

## **FEDERAL RESERVE SYSTEM**

### **12 CFR Part 211**

#### **Regulation K; Docket No. R- 1147 International Banking Operations**

**AGENCY:** Board of Governors of the Federal Reserve System.

**ACTION:** Notice of proposed rulemaking.

**SUMMARY:** The Board of Governors of the Federal Reserve System (Board) is seeking public comment on a proposal to require Edge and Agreement corporations and U.S. branches, agencies and other offices of foreign banks supervised by the Board to establish and maintain procedures reasonably designed to assure and monitor compliance with the Bank Secrecy Act and the regulations issued thereunder.

**DATES:** Written comments on all aspects of the proposal are welcome and must be received on or before June 30, 2003.

**ADDRESSES:** Comments should refer to Docket No. R-1147 and may be mailed to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, DC 20551. However, because paper mail in the Washington area and at the Board of Governors is subject to delay, please consider submitting your comments by e-mail to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov), or faxing them to the Office of the Secretary at 202-452-3819 or 202-452-3102. Members of the public may inspect comments in Room MP-500 between 9:00 a.m. and 5:00 p.m. on weekdays pursuant to 261.12, except as provided in 261.14, of the Board's Rules Regarding Availability of Information, 12 CFR 261.12 and 261.14.

**FOR FURTHER INFORMATION CONTACT:** Pamela J. Johnson, Senior Anti-Money Laundering Coordinator, (202) 728-5829, or Nina A. Nichols, Counsel, Division of Banking Supervision and Regulation, (202) 452-2961; or Melinda Milenkovich, Counsel, (202) 452-3274, or Thomas Scanlon, Counsel, Legal Division, (202) 452-2594. For users of Telecommunications Devices for the Deaf (TDD) only, contact (202) 263-4869.

#### **SUPPLEMENTARY INFORMATION:**

##### **I. Background.**

In 1987, the federal bank supervisory agencies amended their respective regulations to require the banks, savings associations, and credit unions they regulated to establish and maintain procedures to assure and monitor compliance with the requirements of subchapter II of chapter 53 of Title 31, United States Code, commonly known as the "Bank Secrecy Act," and the Treasury regulations promulgated thereunder.<sup>1</sup>

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<sup>1</sup> The notice was issued by the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the

The Bank Secrecy Act generally requires financial institutions to, among other things, keep records and make reports that have a high degree of usefulness in criminal, tax, or regulatory proceedings. The 1987 amendments to the supervisory agencies' regulations were adopted to comply with the requirements of section 1359 of the Anti-Drug Abuse Act of 1986, Pub. L. 99-570, which required the supervisory agencies to prescribe regulations requiring the institutions they regulate to establish and maintain procedures reasonably designed to assure and monitor compliance with the Bank Secrecy Act and to review such procedures during the course of their examinations.

The amendments to the supervisory agencies' regulations incorporated the minimum components of a Bank Secrecy Act compliance program as determined by the supervisory agencies and as generally set forth in the Bank Secrecy Act at 31 U.S.C. 5318(h). These include: (i) a system of internal controls to assure ongoing compliance; (ii) independent testing of compliance by the institution's personnel or by an outside party; (iii) the designation of an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and (iv) training for appropriate personnel.

The amendment to the Board's regulations is now codified in Regulation H at 12 CFR 208.63.<sup>2</sup> The provision applies to state member banks, but corresponding provisions were not included in Regulation K for branches, agencies and representative offices of foreign banks or Edge and Agreement corporations. Such financial institutions are, however, subject to the Bank Secrecy Act and the regulations promulgated thereunder, and should maintain compliance programs accordingly.

## II. Proposed Bank Secrecy Act Program Requirements

The Board is proposing to amend Regulation K to require Edge and Agreement corporations and U.S. branches, agencies, and other offices of foreign banks supervised by the Board to establish and maintain procedures reasonably designed to assure and monitor compliance with the Bank Secrecy Act.<sup>3</sup>

The Board believes that the proposed regulation will not impose any material additional administrative burden for affected institutions. In supervising branches, agencies and other offices of foreign banks or Edge and Agreement corporations, the

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Federal Home Loan Bank Board, and the National Credit Union Administration on January 27, 1987, 52 FR 2858. It was effective January 27, 1987, and required programs to be in place by April 27, 1987.

<sup>2</sup> The amendment was initially made to 12 CFR 208.14, but the provision was moved in subsequent changes to Regulation H.

