DEPARTMENT OF THE TREASURY

Financial Crimes Enforcement Network

31 CFR Parts 1010 and 1032

RIN 1506–AB58

Financial Crimes Enforcement Network: Anti-Money Laundering/ Countering the Financing of Terrorism Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers

AGENCY: Financial Crimes Enforcement Network (FinCEN), Treasury.

ACTION: Notice of proposed rulemaking.

SUMMARY: FinCEN, a bureau of the U.S. Department of the Treasury (Treasury), is issuing this notice of proposed rulemaking (NPRM) to include certain investment advisers in the definition of ''financial institution'' under the Bank Secrecy Act (BSA), prescribe minimum standards for anti-money laundering/ countering the financing of terrorism (AML/CFT) programs to be established by covered investment advisers, require covered investment advisers to report suspicious activity to FinCEN pursuant to the BSA, and make several other related changes to FinCEN regulations. FinCEN is proposing this action to address gaps in the existing AML/CFT regulatory framework in this sector. The proposed regulations will apply to investment advisers that may be at risk for misuse by money launderers, terrorist financers, or other actors who seek access to the U.S. financial system for illicit purposes via investment advisers and threaten U.S. national security.

DATES: Written comments on this notice of proposed rulemaking (NPRM) must be submitted on or before April 15, 2024.

ADDRESSES: Comments may be submitted by any of the following methods:

- *Federal E-Rulemaking Portal: http://www.regulations.gov.* Follow the instructions for submitting comments. Refer to Docket Number FINCEN–2024–0006 and RIN 1506–AB58.
- *Mail:* Policy Division, Financial Crimes Enforcement Network, P.O. Box 39, Vienna, VA 22183. Refer to Docket Number FINCEN–2024–0006 and RIN 1506–AB58.

Please submit comments by one method only.

FOR FURTHER INFORMATION CONTACT: The FinCEN Resource Center at (800) 767–2825 or email *frc@fincen.gov.*

SUPPLEMENTARY INFORMATION:

I. Executive Summary

To address illicit finance risks in the investment adviser industry, FinCEN is proposing to apply certain AML/CFT requirements to certain investment advisers. Currently, there are no Federal or State regulations requiring investment advisers to maintain AML/CFT programs [1] or records under the BSA, although some investment advisers may do so, for example, if they are also licensed as banks (or are bank subsidiaries), registered as broker-dealers, or advise mutual funds.[2] This means that thousands of investment advisers overseeing the investment of tens of trillions of dollars into the U.S. economy currently operate without legally binding AML/CFT obligations.

These proposed regulations aim to close this gap by amending chapter X of title 31 of the Code of Federal Regulations to add ''investment adviser'' to the definition of ''financial institution'' at 31 CFR 1010.100(t). FinCEN has statutory authority to define additional types of businesses as financial institutions where it determines that such businesses engage in any activity ''similar to, related to, or a substitute for'' those in which any of the businesses listed in the statutory definition are authorized to engage.[3] FinCEN proposes to make such a determination with respect to investment advisers, which would be defined to include two types of advisers: those that are (1) registered or required to register with the U.S. Securities and Exchange Commission (SEC, and, such investment advisers, RIAs) and (2) investment advisers that report to the SEC as Exempt Reporting Advisers (ERAs) pursuant to the Investment Advisers Act of 1940, as amended (Advisers Act),[4] and the rules thereunder.

Accordingly, this proposed rule would establish AML/CFT requirements for RIAs and ERAs. In full, the proposed rule would require RIAs and ERAs to implement an AML/CFT program, file Suspicious Activity Reports (SARs) with FinCEN, keep records relating to the transmittal of funds (Recordkeeping and Travel Rule), and other obligations of financial institutions under the BSA. The proposed rule would also apply information-sharing provisions between and among FinCEN, law enforcement government agencies, and certain financial institutions, and would subject investment advisers to the ''special measures'' imposed by FinCEN pursuant to section 311 of the USA PATRIOT Act.

Concurrent with this proposal, FinCEN is withdrawing the 2015 proposed rule that would have applied AML program, SAR filing, and other AML/CFT requirements to RIAs.[5]

In this rulemaking, FinCEN is not proposing to include a customer identification program (CIP) requirement, nor is it proposing to include within the AML/CFT program requirements an obligation to collect beneficial ownership information for legal entity customers at this time. FinCEN anticipates addressing CIP via a future joint rulemaking with the SEC and addressing the requirement to collect beneficial ownership information for legal entity customers in subsequent rulemakings.

Moreover, because mutual funds are already defined as ''financial institutions'' under the BSA (31 CFR 1010.100(t)(10)), and because of the regulatory and practical relationship between mutual funds and their investment advisers, the proposed regulations would also not require investment advisers to apply AML/CFT program or SAR reporting requirements to mutual funds.[6] The proposed regulations would also remove the existing requirement that investment advisers file reports for the receipt of more than $10,000 in cash and negotiable instruments using the joint FinCEN/Internal Revenue Service Form 8300 (Form 8300).[7] Investment advisers would instead be required to file a Currency Transaction Report (CTR) for a transaction involving a transfer of more than $10,000 in currency by, through, or to the investment adviser, unless subject to an applicable exemption.

Finally, FinCEN is proposing to delegate its examination authority to the SEC given the SEC's expertise in the regulation of investment advisers and

[1] Section 6101 of the AML Act, codified at 31 U.S.C. 5318(h), amended the BSA's requirement that financial institutions implement AML programs to also combat terrorist financing. This NPRM refers to ''AML program'' when discussing the obligation prior to the enactment of the AML Act, and to ''AML/CFT program'' in reference to the current obligation contained in the BSA and the proposed rule.

[2] *See infra* section IV.E3 and n. 51.

[3] 31 U.S.C. 5312(a)(2)(Y).

[4] 15 U.S.C. 80b–1 *et seq.*

[5] *See* FinCEN, *Anti-Money Laundering Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers,* 80 FR 52680 (Sept. 1, 2015).

[6] As described below, FinCEN does not propose to permit investment advisers to exempt mutual funds that they advise from the requirements of 31 CFR part 1010, subparts E and F (31 CFR 1010.520, 540, 600–670) that FinCEN proposes to apply to covered investment advisers in the proposed rule (*e.g.,* certain information sharing, special standards, prohibitions, and other requirements).

[7] 31 CFR 1010.330(a)(1)(i), (e)(1); 26 CFR 1.6050I–1(e).

the existing delegation to the SEC of authority to examine brokers and dealers in securities (broker-dealers) and certain investment companies.[8]

This NPRM is divided into six main sections including this executive summary in section I. Section II provides background on the existing AML/CFT regulatory framework; the illicit finance risks that this rulemaking will address; the SEC's regulatory framework for investment advisers; the limited extent to which certain RIAs and ERAs may already implement AML/CFT measures; and a summary of past proposed rules to apply AML/CFT obligations with respect to investment advisers. Section III discusses the scope of the proposed rule. Section IV includes the section-by-section analysis of the elements of the proposed rule. Section V lays out questions on which FinCEN seeks comment, and section VI addresses the severability of the proposed rule's requirements. Section VII includes the Regulatory Analysis required by relevant statutes and executive orders.

II. Background

A. Current BSA Framework

Enacted in 1970, the Currency and Foreign Transactions Reporting Act, generally referred to as the BSA, is designed to combat money laundering, the financing of terrorism, and other illicit financial activity, and to safeguard the national security of the United States.[9] This includes ''through the establishment by financial institutions of reasonably designed risk-based programs to combat money laundering and the financing of terrorism.''[10] The Treasury Secretary is authorized to administer the BSA and to require financial institutions to keep records and file reports that ''are highly useful in . . . criminal, tax, or regulatory investigations, risk assessments, or proceedings'' or ''intelligence or counterintelligence activities, including analysis, to protect against international terrorism.'' [11] The Secretary delegated the authority to implement, administer, and enforce the BSA and its implementing regulations to the Director of FinCEN.[12]

Pursuant to this authority, FinCEN may define a business or agency as a ''financial institution'' if it engages in any activity determined by regulation ''to be an activity which is similar to, related to, or a substitute for any activity'' in which a ''financial institution'' as defined by the BSA is authorized to engage.[13] Additionally, the BSA requires financial institutions to maintain programs to combat money laundering and the financing of terrorism and authorizes the Secretary—and thereby FinCEN—to issue regulations prescribing ''minimum standards'' for such AML/CFT programs.[14] Similarly, under the BSA, FinCEN may require financial institutions to ''report any suspicious transactions relevant to a possible violation of law or regulation.'' This provision authorizes FinCEN to require the filing of SARs.[15] FinCEN also has authority under the BSA to authorize the sharing of financial information by financial institutions [16] in specified circumstances, and to require financial institutions to keep records and maintain procedures to ensure compliance with the BSA and its implementing regulations or to guard against money laundering.[17]

B. Investment Adviser Industry and Regulation

1. Investment Adviser Industry

The investment adviser industry in the United States consists of a wide range of business models geared towards providing advisory services to many different types of customers.[18] Some of the advisory services that investment advisers may provide include portfolio management, financial planning, and pension consulting. Advisory services can be provided on a ''discretionary'' or ''non-discretionary'' basis.[19] Investment advisers provide their expertise to a wide range of customers, including retail investors, high-net-worth individuals, private institutions, and governmental entities (including local, State, and foreign government funds).[20] Investment advisers often work closely with their customers to formulate and implement their customers' investment decisions and strategies. Investment advisers may be organized in a variety of legal forms, including corporations, sole proprietorships, partnerships, or limited liability companies.[21]

The Advisers Act and its implementing rules and regulations form the primary framework governing advisory activity, along with other Federal securities laws and their implementing rules and regulations, such as the Investment Company Act of 1940, the Securities Act of 1933, and the Securities Exchange Act of 1934.[22] Since the Advisers Act was amended in 1996 and 2010, generally only investment advisers who have at least $100 million in assets under management (AUM) or advise a registered investment company [23] may register with the SEC.[24] Other investment advisers typically register with the State in which the adviser maintains its principal place of business.

SEC-Registered Investment Advisers. Unless eligible to rely on an exception,

[8] 31 CFR 1010.810(b)(6).

[9] *See* 31 U.S.C. 5311. Certain parts of the Currency and Foreign Transactions Reporting Act, its amendments, and the other statutes relating to the subject matter of that Act, have come to be referred to as the BSA. The BSA is codified at 12 U.S.C. 1829b, 12 U.S.C. 1951–1960, and 31 U.S.C. 5311–5314 and 5316–5336, and includes notes thereto.

[10] 31 U.S.C. 5311(3).

[11] 31 U.S.C. 5311(1).

[12] Treasury Order 180–01, paragraph 3(a) (Jan. 14, 2020), available at *https://home.treasury.gov/about/general-information/orders-and-directives/treasury-order-180-01*.

[13] 31 U.S.C. 5312(a)(2)(Y).

[14] 31 U.S.C. 5318(h)(1), (2).

[15] 31 U.S.C. 5318(g)(1).

[16] *See* Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (USA PATRIOT Act), Public Law 107–56, sec. 314(a), (b).

[17] *See* 12 U.S.C. 1953; 31 U.S.C. 5318(a)(2).

[18] This proposed rule uses the term ''customers'' for those natural and legal persons who enter into an advisory relationship with an investment adviser. This is consistent with the terminology in the BSA and FinCEN's implementing regulations. FinCEN acknowledges that the Advisers Act and its implementing regulations primarily use the term ''clients,'' and so that term is used in specific reference to Advisers Act requirements; otherwise, the term ''customers'' is used.

[19] An adviser has discretionary authority or manages assets on a discretionary basis if it has the authority to decide which securities to purchase and sell for the client. An adviser also has discretionary authority if it has the authority to decide which investment advisers to retain on behalf of the client. *See* Glossary to Form ADV, general Instructions at p. 28, available at *https://www.sec.gov/about/forms/formadv-instructions.pdf*. According to the Investment Advisers Association (IAA), as of 2021, over 90 percent of RIAs manage client assets on a discretionary basis. Investment Adviser Association, Investment Adviser Industry Snapshot 2022, p. 53 (IAA Snapshot), available at *https://investmentadviser.org/wp-content/uploads/2022/06/Snapshot2022.pdf*.

[20] *See* Part 1A, Item 5 of Form ADV for a list of examples of different types of advisory clients.

[21] *See* Part 1A, Item 3.A of Form ADV.

[22] *See generally* 15 U.S.C. 80a–1 *et seq*. (Investment Company Act of 1940 (Investment Company Act)); 15 U.S.C. 77a *et seq*. (Securities Act of 1933); 15 U.S.C. 78a *et seq*. (Securities and Exchange Act of 1934).

[23] *See* 15 U.S.C. 80a–3 (defining investment company). If an investment company meets the definition of an investment company under 15 U.S.C. 80a–3 and cannot rely on an exception or an exemption from registration, generally it must register with the SEC under the Investment Company Act and must register its public offerings under the Securities Act.

[24] Investment advisers with more than $100 million assets under management *may* register with the SEC, and investment advisers with more than $110 million in assets under management *must* register with the SEC, unless eligible for an exception. *See* 17 CFR 275.203A–1.

investment advisers that manage more than $110 million AUM must register with the SEC, as well as submit a Form ADV and update it at least annually.[25] The SEC administers and enforces the Federal securities laws applicable to RIAs. As of July 31, 2023, there were 15,391 RIAs, reporting approximately $125 trillion in AUM for their clients.[26]

Exempt Reporting Advisers. An ERA is an investment adviser that would be required to register with the SEC but is statutorily exempt from such requirement [27] because: (1) it is an adviser solely to one or more venture capital funds; or (2) it is an adviser solely to one or more private funds and has less than $150 million AUM [28] in the United States.[29] Private funds are privately offered investment vehicles that pool capital from one or more investors to invest in securities and other investments.[30] Private funds do not register with the SEC, and advisers to these funds often categorize the fund by the investment strategy they pursue. These include hedge funds, private equity funds, and venture capital funds, among others. Even though they are not required to register, ERAs must still file an abbreviated Form ADV with the SEC, and the SEC maintains authority to examine ERAs. As of July 31, 2023, there were 5,846 ERAs that were exempt from registering with the SEC but had filed an abbreviated Form ADV.[31]

- *Private Fund Advisers.* Private fund advisers, a type of ERA, are exempt from registering with the SEC if they exclusively advise private funds and have less than $150 million AUM in the United States. As of July 31, 2023, there were approximately 4,400 exempt private fund advisers, approximately 500 of which were also venture capital advisers.[32]
- *Venture Capital Advisers.* Venture capital advisers, another type of ERA, are exempt from registering with the SEC if they provide services only to venture capital funds,[33] regardless of the amount of AUM.[34] As of July 31, 2023, there were approximately 2,000 exempt venture capital advisers, approximately 500 of which were also private fund advisers.[35]

State-Registered Investment Advisers. State-registered investment advisers generally have less than $100 million in AUM. State-registered investment advisers are generally prohibited from registering with the SEC and instead register with and are supervised by the relevant State authority, unless they meet certain exceptions or their State does not supervise these entities.[36] State-registered investment advisers also file a Form ADV, which they submit to the relevant State regulator. As of December 31, 2022, there were 17,063 State-registered investment advisers who have approximately $420 billion in AUM.[37]

Non-U.S. Investment Advisers. Non-U.S. advisers whose principal offices and places of business are outside the United States, but solicit or advise ''U.S. persons,'' are subject to the Advisers Act and must register with the SEC unless eligible for an exception. One of those exceptions is the ''foreign private adviser'' exemption, and an adviser relying on this exemption is not required to make any filing with the SEC.[38] For those non-U.S. advisers registered with the SEC, the Commission states that it does not intend to seek to apply the substantive provisions of the Advisers Act to a non-U.S. adviser that is registered with the SEC with respect to its non-U.S. clients.[39] Non-U.S. advisers may also report to the SEC as ERAs if they meet the requirements to report as ERAs.

2. Existing Regulatory Framework for Investment Advisers

Oversight of the investment adviser industry by Federal and State securities regulators generally is focused on protecting investors and the overall securities market from fraud and manipulation. Most investment advisers are subject to certain reporting requirements and the extent of those requirements depends on whether the investment adviser is an RIA, registered at the State level, exempt from registration as an ERA, or otherwise not required to register with a Federal or State securities regulator.[40] RIAs are subject to various SEC rules and

[25] *See id.;* 17 CFR 275.204–1. Investment advisers register with the SEC by filing Form ADV and are required to file periodic updates. Form ADV is available at *https://www.sec.gov/files/formadv.pdf.* A detailed description of Form ADV's requirements is available at *https://www.sec.gov/oiea/investor-alerts-bulletins/ib_formadv.html.*

[26] The number of RIAs and corresponding AUM, and the number of ERAs, are based on a Treasury review of Form ADV information filed as of July 31, 2023. This Form ADV data is available at Frequently Requested FOIA Document: *Information About Registered Investment Advisers and Exempt Reporting Advisers, http://www.sec.gov/foia/docs/invafoia.htm.* The $125 trillion in AUM includes approximately $22 trillion in assets managed by mutual funds, which are advised by RIAs and are subject to AML/CFT obligations under the BSA and its implementing regulations.

[27] An adviser that is eligible to file reports as an ERA may nonetheless elect to register with the SEC as an RIA so long as it meets the criteria for registration. An investment adviser that relies on one of these exemptions must still evaluate the need for State registration.

[28] Form ADV uses the term ''regulatory assets under management'' (RAUM) instead of ''assets under management.'' Form ADV describes how advisers must calculate RAUM and states that in determining the amount of RAUM, an adviser should ''include the securities portfolios for which [it] provide[s] continuous and regular supervisory or management services as of the date of filing'' the form. *See* Form ADV, Instructions for Part 1A, Instruction 5.b.

[29] *See* sections 203(*l*) and 203(m) of the Advisers Act and 17 CFR 275.203(m)–1, respectively. ERAs are exempt from registration with the SEC, but are required to file reports on Form ADV with the SEC and are subject to certain rules under the Advisers Act.

[30] Section 202(a)(29) of the Advisers Act defines the term ''private fund'' as an issuer that would be an investment company, as defined in section 3 of the Investment Company Act (15 U.S.C. 80a–3), but for section 3(c)(1) or 3(c)(7) of that Act. Section 3(c)(1) excludes from the definition of investment company a privately-offered issuer having fewer than a certain number of beneficial owners. Section 3(c)(7) excludes from the definition of investment company a privately-offered issuer the securities of which are owned exclusively by ''qualified purchasers'' (generally, persons and entities owning a specific amount of investments).

[31] The number of ERAs is derived from a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n. 26.

[32] Based on a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n. 26.

[33] *See* 17 CFR 275.203(*l*)–1 (defining ''venture capital fund'').

[34] Certain venture capital advisers may be registered with the SEC if they no longer satisfy the criteria to be ERAs (*e.g.,* they no longer pursue a venture capital strategy (by seeking to hold securities in companies past the initial public offering stage or pursuing hedge-fund like investment strategies)) or otherwise opt to register with the SEC.

[35] Based on a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n. 26.

[36] *See* 17 CFR 275.203A–2. Other exceptions to the prohibition on SEC registration include: (1) an adviser that would be required to register with 15 or more States (the multi-State exemption); (2) an adviser advising a registered investment company; (3) an adviser affiliated with an RIA; and (4) a pension consultant. Persons satisfying these criteria and the definition of ''investment adviser'' may register as such with the SEC. Investment advisers with a principal office and place of business in New York and over $25 million AUM are required to register with the SEC.

[37] *See* North American Security Administrators Association, *NASAA Investment Adviser Section 2023 Annual Report,* p.3, *https://www.nasaa.org/wp-content/uploads/2023/09/2023-IA-Section-Report-FINAL.pdf.*

[38] The ''foreign private adviser'' exemption is available to an adviser that (i) has no place of business in the United States; (ii) has, in total, fewer than 15 clients in the United States and investors in the United States in private funds advised by the adviser; (iii) has aggregate assets under management attributable to these clients and investors of less than $25 million; and (iv) does not hold itself out generally to the public in the United States as an investment adviser. *See* 15 U.S.C. 80b–2(a)(30), 80b–3(b)(3).

[39] *See* SEC, *Exemptions for Advisers to Venture Capital Funds, Private Fund Advisers With Less Than $150 Million in Assets Under Management, and Foreign Private Advisers,* Final Rule, Investment Advisers Act Release No. 3222 (Jun. 22, 2011), 76 FR 39645, 39667 (Jul. 6, 2011).

[40] For instance, an investment adviser may be exempt from both *Federal and State* registration requirements if they had less than $25 million AUM and fewer than six clients in a State. These advisers are not required to register, nor are they ERAs.

regulations governing, among other things, their marketing and disclosures to clients, best execution for client transactions, and disclosures of conflicts of interest and disciplinary information. State-registered investment advisers may have similar requirements under State securities laws and regulations.[41] Investment advisers, depending on their registration status, are also generally subject to examination by the SEC or State securities regulators. In some circumstances, Federal securities, tax, or other rules and regulations may impose on investment advisers information collection or disclosure obligations similar to some AML/CFT measures.

However, these requirements are not designed to address money laundering, terrorist financing, and other illicit financial activity risks associated with investment advisers. Further, although some investment advisers implement AML/CFT requirements in certain circumstances or for certain customers, as described below in section II.C, application of AML/CFT measures is not uniform across the industry, and investment advisers' implementation of such measures is not subject to comprehensive enforcement or examination. Providers of the same financial services may be subject to different AML/CFT obligations (if any), and an investor or customer seeking to obscure the origin of its funds or identity can choose an investment adviser that does not apply AML/CFT measures to its customers and activities.[42]

Generally, RIAs, State-registered investment advisers, and ERAs are required to file (and annually update) Form ADV with the SEC, the relevant State securities regulator, or both.[43] Form ADV collects certain information about the adviser, including (depending on the adviser's registration status) its AUM, ownership, number of clients, number of employees, business practices, custodians of client funds, and affiliations, as well as certain disciplinary or material events of the adviser or its employees. ERAs who are not registered with the SEC or a State securities regulator are only required to file an abbreviated version of Form ADV—they are required to answer fewer client-related questions and provide less information about the services they provide. Form ADV does not require investment advisers to disclose the names of individual clients or investors.[44]

Some RIAs are also required to file a Form PF, which collects information on private funds advised by the RIA.[45] Information collected on Form PF includes the approximate percentage of a fund's equity that is beneficially owned by different types of investors, including U.S. and non-U.S. investors. Some private fund advisers, including ERAs, that are required to report on Form ADV are not required to file Form PF.[46] Unlike Form ADV, Form PF is non-public. It is provided to both the SEC and the Financial Stability Oversight Council (FSOC) and is intended to enhance investor protection and provide the FSOC with data for use in assessing systemic risk.

C. Illicit Finance Risk Associated With Investment Advisers

As detailed below, Treasury assesses that RIAs and ERAs pose a material risk of misuse for illicit finance. Including investment advisers as ''financial institutions'' under the BSA and applying comprehensive AML/CFT measures to these investment advisers are likely to reduce this risk.

1. Illicit Finance Vulnerabilities

RIAs and ERAs are vulnerable to misuse or exploitation by criminals or other illicit actors for several reasons. First, the lack of comprehensive AML/CFT regulations directly and categorically applicable to investment advisers means they, as a whole, are not required to understand their customers' ultimate sources of wealth or identify and report potentially illicit activity to law enforcement. The current patchwork of implementation by some RIAs and ERAs may also create arbitrage opportunities for illicit actors by allowing them to find RIAs and ERAs with weaker or non-existent customer diligence procedures when these actors seek to access the U.S. financial system. Second, where AML/CFT obligations apply to investment adviser activities, the obliged entities (such as custodian banks, broker-dealers, and fund administrators providing services to investment advisers and the private funds that they advise) do not necessarily have a direct relationship with the customer or, in the private fund context, underlying investor in the private fund. Further, these entities may be unable to collect relevant investor information from the RIA or ERA to comply with the entities' existing obligations[47] (either because the adviser is unwilling to provide, or has not collected, such information). Third, the existing Federal securities laws are not designed to comprehensively detect illicit proceeds or other illicit activity that is ''integrating'' into the U.S. financial system[48] through an RIA or ERA. Fourth, RIAs and ERAs routinely rely on third parties for administrative and compliance activities, and these entities are subject to varying levels of AML/CFT regulation. Fifth, particularly for private funds, it is routine for investors to invest through layers of legal entities that may be registered or organized outside of the United States, making it challenging to collect information relevant to understand illicit finance risk under existing frameworks.

(a) Lack of Comprehensive and Uniform AML/CFT Obligations

''Investment advisers'' is not presently included in the definition of ''financial institution'' under the BSA or its implementing regulations.[49] This means that, although they have Form 8300 obligations to report cash transactions above $10,000, investment advisers are typically not subject to most of the AML/CFT program, recordkeeping, or reporting obligations that apply to banks, broker-dealers, and certain other financial institutions.[50] For example, investment advisers are not required to maintain an AML/CFT program

[41] *See, e.g.,* Cal. Corp. Code, Ch.3, 25230–25238.

[42] For instance, FinCEN research identified two investment advisers with a focus on Russian customers that advertised investment structures that would allow customers to avoid going through ''know your customer'' procedures.

[43] *See* 17 CFR 275.203–1 and 204–4.

[44] Advisers to private funds are, however, required to name their private fund clients on section 7.B.(2) of Schedule D of Form ADV Part 1A. In some cases, those names may be coded.

[45] *See* 15 U.S.C. 80b–4(b). A Form PF must be submitted by any RIA that manages one or more private funds and collectively (with its related persons) had at least $150 million in private fund AUM as of the last day of its most recently completed fiscal year. *See* 17 CFR 275.204(b)–1. ''Related person'' is defined in Form PF, which is available at *https://www.sec.gov/files/formpf.pdf.*

[46] *See* 17 CFR 275.204(b)–1.

[47] *See, e.g.,* FinCEN and Federal Functional Regulators (including SEC,), Joint Release, ''*Guidance on Obtaining and Retaining Beneficial Ownership Information*'' (Mar. 5, 2010) (noting that customer due diligence procedures for legal entity customers may include ''obtaining information about the structure or ownership of the entity so as to allow the [financial] institution to determine whether the account poses heightened risk.'')

[48] Generally, money laundering involves three stages, known as placement, layering, and integration. At the ''placement'' stage, proceeds from illegal activity or funds intended to promote illegal activity are first introduced into the financial system. The ''layering'' stage involves the distancing of illegal proceeds from their criminal source through a series of financial transactions to obfuscate and complicate their traceability. ''Integration'' occurs when illegal proceeds previously placed into the financial system are made to appear to have been derived from a legitimate source.

[49] *See* 31 CFR 1010.100(t).

[50] Investment advisers are, like any other ''person,'' subject to an obligation to file Form 8300. 31 CFR 1010.330(a)(1)(i), (e)(1); 26 CFR 1.6050I–1(e).

(consisting of internal controls, an AML/CFT officer, independent testing, and employee training), and do not have independent SAR filing, customer due diligence (CDD), or CIP obligations. These are key elements of AML/CFT compliance through which an investment adviser would identify and report to law enforcement and regulators a customer, investor, or transaction that may be associated with illicit finance activity.

As noted above, some RIAs and ERAs may perform certain AML/CFT functions if the entity is also a registered broker-dealer or is a bank (*i.e.,* a dual registrant), or is an operating subsidiary of a bank;[51] other investment advisers are affiliates of banks or broker-dealers, which may implement an enterprise-wide AML/CFT program that would include that investment adviser. A Treasury analysis of Form ADV data found that approximately three percent of RIAs were dually registered as a broker-dealer or licensed as a bank, and that these entities held about 10 percent of the AUM held by all RIAs. The same analysis found that approximately 20 percent of RIAs, representing approximately 75 percent of the total AUM of RIAs, were affiliated with either a bank or broker-dealer.

In other circumstances, an investment adviser may perform AML/CFT functions via contract with a broker-dealer (*e.g.,* CIP for joint customers) or other financial institution, such as when the adviser advises an open-end registered investment company (*e.g.,* mutual fund). For instance, some RIAs have already implemented voluntary AML/CFT programs pursuant to the Securities Industry and Financial Markets Association (SIFMA) No-Action Letter under which the staff of the SEC's Division of Trading and Markets stated that it would not recommend enforcement action if a broker-dealer relies on RIAs to perform some or all aspects of the broker-dealer's CIP obligations or the portion of CDD requirements regarding beneficial ownership requirements for legal entity customers, provided that certain conditions are met, including that the RIA implements its own AML/CFT program.[52] Mutual funds,[53] which are advised by approximately 10 percent of RIAs [54] and hold approximately $22.1 trillion in assets,[55] are also subject to AML/CFT obligations under the BSA and its implementing regulations.[56]

Outside of these circumstances, some investment advisers have voluntarily implemented certain AML/CFT measures, such as CDD or other CIP requirements. However, because these programs are not required by any regulations under the BSA, advisers have wide discretion in what information to request from their customers and private fund investors. Additionally, RIAs and ERAs are not examined for compliance with voluntary AML/CFT measures not required by law, so the adviser may not be made aware of deficiencies or gaps in their programs via examination, and thereafter make improvements, and there are more limited enforcement mechanisms to pursue against the adviser for failing to implement such measures.

While the programs discussed above provide some AML/CFT coverage for parts of the investment adviser industry, they mean that RIAs and ERAs providing the same financial services have differing AML/CFT obligations. For example, depending on corporate policies and practice, stand-alone RIAs or ERAs are likely subject to different AML/CFT compliance approaches than RIAs or ERAs that are part of a bank or financial holding company; and an investor or customer seeking to obscure the origin of its funds or its identity can choose an RIA or ERA that has limited or no AML/CFT obligations.

The fact that investment advisers are not currently BSA-defined financial institutions also limits the ability of investment advisers to provide highly useful information to law enforcement, regulators, and other relevant authorities. For instance, unless they are BSA-defined financial institutions, RIAs and ERAs would not be afforded the protection from liability (safe harbor) that applies to financial institutions when filing SARs.[57] Even though investment advisers are able to file voluntary SARs, they could face increased legal risk from customers or other counterparties without the safe harbor. RIAs and ERAs are also currently unable to receive and respond to law enforcement requests for information under section 314(a) of the USA PATRIOT Act as they are not BSA-defined financial institutions.[58]

Additionally, investment advisers, or associations of investment advisers, that are not BSA-defined financial institutions cannot voluntarily share information under section 314(b) of the USA PATRIOT Act. Moreover, at present, existing BSA-defined financial institutions are limited in their ability to share with RIAs and ERAs, or receive from investment advisers, information potentially related to money laundering or terrorist financing that are not themselves BSA financial institutions.[59] Becoming a BSA-defined financial institution would allow RIAs and ERAs to share information potentially related to money laundering or terrorist financing with, and receive requests from, other financial institutions that already utilize section 314(b), such as broker-dealers. This could help financial institutions gain additional insight into their customers' transactions with RIAs and ERAs and,

[51] Investment advisers that are banks (or bank subsidiaries) subject to the jurisdiction of the Office of the Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, and the National Credit Union Administration (collectively, the FBAs) are accordingly also subject to applicable FBA regulations imposing AML/CFT requirements on banks. *See, e.g.,* 12 CFR 5.34(e)(3) and 5.38(e)(3) (OCC requirements governing operating subsidiaries of national banks and Federal savings associations).

[52] *See* SEC, Letter to Mr. Bernard V. Canepa, Associate General Counsel, Securities Industry and Financial Markets Association (SIFMA), Request for No-Action Relief Under Broker-Dealer Customer Identification Program Rule (31 CFR 1023.220) and Beneficial Ownership Requirements for Legal Entity Customers (31 CFR 1010.230) (Dec. 9, 2022), *https://www.sec.gov/files/nal-sifma-120922.pdf* (SIFMA No-Action Letter). This request for No-Action Relief was originally issued in 2004 and has been periodically reissued and remains effective. Any SEC staff statements cited represent the views of the SEC staff. They are not a rule, regulation, or statement of the SEC. Furthermore, the SEC has neither approved nor disapproved their content. These SEC staff statements, like all SEC staff statements, have no legal force or effect: they do not alter or amend applicable law; and they create no new or additional obligations for any person.

[53] As used in this NPRM, ''mutual fund'' has the same definition as in FinCEN's regulations, and refers to an ''investment company'' (as the term is defined in section 3 of the Investment Company Act (15 U.S.C. 80a–3)) that is an ''open-end company'' (as that term is defined in section 5 of the Investment Company Act (15 U.S.C. 80a–5)) that is registered or is required to register with the SEC under section 8 of the Investment Company Act (15 U.S.C. 80a–8). *See* 31 CFR 1010.100(gg). Exchange-traded funds (ETFs) are a type of exchange-traded investment product that must register with the SEC under the Investment Company Act and are generally organized as either an open-end company (''open-end fund'') or unit investment trust. The SEC's ETF Rule (rule 6c-11 under the Investment Company Act), issued in 2019, clarified ETFs are issuing ''redeemable securit[ies]'' and are generally ''regulated as open-end funds within the meaning of section 5(a)(1) of the [Investment Company] Act.'' FinCEN's definition of a mutual fund under 1010.100(gg) applies to an ETF that is registered as an ''open-end company'' (as the term is defined in section 5 of the Investment Company Act).''

[54] Information derived from a Treasury review of Form ADV information. *See supra* n. 26.

[55] According to the Investment Company Institute *2023 Investment Company Factbook,* as of December 31, 2022, U.S. mutual funds held approximately $22.1 trillion in AUM, while ETFs held approximately $6.4 trillion in AUM. Investment Company Institute, *2023 Investment Company Factbook,* p.2, *https://www.ici.org/system/files/2023-05/2023-factbook.pdf.*

[56] *See* 31 CFR 1010.100(gg); 31 CFR part 1024.

[57] 31 U.S.C. 5318(g)(3)(A).

[58] *See* 31 CFR 1010.520.

[59] *See* 31 CFR 1010.540.

potentially, a more accurate and holistic understanding of their customers' activities.

(b) Existing AML/CFT Obligations Often Apply to Intermediaries, But Not the Customer-Facing Entity

Investment advisers engage in trading or transactional activities on behalf of their customers through relationships with financial institutions that are subject to AML/CFT obligations, such as broker-dealers and banks, among others. For instance, Rule 206(4)–2 (the Custody Rule) under the Advisers Act requires RIAs that have custody of client funds or securities generally to maintain those funds and securities with a qualified custodian, defined primarily to encompass BSA-defined financial institutions.[60]

While investment advisers often do not take possession of financial assets, they nonetheless may have the most direct relationship with the customers they advise and thus be best positioned to obtain the necessary documentation and information from and about the customers concerning their assets that the investment adviser is deploying in public or private financial markets.[61] If some of these assets include the proceeds of illegal activities, or are intended to further such activities, an investment adviser's AML/CFT program could help discover such issues and prevent the customer from further using the U.S. financial system, while reporting such information for law enforcement purposes. For example, in some cases, an investment adviser may be the only person or entity with a complete understanding of the source of a customer's invested assets, background information regarding the customer, or the objectives for which the assets are invested.

Other market participants may, for example, hold and trade assets in an account controlled by an adviser, but these parties, as intermediaries, often rely solely on the investment adviser's instructions and lack independent knowledge of the adviser's customers. Further, an investment adviser may use multiple broker-dealers or banks for trading and custody services, making it difficult for one financial institution in the chain to have a complete picture of an investment adviser's activity or to detect suspicious activity involving the investment adviser. Without complete information, such an institution may not have sufficient information to file a SAR, or it may be required to file a SAR that only has partial information concerning the investment adviser's transactions on behalf of a particular customer. This limits the ability of law enforcement to identify illicit activity that may be occurring through investment advisers.

