

May 4, 2012

FinCEN
P.O. Box 39
Vienna, Virginia 22183

Re: Department of the Treasury Financial Crimes Enforcement Network Advance Notice of Proposed Rulemaking—Customer Due Diligence Requirements for Financial Institutions; RIN 1506-AB15, 77 Fed. Reg. 13046 (March 5, 2012)

Dear Sir/Madam:

On behalf of the American Bar Association, which has nearly 400,000 members, I write to express our concerns over the above-referenced advance notice of proposed rulemaking (Notice) issued by the Treasury Department's Financial Crimes Enforcement Network (FinCEN) regarding customer due diligence requirements for financial institutions. As Chair of the ABA Task Force on Gatekeeper Regulation and the Profession, I have been authorized to express the ABA's views with respect to the Notice.

The ABA supports all reasonable and necessary domestic and international efforts to combat money laundering and terrorist financing and has worked diligently with the rest of the legal community, federal and international law enforcement authorities, and the states to advance those reforms. Although the ABA shares FinCEN's overarching goal of "protect[ing] the United States financial system from criminal abuse and to guard against terrorist financing, money laundering and other financial crimes,"¹ the ABA opposes those proposals contained in the Notice that would require law firms that establish accounts at financial institutions on behalf of their clients to disclose the identity and other beneficial ownership information regarding those clients. If adopted in their current form, those proposals could impose unreasonable and excessive burdens on many law firms with client trust accounts and could undermine both the confidential lawyer-client relationship and traditional state court regulation of lawyers. The ABA therefore urges FinCEN not to proceed with those proposals in the Notice.

Ongoing Legal Profession, International and State Reforms are the Most Effective Means of Combating Money Laundering and Terrorist Financing

Over the past several years, the ABA has reached out to and supported efforts by the legal profession, international organizations, and the states to fight money laundering and terrorist financing in ways that minimize the impact on the lawyer-client relationship, the U.S. economy, and state regulators. Towards that end, the ABA worked closely with a number of specialty bar associations to develop and promote the "Voluntary Good Practices Guidance for Lawyers to Detect and Combat Money Laundering and Terrorist Financing" (Voluntary Guidance).

¹ See Notice, 77 Fed. Reg. at 13047.

The Voluntary Guidance, which is based on the principle that the risks posed by certain types of clients and matters are far greater than those posed by others, allows U.S. lawyers to combat money laundering and terrorist financing by taking prudent, proportional, risk-based steps tailored to the individual situation rather than adhering to a burdensome and rigid “one-size-fits-all” approach. This voluntary, legal profession-initiated effort will help lawyers to effectively combat money laundering and terrorist financing, while still complying with their existing court-imposed ethical duties and other legal obligations. Since the ABA House of Delegates adopted the Voluntary Guidance in August 2010, the ABA has worked diligently to educate lawyers, judges, state and local bars, and the general public regarding the problem of money laundering and the benefits of following the Voluntary Guidance. The ABA also has kept key congressional leaders and their staff, as well as the Treasury Department and other relevant federal agencies, apprised of its extensive efforts in this regard.²

In addition to the Voluntary Guidance, the ABA and numerous other relevant law societies and bar associations from around the world have actively engaged with the intergovernmental body known as the Financial Action Task Force on Money Laundering (FATF) in a collaborative effort to update and further refine the existing international anti-money laundering and counter terrorist financing standards known as the “Forty Recommendations,” or the “International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation—the FATF Recommendations.” As part of that engagement, the ABA filed numerous comment letters with the FATF³ last year and earlier this year encouraging it to preserve the “risk-based” approach of the existing standards and to avoid imposing any unworkable or burdensome new beneficial ownership or other “rules-based” reporting requirements on the legal profession.

The ABA also has been working closely with the states’ secretaries of state, the Treasury Department, and other entities on alternative solutions to the problem of money laundering and terrorist financing that would not require new federal legislation or regulations. For example, substantive law groups within the ABA have developed proposals that would require companies to collect, maintain, and disclose more information regarding their incorporators, officers, directors, and shareholders in order to provide additional useful tools to law enforcement officials, but within the existing state company formation system. These proposals would aid law enforcement without creating unnecessary new federal mandates that would preempt or interfere with the confidential lawyer-client relationship, the attorney-client privilege, traditional state court regulation of lawyers, or existing state business formation practices.

