



October 3, 2014

Policy Division
Financial Crimes Enforcement Network
P.O. Box 39
Vienna, VA 22183

Re: Notice of Proposed Rulemaking – Customer Due Diligence
Requirements for Financial Institutions (RIN 1506-AB-25)

Dear Sir or Madam:

The Clearing House Association, L.L.C. (“**The Clearing House**”)¹ is pleased to comment on FinCEN’s proposal to adopt rules under the Bank Secrecy Act (“**BSA**”) to specify customer due diligence (“**CDD**”) requirements for banks and other financial institutions (the “**Proposed Rule**”).² FinCEN’s purpose in specifying these requirements is to “clarify and strengthen” CCD requirements within the BSA regime. In addition to codifying existing CDD requirements the Proposed Rule would create a new requirement to identify beneficial owners of legal entity customers, subject to certain exemptions.

The Proposed Rule follows an advanced notice of proposed rulemaking that FinCEN issued in 2012 (the “**2012 ANPRM**”)³ on which The Clearing House commented.⁴ As a preliminary matter, we note our strong support for the significant improvements FinCEN has made in the Proposed Rule and which we discuss in detail in this letter. At the same time, however, there are a number of aspects of the Proposed Rule that could be improved or clarified. We offer our comments in that spirit.

¹ Established in 1853, The Clearing House is the oldest banking association and payments company in the United States. It is owned by the world’s largest commercial banks, which collectively hold more than half of all U.S. deposits and employ over one million people in the United States and more than two million people worldwide. The Clearing House Association L.L.C. is a nonpartisan advocacy organization that represents the interests of its owner banks by promoting and developing policies to support a safe, sound and competitive banking system. Its affiliate, The Clearing House Payments Company L.L.C., provides payment, clearing and settlement services to its member banks and other financial institutions. It clears almost \$2 trillion each day, representing nearly half of all automated clearing-house, funds transfer and check-image payments made in the United States. See The Clearing House’s web page at www.theclearinghouse.org.

² 79 Fed. Reg. 45,151 (August 4, 2014).

³ 77 Fed. Reg. 13,046 (March 5, 2012).

⁴ Comment letter of The Clearing House Association L.L.C. on RIN 1506-AB15 (Jun. 11, 2012).

In particular we suggest that FinCEN:

- **Revise language in the Proposed Rule that significantly undermines the clarity and consistency of the regulatory CDD framework by suggesting that federal functional regulators have the ultimate authority to determine CDD standards in practice;**
- **With respect to existing customers, adopt an approach consistent with the 2003 implementation of CIP requirements such that financial institutions will not be required to re-identify beneficial owners, provided financial institutions have a reasonable belief that they have previously identified the current beneficial owners;**
- **Expressly allow financial institutions to collect beneficial ownership information through means other than the model certification form;**
- **Allow financial institutions to use a risk-based approach to determine (i) when it is necessary to verify the identity of beneficial owners and (ii) how such verification should be performed;**
- **Include in the list of entities that are excluded from the definition of legal entity customer (i) entities registered and licensed under foreign laws comparable to those enumerated in the Proposed Rule; (ii) registered bank holding companies, registered financial holding companies, and designated financial market utilities; and (iii) private trusts; and**
- **Explicitly incorporate in its final rule certain statements contained in the preamble to the Proposed Rule that articulate FinCEN's position on a number of important compliance matters.⁵**

DISCUSSION

1. ***As the entity delegated by the Secretary of the Treasury to implement, administer, and enforce compliance with the BSA FinCEN should exercise its statutory authority over CDD requirements to ensure that "financial institutions, regulators, and law enforcement all operate under the same set of clearly articulated principles."*⁶**

The Clearing House agrees with FinCEN's observation that codification of CDD requirements into FinCEN's regulations can serve to clarify expectations and ensure that "financial institutions, regulators, and law enforcement all operate under the same set of clearly

⁵ See Appendix 1 for a list of preamble statements that we request to be included in the final rule itself or as official commentary or notes to the final rule.

⁶ 79 Fed. Reg. at 45,155.

articulated principles.”⁷ This is a critical goal for the country’s BSA regime and one that The Clearing House strongly supports.

While we understand the need for FinCEN to coordinate with federal functional regulators in the exercise of its BSA authority, we are concerned that language in the Proposed Rule would grant greater deference than is appropriate to prudential regulators in setting expectations and interpreting CDD standards and requirements. For example, the Proposed Rule states “at the outset” that nothing in the Proposed Rule “is intended to lower, reduce, or limit the due diligence expectations of the federal functional regulators or in any way limit their existing regulatory discretion.”⁸ The Proposed Rule also states that “the CDD requirements proposed herein state *minimum* standards, existing or future guidance, regulations or supervisory expectations may provide for additional requirements or steps that should be taken to mitigate risk.”⁹ Similar statements are made in a number of places throughout the Proposed Rule.