(c) Non-AML/CFT Regulations Do Not Fully Address Illicit Finance Risks

RIAs are subject to various SEC rules and regulations governing, among other things, their marketing and disclosures to clients, best execution for client transactions, and disclosures of conflicts of interest and disciplinary information. In some circumstances, Federal securities, tax, or other rules and regulations may impose obligations similar to some AML/CFT measures by requiring the collection or disclosure of certain information by RIAs and ERAs. However, these regulatory requirements are not designed to explicitly address the risk that an RIA or ERA may be used to move proceeds or funds tied to money laundering, terrorist financing, or other illicit activity; they are instead designed to protect customers against fraud, misappropriation, or other illegal conduct by an investment adviser. Accordingly, even if they require an RIA or ERA to report certain kinds of illegal conduct or collect relevant information, they do not provide a comprehensive framework that incorporates the AML/CFT and national security purposes of the BSA, an understanding of relevant illicit finance risks and activity, and a process to assess and report suspicious activity to law enforcement and other appropriate authorities.

For example, the SEC's Custody Rule[62] generally requires RIAs with custody of client funds and securities to maintain client assets at a qualified custodian and comply with other safeguards, subject to certain limited exceptions. This rule is intended to protect advisory client assets from loss, misuse, theft, or misappropriation by, and the insolvency or financial reverses of, the adviser. Qualified custodians may be able to detect and report certain suspicious activity involving a RIA's customer, such as a high volume of trading or indications of layering activity, but they often may lack identifying information about the RIA's customer and their source of funds because that customer is not their institution's customer. As a result, qualified custodians can be limited in their ability to detect other types of illicit proceeds associated with that RIA's customer.

Other financial intermediaries providing services to an investment adviser or its customers, such as banks, clearing brokers, executing brokers, and futures commission merchants, may have AML/CFT obligations, but often, they may not be well-positioned to have a complete understanding of the identity, source of funds, and investment objectives of the adviser's underlying customer. For instance, some investment advisers may be reluctant to have a broker-dealer contact their customers because they view the broker-dealer as a competitor.[63]

Similarly, the Compliance Rule[64] under the Advisers Act does not require an RIA to implement AML/CFT-related policies and procedures. Under the Compliance Rule, an RIA must adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and its implementing rules and regulations and to designate a chief compliance officer to administer the RIA's compliance policies and procedures. These policies and procedures should take into consideration the nature of that firm's operations and should be designed to prevent, detect, and promptly correct any violations of the Advisers Act or the rules thereunder. The Compliance Rule does not address the requirements of the BSA. While the Compliance Rule establishes a procedural and organizational framework that RIAs may be able to build upon to implement AML/CFT measures, the rule does not mandate that an RIA address AML/CFT in its policies and procedures. Some investment advisers may have policies and procedures to comply with Office of Foreign Assets Control (OFAC) sanctions, which similarly may provide a framework for implementing certain AML/CFT measures included in the proposed rule.[65]

[60] 17 CFR 275.206(4)–2. 17 CFR 275.206(4)–2. The SEC recently proposed amendments to the Custody Rule. *See* SEC, *Safeguarding Advisory Client Assets,* Investment Advisers Act Release No. 6240 (Feb. 15, 2023), 88 FR 14672 (Mar. 9, 2023).

[61] *See* SIFMA No-Action Letter *supra* n.52 (incoming letter to SEC stating ''RIAs often have the most direct relationship with the customers they introduce to broker-dealers and are best able to obtain the necessary documentation and information from and about the customers'').

[62] *See* 17 CFR 275.206(4)–2.

[63] *See* SIFMA No-Action Letter, *supra* n.52*0.*

[64] *See* 17 CFR 275.206(4)–7.

[65] While OFAC sanctions requirements are separate from AML/CFT requirements, investment advisers, like other U.S. persons, must comply with OFAC sanctions. AML/CFT requirements and OFAC sanctions also share a common national security goal, apply a risk-based approach, and rely on similar recordkeeping and reporting requirements to ensure compliance. For this reason, many financial institutions view compliance with OFAC sanctions as related to AML/CFT compliance obligations, and may include sanctions compliance and AML/CFT compliance in a single enterprise-wide compliance program.

(d) Investment Advisers to Private Funds Routinely Rely on Third-Party Administrators Located Outside of the United States

Routine reliance on third-party administrators by investment advisers to private funds for a range of administrative tasks, including investor due diligence and identity verification, poses a material illicit finance risk. While some third-party administrators are located in the United States and may be affiliated with larger financial institutions, others are located in offshore financial centers where private funds are routinely domiciled, usually for tax or other commercial reasons unrelated to AML/CFT regulation, such as the Cayman Islands.[66] The due diligence and verification practices of these offshore fund administrators are not uniform, and may vary based upon the requirements of the local regulatory regime as well as the requirements of the fund's adviser. While some investment advisers may rely on these administrators to manage their perceived risk or to comply with local regulatory requirements, the piecemeal review of investor information is not a substitute for comprehensive AML/CFT compliance measures. These third-party administrators may also face legal and regulatory challenges in receiving and verifying documentation from foreign legal entity investors in funds they service. Further, effective AML/CFT supervision of fund administrators based outside the United States is often still nascent, with foreign regulators taking few enforcement actions to date.[67]

(e) Use of Multiple Legal Entities for Cross-Border Investment Structure

Some investment advisers provide advisory services to customers that structure their investments through several layers of U.S. and foreign legal entities or arrangements, such as limited liability companies (LLCs) and trusts, often referred to colloquially as ''shell companies.'' Such structures may be used for legitimate tax reasons, but can be used to obfuscate the source of funds for either natural person or legal entity investors and obscure unlawful conduct.

An additional challenge is the use of nominee arrangements, in which an intermediary (often a foreign bank or overseas custodial service provider) agrees to be identified as the nominal investor and essentially acts as a ''shield'' for individuals who want to make investments without disclosing their identities or source of funds. These nominee arrangements can be used in connection with other intermediaries in the ownership chain (*e.g.,* the nominee may be acting on behalf of a foreign asset manager, who in turn has the relationship with an illicit actor or politically exposed person (PEP)). While these nominee arrangements often can have legitimate purposes, if they are not explicitly identified in required reports or records, they can be abused to obscure potentially illicit funds and make it extremely difficult (if not impossible) for regulators to identify and fully understand the nature and extent of illicit finance risks in this sector. As of Q4 2022, private fund advisers reporting on Form PF noted that they did not know, and could not reasonably obtain information about, the non-U.S. beneficial ownership of approximately $284 billion in private fund AUM.[68]

In addition, data privacy or other laws or regulations in effect in offshore jurisdictions, or contractual obligations, may impact how certain customer information is shared with investment advisers, broker-dealers, and other financial institutions (and by extension, U.S. law enforcement and regulators). While some investment advisers are introduced to new foreign investors by foreign entities subject to AML/CFT obligations (such as a broker-dealer), this practice is not consistent, as other introducers or promoters may be individuals with no AML/CFT obligations.

2. Illicit Finance Threats to Investment Advisers

Treasury, in coordination with Federal law enforcement and consultation with the SEC, conducted a comprehensive assessment of illicit finance risk in the investment adviser industry. Treasury's review included an analysis of SARs filed between 2013 and 2021 that were associated with RIAs and ERAs.[69] That analysis found that 15.4 percent of RIAs and ERAs were associated with or referenced in at least one SAR (*i.e.,* they were identified either as a subject or in the narrative section of the SAR) during this time. Further, the number of SAR filings associated with an RIA or ERA increased by approximately 400 percent between 2013 and 2021—a disproportionately higher increase than the overall increase in SAR filings, which was approximately 140 percent.[70]

This SAR analysis, along with a review of law enforcement cases and other information available to the U.S. government, identified several illicit finance threats involving RIAs and ERAs. First, in some instances, the investment adviser industry has served as an entry point into the U.S. market for illicit proceeds associated with foreign corruption, fraud, and tax evasion. Second, certain advisers manage billions of dollars ultimately controlled by Russian oligarchs and their associates who help facilitate Russia's illegal and unprovoked war of aggression against Ukraine. Third, certain RIAs and ERAs and the private funds they advise are also being used by foreign states, most notably the People's Republic of China (PRC) and Russia, to access certain technology and services with long-term national security implications through investments in early-stage companies.

(a) Laundering of Illicit Proceeds Through Investment Advisers and Private Funds

Private funds can be a particularly attractive entry point for illicit proceeds because they present a possibility of high returns, in contrast to other, more costly forms of money laundering, such as trade-based money laundering or informal value transfer systems. Like other types of pooled accounts or legal entities, they can be used to obscure the names of individual investors or beneficial owners so that the investment fund is identified as the owner of a particular asset. However, there are a wide variety of private funds, and some have characteristics that have traditionally been seen as less attractive to money launderers. For instance, some hedge funds may have lock-up periods of more than a year while venture capital funds and private equity funds may not permit any withdrawals due to the time it takes for the private companies in which those funds invest to go public or otherwise provide an exit strategy for these funds. While these restrictions may deter criminals who need immediate access to illicit

[66] *See* Caribbean Financial Action Task Force Mutual Evaluation of the Cayman Islands (Mar. 2019), p. 26, 30–31, *https://www.fatf-gafi.org/media/fatf/documents/reports/mer-fsrb/CFATF-Cayman-Islands-Mutual-Evaluation.pdf.* While a fund may be domiciled or registered in the Cayman Islands, the adviser managing that fund may be located in the United States and/or registered with the SEC.

[67] *Id.* at pp. 135–140 (Cayman Islands received the lowest possible rating for supervision). Additionally, fund administrators in the Cayman Islands filed only 37 SARs in 2017. *Id.* at p. 117.

[68] *See* SEC, Private Fund Statistics, Fourth Calendar Quarter 2022, *https://www.sec.gov/files/investment/private-funds-statistics-2022-q4.pdf.*

[69] Information derived from an analysis of select BSA reporting.

[70] From a FinCEN review of the total number of SARs filed between 2013 and 2021.

proceeds, they are unlikely to deter wealthy corrupt foreign actors who seek stable returns, and have a medium- to long-term investment horizon, and do not need immediate access to capital.

The mechanisms for laundering illicit proceeds through investment advisers and private funds vary, but generally consist of obscuring the illicit origins of funds and pooling them with legitimate funds to invest in U.S. securities, real estate, or other assets.

In one significant case involving funds stolen from the Malaysian government, an RIA was used to launder illicit proceeds into the U.S. financial system. In December 2012, investment funds affiliated with Low Taek Jho (Low) laundered approximately $150 million diverted from 1Malaysia Development Berhad's (1MDB) 2012 bond issuance into the U.S. financial system. Low was CEO of Jynwel Capital Limited, an investment adviser to a private equity fund in Asia.[71] Through a subsidiary of Jynwel Capital Limited, Low purchased equity interests in a vehicle managed by the Electrum Group, a private equity firm in the United States ''whose offices are located in New York and Colorado, invests in public and private companies involved in the exploration and development of natural resources, precious metals, base metals, and oil and gas.'' [72] Electrum Group, LLC is registered with the SEC as an RIA. To conceal their origin, the funds were moved through multiple accounts owned by different entities on or about the same day in an unnecessarily complex manner with no apparent business purpose. This illustrates the general problem: without an obligation to determine the source of wealth and purpose for a customer, an investment adviser may unwittingly permit illicit funds to enter the U.S. financial system.[73]

In some instances, the investment adviser or other financial professional may form a private fund through which illicit proceeds can be transferred as part of a money laundering scheme. While past examples have featured investment advisers complicit in illegal activity, an investment adviser may be unwittingly complicit in this type of activity if they are not required to understand the origin of funds or nature of their owner. A customer wishing to launder money could ask an investment adviser to establish a private fund to certain specifications without informing the adviser of the customer's broader scheme. Without an obligation to report potential money laundering or other illicit finance activity, the adviser could participate without inquiring further.

In July 2018, U.S. law enforcement arrested two alleged participants, Matthias Krull and Gustavo Adolfo Hernandez Frieri (Hernandez), in a billion-dollar international scheme to launder funds obtained through embezzlement, fraud, and bribery from Venezuelan state-owned oil company Petroleos De Venezuela S.A. (PDVSA).[74] According to the stipulated factual proffer filed in connection with his plea agreement, Hernandez conspired to launder approximately $12 million in PDVSA bribe proceeds by creating a private fund, domiciled in the Cayman Islands, and with a U.S. bank as custodian.[75] Specifically, he admitted that he conspired to launder $7 million in bribe payments related to a loan scheme, and $5 million in bribe payments related to a separate currency exchange scheme, through his investment advisory firm located in the United States. Separately, a co-conspirator in the scheme set up fraudulent bond schemes in which fake bonds would be issued, money transferred into the private fund, and then the bonds would ''default.'' [76] While in this instance the adviser was complicit in the fraudulent scheme, a client could also direct an unwitting investment adviser to create a private fund to specifications that facilitate money laundering. In the absence of an AML/CFT program requirement for investment advisers, the investment adviser might not have any obligation to evaluate such risks.

(b) Russian Political and Economic Elites' Access to U.S. Investments

Investment advisers and private funds they advise have served as an important entry point into the U.S. financial system for wealthy Russians seeking to obscure their ownership of U.S. assets.[77] Although many of these Russian individuals were not sanctioned by the U.S. Government prior to Russia's full-scale invasion of Ukraine in February 2022, their wealth was sometimes associated with corruption, theft of state assets, or other illicit activity well before their designation.

A Treasury review of select BSA reporting filed between January 2019 and June 2023 identified more than 20 investment advisers located in the United States advising private funds where the adviser was identified as having significant ties to Russian oligarch investors or Russian-linked illicit activities. This review also identified 60 additional investment advisers located in the United States who managed private funds in which identified Russian oligarchs have invested, although there was no indication the adviser was engaged in any illicit activity.

According to information available to the U.S. government, often, a member of the Russian elite or their trusted proxy invests in a public or private U.S. company with the assistance of a wealth management firm, which is usually located in an offshore jurisdiction such as Bermuda, the Caymans, or Cyprus, but services primarily Russian customers. The wealth management firm invests that money in dollars through the U.S. financial system, often into U.S. technology companies in fields including biotechnology and artificial intelligence. The scale of these investments is significant and may include billions of dollars invested for a single Russian oligarch. These investments are sometimes made directly by the foreign wealth management firm, and in other instances through a U.S.-based RIA or ERA.

[71] Low represented to counterparties and potential business partners that Jynwel Capital Limited was an investment adviser to a private equity fund.

[72] Verified Compl. for Forfeiture (Dkt. 3) ¶ 760, *United States* v. *Real Property Located in London, United Kingdom Titled in the Name of Red Mountain Global Ltd.,* No. 19–cv–1326, (C.D. Cal. Feb. 22, 2019), *https://www.justice.gov/opa/press-release/file/1134376/download.*

[73] *See id.* ¶ 204–12.

[74] Department of Justice, ''Former Swiss Bank Executive Pleads Guilty to Role in Billion-Dollar International Money Laundering Scheme Involving Funds Embezzled from Venezuelan State-Owned Oil Company,'' (Aug. 22, 2018), *https://www.justice.gov/opa/pr/former-swiss-bank-executive-pleads-guilty-role-billion-dollar-international-money-laundering;* Department of Justice, ''Two Members of Billion-Dollar Venezuelan Money Laundering Scheme Arrested'' (Jul. 25, 2018), *https://www.justice.gov/opa/pr/two-members-billion-dollar-venezuelan-money-laundering-scheme-arrested.* In August 2018, Krull pleaded guilty to one count of conspiracy to commit money laundering, and in November 2019, Hernandez, a former investment adviser, also pleaded guilty to conspiracy to commit money laundering in connection with his role in the scheme. Plea Agreement (Dkt. 163), *United States* v. *Hernandez,* (S.D. Fl. Nov. 26, 2019), *https://www.justice.gov/criminal-fraud/file/1316826/download.*

[75] Factual Proffer (Dkt. 164), *United States* v. *Hernandez,* No. 18–cr–20685 (S.D. Fl. Nov. 26, 2019), *https://www.justice.gov/criminal-fraud/file/1316831/download.*

[76] Criminal Compl., *United States* v. *Guruceaga* ( ), 18–mj–3119 (S.D. Fl. Jul. 24, 2018), *https://www.justice.gov/criminal-fraud/file/1119981/download.*

[77] *See* FinCEN Alert, FIN–2023–Alert002, *FinCEN Alert on Potential U.S. Commercial Real Estate Investments by Sanctioned Russian Elites, Oligarchs, and Their Proxies,* p.4 (Jan. 25, 2023). In addition to Russian investors, investors tied to China and Saudi Arabia have invested in U.S. private funds. *See, e.g.,* The German Marshall Fund of the United States, *Policy Brief: An Effective American Regime to Counter Illicit Finance* (Dec. 2018), *https://securingdemocracy.gmfus.org/wp-content/uploads/2018/12/An-Effective-American-Regime-to-Counter-Illicit-Finance.pdf.*

In other instances, funds may be routed through a consulting firm or other entity acting as an investment adviser but not registered with or reporting to the SEC or State regulator. For instance, on September 19, 2023, the SEC announced charges against Concord Management LLC (Concord) and its owner and principal, Michael Matlin, for operating as unregistered investment advisers to their only client—a wealthy former Russian official widely regarded as having political connections to the Russian Federation.[78] As of January 2022, Concord and Matlin allegedly managed investments for their sole client with an estimated total value of $7.2 billion in 112 different private funds.

(c) Foreign State Actors Exploiting Investment Advisers To Threaten U.S. National Security

Some strategic nation-state competitors to the United States, most notably the PRC, may see private funds as a back door to acquire assets of interest in the United States, such as equity stakes in companies developing critical or emerging technologies. While there are certain transactions for which notice must be provided to the interagency Committee on Foreign Investment in the United States (CFIUS),[79] most transactions reviewed by CFIUS are filed voluntarily.[80] Where transactions are not voluntarily submitted to CFIUS for review, CFIUS agencies actively work to identify those transactions, including whether such transactions may be a covered transaction under the CFIUS regulations and may raise national security considerations, and assess whether to request that the parties file with CFIUS.[81]

Foreign state-funded investment vehicles may seek to hide their involvement in foreign investments through offshore legal entities and intermediaries in an effort to gain access to sensitive technology, processes, or knowledge that can enhance their domestic development of microelectronics, artificial intelligence, biotechnology and biomanufacturing, quantum computing, and advanced clean energy, among others. These state-funded investment vehicles could persuade an investment adviser to a private fund to grant them access to granular details about the technology or processes used by a company in which the fund is invested, including information that a limited partner investor seeking only an economic return may not typically request.

PRC. According to the Federal Bureau of Investigation (FBI), the PRC government routinely conceals its ownership or control of investment funds to disguise efforts to steal technology or knowledge and avoid notice to CFIUS.[82] According to a report by the Office of the U.S. Trade Representative, State-guided PRC venture capital fund activity in the United States is motivated by the Made in China 2025 plan and the military-civil fusion strategy, directing investments towards developing technology with dual-use capabilities.[83] In 2016, the PRC government explicitly endorsed the use of overseas venture capital funds to invest in ''seed-based and start-up technology,'' demonstrating the link between the funds and government priorities.[84]

Russia. According to information available to the U.S. government, Russian elites and government entities are moving hundreds of millions of dollars annually through the U.S. financial system by using U.S. and foreign venture capital firms to invest in U.S. technology companies. A Treasury review of select BSA reporting identified several U.S. venture capital firms with significant ties to Russian oligarch investors that invested in firms developing emerging technologies with national security applications. These include autonomous vehicle technology and artificial intelligence systems, as well as contractors to the U.S. military, intelligence, and other government agencies. Further, according to information available to the U.S. government, the U.S.-designated, state-owned Russian Venture Company, which is funded by the U.S.-designated Russian Direct Investment Fund, endows Russian seed funds to invest in emerging technology. The seed funds create a venture capital company, often of a similar name to the seed fund and registered outside of Russia, to invest in U.S. technology firms. The U.S. government has also identified instances where the leadership of certain investment firms has attempted to remove overt ties to Russia or Russian names. Russian investors have obfuscated their connections to Russia, including by relocating to other jurisdictions and changing their names, to continue investing in U.S. technology companies through venture capital vehicles.

D. Prior Rulemaking and Regulatory Guidance

FinCEN has previously proposed AML regulations for investment advisers. On September 26, 2002, FinCEN published an NPRM proposing to require that unregistered investment companies, to include private funds, establish AML programs (Proposed Unregistered Investment Companies Rule).[85] This was followed by the May 5, 2003 NPRM proposing to require certain investment advisers to establish AML programs (First Proposed Investment Adviser Rule).[86] Both of these proposed rules would have defined these entities as ''financial institutions'' under the BSA and required the implementation of AML programs only; they did not propose suspicious activity reporting requirements.

In June 2007, FinCEN announced that it would be taking a fresh look at how its broader AML regulatory framework was being implemented to ensure that it was being applied effectively and efficiently across the industries covered

[78] In March 2022, the United Kingdom and the European Union sanctioned Matlin and Concord's client and the client's assets were subsequently frozen. The SEC's complaint alleges that, a month prior, in February 2022, Concord and Matlin assisted the client in his attempts to redeem investments and/or sell his securities portfolio. *See* SEC, Press Release 2023–186, *SEC Charges New York Firm Concord Management and Owner with Acting as Unregistered Investment Advisers to Billionaire Former Russian Official* (Sep. 19, 2023).

[79] CFIUS is an interagency committee authorized to review certain transactions involving foreign investment in the United States in order to determine the effect of such transactions on the national security of the United States.

[80] *See* Treasury, ''Remarks by Assistant Secretary for Investment Security Paul Rosen at the Second Annual CFIUS Conference,'' (Sept. 14, 2023), *https://home.treasury.gov/news/press-releases/jy1732.*

[81] *Id.*

[82] *See* Hearing Before the U.S.-China Economic and Security Review Commission, p.139, ''Chinese Investments in the United States: Impacts and Issues for Policymakers'' Jan. 26, 2017, *https://www.uscc.gov/sites/default/files/transcripts/Chinese%20Investment%20in%20the%20United%20States%20Transcript.pdf; see also* Remarks by FBI Director Christopher Wray, ''Countering Threats Posed by the Chinese Government Inside the U.S.,'' Jan. 31, 2022, *https://www.fbi.gov/news/speeches/countering-threats-posed-by-the-chinese-government-inside-the-us-wray-013122.*

[83] Office of the United States Trade Representative, ''Findings of the Investigation into China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation under section 301 of the Trade Act of 1974,'' Mar. 22, 2018, 14–15 & 95–96, *https://ustr.gov/sites/default/files/Section%20301%20FINAL.PDF.*

[84] PRC State Council, ''National 13th Five-Year Plan for the Development of Strategic Emerging Industries,'' Nov. 29, 2016, *https://cset.georgetown.edu/publication/national-13th-five-year-plan-for-the-development-of-strategic-emerging-industries/#:~:text=During%20the%2013th%20Five%2DYear,healthy%20economic%20and%20social%20development.*

[85] *See* FinCEN, *Anti-Money Laundering Programs for Unregistered Investment Companies,* 67 FR 60617 (Sept. 26, 2002).

[86] *See* FinCEN, *Anti-Money Laundering Programs for Investment Advisers,* 68 FR 23646 (May 5, 2003).

by the BSA.[87] In conjunction with this initiative, and given the amount of time that had elapsed since initial publication of the Proposed Unregistered Investment Companies Rule and the First Proposed Investment Adviser Rule, FinCEN determined that it would not proceed to apply AML requirements for these entities without undertaking further public notice and comment, and therefore withdrew the proposed rules on November 4, 2008.[88]

On September 1, 2015, FinCEN published an NPRM ''to prescribe minimum standards for . . . [AML] programs to be established by certain investment advisers and to require such investment advisers to report suspicious activity to FinCEN pursuant to the . . . BSA'' (Second Proposed Investment Adviser Rule).[89] This proposed rule would have included RIAs within the definition of ''financial institution'' under the BSA and required them to maintain AML programs, report suspicious activity, and comply with other travel and recordkeeping requirements. The Second Proposed Investment Adviser Rule would not have included ERAs as financial institutions under the BSA.

Since 2015, the investment adviser industry has seen substantial growth in assets under management and the expansion of new products and services. At the time the Second Proposed Investment Adviser Rule was published, there were approximately 12,000 RIAs reporting approximately $67 trillion in AUM.[90] As of June 30, 2023, that number had grown to more than 15,000 RIAs with approximately $125 trillion in AUM.[91]

Private funds play an increasingly important role in the financial system and continue to grow in size, complexity, and number. For example, hedge funds engage in trillions of dollars in listed equity and futures transactions each month. Private equity and other private funds are involved in mergers and acquisitions, non-bank lending, and corporate restructurings through leveraged buyouts and bankruptcies. Venture capital funds provide funding to start-ups and early-stage companies. There are approximately 5,500 RIAs who advise more than $20 trillion in private fund AUM.[92] Over the past five years alone, the number of private equity funds advised by RIAs increased 60 percent to more than 24,000, while the number of venture capital funds advised by RIAs increased by almost 300 percent, to more than 3,300 funds.[93]

Since 2015, the U.S. Government has also developed a more detailed understanding of the illicit finance risks associated with the U.S. investment adviser industry. As described in section II, investment advisers have been exploited by sophisticated criminals, Russian oligarchs, and U.S. strategic competitors.

Although the Second Proposed Investment Adviser Rule was not formally withdrawn,[94] Treasury does not intend to issue a final rule based on it and is hereby withdrawing the Second Proposed Investment Adviser Rule. Treasury is issuing this new NPRM to ensure that changes in the risk and factual context relevant to the rulemaking since the Second Proposed Investment Adviser Rule was published are taken into account.

III. Scope of Proposed Rule

For all the reasons described above, FinCEN is proposing to cover both RIAs and ERAs as ''financial institutions'' subject to AML/CFT requirements. FinCEN is not proposing to cover State-registered investment advisers because the Treasury risk assessment found few examples of State-registered investment advisers being misused for money laundering, terrorist financing, or other illicit financial activities.[95] However, FinCEN will continue to monitor activity involving State-registered investment advisers for indicia of money laundering, terrorist financing, or other illicit finance activities, and may take appropriate steps to mitigate any such activity.

As discussed further below, this proposed rulemaking does not impose a CIP requirement or a general requirement that investment advisers identify and verify the beneficial ownership of legal entity customers. Accordingly, the proposed rule would not subject investment advisers to beneficial ownership information identification and verification requirement under 31 CFR 1010.230.[96] Under the BSA, any CIP requirement for financial institutions that engage in financial activities described in section 4(k) of the Bank Holding Company Act ''shall be prescribed jointly with each Federal functional regulator.'' [97] This list of activities includes, among others, ''providing financial, investment, or economic advisory services.'' [98] Pursuant to these provisions, any future application of CIP requirements would be proposed jointly with the SEC in a separate rulemaking. In addition, FinCEN intends to amend the CDD Rule to bring it into conformance with the Corporate Transparency Act.[99]

IV. Section-by-Section Analysis

FinCEN is proposing to: (1) include certain types of investment advisers (both RIAs and ERAs) within the definition of ''financial institution'' in the regulations implementing the BSA, and add a definition of investment adviser to reflect those covered types; and (2) require such investment advisers to (a) establish AML/CFT programs, to include risk-based procedures for conducting ongoing CDD; (b) report suspicious activity and file CTRs; (c) maintain records of originator and beneficiary information for certain transactions; (d) apply information-sharing provisions between and among FinCEN, law enforcement, agencies, and certain financial institutions; and (e) implement special due diligence requirements for correspondent and private banking accounts and special measures under section 311 of the USA PATRIOT Act. These proposals are discussed in greater detail below.

A. Definitions

FinCEN is proposing two changes to 31 CFR 1010.100, the general definitions section of its regulations. First, this proposed rule would amend 1010.100(t) to add ''investment adviser'' to the definition of ''financial institution.''

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[87] *See* FinCEN, *Withdrawal of the Notice of Proposed Rulemaking; Anti-Money Laundering Programs for Unregistered Investment Companies,* 73 FR 65569 (Nov. 4, 2008); and FinCEN, *Withdrawal of the Notice of Proposed Rulemaking; Anti-Money Laundering Programs for Investment Advisers,* 73 FR 65568 (Nov. 4, 2008).

[88] *Id.*

[89] *See* FinCEN, *Anti-Money Laundering Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers,* 80 FR 52680 (Sept. 1, 2015).

[90] Based on a Treasury review of Form ADV data as of December 31, 2015.

[91] *See supra* n. 26.

[92] *Id.*

[93] IAA Snapshot, *supra* n. 19 at Table 5E.

[94] Treasury withdrew the proposal from the Fall 2020 Unified Agenda. *See Anti-Money Laundering Program and Suspicious Activity Reporting Filing Requirements for Investment Advisers,* available at *https://www.regulations.gov/docket/FINCEN-2014-0003/unified-agenda.*

[95] *See* Treasury, *Investment Adviser Illicit Finance Risk Assessment, https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.pdf.*

[96] As described below, the proposed revised § 1010.605(e)(1) would expressly provide that an investment adviser would not be considered a ''covered financial institution'' for the purposes of § 1010.230. *See infra* section IV.H.1.

[97] 31 U.S.C. 5318(*l*)(4).

[98] 12 U.S.C. 1843(k)(4)(C).

[99] FinCEN is required to revise the CDD Rule under the Corporate Transparency Act. Sec. 6403(d)(1), AML Act. (''Not later than 1 year after the effective date of the regulations promulgated under section 5336(b)(4) of title 31, United States Code, as added by subsection (a) of this section, the Secretary of the Treasury shall revise the final rule entitled 'Customer Due Diligence Requirements for Financial Institutions' . . . .'').

Second, it would add a new provision to 1010.100 defining the term ''investment adviser.''

1. Adding ''Investment Adviser'' to the ''Financial Institution'' Definition

The BSA expressly defines various entities as ''financial institutions,'' [100] while also providing Treasury with the authority to define additional entities as financial institutions in its regulations at 31 CFR 1010.100(t). Specifically, the BSA authorizes FinCEN to define additional types of businesses as financial institutions if FinCEN determines that such businesses engage in any activity ''similar to, related to, or a substitute for'' activities in which any of the enumerated financial institutions are authorized to engage.[101] Although ''investment adviser'' is not one of the specifically enumerated financial institutions in the BSA, FinCEN is proposing to make such a determination with respect to the defined set of investment advisers, and thereby add investment advisers to § 1010.100(t)'s definition of financial institution.

Investment advisers provide services that are similar or related to services authorized to be provided by BSA-defined financial institutions. Many investment advisers provide advice to clients who have granted the adviser the power to manage assets on a discretionary basis, which is similar or related to services provided by other BSA-defined institutions, such as broker-dealers or banks. Indeed, many investment advisers provide asset management services that are similar to, and often substituted for, the asset management services that are provided by banks and other financial institutions, such that advisers may compete directly with asset management services provided by certain banks. Investment advisers also often provide services that can substitute for certain products offered by investment companies or insurance companies. For example, investment advisers can sponsor and provide advisory services to pooled investment vehicles such as private funds. As another example, many investment advisers sponsor and provide advisory services to mutual funds and advise on the purchase or sale of mutual fund shares, similar to banks or broker dealers that provide recommendations on mutual fund shares.

Moreover, investment advisers often work closely with, or are otherwise closely associated with, BSA-defined financial institutions. For example, investment advisers work closely with financial institutions when they direct broker-dealers to purchase or sell client securities, and therefore engage in activities that are closely related to the activities of covered financial institutions. In addition, investment advisers are frequently owned by or under common ownership with banks, broker-dealers, and other financial institutions. For example, approximately 20 percent of RIAs and seven percent of ERAs are dually registered as a broker-dealer, licensed as a bank, or affiliated with a bank or broker dealer.[102] Investment advisers typically rely on broker-dealers, banks, and other financial institutions to perform vital functions for them, such as retaining custody of client funds or executing trades of securities.[103] Broker-dealers may recommend securities transactions to customers as well.[104] Accordingly, even investment advisers that lack direct relationships with banks, broker-dealers, or other types of financial institutions engage in activities that are ''similar to'' the types of services authorized to be provided by certain financial institutions.

Further, legislative history during drafting of the USA PATRIOT Act indicates that RIAs are sufficiently similar to certain other financial institutions that Treasury could require them to file SARs: ''The Committee [on Financial Services] notes that, under the Bank Secrecy Act, the Secretary currently has the authority to require Suspicious Activity Reports for all entities similar to futures commission merchants, commodity trading advisors, and commodity pool operators, namely registered investment advisers and registered investment companies.'' [105]

Accordingly, FinCEN hereby determines that investment advisers engage in activities that are ''similar to, related to, or a substitute for'' financial services that other BSA-defined financial institutions are authorized to engage in and, therefore, may be properly included as a ''financial institution'' subject to the requirements of the BSA.

2. Adding a Definition of ''Investment Adviser''

FinCEN is also proposing to add a definition of ''investment adviser'' to 31 CFR 1010.100 to clearly define who qualifies as a covered adviser—and thus as a ''financial institution'' under these proposed amendments to FinCEN regulations. The proposed definition of ''investment adviser'' is: ''[a]ny person who is registered or required to register with the SEC under section 203 of the Advisers Act (15 U.S.C. 80b–3(a)), or any person that currently is exempt from SEC registration under section 203(*l*) or 203(m) of the Investment Advisers Act (15 U.S.C. 80b–3(*l*), (m)).'' [106] In other words, under this proposed definition, an investment adviser would be any RIA (those registered or required to register) or ERA (those exempt from SEC registration under the listed provisions).

The proposed definition relies on well-established and understood terms and definitions used in the Advisers Act and its implementing regulations to define who would be an investment adviser under FinCEN regulations. FinCEN believes that incorporating existing and well-understood regulatory definitions into its definition of investment adviser would simplify the investment advisers' determinations as to whether they are subject to the proposed requirements. FinCEN requests comment on whether the proposed definition of ''investment adviser'' is sufficiently clear, or whether some other definition may be preferable. FinCEN also requests comment on whether the proposed definition includes classes of investment advisers or certain services or activities provided by investment advisers that present a very low risk for money laundering,

[100] 31 U.S.C. 5312(a)(2), (c)(1).

[101] 31 U.S.C. 5312(a)(2)(Y). FinCEN may also designate businesses ''whose cash transactions have a high degree of usefulness in criminal, tax, or regulatory matters'' as financial institutions. *Id.* 5312(a)(2)(Z).

[102] *See supra* n. 26.

[103] *See, e.g.,* SEC, *Commission Interpretation Regarding Standard of Conduct for Investment Advisers,* Investment Advisers Act Release No. 5248 (Jun. 5, 2019), 84 FR 33669, 33674–75 (Jul. 12, 2019) (discussing an investment adviser's duty to seek best execution of a client's transactions where the investment adviser has the responsibility to select broker-dealers to execute client trades)

[104] *See* 15 U.S.C. 80b–2(a)(11)(C) (excluding from the definition of ''investment adviser'' under the Advisers Act any broker or dealer whose performance of advisory services is ''solely incidental to the conduct of his business as a broker or dealer and [the broker or dealer] receives no special compensation therefor''); *see also* SEC, *Commission Interpretation Regarding the Solely Incidental Prong of the Broker-Dealer Exclusion from the Definition of Investment Adviser,* Investment Advisers Act Release No. 5249 (Jun. 5, 2019), 84 FR 33681 (Jul. 12, 2019). 17 CFR 240.15*l*–1.

[105] House Report 107–250(I), *Financial Anti-Terrorism Act of 2001,* 2001 WL 1249988 at *66 (Oct. 17, 2001); *see also* Public Law 107–31, Title III section 321 (Oct. 26, 2001) (section of USA PATRIOT Act adding futures commission merchants, commodity trading advisors, and commodity pool operators to the definition of ''financial institutions'' for purposes of 31 U.S.C. 5312(a)).

[106] *See* 15 CFR 275.203(*l*)–1; 15 CFR 275.203(m)–1.

terrorist financing, or other illicit finance activity such that they should be excluded from the definition, or whether the proposed definition fails to include a type of adviser that presents a risk.

