

**DEPARTMENT OF THE TREASURY**

**Financial Crimes Enforcement Network**

**31 CFR Part 1010--**

**RIN 1506-AB38**

**Proposal of Special Measure against Bank of Dandong as a Financial Institution of Primary Money Laundering Concern**

**AGENCY:** Financial Crimes Enforcement Network (FinCEN), Treasury.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** FinCEN is issuing a notice of proposed rulemaking (NPRM), pursuant to Section 311 of the USA PATRIOT Act, to prohibit the opening or maintaining of a correspondent account in the United States for, or on behalf of, Bank of Dandong.

**DATES:** Written comments on the notice of proposed rulemaking must be submitted on or before [INSERT DATE 60 DAYS AFTER THE DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER].

**ADDRESSES:** You may submit comments, identified by 1506-AB38, by any of the following methods:

- *Federal E-rulemaking Portal:* <http://www.regulations.gov>. Follow the instructions for submitting comments. Include Docket Number FinCEN-2017-0010 and RIN 1506-AB38 in the submission.
- *Mail:* The Financial Crimes Enforcement Network, P.O. Box 39, Vienna, VA 22183. Include RIN 1506-AB38 in the body of the text. Please submit comments by one method only.

- Comments submitted in response to this NPRM will become a matter of public record. Therefore, you should submit only information that you wish to make publicly available.
- *Inspection of comments:* FinCEN uses the electronic, Internet-accessible docket at Regulations.gov as its complete docket; all hard copies of materials that should be in the docket, including public comments, are electronically scanned and placed there. *Federal Register* notices published by FinCEN are searchable by docket number, RIN, or document title, among other things, and the docket number, RIN, and title may be found at the beginning of such notices. In general, FinCEN will make all comments publicly available by posting them on <http://www.regulations.gov>.

**FOR FUTURE INFORMATION CONTACT:** The FinCEN Resource Center at (800) 949-2732.

**SUPPLEMENTARY INFORMATION:**

**I. Statutory Provisions**

On October 26, 2001, the President signed into law the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Public Law 107-56 (the USA PATRIOT Act). Title III of the USA PATRIOT Act amends the anti-money laundering (AML) provisions of the Bank Secrecy Act (BSA), codified at 12 U.S.C. 1829b, 12 U.S.C. 1951-1959, and 31 U.S.C. 5311-5314, 5316-5332, to promote the prevention, detection, and prosecution of international money laundering and the financing of terrorism. Regulations implementing the BSA appear at 31 CFR Chapter X. The authority of the Secretary of the Treasury (the

Secretary) to administer the BSA and its implementing regulations has been delegated to FinCEN.

Section 311 of the USA PATRIOT Act (Section 311), codified at 31 U.S.C. 5318A, grants FinCEN the authority, upon finding that reasonable grounds exist for concluding that a jurisdiction outside of the United States, one or more financial institutions operating outside of the United States, one or more classes of transactions within or involving a jurisdiction outside of the United States, or one or more types of accounts is of primary money laundering concern, to require domestic financial institutions and domestic financial agencies to take certain “special measures.” The five special measures enumerated in Section 311 are prophylactic safeguards that defend the U.S. financial system from money laundering and terrorist financing. FinCEN may impose one or more of these special measures in order to protect the U.S. financial system from these threats. Special measures one through four, codified at 31 U.S.C. 5318A(b)(1)–(b)(4), impose additional recordkeeping, information collection, and reporting requirements on covered U.S. financial institutions. The fifth special measure, codified at 31 U.S.C. 5318A(b)(5), allows FinCEN to prohibit, or impose conditions on, the opening or maintaining in the United States of correspondent or payable-through accounts for, or on behalf of, a foreign banking institution, if such correspondent account or payable-through account involves the foreign financial institution found to be of primary money laundering concern.

Before making a finding that reasonable grounds exist for concluding that a financial institution is of primary money laundering concern, the Secretary is required to

consult with both the Secretary of State and the Attorney General.<sup>1</sup> The Secretary shall also consider such information as the Secretary determines to be relevant, including the following potentially relevant factors:

- the extent to which such a financial institution is used to facilitate or promote money laundering in or through the jurisdiction, including any money laundering activity by organized criminal groups, international terrorists, or entities involved in the proliferation of weapons of mass destruction (WMD) or missiles;
- the extent to which such a financial institution is used for legitimate business purposes in the jurisdiction; and
- the extent to which such action is sufficient to ensure that the purposes of Section 311 are fulfilled, and to guard against international money laundering and other financial crimes.<sup>2</sup>

Upon finding that a financial institution is of primary money laundering concern, the Secretary may require covered financial institutions to take one or more special measures. In selecting which special measure(s) to take, the Secretary “shall consult with the Chairman of the Board of Governors of the Federal Reserve System, any other appropriate Federal banking agency (as defined in Section 3 of the Federal Deposit Insurance Act), the Secretary of State, the Securities and Exchange Commission, the Commodity Futures Trading Commission, the National Credit Union Administration Board, and in the sole discretion of the Secretary, such other agencies and interested parties as the Secretary [of the Treasury] may find appropriate.”<sup>3</sup> In imposing the fifth

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<sup>1</sup> 31 U.S.C. 5318A(c)(1).

<sup>2</sup> 31 U.S.C. 5318A(c)(2)(B).

