§ 914.16 [Amended]

3. Section 914.16 is amended by removing and reserving paragraphs (cc) and (dd).

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DEPARTMENT OF THE TREASURY

31 CFR Part 103

RIN 1506–AA11

Financial Crimes Enforcement Network; Amendment to the Bank Secrecy Act Regulations—Exemptions From the Requirement To Report Transactions in Currency

AGENCY: Financial Crimes Enforcement Network, Treasury.

ACTION: Final rule.

SUMMARY: This document contains a final rule amending the Bank Secrecy Act regulations. The amendment will eliminate the requirement to report transactions in currency in excess of $10,000 between depository institutions and certain classes of ''exempt persons'' defined in the rule. It will modify (and, as modified, will supersede), an interim rule on the same subject, to reflect the comments that were requested when the interim rule was published.

There appears elsewhere in today's edition of the **Federal Register** a notice of proposed rulemaking that would further modify the rules for granting exemptions from the currency transaction report filing requirements. The final rule and the notice of proposed rulemaking are additional steps in a process intended to achieve the reduction set by the Money Laundering Suppression Act of 1994 in the number of Bank Secrecy Act currency transaction reports required to be filed annually by depository institutions.

EFFECTIVE DATE: January 1, 1998.

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SUPPLEMENTARY INFORMATION:

I. Statutory Provisions

The Bank Secrecy Act, Titles I and II of Pub. L. 91–508, as amended, codified at 12 U.S.C. 1829b, 12 U.S.C. 1951–1959, and 31 U.S.C. 5311–5330, authorizes the Secretary of the Treasury, *inter alia*, to issue regulations requiring financial institutions to keep records and file reports that are determined to have a high degree of usefulness in criminal, tax, and regulatory matters, and to implement counter-money laundering programs and compliance procedures. Regulations implementing Title II of the Bank Secrecy Act (codified at 31 U.S.C. 5311–5330) appear at 31 CFR Part 103. The authority of the Secretary to administer Title II of the Bank Secrecy Act has been delegated to the Director of FinCEN.

The reporting by financial institutions of transactions in currency in excess of $10,000 has long been a major component of the Department of the Treasury's implementation of the Bank Secrecy Act. The reporting requirement is imposed by 31 CFR 103.22, a rule issued under the broad authority granted to the Secretary of the Treasury by 31 U.S.C. 5313(a) to require reports of domestic coins and currency transactions.

Four new provisions (31 U.S.C. 5313(d) through (g)) concerning exemptions were added to 31 U.S.C. 5313 by the Money Laundering Suppression Act of 1994 (the ''Money Laundering Suppression Act''), Title IV of the Riegle Community Development and Regulatory Improvement Act of 1994, Pub. L. 103–325 (September 23, 1994). According to subsection (d)(1), the Treasury must exempt a depository institution from the requirement to report currency transactions with respect to transactions between the depository institution and the following categories of entities:

(A) Another depository institution.

(B) A department or agency of the United States, any State, or any political subdivision of any State.

(C) Any entity established under the laws of the United States, any State, or any political subdivision of any State, or under an interstate compact between 2 or more States, which exercises governmental authority on behalf of the United States or any such State or political subdivision.

(D) Any business or category of business the reports on which have little or no value for law enforcement purposes.

Subsection (d)(2) requires the Treasury to publish at least annually a list of entities whose currency transactions are exempt from reporting under the mandatory rules. The companion provisions of 31 U.S.C. 5313(e) authorize the Secretary to permit a depository institution to grant additional, discretionary, exemptions from the currency transaction reporting requirements. Subsection (f) places limits on the liability of a depository institution in connection with a transaction that has been exempted from reporting under either subsection (d) or subsection (e) and provides for the coordination of any exemption with other Bank Secrecy Act provisions, especially those relating to the reporting of suspicious transactions. Subsection (g) defines ''depository institution'' for purposes of the new exemption provisions.

The enactment of 31 U.S.C. 5313 (d) through (g) reflects a congressional intention to ''reform * * * the procedures for exempting transactions between depository institutions and their customers.'' *See* H.R. Rep. 103–652, 103d Cong., 2d Sess. 186 (August 2, 1994).[1] The administrative exemption procedures at which the statutory changes are directed are found in 31 CFR 103.22 (b)–(g).

Several reasons have been given for the administrative exemption system's lack of success in eliminating routine currency transactions from operation of the Bank Secrecy Act rules. The first is the retention by banks of liability for making incorrect exemption determinations. The second is the complexity of the administrative exemption procedures. Finally, advances in technology have made it less expensive for some banks to report all currency transactions than to incur the administrative costs and risks of exempting customers and then administering the terms of particular exemptions properly.

II. The Interim Rule

On April 24, 1996, an interim rule (the ''Interim Rule'') adding a new paragraph (h) to the currency transaction reporting rules in 31 CFR 103.22 was published in the **Federal Register**. *See* 61 FR 18204. The Interim Rule exempted, from the requirement to report transactions in currency in excess of $10,000, transactions occurring after April 30, 1996, between banks[2] and

[1] Section 402(b) of the Money Laundering Suppression Act states simply that in administering the new statutory exemption procedures

the Secretary of the Treasury shall seek to reduce, within a reasonable period of time, the number of reports required to be filed in the aggregate by depository institutions pursuant to section 5313(a) of title 31 * * * by at least 30 percent of the number filed during the year preceding [September 23, 1994,] the date of enactment of [the Money Laundering Suppression Act].

