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December 12, 2007

By electronic delivery

Jennifer J. Johnson, Secretary
Board of Governors of Federal Reserve System
20th Street and Constitution Avenue, N.W.
Washington, DC 20551

Department of the Treasury
Office of Critical Infrastructure Protection and compliance Policy
Room 1327, Main Treasury Building
1500 Pennsylvania Avenue, N.W.
Washington, DC 20220

Re: Notice of Joint Proposed Rulemaking to implement the Unlawful
Internet Gambling Enforcement Act of 2006 (the "Act")
Treas-DO, Docket Number Treas-DO-2007-0015
Federal Reserve Docket Number R-1298

Ladies and Gentlemen:

Citibank, N.A. ("Citibank"), on behalf of itself and its subsidiaries, appreciates the opportunity to submit this comment in connection with the proposed regulation to implement the Act (the "Proposed Regulation"), which was issued by the Board of Governors of the Federal Reserve System and the Department of the Treasury (the "Agencies") on October 1, 2007. We support the Agencies' effort to issue the rulemaking mandated by the Act and their attempts to understand the practical operational constraints of their constituents

who would be required to adopt and implement policies and procedures pursuant to this rulemaking.

The Proposed Regulation would cover five types of payment systems: (i) payment card systems; (ii) automated clearing house (“ACH”) systems; (iii) check collection systems; (iv) wire transfer systems; and (v) money transmitting systems. In general, it would require certain participants in these designated payment systems to develop policies and procedures reasonably designed to identify and block or otherwise prevent “restricted transactions”, as that term is defined in Section __.2(r) of the proposal.

1. Definition of “Restricted Transactions” and “Unlawful Internet Gambling”¹

As stated above, the Proposed Regulation would require certain participants in designated payment systems (“Systems Participants”) to develop policies and procedures to block “restricted transactions”. A “restricted transaction” refers to a business’s acceptance of funds relating to “unlawful internet gambling”.

The Proposed Regulation does not define “unlawful internet gambling”. Rather, it states that a transaction is considered “unlawful” if it is “unlawful under any applicable Federal or State law...in which the bet or wager is initiated, received, or otherwise made.” As a result of this deficiency, there is no workable guideline as to when “unlawful internet gambling” activities constitute “restricted transactions” that would trigger the obligations of a Systems Participant under the proposed regulation.

The Agencies acknowledge this difficulty in determining what actions are unlawful. In explaining their reasons for not providing Systems Participants with a list of unlawful businesses, they state that they would have to

“ensure that the particular business was, in fact, engaged in the activities deemed to be unlawful... This would require significant

¹ Proposed Regulation, §§__6(r) and (t)

investigation and legal analysis. Such analysis could be complicated by the fact that the legality of a particular Internet gambling transaction might change depending on the location of the gambler at the time the transaction was initiated, and the location where the bet or wager was received. In addition, a business that engages in unlawful Internet gambling might also engage in lawful activities that are not prohibited by the Act. The government would need to provide an appropriate and reasonable process to avoid inflicting unjustified harm to lawful businesses by incorrectly including them on the list without adequate review. The high standards needed to establish and maintain such a list likely would make compiling such a list time-consuming and perhaps under-inclusive. To the extent that Internet gambling businesses can change the names they use to receive payments with relative ease and speed, such a list may be outdated quickly.”²

In articulating the difficulties involved in compiling a list of unlawful internet gambling businesses, the Agencies have put their finger on the reasons why Systems Participants cannot, given the current vague definition, determine how to comply with their obligations under the regulation. We need bright-line rules that can be applied to assist us in determining what activities are considered unlawful.

2. Lists

As discussed above, the Agencies have declined at present to prepare and issue lists which Systems Participants could use to prevent or block “restricted transactions.” The Agencies request comment as to whether Systems Participants believe that lists should be required.

We believe that the issuance of lists would be extremely helpful to Systems Participants. It would be very difficult for Systems Participants to determine when a transaction is unlawful without a list or other bright-line guidance from the Agencies. Since we already check against OFAC lists, we are familiar with the operations that are

² 72 Fed. Reg. at 56690, 56691.

required to implement and maintain government-provided lists and can combine our obligations to screen internet gambling businesses with our OFAC screenings with relative ease.

We acknowledge the difficulties in establishing and maintaining lists and the fact that they may become quickly outdated. Nevertheless, if the Agencies do not provide a list, we will probably be forced to prepare our own. We respectfully believe that the Agencies are in a much better position to establish lists and to monitor for events that would require changes to these lists, since this is currently done in the OFAC context. In addition, we believe that Agency lists would better protect lawful businesses than any list which we could prepare, since the Agencies would presumably follow the same process in establishing these lists as those that are followed for OFAC (i.e., by publishing notice to “covered” persons or entities and allowing them to challenge the designation.)³ Because a process would be followed to protect the interests of persons engaged in lawful activities, Systems Participants would be less likely to block legal transactions, and would consequently face less exposure to third party lawsuits. Adoption of a list approach would also allow for the simplification of the safe harbor - so long as Systems Participants blocked in good faith in reliance on the list, they would be protected if they blocked lawful transactions as well as unlawful ones.