²The ABA’s April 27, 2011 letter to the Senate Homeland Security and Governmental Affairs Committee’s Permanent Subcommittee on Investigations outlining our efforts to promote the Voluntary Good Practices Guidance for Lawyers to Detect and Combat Money Laundering and Terrorist Financing, and the full text of the Guidance, is available at: http://www.americanbar.org/content/dam/aba/uncategorized/2011/2011apr27_gatekeepers_1.authcheckdam.pdf.

³See the ABA’s comments to the FATF sent in January, June, September, and December 2011 and March 2012 at: http://www.americanbar.org/advocacy/governmental_legislative_work/letters_testimony/international_law.html and http://www.americanbar.org/content/dam/aba/uncategorized/2011/gao/2011sept16_gatekeep_1.authcheckdam.pdf.

Although the ABA is encouraged by the various proposals described above, the ABA has long opposed attempts by Congress or federal agencies to regulate lawyers and law firms as “financial institutions” under the Bank Secrecy Act or otherwise to impose new federal regulatory mandates on lawyers engaged in the practice of law where the effect would be to impose excessive burdens on the legal profession or undermine the confidential lawyer-client relationship, the attorney-client privilege, or traditional state court regulation of lawyers.⁴ Unfortunately, certain specific proposals contained in the Notice raises some of these same concerns.

FinCEN’s Proposals to Require Law Firms to Disclose Client Identity and Beneficial Ownership Information Regarding Clients On Whose Behalf the Law Firms Establish Accounts

In its Notice, FinCEN seeks comment on a number of new customer due diligence proposals, including a categorical requirement for financial institutions to identify beneficial ownership of their accountholders, subject to risk-based verification and pursuant to an alternative definition of beneficial ownership. Although the Notice is focused primarily on financial institutions such as banks, brokers or dealers in securities, mutual funds, future commission merchants, introducing brokers in commodities, and other financial entities, certain language in the Notice raises the possibility that FinCEN may also seek to impose new client identity and beneficial ownership reporting requirements on law firms that establish financial accounts on behalf of clients.⁵ In particular, the Notice contains the following passage:

FinCEN believes that, although the use of legal entities to mask beneficial ownership presents the primary illicit finance vulnerability and accordingly the need for beneficial ownership identification, the question of beneficial ownership can also arise in the context of accounts established by an individual or entity (*e.g. law or accounting firm*) which could be acting on behalf of another individual or individuals without disclosing this fact. FinCEN is considering how to best address this potential vulnerability. A possible solution would be to require any individual or entity (other than a regulated financial institution) opening an account at a financial institution to state that he, she, or it is not acting on behalf of any other person. Such approach would be analogous to longstanding FinCEN transaction reporting requirements, under which a financial institution must record identifying information with respect to “any person or entity on whose behalf such transaction is to be effected.” [citation omitted] For individuals and entities acting on behalf of another person, the beneficial ownership element of a CDD program requirement would apply to the person on whose

⁴ For example, the ABA has expressed strong opposition to S. 1483, the “Incorporation Transparency and Law Enforcement Assistance Act,” which would superimpose new federally mandated requirements on existing state company formation practices and regulate many practicing lawyers and law firms as “formation agents” subject to the bill’s beneficial ownership mandates. The ABA also opposes those provisions of S. 1483 that would regulate lawyers and law firms as “financial institutions” under the Bank Secrecy Act and thereby impose new federal anti-money laundering (AML), combating the financing of terrorism (CFT), and suspicious activity reporting (SAR) requirements on them. The ABA’s December 16, 2011 letter to Sens. Joseph Lieberman (I-CT) and Susan Collins (R-ME), the Chairman and Ranking Member of the Senate Homeland Security and Governmental Affairs Committee, is available at: http://www.americanbar.org/content/dam/aba/uncategorized/2011/gao/2011dec16_incorptransparency_l.authcheckdam.pdf.