[2] The Interim Rule used the term *bank* to define the class of financial institutions to which the Interim Rule applied. As defined in 31 CFR 103.11(c), that term includes both commercial banks and other classes of depository institutions at which the language of 31 U.S.C. 5313 is directed.

customers who fall into one of five classes of exempt persons:

1. Banks, to the extent of their banking operations and transactions within the United States; [3]

2. Departments and agencies of the United States and of states and their political subdivisions;

3. Any entity established under the laws of the United States [4] or of any state or its political subdivisions, or under an interstate compact, that exercises governmental authority on behalf of the United States or any such state or political subdivision;

4. ''Listed corporations,'' that is, corporations whose common stock is listed on the New York Stock Exchange or the American Stock Exchange or has been designated as a Nasdaq National Market Security listed on the Nasdaq Stock Market; [5]

5. Subsidiaries of listed corporations that are consolidated with such corporations for federal income tax purposes.

See 31 CFR 103.22(h)(2) (i)–(v). The first three categories of exempt persons specified above are those to whom an exemption is required to be granted by 31 U.S.C. 5313(d)(1) (A)–(C). The final two categories are those entities who are exempted pursuant to the authority contained in 31 U.S.C. 5313(d)(1)(D).

To treat a customer as exempt under the Interim Rule, a bank must file a single form (the same form now used by banks to report a transaction in currency) that identifies the exempt person and the bank involved and must generally take such steps to assure itself that a person is an exempt person that a reasonable and prudent bank would take to protect itself from loan or other fraud or loss based on misidentification of a person's status. Treatment of a customer as an exempt person under the Interim Rule protects a bank generally from any penalty for failure to file a currency transaction report with respect to the exempt person's currency transactions, but it does not affect the obligation of banks to file suspicious activity reports. Currency transactions, like other transactions, between a bank and an exempt person remain subject to the suspicious activity reporting requirements of 31 CFR 103.21, as well as the suspicious activity reporting requirements of the federal bank supervisory agencies. *See also* 12 CFR 21.11 (Office of the Comptroller of the Currency); 12 CFR 208.20 (Federal Reserve System); 12 CFR 353.3 (Federal Deposit Insurance Corporation); 12 CFR 563.180 (Office of Thrift Supervision); 12 CFR 748.1 (National Credit Union Administration).

Because the Interim Rule implemented certain provisions of the Bank Secrecy Act and granted significant relief from existing regulatory requirements, it was made effective on May 1, 1996, less than 30 days after its publication date. The Interim Rule was, however, accompanied by a request for comments on the Rule's terms.

It appears that the Interim Rule did not immediately have the intended effect of reducing the number of routine currency transactions filed by depository institutions. This may have been attributable, at least in part, to banks' reluctance to use the new exemption procedures until the Interim Rule and proposals for the projected second stage of currency transaction filing relief (as to which comments were solicited by the preamble to the Interim Rule) were made final. Deferral of a change in a bank's procedures would permit the automated systems on which many institutions rely to be altered to take account of all the revised currency transaction filing rules at one time. Unfamiliarity with and uncertainty about the meaning of certain provisions of the Interim Rule may also have initially retarded the Rule's use.[6]

Statistics based on the first half of this year indicate that banks are making the transition to the new, streamlined exemption procedures set forth in the Interim Rule. The number of CTR filings for each of the months of February, March, April, May, and June of 1997 is less than the number of filings for those same months in 1996. (FinCEN does not yet have complete information concerning CTR filings for July 1997.) Thus, it appears that the Interim Rule is beginning to have some effect on decreasing the number of CTR filings. FinCEN anticipates that banks will continue to make the transition to the new exemption procedures as they become better acquainted, and more comfortable, with the terms of the new procedures. FinCEN also hopes that the clarifications contained in this document will continue to aid in that transition.

III. Summary of Comments and Revisions

A. Comments on the Notice—Overview

FinCEN received fifty-eight written comments on the Interim Rule. Of these, forty-four comments were submitted by banks or bank holding companies, six by banking trade associations, four by credit unions, one by a credit union trade association, and one each by a compliance consulting firm, an accounting firm, and a law firm, each on its own behalf.

The commenters generally applauded FinCEN's efforts to improve the exemption process. One bank commenter, for example, noted with approval ''the scope and aggressiveness of the Interim Rule'' and found the Rule ''a major step in reducing the Bank Secrecy Act's burden on financial institutions without compromising the BSA's effectiveness'' because it permitted banks to eliminate the cost of reporting ''large denomination, repetitive transactions with public entities and major corporations engaged in legitimate retail activity.'' At the same time, the commenters suggested a number of ways in which the Interim Rule might be improved, and they raised several operating issues that banks had encountered in applying the Interim Rule.

Comments on the Interim Rule focused primarily on five subjects: the definition of an exempt subsidiary of a listed corporation; other aspects of the definition of exempt person; the time frame within which a bank was permitted to designate an existing customer as an exempt person; the need to clarify the relationship between the provisions of paragraph (h) and the terms of the administrative exemption provisions of 31 CFR 103.22(b)–(g); and the interplay between the Interim Rule and previous regulatory guidance provided by the Department of the Treasury with respect to the currency transaction reporting requirements. The specifics of the comments and an explanation of resulting modifications to paragraph (h) are outlined below.

After full and careful consideration of all the comments, 31 CFR 103.22(h), as contained in the Interim Rule, is modified, and, as modified, is adopted as a final rule.

B. Final Rule

The format and substance of the final rule and the Interim Rule are generally the same. The final rule reflects the

[3] The broad definition of ''United States'' in section 103.11(nn) applies.

[4] Again, the broad definition of ''United States'' applies.

[5] The NASDAQ category did not include stock listed under the separate ''Nasdaq Small-Cap Issues'' category.