Of course, even if lists were issued, due consideration should be taken to ensure that the screening obligation would fall on the appropriate person(s) in the payment system. For example, in the cards context, the obligation to screen against the list should fall on the merchant acquirer or cards payment system, and not on the card issuer.

3. Knowledge Standard

Section __.6 of the Proposed Regulation provides non-exclusive examples of policies and procedures that could be utilized to prevent restricted transactions. In general, a Systems Participant must implement those procedures if it “becomes aware” that a customer (or

³ See discussion in Supplementary Information, Fed. Reg. at 56692.

another systems participant) is processing a restricted transaction, or, for offshore transactions, if a foreign bank or other participant is “found to have” received unlawful payments or “found to have” otherwise engaged in restricted transactions.

We have significant concerns about these nebulous standards. Instead, we agree with the suggestion of another commenter that the standard in each case should be “actual knowledge”, where a Systems Participant is deemed to have such knowledge only when that fact is “brought to the attention of an individual in the organization who is responsible for the organization’s compliance function with respect to that transaction.”⁴ If transaction coding is determined to be the best method to detect “restricted transactions” in the card payment context, that payment system should be exempt from provisions requiring additional policies and procedures to monitor customer activity.

4. Safe Harbor provisions and “Overblocking”

As the Agencies point out, any policies and procedures developed by Systems Participants would probably prevent many lawful transactions as well as unlawful ones, given the difficulty in defining what is unlawful. Consequently, it is critical that Systems Participants be protected against third party actions from legitimate businesses that are blocked pursuant to the policies and procedures adopted by those participants to meet their obligations under the Act and regulation.

We note, and support, the “overblocking” provision in the Proposed Regulation⁵ and the Agencies’ discussion of this provision in the Supplementary Information⁶, which makes clear that the Safe Harbor in Section __.5(c)(3) is intended to protect any person that identifies and prevents a transaction pursuant to its own policies and procedures developed in accordance with the Proposed Regulation,

⁴ See comment letter dated December 12, 2007 submitted by the American Bankers Association.

⁵ Proposed Regulation, §_5(c)(3).

⁶ 72 Fed. Reg. at 56688.

even if that transaction is not illegal. This will allow System Participants to develop and implement policies and procedures that are flexible and workable so long as they are “reasonably designed to identify and block or otherwise prevent or prohibit restricted transactions”, even if they sometimes result in the prevention of legal transactions.

We note, however, that there is a difference between the Act and the Proposed Regulation in the wording of the Safe Harbor. The Act states that a person that identifies and blocks a transaction shall not be liable to a third party for such action if that person identifies and blocks a transaction “as a designated payment system or a member of a designated payment system in reliance on the policies and procedures of the payment system, in an effort to comply with the... regulations.”⁷

The language in the Proposed Regulation is different. It would offer protection against third party actions if a “person is a participant in the designated payment system and blocks or otherwise prevents the transaction in reliance on the policies and procedures of the designated payment system”, but does not specifically include persons who rely on their own policies and procedures in blocking a transaction. This appears to be inadvertent, since the Agencies state that they intended to cover both circumstances⁸. Nevertheless, since the distinction is critical, we suggest that the Agencies conform the language in Section __.5(c)(3) to the exact language used in the Act.

5. Offshore Transactions

In general, payment systems intermediaries are exempted from the regulation unless they participate in offshore ACH credit or debit transactions, wire transfers or check collection transactions. In these cases, the Proposed Regulation would require participants that are transacting with offshore correspondents to develop policies and

⁷ 31 USC §5364(d)(3).

⁸ See Agencies’ discussion referenced in Footnote 4.

procedures relating to transactions in which customers of those correspondents engage.⁹

These requirements again point to the difficulty in identifying internet gambling transactions and determining whether they are “unlawful”. But now they further complicate matters since they require that determination to be made not only with respect to the activities of one’s customer, but with respect to the activities of a customer of a third party.

The Proposed Regulation attempts to address this difficulty by providing that an ACH participant’s policies and procedures would be considered acceptable if, in the case of debit instructions originating offshore, they:

(i) Address methods for conducting due diligence in establishing or maintain the relationship with the foreign sender designed to ensure that the foreign sender will not send instructions to originate ACH debit transactions representing restricted transactions to the [U.S. recipient], such as including as a term in its agreement with the foreign sender requiring the foreign sender to have reasonably designed policies and procedures in place to ensure that the relationship will not be used to process restricted transactions; and

(ii) Include procedures to be followed with respect to a foreign sender that is found to have sent instructions to originate ACH debit transactions to the [recipient] that are restricted transactions, which may address-

(A) When ACH services to the foreign sender should be denied; and

(B) The circumstances under which the cross-border arrangements with the foreign sender should be terminated.¹⁰

Similar language is included in those provisions relating to offshore ACH credit transactions, wire transfers and check collection transactions.¹¹

⁹ Proposed Regulation, §§_.6(b)(2) and (3), _.6(d)(2) and _.6(f)(2)

¹⁰ Proposed Regulation, Section _.6(b)(2)

¹¹ Proposed Regulation, Section _.6(b)(3), _.6(d)(2) and _.6(f)(2)

We have a number of problems relating to these provisions of the Proposed Regulation. First, although we understand that the examples are non-exclusive¹², we do not believe that the examples are at all practicable, and thus provide little assistance to Systems Participants who are trying to determine how to comply with the regulation. We do not believe that our correspondents will easily agree to the inclusion of the suggested contract term in our agreements with them¹³, either because they have no stake in the issue or because they are concerned about their liability for blocking transactions that are legal in their home country. If they do not agree, the Proposed Regulation is unclear as to what our next steps should be. Although we could provide notice to our correspondents alerting them that we are required to block “restricted transactions”, this notice will not have much effect if we are unable to provide a definition of that term.