<sup>3</sup> 31 U.S.C. 5318A(a)(4)(A).

special measure, the Secretary must do so “in consultation with the Secretary of State, the Attorney General, and the Chairman of the Board of Governors of the Federal Reserve System.”<sup>4</sup>

In addition, in selecting which special measure(s) to take, the Secretary shall consider the following factors:

- whether similar action has been or is being taken by other nations or multilateral groups;
- whether the imposition of any particular special measure would create a significant competitive disadvantage, including any undue cost or burden associated with compliance, for financial institutions organized or licensed in the United States;
- the extent to which the action or the timing of the action would have a significant adverse systemic impact on the international payment, clearance, and settlement system, or on legitimate business activities involving the particular jurisdiction, institution, class of transactions, or type of account; and
- the effect of the action on United States national security and foreign policy.<sup>5</sup>

## **II. Summary of Notice of Proposed Rulemaking**

This NPRM sets forth (i) FinCEN’s finding that Bank of Dandong, a commercial bank located in Dandong, China, is a financial institution of primary money laundering concern pursuant to Section 311, and (ii) FinCEN’s proposal of a prohibition under the fifth special measure on the opening or maintaining in the United States of a correspondent account for, or on behalf of, Bank of Dandong. As described more fully

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<sup>4</sup> 31 U.S.C. 5318A(b)(5).

<sup>5</sup> 31 U.S.C. 5318A(a)(4)(B).

below, FinCEN finds that Bank of Dandong is a financial institution of primary money laundering concern because it serves as a conduit for North Korea to access the U.S. and international financial systems, including by facilitating millions of dollars of transactions for companies involved in North Korea's WMD and ballistic missile programs. Having made such a finding and having performed the requisite consultations set forth in the statute, FinCEN proposes a prohibition on covered U.S. financial institutions from opening or maintaining a correspondent account in the United States for, or on behalf of, Bank of Dandong.

### **III. Background on North Korea Sanctions Evasion and Bank of Dandong**

#### **1. North Korea's Evasion of Sanctions**

North Korea continues to advance its nuclear and ballistic missile programs despite international censure and U.S. and international sanctions. In response to North Korea's continued actions to proliferate WMDs, the United Nations Security Council (UNSC) has issued a number of United Nations Security Council resolutions (UNSCRs), including 1718 (2006), 1874 (2009), 2087 (2013), 2094 (2013), 2270 (2016), and 2321 (2016), that restrict North Korea's financial and operational activities related to its nuclear and ballistic missile programs. Additionally, the President of the United States has issued Executive Orders 13466, 13551, 13570, 13687, and 13722 to impose economic sanctions on North Korea pursuant to the International Emergency Economic Powers Act,<sup>6</sup> and the U.S. Department of the Treasury has designated North Korean persons for asset freezes pursuant to other Executive Orders, such as Executive Order 13382, which targets WMD proliferators worldwide.

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<sup>6</sup> Title II of Pub. L. 95-223, 91 Stat. 1626 (October 28, 1977).

According to the February 2016 annual report by the UN Panel of Experts, established pursuant to UNSCR 1874, although international sanctions have served to significantly isolate North Korean banks from the international financial system, the North Korean government continues to access the international financial system to support its WMD and conventional weapons programs through its use of aliases, agents, foreign individuals in multiple jurisdictions, and a long-standing network of front companies and embassy personnel that support illicit activities through banking, bulk cash, and trade.<sup>7</sup>

According to that report, transactions for front companies for North Korea have been processed through correspondent bank accounts in the United States and Europe. Further, the enhanced vigilance required under the relevant UNSCRs is frustrated by the fact that North Korea-linked companies are often registered by third-country nationals who also use indirect payment methods and circuitous transactions disassociated from the movement of goods or services to conceal their activity.

Additionally, according to the February 2017 annual report produced by the same body, despite expanded financial sanctions adopted by the Security Council in UNSCRs 2270 and 2321, North Korea has continued to access the international financial system to support its activities.<sup>8</sup> Financial networks of North Korea have adapted to these sanctions, using evasive methods to maintain access to formal banking channels and bulk cash transfers to facilitate prohibited activities. According to the report, one way that

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<sup>7</sup> United Nations Security Council, *Report of the Panel of Experts established pursuant to resolution 1874 (2009)*. February 24, 2016. S/2016/157, available at [http://www.un.org/ga/search/view\\_doc.asp?symbol=S/2016/157](http://www.un.org/ga/search/view_doc.asp?symbol=S/2016/157).

<sup>8</sup> United Nations Security Council, *Report of the Panel of Experts established pursuant to resolution 1874 (2009)*. February 27, 2017. S/2017/150, available at [http://www.un.org/ga/search/view\\_doc.asp?symbol=S/2017/150](http://www.un.org/ga/search/view_doc.asp?symbol=S/2017/150).

North Korean financial institutions and networks access the international banking system is through trading companies, including designated entities, that are linked to North Korea. These trading companies open bank accounts that perform the same financial services as banks, such as maintaining funds on deposit and providing indirect correspondent bank account services.

To further protect the United States from North Korea's illicit financial activity, FinCEN has issued three advisories since 2005 detailing its concerns surrounding the deceptive financial practices used by North Korea and North Korean entities and calling on U.S. financial institutions to take appropriate risk mitigation measures. Moreover, on November 9, 2016, FinCEN finalized a rule under Section 311 prohibiting the opening or maintaining of correspondent accounts in the United States by covered financial institutions for, or on behalf of, North Korean banks.<sup>9</sup> The final rule also requires U.S. financial institutions to apply additional due diligence measures in order to prevent North Korean financial institutions from gaining improper indirect access to U.S. correspondent accounts. The notice of finding associated with the final rule highlighted North Korea's use of state-controlled financial institutions and front companies to conduct international financial transactions that, among other things, support the proliferation of its WMD and conventional weapons programs.<sup>10</sup> As explained below, Bank of Dandong facilitates such activity through the U.S. financial system.

## **2. Bank of Dandong**

Established in 1997, Bank of Dandong is a small commercial bank located in Dandong, China that offers domestic and international financial services to both

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<sup>9</sup> 81 FR 78715 (November 9, 2016).

