

**MEMO# 19634**

January 26, 2006

## **FINCEN PROPOSES AML RULE ON "ENHANCED DUE DILIGENCE" FOR CERTAIN TYPES OF FOREIGN BANKS**

©2006 Investment Company Institute. All rights reserved. Information may be abridged and therefore incomplete. Communications from the Institute do not constitute, and should not be considered a substitute for, legal advice. [19634] January 26, 2006 TO: AML COMPLIANCE WORKING GROUP No. 3-06 TRANSFER AGENT ADVISORY COMMITTEE No. 7-06 RE: FINCEN PROPOSES AML RULE ON "ENHANCED DUE DILIGENCE" FOR CERTAIN TYPES OF FOREIGN BANKS As a companion to the rule on correspondent accounts adopted earlier this month,<sup>1</sup> the Financial Crimes Enforcement Network ("FinCEN") has proposed a rule that would require certain financial institutions, including mutual funds, to conduct "enhanced due diligence" to guard against money laundering in accounts established for certain categories of high-risk foreign banks.<sup>2</sup> Comments must be submitted before March 6th. The Institute may comment on this proposal, either individually or jointly with other financial trade associations. If you have issues that you would like the Institute to consider raising, please contact me by phone (202- 371-5430), fax (202-326-5841), or e-mail (rcg@ici.org).

**Categories of Banks Subject to Enhanced Due Diligence** The proposed rule would require enhanced due diligence (described below) with regard to foreign banks operating under any of the following three types of licenses: 1. An offshore banking license; 2. A banking license issued by a foreign country that has been designated as non-cooperative with international anti-money laundering principles or procedures by an intergovernmental group or organization of which the United States is a member and with which designation the U.S. representative to the group or organization concurs; or 1 See memoranda nos. 19496, dated December 19, 2005, and 19580, dated January 6, 2006. 2 71 Fed. Reg. 516 (Jan. 4, 2006). A copy of the proposed rule is attached. 2 3. A banking license issued by a foreign country that has been designated by the Secretary of the Treasury as warranting special measures due to money laundering concerns.

**Enhanced Due Diligence** The proposed rule requires mutual funds to conduct "enhanced scrutiny" of accounts for the types of foreign banks described above to guard against money laundering and to identify and report any suspicious transactions in the accounts. Although the rule states that such "enhanced scrutiny" procedures must "reflect the risk assessment of the account," it also specifically requires the procedures to include, as appropriate, the following elements: 1. Procedures to obtain and review documentation relating to the foreign bank's AML program; 2. Procedures to consider whether such AML program appears to be reasonably designed to detect and prevent money laundering; 3. Procedures to monitor transactions to, from, or through the account in a manner reasonably designed to detect money laundering and suspicious activity; and 4. Procedures to obtain information from the foreign bank about the identity of any person with authority to direct transactions through any payable-through

account, and the sources and beneficial owner of funds or other assets in the payable-through account. The proposed rule also requires mutual funds to determine whether the foreign bank in turn maintains correspondent accounts for other foreign banks that use the account established or maintained by the mutual fund (referred to in the proposing release as “nested banks”). If the foreign bank has customers that are nested banks, the proposed rule requires the mutual fund to take reasonable steps to obtain information about those nested banks. The proposed rule further requires mutual funds to determine the identity of each owner of any foreign bank subject to the rule that is not publicly traded, as well as the nature and extent of each such owner’s ownership interest. Finally, the proposed rule requires the enhanced due diligence program to include procedures to be followed when the mutual fund cannot perform appropriate due diligence or enhanced due diligence, including when the fund should refuse to open an account, suspend transaction activity, file a suspicious activity report, or close an account. Robert C. Grohowski Senior Counsel - International Affairs Attachment Attachment (in .pdf format) 3

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