SIFMA
Securities Industry and
Financial Markets Association

April 9, 2008

VIA ELECTRONIC MAIL

Mr. James H. Freis, Jr.
Director
Financial Crimes Enforcement Network
Department of the Treasury
1500 Pennsylvania Ave., NW
Washington, DC 20220

Dr. Erik R. Sirri
Director, Division of Trading and Markets
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Re: SIFMA's Recommendations to Enhance the Efficiency and Effectiveness of Anti-Money Laundering Provisions under the USA PATRIOT Act

Dear Director Freis and Dr. Sirri:

The Securities Industry and Financial Markets Association ("SIFMA")[1] submits this letter to the U.S. Treasury Department's Financial Crimes Enforcement Network ("FinCEN") and the Securities and Exchange Commission ("SEC") to make recommendations to enhance the efficiency and effectiveness of the anti-money laundering ("AML") regulations for the securities industry. Our recommendations respond to the Regulatory Efficiency and Effectiveness Initiatives announced by Secretary Paulson and Director Freis in 2007, and the goal of ensuring that the USA PATRIOT Act of 2001 ("PATRIOT Act")[2] is being administered in the most effective way.

We first want to acknowledge the outstanding efforts made by the staffs of Treasury, FinCEN, and the SEC to implement the provisions of the PATRIOT Act since it was enacted in the aftermath of September 11th. We also greatly appreciate the time spent by the staffs of FinCEN and the SEC in listening to the concerns of the securities industry and issuing regulatory guidance specific to our industry.

[1] The Securities Industry and Financial Markets Association ("SIFMA") brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Markets Association, is based in Hong Kong. SIFMA was formed in November 2006 through the merger of the Securities Industry Association and the Bond Market Association.

[2] *Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001* ("PATRIOT Act"), Pub. L. No. 107-56 (2001), signed into law by President Bush on October 26, 2001.

The recommendations in this letter reflect a continuation of SIFMA's ongoing dialogue with FinCEN and the SEC, and should not detract from the notable efforts made to protect our financial system.

I. INTRODUCTION

SIFMA and its member firms have long been supporters of anti-money laundering efforts. We submit the following recommendations as part of our strong commitment to the detection and prevention of money laundering. Even prior to the passage of the PATRIOT Act in October 2001, SIFMA worked with its members to increase their level of anti-money laundering compliance as many firms endeavored to develop and implement sophisticated anti-money laundering programs. To that end, SIFMA issued comprehensive industry-wide guidance in February 2002, *The Preliminary Guidance for Deterring Money Laundering Activity*, which we had begun to work on well before the events of September 11th. [3]

The PATRIOT Act imposes significant requirements on broker-dealers and other financial institutions. Broker-dealers are required to establish and maintain formal anti-money laundering compliance programs, monitor and report suspicious activity, identify and verify new customers, maintain certain records for "correspondent accounts" with foreign banks, conduct special due diligence for foreign correspondent and private banking accounts, and not open or maintain correspondent accounts for foreign shell banks. As a result of these new requirements, the long lasting implication for both broker-dealers and securities regulators is that they have been and will continue to be required to devote more resources than ever before to anti-money laundering and counter-terrorist financing efforts.

Since the passage of the PATRIOT Act, we have worked closely with Treasury, FinCEN, and the SEC, as well as the Financial Industry Regulatory Authority ("FINRA")[4], to develop sound and effective rules to protect U.S. securities firms from being used for illicit purposes. [5] We have also continued to work diligently with our member firms to facilitate implementation of the PATRIOT Act's requirements and to further industry-wide anti-money laundering education. For example, we have published industry-wide AML Guidance and Customer Identification Suggested Practices and offer industry members opportunities for AML education through conferences, seminars, and regular email updates.[6]

Now that most of the anti-money laundering regulations under the PATRIOT Act have been finalized with respect to the securities industry, SIFMA would like to address several areas where we believe the anti-money laundering program rules could be made more efficient and be more beneficial to law enforcement. These recommendations reflect a general consensus in the securities industry that in times of rapidly increasing challenges in the global marketplace, the anti-money laundering rules must be flexible and balanced, and allow firms to focus their resources on the areas that present the greatest risk.

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[3] http://www.sifma.org/regulatory/anti-money/pdf/CIPGuidelines.pdf. The guidance was updated in February 2008.

[4] The Financial Industry Regulatory Authority ("FINRA"), formerly known as the National Association of Securities Dealers ("the NASD") and the NYSE Regulation ("the NYSE"), was created in July 2007 when the NASD consolidated with the member regulation, enforcement, and arbitration functions of the NYSE.

[5] A list of comment letters filed by SIFMA on Bank Secrecy Act ("BSA") and PATRIOT Act rules is attached as Appendix B.

[6] See for example, SIFMA's 8th Annual Anti-Money Laundering Compliance Conference at: http://events.sifma.org/2008/aml2008/event.aspx?id=846.

