July 1, 2002

Financial Crimes Enforcement Network,
P.O. Box 39,
Vienna, Virginia 22183.

Attention: Section 312 Regulations
regcomments@fincen.treas.gov

Re: Notice of Proposed Rulemaking on Anti-Money Laundering
Due Diligence Programs for Certain Foreign Accounts

Ladies and Gentlemen:

ABA Securities Association, the American Bankers Association, the Bankers Association for Finance and Trade, the Financial Services Roundtable, the Futures Industry Association, the Institute of International Bankers, the Investment Company Institute, the Securities Industry Association, the Swiss Bankers Association, The Bond Market Association, and The New York Clearing House Association L.L.C. (the "Associations"),[1] which represent virtually every major covered financial institution, as well as a broad spectrum of other financial institutions, appreciate the opportunity to comment jointly on the proposed rule (the "Proposed Rule") issued by the Department of the Treasury and the Financial Crimes Enforcement Network (collectively, the "Department") to implement Section 312 of the USA PATRIOT Act (the "Act").[2] 67 Fed. Reg. 37736 (May 30, 2002).

The Associations and their member institutions are committed to assisting the Government in deterring and preventing money laundering and terrorist financing, and we are eager to assist the Department in developing regulations relating to due

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1 See Annex A for a description of each of the Associations.

2 Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (Pub. L. No. 107-56).

diligence that best achieve this fundamental objective. Our comments on the Proposed Rule cover six basic sets of issues: (i) the need for a risk-based approach, which focuses due diligence on areas where risk is most meaningful, and which includes reliance, in appropriate circumstances, on intermediaries (pp. 2 to 4); (ii) the timing for implementation of the Proposed Rule (pp. 4 to 8); (iii) the scope of the Proposed Rule (pp. 8 to 14); (iv) the enhanced due diligence requirements for correspondent accounts (pp. 14 to 20); (v) the use of "publicly available" information (pp. 20 to 21); and (vi) the due diligence requirements for, and definitions relating to, private banking accounts (pp. 21 to 24). We also include as Annex B some ancillary issues with regard to which we believe clarification would be helpful.

I. Risk-Based Approach

The Proposed Rule describes a risk-based approach to the due diligence requirements of Section 312, both in terms of concept (67 Fed. Reg. at 37737) and specific requirements (67 Fed. Reg. at 37739). Such an approach for Section 312 is consistent with the Department's interim final rules implementing Section 352 of the Act, which direct financial institutions to follow a risk-based approach in establishing anti-money laundering programs and the Department's final rule on suspicious transaction reporting for broker-dealers. 67 Fed. Reg. 21114, 21116 (Apr. 24, 2002) (money services business); 67 Fed. Reg. at 21119 (mutual funds); and 67 Fed. Reg. at 21127 (operators of credit card systems); RIN 1506-AA21 (broker-dealer reporting).

The Associations strongly endorse a risk-based approach. In our view, a fundamental and essential element of an effective due diligence program is a rigorous risk assessment by a covered financial institution of its businesses, its clients, the types of accounts it maintains, and the types of transactions in which it engages. The Proposed Rule mandates five basic due diligence steps for correspondent accounts, and the second step explicitly states that covered financial institutions are to assess the risk presented by foreign financial institutions. 67 Fed. Reg. at 37743 (proposed Section 103.176(a)(2)). We believe that the remaining due diligence requirements are a part of – and should be informed by and graduated according to – that initial risk assessment.

A risk-based approach is particularly essential to the effective implementation of Section 312 and the Proposed Rule because of their wide breadth in terms of both the financial institutions and the financial transactions that are covered. Such an approach enables covered financial institutions to focus their attention and resources on those customers, accounts and transactions that are most vulnerable to money laundering and terrorist financing. We respectfully submit that an approach which does not permit the covered financial institution to differentiate meaningfully among customers, accounts and transactions will result in less rather than more effective deterrence and prevention. Unless due diligence is tailored to the money laundering risks presented, it will be unfocused, overly diffuse and ultimately unproductive, and create a greater risk that unlawful activity will go undetected.

We recommend that the Proposed Rule explicitly recognize two vital components of an effective risk-based due diligence program. The first key component relates to the distinction between proprietary accounts of foreign financial institutions and accounts that such institutions may use to provide services to third parties. The former type of account normally does not create the types of concerns to which the Act is directed, because there is no question on whose behalf the foreign financial institution is acting or whose funds are involved.

The second key component is reliance, in appropriate circumstances, on reputable intermediaries that conduct due diligence with respect to their own clients. A predicate of this reliance would be risk-based due diligence conducted by the covered financial institution on the intermediary with respect to the intermediary's anti-money laundering due diligence on its own clients. The due diligence conducted by the intermediary on its own clients almost inevitably would be superior to a covered financial institution's due diligence capacity on the underlying third parties. The reliance on intermediaries is discussed in greater detail below. See Section III.D.

In this comment letter, the Associations make a number of other recommendations for incorporating a risk-based approach into the requirements of the Proposed Rule. The Associations are committed to working with the Department and the relevant federal functional regulators to enhance further these recommendations through

the development of industry guidance. Many of the Associations have already published guidance on implementation of the due diligence and various other requirements of the Act, and we will continue to work with the Department and jointly within our industry to refine that guidance to achieve our common goal of deterring money laundering and terrorist financing. For example, there is a current industry effort to develop types of representations that would be provided by intermediaries for the purpose of allowing covered financial institutions to rely on due diligence performed by such intermediaries.

