



GLOBAL FINANCIAL INTEGRITY

Policy Division  
Financial Crimes Enforcement Network  
P.O. Box 39  
Vienna, VA 22183

**Submitted Electronically via: <http://www.regulations.gov>**

October 3, 2014

RIN: 1506-AB25  
Docket Number FINCEN-2014-0001

Global Financial Integrity is pleased to provide the following submission in response to the FinCEN notice of proposed rulemaking (NPRM) with respect to Customer Due Diligence Procedures for Financial Institutions (RIN 1506-AB25).

Global Financial Integrity (GFI) is a non-profit, Washington, DC-based research and advocacy organization, which produces high-caliber analyses of illicit financial flows, advises developing country governments on effective policy solutions, and promotes pragmatic transparency measures in the international financial system as a means to global development and security.

Every year, roughly \$1 trillion flows illegally out of developing countries due to crime, corruption, and tax evasion—close to ten times the amount of foreign aid flowing into these same economies. Many developing countries have failed to grow past the point where foreign aid is no longer necessary. For years, development economists were puzzled by the lack of growth in developing economies despite large aid inflows.

This flow of illicit money is facilitated in part by the creation and use of anonymous companies and the bank accounts that these companies are able to open. This proposed rulemaking can be a significant step toward ensuring that the U.S. financial system is not open for this type of business.

If you have any questions with respect to this submission, please do not hesitate to contact me.

Kind regards,

Heather Lowe  
Legal Counsel & Director of Government Affairs

---

1100 17th Street, NW, Suite 505 | Washington, DC | 20036 | USA  
Tel. +1 (202) 293-0740 | Fax. +1 (202) 293-1720 | [www.gfintegrity.org](http://www.gfintegrity.org)

President: Raymond Baker

Managing Director: Tom Cardamone

Board: Lord Daniel Brennan (Chair), Dr. Rafael Espada (Vice Chair), Dr. Lester A. Myers (Secretary-Treasurer), Thomas Pogge, Raymond Baker

Policy Division  
Financial Crimes Enforcement Network  
P.O. Box 39  
Vienna, VA 22183

Submitted Electronically via: <http://www.regulations.gov>

October 3, 2014

**RIN: 1506-AB25**

**Docket Number FINCEN-2014-0001**

We appreciate the opportunity to comment on the FinCEN notice of proposed rulemaking (NPRM) with respect to Customer Due Diligence Procedures for Financial Institutions (RIN 1506-AB25). We look forward to working with FinCEN to create a strong rule that can be a helpful global reference point for other governments in order to make it easier for internationally operating financial institutions to comply with CDD obligations and, most importantly, make it more difficult for criminals to use their services.

We would like to say at the outset that we support FinCEN's commitment to address the use of anonymous entities in international crime, and our goal is to make the costs and efforts expended by financial institutions (FIs) under this regulation as effective as possible. We also agree with the Government's statement that "[b]eneficial ownership information is a means of building a more comprehensive risk profile" and appreciate the inclusion of the additional two points of regulatory clarification that have been added to this rulemaking which address the *use* of CDD information by financial institutions for the purpose of risk assessment. **Finally, we welcome the Government's statement of its broad strategy to enhance financial transparency, in particular the key element of "increasing the transparency of U.S. legal entities through the collection of beneficial ownership information at the time of the legal entity's formation."** We note that with respect to collecting beneficial ownership information at the time of incorporation, any proposal to accomplish this must (i) collect information on the natural persons who directly or indirectly own the entity or control it by other means (which is not simple management of the company), (ii) not permit nominee information to be provided in place of beneficial ownership information, and (iii) require that the information be publicly available and accessible.

With respect to the details of the proposed rulemaking, however, we have the following comments:

**I. Definition of Beneficial Owner**

**A. The Concept of "Control" in Beneficial Ownership versus the Concept of "Management."**

We have no objection to requiring financial institutions to identify an executive officer or senior manager of a legal entity as part of this rulemaking, **but it should not be characterized as the "control" part of a beneficial ownership definition.** It should be required *in addition to* identification of the beneficial owner(s).