<sup>3</sup> Statutory authority for the proposed rule is found in section 1359 of the Anti-Drug Abuse Act of 1986, Pub. L. 99-570, and in section 8(s)(1) of the Federal Deposit Insurance Act, as amended by section 2596(a)(2) of the Crime Control Act of 1990, Pub.L. 101-647. The latter requires the Board to, among other things, issue regulations requiring state member banks and other domestic and foreign banking organizations operating in the United States and supervised by the Board, to establish and maintain internal procedures to ensure compliance with the Bank Secrecy Act. Section 8(s)(1) of the Federal Deposit Insurance Act is made applicable to branches and agencies of foreign banks by sections 8(b)(3) and 8(b)(4).

Board has, as a matter of safety and soundness, consistently expected such entities to maintain programs to ensure compliance with all applicable provisions of the Bank Secrecy Act.

Moreover, section 352 of the Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act, P.L. 107-56 (USA PATRIOT Act), amended 31 U.S.C. 5318(h) of the Bank Secrecy Act to impose a statutory requirement on all financial institutions to maintain anti-money laundering programs. The amendment to 31 U.S.C. 5318(h) was effective on April 24, 2002.

The Treasury Department issued an interim final rule under section 352 of the USA PATRIOT Act that applies to banking organizations.<sup>4</sup> The interim rule provides that if a financial institution is in compliance with the anti-money laundering program requirements of its federal functional regulator or self-regulatory organization, the institution will be deemed to be in compliance with the statutory and regulatory requirements of the Treasury under 31 U.S.C. 5318(h). Because branches, agencies and representative offices of foreign banks and Edge and Agreement corporations are subject to the program requirement of 5318(h) of the Bank Secrecy Act, and the Treasury regulation provides that they will be in compliance if they comply with the Board's program requirement, the proposed regulation will provide necessary clarification. The proposed regulation will clarify the existing obligations of branches, agencies, and representative offices of foreign banks and Edge and Agreement corporations under the Board's rules, section 5318(h) and Treasury's interim final rule under section 352 of the USA PATRIOT Act.

Compliance with the proposed rule will help to assure that institutions have in place policies and procedures to assure compliance with all applicable provisions of the Bank Secrecy Act, and that any deficiencies in the area of anti-money laundering, suspicious activity reporting, and customer due diligence are promptly identified and corrected. Institutions should note, however, that compliance with this requirement alone, while a potentially mitigating factor with regard to penalties or supervisory actions, is not a defense in a criminal prosecution or civil action involving a violation of the Bank Secrecy Act or regulations promulgated thereunder.

The Board seeks comment on all aspects of this proposal.

### III. Regulatory Flexibility Act.

The Board of Governors certifies that this proposed rule will not have a significant economic impact on a substantial number of small entities. The proposal creates a uniform regulatory standard for ensuring and examining compliance with applicable law and regulation. Most institutions covered by the proposed rule, whether small or large, already have policies and procedures substantially equivalent to those

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<sup>4</sup> Treasury's interim final rule was published at 67 FR 21110 (April 29, 2002). The requirement for banks, savings associations, and credit unions is codified in Treasury's Bank Secrecy Act regulations at 31 C.F.R. 103.120(b).

required by the proposed rule. Therefore, the Board believes this proposed rule should not have a significant economic impact.

#### IV. Paperwork Reduction Act.

In accordance with the Paperwork Reduction Act of 1995 (PRA) (44 U.S.C. 3506; 5 CFR 1320 Appendix A.1), the Board reviewed the proposed rule under the authority delegated to the Board by the Office of Management and Budget (OMB). The proposed rule contains recordkeeping requirements that are subject to the PRA. In summary, the proposed rule requires Edge and Agreement corporations and U.S. branches, agencies and other offices of foreign banks supervised by the Board to establish and maintain procedures reasonably designed to assure and monitor compliance with the Bank Secrecy Act and the regulations issued thereunder.

The proposed rule applies only to Edge and Agreement corporations and U.S. branches, agencies, and other offices of foreign banks supervised by the Board. The proposed rule requires each of those entities to establish a written compliance program that includes the following components: (i) a system of internal controls to assure ongoing compliance; (ii) independent testing of compliance by the institution's personnel or by an outside party; (iii) the designation of an individual or individuals responsible for coordinating and monitoring day-to-day compliance; and (iv) training for appropriate personnel. The compliance program must be approved by the board of directors, and noted in the minutes.

The Board believes that little burden is associated with the requirements for establishing a compliance program for the Bank Secrecy Act because the measures involved in the program are consistent with usual and customary business practices. In addition, the entities subject to the proposed rule already must implement procedures to comply with the requirements under the Bank Secrecy Act to file suspicious activity reports (see, e.g., 12 CFR 211.6(k)).

The Federal Reserve may not conduct or sponsor, and an organization is not required to respond to, this collection of information unless it displays a currently valid OMB control number. An OMB control number will be obtained.

Estimated number of financial institutions subject to the proposed rule: 520.