We think it will be very difficult for banks and other financial institutions to rely on the Proposed Rule’s CDD requirements as definitive industry standards when FinCEN has given unqualified deference to the federal functional regulators to determine CDD standards in practice. As we noted in our comment letter on the 2012 ANPRM, The Clearing House strongly supports rules that would provide both institutions and their regulators a clear understanding of financial institutions’ compliance responsibilities. Unfortunately, because the Proposed Rule contains language that blurs the responsibilities of FinCEN and the federal functional regulators with respect to determining financial institutions’ compliance standards and purports to defer to all “existing or future guidance, regulations or supervisory expectations,” issued by the federal functional regulators, we are concerned that the Proposed Rule may undermine, rather than support, a clear, consistent, and shared understanding of CDD requirements.

Recent trends in the anti-money laundering (“AML”) regulation and enforcement environment demonstrate the need for all stakeholders to reach a shared understanding of what is required by law. First, as FinCEN is aware, significant uncertainty can result where (i) different regulators appear to apply different standards under the same legal requirement, and (ii) regulatory expectations with respect to such standards may change without a change in the underlying statutory or regulatory requirements. Second, the large number of significant AML enforcement actions taken against banks in recent years also requires all banks to carefully analyze, and frequently revise their practices, based on apparent changes in regulatory expectations that are reflected in those enforcement actions, the underlying facts of which are not publicly known. The sum result of these trends is an environment in which banks must design and implement AML compliance programs against the backdrop of inconsistent, uncertain, and evolving regulatory expectations. For this reason, it is critical that FinCEN establish CDD requirements that are clear and promote, rather than undermine, consistent application by financial institutions, FinCEN, and functional regulators.

⁷ *Id.* at 45,155.

⁸ *Id.* at 45,152.

⁹ *Id.* at 45,156.

We realize that there is a tension between the notion of clear, uniform CDD standards for the entire industry and the need for a risk-based approach to AML compliance. Different financial institutions and different products offered by those institutions, as well as the different customers served by those institutions, will inevitably present different risk profiles. Hence, we recognize that there will always be a need to exercise judgment in applying CDD standards to meet the risks that individual circumstances present. Nonetheless, without clear and consistent CDD standards, neither financial institutions nor regulators will have a common understanding of the core requirements that are to serve as the base for CDD standards.

As the Proposed Rule notes, the BSA places responsibility for determining the appropriate procedures for BSA compliance as well as the authority to examine financial institutions for compliance with the Act with the Secretary of the Treasury.¹⁰ The Secretary has delegated this responsibility to FinCEN. FinCEN in turn has further delegated examination authority for BSA compliance to the federal functional regulators. We emphasize, however, that such examination should be conducted under standards clearly set by FinCEN and not subject to interpretive discretion by the federal functional regulators.

We believe that clarity regarding CDD, which FinCEN has stated is a primary goal of the Proposed Rule, will remain elusive if the Proposed Rule serves only as a minimum standard that can be varied in any way and without limitation by the federal functional regulators. Therefore, we strongly urge FinCEN to remove language in the preamble to the Proposed Rule that significantly undermines the clarity and consistency of the regulatory CDD framework by suggesting that federal functional regulators determine the ultimate CDD standards in practice.

2. Existing CDD Standards

As in FinCEN's 2012 ANPRM, the Proposed Rule would incorporate three existing CDD requirements: (i) identifying and verifying the identity of customers; (ii) understanding the nature and purpose of customer relationships; and (iii) conducting ongoing monitoring to maintain and update customer information and to identify and report suspicious transactions.¹¹

A. Customer identification programs

The first existing CDD requirement that the Proposed Rule would adopt is "[i]dentifying and verifying the identity of customers." In the Proposed Rule, FinCEN makes clear that this requirement is identical to the current rules on identifying customers as set out in 31 C.F.R. § 1010.220.¹² We are gratified that FinCEN has improved the Proposed Rule with this clarification and strongly support this aspect of the Proposed Rule.

B. Nature and purpose of the customer relationship

The second existing CDD requirement that the Proposed Rule would adopt is "understanding the nature and purpose of customer relationships." On this point the Proposed

¹⁰ 31 U.S.C. § 5318(a).

¹¹ 79 Fed. Reg. at 45,152.

