1) a sufficient time period to implement the rule, 2) provide for a reasonable time period to perform CDD consistent with the CIP Rule, and 3) provide for an effective implementation date going forward, as material aspects of any proposed CDD rule will be new requirements.

•*Trust Accounts*. Because the Proposed Definition focuses solely on entities, it does not adequately explain how it would apply to certain types of legal vehicles, such as trusts, which present unique challenges. For example, there are usually, but not always, multiple parties involved in the formation of a trust and in the oversight of a trust. Providers of funds (e.g., settlors/grantors), those who have control over the funds (e.g., the trustees), and any individuals who may have the power to add or remove the trustees may meet the Proposed Definition of beneficial owner. There are also beneficiaries of the trust, who can change over time based on the terms of the trust, and may not even know that they have been named as trust beneficiaries. As a practical matter, and consistent with guidance from FinCEN, securities firms conduct CIP on the trust itself. They also identify the trustee but may or may not verify that identity because the trustee is not the Customer. Grantors and settlors are usually identified, and in high risk jurisdictions, firms will sometimes verify the identity of the grantor/settlor. However, beneficiaries of trusts should not be part of the "beneficial ownership" definition. Given the complexity of this legal vehicle, FinCEN should simply identify the information required for a trust.

• *Intermediaries*. The role of the intermediary is integral to the efficient function of the securities industry, particularly in the institutional market place. The CIP Rule recognizes the intermediary as the broker-dealer's Customer. Regardless of whether the intermediaries are regulated for AML purposes, in all cases, they are better suited to perform due diligence functions with respect to their own customers. Existing guidance related to the CIP Rule makes clear that where intermediaries are involved, the broker-

dealer's "formal relationship" is with the intermediary, even where an omnibus relationship/account is involved. Under Treasury's existing guidance, as a general matter, a broker-dealer is permitted to treat the intermediary as its Customer and should not have to "look through" the intermediary to identify or verify the clients on whose behalf the intermediary is acting. The continuted application of these principles to the CDD rule is essential, in our view, to the efficiency of the market place.

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Thank you for giving SIFMA the opportunity to appear today at this public hearing and provide our comments on the Proposal. We look forward to the continued partnership between government and industry to strengthen the regulatory structure surrounding securities firms and other U.S. financial institutions.

From: David Landsman, Executive Director
National Money Transmitters Association, Inc.
12 Welwyn Road, Suite C
Great Neck, NY 11021

Dear Sir or Madam:

This is to request permission to attend and, if possible, speak briefly at the subject hearing, representing the members of the National Money Transmitters Association. We would like to register our strong objection to any further CDD rulemaking. The following points constitute what would basically be the complete text of our remarks:

1. *What* is being proposed, is not clear. The purpose of the ANPRM seems to be information gathering, but gives no specific proposals so, in a strict sense, there is nothing yet to comment on. No indication is given as to how new rules night be different than what is already in place.
2. *Why* FinCEN believes new rules are needed has not been explained. FinCEN clearly has the *power* to issue such a rulemaking, but Congress has not passed any new laws, nor have any unusual events occurred, that would seem to have prompted or *require* this rulemaking. Also, it is not clear what role the banking agencies would have in the crafting and implementation of this new rule.
3. Government should focus on prescribing minimum requirements, and not venture into prescribing best practices too specifically. Trying to draft such rules always results in guidelines that are paradoxically too vague and too prescriptive at the same time. Implementation therefore usually results in institutions tightening too much in some places, and loosening too much in others. Additional codification, by itself, runs the risk of tightening too much and cutting off legitimate commerce.
4. Further standardization and clarification is not needed and is not going to help. Expectations are already known and clear enough. Any new rulemaking would be unnecessary and redundant. There is no reason to believe more verbiage will improve compliance. Financial institutions have plenty of guidance right now, and some behave badly in spite of it.
5. The ANPRM does not explain how it would be different than the KYC rulemaking attempted by three banking agencies and withdrawn 21 days after it was proposed, back in 1999. The history of that effort must have some lessons we can learn.
6. The money transmitter industry, at least the small-to-mid-size money transmitters and our agents, would need special protection from the possibility that this rulemaking will result in further account closures. Specific care must be given to defining beneficial ownership expectations, and to the question of guidance on how deeply the bank's customer's customers will have to be scrutinized. This applies especially to foreign financial institutions, who must have a way to clear their US transactions.
7. The real problem with verifying beneficial ownership will not be addressed by this rulemaking. In the United States, such information is not required on any corporate filings so it is literally impossible to verify through any official documentary procedure. With no upper limits on expectations, and no upper limit set to the banks' potential liability, banks will never be able to feel comfortable that they have done sufficient due diligence. Even if beneficial ownership disclosure were required by every state, secret ownership arrangements are, and always will be, easy to hide. Customers can simply lie. Ultimately, for all but the largest accounts, financial institutions need to be able to – and *must* be allowed to - rely on customers' self-

certification of beneficial ownership. Otherwise, we instill a presumption of customer guilt that is inimical to the free flow of commerce.

