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AUGUST 1, 2005

JEWELERS VIGILANCE COMMITTEE
INDUSTRY SEMINAR

NEW YORK, NEW YORK

Introduction

Good morning ladies and gentlemen. It is a real pleasure for me to be with you here at the Jewelers Vigilance Committee seminar: "How to Comply with AML Regulations." This is a great opportunity for me and for the Financial Crimes Enforcement Network to introduce to you our expectations under the Bank Secrecy Act. This regulatory program is new to the jewelry industry. It is, therefore, critical that we enter into a meaningful dialogue about our expectations. I want to thank Cecilia Gardner, Executive Director of the JVC, for inviting me to be here with you this morning. I also want to thank all of you, as top executives and leaders in the jewelry industry, for your constructive and helpful comments, insight and assistance during the development of the anti-money laundering program rule for dealers in precious metals, stones or jewels. I want you to know that I understand the commitment your industry has made to this effort, on both a domestic and global level, and I want you to know that I appreciate it.

Before I discuss the new rule, I'd like to say a few words about my agency, the Financial Crimes Enforcement Network, as I often find that many industry members that I speak with have only a general sense of who we are and what we do. The Financial Crimes Enforcement Network is the administrator of the Bank Secrecy Act, which means that we bear the responsibility for ensuring that the Act is implemented in a way that achieves the policy aims intended by Congress when it enacted, and subsequently amended, the Bank Secrecy Act. The principal policy goal of the Bank Secrecy Act is to safeguard the financial system from the abuses of financial crime, including terrorist financing, money laundering, and other illicit activity. We have implemented the Act to achieve this goal in two ways: First, by requiring each financial industry member that is subject to the Bank Secrecy Act to develop a custom made program, and adopt procedures, systems and controls to address the risk of money laundering and other illicit finance that are posed to that industry member by its business lines, locations and customer base; and, secondly, when appropriate, by maintaining records and reporting information to law enforcement that is highly relevant and useful in the detection, deterrence and investigation of financial crime.

This paradigm recognizes the simple fact that if the industry member is given the tools necessary to assess the risk – and that is an important point I want to come back to – the industry member is in a much better position than the government to design an anti-money laundering/counter terrorist financing program that will address the risks posed by its business lines and customer base. This paradigm also mandates a partnership between the government and industry. Without this partnership, the system is not as effective as it could be.

So, where do we come in? As the Administrator of this Act, we are the principal policy makers in implementing this statute, but we do not examine industry members for Bank Secrecy Act compliance. Instead, that function has been delegated to other federal regulators; in the case of the jewelry industry, the delegated federal agency is the Internal Revenue Service. In addition to setting policy under the Bank Secrecy Act, we collect and maintain the information that is reported by the financial industry under that Act, analyze it, disseminate and network the information and analysis to law enforcement and others, including other financial intelligence units around the world. We achieve this by issuing, interpreting, and enforcing compliance with regulations implementing the Bank Secrecy Act; supporting law enforcement, intelligence, and regulatory agencies through sharing and analysis of financial intelligence; building global cooperation with our counterpart financial intelligence units; and networking people, information and ideas.

The Congress, by amending the Bank Secrecy Act through the USA PATRIOT Act, required us to expand our basic anti-money laundering regime to a wide range of industries that had previously not been subject to regulation under that Act. That is where you come in, because one of the industry sectors the Congress mandated we look at is dealers in precious metals, stones or jewels. While new to the United States, regulation of this industry is not new to our European colleagues: European Union Directives as well as most European Union member and accession countries have established regulations addressing this industry sector. The decision to expand our regulatory regime to include this sector is based in large part on the experience of law enforcement and an assessment that these industries are potentially vulnerable to abuse by financial criminals.

