

FEDERAL RESERVE BANK OF SAN FRANCISCO
101 MARKET STREET, SAN FRANCISCO, CALIFORNIA 94105

July 31, 2002

**BANKING SUPERVISION AND REGULATION:
SECTIONS 312 AND 326
OF THE USA PATRIOT ACT**

To State Member Banks, Bank
Holding Companies, U.S. Branches
and Agencies of Foreign Banks,
and Others Concerned,
in the Twelfth Federal Reserve District

**Section 312 of the USA Patriot Act—Due Diligence for Correspondent and Private Banking
Accounts (SR 02-18)**

Section 312 of the USA Patriot Act¹ generally requires a U.S. financial institution that maintains a correspondent account or private banking account for a non-U.S. person to establish appropriate and, if necessary, enhanced due diligence procedures to detect and report instances of money laundering. Section 312 also describes specific enhanced due diligence standards for U.S. financial institutions that enter into correspondent banking relationships with foreign banks that operate under offshore banking licenses or under banking licenses issued by countries that (1) have been designated as non-cooperative with international anti-money laundering principles by an international body (such as the Financial Action Task Force) with the concurrence of the U.S. representative to that body, or (2) have been the subject of special measures imposed by the Secretary of the Treasury under section 311 of the USA Patriot Act. In addition, section 312 describes anti-money laundering due diligence minimum standards for the maintenance of private banking accounts by U.S. financial institutions for non-U.S. persons.

The Treasury Department is authorized to issue regulations implementing section 312. The law provides that the provisions of section 312 become effective on July 23, 2002, whether or not final regulations are in place. On May 30, 2002, Treasury published in the *Federal Register* a proposed rule implementing section 312.² Treasury received a number of comments on this proposed rule and is still in the process of reviewing and analyzing them. Because of the complexity of the issues raised by the proposed rule, Treasury did not issue a final rule by July 23, 2002, but rather issued an interim final rule that is effective immediately.³

Treasury's interim final rule requires that insured depository institutions, U.S. branches and agencies of foreign banks, and Edge and Agreement corporations comply with the statutory requirements of section 312. A copy of the interim rule is on the Treasury web site at <http://www.treas.gov/press/releases/po3270.htm>. Treasury will be accepting written comments on the interim final rule for 30 days after the date of publication in the *Federal Register*.

In the interim final rule, Treasury also provides compliance guidance to banks and other immediately affected financial institutions. This guidance, which is set forth in supplementary information and not as a regulation, indicates what Treasury would consider as "reasonable" due diligence policies and procedures pending the issuance of a final rule. According to Treasury's guidance, these policies and procedures include (1) focusing on accounts that pose the highest risk of money laundering, (2) according priority to those accounts opened on or after July 23, 2002, and (3) complying with existing best practice standards for banks, such as those issued by the Wolfsberg Group in May 2002, the New York Clearing House in March 2002, and the Bank for International Settlements in October 2001. Treasury noted that it could be reasonable for an institution not to apply every best practice standard if it has a justifiable basis for not adopting a particular practice.

¹ Codified at 31 U.S.C. 5318(i).

² Refer to 67 *Federal Register* 37,736.

³ Treasury anticipates issuing a final rule implementing section 312 by no later than October 25, 2002.

Until Treasury issues a final rule implementing section 312, examiners should make certain that covered banking organizations under the supervision of the Federal Reserve are aware of the specific provisions of the law and have reasonable policies and procedures in place to assure and monitor compliance. Also, in accordance with existing Board practices concerning anti-money laundering related matters, and to ensure consistency throughout the System during this interim period, a Reserve Bank should notify Division staff if examiners believe that a banking organization is not in compliance with the plain terms of section 312.

Finally, it is important to note that Treasury issued the interim final rule and that it may only be interpreted by that agency. Board staff will continue to work with Treasury to provide guidance to examiners and banking organizations supervised by the Federal Reserve.

Treasury and Federal Financial Regulators Issue Patriot Act Regulations on Customer Identification (Docket R-1127)

The Department of the Treasury and seven federal financial regulators today issued proposed rules that would require certain financial institutions to establish minimum procedures for identifying and verifying the identity of customers seeking to open new financial accounts. Written comments on the proposed rules may be submitted by September 6, 2002.

These proposed rules implement section 326 of the USA PATRIOT Act, which directs the issuance of regulations requiring financial institutions to implement reasonable procedures for (1) verifying the identity of any person seeking to open an account, to the extent reasonable and practicable; (2) maintaining records of the information used to verify the person's identity and; (3) determining whether the person appears on any list of known or suspected terrorists or terrorist organizations. Final rules implementing section 326 must be effective by October 25, 2002.

The proposed rules seek to protect the U.S. financial system from money laundering and terrorist financing. Additionally, by requiring identity verification procedures for all new accounts opened after the effective date of the final rules, the rules could also protect consumers against various forms of fraud, including identity theft.

The proposed rules were developed jointly by the Treasury Department, Treasury's Financial Crimes Enforcement Network and seven federal financial regulators, including the Board of Governors of the Federal Reserve System, Commodity Futures Trading Commission, Federal Deposit Insurance Corporation, National Credit Union Administration, Office of the Comptroller of the Currency, Office of Thrift Supervision, and Securities and Exchange Commission.

The proposed rules outline requirements for the following financial institutions: banks and trust companies, savings associations, credit unions, securities brokers and dealers, mutual funds, futures commission merchants, and futures introducing brokers.

The financial institutions subject to the proposed rules would be required to establish programs specifying procedures for obtaining identifying information from customers seeking to open new accounts. This identifying information would be essentially the same information currently obtained by most financial institutions and for individual customers generally, including the customer's name, address, date of birth, and an identification number (for U.S. persons, a social security number and for non-U.S. persons, a similar number from a government-issued document). Customers with signature authority over business accounts would furnish substantially similar information.

A financial institution's program would also have to contain procedures to verify the identity of customers within a reasonable period of time. The proposed rules contemplate that financial institutions will generally use the same forms of identity verification that are already in place, such as examining driver's licenses, passports, credit reports, and other similar means.

While every program must meet these minimum elements, the proposed rules give financial institutions the flexibility to tailor their procedures as appropriate, taking into consideration an individual institution's size, location, and type of business. In developing these regulations, the importance of many factors was taken into account, including the need to guard the U.S. financial system against terrorist financing and money laundering, the legitimate privacy interests of customers, and the need for these regulations to be effectively integrated into the daily operations of financial institutions.

E-Notification

The Federal Reserve Bank of San Francisco will notify depository institutions by e-mail of new Banking Supervision and Regulation circular letters recently posted on the Twelfth District Federal Reserve Bank web site. We will e-mail a summary of the letter as well as a link to the full text of the letter and its attachments to view and print. To subscribe to this free service, simply visit our web site at <http://www.frbsf.org/banking/> and click on the E-Notification logo.

Additional Information

All circulars and documents are available on the Internet through the Federal Reserve Bank of San Francisco's Internet site, at <http://www.frbsf.org/banking/letters>. Paper copies of Docket R-1127 are available from our Corporate Services Department. To request copies to be sent by mail, please call (415) 974-2060.

For additional information about the information in this letter, please contact our Banking Supervision and Regulation Department at (415) 974-3318.

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