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By electronic delivery to
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Financial Crimes Enforcement Network
Department of the Treasury
P.O. Box 39
Vienna, Virginia 22183
Attn: Currency Transaction Report Exemption Rule and Form Amendments

Re: Notice of Proposed Rulemaking on Proposed Amendments to the Bank Secrecy Act Regulations – Exemptions from the Requirement to Report Transactions in Currency, RIN 1506-AA90

Ladies and Gentlemen:

The American Bankers Association (ABA) respectfully submits its comments to the Financial Crimes Enforcement Network's (FinCEN) notice of proposed rulemaking to amend the Bank Secrecy Act Regulations—Exemptions from the Requirement to Report Transactions in Currency.[1] ABA brings together banks of all sizes and charters into one association. ABA works to enhance the competitiveness of the nation's banking industry and to strengthen America's economy and communities. Its members – the majority of which are banks with less than $125 million in assets – represent over 95 percent of the industry's $13.3 trillion in assets and employ over 2 million men and women.

Summary of Comment

ABA believes that the proposed amendments to section 103.22 will not result in an appreciable decrease in the number of Currency Transaction Report (CTR) filings. Although FinCEN states that its intent is "to simplify the current requirements for depository institutions to exempt their eligible customers," the piecemeal amendment of the Regulation will not simplify the process. Rather, ABA believes that the proposed changes merely substitute one set of compliance burdens with another. First, the proposed amendments will result in the establishment of *three* categories of exemptible customers – each with distinct eligibility requirements and record-keeping requirements – where there had been two. Second, although the proposed amendments would remove some of the existing unnecessary filing requirements, it is clear that FinCEN will continue to require banks to document

[1] 31 CFR §103.22(d).

exemption decisions and renewals thoroughly, thereby significantly cutting back on the resulting relief. Third, the proposed amendments will introduce a new, burdensome compliance duty—the responsibility to monitor and to report changes in control of exempt customers. Finally, nothing in the proposed amendments addresses two of the most significant disincentives of the current exemption regime, namely the complexities of determining and documenting eligibility coupled with the fact that exemption decisions and filings create new exposure for banks to regulatory second-guessing, the imposition of civil money penalties, and back-filing orders.

Background

The reporting of currency transactions in excess of $10,000 was the first anti-money laundering component of the Bank Secrecy Act (BSA). In 1994, Congress recognized that the reporting of legitimate and routine business transactions has no value to law enforcement efforts to detect illegal activity, and it passed the Money Laundering Suppression Act (MLSA), amending the BSA to establish a statutory exemption from currency transaction reporting for certain categories of depository institution customers.[2] The MLSA established two categories of exemptions, so-called mandatory and discretionary exemptions, and directed the Secretary of the Treasury (the Secretary) to draft regulations governing exemption criteria and the exemption process.

The current CTR exemption regulation (the Regulation) was the result of a five-part rulemaking by FinCEN that was finally completed in 2000.[3] ABA was an active participant in all phases of the rulemaking and engaged in extensive member outreach to encourage banks to use the exemption process. From the outset, however, acceptance of the exemption process was very limited. The combination of complicated eligibility criteria, burdensome documentation requirements, and fear of regulatory second-guessing of exemption decisions has discouraged banks from exempting eligible customers. Expectations for a 30% reduction of CTR filings were not realized; instead, there has been a steady increase in the number of CTR filings from approximately 11 million in 1994 to 15 million in 2006. As a recent Government Accountability Office (GAO) study demonstrated,[4] CTRs remain overwhelmingly mass reports of the legal activities of law abiding parties, only few of which are ever even viewed by government agencies.

Unsurprisingly, only two years after the exemption regulations were finally enacted, a 2002 report to Congress by FinCEN on the use of the CTR exemption process outlined the issues discouraging use of the exemption process, issues still echoed today.[5] Recognizing that incremental changes would not fix a failed regulation, in

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[2] 31 U.S.C. §5313.

[3] *See* 61 Fed.Reg. 18204 (April 24, 1996); 62 Fed.Reg. 47141 (September 8, 1997); 62 Fed.Reg. 63298 (November 28, 1997); 63 Fed.Reg. (September 21, 1998); 65 Fed.Reg. 46356 (July 28, 2000).

[4] U.S. Government Accountability Office, GAO-08-355, *Bank Secrecy Act: Increased Use of Exemption Provisions Could Reduce Currency Transaction Reporting While Maintaining Usefulness to Law Enforcement Efforts* 1 (2008).