[6] FinCEN has already issued a notice, FinCEN Notice 97–1, to deal with one such uncertainty. That notice makes clear that an institution may decide, after August 15, 1996, that it wishes to adopt the new exemption system for particular customers, even if it did not do so, for existing customers, before that date, so long as the necessary exemption identifications are filed within 30 days of the first transaction in currency that is sought to be exempted under the new exemption procedures.

following significant modifications to the Interim Rule:

1. The definition of exempt person has been clarified to make clear that banks are eligible to be treated as exempt persons because they are banks, and then only with respect to their domestic operations; a bank that is, or is a subsidiary of, a listed company does not for that reason obtain a second ground for exemption;

2. The definition of exempt person has been amended to treat as a ''listed entity'' and entity, rather than just a corporation, whose common stock or analogous equity interests are listed on an applicable stock exchange;

3. The definition of exempt person has been amended to include any subsidiary of a listed entity that is organized under the laws of the United States or a state and at least 51 percent of whose common stock is owned by the listed entity as shown in a reasonably authenticated corporate officer's certificate, a reasonably authenticated photocopy of Internal Revenue Service Form 851 (Affiliation Schedule), or in the Annual Report or Form 10–K that is filed by the listed entity with the Securities and Exchange Commission;

4. The definition of exempt person has been amended to make clear that an exempt person includes a financial institution, other than a bank, that is a listed entity or a subsidiary of a listed entity, but only to the extent of such entity's domestic operations;

5. The time frame for designating a customer as an exempt person has been clarified to provide that a designation may be made, for any customer, by the close of the 30-day period beginning after the day of the first reportable transaction in currency with that person that is sought to be exempted from reporting under the terms of paragraph (h);

6. Examples of entities exercising governmental authority have been added to the Interim Rule; and

7. A paragraph has been added to make clear that, absent knowledge of a loss of an exempt person's status as such, a bank satisfies its obligations under paragraph (h) by verifying the continued status of exempt persons at least annually.

The changes adopted in the final rule are intended to improve, clarify, and refine the rule's provisions in light of the objectives FinCEN outlined when the Interim Rule was published. Those objectives are reducing the burden of currency transaction reporting, requiring reporting only of information that is of value to law enforcement and regulatory authorities, and, perhaps most importantly, creating an exemption system that is cost-effective and that works. *See* 61 FR 18205.

IV. Specific Comments and Explanation of Revisions

A discussion of the significant comments on the Interim Rule appears below. As noted, many of the comments raised questions about the interaction between the terms of paragraph (h) and various operating requirements of the administrative exemption system.

A. 31 CFR 103.22(h)(1)—Transactions in Currency of Exempt Persons With Banks

Paragraph (h)(1) states that general rule that no report is required under 31 CFR 103.22(a)(1) with respect to any transaction in currency between an exempt person and a bank. The only changes made to this paragraph are ministerial: the phrase ''currency transactions'' in the title of paragraph (h)(1) has been revised to read ''transactions in currency,'' and the phrases ''occurring after April 30, 1996,'' in the title of paragraph (h) and in the title of paragraph (h)(1), and ''that is conducted after April 30, 1996,'' at the end of paragraph (h)(1), have been deleted as unnecessary in a final rule.[7] For consistency, the phrase ''occurring after April 30, 1996'' has also been deleted as unnecessary in paragraph (a)(1).

It should be noted that the exemption language of the final rule is fundamentally different from that of the administrative exemption system. Sections 103.22(a)(1) and 103.22(h)(1) state affirmatively that the reporting requirements of the section do not apply to the transactions described in paragraph (h). In contrast, the administrative exemption provision, 31 CFR 103.22(b)(2), simply states that a bank ''may exempt'' transactions described in that paragraph from reporting. Although, as noted in the preamble to the Interim Rule, *see* 61 FR 18206, the provisions of paragraph (h)(1) do not affirmatively prohibit banks from continuing to report routine currency transactions with exempt persons (and the requirement that exempt persons be designated as such provides banks with operational discretion to determine whether or not to recognize the new provisions), banks that continue to report such routing transactions are supplying the government with information that is not required under the Bank Secrecy Act regulations.

1. Use of Word ''Bank'' Rather Than ''Depository Institution''

FinCEN received no comment on its use of the term ''bank'' instead of ''depository institution'' to define the class of financial institutions, subject to the Bank Secrecy Act, that are exempted from the requirement to report transactions in currency by paragraph (h)(1), and the final rule continues to use the former term. Although 31 U.S.C. 5313(d) refers to mandatory exemptions for certain transactions in currency with ''depository institutions,'' the broad definition of bank contained in 31 CFR 103.11(c) appears to include all categories of institutions included in the statutory ''depository institution'' definition, so that a change in terminology was neither necessary nor advisable (in view of the Bank Secrecy Act regulations' general use of the work ''bank'' for the classes of institutions involved).

2. Coverage of all ''Transactions in Currency''

At least one commenter asked whether paragraph (h), intended to exempt from reporting all ''transactions in currency'' between exempt persons and banks, despite the fact that the administrative exemption system rules of 31 CFR 103.22(b)(2) (i)–(ii) permit banks to exempt from currency transactions reporting only deposits and withdrawals, of currency from existing and specified accounts.[8] The use of the broader term is intentional, as paragraph (h) seeks to elimate all transactions in currency between exempt persons and banks from the reporting rules of section 103.22 (subject to the limitation on exemption for transactions carried out by an exempt person as an agent for another person, as set forth in paragraph (h)(5)). As noted in more detail below, however, the changes made to section 103.22 have no impact on the requirement to report suspicious transactions under 31 CFR 103.21, and the fact that an exempt person wishes to conduct a transaction other than a deposit or withdrawal, or a transaction that does not involve an existing account with the bank involved, may merit further investigation, and perhaps reporting, under the rules of section 103.21.

3. Transactions by Exempt Persons With Financial Institutions Other Than Banks

At least one commeter sought to broaden the scope of subsection (h) to include transactions between exempt

[7] Deletion of the reference to a specific date is not intended in any way to alter the effective date of this change in the Bank Secrecy Act regulations.

