ALERT MEMORANDUM

AML Regulators Clarify Diligence Requirements for Politically Exposed Persons

August 31, 2020

On August 21, the Financial Crimes Enforcement Network (**FinCEN**), together with the federal banking agencies[1] (the **Agencies**), released a statement (**Statement**) to clarify banks' customer due diligence (**CDD**) obligations for politically exposed persons (**PEPs**). The Statement affirms that (i) there is no regulatory requirement, and no supervisory expectation, for banks' Bank Secrecy Act (**BSA**) / anti-money laundering (**AML**) programs to include "unique, additional due diligence steps" for customers who are PEPs and (ii) there is no regulatory requirement for banks to screen customers and their beneficial owners for PEPs. Instead, the Statement confirms that PEP customers should be subject to the same risk-based approach to CDD that applies to any other customer, but that PEP status (and screening for PEPs) may be a factor in developing a customer risk profile and assessing money laundering risk. It also reminds banks of the continued U.S. national security and law enforcement interest in detecting and combatting public corruption and other criminality involving PEPs.

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[1] The Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, and the Office of the Comptroller of the Currency.

PEPs are not defined in FinCEN's BSA/AML regulations, and the Statement does not provide a definition, although it notes that the Agencies do not interpret PEPs to include U.S. officials, and observes that the term is "commonly used . . . to refer to foreign individuals who are or have been entrusted with a prominent public function, as well as their immediate family members and close associates." These individuals may present a higher risk of having funds derived from corruption or other illegal activity by virtue of their public position, and therefore may merit additional scrutiny in the context of a bank's AML program.[2]

The Statement is largely consistent with prior Agency guidance on diligence obligations regarding PEPs.[3] It was issued to address inquiries from banks on how to conduct risk-based due diligence on PEPs in light of the CDD requirements contained in FinCEN's 2016 CDD Final Rule (**2016 CDD Rule**). The 2016 CDD Rule amended FinCEN's BSA/AML regulations to introduce a mandatory (not risk-based) requirement to collect the identities of certain ultimate beneficial owners of a bank's customers and to codify a "fifth pillar" for AML program requirements that mandates "appropriate risk-based procedures for conducting ongoing customer due diligence, to include . . . developing a customer risk profile; and conducting ongoing monitoring . . . ."[4] In connection with issuing the Statement, the Agencies also rescinded 2001 guidance that, although nonbinding, could be read to encourage more prescriptive due diligence requirements for PEPs.[5]

The Statement expressly does not alter existing BSA/AML legal or regulatory requirements, nor does it establish new supervisory expectations. But it helpfully confirms that banks may approach PEP identification and diligence flexibly, following a risk-based approach, and acknowledges that PEP relationships present varying levels of money-laundering risk. For example, it notes that PEPs with a limited transaction volume, a low-dollar deposit account, known legitimate source(s) of funds, or access only to products or services that are subject to specific terms and payment schedules, might reasonably be characterized as low risk. By contrast, it observes that wealth management accounts—even those that fall outside of the definition of "private banking account" under FinCEN's regulations—may pose a higher risk of illicit financial activity.

The Statement also suggests factors that could go into developing a customer risk profile for a PEP under the 2016 CDD Rule, including:

— The nature of the PEP's (or the PEP's close associate's or family member's) public position, official government responsibilities, and influence over government activities and officials;

— The PEP's access to significant government assets or funds;

— Any indication the PEP may misuse his or her public position for personal gain;

— For a PEP that is no longer in active government service, the length of time that the PEP has been out of office, and the level of influence he or she may still hold;

— The volume and nature of transactions and the type of products and services used;

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[2] *See, e.g.*, *FATF Guidance: Politically Exposed Persons (Recommendations 12 and 22)*, Financial Action Task Force (June 2013), available at: *http://www.fatf-gafi.org/media/fatf/documents/recommendations/Guidance-PEP-Rec12-22.pdf*.

[3] *See BSA/AML Examination Manual*, Federal Financial Institutions Examination Council, available at: https://bsaaml.ffiec.gov/manual; *Advisory on Human Rights Abuses Enabled by Corrupt Senior Foreign Political Figures and their Financial Facilitators*, FinCEN (June 12, 2018), available at: https://www.fincen.gov/sites/default/files/advisory/2018-06-12/PEP%20Facilitator%20Advisory_FINAL%20508.pdf (**2018 FinCEN Advisory**).

[4] *Customer Due Diligence Requirements for Financial Institutions*, 81 Fed. Reg. 29398 (May 11, 2016); 31 CFR §§ 1010.230 and 1020.210.

[5] *See Guidance on Enhanced Scrutiny for Transactions that May Involve the Proceeds of Foreign Corruption* (January 2001), available at: https://www.newyorkfed.org/medialibrary/media/banking/circulars/11319.pdf.

— The geography of a PEP's activity and domicile, including the jurisdiction's legal and enforcement frameworks, ethics reporting and oversight requirements; and

— The overall nature of the customer relationship.

The Statement is likely to be most helpful for banks offering low-risk products and services that are unlikely to be abused (by a PEP or any other customer) for money laundering purposes, where additional PEP-specific due diligence measures may be of little value. To the extent such banks, or their examiners, were under the impression that additional PEP due diligence procedures were mandatory, even for low-risk relationships, the Statement should provide an opportunity to reassess the value of those additional procedures.

The Statement should not, however, be read as permission to reduce vigilance over the money laundering threat posed by public corruption of foreign officials, which "continues to be a U.S. national security priority" and has been the focus of other recent FinCEN advisories.[6] And it does not alter the existing special due diligence requirements for private banking accounts owned by "senior foreign political figures" under the BSA and FinCEN's implementing regulations, which the Agencies describe as a subset of PEPs.[7]

Although the Statement is primarily focused on bank BSA/AML obligations, and neither the SEC, CFTC, nor securities and commodities self-regulatory organizations joined the Statement, it should be reasonable for other regulated financial institutions, such as broker dealers and futures commission merchants, to view it as a clarification of standards for CDD under the 2016 CDD Rule and BSA/AML programs more broadly.

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[6] *See*, *e.g.*, 2018 FinCEN Advisory, *supra* note 3.

[7] *See* 31 C.F.R. §§ 1010.605, 1010.620.