



## Final Rule Summary: CUSTOMER DUE DILIGENCE of the Bank Secrecy Act

**Coverage:** Federally insured credit unions

**Agency/Citation:** FinCEN 31 CFR Parts  
1010, 1020, 1023, 1024 and 1026

**Effective Date:** May 11, 2018

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### EXECUTIVE SUMMARY

Although in the past there has not been an official “Customer Due Diligence” (CDD) regulation, FinCEN has stressed over the years that customer due diligence is a critical part of any effective BSA compliance program

FinCEN believes that the basis for a CDD obligation has always been implicit in the Bank Secrecy Act (BSA) requirements, such as the Anti-Money Laundering (AML) program and the suspicious activity reports (SAR) rules. Additionally, customer due diligence requirements have been included in the Federal Financial Institution Examination Council’s (FFIEC) BSA/AML Examination Manual for many years.

Due to concerns with a lack of uniformity and consistency in the way financial institutions have addressed their CDD obligations, FinCEN issued an Advanced Notice of Proposed Rulemaking in March 2012, followed by a proposed rule in August 2014, and a final rule in October 2016. The rule goes into effect May 11, 2018.

**Existing Accounts:** The requirement to identify and verify beneficial owner information for your legal entity accounts will be implemented prospectively – only for new accounts opened on or after May 11, 2018. FinCEN recognized that to implement these requirements retroactively would be “too unduly burdensome.”

That said, FinCEN does expect you to obtain beneficial ownership information for accounts already in existence on May 11, 2018 when, in the course of normal monitoring, you detect information relevant to reevaluating the account’s risk.

FinCEN believes the requirements in this new rule will enhance financial transparency and safeguard the financial system against terrorist financing, money laundering, fraud, tax evasion and other financial crimes.

The new provisions include:

### **Beneficial Ownership Requirements**

The new beneficial ownership requirement has several provisions:

- Identification of beneficial owners of legal entity members;
- Verification of beneficial owners of legal entity members;
- Exemptions;
- Written procedures;
- Recordkeeping; and
- Record retention

### **Anti-Money Laundering Program**

In addition to FinCEN's existing requirements for your anti-money laundering program:

- Due diligence requirements for correspondents accounts for foreign financial institutions;
- Due diligence requirements for private banking accounts; and
- Compliance with NCUA's BSA regulations;

the new rule has added the following requirements to FinCEN's BSA rule:

- A system of internal controls to assure ongoing compliance;
- Independent testing for compliance to be conducted by credit union personnel or outside parties;
- Designation of an individual or individuals responsible for coordinating and monitoring day-to-day compliance;
- Training for appropriate personnel; and
- Appropriate risk-based procedures for conducting ongoing member due diligence, to include, but not be limited to:
  - Understanding the nature and purpose of member relationships for the purpose of developing a member risk profile; and
  - Conducting ongoing monitoring to identify and report suspicious transactions, and,
  - on a risk basis, maintain and update member information – including information regarding the beneficial owners of legal entity members.

If most of this sounds familiar to you, it's because NCUA's BSA regulations require the first four bullets – almost verbatim. FinCEN also believes that the fifth bullet shouldn't

be considered a new requirement, as it reflects existing practices necessary to satisfy suspicious activity reporting (SAR) obligations.

## DETAILED ANALYSIS

### **IDENTIFICATION OF BENEFICIAL OWNERS OF LEGAL ENTITY MEMBERS**

A credit union can identify the beneficial owners of legal entity accounts in one of three ways:

(1) by obtaining a “Certification Regarding Beneficial Owners of Legal Entity Customers” provided in the rule (it will be available in electronic form).

*[Using the agency’s form **DOES NOT provide you with a safe harbor** in regard to compliance with this rule.]*

(2) by using the credit union’s own forms, as long as they meet the requirement in the rule; or

(3) by obtaining the required information by any other means – provided the person opening the account and providing the information certifies that it is accurate.

#### **The definition of “beneficial owners” has two prongs:**

Ownership criteria: person owns 25% or more equity interest in the legal entity (this is a baseline threshold – credit unions are permitted to have a lower threshold);

Control criteria: person has significant responsibility to control the legal entity, such as CEO, CFO, VP or other member of the senior management team or a person that regularly performs similar functions.

