

REGULATORY ALERT

NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22134

DATE: October 1998

NO: 98-RA-7

TO: ALL FEDERALLY INSURED CREDIT UNIONS

RE: FinCEN Advisory No. 10

The Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) has published the *FinCEN Advisory*, Issue 10. The subject is "Reformed CTR Exemption Process: Questions & Answers". Treasury has requested NCUA's assistance in distributing the information to all federally insured credit unions. The *FinCEN Advisory* is designed to keep financial institutions, regulatory agencies and law enforcement agencies advised of the trends and developments related to money laundering and financial crime. Advisories will be published periodically and will be distributed to all federally insured credit unions as part of NCUA's effort to keep you informed.

This *Advisory* provides answers to general questions concerning implementation of the new regulation for exemptions from the requirement to report transactions in currency. The Department of the Treasury's rule was forwarded to all federally insured credit unions in Regulatory Alert No. 98-RA-6, dated October 1998.

Comments about the *FinCEN Advisory* should be addressed to the Financial Crimes Enforcement Network, Office of Communications, U.S. Department of the Treasury, 2070 Chain Bridge Road, Vienna, VA 22182 or faxed to (703) 905-3885.

Sincerely,

/S/

Norman E. D'Amours
Chairman

Enclosure



United States Department of the Treasury
Financial Crimes Enforcement Network

FinCEN Advisory

Subject:
**Reformed CTR
Exemption
Process:
Questions &
Answers**

Date:
**October
1998**

Advisory:
Issue 10

This advisory provides answers to several questions concerning the process by which financial institutions may exempt retail and other businesses from the requirement to report currency transactions exceeding \$10,000.

On September 21, the Treasury Department's Financial Crimes Enforcement Network (FinCEN) published a final rule which will substantially revise and simplify the manner in which banks and other depository institutions may be relieved of the obligation to file recurring Currency Transaction Reports (CTRs) on many of their customers. This rule represents the second part of FinCEN's effort to significantly reduce the number of times depository institutions must report large currency transactions. An earlier rule was aimed primarily at larger national and regional customers; this rule further simplifies the process for retail and other businesses.

Financial institutions have until July 1, 2000, to phase in compliance with the simplified procedures, although they may use the new procedures beginning on October 21, 1998.

Background

Eliminating Paperwork

The requirement that financial institutions report currency transactions in excess of \$10,000 by their customers is a cornerstone of the Bank Secrecy Act. The information provided on CTRs is often vital to investigators. At the same time, the reporting requirement includes recurring transactions by legitimate cash intensive businesses that generally are of little interest to investigators. The Money Laundering Suppression Act (MLSA) asked Treasury to study and implement new programs to encourage banks to take the steps necessary to significantly reduce repetitive currency reporting on these kinds of transactions.

More than 12 million CTRs were filed in 1997. It is anticipated that implementation of the procedures in the two regulations could lead banks to decrease their CTR filings by more than the 30 per cent reduction sought in the MLSA.



New Process

The new final rule permits financial institutions to exempt a domestic business that has routine needs for large amounts of currency by simply filing a form stating that the business is exempt, so long as the business has been a customer for at least one year.

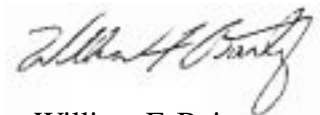
The new procedures may be used by all depository institutions, banks, thrifts, and credit unions, but not by other financial institutions. This rule does not exempt financial institutions from reporting suspicious activity involving these exempted entities. In addition, certain categories of businesses, such as real estate brokers, automobile dealers, and money transmitters, may not be exempted.

The exemption of the businesses covered by the new rule must be renewed every two years, but a proposed requirement that financial institutions include information about a customer's total currency transactions on the renewal form has been eliminated as unduly burdensome and unnecessary; now banks must simply indicate that they have maintained a system of monitoring the transactions in the account for reportable suspicious activity and applied the system to accounts at least annually.

Working Together

FinCEN has worked closely with the American Bankers Association and other groups to simplify and reform our regulatory programs so that they are cost-effective, not burdensome. We look forward to continuing these discussions as we all work together to determine how best to fight money laundering.

The attached guidance is intended to answer general, basic questions concerning the implementation of the new regulations. It is not meant to be comprehensive and does not replace or supersede the regulations.



William F. Baity
Acting Director

Attachment

FinCEN Advisory is a product of the Financial Crimes Enforcement Network, U.S. Department of the Treasury, 2070 Chain Bridge Road, Vienna VA 22182, (703) 905-3773. For more information about FinCEN's programs, visit the FinCEN web site at <http://www.treas.gov/fincen>.

Questions or comments regarding the contents of the FinCEN Advisory should be addressed to the Office of Communications, FinCEN.

Information may also be faxed to (703) 905-3885.

