

FFIEC Issues New Procedures on Examining Financial Institutions for Compliance with FinCEN's CDD Rule, while FinCEN and Congressional Review Continues

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On May 11, 2018, the [customer due diligence rule](#), 31 C.F.R. § 1010.230 (the “**CDD Rule**”), issued by the Financial Crimes Enforcement Network (“**FinCEN**”) became applicable two years after it was issued. The CDD Rule added a new requirement for covered financial institutions to identify, and verify the identity of, the beneficial owners of certain of their legal entity customers, as discussed in our prior memoranda on the [CDD Rule](#) and on the [first](#) and [second](#) sets of FinCEN FAQs related to the rule. It also clarified and enhanced CDD requirements for financial institutions.

FFIEC Guidance

On the same day the CDD Rule went into effect, the Federal Financial Institutions Examination Council (“**FFIEC**”) released an [updated version](#) of the “Customer Due Diligence — Overview and Examination Procedures” section of the FFIEC’s [Bank Secrecy Act/Anti-Money Laundering Examination Manual](#) (the “**FFIEC Manual**”), which was previously issued on December 2, 2014. In addition, the FFIEC developed a new section, [Beneficial Ownership Requirements for Legal Entity Customers – Overview and Examination Procedures](#),” which provides highly anticipated guidance on how the federal bank examiners will conduct examinations for compliance with the CDD Rule’s requirement for financial institutions to identify and verify the beneficial owner(s) of legal entity customers.

The changes to the CDD section, and the new beneficial ownership section, of the FFIEC manual generally track the CDD Rule and FinCEN’s FAQs. The FFIEC noted in its [release](#) that the procedures were developed in close collaboration with FinCEN and the Treasury Department. Significantly, these sections:

- Reiterate and clarify that in circumstances where a legal entity customer opens multiple accounts, “a bank may rely on the pre-existing beneficial ownership records it maintains, provided that the bank confirms (verbally or in writing) that such information is up-to-date and accurate at the time each account is opened.”
- Clarify that “a bank need not establish the accuracy of every element of identifying information obtained” but must verify enough information to form a reasonable belief that it knows the true identity of the beneficial owner(s) of the legal entity customer.
- Advise examiners to “primarily focus on whether the bank has effective processes to develop customer risk profiles as part of the overall CDD program” rather than individual customer risk decisions. In those instances where the bank has an established and effective customer risk decision-making process, and has followed its existing processes, the bank “should not be criticized for individual customer risk decisions unless it impacts the effectiveness of the overall CDD program, or is accompanied by evidence of bad faith or other aggravating factors.”
- Reiterate that the collection of customer information regarding beneficial ownership is governed by the requirements specified in the CDD Rule, which establishes a 25 percent ownership threshold regardless of the customer’s risk profile. The FFIEC guidance further clarifies that “[o]ther than required beneficial ownership information, the level and

type of customer information should be commensurate with the customer's risk profile, therefore the bank should obtain more customer information for those customers that have a higher customer risk profile and may find that less information for customers with a lower customer risk profile is sufficient" (emphasis added).

While the new and updated sections of the FFIEC manual do not answer all the industry's questions about enforcement of the CDD Rule, they should provide some comfort that examiners are not generally expected to penalize good faith decisions regarding individual customers or require a lower than 25 percent beneficial ownership threshold for higher risk customers.

FinCEN Ruling: Temporary Exceptive Relief for Rollovers and Renewals

In addition, on May 16, 2018, FinCEN issued a [ruling](#) to provide a 90-day limited exceptive relief to covered financial institutions from the obligation to identify and verify beneficial ownership information with respect to certain financial products and services that automatically rollover or renew (*i.e.*, certificate of deposits ("**CDs**") or loan accounts) that were established before May 11, 2018. FinCEN explained that it is granting the temporary exception because it "believes that further consideration of this issue is appropriate," given the concern that some covered institutions have expressed over their ability to comply with the beneficial ownership requirements with respect to CD rollovers and loan renewals.

This exception begins, retroactively, on May 11, 2018, and will expire on August 9, 2018. During this time, FinCEN will determine whether and to what extent additional exceptive relief may be appropriate.

House Hearing on Implementation of CDD Rule

Like FinCEN, Congress continues to consider the scope and impact of the CDD Rule. On May 16, 2018, the House Financial Services Committee held a [hearing](#) entitled "Implementation of FinCEN's Customer Due Diligence Rule" in which several Republican representatives raised concerns about the costs and burdens imposed by the CDD Rule. Significantly, in his [written testimony](#), FinCEN Director Kenneth Blanco stated that, although FinCEN expected covered institutions to be ready on May 11, 2018 to begin timely and effective implementation of the CDD Rule requirements, FinCEN also understands that "institutions, regulators, and other stakeholders may need a little extra time to smooth out any wrinkles." He noted that FinCEN will provide further guidance, if necessary, as "new questions often emerge after implementation begins," adding that "we will continue to work with industry and regulators to understand and help address any concerns."

Law Clerk Brooklynn Moore contributed to this post.

If you have any questions regarding the matters covered in this publication, please reach out to any of the lawyers listed below or your usual Davis Polk contact.

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