

# IMPLEMENTATION OF FINCEN'S CUSTOMER DUE DILIGENCE RULE—REGULATOR PERSPECTIVE

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## HEARING BEFORE THE SUBCOMMITTEE ON TERRORISM AND ILLICIT FINANCE OF THE COMMITTEE ON FINANCIAL SERVICES U.S. HOUSE OF REPRESENTATIVES ONE HUNDRED FIFTEENTH CONGRESS SECOND SESSION

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## **IMPLEMENTATION OF FINCEN'S CUSTOMER DUE DILIGENCE RULE—REGULATOR PERSPECTIVE**

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**Wednesday, May 16, 2018**

U.S. HOUSE OF REPRESENTATIVES,  
SUBCOMMITTEE ON TERRORISM  
AND ILLICIT FINANCE  
COMMITTEE ON FINANCIAL SERVICES,  
*Washington, D.C.*

The subcommittee met, pursuant to notice, at 2:01 p.m., in room 2128, Rayburn House Office Building, Hon. Stevan Pearce [chairman of the subcommittee] presiding.

Present: Representatives Pearce, Pittenger, Rothfus, Tipton, Williams, Hill, Emmer, Zeldin, Davidson, Budd, Kustoff, Hensarling, Perlmutter, Maloney, Foster, Kildee, Sinema, Vargas, Gottheimer, Kihuen, and Lynch.

Chairman PEARCE. The subcommittee will come to order.

Without objection, the Chair is authorized to declare a recess of the subcommittee at any time. Members of the full committee who are not members of the Subcommittee on Terrorism and Illicit Finance may participate in today's hearing, and all members will have 5 legislative days within which to submit extraneous materials to the Chair for inclusion in the record. This hearing is entitled, "Implementation of FinCEN's Customer Due Diligence Rule—Regulator Perspective."

I now recognize myself for 3 minutes to give an opening statement.

I want to thank everyone for joining us today. Today's hearing will examine the implementation and enforcement of FinCEN's (Financial Crimes Enforcement Network) customer due diligence (CDD) rule, along with its compliance requirements for financial institutions. Last week, the customer due diligence rule went into effect, capping a 6-year effort by FinCEN to address shortcomings in our anti-money laundering (AML) and countering terrorist financing (CTF) regulatory regime.

I want to applaud FinCEN for their work in this area. As Chairman of the Terrorism and Illicit Finance Committee, I have heard testimony from a variety of experts in the field of detecting and pursuing criminals in the financial system. Many agree that a critical component of success in these investigations is law enforcement's timely access to beneficial ownership information of shell corporations being used to further criminal endeavors. The CDD rule requires covered entities, including banks, brokers, or dealers

of securities, mutual funds, and futures commission merchants to identify and verify any beneficial owner who, directly or indirectly, owns 25 percent or more of the equity interest in a legal entity, along with a single individual who exercises control over the legal entity at the time of account opening.

Although we agree on the importance of this information, there are legitimate concerns about the application of this new rule and the impact it will have on financial institutions. As the GAO reported in February, banks in the southwest border regions are derisking specifically because of concerns with BSA compliance. Adding additional requirements will likely increase this occurrence and cut business off from the financial system. Outstanding questions also remain for institutions that are working to ensure compliance with the CDD rule, including what an appropriate risk-based approach to collection entails. I look forward to the Director's opinion on these issues.

Today's hearing is an opportunity to discuss the implementation and enforcement of FinCEN's CDD rule and the impact it will have on our financial institutions. I hope our members will take this opportunity to learn from our witness about the benefits of collecting beneficial ownership information and how FinCEN plans to work with bank examiners and financial institutions to implement and appropriately enforce the CDD rule.

I would also like to thank Director Blanco for being here today. I look forward to his expert testimony.

The Chair now recognizes Mr. Perlmutter for 2 minutes.

Mr. PERLMUTTER. Thanks, Mr. Chair.

Mr. Blanco, thank you for being here. Thank you for your service.

The lack of transparency in our financial system has created an environment where criminals who should be shut out of the financial system can use anonymous shell companies to launder money, finance terrorism, and engage in other illegal activities.

In the last few years, high-profile leaks, such as the Panama Papers and Paradise Papers, have highlighted this tactic and the need for Congress and agencies to address beneficial ownership and financial transparency. FinCEN's customer due diligence rule seeks to take an important step in requiring beneficial ownership information and preventing criminals from hiding from law enforcement through anonymity. I look forward to your testimony on the implementation of this new rule and our discussion about how FinCEN and this subcommittee can continue to improve our anti-money laundering system and reduce illicit finance.

Obviously, some of the banking institutions that we hear from, from time to time feel that this puts a little additional burden upon them, and we have had complaints about that. But I think, from a law enforcement point of view, the need to know who owns a particular entity is very critical, and so we want to hear about the benefits and the burdens of this rule.

And I thank you today in advance for your testimony.

Chairman PEARCE. The Chair now recognizes Mr. Pittenger for 2 minutes for an opening statement.

Mr. PITTENGER. Thank you, Mr. Chairman and Ranking Member Perlmutter, for holding this hearing today.



I would also like to thank our distinguished panelist, Mr. Kenneth Blanco, for his testimony to our subcommittee this afternoon.

As the Director of the Financial Crimes Enforcement Network, commonly known as FinCEN, his division is responsible for the enforcement of the customer due diligence rule, which went into effect May 11th.

Last month, this committee's Subcommittee on Financial Institutions, of which I am also a member, heard from legal and issue-area experts on financial institution perspective.

I am looking forward to Mr. Blanco's testimony on the regulatory perspective and hearing his thoughts on how we can encourage information sharing while still providing banks clarity and not placing additional burdens on their customers.

Banks value legal compliance, but especially midsize banks value their customers' experience. We must ensure FinCEN is providing banks with adequate information to ensure their compliance, that there is no unintentional noncompliance.

Thank you, Mr. Chairman, and I yield back the balance of my time.

Chairman PEARCE. The gentleman yields back.

Today, we welcome the testimony of Mr. Ken Blanco. He is the Director of the Financial Crimes Enforcement Network, FinCEN, in the U.S. Department of Treasury. Mr. Blanco joined FinCEN in 2017, after serving as the Acting Assistant Attorney General of the Criminal Division at the United States Department of Justice.

During his tenure with the Criminal Division, Mr. Blanco oversaw a number of its sections, including the Money Laundering and Asset Recovery Section, formerly the Asset Forfeiture and Money Laundering Section, the Narcotic and Dangerous Drug Section, the Organized Crime and Gang Section, the Childhood Exploitation Section. Mr. Blanco has supervised many of the Criminal Division's most significant national and international investigations into illicit finance, money laundering, Bank Secrecy Act, and sanctions violations, including the investigation of global financial institutions and money service businesses.

Mr. Blanco joined the Department of Justice almost two decades ago as an Assistant United States Attorney in the Southern District of Florida. Prior to joining the Department of Justice, Mr. Blanco began his career at the Miami-Dade State Attorney's Office, where he served in various sections, including the Organized Crime Section, Public Corruption Section, and the Major Narcotics Section. Mr. Blanco earned his J.D. from the Georgetown University Law Center, where he also currently teaches as an adjunct professor of law.

You will be recognized now for 5 minutes to give an oral presentation of your testimony.

Without objection, your written statement will be made part of the record.

Mr. Blanco, you are recognized for 5 minutes.

#### **STATEMENT OF KENNETH A. BLANCO**

Mr. BLANCO. Thank you, Chairman Pearce, Ranking Member Perlmutter, and members of the subcommittee. Thank you for inviting me to appear today on behalf of the Financial Crimes En-

forcement Network, FinCEN, to discuss our efforts to safeguard our Nation's financial system, by increasing transparency through the implementation of our customer due diligence, or CDD, rule. I have prepared a written statement that I would like to submit for the record, Chairman.

Prior to my appointment as the eighth Director of FinCEN just a few months ago, I had served for almost three decades as a prosecutor in both State and Federal offices and, for the last decade, at the highest levels of the Department of Justice. Over those three decades, I saw firsthand the importance and power of our financial system and the need to keep it safe and secure.

I appreciate the opportunity today to discuss how the CDD rule and its compliance requirements for financial institutions advances our mission of keeping our financial system secure, our Nation safe and prosperous, and our communities and families safe from harm.

The reach, speed, and accessibility of the U.S. financial system make it attractive to criminals, terrorists, state actors, and other bad actors. In response, we have developed and rigorously enforce one of the most effective AML/CFT regimes in the world. Nevertheless, as strong as our AML/CFT framework is, bad actors will continue to exploit its vulnerabilities to move their illicit proceeds undetected through legitimate financial channels in order to hide, foster, and expand the reach of their criminal and terrorist activities.

The misuse of legal entities to disguise illicit activities has been a key vulnerability in the U.S. financial system. This is not breaking news. Corporate structures have facilitated anonymous access to the financial system for criminal activities and terrorism. Transnational organized crime syndicates, rogue states, human traffickers, terrorists, and other bad actors have been able to establish shell companies and then open accounts in the names of those companies without ever having to reveal who ultimately stands to benefit, masking their identities, hiding in the shadows, and making it difficult for law enforcement to pursue investigative leads and for financial intelligence units like FinCEN to generate those leads in the first place, putting our Nation and our people at risk.

An open and transparent financial system in which we can identify the transactions and account owners is, therefore, essential to disrupting and dismantling criminal and terrorist networks that seek to exploit our system and do us harm.

For these reasons, FinCEN and the Department of Treasury have prioritized increasing transparency in corporate formation and have strengthened regulatory requirements regarding customer due diligence for legal entity customers when they open accounts at financial institutions.

FinCEN finalized a CDD rule on May 11, 2016. The CDD rule was the result of extensive and thoughtful engagement with industry and with other stakeholders, notice and comment, hearings and other discussions over many years about the benefits of the rule as well as its potential burdens.

The CDD rule clarifies and strengthens customer due diligence requirements for covered financial institutions by streamlining and standardizing existing regulatory requirements and adding a new requirement for these financial institutions to know and verify the

identities of the actual people who own, control, and profit from companies, also known as beneficial owners.