<sup>10</sup> 81 FR 35441 (June 2, 2016).

individuals and businesses. According to commercial database research, Bank of Dandong is ranked as the 148<sup>th</sup>-largest financial institution out of a total of 196 financial institutions in China's banking sector. As discussed further below, FinCEN is concerned that Bank of Dandong serves as a financial conduit between North Korea and the U.S. and international financial systems in violation of U.S. and UN sanctions.

#### **IV. Finding Bank of Dandong to be a Financial Institution of Primary Money Laundering Concern**

Based on information available to the agency, including both public and non-public reporting, and after performing the requisite interagency consultations and considering each of the factors discussed below, FinCEN finds that reasonable grounds exist for concluding that Bank of Dandong is a financial institution of primary money laundering concern.

##### **1. The Extent to Which Bank of Dandong Has Been Used to Facilitate or Promote Money Laundering, Including by Entities Involved in the Proliferation of Weapons of Mass Destruction or Missiles**

Bank of Dandong serves as a gateway for North Korea to access the U.S. and international financial systems despite U.S. and UN sanctions. Increasing U.S. and international sanctions on North Korea have caused most banks worldwide to sever their ties with North Korean banks, impeding North Korea's ability to gain direct access to the global financial system. As a result, North Korea uses front companies and banks outside North Korea to conduct financial transactions, including transactions in support of its WMD and conventional weapons programs. For example, as of mid-February 2016, North Korea was using bank accounts under false names and conducting financial

transactions through banks located in China, Hong Kong, and various southeast Asian countries. The primary bank in China was Bank of Dandong.

In early 2016, accounts at Bank of Dandong were used to facilitate millions of dollars of transactions on behalf of companies involved in the procurement of ballistic missile technology. Bank of Dandong also facilitates financial activity for North Korean entities designated by the United States and listed by the United Nations for WMD proliferation, as well as for front companies acting on their behalf.

In particular, Bank of Dandong has facilitated financial activity for Korea Kwangson Banking Corporation (KKBC), a North Korean bank designated by the United States and listed by the United Nations for providing financial services in support of North Korean WMD proliferators. As of May 2012, KKBC had a representative embedded at Bank of Dandong. Moreover, Bank of Dandong maintained a direct correspondent banking relationship with KKBC since approximately 2013, when another Chinese bank ended a similar correspondent relationship. As of early 2016, KKBC maintained multiple bank accounts with Bank of Dandong.

Bank of Dandong has also facilitated financial activity for the Korea Mining Development Trading Corporation (KOMID), a U.S.- and UN-designated entity. As of early 2016, a front company for KOMID maintained multiple bank accounts with Bank of Dandong. The President subjected KOMID to an asset blocking by listing it in the Annex of Executive Order 13382 in 2005, and the United States designated KOMID pursuant to Executive Order 13687 in January 2015 for being North Korea's primary arms dealer and its main exporter of goods and equipment related to ballistic missiles and conventional weapons.

FinCEN is concerned that Bank of Dandong uses the U.S. financial system to facilitate financial activity for KKBC and KOMID, as well as other entities connected to North Korea's WMD and ballistic missile programs. Based on FinCEN's analysis of financial transactional data provided to FinCEN by U.S. financial institutions pursuant to the BSA as well as other information available to the agency, FinCEN assesses that at least 17 percent of Bank of Dandong customer transactions conducted through the bank's U.S. correspondent accounts from May 2012 to May 2015 were conducted by companies that have transacted with, or on behalf of, U.S.- and UN-sanctioned North Korean entities, including designated North Korean financial institutions and WMD proliferators. In addition, U.S. banks have identified a substantial amount of suspicious activity processed by Bank of Dandong, including: (i) transactions that have no apparent economic, lawful, or business purpose and may be tied to sanctions evasion; (ii) transactions that have a possible North Korean nexus and include activity between unidentified companies and individuals and behavior indicative of shell company activity; and (iii) transactions that include transfers from offshore accounts with apparent shell companies that are domiciled in financial secrecy jurisdictions and banking in another country.

FinCEN is also concerned that, until recently, an entity designated by the United States for its ties to North Korea's WMD proliferation maintained an ownership stake in Bank of Dandong. Specifically, this entity, Dandong Hongxiang Industrial Development Co. Ltd. (DHID), maintained a minority ownership interest in Bank of Dandong until December 2016. The United States designated DHID in 2016 for acting for, or on behalf of, KKBC, the U.S.- and UN-designated North Korean bank with which Bank of

Dandong maintained a direct relationship since approximately 2013. FinCEN believes that DHID's ownership stake in Bank of Dandong allowed DHID to access the U.S. financial system through the bank. Based on FinCEN's analysis of financial transactional data provided to FinCEN by U.S. financial institutions pursuant to the BSA, Bank of Dandong processed approximately \$56 million through U.S. banks for DHID between October 2012 and December 2014. Even though DHID may no longer maintain an ownership stake in Bank of Dandong, FinCEN is concerned that the close relationship between the two entities helped establish Bank of Dandong as a prime conduit for North Korean activity.

Moreover, FinCEN believes that illicit financial activity involving North Korea continues to infiltrate the U.S. and international financial systems through Bank of Dandong.

## **2. The Extent to Which Bank of Dandong is Used for Legitimate Business Purposes**

According to commercial database research, Bank of Dandong is ranked as the 148<sup>th</sup>-largest financial institution out of a total of 196 financial institutions in China's banking sector. Based on FinCEN's analysis of financial transactional data provided to FinCEN by U.S. financial institutions pursuant to the BSA, Bank of Dandong processed over \$2.5 billion in U.S. dollar transactions between May 2012 and May 2015 through its U.S. correspondent accounts, including at least \$786 million in customer transactions for businesses and individuals (the remaining transactions comprised bank-to-bank transactions). This \$786 million in financial activity consisted largely of letters of credit satisfaction, invoice payments, currency exchange activity, and transfers between individuals, which could be indicative of legitimate business activity. Nonetheless,

FinCEN assesses that the \$786 million in financial activity includes transactions conducted by companies that have transacted with, or on behalf of, U.S.- and UN-sanctioned North Korean entities. FinCEN is concerned that the existence of relationships between designated North Korean entities and Bank of Dandong suggests that the bank likely processes more transactions for North Korean-related front companies than what FinCEN is currently able to identify. Consequently, the exposure of U.S. financial institutions to North Korea's illicit financial activity via Bank of Dandong outweighs concerns for any legitimate business activity at the bank.