[8] Banks are permitted by 31 CFR 103.22(b)(2)(iii) to grant a broader exemption for transactions by government agencies.

persons and financial instituons other than banks. No such change has been made. Although, as noted below, banks are permitted, in a change from prior practice, to recognize ''listed'' non-bank financial institutions as exempt persons, a general grant of automatic exemption for all transactions in currency in excess of $10,000 between exempt persons, on the one hand, and, for example, brokers and dealers in securities, money transmitters, or currency exchange houses, on the other, is neither within the Money Laundering Suppression Act statutory mandate nor justified by the realities of the operation of those businesses.

B. 31 CFR 103.22(h)(2)—Definition of Exempt Person

Paragraph (h)(2) continues to contain the definition of those classes of ''exempt persons'' whose transactions in currency with banks are exempt from reporting under the final rule.

1. Banks

The Interim Rule defines an exempt person to include a bank, to the extent of the bank's domestic operations. One commenter asserted that the treatment of banks as exempt persons ''to the extent of their domestic operations'' is less broad than the present exemption provided for banks by section 103.22(b)(1)(ii). However the language of paragraph (h)(2)(i) is simply a restatement of the language of section 103.22(b)(1)(ii), when the latter definition is read together with the definition of ''domestic'' in section 103.11(k).

The final rule revises paragraphs (h)(2)(iv) and (h)(2)(v) to make clear that a bank is eligible to be treated as an exempt person only with respect to its domestic operations; a bank that is a listed entity or a subsidiary of a listed entity does not for that reason obtain a second ground for exemption.

2. Subsidiaries or Affiliates of Banks

At least one commenter asked whether the exempt person definition included subsidiaries or affiliates of banks (so that a transaction in currency between a bank subsidiary and a second bank would be exempt from reporting in the same manner as a transaction between the subsidiary's bank parent and the second bank.) The bank Secrecy Act regulations do not generally treat bank subsidiaries as falling within the definition of bank for purposes of the regulations, and until that basic concept is re-evaluated, it is premature to extend automatic relief for currency transaction reporting purposes to non-bank subsidiaries and affiliates of banks.

3. Government Entities

Paragraph (h)(2)(ii), which treats various federal, state, and local government departments and agencies as exempt persons, is unchanged.

Several commenters asked about the status of tribal governments and tribal enterprises under paragraph (h). The definition of ''United States'' in section 103.11(nn) includes ''the Indian lands (as that term is defined in the Indian Gaming Regulatory Act),'' [9] so that tribal governments are eligible to be exempt persons under paragraph (h); whether particular enterprises conducted on tribal lands, for example tribal casinos, are themselves exempt depends upon the manner in which they are organized and operated. Thus, a tribal casino that is operated as a department of a tribal government would generally qualify as an exempt person, but an independently operated management company for such a casino, or a corporation of which the tribe was a shareholder, would likely not so qualify. While FinCEN would be pleased to provide further guidance on that question on the basis of the facts of a particular situation, it is not feasible on the current state of the record do so in the Bank Secrecy Act regulations themselves.

One commenter argued that the definition of government agency in paragraph (h)(2)(ii) would exclude exemption for agencies of the District of Columbia. That is not the result of the definition, since the definition of ''United States'' in section 103.11(nn) includes the District of Columbia.

4. Entities That Exercise Governmental Authority

Paragraph (h)(2)(iii), which treats as exempt persons entities established by federal, state, or local governments, or by interstate compact, that exercise governmental authority, also is unchanged.

5. Listed Entities

The Interim Rule defines an exempt person to include corporations listed on national securities exchanges. Several commenters suggested that the definition of exempt person be broadened to include partnerships and other non-corporations listed on those exchanges. One commenter pointed out that the rationale FinCEN gave for exempting listed corporations—*i.e.*, the scale of enterprises listed on the nation's largest securities exchanges, and the variety of internal and external controls to which they are subject, make their use for money laundering sufficiently unlikely to permit relaxation of the current transaction reporting rules—applies to any listed entity regardless of its form. After consideration of such comments, Treasury has amended the Interim Rule to expand the definition of an exempt person in paragraph (h)(2)(iv) to include any entity listed on an applicable national securities exchange.

A number of commenters cited the difficulty of determining whether a customer was listed on one of the three cited stock exchanges or was a subsidiary of a company so listed. As noted in the preamble to the Interim Rule, it is impossible to reduce the volume of currency transaction reports to the extent that the Interim Rule tries to do without creating some temporary inconvenience as the terms of the system change. The determinations required are straightforward and are to be based on easily available information, especially for financial professionals. FinCEN continues to believe that the degree of effort involved in researching whether a company's stock is listed as a national stock exchange, or whether a corporation is a subsidiary of a public company, is well within the scope of what a prudent bank should know about its customers and their activities.

There is no limit on the ''listed entity'' definition based on the nature of a particular company's business. Thus, for example, a listed company that is a gaming enterprise or that issues traveler's checks or money orders or engages in a money remittance business as a principal is not for that reason denied exempt status. See, however, the limitation on exemption for transactions carried out by an exempt person as an agent for another person, as set forth in paragraph (h)(5).