The certification form can be filled out without a beneficial owner that meets the ownership criteria, as long as there is at least one beneficial owner who meets the control criteria.

Additionally, the credit union is permitted (encouraged if the entity is considered higher-risk) to require a lower ownership threshold, thus making it more likely for an owner to meet the beneficial ownership criteria.

The rule defines **legal entities** as:

- corporations,
- limited liability companies,
- Other entities that are created by filing a public document with a Secretary of State or similar office, and
- General partnerships or other similar business entities formed in the United States or a foreign country.

A legal entity **DOES NOT** include:

- sole proprietorships,
- unincorporated associations (such as, Scout Troops and youth sports leagues),
- natural persons opening accounts on their own behalf.

Additionally a “legal entity”, for purposes of this rule does not include the following entities because the information is generally available from other credible sources:

- a financial institution;
- department or agency of the federal, state, or local government;
- any entity established under the federal, state or local laws of the U.S., or any interstate compact;
- any entity whose common stock is listed on one of the stock exchanges,
- any subsidiary of an entity listed on one of the stock exchanges and whose common stock is owned (at least 51 percent) by the listed entity
- an issuer of securities;
- an investment company;
- an investment advisor,
- an exchange or clearing agency;
- an entity registered with the SEC;
- an entity registered with the Commodity Futures Trading Commission;
- A bank holding company;
- A pooled investment vehicle;
- **An insurance company regulated by a State** – this is new, it was not included in the proposal;
- A financial market utility;
- A foreign financial institution, where its regulator maintains beneficial ownership information;
- A non-U.S. governmental department, agency or political subdivision that engages only in governmental activities.

The following entities are **only subject to the control criteria** prong in the definition of “beneficial owner”:

- Any legal entity that is established as a non-profit corporation or similar entity and has filed its organizational documents with the appropriate State authority.
- Any legal entity only to the extent that it opens a private banking account subject to BSA requirements.
- Any pooled investment vehicle that is not exempt.

**IOLTA:** For purposes of the CDD rule, credit unions should treat the attorney opening the IOLTA account as the beneficial owner of the legal entity account.

Similar to other guidance for IOLTA and escrow accounts, the attorney or escrow agent is considered the member and the credit union has no CIP obligations with respect to the underlying clients whose funds are being held in the IOLTA or escrow accounts.

**Trust Accounts:** Business trusts are created by a filing with a state office (statutory trusts), which are included in the definition of “legal entity” in the rule, which means they are covered by the requirements.

Non-statutory trusts are contractual arrangements between the person who provides the funds or other assets and specifies the terms (grantor) and the person with control over the assets (beneficiaries). Formation of this type of trust does not generally require any action by the state – so these trusts do not meet the definition of “legal entity”. FinCEN recognizes that identifying a “beneficial owner”, as defined in this rule, from among these parties would be impossible.

FinCEN further notes that where 25 percent or more of the equity interests of a legal entity are owned by a trust (other than a statutory trust), credit unions would collect and verify the identity of the trustee. In this case, the individual opening the account would still be the one required to provide the credit union with the beneficial owner information.

FinCEN also reminds financial institutions that although they are not required to look through a trust to its beneficiaries, they “may need to take additional steps to verify the identity of a customer that is not an individual, such as obtaining information about persons with control over the account”.

**Filling out the Certification Form:** If you choose to identify beneficial owners of legal entity accounts by using the form provided in the rule, it must be completed by the person opening the new account (on or after May 11, 2018) on behalf of a legal entity. It must be a natural person authorized to open the account – it cannot be the entity itself.

This form requires the person opening the account to provide their name and title, as well as the name, address, date of birth and identification number for the “beneficial owners” of the entity.

The number of individuals that satisfy the rule’s definition of “beneficial owner” may vary from one to five depending on the factual circumstances, and the same person may meet the criteria for both ownership and control.

## **VERIFICATION OF BENEFICIAL OWNERS OF LEGAL ENTITY MEMBERS**

Credit unions must verify each identified beneficial owner of legal entity accounts. At a minimum, these procedures must include all of the elements of the credit union’s Member Identification Program (MIP).