GUIDANCE FOR BANKS ON THE REFORMED CTR EXEMPTION PROCEDURES

On September 21, 1998, the Treasury Department's Financial Crimes Enforcement Network ("FinCEN"), published a final rule which substantially revises and simplifies the manner in which banks and other depository institutions (referred to throughout this document as "banks") may be relieved of the obligation to file currency transaction reports ("CTRs") on many of their customers. This guidance is intended to answer general, basic questions concerning the implementation of the new regulations. It is not meant to be comprehensive and does not replace or supersede the regulations.

1. What are the reformed exemption procedures?

The rule published in the Federal Register on September 21, 1998 (63 FR 50147) contains the second stage ("Phase II") of the process to revise and streamline the procedures by which banks may exempt a transaction in currency in excess of \$10,000 from the requirement to file a CTR. The Phase II exemption procedures become effective October 21, 1998.

In September 1997, FinCEN published the final rule for the first stage ("Phase I") of the process to reform the CTR exemption procedures. The new procedures resulting from the Phase I and Phase II rulemakings are collectively referred to throughout this document as "the reformed exemption procedures." The reformed exemption procedures are located at 31 CFR 103.22(d); copies of the new procedures also can be obtained from FinCEN's website at "www.treas.gov/fincen/".

2. Do the reformed exemption procedures apply to all classes of financial institutions?

The reformed exemption procedures apply only to banks, as that term is defined by 31 CFR 103.11(c). Under that definition, the reformed exemption procedures apply to commercial and private banks, savings and loan associations, thrift institutions, and credit unions.

3. What are the benefits of the reformed exemption procedures?

Under these new procedures, transactions involving customers that fall within one of the defined classes of exempt persons defined by the new rules are exempt from the CTR requirement. The reformed exemption procedures eliminate the requirement that banks determine whether daily transactions exceed a predetermined exemption amount and also eliminate the requirement that banks obtain signed exemption statements from each exempt customer. These were two of the more unwieldy features of the old exemption system. Generally, a bank seeking to exempt a transaction from the CTR requirement need to make only a one-time filing of a document that

identifies the exempt person and the exempting bank; for customers exempted under Phase II (as explained below), the filing must be renewed every two years. Under the reformed procedures, a bank is not liable for a failure to file a CTR with respect to a transaction in currency by an exempt person, unless the bank knowingly files false or incomplete information or has reason to believe that the customer in question does not qualify as an exempt person.

4. What customers can qualify as exempt persons?

Exempt persons are defined as:

Phase I categories

- other banks operating in the United States;
- federal, state or local government departments and agencies, and federal, state or local entities otherwise exercising governmental authority;
- entities listed on the major national stock exchanges;
- certain subsidiaries of the entities listed on those stock exchanges;

Phase II categories

- non-listed businesses; and
- payroll customers.

However, for entities listed on the major national stock exchanges, certain subsidiaries of the entities listed on those stock exchanges, non-listed businesses, and payroll customers, such entities may only be treated as exempt persons to the extent of their domestic operations.

5. What are non-listed businesses and payroll customers?

Non-listed businesses and payroll customers were added as categories of exempt persons by the Phase II rulemaking. The addition of non-listed businesses as a new category of exempt person is intended to capture all established bank customers not included within Phase I with recurring needs for large amounts of currency to support their commercial enterprises in the United States. Thus, for purposes of the new exemption procedures, a non-listed business is defined as an enterprise that: (i) has maintained a transaction account at the bank for at least 12 months, (ii) frequently engages in transactions in currency in excess of \$10,000, and (iii) does business in the United States.

The definition of a payroll customer was adopted, without significant change, from the terms of the old exemption system and tracks the language used to define a non-listed business. Thus, a payroll customer is defined under the reformed exemption procedures as a person that has maintained a transaction account at the bank for at least 12 months, operates a firm that regularly withdraws more than \$10,000 in order to pay its United States employees in currency, and is doing business in the United States.

6. For purposes of determining whether a customer has maintained a transaction account for at least 12 months, may a bank consider non-consecutive periods during which a customer previously maintained such an account?

The reformed exemption procedures contemplate generally that for purposes of treatment as a non-listed business or payroll customer, a customer must have maintained a transaction account for at least 12 consecutive months. However, there may be special situations in which a bank may count non-consecutive months within the scope permitted by the operating rules governing the reformed exemption procedures. For example, two recent, non-consecutive monthly periods separated by a brief period during which a customer may have temporarily switched his or her account to another bank, may be counted when calculating the requisite 12-month period.

7. How does a bank designate a customer as an exempt person?

FinCEN soon will issue a new form, that once issued, must be used when designating a customer as an exempt person. That form will be available to both hard-copy filers and magnetic media filers. That form also will provide the vehicle for banks to make the biennial renewal (including the provision of information relating to the change in ownership of an exempt customer) required with respect to its Phase II exempt customers and to provide notice of exemptions that have been revoked. FinCEN anticipates that banks will be able to use the new form beginning on January 1, 1999.

