



The Blockchain Association
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27 November 2020

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue N.W.
Washington, D.C. 20551

Policy Division
Financial Crimes Enforcement Network
P.O. Box 39
Vienna, VA 22138

Re: Federal Reserve Docket No. R-1726; RIN 7100-AF97
FinCEN Docket No. FINCEN-2020-0002; RIN 1506-AB41

To whom it may concern:

The Blockchain Association¹ (“Association”) appreciates the opportunity to respond to the Board of Governors of the Federal Reserve System (“Board”) and the Financial Crimes Enforcement Network’s (“FinCEN”) (collectively, the “Agencies”) joint notice of proposed rulemaking entitled “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers and Transmittals of Funds That Begin or End Outside of the United States, and Clarification of the Requirement To Collect, Retain, and Transmit Information on Transactions Involving Convertible Virtual Currencies and Digital Assets With Legal Tender Status” (“NPRM”).²

¹ The Blockchain Association is a 501(c)(6) trade association based in the United States working to improve the public policy environment so that blockchain networks and cryptocurrencies can thrive.

² “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers and Transmittals of Funds That Begin or End Outside of the United States, and Clarification of the Requirement To Collect, Retain, and Transmit Information on Transactions Involving Convertible Virtual Currencies and Digital Assets With Legal Tender Status,” *Joint Notice of Proposed Rulemaking*, Board of Governors of the Federal Reserve System and the Financial Crimes Enforcement Network, October 27, 2020, 85 FR 68005, 68005-68019,

The Agencies should reconsider this NPRM, the adoption of which would place a substantial burden on regulated financial institutions—especially virtual asset service providers (“VASPs”) and smaller firms—while undermining individual users’ privacy. The Agencies have not provided sufficient evidence that adopting the proposed changes would materially benefit anti-money laundering or combatting the financing of terrorism enforcement relative to the significant costs it would impose on the public. Therefore, the Association respectfully recommends that the Agencies reissue this NPRM and consider proposing a threshold for compliance that conforms to the Financial Action Task Force’s (“FATF”) recommendation of 1,000USD/EUR.

Issues Specific to Virtual Asset Service Providers

Money services businesses are required by the Agencies to comply with two rules regarding their transmission of funds. The first rule, the Record Keeping Rule, “requires banks and nonbank financial institutions to collect and retain information related to funds transfers and transmittals of funds in amounts of \$3,000 or more,”³ while the second rule, the Travel Rule, “requires banks and nonbank financial institutions to transmit information on certain funds transfers and transmittals of funds to other banks or nonbank financial institutions participating in the transfer or transmittal.”⁴ The Agencies propose to reduce this threshold to \$250, a 95% reduction in real terms,⁵ for international transactions while keeping unchanged the threshold for domestic transactions at \$3,000, creating a discrepancy in the treatment of certain transactions based on the location of counterparty financial institutions. Cryptocurrency businesses considered money services businesses (VASPs) will be required to comply with the two rules that the Agencies propose to change.

With current compliance solutions, VASPs are unable to determine the location of counterparty VASPs, which means that for transactions involving cryptocurrencies, the proposed threshold reductions for international transactions would leave VASPs with two

<https://www.federalregister.gov/documents/2020/10/27/2020-23756/threshold-for-the-requirement-to-collect-retain-and-transmit-information-on-funds-transfers-and>.

³ “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers,” 68006.

⁴ “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers,” 68007.

⁵ The Travel Rule and Recordkeeping Rule thresholds were first set in January 1995. Chained to inflation, \$3,000 in 1995 has the purchasing power of about \$5,197 in October 2020. “CPI Inflation Calculator,” U.S. Bureau of Labor Statistics, accessed November 26, 2020, https://www.bls.gov/data/inflation_calculator.htm.

options: (1) treat all transactions as if they have a foreign leg and therefore consider all transactions \geq \$250 to be subject to the Rules, which would create a de facto threshold of \$250 for all transactions, or (2) for originating VASPs based in the United States that, in the normal course of business, only collect the transmitter’s information and the destination address to effect transactions, assume that no transactions have a foreign leg and only transactions \geq \$3,000 are subject to the Rules. Neither option is ideal. While the second option forces VASPs into a regulatory gray area, a de facto threshold of \$250 for all transactions, the first option, significantly increases not only the regulatory burden for cryptocurrency businesses relative to other industries but also the harm to the public by further expanding the financial surveillance “dragnet” beyond the written text of the Rules.

To quantify the additional burden to VASPs that the proposed threshold reductions would bring, some of the Association’s VASP members analyzed on-chain transactions between May 1, 2020 and October 31, 2020 that would be subject to the Rules at the various thresholds cited in the NPRM. Because VASPs do not have the ability to determine the location of counterparty VASPs, the percentages provided in the table below represent the percentage increase in on-chain transactions—regardless of counterparty location—that would be subject to the Rules over the existing threshold of \$3,000.