In regard to documentary verification, FinCEN has clarified that you may use photocopies or other reproductions of the documents. However, given the vulnerabilities inherent in the reproduction process, you are encouraged to conduct your

own risk-based analyses of the types of photocopies and reproductions that you will accept, for example, optical resolution threshold or digital reproductions transmitted in certain file formats.

Credit unions may rely on the information provided by the person opening the account and filling in the certification form, as long as the credit union has “no knowledge of facts that would reasonably call into question the reliability of the information.”

FinCEN reasons that credit unions generally have sound policies and procedures governing the documentation required to open a business account. It would follow that the same person that meets the credit union’s requirements for opening the account should be able to certify the identity of the beneficial owners.

The rule specifically does not require notarization or credit union board approval. FinCEN recognizes that this would “increase the amount of time to open an account, without commensurate benefit, and would be inconsistent with the agency’s goal of integrating this requirement into financial institutions’ existing onboarding procedures to the greatest extent possible.”

**OFAC compliance:** FinCEN generally expects beneficial ownership information to be treated like CIP and related information, and accordingly used to ensure that you are complying with other BSA-related requirements, such as OFAC. Credit unions should use beneficial ownership information to help ensure that you do not open or maintain an account, or otherwise engage in prohibited transactions or dealings involving individuals or entities subject to OFAC-administered sanctions.

**Section 314(a) compliance:** FinCEN does not expect the beneficial owner information requirement to add additional requirements with respect to Section 314(a) information sharing. The 314(a) rule does not authorize the reporting of beneficial owner information associated with an account or transaction matching a named subject. Under that rule, credit unions need only search their records for account or transactions matching a named subject, and report to FinCEN whether such a match exists using the identifying information that FinCEN provides.

### **EXEMPTIONS:**

The following legal entity accounts are exempt from the identification and verification requirements:

- Private label retail credit cards established at point-of-sale, up to a limit of \$50,000 (co-branded major credit cards not exempt);
- Entities to finance the purchase of postage, where payments are remitted by the credit union \*\*;
- Entities to finance insurance premiums, where payments are remitted by the credit union \*\*;

- Entities to finance the purchase or leasing of equipment, where payments are remitted by credit union \*\*.

\*\* Except where the business account member can make or receive payments from a 3<sup>rd</sup> party or where a cash refund is possible

## **NEW RISK-BASED CDD REQUIREMENTS**

Credit unions must conduct ongoing member due diligence. This will include, but is not limited to:

Member risk profile: Understanding the nature and purpose of your member relationship is meant to provide a baseline against which your member's activity is assessed for suspicious activity reporting. The profile may, but is not required to, include a system of risk ratings or categories of members.

Maintain and update member information: When you detect a change in your member's activity, through normal monitoring, you must update your member's information. Such changes in activity may include executing cross-border wire transfers for no apparent reason, or a significant change in the volume of activity without an explanation.

The rule DOES NOT require credit unions to update member information on a continuous or periodic basis. The updating requirement is event-driven and only occurs as a result of detecting unusual activity through normal monitoring.

Updating beneficial owner information: Although there is no expectation that credit unions update beneficial ownership information on a regular basis, FinCEN notes that if you detect a change in this information for any account (not just those opened on or after May 11, 2018) you should update that account's information.

## **WRITTEN PROCEDURES:**

Credit unions are required to develop written procedures to:

- identify and verify "beneficial owners" of "legal entity" members;
- make and maintain a record of all of the identification and verification information collected; and
- conduct ongoing member due diligence (appropriating risk-based).

These new procedures must be added to the credit union's BSA/AML compliance programs.

## **RECORDKEEPING:**

At a minimum the credit union's record of the identification and verification information collected must include:

- Any identification information obtained, including the Certification Form, if applicable;
- A description (type, identification number, place of issuance and dates of issuance and expiration, if any) of any document relied upon and any non-documentary methods;
- Any non-documentary methods used; and
- Any measures taken and the results of any substantive discrepancies.

## **RECORD RETENTION**

Identification Records: must be retained for 5 years after the date the account is closed.

Verification Records: must be retained for 5 years after the record is made.

