



Federal Deposit Insurance Corporation

550 17th Street NW, Washington, D.C. 20429-9990

Division of Risk Management Supervision

August 3, 2018

TO: Board of Directors

FROM: Doreen R. Eberley
Director

SUBJECT: Customer Identification Program Rule Exemption for
Insurance Premium Financing

EXECUTIVE SUMMARY

A consortium of banks requested the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (FRB), and the National Credit Union Administration (NCUA), (collectively, the “FBAs”) and the Financial Crimes Enforcement Network (FinCEN) to grant an exemption from the requirements of the jointly-issued *Customer Identification Program* (CIP) rule for loans extended by banks and their subsidiaries to commercial customers to facilitate purchases of property and casualty insurance policies. These insurance premium finance loans provide short-term financing to facilitate the purchase of property and casualty insurance policies. The consortium asserts that the collection of CIP information hinders the ability of banks to compete with non-bank financial institutions that are not subject to the CIP rule.

FinCEN exempted insurance premium finance loans from the beneficial ownership rule¹ and also exempted commercial property and casualty insurance policies² from the Bank Secrecy Act (BSA) and anti-money laundering (AML) program requirement. According to FinCEN, insurance premium finance loans present a low risk of money laundering. The FBAs and FinCEN support granting a CIP exemption for loans extended by banks and their subsidiaries to commercial customers to finance property and casualty insurance premiums.

Under 31 C.F.R. §1020.220(b), the appropriate FBA with the concurrence of FinCEN, may grant a CIP exemption by order or regulation after considering whether the proposed exemption would be consistent with the purposes of the BSA and with safe and sound banking practices. The FBAs are proposing the use of an order at this time for a number of reasons. First, an order will grant an exemption more expeditiously to the affected institutions. Second, only a small number

Concur:

Charles Yi
General Counsel

¹ See “Customer Due Diligence Requirements for Financial Institutions,” 81 Fed. Reg. 29398 (May 6, 016).

² 81 FR 29398, 29418 (May , 016).

of institutions are engaged in the premium finance lending business. In addition to the six institutions that comprised the consortium making the request, a consortium representative is aware of only two other institutions engaged in this business. The consortium representative serves as president of the National Premium Finance Association, a trade association for premium finance lenders that can serve as a vehicle for communicating the implementation of an order with any additional institutions engaged in or entering this business. Third, the request is narrow and specific. Finally, conforming changes can be made at a later date should the FBAs reopen the CIP rule.

Once the order is issued, any bank (and any bank subsidiary) that engages in this type of lending, consistent with the order, may do so without collecting CIP information for its borrower and no further exemption would be required.

CIP REQUIREMENTS

The CIP rule requires banks to implement a CIP that enables the bank to form a reasonable belief that it knows the true identity of its customers.³ It specifies the identifying information that a bank will obtain from each customer prior to opening an account, which at a minimum must include the customer's name, date of birth (for an individual), address, and identification number. An account means a formal banking relationship established to provide or engage in services, dealings, or other financial transactions including a deposit account, a transaction or asset account, a credit account, or other extension of credit. The FDIC's CIP regulation, 12 C.F.R. §326.8(b)(2), references the joint rule among the FBAs and FinCEN, 31 C.F.R. §1020.220.

DESCRIPTION OF INSURANCE PREMIUM FINANCE LENDING

The processes for executing an insurance premium finance loan are automated. According to the consortium, these loans are typically submitted, approved, and funded within the same business day and are conducted through insurance agents or brokers with no interaction between the bank and the borrower. The following details regarding the mechanics and the parties to these insurance premium financing arrangements were provided by the consortium and confirmed by an institution supervised by the FDIC that is engaged in this business line.

Insurance premium finance loans provide short-term financing to facilitate the purchase of property and casualty insurance policies. Insurance agents and brokers often assist their customers in arranging financing for the purchase of single-premium insurance policies. They typically solicit loan quotes from one or more insurance premium finance lenders and then present these quotes to their customer. Once the customer selects a loan offer and the terms are finalized, the customer will typically remit a down payment toward the insurance premium directly to the agent or broker. The insurance premium finance lender will advance a loan to the customer covering the remainder of the single premium. Importantly, the bank remits the loan

³ 31 C.F.R. §1020.220.

proceeds to the insurance company directly or through the agent or broker. The customer is obligated to make loan payments either to the bank or to the agent or broker who, as an intermediary, forwards the loan payments to the bank.

Most lenders require that insurance agents or brokers only request financing for insurance policies issued by insurance companies with satisfactory credit ratings. If a customer defaults on the loan, the lender would rely on unearned premiums for repayment of the loan; therefore, the lender has credit exposure to the company that issued the insurance policy. Accordingly, a lender typically will assess the creditworthiness of the insurance company and not that of the customer that is seeking to finance the purchase of a policy. For this reason, bank insurance premium finance lenders have minimal interaction with the customer while the loan is being underwritten.

PROBLEM IDENTIFIED BY INDUSTRY

In a letter dated September 20, 2016, supplemented by a letter dated March 27, 2017, a consortium of banks submitted a request to the FBAs and FinCEN for an exemption or interpretation regarding the application of the CIP rule to banks and their subsidiaries engaged in insurance premium finance lending (the “Request Letters”).⁴ The Request Letters cite FinCEN’s conclusions in connection with related rulemaking and assert that there is no need to apply the CIP rule to insurance premium finance lending because this activity presents a low risk of money laundering.⁵ The letters also assert that because of data privacy concerns, insurance brokers and agents are reluctant to collect personal information such as the date of birth and social security number of individuals owning sole proprietorships. Further, the part of the premium finance industry not subject to the CIP rule does not require that its agents and brokers collect CIP information.

