

Testimony of

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Before the

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Policy, Trade, and Technology

Committee On Financial Services

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Thank you, Chairman Gutierrez, Ranking Member Paul, and members of the Committee for this opportunity to testify today regarding the Unlawful Internet Gambling Enforcement Act of 2006 and proposed regulations under this act.

I. Introduction. In enacting the Unlawful Internet Gambling Enforcement Act of 2006 (the “Act”),¹ Congress endeavored to address certain identified problems associated with unlawful Internet gambling.² In order to address these problems, the Act prohibits any person engaged in the business of betting or wagering from knowingly accepting payments in connection with the participation of another person in unlawful Internet gambling. These payment transactions are termed “restricted transactions.”³

On October 4, 2007, the Board of Governors of the Federal Reserve System and The Departmental Offices of the Department of the Treasury (collectively, the “Agencies”) published a notice of joint proposed rule making and request for comment in the Federal Register⁴ (the “Proposal” or “proposed regulations,” as applicable) to implement applicable provisions of the Act. As required under the Act, the Proposal designates certain payment systems that could be used in connection with unlawful Internet gambling transactions prohibited under the Act. The Proposal requires participants in designated payment systems to establish policies and procedures reasonably designed to identify and block, or otherwise prevent or prohibit, transactions in connection with unlawful Internet gambling. The Proposal also grants exemptions to

¹ Pub.L.No. 109-347, 120 Stat. 1884 (codified at 31 U.S.C. §§ 5361-5367). The Act was signed into law on October 13, 2006.

² See also H.R. 2046, 110th Cong. (2008) for other identified problems with Internet gambling in addition to those identified in the Act.

³ 31 U.S.C. § 5362(7).

⁴ Prohibition on Funding of Unlawful Internet Gambling, 72 Fed.Reg. 56680 (proposed October 4, 2007), to be codified at 12 C.F.R. Part 233 and 31 C.F.R. Part 132.

certain participants in designated payment systems from the requirements to establish such policies and procedures because the Agencies believe that it is not reasonably practical for those exempted participants to identify and block, or otherwise prevent or prohibit, unlawful Internet gambling transactions restricted by the Act. Finally, the Proposal describes the types of policies and procedures that nonexempt participants in each class of designated payment systems may adopt in order to comply with the Act, including nonexclusive examples of policies and procedures which would be deemed to be reasonably designed to prevent or prohibit unlawful Internet gambling transactions proscribed by the Act.

II. Some significant issues for the financial services industry, including Wells Fargo. In reviewing the proposed regulations and the Act, Wells Fargo has identified certain key issues as set forth in its comment letter, dated December 12, 2007, copy attached. We would briefly like to highlight some of them for the committee:

A. The definition of “unlawful Internet gambling.” While this term is a core definition under the Act, “unlawful Internet gambling” is not clearly defined.⁵ In the Proposal, this term is defined as placing, receiving, or transmitting a bet or wager by means that involves the use of the Internet “where such bet or wager is unlawful under any applicable Federal or State law in the State or Tribal lands in which the bet or wager is initiated, received, or otherwise made.”⁶ In short, by merely referencing applicable federal or state law, Congress in effect has passed the obligation of identifying unlawful Internet activities to the financial services industry, the principal participants in the payment systems. That industry is tasked with the unenviable burden of determining if a

⁵ 31 U.S.C. § 5362(10).

⁶ 72 Fed.Reg. at 56697; § __.2(t).

business activity of a customer encroaches upon unlawful Internet gambling activity. This burden is further compounded for a financial service provider with a retail presence in 50 states, such as Wells Fargo. Wells Fargo must identify, interpret, and apply the state laws in all 50 states to prevent or prohibit unlawful Internet activities, in addition to federal law.

To mitigate this burden, we have urged that the Agencies define the term “unlawful Internet gambling” with greater precision. In the event the Agencies are unable to draw the definition with more precision, we have urged the Agencies to expand and broaden the exemptions to include all participants in the automated clearing house (“ACH”) system, the check collection system, and the wire transfer system.

