Federal Deposit Insurance Corporation
550 17th Street NW, Washington, D.C. 20429-9990

Insurance Corporation`

MEMORANDUM TO: Board of Directors

FROM: Doreen R. Eberley
Director, Division of Risk Management Supervision

SUBJECT: Proposed Amendments to Bank Secrecy Act Compliance Rule (12 C.F.R. Part 326)

SUMMARY

The attached, proposed rule would revise and republish the FDIC's Bank Secrecy Act (BSA) compliance program rule at 12 C.F.R. Part 326 with a new Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) compliance program rule to align with the rule concurrently proposed by the Financial Crimes Enforcement Network (FinCEN). Pursuant to the Anti-Money Laundering Act of 2020 (AML Act),[1] FinCEN is revising and replacing its BSA/anti-money laundering (AML) program rules with new AML/CFT program rules to incorporate consideration of new AML/CFT Priorities. The proposed rule and attached preamble would be issued jointly by the FDIC, the Board of Governors of the Federal Reserve System (FRB), the Office of the Comptroller of the Currency (OCC), and the National Credit Union Administration (NCUA), (collectively, the Agencies), in coordination and consultation with the Department of the Treasury (Treasury), including FinCEN. The FDIC and the other Agencies last amended their BSA compliance program rules in 2003, to incorporate Customer Identification Program requirements. The FDIC and the other Agencies intend to take this opportunity to incorporate other BSA requirements and propose additional changes to codify longstanding supervisory expectations.

Accordingly, staff recommends that the Board of Directors (Board) authorize for publication in the *Federal Register* the attached notice of proposed rulemaking to revise and republish subpart B of part 326, revise the heading of part 326, and revise the authority citation for the part.

Concur: ________________________
Harrel Pettway
General Counsel

[1] Anti-Money Laundering Act of 2020, Pub. L. No.116-283, §§ 6001-6511, 134 Stat. 4547-4633 (2021).

BACKGROUND

History of Anti-Money Laundering/Countering the Financing of Terrorism (AML/CFT) Programs for the Agencies

The Money Laundering Control Act of 1986 (MLCA)[2] amended 12 U.S.C. 1818(s) and 12 U.S.C. 1786(q) (Sections 8(s) of the Federal Deposit Insurance Act and 206(q) of the Federal Credit Union Act, respectively) to require the Agencies to issue regulations to "establish and maintain procedures reasonably designed to assure and monitor the compliance" of their supervised institutions with the requirements of the BSA. Consistent with the MLCA, on January 27, 1987, all of the then-Federal bank regulatory agencies issued substantially similar regulations requiring their supervised institutions to develop procedures for BSA compliance.[3] The Agencies' respective BSA compliance program rules required banks to implement a program reasonably designed to assure and monitor compliance with recordkeeping and reporting requirements set forth in the BSA and its implementing regulations.[4]

The Annunzio-Wylie Anti-Money Laundering Act of 1992 (Annunzio-Wylie Act),[5] subsequently amended the BSA by authorizing the Treasury Secretary to issue regulations requiring financial institutions, as defined in the BSA, to maintain an anti-money laundering (AML) program.[6] The "minimum standards" set forth in the statute were substantially similar to the standards previously set forth by the Agencies in their respective BSA compliance program rules, including the four components.[7] Before 2002, BSA compliance program rules for banks with a federal functional regulator were administered exclusively by the Agencies under Sections 8(s) and 206(q). The Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act)[8] further amended the BSA, by, among other things, establishing FinCEN's statutory role as the regulator and administrator of the BSA[9] and mandating financial institutions subject to the BSA to maintain AML programs consistent with the minimum standards established by the Annunzio-Wylie Act.[10] FinCEN, in 2002, issued a rule that deemed banks supervised by the Agencies to be in compliance with the BSA if they satisfied the requirements of the Agencies' BSA compliance program rules.[11]

