

SUMMARY OF ROUNDTABLE MEETING:
ADVANCE NOTICE OF PROPOSED RULEMAKING ON CUSTOMER DUE DILIGENCE

ONE LIBERTY PLAZA,
165 BROADWAY
NEW YORK, NY 10006
OCTOBER 5, 2012
9:00AM-4:00PM

The Financial Crimes Enforcement Network (FinCEN) hosted a roundtable meeting to continue gathering information on the Advance Notice of Proposed Rulemaking (ANPRM) on customer due diligence (CDD) requirements for financial institutions. The meeting was held on October 5, 2012, at the Financial Industry Regulatory Authority (FINRA), One Liberty Plaza, 165 Broadway, New York, NY 10006. To maximize private sector participation, the meeting was divided into a morning session from 9:00am to 12:00pm and an afternoon session from 1:00pm to 4:00pm.

On March 5, 2012, FinCEN issued the ANPRM to solicit public comment on the potential development of an explicit CDD obligation for financial institutions, including a requirement to obtain information on the beneficial ownership of customers.¹ The comment period closed on June 11, 2012. On July 31, 2012, and September 28, 2012, officials from the U.S. Department of the Treasury (Treasury), including FinCEN, hosted public meetings in Washington, DC and Chicago, IL, respectively, to invite additional comment on specific issues raised during the comment period.² This roundtable meeting in New York continued Treasury's outreach efforts to engage with representatives from affected financial institutions on these key issues.

This New York meeting was co-chaired by Jamal El-Hindi, Associate Director, Regulatory Policy and Programs Division, FinCEN, and Chip Poncy, Director, Office of Strategic Policy for Terrorist Financing and Financial Crimes, U.S. Department of the Treasury. Representatives from all interested financial institutions were invited to attend and participate. Set forth below is a general summary of the primary issues discussed at the roundtable meeting, 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 meeting.

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;dc=FR%252BPR%252BN%252BO%252BSR>.

² *Summary of Public Hearing: Advance Notice of Proposed Rulemaking on Customer Due Diligence* (July 31, 2012), available at <http://www.fincen.gov/whatsnew/html/20120913.html>. Public roundtable discussions were also planned for Chicago, New York City, Los Angeles and Miami; summaries of all roundtable discussions will be available on FinCEN's website.

Summary of Roundtable Meeting

Messrs. El-Hindi and Ponce opened the discussion with an overview of Treasury's ongoing outreach process with respect to the ANPRM, and then led an open forum to discuss the following key issues raised during the comment period and at prior public meetings:

Definition of Beneficial Ownership

- To address some confusion expressed by commenters at the prior public meetings, Treasury officials clarified that the ANPRM definition of "beneficial owner" with respect to a legal entity customer includes both concepts of ownership and control.
- Many participants reiterated that any proposed definition of "beneficial owner" intended to cover the wide variety of customers opening accounts, types of accounts opened, and products and services offered must be clear and practical such that financial institutions, their line employees and their customers can understand and apply the definition with certainty.
- Some commenters also requested that financial institutions be provided sufficient flexibility in applying the definition of "beneficial owner." They noted that control may be relevant under some circumstances; ownership may be relevant in others. One commenter suggested that FinCEN propose various alternative definitions. Other commenters questioned how far up a chain of complicated ownership structures they would be expected to conduct diligence in determining beneficial ownership.
- Treasury officials recognized how the various comments highlighted the challenge in proposing a definition that provides flexibility and consistency, but emphasized the need to achieve both.

Obtaining Beneficial Ownership Information – Current Practices

- Treasury officials discussed the importance of beneficial ownership information to law enforcement investigations, and also highlighted its relevance in enabling financial institutions to develop a more comprehensive risk profile. Treasury officials then 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, how and in what circumstances, financial institutions obtain beneficial ownership information. Some financial institutions obtain beneficial ownership information in all circumstances, while some do so only for certain customers (such as certain non-operating entities formed under the laws of foreign jurisdictions) or after a triggering event has been identified. Financial institutions also described varying practices relating to the types of information obtained from customers about beneficial owners (e.g., name and address, name only, etc.). Further, other institutions described the various ways in which they obtain beneficial ownership

information, including the thresholds used to determine whether an individual is a beneficial owner (e.g., one institution uses a 25% threshold for normal risk situations, and a 10% threshold for higher risk situations).

- Commenters noted that widely divergent practices among financial institutions create business competitiveness concerns whereby some institutions with robust compliance procedures risk losing customers to other institutions with more lax procedures. Further, commenters also described inconsistencies among the regulators in enforcing compliance standards.
- Some commenters encouraged FinCEN to consider the practice in other jurisdictions of providing detailed, industry-specific guidance. They noted how such guidance is helpful in facilitating consistent beneficial ownership practices within industries, which also promotes consistent customer expectations. At the same time, however, commenters suggested that financial institutions are in the best position to determine how to operationalize due diligence practices. Accordingly, they suggested that FinCEN should set forth broad policy goals and let the financial institutions determine how best to operationalize them.