(a) Registered Investment Advisers

Including RIAs within the proposed definition of investment adviser would align FinCEN's regulatory framework with the existing framework under the Advisers Act and would also allow FinCEN to work with the SEC to develop consistent application and examination of the AML/CFT requirements to such advisers. Generally, an investment adviser's amount of assets under management determine whether it is required to register or is prohibited from registering with the SEC.[107] In implementing the Dodd-Frank Act amendments to the Advisers Act, the SEC amended the instructions to Part 1A of Form ADV to further implement a uniform method for an investment adviser to calculate its assets under management in order to determine whether it is required to register or is prohibited from registering with the SEC.[108] Per the Dodd-Frank Act and SEC rules, a ''large'' adviser has $110 million or more in regulatory assets under management, and is required to register with the SEC. These are RIAs that would be included in the investment adviser definition in the proposed rule.[109] FinCEN notes that large advisers would comprise a substantial majority of the total number of investment advisers that are included in the definition of investment adviser for purposes of the proposed rule.[110] FinCEN requests comment on whether the definition of investment adviser should apply to non-U.S. advisers registered or required to register with the SEC, or who report to the SEC on Form ADV.

(b) Exempt Reporting Advisers

FinCEN is also including ERAs in the definition of investment adviser under the proposed rule for the reasons described in section II.C above. In addition, ERAs have less detailed reporting requirements than RIAs, are not required to file Form PF, and are not examined by the SEC on a regular basis.[111] Further, exempt venture capital advisers are able to rely on a registration exemption that is not limited by the amount of AUM. FinCEN requests comment on whether ERAs should be excluded from the proposed definition of ''investment adviser,'' and if ERAs are excluded, how could FinCEN otherwise address the money laundering, terrorist financing, and other illicit finance risk associated with ERAs. FinCEN also requests comment on whether there are differences in the risks associated with ERAs who advise private funds versus those that advise venture capital funds.

(c) Other Investment Advisers

FinCEN recognizes that different investment advisers included within the proposed definition may have different degrees of money laundering, terrorist financing, or other illicit finance risk. As discussed at greater length below, the AML/CFT program requirement is risk-based, and FinCEN anticipates that the burden of establishing an AML/CFT program, filing SARs, and complying with the other requirements of the proposed rule would be commensurate with an adviser's risk profile. As noted, the proposed definition of ''investment adviser'' would include certain non-U.S. investment advisers that are physically located abroad (*i.e.,* do not have a branch, office, or staff in the United States), but are nonetheless registered or required to register with the SEC (for RIAs) or file Form ADV (for ERAs). Coverage of these non-U.S. investment advisers is discussed further at section IV.E.7.

While FinCEN is limiting the proposed definition to RIAs and ERAs, FinCEN recognizes that other types of investment advisers or other entities that provide investment advisory services may present risks to the U.S. financial system of money laundering, terrorist financing, and other types of financial crimes, or otherwise pose a threat to U.S. national security. FinCEN, therefore, may consider future rulemakings to expand the application of the BSA to include other investment advisers or similar entities not covered by the proposed definition. FinCEN requests comment on whether other types of investment advisers or entities should also be subject to the proposed rule.

B. Delegation of Examination Authority to the Securities and Exchange Commission

FinCEN has overall authority for enforcement of compliance with the BSA and its implementing regulations.[112] FinCEN, however, may delegate examination authority to appropriate agencies while retaining authority for the coordination and direction of procedures and activities of these agencies.[113] FinCEN has previously delegated examination authority for various financial institutions, as reflected at 31 CFR 1010.810(b).

FinCEN is proposing to amend 31 CFR 1010.810(b) to add investment advisers to the list of financial institutions for which the SEC has the authority to examine for compliance with FinCEN's regulations implementing the BSA. Persons and entities meeting the proposed definition of investment adviser thus would fall under this provision and be subject to SEC examination for compliance with FinCEN regulations. The SEC has expertise in the regulation of investment advisers. The SEC is the Federal functional regulator for certain investment advisers and is responsible for examining investment advisers for compliance with the Federal securities laws, including the Advisers Act and the SEC rules promulgated under those laws.[114] Moreover, FinCEN has delegated to the SEC examination authority for broker-dealers in securities and certain investment companies, which are BSA-defined financial institutions subject to FinCEN's regulations and for which the SEC is the Federal functional regulator.[115]

Accordingly, the proposed rule would designate the SEC as examiner of investment advisers for compliance with the proposed rule.

C. Investment Advisers' Proposed Obligation To File CTRs Instead of Form 8300

Under FinCEN's regulations that apply to a broad range of persons—not just financial institutions—investment

[107] *See* SEC, *Rules Implementing Amendments to the Investment Advisers Act of 1940,* Investment Advisers Act Release No. 3221 (Jun. 22, 2011), 76 FR 42950, 42955 (Jul. 19, 2011).

[108] *See id.; see also* Instructions for Part 1A, Item 5.F of Form ADV.

[109] An investment adviser that is registered with the SEC on a basis other than its AUM would also be an ''investment adviser'' under the proposed rule and subject to the proposed requirements.

[110] Generally, a mid-sized adviser has $25 million or more but less than $110 million in regulatory assets under management and is registered with the State where it maintains its principal office and place of business. A small adviser has less than $25 million in regulatory assets under management and is regulated or required to be regulated in the State where it maintains its principal office and place of business. *See* 15 U.S.C. 80b–3A(a)(1). Mid-sized and small advisers are generally prohibited from registering with the SEC, unless an exemption from the prohibition on SEC registration is available (*see* 17 CFR 275.203A–2), and therefore are unlikely to be covered by the proposed definition of ''investment adviser'' in the proposed rule as RIAs.

[111] *See* 76 FR 42950, 42963, n.188.

[112] Treasury Order 180–1, para. 3; 31 CFR 1010.810(a).

[113] Treasury Order 180–1, paras. 3(b), 4(b); 31 CFR 1010.810(a); 31 U.S.C. 5318(a)(1).

[114] *See* 15 U.S.C. 6809(2)(F); 31 CFR 1010.100(r)(6); *see also* 15 U.S.C. 80b–1 *et seq.* and the rules thereunder, 17 CFR part 275.

[115] *See* 31 CFR 1010.810(b)(6).

advisers are currently required to file reports for the receipt of more than $10,000 in currency and certain negotiable instruments using joint FinCEN/Internal Revenue Service Form 8300.[116] By defining investment advisers as ''financial institutions'' under the BSA, the proposed rule would require investment advisers to file CTRs with FinCEN pursuant to 31 CFR 1010.311 instead of filing reports using Form 8300.[117]

The BSA authorizes FinCEN to promulgate regulations requiring financial institutions to file reports when they participate in certain types of financial transactions.[118] Pursuant to this authority, 31 CFR 1010.311 requires ''financial institutions'' (other than casinos) to file CTRs for ''each deposit, withdrawal, exchange of currency or other payment or transfer, by, through, or to such financial institution which involves a transaction in currency of more than $10,000,'' unless subject to an applicable exemption. FinCEN seeks to extend this requirement to investment advisers under the proposed rule. This proposed rule would also add several provisions, §§ 1032.310 to 1032.315, specifying how investment advisers should fulfill their proposed CTR obligations.

The threshold in 31 CFR 1010.311 applies to transactions in currency of more than $10,000 conducted during a single business day.[119] A financial institution must treat multiple transactions conducted in one business day as a single transaction if the financial institution has knowledge that the transactions are conducted by or on behalf of the same person.[120] This same requirement would extend to investment advisers.

To avoid duplicative requirements, investment advisers would no longer have to report applicable transactions involving certain negotiable instruments reportable on Form 8300. Moreover, since an investment adviser would be required to report suspicious transactions under the SAR rule proposed in this rulemaking, investment advisers would no longer need to use Form 8300 to voluntarily report suspicious transactions.[121] Finally, imposing CTR and SAR requirements rather than a Form 8300 requirement is consistent with the obligations of certain other financial institutions, such as banks, broker-dealers, and mutual funds.

D. Proposed Recordkeeping Requirements for Investment Advisers

FinCEN has broad authority to impose recordkeeping requirements on financial institutions under the BSA.[122] Pursuant to this authority, FinCEN has issued several recordkeeping regulations, codified as 31 CFR part 1010, subpart D (§§ 1010.400 to 1010.440), which apply broadly to financial institutions, subject to specified exceptions. By defining RIAs and ERAs as financial institutions, this proposed rule would apply these recordkeeping regulations to investment advisers. Specifically, 31 CFR 1032.410 (cross-referencing 31 CFR 1010.410) would require investment advisers to comply with the Recordkeeping and Travel Rules, which are codified at 31 CFR 1010.410(e) and 31 CFR 1010.410(f), respectively, for the purposes of this proposed rule.[123] The proposed regulations would not require investment advisers to comply with these recordkeeping requirements with respect to any mutual fund that it advises.[124]

Under the Recordkeeping and Travel Rules, financial institutions must create and retain records for transmittals of funds and ensure that certain information pertaining to the transmittal of funds ''travels'' with the transmittal to the next financial institution in the payment chain.[125] The Recordkeeping and Travel Rules apply to transmittals of funds that equal or exceed $3,000. With certain exceptions, ''transmittal of funds'' includes funds transfers processed by banks, as well as similar payments where one or more of the financial institutions processing the payment (*e.g.,* the transmittor's financial institution, an intermediary financial institution, or the recipient's financial institution) is not a bank.[126]

When a financial institution accepts and processes a payment sent by or to its customer, then the financial institution would be the ''transmittor's financial institution'' or the ''recipient's financial institution,'' respectively. The Recordkeeping and Travel Rules require the transmittor's financial institution to obtain and retain the name, address, and other information about the transmittor and the transaction.[127] The Recordkeeping Rule also requires the recipient's financial institution (and in certain instances, the transmittor's financial institution) to obtain or retain identifying information on the recipient.[128] And the Travel Rule requires that certain information obtained or retained ''travels'' with the

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[116] 31 CFR 1010.330; 26 CFR 1.6050I–1. ''Currency'' includes cashier's checks, bank drafts, traveler's checks, and money orders in face amounts of $10,000 or less, if the instrument is received in a ''designated reporting transaction.'' 31 CFR 1010.330(c)(1)(ii)(A). A ''designated reporting transaction'' is defined as the retail sale of a consumer durable, collectible, or travel or entertainment activity. 31 CFR 1010.330(c)(2). In addition, an investment adviser would need to treat the instruments as currency if the adviser knows that a customer is using the instruments to avoid the reporting of a transaction on Form 8300. 31 CFR. 1010.330(c)(1)(ii)(B).

[117] *See* 31 CFR 1010.330(a) (stating that § 1010.330 [the BSA provision requiring the filing of the Form 8300] ''does not apply to amounts received in a transaction reported under 31 U.S.C. 5313 and 31 CFR 1010.311.''). To the extent an investment adviser conducts transactions other than in currency (as defined in 31 CFR 1010.100(m) for purposes of the CTR requirement), it would be exempt from reporting such transactions because the Form 8300 requirement does not apply to such transactions.

[118] *See, e.g.,* 31 U.S.C. 5313(a); 31 U.S.C. 5326.

[119] *See* 31 CFR 1010.311, 1010.313(b). Multiple transactions must be treated as a single transaction if they are conducted by or on behalf of the same person and result in cash in or cash out of more than $10,000 during any one business day. A Form 8300, meanwhile, must be filed when currency is received in one transaction or two or more related transactions. Transactions conducted between a payer (or its agent) and a recipient in a 24-hour period would be treated as related. Furthermore, a distinction is drawn between transactions and the receipt of payments. Installment payments made within a period of 12 months may need to be aggregated and reported on a Form 8300. *See* 31 CFR 1010.330(b)(3).

[120] *Id.*

[121] Currently an investment adviser can report a suspicious transaction voluntarily by checking box 1(b) in the Form 8300. In addition to the requirement that an investment adviser report on a CTR, under the proposed rule, an investment adviser would also be required to file a SAR if a suspicious transaction exceeds the threshold amount.

[122] *See* 12 U.S.C. 1953; 31 U.S.C. 5311; and 31 U.S.C. 5312(a)(2).

[123] The Recordkeeping Rule is codified at 31 CFR 1010.410(e) and 1020.410(a), but only 1010.410(e) is relevant here: 1020.410(a) describes the recordkeeping requirements for banks, while those for nonbank financial institutions are described in 1010.410(e). The Travel Rule, as codified at 31 CFR 1010.410(f), applies to both bank and nonbank financial institutions. *See* FinCEN, Board of Governors of the Federal Reserve System, *Amendment to the Bank Secrecy Act Regulations Relating to Recordkeeping for Funds Transfers and Transmittals of Funds by Financial Institutions,* 60 FR 220 (Jan. 3, 1995); FinCEN, *Amendment to the Bank Secrecy Act Regulations Relating to Orders for Transmittals of Funds by Financial Institutions,* 60 FR 234 (Jan. 3, 1995).

[124] Specifically, proposed 31 CFR 1032.400 would permit an investment adviser to deem requirements in Subpart D to be satisfied for any mutual fund it advises that is subject to these same reporting requirements under another provision of Subpart D.

[125] *See* 31 CFR 1010.410(e), (f); 31 CFR 1020.410(a). Financial institutions are also required to retain records for five years. *See* 31 CFR 1010.430(d).

[126] *See* 31 CFR 1010.100(ddd) (defining ''transmittal of funds''); *see also* 31 CFR 1010.100(aa), (qq), (ggg) (defining ''intermediary financial institution,'' ''recipient's financial institution,'' and ''transmittor's financial institution'' to include both bank and nonbank financial institutions).

[127] *See* 31 CFR 1010.410(e)(1)(i), (e)(2).

[128] *See* 31 CFR 1010.410(e)(1)(iii), (e)(3) (information that the recipient's financial institution must obtain or retain).

transmittal order through the payment chain.[129]

Under the proposed rule, however, some transmittals involving investment advisers would fall within an existing exception to the Recordkeeping and Travel Rules designed to exclude transmittals of funds from these Rules' requirements when certain categories of financial institutions are the transmitter and recipient.[130] The proposed application of this exception to investment advisers is intended to provide investment advisers with treatment similar to that of banks, brokers or dealers in securities, futures commission merchants, introducing brokers in commodities, and mutual funds.

Additionally, FinCEN recognizes that investment advisers operate varying business models and, that in some circumstances, an adviser would not conduct transactions that meet the definition of ''transmittal order.'' For example, in some advisory relationships, when an investment adviser receives instructions from a customer, the investment adviser would not ''be reimbursed by debiting an account of, or otherwise receiving payment from,'' the customer, such that the investment adviser's receipt of instructions from a customer would not meet the definition of transmittal order.[131]

Because FinCEN is proposing to include investment advisers in the definition of financial institutions, investment advisers would be required to comply with the Recordkeeping and Travel Rules when they engage in transactions that meet the definition of a transmittal order. FinCEN understands that the collection of at least some of this information would be required for accounting or other purposes and seeks comment on the extent to which investment advisers or other BSA-defined financial institutions regularly collect information that would be required under the Recordkeeping and Travel Rules. Similarly, FinCEN seeks comment on understanding the structures that investment advisers use to be credited by customers who seek to wire funds out of their accounts with the investment adviser. FinCEN seeks comment on how investment advisers work with qualified custodians to maintain separate accounts to manage customers' funds, including for wire transfers. FinCEN is also seeking comment on whether investment advisers should be required to comply with the Recordkeeping and Travel Rules as proposed, or if the Recordkeeping and Travel Rules should only apply in certain circumstances.

Finally, the proposed rule would subject investment advisers to requirements to create and retain records for extensions of credit and cross-border transfers of currency, monetary instruments, checks, investment securities, and credit.[132] These requirements currently apply to transactions by other BSA-defined financial institutions in amounts exceeding $10,000.[133]

E. Anti-Money Laundering and Countering the Financing of Terrorism Programs

The BSA requires financial institutions to establish reasonably designed risk-based AML/CFT programs to combat the laundering of money and financing of terrorism through the institution.[134] The Annunzio-Wylie Anti-Money Laundering Act of 1992 amended the BSA by authorizing Treasury to issue regulations requiring financial institutions, as defined in BSA regulations, to maintain ''minimum standards'' of an anti-money laundering program.[135] These anti-money laundering programs must include, at a minimum, the development of internal policies, procedures, and controls; the designation of a compliance officer; an ongoing employee training program; and an independent audit function to test programs.[136] The USA PATRIOT Act further amended the BSA to expand AML program rules applicable to banks to cover certain other industries.[137] The requirements for an anti-money laundering program were further amended by section 6101(b) of the AML Act of 2020 (AML Act), which among other things, expanded the BSA's program rule requirement to include a reference to CFT in addition to AML.[138] FinCEN intends to implement more specific changes to AML/CFT program requirements as a result of section 6101(b) of the AML Act through a separate rulemaking process.[139] FinCEN does not intend to address those more specific changes as part of this rulemaking.

The BSA authorizes FinCEN, after consultation with the appropriate Federal functional regulator (for investment advisers, the SEC), to further prescribe minimum standards for such AML/CFT programs.[140] In developing this proposed rule, FinCEN consulted and coordinated with the SEC staff, including regarding the statutorily specified factors set out in 31 U.S.C. 5318(h)(2)(B). These factors are:

- financial institutions are spending private compliance funds for a public and private benefit, including protecting the United States financial system from illicit finance risks;
- the extension of financial services to the underbanked and the facilitation of financial transactions, including remittances, coming from the United States and abroad in ways that simultaneously prevent criminal persons from abusing formal or informal financial services networks are key policy goals of the United States;
- effective anti-money laundering and countering the financing of terrorism programs safeguard national security and generate significant public benefits by preventing the flow of illicit funds in the financial system and by assisting law enforcement and national security agencies with the identification and prosecution of persons attempting to launder money and undertake other illicit activity through the financial system;
- anti-money laundering and countering the financing of terrorism programs should be—
  - reasonably designed to assure and monitor compliance with the requirements of the BSA and regulations promulgated under the BSA; and
  - risk-based, including ensuring that more attention and resources of financial institutions should be directed toward higher-risk customers and activities, consistent with the risk profile of a financial institution, rather than toward lower-risk customers and activities.

[129] *See* 31 CFR 1010.410(f) (information that must ''travel'' with the transmittal order); 31 CFR 1010.100(eee) (defining ''transmittal order'').

[130] *See* 31 CFR 1010.410(e)(6), (f)(4); 31 CFR 1020.410(a)(6). As relevant here, § 1010.410(e)(6)(i) excludes from the requirements of the Recordkeeping Rule ''[t]ransmittals of funds where the transmitter and the recipient'' are certain types of listed financial institutions. Section 1010.410(f)(4) excludes these same transmittals from the Travel Rule. The proposed rule would amend § 1010.410(e)(6) to add ''investment advisers'' to its list of financial institutions.

[131] *See* 31 CFR 1010.100(eee)(2).

[132] *See* 31 CFR 1010.410(a)–(c). Financial institutions must retain these records for a period of five years. 31 CFR 1010.430(d).

[133] *See* 31 CFR 1010.410(a)–(c).

[134] 31 U.S.C. 5311(2), 5318(h)(1).

[135] Annunzio-Wylie Anti-Money Laundering Act, Title XV of the Housing and Community Development Act of 1992, Public Law 102–550.

[136] 31 U.S.C. 5318(h)(1)(A)–(D).

[137] Section 352(a) of the Act, which became effective on April 24, 2002, amended 31 U.S.C. 5318(h).

[138] Public Law 116–283 (Jan. 1, 2021); *see* 31 U.S.C. 5318(h)(4)(D) (as amended by AML Act section 6101(b)(2)(C)).

[139] *See* FinCEN Regulatory Agenda (Spring 2023), *Establishment of National Exam and Supervision Priorities,* available at *https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=202304&RIN=1506-AB52.*

[140] 31 U.S.C. 5318(h)(2)(A).

FinCEN has considered these factors in section 5318(h)(2)(B) in the drafting of this proposed rule. In proposing this rule, FinCEN has considered the fact that comprehensive AML/CFT requirements for investment advisers, which would require investment advisers to have effective AML/CFT programs and subject them to SAR reporting requirements, would aid in preventing the flow of illicit funds in the financial system and in assisting law enforcement and national security agencies with the identification and prosecution of those who attempt to launder money and undertake other illicit financial activity. Additionally, FinCEN recognizes that AML/CFT programs at investment advisers should be reasonably designed and risk-based consistent with investment advisers' respective risk profiles, and therefore is proposing an AML/CFT program rule that requires policies, procedures, and internal controls reasonably designed to prevent the investment adviser from being used for money laundering, terrorist financing, or other illicit finance activities, as well as risk-based procedures that consider an investment adviser's risk profile. Further, as discussed in the Regulatory Analysis at section VII, FinCEN has analyzed the financial costs to investment advisers in imposing AML/CFT obligations, including AML/CFT program requirements and SAR filing requirements, and has determined that the public and private benefit to this proposed rule would outweigh the private compliance costs.[141]

This proposed rule, by designating investment advisers as financial institutions, would subject investment advisers to AML/CFT program requirements, as reflected in proposed § 1032.210.[142]

Investment advisers are already subject to other regulations similar in certain ways to the AML/CFT program requirements FinCEN is proposing, and thus should be well-positioned to extend their practices to incorporate proposed AML/CFT requirements. RIAs are currently subject to Federal securities laws, which require the establishment of a variety of policies, procedures, and controls. For example, the Advisers Act requires an RIA to maintain certain books and records, as prescribed by the SEC.[143] Under 17 CFR 275.204–2, an RIA is required to keep certain books and records that relate to its investment advisory business.[144] Under 17 CFR 275.203–1 and 275.204–4, RIAs and ERAs, respectively, are also required to complete and submit Form ADV to the SEC. The Advisers Act also prohibits an investment adviser from engaging in fraudulent, deceptive, and manipulative conduct.[145] SEC rules further require RIAs to adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules that the SEC has adopted under that Act.[146] RIAs must conduct annual reviews to ensure the adequacy and effectiveness of their policies and procedures and must designate a chief compliance officer responsible for administering the policies and procedures.[147] ERAs are also subject to Federal securities laws governing the securities industry, required to complete and submit some sections of Form ADV, and comply with other select requirements of the Advisers Act.[148] While ERAs may not have the full compliance infrastructure that RIAs have, their existing compliance obligations nonetheless offer a point of reference and relevant experience for implementing the AML/CFT requirements in the proposed rule.

As FinCEN has noted, the AML/CFT program requirement is not a one-size-fits-all requirement but rather is risk-based and is intended to give investment advisers the flexibility to design their programs to identify and mitigate the specific risks of the advisory services they provide and the customers they advise. As such, ERAs would be able to tailor their AML/CFT programs to the specific risks, activities, and operations associated with their advisory business. Accordingly, FinCEN contemplates that investment advisers, as defined in the proposed rule, would be able to build upon existing policies, procedures, and internal controls, or the processes undertaken to establish those policies, procedures, and internal controls, to comply with the proposed AML/CFT requirements.

Moreover, some investment advisers have already implemented AML/CFT programs either because they are dually registered as a broker-dealer, licensed as a bank, or affiliated with a broker-dealer or bank, or in conjunction with a SIFMA No-Action Letter permitting broker-dealers to rely on RIAs to perform some or all aspects of broker-dealers' CIP obligations.[149] For instance, according to the 2016 Investment Management Compliance Testing Survey of RIAs conducted by ACA Compliance Group and the Investment Adviser Association, 76 percent of participants had adopted AML policies, and 40 percent of participants had adopted AML programs similar to the AML program requirements proposed in the Second Proposed Investment Adviser Rule.[150] FinCEN requests comment on what CDD procedures RIAs and/or ERAs already have in place to comply with the SIFMA No-Action Letter.

1. Overview of AML/CFT Program Requirement

Section 1032.210(a)(1) of the proposed rule would require each RIA and ERA to develop and implement a written AML/CFT program that is risk-based and reasonably designed to prevent the investment adviser from being used for money laundering, terrorist financing, or other illicit finance activities. Each RIA and ERA would also be required to make its AML/CFT program available for inspection by FinCEN or the SEC. The minimum requirements for the AML/CFT program are set forth in

[141] Further discussion relevant to each factor may be found at: Factor (i): the regulatory impact analysis at section VII and other discussions of the costs and benefits of the proposed rule; Factor (ii): we believe that this factor is not relevant to the proposed rule because investment advisers generally do not provide services to the unbanked, process remittances, or participate in informal financial networks. This may be inferred from the risk discussion at section II.C and accompanying discussions of the structure of the investment advisory industry; and Factor (iii): the risk analysis at section II.C; Factor (iv): the risk analysis at section II.C and the discussion of building upon existing requirements and examination programs in this section and at section IV.B.

[142] Additionally, 31 CFR subpart B contains general provisions applicable generally to financial institutions' AML/CFT programs. Proposed § 1032.200 would subject investment advisers those general provisions in subpart B.

[143] *See* 15 U.S.C. 80b–4(a) (requiring investment advisers to make and retain records as defined in section 3(a)(37) of the Exchange Act and to make and disseminate reports as prescribed by the SEC).

[144] *See* 17 CFR 204–2 (books and records to be maintained by investment advisers).

[145] *See, e.g.,* 15 U.S.C. 80b–6(1)–(2)), (4) (prohibiting any investment advisers from engaging in any activity that would defraud a client or prospective client). *See also* 17 CFR 275.206(4)–8 (prohibiting any investment advisers from making false or misleading statements to, or otherwise defrauding, investors or prospective investors to pooled investment vehicles).

[146] 17 CFR 275.206(4)–7(a).

[147] 17 CFR 275.206(4)–7(b), (c).

[148] *See, e.g.,* 15 U.S.C. 80b–6(1)–(2), (4); 17 CFR 275.204–4; 17 CFR 275.206(4)–5; 17 CFR 275.206(4)–8.

[149] *See* SIFMA No-Action Letter, *supra* n. 52. *See also* 31 CFR 1023.220(a)(6) (CIP rule permitting a financial institution to rely on another financial institution to perform all or part of its obligations to verify the identity of its customers as required by 31 U.S.C. 5318(h)).

[150] *See* 2016 Investment Management Compliance Testing Survey (2016 IMCTS Survey), p.21, *https://www.investmentadviser.org/eweb/docs/Publications_News/Reports_and_Brochures/Investment_Management_Compliance_Testing_Surveys/2016IMCTppt.pdf.* This survey included responses from compliance officers at 730 RIAs and is the most recent IMCTS survey to have asked detailed questions about AML policies and programs.

§ 1032.210(b) and discussed in greater detail below.

FinCEN reiterates that the proposed AML/CFT program requirement is not a one-size-fits-all requirement but is risk-based and must be reasonably designed. The ''risk-based and reasonably designed'' approach of the proposed rule is intended to give investment advisers the flexibility to design their programs so that they are commensurate with the specific risks of the advisory services they provide and the customers they advise.[151] For example, large firms may assign responsibilities of the individuals and departments carrying out each aspect of the AML/CFT program, while smaller firms would be expected to adopt procedures that are consistent with their (often) simpler, more centralized organizational structures. This flexibility is designed to ensure that all firms subject to FinCEN's AML/CFT program requirements, from the smallest to the largest, and the simplest to the most complex, have in place policies, procedures, and internal controls appropriate to their advisory business to prevent the investment adviser from being used to facilitate money laundering, terrorist financing, or other illicit finance activities and to achieve and monitor compliance with the applicable provisions of the BSA and FinCEN's implementing regulations. FinCEN requests comment on whether existing requirements under the Advisers Act or existing policies and procedures to implement OFAC sanctions could assist investment advisers in complying with the proposed AML/CFT requirements. FinCEN also requests comment on whether any proposed requirements are duplicative of any existing requirements. Finally, FinCEN requests comment on whether there are certain services or activities provided by investment advisers where applying AML/CFT requirements would result in information of limited value to law enforcement and regulators.

2. Scope

As described above, the proposed rule would require all RIAs and ERAs to develop an AML/CFT program, and that program would be required to cover all advisory activities, with one exception: the program need not cover activities undertaken with respect to mutual funds, which have their own obligations under the BSA.[152] As detailed below, advisory activities with respect to mutual funds would be exempt from the AML/CFT program requirements that would be applied in the proposed rule.

An investment adviser would apply an AML/CFT program to all advisory activities other than with respect to mutual funds. Advisory activities subject to an AML/CFT program would include, for example, the management of customer assets, the provision of financial advice, the execution of transactions for customers, as well as other advisory activities. The requirements of the proposed rule would not apply to non-advisory services. One example of this would be in the context of private equity funds: fund personnel may play certain roles with respect to the portfolio companies in which the fund invests. Activities undertaken in connection with those roles (*e.g.,* making managerial/operational decisions about portfolio companies) would not be ''advisory activities'' for purposes of the rule. FinCEN requests comment on whether certain advisory activities pose a lower risk in all circumstances and on the challenges for advisers in complying with the proposed role when engaged in such activities.

Certain commenters on the Second Proposed Investment Adviser Rule proposed to exempt some advisory activities, such as advising clients without managing client assets and acting as a subadviser, on the ground that such activities are lower risk. Assessing the risk of an adviser's activities requires appreciation of the full context of the activity. For example, subadvisers and advisers who do not manage assets may nonetheless afford their clients access to the U.S. financial system, inadvertently guide the layering or integration of illicit proceeds or other illicit finance activity, or have relationships that provide insight to the investment adviser's AML/CFT program. FinCEN is therefore proposing to include those activities within the scope of this proposed rule. As discussed in the comment request section below, FinCEN requests comment on whether certain subadvisory activities should be excluded from coverage of this proposed rule.

Under the risk-based approach, an investment adviser would tailor its program according to the specific risks presented by its various activities. Factors that may indicate an activity or a customer is lower risk include the jurisdiction of registration of legal person customers, and whether the customer (where a legal person) is subject to U.S. AML/CFT regulatory requirements.

(a) Mutual Funds

FinCEN is proposing to exempt from the proposed requirements activities of investment advisers in advising mutual funds.[153] FinCEN believes that this exemption is appropriate because of the regulatory and practical relationship between mutual funds and their investment advisers. Specifically, although mutual funds are distinct legal entities with distinct legal obligations, mutual funds typically do not have their own independent operations. Rather, mutual funds are entirely operated, and compliance with their legal obligations is undertaken, by their service provider entities, foremost amongst them their investment advisers. As a practical matter, we believe that any AML/CFT requirement imposed on an RIA to a mutual fund is already addressed by the existing AML/CFT requirements imposed on the mutual fund itself.[154] In particular, we expect that the investment adviser to a mutual fund will have both (1) access to the exact same information concerning the mutual fund or its investors that is available to the mutual fund, in part in connection with its AML/CFT obligations and (2) a significant role generally in the operations of the mutual fund's regulatory responsibilities, including its AML/CFT program. Consequently, we are proposing not to require investment advisers to mutual funds to include those mutual funds within the investment advisers' own AML/CFT programs, as we believe including a mutual fund within its investment

[151] The legislative history of the BSA reflects that Congress intended that each financial institution should have some flexibility to tailor its program to fit its business, considering factors such as size, location, activities, and risks or vulnerabilities to money laundering. This flexibility is designed to ensure that all firms, from the largest to the smallest, have in place policies and procedures appropriate to monitor for money laundering. *See* USA PATRIOT Act of 2001: Consideration of H.R. 3162 Before the Senate, 147 Cong. Rec. S10990–02 (Oct. 25, 2001) (statement of Sen. Sarbanes); Financial Anti-Terrorism Act of 2001: Consideration Under Suspension of Rules of H.R. 3004 Before the House of Representatives, 147 Cong. Rec. H6938–39 (Oct. 17, 2001) (statement of Rep. Kelly) (provisions of the Financial Anti-Terrorism Act of 2001 were incorporated as Title III in the Act).

[152] *See* 31 CFR part 1024.

[153] FinCEN's definition of a mutual fund under 1010.100(gg) applies to an ETF as an ''open-end company'' (as the term is defined in section 5 of the Investment Company Act).'' *See supra* n. 53.

[154] FinCEN notes as well that the First Proposed Investment Adviser Rule would have permitted mutual funds to be excluded from the programs required of investment advisers covered by that proposed rule. Commenters to the Second Proposed Investment Adviser Rule, which would not have permitted such an exclusion, supported instead the 2003 NPRM approach.

adviser's AML/CFT program would be redundant. This exemption is permissive and not mandatory; an investment adviser could decide to include the mutual funds it advises in complying with any of the investment adviser's proposed requirements.

Mutual funds are already subject to comprehensive AML/CFT obligations under the BSA and are required to, among other things, establish AML/CFT and customer identification programs, conduct CDD, and report suspicious activity, among other obligations.[155] FinCEN believes that, currently, these requirements sufficiently mitigate the money laundering, terrorist financing, and other illicit finance risks associated with mutual funds and those funds' investors to justify this exemption. FinCEN is requesting comment on whether to exempt mutual funds from coverage in an adviser's AML/CFT program. FinCEN also requests comment on whether there are other categories of entities that, like mutual funds, could be reasonably exempted from an investment adviser's AML/CFT program.

FinCEN is also proposing to exempt investment advisers from having to comply with the reporting and recordkeeping requirements of part 1032, subparts C and D, for its mutual fund customers. FinCEN believes that the proposed regulatory text is sufficiently clear that these subparagraphs would not apply with respect to mutual fund customers, because the internal policies, procedures, and controls to comply with those requirements are closely linked to the AML/CFT program requirement. FinCEN requests comment on whether additional regulatory text in those subparts is needed to clarify this. FinCEN also requests comment on whether the exemption should be dependent on the nature of the relationship between the investment adviser and its mutual fund customer, and whether the exemption would avoid duplication of existing AML/CFT requirements. Lastly, FinCEN requests comment on whether investment advisers to mutual funds should still be required to monitor for and file SARs.

(b) Provision of Other Advisory Services

FinCEN understands that investment advisers provide a range of services that could affect the nature of their AML/CFT programs. An investment adviser may provide customers with advisory services that do not include the management of customer assets or knowledge of customers' investment decisions, such as pension consulting, securities newsletters, research reports, or financial planning.

In the investment advisory industry, an adviser may also act as the ''primary adviser'' or ''subadviser.''[156] Generally, the primary adviser contracts directly with the client, and a subadviser has contractual privity with the primary adviser, though there is variation across the sector with respect to the relationship and function between primary advisers and subadvisers. Because subadvisory services are a subcategory of advisory services, the proposed rule would apply to investment advisers who provide subadvisory services.

FinCEN requests comment on whether specific services provided by investment advisers, such as advisory services that do not involve management of client assets or subadvisory services, should be included or excluded from coverage of this proposed rule. FinCEN also requests comment on any alternative approaches for addressing compliance with the proposed rule when advisers provide particular services, such as allowing subadvisers to rely on the primary adviser or allowing the primary adviser to delegate all AML/CFT obligations to the subadviser. FinCEN further requests comment on whether there is an increased risk for a subadviser when providing advisory services to a customer with a primary adviser that is not an investment adviser as defined in the proposed rule. FinCEN also requests comment on the extent a subadviser's AML/CFT program would overlap with the primary adviser's program and how duplication could be mitigated. Finally, FinCEN requests comment on whether there are similar arrangements where an investment adviser may be sub-contracted to provide services to another investment adviser that should or should not be in the scope of an investment adviser's AML/CFT program.

