

**Testimony of  
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on  
Proposed Regulation on "Know Your Customer"  
before the  
The Subcommittee On Commercial And Administrative Law Committee On The  
Judiciary U.S. House Of Representatives  
10:00 A.M.  
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2141 Rayburn House Office Building**

Thank you Chairman Gekas, Ranking Member Nadler and members of the Subcommittee. I appreciate the opportunity to testify on behalf of the Federal Deposit Insurance Corporation on the proposed "Know Your Customer" regulations. The FDIC insures the nation's 10,483 commercial banks and savings institutions and is the primary federal supervisor of 5,863 state-chartered banks that are not members of the Federal Reserve System. My statement first provides some background on the proposed regulation. Next, I will summarize the main points of the comments we have received, particularly with respect to privacy. Finally, I will address the future of the proposal.

## **BACKGROUND**

The FDIC, the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision published the proposed regulation for public comment in December 1998. The FDIC alone has received over 135,000 comments from the public as of March 2, virtually all of which express vigorous opposition to the proposal. Given this opposition, it is obvious to us that the proposal cannot become final in its current form, if at all.

The integrity of the nation's banking system is rooted in confidence. Confidence between a financial institution and its customers is what enables banks and other financial institutions to attract and retain legitimate funds from legitimate customers. Maintaining confidence in the nation's banking system is the mission of the FDIC. It was never our intention in this proposal to upset that confidence, but rather to affirm it. Illegal activities, such as money laundering, fraud, and other transactions designed to assist criminals in illegal ventures pose a serious threat to the integrity of financial institutions. Recent and highly publicized situations involving money laundering, such as the Raul Salinas case, demonstrate the importance of federal supervision and bank vigilance in this area. While it is impossible to identify every transaction at an institution that is potentially illegal or involves illegally obtained money, financial institutions must take

reasonable measures to identify such transactions in order to ensure their own safe and sound operations.

Under the Bank Secrecy Act, insured financial institutions are required to report suspected illegal activity involving transactions conducted (or attempted) through the insured institution. The proposal was intended to provide consistent, practical, and yet flexible guidance to banks on compliance with anti-money laundering requirements and to assist banks in protecting themselves from being unwitting victims of, or participants in, criminal activity. We never intended, as some commenters have suggested, to require banks to monitor every transaction, every customer and every account in a bank.

Banks need a way to identify transactions that are suspicious from a law enforcement perspective. Many banks already have formal programs to know the customers with which they do business. For the many banks that have already implemented such a program, the proposal would require them to make sure their programs are in writing and approved by their respective boards of directors. Even banks without formal programs require personal identification such as a driver's license from an individual opening an account. For business customers, upon opening an account, a bank will often require articles of incorporation, board resolutions, partnership agreements, or business licenses, as appropriate. Institutions without formal programs have requested the federal banking agencies to provide guidance in this area. Such institutions have held off going forward with formal Know Your Customer programs so that they will not expend financial and personnel resources on programs that would not meet their primary federal regulator's standards.

## **PUBLIC COMMENTS**

When the agencies announced the interagency proposal last December, the FDIC took several steps to ensure public input on privacy and other issues. The FDIC's Board of Directors announced the proposal at a board meeting that was open to members of the public and press. The FDIC posted the proposal on its website; extended the comment period to 90 days; and encouraged the public to submit comments through the Internet. The FDIC also forwarded the proposal to state nonmember banks to solicit their input, and in its cover letter, highlighted the privacy concern and other issues.

In crafting the proposal, the agencies recognized the issues of burden and customer privacy. In the letter the FDIC sent on the proposal to all FDIC-supervised banks, we clearly cautioned financial institutions about avoiding the invasion of customer privacy by safeguarding and handling financial information responsibly. We reiterated our concerns regarding privacy and burden by inviting specific comment on: (i) whether the benefits of implementing Know Your Customer requirements outweighed the costs involved, and (ii) whether the actual or perceived invasion of personal privacy interests is outweighed by the additional compliance benefits anticipated by the proposal.

The agencies expressly solicited comments on a number of other issues, including whether the definition of "customer" for these purposes was too broad and would unnecessarily include individuals who present little risk; and whether a competitive disadvantage for banks would be created with respect to financial entities that offer similar services but are not covered by the proposal.

As noted earlier, virtually all of the public comments are from individuals whose primary concern is the impact of the proposal on their personal privacy. Comments from bankers have expressed great concern about the cost of compliance, customer privacy, and the competitive disadvantage if all financial institutions are not subject to the same requirements. Some bankers also have asserted that the proposal's elements are redundant, ineffective, and unnecessary.

Congress has also expressed its concern over the proposal. As you know, several bills have been introduced that would prohibit the proposal from being implemented in its current form. We appreciate the interest shown by Congress, the public, and the banking industry in the proposal and the issues that it raises. I want to assure you that the FDIC is listening and has received the message loud and clear.

## **FUTURE OF PROPOSAL**

Because the comment period does not close until March 8, under the rules governing federal rulemaking, no final decision regarding the proposal can be made prior to March 8. However, the FDIC is reading every comment letter and is considering them very seriously. After the close of the comment period, the FDIC will carefully consider its options, including simply withdrawing the proposal.

Again, I appreciate the opportunity to present the FDIC's views on these issues and would be happy to answer any questions you might have.

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