6. Subsidiaries of Listed Entities

The Interim Rule treats as an ''exempt'' subsidiary any subsidiary that is included in the consolidated federal income tax return of a listed corporation. FinCEN sought alternative formulations that bank employees would find easy to apply and that would accomplish the goals of the Interim Rule more effectively than the consolidated return formulation. At least one commenter stated that an entity that is listed as a subsidiary on a listed entity's SEC report 10K or an annual report should be considered an exempt person. After consideration of these comments, FinCEN has amended the definition of an exempt subsidiary to include any subsidiary that is organized under the laws of the United States or of any state and at least 51 per

[9] The term Indian Gaming Regulatory Act is itself defined in § 103.11(rr).

cent of whose common stock is owned by the listed entity. Evidence of such ownership may be shown by any of the ways listed in paragraph (h)(4)(iv), including reliance upon a listed entity's Annual Report or Form 10–K, filed in each case by the listed entity with the Securities and Exchange Commission.[10]

7. Financial Institutions Other Than Banks

New paragraph (h)(2)(vi), which relates to financial institutions other than banks, has been added to the Interim Rule. This new paragraph clarifies that non-bank financial institutions that are, or are subsidiaries of, listed entities, are exempt persons only to the extent of their domestic operations.

C. 31 CFR 103.22(h)(3)—Designation of Exempt Person

Paragraph (h)(3) sets forth the procedures for designating an exempt person. A few commenters sought clarification of the time frame in which a bank could designate an exempt person. At least one commenter stated that the Interim Rule could be interpreted as precluding a bank from designating an existing customer as an exempt person after August 15, 1996. After consideration of such comments, FinCEN has amended the Interim Rule, in accord with FinCEN Notice 97–1, to make clear that a bank can designate any customer as an exempt person by the close of the 30-day period beginning after the day of the first reportable transaction in currency with that person that is sought to be exempted from reporting under the terms of paragraph (h).

At least one commenter also requested that FinCEN amend the Interim Rule to allow banks, when designating exempt persons, to file a list of its domestic bank customers instead of filing a form that identifies such a customer as an exempt person. As set forth in new paragraph (h)(3)(iii), a bank, when designating an exempt person, may either file an Internal Revenue Form 4789 in which line 36 is marked appropriately or filed, in such a format and manner as FinCEN may specify, a current list of its domestic bank customers.

At least one commenter further suggested that it would be efficient for banks simply to file designations for all their government customers (as well as their bank customers), regardless of whether those customers engage in transactions in excess of $10,000. FinCEN will consider making such a change to paragraph (h) for government entities at an appropriate time in the future.

D. 31 CFR 103.22(h)(4)—Operating Rules for Designating Exempt Persons

Paragraph (h)(4) continues to state general operating rules for designating exempt persons. Changes to the details of the operating rules are outlined below.

1. General Standard

A number of commenters asked for greater specificity about the manner in which the determination that a customer is an exempt person should be made and documented. Specific questions included, for example, whether a bank was required to keep an ''exemption list'' of exempt persons, whether a signed customer statement was required for each exempt person, whether paper copies of filings designating exempt persons should be maintained by a bank, and how long records relevant to the exemption determination must be retained.

The language of paragraph (h)(4)(i) has been revised to make explicit the general requirement, implicit in the original language, that a bank must document, in the manner that a reasonable and prudent bank would do, its determination that a customer is eligible to be treated as an exempt person, in compliance with the terms of paragraph (h). A new paragraph (h)(4)(v), discussed below, has been added to deal specifically with record retention.

FinCEN believes that specific additional language is unnecessary and would be contrary to the spirit of the changes in the currency transaction filing rules that FinCEN is working with the banking industry to make. Because the situation of each bank is different, any uniform set of rules can only stifle creativity and efficiency in building whatever record an individual bank's situation and determinations warrant. Thus, for example, it would certainly be prudent for a bank to maintain, or to be able to retrieve, in a central location a list of the customers that it treats as exempt persons; but whether the list is separately maintained, or simply retrievable from general records upon need, is a matter for each bank to determine. Similarly many institutions, as a general rule, retain copies of documents filed with the Treasury Department; however, whether forms filed magnetically must be converted into paper copies for examination purposes is a matter that should be decided in accordance with general bank policies, rather than in a universal regulatory document.

As in other situations, FinCEN believes that too much attention has in the past been paid to mechanical compliance with particular ''check list'' requirements, rather than to the spirit of compliance and the monitoring necessary effectively to deter or detect money laundering at the nation's financial institutions. Thus, it hesitates, in attempting to re-engineer the currency transaction reporting system, to recreate the defects of the system being replaced. FinCEN intends to communicate the policy determinations behind the changes in the rules to the federal financial institution supervisory agencies, whose authority includes the authority to examine for compliance with Bank Secrecy Act requirements, to assure, insofar as possible, that the expectations of compliance examiners are in accord with the terms and spirit of the new rules.

At least one commenter suggested that FinCEN should bear the burden of listing all the entities falling within the classes of exempt persons set forth in paragraph (h)(2). This suggestion has not been adopted in the final rule. The list requirement is a flexible one and is amply met by reliance on publicly-available sources. For FinCEN to publish a list of particular exempt customer *ab initio* would amount to a licensing requirement that would neither be efficient nor feasible.

At the same time, as indicated in the preamble to the Interim Rule, *see* 61 FR 18208, FinCEN is exploring the possibility of producing a nationwide list of exempt persons from filed designations. FinCEN also is exploring the possibility of linking its own Web Site to those of the national securities exchanges.

2. Governmental Entities

A few commenters requested that FinCEN provide examples of those entities established under U.S., state, or local law, under an interstate compact, that exercise governmental authority. A sentence has been added to paragraph (h)(4)(ii) to cite the New Jersey Turnpike Authority and the Port Authority of New York and New Jersey as examples of entities that exercise governmental authority.

3. Listing Information

Language has been added to paragraph (h)(4)(iii) to make it clear that a bank may rely, in determining whether a company is a listed company,

[10] Several commenters suggested that non-profit corporations generally be added to the list of exempt persons. FinCEN does not believe that a blanket provision of this sort would be workable or in keeping with the balance of objectives outlined in 31 U.S.C. 5313 (d)–(g), given the variety of organizations that can claim non-profit status.

on information available from the ''Edgar'' electronic information system maintained by the Securities and Exchange Commission (http://www.sec.gov/edgarhp.htm), and on information contained in the Web Sites maintained by the New York Stock Exchange ((http://www.nyse.com), the American Stock Exchange (http://www.amex.com), and the National Association of Securities Dealers (http://www.nasdaq.com).

