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September 3, 2008

Louise L. Roseman
Director,
Reserve Bank Operations and
Payment Systems Division
Federal Reserve System
Room 4134
20th & C Streets, N.W.
Washington, DC 20551

Re: Burden of Proposed Internet Gambling
(UIGEA) Regulations on Financial Institutions

Dear Ms. Roseman:

As detailed in the attachment, the proposed UIGEA regulations would place extensive new mandates on all U.S. financial institutions with the burden falling particularly heavily on small banks and thrifts. The result of these new economic and management burdens would be to further hammer the stability of the financial system, disrupt international payment flows and harm the global competitiveness of U.S. banks.

The Small Business Administration has already informed the Federal Reserve and Treasury Department that the agencies "...have not analyzed properly the full economic impact of the proposal on small entities as required by the Regulatory Flexibility Act (RFA)" and recommended that the agencies "prepare and publish for public comment a revised IRFA [Initial Regulatory Flexibility Analysis] to determine the full economic impact on small entities... and consider significant alternatives to meet its objective while minimizing the impact on small entities before going forward with the final rule."

Consistent with the Federal Reserve's mission of "supervising and regulating financial institutions," we request that you advise the Treasury Department and the Office of Management and Budget of the need for the agencies conduct and publish for stakeholder comment a revised IRFA small business impact analysis "before going forward with the final rule."

Sincerely,

Jim Tozzi, Ph. D
Member, Board of Advisors

UIGEA Recordkeeping Requirements

▶ Automated Clearing House (ACH) Systems

- Due Diligence: Domestic. Develop due diligence procedures to prevent origination and/or receipt of “restricted” transactions. Examples of such procedures include:
 - Screening potential commercial customers to ascertain the nature of their business; and
 - Including as a term in commercial customer agreements a prohibition on restricted transactions, which requires legal research to define the term appropriately for firms based in various states and tribal areas.
- Sanctions Against Customers Believed to be Engaging in Restricted Transactions. Develop procedures specifying actions to be taken against customers believed to have originated or received a restricted transaction. Examples of acceptable sanction procedures include determining:
 - When fines should be imposed;
 - When the customer should not be allowed to originate ACH debit transactions; and
 - The circumstances under which the account should be closed.
- Due Diligence: Foreign-Originated ACH Debit Transaction. Develop due diligence procedures to prevent a foreign sender (non-US banks, third-party payments processors) from originating an ACH debit transaction. An example of acceptable due diligence is:
 - Including in agreements with foreign senders a requirement that the foreign bank and/or other overseas payment processors “have reasonably designed policies and procedures in place to ensure that the relationship will not be used to process restricted transactions.”
- Sanctions Against Foreign Banks Originating a Restricted Debit Transaction. Develop procedures specifying actions to be taken against foreign senders believed to have originated a restricted ACH debit transaction. Examples of acceptable sanction procedures include determining:
 - When ACH services to the foreign sender should be denied; and
 - The circumstances under which the cross-border arrangements with the foreign sender should be terminated.

- Preventing ACH Credit Transactions to Foreign Institutions. Develop policies and procedures to prevent crediting a foreign bank for a restricted transaction. The policies should address:
 - When ACH credit transactions for the foreign bank or through the foreign gateway operator should be denied; and
 - The circumstances under which the cross-border arrangements with the foreign bank should be terminated.

▶ **Card Systems**

- Due Diligence. Card system operators and banks are to develop policies and procedures in establishing or maintaining a merchant relationship designed to ensure that the merchant will not receive restricted transactions through the card system. Examples of such policies include:
 - Screening potential merchant customers to ascertain the nature of their business; and
 - Including as a term of the merchant customer agreement that the merchant may not receive restricted transactions through the card system which requires which requires legal research to define the term appropriately for customers based in various states and tribal areas.
- Identifying and Blocking Restricted Transactions. Develop procedures to identify and block restricted transactions. An example of an acceptable procedure is:
 - Establishing transaction codes and merchant/business category codes that are required to accompany the authorization request for a transaction and creating the operational functionality to enable the card system or the card issuer to identify and deny authorization for a restricted transaction.
- Monitoring/Testing Procedures. Develop procedures for ongoing monitoring and/or testing to detect potential restricted transactions. Examples of acceptable procedures include:
 - Conducting testing to ascertain whether transaction authorization requests are coded correctly;
 - Monitoring of web sites to detect unauthorized use of the relevant card system, including its trademark; and