The CDD rule advances the purpose of the Bank Secrecy Act by making available to law enforcement vulnerable information needed to disrupt financial networks and other criminal organizations and terrorist networks. This, in turn, increases financial transparency and augments the ability of financial institutions and law enforcement to identify the assets and accounts of criminals and national security threats. It also facilitates compliance with sanctions programs and other measures to cut off financial flows to these bad actors.

I understand that this committee has been interested in the readiness of both industry and government regarding the CDD rule's implementation. To that end, I can report that FinCEN has been working collaboratively and regularly in ongoing discussions with our regulatory counterparts and industry to ensure a common understanding of consistent compliance standards within and across regulated industry sectors. This is especially important when we issue a new rule. We understand and we appreciate that there will be a period of fine-tuning for compliance industry, with the examination process itself, both of which will take time. And we know that new questions often emerge when implementation begins.

The purpose of the rule is to enhance AML/CFT, not to serve as a vehicle to punish financial institutions. We are committed to continue working with our partners, agencies, and industry to ensure that covered financial institutions are also implementing the rule effectively, in a way that makes practical sense, and we understand that it won't happen overnight. In the meantime, we encourage our financial institutions to alert their examiners and us and to share their issues and concerns.

Chairman Pearce, Ranking Member Perlmutter, I look forward to answering your questions. Thank you.

[The prepared statement of Mr. Blanco can be found on page 24 of the appendix.]

Chairman PEARCE. Thank you, sir.

I now recognize myself for 5 minutes for questions.

And so I guess one of the key things is if you have any information on the cost-benefit analysis. In other words, there are lots of speculation on how much this is going to cost our banking system. So do you have that information?

Mr. BLANCO. Chairman, I don't have the specifics as far as the numbers. We can get you those numbers with respect to the cost-benefit and how much that is going to cost.

I can just tell you, Chairman, through my experience of 29 years in law enforcement, the benefits are really important and critical to law enforcement, and I think very critical to the financial institutions in order for them to be able to do their due diligence as we move forward.

The information, I have only been at FinCEN for 4 months. I can tell you the information that we collect from the financial institutions and the way we use it is critically important for our mission.

Chairman PEARCE. OK. On the southwest where New Mexico lies, there are reports of how there is something like 80 percent of

the banks have chosen just to eliminate accounts for people who might draw too much attention, so derisking.

So how do you approach that problem when you are talking about this further requirement?

Mr. BLANCO. Chairman, I don't think this further requirement is going to exacerbate any of the derisking that is happening on the southwest border. What we plan on doing is talking with those banks and industry in that area to see if we can come up with any solutions to those issues that they are seeing.

I can tell you we have an outreach program at FinCEN that is very robust, where, in fact, this morning, I met with the Florida Bankers Association. So we are listening to their comments and understanding what they have, but I don't think that the CDD rule is going to do anything to further what is happening on the southwest border.

Chairman PEARCE. Now, there are people that are critics of this CDD rule, and then our attempt to quantify in law the same concept, who declare that the information is readily available right now, that the IRS has the information.

Did you look at other agencies, other less-intrusive ways if this is intrusive? Tell me a little bit about that.

Mr. BLANCO. I can tell you, Chairman, that with respect to the information that the IRS receives, that is very different information, and the way to get the information is much more difficult than what we are proposing.

Having been on the other side and being a prosecutor trying to get that information, you would have to get a court order to get the IRS information, first of all, which takes time, and it defeats the purpose of your AML risk assessment.

In addition, the information that is contained in the IRS records are very different. It is not as specific as the information that we are looking for. It is a little different. It doesn't specifically go to equity owners, and it doesn't specifically go to what we have as a control prong for beneficial owners.

It is a very different standard, much more simple than what we are asking for. It doesn't really get to the point of who actually owns and who actually controls the entity that we are looking at.

Chairman PEARCE. That question of who actually has the say-so over the company is one that has drawn questions also. The language I think says that anyone who has significant input or whatever the language is. How are the banks to interpret who actually has that input? What guidance can you give them?

Mr. BLANCO. In the guidance that we have provided through the FAQs (frequently asked questions) that we provided, both a year ago and just recently, it is pretty clear that somebody who has some decisionmaking, whether it is in a control position, somebody who has a stake in the corporation as far as making decisions, that is really what we are looking for. Who maintains the actual control, or do they have a decisionmaking process within the company? That is what we are looking at.

And if you look at the IRS, what they ask for, it is somebody who has some responsibility, which is very different, and that is more of a mushy standard. We are looking for somebody who has control, makes decisions. That is what we are looking for.

Chairman PEARCE. Now, there have also been statements that this is going to be very onerous to the small businesses. Tell me a little bit about what you visualize the form looking like that the banks are going to get filled out.

Mr. BLANCO. Chairman, we have a form that is attached to our website that they can take a look at. I have a copy of it here. We are happy to give you a copy. It really is very simple, and it asks for very simple things.

It asks for, on the customer side, the name, legal entity, the address, ZIP Code, the name of the person who is the customer. Then it goes into who is the equity owner. Who are they? Is there anybody who has 25 percent? If so, you have to list who they are: Name, address, social security number if that exists, or foreign identification number if that exists as well.

They could also, if they wish, get a copy of the driver's license. It doesn't have to be the actual driver's license that they have to see; it could be a photocopy. And then it goes into the control prong, and that is an individual with significant responsibility for managing or directing the entity.

It is a very simple form. They don't have to use this form. Banks can use their own form, consistent with whatever software or products that they are using, as long as it has that information in it, four or five key points. That is all we are looking for. It is very simple.

Chairman PEARCE. My time has expired.

I would recognize the gentleman from Colorado, Mr. Perlmutter, for 5 minutes.

Mr. PERLMUTTER. Thanks, Director.

And I like terms like "mushy," so we will get to the mushy in a second. But, the debate for us is whether it is most of lower Manhattan coming down or the Murrah Building in Oklahoma City or some terrible act. We want to try to stop those things. And so the cost of those are enormous, if calculable at all. The costs of the compliance certainly are there.

Between the chairman, Mrs. Maloney, Mr. Hill, we have talked about secretaries of State. We have talked about the IRS. We have talked about the lawyers. We have talked about the bankers. Somebody has some responsibility to help you, as the head of FinCEN and the FBI and elsewhere, have good information that stops some terrible act that harms Americans.

So let's just go back to basics. How prolific, how often, in your experience as a law enforcement agent, have you seen shell companies come into play to hide bad actors?

Mr. BLANCO. All the time.

Mr. PERLMUTTER. So explain that.

Mr. BLANCO. It is not a secret, it really isn't. Even when I was a young prosecutor at the State's attorneys' offices and we were doing financial crimes, people would hide behind shell corporations all the time. Yes, eventually you might find out who owns it, maybe.

That time expended in trying to figure that out and the hoops that you have to jump through, by that time those criminals have already left and gone and either defrauded the elderly person who they were defrauding or committed whatever act they are going to

commit, transferred the drug money if they had it to transfer drug money, or took their human traffickers and already sold them into human trafficking. They are done.

What this does for us is, even if the information that is provided to us is false—let's just assume that, because I have heard that. People say, "Well, Ken, how are you going to get them to provide you truthful information? The fact that they are providing false information to us is a key indicator of who you are dealing with at that point. And it gives you a lead of how you should be investigating these people, and it is a red flag.

But let's just assume the information is correct, which I think much of it will be. It gives you leads. The time you are saving in doing your investigation is exponential. For example, a terrorist act, and many of you may understand this, we have a group that responds 24/7. They come into the FinCEN office. We run names. We run numbers. We run phone numbers. We run corporations.

Without the beneficial ownership information, it takes a lot more time. With that information, both at the time of the account being opened and, frankly, at the time the business is incorporated, it is going to be critical for us to respond. It is about stopping acts before they happen. And this critical information, which is very simple information, it really is, we are not asking for a lot here, very simple information that gives us a heads-up what is going on.

And the—I am sorry; I am talking a lot.

Mr. PERLMUTTER. So my question was: You talked about at the formation of the company. How often do you update this through your particular rule? Is it every month? Is it upon a loan renewal? Is it a change of somebody who signs the credit card? What is it?

Mr. BLANCO. So those are triggering events that would cause you then to update it. And that is, we have been having a lot of conversation with both industry, and we have been having a lot of conversation with law enforcement. And the way that we have left it with industry and law enforcement is that, through your normal AML program, whatever AML program you have, if you notice that there has been a change event, a triggering event, that is when you update it.

Triggering events could be all kinds of things. They could be an extensive money flow that all of a sudden appears in the bank account. That gives you indication something is different. A change in ownership, different name being used, a different account being opened, all those things that are common sense would cause us to update the beneficial ownership information.

Mr. PERLMUTTER. So just if I were the banker at that point and there is a new signer on the account, a signatory on the account, is that a triggering event? The question I have—and I think you are on the right track. I am not fighting with you on this.

And you used the word "fine-tuning," and that is what this is going to be, but, if I am that banker, every time that customer walks in the bank, is that a triggering event? And how often are you expecting stuff from these guys? Because it sounds like a lot.

Mr. BLANCO. Not every time a customer walks in the bank, I don't think that is a triggering event. But let's just say there is a new signatory on the account. Yes, I think that is a triggering event. That is a changed circumstance that you are going to want

to take a look into, and you may want to verify the beneficial ownership information.

And in our FAQs, we also said, look, you can also just update the information as long as you get an oral or verbal confirmation that the information is still correct except there is a different signator or a change event. It doesn't have to be a drastic event.

We are not looking for things that are very rogue. We just want people to think. What would cause them to want to update the beneficial ownership information? What makes sense? What is the triggering event?

Like you said, we are going to be working through this with industry and with law enforcement. We are not using this as a hammer on anybody. It is not a gotcha game. What we are trying to do is make sure that we have the right information.

Mr. PERLMUTTER. Thank you, and my time has expired.

Chairman PEARCE. The gentleman's time has expired.

The Chair would now recognize Mr. Pittenger for 5 minutes. And be advised that we just had a vote call. There are 14 minutes left in that. So we will take probably two more rounds of questions: Mr. Pittenger, and Mrs. Maloney I think would be the next. So we will try to get those in. Then we will take a recess for votes and return to the hearing.

So, Mr. Pittenger.

Mr. PITTENGER. Thank you, Mr. Chairman.