4. Subsidiary Status

Paragraph (h)(4)(iv) has been amended to provide banks with the additional options, when determining whether a person is exempt as a subsidiary of a listed entity, of relying upon the listed entity's Annual Report or Form 10–K (filed with the Securities and Exchange Commission) for designation of the listed entity's subsidiaries.

5. Records Maintenance

New paragraph (h)(4)(v) has been added to the Interim Rule to make clear that records maintained by a bank to document its administration of the rules of this paragraph (h) must be maintained in accordance with the terms of 31 CFR 103.38, which, *inter alia,* requires that records be maintained for a period of five years.

E. 31 CFR 103.22(h)(5)—Limitation on Exemption

Paragraph (h)(5) states that the exemption from reporting contained in paragraph (h)(1) does not apply to a transaction carried out by an exempt person as an agent of another person who is the beneficial owner of the funds that are the subject of a transaction in currency. At least one commenter requested that FinCEN eliminate this limitation. This requested change has not been adopted in the final rule. Such a change would allow an exempt person to lend its status to any person's transactions, thereby circumventing the purposes of carefully defining the classes of exempt persons.

At least one commenter noted a difficulty involved in tracking deposits from large grocery stores, because some of the deposits involved may be monies sent to holding accounts for money order or traveler's check companies for which the grocery stores act as agent. Although FinCEN recognizes that distinguishing between the two (or more) sources of deposits represents an additional effort, it believes that the holding accounts are ultimately relatively easy to distinguish from the store's own operating accounts and do not commingle operating funds and funds used to pay for money service products sold by grocery stores as agents for other concerns. To the extent that the industry still finds that the limitation set forth in paragraph (h)(5) will result in unnecessary inconvenience, FinCEN will consider additional comments on this subject when it considers comments to the notice of proposed rulemaking on exemptions that appears elsewhere in today's edition of the **Federal Register**.

F. 31 CFR 103.22(h)(6)—Effect of Exemption: Limitation on Liability

Paragraph (h)(6) continues to state the general rule that once a bank has complied with the terms of paragraph (h), it is protected from any penalty for failure to file a currency transaction report concerning a transaction in currency by an exempt person. The language set forth in paragraph (h)(6)(i) of the Interim Rule has been deleted in the final rule; the issue of when a bank must designate customers it has previously treated as exempt, is addressed in the notice of proposed rulemaking regarding exemptions.

At least one commenter expressed the concern that the ''automatic revocation'' provisions of paragraph (h)(8), in effect, force banks to maintain a constant vigil of the status of entities they have designated as exempt persons. New paragraph (h)(6)(ii) has been added to clarify that, absent specific knowledge of any information that would be grounds for revocation, a bank is required to verify the status of those entities it has designated as exempt persons only once each year.

A bank may, at present, elect to treat a person as exempt under either the administrative exemption system rules of sections 103.22(b)–(g) or the rules of section 103.22(h). As outlined in the Interim Rule, and as confirmed above, the exemption procedures for each system are independent of the other. Thus, if a bank treats a person as exempt under the new exemption procedures set forth in paragraph (h), it need not place that person on its exempt list under the administrative exemption system rules, *see* sections 103.22(b)–(g), but, conversely, the fact that a person is on an exemption list (whether it is a bank, a government entity, or a listed company), does not eliminate the obligation of a bank that wants to adopt the new system from filing the single form designating the customer as an exempt person.

The limitation on liability set forth in paragraph (h)(6) does not apply if a bank chooses to exempt a person on a basis as provided by the administrative exemption system. One comment found this result slightly puzzling, since the Interim Rule is clearly designed to designate those entities whose routine transactions is currency with banks are of little or no law enforcement value. However, even the Interim Rule involves some trade-off in policy outcomes, and the proper designation of exempt persons, to provide the Department of the Treasury with a list of exempt entities, is an important part of the overall system of which the Interim Rule is a component. The statutory liability limitation of 31 U.S.C. 5313(f) does not extend to banks that continue to use the administrative exemption system during the pendency of the rulemaking that would reform that system.

One commenter on the Interim Rule argued that ''the process of exempting a business and the liability for same should be primarily borne by the customer and FinCEN.'' That is neither the scheme of the Bank Secrecy Act nor of this rule, and such an approach would place the Treasury Department, in effect, directly on the banking floor in dealing with a bank's customers. The final rule, like the notice of proposed rulemaking also issued today, is an effort to work with the banking industry to fashion an effective and workable exemption system.

G. 31 CFR 103.22(h)(7)—Obligation to File Suspicious Activity Reports, Etc

No changes were made to this paragraph. Paragraph (h)(7) continues to state that the new exemption procedures set forth in paragraph (h) do not create any exemption, or have any effect at all, on the requirement that banks file suspicious activity reports with respect to transactions that satisfy the requirements of the rules of FinCEN, 31 CFR 103.21, and the federal bank supervisory agencies relating to suspicious activity reporting. Similarly, a customer's status under paragraph (h) has no impact on other Bank Secrecy Act requirements relating to record retention or reporting. Thus, for example, the fact that a customer is an exempt person for purposes of the currency transaction reporting rules has *no* effect on the obligation of a bank to retain records of funds transfers by such person, to the extent required by 31 CFR 103.33(e), or to retain records in connection with an issuance or sale of bank or cashier's checks, money orders or traveler's checks to such person, as required by 31 CFR 103.29.