Verification of Beneficial Ownership – Identity and/or Status

- Treasury officials 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.
- With respect to verifying the identity of a beneficial owner, some comments expressed general support for a process similar to customer identification program (CIP) rules, but with greater clarity with respect to verification through documentary and non-documentary means. Other commenters noted that a requirement to conduct the verification component of CIP on all persons identified as beneficial owners would significantly increase compliance costs. Treasury contemplates that any requirement to obtain information on beneficial ownership would lead to the identification of only one or a few individuals in most circumstances.
- Many commenters noted that verifying the status of an individual as a beneficial owner (i.e., that the individual identified as a beneficial owner is in fact a beneficial owner) would impose a substantial burden on financial institutions. Some financial institutions do have policies to identify and verify the status of beneficial owners in certain customer relationships, such as private banking and other personalized relationships, but it may not be possible in all circumstances.
- Various commenters expressed support for legislation that would require the disclosure of beneficial ownership information at the time of company formation because it would provide an independent source of verification. Treasury officials also noted that such legislation would familiarize customers with the process of providing beneficial

ownership information, which some commenters welcomed as this would promote consistent customer expectations when opening accounts at financial institutions.

- Some commenters acknowledged that a beneficial ownership requirement that permits reliance on a customer's self-certification (with no requirement for the financial institution to verify the status of an individual as a beneficial owner) could be workable as a broad-based approach, but questioned the utility of such a requirement as the information may be inaccurate or misleading. Treasury officials reiterated that an intentionally misleading customer response could have significant prosecutorial value, including for purposes of proving criminal intent.

Challenges Associated with Certain Products, Services, and Relationships

- Treasury officials sought comment on the challenges associated with obtaining beneficial ownership information in specific contexts, such as intermediated relationships and other unique circumstances.
- Some commenters noted that reliance on intermediaries and other market participants is important in mitigating risk efficiently. To facilitate such reliance, some commenters expressed support for FinCEN to regulate other market participants, including investment advisers and hedge fund administrators.
- 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 significant diversion of limited resources. Commenters from the securities industry, where intermediation is particularly common, highlighted the importance of existing FinCEN guidance related to omnibus accounts and other intermediated relationships, and urged FinCEN to affirm such guidance and extend its application to the beneficial ownership requirement.
- Treasury officials also acknowledged the importance of existing FinCEN guidance with respect to CIP for omnibus accounts and other intermediated relationships, and acknowledged its potential relevance to a beneficial ownership requirement.³

³ See, e.g., FinCEN Guidance, FIN-2007-G001, *Application of the Customer Identification Program Rule to Futures Commission Merchants Operating as Executing and Clearing Brokers in Give-Up Arrangements* (April 20, 2007), available at http://www.fincen.gov/statutes_regs/guidance/html/cftc_fincen_guidance.html; FinCEN Guidance, FIN-2006-G004, *Frequently Asked Question Regarding Customer Identification Programs for Futures Commission Merchants and Introducing Brokers* (31 CFR § 103.123 (February 14, 2006)), available at http://www.fincen.gov/statutes_regs/guidance/html/futures_omnibus_account_qa_final.html; Guidance from the Staffs of the Department of the Treasury and the U.S. Securities and Exchange Commission, *Question and Answer Regarding the Broker-Dealer Customer Identification Program Rule* (31 CFR 103.122) (October 1, 2003), available at http://www.fincen.gov/statutes_regs/guidance/html/20031001.html.

Other Issues Pertaining to the Advance Notice of Proposed Rulemaking

- Some comments expressed confusion about whether the fourth element of a customer due diligence program (“Ongoing Customer Due Diligence”) referred to transaction monitoring or an update of information provided by the customer. Treasury officials clarified that this element referred primarily to transaction monitoring and the general current practice of collecting additional customer information when the monitoring systems identify a triggering event.
- One commenter described the current practice of obtaining additional information from customers after the transaction monitoring system generated an alert, and noted that standardizing the collection of more information during the onboarding process would reduce costs associated with this practice.
- 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 customer identification program rules,⁴ 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.
- Commenters also discussed other possible options for exempting certain customers. One potential option includes exemptions based on a financial institution’s demonstrated conclusion that a certain customer relationship is low risk. Another commenter discussed the concept of industry designating specific customer relationships in which certain exemptions may apply and providing information to the government on the assertion of such an exemption (akin to the Designation of Exempt Person process applicable to currency transaction reporting). Another option included exemptions granted by FinCEN pursuant to a request submitted by a financial institution. In response, participants noted a preference for exemptions that would not entail a separate reporting or request requirement. Further, another commenter recommended an exemption based on dollar thresholds.
- Commenters generally agreed that coordination between Treasury and the federal functional regulators is critical in promoting consistent compliance examinations. Commenters also welcomed Treasury’s continued outreach to the industry on the ANPRM.

⁴ See, e.g., 31 CFR §1020.100(c)(2).

Conclusion

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 regional and industry-specific outreach events. Treasury officials encouraged participants to continue to send comment letters to FinCEN on any of the issues discussed in the meeting.