Thank you again, Mr. Blanco. It seems to me that the new CDD rule makes financial institutions weigh convenience and customer experience against cost of compliance. Do you think that is an accurate assessment?

Mr. BLANCO. I am sorry, sir. I—

Mr. PITTENGER. It makes the financial institutions weigh convenience and customer experience against cost of compliance. Do you believe that is a valid and accurate assessment?

Mr. BLANCO. Yes, one could assume that is a valid assessment. I think here, though, when we talk about cost weighed against a secure financial system, I am not so sure we are talking about cost.

I think what we are talking about is the financial system that is safe and secure, that everybody can benefit from, including the banks and including the customer. And the customer too also wants a secure financial system so that they can put their money in a place where they can invest and make sure that it is safe and secure.

So I know we talk a lot about costs, but I can just tell you what we are asking for is something very simple. I cannot imagine it costing too much.

Mr. PITTENGER. Yes, sir. Do you think, with that in mind, that some institutions will opt to derisk some customers due to the difficulty in understanding the CDD rule or complying with it?

Mr. BLANCO. I hope that does not happen. We are going to look for that. We take derisking very seriously. We believe people should have access to capital and access to the banking system, and we want to make sure that happens. May it happen? It might. And those are things that we are going to take a look at and make sure that those things do not happen for the wrong reasons. They

may derisk them for other reasons, but we want to make sure it isn't because of this.

Mr. PITTENGER. Sure. Mr. Blanco, it is my understanding that the CDD rule will only apply to new accounts opened after the effective date.

Mr. BLANCO. That is correct.

Mr. PITTENGER. If that is true, what happens to a financial institution if they fail to meet the new CDD rule requirements?

Mr. BLANCO. So we have spoken with our regulators, and we have spoken with institutions, our financial institutions, and we know there is going to be this time period where everybody is adjusting to it. And all we are asking for is that they have a good faith effort to comply with it.

We are not using it to ding anybody. We will work with them. We have fielded hundreds of questions since this came out in 2016, actually thousands of questions, and we are going to continue to do that. It is not a gotcha game.

Mr. PITTENGER. Yes, sir. With that in mind, would a financial institution be restricted with their customer accounts across the entire customer relationship or solely with respect to the new accounts opened after the implementation date?

Mr. BLANCO. I am sorry, sir. I am having trouble understanding.

Mr. PITTENGER. I understand. Would a financial institution be restricted with their customer accounts across their entire customer relationship or solely with respect to the new accounts opened after the implementation date?

Mr. BLANCO. If I understand your question correctly, you are talking about a customer across their entire relationship with the bank.

Mr. PITTENGER. Versus new accounts opened.

Mr. BLANCO. Once they start opening new accounts—and remember, what we are talking about here are legal entities that are opening new accounts.

What the financial institution will have to do is make sure that it corresponds correctly with the other information that they have on other accounts, yes.

Mr. PITTENGER. FinCEN released two sets of FAQs—one in 2016 and then one in the final days before implementation—to help bring clarity to the CDD ruling. However, these FAQs do not specify the extent to which a financial institution should integrate technology changes to the better use of information it obtains through CDD.

Is there any clear guidance on what to do with the information once it is gathered and how it should be used to enhance AML programs?

Mr. BLANCO. We can provide better guidance, Congressman. But I believe, in the FAQs themselves, they talk about where the information should be stored and how it should be used in the regular course of their AML/CFT risk assessment. That is something that they can use in the normal course of how they review their risk with respect to that one client.

Mr. PITTENGER. Then how would or should the information then be integrated into the transaction, monitoring, or sanctions compliance programs?



Mr. BLANCO. In the normal course, each of the institutions has their own procedures and policies that they use, and it should just be done with their normal policies.

Mr. PITTENGER. Thank you. I yield back.

Chairman PEARCE. The gentleman yields back.

The Chair will now recognize the gentlelady from New York, Mrs. Maloney, for 5 minutes.

Mrs. MALONEY. Thank you, Mr. Chairman and Mr. Ranking Member, for calling this hearing.

And thank you, Director Blanco. I have had a bill in on beneficial ownership at the request of law enforcement for quite some time. And I think that the customer due diligence rule is a huge step forward. I support it, but I also believe that the responsibility shouldn't be entirely on financial institutions. Banks should know their customers, but it shouldn't be this hard to figure out who their customers really are.

And law enforcement and banks have expressed to me that they are unable to figure out who these people are. That is why I have introduced a bill, the Corporate Transparency Act, that would require companies to disclose their beneficial owners at the time they are formed, and then financial institutions would have access—and law enforcement—to that beneficial ownership information, so that they can assure themselves that these companies that open accounts with them are not money launderers, sex traffickers, or other types of criminals. Under my bill, FinCEN would be in charge of collecting this beneficial ownership information.

And in your view, should companies be required to disclose their beneficial owners at the time they are formed?

Mr. BLANCO. Yes.

Mrs. MALONEY. And is FinCEN capable of maintaining a database of beneficial ownership information that would be available to law enforcement and financial institutions?

Mr. BLANCO. Congresswoman, if that is what ultimately happens, we have to keep in mind that we are going to have to be well resourced in order to do it. If you are asking me today if we are well resourced to do it, I would tell you it would be very difficult for us to pull that off.

If, in fact, the ultimate decision is going to be to have FinCEN house it, then we are going to have to be resourced to do it, but we can do it.

Mrs. MALONEY. Great. Do you think that a bill that would have FinCEN collecting beneficial ownership information and then allowing financial institutions to access that information from FinCEN would complement your customer due diligence rule?

Mr. BLANCO. I do.

Mrs. MALONEY. Great. And in 2016, FinCEN issued two geographical targeting orders (GTOs) covering Manhattan and Miami that required title insurers to collect beneficial ownership information for any legal entity making all-cash real estate transactions. And the findings from the first 6 months were just shocking. FinCEN found that about 30 percent of the transactions reported involved a beneficial owner or purchaser that had previously been the subject of a suspicious activity report (SAR), which is a shockingly high number and strongly suggests that criminals and

other bad actors are using anonymous shell companies to launder money.

FinCEN's GTOs were then extended last year and also expanded to include L.A., San Francisco, San Diego, and San Antonio.

So I have two quick questions: First, has the beneficial ownership information that you have collected after you renewed the program continued to be useful for FinCEN? Second, doesn't this suggest that one of the keys to cracking down on money laundering and terrorist financing, which is a top concern of New York, the city I represent, is requiring companies to disclose their beneficial owners at least to law enforcement?

Mr. BLANCO. The answer is yes to both.

Mrs. MALONEY. OK. Thank you very much, and I hope we didn't miss our votes. We have to run. Thank you.

Thank you, Mr. Chairman.

Chairman PEARCE. We have 6 minutes left. So the Chair now places the committee in recess until after the votes.

[Recess.]

Chairman PEARCE. The subcommittee will come to order.

We have a couple of members coming in for questions.

Until then, I would recognize myself.

So you talked about implications for bankers and that we are there to work together; you are just not after gotchas. What about the people who are filling out the forms, if they fill them out incorrectly on purpose? Tell me a little bit about the consequences.

Mr. BLANCO. That is a very good question, Congressman. That actually was a question that I asked myself. Of course, being a prosecutor, I want to know what the consequences are.

Right now, the consequences are there are no penalty provisions to the false information given. However, I think it really depends on what they say. They could be prosecuted for bank fraud, depending on what information they choose to lie about, and the consequences to the bank in which lying it. But right now the consequences are that they will be investigated probably, but there is no crime with respect to that, at least that I know of, no penalty provision with respect to the CDD rule.

Chairman PEARCE. So how do they come to the attention, how do we know that the banks are not gathering the latest information and that people are submitting bad or improper information?

Mr. BLANCO. I think two ways, Chairman. One way would be that the banks, through their normal due diligence, would discover that this information is false information.

It could be that the bank person who is actually doing the intake of the information will recognize the red flags.

And I think the third way to do it is that law enforcement themselves, when they run these names, realize that the information is incorrect. And right there, that is a red flag that perhaps this legal entity should be looked at or the individual opening the legal entity, the customer himself or herself should be looked at.

Chairman PEARCE. I would recognize the gentleman from Nevada, Mr. Gottheimer, for 5 minutes.

I would then recognize the gentleman from Ohio, Mr. Davidson, for 5 minutes.

Mr. DAVIDSON. Thank you, Chairman.

And I really appreciate your testimony today, Director, and I appreciate the opportunity to talk about some of the rulemaking there. A number of issues have been raised as banks have attempted to come into compliance with the consumer due diligence rule. And the frequently asked questions, that have been issued by FinCEN aiming to clarify the rule, have in some cases had the reverse effect of complicating and confusing its requirements.

For example, who should actually be listed as the beneficial owners that a bank might need to report. It is very clear when you say 25 percent or greater, but when, for example, significant influence. And from your previous testimony, perhaps every time a company updates their org chart, there might be a trigger to say, "Gee, we just hired a new plant manager at one of our facilities; do we have to update our org chart with FinCEN?" And then the premise is, that all the small businesses in America, many of the smallest, least sophisticated businesses of America are criminals if they don't keep these forms updated. So it seems the burden is heavily shifted to law-abiding citizens to somehow keep the government apprised of their privately held business, instead of on this organization that we created and asked you to lead to do the work to find this information out.

I guess, do you believe that some of the same, perhaps even some complicating factors may arise in terms of how beneficial owners should be reported? Do you think about the kinds of businesses that you are asking to comply with this admittedly simple-to-use form, but at what level in the org chart do I say this person isn't exercising significant influence over my business?

Mr. BLANCO. Congressman, what the form asks for is just one individual if we are talking about a control prong. We are only asking for one person. We are not asking for a litany of people who may have responsibility or control over the legal—

Mr. DAVIDSON. You just need the CEO?

Mr. BLANCO. You could. You could put the CEO. You could put the controller. You could put a senior manager. It has to have somebody who has decisionmaking and that is responsible for making decisions.

Mr. DAVIDSON. You just need a name. You don't need all the names; you just need a name.

Mr. BLANCO. You do not need all the names.