II. Timing for Implementing the Proposed Rule

The Associations are appreciative of the Department's constructive efforts to develop realistic implementation deadlines throughout the process of promulgating regulations under the Act. For example, the Department's interim guidance that implemented the Sections 313 and 319(b) certification process allowed covered financial institutions the flexibility to accord priority to foreign banks from which the certification could be most readily obtained, i.e., those foreign banks for which covered financial institutions maintained correspondent deposit accounts (or their equivalents). 66 Fed. Reg. 59342, 59343 (Nov. 27, 2001). The interim final rules under Section 352 of the Act, which were issued on April 23, 2002 and became effective on April 24, 2002, allowed certain U.S. financial institutions to be in compliance with the requirements of the Act by implementing their anti-money laundering programs by July 24, 2002. 67 Fed. Reg. at 21117 (money services businesses); 67 Fed. Reg. at 21121 (mutual funds); 67 Fed. Reg. at 21127 (operators of credit card systems). The final rule on suspicious transaction reporting for broker-dealers applies to transactions occurring after 180 days after the date of publication in the *Federal Register*. RIN 1506-AA21.

The Associations urge the Department to adopt a similar approach with regard to implementation of the Proposed Rule. Section 312(b)(2) of the Act provides that Section 312 will take effect on July 23, 2002, and will apply with respect to all accounts covered by the requirement, regardless of when they were established. Although our member institutions will seek to conform their current due diligence practices to the new rule as promptly as feasible, it is simply impossible, as a practical matter, for the Associations' member institutions to comply with the comprehensive and

detailed requirements of the Proposed Rule by the July 23 statutory date. There are a number of reasons, each of which alone may be preclusive, and which in combination render full compliance impossible.

First, there is likely to be very close proximity, and perhaps virtual simultaneity, between the July 23 statutory date and the promulgation of the final rule. Under the best of circumstances, the final rule is unlikely to be published until days before July 23, 2002. Once published, the final rule will have to be reviewed and analyzed by covered financial institutions, and responsive due diligence and enhanced due diligence procedures put in place. Although, since publication of the Proposed Rule on May 30th, covered financial institutions have been attempting to craft due diligence procedures based upon their present understanding of the requirements of the Proposed Rule, anti-money laundering compliance systems cannot be finalized until the final terms of the rule are known.

Second, as discussed below, unless there are substantial changes in the proposed definitions of "correspondent account" and "foreign financial institution," member institutions of the Associations would apparently be required to conduct due diligence with respect to practically all business relationships with all foreign financial institutions and enhanced due diligence with respect to practically all business relationships with foreign banks subject to enhanced due diligence under the Proposed Rule. Although certain of our member institutions have been conducting due diligence on traditional types of correspondent accounts and enhanced due diligence on certain correspondent accounts and other accounts viewed as creating a special risk of money laundering, they have not conducted a similar level of due diligence in connection with their entire range of dealings with all foreign financial institutions. Other member institutions are dealing with the concept of correspondent accounts for the first time. To comply with the Proposed Rule, numerous additional accounts and transactions must be identified, and substantial new systems and procedures must be developed and implemented.

Third, some of the elements of the proposed enhanced due diligence requirements applicable to certain correspondent accounts do not currently form part of

the anti-money laundering programs in place at most covered financial institutions. For example, covered financial institutions do not presently ask their foreign bank customers to identify all the other foreign banks for which accounts are maintained. Obtaining this information from foreign bank customers may be problematic, and will, at the very least, take substantial time.

Fourth, although some of the Associations' member institutions have for years been subject to anti-money laundering due diligence requirements, for others, parts of the process are new.

In order to deal with these timing difficulties, the Associations urge the Department to adopt a bifurcated approach to implementation that distinguishes between new accounts (prospective application) and existing accounts (retrospective application). This approach is designed to achieve implementation as soon as feasibly, as opposed to theoretically, possible.

With respect to new accounts, the Associations recommend that the Proposed Rule should utilize a risk-based approach under which the requirements would become effective in two stages. First, the effective date with regard to new correspondent accounts that are subject to enhanced due diligence and private banking accounts should be 30 days after publication of the final rule in the *Federal Register*. These accounts are recognized in the Act as presenting a higher risk of money laundering and terrorist financing. Second, the effective date with regard to all other new correspondent accounts should be no earlier than 90 days after publication of the final rule.

Retrospective application of the Proposed Rule with regard to existing accounts presents a significant additional problem. Many member institutions have not previously identified and classified foreign financial institutions, as defined in the Proposed Rule, for due diligence purposes. Nor have they identified and classified all business relationships with foreign financial institutions for due diligence purposes. In addition, the member institutions have not previously obtained information about all the "beneficial owners" of private banking accounts or their foreign banks' bank customers as provided in the Proposed Rule. These additional requirements will involve a lengthy process that must be performed by human beings rather than computers. Indeed,

computers cannot conduct this subjective analysis that is essential to the due diligence that is required by the Proposed Rule. Moreover, covered financial institutions' computer systems are not currently coded to identify and classify foreign financial institutions and business relationships according to the requirements of the Proposed Rule. Also, the full scope of these requirements will only be known once the final rule is promulgated.