The question remains as to how a Systems Participant may satisfy its “due diligence” obligations in establishing or maintaining the relationship with the foreign correspondent, since it would be very difficult to monitor the operations of that correspondents vis-à-vis its customers, as the Supplementary Information suggests¹⁴. The Agencies themselves recognize that “a bank’s responsibility to have knowledge of its correspondent bank’s customers is a difficult one.”¹⁵ This is an additional conundrum which would be solved if the “list approach” is adopted.

Another possible solution would be for the Agencies to adhere more closely to their enunciated principal of “exempt[ing] all participants in the ACH systems, check collection systems, and wire transfer systems, except for the participant that possesses the customer relationship with the Internet gambling business.”¹⁶ We believe that, due to the practical difficulties of implementation in the offshore

¹² Proposed Regulation, Section __.6(a).

¹³ Indeed, in many cases we do not even have formal agreements with our payment system correspondents.

¹⁴ The Supplementary Information goes so far as to suggest that Systems Participants “audit” the operations of correspondent banks, which would be very difficult indeed. See Fed. Reg. at 56688, 56689

¹⁵ Fed. Reg. 56690.

¹⁶ Fed. Reg. at 56685

context, the Agencies should consider including in the regulation's general exemption ¹⁷ all intermediary systems participants in offshore transactions, except to the extent that any of these participants possess the customer relationship with the Internet gambling business.

6. Card Payment Systems

We believe that the card systems examples provided in Section __.6(c) of the Proposed Regulations should be modified to more closely reflect the parties to whom the stated obligations apply. For example, it appears that the requirements to monitor and test merchant websites, to test transactions for appropriate coding, and to analyze payment patterns should apply only to systems operators and not card issuers and merchant acquirers, although the Proposed Regulation as written would apply these obligations to all three. ¹⁸

In addition, we do not understand the reference in Section __.6(c)(3)(i) to the assessment of fines against merchant customers by card systems, card issuers or merchant acquirers, since fines are typically not levied in this manner. We are wondering whether this was intended to suggest that card systems should levy fines against merchant acquirers whose customers engage in illegal acceptance of internet bets and wagers, which fines would be passed on by merchant acquirers to those customers. We ask that this provision be deleted or clarified to provide further guidance.

7. Use of Term "Block"

We ask the Agencies to clarify that the term "block" as used in the regulation¹⁹ refers only to rejection of a transaction and return of any payment that a Systems Participant has received in connection with that transaction, and not to the "blocking" that is required by OFAC regulations, where the blocking party must cease processing a

¹⁷ Proposed Regulation, § __.4

¹⁸ Proposed Regulation, § __.6(c)(2)

¹⁹ Proposed Regulation, § __.5(a)

transaction AND deposit the proceeds of the transaction into an account not accessible by the customer.

8. Implementation Time

The Agencies have suggested that the final rule take effect six months after publication. We do not believe this will provide us with sufficient implementation time.

The Proposed Regulation currently requires payment systems participants to develop their own policies and procedures in some cases, and follow policies and procedures issued by payment systems of whom they are a member in other cases - for example, credit card associations, ACH networks, and check-clearing networks. This means that, in many cases, we will have to wait until multiple overarching payment systems issue their own rules before we can begin to develop our own procedures to comply with them.

Unless the coverage of the regulation is clarified – that is, unless the Agencies provide screening lists or additional guidance as to what constitutes an “unlawful Internet gambling transaction” - we expect that it will not be a simple task to develop policies and procedures to prevent such transactions. In addition, unless offshore transactions are exempted in the final rule, we will have to devise a means of communicating with our correspondent banks and determining measures we are required to take in those instances.

In light of these many complicating factors, and given the fact that the proposal will affect multiple payment systems across multiple businesses, preparing for the effectuation of this regulation will involve considerable time and effort. Consequently, we ask that the Agencies provide for a lead time of no less than 24 months from the final regulation’s publication date in the Federal Register.

We appreciate the opportunity to comment on the Proposed Regulation and hope that our comments are useful. If you have any questions relating to these comments or would like to discuss them in greater detail, please call me at (212) 559-2938 or Joyce Elkhateeb of my office at (212) 559-9342.

Sincerely,

A handwritten signature in black ink, appearing to read "Carl V. Howard". The signature is written in a cursive style with a large initial "C" and a stylized "H".

Carl V. Howard
General Counsel – Bank Regulatory