[5] Financial Crimes Enforcement Network, *Report to Congress: Use of Currency Transaction Reports* 15 (2002).

2005 ABA requested reform, calling for abandonment of the current exemption regulation and the adoption of a simplified "seasoned customer exemption." The proposed seasoned customer exemption is intended to streamline the exemption process, requiring a one-time notice to FinCEN that is based on the customer's seasoned relationship with the bank as the grounds for the exemption. On three occasions—twice in 2006 and once in 2007—the House of Representatives has passed legislation to end CTR requirements for well known business customers. [6]

ABA looked forward to the findings of 2008 GAO study, and the possibility that it would reinvigorate the push for legislative reform. As expected, the information contained in the study reaffirmed ABA arguments for reform, updating statistics on the number of CTRs filed annually, the considerable costs incurred, the limited usefulness of CTRs to law enforcement, and the reluctance of banks to exempt customers. Although the GAO Study recommended several simplifying changes to the existing exemption process, FinCEN's proposed amendments while purportedly following the GAO recommendations, actually complicate rather than simplify the exemption process. ABA believes that these proposed amendments only tinker with the current exemption regulation and fail to adequately address the significant regulatory disincentives of the exemption process, and therefore, will do nothing but perpetuate a broken system that continues to divert resources away from a focus on criminals and terrorists to the collection of mass data on the legal transactions of law abiding parties.

The proposed amendments introduce an arbitrary distinction between Phase I customers and offer illusory relief

As previously explained, in the MLSA Congress established two categories of customers eligible for exemption, "mandatory" and "discretionary" customers. Pursuant to a delegation of authority from the Secretary, FinCEN promulgated regulations that parallel the MLSA's scheme by creating two categories of exemptible customers, Phase I and Phase II customers. Phase I customers include depository institutions; federal, state, and local government agencies; entities that exercise governmental authority; and companies that are publically traded on one of the nationally recognized stock exchanges (listed companies). Phase II customers include eligible non-listed businesses and payroll customers.[7] The regulatory regime is different depending on whether a customer is a Phase I or Phase II customer.

In the name of simplification, however, the proposed amendments will result in the de facto establishment of *three* categories of exemptible customers, each with its own exemption criteria and procedure, where there currently are two. FinCEN proposes to amend sections 103.22(d)(3)(ii) and (d)(4) by eliminating the requirements for filing an initial designation of exempt persons and for annually reviewing this designation for Phase I customers that are depository institutions, federal, state, or local governments, or entities exercising governmental authority. Listed companies

[6] *See* Financial Services Regulatory Relief Act, HR 3505, 109th Cong. (2006); Seasoned Customer Exemption Act of 2006, HR 5341, 109th Cong. (2006); Seasoned Customer CTR Exemption Act of 2007, HR 323, 110th Cong. (2007).
[7] 31 C.F.R. § 103.22 (d).

and their majority owned subsidiaries, however, are excluded from these regulatory reforms, introducing a new arbitrary distinction between Phase I customers.

Like reports of currency transactions by other Phase I customers, reports of the currency transactions of listed companies are highly unlikely to have a high degree of usefulness to law enforcement. Listed companies and their subsidiaries are subject to significant federal and state regulation as well as to the self-regulatory compliance obligations of the Financial Industry Regulatory Authority. With this level of external and internal regulation, there is a low likelihood that listed companies could be conduits for illegal money laundering or terrorist financing, and enforcement experience does not contradict this view.

The distinction between "mandatory" and "discretionary" or "Phase I" and "Phase II" customers was based on Congress' and FinCEN's recognition that the certain customers posed inherently less risk than others, and the exemption regime varied accordingly. Without proof that listed companies present a heightened risk of money laundering or terrorist financing, ABA believes that there is no reason to exclude listed companies from the relief proposed for other Phase I customers. If FinCEN's intent is indeed simplification of the exemption process in order to encourage its use and to reduce the number of currency transaction report filings on routine business activity, ABA respectfully urges FinCEN not to exclude listed companies from the proposed relief. Moreover, by excluding listed companies and their subsidiaries from this relief, FinCEN significantly curtails the limited probable benefit of the proposed regulatory amendments. The annual volume of CTRs being filed on banks, governments, or agencies exercising governmental authority is approximately 112,000, or less than 1% of the total number of CTRs filed. Therefore, the impact these changes will have on the total number of CTRs filed each year will be quite limited even if utilized to their maximum potential.