Until that new form is issued, a bank must file Internal Revenue Service Form 4789 (the form now used to file a CTR), in which line 36 is marked "Designation of Exempt Person" and items 2-14 (Part I, Section A) and items 37-49 (Part III) are completed. It is very important that this phrase appear on the CTR form exactly as specified above, without abbreviations, substitutions or other modifications. Generally, the designation must be made separately by each bank that treats the customer in question as an exempt person. (See Q&A # 14 for an exception for affiliated banks.)

A bank must make the designation of exempt person within 30 days of the first reportable transaction in currency with that person sought to be exempted from reporting under the reformed exemption procedures. When filing this initial designation of exempt person, a bank need not include specific information about the nature and amount of the transaction in currency itself.

The reformed exemption procedures contemplate a special procedure for use by banks when exempting other banks. A suitable form has not yet been developed for this purpose. FinCEN will consider any suggestions as to the nature of the form to be used in this regard.

8. Are there any special procedures applicable only to non-listed businesses and payroll customers?

For non-listed businesses and payroll customers, a bank must establish and maintain a monitoring system that is reasonably designed to detect, for each transaction account of those customers, those transactions in currency that would require a bank to file a suspicious transaction report, and must certify every two years that it has applied, at least annually, such a monitoring system to each transaction account of those customers. That certification must be done as part of the biennial renewal described in Q&A #7.

9. Are certain businesses ineligible for treatment as non-listed businesses?

Yes. A business engaged primarily in one or more of the activities listed in 31 CFR 103.22(d)(6)(viii) may not be treated as a non-listed business for purposes of the reformed exemption procedures (although it may be treated as an exempt person if it otherwise meets the definition of another class of exempt person — e.g., a casino whose stock is listed on the New York Stock Exchange may be treated as an exempt person). A business that engages in multiple business activities may be treated as a non-listed business so long as no more than 50% of its gross revenues per year is derived from one or more of the ineligible business activities listed below. Thus, a grocery store that devotes only a part of its business to cashing checks on behalf of its customers would, if it otherwise meets the applicable requirements, be eligible for treatment as a non-listed business.

Ineligible business activities are:

- serving as financial institutions or agents of financial institutions of any type;
- the purchase or sale to customers of motor vehicles of any kind, vessels, aircraft, farm equipment or mobile homes;
- the practice of law, accountancy, or medicine;
- the auctioning of goods;
- chartering or operation of ships, buses, or aircraft;
- pawn brokerage;
- gaming of any kind (other than licensed pari-mutuel betting at race tracks);
- investment advisory services or investment banking services;
- real estate brokerage;
- title insurance and real estate closings;
- trade union activities; and
- any other activities that may be specified by FinCEN.

10. What sorts of steps should a bank take to document and verify the status of a customer it has designated as an exempt person?

Generally, a bank must take such steps to assure itself that a person is an exempt person that a reasonable and prudent bank would take and document to protect itself from loan or other fraud based on misidentification of a person's status. At a minimum, a bank is required to review and verify the information supporting each designation of exempt person at least once each year. Assuming that a bank takes those steps described above, and absent any specific knowledge of information indicating that a customer no longer meets the requirements of an exempt person, a bank satisfies the terms of the reformed exemption procedures to the extent it continues to treat that customer as an exempt person until the customer's next, no less than annual, periodic review. In the case of the requirement to maintain a system for monitoring the accounts of non-listed businesses and payroll customers for suspicious activity, a bank must take such steps that a reasonable and prudent bank would take and document to identify suspicious transactions.

11. What kind of documentation is required to be maintained by the reformed exemption procedures and how long must such documents be kept?

A bank is required to take such steps to document the basis for its conclusions that a customer is an exempt person and document its compliance with the terms of the reformed exemption procedures, that a reasonable and prudent bank would take and document to protect itself from loan or other fraud or loss based on misidentification of a person's status. Records documenting a bank's exemption decisions must be maintained for five years.

12. What is the relationship between the reformed exemption procedures and the obligation of a bank to file, where appropriate, a suspicious activity report ("SAR")?

The reformed exemption procedures do not, in any way, lessen the obligation of a bank to file, where appropriate, a SAR with regard to the activities of any of its exempt customers. Thus, for example, a sharp increase from one year to the next in the gross total of currency transactions made by an exempt customer (including those designated as exempt persons because they are listed on an applicable national stock exchange), or similarly anomalous transaction trends or patterns in the accounts of an exempt customer, may trigger the obligation of a bank to file a SAR. The requirement for a bank, with respect to its exempt customers that are non-listed businesses or payroll customers, to maintain a monitoring system to detect suspicious activity does not by implication limit the obligation of a bank to comply with its SAR requirements under 31 CFR 103.21 with respect to its other exempt customers.