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[2] Pub. L. No. 99–570, § 5318, 100 Stat. 3207, 3207-27 (1986).
[3] 52 FR 2858 (Jan. 27, 1987).
[4] 12 CFR 208.63(b), 211.5(m), and 211.24(j) (Federal Reserve); 12 CFR 326.8(b) (FDIC); 12 CFR 748.2 (NCUA); 12 CFR 21.21(c) (OCC).
[5] Title XV of Pub. L. No. 102–550, 106 Stat. 3672 (1992).
[6] *Id*. at section 1517.
[7] The minimum standards for an AML program set forth in the Annunzio-Wylie Act, and codified at 31 U.S.C. 5318(h), include: ''(A) the development of internal policies, procedures, and controls, (B) the designation of a compliance officer, (C) an ongoing employee training program, and (D) an independent audit function to test programs.''
[8] Pub. L. No. 107–56, 115 Stat. 272 (2001).
[9] 31 U.S.C. 310(b)(2)(I), as added by section 361 of the USA PATRIOT Act (Pub. L. No. 107–]56).
[10] 31 U.S.C. 5318(h), as added by section 352 of the USA PATRIOT Act (Pub. L. No. 107–56) became effective on April 24, 2002.
[11] 67 FR 21110 (Apr. 29, 2002).

Although in practice FinCEN and the Agencies' compliance program rules operated together, since the USA PATRIOT Act, banks have been required to maintain compliance programs pursuant to separate authorities administered by FinCEN under Title 31[12] and the Agencies under Sections 8(s) and 206(q). With the exception of the customer due diligence (CDD) requirements, FinCEN's rule was substantially similar to the Agencies' rules, and banks must currently comply with both FinCEN and the Agencies' compliance program rules.

The Anti-Money Laundering Act of 2020

On January 1, 2021, Congress enacted the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, of which the AML Act was a component.[13] Section 6101(b) of the AML Act made several changes to the BSA, including, but not limited to: (1) inserting countering the financing of terrorism (CFT) as a term in the statutory compliance program requirement; (2) requiring the Secretary of the Treasury to establish and make public the AML/CFT Priorities and to promulgate regulations, as appropriate; (3) providing that a bank's review of the AML/CFT Priorities and the incorporation of those priorities, as appropriate, into its risk-based program be included as a measure on which a bank is supervised and examined; (4) requiring the duty to establish, maintain, and enforce an AML/CFT program to be the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to, oversight and supervision by the Secretary of the Treasury and the appropriate federal functional regulator; and (5) requiring the Secretary of the Treasury and federal functional regulators to take into account certain factors when prescribing the minimum AML/CFT standards and examining for compliance with those standards.

PROPOSED AMENDMENTS

The proposed rule would revise and replace the BSA compliance program rule for banks supervised by each of the Agencies in a way that aligns with the rule concurrently proposed by FinCEN, including changing the terminology used to describe them. As explained below, pursuant to the AML Act, FinCEN is revising and replacing its BSA/AML program rules to incorporate the AML/CFT Priorities. Other changes proposed by FinCEN to the BSA/AML program rules are not required by the AML Act but are intended to clarify regulatory requirements. The Agencies have independent authority to prescribe regulations requiring banks to establish and maintain procedures reasonably designed to assure and monitor the compliance of such banks with the requirements of subchapter II of chapter 53 of title 31, under 12 U.S.C. 1818(s) and 12 U.S.C. 1786(q), and are proposing to amend their rules concurrently. Although not required by the AML Act, the Agencies are revising and replacing their BSA compliance program regulations to, among other reasons, address how the AML/CFT Priorities will be incorporated into banks' AML/CFT compliance programs. The Agencies' intent is to have their program requirements for banks remain consistent with those imposed by FinCEN. Further, with consistent regulatory text, banks will not be subject to any additional burden or confusion from needing to comply with differing requirements between FinCEN and the Agencies. The

[12] 67 FR 21110 (Apr. 29, 2002), formerly codified at 31 CFR 103.120(b) and now codified at 31 CFR 1020.210(a)(3).
[13] Pub. L. No. 116-283, 134 Stat. 3388 (2021).

proposed regulation text was subject to significant negotiation with FinCEN and Treasury and has been agreed to at an overview level by agency principals.