Accordingly, the Associations recommend that the Proposed Rule become effective with respect to existing correspondent and private banking accounts no earlier than 180 days after publication of the final rule in the *Federal Register*. On the effective date, covered financial institutions would be required to: (i) have programs in place to address the new requirements; and (ii) have made a good faith effort to apply the new requirements to existing accounts. As part of this process, covered financial institutions would be instructed to review existing accounts on a risk-focused basis, with priority accorded to those accounts believed to create meaningful risk of money laundering or the financing of terrorist activities.

Even within a 180-day period, major covered financial institutions may find it difficult to identify and review all the accounts that may come within the purview of the Proposed Rule, because the retrospective review of existing correspondent accounts (as so broadly defined) will necessarily involve numerous time-consuming steps, virtually all of which would require substantial human participation. At the outset, covered financial institutions will have to identify (i) all their existing clients that are foreign financial institutions as defined in the Proposed Rule; and (ii) those relationships with foreign financial institutions that are subject to the Proposed Rule. Thereafter, depending upon the relevant circumstances and a risk-based approach, covered financial institutions may need to: (i) evaluate the adequacy of documentation on file regarding these foreign financial institution clients; (ii) review the overall client relationship; (iii) review the anti-money laundering regime in the client's home country; (iv) review the client's individual anti-money laundering program; (v) organize and centralize relevant documentation; (vi) distribute requests for information or additional information where needed to these clients; and (vii) administer the process of receiving and processing the responses to requests for information from these clients.

III. Scope of the Proposed Rule

The combination of extremely broad definitions of "correspondent account", "foreign financial institution" and "covered financial institution" expands significantly the scope of the due diligence and enhanced due diligence requirements in the Proposed Rule. With respect to these terms, the Associations recognize the inherent difficulty in arriving at definitions that are both sufficiently focused and sufficiently inclusive. The Associations believe, however, that the key definitions in the Proposed Rule have unnecessarily sacrificed focus for total inclusiveness. Our recommendations attempt to incorporate a risk-based approach that balances the need for comprehensive coverage with the equally important need for focused and effective resource allocation.

A. "Correspondent Account"

As proposed, the definition of "correspondent account" reaches practically every relationship of a covered financial institution with a foreign financial institution. In separate comment letters in response to the Department's proposed rule implementing Sections 313 and 319(b) of the Act, many of the Associations have previously set forth the reasons why they believe that the Department has the legal authority to define the term "correspondent account" on a more focused, risk-oriented basis and why such a focused definition would be consistent with both sound public policy and legal authority.

In these comment letters, the individual Associations proposed somewhat different definitions of "correspondent account". There is, however, a common denominator in all these proposed definitions – an attempt to apply the concept of "correspondent account" only to those accounts and transactions where the risk of money laundering is meaningful. This would enable covered financial institutions to focus their attention where it is most needed. We strongly urge that this should also be the focus of the final rule, and we are convinced that such an approach would be consistent with both the Act and sound public policy.

Specifically, as set forth in prior comment letters, the Associations believe that the risk of money laundering and terrorist financing is not meaningful in the following situations involving accounts or transactions with foreign financial institutions:

(i) Where a foreign financial institution (either a client or a counterparty) is acting as principal (as is often the case with foreign exchange, derivatives and other capital markets transactions, and extensions of credit);

(ii) Where the covered financial institution's relationship or account with the foreign financial institution is established for a specific purpose and funds are received or disbursed under limited defined circumstances to identified third parties, as set forth in an agreement with the foreign financial institution (*e.g.*, escrow, corporate trust, paying agency and custody);

(iii) Where the account is for investment of funds that are subject to a regulatory scheme (*e.g.*, investment of funds of regulated pension or retirement plans); and

(iv) Where the account is held by a foreign financial institution that is itself subject to and complies with a robust anti-money laundering regime.

We therefore urge the Department to refine the definition of "correspondent account" to achieve an approach that is truly risk-based. This could be accomplished by focusing on types of transactions and the role of the client. At the very least, a risk-based approach should be emphasized as a fundamental element of covered financial institutions' due diligence efforts.

B. "Covered Financial Institution"

The bank members of the Associations believe strongly that the definition of "covered financial institution" should not be applied to foreign branches of insured depository institutions. As a matter of law, the application of Section 312 to foreign branches is clearly beyond the scope of that Section. Section 312's due diligence requirements are explicitly limited to correspondent accounts and private banking accounts established or maintained "in the United States". Accounts at foreign branches of U.S. banks are therefore not included within this definition. Accordingly, the Proposed Rule extends beyond the permissible statutory boundaries.

The Associations' bank members recognize, however, the Department's concern that a failure to include foreign branches of U.S. banks in the definition of

"covered financial institution" could result in a gap in application of the Act's due diligence requirements. The Associations' bank members believe that, as a practical matter, such a gap would not exist, because they apply a high standard of anti-money laundering programs across their organizations globally. In fact, a foreign branch or foreign affiliate of a covered financial institution is normally subject to both the anti-money laundering policies and procedures of its head office and the anti-money laundering regime of the jurisdiction in which it operates. This situation should mitigate the Department's concern, but not the need of the Associations' bank members for relief. There is an important difference between voluntary compliance with the requirements of a covered financial institution's own due diligence policies on a risk-focused basis in a foreign market and compliance with a one-size-fits-all regulatory regime. Broad-based regulatory due diligence requirements may not fit the specific market conditions or legal requirements in foreign jurisdictions.