3. Dually Registered Investment Advisers and Advisers Affiliated With or Subsidiaries of Entities Required To Establish AML/CFT Programs

According to a Treasury review of Form ADV filings, approximately three percent of RIAs were dually registered with the SEC as investment advisers and broker-dealers in securities, and approximately 20 percent of RIAs may be affiliated with, or subsidiaries of, banks or broker-dealers, which are required to establish AML/CFT programs. With respect to an investment adviser that is dually registered as a broker-dealer or is a bank (or is a bank subsidiary), FinCEN is not proposing to require such an adviser to establish multiple or separate AML/CFT programs so long as a comprehensive AML/CFT program covers all of the entity's relevant business and activities that are subject to BSA requirements. The program should be designed to address the different money laundering, terrorist financing, or other illicit finance activity risks posed by the different aspects of the entities' businesses and, accordingly satisfy each of the risk-based AML/CFT program requirements to which it is subject in its capacity as both an investment adviser and broker-dealer or bank.[157] Similarly, an investment adviser affiliated with, or a subsidiary of, another entity required to establish an AML/CFT program in another capacity would not be required to implement multiple or separate programs as one single program can be extended to all affiliated entities that are subject to the BSA, so long as it is designed to identify and mitigate the different money laundering, terrorist financing, and other illicit finance activity risks posed by the different aspects of the entity's business and satisfy each of the risk-based AML/CFT program and other BSA requirements to which the organization is subject in all of its regulated capacities, as for example an investment adviser and a bank or insurance company.[158]

[155] *See* 31 CFR 1010.100(gg); 31 CFR part 1024.

[156] The Advisers Act does not distinguish between advisers and subadvisers; all are ''investment advisers.'' *See* 76 FR 39646, 39680 (Jul. 6, 2011) at n. 504 and accompanying text.

[157] FinCEN notes that while broker-dealers in securities are subject to the full panoply of FinCEN's regulations implementing the BSA, investment advisers would not immediately be subject to certain of those AML/CFT requirements, *e.g.,* the CIP Rule, because the proposed rule does not include CIP requirements at this time. FinCEN intends to address CIP requirements in a subsequent joint rulemaking with the SEC, after notice-and-comment.

[158] FinCEN notes that although certain insurance companies are required to establish and implement AML programs and report suspicious activity, the term ''insurance company'' is not included within the general definition of financial institution under FinCEN's regulations. *See* 31 CFR 1010.100(t). Therefore, such insurance companies are not required to file CTRs with FinCEN or comply with the Recordkeeping and Travel Rules and other related recordkeeping requirements. Accordingly, FinCEN would not expect an insurance company that is affiliated with or owns an investment adviser to design an enterprise-wide AML/CFT compliance program that would subject the insurance company to AML/CFT requirements not required by FinCEN's regulations. Conversely, FinCEN would not expect a bank, which is subject to the full panoply of FinCEN's regulations implementing the BSA, to design an enterprise-wide AML/CFT compliance program that would subject an affiliated or controlled investment adviser to AML/CFT requirements that would not be required by the proposed rule.

FinCEN recognizes the importance of enterprise-wide compliance and, therefore, believes it would be beneficial and cost-effective for these types of entities to implement one comprehensive AML/CFT program that includes all activities covered by FinCEN's regulations. However, these entities would not be required to establish one comprehensive AML/CFT program; they may instead establish multiple programs to satisfy their AML/CFT obligations. What would be required, however, is that the covered investment adviser and its affiliated financial institution(s) identify and mitigate the risks arising across the organization or organizations—for example, as they relate to one customer served by both an affiliated bank and an investment adviser. If each of these affiliates conducts due diligence on the same customer individually, without assessing all of this information between both aspects of its business, these businesses' understanding of their shared customer would be incomplete, which could lead to a less effective understanding of risk and detection of suspicious activity.

FinCEN is requesting comments on how dually registered investment advisers and broker-dealers, or investment advisers affiliated with, or a subsidiary of, a bank, broker-dealer, or other BSA-defined financial institution, should apply their existing AML/CFT program to their investment advisory activities. FinCEN also requests comment on whether RIAs or ERAs that are affiliated with a bank or broker-dealer presently apply enterprise-wide AML/CFT requirements, and whether certain AML/CFT requirements are presently tailored for advisory activities.

4. Delegation of Duties

Investment advisers' services routinely involve other financial institutions that have their own AML/CFT program requirements, such as broker-dealers, banks, mutual funds, as well as other investment advisers. FinCEN also recognizes that an investment adviser may conduct some of its operations through agents or third-party service providers, such as broker-dealers in securities (including prime brokers), custodians, transfer agents, and fund administrators. For instance, many investment advisers that operate private funds delegate the implementation and operation of certain aspects of their AML program to a third party, most often the fund's administrator, which is an independent third-party that provides valuation, administrative, and other services to the fund and its investors.[159]

FinCEN recognizes that it is common in the advisory business to delegate a range of compliance, administrative, and other activities to third-party providers. In the proposed rule, similar to other BSA-defined financial institutions, FinCEN would permit an investment adviser to delegate contractually the implementation and operation of aspects of its AML/CFT program. However, if an investment adviser delegates the implementation and operation of any aspects of its AML/CFT program to another financial institution, agent, fund administrator, third-party service provider, or other entity, the investment adviser would remain fully responsible and legally liable for, and need to demonstrate, the program's compliance with AML/CFT requirements and FinCEN's implementing regulations. The investment adviser also would be required to ensure that FinCEN and the SEC are able to obtain information and records relating to the AML/CFT program.

Because investment advisers operate through a variety of different business models, each investment adviser may decide which aspects (if any) of its AML/CFT program are appropriate to delegate. In certain circumstances, for instance, an investment adviser may deem it appropriate to delegate certain aspects of its suspicious activity monitoring and reporting obligation to a third party, such as a qualified custodian.

In addition to these financial institutions, there are other third-party service providers that play an important role in advisory activities, such as fund administrators. As FinCEN understands it, for advisers who presently implement AML/CFT policies and procedures, it is often current practice for those advisers to delegate the administration of AML/CFT policies and procedures to their fund administrator, along with non-AML/CFT activities such as processing subscriptions, transfers, and redemptions administrators. Some fund administrators are subsidiaries of U.S. financial or bank holding companies that may have enterprise-wide AML/CFT programs, while those in foreign jurisdictions may be subject to AML/CFT requirements under local law.

However, as noted above, liability for noncompliance would remain with the investment adviser. The investment adviser would still be required to identify and document the procedures implemented to address its vulnerability to money laundering, terrorist financing, and other illicit finance activity, and then undertake reasonable steps to assess whether the service provider carries out such procedures effectively. For example, it would not be sufficient to simply obtain a ''certification'' from a service provider that the service provider has a satisfactory AML/CFT program. Similarly, if an investment adviser delegates the responsibility for suspicious activity reporting to an agent or a third-party service provider, the adviser remains responsible for its compliance with the requirement to report suspicious activity, including the requirement to maintain SAR confidentiality.

FinCEN requests comment on the scope of information fund administrators currently collect that would support implementation of the proposed rule, and on the practical effect of permitting an investment adviser to delegate some or all of the requirements in the proposed rule. FinCEN also requests comment on the quality of AML/CFT programs implemented by fund administrators whose operations are primarily conducted outside of the United States, the extent to which these fund administrators are able to collect and provide information on the natural person and legal entity investors in offshore pooled investment vehicles when that information is requested by a U.S. investment adviser, the ability of the U.S. investment adviser to effectively monitor the implementation of proposed requirements by fund administrators, and the quality of suspicious activity or suspicious transaction reports submitted by those fund administrators.

5. AML/CFT Program Approval

Section 1032.210(a)(2) of the proposed rule would require that each investment adviser's AML/CFT program be approved in writing by its board of directors or trustees, or if it does not have a board, by its sole proprietor, general partner, trustee, or other persons that have functions similar to a board of directors. This provision of the proposed rule would ensure that the

[159] FinCEN understands that some fund administrators are nonbank subsidiaries of U.S. bank holding companies and, as such, are subject to the global AML policies and procedures of these U.S. institutions. FinCEN also understands that some investment advisers delegate AML compliance to administrators located outside the United States. These administrators are generally located in jurisdictions that require regulated entities to have their own AML/CFT policies, procedures, and controls. *See, e.g.,* Managed Funds Association, Letter to Financial Crimes Enforcement Network, Re: AML Program and SAR Filing Requirements for Registered Investment Advisers (RIN: 1506–AB10), Docket Number FinCEN–2014–003 (Nov. 2, 2015).

requirement to have an AML/CFT program receives the appropriate level of attention and is intended to be sufficiently flexible to permit an investment adviser to comply with this requirement based on its particular organizational structure. The proposed rule would require an investment adviser's written program to be made available for inspection by FinCEN or the SEC.

6. The Required Elements of an Anti-Money Laundering/Countering the Financing of Terrorism Program

(a) Required Policies, Procedures, and Internal Controls

Section 1032.210(b)(1) would require an investment adviser to establish and implement policies, procedures, and internal controls reasonably designed to prevent money laundering, terrorist financing, and other illicit finance activities. As noted in section II, these risks may include not only activities tied to money laundering, such as fraud or corruption, but also any affiliation or relationship with either persons designated by the United States or other jurisdictions with which the United States regularly coordinates sanctions actions, or foreign state-sponsored investment activity in critical or emerging technologies. FinCEN recognizes that some types of customers or customer activities would pose greater risks for money laundering, terrorist financing, or other illicit finance activity than others.

Generally, under the proposed rule, an investment adviser would be required to review, among other things, the types of advisory services it provides and the nature of the customers it advises to identify the investment adviser's vulnerabilities to money laundering, terrorist financing, and other illicit finance activities. It would also need to review investment products offered, distribution channels, intermediaries that it may operate through, and geographic locations of customers and business activities. Accordingly, an investment adviser's assessment of the risks presented by the different types of advisory services it provides to such customers would need to, among other factors, consider the types of accounts offered (*e.g.,* managed accounts), the types of customers opening such accounts, the geographic location of such customers, and the sources of wealth for customer assets. FinCEN expects that investment advisers would generally be able to adapt existing policies and procedures to meet this requirement.[160] FinCEN requests comment on whether it should require an investment adviser to include all the advisory services it provides in its AML/CFT program.

The discussion below focuses on how an investment adviser's AML/CFT program may address the money laundering, terrorist financing, or other illicit finance risks that may be presented by certain specific types of advisory customers, as well as how an adviser's program may address the risks presented by certain specific advisory services provided to those customers. In addition, this section describes FinCEN's expectations under a risk-based approach regarding advisory services to wrap fee programs. FinCEN requests comment on whether closed-end registered funds, wrap fee programs, or other types of accounts advised by investment advisers should be, on a risk-basis, reasonably exempted from an investment adviser's AML/CFT program.

Registered Closed-End Funds. Based on one available estimate, at the end of 2022, there were approximately 440 registered closed-end funds that had approximately $250 billion in AUM.[161] Unlike open-end funds, closed-end funds do not have an existing AML/CFT program or SAR requirement. Registered closed-end funds, however, are subject to comprehensive SEC regulation and oversight and typically trade in the secondary market through broker-dealers who have AML/CFT obligations and where there are additional required disclosures and greater transparency.

For these reasons, although FinCEN is not proposing to exempt closed-end funds from the AML/CFT or SAR requirements in the proposed rule, FinCEN would expect, absent other indicators of high-risk activity, investment advisers could treat closed-end funds as lower-risk for purposes of their AML/CFT programs. FinCEN requests comments on the money laundering, terrorist financing, and other illicit finance risks faced by closed-end funds, and how entities with existing AML/CFT requirements, such as banks and broker-dealers, apply those requirements to activity involving closed-end funds.

Private Funds. As described above, the money laundering, terrorist financing, or illicit finance activity risk for private funds may vary with the individual fund's investment strategy, targeted investors, and other characteristics. Some private funds have traditionally been seen as less attractive to certain illicit actors. For instance, due to their long-term investment focus and illiquid nature, certain private equity funds may be less likely to be used by money launderers, terrorist financiers, and others engaging in illicit finance.[162] Other relevant characteristics of private funds include minimum subscription amounts, restrictions on the type of investors they can accept, and the fact that most funds prohibit the receipt of paper currency. However, those factors may not be a barrier to more sophisticated fraudsters or corrupt officials, among others, that have already placed their funds into a foreign bank and are seeking long-term returns outside of their home country.

An investment adviser that is the primary adviser to a private fund or other unregistered pooled investment vehicle is required to make a risk-based assessment of the money laundering and terrorist financing risks presented by the investors in such investment vehicles by considering the same types of relevant factors, as appropriate, as the adviser would consider for clients for whom the adviser manages assets directly. As noted above, the risk-based approach of the proposed rule is intended to give investment advisers the flexibility to design their programs to meet the specific risks presented by their customers, including any funds they advise. In assessing the potential risk of a private fund under the proposed rule, investment advisers generally should gather pertinent facts about the structure or ownership of the fund, including both the extent to which they are provided with relevant information about the investors in that private fund, who may or may not themselves also be customers of the investment adviser, and the nature of such investor-related information that they receive.

[160] *See* discussion in section II.B, *infra,* for a discussion of existing Advisers Act recordkeeping and reporting obligations that may enable investment advisers to adapt existing policies, procedures, and internal controls. In addition, as noted above, according to one industry survey, as of 2016, 40 percent of participants had adopted AML programs similar to the AML program requirements proposed in the Second Proposed Investment Adviser Rule.

[161] *See 2023 Investment Company Factbook* at p.2,17, *supra* n. 55. Unlike traditional mutual funds (or ''open-end funds''), closed-end funds are not required to buy back shares from shareholders. Closed-end funds sell their shares in a public offering. After that, their shares trade on national securities exchanges at market prices. The market price may be greater or less than the market value of the fund's underlying investments.

[162] For instance, in the Proposed Unregistered Investment Companies Rule, FinCEN proposed to exclude from the scope of its proposed AML requirements those funds that did not offer their investors the right to redeem any portion of their ownership interests within two years after those interests were acquired. *See* 68 FR at 60619.

Under the proposed rule, where an investment adviser attempted to and was unable to obtain identifying information about the investors in a private fund, the private fund may pose a higher risk for money laundering, terrorist financing, or other illicit finance activity. When a private fund's potential vulnerability to money laundering, terrorist financing, or other illicit finance activity is high, the adviser's procedures would need to reasonably address these higher risks so that the adviser is able to prevent the investment adviser from being used for money laundering or the financing of terrorist activities, and to achieve and monitor compliance with the BSA (including to obtain sufficient information to monitor and report suspicious activity). FinCEN requests comment on what information is currently available to advisers to private funds regarding their investors that could help advisers comply with the proposed AML/CFT requirements. FinCEN also requests comment on whether a subadviser to a private fund or other unregistered pooled investment vehicle should be required to establish the same policies, procedures, and internal controls as when the primary adviser is the investment adviser, or should be required to mitigate the risks of money laundering, terrorist financing, or other illicit activity to the investing pooled investment vehicle's investors, sponsoring entity, and/or intermediaries.

FinCEN recognizes that certain private funds and other unregistered pooled investment vehicles may present lower risks for money laundering or terrorist financing than others. Consequently, FinCEN would not expect an investment adviser to risk-rate the advisory services it provides to a pooled investment vehicle that presents a lower risk the same as it might rate the advisory services it provides to other types of pooled investment vehicles that may present higher risks for attracting money launderers, terrorist financers, or other illicit actors. FinCEN requests comment on factors related to the activities, investors, or structure of private funds or other unregistered pooled investment vehicles that could be higher- or lower-risk. FinCEN also requests comment on how the proposed rule should apply to advisers who manage private funds that receive investments from in-funds or who have funds-of-funds who are investors.

Wrap Fee Programs. In a wrap fee program, investment advisory and brokerage services are provided together as a single product.[163] For the purposes of this discussion, FinCEN will focus on wrap fee arrangements where an investment adviser is solely acting as a portfolio manager and generally managing the customer account to a selected model. In these programs, even if both advisers or broker-dealers are providing services, there is a single ''relationship'' entity that is responsible for the relationship with the customer, managing the account overall, and selecting the account strategy. That program sponsor has the primary relationship with the customer, which means that the program sponsor is typically best positioned to recognize illicit financial activity in the program.

While FinCEN recognizes the characteristics described above regarding the most common structure of wrap fee programs, it is not proposing to exempt wrap fee programs from coverage of the proposed rule. Depending on the structure of the wrap fee program, the investment adviser may be best positioned to spot illicit finance activity (if, for example, it is the program sponsor). Moreover, even a non-sponsoring investment adviser may have additional insights into the activity of the wrap fee program. FinCEN requests comments on how the requirements of the proposed rule can be applied to advisers participating in a wrap fee program, to include when an adviser acting as portfolio manager is either affiliated or not affiliated with the sponsoring entity of the program.

(b) Provide for Independent Testing for Compliance To Be Conducted by Company Personnel or by a Qualified Outside Party

Section 1032.210(b)(2) would require that an investment adviser provide for independent testing of the AML/CFT program by the adviser's personnel or a qualified outside party. The purpose of this provision is to ensure that an investment adviser's AML/CFT program complies with the requirements of § 1032.210 and that the program functions as designed. Employees of either the investment adviser, its affiliates, or unaffiliated service providers may conduct the independent testing, so long as those same employees are not involved in the operation and oversight of the program.[164] The employees would have to be knowledgeable regarding AML/CFT requirements and qualified to conduct independent testing. The frequency of the independent testing would depend upon the money laundering, terrorist financing, and other illicit finance risks of the adviser and the adviser's overall risk management strategy. For instance, an adviser could conduct independent testing *over* periodic intervals (*e.g.,* every 12 to 18 months) or when there are significant changes in the adviser's risk profile (with respect to money laundering, terrorist financing, or other illicit finance risks), systems, compliance staff, or processes. More frequent independent testing may be appropriate when errors or deficiencies in some aspect of the AML/CFT compliance program have been identified or to verify or validate mitigating or remedial actions. Any recommendations resulting from such testing would need to be promptly implemented or submitted to senior management for consideration.

(c) Designate a Person or Persons Responsible for Implementing and Monitoring the Operations and Internal Controls of the Program

Section 1032.210(b)(3) would require that an investment adviser designate a person or persons to be responsible for implementing and monitoring the operations and internal controls of the AML/CFT program. Under the proposed rule, an investment adviser may designate a single person or persons (including in a committee) to be responsible for compliance. The person or persons should be knowledgeable and competent regarding AML/CFT requirements, the adviser's relevant policies, procedures, and controls, as well as the adviser's money laundering, terrorist financing, and other illicit finance risk. The person or persons should have full responsibility and authority to develop and implement appropriate policies, procedures, and internal controls reasonably designed to prevent the investment adviser from being used for those risks. Whether the compliance officer is dedicated full time to AML/CFT compliance would depend on the size and type of advisory services the adviser provides and the customers it serves. A person designated as a compliance officer should be an officer

[163] A ''wrap fee program'' for purposes of the proposed rule is a program under which investment advisory and brokerage execution services (as well as administrative expenses and other fees and expenses) are provided for a single ''wrapped'' (*i.e.,* bundled) fee.

[164] As noted in this NPRM, some investment advisers may implement enterprise-wide AML/CFT programs that are evaluated at the holding company level. It would not be consistent with the requirements of this proposed regulation for an employee at an affiliated financial institution, including the holding company, to be responsible for testing the adviser's AML/CFT program, or carry out such testing, if the affiliate's employee is responsible for administering the adviser's AML/CFT program.

of the investment adviser (or individual of similar authority within the particular corporate structure of the investment adviser) and someone who has established channels of communication with senior management demonstrating sufficient independence and access to resources to implement a risk-based and reasonably designed AML/CFT program.[165]

(d) Provide Ongoing Training for Appropriate Persons

Section 1032.210(b)(4) would require that an investment adviser provide for ongoing training of appropriate persons. Employee training is an integral part of any AML/CFT program. To carry out their responsibilities effectively, employees of an investment adviser (and of any agent or third-party service provider that is charged with administering any portion of the investment adviser's AML/CFT program) would have to be trained in AML/CFT requirements relevant to their functions and to recognize possible signs of money laundering, terrorist financing, and other illicit finance activity that could arise in the course of their duties. Such training may be conducted through, among other things, outside or in-house seminars, and may include computer-based or virtual training. The nature, scope, and frequency of the investment adviser's training program would be determined by the responsibilities of the employees and the extent to which their functions would bring them in contact with AML/CFT requirements or possible money laundering, terrorist financing, or other illicit finance activity. Consequently, under the proposed rule, the training program should provide a general awareness of overall AML/CFT requirements and money laundering, terrorist financing, and other illicit finance risks, as well as more job-specific guidance tailored to particular employees' roles and functions with respect to the entities' particular AML/CFT program.[166] For those employees whose duties bring them in contact with AML/CFT requirements or possible money laundering, terrorist financing, or other illicit finance risks, the requisite training would have to occur when the employee assumes those duties. Moreover, these employees should receive periodic updates and refreshers regarding the AML/CFT program.[167]

(e) Ongoing Customer Due Diligence (CDD)

Section 1032.210(b)(5) would require that an investment adviser implement appropriate risk-based procedures for conducting ongoing CDD that includes (i) understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile; and (ii) conducting ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

These obligations were added to the AML/CFT program requirements for financial institutions in May 2016, when FinCEN issued the CDD Rule.[168] The CDD Rule clarified and strengthened CDD requirements for covered financial institutions (banks, mutual funds, brokers or dealers in securities, futures commission merchants, and introducing brokers in commodities) and added a new requirement for these covered financial institutions to identify and verify the identity of the natural persons who own or control (known as beneficial owners of) legal entity customers when those customers open accounts.

The CDD Rule identifies the four core elements of CDD: (1) identifying and verifying the identity of customers; (2) identifying and verifying the identity of the beneficial owners of legal entity customers opening accounts; (3) understanding the nature and purpose of customer relationships; and (4) conducting ongoing monitoring.[169] FinCEN requests comment on the types of information investment advisers regularly receive from their customers, and how investment advisors would exchange information with other financial institutions, that could be used to understand the nature and purpose of the customer relationship and identify and monitor suspicious transactions.

Requiring investment advisers to perform effective CDD so that they understand who their customers are and what type of transactions they conduct is a critical aspect of combating all forms of illicit finance activity, from terrorist financing and sanctions evasion to more traditional financial crimes, including money laundering, fraud, and tax evasion. These measures would also enable investment advisers to identify and report suspicious transactions by filing SARs in the manner that best serves the purposes of the BSA. For investment advisers covered by the proposed rule, FinCEN expects to address the first requirement of customer identification and verification in a future joint rulemaking with the SEC, as noted above, while the third and fourth elements of the CDD Rule are being incorporated into these AML/CFT Program requirements through proposed § 1032.210(b)(5).

FinCEN will take the first steps towards incorporating the second element by including investment advisers in the definition of ''covered financial institution'' under 31 CFR 1010.605(e)(1), discussed at further length below. However, the requirement to identify and verify the beneficial owners of legal entity customer accounts is predicated on the existence of a CIP requirement, which, as just stated, FinCEN anticipates addressing in the future joint rulemaking with the SEC.

The CDD Rule is affected by the Corporate Transparency Act (CTA), passed as part of the AML Act. The CTA requires certain types of domestic and foreign entities, called ''reporting companies,'' to submit specified beneficial ownership information (BOI) to FinCEN.[170] In certain circumstances, FinCEN is authorized to share this BOI with government agencies, financial institutions, and financial regulators, subject to appropriate protocols.[171]

FinCEN is issuing three key rules pursuant to the CTA. The first rule—the BOI reporting rule—requires certain corporations, limited liability companies, and other entities created in or registered to do business in the United States to report information about their beneficial owners.[172] This rule was promulgated on September 30, 2022.[173] The second establishes rules for who may access BOI for what purposes, and what safeguards will be required to ensure that the information is secured and protected.[174] This rule was promulgated on December 21, 2023

[165] In particular, RIAs who are subject to the SEC's Compliance Rule (17 CFR 275.206(4)–7), could designate their chief compliance officer under that rule to be responsible for this provision of the proposed rule. The proposed rule does not, however, require that an investment adviser designate the same person.

[166] *See e.g.,* DWS Investment Management Americas Inc., Investment Company Act Rel. No. 6431, ¶ 28 (Sept. 25, 2023) (noting DWS' failure to conduct AML training that was specific to the DWS Mutual Funds or the risks applicable to mutual funds for those employees with mutual fund responsibilities).

[167] The frequency of these periodic updates and refreshers would depend upon the money laundering, terrorist financing, and other illicit finance risks of the adviser and the adviser's overall risk management strategy.

[168] FinCEN, *Customer Due Diligence Requirements for Financial Institutions,* final rule, 81 FR 29398 (May 11, 2016).

[169] *Id.* at 29398.

[170] *See generally* 31 U.S.C. 5336(b), (c).

[171] *See* 31 U.S.C. 5336(c)(2).

[172] *See* 31 CFR 1010.380.

[173] FinCEN, *Beneficial Ownership Information Reporting Requirements,* final rule, 87 FR 59498 (Sep. 30, 2022).

[174] *See* 31 CFR 1010.955.

and goes into effect on February 20, 2024.[175]

The CTA also requires FinCEN to revise the CDD Rule no later than January 1, 2025.[176] FinCEN is required to rescind the existing specific beneficial ownership identification and verification requirements of 31 CFR 1010.230(b)–(j), while retaining the general requirement for financial institutions to identify and verify the beneficial owners of legal entity customers under 31 CFR 1010.230(a).[177] FinCEN expects to undertake a third rulemaking to revise the CDD Rule and anticipates that, because of the changes required by the AML Act, such a rulemaking could have a significant impact on financial institutions' CDD obligations.

In light of these anticipated forthcoming changes to the CDD Rule and the statutory deadline of January 1, 2025, to complete them, FinCEN assessed that investment advisers should not be required to apply the current CDD requirements to identify and verify the beneficial owners of legal entity customer accounts during the period between this proposed rulemaking and the effective date of the revised CDD Rule. Therefore, FinCEN has not included requirements to identify and verify the beneficial owners of legal entity customer accounts in this proposed rule. However, FinCEN invites comment regarding whether it should apply such requirements once a joint rulemaking addressing CIP requirements is finalized, notwithstanding the forthcoming CDD Rule.

Requirement to Identify and Verify Customers. Existing requirements for other BSA-defined financial institutions require that the relevant financial institution's CIP include risk-based procedures to verify the identity of each customer, to the extent reasonable and practicable. The elements of such program must include identifying the customer, verifying the customer's identity (through documents or non-documentary methods, or a combination thereof), procedures for circumstances where the institution cannot form a reasonable belief that it knows the true identity of the individual, and determining whether the names of customers appear on any government-provided list of known terrorists or terrorist organizations. As noted above, Treasury expects to address CIP requirements through a future joint rulemaking with the SEC, as required by section 326 of the USA PATRIOT Act.[178]

Understand the Nature and Purpose of Customer Relationships to Develop Customer Risk Profiles. As is the case for banks, broker-dealers, and mutual funds, the term ''customer risk profile'' for covered investment advisers refers to information gathered—typically at the time of account opening or, in the case of a covered investment adviser, at the onset of an advisory relationship—about a customer to develop the baseline against which customer activity is assessed for suspicious activity reporting.

Under the proposed rule, investment advisers are obligated to report suspicious activity by filing SARs on transactions that, among other things, have no business or apparent lawful purpose or are not the sort in which the particular customers would normally be expected to engage. Fulfilling this proposed requirement would necessitate that an investment adviser understands the nature and purpose of the customer relationship, which informs the baseline against which aberrant, suspicious transactions are identified. In some circumstances, an understanding of the nature and purpose of a customer relationship can also be developed by inherent or self-evident information about the product or customer type, such as the type of customer or the service or product offered, or other basic information about the customer, and such information may be sufficient to understand the nature and purpose of the relationship. This may include the customer's explanation about its initial decision to seek advisory services from the adviser and may be reflected in the particular type of advisory service the customer seeks, as well as information already collected by the investment adviser, such as net worth, domicile, citizenship, or principal occupation or business.

For investment advisers, the risk associated with a particular type of customer may vary significantly. For instance, key risk factors for natural person customers may include the source of funds, the jurisdiction in which they reside, their country(ies) of citizenship, and their status as a PEP,[179] among other things. For legal entity customers, an investment adviser may consider the type of entity, the jurisdiction in which it is domiciled and located, and the statutory and regulatory regime of that jurisdiction for company formation and other financial transparency requirements, if relevant. The investment adviser's historical experience with the individual or entity and the references of other financial institutions may also be relevant factors.

Regarding the legal entity customers of an adviser, some may be financial intermediaries or third parties that are BSA-defined financial institutions and have their own AML/CFT requirements. Consequently, the investment adviser may not always have a direct relationship with the investors in its legal entity customers. Those investors may be introduced to the adviser by other entities who or may or may not have their own AML/CFT obligations (such as a broker-dealer, other investment adviser, or other intermediary). For these intermediary entities, and even though investment advisers would not be required to categorically collect beneficial ownership information on legal entity customers, investment advisers should collect sufficient information such that they are able to detect and report suspicious activity associated with intermediated accounts, including activity related to underlying clients.[180] FinCEN expects that non-intermediary legal entity customers that are not BSA-defined financial institutions with their own AML/CFT requirements would be subject to a different assessment than intermediary customers that are BSA-defined financial institutions for understanding the nature and purpose of the customer relationship. The requirement to assess customer risk laid out in this proposed rule must be understood in this context.

For understanding the nature and purpose of customers who are private funds, FinCEN notes that investment advisers can (1) create and administer a private fund or (2) provide advice to a

[175] .FinCEN, *Beneficial Ownership Information Access and Safeguards,* final rule, 88 FR 88732 (Dec. 21, 2023).

[176] *See* AML Act section 6403(d)(1) (''Not later than 1 year after the effective date of the regulations promulgated under section 5336(b)(4) of title 31, United States Code, as added by subsection (a) of this section, the Secretary of the Treasury shall revise the final rule entitled 'Customer Due Diligence Requirements for Financial Institutions' . . . .''). The effective date of the relevant final rule is January 1, 2024.

[177] *See* AML Act section 6403(d)(2) (''[T]he Secretary of the Treasury shall rescind paragraphs (b) through (j) of section 1010.230 of title 31 . . . upon the effective date of the revised rule promulgated under this subsection. Nothing in this section may be construed to authorize the Secretary of the Treasury to repeal the requirement that financial institutions identify and verify beneficial owners of legal entity customers under section 1010.230(a).'').

[178] *See* 31 U.S.C. 5318(*l*).

[179] *See generally* Joint Statement on Bank Secrecy Act Due Diligence Requirements for Customers Who May Be Considered Politically Exposed Persons, (Aug. 21, 2020), *https://www.fincen.gov/sites/default/files/shared/PEP%20Interagency%20Statement_FINAL%20508.pdf.*

[180] *See* FinCEN, *Customer Due Diligence Requirements for Financial Institutions,* notice of proposed rulemaking, 79 FR 45141, 45161 (Aug. 4, 2014).

private fund that is created and administered by a third party or an intermediary. While the particular role played by the investment adviser will affect the type of information the adviser can collect about the investors in such a fund, the adviser should collect sufficient information to develop a customer baseline for suspicious activity reporting regarding the private fund. FinCEN invites comments on other types of information, other than beneficial ownership information, that could be collected to understand the nature and purpose of a customer relationship with a private fund.

Ongoing Monitoring to Identify Suspicious Transactions and Update Customer Information. This element of CDD would oblige investment advisers to perform ongoing monitoring drawing on customer information, as well as to file SARs in a timely manner in accordance with their reporting obligations.[181] As proposed, the obligation to update customer information would generally only be triggered when the investment adviser became aware of information as part of its normal monitoring relevant to assessing the potential risk posed by a customer; it is not intended to impose a categorical requirement to update customer information on a regularly occurring, pre-determined basis. Similar to the CDD obligations for mutual funds,[182] under the proposed § 1032.210(b)(5)(ii), investment advisers would be required to implement appropriate risk-based procedures to conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

Ongoing monitoring may be accomplished in several ways. Customer information may be integrated into the financial institution's transaction monitoring system and may be used after a potentially suspicious transaction has been identified, as one means of determining whether the identified activity is suspicious. An investment adviser may also utilize the information sharing provisions under section 314(b) of the USA PATRIOT Act to request relevant information from other financial institutions that may hold relevant information, such as the qualified custodians of customer funds.

Regarding legal entity customers, FinCEN assesses that in some circumstances, on a risk-basis, an investment adviser would not need information relating to investors in those legal entity customers to comply with the requirements of the ongoing monitoring obligation. However, in other circumstances, investment advisers may need to request information regarding investors in their legal entity customers. As FinCEN noted in the CDD Rule, the ongoing monitoring obligation is intended to apply to ''all transactions by, at, or through the financial institution,'' [183] and not just those that are direct customers of the financial institution. Given that risks posed by each customer differ, FinCEN finds that the level of risk posed by a customer relationship should be a factor influencing the decision to request information regarding underlying customers, and if the legal entity customer does not provide such information, how the investment adviser should adjust the risk profile of that legal entity customer. FinCEN is requesting comment on several aspects of the proposed requirement to apply CDD obligations described above.

Compliance Date. Section 1032.210(c) states the effective date by which an investment adviser would be required to comply with this section. Specifically, under this proposed rule, an investment adviser would be required to develop and implement an AML/CFT program that complies with the requirements of this section on or before twelve months from the effective date of the regulation.

7. Duty To Establish, Maintain, and Enforce an AML/CFT Program by Persons in the United States

FinCEN recognizes that many investment advisers are located outside the United States or contract certain of their operations outside the United States. As FinCEN seeks to harmonize this AML/CFT framework in a manner consistent with the SEC's existing framework for investment advisers, the proposed rule follows the scope of the SEC's registration requirements for RIAs and Form ADV filing requirements for ERAs. Consistent with longstanding SEC practice and guidance interpreting investment adviser registration requirements under the Advisers Act,[184] unless subject to an exemption, investment advisers located abroad generally must register with the SEC if they ''make use of the mails or any means or instrumentality of interstate commerce in connection with [their] business as an investment adviser.'' [185] The BSA permits FinCEN to regulate financial institutions located outside the United States in such circumstances, and FinCEN has previously similarly defined certain financial institutions on the basis of SEC registration, regardless of their physical location.[186] In line with these requirements and SEC guidance, the proposed rule's requirements would therefore apply on the same basis to RIAs and ERAs located outside the United States.

FinCEN requests comment on any challenges for investment advisers in following the scope of the SEC's registration and filing requirements for advisers located outside the United States and any potential conflicts with domestic and foreign law. FinCEN also requests comment on whether requiring such non-U.S. advisers to file reports of suspicious activity with FinCEN is consistent with how the applicable SAR rules are applied to broker-dealers or other BSA-defined financial institutions or poses any concerns under foreign law, including foreign privacy laws.

For investment advisers covered by the proposed rule, it may be appropriate to outsource certain aspects of compliance with the proposed rule outside the United States. But section 6101(b)(2)(C) of the AML Act, codified at 31 U.S.C. 5318(h)(5), provides that the duty to establish, maintain, and enforce a financial institution's AML/CFT program shall remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to oversight and supervision by, the Secretary of the Treasury and the appropriate Federal functional regulator.[187] Proposed § 1032.210(d) would incorporate this statutory requirement with respect to the AML/CFT program by restating that the duty to establish, maintain, and enforce the AML/CFT program must remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to oversight and supervision by, FinCEN and the financial institution's appropriate Federal functional regulator (*i.e.,* for covered investment advisers, the SEC).[188]

FinCEN recognizes RIAs and ERAs (as well as other financial institutions) may currently have AML/CFT staff and operations outside of the United States to improve cost efficiencies, to enhance coordination particularly with respect to cross-border operations, or for other

[181] FinCEN's proposed SAR filing obligations for investment advisers are discussed below.

[182] 31 CFR 1024.210(b)(5)(ii); *see also* FinCEN, 81 FR at 29424.

[183] *Id.*

[184] 15 U.S.C. 80b–3(a), (d); *see also* 76 FR 39646, 39668–72 (Jul. 6, 2011).

[185] 15 U.S.C. 80b–3(a).

[186] *See, e.g.,* 31 CFR 1023.100(b).

[187] 31 U.S.C. 5318(h)(5).