Percentage Increase in On-Chain Transactions Captured by Threshold

Threshold	\$3,000	\$1,000	\$500	\$250	\$0
VASP #1	-	180%	242%	312%	557%
VASP #2	-	112%	117%	120%	147%
VASP #3	-	150%	-	250%	-

In addition to on-chain cryptocurrency transactions being considered money transmission for the purposes of the Rules, FinCEN has previously found that credit card transactions that settle in cryptocurrency are also considered to be money transmission.⁶ Transactions conducted by card networks and other card processors that settle in fiat currency, on the other hand, are excluded from the definition of money transmission, meaning that they are not responsible for compliance with the Rules. In payments

⁶ “Request for Administrative Ruling on the Application of FinCEN’s Regulations to a Virtual Currency Payment System,” the Financial Crimes Enforcement Network, October 27, 2014, https://www.fincen.gov/sites/default/files/administrative_ruling/FIN-2014-R012.pdf.

processing, both the card issuer and the acquirer are regulated institutions that operate an account-based model. As such, the transmitter and recipient are subject to know your customer (KYC) requirements by default, in addition to the payment being in exchange for a specific good or service.

The proposed change to the Rules' thresholds would result in VASPs that process credit card transactions on behalf of their customers, who are merchants, having to identify the cardholder for a point of sale transaction. This requirement would be extremely burdensome for the processor, which has no relationship with the cardholder. For example, if an individual wished to purchase a phone for \$255.00 at a merchant that has elected to settle their transactions in cryptocurrency, the individual, in order to purchase the phone, would have to provide their personally identifiable information (PII), including social security number (SSN), to the merchant in order to enable compliance with the lowered reporting thresholds. Even though the individual is blind to the fact that the merchant elected to settle their transactions in cryptocurrency, they will still have to share a significant amount of personal information with the merchant in order to engage in a transaction. Had the merchant elected to use a fiat-based settlement provider, however, none of these burdens would be borne.

The fact that these transactions are considered money transmission, while the same transactions settled in fiat are not, places VASPs at a disadvantage compared to other credit card processors because of the underlying technology they use. The threshold reductions would create a monumental burden for these VASPs. One member VASP's analysis of their credit card processing transactions suggests that a reduction in the threshold to \$250 will result in an increase in the number of transactions subject to the Rules of 82,500% (3,200% increase at \$1,000; 16,189% at \$500; 1,787,878% at \$0), with the number of unique transmitters requiring KYC increasing by 73,000% (3,017% increase at \$1,000; 13,117% at \$500; 1,213,683% at \$0). Even if the requirement to collect SSN was removed in a future version of the Travel Rule, as is contemplated by the NPRM, the burden of collecting the other information about a cardholder, and then collecting a copy of the cardholder's ID to verify the same, would be enormous.

The vast increase in the volume of transactions captured—on-chain as well as with credit cards—would also bring significant downstream compliance burdens for VASPs. The additional volume would increase the cost of application programming interface (API) calls to Travel Rule compliance solutions and end-point connections. In addition, when VASPs collect and/or receive additional information regarding the wallet address clients are sending and/or receiving funds to/from, they will be responsible for additional

screenings (e.g. Office of Foreign Asset Control (OFAC) sanctions, politically exposed person (PEP), negative news, determination of the purpose and relationship of the transactions for anti-money laundering (AML) review, etc.) that significantly aggravate the compliance costs of the proposed threshold reductions. These additional compliance costs will come in the form of vendor costs and person-hours needed to not only manage the additional collection volume but also screen resulting alerts.

The additional volume of transactions subject to the Rules would not only increase direct compliance costs but also decrease efficiency and expediency, resulting in additional customer friction. Because cryptocurrency networks operate 24/7, VASPs will be forced to either have 24/7 compliance coverage or risk customers having funds frozen until regular business hours, which will negatively affect the viability of VASP-to-VASP cryptocurrency transactions and increase customer friction. In this manner, the threshold reductions will again prove particularly burdensome for VASPs relative to other financial institutions.

General Considerations

The Association is also concerned that the Agencies' cost-benefit assessment failed to consider the interests of an important constituency—the American public and the users of the United States financial system—and encourages the Agencies to consider the cost that the proposed rule, if adopted, would inflict on individuals and society. Compliance costs are invariably borne by consumers. While such costs can be direct, indirect, or difficult to quantify, they must be considered. For example:

- The significant increase in the volume of transactions that would be captured means that regulated entities would be required to store significantly more PII, including the PII of individuals with whom the financial institutions have no direct relationship.
- The Agencies state that the intent of the NPRM is to lower “...the threshold to capture smaller-value cross-border funds transfers and transmittals of funds...,”⁷ in other words, remittances. Indeed, the proposed reductions will have a particular effect on the cost of remittances, which are already among the most expensive financial transactions. According to the United Nations, the average remittance transaction ranges from \$200-\$300,⁸ and the average cost of sending a

⁷ “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers,” 68008.