Moreover, Bank of Dandong maintains euro, Japanese yen, Hong Kong dollar, pound sterling, and Australian dollar correspondent accounts that would not be affected by this action. A prohibition under the fifth special measure would not prevent Bank of Dandong from conducting legitimate business activities in other foreign currencies so long as such activity does not involve a correspondent account maintained in the United States. Bank of Dandong would, therefore, still have other avenues through which it could provide services.

### **3. The Extent to Which This Action is Sufficient to Guard against International Money Laundering and Other Financial Crimes**

A prohibition under the fifth special measure would sufficiently guard against international money laundering and other financial crimes related to Bank of Dandong by restricting the ability of Bank of Dandong to access the U.S. financial system to process transactions for entities connected to the proliferation of WMDs and ballistic missiles. Given the national security threat posed by such activity, FinCEN views this action as necessary to prevent Bank of Dandong from continuing to access the U.S. financial system.

**V. Proposed Prohibition on Covered Financial Institutions from Opening or Maintaining Correspondent Accounts in the United States for Bank of Dandong**

After performing the requisite interagency consultations, considering the relevant factors, and making a finding that Bank of Dandong is a financial institution of primary money laundering concern, FinCEN proposes a prohibition under the fifth special measure. A prohibition under the fifth special measure is the most effective and practical measure to safeguard the U.S. financial system from the illicit finance risks posed by Bank of Dandong.

**1. Factors Considered in Proposing a Prohibition under the Fifth Special Measure**

Below is a discussion of the relevant factors FinCEN considered in proposing a prohibition under the fifth special measure with respect to Bank of Dandong.

**A. Whether Similar Action Has Been or Will Be Taken by Other Nations or Multilateral Groups against Bank of Dandong**

FinCEN is not aware of any other nation or multilateral group that has taken or is taking similar action regarding Bank of Dandong. The international community has, however, taken a series of steps to address the illicit financial threats emanating from North Korea, for which Bank of Dandong serves as a conduit. Between 2006 and 2016, the UNSC adopted multiple resolutions that generally restrict North Korea's financial activities related to its nuclear and missile programs and conventional arms sales. In March 2016, the UNSC unanimously adopted UNSCR 2270, which contains provisions that generally require nations to: (i) prohibit North Korean banks from opening branches in their territory or engaging in certain correspondent relationships with these banks; (ii) terminate existing representative offices or subsidiaries, branches, and correspondent accounts with North Korean financial institutions; and (iii) prohibit their financial

institutions from opening new representative offices or subsidiaries, branches, or bank accounts in North Korea. Additionally, UNSCR 2321, unanimously adopted by the UNSC in November 2016, requires nations to close existing representative offices or subsidiaries, branches, or bank accounts in North Korea within 90 days and expel individuals working on behalf of, or at the direction of, a North Korean bank or financial institution.

Similarly, the Financial Action Task Force (FATF) has emphasized its concerns regarding the threat posed by North Korea's illicit activities related to the proliferation of WMDs and related financing. Reiterating the UNSCR requirements, the FATF called upon its members and urged all jurisdictions to take the necessary measures to close existing branches, subsidiaries, and representative offices of North Korean banks within their territories and terminate correspondent relationships with North Korean banks, where required by relevant UNSC Resolutions.

Despite these measures, North Korea continues to use the U.S. and international financial systems through front companies and other surreptitious means. It is necessary to protect the U.S. financial system, directly and indirectly, from banks like Bank of Dandong that facilitate such access. Moreover, given the interconnectedness of the global financial system, the potential for Bank of Dandong to access the U.S. financial system indirectly, including through the use of nested correspondent accounts, exposes the U.S. financial system to the risks associated with conducting transactions with entities operating for, or on behalf of, North Korea.

B. Whether the Imposition of the Fifth Special Measure Would Create a Significant Competitive Disadvantage, Including Any Undue Cost or Burden Associated with Compliance, for Financial Institutions Organized or Licensed in the United States

A prohibition under the fifth special measure would not cause a significant competitive disadvantage or place an undue cost or burden on U.S. financial institutions. Pursuant to sanctions administered by OFAC, U.S. financial institutions are currently subject to a range of prohibitions related to financial activity involving North Korea. Accordingly, a prohibition on covered financial institutions from opening or maintaining correspondent accounts for, or on behalf of, a bank that facilitates North Korean financial activity would not create any competitive disadvantage for U.S. financial institutions.

Similarly, the proposed due diligence obligations would not create any undue costs or burden on U.S. financial institutions. U.S. financial institutions already generally have systems in place to screen transactions in order to identify and report suspicious activity and comply with the sanctions programs administered by OFAC. Institutions can modify these systems to detect transactions involving Bank of Dandong. While there may be some additional burden in conducting due diligence on foreign correspondent account holders and notifying them of the prohibition (as described below), any such burden will likely be minimal, and certainly not undue, given the national security threat posed by Bank of Dandong's facilitation of activity for front companies associated with North Korea, some of which are involved in activities that support the proliferation of WMD or missiles.