The proposed rule incorporates a risk assessment process that requires, among other things, consideration of the national AML/CFT Priorities published by FinCEN. The proposed rule also would add CDD requirements to reflect prior amendments to FinCEN's rule and, concurrently with FinCEN, clarifying and other amendments to codify longstanding supervisory expectations and conform to AML Act changes.

A section-by-section analysis of specific changes is described below:

Proposed Paragraph (a) – Purpose

(a) Purpose. The purpose of this section is to ensure that all FDIC-supervised institutions implement an effective, risk-based, and reasonably-designed AML/CFT program to identify, manage, and mitigate illicit finance activity risks that: complies with the requirements of subchapter II of chapter 53 of title 31, United States Code, and the implementing regulations promulgated thereunder by the Department of the Treasury at 31 CFR chapter X (Bank Secrecy Act); focuses attention and resources in a manner consistent with the risk profile of the FDIC-supervised institution; may include consideration and evaluation of innovative approaches to meet its AML/CFT compliance obligations; provides highly useful reports or records to relevant government authorities; protects the financial system of the United States from criminal abuse; and safeguards the national security of the United States, including by preventing the flow of illicit funds in the financial system.

FinCEN and the Agencies are proposing a statement describing the purpose of an AML/CFT program rule. The proposed statement of purpose is not intended to establish new obligations separate and apart from the specific requirements set out for banks or impose additional costs or burdens. Rather, this language is intended to summarize the overarching goals of banks' effective, risk-based, and reasonably designed AML/CFT programs.

Proposed Paragraph (b)—Establishment and Contents of an AML/CFT Program

(b) Establishment and contents of an AML/CFT program.
(1) General. An FDIC-supervised institution must establish, implement, and maintain an effective, risk-based, and reasonably designed AML/CFT program to ensure and monitor compliance with the requirements set forth in subchapter II of chapter 53 of title 31, United States Code, and the implementing regulations issued by the Department of the Treasury at 31 CFR Chapter X.

(2) AML/CFT Program. An effective, risk-based, and reasonably designed AML/CFT program focuses attention and resources in a manner consistent with the FDIC-supervised institution's risk profile that takes into account higher-risk and lower-risk customers and activities and must, at a minimum:

Paragraph (b)(1) of the proposed rule introduces the general requirement that "An FDIC-supervised institution must establish, implement, and maintain an effective, risk-based, and reasonably designed AML/CFT program…" The Agencies are replacing "BSA compliance program" with the phrase "AML/CFT program" to align with the AML Act. The inclusion of "CFT" in the program rule also does not establish new obligations or impose additional costs or burdens as the USA PATRIOT Act already requires financial institutions to account for risks related to terrorist financing.

Banks are currently required to maintain a "reasonably designed" BSA compliance program. The proposed rule would add the terms "effective" and "risk-based" to the text of the existing program requirement. The addition of the term "effective" to describe the AML/CFT program requirement more directly reflects this purpose and would make clear that the Agencies evaluate the effectiveness of the implemented program and not only its design. As the addition of the term "effective" is a clarifying amendment, it would not be a substantive change for banks.[14] The addition of the term "risk-based" also reinforces the longstanding position of the Agencies, which have consistently stated that AML/CFT programs should be risk based.

Paragraph (b)(2) describes the contents of an AML/CFT program as follows: "An effective, risk-based, and reasonably designed AML/CFT program focuses attention and resources in a manner consistent with the FDIC-supervised institution's risk profile that takes into account higher-risk and lower-risk customers and activities…" followed by setting forth the minimum requirements for such a program. This proposed requirement reflects the longstanding industry practice and expectation of the Agencies that AML/CFT programs be risk based. Implicit in the existing requirement that banks implement a program "reasonably designed" to ensure and monitor compliance with the BSA is the expectation that banks allocate their resources according to their money laundering and terrorist financing (ML/TF) risk. Moreover, as part of existing CDD and suspicious activity monitoring requirements, banks already consider risk when evaluating customers and activities.

