



Department of the Treasury Financial Crimes Enforcement Network

Ruling

FIN-2008-R008

Issued: June 3, 2008

**Subject: Bank Secrecy Act Obligations of a U.S. Clearing Broker-Dealer
Establishing a Fully Disclosed Clearing Relationship with a Foreign
Financial Institution**

Dear []:

I am responding to your letter of April 15, 2008 to the Financial Crimes Enforcement Network (“FinCEN”), in which you seek an administrative ruling on the Bank Secrecy Act (“BSA”) obligations of a U.S. clearing broker-dealer (“clearing firm”) establishing a fully disclosed clearing relationship with a foreign financial institution (“foreign introducing firm”). Specifically, in this ruling we will clarify (1) whether a fully disclosed clearing agreement between a U.S. clearing firm and a foreign introducing firm is a correspondent account for the purposes of our regulations implementing section 312 of the USA PATRIOT Act (the “correspondent account rule”);¹ (2) whether a clearing firm is obligated to regard the fully disclosed accounts of a foreign introducing firm as its own accounts for the purposes of complying with the customer identification program regulations (the “CIP rule”);² and (3) whether we expect a clearing firm to obligate the foreign introducing firm to comply with the obligations of the CIP rule, the correspondent account rule, and other U.S. anti-money laundering regulations respecting any accounts it may introduce to the clearing firm on a fully disclosed basis.

As you have described, your client is a small [foreign] broker who has customers that wish to invest in securities traded in the United States. Your client, which is a foreign financial institution as that term is defined in the regulations implementing the BSA,³ has been in discussions with a U.S. clearing firm with the intention of establishing a clearing and carrying relationship. The clearing firm and your client contemplate that your client will introduce accounts to the clearing firm according to the terms of a fully disclosed clearing agreement under which your client, operating as a foreign introducing

¹ 31 C.F.R. § 103.176 (requiring a broker-dealer, among others, to establish and implement a due diligence program for the correspondent accounts it establishes, maintains, administers, or manages for foreign financial institutions, including foreign banks and foreign securities brokers).

² See 31 C.F.R. § 103.122 (rule obligating broker-dealers to establish and implement a customer identification program).

³ 31 C.F.R. § 103.175(h) (defining the term “foreign financial institution” to include, among other things, a foreign bank or a foreign broker-dealer).

firm, will be allocated the responsibilities of opening and approving new accounts and of receiving and accepting orders from the customers it will introduce to the clearing broker. The fully disclosed clearing agreement that the clearing firm has proposed would obligate your client to, among other things, implement customer identification and verification procedures and conduct other due diligence as if it were operating as a broker-dealer in the United States.

The correspondent account rule obligates a U.S. clearing firm, among others, to “establish a due diligence program [that is] reasonably designed to ... detect and report any known or suspected money laundering conducted through or involving any correspondent account established, maintained, administered, or managed ... for a foreign financial institution.”⁴ Whether a clearing firm has established or maintained a correspondent account with a foreign financial institution, thus obligating the clearing firm to comply with the provisions of the correspondent account rule, will depend on whether the clearing firm has established a “formal relationship” with the foreign financial institution.⁵

FinCEN previously clarified that the relationship between a clearing firm and a customer that has been introduced to it is not a formal relationship for the purposes of complying with the correspondent account rule when the customer is introduced to the clearing firm according to a fully disclosed clearing agreement under which an introducing firm, and not the clearing firm, is responsible for receiving and accepting orders for securities from the customer.⁶ FinCEN also recently stated that it will take no action against a clearing firm for not complying with the CIP rule with respect to a customer that has been introduced to it by an introducing firm when the functions of opening and approving customer accounts and directly receiving and accepting orders from the introduced customer are allocated exclusively to an introducing firm.⁷ This no-action position applies equally to a clearing firm’s fully disclosed clearing agreements with domestic and foreign introducing firms.

We do, however, view the relationship between a clearing firm and a foreign introducing firm such as your client to be a formal relationship, and therefore a correspondent account, for purposes of complying with the correspondent account rule, thus obligating the clearing firm to conduct due diligence on the foreign introducing firm

⁴ 31 C.F.R. § 103.176(a).

