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Department of the Treasury
Office of Critical Infrastructure
Protection and Compliance Policy
Room 1327
Main Treasury Building
1500 Pennsylvania Ave., NW.
Washington, DC 20220

December 12, 2007

Re: **FRB** Docket No. R-1298; **Treasury** Docket No. DO-2007-0015; Prohibition on Funding of Unlawful Internet Gambling; 72 Federal Register 56680; October 4, 2007

Dear Sir/Madam:

The Consumer Bankers Association (“CBA”) is pleased to submit comments on the proposed “Prohibition on Funding of Unlawful Internet Gambling” (the “Proposal”), issued by the Board of Governors of the Federal Reserve System and the Department of Treasury (the “Agencies”). The CBA is the recognized voice on retail banking issues in the nation’s capital. Member institutions are the leaders in consumer, auto, home equity and education finance, electronic retail delivery systems, privacy, fair lending, bank sales of investment products, small business services and community development. The CBA was founded in 1919 to provide a progressive voice in the retail banking industry. The CBA represents over 750 federally insured financial institutions that collectively hold more than 70% of all consumer credit held by federally insured depository institutions in the United States.

Overview

CBA’s comment will be primarily directed towards the provisions relating to automated clearing house systems (ACH); check collection systems; and wire-transfers (____.3 (a), (b), and (c)). We are in large part favorably disposed towards those portions of the Proposal affecting credit card transactions, but have included suggestions that may help to clarify certain requirements. We wish to emphasize that the Proposal’s focus on “policies and procedures” intended to effect compliance for card issuers is, in our opinion, appropriate and urge its retention, rejecting attempts to mandate the blocking of

specific transactions. The volume of credit card transactions makes any search for particular items infeasible.

CBA and its members believe that the use of the US payment system to enforce various legal requirements imposed by legislation often not directly related to banking places unnecessary stress on this system and has grown to a point that it is a serious burden on banks and other payment system participants. Nevertheless we desire to be helpful in implementation of the government's policy decision expressed through the Congress to "block" Internet gambling transactions in order to ensure the best possible result for the continued functioning of the banking and payment systems. We will address our concerns primarily through a discussion of the terminology used in the Proposal.

Clarification of Terminology

Unlawful Internet Gambling

In order to achieve this goal, a smooth implementation of the anti-gambling policy within the payment system, a clear delineation of the responsibilities of financial institutions is absolutely necessary in order to avoid costly and counterproductive compliance problems, as well as liability that could arise from any violation of federal law, pursuant to state unfair and deceptive practices acts. For example, clarification should start with the term "Unlawful Internet Gambling", as defined in section __.2, which covers placing, receiving, or transmitting a bet or wager by means that involve the use of the Internet "where such bet or wager is unlawful under any applicable Federal or State law in the State or Tribal lands in which the bet or wager is initiated, received, or otherwise made . . ." Incorporation of other statutes, which may be amended from time to time, into a final rule presents a complex and ever-changing compliance challenge. However, the complexity inherent in this directive is not limited to the dynamic nature of state and federal law. Illegality may depend upon the location of the bettor, who would not be restricted to placing bets while at his home address, but could do so while visiting a location where such bets are legal. Tracking this series of unknowns is not technologically possible. Another solution must be found.

While the Agencies have hesitated to create a list of organizations engaged in unlawful Internet gambling (on the style of OFAC lists), it may nevertheless be the best approach to assign a government agency the responsibility of creating a list that would be based upon an interpretation of various state and federal gambling laws and a review of the activities of the entities that may be involved in these kinds of transactions, at least as applied to ACH, check and wire-transfer transactions. CBA members have generally expressed support for the Proposal's coding approach in the card issuer context. For other transactions, while it is a difficult, time-consuming task, an exclusive list of entities from which transactions must be blocked would facilitate compliance. Responsibility to go beyond the list must be definitively eliminated. This approach would eliminate many of the problems described in this comment letter and would aid in the creation of plans that could credibly claim to provide for high levels of compliance.

Otherwise, in order to create an adequate compliance system to block “unlawful Internet gambling,” at least for ACH, check and wire-transfer transactions, banks would need specific and well-defined rules regarding the types of transactions that must be identified or blocked as well as protection from liability for any transaction in which the legality at the time of the transaction is unclear. The standards and definitions currently in the Proposal fall far short of this goal. This problem is exacerbated when banks attempt to instruct their correspondents on the monitoring of Internet gambling transactions, as also contemplated in the Proposal (see section __.6(b)(2) and (d)(2)). It may be that the only real leverage a bank has over its correspondent to require compliance with monitoring requirements is to terminate the relationship. This cannot be a result intended by the Proposal.

Knowledge

The Proposal in section __.6, contains a list of policies and procedures to identify and block or otherwise prevent or prohibit restricted transactions for each type of non-exempt participant in a designated payment system. The standards applicable to each of the policies fall into one of two categories: the participant is required to have in place procedures to be followed if the participant “becomes aware” that a customer has received a restricted transaction; or the participant must have procedures to be followed with respect to a foreign or other recipient that is “found to have” received payments or otherwise engaged in transactions that are restricted transactions. These standards lack clarity and, without further explicit definition, will be extremely problematic in the development of a credible compliance plan. The only workable standard is *actual* knowledge by a person in the relevant organization that is responsible for the organization’s compliance function as it relates to the transaction in question. CBA urges the adoption of this standard.