<u>Proposed Paragraph (b)(2)(i) – Risk Assessment Component</u>

(i) Establish a risk assessment process that serves as the basis for the FDIC-supervised institution's AML/CFT program, including implementation of the components required under paragraphs (b)(2)(ii)-(vi) of this section. The risk assessment process must:

(A) Identify, evaluate, and document the FDIC-supervised institution's money laundering, terrorist financing, and other illicit finance activity risks, including consideration of the following:

(1) The AML/CFT Priorities issued pursuant to 31 U.S.C. § 5318(h)(4), as appropriate;
(2) The money laundering, terrorist financing, and other illicit finance activity risks of the FDIC-supervised institution based on the FDIC-supervised institution's business activities, including products, services, distribution channels, customers, intermediaries, and geographic locations; and

[14] 31 U.S.C. 5318(h)(2)(B)(iii).

(3) Reports filed by the FDIC-supervised institution pursuant to the Bank Secrecy Act;

(B) Provide for updating the risk assessment using the process required under paragraph (b)(2)(i) of this section on a periodic basis, including at a minimum, when there are material changes to the FDIC-supervised institution's money laundering, terrorist financing, and other illicit finance activity risks;

FinCEN is amending its program rules to incorporate the national AML/CFT Priorities. Consistent with FinCEN's proposal, the Agencies are proposing to require a risk assessment process as the means to incorporate the AML/CFT Priorities. This proposed subparagraph would require banks to establish a risk assessment process that serves as the basis for a bank's AML/CFT program that implements the components described in paragraphs (b)(2)(ii-vi).

Agencies have traditionally viewed a risk assessment as a critical tool of a reasonably designed BSA compliance program; a bank cannot implement a reasonably designed program to achieve compliance with the BSA unless it understands its risk profile. The inclusion of a risk assessment process that serves as the basis of a risk-based AML/CFT program also is supported by several provisions of the AML Act, including section 6101(b), which states that AML/CFT programs should be risk-based.[15]

The objective of requiring the risk assessment process to serve as the basis for a bank's AML/CFT program would be to promote programs that are appropriately risk-based and tailored to the AML/CFT Priorities and a bank's risk profile. Most banks already design their BSA compliance programs based on their assessment of ML/TF risk.

The proposed risk assessment process would conform to the changes in FinCEN's proposed AML/CFT program and standardize the risk assessment process by requiring banks to identify, evaluate, and document their ML, TF, and other illicit finance activity risks. Banks must consider: (1) the AML/CFT Priorities; (2) the ML/TF and other illicit finance activity risks of the bank based on its business activities, including products, services, distribution channels, customers, intermediaries, and geographic locations; and (3) reports filed pursuant to the BSA and its implementing regulations.

The proposed rule would include a new requirement under paragraph (b)(2)(i)(B) that banks update their risk assessments "on a periodic basis, including, at a minimum, when there are material changes to the" bank's ML/TF or other illicit finance activity risks. Current bank practices generally include updating risk assessments (in whole or in part) to reflect changes in the bank's products, services, customers, and geographic locations and to remain an accurate reflection of the bank's ML/TF and other illicit financial activity risks. Periodic updates of the risk assessment assist banks in maintaining a risk-based AML/CFT program. For purposes of this proposed rule, a material change would be one that significantly alters a bank's exposure to ML/TF risks, such as a significant change in business activities.

[15] 31 U.S.C. 5318(h)(2)(B)(iv)(II).