The NPRM refers to the FATF definition of beneficial owner as "the natural person(s) who ultimately owns or controls a customer and/or the person on whose behalf a transaction is being conducted. It also incorporates those persons who exercise ultimate effective control over a legal person or arrangement." The NPRM correctly identifies that this definition captures both the concepts of

**GLOBAL FINANCIAL INTEGRITY**

ownership and effective control. However, ultimate effective control in the sense of this definition and the generally understood meaning of beneficial ownership is where a person or persons that have no legal ownership of the company are ultimately controlling the entity through legal or extra-legal means and/or are the primary beneficiaries of its existence without actually holding a significant equity stake in the company. It is referring to those who are behind the scenes pulling the strings, as it were. This is a common method of misusing legal entities to access the U.S. financial system, as in numerous cases that a recent Global Witness report identified.<sup>1</sup> These cases include the use of “control by other means” by organized crime syndicates, politically exposed persons (PEPs), sanctioned foreign governments, and fraudsters of every stripe—precisely the sort of risky customers the proposed rule is designed to target.

We understand that this type of effective control is difficult to determine and even the best CDD efforts may not flush it out. We understand that including a requirement that financial institutions *must* have identified *every* beneficial owner with this type of effective control is not realistic or possible. But it is critical that (i) personnel carrying out CDD in a financial institution understand what effective control means and that it may exist, and (ii) that they are required to make inquiries with respect to that aspect of beneficial ownership.

In the context of this rulemaking, that means that such a question must be included in the rule’s requirements and must be included on the Certification Form.

An officer or manager of a company, merely by virtue of being an officer or manager of a company, is NOT exercising effective control over the company in the sense of what is meant by effective control in a beneficial ownership inquiry (as discussed above). To include this as a second prong of a *definition* of beneficial ownership therefore (i) misses a key element of the internationally understood concept of beneficial ownership, and (ii) will be extremely confusing and misleading for governments and financial institutions around the world who look to U.S. laws and regulations for suggested guidance. If it is an indication of Treasury’s intention to try to craft a new global normative understanding of what beneficial ownership means, we strongly oppose that approach for the reasons set forth above.

Again, to be very clear, we do not object to requiring the inclusion of senior officers or managers in a CDD inquiry/file on the client, but it is neither appropriate nor advisable for it to be included in a *definition* of beneficial ownership.

**Recommendation: The definition of beneficial owner needs to include the concept of effective control so that it captures individuals who control a company through unofficial means, such as trusts or power-of-attorney arrangements, outside of legal ownership or acting as a corporate officer. The Certification Form must include an explanation of control by other means in the definition of beneficial owner and in a question that explicitly asks for information about individuals who fit the definition.**

## **B. The 25 Percent Threshold.**

**A 25 percent ownership threshold is too high for the ownership prong of the definition. We have concerns that including any ownership threshold provides money launders with a clear guide on how**

---

<sup>1</sup> See Global Witness, “The Great Rip Off: Anonymous Company Owners and the Threat to American Interests,” Sept. 2014, available at <http://www.globalwitness.org/greatripoff/>.

**to avoid anti-money laundering checks. As the efficient compromise between a requirement to ascertain all beneficial ownership information and the cost of compliance for financial institutions, we strongly recommend a 10 percent threshold.**

We have significant reservations about identifying only those with a 25 percent or greater ownership interest in the legal entity as beneficial owners. The reasons for this reservation are as follows:

1. In order to subvert an FI's CDD under a 25 percent threshold regime, a criminal would have to find only five people to agree to serve as beneficial owners of his company in order to avoid a problem where beneficial owner information records are kept by the FI. He would need to find 11 people to serve that purpose if the threshold was 10 percent – a much higher hurdle. Of course, if there were no threshold at all then there is no way for a criminal to escape that reporting requirement – the best possible outcome.
2. As FinCEN notes in the NPRM, many FIs already apply a 10 percent threshold.<sup>2</sup> Our discussions with FI representatives confirms that understanding.
3. That being said, it is critical to remember that the task of identifying beneficial owners under this rulemaking rests with the client company, not with the FI. Therefore a 25 percent or 10 percent level does not actually change the “burden” on the FI itself. Knowing the beneficial ownership of your own company is actually a matter of sound corporate governance, as recognized by other arms of the U.S. Government. For example, the SEC requires individual investors who hold a five percent or greater stake in a public company (which are exempted under this rulemaking) to report their interest in order to notify the companies of the individual's stake.<sup>3</sup> Additionally, this point was raised repeatedly in the early meetings of the Private Sector Preparatory Group when beginning to construct the Legal Entity Identifier program. While “sound corporate governance” is not a primary objective of FinCEN, nor of this rulemaking, it is one of the basic principles upon which all theories of corporate accountability (and U.S. laws and regulations that arise from them) rest.
4. Requiring companies to provide information about their beneficial ownership at a 10 percent level will also assist FIs in complying with information exchange requests under the Foreign Account Tax Compliance Act (FATCA) Inter-Governmental Agreements. Congress determined that the threshold for determination of who benefits from the existence of a bank account under FATCA should be 10 percent.<sup>4</sup> It is therefore a useful way to leverage compliance under both requirements, increase efficiency, and decrease compliance costs.
5. Finally, regardless of whether the threshold is set at 10 or 25 percent, we believe that the rule should include a fallback provision, requiring collection of information on at least one individual