¹² *Id.* at 45,155.

Rule provides that each financial institution have an AML program that includes “[a]ppropriate risk-based procedures for conducting ongoing customer due diligence, to include, but not be limited to: (i) Understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile.”¹³

As we have noted previously, The Clearing House believes that financial institutions must have sufficient information about the customer and the account to be able to form a judgment about the customer’s AML risk profile and generally understand the nature and purpose of the account, which need not necessarily be specifically obtained from the customer and may be inherent in the nature of the product or service or the type of customer.¹⁴ In the preamble to the Proposed Rule, FinCEN expresses a similar view, noting that it

does not intend for this element to necessarily require modifications to existing practice or customer onboarding procedures, and does not expect financial institutions to ask each customer for a statement as to the nature and purpose of the relationship or to collect information not already collected pursuant to existing requirements.

. . . .

*FinCEN believes that in some circumstances an understanding of the nature and purpose of a customer relationship can also be developed by inherent or self-evident information about the product or customer type, or basic information about the customer. FinCEN recognizes that inherent information about a customer relationship, such as the type of customer, the type of account opened, or the service or product offered, may be sufficient to understand the nature and purpose of the relationship. . . . Each case depends on the facts and circumstances unique to the financial institution and its customers.*¹⁵

This language is consistent with our belief that banks may gain an understanding of the nature and purpose of customer relationships in a variety of ways, and we support FinCEN’s approach in this regard. We are concerned, however, that a final rule along the lines set out in proposed section 1020.210(b)(5)(i) may not be sufficient to alert supervisors to the flexibility that FinCEN clearly intends to provide to financial institutions in this regard. Accordingly we suggest that FinCEN publish a commentary or interpretative note to the rule formally incorporating the statements quoted above.¹⁶

C. On-going monitoring

With respect to the third existing CDD requirement, the Proposed Rule would require that a bank conduct “ongoing monitoring to maintain and update customer information and to

¹³ Proposed 31 C.F.R. § 1020.210(b)(5)(i).

¹⁴ Comment letter of The Clearing House Association L.L.C. on RIN 1506-AB15 (June 11, 2012).

¹⁵ 79 Fed. Reg. at 45,163.

¹⁶ See, e.g., Appendix E to 12 C.F.R. pt. 229 (the Federal Reserve Board’s commentary to its regulation implementing the Expedited Funds Availability Act).

identify and report suspicious transactions.”¹⁷ In its discussion of this requirement, FinCEN states that financial institutions would satisfy the requirement “by continuing their current monitoring practices, consistent with existing guidance and regulatory expectations,”¹⁸ and cites the BSA/AML Examination Manual as an example of existing guidance.¹⁹ FinCEN goes on to state that “monitoring is also a necessary element of detecting and reporting suspicious activities, and as such must apply not only to ‘customers’ for purposes of the CIP rules, but more broadly to all account relationships maintained by the covered financial institution.”²⁰

While The Clearing House agrees that financial institutions have a responsibility to detect and report the suspected use of their facilities for illicit purposes, FinCEN’s blanket statement extending the on-going monitoring requirement to “all account relationships” seems to imply a uniform requirement that is not necessary and may actually be detrimental to effective AML compliance because it would divert resources from the account relationships that pose the greatest risk of money laundering or other financial crimes. We therefore recommend that FinCEN expressly articulate that the requirement that banks and other financial institutions conduct on-going monitoring of customer accounts is a risk-based standard.

We also note that the intention of language in the preamble to the Proposed Rule that alludes to an expectation that financial institutions “should” update beneficial ownership information “in connection with ongoing monitoring”²¹ is unclear. We suggest that this language be revised to clarify that it is only with respect to the monitoring of a customer *relationship*, rather than transactions, that an event may trigger a financial institution’s need to update a customer’s beneficial ownership information. This is because we are unable to imagine a scenario in which transaction monitoring would alert a financial institution to a potential change in beneficial ownership.

3. Beneficial Ownership

The Proposed Rule would add a new CDD requirement that would require financial institutions to identify and verify the identity of natural persons who are the beneficial owners of certain legal entity customers. FinCEN appears to have given the comments on the 2012 ANPRM a great deal of thought and we are pleased that FinCEN made many improvements in the Proposed Rule. However, as discussed below, we believe further changes and clarifications are necessary to ensure that the new requirement can be practically implemented.

- A. *FinCEN should clarify that the requirement to identify beneficial owners is required on a per-customer basis and not a per-account basis and should not require financial institutions to re-identify beneficial owners for existing customers, provided financial institutions have a reasonable belief that they have identified such owners.*

¹⁷ Proposed 31 C.F.R. § 1020.210(b)(5)(ii).