[188] Not all financial institutions that are required to have AML/CFT programs under the BSA have Federal functional regulators pursuant to 15 U.S.C. 6809.

reasons. FinCEN requests comment on a variety of potential questions or challenges that may arise for financial institutions as they address this requirement, including questions about the scope of the requirement and the obligations of persons that are covered. FinCEN intends to consider whether additional interpretive language would be appropriate in a final rule.

F. Reports of Suspicious Transactions

Under the BSA, FinCEN (through a delegation from the Secretary) is authorized to require financial institutions to report suspicious transactions relevant to a possible violation of law or regulation.[189] FinCEN has issued regulations under this authority requiring banks, casinos, money services businesses, broker-dealers in securities, mutual funds, insurance companies, futures commission merchants, loan or finance companies, futures commission merchants, and introducing brokers in commodities to report suspicious activity by submitting SARs to FinCEN.[190] Suspicious activity reporting by these and other types of financial institutions provide information that is highly useful to law enforcement and regulatory investigations and proceedings, as well as in the conduct of intelligence activities to protect against international terrorism.[191]

Accordingly, this proposed rule would add a new section to FinCEN regulations, proposed § 1032.320, that would similarly require investment advisers to file SARs for any suspicious transaction relevant to a possible violation of law or regulation. FinCEN would expect that requiring investment advisers to report suspicious activity would similarly provide highly useful information for investigations and proceedings involving domestic and international money laundering, terrorist financing, and other illicit finance activity, as well as for intelligence purposes. Requiring investment advisers to report suspicious activity would also narrow the regulatory gap that may be exploited by money launderers, terrorist financiers, or other illicit actors seeking access to the U.S. financial system through financial institutions not required to report suspicious transactions. The proposed requirement is also generally consistent with the existing SAR filing requirements for other financial institutions under existing regulations. As explained above, the proposed rule would not require investment advisers to file SARs with respect to any mutual fund that it advises.

1. Reports by Investment Advisers of Suspicious Transactions

Proposed § 1032.320(a) sets forth the criteria for which an investment adviser would be obligated to report suspicious transactions that are conducted or attempted by, at, or through an investment adviser and involve or aggregate at least $5,000 in funds or other assets. Filing a report of a suspicious transaction would not relieve an investment adviser from the responsibility of complying with any other reporting requirement imposed by the SEC.

Proposed § 1032.320(a)(1) contains the general statement of the obligation to file reports of suspicious transactions. The obligation would extend to transactions conducted or attempted by, at, or through an investment adviser. To clarify that the proposed rule imposes a reporting requirement that is uniform with those for other financial institutions, § 1032.320(a)(1) incorporates language from the SAR rules applicable to other financial institutions, such as banks, broker-dealers in securities, mutual funds, casinos, and money services businesses.

Proposed § 1032.320(a)(2) would require the reporting of suspicious activity that involves or aggregates at least $5,000 in funds or other assets. The $5,000 threshold in this proposed rule is consistent with the SAR filing requirements for most other financial institutions that are subject to a SAR reporting requirement under FinCEN's rules implementing the BSA.[192] Furthermore, proposed § 1032.320(a)(1) would permit an investment adviser to report voluntarily any transaction the investment adviser believes is relevant to the possible violation of any law or regulation but that is not otherwise required to be reported by this proposed rule. Thus, the rule would encourage the voluntary reporting of suspicious transactions, such as those below the $5,000 threshold of the proposed rule in § 1032.320(a)(2). Such voluntary reporting would be subject to the same protection from liability as mandatory reporting pursuant to 31 U.S.C. 5318(g)(3).

Section 1032.320(a)(2)(i) through (iv) specify that an investment adviser would be required to report a transaction if it knows, suspects, or has reason to suspect that the transaction (or a pattern of transactions of which the transaction is a part): (i) involves funds derived from illegal activity or is intended or conducted to hide or disguise funds or assets derived from illegal activity as a part of a plan to violate or evade any Federal law or regulation or to avoid any transaction reporting requirement under Federal law or regulation; (ii) is designed, whether through structuring or other means, to evade the requirements of the BSA; (iii) has no business or apparent lawful purpose, and the investment adviser knows of no reasonable explanation for the transaction after examining the available facts; or (iv) involves the use of the investment adviser to facilitate criminal activity.

The proposed rule would also require, including through the obligation to conduct ongoing CDD, at proposed § 1032.210(b)(5), that an investment adviser evaluate customer activity and relationships for money laundering, terrorist financing, and other illicit finance risks and design a suspicious transaction monitoring program that is appropriate for the particular investment adviser in light of such risks. For some investment advisers, such a program may include information that may be held by a qualified custodian receiving and sending customer funds. Some of the types of suspicious activity an investment adviser may identify and report are transactions designed to hide the source or destination of funds and fraudulent activity. Other suspicious activity tied to private funds, particularly venture capital funds, could include an investor in such a fund requesting access to detailed non-public technical information about a portfolio company that is inconsistent with a professed focus on economic return. A money launderer also could engage in placement and layering by funding a managed account or investing in a private fund by using multiple wire transfers from different accounts maintained at different financial institutions or requesting that a transaction be processed in a manner to

[189] 31 U.S.C. 5318(g)(1). As amended by the USA PATRIOT Act, subsection (g)(1) states generally that ''the Secretary may require any financial institution, and any director, officer, employee, or agent of any financial institution, to report any suspicious transaction relevant to a possible violation of law or regulation.''

[190] *See* 31 CFR 1020.320, 1021.320, 1022.320, 1023.320, 1024.320, 1025.320, 1026.320, and 1029.320.

[191] *See* 31 U.S.C. 5311. *See also* FinCEN, *Year in Review for FY 2022* (Apr. 21, 2023) (providing additional information on the value of BSA data), *https://www.fincen.gov/sites/default/files/shared/FinCEN_Infographic_Public_2023_April_21_FINAL.pdf.*

[192] *See* 31 CFR 1020.320(a), 1021.320(a), 1024.320(a), 1023.320(a), 1026.320(a), and 1029.320(a) (requiring mutual funds, broker-dealers in securities, banks, casinos, futures commission merchants and introducing brokers, and loan or finance companies to report suspicious transactions if they involve in the aggregate at least $5,000).

avoid funds being transmitted through certain jurisdictions.

Suspicious activity could include other unusual wire activity that does not correlate with a customer's stated investment objectives; transferring funds or other assets involving the accounts of third parties with no plausible relationship to the customer, transfers of funds or assets involving suspicious counterparties—such as those subject to adverse media, exhibiting shell company characteristics, or located in jurisdictions with which the customer has no apparent nexus; the customer behaving in a manner that suggests that the customer is acting as a ''proxy'' to manage the assets of a third party; or an unusual withdrawal request by a customer with ties to activity or individuals subject to U.S sanctions following or shortly prior to news of a potential sanctions listing. Additionally, suspicious activity could include potential fraud and manipulation of customer funds directed by the investment adviser. These typologies can consist of insider trading, market manipulation, or an unusual wire transfer request by an investment adviser from a private fund's account held for the fund's benefit at a qualified custodian.

FinCEN notes, however, that the techniques of money laundering, terrorist financing, and other illicit finance activity are continually evolving, and there is no way to provide a definitive list of suspicious transactions. A determination to file a SAR should be based on all the facts and circumstances relating to the transaction and the customer in question. As discussed above, FinCEN believes that investment advisers should be able to build upon existing policies, procedures, and internal controls they currently have in place to comply with the Federal securities laws to which they are subject to report suspicious activity.

Section 1032.320(a)(3) would provide that more than one investment adviser may have an obligation to report the same suspicious transaction and that other financial institutions may have separate obligations to report suspicious activity with respect to the same transaction pursuant to other provisions in the BSA. However, where more than one investment adviser, or another financial institution with a separate suspicious activity reporting obligation,[193] is involved in the same transaction, only one report jointly filed on behalf of all involved financial institutions would be required. FinCEN recognizes that other financial institutions, such as broker-dealers in securities, mutual funds, and banks have separate reporting obligations that may involve the same suspicious activity. Furthermore, as discussed above, some investment advisers are dually registered or affiliated with another financial institution. It would be permissible for either the investment adviser or the other financial institution to file a single joint report provided that the joint report contained all relevant facts and that each institution maintained a copy of the report and any supporting documentation. The same approach would apply when more than two financial institutions are involved. FinCEN requests comment on whether there are existing requirements under the Advisers Act or other laws or regulations that could assist investment advisers in complying with the proposed SAR requirements. FinCEN also requests comment on what guidance would be useful in identifying activity that may require the filing of a SAR.

2. Filing and Notification Procedures

Proposed § 1032.320(b)(1) through (4) sets forth the filing and notification procedures investment advisers would need to follow to make reports of suspicious transactions. Within 30 days of initial detection by the reporting investment adviser of facts that may constitute a basis for filing a SAR, the adviser would need to report the transaction by completing and filing a SAR with FinCEN in accordance with all form instructions and applicable guidance. The investment adviser would also need to collect and maintain supporting documentation relating to each SAR separately and make such documentation available to FinCEN, any Federal, State, or local law enforcement agency; or any Federal regulatory authority, such as the SEC, that examines the investment adviser for compliance with the BSA under the proposed rule, upon request of that agency or authority. Under the proposed rule with respect to SAR filing obligations for investment advisers, which are in line with existing SAR regulations for other BSA-defined financial institutions, any supporting documents filed with the SAR could also be disclosed to those authorities or agencies to whom a SAR may be disclosed. For situations requiring immediate attention, such as suspected terrorist financing or ongoing money laundering schemes, investment advisers would be required under § 1032.320(b)(4) to notify immediately by telephone the appropriate law enforcement authority in addition to filing a timely SAR.

FinCEN requests comment on how an investment adviser would apply the proposed SAR filing obligation for assets held by a qualified custodian. FinCEN also requests comment on whether there should be an exception to the proposed SAR filing requirement for certain violations that are appropriately reported to the SEC under the Federal securities laws, or for violations with respect to a mutual fund advised by the investment adviser. Lastly, FinCEN requests comment on whether the proposed SAR filing requirement would produce operational or other challenges.

3. Retention of Records

Proposed § 1032.320(c) would provide that investment advisers must maintain copies of filed SARs and the underlying related documentation for a period of five years from the date of filing. As indicated above, supporting documentation would need to be made available to FinCEN and the prescribed law enforcement and regulatory authorities, upon request.

4. Confidentiality of SARs

Proposed § 1032.320(d) would provide that a SAR and any information that would reveal the existence of a SAR are confidential and shall not be disclosed except as authorized in § 1032.320(d)(1)(ii). Section 1032.320(d)(1)(i) would generally provide that no investment adviser, and no current or former director, officer, employee, or agent of any investment adviser, shall disclose a SAR or any information that would reveal the existence of a SAR. This provision of the proposed rule would further provide that any investment adviser and any current or former director, officer, employee, or agent of any investment adviser that is subpoenaed or otherwise requested to disclose a SAR or any information that would reveal the existence of a SAR, would decline to produce the SAR or such information and would be required to notify FinCEN of such a request and any response thereto. In addition to reports of suspicious activity required by the proposed rule, investment advisers would be prohibited from disclosing voluntary reports of suspicious activity.

Proposed § 1032.320(d)(1)(ii) would provide three rules of construction that clarify the scope of the prohibition

[193] Other BSA-defined financial institutions, such as broker-dealers in securities, mutual funds, and banks have separate reporting obligations that may involve the same suspicious activity. *See* 31 CFR 1023.320, 1024.320, 1020.320.

against the disclosure of a SAR by an investment adviser and closely parallel the rules of construction in the suspicious activity reporting rules for other financial institutions. As discussed above, the proposed rules of construction would primarily describe situations that are not covered by the prohibition against the disclosure of a SAR or information that would reveal the existence of a SAR contained in § 1032.320(d)(1). The rules of construction proposed in this rulemaking would remain qualified by, and subordinate to, the statutory mandate that revealing to one or more subjects of a SAR of the SAR's existence would remain a crime.

The first rule of construction, in § 1032.320(d)(1)(ii)(A)(*1*), would authorize an investment adviser, or any director, officer, employee or agent of an investment adviser, to disclose a SAR, or any information that would reveal the existence of a SAR, to various authorities—FinCEN; any Federal, State or local law enforcement agency; or a Federal regulatory authority that examines the investment adviser for compliance with the BSA—provided that no person involved in the reported transaction is notified that the transaction has been reported. As discussed above, FinCEN is proposing to delegate its examination authority for compliance by investment advisers with FinCEN's rules implementing the BSA to the SEC.

The second rule of construction, in § 1032.320(d)(1)(ii)(A)(*2*), would provide two instances where disclosures of underlying facts, transactions, and documents upon which a SAR was based would be permissible: in connection with (i) preparation of a joint SAR or (ii) certain employment references or termination notices. An investment adviser, or any current or former director, officer, employee, or agent of an investment adviser, therefore, would not be prohibited from disclosing the underlying facts, transactions, and documents upon which a SAR is based, including but not limited to, disclosures of such information to another financial institution or any director, officer, employee, or agent of a financial institution, for the preparation of a joint SAR, provided that no person involved in the reported transaction is notified that the transaction has been reported.[194] Similarly, an investment adviser, or any current or former director, officer, employee, or agent of an investment adviser would not be prohibited from disclosing the underlying facts, transactions, and documents upon which a SAR is based connection with certain employment references or termination notices, to the full extent authorized in 31 U.S.C. 5318(g)(2)(B).

The third rule of construction, in § 1032.320(d)(1)(ii)(B), would authorize sharing of a SAR within an investment adviser's corporate organizational structure for purposes consistent with the BSA as determined by regulation or in guidance.

FinCEN recognizes that the sharing of SARs and other relevant information indicative of illicit activity can strengthen the ability of financial institutions to prevent illicit finance activity from entering the U.S. financial system. FinCEN will consider permitting investment advisers to share SARs with certain U.S. affiliates, provided the affiliate is subject to a regulation providing for the confidentiality of SARs issued by FinCEN or by the affiliate's Federal functional regulator, and consistent with SAR sharing guidance finalized in 2010 and applicable to other BSA-defined financial institutions.[195] FinCEN requests comment on this specific issue. FinCEN further requests comment on whether there are other entities or activities where the sharing of SARs would further the purposes of the BSA, and if so, how such sharing would be consistent with the BSA and how investment advisers would be able to maintain the confidentiality of shared SARs.

Section 1032.320(d)(2) would also incorporate the statutory prohibition against disclosure of SAR information by government authorities that have access to SARs other than in fulfillment of their official duties consistent with the BSA. The paragraph would clarify that official duties do not include the disclosure of SAR information in response to a request by a non-governmental entity for non-public information [196] or for use in a private legal proceeding, including a request under 31 CFR 1.11.[197] Accordingly, the provision would not permit such disclosure by government users in response to these requests or uses.

5. Limitation of Liability

Proposed § 1032.320(e) would provide protection from liability, also known as safe harbor, for making either required or voluntary reports of suspicious transactions, or for failures to provide notice of such disclosure to any person identified in the disclosure to the full extent provided by 31 U.S.C. 5318(g)(3).[198] This protection would extend to an investment adviser and any current or former director, officer, employee, or agent of an investment adviser.

6. Compliance

Proposed § 1032.320(f) would note that FinCEN or its delegates would examine compliance by investment advisers with the obligation to report suspicious transactions and provide that failure to comply with the proposed rule may constitute a violation of the BSA and FinCEN's regulations. As discussed above, pursuant to 31 CFR 1010.810(a), FinCEN has overall authority for enforcement and compliance with its regulations, including coordination and direction of procedures and activities of all other agencies exercising delegated authority. Further, pursuant to § 1010.810(d), FinCEN has the authority to impose civil penalties for violations of the BSA and its regulations.

7. Consultation

FinCEN will consult on the SAR filing requirements contained in the proposed rule with the Attorney General and appropriate representatives of State bank supervisors, State credit union supervisors, and the Federal functional regulator as required by section 6202 of the AML Act of 2020 (codified at 31 U.S.C. 5318(g)(5)). Pursuant to this section, in imposing any requirement to report any suspicious transaction under this subsection, the Secretary of the Treasury, in consultation with the Attorney General, appropriate

[194] To the extent permitted by existing FinCEN regulations and guidance, this would include non-U.S. financial institutions.

[195] *See* FinCEN, *Sharing Suspicious Activity Reports by Securities Broker-Dealers, Mutual Funds, Futures Commission Merchants, and Introducing Brokers in Commodities with Certain U.S. Affiliates,* FIN–2010–G005 (Nov. 23, 2010); FinCEN, *Sharing Suspicious Activity Reports by Depository Institutions with Certain U.S. Affiliates,* FIN–2010–G006 (Nov. 23, 2010).

[196] For purposes of this rulemaking, ''non-public information'' refers to information that is exempt from disclosure under the Freedom of Information Act.

[197] 31 CFR 1.11 is the Department of the Treasury's regulation governing demands for testimony or the production of records of Department employees and former employes in a court or other proceeding.

[198] To encourage the reporting of possible violations of law or regulation and the filing of SARs, the BSA contains a safe harbor provision that shields financial institutions making such reports from civil liability. In 2001, the USA PATRIOT Act clarified that the safe harbor also covers voluntary disclosure of possible violations of law and regulations to a government agency and expanded the scope of the safe harbor to cover any civil liability which may exist under any contract or other legally enforceable agreement (including any arbitration agreement). *See* USA PATRIOT Act, section 351(a). Public Law 107–56, Title III, 351, 115 Stat. 272, 321(2001); 31 U.S.C. 5318(g)(3).

representatives of State bank supervisors, State credit union supervisors, and the Federal functional regulators, shall consider items that include—

- the national priorities established by the Secretary;
- the purposes described in section 5311 of the BSA; and
- the means by or form in which the Secretary shall receive such reporting, including the burdens imposed by such means or form of reporting on persons required to provide such reporting, the efficiency of the means or form, and the benefits derived by the means or form of reporting by Federal law enforcement agencies and the intelligence community in countering financial crime, including money laundering and the financing of terrorism.[199]

These items have been considered by the Treasury as described elsewhere in this proposed rule. The AML/CFT National Priorities include combatting corruption, fraud, and transnational crime.[200] For example, as discussed in section II.C above, the absence of AML/CFT requirements for investment advisers, including SAR filing requirements, enables criminals to gain access to the U.S. financial system for purposes of fraud, laundering the proceeds of corruption, and other forms of transnational crime. For these reasons, and the risk of foreign adversaries using investment advisers to gain access to U.S. technology as discussed in section II.C.2, requiring investment advisers to file SARs will be highly useful for criminal and regulatory investigations and intelligence or counterintelligence activities to combat terrorism, and are otherwise consistent with the purposes set forth in section 5311 of the BSA. This section, particularly subsection F.2, details the typologies that should be reported and how advisers may do so in a risk-based manner most beneficial to Federal law enforcement and intelligence agencies.

Through this rulemaking process, Treasury will consult with the relevant State and Federal regulators. This proposed rule has already been sent to the Department of Justice and to the SEC as the Federal functional regulator for investment advisers for interagency consultation, and their input on this issue has been invited. Federal banking regulators have also been invited to comment on all aspects of this proposed rule. Treasury plans to reach out to the Conference of State Banking Supervisors as a representative of State banking and credit union supervisors for consultation on this issue and such supervisors are invited to comment on this proposed rule through the public comment process as well.

G. Special Information-Sharing Procedures To Deter Money Laundering and Terrorist Activity

Proposed §§ 1032.500, 1032.520, and 1032.540 would expressly subject investment advisers to FinCEN's rules implementing the special information-sharing procedures to detect money laundering or terrorist activity of sections 314(a) and 314(b) of the USA PATRIOT Act.[201] Section 314(a) provides that the Secretary of the Treasury adopt regulations to encourage the further cooperation and sharing of information regarding credible evidence of terrorist acts or money laundering activities among financial institutions, their regulatory authorities, and law enforcement authorities.[202] Section 314(b) provides financial institutions with the ability to share information regarding parties suspected of possible terrorist or money laundering activities with another financial institution upon notice to the Treasury under a safe harbor that offers protections from liability.[203]

FinCEN's regulations at 31 CFR part 1010, subpart E—in particular, 31 CFR 1010.520 and 1010.540—implement sections 314(a) and 314(b) of the USA PATRIOT Act, respectively. Section 1010.520, regarding information sharing with government agencies, applies to financial institutions generally. Section 1010.540, regarding voluntary information sharing between financial institutions, applies to financial institutions that are required to have AML/CFT programs—*i.e.,* financial institutions that have not been exempted from that requirement—with certain exclusions. In contrast to the approach described above, FinCEN proposes to require investment advisers to apply these requirements to any mutual funds that they advise.

This proposed rule, by designating investment advisers as financial institutions under the BSA, would apply 1010.520 and 1010.540 to investment advisers. Proposed §§ 1032.500, 1032.520, and 1032.540, moreover, would explicitly subject investment advisers to the provisions of §§ 1010.520 and 1010.540. Section 1032.500 would state generally that investment advisers are subject to the special information sharing procedures of subpart E. In turn, proposed 1032.520 would cross-reference 31 CFR 1010.520, and proposed § 1032.540 would cross-reference 31 CFR 1010.540, expressly applying these provisions to investment advisers. The proposed provisions, therefore, would make clear that FinCEN's rules implementing section 314 would apply to investment advisers. These provisions generally would require an investment adviser, upon request from FinCEN, to expeditiously search its records for specified information to determine whether the investment adviser maintains or has maintained any account for, or has engaged in any transaction with, an individual, entity, or organization named in FinCEN's request.[204] An investment adviser would then be required to report any such identified information to FinCEN.[205]

FinCEN is proposing to apply these information sharing requirements so that investment advisers would be better able to identify and report money laundering, terrorist financing, and other illicit finance activity, and the U.S. Government would have a more detailed understanding of illicit finance activity and risk among investment advisers. Under the proposed rule, which adopts by reference 31 CFR. 1010.540, law enforcement would be able to request from investment advisers, where there is reasonable suspicion and credible evidence, potential lead information that might otherwise never be uncovered.[206] Further, investment advisers would be able to participate in voluntary section 314(b) information sharing arrangements, through which they would be able to gather additional information from other financial institutions, which would enable broader understanding of customer risk and filing of/or file more comprehensive SARs, for example.[207]

FinCEN seeks comment on whether the proposed rule should apply the special information sharing procedures

[199] 31 U.S.C. 5318(g)(5).

[200] *See* FinCEN, *Anti-Money Laundering and Countering the Financing of Terrorism National Priorities (FinCEN, AML/CFT Priorities),* (Jun. 30, 2021), *https://www.fincen.gov/sites/default/files/shared/AML_CFTPriorities(June30%2C2021).pdf.*

[201] *See* 31 CFR 1010.520, 1010.540.

[202] *See* 31 U.S.C. 5311 (statutory notes).

[203] *Id.*

[204] 31 CFR 1010.520(b)(3)(i).

[205] 31 CFR 1010.520(b)(3)(ii).

[206] FinCEN, *FinCEN's 314(a) Fact Sheet* (Sept. 5, 2023), *https://www.fincen.gov/sites/default/files/shared/314afactsheet.pdf.* Covered financial institutions are instructed not to reply to the 314(a) request if a search does not uncover any matching of accounts or transactions.

[207] FinCEN, *FinCEN's 314(b) Fact Sheet* (Dec. 2020), available at *https://www.fincen.gov/sites/default/files/shared/314bfactsheet.pdf* (noting, in part, that participation in information sharing pursuant to section 314(b) is voluntary, and FinCEN strongly encourages financial institutions to participate).

under 31 CFR 1010.520 and 1010.540 to investment advisers. FinCEN also seeks comment on the circumstances under which investment advisers would enter into voluntary 314(b) information sharing arrangements.

H. Special Standards of Diligence; Prohibitions; and Special Measures for Investment Advisers

FinCEN's regulations contain several standards, prohibitions, and other requirements for financial institutions under certain circumstances in 31 CFR part 1010, subpart F (31 CFR 1010.600 through 1010.670). FinCEN is proposing to apply several of these provisions to investment advisers. FinCEN would reflect this in a general cross-reference, proposed § 1032.600, that would state that investment advisers are subject to those ''special standards of diligence; prohibitions; and special measures'', and explicitly cross-reference 31 CFR part 1010, subpart F. FinCEN does not propose to permit investment advisers to exempt from any mutual funds that they advise these requirements under Subpart F. FinCEN is also proposing several other regulatory changes to apply these provisions to investment advisers as discussed further below.

1. Definition of ''Correspondent Account'' and ''Covered Financial Institution''

FinCEN is proposing to amend two definitions in 31 CFR 1010.605 as these definitions would apply to investment advisers. First, it would amend the definition of ''account'' in § 1010.605(c), as applied to the meaning of ''correspondent account,'' to include, as applied to investment advisers, ''any contractual or other business relationship established between a person and an investment adviser to provide advisory services.'' FinCEN seeks public comment on this definition—and more broadly how the concept of a ''correspondent account'' may apply to investment advisers, to the extent investment advisers establish accounts to handle financial transactions, such as treasury investment clearing, for foreign financial institutions.

Second, FinCEN is also proposing to revise 31 CFR 1010.605(e)(1) (as well as add corresponding cross-references as proposed §§ 1032.610 and 1032.620) to include investment advisers in the definition of ''covered financial institution.'' This would have several effects. First, it would expressly subject investment advisers to FinCEN's rules implementing special standards of due diligence for correspondent accounts established or maintained for foreign financial institutions and private banking accounts established or maintained for non-U.S. persons.[208] As described previously and discussed at greater length below, defining investment advisers as ''covered financial institutions'' would ordinarily place investment advisers within the scope of requirements for the collection and verification of beneficial ownership information of legal entity customers as laid out in § 1010.230. However, as described above, FinCEN expects that the requirement to collect and verify beneficial ownership information for legal entity customers to be addressed in a future rulemaking. Accordingly, the proposed revised § 1010.605(e)(1) would expressly provide that an investment adviser would not be considered a ''covered financial institution'' for the purposes of § 1010.230.

2. Special Standards for Diligence

Proposed §§ 1032.610 and 1032.620 adopt by reference §§ 1010.610 and 1010.620, which rely on definitions in 1010.605 in implementing section 312 of the USA PATRIOT Act. Section 312 of the USA PATRIOT Act establishes special due diligence requirements for private banking and correspondent bank accounts involving foreign persons.[209] Because the due diligence requirements of §§ 1010.610 and 1010.620 apply to ''a covered financial institution'' as defined by § 1010.605(e)(1), adding investment advisers to this definition, as discussed, would subject investment advisers to the requirements of §§ 1010.610 and 1010.620. The proposed rule would add cross references (proposed §§ 1032.610 and 1032.620) in the proposed investment adviser regulatory part of the FinCEN regulations, part 1032, directing investment advisers to the due diligence requirements of §§ 1010.610 and 1010.620.

Section 312's implementing regulations require that covered financial institutions maintain due diligence programs for correspondent accounts for foreign financial institutions and for private banking accounts that include policies, procedures, and controls that are reasonably designed to detect and report any known or suspected money laundering or suspicious activity conducted through or involving any such correspondent or private banking accounts.[210] These provisions also set certain minimum standards for such due diligence programs, as well as procedures for enhanced due diligence for correspondent accounts for foreign banks [211] and private banking accounts for senior foreign political figures.[212]

Applying these special standards of due diligence to investment advisers would assist RIAs and ERAs in understanding risk and identifying illicit activity in certain intermediated advisory relationships. Specifically, these standards would address relationships with high-net worth non-U.S. customers and foreign financial institutions that may be acting on behalf of higher-risk non-U.S. customers, when those relationships involve correspondent accounts for foreign financial institutions or private banking accounts.

FinCEN's proposed rule would subject investment advisers to special due diligence standards consistent with the special due diligence standards applied to similarly situated financial institutions under the BSA. For instance, mutual funds, which are advised by RIAs, are already subject to the section 312 requirements.[213] FinCEN requests comment on whether it is appropriate to apply the special due diligence requirements for correspondent and private banking accounts as proposed at §§ 1032.610 and 1032.620 to investment advisers, and if doing so would further the purposes of the BSA and protect the U.S. financial system from national security threats.

3. Special Measures

Section 311 of the USA PATRIOT Act requires U.S. financial institutions to implement certain ''special measures'' if the Secretary finds that reasonable grounds exist to conclude that a foreign jurisdiction, institution, class of transaction, or type of account is a ''primary money laundering concern.'' [214] Section 9714(a) of the Combatting Russian Money Laundering Act allows for similar special measures in the context of Russian illicit finance.[215] FinCEN is proposing that investment advisers be required to comply with special measures issued pursuant to sections 311 and 9714(a) in order to maintain the options available under these sections to protect the U.S. financial system from certain illicit finance threats and to require investment advisers to meet obligations

[208] *See* 31 CFR 1010.610 and 1010.620. FinCEN notes that it does not propose in this rulemaking to amend the definition of ''private banking account'' at 31 CFR 1010.605(m).

[209] Public Law 107–56, section 312 (Oct. 26, 2011), codified as 31 U.S.C. 5318(i).

[210] 31 CFR 1010.610 through 1010.620.

[211] 31 CFR 1010.610(b).

[212] 31 CFR 1010.620(c).

[213] 31 CFR 1024.610 and 1024.630.

[214] 31 U.S.C. 5318A.

[215] Section 9714 (as amended) can be found in a note to 31 U.S.C. 5318A.

consistent with obligations imposed on other BSA-defined financial institutions under sections 311 and 9714 special measures.

As noted above, proposed § 1032.600 would state generally that investment advisers are subject to FinCEN special measures as set forth in subpart F of part 1010 and would cross-reference 31 CFR part 1010, subpart F, which includes section 311 special measures. FinCEN is not proposing any other regulatory changes specifically to apply sections 311 and 9714 special measures to investment advisers. Some special measures, however, base their scope in part on 31 CFR 1010.605's definition of ''covered financial institution.'' [216] Thus, by amending that definition to include investment advisers, as discussed, the proposed rule would be expressly placing investment advisers among the financial institutions subject to these special measures. FinCEN requests comment on whether investment advisers enter into advisory relationships that are similar to a ''private banking account'' relationship as defined at 31 CFR 1010.605.

V. Request for Comment

FinCEN seeks comment on the rule proposed here and whether the proposed rule is appropriate in light of the nature of investment adviser activities and money laundering, terrorism financing, and other illicit finance risks associated with investment advisers. In particular, FinCEN seeks comment on the following aspects of the proposed rule. For all responses, commenters are encouraged to provide the basis for any conclusions drawn in their comments.

Proposed Definition of Investment Adviser

FinCEN requests comment on all aspects of the definition of ''investment adviser'' as proposed in § 1010.100(nnn). In particular:

- Is the definition of ''investment adviser'' sufficiently clear?
- Are there classes of investment advisers included in the proposed definition of investment adviser that present a very low risk for money laundering, terrorist financing, or other illicit finance activity such that they should appropriately be excluded from the definition? If so, why would it be appropriate to exclude such advisers from the definition as opposed to retaining those advisers in the definition and requiring them to adopt an AML/CFT program that is appropriate to their level of risk?
- To what extent are State-registered and foreign investment advisers that do not meet the definition of ''investment adviser'' proposed here at risk for being used for money laundering, terrorist financing, or other illicit finance activity? Should these types of advisers be included in the proposed definition?
- Are there other types of investment advisers that may not meet the definition in the proposed rule that are at risk for abuse by money launderers, terrorist financers, or other illicit actors that should also be subject to the proposed rule for RIAs and ERAs and the corresponding supervision and examination? Are there any entities excluded from the definition of ''investment adviser'' under section 202(a)(11) of the Advisers Act, such as family offices, that are at risk for such abuses?
- Should ERAs be excluded from the proposed definition of investment adviser? How could FinCEN otherwise address the money laundering, terrorist financing, and other illicit finance risk associated with ERAs? Are there such risks that are specific to ERAs?
- With regard to ERAs, are there differences in the risks associated with an adviser that qualifies for and elects to use the exemption under section 203(l) of the Advisers Act as compared to those associated with an adviser that qualifies for and elects to use the exemption under section 203(m) of the Advisers Act that would warrant different treatment under the BSA and the rule proposed here? If so, please offer examples of how each group may be treated under the proposed rule noting how their treatment differs in line with their differing risks.
- Are there certain services or activities provided by investment advisers that present a very low risk for money laundering, terrorist financing, or other illicit finance activity such that they could appropriately be excluded, or cases where applying AML/CFT requirements would result in information of limited value to law enforcement and regulators? Please provide specific examples if so.
- Should the definition of investment adviser apply to non-U.S. advisers registered or required to register with the SEC (for RIAs) or that report to the SEC on Form ADV (for ERAs)? What would be the logistical challenges of this approach?
- What are the benefits to and challenges of requiring such non-U.S. advisers to file reports of suspicious activity with FinCEN on activities involving U.S. customers or the U.S. financial system?

A. Proposed Requirement To Require Advisers To File CTRs and Comply With the Recordkeeping and Travel Rules

FinCEN requests comment on the application of the Recordkeeping and Travel Rules and CTR filing requirements. In particular:

- Are there circumstances where investment advisers should be exempt from complying with the requirements of the Recordkeeping and Travel Rules?
- Do other BSA-defined financial institutions, such as qualified custodians, already collect and record this information for customers of investment advisers that they facilitate transactions for?
- To what extent do investment advisers already regularly and consistently collect the information required under the Recordkeeping and Travel Rules? If you or your firm would be subject to these requirements, to what extent would it represent an additional regulatory cost?
- To what extent do investment advisers work with qualified custodians to maintain separate accounts, subaccounts, or similar products and services to manage a customer's funds, including for purposes of effecting wire transfers?

B. AML/CFT Program Requirement

FinCEN requests comment on all aspects of the proposed AML/CFT program requirement for investment advisers. In particular:

- Which existing requirements under the Advisers Act or the regulations adopted thereunder, or other laws or regulations, could assist investment advisers in complying with the proposed AML/CFT Program requirements? Are any such existing requirements duplicative with any proposed requirements?
- Which existing measures, such as any existing policies and procedures, to implement OFAC sanctions may investment advisers be able to rely on to comply with certain requirements in the proposed rule?
- Would an exemption from the requirements of the proposed rule with respect to customers that are mutual funds be consistent with the purposes of the BSA and avoiding duplication of existing AML/CFT requirements for mutual funds?
- Instead of exempting investment advisers from the requirements of the proposed rule with respect to customers that are mutual funds, should the proposed rule permit investment advisers and their mutual fund

[216] *See, e.g.,* 31 CFR 1010.658(a)(3), 1010.659(a)(5), 1010.660(a)(3), and 1010.661(a)(3).

customer to delegate their AML obligations amongst each other?

- Should investment advisers to mutual funds still be required to monitor for and file SARs on the mutual fund investors? Why or why not?
- Should the exemption for mutual funds be dependent on the nature of the relationship between the investment adviser and its mutual fund customer and the ability of the investment adviser to meet AML/CFT obligations?
- Other than mutual funds, are there other categories of entities that could be, on a risk-basis, reasonably exempted from an investment adviser's AML/CFT program? Why or why not?
- Should we require an investment adviser to include in its AML/CFT program all of the advisory services it provides, including whether acting as the primary adviser or a subadviser?
- Are there certain subadvisory activities or circumstances that should be included or excluded from coverage of this proposed rule, such as the specific services provided as a subadviser or the particular type of investment adviser serving as the primary adviser?
- To what extent would a subadviser's AML/CFT program overlap with the primary adviser's AML/CFT program and how could possible duplication of effort be mitigated? For example, should the proposed rule expressly permit a subadviser to consider the existence and operation of the primary adviser's program in satisfying the subadviser's own obligations?
- Is there an increased risk for a subadviser to be used for money laundering, terrorist financing, or other illicit finance activity when providing advisory services to a customer that has a primary adviser that is not an investment adviser (as defined in the proposed rule)?
- Are there other similar arrangements where an investment adviser may be sub-contracted to provide services to another investment adviser that should or should not be in scope of an investment adviser's AML/CFT program?
- Do investment advisers that are affiliated with a dually registered bank or broker-dealer currently apply AML/CFT program requirements and other AML/CFT measures applicable to the bank or broker-dealer in any of their advisory activities? If so, which activities and which requirements are applied?
- How do investment advisers that are subsidiaries of banks currently apply AML/CFT measures that are applicable to their parent banks?
- How do investment advisers that are affiliated with a bank or broker-dealer apply enterprise-wide AML/CFT requirements? Are there certain enterprise-wide AML/CFT requirements that are presently tailored to address the risks arising in advisory activities?
- What information do fund administrators currently collect that would support implementation of the proposed rule?
- Is it appropriate to allow an adviser to delegate some elements of its AML/CFT program to an entity with which the customer, and *not* the adviser, has the contractual relationship? This would include entities providing services to funds advised by the RIA or ERA.
- Are there challenges for delegating certain requirements of the proposed rule to fund administrators? Are there differences in those challenges for fund administrators whose operations are primarily conducted inside the United States compared to those whose operations are primarily conducted outside of the United States?
- Can fund administrators whose operations are primarily conducted outside of the United States collect and provide information on offshore pooled investment vehicles when that information is requested by a U.S. investment adviser? What types of challenges might U.S. investment advisers face in receiving such information?
- If some or all requirements of the proposed rule are delegated to fund administrators whose operations are primarily conducted outside of the United States, will the investment adviser be able to effectively monitor implementation of those requirements?