8. Public confidence in using the legitimate financial system would be harmed by real or perceived invasions of privacy.
9. Compliant institutions of all financial service sectors, but especially banks, will be unfairly disadvantaged in the marketplace by uneven expectations, transactions driven underground. Such uneven tightening would incentivize more malefactors to use less-regulated channels.

Thank you for holding this hearing, and for the opportunity to comment.

Regards,

-David

INVESTMENT COMPANY INSTITUTE

1401 H Street, NW, Washington, DC 20005-2148, USA
202/326-5800 www.ici.org

July 23, 2012

By Electronic Transmission

Re: RIN 1506-AB15: Request to attend and/or provide oral comments

Dear Mr. Colucci:

As discussed in the attachment, the Investment Company Institute ("ICI")[1] would appreciate the opportunity to provide comments at the July 31, 2012 public hearing on the advance notice of proposed rulemaking concerning customer due diligence obligations for financial institutions.

(1) Name of Person(s) Wishing to Attend and/or Provide Comments

Oral comments would be provided by Thomas C. Bogle, Dechert LLP, as legal counsel to the ICI. ICI requests that Jeanette Wingler of Dechert LLP also be permitted to attend the public hearing.

(2) Contact Information

Both Mr. Bogle and Ms. Wingler are with Dechert LLP, 1775 I Street NW, Washington, DC 20006, and may be reached by phone at (202) 261-3300 or by email at thomas.bogle@dechert.com and jeanette.wingler@dechert.com.

(3) Organizations Represented

Mr. Bogle and Ms. Wingler represent the Investment Company Institute.

Attached is a two-page outline of the topics the ICI wishes to address at the hearing. If you have any questions concerning this request, please contact me at (202) 326-5813.

Sincerely,

Susan M. Olson
Senior Counsel – International Affairs

[1] The Investment Company Institute is the national association of U.S. registered investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $12.9 trillion and serve over 90 million shareholders.

Topics for July 31, 2012 Hearing on Customer Due Diligence ANPRM

The Investment Company Institute ("ICI") would appreciate the opportunity to provide comments at the July 31, 2012 public hearing on the advance notice of proposed rulemaking concerning customer due diligence ("CDD") obligations for financial institutions (the "ANPRM").[1] Specifically, the ICI would appreciate the opportunity to provide comments on the following matters:

- The statutory authority on which the ANPRM is premised. As discussed in ICI's comment letter dated May 4, 2012 ("ICI Letter"), the legislative history of the USA PATRIOT Act makes clear that Congress never intended for mutual funds to be required to identify or verify beneficial owners as part of their Bank Secrecy Act ("BSA") obligations. The Financial Crimes Enforcement Network ("FinCEN") should acknowledge this legislative history as part of any CDD rulemaking, and address the precise statutory authority for proposing to subject mutual funds to beneficial ownership requirements.[2]

- The treatment of intermediated accounts. ICI commends FinCEN for seeking additional comment on the challenge of performing CDD and obtaining beneficial ownership information in connection with intermediated accounts. A substantial amount of mutual fund assets are held through intermediaries, which increasingly are using omnibus accounts to transact with mutual funds. Under these circumstances, mutual funds are not in the best position to conduct CDD or obtain reliable information about beneficial owners. As requested, at the hearing we will address due diligence practices in the context of mutual fund intermediated accounts.

- Allowing financial institutions to obtain beneficial ownership information using a risk-based approach. ICI strongly believes that financial institutions should be allowed to follow a risk-based approach in determining when to obtain beneficial ownership information.[3] Consistent with the approach taken under other BSA rules, financial institutions should conduct a risk assessment of their businesses, and document the circumstances under which they will obtain information about a customer's beneficial owners on a risk-based basis.

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[1] Customer Due Diligence Requirements for Financial Institutions, 77 FR 13,046 (proposed March 5, 2012), available at http://www.gpo.gov/fdsys/pkg/FR-2012-03-05/pdf/2012-5187.pdf (the "ANPRM").

[2] In addition, because the ANPRM incorporates many of the elements of Section 326 of the USA PATRIOT Act, ICI believes that any CDD rule applicable to mutual funds should follow the procedural requirements of Section 326, and be adopted jointly by FinCEN and the appropriate federal functional regulator.

[3] For example, a financial institution should not be required to obtain beneficial ownership information in cases where the financial institution is not required to verify the customer's identity under the Customer Identification Program rules.