If the Department nonetheless continues to have a significant concern, the Associations' member banks recommend the following approach to close any gap in coverage. For purposes of Section 312 and the Proposed Rule, foreign branches would be treated, similar to the proposed treatment for foreign affiliates of covered financial institutions, as foreign financial institutions.[3] If a foreign branch is in a jurisdiction that would subject it to enhanced due diligence, it might be treated as a foreign bank. A covered financial institution would not be required, however, to conduct due diligence on the foreign branches and affiliates of another covered financial institution, provided that such other covered financial institution provides a certification stating that a particular foreign branch or affiliate is subject to the due diligence policies and procedures of the head office.

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[3] It should be noted that separate offices of a bank are treated as separate banks for purposes of Article 4A of the Uniform Commercial Code, the basic law governing funds transfers in the United States. See U.C.C. §4A-105(a)(2).

C. "Foreign Financial Institution"

1. Definition

The breadth of the definition of "foreign financial institution" creates two principal problems.

The first problem is logistical. In the Proposed Rule, the definition of "foreign financial institution" is tied to the definition of "covered financial institution". 67 Fed. Reg at 37738. It will be extremely difficult to apply a definitional concept tailored for U.S. financial institutions to foreign entities where there is different terminology, different methods of conducting business and different licensing and regulatory schemes.[4]

In order to facilitate a workable process for identifying the entities whose correspondent accounts are covered, we strongly recommend that the Department define "foreign financial institution" by a specific list of enumerated categories of financial institutions that are regulated or licensed in the foreign country and other institutions that perform the same functions. We would recommend that this list be comprised of banks, broker-dealers, mutual funds (or some other term such as "publicly offered investment funds" that has the same connotation), currency exchanges and money transmitters. We further request that the Proposed Rule recognize the potential of relying upon private-sector compilations of foreign financial institutions.

2. Due Diligence

The second problem is more substantive. In our view, there is a wide variety of risk involved in the broad gamut of financial transactions with a broad gamut of foreign financial institutions covered by the Proposed Rule. Consistent with a risk-based approach, the Associations propose that the Department allow covered financial institutions to use a risk-based system in applying the requirements of the Proposed Rule to foreign financial institutions, as defined in the Proposed Rule, and in identifying

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[4] As stated above, U.S. financial institutions do not currently have the logistical electronic capabilities to identify and classify all foreign financial institutions (as defined), as they have not historically tracked such a broad range of foreign entities.

specific transactions with those institutions. Covered financial institutions should be permitted to assess the risks of money laundering and terrorist financing presented by various foreign financial institutions and transactions with them and apply due diligence or enhanced due diligence to those institutions and transactions, as appropriate. In performing that risk assessment, covered financial institutions may consider, among other factors: (i) the depth and duration of the foreign financial institution's relationship with the covered financial institution; (ii) whether the foreign financial institution is part of a regulated group or is subject to comprehensive consolidated supervision; (iii) the geographic location of the foreign financial institution; (iv) the reputation and background of the foreign financial institution; (v) the reputation of the foreign financial institution's regulator; (vi) whether the foreign financial institution is publicly held; (vii) whether the particular type of foreign financial institution has been known to raise money laundering concerns; (viii) the scope of the foreign financial institution's own anti-money laundering program; and (ix) the scope of the anti-money laundering regime of the principal regulator of the foreign financial institution.

D. "Intermediaries"

An essential element of achieving a balanced, risk-based approach would be explicit recognition in the Proposed Rule that covered financial institutions are entitled to rely, in appropriate circumstances, on the due diligence conducted by intermediaries. Numerous "accounts" at covered financial institutions that are subject to Section 312 involve foreign entities which trade, make payments and transact other business on behalf of third parties. These intermediaries are often large, well-regarded, publicly traded and highly regulated entities with strong anti-money laundering programs. Many are organized in foreign jurisdictions with robust anti-money laundering regimes.

Assuming that a covered financial institution has conducted appropriate due diligence on the intermediary, and has determined that the intermediary has satisfied relevant criteria, it would be unfruitful and unnecessary to repeat the due diligence process that has already been conducted by the intermediary on its own client base. It is not reasonable to expect that the covered financial institution could perform due diligence superior to that conducted by the intermediary; indeed, in many cases, the covered

financial institution would have at most limited ability to conduct due diligence on the intermediary's clients.

Appropriate due diligence on an intermediary could include, in addition to the risk assessment factors described in Section III.C. above: (i) determining whether the intermediary is from a jurisdiction that follows the Financial Action Task Force on Money Laundering ("FATF") recommendations on anti-money laundering (or has procedures consistent with the FATF recommendations); (ii) determining whether the intermediary is from a country or territory designated by FATF as noncooperative with international anti-money laundering policies and procedures; and (iii) representations from the intermediary as to its own due diligence program.

The Associations are preparing a proposed attestation form (which could be adapted for various purposes) setting forth the types of representations that would be obtained from intermediaries.

IV. Enhanced Due Diligence Requirements Applicable to Certain Correspondent Accounts

The Associations are deeply concerned about the imposition of enhanced due diligence requirements on every bank licensed in every jurisdiction that appears on the list of countries and territories designated by FATF as noncooperative with international anti-money laundering policies and procedures (the "FATF NCCT List"). This concern does not extend to the offshore banks subject to enhanced due diligence, nor to banks in jurisdictions on the FATF NCCT List that are reputed to be money laundering havens. The Associations' member institutions understand the need to conduct enhanced due diligence on correspondent accounts from these two groups of banks.