¹⁸ 79 Fed. Reg. at 45,164.

¹⁹ *Id.* at 45,164 n.59.

²⁰ *Id.* at 45,164.

²¹ *Id.* at 45,162.

The Proposed Rule provides that “with respect to legal entity customers” a financial institution’s CDD program should enable it to identify the beneficial owners of each legal entity customer.²² The Proposed Rule defines legal entity customer as a corporation, limited liability company, partnership, or similar business entity that *opens a new account*.²³ FinCEN has defined legal entity customer in this manner so that financial institutions will not be required to identify beneficial owners of existing legal entity customers retroactively. As discussed in Section 3.F below, The Clearing House strongly agrees that financial institutions should not be required to identify the beneficial owners of all existing customers when the final rule becomes effective. However, we find that the definition of legal entity customer is problematic when applied to the identification requirement as the requirement becomes one to identify the beneficial owners of *an existing customer each time that same customer opens another account*. This would mean that even for legal entity customers whose beneficial owners have been previously identified, the opening of a new account would trigger a mandatory re-identification of the customer’s beneficial owners.

The preamble to the Proposed Rule suggests that FinCEN does not intend that an account opening will trigger a requirement to identify (or re-identify) beneficial ownership in all instances. Instead FinCEN states that with respect to a customer whose beneficial owners have been identified after the effective date of the final rule, it may be reasonable for a financial institution to rely on the existing certification when the customer opens a new account.²⁴ We believe that once a financial institution has identified the beneficial owners of a legal entity customer, whether identified as part of a financial institution’s CDD program that was in place prior to the final rule or as part of an updated CDD program after the final rule, the opening of a new account by that customer should not automatically trigger a requirement to re-identify the beneficial owners. Rather, a financial institution should be able to determine whether re-identification is necessary based on whether it has a reasonable belief that it has identified the customer’s current beneficial owners by ownership criteria at least as stringent as those required by the Proposed Rule (i.e., any 25% equity owners and one individual with significant responsibility to control, manage, or direct the customer).

We note that this approach would be consistent with the approach taken when the Treasury and federal functional regulators issued their joint customer identification program rules.²⁵ In the issuance of those rules the Treasury and regulators agreed with comments that imposing CIP requirements on existing customers, even when they open new accounts, “might have unintended consequences for bank customers.”²⁶ Hence, the definition of customer for purposes of CIP requirements expressly excludes “a person that has an existing account with the bank, provided the bank has a reasonable belief that it knows the true identity of the person.”²⁷

²² Proposed 31 C.F.R. § 1010.230(b)(1).

²³ Proposed 31 C.F.R. § 1010.230(d)(1).

²⁴ 79 Fed. Reg. at 45,159 n.31.

²⁵ 68 Fed. Reg. 25,090 (May 9, 2003).

²⁶ *Id.* at 25,095.

²⁷ 31 C.F.R. § 1020.100(c)(2)(iii).

Allowing financial institutions to rely on a previous identification of a customer's beneficial owners is also consistent with FATF Recommendation 10 (Customer Due Diligence). That recommendation states that financial institutions should be required to apply CDD measures (including the identification of beneficial owners) to existing customers "on the basis of risk and materiality." The interpretive note to Recommendation 10 regarding existing customers further provides that financial institutions should conduct due diligence (again, including identification of beneficial owners) "at appropriate times, taking into account whether CDD measures have been previously undertaken and the adequacy of data obtained."²⁸

For the reasons explained above, we urge that the definition of legal entity customer be revised to exclude an existing customer, provided that a financial institution has a reasonable belief that it has previously identified the customer's current beneficial owners using ownership criteria at least as stringent as provided in the definition of beneficial owner.

B. FinCEN should expressly allow financial institutions to collect beneficial ownership information through means other than the model certification form.

The Clearing House supports use of the model certification form as a means for financial institutions to identify beneficial owners. We think the certification will be a clear and practical means for many financial institutions to meet the new beneficial ownership identification requirement. However, we also think that some institutions will want to have an electronic version of the certification to allow for electronic account opening processes. We note that an on-line form could replace the signature line of the paper form with a box to be checked or a button to be clicked in a manner that is consistent with the Electronic Signatures in Global and National Commerce Act.²⁹ Hence, the final rule should allow for electronic equivalents of the form.

