#12

July 1, 2002

Financial Crimes Enforcement Network
Department of the Treasury
P.O. Box 39
Vienna, VA 22183

Attention: Section 312 Regulations

Dear Sir or Madam:

Mellon Financial Corporation, Pittsburgh, Pennsylvania ("Mellon"), welcomes this opportunity to comment on the proposed regulation to implement Section 312 of the USA PATRIOT Act of 2001 ("Patriot Act") regarding due diligence for foreign correspondent and private banking accounts. Mellon wishes to reiterate its strong support for the federal government's goal of implementing measures making it easier to prevent, detect and prosecute international money laundering and the financing of terrorism. As outlined below, Mellon submits that covered financial institutions could more readily facilitate the achievement of this laudable goal if the proposed section 312 regulation were narrowly tailored to focus on areas with the greatest potential for money laundering and terrorist activity. In addition, Mellon believes that the federal government should take an active role in compiling and sharing with covered financial institutions certain information that they need to meet their obligations under Section 312.

1. Definition of "correspondent account"

FinCEN proposes to define a "correspondent account" as "an account established to receive deposits from, make payments on behalf of a foreign financial institution, or handle other financial transactions related to such institution." This definition is more comprehensive than the definition proposed by Treasury in connection with Sections 313 and 319(b) of the Patriot Act, because it applies to accounts maintained by any covered financial institution (not just depository institutions and securities broker-dealers) and to accounts maintained for any foreign financial institution (not just foreign banks). Mellon wishes to echo the comments that it raised in connection with the Section 313/319 proposal regarding the overbreadth of such a definition. Mellon submits that a broad definition is likely to unnecessarily divert law enforcement and financial institution resources to account relationships that pose little or no money laundering or terrorist risk and away from those that pose a more significant risk.

As an alternative, Mellon strongly urges FinCEN to adopt the New York Clearing House Association definition of a correspondent account, which is "a deposit account established by a Respondent Bank to receive deposits, to make payments, or to otherwise disburse funds." This definition is preferable because it more clearly reflects that correspondent banking relationships are covered by the Section 312 requirements only if they involve a deposit account with the covered financial institution. This is a known, workable standard that removes the ambiguity inherent in the proposed definition about whether and to what extent a financial transaction with a covered financial institution that does not involve a deposit account with that institution will nevertheless be deemed a correspondent account. This framework would not increase the risk of unchecked money laundering and terrorist financing because financial transactions will still be subject to due diligence at the point where the financial transaction reaches a deposit account with a covered financial institution. To require covered financial institutions to apply the Section 312 due diligence requirements beyond these true account relationships would be unwieldy and costly and an unnecessary diversion of resources.

In addition to clarifying that only financial transactions that involve deposit accounts with covered financial institutions can be considered correspondent accounts, FinCEN should also explicitly recognize that not all deposit accounts with covered financial institutions should be considered correspondent accounts subject to the Section 312 due diligence requirements. Certain accounts are less likely to present a risk of money laundering or terrorist financing and thus do not warrant the scrutiny contemplated by the regulation. For example, Mellon believes that mutual fund accounts for foreign financial institutions in which the foreign financial institution holds mutual fund shares for its own account on a principal basis should fall outside the Section 312 requirements.

2. Definition of "foreign financial institution"

Mellon similarly urges FinCEN to narrow the potentially overbroad reach of the term "foreign financial institution" and to assist covered financial institutions in identifying those institutions that are properly categorized as foreign financial institutions. Because "foreign financial institution" goes beyond foreign banks and includes non-bank entities engaged in such activities as check cashing, virtually any foreign institution could conceivably be a foreign financial institution. Moreover, what constitutes a foreign financial institution is a moving target. Because a foreign financial institution is defined as a person or entity organized under foreign law that would be subject to the anti-money laundering program requirement of Section 352 of the Patriot Act if it were organized under U.S. law, and because Treasury has announced that it will be extending the anti-money laundering program requirements of Section 352 to additional financial institutions over time, the definition of foreign financial institution would evolve over time. Under such a framework, in order to comply with the section 312 requirements, each time that the Section 352 definition is changed covered financial institutions would need to review their records and solicit additional information from their correspondents to identify whether additional accounts with foreign entities have been swept within their reach. This process would be extremely burdensome.