H. 31 CFR 103.22(h)(8)—Revocation

Paragraph (h)(8) continues to provide that the status of an exempt person automatically ceases, without any action

or notice by the Department of the Treasury, when an entity ceases to be listed on the applicable stock exchange or a subsidiary of a listed entity ceases to have at least 51 per cent of its common stock owned by a listed entity. Paragraph (h)(8) explicitly refers back to the limitation on liability set forth in paragraph (h)(6)(ii), to make clear that absent specific knowledge that would be grounds for revocation, a bank is required to verify the status of those entities it has designated as exempt persons only once each year.

I. 31 CFR 103.22(h)(9)—Transitional Rule

New paragraph (h)(9) states the transitional rule for applying new paragraph (h)(2)(vi). The rule provides that during the period ending May 1, 1998, no penalty will be imposed on a bank that treats as an exempt person a non-bank financial institution, to an extent beyond that institution's domestic operations, that is a listed entity or a subsidiary of a listed entity.

V. Regulatory Matters

A. Executive Order 12866

The Department of the Treasury has determined that this final rule is not a significant regulatory action under Executive Order 12866.

B. Unfunded Mandates Act of 1995 Statement

Section 202 of the Unfunded Mandates Reform Act of 1995 (''Unfunded Mandates Act''), Pub. L. 104–4 (March 22, 1995), requires that an agency prepare a budgetary impact statement before promulgating a rule that includes a federal mandate that may result in expenditure by state, local and tribal governments, in the aggregate, or by the private sector, of $100 million or more in any one year. If a budgetary impact statement is required, section 202 of the Unfunded Mandates Act also requires an agency to designate and consider a reasonable number of regulatory alternatives before promulgating a rule. FinCEN has determined that it is not required to prepare a written statement under section 202 and has concluded that on balance this final rule provides the most cost-effective and least burdensome alternative to achieve the objectives of the rule.

C. Regulatory Flexibility Act

The provisions of the Regulatory Flexibility Act relating to an initial and final regulatory flexibility analysis (5 U.S.C. 604) are not applicable to this final rule because the agency was not required to publish a notice of proposed rulemaking under 5 U.S.C. 553 or any other law.

D. Paperwork Reduction Act

By expanding the applicable exemptions from an information collection that has been reviewed and approved by the Office of Management and Budget (OMB) under control number 1505–0063, the final rule significantly reduces the existing burden of information collection under 31 CFR 103.22. Thus, although the final rule advances the purposes of the Paperwork Reduction Act of 1995, 44 U.S.C. 3501, *et seq.*, and its implementing regulations, 5 CFR Part 1320, the Paperwork Reduction Act does not require FinCEN to follow any particular procedures in connection with the promulgation of the final rule.

List of Subjects in 31 CFR Part 103

Administrative practice and procedure, Authority delegations (Government agencies), Banks and banking, Currency, Foreign banking, Foreign currencies, Gambling, Investigations, Law enforcement, Penalties, Reporting and recordkeeping requirements, Securities, Taxes.

Amendment

For the reasons set forth above in the preamble, the interim rule amending 31 CFR Part 103, which was published at 61 FR 18204 on April 24, 1996, is adopted as a final rule with the following changes:

PART 103—FINANCIAL RECORDKEEPING AND REPORTING OF CURRENCY AND FOREIGN TRANSACTIONS

1. The authority citation for Part 103 continues to read as follows:

Authority: 12 U.S.C. 1829b and 1951–1959; 31 U.S.C. 5311–5330.

2. Section 103.22 is amended by revising the second sentence in paragraph (a)(1) and by revising paragraph (h) to read as follows:

§ 103.22 Reports of currency transactions.

(a)(1) * * * Transactions in currency by exempt persons with banks are not subject to this requirement to the extent provided in paragraph (h) of this section. * * *

* * * * *

(h) *No filing required by banks for transactions by exempt persons.*

(1) *Transactions in currency of exempt person with banks.* Notwithstanding the provisions of paragraph (a)(1) of the section, no bank is required to file a report otherwise required by that section, with respect to any transaction in currency between an exempt person and a bank.

(2) *Exempt person.* For purposes of this section, an exempt person is:

(i) A bank, to the extent of such bank's domestic operations;

(ii) A department or agency of the United States, of any state, or of any political subdivision of any state;

(iii) Any entity established under the laws of the United States, of any state, or of any political subdivision of any state, or under an interstate compact between two or more states, that exercises governmental authority on behalf of the United States or any such state or political subdivision;

(iv) Any entity, other than a bank, whose common stock or analogous equity interests are listed on the New York Stock Exchange or the American Stock Exchange or whose common stock or analogous equity interests have been designated as a Nasdaq National Market Security listed on the Nasdaq Stock Market (except stock or interests listed under the separate ''Nasdaq Small-Cap Issues'' heading);

(v) Any subsidiary, other than a bank, of any entity described in paragraph (h)(2)(iv) of this section (a ''listed entity'') that is organized under the laws of the United States or of any state and at least 51 per cent of whose common stock is owned by the listed entity; and

(vi) Notwithstanding paragraphs (h)(2)(iv) and (h)(2)(v) of this section, any financial institution other than a bank, that is an entity described in paragraph (h)(2)(iv) or (h)(2)(v) of this section, to the extent to such financial institution's domestic operations.

(3) *Designation of exempt persons.* (i) A bank must designate each exempt person with whom it engages in transactions in currency by the close of the 30-day period beginning after the day of the first reportable transaction in currency with that person that is sought to be exempted from reporting under the terms of paragraph (h) of this section.

(ii) Except where the person sought to be exempted is another bank as described in paragraph (h)(2)(i) of this section, designation of an exempt person shall be made by a single filing of Internal Revenue Service Form 4789, 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, or by filing any form specifically designated by FinCEN for this purpose. The designation must be made separately by each bank that treats the person in question as an exempt person.