Further, some institutions that capture CDD information in electronic systems today or that choose to identify beneficial owners of certain legal entities using more stringent ownership criteria than the Proposed Rule will need the ability to collect such information in a manner that is consistent with their electronic systems or enhanced criteria. Such institutions should not have to use the certification form when they have other means to capture beneficial ownership information. Additionally, we are concerned that for U.S. financial institutions that provide services to legal entities in other countries, a mandate to use the form may become a hindrance to account opening if the form is duplicative of other CDD information that the institutions collect. Foreign financial institutions with which U.S. institutions compete for business will not face the same impediments in their account opening procedures. Accordingly we request that the certification form be treated as one of various means to comply with the requirement to identify beneficial owners.³⁰

²⁸ Interpretive Note H to FATF Recommendation 10.

²⁹ 15 U.S.C. § 7001 et seq.

³⁰ We recognize that the affirmative statement provided on the model form in which the signer certifies to the best of his or her knowledge that the information on the form is complete and correct will be helpful to law enforcement in circumstances in which there is a need to show an intent to provide false information to a financial institution. Nonetheless, we expect that financial institutions that use other

The Clearing House also requests guidance regarding FinCEN's requirement that financial institutions obtain the model certification form "directly from the individual opening the account."³¹ It is unclear who FinCEN would consider to be the person opening the account in situations in which a financial institution has direct interaction with a designee of a person with authority to open an account. For example, if a corporation's resolution authorizes its Treasurer to open accounts but a financial institution is directly interacting with a delegate of the Treasurer, would the delegate or the Treasurer be considered the individual opening the account?

Lastly, with respect to the model form we suggest that (i) the instructions for the model certification form state explicitly that if a legal entity is owned by another entity or is part of a more complex organization, equity owners may be individuals who own interests in other entities that are owners of the legal-entity customer and (ii) in the section that identifies the individual with significant responsibility for controlling, managing, or directing the customer, the control person's title should be included. FinCEN may also wish to consider placing on the form a statement that providing false statements to a financial institution may lead to legal penalties.

- C. FinCEN should broaden the list of entities excluded from the definition of legal entity customer to include entities that are (i) registered and licensed under foreign laws comparable to those enumerated in the Proposed Rule; (ii) registered bank holding companies, registered financial holding companies, and designated financial market utilities; and (iii) private trusts.*

Proposed section 1010.230(d)(2) contains a list of entities that are not included in the definition of legal entity customer and thus are not subject to the requirement for beneficial owner identification. This list is restricted to institutions that are covered by a specific U.S. law (e.g., "[a]n investment adviser, as defined in section 202(a)(11) of the Investment Advisers Act of 1940, that is registered with the Securities and Exchange Commission under that Act").³² This approach is very U.S.-centric—the customers must be subject to a specific provision of U.S. law or regulated by a U.S. regulator in order to be excluded from the beneficial ownership requirement. Covered financial institutions, however, often deal with non-U.S. clients—even in their U.S. offices. For example, a U.S. bank or a U.S. branch or agency of a foreign bank may hold an account for a major foreign corporation. If that corporation's shares were issued in the United States, the bank would not have to obtain beneficial owner information about the entity, whereas if the corporation's shares were not issued in the United States, the bank would be required to obtain such information.

Where a foreign entity is subject to a regulatory regime that is similar to the one that would govern a comparable U.S. entity, there should be no difference in treatment between

means to capture beneficial ownership information will be able to explain their information collection practices and assist law enforcement in demonstrating when a customer has provided false information to the institution.

³¹ 79 Fed. Reg. at 45,156.

³² Proposed 31 C.F.R. § 1010.230(d)(2)(v)

these entities. We therefore recommend that the list of excluded entities account for entities that are subject to comparable regulatory regimes, as determined by a financial institution.

In our 2012 comment letter, we also suggested a few exclusions that were not adopted in the Proposed Rule, namely registered bank holding companies and financial holding companies³³ and designated financial-market utilities.³⁴ We continue to believe that these entities are thoroughly regulated and fall into the same very low-risk class as the entities that the Proposed Rule excludes from the definition of legal entity customer. These entities are subject to a regime of supervision, regulation, and examination that is every bit as rigorous as banks are subject to, and we see no reason not to exclude them from this rule to the same extent that banks and similar regulated entities are excluded.

Additionally, we note that FinCEN has stated in the preamble of the Proposed Rule that the definition of legal entity customer does not include trusts other than those that might be created through a filing with a state, such as a statutory business trust.³⁵ The Clearing House supports the exclusion of private trusts from the definition of legal entity customer and refers FinCEN to the comment letter submitted by the American College of Trust and Estate Counsel for a thorough discussion of the practical difficulties of identifying equity owners of private trusts. We think that FinCEN's decision to exclude private trusts from the definition of legal entity customer should be codified in the final rule to ensure that there is no misunderstanding regarding the treatment of private trusts.