C. Proposed Minimum Requirements of the AML/CFT Program

FinCEN seeks comment on the minimum requirements for an investment adviser's AML/CFT program as proposed in § 1032.210(b). In particular:

- Should closed-end registered funds, wrap fee programs, or other types of accounts advised by investment advisers be, on a risk-basis, reasonably exempted from an investment adviser's AML/CFT program?
- How can the requirements of the proposed rule be applied to advisers participating in a wrap fee program, to include when an adviser acting as portfolio manager is either affiliated or not affiliated with the sponsoring entity of the program?
- The requirements of 31 U.S.C. 5318(h)(5) state that the ''duty to establish, maintain and enforce'' the financial institution's AML/CFT program ''shall remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to oversight and supervision by, the Secretary of the Treasury and the appropriate Federal functional regulator.'' FinCEN invites comments on how this would impact RIAs and ERAs, including the extent to which compliance with this requirement would require changes to existing AML/CFT programs and estimated associated costs with any such changes.

1. Applicability to Private Funds

- What information is currently available to advisers to private funds regarding the investors in private funds that could help advisers comply with the proposed AML/CFT Program requirement?
- Are there other factors related to the activities, investors, or structure of a private fund that could be higher- or lower-risk?
- Should a subadviser to a private fund or other unregistered pooled investment vehicle with a primary adviser that is not an investment adviser (as defined in the proposed rule) be required to establish the same policies, procedures, and internal controls as when the primary adviser is an investment adviser (as defined in the proposed rule)?
- If an investor in the private fund or other unregistered pooled investment vehicle is itself a pooled investment vehicle, should a subadviser to the private fund be required to identify risks and incorporate policies, procedures, and internal controls within its AML/CFT program to mitigate the risks of the investing pooled investment vehicle's investors, sponsoring entity, and/or intermediaries when there is an increased risk of money laundering, terrorist financing, or other illicit activity? How might a subadviser identify when increased risks are present?
- How should the proposed rule apply to advisers who manage private funds that receive investments from in-funds? To what extent should advisers be able to rely on the AML/CFT Program of advisers to other funds?
- How should the proposed rule apply to an adviser to a private fund who has funds-of-funds who are investors? To what extent should they be able to rely on the AML/CFT Program of advisers who advise funds-of-funds?

2. Risk-Based Procedures for Ongoing Customer Due Diligence

- What customer diligence procedures do RIAs already have in place to meet the representations in the SIFMA No-Action Letter? Do ERAs have similar procedures in place?
- What other types of information do investment advisers regularly receive from their customers that could be used to understand the nature and purpose of a customer relationship?
- How would investment advisers exchange information with other financial institutions involved in facilitating customer transactions, such as qualified custodians, to understand the nature and purpose of a customer relationship and conduct ongoing monitoring to identify suspicious transactions?
- How may investment advisers apply the requirement for ongoing monitoring to identify suspicious transactions differently than other financial institutions, such as banks and broker-dealers?

3. Identification and Verification of Beneficial Owners of Legal Entity Customers

- Do you agree with the proposal to wait to apply the requirement to collect and verify the beneficial ownership information of legal entity accounts at § 1010.230 to investment advisers until at or after the CTA-mandated revisions to the CDD Rule, or should Treasury apply the existing requirement as soon as a CIP requirement for investment advisers is effective?
- What types of information regarding private funds, other than beneficial ownership information, could an investment adviser collect to understand the nature and purpose of a customer relationship with a private fund and conduct ongoing monitoring to identify suspicious transactions involving the private fund?

D. Proposed Suspicious Activity Reporting Rule

FinCEN seeks comment on all aspects of the suspicious activity reporting rule as proposed in § 1032.320. In particular:

- Which existing requirements under the Advisers Act or other laws or regulations could assist investment advisers in complying with the proposed SAR requirements?
- Should there be an exception to the proposed SAR filing requirement for certain violations that are appropriately reported to the SEC under the Federal securities laws?
- Should there be an exception to the proposed SAR filing requirement for violations with respect to a mutual fund advised by the investment adviser, as proposed? If not, would requiring investment advisers to file SARs while exempting mutual funds from an investment adviser's AML/CFT program (as proposed) produce any operational or other difficulties or challenges?
- What guidance would be useful in identifying activity that may require the filing of a SAR?
- How would an investment adviser apply the proposed SAR filing obligation for assets held by a qualified custodian? How would an investment adviser obtain, share, and receive information about a customer or transactions with a qualified custodian regarding potential suspicious activity?
- Would the ability to share SARs with corporate affiliates that are subject to their own SAR confidentiality regulation assist in furthering the purposes of the BSA?
- Are there other entities or activities where the sharing of SARs would further the purposes of the BSA? How would such sharing be consistent with the purposes of the BSA and how would investment advisers be able to maintain the confidentiality of shared SARs?

E. Special Information Sharing Procedures

- FinCEN seeks comment on whether the proposed rule should apply the special information sharing procedures under 31 CFR 1010.520 and 1010.540 implementing sections 314(a) and 314(b) of the USA PATRIOT Act to investment advisers, as proposed at §§ 1032.500 and 1032.540 (cross-referencing 31 CFR part 1010, subpart E, and 31 CFR 1010.540, respectively).
- Under what circumstances would investment advisers enter into voluntary 314(b) information sharing arrangements?

F. Special Due Diligence and Section 311 Measures

- FinCEN seeks comment on whether it is appropriate to apply the special due diligence requirements for correspondent and private banking accounts to investment advisers as proposed at 1032.610 and 1032.620 (cross-referencing 31 CFR 1010.610 and 1010.620, respectively), and the special measures under section 311 of the USA PATRIOT Act as proposed at 31 CFR 1032.600. Would doing so further the purposes of the BSA and protect the U.S. financial system from national security threats?
- To what extent do investment advisers provide advisory services or enter into advisory relationships that are similar to a ''correspondent account'' relationship as defined at 31 CFR 1010.605? What about with respect to a ''correspondent account'' as that term would be amended, as proposed?
- To what extent do investment advisers enter into advisory relationships that are similar to a ''private banking account'' relationship as defined at 31 CFR 1010.605?

VI. Severability

If any of the provisions of this proposed rule, or the application thereof to any person or circumstance, is held to be invalid, such invalidity shall not affect other provisions or application of such provisions to other persons or circumstances that can be given effect without the invalid provision or application.

VII. Regulatory Analysis

In accordance with Executive Orders 12866, 13563, and 14094 (E.O. 12866 and its amendments),[217] this regulatory impact analysis (Impact Analysis) is composed of a number of assessments of the anticipated impacts of the proposed rule in terms of its expected costs and benefits to affected parties. This analysis also includes assessments of the impact on small entities pursuant to the Regulatory Flexibility Act (RFA) and reporting and recordkeeping burdens under the Paperwork Reduction Act (PRA), as well as consideration of whether an assessment under the Unfunded Mandates Reform Act of 1995 (UMRA) is required.

This Impact Analysis finds that the impact associated with the proposed rule would primarily affect investment advisers (specifically, RIAs and ERAs) and U.S. Federal agencies, and estimates that the total present value of costs of the proposed rule over a 10-year time horizon ranges from $4.6 billion to $9.3 billion, with a primary estimate of $8 billion, using a 2 percent discount rate. The annualized costs over a 10-year time horizon range from $500 million to $1 billion, with a primary estimate of $870 million, using a 2 percent discount rate.[218] This proposed rule has been determined to be a ''significant regulatory action'' under section 3(f) of Executive Order 12866 and significant under section 3(f)(1) because it may have an annual effect on the economy of $200 million or greater.

Table 1 summarizes the benefits and costs of the proposed regulation. The potential benefits are difficult to quantify—and thus are unquantified in

[217] *See infra.*

[218] All aggregate figures are approximate and not precise estimates unless otherwise specified.

this Impact Analysis—but are reported alongside the monetized costs:

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Table 1. Summary of Benefits and Costs of the Proposed Regulation

Category	Primary Estimate ($M)	Low Estimate ($M)	High Estimate ($M)	Dollar Year	Discount Rate	Time Horizon	Notes
BENEFITS							
Annualized Monetized Benefits	N/A	N/A	N/A	2022	2%	10 years	
Unquantified Benefits	• Increase access for law enforcement to relevant information for complex financial crime investigations and asset forfeiture. • Enhance the ability of law enforcement to identify and prosecute money laundering and other financial crimes. • Enhance interagency understanding of priority national security threats and their associated financial activity. • Enhance the ability of national security personnel to protect against priority national security threats. • Improve financial system transparency and integrity, and align with international financial standards to strengthen the U.S. financial system from abuse by illicit actors.						
COSTS							
Annualized Monetized Costs	$870	$490	$1,000	2022	2%	10 years	
Unquantified Costs	• N/A						

Category	Effects	Notes
Effects on State, Local, or Tribal Governments	No estimated impact to State, local, or Tribal governments.	
Effects on Small Businesses	Estimated annualized cost burden of $41,000 for small investment advisers, or approximately 2.4 percent of average revenues.	Annualized cost burden estimated over 10 years using a 2 percent discount rate.
Effects on Wages	The proposed regulation is not anticipated to have significant impacts on wages.	
Effects on Growth	Investment advisers are likely to pass on the increased costs of managing accounts to clients through higher fees, which may reduce earnings on investments.	

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FinCEN has chosen to issue the proposed rule applying AML/CFT requirements to RIAs and ERAs instead of two regulatory alternatives: (1) applying AML/CFT requirements to RIAs, ERAs, and State-registered investment advisers and (2) requiring private funds to collect beneficial ownership information on legal entity investors. The first alternative would expand the requirements of the BSA to nearly twice as many entities (as compared to the proposed rule) at a greater overall cost but provide a similar level of benefits (with only limited

incremental benefits attributable to State-registered investment advisers), while the second would reduce the costs of the regulation (as compared to the proposed rule) while providing fewer benefits and only achieving a small proportion of the objectives of the BSA.

FinCEN has conducted an initial regulatory flexibility analysis (IRFA) pursuant to the RFA and finds that the proposed rule would have a significant economic impact on small entities, although FinCEN does not assess the number of small entities impacted to be substantial.

As detailed in the PRA analysis, for the private sector the proposed rule is estimated to result in an estimated one-time, upfront information collection burden of 7.65 million hours and an average annual information collection burden of 5.49 million hours thereafter. The estimated one-time, upfront information collection cost is approximately $454 million and the estimated average annual recurring information collection cost is approximately $316 million thereafter. These costs are included in the Impact Analysis.

Pursuant to its UMRA-related analysis, FinCEN has not anticipated any expenditures for State, local, and Tribal governments. FinCEN anticipates expenditures by the private sector of more than $176 million.[219] The UMRA-related analysis for private sector entities has been incorporated into this Impact Analysis.

A. Executive Orders 12866 and Its Amendments

As detailed below, Treasury assesses that RIAs and ERAs pose a material risk of misuse for illicit finance. Including investment advisers as ''financial institutions'' under the BSA and applying comprehensive AML/CFT measures to these investment advisers are likely to reduce this risk.

1. Introduction

Executive Order 12866 and its amendments direct agencies to assess costs and benefits of available regulatory alternatives and, if regulation is necessary, to select regulatory approaches that maximize net benefits (including potential economic, environmental, and public health and safety effects; distributive impacts; and equity). Executive Order 13563 emphasizes the importance of quantifying both costs and benefits, reducing costs, harmonizing rules, and promoting flexibility. This proposed rule has been designated a ''significant regulatory action'' under section 3(f) of Executive Order 12866 and significant under section 3(f)(1). Accordingly, the proposed rule has been reviewed by the Office of Management and Budget (OMB).

In accordance with OMB guidance, this Impact Analysis contains, as follows: (1) a statement of the need for the regulatory action; (2) a clear identification of a range of regulatory approaches; and (3) an estimate of the benefits and costs—quantitative and qualitative—of the proposed regulatory action and its alternatives.

(a) Statement of the Need for, and Objectives of, the Proposed Rule

The primary purpose of the proposed rule is to address identified illicit finance risks among investment advisers (*i.e.,* RIAs and ERAs). Currently, investment advisers are not required by regulation to apply measures designed to address money laundering, terrorist financing, and other illicit finance risks similar to those which other financial institutions are subject. For example, investment advisers are generally not required to establish an AML/CFT program, to conduct customer due diligence, or to report suspicious customer activity to FinCEN. This means that tens of thousands of investment advisers overseeing the investment of hundreds of trillions of dollars into the U.S. economy currently do not face regulatory sanction for failing to implement the above-mentioned measures, creating a material weakness in the United States's framework to combat illicit finance.

As described in detail above, investment advisers work closely with and provide services that are similar or related to services authorized to be provided by other BSA-defined financial institutions.[220] While investment advisers do not directly custody customer assets, they generally must understand their customers' financial background and investment goals to provide advisory services, and they direct banks and broker-dealers to execute transactions and disperse funds to support their customers' investment objectives.

Under the current AML/CFT regulatory framework applicable to investment advisory activities, the financial institutions that engage in trading or transactional activities on behalf of investment advisers, such as banks and broker-dealers, are subject to AML/CFT reporting and recordkeeping obligations. However, for many of these financial institutions, the investment adviser, and not the investment adviser's customers, is their customer. Consequently, they may rely solely on an investment adviser's instructions and lack independent knowledge of the adviser's customers. In some cases, an investment adviser may be the only person or entity with a complete understanding of the source of a customer's invested assets, background information regarding the customer, or the objectives for which the assets are invested. Additionally, an investment adviser may use multiple broker-dealers or banks for trading or custody services.

As a result, one financial institution may not have the complete picture of an adviser's activity or information regarding the identity and source of wealth of the advisers' customers, and thus may not be well-positioned to assess whether funds managed by the adviser may be derived from illicit proceeds or associated with a criminal or other illicit finance activity. Without complete information, such an institution may not have sufficient information to warrant filing a SAR, or may be required to file a SAR that only has partial information concerning the investment adviser's transactions on behalf of a particular customer. This limits the ability of law enforcement to identify illicit activity that may be occurring through investment advisers.

As discussed in the preamble, the proposed rule would address this gap by requiring RIAs and ERAs to implement AML/CFT programs, which include risk-based procedures for conducting ongoing customer due diligence, and report suspicious activity to FinCEN, among other requirements. RIAs and ERAs would be subject to examination for compliance with these requirements by the SEC. This would reduce instances of investment advisers unwittingly laundering the illicit proceeds on behalf of clients and increase the likelihood that authorities could detect illicit activity occurring through investment advisers and better

[219] The U.S. Bureau of Economic Analysis reported the annual value of the gross domestic product (GDP) deflator in 1995 (the year in which UMRA was enacted) as 71.823; and in 2022 as 127.215. *See* U.S. Bureau of Economic Analysis, Table 1.1.9. ''Implicit Price Deflators for Gross Domestic Product,'' *https://apps.bea.gov/iTable/?reqid=19&step=2&isuri=1&categories=survey%23eyJhcHBpZCI6MTksInN0ZXBzIjpbMSwyLDMsM10sImRhdGEiOltbIkNhdGVnb3JpZXMiLCJTdXJ2ZXkiXSxbIk5JUEFfVGFibGVfTGlzdCIsIjEzIl0sWyJGaXJzdF9ZZWFyIiwiMTk5NSJdLFsiTGFzdF9ZZWFyIiwiMjAyMSJdLFsiU2NhbGUiLCIwIl0sWyJTZXJpZXMiLCJBll1dfQ.* Thus, the inflation adjusted estimate for $100 million is 127.215 divided by 71.823 and then multiplied by 100, or $177 million.

[220] *See supra* section IV.A.

detect complicit investment advisers that knowingly facilitate money laundering, terrorist financing, or other illicit finance activity. The proposed rule would also bring the investment adviser industry more in line with its counterparts in the U.S. financial sector and around the world.

(b) Summary of the Proposed Rule

The proposed regulations would add ''investment adviser'' to the definition of ''financial institution'' at 31 CFR 1010.100(t) and add a new provision to § 1010.100 defining the term ''investment adviser'' to mean RIAs and ERAs.

With these changes to 31 CFR 1010.100, the proposed rule would then subject RIAs and ERAs to AML/CFT requirements applied to financial institutions, including requiring them to: (i) develop and implement an AML/CFT program; (ii) file SARs and CTRs; (iii) record originator and beneficiary information for transactions (Recordkeeping and Travel Rules); (iv) respond to section 314(a) requests; and (v) implement special due diligence measures for correspondent and private banking accounts.

AML/CFT Program. RIAs and ERAs would be required to maintain an AML/CFT program, including: (i) developing internal policies, procedures, and controls to comply with the requirements of the BSA and address money laundering, terrorist financing, and other illicit finance risks; (ii) designating an AML/CFT compliance officer; (iii) instituting an ongoing employee training program; (iv) soliciting an independent test of AML/CFT programs for compliance; and (v) implementing risk-based procedures for conducting ongoing customer due diligence.

File SARs and CTRs. RIAs and ERAs would be required to file a report of any suspicious transaction relevant to a possible violation of law or regulation with FinCEN. In addition, RIAs and ERAs would be required to report transactions in currency over $10,000. Currently, all investment advisers report such transactions on Form 8300. Under the proposed rule, a CTR would replace Form 8300 for RIAs and ERAs.

Recordkeeping and Travel Rules. RIAs and ERAs would be required to obtain and retain originator and beneficiary information for certain transactions and pass on this information to the next financial institution in certain funds transmittals involving more than one financial institution.

Respond to Section 314(a) Requests. FinCEN's regulations under section 314(a) enable law enforcement agencies, through FinCEN, to reach out to financial institutions to locate accounts and transactions of persons that may be involved in terrorism or money laundering. Requests contain subject and business names, addresses, and as much identifying data as possible to assist the financial industry in searching their records.

Special Due Diligence Measures for Correspondent and Private Banking Accounts. The proposed rule would require RIAs and ERAs to maintain due diligence measures that include policies, procedures, and controls that are reasonably designed to enable the investment adviser to detect and report, on an ongoing basis, any known or suspected money laundering or suspicious activity conducted through or involving any correspondent or private banking account that is established, maintained, administered, or managed in the United States for a foreign financial institution.

(c) Discussion of Concurrent/Overlapping/Conflicting Regulations

There are no Federal rules that directly and fully duplicate, overlap, or conflict with the proposed rule. The majority of the investment adviser industry is not subject to any comprehensive AML/CFT requirements. FinCEN is aware that requirements within the Advisers Act and other Federal securities laws impose requirements upon investment advisers that in some instances are similar to the requirements proposed within the proposed rule and perform similar roles (*i.e.,* improving the integrity of the U.S. financial system and protecting customers). FinCEN also recognizes that the Advisers Act and its implementing regulations authorize the SEC to regulate the investment adviser industry for compliance with these requirements.

However, while these existing requirements are important, and may provide a supporting framework for implementing certain obligations in the proposed rule, they do not impose the specific AML/CFT measures in the proposed rule in support of the BSA's statutory purposes. Specifically, investment advisers are not required to develop policies, procedures, and internal controls to identify and mitigate the risk that the adviser might be used for money laundering, terrorist financing, or other illicit finance purposes. Currently, investment advisers are not required to appoint an AML/CFT officer or train their employees to comply with AML/CFT requirements. They are not required to report suspicious activity, maintain certain transaction records, or respond to section 314(a) requests for information on customer accounts or transactions. The existing rules and regulations under the Advisers Act are designed to prevent adviser fraud or theft of client assets and otherwise protect investors, maintain fair, orderly and efficient markets, and facilitate capital formation. Preventing illicit actors from using the investment adviser industry to launder the proceeds of crime or finance terrorism is not contemplated in existing obligations on the industry.

FinCEN recognizes that investment advisers that are dually registered as a broker-dealer or are chartered as a banks (and bank subsidiaries) or are already subject to AML/CFT requirements. As noted above, FinCEN is not proposing to require such entities to establish multiple or separate AML/CFT programs so long as a comprehensive AML/CFT program covers all of the entity's applicable legal and regulatory obligations. The program should be designed to address the different money laundering, terrorist financing, or other illicit finance activity risks posed by the different aspects of the entities' businesses and satisfy each of the risk-based AML/CFT program requirements to which it will be subject in its capacity as an investment adviser, broker-dealer, or bank under the proposed rule. Similarly, an investment adviser that is affiliated with, or a subsidiary of, another entity required to establish an AML/CFT program in another capacity would not be required to implement multiple or separate programs because one single program can be extended to all affiliated entities that are subject to the BSA, so long as it is designed to identify and mitigate the different money laundering, terrorist financing, and other illicit finance activity risks posed by the different aspects of the entity's business and satisfies each of the risk-based AML/CFT program and other BSA requirements to which the entity is subject in all of its regulated capacities.

FinCEN is likewise aware that investment advisers serve as advisers to mutual funds, which have their own AML/CFT program requirements. For the reasons described above, FinCEN is proposing that an RIA advising a mutual fund may deem its AML/CFT program requirements with respect to such mutual fund satisfied so long as the mutual fund has developed and implemented an AML/CFT program compliant with the AML program requirements applicable to mutual funds.

FinCEN is also aware that the SEC already examines certain investment

advisers for compliance with the Advisers Act and implementing regulations. FinCEN anticipates that the SEC's examination of RIA and ERA compliance with new requirements will be incorporated into its risk-based examination program.

(d) Report Organization

This Impact Analysis is structured as follows. Section 2 assesses the nature and characteristics of the entities and their business that will be affected by the proposed rule. Section 3 then identifies the expected benefits of the proposed rule, and section 4 then assesses the expected costs of the proposed rule to both the private sector and government and explains the methodology for doing so. Section 5 then assesses potential regulatory alternatives to issuing the proposed rule.

Following the Impact Analysis are the regulatory analyses required by the RFA, PRA, UMRA, and other similar laws. These analyses rely on certain calculations in the Impact Analysis. Following those are a series of questions for public comment regarding the Impact Analysis and its methodology which aim to test and refine the assumptions and calculations made within the Impact Analysis.

2. Affected Entities

This section identifies and characterizes the population of investment advisers that are likely to be impacted by the proposed rule. The proposed rule would cover both RIAs and ERAs. These groups generally may vary in terms of their business structure, AUM, number of employees, and number of client relationships. As explained below, these differences affect the estimated burden of the proposed rule, in part, because depending on their business structure, some RIAs and ERAs may already be implementing AML/CFT measures to some degree.

To establish a pre-regulation baseline, this section provides a profile of investment advisers likely to be affected by the proposed rule. First, it describes which investment advisers will be affected by the proposed rule and on what basis. Next, it describes how RIAs and ERAs are categorized based on business structure, in ways that align with the expected costs of the proposed rule. Next, it describes the baseline level of economic activity for each type of entity. Finally, it describes other characteristics of the regulated population, including the number of small businesses.

(a) Universe of Investment Advisers Affected by the Proposed Rule

The Advisers Act defines an investment adviser as a person or firm that, for compensation, is engaged in the business of providing advice to others or issuing reports or analyses regarding securities.[221] The proposed rule would cover two subsets of investment advisers: RIAs, who register or are required to register with the SEC; and ERAs, who are exempt from registration but must report certain information to the SEC.

Each RIA and ERA must submit the Uniform Application for Investment Adviser Registration (commonly known as Form ADV) and update it on an annual basis with the SEC.[222] Form ADV is an SEC-administered self-disclosure form that collects certain information about each RIA and ERA. RIAs must report ownership, clients, employees, business practices, custodians of client funds, and affiliations, as well as any disciplinary events of the adviser or its employees, and marketing and certain disclosure reporting materials it provides to clients. ERAs report a subset of this information.

i. SEC Registration and Reporting Criteria

Unless eligible to rely on an exemption, investment advisers that manage more than $110 million must register with the SEC, rather than a State authority, as well as submit a Form ADV and update it at least annually.[223] Besides having AUM above $110 million, additional criteria may result in an investment adviser registering with the SEC.[224] For example, investment advisers with AUM of at least $100 million but less than $110 million are allowed, but not required, to register with the SEC. Unless a different exception from the prohibition on registration applies, investment advisers with AUM under $100 million are prohibited from registering with the SEC,[225] but must register instead with the relevant State securities regulator.

An ERA is an investment adviser that would be required to register with the SEC but is statutorily exempt from such requirement because: (1) it is an adviser solely to one or more venture capital funds, or (2) it is an adviser solely to private funds and has AUM in the United States of less than $150 million.[226] ERAs are required to report to the SEC on Form ADV.

ii. Size of the Regulated Population

The number of RIAs and ERAs is well-defined based on the number of Form ADV filings. Table 2.1 shows the number of RIAs and ERAs as of July 2023 based on each inclusion criterion listed above. One RIA was excluded from the regulated population because they reported an implausibly high number of total clients.

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[221] *See* 15 U.S.C. 80b–2(a)(11) for this definition of ''investment adviser.'' The statute excludes some persons and firms: certain banks, certain professionals, certain broker-dealers, publishers, statistical ratings agencies, and family offices. *See* 15 U.S.C. 80b–2(a)(11)(A)–(G).

[222] *See* 17 CFR 275.203–1 and 204–4. A detailed description of Form ADV's requirements is available at *https://www.sec.gov/oiea/investor-alerts-bulletins/ib_formadv.html.*

[223] Exceptions to this registration requirement include (1) venture capital advisers, (2) private fund advisers with AUM under $150 million, (3) advisers to life insurance companies, (4) foreign private advisers, (5) advisers to charitable organizations, (6) certain commodity trading advisers, (7) advisers to small business investment companies, and (8) advisers to rural business investment companies. *See* 15 U.S.C. 80b–3(b).

[224] Other exceptions to the prohibition on SEC registration include: (1) an adviser that would be required to register with 15 or more States (the multi-State exemption); (2) an adviser advising a registered investment company; (3) an adviser affiliated with an RIA; and (4) a pension consultant. Persons satisfying these criteria and the definition of ''investment adviser'' are required to register as investment advisers with the SEC. *See* Form ADV: Instructions for Part IA, Item 2. Advisers with a principal office and place of business in New York and over $25 million AUM are required to register with the SEC.

[225] 17 CFR 275.203A–1. Note that if an RIA's AUM falls below $90 million as of the end of such RIA's fiscal year then it must withdraw its registration with the SEC, unless otherwise eligible for an exception to the prohibition on SEC registration.

[226] *See* sections 203(*l*) and 203(m) of the Advisers Act and 17 CFR 275.203(*l*)–1 and 275.203(m)–1, respectively.

Table 2.1. Regulated Population of RIAs and ERAs[227]

	RIAs			ERAs	
	AUM at Least $100 Million[228]	AUM > $25 Million, no State-level Exam	Other Reason for Registration	VC Fund	Private Fund
Number of investment advisers	13,313	468	2,986	2,016	4,422
Total	**15,391**			**5,846**	

In total, there are 15,391 RIAs, with total AUM of $125 trillion and roughly 972,000 total employees. There are also 5,846 ERAs with total gross assets of $5.2 trillion (ERAs do not report the number of employees to the SEC).[229] With limited exceptions, the proposed rule would not apply to RIAs with respect to their mutual funds[230] (ERAs do not advise mutual funds).[231] Therefore, as a practical matter, RIAs that exclusively advise mutual funds would be exempt from most the requirements of this rule. Details on cost estimates for these advisers are provided in the next sub-section.

(b) Categorizing the Regulated Population Based on Business Structure

The economic impact of the proposed rule will depend on an adviser's business structure and the extent to which such an adviser is already implementing some AML/CFT requirements. FinCEN assesses that RIAs and ERAs dually registered as broker-dealers or banks, are a subsidiary or affiliate of a bank or broker-dealer are more likely to already apply a *significant* or *moderate* number of the requirements of the proposed rule. Additionally, as described below, survey data indicates that some RIAs are already implementing certain requirements of the proposed rule.

RIAs and ERAs are also subject to a variety of regulations and reporting requirements, such as those under the Federal securities laws, in addition to the proposed rule. In some cases, compliance with existing regulations under the Federal securities laws may reduce the burden of the proposed rule. In addition, RIAs and ERAs rely on third-party entities to execute business services, and those entities may be required to comply with AML/CFT regulations. Depending on the business structure of an RIA or ERA, such third-party relationships may also reduce the burden of the proposed rule.

Therefore, FinCEN categorized RIAs and ERAs based on their likelihood of having existing AML/CFT measures in place, and the extent of those measures. This subsection first details the justification for the categorization, based on the regulatory structure of the investment adviser industry and associated institutions. The subsection then describes each category of the regulated population.

i. Dual Registrants and AML/CFT-Compliant Entities Associated With RIAs and ERAs

Some RIAs and ERAs are dually registered as, subsidiaries of, or affiliated with, entities that are already subject to AML/CFT obligations and, therefore, may already be applying such obligations to their advisory activities, although they may not be legally obligated to do so.[232] For instance, dual registrants may seek to provide customers with both brokerage and advisory services, and apply AML/CFT measures across their businesses rather than incurring greater costs by duplicating measures across each business. Additionally, some AML/CFT measures, such as employee training and initial customer due diligence, can be designed to apply across a firm rather than to specific activities.

Further, in past Treasury outreach to financial institutions, those that have a financial subsidiary subject to AML/CFT program obligations as well as a subsidiary investment adviser have indicated they choose to typically apply an enterprise-wide AML/CFT program extending to all their subsidiaries and their customers so that all business lines or entities in their corporate enterprise are subject to consistent risk practices and procedures.

In other circumstances, an RIA or ERA may perform AML/CFT functions via contract with a broker-dealer or other financial institution, such as when the adviser advises a mutual fund, or the adviser may have voluntarily implemented certain AML/CFT measures, such as due diligence or identification requirements.[233] Many RIAs and ERAs also frequently use the services of certain third-party entities that are required to comply with AML/CFT regulations, namely, prime brokers, qualified custodians (*e.g.,* banks), and in some circumstances, fund administrators.

[227] Based on a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n.26. The sum across individual categories for RIAs and ERAs is greater than the total because each investment adviser may belong in more than one category.

[228] This category also includes already-registered RIAs whose AUM is less than $100 million but at least $90 million.

[229] ERAs report gross assets for each fund they advise, but only if that fund is not reported by another RIA in its own Form ADV; therefore, some ERAs report zero gross assets because all of the funds they advise are also reported by another RIA.

[230] *See* 31 CFR 1010.100(gg). *See* section IV.B for additional detail on the treatment of mutual funds under the proposed rule.

[231] FinCEN does not propose to permit investment advisers to exempt mutual funds that they advise from the requirements 31 CFR part 1010, subparts E and F (31 CFR 1010.520, 1010.540, and 1010.600 through 1010.670) that FinCEN proposes to apply to RIAs and ERAs in the proposed rule (*e.g.,* certain information sharing, special standards, prohibitions, and other requirements).

[232] *See* Treasury, *2022 National Money Laundering Risk Assessment,* p. 63–66, *https://home.treasury.gov/system/files/136/2022-National-Money-Laundering-Risk-Assessment.pdf.*

[233] *See* SIFMA No Action Letter, supra n. 52; *see also* Managed Funds Association, Sound Practices for Hedge Fund Managers (2009), Chapter 6 (Anti-Money Laundering).

ii. Existing Laws and Regulations

The Advisers Act and its implementing rules and regulations form the primary existing framework governing investment adviser activity. Some rules and regulations that apply to RIAs are relevant to AML/CFT compliance and may lower the cost of compliance, including, as discussed further below: (1) the Custody Rule, which governs the custody of client funds and securities, often through relationships with qualified custodians who are often subject to AML/CFT requirements; and (2) the Compliance Rule, which governs policies and procedures designed to prevent violations of the Advisers Act, and establishes a procedural and organizational framework that RIAs may be able to build upon to implement AML/CFT measures, thus lowering the cost of compliance with the proposed rule.

Custody Rule. The Custody Rule requires that client funds or securities over which an RIA has custody be held at a qualified custodian.[234] The qualified custodian may hold the funds or securities in separate accounts for each client under that client's name; or in accounts under the name of the RIA as agent or trustee for clients, with only client funds and securities inside. Qualified custodians can be banks, registered broker-dealers, futures commission merchants, or certain foreign entities. Because such qualified custodians are BSA-defined financial institutions (or their equivalents under foreign law) that must comply with AML/CFT regulations, accounts maintained on behalf of an RIA—and the associated client relationships—are subject to AML/CFT requirements.

Compliance Rule. Under the Compliance Rule,[235] an RIA must adopt and implement written policies and procedures reasonably designed to prevent violations of the Advisers Act and the rules thereunder. RIAs must review their policies and procedures at least annually and designate a chief compliance officer to administer the policies and procedures. Although these policies and procedures do not include requirements that an RIA comply with the BSA, having written policies in place may reduce the time needed to develop and review specific AML/CFT policies and procedures. Alternatively, having a framework in place for establishing policies and procedures may be useful for RIAs in complying with the proposed rule. Additionally, the presence of a compliance officer may reduce costs associated with designating an AML/CFT compliance officer, for example by dual-hatting the current chief compliance officer.

Other Requirements. Certain private fund advisers also fill out Form PF, which requires disclosure of limited beneficial ownership information; for example, the percentage of the fund's equity owned by broker-dealers, pension plans, and U.S. and non-U.S. persons.[236] Some investment advisers may have policies and procedures to comply with OFAC sanctions, which similarly may provide a framework for implementing certain AML/CFT measures included in the proposed rule.

Due to these information collection requirements, RIAs and ERAs already compile varying amounts of information that could be useful in AML/CFT compliance—particularly information related to the identity and citizenship of various clients. Such information collection activities would lower the burden of the proposed rule on RIAs and ERAs.

iii. RIA and ERA Categories for Cost Analyses

As described above, some RIAs and ERAs are already applying some AML/CFT requirements (although there is no legal requirement to do so). This is primarily because of their registration as or affiliation with another type of BSA-defined financial institution (such as a broker-dealer). Therefore, the baseline level of AML/CFT measures for an RIA or ERA may vary with their business structure. For the purposes of the cost analysis, FinCEN categorized RIAs and ERAs based on business structure and likelihood of having existing AML/CFT measures in place in the baseline.

Based on discussions with industry, information from the 2016 Investment Management Compliance Testing Survey (IMCTS Survey), and the framework described above, FinCEN assessed that dual registrants are most likely to already have a *significant* number of AML/CFT measures in place. An RIA or ERA with a *significant* number of AML/CFT measures in place is assessed to be applying most requirements in the proposed rule, including filing SARs, recordkeeping, information sharing, and special due diligence measures. Any modifications to existing policies or procedures, such as training programs, are assumed to be small and would be incorporated into existing routine maintenance, review, and updating procedures.