(iii) When designating another bank as an exempt person, a bank must make either the filing as described in

paragraph (h)(3)(ii) of this section or file, in such a format and manner as FinCEN may specify, a current list of its domestic bank customers. In the event that a bank files its current list of domestic bank customers, the bank must make the filing as described in paragraph (h)(3)(ii) of this section for each bank that is a new customer and for which an exemption is sought under this paragraph (h).

(iv) The designation requirements set forth in this paragraph (h)(3) apply whether or not the particular exempt person to be designated has previously been treated as exempt from the reporting requirements of section 103.22(a) under the rules contained in paragraph (b) or (e) of this section.

(4) *Operating rules for designating exempt persons.* (i) Subject to the specific rules of this paragraph (h), a bank must take such steps to assure itself that a person is an exempt person (within the meaning of applicable provisions of paragraph (h)(2) of this section), and to document the basis for its conclusions and its compliance with the terms of this paragraph (h), 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.

(ii) A bank may treat a person as a governmental department, agency, or entity if the name of such person reasonably indicates that it is described in paragraph (h)(2)(ii) or (h)(2)(iii) of this section, or if such person is known generally in the community to be a State, the District of Columbia, a tribal government, a Territory or Insular Possession of the United States, or a political subdivision or a wholly-owned agency or instrumentality of any of the foregoing. An entity generally exercises governmental authority on behalf of the United States, a State, or a political subdivision, for purposes of paragraph (h)(2)(iii) of this section, only if its authorities include one or more of the powers to tax, to exercise the authority of eminent domain, or to exercise police powers with respect to matters within its jurisdiction. Examples of entities that exercise governmental authority include, but are not limited to, the New Jersey Turnpike Authority and the Port Authority of New York and New Jersey.

(iii) In determining whether a person is described in paragraph (h)(2)(iv) of this section, a bank may rely on any New York, American or Nasdaq Stock Market listing published in a newspaper of general circulation, or any commonly accepted or published stock symbol guide, on any information contained on the Securities and Exchange Commission ''Edgar'' System, or on any information contained in an Internet World-Wide Web site or sites maintained by the New York Stock Exchange, the American Stock Exchange, or the National Association of Securities Dealers.

(iv) In determining whether a person is described in paragraph (h)(2)(v) of this section, a bank may rely upon:

(A) Any reasonably authenticated corporate officer's certificate;

(B) Any reasonably authenticated photocopy of Internal Revenue Service Form 851 (Affiliation Schedule) or the equivalent thereof for the appropriate tax year; or

(C) A person's Annual Report or Form 10–K, as filed in each case with the Securities and Exchange Commission.

(v) The records maintained by a bank to document its compliance with and administration of the rules of this paragraph (h) shall be kept in accordance with the provisions of section 103.38.

(5) *Limitation on exemption.* A transaction carried out by an exempt person as an agent for another person who is the beneficial owner of the funds that are the subject of a transaction in currency is not subject to the exemption from reporting contained in paragraph (h)(1) of this section.

(6) *Effect of exemption; limitation on liability.* (i) No bank shall be subject to penalty under this part for failure to file a report required by section 103.22(a) with respect to a transaction in currency by an exempt person with respect to which the requirements of this paragraph (h) have been satisfied, unless the bank:

(A) Knowingly files false or incomplete information with respect to the transaction or the customer engaging in the transaction; or

(B) Has reason to believe that the customer does not meet the criteria established by this paragraph (h) for treatment of the transactor as an exempt person or that the transaction is not a transaction of the exempt person.

(ii) Absent specific knowledge of any information that would be grounds for revocation as provided in paragraph (h)(8) of this section, a bank is required to verify the status of those entities it has designated as exempt persons only once each year.

(iii) A bank that files a report with respect to a currency transaction by an exempt person rather than treating such person as exempt shall remain subject, with respect to each such report, to the rules for filing reports, and the penalties for filing false or incomplete reports that are applicable to reporting of transactions in currency by persons other than exempt persons. A bank that continues to treat a person described in paragraph (h)(2) as exempt from the reporting requirements of section 103.22(a) on a basis other than as provided in this paragraph (h) shall remain subject to the rules governing an exemption on such other basis and to the penalties for failing to comply with the rules governing such other exemption.

(7) *Obligation to file suspicious activity reports, etc.* Nothing in this paragraph (h) relieves a bank of the obligation, or alters in any way such bank's obligation, to file a report required by section 103.21 with respect to any transaction, including any transaction in currency, or relieves a bank of any reporting or recordkeeping obligation imposed by this Part (except the obligation to report transactions in currency pursuant to this section to the extent provided in this paragraph (h)).

(8) *Revocation.* The status of any person as an exempt person under this paragraph (h) may be revoked by FinCEN by written notice, which may be provided by publication in the **Federal Register** in appropriate situation, on such terms as are specified in such notice. Without any action on the part of the Treasury Department and subject to the limitation on liability set forth in paragraph (h)(6)(ii) of this section:

(i) The status of an entity as an exempt person under paragraph (h)(2)(iv) of this section ceases once such entity ceases to be listed on the applicable stock exchange; and

(ii) The status of a subsidiary as an exempt person under paragraph (h)(2)(v) of this section ceases once such subsidiary ceases to have at least 51 per cent of its common stock owned by a listed entity.

(9) *Transitional rule.* No penalty will be imposed for the failure to apply paragraph (h)(2)(vi) of this section, if a bank treats a person described in paragraph (h)(2)(iv) or (h)(2)(v) of this section as an exempt person during the period ending May 1, 1998.

Dated: August 27, 1997.

Stanley E. Morris,

Director, Financial Crimes Enforcement Network.

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