---

<sup>2</sup> Financial Crimes Enforcement Network, Customer Due Diligence Requirements for Financial Institutions, 79 Fed. Reg. 45151, 45158 (Aug. 4, 2014).

<sup>3</sup> Sec. 13(d) of the Securities Act of 1934, codified at 15 U.S.C. § 78m(d).

<sup>4</sup> 26 U.S.C. § 1473(2)(A) (defining “substantial United States owner” of a corporation, partnership, or trust for purposes of FATCA withholding).

with significant shareholding for the company even when none meet the 10 percent threshold. Such a provision, requiring the reporting of “an individual who . . . has at least as great an equity interest in the entity as any other individual,” was included in the ANPRM.<sup>5</sup> While we appreciate that it may be difficult to identify the individual with the single largest equity stake in an entity, we do not consider it an acceptable solution to allow FIs to simply “identify no individuals under the ownership prong.”

**Recommendation: We strongly recommend a 10 percent threshold for legal ownership as the efficient compromise between a requirement to ascertain all beneficial ownership information and the cost of compliance for financial institutions.**

## II. Definition of Legal Entity Customer

The list of Legal Entity Customers seems appropriate apart from the inclusion of “unincorporated nonprofit association.” Very few people would be familiar with or understand this term, and whether one has formed an unincorporated nonprofit association is likely something that an FI would only determine after specific questioning to that effect (as the average person is unlikely to even know/understand that they have formed one). The approach taken in this rulemaking is for the client to fill out a certification form if they represent a legal entity. Someone who has *de facto* formed an unincorporated nonprofit association is unlikely to know that they have done so and that they should indicate that to the banker.

If FinCEN does proceed to include unincorporated nonprofit associations, they should actually cover *all* unincorporated associations<sup>6</sup>. There is no reason to single out a nonprofit version. While we understand that the IRS generally considers unincorporated for-profit associations to be joint ventures or partnerships for tax purposes, we do not believe that the average person would be aware of having formed any unincorporated association when they do so. Therefore, the same problem arises with respect to the certification form.

While this is an appropriate inquiry in terms of guidance for CDD, we do not believe that it should be part of the regulatory requirement.

**Recommendation: If FinCEN includes unincorporated nonprofit associations in this rulemaking, they should actually cover *all* unincorporated associations.**

## III. Existing Accounts

There are significant risks associated with not obtaining beneficial ownership certifications from existing customers. In fact, by exempting existing accounts, implementation of this rule will do nothing to address risks related to a bank’s current clients. We appreciate that obtaining beneficial ownership

---

<sup>5</sup> Financial Crimes Enforcement Network, Customer Due Diligence Requirements for Financial Institutions, 77 Fed. Reg. 13046, 13052 (Mar. 5, 2012).

<sup>6</sup> Defined as a “voluntary group of persons, without a charter, formed by mutual consent for the purpose of promoting common enterprise or prosecuting common objective.” Blacks Law Dictionary, 6th Ed.

certifications for all existing customers since the dawn of time may be both cost-prohibitive and not the most effective use of an FI's compliance resources. We therefore propose a middle ground:

- Collect certification forms for all new accounts opened on or after January 1, 2013 (which is FATCA's Effective Date), AND
- Collect certification forms for all other existing customers on a risk basis, in line with the FI's risk-based approach.

This look-back could be phased in. Perhaps the rule could provide on additional year from the Effective Date of this new rule to accomplish the look-back for all accounts established on or after January 1, 2013, two additional years to complete the look-back for high-risk accounts existing prior to January 1, 2013, and a requirement to look back at all other existing accounts on a risk basis.