With regard to certain jurisdictions on the FATF NCCT List, however, the Associations' concern is that the enhanced due diligence requirements may force covered financial institutions to consider closing all the correspondent accounts of, and terminate all other business relationships with, banks that are licensed in these jurisdictions. These jurisdictions include major United States allies in the War against Terrorism – the Philippines, Russia and Egypt – that could be totally cut off from direct access to U.S.

financial markets. Ironically, this would be directly contrary to FATF's own directives, which provide that the appearance of a jurisdiction's name on the FATF NCCT List should not halt normal business relations.

The Associations believe that such a dire result is not an unrealistic scenario. In some cases, foreign banks will be precluded by the laws of their home country jurisdictions from providing the enhanced due diligence information regarding their customers required under the Proposed Rule. In other cases, they may simply refuse to provide this information because it may be deemed to be too sensitive competitively. And even if the information is provided, covered financial institutions would be at substantial risk if they continued to conduct business with the foreign bank because of the difficulty of conducting adequate due diligence on such information.

Once again, the Associations recommend a risk-based approach, under which covered financial institutions would perform a risk assessment of each foreign bank for the purpose of evaluating the degree to which the covered financial institution could justifiably rely on the due diligence performed by the foreign bank on its foreign bank customers. These factors could include, in addition to the risk assessment factors described above in Section III.C.: (i) the extent to which the foreign bank had due diligence policies and procedures that were consistent with the FATF recommendations; (ii) official pronouncements by FATF or other intergovernmental groups or organizations and the United States Government regarding efforts by the relevant jurisdiction to improve its anti-money laundering regime; (iii) whether the Board of Governors of the Federal Reserve System has determined that banks in the relevant jurisdiction are subject to comprehensive supervision or regulation on a consolidated basis; and (iv) whether the Department has approved institutions in the foreign bank's home country to operate as Qualified Intermediaries.

Based on this risk assessment, the covered financial institution would determine whether it could rely exclusively on the foreign bank's due diligence of its foreign bank customers or should obtain additional information about the identities of those customers. Such information could include, depending on the relevant risk-related circumstances, a list of names and addresses of the customers, representations about the

general character of those customers, or specific due diligence information regarding those customers.

The Associations believe that this approach represents a practical solution to the enhanced due diligence requirements in that it will focus the greatest attention on the accounts that create the greatest risk. This approach also provides the flexibility to take into account the potential that a jurisdiction will be removed from the FATF NCCT List, as recently occurred for Hungary and Israel.

In addition, the Associations have the following specific comments on the enhanced due diligence requirements set forth in the Proposed Rule:

A. Requirement to Review and Evaluate a Foreign Bank's Anti-Money Laundering Program

Under the Proposed Rule, the enhanced due diligence requirement for reviewing a foreign bank's anti-money laundering program is satisfied by obtaining and reviewing the foreign bank's documents relating to its anti-money laundering program. The Associations strongly endorse this approach, under which this review would be one component of the overall risk-based assessment. It should be noted that covered financial institutions are in no position to audit, on a periodic basis or otherwise, a foreign bank's anti-money laundering program. An audit obligation would not merely be burdensome; it would impose a standard that often could not be satisfied, even assuming the foreign bank would permit it.

B. Requirement to Identify Persons With the Authority to Direct Transactions Through the Account

This issue is presumably only one of clarification. We assume that this requirement is directed at so-called payable through accounts at depository institutions.[5]

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[5] A payable through account, as defined in Section 311(e)(1)(C) of the Act, is an account of a foreign financial institution at a depository institution "by means of which the foreign financial institution permits its customers to engage, either directly or through a subaccount, in banking activities usual in connection with the business of banking in the United States."

If our assumption is correct, the requirement is understandable, and it does not create a serious compliance issue.

If, however, this requirement is directed at something broader than payable through accounts (*e.g.*, traditional correspondent accounts in the banking industry and omnibus accounts in the futures and the securities industries), the requirement is less understandable and quite probably impossible to implement. There would be many thousands of persons covered by the identification requirement and they could change frequently.[6] Moreover, both the foreign bank and its customers may object to the disclosure of the information, and local privacy laws may be violated. In addition, even if covered financial institutions received the names, in most cases it would be impossible to conduct meaningful due diligence with regard to those names.

The Associations accordingly request confirmation that this requirement of identifying persons with authority to direct transactions through the correspondent account applies only to payable through accounts.

C. Requirement That a Covered Financial Institution Identify a Foreign Bank's Bank Customers

This requirement creates the principal risk that the enhanced due diligence process will close U.S. financial markets to those foreign banks subject to it. Foreign banks may be legally precluded from providing information regarding their bank customers to a covered financial institution because it would violate foreign privacy or data protection laws. Even absent any legal prohibition, foreign banks will be highly reluctant, for competitive reasons, to provide the names of all their bank customers.

We believe that the Department could take several steps in the final rule to reduce this possibility. Of most importance, the Department should adopt the risk-based approach described above. The Department also should define "correspondent account" for these purposes in a way that excludes accounts in which no transactions are conducted

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[6] For traditional correspondent accounts, this requirement would apply to every customer of the foreign bank that might request the bank to make an international payment on its behalf, as well as multiple individuals at each customer that are authorized to instruct the foreign bank to make a payment on the customer's behalf.

for third parties, for example, where a foreign bank is trading for its own account using proprietary funds. In addition, the final rule should clarify that the identification requirement does not constitute a continuous obligation, but that information should be updated periodically.