Mr. DAVIDSON. OK. So the other complicating factor is there are a number of folks that will have issues with the shift in bases, which is the default is, if a newly created business is established, the government collects a fair bit of information. And they don't necessarily collect all this in a way that would make it easy for FinCEN to access, but in a lot of ways it seems that it would be easier for us to lower the threshold for you to obtain this information than to criminalize every business in America unless they fill out this admittedly easy-to-fill-out form.

Mr. BLANCO. Congressman, we are not criminalizing these individuals. People are going to make mistakes. We get that. The question is, are they intentionally falsifying documents to avoid actually listing who the beneficial owners are?

Mr. DAVIDSON. I understand. And the basis there is to say that you are going to focus on a certain number of companies. You are

not focused on every small business in America, yet you make every small business in America fill out the forms. That is the gap.

So you are heavily focusing on financial institutions, it seems, and they are charged with enforcing the rule. Do you believe FinCEN has the technical expertise and capacity to properly enforce the CDD regime being applied to small businesses which have never heard of this CDD rule? Or FinCEN, for that matter.

Mr. BLANCO. I am with you on that, Congressman. I think we can. I think we do have the tools to enforce it. And I think we are doing a great job of doing outreach also to these small institutions and other institutions who are covered by this rule. We are going to do a better job of doing it. We are out there speaking. This whole hearing, I am sure many of them are going to be interested in watching it as well. So we are going to get out there and make sure that there is—

Mr. DAVIDSON. Do you believe the IRS already has enough information or any other part of the government would already have enough information if you could just ask them?

Mr. BLANCO. No. We wouldn't be doing the CDD rule if we thought that.

Mr. DAVIDSON. I guess we can disagree on that.

And I think the last thing is just a specific one on CDs. Every time a certificate of deposit changes, you roll it over. You might hold it with a bank. It is the same thing. So you might have, every 90 days, you are updating a certificate of deposit. It seems like a pretty heavy burden on banks. You are confident you have the rule right on that?

Mr. BLANCO. In fact, today, we are issuing exemptive temporary relief on instruments just like the CDs that roll over. We are going to spend more time thinking about them and what we need to do. And these are for CDs that preexist the implementation of the rule on May 11th.

Looking into the future, these CD rules, as long as the information doesn't change—and we leave that for the banks to tell the customers and the customers must agree: If any of the information on your beneficial ownership changes, you must notify us.

So I don't see that that is going to be too much of a burden moving forward. As you will see today on our website, and we have noticed it today, that we are issuing temporary exemptive relief on those that preexist the date of the implementation.

Mr. DAVIDSON. I think that you feel too much immunity from the regulatory impact that is being inflicted on America's economy and America's small businesses.

With that, my time has expired, and I yield, Chairman.

Chairman PEARCE. The gentleman's time has expired.

The Chair now recognizes Mr. Lynch for 5 minutes.

Mr. LYNCH. Thank you very much, Mr. Chairman. Thank you for your work on this committee.

And thank you, Mr. Blanco, and congratulations. I haven't seen you since you received your promotion.

Mr. BLANCO. Thank you.

Mr. LYNCH. I am a big fan of FinCEN, and I am a frequent flier to FinCEN's offices and a frequent advocate for more funding for the work that you do and your folks do within Treasury, although

I know there are a lot of competing claims within Treasury for those resources.

Mr. BLANCO. There are.

Mr. LYNCH. So I try not to cause too much trouble there.

Mr. BLANCO. Thank you for your support.

Mr. LYNCH. But suffice it to say we work with your folks regularly. Everybody up on the committee does, and we really appreciate the work that you do, and we understand the relevancy of all the work you are doing.

So among the key findings that FATF had back in 2016, the Financial Action Task Force, they evaluated our AML, anti-money laundering protocols, and counterterrorism, counterfinancing terrorism protocols. And they said that one of the chief weaknesses was, and I will quote them, “lack of timely access to adequate, accurate, and current beneficial ownership information that created fundamental gaps in the U.S. context.”

So the new implementation of Customer Due Diligence requirements, do you think that will be enough to address the weaknesses that they have identified in our system?

Mr. BLANCO. I think it is one step in identifying the weakness. I think there is another weakness, as most of you know and talk about, and that is beneficial ownership information at the point of opening a corporation, of starting the legal entity itself. That is going to be critical for us to know and to understand and to use.

Mr. LYNCH. Right. The other piece that we are working on quite a bit—the chairman has put a lot of focus on this—is cybersecurity within the financial sector. And I have been thinking this through to try to figure out a way that we might get the financial services industry to more robustly police themselves. They are always complaining about overregulation. If we can get them in as a partner, a willing partner, then it might be a better result.

But one of the things I have been considering is draft legislation to establish a financial sector cyber stress test council. This is unlike the other stress test, which is governed by FSOC, an external regulator. It would really be industry-driven, but we would obviously see what they are doing. But require them to periodically upgrade their system so that it seems, as the hackers evolve, they find these weaknesses in our system. And we don’t regularly update, so we are having these repeated failures.

Would something like that help you, in terms of establishing a standard out there and a level of accountability that requires continual upgrade periodically? Because that is what the hackers are doing. They are plus-upping their methods, and they seem to be able to find that weak link.

Mr. BLANCO. One of the priorities I have here at FinCEN—and I think I might have spoken to you about this—is cybersecurity and cybercrime, and I think it is going to be really important for us to get a handle on that, moving forward. And to your point, it does. It evolves. There has to be a constant effort to renew what resources we are looking at, what technology we have, to move ahead of the game.

In fact, I have put somebody in my front office that has been charged with innovation development and tactical development moving forward for FinCEN to look at issues just like that.

Happy to work with your staff on anything that you are proposing. Happy to have that discussion about it. I can tell you that we work regularly with industry about this technology. We were just on the West Coast talking to some of the virtual currency exchangers about this technology and how we move forward and the attacks that cyber hackers are doing on information that we have, but in general the financial system.

Mr. LYNCH. So I will work with my Republican colleagues to see if we can come up with something that is suitable to both sides, and also reach out to you and to the industry to see if we can come up with something that is a consensus approach to this rather than have people have to amend it later on.

Mr. BLANCO. Happy to talk to you about it.

Mr. LYNCH. Thanks for your great work.

And thank you, Mr. Chairman. I yield back.

Chairman PEARCE. The gentleman yields back.

The Chair now recognizes Mr. Budd for 5 minutes.

Mr. BUDD. Thank you, Mr. Chairman.

And thank you, Director Blanco, for joining us today. I appreciate that.

I want to talk this afternoon about the lack of clarity surrounding compliance requirements under the CDD rule. Financial institutions back home are still not entirely sure what they could potentially be held liable for. In the latest FAQs on the rule released by FinCEN, while it is helpful, it still highlighted some issues that need to be addressed.

First, I am curious, in developing the FAQs that were published on April 3rd, was there any discussion with industry representatives to understand the potential impact? And let me give you an example. Question 12 treats the renewal of a CD or a loan as a new account, which is inconsistent with the industry's approach. So was there any discussion with industry on that?

Mr. BLANCO. Lots of discussion, Congressman. In fact, today I issued temporary exemptive relief on that one issue so that we can have further discussion on it. We have given industry 90 days, exempting them from having to comply with it, so we can better understand the rule. They have a very sympathetic ear in me with respect to that, and we will take a look at it. I will make a decision whether or not we provide permanent exemptive relief moving forward.

But we have had—I have to tell you, Congressman, one of the things—and look, I have only been in this job for 4 months, but I have to credit our FinCEN staff who, since 2012, has really been talking to industry about this and learning from them.

And we have taken what we have learned, and you will see we have done seven or eight different tweaks to the rule. We provided several exemptive reliefs, not only in premium financing but also on the rollover, automatic rollover accounts for preexisting accounts.

So we are listening. And I think that they should be happy about the fact that we are engaging with them regularly.

Mr. BUDD. I appreciate your ear toward industry on that. I want to continue.

The FinCEN FAQs as well as the FFIEC manual update, it stated that banks still must update beneficial ownership details when opening multiple accounts. So what is this bank supposed to do if a customer doesn't respond to calls or emails or letters to confirm that their information hasn't changed?

Mr. BLANCO. So I think that really goes to the bank's risk assessment and how they use their protocols to make that determination. I can tell you, Congressman, that what we have done, both with our Federal regulators and also industry, is we discuss with them that any time a new rule like this one is being issued, there is going to be this time period where we are going to take a look and give people the ability to implement it without coming and saying, you didn't do this or you didn't close that account. There is this timeframe where things need to be worked out, both in the regulatory side and in the implementation side. We are very mindful of that.

But in the instance that you just talked about, I have to tell you it certainly is wondering if I am the banker, why you are not getting back to me. And they have a better risk assessment of their client than I would, and I think the regulators will take that into account.

Mr. BUDD. I appreciate your thoughts on that. And so do you expect banks to follow the FinCEN FAQs as if they equate to regulations or, rather, if it was formal guidance, even though they were released without industry feedback and a comment period?

Mr. BLANCO. Actually, they were released with industry feedback. One thing about the FAQs which is really interesting—

Mr. BUDD. Sorry to interrupt. Also, did it have a comment period?

Mr. BLANCO. It didn't have a comment period.

Mr. BUDD. Did not have a comment period?

Mr. BLANCO. Not with the FAQs, but the rule certainly had a comment period that lasted for quite a while. If I am not mistaken I think it lasted for 2 years or more, correct?

But the FAQs, one interesting thing about the FAQs is before we issue FAQs, there is a lot of discussion with industry and with law enforcement and with other individual stakeholders before those FAQs come out.

So it isn't as though industry is seeing those FAQs the day we publish them. Some of them are, but, for the most part, many of them have had discussions in panels, in hearings, in conversations with us, through our call-in line. We have a call-in line where people can ask questions about the rule.

So a lot of this has already been hammered out before those FAQs have even come out. And these tricky issues, the FAQ answers the tricky ones. So you are talking about the ones that are the most difficult for industry and, frankly, for regulators too, to understand as we implement the new rule. And we are working with industry to make sure that we do it right.

Mr. BUDD. Thank you very much.

In the time remaining, one question: Finally, is FinCEN concerned that banks might close accounts if they can't collect the information, particularly since that would cause FinCEN and law enforcement to lose that information?

Mr. BLANCO. That certainly, Congressman, is something that we are going to look at and make sure that, if there is a trend in that way, we will certainly look into it and see why it is happening and what we can do about it.

