

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

525 WEST MONROE STREET
SUITE 1100
CHICAGO, IL 60661
SEPTEMBER 28, 2012
9:00AM - 4:00PM

The Financial Crimes Enforcement Network (FinCEN) hosted a roundtable meeting to continue gathering information on the Advance Notice of Proposed Rulemaking (ANPRM) on customer due diligence (CDD) requirements for financial institutions. The meeting was held on September 28, 2012, at the Commodity Futures Trading Commission (CFTC), 525 West Monroe Street, Suite 1100, Chicago, IL 60661. To focus on specific industry issues, the meeting was divided into a morning session from 9:00 am to 12:00 pm for representatives from the futures industry, and an afternoon session from 1:00 pm to 4:00 pm for all other interested financial institutions.

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

This Chicago meeting was co-chaired by Chip Poncy, Director, Office of Strategic Policy for Terrorist Financing and Financial Crimes, U.S. Department of the Treasury and Alan Cox, Assistant Director, Office of Outreach Resources, FinCEN. Set forth below is a general summary of the primary issues discussed at the roundtable meeting, as understood by Treasury officials, in attendance. It is not intended to be a transcript, and does not purport to include every comment or issue raised during the meeting.

Summary of Roundtable Meeting

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

Definition of Beneficial Ownership

¹ Financial Crimes Enforcement Network, *Customer Due Diligence Requirements for Financial Institutions*, 77 FR 13046 (March 5, 2012), available at: <http://www.regulations.gov/#!docketDetail;D=FINCEN-2012-0001;ct=FR%252BPR%252BN%252BO%252BSR>.

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

- To address some confusion expressed by commenters in the earlier hearing sessions, Treasury officials clarified that the ANPRM definition of “beneficial owner” with respect to a legal entity customer includes both concepts of ownership and control. Including both concepts in the definition may be necessary to accommodate the vast array of complex ownership structures of legal entities that may become customers of financial institutions. The co-chairs asked participants to comment on the definition set forth in the ANPRM.
- Some commenters suggested that alternative sources may provide helpful guidance with respect to the definition of “beneficial owner,” such as the Glossary of the Financial Action Task Force (FATF) Recommendations.
- During a discussion about different thresholds associated with the definition of beneficial ownership, one commenter asked what the expectation would be when the ownership of an entity is so widely dispersed that no one natural person holds more than one percent. Treasury recognized that this is a key point to consider when contemplating how deep to delve into ownership.
- Treasury officials recognized how the various comments highlighted the challenge in proposing a definition that provides flexibility and consistency, but emphasized the need to achieve both.

Obtaining Beneficial Ownership Information – Current Practices

- Treasury officials asked participants to provide examples of the circumstances in which financial institutions currently obtain beneficial ownership information, and how financial institutions define “beneficial owner” in such circumstances.
- Commenters described widely divergent practices with respect to obtaining beneficial ownership information. For example, some institutions use a threshold of 10% for all customers, others use a higher threshold such as 25%, some obtain information on beneficial ownership only from certain high-risk customers, and others rarely obtain beneficial ownership information. The method of obtaining information on beneficial ownership also varied significantly across financial institutions. These variations were largely based on the type of financial institution, the type of customer and the type of product or service offered. Some institutions also base the threshold used to determine beneficial ownership on standards set in foreign jurisdictions, which have been subject to beneficial ownership obligations for several years.
- Commenters also described widely divergent practices with respect to updating information collected from the customer during the onboarding process. Some institutions do not refresh information, some do so upon a triggering event, and others may do so periodically (e.g., every five years for low-risk customers; every 3 years for medium-risk customers; and every year for high-risk customers).
- To determine control of legal entity customers, some institutions ask for and verify the identity of all directors and officers. Treasury contemplates that the control prong of the ANPRM definition will lead to the identification of only one or a limited number of individuals. Further, officers and directors of a legal entity may be beneficial owners in some instances, but that is not always the case. Treasury officials further clarified that the

ANPRM intended to distinguish between control of an account and control of a legal entity customer.

- In addition to obtaining beneficial ownership information to mitigate money laundering risk, some financial institutions also obtain beneficial ownership information to monitor and mitigate market exposure.

Verification of Beneficial Ownership – Identity and/or Status

- Treasury officials sought comments on a potential obligation for financial institutions to verify a beneficial owner's (i) identity and (ii) status as beneficial owner, as described in the ANPRM.
- For verifying the status of a beneficial owner (i.e., that the individual identified as a beneficial owner is in fact a beneficial owner), most commenters indicated that they should be permitted to rely on information provided by the customer. Treasury officials clarified that a rule on beneficial ownership could allow financial institutions to rely on information provided by customers in verifying status, but noted that conducting CIP on the beneficial owner may be an appropriate method in verifying the identity of the individual. Commenters generally acknowledged that conducting procedures similar to CIP on beneficial owners would be manageable as they are already familiar with the process.
- Some commenters suggested that a beneficial ownership requirement that permits reliance on a customer's self-certification (with no requirement for the financial institution to verify the status of the beneficial owner) could be workable as a broad-based approach.
- Other commenters, however, questioned the utility of a self-certification form as the information may be inaccurate or misleading. Treasury officials reiterated that an intentionally misleading customer response could have significant prosecutorial value, including for purposes of proving criminal intent.