⁵ See Notice at 13052.

behalf the account is being opened. FinCEN seeks comment on this approach, as well as suggestions for other approaches. [emphasis supplied]⁶

The Notice also states that:

...there may be instances in which obtaining information about the beneficial owners of *assets* in an account may be warranted instead [of information about the beneficial owner of the legal entity establishing the account], such as where a legal entity...opens an account for the benefit of its customers (as opposed to for its own benefit), as those customers could pose a money laundering risk through their ability to access the financial system through that account relationship. In such instances, FinCEN recognizes that the potential definition of “beneficial owner” described above may not generally be relevant or appropriate for AML/CFT purposes. Accordingly, FinCEN seeks comment on potential alternative definitions of “beneficial owner” in instances where obtaining information about the beneficial owners of assets in an account may be warranted. [emphasis supplied]⁷

The ABA’s Concerns Regarding the Notice

The ABA opposes those proposals contained in the Notice quoted above, which could require law firms to report sensitive and confidential information regarding their clients whenever the law firms establish accounts on behalf of those clients, for several important reasons.

1. The Proposals in the Notice are Overly Broad and Could Require Law Firms to Report the Identity of Their Clients and Beneficial Ownership Information Regarding Their Corporate Clients⁸

The ABA is concerned that if these proposals in the Notice were adopted, they could have the unintended—and onerous—effect of requiring law firms to report the identity of their individual and corporate clients and to collect and submit detailed beneficial ownership information regarding each of their corporate clients. Lawyers often hold funds of clients in one or more separate trust accounts they establish at banks or other financial institutions. The U.S. Supreme Court has explained that “attorneys are frequently required to hold clients’ funds for various lengths of time. It has long been recognized that they have a professional and fiduciary obligation to avoid commingling their clients’ money with their own, but it is not unethical to pool several clients’ funds in a single trust account.” *Brown v. Legal Foundation of Washington*, 538 U.S. 216, 220-221 (2003) (discussing *Phillips v. Washington Legal Foundation*, 524 U.S. 156, 160-161 (1998)). In fact, ABA Model Rule of Professional Conduct 1.15 dealing with “Safekeeping of Property” requires lawyers to deposit into a client trust account any legal fees and expenses that have been

⁶ Id. at 13052-13053.

⁷ Id. at 13052.

⁸ For convenience, references in this letter to “corporate clients” means those clients that are corporations, partnerships, limited liability companies, and other legal entities.

paid in advance, and the lawyer is permitted to withdraw funds from the trust account “only as fees are earned or expenses incurred.”⁹

Every state court system has adopted—and vigorously enforces—binding rules similar to ABA Model Rule 1.15 that require lawyers to keep their client funds in separate trust accounts until the fees are earned or expenses incurred.¹⁰ Because all lawyers and law firms are subject to this fundamental ethical requirement, the proposals in the Notice could have the practical effect of requiring any law firm receiving an advance fee (or advance expenses) from its clients, whether individual or corporate clients, to report the identity of those clients, as well as detailed beneficial ownership information to the government for all of the law firm’s corporate clients. The considerable time and expense that would be required to collect and report this beneficial ownership information for many—if not most—of a law firm’s corporate clients is clearly disproportionate to any marginal AML or CFT benefits that this information might be expected to provide to FinCEN and other federal agencies.

2. The Proposals in the Notice Could Force Lawyers to Violate Client Confidentiality

The ABA is concerned that by requiring law firms to disclose confidential information to the government regarding the identity of their individual and corporate clients—as well as additional confidential information regarding the beneficial owners of their corporate clients—whenever the law firm establishes an account for the client or deposits advance fees or expenses received from the client into the law firm’s trust account, the proposals in the Notice outlined above are inconsistent with ABA Model Rule of Professional Conduct 1.6 dealing with “Confidentiality of Information” and with the many binding state rules of professional conduct that closely track the ABA Model Rule.¹¹ ABA Model Rule 1.6 states that “a lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent...” or unless one or more of the narrow exceptions listed in the Rule is present.¹²

The range of client information that lawyers are not permitted to disclose under ABA Model Rule 1.6 is broader than that covered by the attorney-client privilege. Although Rule 1.6 prohibits lawyers from disclosing information protected by the attorney-client privilege and the work product doctrine, the Rule also forbids lawyers from voluntarily disclosing other non-privileged information

⁹ See ABA Model Rule of Professional Conduct 1.15(c).

¹⁰ See chart comparing ABA Model Rule 1.15 in the various individual states, available at:

http://www.americanbar.org/content/dam/aba/administrative/professional_responsibility/mrpc_1_15.authcheckdam.pdf

¹¹ See ABA Model Rule of Professional Conduct 1.6, and the related commentary, available at

http://www.americanbar.org/groups/professional_responsibility/publications/model_rules_of_professional_conduct/rule_1_6_confidentiality_of_information.html. See also Charts Comparing Individual Professional Conduct Rules as Adopted or Proposed by States to ABA Model Rules, available at

http://www.americanbar.org/groups/professional_responsibility/policy.html.