In order to facilitate compliance with the spirit of Section 312 without unduly burdening covered financial institutions Mellon requests FinCEN to consider two modifications to its

proposal. First, Mellon submits that the federal government is in a better position than individual financial institutions to develop and maintain a list of categories of foreign entities that should be considered "foreign financial institutions." By compiling such a list and making it available to covered financial institutions the federal government could greatly decrease the compliance burden of these institutions. Government-compiled lists should also be developed to allow covered financial institutions to identify specific offshore banks, banks located in blacklisted jurisdictions and financial institutions that have been the subject of any criminal action or a regulatory action relating to money laundering. As part of this latter list of specific institutions Mellon submits that FinCEN should incorporate the New York Clearing House list of "High Risk Respondent Banks" as this list is published, readily available, and respected in the industry. Second, Mellon believes that FinCEN should expressly recognize in its 312 regulation that covered institutions may comply with their section 312 obligations by having foreign entities complete and submit to the covered financial institution a certification form setting forth whether or not they are foreign financial institutions. In the absence of actual knowledge of, or willful blindness to, the falsity of statements contained in such certifications covered financial institutions should be allowed to rely on the information that they contain.

3. Enhanced due diligence for certain correspondent accounts

Mellon similarly urges FinCEN to narrow the range of foreign financial institutions that are subject to the enhanced due diligence requirements of the proposed section 312 regulation. Mellon supports the proposal by FinCEN to exclude from the enhanced due diligence requirements for correspondent accounts those accounts that are maintained for branches of offshore foreign banks found by the Federal Reserve to be subject to comprehensive supervision or regulation in the foreign jurisdiction. Mellon submits that the proposed regulation should go even further and extend the exclusion beyond branches of the foreign banks to subsidiaries of such foreign banks. Mellon also requests FinCEN to clarify that if a foreign bank is subject to comprehensive supervision or regulation in a foreign jurisdiction that is considered cooperative with international money laundering principles, then a covered financial institution need not subject any accounts of branches or subsidiaries of that institution to enhanced due diligence, even if those branches or subsidiaries are themselves physically located in non-cooperative jurisdictions. Excluding such branches and subsidiaries from the enhanced due diligence requirements would allow covered financial institutions to devote more of their resources to due diligence on accounts that are more vulnerable to money laundering or terrorist financing.

Another aspect of the enhanced due diligence provisions for correspondent accounts that FinCEN should modify is the requirement that covered financial institutions obtain and review documentation regarding a correspondent bank's anti-money laundering program and consider its effectiveness. First, a foreign bank, like a U.S. bank, is going to be very reluctant to share with an outsider internal corporate policies and procedures that it considers proprietary and confidential. Second, even if the covered financial institution is able to obtain documentation regarding the foreign bank's anti-money laundering program, it is unlikely to have enough other information about the foreign bank to determine whether that particular program is effective for that particular bank. A far less burdensome and ultimately more workable solution would be for FinCEN to promulgate a list of points that an effective money laundering program should

contain and then allow covered financial institutions to rely on certifications provided by foreign banks that their internal money laundering programs address these points.

4. Definition of "private banking account"

As currently drafted, the proposed definition of "private banking account" is both ambiguous and overbroad. The proposed definition provides that this term means an account or combination of accounts that "requires a minimum aggregate amount of funds or other assets of not less than $1,000,000." Mellon urges FinCEN to clarify two aspects of this proposal. First, FinCEN should make clear than an account is a private banking account only if the individual is required to have $1,000,000 with the covered financial institution. Thus, an institution that requires an individual to have a net worth or investable assets of at least $1,000,000 in order to have an account with the institution, but does not require the individual to place that $1,000,000 with the institution, would not be considered to offer private banking accounts. Second, Mellon urges FinCEN to clarify that an institution's accounts are not considered private banking accounts unless the individual is required to make an initial deposit of $1,000,000 to establish the banking relationship, and that an account does not become a private banking account simply because the customer at some point maintains a balance of at least $1,000,000 with a covered financial institution.

5. Definition of "non-U.S. person"

For those institutions that do require individuals to place at least $1,000,000 with a covered financial institution and thus offer private banking accounts, it will be quite difficult for the institutions to determine whether the accounts are maintained by or on behalf of a non-U.S. person. According to the proposal, a "non-U.S. person" means someone who is neither a U.S. citizen nor a lawful permanent resident. Determining whether an existing customer is a lawful permanent resident of the U.S. cannot easily be done on an automated basis. Moreover, even if an institution correctly identifies an individual as a lawful permanent resident, that status could subsequently change. As currently drafted, the regulation could be read to require covered financial institutions that offer private banking accounts to develop a mechanism for monitoring a customer's lawful residency status on an ongoing basis. Developing such a mechanism may be difficult, if not impossible. An alternative would be to require covered financial institutions to obtain certifications from individuals establishing new private banking accounts about whether or not they are non-U.S. persons. Institutions could continue to rely on those certifications unless and until they received actual notice that the certifications were no longer accurate.