II. SUMMARY

A summary of SIFMA's recommendations are set out below:

A. Conduct a review of the effectiveness of PATRIOT Act rules by industry sector;

B. Establish a joint industry-government task force within the BSAAG dedicated to terrorism and other issues related to the U.S. financial system's security;

C. Create an office within the SEC that is dedicated solely to anti-money laundering and terrorist financing prevention;

D. Increase comprehensive information sharing among regulators, law enforcement, and the industry, including:

(1) Increase information flow under Sections 314(a) and 314(b), including expanding the ability of financial institutions to share SARs;

(2) A greater exchange of information that will assist firms to detect suspicious activity; and

(3) More transparency in the anti-money laundering examination process.

E. Increase coordination among regulators, both domestically and internationally;

F. Enhance the ability of broker-dealers and other financial institutions to rely on other regulated and/or reputable financial institutions:

III. RECOMMENDATIONS

A. Conduct an overall review of the effectiveness of PATRIOT Act rules across industries.

We believe that an overall review of the PATRIOT Act rules across industries is consistent with FinCEN's goal of reviewing the regulatory framework to ensure that the requirements on financial institutions are efficient, yet effective. A review to determine the efficiency and effectiveness of such rules as applied to different sectors would be particularly appropriate now that most of the implementing rules have been finalized. In particular, a review of the effectiveness of the rules by industry would allow Treasury to identify areas where clarification or revision is necessary for the rules to be effective as applied to particular business sectors.

Further, we believe such an analysis is necessary because the application of several rules to certain non-bank financial institutions is unclear, given that many of the rules were drafted with the banking industry in mind. For example, with respect to Rule 312, the definition of "correspondent account," while easily understood in the context of banking, is not well known to the securities industry, except in a totally

different context.[7] Therefore, many firms find it difficult to determine how to apply the rule to an account in the securities industry. In addition, there are different types of accounts in the securities industry that have no parallel in the banking industry, yet these accounts are treated the same as retail banking accounts under the PATRIOT Act. For example, a delivery-versus-payment ("DVP") account holds no assets; and an executing brokerage account has no new account opening process due to the nature of its activities. These accounts are historically part of the securities industry and are important to the ways in which business is conducted, yet in many cases treated no differently than retail banking.

We should note, however, that the agencies have made significant efforts to address many areas of the PATRIOT Act that require clarification by issuing industry specific guidance. SIFMA has requested and received guidance on many such issues and we commend the agencies for these efforts, which have resulted in real practical benefits to the industry.

B. Create a Joint Industry-Government Task Force within the BSAAG to improve collaboration for money laundering and terrorist financing prevention.

We wish to commend the continued usefulness of the Bank Secrecy Act Advisory Group ("BSAAG")[8] as a forum for sharing ideas between FinCEN, the SEC, other regulators, FINRA, and the industry, as well as the various sub-committees of the BSAAG, of which SIFMA is an active participant. However, we believe that more attention needs to be given to efforts against terrorist financing and other issues related to the U.S. financial system's security. We therefore recommend the creation of a task force within the BSAAG dedicated to terrorist financing and other issues related to the U.S. financial system's security.

The challenges for industry and law enforcement in detecting terrorist financing are great because of the difficulties of distinguishing terrorist funds from legitimate funds. This is because terrorist activity is often financed with funds derived from legitimate activity. Therefore, we believe that one of the most effective measures against terrorist financing would be enhanced information sharing from government to industry. The goal of a terrorist financing task force within the BSAAG, in part, would be to determine what information – sensitive or otherwise – would be helpful to financial institutions in identifying terrorist financing and how such information could be shared without jeopardizing any national security interest. In short, by strengthening the partnership between government and industry, and maximizing the resources of each, such a task force could be extremely beneficial to protecting investors, our capital markets, and financial systems from being used to fund terrorist activity.

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[7] Specifically, in the context of a relationship between a clearing broker and an introducing broker, the introducing broker's customer's account is called a "correspondent account." In contrast, the statutory definition of a "correspondent account" is specifically applicable to banks, which indicates that the original legislative intent was to focus on establishing anti-money laundering policies for accounts that mirror correspondent banking.

[8] The Bank Secrecy Act Advisory Group ("BSAAG") is a task force established by Congress for industry and regulators to discuss ways to improve anti-money laundering programs, among other things, and advise the U.S. Treasury Department.

C. Create an office within the SEC that is dedicated solely to anti-money laundering and terrorist financing prevention.

SIFMA believes that an office dedicated to the prevention of money laundering and terrorist financing is necessary within the SEC. We first made this recommendation to the SEC in a letter dated May 20, 2003, and many of the bank regulatory agencies have followed this structure.

While a number of SEC staff members have developed expertise in the area of anti-money laundering issues, we believe that this expertise is distributed across three or four different Divisions/Offices within the SEC.[9] This distribution of anti-money laundering responsibilities creates confusion for industry participants who may not understand which Division or Office to approach with anti-money laundering questions and issues. Therefore, we believe that there is a need for a specialized group of SEC staff members with expertise in the anti-money laundering and terrorist financing provisions of the PATRIOT Act.