C. The Extent to Which the Proposed Action or Timing of the Action Will Have a Significant Adverse Systemic Impact on the International Payment, Clearance, and Settlement System, or on Legitimate Business Activities of Bank of Dandong

Bank of Dandong is a relatively small financial institution in China's banking sector, is not a major participant in the international payment system, and is not relied upon by the international banking community for clearance or settlement services. Therefore, a prohibition under the fifth special measure with respect to Bank of Dandong will not have an adverse systemic impact on the international payment, clearance, and settlement system.

FinCEN also considered the extent to which this action could have an impact on the legitimate business activities of Bank of Dandong and has concluded that the need to protect the U.S. financial system from banks that facilitate North Korea's illicit financial activity strongly outweighs any such impact. Financial transactional data provided to FinCEN by U.S. financial institutions pursuant to the BSA indicates that Bank of Dandong's financial activity conducted through its U.S. correspondent accounts has consisted largely of letters of credit satisfaction, invoice payments, currency exchange activity, and transfers between individuals, which could be indicative of legitimate business activity. Nonetheless, FinCEN assesses that this financial activity also includes transactions conducted by companies that have transacted with, or on behalf of, entities that threaten the national security of the United States.

As stated above, Bank of Dandong maintains euro, Japanese yen, Hong Kong dollar, pound sterling, and Australian dollar correspondent accounts. A prohibition under the fifth special measure would not prevent Bank of Dandong from conducting legitimate business activities in other foreign currencies so long as such activity does not involve a

correspondent account maintained in the United States. Bank of Dandong would, therefore, still have other avenues through which it could provide legitimate services.

D. The Effect of the Proposed Action on United States National Security and Foreign Policy

Excluding from the U.S. financial system foreign banks that serve as conduits for significant money laundering activity, for the financing of WMDs or their delivery systems, and for other financial crimes enhances national security by making it more difficult for proliferators and money launderers to access the U.S. financial system. As Bank of Dandong has been used to facilitate financial activity related to North Korean entities designated by the United States and United Nations for WMD proliferation, the proposed rule, if finalized, would serve as an additional measure to prevent North Korea from accessing the U.S. financial system and would both support and uphold U.S. national security and foreign policy goals. A prohibition under the fifth special measure would also complement the U.S. Government's worldwide efforts to expose and disrupt international money laundering.

**2. Consideration of Alternative Special Measures**

Under Section 311, special measures one through four enable FinCEN to impose additional recordkeeping, information collection, and information reporting requirements on covered financial institutions. The fifth special measure enables FinCEN to impose conditions as an alternative to a prohibition on the opening or maintaining of correspondent accounts. FinCEN considered these alternatives to a prohibition under the fifth special measure, but believes that a prohibition under the fifth special measure would most effectively safeguard the U.S. financial system from the illicit finance risks posed by Bank of Dandong.

North Korea is subject to numerous U.S. and UN sanctions, and it has also been consistently identified by the Financial Action Task Force for its anti-money laundering deficiencies. Further, FinCEN has issued three advisories since 2005 detailing its concerns surrounding the deceptive financial practices used by North Korea and North Korean entities and calling on U.S. financial institutions to take appropriate risk mitigation measures.

Despite these measures, North Korea continues to access the international financial system to support its WMD and conventional weapons programs through its use of aliases, agents, foreign individuals in multiple jurisdictions, and a long-standing network of front companies. Given Bank of Dandong's apparent disregard for numerous international calls to prevent North Korean illicit financial activity, FinCEN does not believe that any condition, additional recordkeeping requirement, or reporting requirement would be an effective measure to safeguard the U.S. financial system. Such measures would not prevent Bank of Dandong from accessing, directly or indirectly, the correspondent accounts of U.S. financial institutions, thus leaving the U.S. financial system vulnerable to processing illicit transfers that pose a national security risk. In addition, no recordkeeping requirement or conditions on correspondent accounts would be sufficient to guard against the risks posed by a bank that processes transactions that are designed to obscure their involvement with North Korea, and are ultimately for the benefit of sanctioned entities. Therefore, a prohibition under the fifth special measure is the only special measure that can adequately protect the U.S. financial system from the illicit finance risks posed by Bank of Dandong.

## **VI. Section-by-Section Analysis for the Proposal of a Prohibition Under the Fifth Special Measure**

### 1010.660(a) – Definitions

#### **1. Bank of Dandong**

The proposed rule defines “Bank of Dandong” to mean all subsidiaries, branches, offices, and agents of Bank of Dandong Co., Ltd. operating in any jurisdiction.

#### **2. Correspondent account**

The proposed rule defines “Correspondent account” to have the same meaning as the definition contained in 31 CFR 1010.605(c)(1)(ii). In the case of a U.S. depository institution, this broad definition includes most types of banking relationships between a U.S. depository institution and a foreign bank that are established to provide regular services, dealings, and other financial transactions, including a demand deposit, savings deposit, or other transaction or asset account, and a credit account or other extension of credit. FinCEN is using the same definition of “account” for purposes of this proposed rule as was established for depository institutions in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act requiring enhanced due diligence for correspondent accounts maintained for certain foreign banks.<sup>11</sup> Under this definition, “payable through accounts” are a type of correspondent account.

In the case of securities broker-dealers, futures commission merchants, introducing brokers-commodities, and investment companies that are open-end companies (“mutual funds”), FinCEN is also using the same definition of “account” for purposes of this proposed rule as was established for these entities in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act requiring

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<sup>11</sup> See 31 CFR 1010.605(c)(2)(i).

enhanced due diligence for correspondent accounts maintained for certain foreign banks.<sup>12</sup>

### **3. Covered financial institution**

The proposed rule defines “covered financial institution” with the same definition used in the final rule implementing the provisions of Section 312 of the USA PATRIOT Act, which in general includes the following:

- an insured bank (as defined in section 3(h) of the Federal Deposit Insurance Act (12 U.S.C. 1813(h)));
- a commercial bank;
- an agency or branch of a foreign bank in the United States;
- a Federally insured credit union;
- a savings association;
- a corporation acting under section 25A of the Federal Reserve Act (12 U.S.C. 611);
- a trust bank or trust company;
- a broker or dealer in securities;
- a futures commission merchant or an introducing broker-commodities; and
- a mutual fund.

