



27 November 2020

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VIA EMAIL: regs.comments@federalreserve.gov

Comment on Proposed Rule under Bank Secrecy Act

Docket No. FINCEN-2020-0002
RIN 1506-AB41

To whom it may concern,

Global Digital Finance supports efforts by global standard setters, national authorities and regulators to consult and work with the nascent global digital / virtual asset industry.

To that end, we are hereby providing comment to the Joint Notice of Proposed Rulemaking [JNPR] to amend the Travel Rule threshold for funds transfer that begin or end outside the United States .

The input has been drafted and led by the GDF Anti-Money Laundering Working Group. Contributors who wish to be named are listed at the end of this document.

About GDF

Global Digital Finance (“GDF”) is a not-for-profit industry body that promotes the adoption of best practices for crypto and digital assets, and digital finance technologies through the development of conduct standards, in a shared engagement forum with market participants, policymakers and regulators.

Established in 2018, GDF has convened a broad range of industry participants, with 300+ global community members—including some of the most influential digital asset and token companies, academics and professional services firms supporting the industry. GDF is proud to include 100x Group, Coinbase, Diginex, DLA Piper, Ernst & Young, Hogan Lovells, Huobi, R3 and SIX Digital Exchange as patron members.

The GDF Code of Conduct is an industry-led initiative driving the creation of global best practices and sound governance policies, informed by close conversations with regulators and developed through open, inclusive working groups of industry participants, legal, regulatory and compliance experts, financial services incumbents

and academia. Code principles undergo multiple stages of community peer review and open public consultation prior to ratification.

Comments on the Proposed Rule

1. Lowering the Travel Rule threshold will negatively impact financial inclusion.

When assessing the costs of a proposed rule, we argue that the potential negative consequences (including those unintended) costs should be considered, especially the impact on engagement of financially underserved, de-risked and/or excluded parties (including individuals, households, businesses and other organizations).

Financial exclusion and de-risking practices have disproportionately impacted certain segments of the economy with profound consequences to the ability to ensure one's own financial stability and economic security. De-risking due to ever-increasing AML/CFT requirements have been particularly harmful to cross-border remittances, a noted lifeline of hundreds of millions of people along numerous corridors whose livelihoods and economic wherewithal depend on these flows. Indeed, cross-border remittances to low- and middle-income countries eclipsed \$500B in 2019¹ and constitute 3-4 times official development assistance. In certain countries, remittances account for a significant portion of their growth (GDP).

The proposed rule change will increase the record-keeping burden for financial institutions and money services businesses that serve low-income individuals who tend to transfer amounts in a range between the proposed and current thresholds.² This will impact millions who would find it increasingly difficult to comply with customer information provisions and the related record-keeping provisions attendant to the Travel Rule and increase the burden and friction faced by individuals reliant on safe, secure and formal remittance channels.

The potential negative impact of the proposed rule on the convertible virtual currency (CVC) sector is of particular concern. CVCs present a transformative opportunity to expand financial inclusion by providing a viable alternative to payment products and services that are currently inaccessible or unreasonably costly to access for large segments of society. Indeed remittances (and international payments more broadly) are increasingly being facilitated via these channels given the cost and time efficiencies afforded to many who are challenged to do so through traditional money services business / money transfer operator (MSB/MTO), existing banking/payment rails and alternative fiat-based payments channels. An example of this is the ability to make remote payments, which has traditionally required use of a payment card, which may be difficult to access or, in the case of prepaid cards, be unreasonably costly or pose additional security or fraud concerns. Remote payment using CVCs represents a viable alternative for individuals to make payments (and, indeed, for individuals or small businesses to receive payment) globally.

¹ <https://www.worldbank.org/en/topic/labormarkets/brief/migration-and-remittances>

² Average migrant remittances are between \$200-\$300 per transaction; <https://news.un.org/en/story/2019/06/1040581>

2. Lowering the Travel Rule threshold could be counter-productive

In addition to the negative social impact of reduced financial inclusion, there is a risk that affected individuals will seek out alternative, unregulated remittance channels, thus bolstering the viability of unregulated money services businesses and decreasing the transparency of remittances and payments made at low value thresholds, which would ultimately reduce the overall effectiveness of the AML/CFT regime.