Specifically, we recommend that the SEC create an office dedicated solely to money laundering and terrorist financing prevention, to centralize expertise, to coordinate and serve as a point of contact with regulators, the SROs, law enforcement, the industry, and within the SEC itself, and to ensure harmonization of anti-money laundering requirements. This office would allow the SEC to focus more resources on anti-money laundering and terrorist financing prevention, and enable coordination of effort among regulators. In addition, such an office would facilitate the examination process and help regulators clarify and avoid inconsistent requirements for the securities industry. We recommend that this office be staffed with personnel having a broad range of expertise, including law enforcement, broker-dealer operations, market regulation, and the inspection and examination processes. Such an office would strongly help the SEC prevent the U.S. financial system from being used by money launderers and terrorists and carry out its other responsibilities.

We understand and appreciate that there has been a good deal of coordination within the SEC on this issue, but we still urge that there be more. To this end, we recommend that the functions of the new office include:

- Coordination with law enforcement and other regulators (and FINRA), both on domestic and international levels, which is essential to ensure harmonization of anti-money laundering requirements;

- Responsibility for interpretation of the PATRIOT Act rules issued and enforced by the SEC. The office should also be tasked, in coordination with Treasury, to continually evaluate the effectiveness of the anti-money laundering regulations and address and quickly respond to the questions of interpretation that are likely to arise as firms undertake efforts to comply with the requirements;

- Training of SEC divisions on anti-money laundering regulations and issues, which would likely include SEC staff involved in examinations, enforcement, investment management, and market

[9] It is our understanding that anti-money laundering responsibilities at the SEC presently are divided among at least the following Divisions and/or Offices: Enforcement Division; Trading and Markets Division; and the Office of Compliance Inspections and Examinations.

regulation. Understanding of the PATRIOT Act requirements by staff throughout the agency is essential to enhance effective compliance and to avoid duplication of efforts and misuse of resources.

- Coordinating with other SEC divisions on examination and enforcement of the PATRIOT Act requirements; and

- Coordinating with industry and providing anti-money laundering education to industry.

D. Improve Information Flow between Regulators, Law Enforcement, and the Industry.

The information flow between regulators, law enforcement and the industry should be improved, including more comprehensive information to assist in detecting suspicious activity. The efforts made by law enforcement up until now, while helpful, should be enhanced.

(1) Information Sharing under Sections 314(a) and (b), and SAR Sharing

Pursuant to PATRIOT Act Section 314(a), Congress authorized FinCEN to adopt regulations for the "specific purpose of encouraging regulatory and law enforcement authorities to share with financial institutions information regarding individuals, entities, and organizations engaged in…terrorist acts or money laundering." By including this provision, Congress clearly intended the federal government and law enforcement, as part of the coordinated effort against money laundering and terrorist financing, to share information with the industry to help it identify suspicious activity. FinCEN's rule implementing Section 314(a), however, does not authorize information sharing between government and industry as mandated by Congress. Instead, the rule merely requires financial institutions to check their records for names provided by the Treasury that may be tied to money laundering or terrorism. As a result, the rule does not create the sharing of information intended by Congress.

The government's providing more and better information is critical to the industry's ability to identify potentially suspicious and unusual activity. Financial institutions do this in part by monitoring transactions across their systems to determine if any particular transaction is unusual or suspicious in nature or may be related to money laundering. The process of monitoring transactional activity is a complex and costly process, but would be enhanced if regulators and law enforcement could provide more information to the industry on a timely basis to make transaction monitoring systems more effective and to help industry identify suspicious activity.

In particular, we recommend that FinCEN provide the following information to industry:

(i) Senior Foreign Political Figures

There needs to be improved coordination between industry and government in efforts to identify accounts or transactions, and monitor the accounts of senior foreign political officials, which the government has stated may pose a higher risk of money laundering. We urge the government now, as we have in the past, to help the industry with respect to the identification of senior foreign political figures because we believe the government is in a better position to identify these persons, and to suggest particular areas for monitoring, through its world-wide intelligence network and with the vast law enforcement resources at its disposal. The industry's efforts in this area would be aided greatly if the government provided a list of all such individuals to financial institutions (perhaps via FinCEN's website).

Such a list could be similar to those issued by the Office of Foreign Assets Control ("OFAC") and could be updated on a regular or ongoing basis, similar to the way in which OFAC issues its updates. We think the government's sharing of such information would be extremely beneficial in identifying possible suspicious activity, and would permit industry to focus more of its resources on "know your customer" practices and monitoring accounts, or on other areas that present the most significant risk, rather than attempting to prepare its own list of senior foreign political figures.