Even if foreign banks are prepared to identify all their bank customers, a significant issue remains. The Proposed Rule requires a covered financial institution's due diligence program to provide for policies, procedures and controls to assess and minimize risks associated with a foreign bank's correspondent account for other foreign banks. 67 Fed. Reg. at 37743. This requirement can be read as containing an implicit obligation upon covered financial institutions to conduct due diligence with regard to a foreign bank's bank customers. Covered financial institutions cannot practically conduct due diligence on all the bank customers of the foreign bank, which, in some cases, may number in the thousands. The Associations believe that it is essential that the final rule clarify that covered financial institutions do not have any due diligence obligations with respect to a foreign bank's bank customers.

D. Requirement to Identify the Owners of a Privately Held Foreign Bank

The Associations believe that the 5% threshold for the definition of "owner" of a privately held foreign bank is too low. A more appropriate test would be the definition of "owner" used in the certifications for purposes of Sections 313 and 319(b) of the Act. 66 Fed. Reg. 67460, 67466 (December 28, 2002). For purposes of that certification, each of the constituent elements of the definition of an "owner" of a foreign bank—a "large direct owner", an "indirect owner", and certain "small direct owners"—is defined to capture persons who, individually or together with others, own 25% or more of any class of voting securities or other voting interests of a foreign bank. This approach should provide the necessary information, and both covered financial institutions and foreign banks have become accustomed to the application of this standard.

E. Timing Issues

The enhanced due diligence requirements of the Proposed Rule raise certain practical timing issues which the Associations request the Department to clarify. First, unlike standard due diligence, enhanced due diligence requires foreign banks to provide certain information. It is not clear whether covered financial institutions will be required to close immediately the existing correspondent accounts of a foreign bank subject to enhanced due diligence if that bank has not provided the requisite information by the implementation date. The Associations respectfully submit that the final rule should clarify that, if termination of a correspondent account of a foreign bank is warranted, the covered financial institution may follow its normal business practices in terminating the account.[7] The Department has helpfully recognized that in certain circumstances, such as where an account contains open securities or futures positions, a covered financial institution should be permitted to exercise "commercially reasonable discretion" in liquidating such open positions. 66 Fed. Reg. at 67462.

Second, if additional jurisdictions are added to the FATF NCCT List (as occurred in September, 2001), we believe that the Department will need to provide a grace period to allow covered financial institutions to amend their enhanced due diligence policies and procedures for foreign banks licensed in the added jurisdictions.

F. Offshore Bank Affiliates of Regulated Institutions

The Associations fully endorse the exemption from the enhanced due diligence requirements of the Proposed Rule for offshore branches of a foreign bank that (i) is not licensed in a jurisdiction that has been designated as noncooperative with international money laundering standards or as warranting special measures due to money laundering concerns, and (ii) has been found, or is chartered in a jurisdiction where one or more foreign banks have been found, by the Board of Governors of the Federal Reserve System, to be subject to comprehensive supervision or regulation on a

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[7] The Proposed Rule recognizes that termination of an account may not always be warranted when due diligence cannot adequately be performed. Other options may include, where appropriate, filing suspicious activity reports or freezing the account. 67 Fed. Reg. at 37744.

consolidated basis by the relevant supervisors in that jurisdiction. 67 Fed. Reg. at 37743. The Associations believe that this exemption is consistent with the risk-based approach of the Proposed Rule, and we believe the exemption should also apply to offshore bank subsidiaries and affiliates of foreign financial institutions that satisfy similar criteria. For example, if a foreign bank operating under an offshore license is affiliated with a foreign financial institution and is subject to comprehensive consolidated supervision by the home country regulator of the foreign financial institution, the offshore bank should not be subject to enhanced due diligence.

V. The Concept of "Public Information"

In a number of situations, the Proposed Rule imposes an obligation upon covered financial institutions to search "public information" as an essential element of the due diligence requirements. This obligation is imposed, for example, in determining (i) whether a person maintains a close personal or professional relationship with a senior foreign political figure (proposed Section 103.175(o)(iv)); (ii) the supervisory and regulatory regime applicable in a foreign financial institution's home country jurisdiction (proposed Section 103.176(a)(3), as explained at 67 Fed. Reg. at 37739); and (iii) whether a foreign financial institution has been the subject of a criminal action of any nature or regulatory action relating to money laundering (proposed Section 103.176(a)(5)). In addition, although not explicitly required by the Proposed Rule, the preamble indicates that covered financial institutions should avail themselves of public information about jurisdictions in which their foreign financial institution customers are organized or licensed (67 Fed. Reg. at 37739).

The Associations agree that covered financial institutions should scrutinize publicly available information as part of their due diligence efforts. But this must be public information that is both readily accessible and reasonably reliable. The Associations recommend that the "public information" referred to throughout the Proposed Rule be defined as information that is disseminated through a form of print media that is (i) widely and readily available; (ii) generally regarded as a leading publication in its country; and (iii) generally regarded as reliable. The Associations recognize that the concept of "leading publication" and "reliability" represent subjective

judgments, but we expect that such standards would lead to an industry effort to identify those publications.

In addition, recognition should be given to both current industry efforts to utilize existing private sector databases and to create private sector repositories of relevant data. Covered financial institutions should be allowed to meet their statutory and regulatory obligations by availing themselves of these databases and repositories.