D. FinCEN should provide guidance for customers who must identify beneficial owners as to how indirect ownership interests should be calculated.

The Proposed Rule defines beneficial owner as:

- (1) Each individual, if any, who, directly or indirectly, through any contract, arrangement, understanding, relationship or otherwise, owns 25% or more of the equity interests of a legal entity customer; or
- (2) A single individual with significant responsibility to control, manage, or direct a legal entity customer, including
 - (i) An executive officer or senior manager (e.g., a Chief Executive Officer, Chief Financial Officer, Chief Operating Officer, Managing Member, General Partner, President, Vice President, or Treasurer); or
 - (ii) Any other individual who regularly performs similar functions.³⁶

³³ See 12 U.S.C. § 1841 et seq.

³⁴ See 12 U.S.C. § 5461 et seq.; see also 12 C.F.R. pt. 234.

³⁵ 79 Fed. Reg at 45,159.

³⁶ Proposed 31 C.F.R. § 1010.230(c).

FinCEN clarifies this definition by noting that the two prongs are intended to be used in tandem. A financial institution would ask the customer to identify each individual that owned 25% or more of the customer's equity. Depending on how many individuals met that standard, up to four individuals could be identified, but the result could be that no individuals would meet this standard, in which case no individuals would be listed. The bank would also ask the customer to identify one individual, such as the CEO or CFO, with significant authority to manage the company. There would always be a single person listed under this prong.

As to the first, or ownership prong, we believe that the proposed 25% ownership standard is appropriate. We understand that a number of other countries have adopted a 10% standard, and the Foreign Account Tax Compliance Act ("FATCA") also adopts a 10% standard.³⁷ Nonetheless, a 25% threshold is appropriate for the purposes of this regulation. Application of a less than 25% ownership standard to all non-exempt legal entity customers would be a significant burden on the customer on-boarding process for every bank—one that we believe is not necessary for the vast majority of customers. Moreover, as noted above, in a risk-based system, banks evaluate the risks of their legal-entity customers and may, if they deem appropriate, go beyond the minimum standard.

In addition, The Clearing House believes that FinCEN's proposed definition is clear except in one crucial respect, which is its reference to direct or indirect ownership of the customer's equity interests. FinCEN states that:

the phrase "directly or indirectly" in the ownership prong of the definition is intended to make clear that where a legal entity customer is owned by (or controlled through) one or more other legal entities, the proposed rule requires customers to look through those other legal entities to determine which natural persons own 25 percent or more of the equity interests of the legal entity customer.³⁸

In other words, where a customer is a subsidiary of another organization, FinCEN expects the individual who provides beneficial ownership information to a financial institution to identify any individuals who indirectly control 25% or more of the customer through their ownership of other entities that own 25% or more of the customer.

FinCEN recognizes that identifying these owners can be challenging in cases of complex corporate organizations,

but FinCEN does not expect financial institutions—or customers—to undergo complex and exhaustive analysis to determine with legal certainty whether an individual is a beneficial owner under the definition. Instead, FinCEN expects financial institutions to be able to rely generally on the representations of the customer when answering the financial institution's questions about the

³⁷ See 26 U.S.C. § 1473(2)(A).

³⁸ 79 Fed. Reg. at 45,158.

*individual persons behind the legal entity, including whether someone identified as a beneficial owner is in fact a beneficial owner under this definition.*³⁹

The Clearing House agrees with the expectation FinCEN articulates in this language and strongly suggests that it should be codified in a note or commentary to the final rule. However, we also believe that although FinCEN does not expect customers to undergo a complex and exhaustive analysis of indirect beneficial ownership, customers will nevertheless need some guidance as to how indirect ownership interests should be calculated within corporate groups. FinCEN should therefore provide examples or instructions that explain how ownership interests are calculated when natural persons have indirect equity interests in a legal entity customer.

We also note that FinCEN should clarify that when a legal entity customer has a 25% or greater equity owner that itself is an entity that is excluded from the definition of legal entity customer, there is no requirement to look through the exempted entity to identify individual owners. For example, if a legal entity customer has a 50% owner that is a registered investment company, as defined in the Investment Company Act of 1940, our understanding is that there would be no requirement to identify any individuals who own a sufficient interest in the investment company to be a 25% owner of the legal entity customer since there would be no requirement to identify the beneficial owners of the investment company itself if it were the customer.