(ii) Offshore Banking Jurisdictions

SIFMA recommends that FinCEN issue a list of known offshore banking jurisdictions that financial institutions can reference to identify offshore banking institutions more efficiently. This is necessary because Section 312 under the PATRIOT Act requires enhanced due diligence for offshore banks. The difficulty is that there is no single source or body of information, to our knowledge, where broker-dealers can look to find information on offshore banking jurisdictions or institutions. Therefore, to comply with the enhanced due diligence requirements under Section 312 of the Act, each financial institution is effectively conducting the same research to identify the jurisdictions that offer offshore banking licenses and each financial institution sustains the cost and delays associated with identifying such jurisdictions. As a result, the process of identifying offshore banking jurisdictions is inefficient and wastes resources that could be better spent elsewhere to address anti-money laundering risk.

We also suggest that financial institutions, as part of the due diligence they are required to do, be allowed to accept representations from foreign banks regarding the types of banking licenses they hold, *i.e.*, stating that they are not offshore banking institutions. We believe this can be done most efficiently by amending the 313/319(b) foreign bank certifications to include such a representation.

(iii) Feedback on Suspicious Activity Reports

We recommend that FinCEN continue to improve the feedback and information provided to financial institutions on SARs that are filed with FinCEN. This is crucial because the PATRIOT Act requires broker-dealers and other financial institutions to monitor for activity that is difficult to detect, *e.g.*, activity that appears to serve no business or lawful purpose or is not the sort in which the particular customer would be expected to engage, as well as the funding of terrorist activity.

Although there is a need for improved information flow between government, law enforcement, and the industry, we appreciate that FinCEN increasingly has provided the industry with useful guidance and information. For example, through its publication of the SAR Activity Review, FinCEN analyzes and discusses suspicious activity with respect to particular topics or types of activity. Additionally, in October 2007, FinCEN provided guidance with respect to information derived from its analysis of SARs filed by Money Services Businesses that is informative for all financial institutions.[10] These are significant accomplishments and should be acknowledged.

While the feedback provided by FinCEN has drastically improved, it is not enough to significantly improve the ability of broker-dealers and other financial institutions to identify potentially suspicious

[10] FinCEN, *Suggestions for Addressing Common Errors Noted in Suspicious Activity Reporting* (Oct. 10, 2007), *available at* http://www.fincen.gov/SAR_Common_Errors_Web_Posting.pdf.

activity. Because the activities – and the money trail – of money launderers are becoming more sophisticated, and at times under "radar" levels, to maximize the industry's ability to effectively monitor transactions to assist law enforcement, we strongly urge the government to provide more feedback as to the suspicious activity reports that have been helpful in law enforcement efforts.

We also believe that there needs to be a better understanding by regulators of the capabilities and limitations of a firm's transaction monitoring systems, and the role that such systems play in overall anti-money laundering compliance. In general, monitoring systems do not provide "one-stop" solutions to detecting suspicious activity. Rather they are systems with limitations that are heavily dependent upon the personnel of each firm. For this reason, we request that the government provide industry with monitoring tips or techniques that will assist firms to identify suspicious activity. Further, regulators should work with the industry to address the difficulties associated with identifying suspicious activity in the context of DVP transactions, where the title to an asset and payment are exchanged simultaneously to minimize the risk associated with settlement. The industry has been attempting to find appropriate types of monitoring to identify suspicious activity in the institutional area, especially DVP accounts. We are aware of no available technological solutions that address these issues.

SIFMA also believes that there should not be restrictions on U.S. financial institutions with respect to SAR sharing with affiliates. While we understand that this is an issue that is under review by the BSAAG, we recommend that FinCEN issue guidance permitting firms to share information with both U.S. and non-U.S. affiliates. Currently, U.S. financial institutions that are subsidiaries of a foreign parent are allowed to share SARs with their foreign parent, as applicable, but not permitted to share with affiliates – even U.S. affiliates. We do not think that a distinction which allows for vertical sharing with non-U.S. parent entities, but not horizontal sharing with U.S. affiliates makes sense.

Additionally, under PATRIOT Act Section 314(b), Congress authorized the sharing of information among financial institutions. The PATRIOT Act provides that information sharing by financial institutions about persons suspected of being involved in money laundering or terrorism is exempt from the privacy provisions of the Gramm-Leach-Bliley Act. We believe that FinCEN's rule regarding information sharing among financial institutions does a good job of achieving the intent of the PATRIOT Act, but needs some fine-tuning. In particular, the scope of institutions permitted to share information is too narrow, limiting the rule's effectiveness. For example, a broker-dealer may have information regarding a suspicious customer that would be beneficial to an investment adviser dealing with the same customer, or vice versa, but investment advisers are not covered under the rule and thus would not be able to engage in information sharing. In addition, the scope of the activities that may be considered possible terrorist or money laundering activity under Section 314(b) is unclear and should be broadened.

