CADWALADER

Cabinet **News and Views**

Informed analysis for the financial services industry

FinCEN Proposes New Rule Requiring AML Compliance Programs for Investment Advisers

By **Christian Larson**
Special Counsel | White Collar Defense and Investigations

On February 15, the U.S. Treasury's Financial Crimes Enforcement Network ("FinCEN"), published a proposed rule that would define specified investment advisers as "financial institutions" required to implement anti-money laundering ("AML") compliance programs.

The proposed rule would apply to investment advisers registered with the Securities and Exchange Commission ("SEC") and investment advisers that report to the SEC as exempt reporting advisors. It would require covered investment advisers to implement an AML compliance program that includes:

- Policies, procedures, and internal controls reasonably designed to prevent money laundering, terrorist financing, and other illicit financial activities;
- Diligence to understand the nature and purpose of customer relationships in order to develop a customer risk profile;
- Ongoing monitoring to identify and report suspicious activity;
- Ongoing training for personnel;
- A designated person responsible for implementing and monitoring the AML compliance program; and
- Independent testing of the AML compliance program for compliance with the Bank Secrecy Act ("BSA").

The proposed rule would not require covered investment advisors to immediately implement a Customer Identification Program ("CIP") Rule (*e.g.*, 31 C.F.R. 1023.220), or comply with FinCEN's Customer Due Diligence ("CDD") Rule (31 C.F.R. 1010.230), which requires certain financial institutions to identify the individual beneficial owners of entities. Instead, FinCEN plans to impose CIP obligations as

part of a joint rulemaking with the SEC, and beneficial ownership obligations after FinCEN completes a separate rulemaking to conform the CDD Rule with the requirements of the Corporate Transparency Act (31 C.F.R. 1010.380). Nonetheless, covered investment advisers would need to collect information about customers in order to develop a customer risk profile and for the purpose of effectively monitoring customer conduct to identify suspicious activity.

FinCEN proposes to delegate its examination authority to the SEC, as it has done for broker-dealers and mutual funds. Although many investment advisors already implement some form of an AML compliance program, whether voluntarily, as a contractual obligation, or due to the advisor's affiliation with another regulated financial institution, covered investment advisors would need to review those programs to assess whether they meet the requirements of the proposed rule. Notably, investment advisors would not need to apply an AML compliance program to mutual fund customers, because mutual funds are subject to separate AML program requirements under the BSA and its implementing regulations.

As "financial institutions," covered investment advisors would also be subject to additional reporting and compliance obligations, including:

- Compliance with the Travel Rule (31 C.F.R. 1010.410(e)) and related recordkeeping requirements;
- Filing currency transaction reports for cash transactions exceeding $10,000;
- Enhanced due diligence requirements for private bank accounts and correspondent accounts for foreign financial institutions;
- Special measures that the U.S. Treasury imposes under Section 311 of the USA PATRIOT Act; and
- Information sharing rules under sections 314(a) and 314(b) of the USA PATRIOT Act.

FinCEN issued a similar proposed rule in 2015, but never finalized it. The 2015 proposed rule has now been formally withdrawn.

FinCEN has set a deadline of April 15, 2024 for the submission of comments on the proposed rule.