- The expected costs and benefits associated with complying with a CDD rule. Since the parameters of the CDD rule under consideration are uncertain at this time, it is impossible to reliably estimate the costs associated with an explicit CDD obligation. However, because CDD (as described in the ANPRM) represents a fundamental change in the existing BSA obligations of mutual funds, and since mutual funds are not currently subject to suitability obligations, ICI believes that mutual funds will be impacted disproportionately by a new CDD rule (*e.g.*, requiring a fund to assess the "purpose" of an investment or an investor's "expected account activity"). In addition to these concerns about *costs*, ICI questions the *benefit* of requiring financial institutions to obtain information about beneficial owners of legal entities, since financial institutions currently do not have a reliable mechanism for verifying such information with relevant state authorities. These concerns about costs and benefits should be carefully evaluated before proposing a CDD rule applicable to mutual funds.

- The proposed definition of "beneficial owner" in the ANPRM. As discussed in the ICI Letter and numerous other comment letters, the definition of "beneficial owner" in the ANPRM is vague and unworkable. Approaches used outside the United States for identifying controlling beneficial owners should be considered. Ownership thresholds are clear and understandable and are used globally in many FATF member jurisdictions.

We look forward to working with FinCEN to address these issues, and appreciate your consideration of our request to provide comments at the July 31 public hearing.

My name is John W. Moscow. From August 1972 through December 2004 I served as an assistant district attorney—a prosecutor—in the New York County District Attorney's Office, starting with Frank S. Hogan and continuing for the past thirty years with Robert M. Morgenthau. Over the last twenty five of those years I personally prosecuted and supervised the prosecution of sophisticated economic crimes involving large and small scale international theft, fraud, and, of necessity, money laundering. I am pleased to comment on proposed FinCEN regulations requiring financial institutions to know the beneficial ownership of accounts which they maintain.

In talking about money laundering I bring to bear a perspective which is uniquely my own, with a background that not everyone here shares. I am not a banker, nor a bank regulator. I do not work for a Fortune 500 company, or a trade association. I speak for myself.

Money is power. The ability to move money without detection is the ability to exercise power without being held accountable for the uses to which the money is put. From the funding of narcotics dealers, to the protection of plutocrats destroying the economies of their home countries to put money aside for themselves, their families, and friends; to the destruction of the tax bases of the industrialized nations, and the use of foreign funds to swing elections and all the horrible corrosive consequences to the idea of government legitimacy that entails, the reality of money laundering through financial institutions must be of concern to us all.

I prosecuted economic crimes, sophisticated and simple, which make up the criminal side of the white-collar world in Manhattan. I have dealt with securities frauds, frauds against government agencies, tax shelter frauds, and corruption cases. Starting in 1989 I examined or prosecuted the Bank of Credit and Commerce, International (BCCI), certain aspects of the collapse of the Venezuelan banking system, events at the Bank of New York, the involvement of New York banks with Enron and a number of substantial international securities frauds involving victims from around the world. My views are those of someone who has sought to gather evidence of financial crimes, and has seen that evidence withheld.

First some definitions are in order. There are statutes in numerous jurisdictions making "money laundering", as variously defined, a crime. And money laundering should be a crime. But it is more important to consider what money laundering really is, a process of concealment, than to get caught up in trivializing definitions.

"Money laundering" is the concealment of evidence, in which a person seeks to evade responsibility for the ownership, origin or the use of funds. A person who seeks to launder funds wants to be able to use money to achieve results without having to accept responsibility for such results or the means used to achieve them. He or she wants the benefits of ownership, without any of its liabilities. And this result can be achieved by laundering money. Money can be laundered in a variety of ways, among them smuggling currency, unwritten underground banking transactions, use of banks in jurisdictions with bank secrecy, or corporate secrecy, or the inappropriate use of trusts.

The way to avoid the problems posed by money laundering is to require financial institutions to know the beneficial owners of the funds that they are handling. As you know, this is what FATCA seeks to require abroad. But we must do the same at home.

In 1986 Congress passed an anti-money laundering law which has dramatically changed the face of American law enforcement, even though it did not make illegal the transfer of funds to US banks from such national leaders as Marcos, Salinas, Mobutu, Suharto, Abacha or Pinochet.

Bank regulators have, over the past nineteen years, adopted the anti-money laundering cause as their own. Entire new bureaucracies have been created within the ranks of the regulators and the regulated to deal with the problem; this aspect of the war against drugs looks as though it has become an employment tool. With the passage of the USA PATRIOT Act in October 2001 anti-terrorism was added to the tasks anti-money laundering personnel are supposed to undertake.

Entire new regulatory entities—the Financial Action Task Force, Financial Stability Forum, and now even groups from OECD—have sprung up to measure compliance with anti-money laundering suggestions, best practices or regulations. And, while that has been going on, there has been a serious change in emphasis over time from fighting the narcotics trade to fighting terrorism to collecting taxes.