FATF highlighted this risk in their November 2017 guidance:

The application of measures that enable more individuals and businesses, especially low-income, unserved and underserved groups, to access and use regulated financial services increases the reach and the effectiveness of anti-money laundering/countering the financing of terrorism (AML/CFT) regimes. [...] Enabling these groups of people to use regulated and supervised channels [...] expands the scope of traceable transactions, facilitating the detection, reporting and investigation of suspicious transactions, thereby reducing overall money laundering (ML) and terrorist financing (TF) risks. Financial inclusion and financial integrity are thus mutually reinforcing.³

AML/CFT regulation should be evaluated for its effectiveness in accomplishing the twin aims of financial inclusion and protecting system integrity. Given the de-risking by traditional financial institutions of certain communities and activities stemming from growing AML/CFT obligations and the perceptions of compliance-related risks, it is no longer sufficient to be technically compliant with AML/CFT regulation. An effective AML/CFT regime should extend its scope to encompass those who are financially underserved or excluded from the traditional financial sector. In short, effective programs should reflect the engagement of a greater number of legitimate actors, in addition to deterring and detecting illicit actors.

Indeed, global standards and evaluations have already moved in this direction. In 2013, the Financial Action Task Force (FATF) acknowledged that “reasonable legal frameworks” to prevent financial crime were no longer sufficient. FATF stated that “each country must enforce these measures, and ensure that the operational, law enforcement and legal components of an AML/CFT system work together effectively to deliver results: the 11 immediate outcomes.”⁴ This resulted in the FATF amending its mutual evaluation process of member states.⁵

Related to record-keeping, the BSA does stress effectiveness and recent FinCEN guidance and ANPRM indeed requests sector guidance on how to evaluate and

³ <http://www.fatf-gafi.org/media/fatf/content/images/Updated-2017-FATF-2013-Guidance.pdf>

⁴ <https://www.fatf-gafi.org/publications/mutualevaluations/documents/effectiveness.html>

⁵ The Wolfsberg Group recently reinforced the importance of effectiveness, referencing the benefit to inclusion efforts:

https://www.wolfsberg-principles.com/sites/default/files/wb/pdfs/Effectiveness%201%20pager%20Wolfsberg%20Group%202019%20FINAL_Publication.pdf

determine what may constitute a 'reasonable and effective AML regime'.⁶ In this context, it is unclear that lowering the threshold as proposed is consistent with a view to effectiveness. FinCEN believes that the proposed regulatory approach furthers the statutory BSA purpose of providing information with a high degree of usefulness to government authorities. The change in the threshold seems to do the opposite.

Financial inclusion outcomes should be explicitly evaluated alongside those technical aspects related to the legal framework, system operations, and enforcement mechanisms of an FCC regime in assessing effectiveness.

3. Lowering the Travel Rule Threshold will Increase Compliance Costs

The proposed rule change will inevitably lead to an increase in compliance costs for affected businesses. In particular, the obligation imposed by the Travel Rule to verify that the sender information is correct, seems likely to result in a significant increase in the proportion of customers that money services businesses will be required to introduce. The resultant increase in costs could cause some money services businesses to cease offering cross-border remittances, reducing competition and potentially further raising the barriers for consumers to access these services, and driving more consumers towards unregulated remittance channels.

According to analysis published by blockchain analytics firm Ciphertrace⁷, lowering the Travel Rule threshold to \$250 will drastically increase (by at least 250%) the number of CVC transactions that are subject to the Travel Rule, potentially triggering more than one million compliance events.

⁶ Note FinCEN is seeking comment on Enhancing the Effectiveness of Anti-Money Laundering Programs, Sept. 16, 2020, at: <https://www.fincen.gov/news/news-releases/fincen-seeks-comments-enhancing-effectiveness-anti-money-laundering-programs>.

⁷ "FinCEN's Proposed Rule Change for Travel Rule Threshold Would More Than Double Compliance Events at US VASPs", 13 November 2020: <https://ciphertrace.com/fincens-proposed-rule-change-for-travel-rule-would-trigger-more-than-double-the-compliance-events-at-us-vasps/>

Number of Travel Rule Messages Required by U.S. VASPs
Monthly Transactions

Region	Txs Over 250	Txs Over 1000	Txs Over 3000	Current 3000	Proposed Change
US Domestic	15,921	11,016	7,510	7,510	7,510
Cross US Border	79,011	46,780	27,295	27,295	79,011
International	392,952	260,439	178,664		
Global	487,884	318,235	213,469		
Monthly Travel Rule Correspondences	-	-	-	34,805	86,521
Annual Travel Rule Correspondences	-	-	-	417,660	1,038,252

Additionally, there are a number of CVC business models (e.g. a VASP processing CVC payments for merchants) where the typical transaction value is below \$3,000 and, therefore, do not trigger the Travel Rule requirements. Reducing the threshold will result in a steep change in the cost of compliance incurred by these VASPs, likely changing the economics of such business models.