Proposed Paragraph (b)(2)(ii) –Internal Policies, Procedures, and Controls

(ii) Reasonably manage and mitigate money laundering, terrorist financing, and other illicit finance activity risks through internal policies, procedures, and controls that are commensurate with those risks and ensure ongoing compliance with the Bank Secrecy Act and its implementing regulations Such internal policies, procedures, and controls may provide for an FDIC-supervised institution's consideration, evaluation, and, as warranted by the FDIC-supervised institution's risk profile and AML/CFT program, implementation of innovative approaches to meet compliance obligations pursuant to the Bank Secrecy Act and its implementing regulations.

The Agencies currently require BSA compliance programs to "provide for a system of internal controls to assure ongoing compliance" with the BSA. The proposed paragraph (b)(2)(ii) would amend the existing internal controls component to require that a bank "reasonably manage and mitigate money laundering, terrorist financing, and other illicit finance activity risks through internal policies, procedures, and controls that are commensurate with those risks and ensure ongoing compliance with the requirements of the Bank Secrecy Act." The Agencies generally expect banks to implement the proposed rule in a similar manner to the current rule.

The proposed rule would encourage, but would not require, banks to consider, evaluate, and, as appropriate, implement innovative approaches to meet compliance obligations pursuant to the BSA. This provision should not be viewed as restricting or limiting the current ability of banks to consider or engage in responsible innovation consistent with the December 2018 joint statement issued by FinCEN and the Agencies that encouraged banks to take innovative approaches to combat ML/TF and other illicit finance threats.

Proposed Paragraph (b)(2)(iii) –AML/CFT Officer

(iii) Designate one or more qualified individuals to be responsible for coordinating and monitoring day-to-day compliance;

Paragraph (b)(2)(iii) of the proposed rule adds the word "qualified" to the regulation text but is not intended to substantively change the current requirement concerning a bank's BSA officer. Inherent in the statutory requirement that a bank designate a compliance officer as part of a program that is "reasonably designed" to achieve compliance with the BSA and its implementing regulations is the expectation that the designated individual is qualified, including the ability to coordinate and monitor compliance with the BSA and its implementing regulations.

Proposed Paragraph (b)(2)(iv) – Training

(iv) Include an ongoing employee training program; and

The proposed paragraph (b)(2)(iv) would amend the existing training requirement in the Agencies' AML/CFT compliance program rules to mirror 31 U.S.C. 5318(h)(1)(C) and clarify that banks must have an "ongoing" employee training program. The Agencies view this to be a clarifying rather than substantive change. The proposed rule makes clear that AML/CFT

programs must include an ongoing program in which AML/CFT training is provided to appropriate personnel.

Proposed Paragraph (b)(2)(v) – Independent Testing

(v) Include independent, periodic AML/CFT program testing to be conducted by qualified FDIC-supervised institution personnel or by a qualified outside party.

The proposed rule would require each bank's program to include independent, periodic AML/CFT program testing by clarifying that the testing is to be conducted by qualified personnel of the bank or by a qualified outside party. The Agencies consider these changes to be consistent with longstanding requirements for independent testing and not substantive.

Proposed Paragraph (b)(2)(vi) – Customer Due Diligence

(vi) Include appropriate risk-based procedures for conducting ongoing customer due diligence, to include, but not be limited to:

(A) Understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile; and
(B) Conducting ongoing monitoring to identify and report suspicious transactions and to maintain and update customer information. For purposes of this paragraph (b)(2)(vi)(B), customer information must include information regarding the beneficial owners of legal entity customers (as defined in 31 CFR § 1010.230).

The proposed rule would add CDD as a required component of the Agencies' AML/CFT program rule. CDD is currently a required component in FinCEN's AML program rule, and, therefore, banks are already required to comply with CDD under FinCEN's rules. The inclusion of CDD in the proposed rules for the Agencies would mirror FinCEN's existing rule and reflect longstanding supervisory expectations of the Agencies. Well before FinCEN amended its AML program rule to expressly include the CDD component requirement, the Agencies had considered CDD an integral component of a risk-based program, enabling the bank to understand its customers and its customers' activity to better identify suspicious activity.