Policy of Risk-Based Regulation

As is true of all of our anti-money laundering program rules, our approach to developing the anti-money laundering program requirements for dealers in precious metals, stones and jewels is risk-based. We believe effective implementation must be predicated upon your knowledge of your business, a careful assessment of the vulnerabilities of your business to money laundering and terrorist financing, and adoption of controls appropriate to that risk. For example, business conducted with other U.S. dealers subject to the rule, and established customers or suppliers, presents a relatively low level of risk. On the other hand, business conducted with parties located in jurisdictions that have been identified as particularly vulnerable to money laundering or terrorist financing, may present a higher risk, and therefore require greater diligence for detecting transactions that may involve money laundering or terrorist financing.

We designed both the proposed and interim final rules to provide individual dealers with as much flexibility as possible to tailor their anti-money laundering programs to the operations of their businesses. In this way, we can achieve our goal of guarding against money laundering without imposing undue burden. We do not expect any business's program to prevent all potential financial crime. We do expect businesses to take prudent steps to protect their businesses from financial crime, with the same kind of thought and care that they take to guard against theft or fraud.

The Interim Final Rule

On February 21, 2003, the Financial Crimes Enforcement Network issued for public discussion and comment a proposed rule to require dealers in precious metals, stones or jewels to establish written anti-money laundering programs reasonably designed to detect and prevent money laundering or the financing of terrorism. We sought to tailor our regulation to businesses that engaged in the type of transactions that may be most susceptible to abuse. Therefore, our focus in the proposed rule was on those businesses in the United States that both buy and sell precious metals, stones or jewels, given our conclusion that the most significant risks of money laundering or the financing of terrorism lie within those businesses that do both.

Furthermore, the proposed rule excluded most retailers from the scope of the regulation, based on the conclusion that retailers simply do not face the same level of risk. The elements of the anti-money laundering program outlined in the proposed rule mirrored those found in our regulations for other types of financial institutions.

During the notice and comment period for the proposed rule, we received many constructive and helpful comments from industry. We have benefited greatly from the insight and assistance of members of the industry as they explained their operations and assisted us in developing regulations tailored to their businesses. As a result of the comments received, we made a number of adjustments in the final rule, particularly in the regulatory definitions and exceptions thereto. For instance, in response to comments, FinCEN clarified in the preamble to the interim final rule that toll-refining does not constitute a purchase or sale of precious metals for purposes of the interim final rule.

The interim final rule requires dealers in covered goods to develop and implement written anti-money laundering programs reasonably designed to prevent the dealers from being used to facilitate money laundering and the financing of terrorist activities through the purchase and sale of covered goods.

At a minimum, an anti-money laundering program must:

- incorporate policies, procedures, and internal controls based upon the dealer's assessment of the money laundering and terrorist financing risks associated with its lines of business;
- designate a compliance officer who will be responsible for ensuring the effective implementation and operation of the anti-money laundering program;
- provide for on-going education and training of appropriate persons concerning their responsibilities under the program; and
- provide for independent testing to monitor and maintain an adequate program.

A "dealer" is defined as a person that both purchases and sells items that meet the definition of covered goods, in sufficient quantity to meet the $50,000 definitional thresholds. Therefore, a person that engages only in the sale of such products, for example a mining company that only sells precious metals that it mines, would not be covered by the definition. Similarly, a person who only engages in the purchase of such products, for example a person who purchases gold coins for gifts to family members, would not be covered by the rule. The interim final rule retains the minimum dollar threshold that was proposed, but has been modified to apply the threshold to both purchases and sales. This change reflects FinCEN's determination that a person that does not reach the $50,000 threshold for both purchases and sales is not of sufficient size or risk to be required to implement an anti-money laundering program.

One particularly frequent question we have received is why the rule is characterized as an "Interim Final Rule." Anticipating this question, we created a "Frequently Asked Question" that was published in the Interim Final Rule to explain the purpose of the interim final rule. In sum, the interim final rule gives us the flexibility to more narrowly tailor certain aspects of the rule in response to our request for additional public comment on four discrete issues, while still ensuring that dealers immediately begin to develop their anti-money laundering programs. The specific issues on which we requested comment included whether silver should be removed from the definition of a "precious metal," whether "precious stones" and "jewels" should be defined more specifically, for example, by reference to a minimum price per carat, and if so, how, and whether 50 percent is the appropriate value threshold for determining whether finished goods (including jewelry) containing jewels, precious metals, or precious stones should be subject to the rule. We also requested additional comment on the potential impact of the rule on small businesses that may be covered by the rule. The comment period closed July 25, and the 31 comments we received are posted on our website.
I commend to you the fuller discussion in the FAQ and in the preamble to the Interim Final Rule.