To substantiate our view that these three payment systems should be exempted under the Proposal, we provide some sense of the sheer number of transactions Wells Fargo may be required to monitor, review, and block in these three payment systems, as follows:

- **ACH system.** As an originating depository financial institution (“ODFI”) with responsibility under the Proposal to identify restricted ACH debit transactions, we originate in excess of approximately 3.1 million debit transactions daily. As a receiving depository financial institution (“RDFI”) with responsibility to identify restricted ACH credit transactions, we receive approximately 1.2 million credit entries daily. In sum, in ACH transactions alone, we would on a daily basis need to deal with over 4.3 million transactions.

- **Check collection system.** As a depository financial institution, we handle for forward collection approximately 11 million checks daily, with approximately 6 million of such checks drawn on third party financial institutions.
- **Wire transfer system.** As a beneficiary's bank of wire transfers with responsibility to prevent restricted transactions, we receive daily approximately 25,000 to 30,000 incoming wire transfers. As an originator's bank or intermediary bank sending a wire transfer directly to a foreign bank, with the responsibility to deny access to such bank as to restricted transactions, we send approximately 5,000 to 6,000 such wires daily. We would, in short, be required to review these numerous wire transfer transactions daily.

These foregoing numbers should provide some sense of the high volume of transactions we process daily. To oversee these payment systems to identify restricted transactions is a significant and difficult mission.

If the Agencies are unable to draw a clearer definition of the term and if the Agencies do not have an appetite to exclude the three enumerated payment systems, we have urged the Agencies to consider a government generated list in some form, even if the list may have limited utility.

B. Applicability of the proposed regulations to existing customers. While the Proposal is not entirely clear, we are gravely concerned that the final regulations to be issued by the Agencies under the Act may apply to existing customers as of the effective date of the final regulations. If the Agencies contemplate the application of the final regulations to existing customers as of the effective date, we confront significant burdens in complying with the final regulations.

Due diligence would need to be undertaken as to existing customers to confirm the nature and scope of their business activities, to determine whether they are engaged in restricted transactions. We currently have over 24 million consumer customers and 1.8 million business customers. While we are familiar with the nature of the business activities of many of these customers due to the due diligence under the regulations issued under § 326 of the USA PATRIOT Act, effective as of October 1, 2003,⁷ many of our customers predate these regulations. Consequently, these customers may not have been subjected to the more robust due diligence process evidenced in these regulations.

Agreements with existing customers would have to be amended to incorporate provisions advanced in the Proposal. For example, under § __.6(c)(1)(ii), the proposed regulations set forth examples of policies and procedures reasonably designed to prevent or prohibit restricted transactions in card systems. In this regard, the proposed regulations provide that such policies and procedures are deemed to be so reasonably designed if they include as a term of the merchant customer agreement that the merchant may not receive restricted transactions through the card system. Wells Fargo has a significant number of merchant customers, totaling approximately 140,000. If Wells Fargo seeks to provide such a provision prohibiting the receipt of restricted transactions in the merchant customer agreement as to existing merchant customers, it would face a significant administrative and operational challenge timely amending existing agreements, if the final regulations were applied retroactively.

While the originator's bank and intermediary bank sending a wire transfer are generally exempt from the requirements for establishing written policies and procedures

⁷ 31 C.F.R. § 103.120, *et seq.*; 68 Fed.Reg. 25090 (May 9, 2003).

reasonably designed to prevent or prohibit restricted transactions,⁸ an originator's bank or intermediary bank sending a wire transfer directly to a foreign bank are nevertheless required to have policies and procedures reasonably designed to identify and block, or otherwise prevent or prohibit, restricted transactions.⁹ Policies and procedures deemed to be reasonably designed must include instances when wire transfer services should be denied and circumstances under which the correspondent account should be closed "... with respect to a foreign bank that is found to have received from the originator's bank or intermediary bank wire transfers that are restricted transactions"¹⁰ The right to block wire transfer transactions and close foreign correspondent accounts is plainly matters to be addressed in foreign correspondent banking agreements. Inasmuch as such rights are not currently addressed in such agreements, we would need to adopt amendments thereto with over 200 foreign correspondent banks. We are confident that committee members can well appreciate the hardship we would confront in seeking adoption of such amendments with foreign banks.

III. Conclusion. These observations conclude my remarks. I am pleased to respond to any questions the committee may have. Thank you for this opportunity to speak before this committee.

⁸ § __.4(c)(2).

⁹ § __. 6(f)(2).

¹⁰ *Ibid.*