⁸ “Remittances matter: 8 facts you don’t know about the money migrants send back home,” United Nations Department of Economic and Social Affairs, June 17, 2019, <https://www.un.org/development/desa/en/news/population/remittances-matter.html>.

remittance from the United States in Q3 2020 was 5.14%.⁹ In the words of the Bank of International Settlements, “payments across borders are not only typically slow and opaque, but also especially costly. Lower-value payments, such as remittances, are the prime example.”¹⁰ The proposed threshold reductions would aggravate this situation by increasing the compliance costs of the firms that facilitate these transactions. These increased compliance costs will inevitably fall on the senders, reducing even further the amount that is actually received by individuals who often need these funds to sustain basic household costs.

- Lowering the threshold to \$250 would also stifle competition. While larger, more established companies will be able to bear the compliance costs associated with these changes, smaller financial institutions and new entrants may struggle. As such, the proposed reductions will further entrench regulatory moats in the financial system and act as an additional barrier-to-entry for start-ups. Moreover, reducing the thresholds to \$250 would create a more restrictive regime in the United States than is the international standard, harming the general competitiveness of the U.S. economy and market. The Financial Action Task Force suggests a threshold for compliance of 1,000USD/EUR.¹¹

While the Agencies’ proposed changes would impose costs on stakeholders beyond only “financial institutions and the payments system,”¹² the proposed threshold reductions also appear contrary to FinCEN’s current efforts “to modernize the national AML regime.”¹³ In September 2020, FinCEN released an advanced notice of proposed rulemaking (ANPRM) seeking “public comment on potential regulatory amendments to establish that all covered financial institutions subject to an anti-money laundering program requirement must maintain an ‘effective and reasonably designed’ anti-money laundering program.”¹⁴

⁹ “Remittance Prices Worldwide,” The World Bank, Issue 35, September 2020, https://remittanceprices.worldbank.org/sites/default/files/rpw_report_september_2020.pdf.

¹⁰ “Annual Economic Report 2020,” Bank of International Settlements, June 2020, 72, <https://www.bis.org/publ/arpdf/ar2020e.htm>.

¹¹ “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers,” 68009.

¹² Ibid.

¹³ “Anti-Money Laundering Program Effectiveness,” *Advanced Notice of Proposed Rulemaking*, the Financial Crimes Enforcement Network, September 17, 2020, 85 FR 58023, <https://www.federalregister.gov/documents/2020/09/17/2020-20527/anti-money-laundering-program-effectiveness>.

¹⁴ “Anti-Money Laundering Program Effectiveness,” 58023.

This subsequently issued NPRM ultimately belies the goals of the September ANPRM. Indeed, part of FinCEN’s analysis in the NPRM relies on (a relatively limited sample size of) “2,000 SARs filed by money transmitters between 2016 and 2019 related to *potential* terrorist financing related transmittals of funds. These SARs referenced approximately *1.29 million underlying transmittals of funds...*”¹⁵ [emphases added]. Measuring the effectiveness of these disclosures is difficult given that FinCEN’s analysis did not state whether the SARs in question led to the identification of *actual* terrorist financing. As such, FinCEN has not adequately explained how expanding the financial surveillance “dragnet” by reducing the thresholds in question to capture millions of additional smaller-value cross-border transfers and transmittals creates an “‘effective and reasonably designed’ anti-money laundering program.”¹⁶ Moreover, dramatically expanding the collection of individuals’ financial data does not “place greater emphasis on providing information with a high degree of usefulness to government authorities,”¹⁷ does not modernize or streamline “AML monitoring and reporting practices... to maximize efficiency, quality, and speed of providing data to government authorities,”¹⁸ and does not provide “due consideration for privacy and data security”¹⁹ trade-offs associated with the reductions, all goals delineated in the September 2020 ANPRM.

Finally, the Association requests that the Agencies provide an additional comment period to allow both respondents and the Agencies themselves the opportunity to more thoroughly assess the costs and benefits of the changes proposed by the NPRM.

¹⁵ “Threshold for the Requirement To Collect, Retain, and Transmit Information on Funds Transfers,” 68008.

¹⁶ “Anti-Money Laundering Program Effectiveness,” 58023.

¹⁷ “Anti-Money Laundering Program Effectiveness,” 58025.

¹⁸ Ibid.

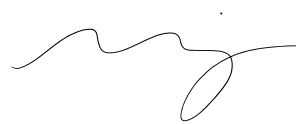
¹⁹ Ibid.

In sum, adopting the proposed rule in its current form would significantly increase the compliance burden of regulated financial institutions (particularly VASPs). Moreover, the NPRM fails to consider the significant costs to stakeholders beyond regulated entities and the payments system and runs contrary to FinCEN's wider efforts to modernize the national AML regime. We encourage the Agencies to reissue this proposal with a more complete cost benefit analysis and a threshold that is consistent with the FATF's recommended threshold for compliance of 1,000USD/EUR.

Sincerely,

A handwritten signature in cursive script, appearing to read "Kristin Smith".

Kristin Smith

A handwritten signature in cursive script, appearing to read "Miller Whitehouse-Levine".

Miller Whitehouse-Levine