13. Is a bank required to treat all transaction accounts of a customer as a single account for purposes of determining the qualification of that customer as an exempt person?

No. A bank may, but is not required to, treat all transaction accounts of a customer as a single account for purposes of determining whether that customer qualifies as an exempt person, as defined by 31 CFR 103.22(d)(2). Treatment of multiple accounts as a single account must, if adopted, be continued. For example, a bank that chose to treat all of a customer's transaction accounts as a single account would combine the transaction history of the accounts to apply the requirement that a business must frequently engage in transactions in currency in excess of \$10,000 in order to be treated as non-listed business customer, but it would then be required to exempt all such accounts, not simply one of them.

Whatever treatment a bank adopts for multiple accounts, the ineligible business activity rule described in Q&A #9 above applies on a customer-wide basis (gross revenues per year).

14. Can a bank designate a customer as an exempt person on behalf of all of its affiliates?

Yes. A parent bank holding company or one of its bank subsidiaries on behalf of all bank subsidiaries of the holding company may make the designation of exempt person, so long as the designation lists each bank that will treat the customer as an exempt person.

15. Are sole proprietorships eligible for treatment as exempt persons?

A sole proprietorship may be treated as an exempt person if it meets the definition of a non-listed business or a payroll customer. When designating a sole proprietorship as an exempt person, a bank must take those reasonable and prudent steps to assure itself that the sole proprietorship is a bona fide business.

16. Are there any limitations on the exemption granted under the reformed procedures?

There is only one limitation on the exemption granted under the reformed procedures — the exemption does not apply to a transaction carried out by an exempt person as an agent of another person who is the beneficial owner of funds that are the subject of a transaction in currency. For example, where a grocery store deposits cash receipts derived from its sale of money orders sold on consignment directly into an account opened by the money order issuer or consignor, the grocery store is acting as an agent of the issuer or consignor with respect to that deposit. In that situation, the exemption of the deposit transaction from the CTR requirement would depend on the status of the issuer or consignor, and not of the grocery store.

Banks should note that this limitation on exemption does not require bank customers to segregate funds derived from agent activities to be eligible for treatment as an exempt person. Thus, for example, a grocery store that commingles funds from its sale of money orders sold on consignment with its normal business receipts, for the purpose of depositing all funds into its general account, engages in a transaction that is exempt or not depending upon the grocery store's own exempt status. (Businesses engaged in multiple business activities are discussed in Q&A #9.)

17. Are the reformed exemption procedures mandatory?

Banks may, but are not required, to use the new exemption procedures. Thus, banks may choose to continue to file a CTR with respect to each transaction in currency in excess of \$10,000 involving an exempt person so long as they do so consistently. FinCEN hopes and anticipates, however, that given the advantages of the simplified and streamlined exemption procedures, banks will continue to make the transition to those procedures as they become better acquainted, and more comfortable, with the terms of the new procedures.

18. If a bank chooses not to apply the new exemption procedures, is it obligated to file, where appropriate, a CTR?

Yes. Subject to the transitional rule set forth at 31 CFR 103.22(d)(11) (as explained in the next Q&A), a bank must file a CTR for each transaction in currency in excess of \$10,000 if the bank elects not to use the reformed exemption procedures that appear at 31 CFR 103.22(d).

19. As applied to accounts currently exempted under the old exemption system, how much longer can a bank continue to apply the old exemption procedures?

Through June 30, 2000, banks may continue to apply the old exemption procedures (old 31 CFR 103.22(b)-(g)) to exempt accounts that the bank previously treated as exempt under the old exemption system. To treat a person as exempt after that date, a bank must apply the terms of the reformed exemption procedures. Banks should note, however, that beginning on October 21, 1998, new exemptions may only be granted under the reformed exemption procedures.

20. What is the status of special exemptions under the reformed exemption procedures?

The special exemption procedures are eliminated entirely by the reformed exemption procedures. Thus, as of October 21, 1998, requests for special exemptions no longer will be reviewed and granted by the Department of the Treasury. In accordance with the transitional rule described above in Q&A #19, however, a bank may continue to rely on a special exemption granted under the old exemption system through June 30, 2000. Banks should note that it is likely that many of the accounts of customers previously exempted (or currently are exempting) through a special exemption, may be exempted under the reformed exemption procedures.

21. Who should a bank contact with any further questions concerning the reformed exemption procedures?

Any bank may contact its primary Bank Secrecy Act examination authority, FinCEN's Office of Program Development at (703) 905-3975, or FinCEN's Office of Chief Counsel at (703) 905-3590 regarding questions on the Bank Secrecy Act rules.