FinCEN bases its decision to continue to require an annual review of listed companies on its belief that listed companies, in contrast to banks and governmental entities, "are more likely to reorganize or enter new lines of business." ABA notes that withholding Phase I streamlined treatment from listed companies because they may "reorganize or enter new lines of business" is a non-sequitur. Listed companies reorganize or add business lines without changing their listed status. It is their listed status—not their corporate intricacies or business components—that subjects them to existing regulatory review regimes, and these regimes in turn entitle them to exemption. Therefore, there is no need to require banks to conduct a mandatory annual review of all public companies, just as FinCEN recognizes that there is no need to require an annual review of banks and government agencies.

Also, the GAO Study found that "if such a Phase I exempted entity was 'delisted,' the relevant bank could immediately exempt the customer from CTR reporting requirements pursuant to a Phase II exemption providing the necessary requirements were met."[8] Thus, the GAO correctly recognizes that the loss of listed status is

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[8] *Bank Secrecy Act: Increased Use of Exemption Provisions Could Reduce Currency Transaction Reporting While Maintaining Usefulness to Law Enforcement Efforts, supra* at 48.

generally immaterial to an entity's exemptibility; instead, in most instances it only affects whether an entity is eligible for Phase I or Phase II exemption.

The elimination of the requirement to file Form 110 to exempt certain Phase I customer offers only illusory relief. The filing of Form 110 is merely a ministerial task; the true burden lies in documenting the basis for the exemption, and in its discussion of the proposed amendment to section 103.22(d)(3)(ii) FinCEN makes it clear that this documentation will still be required. After announcing the elimination of the requirement for filing Form 110, FinCEN states in footnote 29:

> Even though FinCEN Form 110 would not be filed for these Phase I customers, a depository institution will continue to be required to take such steps to assure itself that the Phase I customer is an exempt person and to document the basis of its conclusions that a reasonable and prudent bank would take and document to protect itself from loan or other fraud or loss based on misidentification of a person's status. *See* 31 CFR 103.22(d)(6)(i).

ABA member banks report that the duty to document the basis for an exemption—coupled with the regulatory risk inherent in exposure of such documentation to further regulatory scrutiny—is the basis for a decision not to file an exemption, not the fact that Form 110 must be completed and filed. As a result, ABA believes that standing alone, the proposed elimination of the requirement to file Form 110 for certain Phase I customers will not encourage significant additional use of the exemption process. ABA urges FinCEN to make it clear in the final rule that a bank need not create an independent file to document the basis for exemption of a Phase I customer. Because Banks are required to collect customer identification information at account opening, and this information is available to examiners on request, banks should be permitted to rely on it as they make their exemption decisions without creating a duplicative file for examiner review.

It is time for FinCEN to acknowledge the distinction Congress drew between mandatory and discretionary exemptions and to establish bright line tests for Phase I exemption eligibility. The Phase I exemption process should be straightforward—the simple determination that a customer falls within one of the four categories. Moreover, banks should be able to rely on their Customer Identification Program (CIP) file documentation to demonstrate Phase I eligibility, including listed company eligibility, without the need for further duplicative documentation.

The proposed Phase II amendments increase complexity and add to compliance burdens

The GAO study reports that less than 49% of financial institutions filed exemptions for eligible Phase II customers;[9] therefore, the proposed rulemaking claims to simplify the Phase II exemption process in order to encourage banks to exempt

[9] *Bank Secrecy Act: Increased Use of Exemption Provisions Could Reduce Currency Transaction Reporting While Maintaining Usefulness to Law Enforcement Efforts, supra* at 41.

eligible Phase II customers. ABA believes, however, that FinCEN's proposed amendments to the exemption regime for Phase II customers are an example of the failure of incremental changes to result in real reform. ABA believes that the regulatory amendments do not address the true compliance burdens; instead, they simply replace one duty with another and even threaten to add to the existing obligations. In fact, several ABA members have contacted us to say the additional new burdens may cause them to use exemptions *less often* because they provide for less certainty and more opportunity for examiner second-guessing about what constitutes adequate qualifying documentation.