Two issues raised during the comment process merit particular attention and I'd like to discuss how those issues were addressed in the Interim Final Rule.

Application of the definition of "purchase" to trade-in transactions.

In commenting on the proposed rule, industry members told us that it is quite common for dealers and retailers in covered goods to allow retail customers to trade-in existing items for credit against the purchase of a new item. They also told us that if the rule were to treat all trade-in transactions as purchases, a large percentage of retailers would be unable to take advantage of the retailer exception. To address these concerns, the Interim Final Rule provides that, so long as the value of the trade-in is credited to the account of the customer, and so long as a dealer or a retailer does not provide funds to the customer in exchange for the trade-in, these transactions need not be taken into account in determining the dollar value of covered goods purchased. This "trade-in exception" only applies for purposes of determining who is a "dealer," and not to the scope of the anti-money laundering program required of a dealer. Therefore, a dealer that is not a retailer would be required to evaluate the risks posed by trade-in transactions in determining the appropriate program requirements, as it would with other transactions in covered goods.

Application of Retailer Exception to Retailers that Purchase from Foreign-Located Sources

As explained in the proposed rule, FinCEN believes that the risks of money laundering or terrorist financing are less significant in those businesses that engage primarily in retail sales of precious metals, stones or jewels. As proposed, the rule excluded from the requirement to establish an anti-money laundering program retailers that purchase products predominantly from other dealers subject to the rule.

The interim final rule continues to provide that so long as retailers generally purchase their covered goods from U.S.-based dealers and other retailers, the retailers will not be required to establish anti-money laundering programs. To the extent that a retailer's purchases from persons other than dealers subject to the rule, the retailer would be required to establish an anti-money laundering compliance program. However, the required program would only need to address such purchases, and would not be required to address sales, or purchases that would otherwise be exempt from the rule. We did this because of the risk-based nature of our approach to these regulations -- we believe that the anti-money laundering program requirement should be limited to guarding against the risks presented. Retailers that purchase excess inventory from other retailers from time to time would still be covered by the retailer exemption.

I want to tackle straight-on an issue that surfaced during the comment process and that has taken on a life of its own since publication of the Interim Final Rule. A number of commenters urged FinCEN to allow retailers to maintain their exception even if they purchase covered goods predominately from foreign-located sources, or to extend the exception to retailers that purchase from suppliers located in countries that are members of the Financial Action Task Force, known as FATF. As we explained in the preamble to the Interim Final Rule, these approaches ignore the very real risks of money laundering and terrorist financing through international sources of supply and are contrary to the approach generally taken by FinCEN with respect to other industries. The fact that a country is a member of the FATF does not mean that the country requires dealers located within its borders to implement a anti-money laundering program, much less an anti-money laundering program that is similar to that contained in this interim final rule. Thus, to extend the exception in the manner suggested would be contrary to the rationale underlying the exception.

While we have not previously recognized a dispensation even for financial institutions located in foreign jurisdictions with robust anti-money laundering requirements, we have always taken the position that such requirements will reduce, sometimes substantially, the risk posed by products and services offered by such financial institutions. Thus, purchasing covered products from a supplier located in a jurisdiction with a comprehensive anti-money laundering regime will be a strong factor for the U.S. dealer in assessing the overall risk posed by that foreign supplier.

Since adoption of the interim final rule, the rhetoric surrounding this issue has been ramped up considerably, with thinly-veiled charges that the rule acts as a trade barrier to protect U.S. dealers, or that the rule discriminates against small firms. Let me make our position clear.

1. **The anti-money laundering program requirement is not a trade barrier**.