The Request Letters maintain that the high-speed insurance premium lending process makes it difficult for banks to fully comply with the CIP information collection requirements. Specifically, agents and brokers do not initially provide bank insurance premium finance lenders with taxpayer identification numbers and, in the case of sole proprietorships, the date of birth and social security number of the borrower. To comply with existing CIP requirements, banks providing insurance premium finance loans, must request this information from the agent or broker, creating delays in processing. A bank would not be in compliance with the CIP rule if it approved an insurance premium finance loan and opened an account on behalf of a customer without having the required information to identify and verify the customer’s identity.

RELIEF REQUESTED

⁴ The consortium included the following institutions and subsidiaries: Pacific Enterprise Bank; BankDirect Capital Finance, LLC – BankDirect Capital Finance, a Division of Texas Capital Bank, N.A.; Premium Assignment Corporation, a subsidiary of SunTrust Bank; First Insurance Funding Corp.; AFCO Credit Corporation – AFCO Acceptance Corporation- Prime Rate Premium Finance Corp., subsidiaries of Branch Banking & Trust Company (BB&T); and Metabank (its AFS/IBEX division).

⁵ See “Customer Due Diligence Requirements for Financial Institutions,” 81 Fed. Reg. 29398 (May 16, 2016).

The consortium requests that the FBAs, with FinCEN's concurrence, grant an exemption from the requirements of the CIP rule for loans extended by banks and their subsidiaries to commercial customers to facilitate purchases of property and casualty insurance policies.

FINCEN'S POSITION

Previously, FinCEN made the independent determination that these types of accounts present a low risk of money laundering, both because of the purpose for which such accounts are established and because the characteristics of these accounts that make them poor vehicles for money laundering.⁶ Moreover, according to FinCEN, property and casualty insurance policies themselves are not an effective means for transferring illicit funds. Based on these determinations, FinCEN exempted financial institutions that finance insurance premiums from the general requirement to identify and verify the identity of the beneficial owner(s) of legal entity customers.⁷ In May 2018, FinCEN issued a ruling to provide additional exceptive relief to premium finance lending products that allow for cash refunds.⁸ Similarly, FinCEN exempted commercial property and casualty insurance policies from the BSA's AML program requirement for insurance companies.⁹

INTENTION OF OTHER FBAs

The OCC and the FRB are prepared to move forward and grant an exemption from the requirements of the CIP rule for loans extended by banks (and their subsidiaries), subject to their jurisdiction, to commercial customers to facilitate purchases of property and casualty insurance policies. The NCUA is also prepared to grant the same CIP exemption for loans extended by credit unions (and their subsidiaries) to commercial customers to finance property and casualty insurance premiums. Staff from the OCC and the FRB has stated that the Order does not require a notice in the Federal Register. FDIC legal has concluded that notice in the Federal Register is a policy issue and is not legally required.

REGULATORY REQUIREMENTS FOR GRANTING AN EXEMPTION

Under 31 C.F.R. § 1020.220(b), the appropriate FBA, with the concurrence of the Secretary of the Treasury, may by order or regulation exempt any bank or type of account from the requirements of the CIP rules. The Secretary's authority under this provision has been delegated to FinCEN. The FBA and FinCEN must consider whether the proposed exemption would be consistent with the purposes of the BSA¹⁰ and with safe and sound banking practices, and may consider other appropriate factors.

⁶ 81 FR 29398, 29418 (May 11, 2016).

⁷ 31 C.F.R. 1010.230(h)(iii).

⁸ FIN-2018-R001, May 11, 2018

⁹ 70 FR 66754; 66757 (Nov. 3, 2005); 31 C.F.R. 1025.100(b) (defining covered products to include permanent life insurance, annuity contracts and other insurance products with features of cash value or investment.).

¹⁰ 31 U.S.C. § 5311 (setting forth the purposes of the BSA).

FINDINGS SUPPORTIVE OF AN EXEMPTION

First, FinCEN has determined that this Order is consistent with the purposes of the BSA. As stated above, FinCEN exempted these loans from the beneficial ownership rule and also exempted commercial property and casualty insurance policies from the BSA's AML program requirement. The purpose of the BSA is "to require certain reports or records where they have a high degree of usefulness in criminal, tax, or regulatory investigations or proceedings, or in the conduct of intelligence or counterintelligence activities, including analysis, to protect against international terrorism."¹¹ FinCEN's position indicates that the CIP information in insurance premium finance lending does not have a high degree of usefulness.

Second, this exemption is generally consistent with safe and sound banking practices. The resulting banking practices will not be contrary to generally accepted standards of prudent banking operation, and will not give rise to abnormal risk or loss or damage to an institution, its shareholders, or the agencies administering the insurance funds. The Request Letters represent the belief of the consortium that insurance premium financing is a form of secured lending. Should a borrower default, the insurance company is legally obligated to return any unearned premiums to the lender. Further, most lenders require that insurance agents or brokers only request financing for insurance policies issued by insurance companies with a satisfactory credit rating.

PROPOSED COURSE OF ACTION

In light of the position taken by FinCEN and the other FBAs, it is recommended the FDIC grant an exemption from the requirements of the CIP rule for loans extended by banks (and their subsidiaries) to commercial customers to facilitate purchases of property and casualty insurance policies. Importantly, FinCEN has determined that granting an exemption is consistent with the BSA. The FDIC defers to FinCEN in light of its role in administering the BSA. On July 24, 2018, FinCEN transmitted its intent to execute the attached Order. With respect to safety and soundness, the nature of insurance premium finance loans is unlikely to affect a bank's safety and soundness even if CIP information is not collected. In the event the FDIC Board of Directors grants the exemption, staff recommends that the Board delegate authority to the Director, Division of Risk Management Supervision, to execute the Order on behalf of the FDIC.

¹¹ 31 U.S.C. § 5311.