(2) Increase Transparency of Examinations

We recommend that there be increased transparency in the examination process because anti-money laundering goals cannot be achieved effectively if regulators do not provide the industry with clear standards. If regulators develop and apply transparent procedures for anti-money laundering and counter-terrorism financing compliance, the process will be more efficient and effective. Further, the examinations by the regulators should measure compliance by a consistent and transparent standard. While FinCEN has taken steps in this direction, more needs to be done. Transparency could be advanced by making the anti-money laundering examination module for the securities industry publicly available as

the banking regulatory agencies have done for some time. Publishing the examination module would allow firms to have a clear understanding of the requirements of the rules, and the levels of compliance the regulators expect.

Additionally, we are concerned that there seems to be a "check the box" approach to examinations. Broker-dealers with various business structures have found the "check the box" approach problematic, as have small firms, which believe certain portions of the PATRIOT Act are not clearly relevant to their business model. Instead, we believe the examination process should include risk-based requirements that reflect the shared goal of regulators and industry to improve compliance. Therefore, we recommend that regulators apply a more outcome-focused and principles-based approach when conducting examinations to determine whether a firm has taken adequate steps to address the specific risk associated with its business.

We believe these recommendations are consistent with FinCEN's regulatory and efficiency initiatives. In fact, under the first of four initiatives announced by Secretary Paulson, FinCEN is commencing a joint effort with the federal bank regulators to ensure that financial institutions and regulators treat compliance obligations in a manner that helps to avoid expenditures that are not commensurate with actual risk[11].

We encourage FinCEN and the SEC to continue improving the transparency of the examinations and enforcement process and to develop a more principles-based approach that focuses on the specific risks associated with a particular firm and its business.

E. Increase Coordination Among Domestic and International Regulators.

We strongly recommend that that there be increased coordination between and among regulators, both on domestic and international levels. Greater coordination is essential to ensure harmonization of anti-money laundering requirements, to enhance effective compliance, and to avoid duplication of efforts and misuse of resources. We note that Treasury itself has stressed the need for interagency coordination in conducting anti-money laundering policy in its 2007 National Money Laundering Strategy.

(1) Coordination between U.S. Regulators

We believe that to improve coordination, regulators must work hand-in-hand to achieve effective regulation. Coordination is particularly necessary with respect to the securities industry because broker-dealers are subject to regulation not only by Treasury, but also by the SEC, FINRA, and other regulators. The division of responsibility between Treasury, which has primary responsibility for anti-money laundering policy, and the SEC (in conjunction with the SROs), which is the primary and functional regulator, makes this coordination crucial. While Treasury is intimately familiar with the mandates of the PATRIOT Act, it is the SEC that understands the securities business, the diverse types of broker-dealers, and the many ways in which the securities business operates. Effective anti-money laundering policies that fully appreciate the impact on broker-dealers – the changes to their systems, the resources available

[11] To this end, on July 19, 2007, the federal financial regulatory agencies issued the *Interagency Statement on Enforcement of Bank Secrecy Act/Anti-Money Laundering Requirements*, setting forth the agencies' policy for enforcing specific anti-money laundering requirements of the BSA and aiming to provide greater insight into the considerations that form the basis of enforcement decisions in BSA matters.

and the time needed to adjust – can only be achieved if there is complete collaboration between and among the various regulators.

On a practical level, "coordination" means that the regulation of anti-money laundering policies must be effected so that securities firms are not subject to duplicative rules, overlapping examinations, varying interpretations, concepts not applicable in the securities industry and multiple enforcement actions. To achieve efficient and effective regulation, the regulators must not only work hand-in-hand, but delegate appropriate functions to one another. Such coordinated efforts will lead to an effective partnership with the industry, culminating, hopefully, in the resources of each maximized to their fullest extent to combat illicit activity.

(2) Coordination between Regulators Internationally

Our government must also work multi-laterally to develop international anti-money laundering standards which promote cooperation and efficacy, but at the same time respect issues of nationality and the unique concerns of particular jurisdictions.[12] While we recognize the efforts of U.S. regulators to date, we recommend even greater coordination by FinCEN, as well as other U.S. regulators, on the international level. This is especially so because our markets and our member firms are becoming increasingly global and less defined by jurisdictional boundaries. As a result, some firms that have a global presence have attempted to reconcile their procedures throughout the world so that clients can deal with them on a global basis.

Anti-money laundering policymaking should also take into account the extra-territorial application and effect of the PATRIOT Act and other U.S. anti-money laundering laws. Our members have well-founded concerns that their obligations under the PATRIOT Act could well conflict with obligations under the laws of other jurisdictions. For example, many global firms struggle with the definition of beneficial ownership. Depending on the jurisdiction, anti-money laundering requirements are either silent on the issue of what percentage of interest constitutes beneficial ownership or establish varying percentage requirements. These and similar issues must be considered in the formulation of U.S. anti-money laundering policy, and industry input should be solicited. We therefore recommend that FinCEN issue guidance to the industry regarding how broker-dealers and other financial institutions can comply with applicable requirements under the PATRIOT Act when such requirements create a conflict of law with the privacy or anti-money laundering requirements of another country.