For example, although FinCEN proposes to eliminate the 12-month waiting period before an initial exemption decision may be made, it seeks to replace it with either a subjective new "risk-based" analysis or another arbitrary time period. ABA believes that neither alternative alone will bring about a significant increase in use of the exemption process. Although ABA agrees that the time an account has been opened is one factor a bank may consider as it decides whether to exempt a particular customer, ABA cautions FinCEN against imposing another compliance hurdle to the exemption process— the requirement that banks conduct a formulaic "risk-based assessment of the transactional activity of that customer." In addition to the burden imposed by adding another compliance test, the subjective nature of such a risk assessment would likely only further deter financial institutions from making use of the exemption. The written record of each determination will be subject to regulatory review, carrying the threat of examiner criticism and the possible imposition of civil money penalties or back-filing orders.

Moreover, ABA fears that the following language in the proposed rulemaking suggests FinCEN's intent to require banks to document this risk-assessment:

> The risk-based analysis requirement proposed in this notice should be read as a *separate, specific rule of paragraph (d),* and is not meant to supersede the operating rules of existing 31 CFR 103.22(d)(6)(i) subject to paragraph (d)(emphasis added).

Although the quoted language is confusing, it appears to require documentation of the risk- assessment in addition to section 103.22(d)(6)(i)'s *existing* requirement that a bank "must take such steps to assure itself that a person is an exempt person…, to document the basis for its conclusions, and document its compliance with the terms of this paragraph (d)." [10] ABA believes that to impose an additional record-keeping requirement to the already cumbersome process of documenting eligibility will further discourage banks from exempting Phase II customers. Accordingly, ABA urges FinCEN not to adopt a risk-based requirement, but rather to rely on the existing standard under section 103.22(d)(6)(i)—and to point out that this standard can be satisfied by existing CIP or other due diligence activity without creating a separate file.

As an alternative to a new risk-based test, FinCEN proposes the adoption of a minimum period of time—two months—that must pass before a bank may exempt a

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[10] *See* 31 C.F.R. §103.22(d)(6)(i).

customer. ABA believes that such a two-month period can be part of a bright-line fall back[11] and supports its adoption. However, the regulation should also allow a bank to exempt an eligible customer at any time, including at account opening, if its knowledge of the customer and its expected business activities demonstrate that its anticipated currency transactions will likely be consistent with the conduct of legitimate and routine business operations.

ABA respectfully urges FinCEN to recognize that banks have demonstrated a sincere commitment to the battle against money laundering and terrorist financing. Banks have sophisticated policies and procedures in place to comply with the BSA and the USA PATRIOT Act's record-keeping and reporting requirements, and they are acutely aware of the consequences—both to their institution and to society—of non-compliance. Therefore, ABA urges FinCEN to give deference to a bank's decision to exempt an eligible Phase II customer and to resist the temptation to impose burdensome risk-assessment requirements or arbitrary time frames as conditions precedent to exemption. Although ABA member banks seek the flexibility to exempt a Phase II customer at any time, they report that they will make exemption decisions judiciously, carefully considering the nature of the business and their familiarity with it. They also report no interest in exempting an unknown customer.

Another piece of the proposed rulemaking is FinCEN's proposed elimination of section 103.22(d)(5), the section of the Regulation that requires depository institutions to file a biennial designation of exempt person for non-listed and payroll customers. ABA supports the elimination of this unnecessary filing. However, ABA believes that FinCEN's proposed addition of a duty to notify FinCEN of any "change in control" of a Phase II customer that a bank "knows of, or should know of"[12] will be an even greater disincentive to use of the exemption process than the biennial review process has been. First, nothing in the proposed rule-making defines what constitutes a "change in control;" whether every change in control is to be reported to FinCEN, or just those that effect eligibility; or the documentation that will be required to demonstrate such events. Indeed, even the relevance of information about a change in control is unclear.

Second, the rulemaking solicits comment on whether FinCEN should require notification of a change in control within 30 days of the change, or whether notification should be accomplished by "filing an amended FinCEN Form 110 by March 15 of the calendar year following every second year in which the bank knew or should have known of the change in control." ABA respectfully suggests that either notification requirement will impose significant compliance disincentives. Member banks report that requiring notification within 30 days of a status change would effectively bar Phase II exemptions. Compliance with a 30-day reporting requirement would require banks to implement expensive new monitoring and reporting procedures. In addition, the subjective nature of the trigger—determining

[11] FinCEN requests comment on the number of transactions that should represent "frequent" activity in a two-month period. ABA believes that, given 8 transactions in a year currently constitute "frequent," it would be enough to say that no more than two in any two-month period be demonstrated for a bright-line test of qualification.

