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Via e-mail

Dear Charles:

Thank you for agreeing to meet with Cecilia Gardner and me on Thursday, 10 April, to discuss the proposed AML regulation. An informal discussion will help in our ongoing preparations for compliance. I have been exchanging email with precious metal companies since last April, when the ANPR was published. Late last month representatives of a number of precious metal refining companies met in Tampa, and one company presented information about its newly completed AML program. The International Precious Metals Institute will be submitting a written comment for submission on 22 April, and guidance for compliance with the AML regulation is on the agenda for its annual meeting in June.

The precious metals industry concurs with the purpose of avoiding its use for money laundering and terrorist finance, and believes that the flexibility provided by the proposed regulation should permit its fulfillment with sound business practices, many already in use. Nevertheless, questions have arisen, and I want to advise you of points that have been raised within the industry, so that our meeting discussion might be more efficient. The points set forth below are numbered for convenience of discussion, rather than in some priority or rank.

Please note that these points all deal with a subset of the category of financial institution - a "dealer in precious metals" - rather than with the full category of "dealer in precious metals, stones and jewels." I think that some of these points may be of interest to the entire category, but I will leave the concerns and interests of stones and jewels to Cecilia and other knowledgeable people.

1. There are two parts to the basic definition of a "dealer," and it appears to us that both must be satisfied. First, a dealer is someone who is in business: "a person engaged in the business of purchasing and selling .. precious metals." Therefore a person who purchases precious metals for reasons other than business is not encompassed by that definition. Thus, for example, a person who buys \$100,000 in gold coins for gifts would not be encompassed as a dealer. Of course, we are aware of the potential for evasion, but the proposed definition would seem to require that a dealer actually be in the business of buying and selling precious metals. (For comparison purposes, I have noted the IRS considerations for determining if a person is engaged in a business, rather than a hobby, in regard to the deduction of "business" expenses from income.) In perhaps a closer question, a person who buys \$100,000 in gold bullion for an investment would also seem to not be a dealer, even if that investment is sold within the same year as purchase. If we are incorrect, please clarify.

2. Second, within a business of buying and selling, the business must be above a threshold level: "(A) Purchased more than \$50,000 in .. precious metals, .. or (B)

Received more than \$50,000 in gross proceeds from transactions in .. precious metals." We do not have any objection or concern with that threshold.

3. We understand that both of these parts of the basic definition of a "dealer" are inextricably tied to the definition of "precious metal," particularly to its threshold purity of 500 parts per thousand. Thus a company that is in the business of buying and selling "low grade" scrap which always contains lower than .500 concentrations of precious metals is not a "dealer in precious metals" for purposes of this regulation, even if it engages in much more than \$50,000 in purchases and sales of such "low grade" scrap. That is because each transaction in "low grade" scrap is not a transaction in "precious metals" for purposes of this regulation. We know, and are sure that you do as well, that it is possible to launder money at lower concentrations. We assume that in setting the bar at .500, you are focusing our attention, and your resources, at the materials in which money laundering would be more likely, because of the higher values and more rapid transactions. We do not object to the proposed threshold.

4. Of course, if that same company also buys or sells "high grade" .500 or more precious metal materials, in an annual amount greater than \$50,000, it then falls into the definition of "dealer in precious metals." There are many companies which engage primarily in low grade transactions, but these companies will occasionally find an opportunity to deal in high grade materials. But we understand that the AML requirement for that company would only apply to its "high grade" transactions. If we are incorrect, please clarify.

5. We have a similar understanding about the "fabricating finished goods" exception. A company that fabricates products with minor amounts of precious metals is not a "dealer in precious metals." However, for example, if that company sells some of its excess precious metal inventory in a high grade state, such a sale or sales, if over \$50,000, would make that company a dealer in precious metals. Again, however, that company's AML program would have to encompass only its transactions that were of precious metals with a .500 or higher concentration. If we are incorrect, please clarify.

6. The refining of precious metals is an international business, and a number of foreign companies buy and sell precious metals in the United States. We assume that a foreign company is subject to the proposed AML regulation if it engages in purchase or sales transactions which satisfy the \$50,000 and .500 thresholds and which take place, at least in part, within the United States. We also assume that the required AML program of such a company would encompass only such transactions. If we are incorrect, please clarify.

7. Some precious metal refining transactions provide for toll refining, in which a refiner does not buy metal, but performs a service, and returns metal to the customer. For example, a company which uses precious metal in fabrication always sends its manufacturing scrap to a refiner. The fabrication customer wants the same precious metals back, in a refined state, for use in its production. The refiner will sample and assay the received batch of manufacturing scrap, and will return the assayed amount of precious metal content to the customer, after taking a fee for its refining services. We do not see a toll refining transaction, in which refined metal is returned without purchase or

sale, to the original customer, as a purchase or sale of precious metals, even if the scrap is greater than .500 in concentration, and therefore not a transaction in precious metals subject to the AML requirement. If we are incorrect, please clarify.

8. We understand that the proposed regulation applies only to purchases and sales of physical metal. That is, the purchase and sale of a derivative in which a precious metal is the underlying commodity would not be a covered transaction, unless and until the derivative was closed out by actual delivery of physical metal (or actual title to stored physical metal). Most derivatives in precious metals are closed not by actual delivery of the physical metal but by financial payment, and thus are not different from derivatives in wheat or pork bellies. We do not see these paper transactions as appropriate for defining a "dealer in precious metals" or being transactions that are subject to an AML requirement, at least not under this category of financial institution.

9. We note that a person is not a dealer subject to this proposed regulation until he is in the business and has engaged in \$50,000 of purchases or sales "during the prior calendar or tax year." A person could therefore begin engaging in this business on January 1, 2004, and would not have any "prior calendar or tax year" transactions until 2005, and thus would not be required to have an AML program until April 1 of 2005. That seems to be an unnecessary, and probably unintended, delay.

10. Finally, we note that the USA PATRIOT Act provides for cooperative exchanges of information between governments and financial institutions. A common source of relevant information, hopefully available on the internet, would be very useful. Also in this regard, we note that there are some obstacles in some state laws to private persons obtaining background information about customers. Will the federal AML requirement now override such state law objections? It would be useful if Treasury would clarify the rights and obligations of dealers in precious metals to such information as is reasonably appropriate and necessary to fulfill our AML obligations. If there is not a federal preemption, a Treasury statement in the preamble of the final rule would assist dealers in seeking permission from state agencies to obtain background information.

I hope that this list is of some assistance in our meeting, and look forward to seeing you on Thursday.

Regards,  
John Bullock