FinCEN also assessed that the majority of RIAs and ERAs affiliated with a bank or broker-dealer are most likely to have a *moderate* number of AML/CFT measures, though they are less likely than dual registrants to have a *significant* number AML/CFT measures in place. An RIA or ERA with a *moderate* number of AML/CFT measures in place are assessed as more likely to implement internal recordkeeping, annual training programs, and initial customer due diligence. However, these RIAs and ERAs are less likely to meet SAR filing, ongoing due diligence, information sharing, and special due diligence requirements under the BSA. These additional measures would need to be implemented under the proposed rule.

Finally, FinCEN assessed that while most RIAs or ERAs that are not dually registered or affiliated with a bank or broker-dealer are currently implementing a *limited* number of AML/CFT measures, a minority of that subgroup are currently implementing a *moderate* number of—rather than a *limited* number of—AML/CFT measures. An RIA or ERA with a *limited* number of AML/CFT measures in place would need to implement most of the requirements in the proposed rule, except that they are likely to be collecting some customer information at the beginning of the client relationship and filing reports (Form 8300) that are substantially similar to CTRs.

[234] *See* 17 CFR 275.206(4)–2.

[235] *See* 17 CFR 275.206(4)–7.

[236] *See* 15 U.S.C. 80b–4(b).

First, RIAs and ERAs were categorized into three types of entities based on business structure: advisers that are dually registered as broker-dealers or as banks (''dual registrants''); advisers that are affiliated with a broker-dealer or bank (''affiliated advisers''); and all others that are not affiliated advisers or dual registrants (*i.e.,* ''other advisers''). Because broker-dealers and banks must comply with AML/CFT requirements, dual registrants are more likely to have a *significant* number of AML/CFT measures in place, and this is reflected in the baseline. Similarly, affiliated advisers are more likely than other advisers to have a *moderate* number of AML/CFT measures in place in the baseline. Formally, FinCEN defined each group based on Form ADV filings as follows:

- *Dual registrants.* RIAs or ERAs that report to the SEC that they are actively engaged in business as a broker-dealer or bank, responding ''Yes'' to Item 6.A.(1) and/or Item 6.A.(7).[237]
- *Affiliated advisers.* RIAs or ERAs that report to the SEC that they have a related person that is a broker-dealer or bank (responding ''Yes'' to Item 7.A.(1) and/or Item 7.A.(8)) and are not also dual registrants.[238]
- *Other advisers.* All RIAs or ERAs that are neither dual registrants nor affiliates of broker-dealers or banks.

FinCEN separately categorized RIAs and ERAs into the three groups. Although the size of each group is well-defined based on Form ADV data, the extent of existing AML/CFT measures within each group is uncertain and may vary considerably. The 2016 IMCTS Survey collected information from approximately 700 RIAs on their existing implementation of AML/CFT measures.[239] According to the 2016 IMCTS Survey, as of 2016, approximately 40 percent of RIAs had already adopted AML/CFT policies consistent with the Second Proposed Investment Adviser Rule.[240] An additional 36 percent of RIAs adopted some AML/CFT policies and procedures, but those were not in line with those in the Second Proposed Investment Adviser Rule. Therefore, approximately 76 percent of RIAs had at least some AML/CFT measures in place as of 2016. In particular, 49 percent had annual employee AML/CFT training, 24 percent had a designated an AML/CFT compliance officer, and 40 percent performed independent testing of their AML/CFT program annually. Similar information was not available for ERAs.

Based on this information, FinCEN assumed in the baseline for the proposed rule, that a minority—but as many as 40 percent—of RIAs had in place AML/CFT measures consistent with the requirements of the proposed rule. However, that proportion likely varies across the three groups defined above. Based on discussions with industry and the framework described above, FinCEN assessed that dual registrants are most likely to already have a *significant* number of AML/CFT measures in place (even if such measures are not required for their advisory activities). FinCEN also assessed that the majority of affiliated advisers implement a *moderate* number of AML/CFT measures, though they are less likely than dual registrants to have a *significant* number of AML/CFT measures in place. Finally, FinCEN assessed that while most ''other'' advisers are currently implementing a *limited* number of AML/CFT measures, a minority are currently implementing a *moderate* number of—rather than a *limited* number of—AML/CFT measures.

Specifically, FinCEN assessed that a dual registrant is highly likely to be applying a *significant* number of AML/CFT measures, including filing SARs, recordkeeping, information sharing, and special due diligence measures. Any modifications to existing policies or procedures, such as training programs, are likely to be small and would be incorporated into existing routine maintenance, review, and updating procedures.

For RIAs and ERAs with a *moderate* number of AML/CFT measures in place, such as most affiliated advisers, FinCEN assessed that existing programs most likely include internal recordkeeping, annual training programs, and initial customer due diligence.[241] However, these RIAs and ERAs are less likely to meet SAR filing, ongoing due diligence, information sharing, and special due diligence requirements under the BSA. These RIAs and ERAs would need to implement additional measures under the proposed rule.

The remaining RIAs and ERAs, which have a *limited* number of AML/CFT measures in place, would need to implement most of the additional AML/CFT requirements under the proposed rule. However, FinCEN assessed that all RIAs and ERAs are likely to be collecting some customer information at the beginning of the client relationship and filing reports [242] that are substantially similar to CTRs.

Based on this assessment, the RIAs and ERAs in each of the three groups were divided based on the proportion that FinCEN estimated to be implementing a *significant,* a *moderate,* or a *limited* number of AML/CFT measures in the baseline. Because the exact distribution is unknown, FinCEN used different assumptions to generate lower and upper bounds and identify a primary estimate. In this case, ''lower bound'' means more RIAs and ERAs have a *significant* or *moderate* number of AML/CFT measures in place and will have to implement relatively *fewer* additional measures under the proposed rule, while ''upper bound'' means more RIAs and ERAs have a *limited* number of AML/CFT measures in place and will have to implement relatively *more* additional measures under the proposed rule. To inform the primary estimate, FinCEN used the following assumptions. For RIAs, FinCEN used information from the 2016 IMCTS Survey as a benchmark for the primary estimate.

Based on the 2016 IMCTS Survey, FinCEN assumed that 75 percent of affiliated RIAs had implemented a *moderate* number of AML/CFT measures. Based on the number of affiliated RIAs, the remaining approximately 34 percent of other RIAs are implementing a *moderate* number of AML/CFT measures. For the upper bound estimate, FinCEN assumed that the AML/CFT measures implemented by RIAs and ERAs either under the current regulatory framework or voluntarily would not meet the requirements of the proposed rule, therefore all RIAs that are not dually registered would have to implement the complete set of AML/CFT measures under the proposed rule. Based on that assumption, all RIAs and ERAs except dually registered entities are assumed to have implemented a *limited* number of AML/CFT measures. For the lower bound estimate, FinCEN assumed that 40 percent of all RIAs regardless of business structure are implementing a *significant* number of AML/CFT measures and 36 percent are

[237] Items 6.A.(1) and 6.A.(7) on Form ADV require an investment adviser to identify whether it is actively engaged in a particular business. This response does not necessarily mean that the investment adviser is registered as a broker-dealer or as a bank. The phrase ''dual registrant'' should be interpreted on this basis for purposes of this analysis.

[238] A related person is any advisory affiliate (as defined for purposes of Form ADV) of and any person that is under common control (as defined for purposes of Form ADV) with the investment adviser. *See* Form ADV, Glossary of Terms.

[239] *See* 2016 IMCTS Survey, *supra* n. 150.

[240] *Id.*

[241] *See, e.g.,* SIFMA No Action Letter, supra n. 52.

[242] Investment advisers are currently required to file reports for the receipt of more than $10,000 in cash and negotiable instruments using joint FinCEN/Internal Revenue Service Form 8300. *See supra,* n. 50.

implementing a *moderate* number of measures—this includes a mix of affiliated and other RIAs.

FinCEN lacks information on the extent to which ERAs are already implementing AML/CFT requirements. Absent a better method to estimate, FinCEN assumed the proportion of dual-registered, affiliated, and other ERAs meeting AML/CFT requirements was the same as for RIAs across all scenarios. FinCEN seeks comment on this assumption, including whether a more appropriate method to estimate these proportions is available.

Classification of RIAs Advising Registered Funds. As discussed above, RIAs that exclusively advise mutual funds will be largely exempt from the requirements of the proposed rule. However, these RIAs have not been identified specifically through the Form ADV data. FinCEN assumed these advisers were most likely in the other advisers group. Because the clients (*i.e.,* the mutual funds) of these RIAs are subject to comprehensive AML/CFT obligations, FinCEN assessed these advisers as having a *moderate* number of AML/CFT measures in place.

Table 2.2 shows the resulting size of the population for each of the scenarios described above.

Table 2.2. Number of RIAs and ERAs, by Scenario[243]

Scenario	Baseline AML/CFT Measures	Registered Investment Advisers			Exempt Reporting Advisers			Total
		Dual Registrants	Affiliated Advisers	Other Advisers	Dual Registrants	Affiliated Advisers	Other Advisers	
Lower Bound	*Significant*	436 (100%)	1,727 (75%)	4,307 (34%)	44 (100%)	216 (75%)	1,877 (34%)	**8,607**
	Moderate	0	576 (25%)	4,795 (38%)	0	72 (25%)	2,090 (38%)	**7,533**
	Limited	0	0	3,550 (28%)	0	0	1,547 (28%)	**5,097**
	Total	**436**	**2,303**	**12,652**	**44**	**288**	**5,514**	**21,237**
Primary Estimate	*Significant*	436 (100%)	0	0	44 (100%)	0	0	**480**
	Moderate	0	1,727 (75%)	4,307 (34%)	0	216 (75%)	1,877 (34%)	**8,127**
	Limited	0	576 (25%)	8,345 (66%)	0	72 (25%)	3,637 (66%)	**12,630**
	Total	**436**	**2,303**	**12,652**	**44**	**288**	**5,514**	**21,237**
Upper Bound	*Significant*	436 (100%)	0	0	44 (100%)	0	0	**480**
	Moderate	0	0	0	0	0	0	**0**
	Limited	0	2,303 (100%)	12,652 (100%)	0	288 (100%)	5,514 (100%)	**20,757**
	Total	**436**	**2,303**	**12,652**	**44**	**288**	**5,514**	**21,237**

(c) Baseline Economic and Financial Characteristics of Regulated Population

This subsection describes the economic and financial profiles of RIAs and ERAs subject to the proposed rule in the baseline, including the number of employees and customer relationships with legal entities, natural persons, and pooled investment vehicles (PIVs)—and annual changes in these numbers.

i. Number of Employees

RIAs report their employee numbers on Form ADV, but ERAs do not. To estimate the number of employees at ERAs, FinCEN assumed that the number of employees was similar to those at RIAs with the same number of private funds. In particular, the number of ERA employees was approximated as follows. First, FinCEN focused on RIAs with private funds only. FinCEN calculated deciles for the number of funds among each RIA category: dual registrants, affiliated RIAs, and other RIAs. Then, for each category of ERA, FinCEN calculated the average number of employees for the decile of the corresponding distribution of RIAs, based on the number of private funds advised by that ERA. This served as the approximation for the total number of ERA employees in the cost calculation. Table 2.3 shows the average number of employees for each category of investment adviser.

[243] Parentheses indicate the percentage of entities within a given category by scenario. Totals may not sum precisely due to rounding.

Table 2.3: Average Number of Employees, by Type of Investment Adviser[244]

Investment Adviser Type	RIAs	ERAs
Dual Registrant	878	27
Affiliated Adviser	149	26
Other Adviser	19	11

ii. Number of Clients

On Form ADV, RIAs report the number of clients, enumerated for specific types of clients.[245] As described in section 3 of this Impact Analysis, certain costs of the proposed rule vary depending on the type of client, across three categories of clients: individual persons including high-net worth individuals, collectively known as ''natural persons''; PIVs; and various other types of clients collectively denoted as ''legal entities.'' Table 2.4 shows the average number of clients of each type, based on the RIA categories defined above.

Table 2.4: Average Number of Clients per RIA, by Client Type and Category

Investment Adviser Type	Natural Persons	Legal Entities	PIVs
Dual Registrant	43,450	919	14
Affiliated Adviser	10,476	254	18
Other Adviser	682	142	4

ERAs report the number of private funds they advise (*i.e.,* an ERA's clients), including the number of funds for which another investment adviser already reports fund-specific information. Table 2.5 reports the average number of funds reported per ERA, based on the investment adviser categories described above.

Table 2.5: Average Number of Private Funds per ERA, by Category[246]

Investment Adviser Type	Average Number of Private Funds Reported
Dual Registrant	4
Affiliated Adviser	63
Other Adviser	5

(d) Other Characteristics of Regulated Entities

This section describes the industry classification and business size of RIAs and ERAs to be regulated under the proposed rule.

i. Industry Classification by NAICS Code

In general, businesses may be categorized under multiple industries due to having multiple lines of revenue or multiple business functions. Many RIAs and ERAs, including but not limited to dual registrants, accordingly may report multiple lines of revenue (for purposes of the NAICS Codes) on Form ADV, and it is challenging to identify their primary line of business. Using the North American Industry Classification System (NAICS), the standard classification system used by Federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data on U.S. businesses, FinCEN assesses that most (if not all) RIAs and ERAs are classified within NAICS subsector 523 (Securities, Commodity Contracts, and Other Financial Investments and Related Activities)—with most entities classified in NAICS 5239 (Other Financial Investment Activities). However, that subsector may not account for the primary line of business of all investment advisers and some may be classified under NAICS 522 (Credit Intermediation and Related Activities) or NAICS 525 (Funds, Trusts, and Other Financial Vehicles).

ii. Small Entities

To assess the prevalence of small businesses affected by the proposed rule, FinCEN relied on the small entity definition under the Advisers Act rule adopted for purposes of the RFA. Under this definition, an investment adviser is considered a small entity if (i) it has, and reports on Form ADV, less than $25 million in assets under management ; (ii) it has less than $5 million in total assets on the last day of its most recent fiscal year; and (iii) it does not control, is not controlled by, and is not under common control with another

[244] Based on a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n. 26. RIAs report total employees in Item 5.A. ERA data come from FinCEN calculations, calculated as the median employment among RIAs that report only private fund clients.

[245] *Id.* Clients are reported in Item 5.D. Natural persons are calculated as the sum of 5.D.(a).(1) and 5.D.(b).(1). PIVs are reported in 5.D.(f).(1), and exclude investment companies and business development companies. Legal entities are the sum of the remaining rows of column 1 of Item 5.D. Numbers are rounded to the nearest integer.

[246] *Id.* The total number of funds is calculated as the sum of the number of funds reported in Schedule D, sections 7.B.(1) and 7.B.(2). Numbers are rounded to the nearest integer.

investment adviser that is not a small entity.[247]

On Form ADV, RIAs report whether they meet the conditions listed above. As of July 2023, there were 573 small entities, as reported in Table 2.6. ERAs do not report whether they meet the conditions above. However, based on a recent SEC rulemaking, and using the SEC's rationale here, FinCEN concluded that zero ERAs met the definition of small entity.[248]

Table 2.6: Number of Small Entities, by Type of Investment Adviser[249]

Investment Adviser Type	RIAs	ERAs
Dual Registrant	5	0
Affiliated Adviser	49	0
Other Adviser	519	0

Table 2.7 shows the characteristics of small RIAs compared to all other RIAs.

Table 2.7: Characteristics of RIAs by Business Size[250]

Characteristic	Small Entities	All Other RIAs
Average No. Employees	6	65
Percent that Advise Private Funds	23%	55%
Avg. No. Individual Clients	1,003	3,450
Avg. No. High-net Worth Clients	1	492
Avg. No. PIV Clients	0	7
Avg. No. Legal Entity Clients	15	187

3. Assessment of Benefits

The benefits assessed here are more difficult to quantify than the costs, but are nonetheless substantial. The primary direct benefits of the proposed rule are expected to primarily accrue in the public sector, most notably to U.S. law enforcement and the national security community, as well as certain Federal functional regulators, as well as to the investment adviser industry. Further, the identification of illicit activity in the investment adviser industry by applying reporting and recordkeeping obligations to those industry participants, RIAs and ERAs, that have direct access to customer information would enhance detecting, investigating and prosecuting illicit finance activity occurring through the industry. The AML/CFT requirements in the proposed rule will help address existing information gaps regarding suspicious activity reporting discussed in section 1. They will also help harmonize AML/CFT requirements between investment advisers and similarly situated financial institutions that must comply with these requirements.

In addition, while each provision in the proposed rule may not directly provide a benefit, each provision indirectly does so because it forms part of a comprehensive framework for identifying and reporting money laundering, terrorist financing, or other illicit finance activity. For instance, while the requirement for employee training and independent testing do not directly lead to increased identifying of illicit finance activity, they help ensure that the systems and employees who will identify whether an investment adviser is being used for such activity are best positioned to do so.

Specific benefits from the proposed rule include (i) increasing access for law enforcement to relevant information for complex financial crime investigations, (ii) enhancing interagency understanding of priority national security threats and their associated financial activity, and (iii) improving financial system transparency and integrity, including by aligning with international financial standards to strengthen the U.S. financial system from abuse by illicit actors. Through these direct benefits, crucial indirect benefits would accrue to the public at large by reducing money laundering, countering the financing of terrorism and other illicit finance activity, and protecting national security.

(a) Strengthening Law Enforcement Investigations of Certain Financial Crimes

Requiring RIAs and ERAs to file SARs and keep certain customer records would make that information more readily available to law enforcement authorities, assisting those authorities in detecting, investigating, and prosecuting financial crimes. The FBI reported that 36.3 percent of active complex financial crimes investigations and 27.5 percent of public corruption investigations involved BSA reporting.[251] However, for other types of criminal investigations, the percentage of criminal investigations supported by BSA reporting was even higher. For example, 46 percent of

[247] 17 CFR 275.0–7 (defining ''small business'' or ''small organization'' for purposes of the Advisers Act).

[248] The SEC's rationale, which FinCEN adopts, is that for an investment adviser to constitute an ERA for SEC purposes, the adviser would need to have an obligation to register with the SEC. An investment adviser with assets under management low enough to qualify as a small entity would not have an obligation to register with the SEC. *See* 88 FR 63206, 63383 n. 1895 regarding small entity ERAs.

[249] Based on a Treasury review of Form ADV information filed as of July 31, 2023. *See supra* n. 26. An RIA qualifies as a small entity under the SEC's definition if it has fewer than $25 million in regulatory AUM (Item 5.F.(2)(c)) and answers ''No'' to each of the questions in Item 12. ERAs were presumed not to meet the definition of small entity, as discussed above.

[250] *Id.* See tables above for details on the Form ADV items used to calculate each table entry. Numbers are rounded to nearest whole number or percent.

[251] *See* FinCEN, *Year in Review for FY 2022* (Apr. 21, 2023), p.2, *https://www.fincen.gov/sites/default/files/shared/FinCEN_Infographic_Public_2023_April_21_FINAL.pdf.*

transnational organized crime investigations were supported by BSA reporting.[252] SAR filing by RIAs and ERAs may increase BSA information availability to support investigations into corruption, fraud, and tax evasion, the criminal activities that the Treasury risk assessment identified as being most prominently tied to illicit proceeds moving through investment advisers.[253]

In particular, information from the reporting of suspicious activity and recordkeeping by RIAs and ERAs may benefit specific types of law enforcement financial crime investigations, particularly those involving the proceeds of foreign corruption, along with other transnational financial crimes. For instance, according to the FBI, in the 1MDB criminal investigation, at least $1 billion traceable to the conspiracy was laundered through the United States, including through private funds advised by at least one RIA, and used to purchase assets here.[254] In another case involving the misuse of private funds, the defendant established fake private equity investment funds in the British Virgin Islands to launder approximately $400 million in proceeds of a large international pyramid fraud scheme called OneCoin.[255] These examples demonstrate that investment advisers and the funds they advise have been implicated in certain financial crimes, and show the scope of potential benefit from covering RIAs and ERAs under this proposal.

Further, requiring RIAs and ERAs to respond to section 314(a) requests is likely to increase the number of positive responses for law enforcement when trying to locate accounts and transactions of persons that may be involved in terrorism or money laundering activity. In FY 2022, 66 law enforcement agencies made 519 requests under section 314(a) to over 14,000 financial institutions, which resulted in 37,865 positive responses.[256] Adding RIAs and ERAs to these requests is likely to increase positive responses for account and transactions information and then support further investigations using other legal tools.

(b) Improve Understanding of Priority National Security Threats

Applying AML/CFT obligations to RIAs and ERAs may help increase U.S. government understanding of two priority national security threats: (1) funds moving through the U.S. financial system that may be associated with Russian oligarchs and (2) investment activity that may be tied to foreign-state efforts to invest in early-stage companies developing critical or emerging technologies with national security implications.

SAR filings or information collected by RIAs and ERAs in the CDD process could improve the U.S. government's understanding of how illicit funds linked to Russian oligarchs may be accessing the U.S. financial system. According to FinCEN, BSA data provides significant financial intelligence about the movement of oligarch-related funds and assets with a nexus to the United States around the time of Russia's unprovoked military invasion of Ukraine, including likely attempts by Russian oligarchs and elites to conceal their assets, property, and financial activities.[257] Both U.S. law enforcement and press reporting have identified instances where Russian oligarchs and elites have accessed U.S. investment opportunities and the financial system through private funds or other PIVs, to avoid disclosing their identities to other parties.[258]

However, FinCEN currently receives only limited information from investment advisers and the securities industry in general regarding illicit Russian financial activity. For instance, of 454 SARs reviewed as part of a FinCEN Financial Trend Analysis on U.S. financial activity linked to Russian oligarchs, only 11, or less than 3 percent, were filed by the securities and futures industry.[259]

Applying SAR filing, CDD, and other recordkeeping requirements to RIAs and ERAs may also assist the U.S. government in identifying foreign-linked investments in certain U.S. companies that could raise national security issues. While there are certain transactions of which CFIUS must be notified, most transactions reviewed by CFIUS are filed voluntarily.[260] Where transactions are not voluntarily submitted to CFIUS for review, CFIUS agencies must invest staff time and resources into identifying those transactions and assessing whether to request that the parties file with CFIUS.[261] CFIUS transactions that originate through this non-notified process remain among the most complicated that CFIUS considers, and often require mitigation measures to address national security risks.[262]

Assessing the national security consequences of investments into early-stage companies developing emerging technology can be particularly challenging.[263] Requiring ERAs, particularly venture capital advisers, to submit SARs may help CFIUS agencies identify transactions where investors affiliated with foreign governments are attempting to use an investment to acquire technology or know-how with national security implications. This could include providing information about transactions CFIUS was unaware of, or providing new information about investors or other parties to transactions CFIUS was already investigating. In addition, law enforcement agencies involved in CFIUS reviews could use section 314(a) information sharing authorities to engage venture capital advisers or other RIAs or ERAs on particular technologies or concerning foreign investors.

(c) Protect the U.S. Financial System From Abuse

Applying AML/CFT obligations to RIAs and ERAs will also strengthen the

[252] *Id.*

[253] *See* Treasury, *Investment Adviser Illicit Finance Risk Assessment, https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.*

[254] *See* FBI, ''U.S. Seeks to Recover $1 Billion in Largest Kleptocracy Case to Date,'' (Jul. 20, 2016), *https://www.fbi.gov/news/stories/us-seeks-to-recover-1-billion-in-largest-kleptocracy-case-to-date.*

[255] *See* Department of Justice, ''Former Partner Of Locke Lord LLP Convicted In Manhattan Federal Court Of Conspiracy To Commit Money Laundering And Bank Fraud In Connection With Scheme To Launder $400 Million Of OneCoin Fraud Proceeds,'' (Nov. 21, 2019), *https://www.justice.gov/usao-sdny/pr/former-partner-locke-lord-llp-convicted-manhattan-federal-court-conspiracy-commit-money.*

[256] *Id.*

[257] *See* FinCEN, *Trends in Bank Secrecy Act Data: Financial Activity by Russian Oligarchs in 2022* (Dec. 2022), *https://www.fincen.gov/sites/default/files/2022-12/FinancialTrendAnalysisRussianOligarchsFTA_Final.pdf.*

[258] *See* Department of the Treasury, *Global Advisory on Russian Sanctions Evasion Issued Jointly by the Multilateral REPO Task Force,* p. 3, (Mar. 9, 2023), *https://home.treasury.gov/system/files/136/REPO_Joint_Advisory.pdf; see also* FinCEN, *Alert on Potential U.S. Commercial Real Estate Investments by Sanctioned Russian Elites, Oligarchs, and Their Proxies,* p. 4, (Jan. 25, 2023), *https://www.fincen.gov/sites/default/files/shared/FinCENAlertRealEstateFINAL508_1-25-23FINALFINAL.pdf.*

[259] *See supra* n. 257.

[260] *See* Treasury, ''Remarks by Assistant Secretary for Investment Security Paul Rosen at the Second Annual CFIUS Conference,'' (Sept. 14, 2023), *https://home.treasury.gov/news/press-releases/jy1732.*

[261] See *id.*

[262] Committee on Foreign Investment in the United States—Annual Report to Congress CY 2022 (*https://home.treasury.gov/system/files/206/CFIUS%20-%20Annual%20Report%20to%20Congress%20CY%202022_0.pdf*), p. 52

[263] *See* The Washington Post, ''Scrutiny mounts over tech investments from Kremlin-connected expatriates,'' (Dec. 19, 2022), *https://www.washingtonpost.com/technology/2022/12/19/russia-expatriates-links-probed/; see also* The Wall Street Journal, ''Government 'SWAT Team' Is Reviewing Past Startup Deals Tied to Chinese Investors,'' Jan. 31, 2021, *https://www.wsj.com/articles/government-swat-team-is-reviewing-past-startup-deals-tied-to-chinese-investors-11612094401.*

ability of the Federal Government and private sector to better protect the U.S. financial system from being misused for illicit finance. First, the proposed rule would apply a set of AML/CFT obligations to RIAs and ERAs, and those investment advisers would be subject to enforcement actions for failure to comply with those requirements. Those investment advisers would be required to, as described above, implement AML/CFT programs, conduct due diligence on customers, report suspicious activity, and keep certain records, among other obligations. In doing so, these obligations imposed on investment advisers would help identify, prevent, and deter bad actors from using investment advisers to further illicit financial activity, as investment advisers would be required to obtain information from customers to comply with these requirements.

Moreover, the proposed rule will also strengthen the ability of RIAs, ERAs, and other financial institutions to identify and report illicit activity. RIAs and ERAs would be able to coordinate with broker-dealers and banks to file joint SARs, and voluntarily share information on illicit activity under section 314(b) of the USA PATRIOT Act. Reporting by financial institutions under the BSA—and their broader efforts to implement effective AML/CFT programs—are thus fundamental to the government's effort to detect and prevent illicit financial activity and to protect the integrity of the financial system as a whole.

The proposed rule would also help bring the United States into full compliance with several international AML/CFT standards established by the Financial Action Task Force (FATF). In the 2016 FATF Mutual Evaluation Report (MER) of the United States, the United States was rated (and remains rated) ''partially compliant'' on nine of the 40 FATF Recommendations.[264] These included partially compliant ratings on Recommendations 1, 12, and 20 for the failure to apply AML/CFT requirements to investment advisers, among other reasons.[265]

As a result of its MER, the United States was put in ''enhanced follow-up.'' [266] For countries in enhanced follow-up, the FATF can take several actions, including ''issuing a formal FATF statement to the effect that the member jurisdiction is insufficiently in compliance with the FATF Standards, and recommending appropriate action.'' [267] These statements and other actions by the FATF can have material consequences on the economy of a jurisdiction.[268] If the proposed rule is finalized, it will assist the U.S. in avoiding these consequences and strengthening compliance with the FATF standards.

As noted in the Treasury investment adviser risk assessment,[269] investment advisers manage tens of trillions of dollars in assets. While some of these assets are subject to AML/CFT requirements, others are not. For instance, RIAs manage approximately $20 trillion in private fund assets, and as of Q4 2022, this included $284 billion in AUM owned by non-U.S. investors where the RIA did not have the information on hand to identify the beneficial owner because the beneficial interest was held through a chain involving one or more third-party intermediaries.[270] ERAs held approximately $5 trillion in AUM in private funds.

4. Assessment of Costs

This section assesses the potential costs to RIAs and ERAs, their clients, and government agencies associated with the proposed rule. Specifically, this Impact Analysis estimates the one-time, upfront costs and recurring administrative and maintenance costs incurred by RIAs and ERAs to establish or modify an existing AML/CFT program, which includes conducting ongoing CDD, filings SARs, and the other requirements of the proposed rule. It also estimates costs to customers to provide additional information to RIAs and ERAs and to the government to enforce those requirements. This Impact Analysis estimates the incremental costs of the proposed regulation over a 10-year period.

Some RIAs and ERAs may have reduced costs because they may already perform certain AML/CFT functions because they are dual registrants or affiliated advisers, as described in section 2, although, depending on the entity and its structure, may not currently be required to do so. RIAs that are dual registrants or affiliated advisers would not be legally required to establish a separate AML/CFT program for their advisory activities, provided that an existing comprehensive AML/CFT program covers all of the entity's legal and regulatory obligations. RIAs would also be exempt from having to apply most of the proposed requirements with respect to the mutual funds they advise, as mutual funds have their own AML/CFT program requirements, must file SARs, and are otherwise required to comply with the other reporting and recordkeeping requirements included in the proposed rule. Certain RIAs and ERAs may also already collect and verify certain information provided by customers via contract for a joint customer with another financial institution or through a voluntary AML/CFT program.

This section is organized as follows. First, it describes and compiles relevant cost information associated with these activities. Based on this information, it estimates the costs likely to be incurred by RIAs and ERAs. It then describes government implementation costs for oversight and enforcement. Finally, it summarizes the total costs of the proposed regulation.

(a) Cost Methodology

This section describes and compiles relevant cost information for this Impact Analysis. Based on this information, FinCEN estimates the typical costs RIAs and ERAs are anticipated to incur to comply with the requirements of the proposed rule. The cost information consists of the amount of time (in hours) and hourly labor cost of staff involved in compliance activities, such as developing and updating AML/CFT policies and procedures and training staff on new requirements, as well as costs associated with third party software licensing and independent testing. The implementation and scope of these activities, however, will vary widely and depend on a number of factors, such as the degree of automation of compliance activities and level of filer sophistication.

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[264] *See* FATF (2016), *Mutual Evaluation of the United States,* pp. 255–258, *https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER-United-States-2016.pdf.coredownload.inline.pdf.* In 2020, the U.S. was re-rated from ''partially compliant'' to ''largely compliant'' on Recommendation 10. *See* FATF (2020), *Anti-money laundering and counter-terrorist financing measures—United States, 3rd Enhanced Follow-up Report & Technical Compliance Re-Rating* (2020 US FUR), *https://www.fatf-gafi.org/content/dam/fatf-gafi/fur/Follow-Up-Report-United-States-March-2020.pdf.coredownload.pdf.*

[265] A ''partially compliant'' rating is generally not considered an acceptable rating for purposes of the FATF Follow-Up Process. *See* FATF (2023), Procedures for the FATF Fourth Round of AML/CFT Mutual Evaluations (FATF Fourth Round Procedures), pp. 22–23, *http://www.fatf-gafi.org/publications/mutualevaluations/documents/4th-round-procedures.html.*

[266] *See* 2020 US FUR, p. 1, *supra* n. 264.

[267] *See* FATF Fourth Round Procedures, p. 24, *supra* n. 265.

[268] *See* Julia Morse, *The Bankers Blacklist: Unofficial Market Enforcement and the Global Fight against Illicit Financing* (Cornell University Press 2021), pp. 131–138 (discussing the consequences of FATF listing).

[269] *See* Treasury, *Investment Adviser Illicit Finance Risk Assessment, https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.*

[270] *See* SEC, Private Fund Statistics, First Calendar Quarter 2022, private-funds-statistics-2022-q1.pdf (*sec.gov*).

All costs are reported in 2022 dollars. For transparency, all costs in this section are reported on an undiscounted basis. At the end of this section, costs are also reported on a discounted basis and the annualized costs of the proposed rule are calculated. To estimate the value of time associated with various compliance activities, FinCEN identified roles and corresponding staff positions involved in reviewing regulatory requirements, developing policies and procedures, filling out forms, transmitting data, conducting training, and maintaining, updating, and obtaining written approval of AML/CFT programs. FinCEN calculated the fully loaded (*i.e.,* wages plus benefits, leave, etc.) hourly labor cost for each of these roles by using the median hourly wage estimated by the U.S. Bureau of Labor Statistics and computing an additional factor accounting for fringe benefits as reported in Table 4.1.[271] Note, the proposed regulation requires, at a minimum, that an AML/CFT program must designate an AML/CFT compliance officer. This Impact Analysis does not include the direct cost of hiring a full-time equivalent AML/CFT compliance officer, which is not required by the proposed rule.[272] RIAs must already designate a chief compliance officer responsible for administering policies and procedures to comply with the Advisers Act and the rules thereunder. In smaller banks and broker-dealers, compliance or legal officers are often dual-hatted as AML/CFT compliance officers. Similarly, FinCEN assumes many RIAs and ERAs will appoint or dual hat a compliance or legal officer as their AML/CFT compliance officer. Therefore, this Impact Analysis accounts directly for the fully loaded hourly labor costs (*i.e.,* salary plus fringe benefits) for each compliance activity that would be performed by this individual rather than by calculating an annual salary, to avoid double-counting labor costs for each requirement.

Table 4.1 Hourly Labor Costs (in 2022 dollars)

Occupation	Median Hourly Wage[273]	Adjustment Factor for Fringe Benefits for Private Industry[274]	Fully Loaded Hourly Labor Cost
Chief Executives	$115.00	1.50	$172.42
Financial Managers	$100.28	1.50	$150.35
Compliance Officers	$39.66	1.50	$59.46
New Accounts Clerks	$23.17	1.50	$34.74
Financial Clerk	$23.10	1.50	$34.63
All Employees	$47.45	1.50	$71.14

FinCEN estimates that, in general and on average, each role would spend different amounts of time on each portion of the compliance burden associated with the proposed rule. These assumptions are provided in detail below for each compliance activity.

In addition to incurring labor costs, RIAs and ERAs will likely need to invest in new technology to comply with the proposed rule, including purchasing software and entering into licensing agreements with third party vendors. Although financial institutions are not required to use software to meet their AML/CFT requirements, most entities currently subject to the BSA use specialized AML/CFT software for this purpose. It is challenging to allocate technology costs to specific provisions of the proposed regulation as technology may be used to implement and automate several processes.[275] This Impact Analysis uses estimates derived from a 2020 Government Accountability Office (GAO) report assessing the costs of financial institutions to comply with the BSA to quantify these technology costs.[276] GAO documented a wide range of compliance costs across a diverse group of banks. For estimating technology and other costs in this Impact Analysis, FinCEN relied on the reported values for ''Large Community Bank B,'' for which the costs were assessed to be most similar to the costs likely to be incurred by the entities affected by the proposed regulation. FinCEN seeks comment on this assumption. Table 4.2 reports selected characteristics for this benchmark.

[271] U.S. Bureau of Labor Statistics, May 2022 National Industry-Specific Occupational Employment and Wage Estimates for NAICS 523000—Securities, Commodity Contracts, and Other Financial Investments and Related Activities. The adjustment factor for fringe benefits is calculated as 1 + ($18.26 per hour in total benefits ÷ $36.57 per hour in wages and salaries) = 1.50. Based on U.S. Bureau of Labor Statistics, Table 4. Employer Costs for Employee Compensation for Private Industry Workers by Occupational and Industry Group—Financial Activities Industry, June 2022.

[272] This is consistent with how FinCEN assesses burden hours and costs associated with the designation of a BSA officer, whereby the costs are assessed individually across other BSA regulatory requirements that the designated officer may implement. *See* FinCEN, Agency Information Collection Activities; Proposed Renewal; Comment Request; Renewal Without Change of Anti-Money Laundering Programs for Certain Financial Institutions, 85 FR 49418 (Oct. 13, 2020).