- Monitoring and analyzing payment patterns to detect suspicious payment volumes from a merchant customer.
- Sanctions Against Merchant Customers. Develop procedures specifying actions to be taken against merchant customers by card systems and/or issuing banks if they become aware that the merchant has received restricted transactions. Examples of such procedures include determining:
 - When fines should be imposed; and
 - When access to the card system should be denied.

▶ **Check Systems/Banks**

- Due Diligence: Domestic. Banks are to develop due diligence procedures in establishing and/or maintaining a customer relationship to prevent the customer from receiving restricted transactions. Examples of such procedures include:
 - Screening potential commercial customers to ascertain the nature of their business; and
 - Including as a term of the commercial customer agreement that the customer may not deposit checks that constitute restricted transactions.
- Sanctions Against Customers. Develop procedures specifying actions to be taken against customers depositing checks that constitute a restricted transaction. Examples of such procedures include determining:
 - When checks for deposit should be refused; and
 - The circumstances under which the account should be closed.
- Due Diligence: Foreign Banks. Banks are to develop due diligence procedures in establishing and/or maintaining a correspondent relations with foreign banks to prevent the foreign institutions from sending checks which are part of a restricted transaction to the domestic depository institution for collection. An acceptable example of such a procedure is:
 - Negotiating with foreign banks to include as a term in agreements with them the requirement that the foreign bank have reasonably designed policies and procedures in place to ensure that the correspondent relationship will not be used to process restricted transactions.

- Sanctions Against Foreign Banks. Develop procedures specifying actions to be taken against foreign banks found to have sent checks to the domestic institution for collection. Examples of such sanctions include determining:
 - When check collection services for the foreign bank should be denied; and
 - The circumstances under which the correspondent account should be closed.

▶ **Money Transmitting Businesses**

- Due Diligence. Money transmitting businesses are to develop due diligence procedures in establishing and/or maintaining commercial subscriber relationships to ensure that they will not receive restricted transactions using such techniques as:
 - Screening potential commercial subscribers to ascertain the nature of their business; and
 - Including as a term of the commercial subscriber agreement that the subscriber may not receive restricted transactions.
- Monitoring/Testing Procedures. Develop procedures for ongoing monitoring and/or testing to detect potential restricted transactions such as
 - Monitoring and analyzing payment patterns to detect suspicious payment volumes to any recipient; or
 - Monitoring web sites to detect unauthorized use of the relevant money transmitting business, including their trademarks.
- Sanctions Against Fund Recipients. Develop procedures specifying actions to be taken against recipients of restricted transactions. Examples of such sanctions include determining:
 - When fines should be imposed;
 - When access should be denied; and
 - The circumstances under which an account should be closed.

▶ **Wire Transfer Systems**

- Due Diligence. The beneficiary bank of a wire transfer are to develop due diligence procedures in establishing and/or maintaining commercial customer relationship to

ensure that the customer does not receive restricted transactions using such techniques as:

- Screening potential commercial subscribers to ascertain the nature of their business; and
 - Including as a term of the commercial customer agreement a prohibition against the customer receiving restricted transactions which requires legal research to define the term appropriately for firms based in various states and tribal areas.
- Sanctions Against Commercial Customers. Develop procedures specifying actions to be taken against commercial customers receiving restricted transactions. Examples of such sanctions include determining:
 - When access to the wire transfer system should be denied; and
 - The circumstances under which an account should be closed.
 - Preventing Restricted Foreign Transactions. A bank sending/crediting funds to a foreign bank shall have procedures to identify and block restricted transactions. These procedures shall include sanctions against foreign banks such as determining:
 - When wire transfer services for the foreign bank should be denied; and
 - The circumstances under which the correspondent account should be closed.