6. Due diligence for private banking accounts

For those covered financial institutions that do offer private banking accounts, the requirement to ascertain the identity of all nominal holders and holders of beneficial ownership interests and information on their lines of business and source of wealth is extremely far-reaching, burdensome and in many cases unnecessarily intrusive. First, institutions will need to conduct a rather sophisticated analysis to determine the list of individuals for whom the due diligence is required. For existing accounts, this could be a time-consuming process that would extend beyond the mandatory compliance date for the regulation. In the absence of additional

guidance from FinCEN regarding the reach of "noncontigent legal entitlement," covered financial institutions will experience difficulties identifying those beneficial owners who are covered by the due diligence requirements. Second, individuals who are merely beneficiaries of private banking accounts and are not themselves placing funds with the covered financial institution are likely to rebuff inquiries about their lines of business and sources of wealth and refuse to supply the requested information. FinCEN should clarify that institutions are not required to close private banking accounts based solely on a beneficiary's failure to supply the requested information. Third, the requirement to perform due diligence on holders of certain beneficial ownership interests is problematic because the value of an owner's interest can vary from day to day as the value of the underlying account varies. Institutions should not be required to monitor individual ownership interests on a contractual basis to determine whether and when a particular interest reaches the regulatory threshold.

The proposed regulation also requires covered financial institutions to ascertain the source of funds deposited into the private banking account. However, FinCEN has not clearly indicated what this requirement entails. For example, if an individual opens an account with bank X with a check drawn on that individual's account at bank Y, is it sufficient for bank X to note that fact? Or must bank X inquire further to determine how the individual came to possess the funds on deposit in bank Y? Is bank X required to conduct this analysis for each and every deposit that the customer makes into his private banking account with bank X? Or is bank X required to inquire in some general way about the individual's source of funds? If so, the "source of wealth" requirement overlaps the "source of funds" requirement. If not, and if the institution is required to analyze and document the source of funds for each deposit, the compliance burden will be overwhelming.

The proposed regulation requires covered financial institutions to include in their due diligence program reasonable steps to ascertain whether any accountholder or beneficial owner is a senior foreign political figure. FinCEN has suggested that these reasonable steps should include searching publicly available information, such as information on the Internet. Mellon respectfully submits that it is unreasonable and inefficient to create a regulatory framework in which each covered financial institution is required to search all information available by Internet to determine who is a senior political figure and whether the institution maintains any accounts for any such individual. Information on the Internet is available in hundreds of languages; under the proposed regulation each covered financial institution is arguably charged with knowledge of all information accessible over the Internet, regardless of the language in which the information is written. It is unreasonable to charge institutions with this knowledge. In addition, while information on the Internet is publicly available, it is not necessarily accurate, reliable or current. Covered financial institutions would not only have to spend time and effort locating this information, they would have to devote significant resources to evaluating the quality of the information. As an alternative, Mellon urges FinCEN to adopt a two-pronged approach. First, FinCEN should make the enhanced due diligence requirements applicable only if the customer is a citizen of a non-FATF (Financial Action Task Force) member country. Second, covered financial institutions should be permitted to rely on a certification provided by a citizen of a non-FATF member country that he is not a senior foreign political figure of that country unless the institution has received information to the contrary.

7. Extended Compliance Date

Under the Patriot Act, the provisions of Section 312 take effect on July 23, 2002 and apply to all covered accounts, including those established before that date. However, because interested parties have until July 1, 2002 to submit comments on the proposed regulation implementing the Section 312 requirements, a final regulation will not be published sufficiently far in advance of the statutory effective date to allow covered financial institutions adequate time to adopt or revise policies, procedures and controls that conform to the requirements of the regulation. Moreover, because the final regulation may differ significantly from the proposed regulation, covered financial institutions cannot finalize their policies, procedures and controls in advance of publication of the final regulation. In order to allow covered financial institutions sufficient time to put appropriate due diligence measures into place, Mellon respectfully requests FinCEN to extend the compliance date beyond July 23, 2002.

* * *

Once again, Mellon is appreciative of the opportunity to submit these comments. If you have any questions, please feel free to contact me at 412-234-1537 or, in my absence, Moira Hogan Murphy at 215-553-2363.

Respectfully submitted,

Michael E. Bleier
General Counsel

cc: Moira H. Murphy
George J. Orsino
Frank J. Riccardi

section312.doc