You are right: We end up losing valuable information. Also, people end up losing access to capital, which is not what we want either. So we will be monitoring that.

Mr. BUDD. Thanks for your time, Director.

Chairman, I yield back.

Chairman PEARCE. The gentleman yields back.

The Chair now recognizes Mr. Hill for 5 minutes.

Mr. HILL. Thank you, Chairman. Thanks for holding this hearing.

Mr. Blanco, glad to have you with us today. Thanks for your work on behalf of law enforcement.

I read in the CDD discussion that the annual cost had a range that you all have assessed up to around \$280 million on the high end.

How many SARs that FinCEN receives every year would be directly related to a shell company report from a financial institution? Would you just hazard a guess?

Mr. BLANCO. I think I would probably guess incorrectly. Given my background, I would say a lot, but I don't want to give you the wrong figure. We are happy to get back to you.

Mr. HILL. Yes, if you would get back to me on that. So I know you report the total number of SARs, but if you would tell me how many SARs relate directly to a bank reporting to you about a concern over a, quote, "shell company," however the bank defines shell company.

Mr. BLANCO. Yes.

Mr. HILL. From criminal indictments that you have brought in this arena, how many would turn on a shell company? And how much money have you recovered from indictments that are connected directly to a shell company?

Mr. BLANCO. So I can tell you, with respect to investigations that we have done, if they are sophisticated investigations, multimillion dollar, whether they are fraud investigations—so we are not just talking about drug trafficking and human tracking or terrorism. We are talking—

Mr. HILL. But they meet the definition of FinCEN.

Mr. BLANCO. Right. We are talking about fraud of elderly. We are talking about really significant things that affect people. Almost in every one of those very sophisticated cases, you are going to have a shell company someplace involved because that is the way they are laundering their money, and that is the way they are moving their money, and that is the way they hide what they do. And you don't have to go too far to see those kinds of cases. So it depends on the level.

Mr. HILL. Do you think the banks are doing a bad job collecting that information and reporting it since the Know Your Customer rules were put in place?

Mr. BLANCO. Can I just tell you I think the banks are doing a great job. I think they are doing their best, and I think they want



to do even more and even better. So I wouldn't say they are doing a bad job.

I think what we need to do is what we are doing here today: Having hearings like this, inviting industry, having the conversation, giving them priorities. These are our priorities, banks, and this is what we are looking at, together with law enforcement. I think that would better help the banks.

Mr. HILL. When I think of a tax haven, when I say the word "tax haven," what pops in your head? Name a country.

Mr. BLANCO. Congressman, I can't go there. That—

Mr. HILL. Is Panama a tax haven?

Mr. BLANCO. The obvious ones. I have done a lot of work in Panama, and I have done great work with their government. And I enjoy working with them, and they are dedicated public servants just like we are. So I wouldn't identify—

Mr. HILL. So would this sentence in the memo that we were given be hyperbole where it says that the United States risks being labeled as a money laundering, tax avoidance, and terror financing haven? Would you say that is hyperbole?

Mr. BLANCO. I think there may be some countries that would say that, but I think that is hyperbole. But—

Mr. HILL. Yes. The Financial Action Task Force said it. So I find that shocking that an organization that we support would say that.

Mr. BLANCO. One thing, Congressman—

Mr. HILL. Let me keep going. I have limited time. Sorry.

Has Congress asked or has the Treasury Department asked States for changes in State law that would be best practices for secretaries of State that they capture name, email address, address, all the data that you are looking for, for all company formations by State and make that available online and that it also contain some State penalty for nonaccuracy or not being updated? Have you ever called for that, or, to your knowledge, has Congress ever asked the States to do that in model legislation?

Mr. BLANCO. Not in my recollection. They may have. I wouldn't know.

Mr. HILL. Would you support that? Would Treasury support that if the States said a telephone number, email address, address, and contact person is just a best practice that was required under their State law?

Mr. BLANCO. The devil is always in the details in how it works out. I think it is something that we can certainly think about and discuss. I think it is always great to have the States involved at the corporate formation level, but we can't make them do it.

Mr. HILL. Yes. So Mr. Davidson asked you a question about access to information you have or could have under a criminal investigation. So the SS-4 taxpayer ID number form that the IRS has and the annual tax reform data, including ownership, is that data that would be helpful to you in searching for shell company beneficial owners?

Mr. BLANCO. Honestly, Congressman, no. It is different information.

Mr. HILL. Why?

Mr. BLANCO. Because what they are asking for is something very different. And if you look at their definition of it—first of all, two

things: One is getting the information is very difficult because you need to get a court order. And having done that and spent months trying to get one, that defeats the whole AML purpose. But if you look at the definition of what they are asking for when they talk about responsible party, they are not talking about an equity party. They are not talking about somebody who would benefit from that legal entity and what they are doing.

They are asking for a responsible person. A responsible person could be—I am sure the IRS has their own definition of what a responsible person is, but it is not what we are looking for. We are looking for somebody who is making decisions, who has some interest in the corporation, both either on the equity side or the control side.

Mr. HILL. My time has expired, Mr. Chairman. Thank you.

Chairman PEARCE. The gentleman's time has expired. The Chair would now recognize Mr. Tipton for 5 minutes.

Mr. TIPTON. Thank you, Mr. Chairman. Appreciate your holding this hearing.

Mr. Blanco, thank you for taking the time to be able to be here.

I would like to be able to follow up on Mr. Budd's questions just a little bit. We seem to have some evidence that, in terms of derisking, it has been showing to be able to push customers from larger institutions into smaller institutions. Obviously, the bigger institutions have the financial resources to be able to do the exams, to be able to handle and have the backup people that are there.

And I guess my question to you is a little bit twofold. Do you anticipate that the CDD rule and derisking trend is going to trickle this down to the smaller institutions to the point to where they may stop offering products and services, getting people unbanked?

And then, as a little bit of a follow up to that, I think it was a comment in relation to the CDs being individual new accounts coming up. You had made the comment that, I think you said, "I think the regulators will take this into account." So I would like to know if you have had conversations with the Federal Reserve, OCC, FDIC, and others issuing guidance in terms of how they are interpreting what you are trying to be able to develop?

Mr. BLANCO. Let me answer the first one on whether it would trickle down. I don't believe that the CDD rule would trickle down and have an effect, but it is something that has been commented on by more than several people, and it is something that we will monitor.

We want to make sure that we are looking at that very carefully. And if bank accounts are being closed or denied, we want to make sure that we understand why that is happening. As we have done in the last couple of weeks, we are happy to make tweaks as we go along in this rule. We are not averse to doing that as the rule becomes implemented and as our Federal examiners begin doing exams.

With respect to the CD rollover, we have had conversations with our Federal counterpart regulators, and I think we are all in agreement that there is going to be this time period where we are learning how better to do the exams with respect to the CDD, and we are learning also how industry is beginning to implement it.

It is not a gotcha game. I think we all agree to that. We have agreed to work with them as they do their exams and learn from their exams and maybe participate in some of their exams as we move forward. I think it is going to be a collective effort. Nobody here is playing the gotcha game.

What we really want, Congressman, what we really need is accurate information. That is what we want. That is what we are looking for. We are not looking to punish the financial institutions. That is not what we want. There is no value in that.

Mr. TIPTON. I would concur. I think we all want to be able to achieve the same goal, but just given the industry concerns that currently are there, I think that it does beg for some real actual clarity in terms of some of the enforcement that is going to be going on.

You have just said that we are going to be—it is a work in process. But I think when we are talking to, and I have a primary concern for a lot of our smaller financial institutions, smaller credit unions as well, in terms of some of the compliance costs in that they are going to be associated with this. How does that actually play out when they have a moving target, while they have some enforcement activities, if they are deemed to have been at fault at some level?

Mr. BLANCO. Congressman, I will disagree with you in that aspect that it is a moving target.

The conversations regarding CD really have gone back all the way to 2016 when we started talking about these things. And then it morphed into conversation with industry. We have had several hearings. In 2012, it came up. In 2016, we issued the rule. We have had extensive conversations. Congressman, just recently, in meetings with industry, they all said—I was approached myself and said: Ken, this thing needs to happen. Do not delay it anymore. We are ready.

So I think that—and I am very sympathetic to the community banks and the credit unions. I really am, coming from a suburb of Miami. I am very sympathetic to it.

We will be watching it, Congressman. They are ready. And I think they are going to do a great job moving forward. We are working with our examiners to make sure that they understand what we are looking for. We are sympathetic to what they are examining for. Soundness and safety and also AFC—AML/CFT.

It is a work in progress like any new rule or any new legislation that is passed. You have to work through the difficulties of how you are going to examine and how you are going to enforce it. But we are going to be doing it with our ultimate goal of making sure that we get the right information, not necessarily hammering people.

But there are going to be some people who frankly, I can tell, we are all adults here, who feel like they don't have to comply or they have to comply only when we issue a notice of exam. That is when, all of a sudden, you see 50, 60 people show up because now they have a compliance section.

That is not compliance. And that is not complying with the CDD rule.

Mr. TIPTON. I appreciate the efforts that you are making on it. And I think am actually empathetic to the point of making sure

that we are trying to be able to get it right rather than just issuing a hard and fast rule. We like to make sure that I, personally at least, encourage you, when we are looking at some of the enforcement, we get as much clarity as soon as we possibly can and then implement some of that flexibility as we are seeing this work through the various institutions of different size as well.

So thank you. I yield back, Mr. Chairman.

Chairman PEARCE. The gentleman's time has expired.

Mr. Blanco, thank you very much for your testimony. Thank you for your service and for being here today.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

This hearing is adjourned.

[Whereupon, at 3:45 p.m., the subcommittee was adjourned.]

# **A P P E N D I X**

May 16, 2018

**Testimony for the Record**  
**Kenneth A. Blanco**  
**Director, Financial Crimes Enforcement Network**  
**U.S. Department of the Treasury**  
**House Committee on Financial Services**  
**Subcommittee on Terrorism and Illicit Finance**  
**May 16, 2018**

**Introduction**

Chairman Pearce, Ranking Member Perlmutter, and members of the Subcommittee, thank you for inviting me to appear before the Subcommittee on Terrorism and Illicit Finance on behalf of the Financial Crimes Enforcement Network ("FinCEN"). FinCEN's mission is to safeguard the financial system from illicit use and to promote national security through the collection, analysis, and dissemination of financial intelligence. I appreciate the opportunity to discuss how the Customer Due Diligence ("CDD") rule and its compliance requirements for financial institutions advance our efforts to combat money laundering, terrorist financing and other serious crimes.