VI. Private Banking Accounts

A. Due Diligence

The Associations have two principal concerns with the Proposed Rule's due diligence requirements for private banking accounts.

First, the Associations believe that these requirements clearly are intended to be directed at accounts of foreign individuals. However, the use of the phrase "on behalf of" in Section 103.178(a) to describe private banking accounts may create ambiguity with respect to this issue. We recognize the need to prevent evasion through the use of nominees for individuals. Nonetheless, this phrase is so broad that it potentially encompasses a wide variety of accounts that are not accounts of individuals. We do not believe this was the intent of the Proposed Rule. Although we recognize that individuals can act through various investment vehicles, such as personal holding companies and trusts, and we do not seek to exclude such entities from the scope of the Proposed Rule, we respectfully request that the Proposed Rule be clarified to make clear that the private banking account requirement applies only to accounts of individuals.

The Associations' concerns arise primarily when individuals are participants in a fund or other collective investment vehicle which has an account at a covered financial institution. We assume that "private banking account" does not apply to an account held by a mutual fund or a publicly held company at a covered financial institution even if one or more foreign individuals owns shares of the fund or company with a value exceeding $1,000,000. The breadth and public nature of ownership should preclude any argument that the mutual fund or company has established an account on behalf of an individual.

The analysis becomes more difficult when dealing with a privately owned fund or other investment vehicle. At some level of breadth of ownership, it should be clear that the fund or other vehicle was not established "on behalf of" or "by" individual investors. Section 356 of the Act provides helpful guidance here. That Section, which was intended to focus attention on applying the Bank Secrecy Act requirements to privately owned funds, instructs the Board of Governors of the Federal Reserve System and the Securities and Exchange Commission to submit a report to Congress by October 26, 2002 on recommendations as to (i) whether certain personal holding companies should be regarded as financial institutions for purposes of the Bank Secrecy Act, and (ii) whether to require such personal holding companies to disclose their beneficial owners when opening accounts or initiating funds transfers at any U.S. financial institution. The test suggested in Section 356 is five or more holders. Accordingly, we recommend that the hedge funds and other investment vehicles be excluded from the definition of private bank account unless they have fewer than five holders. To protect against evasion, the exemption would not be available if any individual owned 75% or more of the fund or other entity.

Our second principal concern relates to the need for recognition of reliance on intermediaries as part of a risk-based due diligence approach in the private banking context. The Associations believe that, consistent with a risk-based approach, covered financial institutions can rely, in appropriate circumstances, on reputable intermediaries with respect to due diligence on the beneficial owners of private banking accounts. This is similar to the reliance on intermediaries discussed above in the context of correspondent accounts.

To be clear, the Associations are not advocating that foreign individuals should have access to the U.S. financial system without sufficient due diligence being performed. The question is whether that due diligence must in all cases be performed by a covered financial institution, or whether some other regulated or otherwise responsible party can be relied upon to perform that due diligence. The Associations believe that the final rule should provide for this second option where the intermediary has been subject to appropriate due diligence by the covered financial institution as described above. See Section III.D.

In summary, the Associations recommend that the special due diligence not be required under the rubric of "private banking accounts" if (i) the fund or other entity has five or more investors and no investor has 75% or more of the fund ownership; (ii) the covered financial institution can justifiably rely on an intermediary to conduct due diligence on its customers; or (iii) the intermediary is a foreign financial institution subject to the correspondent account rules. The due diligence involved in the first case would consist of obtaining reliable representations from the intermediary on the number and holdings of investors. The due diligence involved in the second case would consist of a risk-based assessment which would include consideration of relevant factors, such as those described above in Section III.D. The due diligence in the last case would consist of following the procedures for correspondent accounts of foreign financial institutions.

B. Definitions

The Associations believe that the definition of "private banking account" is overly broad. First, it should not be read to capture every account held for a foreign individual that contains a large amount of funds or other assets. The preamble to the Proposed Rule clearly states that the definition applies only to accounts that "require a minimum deposit" of $1,000,000 or more. The Associations respectfully request that the Department revise the language in the Proposed Rule to be consistent with that of the preamble.

Second, the calculation of the $1,000,000 threshold should not include the requirement by a covered financial institution that initial margin or other collateral be posted. Futures commission merchants, banks and broker-dealers might require initial margin, deposits to meet maintenance calls, or other collateral for legal or business reasons. Accordingly, the Associations recommend that "private banking account" be defined as an account that requires a minimum aggregate deposit of funds or other assets of not less than $1,000,000 without regard to the customer's posting of collateral for its financial obligations to the covered financial institution.

Third, the Associations believe that the definition of "beneficial ownership interest" is overly broad. A possible approach could be that the final rule would not seek to define "beneficial ownership interest" with general terminology, but rather allow

covered financial institutions to determine which persons, in particular circumstances, should be viewed as having the requisite beneficial ownership. The requisite beneficial ownership could be determined by reference to that level of ownership that, as a practical matter, equates with control over or entitlement to the account.

Finally, the definition of "beneficial ownership" includes a non-contingent legal entitlement to any part of the corpus or income of the account, but shall not include an immaterial interest, *i.e.*, an interest of less than the lesser of $1,000,000 or five percent of either the corpus or income of the account. The effect of this provision may be to lower the threshold for private banking accounts to below $1,000,000. The Associations request that the materiality standard be changed to either "the greater of $1,000,000 or five percent", or "$1,000,000 or more".