### **4. Foreign banking institution**

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<sup>12</sup> See 31 CFR 1010.605(c)(2)(ii)-(iv).

The proposed rule defines “foreign banking institution” to mean a bank organized under foreign law, or an agency, branch, or office located outside the United States of a bank. The term does not include an agent, agency, branch, or office within the United States of a bank organized under foreign law. This is consistent with the definition of “foreign bank” under 31 CFR 1010.100(u).

## **5. Subsidiary**

The proposed rule defines “subsidiary” to mean a company of which more than 50 percent of the voting stock or analogous equity interest is owned by another company.

### **1010.660(b) – Prohibition on Accounts and Due Diligence Requirements for Covered Financial Institutions**

#### **1. Prohibition on Opening or Maintaining Correspondent Accounts**

Section 1010.660(b)(1) and (2) of this proposed rule would prohibit covered financial institutions from opening or maintaining in the United States a correspondent account for, or on behalf of, Bank of Dandong. It would also require covered financial institutions to take reasonable steps to not process a transaction for the correspondent account of a foreign banking institution in the United States if such a transaction involves Bank of Dandong. Such reasonable steps are described in 1010.660(b)(3), which sets forth the special due diligence requirements a covered financial institution would be required to take when it knows or has reason to believe that a transaction involves Bank of Dandong.

#### **2. Special Due Diligence for Correspondent Accounts**

As a corollary to the prohibition set forth in section 1010.660(b)(1) and (2), section 1010.660(b)(3) of the proposed rule would require covered financial institutions

to apply special due diligence to all of their foreign correspondent accounts that is reasonably designed to guard against such accounts being used to process transactions involving Bank of Dandong. As part of that special due diligence, covered financial institutions would be required to notify those foreign correspondent account holders that the covered financial institutions know or have reason to believe provide services to Bank of Dandong that such correspondents may not provide Bank of Dandong with access to the correspondent account maintained at the covered financial institution. A covered financial institution may satisfy this notification requirement using the following notice:

Notice: Pursuant to U.S. regulations issued under Section 311 of the USA PATRIOT Act, see 31 CFR 1010.660, we are prohibited from opening or maintaining in the United States a correspondent account for, or on behalf of, Bank of Dandong. The regulations also require us to notify you that you may not provide Bank of Dandong, including any of its subsidiaries, branches, offices, or agents with access to the correspondent account you hold at our financial institution. If we become aware that the correspondent account you hold at our financial institution has processed any transactions involving Bank of Dandong, including any of its subsidiaries, branches, offices, or agents, we will be required to take appropriate steps to prevent such access, including terminating your account.

The purpose of the notice requirement is to aid cooperation with correspondent account holders in preventing transactions involving Bank of Dandong from accessing the U.S. financial system. FinCEN does not require or expect a covered financial institution to obtain a certification from any of its correspondent account holders that access will not be provided to comply with this notice requirement.

Methods of compliance with the notice requirement could include, for example, transmitting a notice by mail, fax, or e-mail. The notice should be transmitted whenever

a covered financial institution knows or has reason to believe that a foreign correspondent account holder provides services to Bank of Dandong.

Special due diligence also includes implementing risk-based procedures designed to identify any use of correspondent accounts to process transactions involving Bank of Dandong. A covered financial institution would be expected to apply an appropriate screening mechanism to identify a funds transfer order that on its face listed Bank of Dandong as the financial institution of the originator or beneficiary, or otherwise referenced Bank of Dandong in a manner detectable under the financial institution's normal screening mechanisms. An appropriate screening mechanism could be the mechanisms used by a covered financial institution to comply with various legal requirements, such as the commercially available software programs used to comply with the economic sanctions programs administered by OFAC.

### **3. Recordkeeping and Reporting**

Section 1010.660(b)(4) of the proposed rule would clarify that the proposed rule does not impose any reporting requirement upon any covered financial institution that is not otherwise required by applicable law or regulation. A covered financial institution must, however, document its compliance with the notification requirement described above.

## **VII. Request for Comments**

FinCEN invites comments on all aspects of the proposal to impose a prohibition under the fifth special measure with respect to Bank of Dandong and specifically invites comments on the following matters:

1. FinCEN’s proposal of a prohibition under the fifth special measure under 31 USC 5318A(b), as opposed to special measures one through four or imposing conditions under the fifth special measure;
2. The form and scope of the notice to certain correspondent account holders that would be required under the rule; and
3. The appropriate scope of the due diligence requirements in this proposed rule.

## **VIII. Regulatory Flexibility Act**

When an agency issues a rulemaking proposal, the Regulatory Flexibility Act (RFA) requires the agency to “prepare and make available for public comment an initial regulatory flexibility analysis” that will “describe the impact of the proposed rule on small entities.” (5 U.S.C. 603(a)). Section 605 of the RFA allows an agency to certify a rule, in lieu of preparing an analysis, if the proposed rulemaking is not expected to have a significant economic impact on a substantial number of small entities.