The reach, speed, and accessibility of the U.S. financial system make it an attractive target to money launderers, fraudsters, terrorists, rogue states, and other bad actors. To combat efforts by these individuals, groups or networks to abuse the U.S. financial system, we have developed and rigorously enforce one of the most effective anti-money laundering ("AML") and countering the financing of terrorism ("CFT") regimes in the world. But, as strong as our AML/CFT framework is, malicious actors will continue to attempt to exploit any vulnerability to move their illicit proceeds undetected through legitimate financial channels, in order to hide, foster, or expand the reach of their criminal or terrorist activity. We must therefore be vigilant in our mission to protect the U.S. financial system by: (1) aggressively investigating and pursuing criminal and terrorist activity; (2) ensuring that we collect the financial intelligence necessary to support these investigations; (3) understanding the evolving trends and typologies of criminal and terrorist activity; and (4) closing any regulatory gaps that expose our financial system to money laundering, other criminal activity, and terrorist financing risks that threaten our financial system and put our nation, communities, and families in harm's way.

The misuse of legal entities to disguise illicit activity has been a key vulnerability in the U.S. financial system. Corporate structures have facilitated anonymous access to the financial system for criminal activity and terrorism. Narcotraffickers, proliferation financiers, money launderers, terrorists and other criminals have been able to establish shell companies, which then use accounts at financial institutions, directly or indirectly, without ever having to reveal who ultimately is behind the transactions being facilitated. This has made it difficult for law enforcement to pursue investigative leads, and for financial intelligence units to produce those leads in the first instance. And, just as important, this has made it difficult for financial institutions to apply effective risk-based AML programs.

An open and transparent financial system in which we can identify the trail of transactions and actual account owners is therefore essential to disrupting illicit activities and dismantling criminal and terrorist networks. For these reasons, FinCEN and the Department of the Treasury

more broadly have prioritized increasing transparency in corporate formation and have strengthened regulatory requirements regarding customer due diligence for legal entity customers when they open accounts at financial institutions.

#### **Background on CDD Rulemaking**

FinCEN finalized the “Customer Due Diligence Requirements for Financial Institutions,” (or “CDD Rule”) on May 11, 2016. Before finalizing the CDD Rule, FinCEN engaged in a transparent rulemaking process, to develop the best rule possible: and one that accounted for concerns raised by the public and private sectors. To this end, FinCEN first issued an Advance Notice of Proposed Rulemaking (“ANPRM”) in 2012, to seek early feedback regarding potential CDD and beneficial ownership requirements for financial institutions.<sup>1</sup> We received approximately 90 comments in response to the ANPRM. To better understand and address the concerns raised in those comments, FinCEN and Treasury representatives held five public hearings in Washington, D.C., and across the country.<sup>2</sup> These engagements allowed stakeholders to express their views on the ANPRM and offer recommendations on how best to develop a workable rule that would help financial institutions better know their customers and assist law enforcement in identifying illicit actors hiding behind the veils of corporate structures. We then issued a Notice of Proposed Rulemaking (“NPRM”) on August 4, 2014, incorporating feedback received from this engagement.<sup>3</sup> FinCEN received 141 comments in response to the NPRM from financial institutions, trade associations, Federal and State agencies, non-governmental organizations, members of Congress, and others.

The extensive and thoughtful engagement with industry and other stakeholders, through notice and comment, hearings, and other discussions over several years about the benefits of the rule and potential costs and burdens has deeply influenced the resulting regulations. We believe that the CDD Rule takes a pragmatic approach, balancing the need for information and the practicality of obtaining it in certain circumstances.

The CDD Rule clarifies and strengthens CDD requirements for covered financial institutions, which include banks, securities broker-dealers, mutual funds, and futures commission merchants and introducing brokers in commodities. The rule streamlines and standardizes existing regulatory requirements to promote consistency in both implementing and enforcing these requirements across and within financial sectors; it adds a new requirement for these financial institutions to know the real people who own, control, and profit from companies (also known as “beneficial owners”)—and verify their identities.

The CDD Rule advances the purpose of the Bank Secrecy Act by making available valuable information needed to disrupt illicit finance networks and other criminal or terrorist activities. This in turn increases financial transparency and augments the ability of financial institutions and law enforcement to identify the assets and accounts of criminals and national security threats. It also facilitates compliance with sanctions programs and other measures that cut off financial

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<sup>1</sup> 77 FR 13046 (Mar. 5, 2012).

<sup>2</sup> 81 FR 29,398, 29,402 n. 31 (May 11, 2016).

<sup>3</sup> 79 FR 45,151 (Aug. 4, 2014).

flows to these actors, just as it facilitates reporting and investigations in support of tax compliance.

In addition, by promoting consistency in implementing and enforcing CDD regulatory expectations, the rule also helps financial institutions assess and mitigate risk and comply with all existing legal requirements.

*Final Beneficial Ownership and Customer Due Diligence (CDD) Rule for Legal Entity Customers*

In brief, the CDD Rule includes four core requirements. Covered financial institutions must:

- 1) Identify and verify the identity of customers (this was an existing requirement prior to the CDD Rule);
- 2) Identify and verify the identity of the beneficial owners of companies opening accounts (this is a new requirement);
- 3) Understand the nature and purpose of customer relationships; and
- 4) Conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information. (These last two elements are AML program requirements in the CDD Rule that codify regulatory expectations of what financial institutions should have been doing prior to the CDD Rule to comply with their suspicious activity reporting requirements effectively.)

The definition of beneficial owner contains two prongs— the ownership or equity prong and the control prong. Financial institutions must collect information under each prong at account opening to comply with the rule. Under the ownership or equity prong, a covered financial institution must obtain information from a legal entity customer on any natural person who owns, directly or indirectly, 25 percent or more of the legal entity customer. This could include up to four individuals, or, no individuals (if no one owned 25 percent or more). When no individual meets the threshold for ownership interest under the rule, the control prong becomes all the more important. Under the control prong, the covered financial institution must collect information on at least one natural person with significant responsibility to control, manage, or direct the legal entity customer. This could include, for example, a company's president, chief executive officer, or another individual having significant control over and decision-making authority within the company.

Significantly, in obtaining this information, covered financial institutions can rely on the information provided and certified by the legal entity customer opening the account. The covered financial institution generally does not have to go beyond what is provided, unless it has reason to believe that the information provided is unreliable.

**Implementation of the Customer Due Diligence Rule**

FinCEN is committed to ensuring effective implementation of the CDD Rule. As noted earlier, prior to issuance of the NPRM for the CDD Rule, FinCEN actively solicited feedback from industry and engaged in robust engagement with stakeholders. After considering comments on



our proposed rule, we extended the proposed one-year compliance period in the NPRM to two years, in order to provide financial institutions additional time to address operational needs, including developing related policies and procedures, providing training to employees, and preparing customer communication.

During the past two years, FinCEN also has taken additional steps to ensure that covered financial institutions and other stakeholders understand the rule's requirements. For example, in July 2016, shortly after FinCEN issued the final rule, FinCEN published an initial set of Frequently Asked Questions ("FAQs"), which provided guidance to financial institutions on the key components of the rule, such as:

- A summary of the rule's requirements;
- An explanation of which financial institutions are covered by the rule;
- A description of the identification information to be obtained from legal entity customers at account opening;
- The mechanism for collecting and verifying the identity of beneficial owners;
- The required policies and procedures financial institutions must implement to obtain information on beneficial owners and to conduct ongoing customer due diligence; and
- Information regarding how financial institutions must use the collected information.

FinCEN and other Treasury representatives have also engaged with various stakeholders, including financial institutions, trade associations, regulators, and examiners, at conferences, workshops and in other fora, to explain and clarify various aspects of the rule and hear about emerging questions. FinCEN also has provided ongoing feedback to financial institutions by responding to questions about the rule submitted to the FinCEN Resource Center.

Based on continued feedback from industry, more recently, on April 3, 2018, FinCEN published a second set of 37 FAQs that provides detailed responses to a wide array of questions stakeholders have raised since the rule was published. Many of the FAQs incorporate topics and address scenarios that had been discussed with stakeholders before the FAQs were published.

As reflected in the recent FAQs, FinCEN takes a practical approach to how the rule should be implemented—an approach that continues to balance the need for transparency in corporate ownership and control with the compliance burden and costs to industry.

Lastly, FinCEN has participated in webinars sponsored by industry and regulators to discuss the rule's requirements and any additional questions stakeholders, including financial institutions and examiners, may raise.

#### **Compliance and Enforcement of the Customer Due Diligence Rule**

As you may be aware, FinCEN has delegated its examination authority to the Federal functional regulators responsible for supervising and examining covered financial institutions, including the Federal Banking Agencies (i.e., Federal Reserve, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, and the National Credit Union Administration), the U.S. Securities and Exchange Commission, and the Commodity Futures Trading Commission, as

well as with the self-regulatory organizations (i.e., the Financial Industry Regulatory Authority for broker-dealers and the National Futures Association for futures firms).

FinCEN has worked collaboratively and has maintained regular and ongoing discussions with its regulatory counterparts to ensure a common understanding and consistent compliance and enforcement standards within and across regulated industry sectors. FinCEN will continue to work with these agencies regarding their examination approach to ensure that we help covered financial institutions achieve compliance.

Although we expect covered institutions to be ready on May 11, 2018, to begin timely and effective implementation of the policies, procedures, and controls required under the CDD Rule—and we are pleased to have heard from many in industry that they were ready—we also understand that institutions, regulators and other stakeholders may need a little extra time to smooth out any wrinkles. This is the case whenever we issue a new rule, the purpose of which is always to enhance our AML regime and not to serve as a vehicle for punishing financial institutions. There is always an understandable expectation that industry’s fine-tuning of its implementation, and the government’s fine-tuning of the examination process itself, takes time and that new questions often emerge after implementation begins. We have spoken with our counterparts, including the Federal Banking Agencies, the U.S. Securities and Exchange Commission, and the Commodity Futures Trading Commission, to discuss these issues. We are all committed to ensuring that covered financial institutions are able to implement the rule effectively, and in a way that makes practical sense.