SIFMA and its member institutions are committed to assisting the U.S. government and international cooperating bodies, such as FATF, in deterring and preventing money laundering and terrorist financing.

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[12] Indeed, a May 2006 GAO report found that the U.S. interagency community, guided by Treasury, is accomplishing negotiations with foreign jurisdictions through U.S. interaction with the Financial Action Task Force on Money Laundering ("FATF").

F. Enhance the ability of U.S. broker-dealers and other financial institutions to rely on the customer identification and other anti-money laundering procedures of other regulated and/or reputable financial institutions.

It is commonplace for broker-dealers to engage in various types of routine business transactions with other financial institutions in which both parties are providing services to the same customer. In some instances, both financial institutions have a separate relationship with the same customer but provide services in tandem, for example, where an institutional customer transacts with both its prime broker and an executing broker. In other instances, one financial institution is introduced to the customer by the other which is serving essentially as a financial intermediary, e.g., purchases or redemptions of mutual fund shares that are conducted through a "financial intermediary." Where both financial institutions transact business with the same customer, SIFMA recommends that FinCEN permit broker-dealers and other financial institutions to rely on those other financial institutions and intermediaries for purposes of meeting their anti-money laundering obligations, including customer identification obligations under the Customer Identification Program ("CIP") Rule. Of course, in all circumstances, the reasonableness of a broker-dealer's reliance would be determined by a risk-based analysis of the nature of the other financial institution and, where appropriate, the results of the broker-dealer's due diligence into the financial institution. As discussed below, reliance may be appropriate when the financial intermediary is a U.S. financial institution that is subject to anti-money laundering requirements, a foreign financial institution that is subject to anti-money laundering requirements similar to the PATRIOT Act, or an affiliate that is subject to the firm's global AML program.

We appreciate that FinCEN and the SEC have recognized that there are appropriate circumstances in which a broker-dealer should be able to rely on another regulated U.S. financial institution's performance of some or all of its CIP, particularly given that both institutions are subject to the same anti-money laundering regulations. For purposes of the CIP Rule, however, SIFMA believes that it should not be necessary for a broker-dealer to obtain a written reliance agreement, when dealing with another U.S. regulated financial institution, which is itself subject to the PATRIOT Act. In such circumstances, it makes no sense to us that a regulated financial institution must obtain a written reliance agreement rather than just confirm that the other entity is subject to such regulation. Thus, we suggest that FinCEN examine the kinds of relationships where reliance agreements are used, whether they could be more easily replaced by representation letters, whether they need to be annually re-certified, assess whether reliance agreements could be more useful, or alternatively, determine whether reliance agreements should be necessary at all between regulated financial institutions.

Additionally, we believe that there may be appropriate circumstances in which a broker-dealer should be able to rely on the anti-money laundering compliance efforts and customer identification procedures of the foreign financial institutions with which it has a customer or business relationship. FinCEN's AML Program and CIP Rules have not fully incorporated a risk-based approach regarding U.S. securities firms' ability to rely on such foreign financial institutions. The importance of adopting a risk-based approach with respect to foreign financial institutions cannot be over-emphasized given our increasingly global markets and the complexity of financial transactions. Therefore, we strongly suggest that broker-dealers be permitted to rely on the representations and due diligence efforts of reputable foreign financial institutions, such as broker-dealers, banks, and investment advisers that are themselves subject to comprehensive laws and regulations similar to the PATRIOT Act. While many firms dealing with a foreign financial institution presently incorporate into their own anti-money laundering procedures

an assessment that takes into account whether the foreign financial institution is located in a jurisdiction with sound anti-money laundering laws, it would be helpful if the U.S. government would recognize the efficacy of these procedures.

Likewise, SIFMA believes it is particularly important – and appropriate – for FinCEN to permit broker-dealers and other financial institutions, subject to a risk-based approach, to rely on the CIP and other anti-money laundering steps taken by their domestic and foreign affiliates, regardless of whether they are regulated. We believe this recommendation is consistent with the goal of increasing efficiency because no purpose is served by having two affiliated financial institutions – operating under essentially the same global firm-wide anti-money laundering policies and procedures – duplicate efforts to perform the same identification steps on the same customer. Absent the ability to rely, the two institutions must conduct parallel and redundant verification and diligence efforts. Broker-dealers and other financial institutions that are able to rely on an affiliate's customer identification procedures may redirect limited resources to other areas that present a higher risk.

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IV. CONCLUSION

We hope that the Treasury, FinCEN, and the SEC can facilitate our recommendations set forth in this letter. SIFMA stands ready to work with you to provide any necessary support. We are committed to a strong partnership between government and industry, culminating, hopefully, in the resources of each being maximized to their fullest extent to combat illicit activity. The infiltration of ill-begotten funds into our financial system only serves to undermine our economy and investor confidence. We look forward to continuing to work with Treasury, FinCEN, and the SEC to strengthen the regulatory structure surrounding securities firms and other U.S. financial institutions.