Regarding the second, or senior officer, prong, FinCEN should clarify that just as financial institutions can rely upon a customer's identification of equity owners, financial institutions can also rely upon the customer's identification of an individual with significant responsibility to control, manage, or direct the customer.

Lastly, we request guidance as to how the new CDD beneficial ownership requirement relates to the existing requirement under 31 C.F.R. § 1010.620 that banks identify the beneficial owners of private banking accounts.

E. The requirement to verify the identity of beneficial owners should be risk based.

The Proposed Rule provides that institutions must verify the identity of each beneficial owner, according to risk-based procedures to the extent reasonable and practicable and that such procedures must be identical to the covered financial institution's Customer Identification Program (CIP) procedures required for verifying the identity of customers that are individuals.

We are grateful that FinCEN has limited the verification requirement to the *identity* of the beneficial owner rather than that person's *status* as an owner.⁴⁰ For the reasons set out in our 2012 comment letter, we strongly agree with this approach. However, we believe that identification in the context of beneficial ownership has a different purpose than in the context of CIP and, thus, should not be required in all instances or when undertaken should not have to be done in a manner identical to a financial institution's CIP procedures.

³⁹ *Id.*

⁴⁰ *Id.* at 45,162.

In particular, we note that CIP applies to individuals who are account holders with a financial institution and with whom the financial institution has direct communication. In contrast, the beneficial owners of a legal entity customer are not themselves account holders by virtue of their ownership or control of the entity. While we recognize that there will be circumstances under which a financial institution will need to verify the identity of a beneficial owner, such circumstances should be determined on a risk-based basis rather than required for all beneficial owners.

Moreover, a financial institution may have no means of directly contacting beneficial owners. Hence, to require financial institutions to verify the identity of all beneficial owners in a manner *identical* to CIP is likely to result in financial institutions closing accounts, including low risk accounts such as credit cards, mortgages, and equipment financing, for no reason other than an inability to meet CIP level requirements for non-account holding individuals with which they have no relationship or direct means of contact. For example, some financial institutions may have CIP procedures that only allow them to accept photo identification if the person identified is physically present. In the case of a beneficial owner who lives far away from a financial institution's offices, it may not be possible for the individual to personally present their photo identification to the financial institution. We further note that for U.S. institutions competing with foreign institutions for business with foreign legal entities, a strict CIP requirement for foreign beneficial owners may create a material disadvantage for U.S. institutions as the CIP requirements are likely to be quite cumbersome to carry out in this context.

For these reasons we recommend that the requirement to verify the identity of beneficial owners be limited to circumstances in which a financial institution has determined, based on its risk assessment of the legal entity customer, that verification is necessary. Further, when a financial institution determines that identification is necessary, it should have discretion as to the procedures it will use for such identification, again based on its own risk determination.

F. We strongly support FinCEN's proposal to not require identification of beneficial owners on a "look back" basis for existing accounts.

In the Preamble to the Proposed Rule, FinCEN notes that in response to comments it received in response to the 2012 ANPRM, it is "not proposing a prescriptive rule requiring financial institutions to look back and obtain beneficial ownership information for pre-existing accounts."⁴¹

While some commenters to the 2012 ANPRM expressed fear that failure to bring existing accounts under the rule will create a huge gap in coverage, we believe that this concern is misplaced. In the first place, banks will typically use the initial information obtained under the CIP to do a risk assessment of the customer. Customers that the bank views as higher risk will normally be subjected to additional levels of due diligence, which may involve obtaining beneficial-owner information. Moreover, banks typically seek to refresh information about accountholders when certain events trigger a review. For example, when a customer applies for a new service, such as a loan or line of credit, the bank will confirm the information on the

⁴¹ *Id.* at 45,160.

account and initiate additional due diligence, if warranted. Thus, customers that really do present greater risk of money laundering or other financial crimes will be given greater scrutiny—which will often include obtaining information on beneficial owners.

The Clearing House believes that requiring financial institutions to obtain beneficial ownership information on all existing accounts would impose a significant burden on all financial institutions while providing little incremental benefit. In the first place, this requirement would require large financial institutions to obtain information on millions of accounts, few of which have any risk of illicit finance thereby limiting institutions' ability to concentrate on accounts that really present risk. Also, customers may not be inclined to respond to their financial institution's inquiries regarding beneficial ownership.⁴² Unresponsive customers may be at risk of having their accounts closed simply because they are ignoring communications from their financial institution. We think this would be a very negative and unnecessary result for customers and their financial institutions. Hence, we strongly support FinCEN's proposal that there be no requirement to "look back" and obtain beneficial ownership information for existing customers.