Our goal in this rule is to gain the transparency needed to protect the U.S. financial system and to prevent, deter, detect and disrupt money laundering, terrorist financing, and other serious crimes. It is important for us to continue to work with our regulatory partners, their examiners and financial institutions to achieve these objectives through compliance with the rule. It is equally important, however, to understand that seamless implementation does not happen overnight and, for some areas, we all will need time to benefit from cumulative practical experiences with the new rule as part of the process. In the meantime, we would encourage financial institutions to alert their examiners to any issues early on, and to share such concerns with FinCEN. We will continue to work with industry and regulators to understand and help address any concerns.

FinCEN will continue to engage industry groups and other stakeholders to understand any specific unintended challenges that the rule may present and, if necessary, FinCEN will provide further guidance. Likewise, we will work with regulatory and law enforcement partners to understand and address any compliance issues appropriately.

### **Conclusion**

I would like to thank the Committee for its efforts on this important matter and look forward to working with this Committee and other members of Congress to continue combatting money laundering and illicit finance threats to secure our financial system, keep our nation safe and prosperous, and protect our communities and families from harm.



May 15, 2018

The Honorable Steve Pearce  
Chairman  
Subcommittee on Terrorism and Illicit  
Finance  
Committee on Financial Services  
U.S. House of Representatives  
2432 Rayburn House Office Building  
Washington, D.C. 20515

The Honorable Ed Perlmutter  
Ranking Member  
Subcommittee on Terrorism and Illicit  
Finance  
Committee on Financial Services  
U.S. House of Representatives  
1410 Longworth House Office Building  
Washington, D.C. 20515

Dear Chairman Pearce and Ranking Member Perlmutter:

The Consumer Bankers Association (CBA) appreciates the Subcommittee holding a hearing entitled, "Implementation of FinCEN's Customer Due Diligence Rule – Regulator Perspective." CBA is the voice of the retail banking industry whose products and services provide access to credit to millions of consumers and small businesses. Our members operate in all 50 states, serve more than 150 million Americans and collectively hold two-thirds of the country's total depository assets.

CBA's member institutions support the Financial Crimes Enforcement Network (FinCEN) and its mission to safeguard the financial system from illicit use, combat money laundering, and promote national security. Recently, on May 11, 2018, FinCEN made effective its customer due diligence rule (CDD rule), which is meant to allow financial institutions to better identify their client populations and help create better financial transparency, while at the same time, reducing the number of illegal transactions. Specifically, the highly complex CDD rule requires covered financial institutions to establish procedures to identify and verify the identity of the "beneficial owners" of legal entity customers that open new accounts and ensure their anti-money laundering compliance programs include appropriate risk-based procedures, including developing customer risk profiles and periodically updating the beneficial ownership information of existing customers.

CBA members understand the need for a CDD rule and appreciate the time banks were given to implement such a complex data collection rule. Unfortunately, covered financial institutions have experienced unexpected delays by unforeseen challenges which will require more time for systems and processes to be fully operational and compliant. Due to the complexity of the rule, we encourage Congress to work with the federal banking regulators to provide greater flexibility during the implementation and examination process of the new CDD rule.

Specifically, financial institutions need sufficient time to interpret and seek clarification on federal guidance related to the CDD rule to ensure compliance. Recently, on April 3, 2018, FinCEN issued long-awaited frequently asked questions (FAQs) regarding the final CDD rule, which covered a wide range of topics, including beneficial ownership threshold issues, specific

identification, and verification scenarios, along with various exemptions and exclusions. In July 2016, FinCEN published a first set of FAQs, and the agency says it may issue additional FAQs and guidance, or grant exceptive relief as appropriate, further adding to the complexity of compliance and uncertainty for many covered institutions.

Additionally, the Federal Financial Institutions Examination Council's (FFIEC) exam manual incorporating the new CDD rule was not released until the day the CDD rule became effective, May 11, 2018. Given the complexities of the CDD rule, it appears the two-year timeline did not give the FFIEC adequate time to complete the exam manual and incorporate the rule prior to its effective date. Full knowledge of the exam manual is critical to understanding how examiners will examine banks for compliance with the CDD rule, and covered financial institutions will need additional time to complete their preparations to ensure compliance.

CBA encourages Congress to support greater regulatory flexibility for the implementation of the CDD rule for covered financial institutions as it will ensure appropriate compliance to achieve critical national security goals. Thank you for holding this important hearing and we appreciate the opportunity to submit this statement for the record.

Sincerely,

A handwritten signature in black ink, appearing to read "Richard Hunt".

Richard Hunt  
President and CEO  
Consumer Bankers Association



**Jim Nussle**  
President & CEO  
  
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May 15, 2018

The Honorable Stevan Pearce  
Chairman  
Subcommittee on Terrorism and Illicit Finance  
Committee on Financial Services  
House of Representatives  
Washington, DC 20515

The Honorable Ed Perlmutter  
Ranking Member  
Subcommittee on Terrorism and Illicit Finance  
Committee on Financial Services  
House of Representatives  
Washington, DC 20515

Dear Chairman Pearce and Ranking Member Perlmutter:

On behalf of America's Credit Unions, I am writing regarding the hearing entitled "Implementation of FinCEN's Customer Due Diligence Rule." The Credit Union National Association (CUNA) represents America's credit unions and their 110 million members.

The Financial Crimes Enforcement Network's (FinCEN) Customer Due Diligence (CDD) Rule went into effect for credit unions and other financial institutions last week. The rule requires financial institutions to obtain identifying information about the beneficial owners of their legal entity accounts. The CDD Rule amends Bank Secrecy Act regulations in an effort to improve financial transparency and prevent criminals and terrorists from misusing companies to disguise illicit activities and launder ill-gotten gains. CUNA strongly supports these objectives.

Specifically, the CDD Rule requires covered financial institutions to establish and maintain written policies and procedures that are reasonably designed to (1) identify and verify the identity of customers; (2) identify and verify the identity of the beneficial owners of companies opening accounts; (3) understand the nature and purpose of customer relationships to develop customer risk profiles; and (4) conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

While the changes necessary to comply with the CDD Rule are significant, particularly for smaller credit unions, credit unions have largely been able to come into compliance during the preceding two-year implementation period. Additionally, the several exemptions included in the final CDD Rule provide some relief for credit unions on an on-going basis.

We would like to express to this Subcommittee our appreciation of FinCEN's responsiveness over the past two plus years as the industry shared concerns and suggestions with the agency before and after the CDD Rule was finalized. FinCEN solicited input on the CDD Rule and directly addressed issues raised by the industry, including specific concerns and suggestions from CUNA and our member credit unions. The guidance was released last month in the form of a Frequently Asked Questions (FAQ) document; we greatly appreciate such guidance ahead of the effective date, which is an uncommon practice among federal financial regulatory agencies.


We urge this subcommittee to continue to encourage FinCEN to work with the industry on implementation issues as they arise. While the CDD Rule is already in effect, matters requiring clarification will undoubtedly continue to present themselves. In addition, we hope FinCEN continues

its practice of providing timely responses to specific inquiries by credit unions and other affected financial institutions.

While the National Credit Union Administration (NCUA) is the lead agency that will examine credit unions for compliance with the CDD Rule, we urge FinCEN and NCUA to work closely together as examiners become more comfortable with the specific requirements of the rule. We believe it is much more efficient and effective for NCUA, the credit union system, and ultimately FinCEN to work together to ensure proper compliance.

On behalf of America's credit unions and their 110 million members, thank you very much for your consideration of our views.

Sincerely,



Jim Nussle  
President & CEO



May 16, 2018

## FinCEN's Customer Due Diligence Rule: The Community Bank Perspective

On behalf of the nearly 5,700 community banks represented by ICBA, we thank Chairman Pearce, Ranking Member Perlmutter, and members of the Financial Services Subcommittee on Terrorism and Illicit Finance for convening today's hearing on "Implementation of FinCEN's Customer Due Diligence Rule – Regulator Perspective." ICBA is pleased to have the opportunity to submit this statement for the hearing record.

Community bankers are committed to supporting balanced, effective measures that will prevent terrorists from using the financial system to fund their operations and prevent money launderers from hiding the proceeds of criminal activities. The Financial Crimes Enforcement Network (FinCEN) Customer Due Diligence (CDD) Rule under the Bank Secrecy Act requires "covered financial institutions" to identify the beneficial owners who own or control certain legal entity customers at the time a new account is opened. Mandatory compliance with the CDD Rule began May 11, 2018. In this statement, ICBA recommends certain revisions to the CDD Rule that will make it more effective in meeting its stated goal of combating money laundering and other illicit financing.

### ICBA Recommended Revisions to CDD Rule

ICBA's position is that if the government has an interest in collecting and maintaining records of beneficial ownership, such information should be collected and verified at the time a legal entity is formed, rather than requiring financial institutions to collect this information. Collecting and verifying the identity of all natural person owners of each entity by either the Internal Revenue Service or other appropriate federal agency and/or state in which the entity is formed would provide uniformity and consistency across the United States. Making the formation of an entity contingent on receiving beneficial owner information would create a strong incentive for equity owners and investors to provide such information. Additionally, periodic renewal of an entity's state registration would provide an efficient and effective vehicle for updating beneficial ownership information.

If responsibility for collecting beneficial ownership information remains with financial institutions, ICBA recommends that information collection be based on customers rather than accounts. This change would be consistent with the customer information program (CIP) set forth in the Bank Secrecy Act. A focus on customers rather than accounts would greatly facilitate information collection, alleviating community bank burden and producing more accurate information. The creation of an additional account by an existing customer or the renewal of a customer account should not trigger a new obligation to verify beneficial ownership information as long as the bank has no knowledge of facts that would reasonably call into question the reliability of the information the bank already has on file. A customer basis for the rule, combined with a risk-based approach, would obligate a financial institution to perform additional due diligence when warranted by a higher level of risk.

**Compensation for Anti-Money Laundering and Anti-Terrorist Financing Efforts**

For community banks, BSA compliance represents a significant expense in terms of both direct and indirect costs. BSA compliance is fundamentally a governmental, law enforcement function. As such, the costs should be borne by the government. ICBA supports the creation of a tax credit to offset the cost of BSA compliance.