### **1. Proposal to Prohibit Covered Financial Institutions from Opening or Maintaining Correspondent Accounts with Certain Foreign Banks Under the Fifth Special Measure**

#### **A. Estimate of the Number of Small Entities to Whom the Proposed Fifth Special Measure Will Apply**

For purposes of the RFA, both banks and credit unions are considered small entities if they have less than \$550,000,000 in assets.<sup>13</sup> Of the estimated 6,192 banks, 80

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<sup>13</sup> *Table of Small Business Size Standards Matched to North American Industry Classification System Codes*, Small Business Administration Size Standards (SBA Feb. 26, 2016) [hereinafter “*SBA Size Standards*”]. ([https://www.sba.gov/sites/default/files/files/Size\\_Standards\\_Table.pdf](https://www.sba.gov/sites/default/files/files/Size_Standards_Table.pdf)).

percent have less than \$550,000,000 in assets and are considered small entities.<sup>14</sup> Of the estimated 6,021 credit unions, 92.5 percent have less than \$550,000,000 in assets.<sup>15</sup>

Broker-dealers are defined in 31 CFR 1010.100(h) as those broker-dealers required to register with the Securities and Exchange Commission (SEC). For the purposes of the RFA, FinCEN relies on the SEC's definition of small business as previously submitted to the Small Business Administration (SBA). The SEC has defined the term small entity to mean a broker or dealer that: (1) had total capital (net worth plus subordinated liabilities) of less than \$500,000 on the date in the prior fiscal year as of which its audited financial statements were prepared pursuant to Rule 17a-5(d) or, if not required to file such statements, a broker or dealer that had total capital (net worth plus subordinated debt) of less than \$500,000 on the last business day of the preceding fiscal year (or in the time that it has been in business if shorter); and (2) is not affiliated with any person (other than a natural person) that is not a small business or small organization as defined in this release.<sup>16</sup> Based on SEC estimates, 17 percent of broker-dealers are classified as small entities for purposes of the RFA.<sup>17</sup>

Futures commission merchants (FCMs) are defined in 31 CFR 1010.100(x) as those FCMs that are registered or required to be registered as a FCM with the Commodity Futures Trading Commission (CFTC) under the Commodity Exchange Act (CEA), except persons who register pursuant to section 4f(a)(2) of the CEA, 7 U.S.C.

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<sup>14</sup> Federal Deposit Insurance Corporation, *Find an Institution*, <http://www2.fdic.gov/idasp/main.asp>; *select* Size or Performance: Total Assets, *type* Equal or less than \$: "550000" and *select* Find.

<sup>15</sup> National Credit Union Administration, *Credit Union Data*, <http://webapps.ncua.gov/customquery/>; *select* Search Fields: Total Assets, *select* Operator: Less than or equal to, *type* Field Values: "550000000" and *select* Go.

<sup>16</sup> 17 CFR 240.0-10(c).

<sup>17</sup> 76 FR 37572, 37602 (June 27, 2011) (the SEC estimates 871 small broker-dealers of the 5,063 total registered broker-dealers).

6f(a)(2). Because FinCEN and the CFTC regulate substantially the same population, for the purposes of the RFA, FinCEN relies on the CFTC's definition of small business as previously submitted to the SBA. In the CFTC's "Policy Statement and Establishment of Definitions of 'Small Entities' for Purposes of the Regulatory Flexibility Act," the CFTC concluded that registered FCMs should not be considered to be small entities for purposes of the RFA.<sup>18</sup> The CFTC's determination in this regard was based, in part, upon the obligation of registered FCMs to meet the capital requirements established by the CFTC.

For purposes of the RFA, an introducing broker-commodities dealer is considered small if it has less than \$38,500,000 in gross receipts annually.<sup>19</sup> Based on information provided by the National Futures Association (NFA), 95 percent of introducing brokers-commodities dealers have less than \$38.5 million in adjusted net capital and are considered to be small entities.

Mutual funds are defined in 31 CFR 1010.100(gg) as those investment companies that are open-end investment companies that are registered or are required to register with the SEC. For the purposes of the RFA, FinCEN relies on the SEC's definition of small business as previously submitted to the SBA. The SEC has defined the term "small entity" under the Investment Company Act to mean "an investment company that, together with other investment companies in the same group of related investment companies, has net assets of \$50 million or less as of the end of its most recent fiscal

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<sup>18</sup> 47 FR 18618, 18619 (Apr. 30, 1982).

<sup>19</sup> SBA, Size Standards to Define Small Business Concerns, 13 CFR 121.201 (2016), at 28.

year.”<sup>20</sup> Based on SEC estimates, seven percent of mutual funds are classified as “small entities” for purposes of the RFA under this definition.<sup>21</sup>

As noted above, 80 percent of banks, 92.5 percent of credit unions, 17 percent of broker-dealers, 95 percent of introducing broker-commodities dealers, no FCMs, and seven percent of mutual funds are small entities.

B. Description of the Projected Reporting and Recordkeeping Requirements of a Prohibition Under the Fifth Special Measure

The proposed prohibition under the fifth special measure could require covered financial institutions to provide a notification intended to aid cooperation from foreign correspondent account holders in preventing transactions involving Bank of Dandong from being processed by the U.S. financial system. FinCEN estimates that the burden on institutions providing this notice is one hour.

Covered financial institutions would also be required to take reasonable measures to detect use of their correspondent accounts to process transactions involving Bank of Dandong. All U.S. persons, including U.S. financial institutions, currently must comply with OFAC sanctions, and U.S. financial institutions have suspicious activity reporting requirements. The systems that U.S. financial institutions have in place to comply with these requirements can easily be modified to adapt to this proposed rule. Thus, the special due diligence that would be required under the proposed rule – *i.e.*, preventing the processing of transactions involving Bank of Dandong and the transmittal of notice to certain correspondent account holders – would not impose a significant additional economic burden upon small U.S. financial institutions.

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<sup>20</sup> 17 CFR 270.0-10.

<sup>21</sup> 78 FR 23637, 23658 (April 19, 2013).

## **2. Certification:**

For these reasons, FinCEN certifies that the proposals contained in this rulemaking would not have a significant impact on a substantial number of small businesses.

FinCEN invites comments from members of the public who believe there would be a significant economic impact on small entities from the imposition of a prohibition under the fifth special measure regarding Bank of Dandong.