**Recommendation: This rulemaking should apply retroactively to legal entity accounts, not just new accounts. FIs must be required to collect Certification Forms for all new accounts opened on or after January 1, 2013 and should collect Certification Forms for all other existing customers on a risk basis.**

#### IV. Proposed Exemptions from the Beneficial Ownership Rule

We have no comments on the proposals with respect to the remaining exemptions.

#### V. Intermediated Accounts

We have no comments on the proposals with respect to intermediated accounts.

#### VI. Pooled Investment Vehicles

We have no comments on the proposals with respect to pooled investment vehicles.

#### VII. Trusts

While we appreciate that "beneficial ownership" information, as defined in this proposed rule, cannot be collected for trusts (apart from statutory trusts), that does not preclude the need for FIs to collect other identifying information for trusts. Contrary to FinCEN's assertion, it can be accomplished within this rulemaking.

Trusts generally have at least three identifying elements – trustees, settlors, and beneficiaries (whether by name or class). We would recommend a separate certification form for trusts. In terms of filling out a certification form, it is quite simple to create fields for information about all trustees, settlors, and beneficiaries. We appreciate that there are trust that have beneficiaries that are not determined until a later time, and the form could allow for such indication instead of a list of beneficiaries where that is the case.

We see no reason why a separate section including requirements with respect to identifying information for trusts cannot be included in this rulemaking.

**Recommendation: FinCEN should require FIs to have a separate certification form for trusts that collects information about the type of trust and identifying information about the trustee, the settlor, and beneficiaries (where determined).**

---

#### GLOBAL FINANCIAL INTEGRITY

## VIII. Certification Form

We have a few comments with respect to the Certification Form. At present, the Certification Form has a very low “knowledge” threshold for certification. When an administrative person who knows little other than the name of his/her company, the name of the CEO, and his/her immediate boss is sent to the bank to open this account, he/she is unlikely to have the requisite knowledge to fill the form out with the correct beneficial ownership information. As drafted, the certification says that, if the person filling out the form doesn’t have the requisite knowledge, they can write down whatever they happen to know. As the basis for an FI’s subsequent CDD, the standard of knowledge/inquiry of the person filling out this form on behalf of the company must be higher than whatever they happen to know at the time the form is placed in front of them.

- A. Given that FI’s will be relying on this certification form, the certification itself should be a higher standard of knowledge—one that requires some inquiry on the part of the certifier, and the certification should be made under penalty of perjury. We recommend “I, \_\_\_\_\_, hereby certify under penalty of perjury that to the best of my knowledge after due inquiry, the information provided is complete and correct.”
- B. In conjunction with the points above, it would be better if the certification form was a U.S. Government document, and, therefore, the certifications are to the U.S. Government.
- C. With respect to foreign persons, information about their country of residence and country of domicile should be collected.
- D. As discussed above, the ownership threshold should be no higher than 10 percent.

**Recommendation: The Certification Form should be a U.S. Government document and the certification should be made under the penalty of perjury that to the best of the certifier’s knowledge, after due inquiry, the information provided is complete and correct.**

## IX. Verification of Beneficial Owners

We understand that FinCEN is proposing that FIs be able to rely on the information provided on the Certification Form as evidence of beneficial ownership. The verification proposed is that of existence (through copies of official identification with photos, and by other means) and not that of status (whether the person listed is indeed the beneficial owner).

A requirement to only verify the existence of the individuals listed as beneficial owners on the Certification Form does not meet the standard set out by FATF Recommendation 10, which states:

*Identifying the beneficial owner, and taking reasonable measures to verify the identity of the beneficial owner, such that the financial institution is satisfied that it knows who the beneficial owner is. For legal persons and arrangements this should include financial institutions understanding the ownership and control structure of the customer.<sup>7</sup>*

---

<sup>7</sup> The FATF Recommendations, page 14: [http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF\\_Recommendations.pdf](http://www.fatf-gafi.org/media/fatf/documents/recommendations/pdfs/FATF_Recommendations.pdf)

We believe that **the responses on the Certification Form should be the *beginning* of a FI's due diligence with respect to status, and not the dispositive proof of beneficial ownership status.** In other words, we expect reasonable due diligence inquiries to be made to test the veracity and/or reasonableness of the responses provided, and, where questions arise, to follow up as necessary with either the company or independent research to either satisfy those questions, put the client in a higher risk category, or refuse to open the account if that is warranted. Simply running the names received through World Check or the equivalent is not satisfactory.