¹² Although ABA Model Rule 1.6(6) allows a lawyer to disclose confidential client information “to comply with other

law or a court order,” nothing in the Notice, the Bank Secrecy Act, or the other statutes cited by FinCEN expressly or implicitly requires lawyers to reveal client confidences to the government.

that the client wishes to keep confidential.¹³ This category of non-privileged, confidential client information includes the identity of the client as well as other information related to the legal representation, including, for example, the beneficial ownership of the corporate client and other confidential information that the client may choose to reveal to the lawyer but does not wish to be revealed to third parties.

FinCEN suggests in the Notice that a lawyer or law firm opening an account at a financial institution should be required to state that he, she, or it is not acting on behalf of any other person. Because law firms routinely open trust accounts for the express purpose of holding funds in trust for their clients—or simply deposit advance fees and expenses received from their clients into the law firm's existing trust accounts—lawyers and law firms would be unable to make this type of statement without violating their ethical duties under Rule 1.6 and the corresponding state court ethical rules. As noted above, other language in the Notice goes even further and suggests that FinCEN may seek to require every law firm to disclose the identity of their individual and corporate clients—as well as the beneficial owners of its corporate clients—whenever it helps those clients establish an account or simply receives advance fees or expenses from the client and deposits those fees in the law firm's trust account.

To the extent that the Notice suggests that lawyers and law firms must disclose their clients' identities or their corporate clients' beneficial owners whenever they establish accounts for those clients or deposit client funds into the law firms' trust accounts, that language is clearly inconsistent with lawyers' existing ethical duties outlined in Model Rule 1.6 and the binding state rules of professional conduct that mirror the ABA Model Rule. In addition, the risk that the client's identity—and other confidential beneficial ownership information regarding corporate clients—could be divulged by the lawyer or law firm could discourage a client from retaining a law firm and entrusting funds with the lawyer or law firm, thereby interfering in a substantial way with a client's fundamental right to counsel.

Conclusion

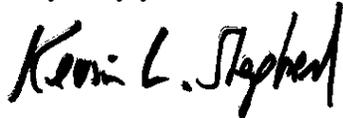
In sum, the ABA has serious concerns regarding those provisions in the Notice proposing that lawyers or law firms that establish accounts at financial institutions on behalf of their clients may be required to disclose the identity of those clients or other confidential information regarding their corporate clients' beneficial owners. If adopted in their current form, these proposals could impose substantial and unjustified burdens on lawyers, law firms, and their clients, while undermining the lawyer-client relationship, client confidentiality under ABA Model Rule 1.6 and the corresponding state court rules, as well as traditional state court regulation of lawyers. Therefore, we urge you to not proceed with these proposals contained in the Notice.

¹³ See, e.g., Alabama Ethics Op. 89-111 (1989) (lawyer may not disclose name of client to funding agency); Texas Ethics Op. 479 (1991) (law firm that obtained bank loan secured by firm's accounts receivable may not tell bank who firm's clients are and how much each owes); South Carolina Ethics Op. 90-14 (1990) (lawyer may not volunteer identity of client to third party); and Virginia Ethics Op. 1300 (1989) (in absence of client consent, nonprofit legal services corporation may not comply with federal agency's request for names and addresses of parties adverse to certain former clients, since that may involve disclosure of clients' identities, which may constitute a client secret).

May 4, 2012
Page 7

Thank you for considering the views of the ABA on these important issues. If you have any questions regarding the ABA's position on the Notice, please contact me at (410) 244-7772 or klshepherd@venable.com or Thomas M. Susman, Director of the ABA Governmental Affairs Office, at (202) 662-1765 or thomas.susman@americanbar.org

Very truly yours,

A handwritten signature in black ink that reads "Kevin L. Shepherd". The signature is written in a cursive, slightly slanted style.

Kevin L. Shepherd

cc: Members, ABA Task Force on Gatekeeper Regulation and the Profession
Thomas M. Susman, Director, ABA Governmental Affairs Office
R. Larson Frisby, Associate Director, ABA Governmental Affairs Office
Duncan E. Osborne, Esquire
William H. Clark, Jr., Esquire
Leigh Basha, Esquire
Gary W. Sutton, Esquire
Ms. Sarah Runge