We greatly appreciate the opportunity to share our views on the PATRIOT Act and anti-money laundering regulation. If you wish to receive additional information or to schedule a meeting to discuss these comments, please feel free to contact the undersigned.

Sincerely,

Alan E. Sorcher
Managing Director and
Associate General Counsel
Securities Industry and
Financial Markets Association

cc: The Honorable Christopher Cox, Chairman, SEC
The Honorable Paul S. Atkins, Commissioner, SEC
The Honorable Kathleen L. Casey, Commissioner, SEC
Lori Richards, Director, Office of Compliance Inspections and Examinations, SEC
Karen Burgess, Senior Advisor, Office of Compliance Inspections and Examinations, SEC
Lourdes Gonzalez, Assistant Chief Counsel, Sales & Practices, SEC

Jamal El-Hindi, Associate Director for Regulatory Policy and Programs, FinCEN
Beverly Loew, Regulatory Policy Specialist, FinCEN

Michael G. Rufino, Senior Vice President, FINRA

APPENDIX A

SIFMA'S ADDITIONAL COMMENTS ON PARTICULAR PATRIOT ACT RULES

SIFMA and its members support active engagement with FinCEN concerning Treasury's initiative to improve the efficiency and effectiveness of the regulatory administration of the Bank Secrecy Act. In addition to the comments in our letter, we recommend that the comments below be considered to improve the efficiency and effectiveness of the PATRIOT Act rules as applied to broker-dealers:

A. CIP - With respect to broker-dealers

(1) *CIP Guidance:* Given the complexity of transactions in the securities industry, it is often not clear who the customer is for purposes of the CIP requirements. In particular, determining who the customer is on the institutional side of the business can be difficult. Guidance needs to be issued on the different kinds of relationships to help clarify where customer relationship exists.

(2) *CIP Notice:* Section 326 provides that financial institutions must give their customers adequate notice of their identity verification procedures. As we understand it, CIP verification notice is meant to address privacy concerns with respect to customers who are individuals. However, those concerns are not present when the customer is an institution, although the rule still applies. Moreover, due to the nature and speed of transactions, notice to such institutional clients is difficult to give prior to the opening of the account. Given our belief that such notice to sophisticated institutional clients is unnecessary and burdensome, we recommend that the CIP Notice requirement be eliminated for customers that are institutions.

B. Rule 311 (Special Measures Notices)

(1) *Eliminate the 311 Special Measures Notice Requirement*

The Section 311 Special Measures require a financial institution to notify all of its foreign bank correspondent account holders that they may not provide any institution that has been determined to be of primary money laundering concern with access to their correspondent account. We believe this provision is unnecessarily burdensome, redundant, and not an effective way of achieving the goals of the special measures.

Given that many U.S. financial institutions have thousands of correspondent accounts, it is an extremely inefficient use of resources to provide notice to all such account holders. Moreover, many foreign banks are inundated with the same notification from many different U.S. financial institutions that are required to send the notice because they have correspondent relationships with these firms.

SIFMA has raised the issue of the usefulness of the correspondent account notice requirement contained in many of the Section 311 Special Measures notices in various comment letters and through the BSAAG's Securities and Futures Subcommittee. We recommend that FinCEN reconsider the necessity of the notice provision under existing special measures and not include such requirement in future 311 notices.

(2) *Utilize Alternate Means of Notice*

If FinCEN determines notice by financial institutions is necessary in some situations, we suggest that FinCEN allow sufficient flexibility for firms to utilize systems already established under other provisions of the PATRIOT Act to give such notice. This will allow firms to build on current systems to provide notice efficiently and effectively. For example:

(i) FinCEN could permit the inclusion of a notice provision in the certificates utilized by financial institutions as part of their compliance with Sections 313 and 319 of the PATRIOT Act, as an appropriate means of meeting this requirement. Some firms have already included 311 notice in their procedures designed to satisfy Sections 313 and 319 through Foreign Bank Certifications; or

(ii) Financial institutions could include a first-time 311 notice to customers as part of their CIP notice. For example, they could post 311 notices on their website, advising customers to review the Federal Register for information regarding Section 311 Special Measures.

(iii) Additionally, firms could provide notice to certain correspondent accounts on a risk-based basis.

C. Sections 313/319(b) Rule (Shell bank prohibitions and foreign bank ownership/agent requirements)

(1) In enacting two key provisions (Sections 313 and 319(b)) of the PATRIOT Act that are directed at "correspondent accounts" with foreign shell banks and foreign banks, Congress was concerned about the risks posed by unregulated foreign shell banks that evade regulatory scrutiny because they lack a physical presence. Congress was also concerned about unidentified owners of foreign banks or funds that might be tied to money laundering or terrorist activities. We continue to recommend the creation of an Internet site containing a listing of foreign banks, known shell banks, countries that permit shell banks and foreign banks that indirectly provide banking services to shell banks.