Our concern here is to avoid the creation of a system that is characterized by plausible deniability. Plausible deniability is already a problem within the industry, and full and total reliance on the certification would exacerbate the problem.

It is not altogether clear to us whether FinCEN intended the certification form as dispositive proof of beneficial owner status, so we would like it to be made explicit in the regulation that the form is not so intended.

**Recommendation: The Certification Form should be the *beginning* of a FI's due diligence with respect to status, and not the dispositive proof of beneficial ownership status. FIs must take reasonable measures to satisfy that they know who the beneficial owner of the legal entity is.**

**X. Updating of Beneficial Ownership Information**

We agree that beneficial ownership information should be updated as appropriate on a risk-basis.

**Recommendation: The rule should make it clear that beneficial ownership information should be updated as appropriate on a risk-basis.**

**XI. Recordkeeping Requirements**

We have no comments on the proposals with respect to recordkeeping requirements.

**XII. Understanding the Nature and Purpose of Customer Relationships and Ongoing Monitoring**

We support FinCEN's proposal to make this mandatory.

**XIII. Proposed Amendments to the AML Program Rules**

We support FinCEN's proposal to make this mandatory.

**XIV. Effective Date of the Rule**

We support FinCEN's proposed Effective Date. We note that adjustments could be made in light of additional look-back requirements, as discussed above under Part III.

**XV. Relation to Other Regulations, Guidance or Authority**

Although FinCEN has not asked for comments on the issue, we feel that it is important to provide comments regarding the proposal that this new regulation "not to supersede[,] any regulations, guidance or authority of any federal banking agency, the Securities and Exchange Commission (SEC), the

**GLOBAL FINANCIAL INTEGRITY**

Commodity Futures Trading Commission (CFTC), or of any self-regulatory organization (SRO) relating to customer identification, including with respect to the verification of the identities of legal entity customers.” We have a number of concerns.

- A. We would understand that, if any of these bodies had promulgated a *stricter* standard, that it would be best for this rule not to supersede it. However, **where any of these bodies have in place weaker standards, this federal regulation should indeed supersede those standards.**
- B. The drafting suggests that even if one of these bodies adopted a different standard *after* this rule was promulgated, the alternative standard would supersede this rule. That opens the door for anybody that disagrees with this approach to provide a different standard.
- C. Mere *guidance* from any of these bodies should not be able to supersede this federal regulation.
- D. Absolutely no decision from a self-regulatory agency should be able to supersede this federal regulation, in any form. They have an opportunity to provide comments through this process, and the federal government can consider their views as they do other stakeholders.

It seems almost pointless to adopt a federal regulation if it can be superseded by a guidance document provided by any regulator.

**Recommendation: This regulation should supersede other regulations, guidance, and authority that is weaker than this federal regulation.**

While we are supportive of this rulemaking and believe requiring financial institutions to obtain and verify beneficial ownership information for all accountholders is critical to keeping the proceeds of corruption and other crimes from being laundered through the U.S. financial system, the rule by itself isn’t enough. There is far too little beneficial ownership information available to FIs or in the public domain. To close this gaping loophole in U.S. law that is regularly exploited by criminals and leaves our financial system vulnerable to dirty money, the government must require all American companies to disclose information about their beneficial owners at the time of incorporation and keep it up to date, and this information must be available to the public.

We thank you for your time and appreciate your consideration of our views. We would welcome the opportunity to discuss any of our comments in greater detail during your deliberations.

To discuss this comment in greater detail, please contact:

Heather A. Lowe  
Legal Counsel & Dir. of Government Affairs  
Global Financial Integrity  
[hlowe@gfintegrity.org](mailto:hlowe@gfintegrity.org)

Joshua Simmons  
Policy Counsel  
Global Financial Integrity  
[jsimmons@gfintegrity.org](mailto:jsimmons@gfintegrity.org)

Stefanie Ostfeld  
Deputy Head of U.S. Office  
Global Witness  
[sostfeld@globalwitness.org](mailto:sostfeld@globalwitness.org)

---

**GLOBAL FINANCIAL INTEGRITY**