As I explained before, the Bank Secrecy Act regulatory regime is all about risk management – it is about identifying and mitigating risk. Under the Bank Secrecy Act, financial institutions are required to identify and mitigate the risk that their business will be abused by criminals and terrorists. Risks can be jurisdictional, product-related, service-related, or client related. Regardless of where those risks arise, financial institutions covered by our regulations must take reasonable steps to mitigate them. Compliance is risk-based, meaning that financial institutions must devote more compliance resources to the areas of its business that pose the greatest risk. Moreover, as is true for all industries we regulate, we do not expect businesses of different sizes and circumstances to have the same types of anti-money laundering programs.

As is the case with respect to depository institutions, securities dealers, and other financial institutions, we have required U.S. based dealers in precious metals, stones or jewels to establish anti-money laundering programs reasonably tailored to the risks of money laundering and terrorist financing posed by those businesses.

The Interim Final Rule recognizes that a dealer that purchases covered products from another dealer that is subject to our regulation will generally face less risk than a dealer that purchases covered products from a business that is not subject to our regulation. This does not mean that all foreign dealers pose a higher risk of money laundering. It does mean that the risks posed by a foreign supplier must be evaluated.

It is possible that a foreign-based supplier will have a robust anti-money laundering program, either because such a program is required by another jurisdiction or to facilitate the sale of covered products to the United States. A U.S. based dealer will look to the existence of such a program when evaluating the risk posed by the foreign supplier and correctly identify the risks as lower.

Further, the fact that a U.S. dealer has to adopt an anti-money laundering program to address purchases from foreign suppliers does not mean that compliance will be prohibitively expensive or burdensome. In fact, in cases where U.S. dealers have relationships with established suppliers in well-regulated jurisdictions, the costs should be minimal. For example, representatives from the diamond industry have confirmed repeatedly that the business is characterized by close relationships between dealers and suppliers. In such cases, compliance with our regulation – taking reasonable steps to identify and mitigate the risk that the purchase of diamonds from a supplier would involve money laundering or terrorist financing – should be no more than a natural extension of existing policies and procedures, and quite simple to implement.

Finally, since the United States must import diamonds, there is no trade barrier on foreign suppliers vis-à-vis U.S. dealers.

2. **The Interim Final Rule does not discriminate.**

The existence of a U.S. operation – and thus being subject to this Interim Final Rule – requires a business to establish an effective anti-money laundering program. As a result, the risk of money laundering associated with purchasing products from such a business is reduced. Furthermore, a non-U.S business with long standing clients will likely be able to work with their U.S. clients to demonstrate how risks of money laundering are mitigated, thereby posing no impediment to continued supplying of covered products.

Conclusion

I can't emphasize enough how important the opportunity to speak with industry in forums such as this is to me personally and to us as an agency in helping all of us do this job more effectively. We want you to continue to give us your honest and candid feedback on how this process is going, so we can assess our efforts and adjust course if necessary.

We cannot be unrealistic in our expectations of the ability of financial institutions to identify financial crime or terrorism financing. We have been consistent in acknowledging the limitations, but we believe, and my time here at FinCEN has only strengthened this conviction, that effective anti-money laundering programs across the spectrum of financial industries can't help but have a positive effect on combating the financing of terrorism, and ultimately improve the national security of the United States.

As I have said before, while FinCEN's mission is focused on protection of the U.S. financial systems, we recognize that this is a global problem. I remain committed to working with our colleagues in the international gems and jewelry community to address the challenges that confront us globally and to facilitate the flow of information necessary for U.S. dealers to minimize risks of money laundering.

Let me conclude by stating that a risk-based approach to Bank Secrecy Act regulation, as we have embraced, requires you to make a serious commitment to comply from the top down. The message that each of you, as top executives, sends throughout your institution about compliance sets the tone for the whole of the anti-money laundering program your institution puts in place. The level of cooperation that we have received from your industry has been outstanding, and we ask for your continued input, cooperation and support.

Thank you again for your time this morning and I would be happy to answer any questions that you might have.