Estimated average annual burden for establishing the written compliance program per financial institution: 16 hours (2 business days).

Estimated total annual burden: 8,320 hours.

The Board requests comment on the recordkeeping requirements contained in this proposed rule, including how burdensome it would be for affected financial institutions to comply with these requirements. Also, the Board requests comment on whether these institutions currently maintain procedures or other aspects of a compliance program as described in the proposed rule. The Board also invites comment on:

(1) Whether the collections of information contained in the notice of proposed rulemaking are necessary for the proper performance of the Board's functions, including whether the information has practical utility;

(2) The accuracy of the Board's estimate of the burden of the proposed information collections;

(3) Ways to enhance the quality, utility, and clarity of the information to be collected;

(4) Ways to minimize the burden of the information collections on respondents;  
and

(5) Estimates of capital or start-up costs and costs of operation, maintenance, and purchases of services to implement appropriate compliance procedures.

Comments may be mailed to Ms. Jennifer J. Johnson, Secretary, Board of Governors of the Federal Reserve System, 20th Street and Constitution Avenue, N.W., Washington, DC 20551. However, because paper mail in the Washington area and at the Board of Governors is subject to delay, please consider submitting your comments by e-mail to [regs.comments@federalreserve.gov](mailto:regs.comments@federalreserve.gov), or faxing them to the Office of the Secretary at 202-452-3819 or 202-452-3102. Members of the public may inspect comments in Room MP-500 between 9:00 a.m. and 5:00 p.m. on weekdays pursuant to 261.12, except as provided in 261.14, of the Board's Rules Regarding Availability of Information, 12 CFR 261.12 and 261.14.

V. Solicitation of Comments Regarding Use of "Plain Language"

Section 722 of the Gramm-Leach-Bliley Act, P.L. 106-102, requires the Board to use "plain language" in all proposed and final rules published after January 1, 2000. The Board invites comments about how to make the proposed rule easier to understand, including answers to the following questions: (1) Has the Board organized the material in an effective manner? If not, how could the material be better organized? (2) Are the terms of the rule clearly stated? If not, how could the terms be more clearly stated? (3) Does the rule contain technical language or jargon that is unclear? If so, which language requires clarification?

**List of Subjects**  
**12 CFR part 211**

Exports, Federal Reserve System, Foreign banking, Holding companies, Investments, Reporting and recordkeeping requirements.

For the reasons set forth in the preamble, part 211 of chapter II of title 12 of the Code of Federal Regulations is proposed to be amended as follows:

**PART 211--INTERNATIONAL BANKING OPERATIONS (REGULATION K)**

1. The authority citation for 12 CFR part 211 continues to read as follows:

Authority: 12 U.S.C. 221 et seq., 1818, 1835a, 1841 et seq., 3101 et seq., and 3901 et seq.; 15 U.S.C. 6801 and 6805; 31 U.S.C. 5318

2. In § 211.5 add new paragraph (m)(1) to read as follows:

**§ 211.5 Edge and agreement corporations.**

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(m) Procedures for monitoring Bank Secrecy Act compliance.

(1) Establishment of Compliance Program. Each Edge corporation and each Agreement corporation shall, in accordance with the provisions of § 208.63 of the Board's Regulation H, 12 CFR 208.63, develop and provide for the continued administration of a program reasonably designed to assure and monitor compliance with the provisions of subchapter II of chapter 53 of title 31, United States Code, the Bank Secrecy Act, and the implementing regulations promulgated thereunder by the Department of the Treasury at 31 CFR part 103. The compliance program shall be reduced to writing, approved by the board of directors, and noted in the minutes.

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3. In § 211.24 revise the section heading and add new paragraph (j)(1) to read as follows:

**§ 211.24 Approval of officers of foreign banks; procedures for applications; standards for approval; representative office activities and standards for approval; preservation of existing authority; reports of crimes and suspected crimes; government securities sales practices.**

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(j) Procedures for monitoring Bank Secrecy Act compliance.

(1) Establishment of Compliance Program. Except for a federal branch or a federal agency or a state branch that is insured by the FDIC, a branch, agency, or representative office of a foreign bank operating in the United States shall, in accordance with the provisions of § 208.63 of the Board's Regulation H, 12 CFR 208.63, develop and provide for the continued administration of a program reasonably designed to assure and monitor compliance with the provisions of subchapter II of chapter 53 of title 31, United States Code, the Bank Secrecy Act, and the implementing regulations promulgated thereunder by the Department of the Treasury at 31 CFR part 103. The compliance program shall be reduced to writing, approved by the board of directors, and noted in the minutes.

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By order of the Board of Governors of the Federal Reserve System, May 23, 2003.

Jennifer J. Johnson (signed)

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Jennifer J. Johnson,  
Secretary of the Board.