⁵ See 31 C.F.R. § 103.175(d)(2)(ii) (defining the terms “correspondent account” and “account” as a “formal relationship”).

⁶ *Application of the Regulations Requiring Special Due Diligence Programs for Certain Foreign Accounts to the Securities and Futures Industries*, FIN-2006-G009 at note 14 and accompanying text (May 10, 2006) (a clearing firm is not subject to the due diligence requirements of the correspondent account rule in circumstances where it has not established a relationship with an introduced account holder that would cause it to recommend securities or strategies to that account holder).

⁷ *Customer Identification Program Rule No-Action Position Respecting Broker-Dealers Operating Under Fully Disclosed Clearing Agreements According to Certain Functional Allocations*, FIN-2008-G002 (March 4, 2008).

itself.⁸ We additionally view the relationship between a clearing firm and a foreign introducing firm as an account for the purposes of complying with the CIP rule, thus obligating the clearing firm to verify the identity of the foreign introducing firm in order to form a reasonable belief that it knows the true identity of the foreign introducing firm.⁹

A clearing firm typically is not required to look through the fully disclosed clearing relationship to perform due diligence directly on the customers that may be introduced to it by a foreign introducing firm.¹⁰ Rather, the clearing firm is obligated to assess the money laundering risk presented by its fully disclosed clearing arrangement with the foreign introducing firm including, but not limited to, the risk factors enumerated in the correspondent account rule.¹¹

The clearing firm also is not required to obligate a foreign introducing firm to comply with the provisions of the CIP rule, the correspondent account rule, or any other U.S. anti-money laundering regulations respecting any accounts it may introduce to the clearing firm on a fully disclosed basis.¹² Instead, the clearing firm is obligated to apply risk-based policies, procedures, and controls to each correspondent account that are reasonably designed to detect and report known or suspected money laundering activity.¹³ The clearing firm is expected to monitor transactions conducted for introduced customers through the fully disclosed clearing agreement with the foreign introducing broker incorporating, among other information, any information the clearing firm acquires about the customers that are introduced by the foreign introducing firm in the ordinary course of its business.¹⁴

This ruling is provided in accordance with the procedures set forth at 31 C.F.R. § 103.81. In arriving at the conclusions in this letter, we have relied upon the accuracy and completeness of your representations. Nothing precludes us from reaching a

⁸ *Id* at 3.

⁹ See 31 C.F.R. § 103.122(a)(4)(ii) (foreign financial institutions are not excluded from the definition of the term “customer” in the CIP rule).

¹⁰ See *Anti-Money Laundering Programs; Special Due Diligence for Certain Foreign Accounts*, 71 Fed. Reg. 496, 503 (Jan. 4, 2006) (“the due diligence requirement ... generally requires an assessment of the money laundering risks presented by the foreign financial institution for which the correspondent account is maintained, and not for the customers of that institution”).

¹¹ See 31 C.F.R. § 103.176(a)(2) (the relevant risk factors include, among others, the nature of a foreign introducing firm’s business and the markets that it serves, the supervisory regime in which the foreign introducing firm is chartered or licensed to conduct business, and any information that is known or reasonably available about the foreign introducing firm’s anti-money laundering record).

¹² See *supra* note 11. As most foreign introducing firms already are subject to anti-money laundering regulations in their home jurisdictions, we instead expect a clearing firm to consider, when appropriate, the regulatory regime of that jurisdiction in assessing the money laundering risk of the foreign introducing firm.

¹³ 31 C.F.R. § 103.176(a)(3). See also 31 C.F.R. § 103.19 (obligation of broker-dealers to detect and report suspicious activity).

¹⁴ See FIN-2006-G009 at 3-4.

different conclusion or taking further action if circumstances change or any of that information provided is inaccurate or incomplete. We reserve the right, after redacting your name and address, to publish this letter as guidance to financial institutions in accordance with our regulations for requesting an administrative ruling.¹⁵ You have fourteen days from the date of this letter to identify any other information you believe should be redacted and the legal basis for redaction.

If you have any questions about this letter, please contact [FinCEN's regulatory helpline at (800) 949-2732].

Sincerely,

// signed //

Jamal El-Hindi
Associate Director
Regulatory Policy and Programs Division

¹⁵ 31 C.F.R. §§ 103.81-87.