(2) We also recommend, as others have as well, the creation of an Internet site where foreign banks can post and update their model certification forms, which could be relied upon by covered financial institutions, or any comparable methods. These mechanisms would greatly help eliminate unnecessary duplication in recordkeeping that is occurring throughout the industry as firms comply with the shell bank and recordkeeping provisions.

(3) *Renewal Process:* The issue of foreign bank certifications comes up frequently in anti-money laundering examinations. SIFMA believes the renewal process for foreign bank certifications is very burdensome and offers little benefit to the overall effort to deter money laundering and illicit activity. Once firms have a Foreign

> Bank Certification on file, we recommend that firms should not be required to obtain renewals of the Foreign Bank Certification absent actual notice of any changes in the information provided by the foreign bank.

Although these rules are now final, we hope Treasury will continue to listen to industry's experience and re-examine the rule's effectiveness. Industry and government efforts should focus on the development of rules that strike an appropriate balance between advancing the PATRIOT Act's goals of identifying funds from foreign banks that may be tied to money laundering and avoiding unnecessary burdens on financial institutions or discouraging legitimate foreign investment in U.S. financial markets.

Appendix B
SIFMA Comment Letters on BSA and PATRIOT Act Rules

1. Letter dated March 6, 2006 to FinCEN regarding proposed regulation that would implement certain provisions of Section 312 of the USA PATRIOT Act.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/11414.pdf

2. Letter dated March 3, 2006 to FinCEN requesting extension to implement due diligence provisions for new accounts under rule 312 of the USA PATRIOT Act.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/10796.pdf

3. Letter dated February 23, 2006 to FinCEN for clarification of due diligence provisions for new accounts under Rule 312 of the USA PATRIOT Act.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/10797.pdf

4. Letter dated December 7, 2005 regarding the Depository Trust Company Notice of filing of proposed rule change relating to compliance with regulations administered by the Office of Foreign Assets Control.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/9319.pdf

5. Letter dated July 27, 2005 to SEC regarding notice of proposed rule changes relating to amendments to NASD Rule 3011 and the adoption of related interpretive material and amendments to NYSE Rule 445.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/7380.pdf

6. Letter dated July 26, 2005 to FinCEN regarding proposed revision to suspicious activity report by the Securities and Futures Industries (SAR-SF).
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/7379.pdf

7. Letter dated May 25, 2005 to FinCEN regarding proposed special measures against Multibanka and VEF Banka as primary money laundering concerns.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/6556.pdf

8. Letter dated September 23, 2004 to FinCEN regarding two proposals concerning the imposition of special measures against Infobank and First Merchant Bank OSH Ltd as primary money laundering concerns.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30452742.pdf

9. Letter dated June 17, 2004 to FinCEN regarding the imposition of special measure against Commercial Bank of Syria as primary money laundering concern.
   http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30452760.pdf

10. Letter dated January 6, 2004 to SEC regarding no action relief with regard to the PATRIOT Act CIP Rule.
    http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30452552.pdf

11. Letter dated April 21, 2003 to FinCEN regarding the expiration of a conditional exception to certain requirements of the regulations under the Bank Secrecy Act.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30530672.pdf

12. Letter dated March 7, 2003 to Treasury regarding recommendations for improvements to the anti-money laundering provisions under the USA Patriot Act.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30502207.pdf

13. Letter dated January 27, 2003 to Treasury filed by the New York Clearing House, SIA, and the Banker's Association for Finance and Trade regarding designations under section 311 of certain jurisdictions as primary money laundering concerns.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30502214.pdf

14. Letter dated October 4, 2002 to Treasury regarding the proposed suspicious activity form for the securities and futures industry.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597133.pdf

15. Letter dated September 10, 2002 to Treasury and the SEC regarding section 326 establishing identification and verification procedures for all new account openings.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597190.pdf

16. Letter dated August 22, 2002 to Treasury regarding the interim rule under section 312 requiring broker-dealers to establish enhanced due diligence requirements for private banking accounts.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597138.pdf

17. Letter dated July 1, 2002 filed by SIA and other trade associations regarding section 312 establishing enhanced due diligence requirements on foreign correspondent and private banking accounts.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597196.pdf

18. Letter dated April 3, 2002 to Treasury regarding section 314 requiring financial institutions to respond to requests from Treasury's Financial Crimes Enforcement Network and authorizing financial institutions to share with each other information concerning persons or entities suspected of terrorist activities or money laundering.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597150.pdf

19. Letter dated March 18, 2002 to the SEC regarding rules under section 352 by the New York Stock Exchange and NASD requiring firms to establish anti-money laundering compliance programs.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30599750.pdf

20. Letter dated March 1, 2002 to Treasury regarding section 356 requiring broker-dealers to file suspicious activity reports.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597161.pdf

21. Letter dated February 11, 2002 to Treasury regarding section 313 and 319(b) prohibiting "correspondent accounts" with foreign shell banks and certain recordkeeping for "correspondent accounts" with foreign banks.
http://www.sifma.org/regulatory/comment_letters/comment_letter_archives/30597168.pdf