Identification of Restricted Transactions

The Proposal requires that policies and procedures of a card-system operator, merchant acquirer or a card issuer are reasonably designed to prevent or prohibit restricted transactions if they establish transaction and merchant codes that are required to accompany authorization requests and provide the means for the card system or issuer to identify and block restricted transactions. As long as card issuers are clearly protected in their reliance on card systems’ development of appropriate policies and procedures, this approach seems workable. Creation of these policies and reliance upon them should provide absolute protection, without further reasonableness tests, as further discussed below.

Blocking, Prevention, Prohibition of Transactions

The requirement to block, prevent or prohibit unlawful Internet gambling transactions—a fundamental concept in the Proposal—is lacking in fulsome definition. Is this blocking responsibility the same prescribed action set forth in anti-money laundering regulations like those followed under programs administered by the Treasury Department’s Office of

Foreign Assets Control (“OFAC”); or does it carry a different connotation? Does the Proposal envision a procedure that includes not only cessation of processing, but also (similar to OFAC procedures) payment of the amount of the transaction into a blocked account in order to preclude use of the funds? This requirement must be translated into specific operational acts that may not be consistent with other types of mandated blocking of transactions. The differences in the types of blocking that may be required should be reviewed and distinguished in a final rule. Preventing or prohibiting transactions should likewise be subject to clear definition.

In addition, section __.6(c) (2) (ii) specifies that policies and procedures are reasonably designed to prevent or prohibit restricted transactions if they provide for on-going “monitoring or testing to detect potential restricted transactions.” CBA submits that there should be no monitoring or testing by issuers to determine if a merchant has used appropriate transaction codes if the card system has policies designed to do so. Issuers and merchant acquirers should be allowed to rely on the card systems’ testing and monitoring, without further, duplicative testing.

Finally, we note that, under the Truth In Lending Act and Regulation Z, home equity lines of credit advances may be denied only for the reasons specified in the Regulation (see section 226.5b (f)(3)(vi)). There is no exception in Truth In Lending or Regulation Z for blocking a gambling transaction executed under a home equity line of credit. Exceptions for “unsafe or unsound” practices or for transactions in violation of “material obligations” in the agreement are insufficient to provide creditor protection for blocking gambling transactions. Accordingly another safe harbor covering home equity transactions is necessary in order to avoid regulatory violations and other legal liability.

Reasonable Standard

Similarly, the frequent use of the term “reasonable” in the Proposal presents a subjective standard that will be vulnerable to criticism, not only by regulators, but also by plaintiffs’ attorneys seeking to explore opportunities for litigation possibly under state consumer protection laws. This is not a plea to allow unreasonable behavior, but merely a request for consideration of what compliance professionals will be required to set as standards for operating within the law. Section __.5 (a), for example, requires a financial institution to establish and implement written policies and procedures “reasonably” designed to effect compliance with the rule. Section __.5 (b) (1) then allows a financial institution to rely on “written policies and procedures of the designated payment system that are *reasonably* designed” to comply with the blocking requirements of the Proposal (emphasis mine). Who will determine if a financial institution has acted reasonably in relying on the policies and procedures of a designated payment system; how can a financial institution know if these same policies and procedures were “reasonably designed” to effect compliance (i.e., has the payment system taken the steps required in the rule and what verification of this due diligence is needed); what are the standards for making the determinations that the payment system has acted appropriately in designing its systems reasonably?

The so-called “safe harbor” provision (____.5 (c)) further requires a determination that a person *reasonably* believes that a blocked transaction is a “restricted transaction” as one qualification for “safe harbor” treatment. This third level of reasonableness will create havoc in our attempts to develop testable compliance plans, not only because of the vagueness of the standard, not only because it is the third level of reasonableness required, but also because the text now shifts from reasonable *procedures* on a *systems* level to a determination of reasonableness on a *transaction* level.

Effective Date

Currently the Proposal includes a six-month lead time before the final Internet gambling rule becomes effective. However, we believe that unless the clarifications recommended in this comment are adopted, compliance planning will be lengthy and difficult, especially as those plans cover ACH, checks and wire-transfers. Accordingly, our members will need at least 18 months to create and test the systems necessary to produce a credible compliance plan. Our further recommendation is that the rule be re-proposed so that less speculation is involved in the creation of compliance plans and less disruption of the payment system occurs.

In the alternative, given the nature of the operational problems identified, it may be appropriate to create a final rule dealing only with card issuers and defer regulating the more complex operations related to ACH, check and wire-transfer transactions. This would likely capture the greater portion of restricted transactions and further study could facilitate creation of a final rule that would provide for a smoother operation of the payment system.

Conclusion

Compliance officers expend substantial efforts to construct plans that are logical and, to the extent possible, internally consistent with other, similar requirements, like anti-money laundering regulations, and employ objective metrics to ensure proper application of rules. At a minimum, we would request that the rules for blocking illegal transactions should be distinguished from those in place for other proscribed transactions, and that vague standards like “reasonableness” either be deleted or described in terms of objective standards that can easily be implemented by our compliance personnel and examined by our regulators. Banks face the possibility of disrupted transactions and liability flowing from the lack of clarity in the Proposal.

For the reasons discussed above, we believe that the Proposal, in its current form, is unworkable and cannot be implemented in a way that will produce measurable compliance in an objective fashion. We have suggested different approaches that we believe are more likely to produce proper implementation of the proscribed unlawful activities without creating another burden on the US payment system and another unnecessarily costly compliance requirement. We urge their adoption in a re-proposed rule.

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On behalf of CBA, I truly appreciate the opportunity to comment on the Proposal. If you have any questions regarding these comments, please contact Joseph R. Crouse at (703) 276-3869 or by e-mail at jcrouse@cbanet.org.

Sincerely,

Joseph R. Crouse
Legislative & Regulatory Counsel