When Bob Morgenthau started to fight bank secrecy statutes, many countries took the view that it was not their place to enforce the tax laws of another country. They wanted to have bank secrecy in place so that they could profit by assisting people with commission of "fiscal" offenses' or tax fraud. It appears that much of the social acceptance underlying this was based on the post-World-War II tax regime in England (and much of Europe) under which Labor governments set levels of taxation of income and estates so high that much of society was quite willing to violate the law, or at least was willing to support ostensible lawful excuses for tax evasion.

Great Britain, after World War II, became an intellectual centre of bank secrecy practices, designed by the upper classes to protect their family wealth from confiscatory taxes; the intellectual heritage of that tradition continues today, even though the facts have changed enormously since then. Crown colonies and Crown dependencies such as Jersey, Guernsey, Isle of Man, Gibraltar, and Cayman started as offshore financial jurisdictions to assist UK residents. But the tradition of asking no questions left those money centers wide open to abuse by others than British aristocrats seeking to preserve their inherited wealth.

Narcotics dealers, and the money launderers they employed starting in the 1970s, gleefully exploited then existing bank secrecy practices originally adopted to protect mere tax evaders. The money-launderers' use of bank secrecy statutes became the stuff of legend, and fraudsters seeking to hide money other than tax money and narcotics proceeds started to use the same techniques.

By the mid 1990s the European Union and the United States were beginning to attack tax havens bitterly. For the governments it was and still is, a matter of survival. As transnational corporations manage their affairs to minimize taxes paid, they deprive all governments of tax revenue. In Europe and the United States the middle classes have been following their lead. For those of us who believe in the rule of law, depriving democratic governments of revenue by manipulating the laws of offshore havens is exceptionally bad government.

Congress, in dealing with the problem of Americans hiding assets offshore, passed FATCA, which requires Foreign Financial Institutions to know whether the ultimate beneficial ownership of financial accounts is American, or otherwise.

FinCEN, in parallel, should impose the same rules on domestic institutions, to accomplish anti-money laundering goals for reasons of fairness.

Following the attacks on the United States on September 11, 2001, Congress dealt with that in the USA PATRIOT Act, but the money launderers have changed their tactics, and are using corporate secrecy jurisdictions and trusts to hide the identity of the principals for whom they act.

We should work together to establish the rule of law, worldwide. For the reasons I describe below we should join to abolish bank secrecy laws and practices, including corporate secrecy laws and abusive trusts, insofar as they keep evidence from prosecutors and courts. We should abolish corporate secrecy even in states of the United States or at least deny those corporations access to the banking system. We should refuse to deal with anonymous corporations without requiring accurate disclosure of their beneficial ownership while allowing their corporate form to protect investors from risk. We should bar anonymous trusts through which billions of dollars a year pass without the beneficial owners' identities being known as it should be, much less being published, for which there is no good reason.

We should make sure that we know or when necessary can learn which people are responsible for each amount of money going through financial institutions. Keep in mind that prosecutors and counter-terrorism agents need evidence to proceed. They need real evidence, not tick marks in boxes on forms. An agent who asks for the name of the person who authorized a transfer of money does not want to be told that the transfer was authorized by a British Virgin Islands company established in Tortola by a Mexico City law firm at the request of a Swiss lawyer who said that his unnamed client was highly valued. The question was "who authorized the transfer?" The answer should be a name. The regulations should require this.

We have, since the passage of the Bank Secrecy Act, made bank secrecy unacceptable in polite society. It has lost much of its legitimacy.

But the people who seek to launder money have merely switched names; they now use corporate secrecy to evade accountability while claiming full formal compliance with KYC requirements. Even states in the United States are seeking revenue by enabling corporations to act without disclosure of the identity of their owners.

Without challenging state law FinCEN can bar such anonymous corporations from using U.S. financial institutions for their anonymous and unaccountable transactions. FinCEN should do so.

Just as Bank secrecy and Corporate secrecy need to be outlawed, trusts need to be accountable as well.

There is no reason why a trust, itself a creature of law, should not be required to disclose its trustees, protectors if any, other control persons, and immediate and ultimate beneficial

owners. I ran into a collection of trusts a few years ago, as to which a person other than the trustee (or the Grantor) had the right to decide whom the beneficiaries would be. That sort of "trust" is entirely unacceptable. Financial institutions dealing with self-styled "trusts" need to obtain, analyze and read the trust documents to make sure the Bank knows who the beneficiaries of the trust are. And if the matter is not clear, the Bank should not do the business.

As with all of the accounts a financial institution maintains, if the beneficial ownership cannot be ascertained the business should not be engaged in by the bank.

For all of these reasons, FinCEN should require all financial institutions to know the beneficial owners – down to the level of real human beings – of the accounts they maintain.

In the interests of fairness the FATCA standards should be applied to domestic institutions as well as foreign financial institutions.

Where the costs of identifying the beneficial owner are too high – leaving aside publicly owned businesses – the business should not be done.