[12] *See* 31 C.F.R. §103.22(d)(4).

whether or when a bank "should have known" of the customer status change—introduces prohibitive regulatory risk to the Phase II exemption process.

ABA member banks also point out that the implementation of the alternative proposal—requiring a bank to report status changes by March 15 of the second year following a change— is essentially the re-implementation of the biennial renewal process. ABA notes that because FinCEN will continue to require an annual review of all Phase II customers and any status changes will be identified and acted upon during that review, either status change notification requirement will impose an unnecessary and significant disincentive to the Phase II exemption process. Therefore, ABA respectfully urges FinCEN to remove section 103.22(d)(5) without imposing additional compliance obligations.

Finally, FinCEN proposes to amend re-designated section 103.22(d)(9) to require banks to file a revocation of exemption when a bank decides that a customer is no longer eligible. ABA objects to this proposal. Mandating the filing of a revocation form—currently a voluntary filing—is incompatible with FinCEN's stated intent of simplifying and streamlining the exemption process. The resumption of CTR filings provides notice to FinCEN that a bank has decided to revoke an exemption, and to require that banks file Form 110 only adds another unnecessary step to the exemption regime.[13] Nothing on the form provides additional information to FinCEN about the basis for a decision to revoke a customer's exemption.

The rulemaking ignores the primary disincentives of the Phase II exemption process

A notable failure of the proposed amendments is that they do not address the most significant barrier to the exemption process, the problem of determining and documenting eligibility for Phase II customers. The GAO Study reported that 70% of institutions cited eligibility determinations as the grounds for a decision not to exempt a Phase II customer;[14] these banks reported that calculating the percentage of a business' income that is derived from a particular business line is time consuming, confusing, expensive, and fraught with uncertainty.[15] The research required to make these determinations typically involves a sophisticated analysis of tax returns or financial statements by an individual qualified to interpret these documents. Moreover, the eligibility determination, including the documents relied upon, is subject to regulatory review and criticism, and as the GAO found, regulator expectation for documentation has not been standardized. Therefore, judgments about acceptability often vary significantly, further adding to the regulatory risk involved with exemption decisions.[16]

[13] In the proposed rulemaking, FinCEN does not state that it will create a new form banks are to use to announce revocation decisions. Presumably, FinCEN contemplates the continued use of Form 110.
[14] *Bank Secrecy Act: Increased Use of Exemption Provisions Could Reduce Currency Transaction Reporting While Maintaining Usefulness to Law Enforcement Efforts, supra* at 94.
[15] *Id*. at 42.
[16] *Id.* at 43, 53.

These issues resurface each year as banks struggle to document the annual review of Phase II customers. Member banks report wide variation in exam expectation for documentation of continued eligibility and for demonstrating that all exempt accounts are monitored for suspicious activity. The regulation calls for an annual review of eligibility and for the certification that monitoring systems are in place. Exam expectation, however, has turned the annual review into a time consuming and burdensome process that discourages Phase II exemptions. Not only must banks struggle with re-verifying eligibility; they are also expected to document this review thoroughly as well as their review of the suspicious activity monitoring process. To the extent that FinCEN intends to retain the annual review, ABA urges FinCEN to articulate clearly its intent that the annual review is in fact a *review* of eligibility and that a bank's certification that suspicious activity monitoring systems are in place is sufficient.

The GAO noted that eligibility determinations were a significant disincentive to the exemption process, and it encouraged FinCEN to provide additional guidance and training. In the current rulemaking, however, FinCEN fails even to mention these disincentives to the Phase II exemption process, and the industry is left with a regulatory "solution" that ignores the primary reason that depository institutions do not exempt their customers. ABA believes that FinCEN's silence underscores the failure of the current effort to provide genuine, useable improvement in the CTR exemption process. Incremental amendments and training cannot fix a regulation that is so fundamentally flawed by its complexity. Indeed, the proposed amendments threaten to create new compliance burdens and disincentives without even addressing the eligibility issues that preclude the vast majority of exemptions.

As it has since 2005, ABA urges FinCEN to abandon the failed exemption regime and to work with the banking industry to implement a simple and streamlined exemption process. By adopting a seasoned customer exemption, the flood of unnecessary CTR filings will be addressed, and banks and law enforcement will be free to focus their limited time and resources on detecting and reporting genuinely suspicious currency transactions.

If you have any questions about these comments, please contact Virginia O'Neill at (202) 663- 5073 or via e-mail at voneill@aba.com.

Respectfully submitted,

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