CLIENT ALERT

FinCEN's New Customer Due Diligence Rule Becomes Applicable

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The deadline for financial institutions to implement the new customer due diligence ("CDD") procedures required by the U.S. Department of the Treasury's Financial Crimes Enforcement Network ("FinCEN") occurred on May 11, 2018. FinCEN originally published the final version of anti-money laundering ("AML") regulations requiring certain financial institutions to identify the "beneficial owners" of each "legal entity customer" and to verify the identities of such owners on May 11, 2016.[1] FinCEN maintains a set of frequently asked questions ("FAQs") pertaining to the new requirements on its website.[2]

The new CDD requirements apply to "covered financial institutions," which include banks and other depositary institutions, broker-dealers, mutual funds, futures commission merchants, and introducing brokers in commodities. However, they do

[1] The final rule was published at 81 Fed. Reg. 29398-29458 (May 11, 2016) and adds a new section to the AML regulations at 31 C.F.R. § 1010.230. For a description of the regulations in their final form, please see Willkie Farr & Gallagher LLP, "FinCEN Issues Long-Anticipated Requirements for AML Due Diligence on Beneficial Owners" (May 24, 2016), available here.

[2] The "Frequently Asked Questions Regarding Customer Due Diligence Requirements for Financial Institutions" are available on FinCEN's website and are linked here. For a description of particularly noteworthy FAQs, please see Willkie Farr & Gallagher LLP, "FinCEN Publishes Frequently Asked Questions for AML Due Diligence on Beneficial Owners" (August 2, 2016), available here.

not apply to all entities considered financial institutions under the Bank Secrecy Act[3] ("BSA"). For example, registered investment advisers are not currently considered financial institutions under the BSA.[4]

Covered financial institutions must establish and maintain written procedures "reasonably designed" to identify and verify the identities of two types of "beneficial owners" of legal entity customers. First, a covered financial institution must identify and verify the identity of any natural person having an equity ownership interest of 25% or more in a legal entity customer. Second, a covered financial institution must also identify and verify the identity of a "control person," meaning any individual having significant responsibility for controlling, managing, or directing the legal entity customer. Examples of a control person include a chief executive officer, managing member, general partner, or senior executive officer, or other individual who regularly performs such functions. If no individual satisfies the ownership prong, the covered financial institution must still identify and verify the identity of a control person.

Financial institutions may rely on beneficial ownership information supplied by the customer, so long as they have no knowledge that would reasonably call into question the validity of that information. They do not have to verify an individual's status as a beneficial owner. Beneficial owner due diligence must be conducted at the time a new account is opened and also when, in the course of normal customer transaction monitoring, the financial institution detects information pertinent to its assessment of the money-laundering risk posed by the customer and such information indicates a possible change of beneficial ownership. The regulations do not apply retroactively, in that financial institutions do not need to conduct this due diligence on all existing accounts.

There are exceptions to the CDD requirements for certain types of legal entity customers, such as: companies publicly traded in the United States and issuers subject to section 15(d) of the Securities Exchange Act of 1934 that already have to disclose beneficial ownership in U.S. Securities and Exchange Commission filings; financial institutions regulated by a federal functional regulator or state bank regulator; registered investment companies and investment advisers; entities required to register with the U.S. Commodity Futures Trading Commission; public accounting firms; insurance companies regulated by a state; and others.[5]

In addition to imposing new due diligence requirements, the final regulation makes explicit certain AML program requirements that had previously been implicit in suspicious activity reporting requirements. It requires covered financial

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[3] *See* 31 U.S.C. § 5312(a)(2).

[4] On September 1, 2015, FinCEN published proposed regulations that would define registered investment advisers as "financial institutions" and require them to implement AML programs meeting certain minimum standards. The proposed regulations are still pending and have no clear timeline for finalization. As proposed, these regulations do not require investment advisers to implement CDD procedures with respect to beneficial owners of their customers (i.e., investors), but this could change when the final regulations are issued. For more information about the proposed AML regulations for Investment Advisers, please see Willkie Farr & Gallagher LLP, "Treasury Department Proposes Anti-Money Laundering Regulations for Investment Advisers" (Aug. 28, 2015), available here.

[5] *See* 31 C.F.R. § 1010.230(e)(2).

institutions to develop an understanding of the nature and purpose of customer relationships in order to develop individual customer risk profiles, as well as to conduct ongoing monitoring and, on a risk basis, maintain and update customer information.

If you have any questions regarding this client alert, please contact the following attorneys or the attorney with whom you regularly work.

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