G. Issues regarding certain kinds of legal-entity customer

Non-exempt Pooled Investment Vehicles. FinCEN has stated in the preamble to the Proposed Rule that it is considering limiting the beneficial ownership requirement for non-exempt pooled investment vehicles so that a financial institution would only be required to identify individuals under the "control" prong of the definition of beneficial ownership and not the ownership prong.⁴³ The Clearing House supports this approach and believes it would be extremely difficult to identify equity owners of such customers.

Syndicated Loans. The Clearing House notes that in the case of syndicated loans, which are loans made by a group of financial institutions and administered by a common agent, it may be difficult for each financial institution to separately collect the model certification form directly from the borrower because standard practice in this industry dictates that only the agent has direct contact with the borrower. The Clearing House suggests that in these circumstances FinCEN allow the agent to obtain the model certification form, or otherwise obtain the requisite information pursuant to one of the alternatives discussed above, and provide copies of the model certification form, or such other information, to the other financial institutions, and that this would enable them to meet their beneficial ownership requirement. We note that this model, in which the agent is responsible for obtaining necessary documentation from a borrower and then providing copies of the documentation to the non-agent financial institutions, is consistent with how syndicated loans are arranged today. Hence, this would be

⁴² We note that even under existing CIPs in which financial institutions are only required to seek information from a single person who is an account holder (rather than potentially five non-account holders under the Proposed Rule), multiple communications by phone, mail, or email may be needed before the individual responds with the information requested. Further, in a small percentage of cases, individuals never respond and accounts are closed. It is likely that if financial institutions were forced to engage in a "look back" exercise the non-response rate would be similar, if not higher, putting many existing accounts at risk of closure.

⁴³ 79 Fed. Reg. at 45,161.

the most efficient way for financial institutions to meet their beneficial ownership requirements for syndicated loan customers.

4. Timing and Effective Date

FinCEN has proposed an effective date of one year from the time that the final rule becomes effective to allow banks to make the required changes, including modifying existing customer on-boarding processes.⁴⁴

The Clearing House believes that 12 months will not be a sufficient amount of time to make the modifications to their operations. Financial institutions cannot begin to plan their compliance efforts until the Proposed Rule is finalized. Information technology budgets for the coming year are usually set in the third quarter of the current year, so if the rule is finalized during the last half of the year, implementing the IT changes necessary to comply with the new rule in the next year will be extremely difficult, and may require deferment of needed upgrades to other systems. IT changes represent only one facet of the compliance effort. In addition, all personnel involved in the customer on-boarding process will have to be educated in the new rules and in the processes necessary to implement them at the bank. Because financial institutions do not know what the final requirements of the rule will be, they cannot begin to plan their compliance efforts. For all these reasons, we believe that FinCEN should provide for at least 24 months between the date that the final rule is published in the Federal Register and its effective date.

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The Clearing House appreciates the opportunity to provide these comments on the Proposed Rule. If you have any questions, please contact Alaina M. Gimbert at alaina.gimbert@theclearinghouse.org or (336) 769-5302 or Joseph R. Alexander at joe.alexander@theclearinghouse.org or (212) 612-9234.

Very truly yours,



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⁴⁴ *Id.* at 45,164.

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Appendix 1

The Clearing House suggests that the guidance from the preamble to the Proposed Rule that is set forth below be included explicitly in the final rule.

Guidance from Preamble	Citation
“. . . FinCEN expects financial institutions to be able to rely generally on the representations of the customer when answering the financial institution’s questions about the individual persons behind the legal entity, including whether someone identified as a beneficial owner is in fact a beneficial owner under this definition.”	79 Fed. Reg. 45, 158
Legal Entity Customer “does not include trusts other than those that might be created through a filing with a state (e.g. statutory business trusts).”	79 Fed. Reg. 45, 159
“FinCEN intends for this amendment [understanding the nature and purpose of customer relationship] to be consistent with existing rules and related guidance.”	79 Fed. Reg. 45, 163
“FinCEN recognizes that inherent information about a customer relationship, such as the type of customer, the type of account opened, or the service or product offered, may be sufficient to understand the nature and purpose of the relationship.”	79 Fed. Reg. 45, 163
“The fourth element of CDD requires financial institutions to conduct ongoing monitoring for the purpose of maintaining and updating customer information and identifying and reporting suspicious activity. As with the third element, FinCEN intends for this element to be consistent with a financial institution’s current suspicious activity reporting and AML program requirements.”	79 Fed. Reg. 45, 163-164