Challenges Associated with Certain Products, Services, and Relationships

- Treasury officials sought comments on the challenges associated with obtaining beneficial ownership information in specific contexts. Several commenters reiterated that, due to their complexity, trusts should require separate treatment. Many financial institutions noted that they do not maintain an entire trust document. Generally, financial institutions retain the first and last page of the trust document. However, some financial institutions retain a certification document that may contain additional information. In certain circumstances, financial institutions do not have trust beneficiary information and thus exclude beneficiaries when obtaining information on beneficial ownership. Generally, financial institutions maintain trustee information on trust accounts, and might maintain grantor information.
- Treasury officials sought comment on the CDD challenges in specific contexts, including intermediated relationships and similar relationships where the customer is another financial institution that serves its own underlying customers. These relationships arise in

a number of different circumstances, such as correspondent banking or intermediated accounts that are common in the futures and securities industries. In these situations, the financial institution's customer is often another financial institution, which may be subject to varying degrees of AML regulation. Treasury officials recognized that these situations present unique diligence challenges.

- In this context, commenters discussed their due diligence practices with respect to foreign financial institutions (FFIs). As an example, some institutions assume that an affiliated FFI's AML controls are sufficient, and therefore focus mostly on the risk associated with the jurisdiction in which the affiliated FFI operates. Treasury officials acknowledged that jurisdictional risk is an important consideration, but emphasized it should not be the sole factor to consider.
- Treasury officials asked participants how they assess and mitigate jurisdictional risk. Some commenters noted that they conduct their own risk assessments, which may consider Financial Action Task Force ratings or European Union equivalence. To mitigate risk associated with non-affiliated FFIs, some institutions obtain the FFI's policies and procedures, and in some cases, request that the implementation of those procedures be externally audited.
- Several commenters, particularly those representing futures commission merchants and introducing brokers in commodities, emphasized that intermediated relationships pose unique due diligence challenges when a financial institution interacts with its intermediary customer only, and not that customer's underlying clients. According to these commenters, obtaining beneficial ownership information on such underlying clients would be particularly burdensome, and would result in a significant diversion of limited resources. These commenters from the futures industry, where intermediation is particularly common, also highlighted the importance of existing FinCEN guidance related to omnibus accounts and other intermediated relationships, and urged FinCEN to affirm such guidance and extend its application to the beneficial ownership requirement.
- Treasury officials also acknowledged the importance of existing FinCEN guidance with respect to CIP for omnibus accounts and other intermediated relationships, and acknowledged its potential relevance to a beneficial ownership requirement.³

Other Issues Pertaining to the Advance Notice of Public Rulemaking

- Commenters, particularly those that already collect beneficial ownership information, expressed concern that failing to apply a beneficial ownership requirement across all

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

relevant industries will create business competitiveness concerns whereby some institutions subject to the requirement risk losing customers to those institutions not covered. Treasury officials acknowledged this concern and emphasized that a primary purpose of a CDD program rule would be to clarify obligations in a manner that levels the playing field across and within financial sectors.

- With respect to pooled investment vehicles, several commenters from the futures industry indicated that ownership fluctuates too often to meaningfully identify a beneficial owner according to a percentage threshold. Accordingly, some financial institutions currently rely on representations from a fund's advisor or administrator that they conducted due diligence on the fund, including its investors. Treasury officials acknowledged the challenges associated with identifying a beneficial owner of a pooled investment vehicle.
- Some commenters asked Treasury to consider excluding existing accounts from the customer due diligence program rule as the costs associated with conducting a look-back on existing customers could be significant. Treasury officials noted that the ANPRM contemplates treating existing customers in a manner similar to their treatment under the CIP rules.
- Some commenters stated that they could not estimate the cost of compliance with a CDD program rule as it would depend on the specific proposals set forth in the notice of proposed rulemaking. Most commenters noted, however, that a self-certification form on which financial institutions could rely would significantly reduce costs and promote consistency across and within financial sectors.
- Commenters noted that financial institutions would need a significant amount of time to implement requirements relating to the collection of beneficial ownership information.

Conclusion

The co-chairs thanked all participants for attending and described the ongoing outreach process with respect to the ANPRM. In particular, Treasury intends to continue direct engagement with financial institutions, industry associations and other relevant stakeholders through regional and industry-specific outreach events. Treasury officials encouraged participants to continue to send comment letters to FinCEN on any of the issues discussed in the meeting.