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The Associations appreciate the opportunity to comment on the Proposed Rule, and would be pleased to discuss any of the points made in this letter in more detail. Should you have any questions, please contact H. Rodgin Cohen or Elizabeth T. Davy of Sullivan & Cromwell at (212) 558-4000.

Very truly yours,

ABA Securities Association

American Bankers Association

Bankers Association for Finance and Trade

Financial Services Roundtable

Futures Industry Association

Institute of International Bankers

Investment Company Institute

Securities Industry Association

Swiss Bankers Association

The Bond Market Association

The New York Clearing House Association L.L.C.

ANNEX A

1. The **ABA Securities Association** is a separately chartered affiliate of the American Bankers Association representing those holding company members of the American Bankers Association that are the most actively engaged in securities underwriting and dealing activities, offering proprietary mutual funds, and derivatives activities.

2. The **American Bankers Association** brings together all categories of banking institutions to best represent the interests of this rapidly changing industry. Its membership -- which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks -- makes ABA the largest banking trade association in the country.

3. The **Bankers' Association for Finance and Trade** has, since 1921, been the spokesperson for the international interests of the U.S. commercial banking industry.

4. The **Financial Services Roundtable** represents 100 of the largest integrated financial services companies providing banking, insurance, and investment products and services to the American consumer. Member companies participate through the Chief Executive Officer and other senior executives nominated by the Chief Executive Officer. Roundtable member companies provide fuel for America's economic engine, accounting directly for $12.4 trillion in managed assets, $561 billion in revenue, and 1.8 million jobs.

5. The **Futures Industry Association** is a principal spokesperson for the commodity futures and options industry. FIA's regular membership is comprised of approximately 50 of the largest futures commission merchants in the United States, the majority of which are also registered broker-dealers. Among its associate members are representatives from virtually all other segments of the futures industry, both national and international. Reflecting the scope and

diversity of its membership, FIA estimates that its members effect more than 80% of all customer transactions executed on United States futures exchanges.

6. The **Institute of International Bankers** represents internationally headquartered financial institutions from over 40 countries that engage in banking, securities and/or insurance activities in the United States. The U.S. operations of international banks play an important role in the U.S. financial markets and economy, holding over $3 trillion in banking and financial affiliate assets and employing over 120,000 U.S. citizens and residents.

7. The **Investment Company Institute** is the national association of the American investment company industry. Its membership includes 8,984 open-end investment companies ("mutual funds"), 504 closed-end investment companies and 6 sponsors of unit investment trusts. Its mutual fund members have assets of about $6.925 trillion, accounting for approximately 95% of total industry assets, and over 88.6 million individual shareholders.

8. The **Securities Industry Association** brings together the shared interests of nearly 700 securities firms to accomplish common goals. SIA member firms (including investment banks, brokers-dealers and mutual fund companies) are active in all U.S. and foreign markets and in all phases of corporate and public finance. The U.S. securities industry manages the accounts of nearly 80 million investors directly and indirectly through corporate, thrift and pension plans. The industry generates $358 billion of revenue and employs approximately 760,000 individuals.

9. The **Swiss Bankers Association** represents approximately 400 banks, including non-Swiss banks, with operations in Switzerland. Several members of the SBA have substantial operations in the United States through branches, agencies and affiliates.

10. **The Bond Market Association** represents securities firms and banks that underwrite, trade and sell debt securities, both domestically and internationally. The Association's member firms collectively represent in excess of 95% of the

initial distribution and secondary market trading of municipal bonds, corporate bonds, mortgage and other asset-backed securities, and other fixed-income securities.

11. **The New York Clearing House Association L.L.C.** is the nation's oldest and largest clearing house. It frequently takes positions on legal and regulatory issues that are of importance to the banking industry. The members of the Clearing House are: Bank of America, National Association; The Bank of New York; Bank One, National Association; Citibank, N.A.; Deutsche Bank Trust Company Americas; Fleet National Bank; HSBC Bank USA; JPMorgan Chase Bank; LaSalle Bank National Association; Wachovia Bank, National Association; and Wells Fargo Bank, National Association.

ANNEX B

Although the Associations believe that the issues described in the comment letter are the most critical, there are a variety of other important issues raised by the Proposed Rule, and the Associations have the following additional suggestions regarding these other issues:

I. Clarify the Concept of a "Liaison"

Some clarification regarding the concept of a liaison, as it is used in the private banking context, would also be helpful. Specifically, the Associations request confirmation that a liaison must be an individual employed at a covered financial institution who has been designated – formally or informally – by the institution to manage the private banking account and provide regular and on-going assistance to the account owner.

II. Expand the Authorization to Rely on Denials of Senior Foreign Political Figure Status

The Associations appreciate that the Proposed Rule allows covered financial institutions to rely on an account owner's statement that he or she is not a "former senior foreign political figure" as long as the covered financial institution has not received information to the contrary. 67 Fed. Reg. at 37744. The Associations believe, however, that this authorization to rely should apply to a statement from an account owner denying any type of senior foreign political figure status. That is, a covered financial institution should be permitted to rely on a statement from an account owner that he or she is not a current or former senior foreign political figure as long as the covered financial institution has not received information to the contrary. There is no apparent reason for limiting the authorization to rely on denials of only *former* senior foreign political figure status.