**Closing**

Thank you again for convening today's hearing. The integrity of our financial system is among the highest concerns of America's community bankers. ICBA looks forward to continuing to work with the committee to ensure the CDD Rule is workable and to modernize the Bank Secrecy Act in a way that will strengthen critical law enforcement while rationalizing community bank compliance with this important law.



**House Committee on Financial Services**

Hearing: **"Implementation of FinCEN's Customer Due Diligence Rule (CDD)"**

May 17, 2018

*Questions for the Record from U.S. Representative Ted Budd (R-NC)*

**Witness:** Mr. Kenneth A. Blanco, Director, Financial Crimes Enforcement Network (FinCEN)

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1.) There is an item in the FFIEC manual update pulled directly from the FAQs related to a legal entity customer opening multiple accounts. It states:

"If a legal entity customer opens multiple accounts a bank may rely on the pre-existing beneficial ownership records it maintains, provided that the bank confirms (verbally or in writing) that such information is up-to-date and accurate at the time each account is opened."

So, what is a bank supposed to do if a customer doesn't respond to calls, emails or letters to confirm the information hasn't changed? Do you feel this will lead to a new wave of "de-risking," as some pundits have prognosticated?

**Answer:**

*One of the purposes behind this rule was to level the playing field for all covered institutions. In the past, some financial institutions would independently collect beneficial ownership information at varying thresholds. To avoid those controls, bad actors would simply bypass those institutions and open accounts at institutions without a policy on collecting ownership information. Now, under the Customer Due Diligence (CDD) Rule, all covered financial institutions (big and small) have to obtain this information from their customers, without fear that the customers will shop around for less stringent information requirements. Moreover, to help financial institutions educate their clients about what information financial institutions are required to collect under the Rule, FinCEN has posted a reminder of the Rule's obligations on its website, to which financial institutions can cite.<sup>1</sup>*

*If a legal entity customer of a covered financial institution<sup>2</sup> chooses not to provide the information that a financial institution is required to collect, then FinCEN would expect that the financial institution would follow its documented procedures for responding to such circumstances. Those procedures could be similar to the procedures under the Customer Identification Program Rule (another situation where customers must provide information in*

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<sup>1</sup> See, <https://www.fincen.gov/news/news-releases/fincen-reminds-financial-institutions-cdd-rule-becomes-effective-today>, May 11, 2018.

<sup>2</sup> For purposes of the CDD Rule, covered financial institutions are federally regulated banks and federally insured credit unions, mutual funds, brokers or dealers in securities, futures commission merchants, and introducing brokers in commodities. 31 CFR 1010.605(e)(1).

support of a financial institution's regulatory requirements) for responding to circumstances in which the financial institution cannot form a reasonable belief that it knows the true identity of a customer, which should describe: when the financial institution should not open an account; the terms under which a customer may use an account while the financial institution is attempting to verify the customer's identity; when the financial institution should close an account, after attempts to verify a customer's identity have failed; and when the financial institution should file a Suspicious Activity Report, in accordance with applicable law and regulation.<sup>3</sup>

2.) Do you think that if a bank follows what appears to be required by the FAQs, the bank could potentially get in trouble with regulators because the questions were released without industry feedback and a comment period?

Related to that, if a bank decides to hold off on transactions for, say, a business account due to waiting for beneficial ownership responses, could the financial institutions be sued by the business for breach of contract? In those situations, who does a bank please: FinCEN, the regulator or the customer?

**Answer:**

*We have an ongoing dialogue with our regulatory partners to ensure a common understanding and consistent interpretation of the Rule's requirements. We have worked closely with Federal Functional Regulators on the revisions to their FFIEC Bank Secrecy Act/Anti-Money Laundering Examination Manual<sup>4</sup> (FFIEC BSA/AML Examination Manual), which outlines their examination procedures when examining financial institutions for compliance with the CDD Rule. We believe that the Federal Functional Regulators understand our approach to the Rule and are reasonable in their approach to examination. Moreover, since the release of the Rule, FinCEN has participated in several training events with examiners to ensure that they understand and examine financial institutions in a manner that is consistent with FinCEN's intent and the Rule's requirements. While it has only been a short time since the Rule has come into effect, we have heard feedback that examiners are examining institutions in a manner that is consistent with FinCEN's intent and the Rule's requirements. Financial institutions are encouraged to contact FinCEN, as the agency promulgating the Rule, for specific guidance regarding the Rule's requirements.*

3.) What are banks supposed to do if the actual regulations, FAQs and now the exam manual conflict? What interpretation do they follow?

**Answer:**

*Guidance, such as FinCEN's CDD FAQs, is intended to clarify issues or respond to questions of general applicability that arise under FinCEN regulations, so FinCEN sees no conflict between*

<sup>3</sup> See for example, 31 CFR 1020.220(a)(2)(iii).

<sup>4</sup> Bank Secrecy Act/Anti-Money Laundering Examination Manual issued by the Federal Financial Institutions Examination Council.

*the regulation and the guidance. In addition, FinCEN and the FFIEC member agencies have coordinated extensively to ensure that examination manual chapters regarding CDD and Beneficial Ownership are consistent with FinCEN's regulations and guidance. If financial institutions identify potential inconsistencies among the different source materials, they should contact FinCEN for further guidance.*

4.) Is the 25 percent ownership level a “floor or ceiling?” Can you please elaborate or give examples of some bright line boundaries as to what issue, or combination of issues, you would consider reasonable to require a bank on a “risk-based basis” to go below the 25 percent threshold?

This is kind of a chicken and egg issue here, but my question is, is there an expectation that banks always have to do enhanced due diligence lower than the 25 percent level, for even what they perceive as low risk entities, to justify the original low risk assessment?

**Answer:**

*The Rule requires covered financial institutions to collect beneficial ownership information on individuals owning 25 percent or more of a covered legal entity customer. Under the equity prong, financial institutions are not required to collect beneficial ownership information on equity owners with less than a 25 percent interest, even in circumstances of heightened risk. Although not required by the Rule, financial institutions may consider collecting further customer information, including beneficial ownership information, at an ownership threshold lower than 25 percent, in situations where this would be helpful to adequately identify and mitigate risks associated with that legal entity customer.*

*As we have stated in Question #2 of the April 2018 FAQs: “Transparency in beneficial ownership, however, is only one aspect of a covered financial institution’s customer due diligence obligations. A financial institution may reasonably conclude that collecting beneficial ownership information at a lower equity interest than 25 percent would not help mitigate the specific risk posed by the customer or provide information useful to the financial institution in analyzing the risk. Rather, any additional heightened risk could be mitigated by other reasonable means, such as enhanced monitoring or collecting other information, including expected account activity, in connection with the particular legal entity customer.”*

5.) Which, in your mind, should be the best indicator or predictor of risk: Is it the inherent risk of the legal entity or where it’s located, transparency of its ownership structures or believability of what is attested on the self-certification forms?

**Answer:**

*An assessment of anti-money laundering risk is dependent on all relevant facts and circumstances, including, among other things, the nature and location of the customer, and the*

*products and services involved. For any given customer, FinCEN expects financial institutions to have procedures for conducting sufficient due diligence to understand the nature and purpose of the customer relationships for the purpose of a customer risk profile. Given their knowledge of their customers, financial institutions are in the best position to identify which factors, or combination of factors, are most determinative to their risk assessment.*

6.) The CDD requirements also don't end after a bank finally gets a self-certification form as the institution could, at any time, encounter "knowledge of facts that would reasonably call into question the reliability of such information" provided on the self-certification form. What is an example of how a bank would encounter this or what should it be doing proactively to comply?

**Answer:**

*A covered financial institution may rely on the information supplied by a legal entity customer regarding the identity of its beneficial owner or owners, provided that it has no knowledge of facts that would reasonably call into question the reliability of such information. As FinCEN noted in the CDD final rule, it anticipates that, in the overwhelming majority of cases, a covered financial institution should be able to rely on the accuracy of the beneficial owner or owners identified by the legal entity customer, absent the institution's knowledge to the contrary. (See p. 29407 of the final rule: <https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf>).*

*Financial institutions, however, do have an obligation to "conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information." (See p. 29457-8 of the final rule: <https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf>). The preamble of the Rule further clarifies this: "When a financial institution detects information (including a change in beneficial ownership information) about the customer in the course of its normal monitoring that is relevant to assessing or reevaluating the risk posed by the customer, it must update the customer information, including beneficial ownership information. Such information could include, e.g., a significant and unexplained change in the customer's activity, such as executing cross-border wire transfers for no apparent reason or a significant change in the volume of activity without explanation. It could also include information indicating a possible change in the customer's beneficial ownership, because such information could also be relevant to assessing the risk posed by the customer." (See p. 29399 of the final rule: <https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf>).*

7.) It's still unclear when, how or what news could constitute a reason for a bank to doubt the sworn statements of someone who self-certifies they exert "managerial control."

So the question here is: after a bank corroborates the identity of the individual, what is expected of the bank to verify that their high level of control makes sense for their business background or

expertise? Because it appears difficult at first blush to determine if someone is a nominee holding a figurehead title without doing more due diligence.

**Answer:**

*A covered financial institution may rely on the information supplied by a legal entity customer regarding the identity of its beneficial owner or owners, provided that it has no knowledge of facts that would reasonably call into question the reliability of such information. As FinCEN noted in the CDD final rule, it anticipates that, in the overwhelming majority of cases, a covered financial institution should be able to rely on the accuracy of the beneficial owner or owners identified by the legal entity customer, absent the institution's knowledge to the contrary. (See p. 29407 of the final rule: <https://www.gpo.gov/fdsys/pkg/FR-2016-05-11/pdf/2016-10567.pdf>).*

8.) How does a bank detail control for incorporated clubs, like the Boy Scouts or Lions Clubs? Does a bank name the President of the overall club or a local leader?

**Answer:**

*In the cases where the local chapter is itself a legal entity as defined under the applicable Rule, the financial institution is required to collect beneficial ownership information.*

9.) Should banks tag ownership on a per-account or per-customer basis?

**Answer:**

*Financial institutions are obligated to identify and verify beneficial ownership information for legal entity customers at the time each account is opened.*