Adding the CDD component to the Agencies' AML/CFT program rule at paragraph (b)(2)(vi) will eliminate confusion for banks concerning the current differences with FinCEN's AML/CFT program rule. Because banks must already comply with FinCEN CDD's component requirement, the proposed change should not alter current compliance practices.

Proposed Paragraph (c) – Board Oversight

(c) Board Oversight. The AML/CFT program and each of its components, as required under paragraphs (b)(2)(i)-(vi) of this section, must be documented and approved by the FDIC-supervised institution's board of directors or, if the FDIC-supervised institution does not have a board of directors, an equivalent governing body. The AML/CFT program must be subject to oversight by the FDIC-supervised institution's board of directors, or equivalent governing body.

The Agencies' BSA compliance program rules currently require banks to have written programs approved by the board of directors. The proposed rule would maintain this requirement but move it to a separate subsection and add clarifying text to harmonize the language with FinCEN's proposed rule. The Agencies do not intend for there to be a substantive change from the current requirement. While banks already must obtain board approval for their BSA compliance programs, the proposed rule also would require that the AML/CFT program be subject to board oversight, or oversight of an equivalent governing body.

Proposed Paragraph (d) – Presence in the United States

(d) Presence in the United States. The duty to establish, maintain, and enforce the AML/CFT program must remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to the oversight and supervision by the FDIC.

The proposed rule would incorporate the statutory requirement codified at 31 U.S.C. 5318(h)(5) into the AML/CFT program rule by restating that the duty to establish, maintain, and enforce the AML/CFT program must remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to the oversight and supervision by, the FDIC.

Proposed Paragraph (e) — Customer Identification Program

(e) Customer identification program. Each institution is subject to the requirements of 31 U.S.C. § 5318(l) and the implementing regulations jointly promulgated by the FDIC and the Department of the Treasury at 31 CFR § 1020.220, which require a customer identification program to be implemented as part of the AML/CFT program required under this section.

The proposed rule would maintain the current Customer Identification Program requirements but move it to a separate section. The Agencies propose minor, non-substantive updates to reference the "AML/CFT" terminology and harmonize the language between the Agencies to "require a customer identification program to be implemented as part of the AML/CFT program." These technical changes do not establish new obligations.

REQUEST FOR COMMENT

The FDIC seeks comments on all facets of the proposed rule and invites specific comments on the proposed rule including such items as: whether banks could leverage their existing risk assessment process; the time frame for banks to update their risk assessments using the process proposed in the rule; factors a bank might consider when determining the frequency of updating its risk assessment using the process proposed in the rule; whether the rule and/or preamble warrant further explanation of the term "material" used to indicate when an AML/CFT program's risk assessment would need to be reviewed and updated; and what approaches would be appropriate to demonstrate that attention and resources are focused appropriately and consistent with the bank's risk profile.

Regarding innovation, the proposed rule encourages, but does not require, the consideration of

innovative approaches to help banks meet compliance obligations pursuant to the BSA. Comments are requested on the benefits banks currently realize, or anticipate, from these innovative approaches and whether alternative methods for encouraging innovation should be considered in lieu of a regulatory provision.

Comments are also invited on the scope of the statutory requirement that individuals with a duty to "establish, maintain and enforce" the AML/CFT program remain in the United States. Specifically, comments are invited on whether further clarification is needed on the meaning of the phrase "establish, maintain and enforce"; the range of individuals covered by the requirement to remain in the United States; and whether this should be interpreted to mean they are performing their relevant duties while physically present in the United States.

Additionally, comments are sought on proposed rule changes regarding: whether the inclusion of the term "qualified" for persons serving as AML/CFT officers or conducting testing of the AML/CFT program is sufficiently clear and the potential costs and burdens of complying with the proposed rule.

RECOMMENDATION

Staff recommends that the FDIC Board of Directors authorize for publication in the *Federal Register* the attached notice of proposed rulemaking to revise and republish subpart B of Part 326, revise the heading of part 326, and revise the authority citation for the part.

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