Given that we are still in the “sunrise” phase of Travel Rule compliance, it is not yet clear what the costs will be to the CVC sector of complying with the Travel Rule, so it is not possible to quantify the increase in costs that would result from the proposed reduction of the threshold.

It is important to note that the technology infrastructure and operational attributes supporting VASP activities can allow for consistent and even more robust recordkeeping and KYC processes especially when compared with traditional financial institutions. However, in evaluating the impacts of lowering the proposed threshold related to the travel rule, these operational attributes must be taken into consideration, and the 30 day comment period afforded in the JNPR does not provide sufficient time to calculate the operational and commercial costs that would impact individual VASPs or the broader CVC sector.

Such impacts may require significant changes by VASPs related to personnel and technology operations, customer engagement practices, such as onboarding of customers, collection and verification of information related to know-your-customer (KYC), Customer Identification Programs (CIP), sanctions and relevant watchlist screening (including filters for potential false positives and related remediation), monitoring and reporting. These costs do not include potential customer-related costs that may be incurred to address customer service inquiries, potential pauses in service as compliance-related elements above are addressed and potential holds on

customer transactions to address such concerns, which also relate to inclusion related impacts noted above. Industry feedback should include sufficient time for such an evaluation to understand the overall cost and operational implications before the threshold is adjusted and made mandatory for compliance.

4. There is a Lack of Rigorous Cost Benefit Analysis, particularly in relation to Virtual Currencies

The JNPR states that “the Agencies believe that lowering the threshold to capture smaller-value cross-border funds transfers and transmittals of funds would be valuable for law enforcement and national security authorities” and that the “benefits from the proposed rule include enhanced law enforcement ability to investigate, prosecute and disrupt the financing of international terrorism and other priority transnational security threats, as well as other types of transnational financial crime.”

However, it appears that the data analysis performed by the Agencies relates solely to transfers and transmittals of funds other than virtual currencies and failed to consider any data specific to virtual currencies. The Agencies appear to assume, without specific evidence-based justification, that adjustment to the threshold for virtual currencies should move in lockstep with the thresholds applicable to fiat-related funds transfers and traditional payment rails. The Agencies however have been active participants in international efforts through FATF to apply the Travel Rule to virtual currencies. Guidance establishing this application was adopted in 2019 and has only just begun to be implemented in the U.S. and internationally. There has not been sufficient time, or data, to establish whether the standard adopted in 2019 is effective or not. The proposal would thus increase burdens without adequate demonstration of benefits.

Moreover, there is a notable absence of quantitative analysis of these benefits. The Agencies cite an example of a 0.29 percent reduction in the annual probability of a major terrorist attack with an economic impact of \$30 billion but this example appears to be purely hypothetical, rather than based on estimates of the likely benefit of the proposed rule.

We argue that a rigorous cost benefit analysis of the proposed rule should include a quantitative analysis of the likely benefits. For example, it should be possible to estimate (a) the total amount of terrorist funding that currently flows across the US border, (b) the proportion that the Agencies expect will be detected and/or prevented as a result of lowering the Travel Rule threshold, and (c) how this compares with the total amount of terrorist funding globally, and, therefore, what the likely impact will be on terrorism. A similar methodology could be employed to analyze the likely benefits to preventing money laundering, narcotics trafficking and other illicit activity. This quantitative analysis could also be applied specifically to virtual currencies to demonstrate how the proposed adjustment should take place in lockstep.

Such benefits must be weighed against the likely costs. The JNPR includes estimates of the costs of compliance with the proposed rules. However, as noted in section

VI.A, the estimates do not include information technology implementation costs. This is an important omission in respect of the costs to the CVC sector, particularly as the hourly cost of such activity exceeds the \$24 used by FinCEN to estimate the labor cost of the requirements imposed by the proposed rule.

Additionally, it appears that the burden estimates included in the JNPR do not take into account the burden that will result from the need to conduct identity verification on a greater number of customers. We believe that guidance on appropriate verification procedures for lower-value transactions is a prerequisite for such estimates.

Conclusion

We propose that implementation of the proposed rule be suspended until a full cost benefit analysis can be undertaken, taking into account the likely impact on financial inclusion as well as the consequences thereof, and a more comprehensive estimate of the costs of complying with the proposed rule.

Consultation Response Contributors

The following table lists contributors to this response who wish to be identified. The full list of contributions from the GDF AML/CFT Working Group may be larger.

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Carol Van Cleef	Luminous Group
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David Carlisle	Elliptic

Yours faithfully,

The GDF Board and GDF AML Working Group