## **IX. Paperwork Reduction Act**

The collection of information contained in this proposed rule is being submitted to the Office of Management and Budget for review in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507(d)). Comments on the collection of information should be sent to the Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Office of Management and Budget, Paperwork Reduction Project (1506), Washington, D.C. 20503 (or by e-mail to [oirasubmission@omb.eop.gov](mailto:oirasubmission@omb.eop.gov)) with a copy to FinCEN by mail or e-mail at the addresses previously specified. Comments should be submitted by one method only. Comments on the collection of information should be received by [INSERT DATE THAT IS 60 DAYS AFTER DATE OF PUBLICATION IN THE FEDERAL REGISTER]. In accordance with the requirements of the Paperwork Reduction Act and its implementing regulations, 5 CFR 1320, the following information concerning the collection of information as required by 31 CFR 1010.660 is presented to assist those persons wishing to comment on the information collection.

The notification requirement in section 1010.660(b)(3)(i)(A) is intended to aid cooperation from correspondent account holders in denying Bank of Dandong access to the U.S. financial system. The information required to be maintained by that section would be used by federal agencies and certain self-regulatory organizations to verify compliance by covered financial institutions with the provisions of 31 CFR 1010.660. The collection of information would be mandatory.

Description of Affected Financial Institutions: Banks, broker-dealers in securities, futures commission merchants and introducing brokers-commodities, money services businesses, and mutual funds.

Estimated Number of Affected Financial Institutions: 5,000.

Estimated Average Annual Burden in Hours Per Affected Financial Institution:  
The estimated average burden associated with the collection of information in this proposed rule is one hour per affected financial institution.

Estimated Total Annual Burden: 5,000 hours.

FinCEN specifically invites comments on: (a) whether the proposed collection of information is necessary for the proper performance of the mission of FinCEN, including whether the information would have practical utility; (b) the accuracy of FinCEN's estimate of the burden of the proposed collection of information; (c) ways to enhance the quality, utility, and clarity of the information required to be maintained; (d) ways to minimize the burden of the required collection of information, including through the use of automated collection techniques or other forms of information technology; and (e) estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to report the information.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid OMB control number.

**X. Executive Order 12866**

Executive Orders 12866 and 13563 direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, public health and safety effects, distributive impacts, and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, of reducing costs, of harmonizing rules, and of promoting flexibility. It has been determined that the proposed rule is not a “significant regulatory action” for purposes of Executive Order 12866.

**List of Subjects in 31 CFR Part 1010**

Administrative practice and procedure, banks and banking, brokers, counter-money laundering, counter-terrorism, foreign banking.

**Authority and Issuance**

For the reasons set forth in the preamble, part 1010, chapter X of title 31 of the Code of Federal Regulations, is proposed to be amended as follows:

**Part 1010—GENERAL PROVISIONS**

1. The authority citation for part 1010 continues to read as follows:

Authority: 12 U.S.C. 1829b and 1951-1959; 31 U.S.C. 5311-5314, 5316-5332; Title III, sec. 314 Pub. L. 107-56, 115 Stat. 307; sec. 701 Pub. L. 114-74, 129 Stat. 599.

2. Add § 1010.660 to read as follows:

**§ 1010.660 Special measures against Bank of Dandong**

(a) Definitions. For purposes of this section:

(1) Bank of Dandong means all subsidiaries, branches, offices, and agents of Bank of Dandong Co., Ltd. operating in any jurisdiction.

(2) Correspondent account has the same meaning as provided in § 1010.605(c)(1)(ii).

(3) Covered financial institution has the same meaning as provided in § 1010.605(e)(1).

(4) Foreign banking institution means a bank organized under foreign law, or an agency, branch, or office located outside the United States of a bank. The term does not include an agent, agency, branch, or office within the United States of a bank organized under foreign law.

(5) Subsidiary means a company of which more than 50 percent of the voting stock or analogous equity interest is owned by another company.

(b) Prohibition on accounts and due diligence requirements for covered financial institutions—

(1) Opening or maintaining correspondent accounts for Bank of Dandong. A covered financial institution shall not open or maintain in the United States a correspondent account for, or on behalf of, Bank of Dandong.

(2) Prohibition on use of correspondent accounts involving Bank of Dandong. A covered financial institution shall take reasonable steps to not process a transaction for the correspondent account of a foreign banking institution in the United States if such a transaction involves Bank of Dandong.

(3) Special due diligence of correspondent accounts to prohibit use.

(i) A covered financial institution shall apply special due diligence to its foreign correspondent accounts that is reasonably designed to guard against their use to process transactions involving Bank of Dandong. At a minimum, that special due diligence must include:

(A) Notifying those foreign correspondent account holders that the covered financial institution knows or has reason to believe provide services to Bank of Dandong that such correspondents may not provide Bank of Dandong with access to the correspondent account maintained at the covered financial institution; and

(B) Taking reasonable steps to identify any use of its foreign correspondent accounts by Bank of Dandong, to the extent that such use can be determined from transactional records maintained in the covered financial institution's normal course of business.

(ii) A covered financial institution shall take a risk-based approach when deciding what, if any, other due diligence measures it reasonably must adopt to guard against the use of its foreign correspondent accounts to process transactions involving Bank of Dandong.

(iii) A covered financial institution that knows or has reason to believe that a foreign bank's correspondent account has been or is being used to process transactions involving Bank of Dandong shall take all appropriate steps to further investigate and prevent such access, including the notification of its correspondent

account holder under paragraph (b)(3)(i)(A) of this section and, where necessary, termination of the correspondent account.

(4) Recordkeeping and reporting.

(i) A covered financial institution is required to document its compliance with the notice requirement set forth in this section.

(ii) Nothing in this section shall require a covered financial institution to report any information not otherwise required to be reported by law or regulation.

Dated: June 29, 2017

/s/

Jamal El-Hindi  
Acting Director  
Financial Crimes Enforcement Network