[273] *See* U.S. Bureau of Labor Statistics, May 2022 National Industry-Specific Occupational Employment and Wage Estimates for NAICS 523000—Securities, Commodity Contracts, and Other Financial Investments and Related Activities.

[274] *See* U.S. Bureau of Labor Statistics, Table 4. Employer Costs for Employee Compensation for Private Industry Workers by Occupational and Industry Group—Financial Activities Industry, June 2022.

[275] Government Accountability Office, *Anti-Money Laundering: Opportunities Exist to Increase Law Enforcement Use of Bank Secrecy Act Reports, and Banks' Costs to Comply with the Act Varied* (GAO–20–574), (Sept. 2020), *https://www.gao.gov/products/gao-20-574* (2020 GAO BSA Report). The 2020 GAO BSA Report noted that it reported software costs separately and did not allocate them by requirement because the banks reviewed commonly used the same software to meet multiple BSA/AML requirements.

[276] *Id.*

Table 4.2 Characteristics of Selected Financial Institution Benchmark[277]

Characteristic	Value (in 2018)
Financial Institution Type	Community bank
Total Assets Under Management	$401 million to 4500 million
Total Noninterest Expenses	$20.1 million to $30 million
Number of Employees	101 to 500
Number of New Accounts Opened	1,001 to 5,000
Number of SARs filed	51
Number of CTRs filed	73

Table 4.3 reports the estimated compliance costs for specialized AML/CFT software and an independent annual audit to test the AML/CFT program. The costs are based on values for the financial institution benchmark described in the previous paragraph adjusted for inflation to 2022 dollars using the GDP implicit price deflator.[278]

Table 4.3 Estimated Compliance Costs for Independent Testing, Software, and Other Third-Party Technology Vendors (in 2022 dollars)[279]

Compliance Activity	Average Annual Cost
AML/CFT Software Costs	$12,400
Independent Testing	$17,000

(b) Compliance Costs to Industry by Regulatory Provision

As described in section 2, the regulated universe for purposes of the proposed rule consists of RIAs and ERAs, which vary in terms of their business structure, size, client relationships, and degree of existing AML/CFT measures already in place. Across these advisers, several characteristics vary across groups that directly impact the magnitude of the estimated costs, including the average number of employees and the number/type of customer relationships. However, the most significant cost determinant is the extent of existing AML/CFT measures in place—RIAs and ERAs with established AML/CFT programs in place will likely incur relatively fewer costs under the proposed rule, while those with few AML/CFT measures in place may incur potentially more significant costs.

For the purposes of estimating the cost impacts of the proposed rule, this Impact Analysis has sub-divided RIAs and ERAs into groups based on: (1) whether they are dual registrants, affiliated advisers, or other advisers (as described in section 2); and (2) whether they have a *significant, moderate,* or a *limited* number of AML/CFT measures already in place (see Table 2.2). FinCEN believes that these sub-divisions are the best available method of estimating the cost impacts, but FinCEN invites comment on whether some other method of sub-dividing the industry for cost-estimate purposes would be preferable.

i. AML/CFT Program Costs

RIAs and ERAs subject to the proposed rule will need to implement and maintain an AML/CFT program that meets the minimum requirements of the BSA. This includes developing internal policies, procedures, and controls to comply with the requirements of the BSA and address money laundering, terrorist financing, and other illicit finance risks. Entities that do not already have a AML/CFT program in place will incur costs to establish such a program. In addition, those entities will incur costs for maintaining, updating, storing, and producing upon request the written AML/CFT program. Dual registrants or affiliated advisers would not have to establish multiple AML/CFT programs, provided that an existing comprehensive AML/CFT program would cover all of the entity's advisory businesses. Entities that already have an existing AML/CFT program will need to review and/or modify their AML/CFT program to ensure it complies with the requirements of the proposed rule. As firms that have an existing AML/CFT program are expected to be already maintaining, updating, storing, and producing upon request the written program, FinCEN estimates these firms will incur no additional costs beyond reviewing/modifying and obtaining written approval in the first year after the promulgation of the proposed regulation.

Based on public comments on the Second Proposed Investment Adviser Rule,[280] FinCEN estimates it will take approximately 120 hours to develop the necessary policies and procedures to establish an AML/CFT program for affiliated or other RIAs and ERAs that have a *limited* number of existing AML/CFT measures in place. FinCEN assumes that dually registered entities covered by an existing AML/CFT program and entities that have a *significant* or *moderate* number of AML/CFT measures in place would only need to update their existing program. FinCEN assumes the vast majority of entities would develop or update a written program within the first year after the promulgation of the regulation. Once established, FinCEN estimates annually it will take approximately 1

[277] *Id* at Table 111: Selected Characteristics of Large Community Bank B, 2018.

[278] Bureau of Economic Analysis, National Income and Product Accounts Tables, Table 1.1.9. Implicit Price Deflators for Gross Domestic Product, *https://www.bea.gov/itable/national-gdp-and-personal-income.*

[279] *See* 2020 GAO BSA Report at Table 113, *supra* n. 275.

[280] *See* Public Comments, Docket ID FINCEN–2014–0003, *https://www.regulations.gov/docket/FINCEN-2014-0003/comments.*

hour to maintain and update the existing AML/CFT program plus an average of 10 minutes to store and produce upon request the written AML/CFT program. Table 4.4 reports the average costs of establishing and maintaining an AML/CFT program.

Table 4.4. Average Cost of Establishing and Updating AML/CFT Program

Activity	Financial Manager		Compliance Officer		Total Hours	Total Cost per Entity
	% Time	Hourly Cost	% Time	Hourly Cost		
Develop AML/CFT Program	10%	$150.35	90%	$59.46	120	$8,226
Maintain and Update Written AML/CFT Program	10%	$150.35	90%	$59.46	1.0	$69
Store the Written AML/CFT Program	10%	$150.35	90%	$59.46	0.833	$6
Produce Written AML/CFT Program Upon Request	10%	$150.35	90%	$59.46	0.833	$6

In addition, the AML/CFT program must be approved in writing by an RIA's or ERA's board of directors or trustees.[281] FinCEN estimates that it will take approximately 4 hours for a trustee or director to review and approve a written AML/CFT program the first year it is implemented and approximately 2 hours each subsequent year to review the program.[282] For this activity, FinCEN uses an average hourly wage based on the minimum BLS estimate for a chief executive as a proxy for a trustee of director's hourly compensation. Therefore, using the fully loaded labor cost of $172.42 per hour, the estimated labor cost for program review and approval is approximately $690 for a new AML/CFT program and $345 for an existing AML/CFT program. FinCEN seeks comment on the accuracy of this estimation. This represents an upfront and recurring cost for RIAs and ERAs that do not have an existing AML/CFT program, but only a one-time cost for RIAs and ERAs that currently have a *significant* or *moderate* number of AML/CFT measures in place.

Further, RIAs and ERAs would need to implement an AML/CFT training program for employees.[283] FinCEN estimates approximately two-thirds of employees would need to be trained on the AML/CFT program requirements, and assumes that such training could occur annually.[284] FinCEN assesses that RIAs and ERAs with a *significant* or *moderate* number of AML/CFT measures in place are already training staff and would not incur additional training costs under the proposed rule—with the exception of reviewing and updating the training materials to ensure they cover all of the proposed requirements. For RIAs and ERAs with a *limited* number of AML/CFT measures in place, FinCEN estimates it would initially take 50 hours to develop an AML/CFT training program. For entities that have an existing AML/CFT training program (those entities with a *significant* or *moderate* number of AML/CFT measures in place), FinCEN estimates the one-time burden to review and update training materials would be 10 hours. FinCEN seeks comment on these assumptions. Some RIAs and ERAs may choose to use a third-party consultant or external training event to conduct trainings, but this would not be required under the proposed rule.[285] FinCEN estimates the training would take approximately 1 hour for each employee, assuming such training occurs annually.[286] Table 4.5 reports the estimated average cost of developing and conducting AML/CFT program compliance training annually. The number of total hours is estimated based on the average number of employees for each type of RIA or ERA.

[281] If an RIA or ERA does not have a board, then the program must be approved by the adviser's sole proprietor, general partner, trustee, or other persons that have functions similar to a board of directors.

[282] FinCEN notes that this estimate reflects the time spent by one trustee/director, and that for those RIAs or ERAs with a full board of directors, there could be incremental cost for each additional director.

[283] Employees of an investment adviser (and of any agent or third-party service provider that is charged with administering any portion of the AML/CFT program) would have to be trained in AML/CFT requirements relevant to their functions and to recognize possible signs of money laundering, terrorist financing, or other illicit finance activity that could arise in the course of their duties.

[284] The frequency of the investment adviser's training program would be determined by the responsibilities of the employees and the extent to which their functions would bring them in contact with AML/CFT requirements or possible money laundering, terrorist financing, or other illicit finance activity.

[285] The 2020 GAO BSA Report estimated the average cost per employee trained ranged between $20 and $400 with a mean estimate of approximately $116 per employee (measured in 2022 dollars). For ''Large Community Bank B'' the average estimated cost per employee trained was approximately $130 (measured in 2022 dollars).

[286] *See id.* at p. 52.

Table 4.5. Average Cost of AML/CFT Program Compliance Training[287]

Activity	Financial Manager		Compliance Officer		All Employees		Total Hours[1]	Total Cost per Entity[2]
	% Time	Hourly Cost	% Time	Hourly Cost	% Time	Hourly Cost		
Develop AML/CFT Program Training (one-time cost)	10%	$150.35	90%	$59.46			50	$3,428
Review and Update AML/CFT Program Training (one-time cost)	10%	$150.35	90%	$59.46			10	$686
Conduct Annual Training			100%	$59.46			1	$59
Costs for Employees to Attend Training								
RIA, Affiliated					100%	$71.14	100	$7,087
RIA, Other					100%	$71.14	13	$924
ERA, Affiliated					100%	$71.14	17	$1,209
ERA, Other					100%	$71.14	7	$522

In addition, all RIAs and ERAs will need to implement independent testing of their AML/CFT program. As described in the previous section, FinCEN estimates the average cost of such testing will be approximately $17,000.[288] FinCEN seeks comment on this assumption. This reflects a new recurring cost for all RIAs and ERAs affected by the proposed rule with the exception of dually registered entities, which are assumed to already use independent auditors. Table 4.6 summarizes the average incremental costs per entity of developing or maintaining and updating an AML/CFT program by type and characteristics of each RIA or ERA.

Table 4.6. Average Cost of AML/CFT Program[289]

Investment Adviser Type	Upfront Cost (Year 1)[1]	Recurring Cost (Year 2+)[1]
Dual Registrant	$1,000	$0
RIA, Affiliated Adviser, with a *moderate* number of AML/CFT measures	$18,000	$17,000
RIA, Affiliated Adviser, with a *limited* number of AML/CFT measures	$36,000	$25,000
RIA, Other, with a *moderate* number of AML/CFT Measures	$18,000	$17,000
RIA, Other, with a *limited* number of AML/CFT Measures	$30,000	$18,000
ERA, Affiliated Adviser, with a *moderate* number of AML/CFT measures	$18,000	$17,000
ERA, Affiliated Adviser, with a *limited* number of AML/CFT measures	$31,000	$19,000
ERA, Other, with a *moderate* number of AML/CFT Measures	$18,000	$17,000
ERA, Other, with a *limited* number of AML/CFT Measures	$30,000	$18,000

ii. Customer Due Diligence Costs

The proposed rule would require RIAs and ERAs to implement appropriate risk-based procedures for conducting ongoing customer due diligence. Specifically, RIAs and ERAs would be required to (1) understand the nature and purpose of customer relationships for the purpose of

[287] For annual training, total hours includes 1 hour per employee. FinCEN assumes approximately two-thirds of employees will require training each year, to include periodic updates and refresher training. Total cost may differ from hourly cost multiplied by total hours shown in table due to rounding.

[288] *See* 2020 GAO BSA Report at Table 113.

[289] Costs are rounded to the nearest thousand dollars.

developing a customer risk profile; and (2) conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

FinCEN assumes that all RIAs and ERAs have some existing information on their customers and processes to identify and conduct additional diligence on certain customers. For instance, in reviewing the data from the 2016 IMCTS Survey, in addition to the 40 percent who had implemented a full AML/CFT program consistent with the requirements of the Second Proposed Investment Adviser Rule, an additional 36 percent of RIAs implemented some AML/CFT measures.[290] Based on this information as well as industry input about some of the voluntary AML/CFT measures firms have in place, it is more common for firms to develop voluntary CDD programs as part of their onboarding process as compared to other AML/CFT measures.[291] Therefore, FinCEN assumes that any RIAs and ERAs with a *moderate* number of AML/CFT measures in place will likely not need to modify their existing ongoing CDD measures, while RIAs and ERAs with a *limited* number of AML/CFT measures in place will need to perform additional customer review for existing customers and at the time of account opening for new customers. Since investment advisers generally already collect some of this information, the estimated cost burden is less than implementing a fully comprehensive customer review at the time of account opening, and accounts primarily for the costs of modifying existing procedures. FinCEN assumes the cost of modifying existing CDD procedures will be approximately 25 percent of the full cost for initial customer review and risk profiling. FinCEN seeks comment on these assumptions.

RIAs and ERAs with a *limited* number of AML/CFT measures in place will need to collect additional information to develop a customer risk profile for legal entities and PIVs. Table 4.7 documents key assumptions regarding the number of customer accounts at affiliated and other RIAs and ERAs. ERAs only have legal entity customers—therefore, they have no natural person customers. Based on an analysis of Form ADV Filings, as of July 2023, RIAs had approximately 51.7 million natural person customers, 2.8 million legal entity customers, and 100,000 PIV accounts. FinCEN estimates the average number of customer accounts will grow at an annual rate of 9.5 percent—and PIV accounts will grow at an annual rate of 6 percent—based on average industry growth in individual and PIV accounts from 2018 to 2023.[292]

Table 4.7 Average Number of Customer Relationships (as of July 2023)[293]

	Registered Investment Advisers			Exempt Reporting Advisers		
	Dual Registrant	Affiliated	Other	Dual Registrant	Affiliated	Other
Avg. Number of Natural Person Relationships	43,450	10,476	682	0	0	0
Avg. Number of Legal Entity Relationships	919	254	142	4	63	5
Avg. Number of PIV Accounts	14	18	4	0	0	0

Affiliated and other RIAs and ERAs with a *limited* number of existing AML/CFT measures will also need to collect and review customer information to implement risk-based procedures for conducting ongoing CDD. As described above, FinCEN estimates the costs associated with modifying existing customer diligence information and procedures will be significantly less than the full cost for developing the initial customer risk profile. In this Impact Analysis, FinCEN estimates the average cost of collecting additional information for new accounts to develop a customer risk profile will be approximately 25 percent of the total estimated cost of this information collection (30 minutes per natural person or 1 hour per legal entity).[294] Thus, the estimated cost of information collection is approximately 7.5 minutes per natural person or 15 minutes per legal entity. For this activity, FinCEN uses an average hourly labor cost of $34.76 for a new account clerk. Therefore, the estimated labor cost to develop a risk profile is approximately $4.34 for per natural person and $8.68 per legal entity. In addition to new accounts, FinCEN anticipates that RIAs and ERAs will need to conduct this information collection for existing accounts. FinCEN estimates this information collection for existing accounts will be conducted over the first three years after the promulgation of the proposed regulation.[295] FinCEN seeks comment on the accuracy of this estimate. The costs to build and maintain technology and information systems to house this customer information is not reflected here but is included in the annual costs of software licensing described elsewhere in this Impact Analysis. These costs are multiplied by the average number of natural persons, legal entities, and PIV accounts, respectively, for each RIA and ERA.

In addition to the costs to the adviser, this requirement likely represents an information collection burden for legal entities that hold accounts with investment advisers. FinCEN estimates it would take between approximately 15 and 30 minutes, or an average of 22.5 minutes, for legal entity customers to provide any additional data required for this information collection. Since these

[290] *See* 2016 IMCTS Survey, Question 15, *supra* n. 150

[291] *See, e.g.,* Managed Funds Association, Sound Practices for Hedge Fund Managers (2009), Chapter 6 (Anti-Money Laundering).

[292] *See* Investment Adviser Association, *Investment Adviser Industry Snapshot 2023* (Jul. 2023), p. 26, *https://investmentadviser.org/wp-content/uploads/2023/06/Snapshot2023_Final.pdf.*

[293] *See supra* n. 26.

[294] *See* 81 FR at 29448.

[295] Current industry practices suggest customers are often re-rated for risk purposes. Industry input suggests high-risk customers, which make up a small portion of many RIAs customer base, are re-rated at least annually or when SARs are filed, while medium- or low-risk customers are re-rated less frequently.

customers are not employees of the regulated entities, but rather other investment advisers in most cases, FinCEN uses an hourly burden estimate of $49.17 that is representative of the customer base.[296] Therefore, the average information collection cost is approximately $18.44 per customer. This average cost is multiplied by the number of legal entity customers for each RIA or ERA.

Table 4.8 summarizes the average ongoing CDD costs per entity by type and characteristics of each RIA or ERA. The relatively higher costs in the first three years reflects the compliance burden associated with data collection activities to develop a customer risk profile for existing customer accounts and new customer accounts, while the ongoing costs after 2026 reflect the burden associated with data collection for only new customer accounts.

Table 4.8. Average Cost of Ongoing Customer Due Diligence

Year	RIAs and ERAs with a *Significant* or *Moderate* Number of AML/CFT Measures[297]	RIAs, Affiliated, with a *Limited* Number of AML/CFT Measures[298]	RIAs, Other, with a *Limited* Number of AML/CFT Measures[2]	ERAs, Affiliated, with a *Limited* Number of AML/CFT Measures[2]	ERAs, Other, with a *Limited* Number of AML/CFT Measures[2]
2024	$0	$8,000	$2,000	$400	$300
2025	$0	$11,000	$2,000	$500	$300
2026	$0	$11,000	$2,000	$500	$300
2027	$0	$3,000	$1,000	$300	$200
2028	$0	$3,000	$1,000	$300	$200
2029	$0	$4,000	$1,000	$300	$200
2030	$0	$4,000	$1,000	$300	$200
2031	$0	$4,000	$1,000	$300	$200
2032	$0	$5,000	$1,000	$300	$200
2033	$0	$5,000	$1,000	$300	$200

iii. Suspicious Activity Report Filing Costs

As part of their AML/CFT program, RIAs and ERAs will be required to conduct ongoing monitoring of customers and file SARs. FinCEN assumes that RIAs and ERAs that are dually registered as a broker-dealer or bank are already submitting SARs. The extent of SAR filing by affiliated or other advisers is uncertain. Therefore, FinCEN assumes that all RIAs and ERAs that are not dually registered as a broker-dealer or bank would have to begin filing SARs due to the proposed regulation. FinCEN seeks comment on this assumption. To the extent that some RIAs and ERAs in this category are already filing SARs, this may overestimate the costs of the proposed regulation.

Based on an analysis of SAR filings by dual registrants between 2018 and 2022, FinCEN estimates that RIAs will file an average of approximately 60 SARs per year.[299] Since no information was available for ERAs, FinCEN applies the same estimate of 60 SARs per year. FinCEN seeks comment on this assumption. Based on the analysis, FinCEN estimates the following regarding the SARs investment advisers would file:

- 51 (85 percent) would be initial SARs and 9 (15 percent) would be continuing SARs.
- 51 (85 percent) would be discrete SARs and 9 (15 percent) would be batch SARs.
- 55 (92 percent) would be standard SARs and 5 (8 percent) would be extended SARs.

Without a detailed breakdown, FinCEN assumes the distribution of SARs is proportionally distributed across each category as discussed below. Each type of filing is expected to have a different reporting burden.

In addition, the estimated costs of ongoing monitoring in (Table 4.8 above) include the review of alerts that do not result in a SAR being filed. FinCEN previously estimated that approximately 42 percent of suspicious activity alerts were turned into SARs.[300] Therefore, for each case filed as a SAR, approximately 1.4 cases were not filed. Table 4.9 reports the average cost of determining whether a SAR is needed and filing SARs. While the burden estimates are based on FinCEN's previous analysis,[301] in this Impact Analysis the burden is attributed primarily to a compliance officer rather than a financial clerk or teller due to the smaller size of RIAs and ERAs relative to banks and to avoid potentially underestimating the average hourly labor costs associated with these activities. To the extent that a portion of this work can be completed by clerical staff that report to a compliance officer, this may slightly overestimate certain costs. FinCEN seeks comment on this assumption. The licensing cost for transaction monitoring software is not reflected here but is included in the software costs described elsewhere in this Impact Analysis.

[296] This estimate is based on a population-weighted average of $32.79, which represents the median salary for all employees in NAICS 522, 523, and 525, multiplied by an adjustment factor for fringe benefits of 1.50.

[297] This category includes dual registrants that are applying a significant number of AML/CFT measures and affiliated advisers that are applying a moderate number of AML/CFT measures.

[298] Costs are rounded to the nearest thousand dollars for RIAs and to the nearest hundred dollars for ERAs.

[299] Dual registrants were assessed to be the population of investment advisers most likely to file SARs and best represent an investment adviser subject to SAR filing obligations.

[300] *See* FinCEN, *Proposed Renewal: Reports by Financial Institutions of Suspicious Transactions,* 85 FR 31598 (May 26, 2020).

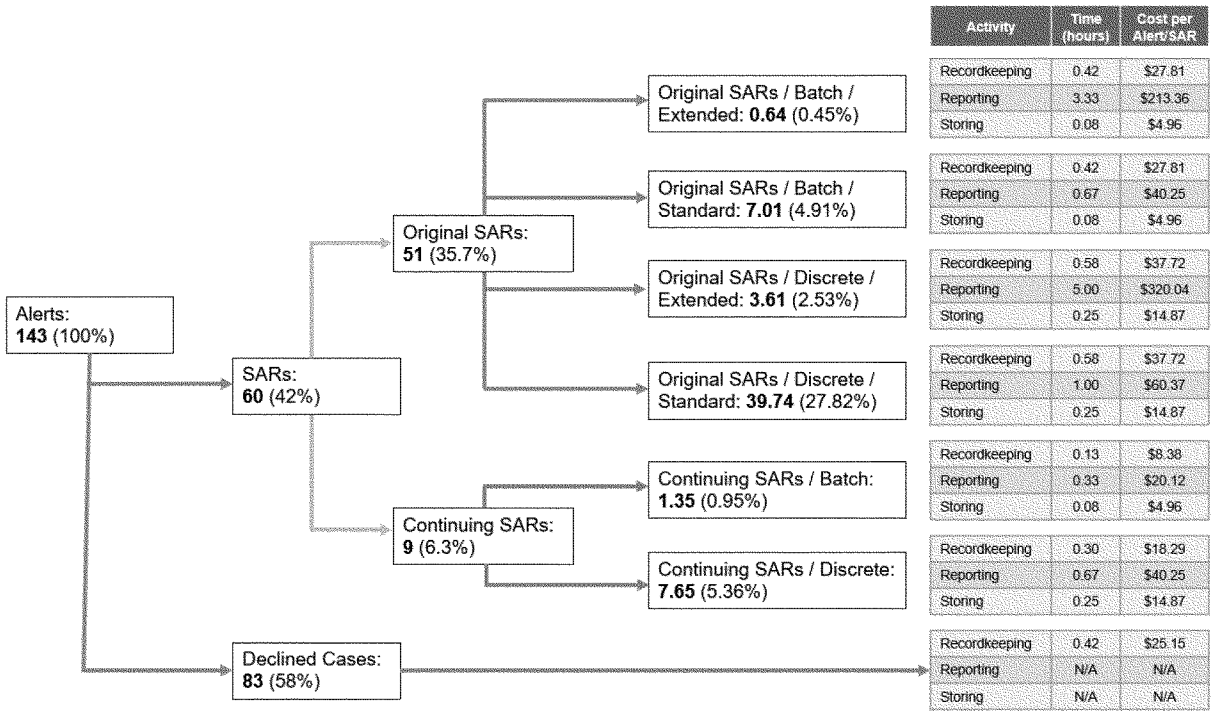
[301] *See id.*

Table 4.9. Weighted Average Hourly Cost of Reviewing Alerts and Drafting, Writing, and Submitting a Suspicious Activity Report

Activity	Financial Manager		Compliance Officer		Weighted Average Hourly Cost
	% Time	Hourly Cost	% Time	Hourly Cost	
Determining Whether a SAR is Merited	10%	$150.35	90%	$59.46	$68.55
Documenting Cases not Submitted as SARs	1%	$150.35	99%	$59.46	$60.37
Drafting, Writing, and Submitting SARs (standard content)	1%	$150.35	99%	$59.46	$60.37
Drafting, Writing, and Submitting SARs (extended content)	5%	$150.35	95%	$59.46	$64.01
Storing SARs and Supporting Documentation	0%	$150.35	100%	$59.46	$59.46

Figure 4.1 illustrates FinCEN's estimates regarding the average number and distribution of SARs, including for suspicious activity alerts that do not result in a SAR being filed, as well as the hourly recordkeeping, reporting, and storing burden estimates by type of filing.

Figure 4.1. Average Number and Distribution of Suspicious Activity Alerts and Estimated Burden by Type of Filing per Investment Adviser[302]



Based on this information, the average annual cost of SAR filings is estimated to be approximately $10,000 per entity for any RIA or ERA that does not have a full AML/CFT program in place. No incremental costs are estimated for dual registrants because those entities are already submitting SARs in the baseline.

[302] Information on the number and distribution of SARs by type of filing based on an analysis of SAR filings. Information on the number of alerts and burden estimates based on FinCEN, *Proposed Renewal: Reports by Financial Institutions of Suspicious Transactions*. 85 FR 31598 (May 26, 2020).

iv. Other Compliance Costs

As discussed above, there are certain costs associated with the proposed rule that may be spread across several of the proposed requirements. It is challenging to allocate those expenditures to specific provisions of the proposed rule described above. These include software licensing and general recordkeeping costs.

Dual registrants, affiliated, and other RIAs and ERAs that already apply a *significant* or *moderate* number of AML/CFT measures are expected to already be using specialized AML/CFT software as part of their AML/CFT program. Affiliated or non-affiliated entities that have a *limited* number of AML/CFT measures in place will likely have to invest in this type of software to implement an AML/CFT program. FinCEN estimates that annual licensing fees for specialized AML/CFT software will be approximately $12,400.[303]

The proposed rule requires RIAs and ERAs to comply with certain recordkeeping obligations (under the Recordkeeping Rule and Travel Rule),[304] including recording and maintaining originator and beneficiary information for certain transactions. FinCEN assumes that RIAs and ERAs that are dually registered as a broker-dealer or as a bank with a *significant* number of AML/CFT measures in place are already in compliance with the recordkeeping requirements, while other RIAs and ERAs would have to take additional steps to comply with these measures. FinCEN estimates the annual recordkeeping burden per RIA or ERA for these requirements is 50 hours.[305] Table 4.10 summarizes the average cost associated with these recordkeeping requirements.

Table 4.10. Average Cost Associated with AML/CFT Recordkeeping Requirements

Activity	Financial Manager		Compliance Officer		Financial Clerk		Total Hours	Total Cost per Entity
	% Time	Hourly Cost	% Time	Hourly Cost	% Time	Hourly Cost		
Creating and Maintaining Records	5%	$150.35	15%	$59.46	80%	$34.63	50	$2,207

In addition, the proposed rule requires RIAs and ERAs to implement the information sharing procedures contained in section 314(a) of the USA PATRIOT Act.[306] Upon receiving an information request from FinCEN, an RIA or ERA would be required to search its records to determine whether it maintains or has maintained any account or engaged in any transaction with an individual, entity, or organization named in the request. Covered financial institutions are instructed not to reply to the 314(a) request if a search does not uncover any matching of accounts or transactions. Currently, all 314(a) responses are filed using automated technology.[307] FinCEN assumes that dually registered entities with a *significant* number of AML/CFT measures in place are already complying with these requirements, while most other RIAs and ERAs will likely incur additional reporting costs to comply with these measures. FinCEN estimates the average burden will be approximately 4 minutes per 314(a) request for 365 reports per year per investment adviser, an average of one request per calendar day.[308] Therefore, the estimated burden is approximately 24 hours (4 minutes × 365 reports = 1,460 minutes) per year per investment adviser. The information technology costs associated with 314(a) requests are assumed to be included within the overall software costs. Table 4.11 summarizes the information collection costs for 314(a) measures.

Table 4.11. Average Cost for Section 314(a) Measures

Activity	Financial Manager		Compliance Officer		Financial Clerk		Total Hours	Total Cost per Entity
	% Time	Hourly Cost	% Time	Hourly Cost	% Time	Hourly Cost		
Research and Respond to 314(a) Requests	10%	$150.35	60%	$59.46	30%	$34.63	24.33	$1,487

As ''covered financial institutions'' under FinCEN regulations, RIAs and ERAs will also be required to maintain due diligence measures that include policies, procedures, and controls that are reasonably designed to detect and report any known or suspected money laundering or other suspicious activity conducted through or involving any correspondent or private banking account that is established, maintained, administered, or managed in the United States. FinCEN estimates the annual hourly burden of maintaining and updating the due diligence program for foreign correspondent accounts and private banking accounts would be approximately two hours for each RIA and ERA—one hour to maintain and update the program and one hour to obtain the approval of senior management.[309] Information technology costs associated with this requirement are included within the overall software costs. Table 4.12 summarizes the cost burden associated with special due diligence measures.

[303] *See* 2020 GAO BSA Report at Table 113.

[304] *See* 31 CFR 1020.410(a), (e); *see also* 31 CFR 1010.410(f).

[305] FinCEN, *Proposed Renewal: Renewal Without Change of Regulations Requiring Records to be Made and Retained by Financial Institutions, Banks, and Providers and Sellers of Prepaid Access,* 85 FR 84105 (Dec. 23, 2020).

[306] FinCEN, *Special Information Sharing Procedures to Deter Money Laundering and Terrorist* Activity, Final Rule, 67 FR 60579 (Sept. 26, 2002).

[307] FinCEN, *Proposed Renewal: Renewal Without Change on Information Sharing Between Government Agencies and Financial Institutions,* 87 FR 41186 (Jul. 11, 2022).

[308] Id.

[309] FinCEN, *Proposed Renewal: Due Diligence Programs for Correspondent Accounts for Foreign Financial Institutions and for Private Banking Accounts,* 85 FR 61104 (Sep. 9, 2020).

Table 4.12. Average Cost Associated with Updating and Maintaining Special Due Diligence Measures

Activity	Trustee or Director		Financial Manager		Compliance Officer		Total Hours	Total Cost per Entity
	% Time	Hourly Cost	% Time	Hourly Cost	% Time	Hourly Cost		
Maintain and Update Special Due Diligence Program			10%	$150.35	90%	$59.46	1	$68.55
Obtain Written Approval	100%	$172.42					1	$172.42

Under the proposed rule, RIAs and ERAs must also comply with special measures procedures and prohibitions contained in section 311 of the USA PATRIOT Act.[310] Section 9714 of the Combatting Russian Money Laundering Act allows for similar special measures in the context of illicit Russian finance. Sections 311 and 9714 grant FinCEN the authority, upon finding that reasonable grounds exist for concluding that a foreign jurisdiction, financial institution, class of transactions, or type of account is of ''primary money laundering concern,'' to require domestic financial institutions and financial agencies to take one or more ''special measures,'' which impose additional recordkeeping, information collection, and reporting requirements on covered U.S. financial institutions. They also allow FinCEN to impose prohibitions or conditions on the opening or maintenance of certain correspondent accounts. Currently, such prohibitions are in place for three foreign financial institutions and two foreign jurisdictions, all imposed under section 311.[311] These special measures require financial institutions to provide notice to foreign account holders and document compliance with the statute. FinCEN assumes that dually registered RIAs and ERAs with a *significant* number of AML/CFT measures in place are already complying with these requirements, while most other RIAs and ERAs will likely incur additional costs to comply with these special measures. FinCEN estimates the average burden will be approximately 1 hour per special measure.[312] Therefore, the estimated burden is approximately 5 hours. FinCEN seeks comment on this assumption. Table 4.13 summarizes the average cost for implementation section 311 special measures.

Table 4.13. Average Cost for Section 311 Special Measures

Activity	Financial Manager		Compliance Officer		Financial Clerk		Total Hours	Total Cost per Entity
	% Time	Hourly Cost	% Time	Hourly Cost	% Time	Hourly Cost		
Section 311 Special Measures	10%	$150.35	60%	$59.46	30%	$34.63	5	$1,222

Finally, in addition to filing SARs, financial institutions must file CTRs under the BSA's reporting obligations. Currently, all investment advisers are required to report transactions in currency over $10,000 on Form 8300, which is being replaced by the CTR.[313] Therefore, FinCEN estimates that the incremental cost for RIAs and ERAs to use the CTR is *de minimis*.[314] FinCEN seeks comment on this assumption.

Based on this information, the average annual cost of other compliance measures not characterized elsewhere in this regulatory impact analysis are estimated to be approximately $4,000 for affiliated or other RIAs and ERAs with a *moderate* number of AML/CFT measures already in place and approximately $16,000 for affiliated or other RIAs and ERAs with a *limited* number of AML/CFT measures already in place.

(c) Costs to Government

This section describes the costs to Federal Government agencies to implement and enforce the proposed regulation.

i. Costs to FinCEN

Administering the proposed regulation is estimated to entail costs to FinCEN as well as other government agencies. In terms of technology and IT costs, the proposed rule does not create new kinds or requirements or new reporting forms, and instead applies existing SAR and CTR filing obligations to investment advisers. As a result, technology and IT costs are estimated to be small but are included in this analysis for comprehensiveness. The primary costs that FinCEN and other government agencies are expected to incur with respect to administering this proposed rule relate to personnel costs for enforcing compliance with the regulation, as well as providing guidance and engaging in outreach, training, investigations, and policy development in support of this regulation. FinCEN estimates the total annual personnel cost relating to administering this proposed rule to be

[310] FinCEN, *Final Rule: Special Information Sharing Procedures to Deter Money Laundering and Terrorist Activity*. 67 FR 60579 (Sept. 26, 2002).

[311] These foreign financial institutions and jurisdictions are: (1) Bank of Dandong, (2) Commercial Bank of Syria, including Syrian Lebanese Commercial Bank, (3) FBME Bank Ltd., (4) Islamic Republic of Iran, and (5) Democratic People's Republic of North Korea. *See* FinCEN, Special Measures for Jurisdictions, Financial Institutions, or International Transactions of Primary Money Laundering Concern, *https://www.fincen.gov/resources/statutes-and-regulations/311-and-9714-special-measures,*

[312] *See, e.g.,* FinCEN, *Proposed Renewal: Imposition of a Special Measure against Bank of Dandong as a Financial Institution of Primary Money Laundering Concern,* 88 FR 48285 (Jul. 26, 2023).

[313] FinCEN, Proposed Renewal: *Renewal Without Change of the Bank Secrecy Act Reports of Transactions in Currency Regulations at 31 CFR 1010.310 Through 1010.314, 31 CFR 1021.311, and 31 CFR 1021.313, and FinCEN Report 112—Currency Transaction Report,* 85 FR 29022 (July 13, 2020).

[314] In the Second Proposed Investment Adviser Rule, FinCEN estimated each investment adviser would file an average of one CTR per year, at a time cost of one hour per CTR. Incorporating these costs in the model would change the total hour and dollar burden by less than one percent.

$7.5 million, as reflected in Table 4.14, with continuing recurring annual costs of roughly the same magnitude for ongoing outreach, policy, and enforcement activities thereafter.

Table 4.14 Estimated Personnel Costs to FinCEN Related to Administering the Proposed Rule (in 2022 dollars)

Division	Grade	Number of Employees	Average Annual Salary[315]	Adjustment Factor for Fringe Benefits and Overhead for Federal Employees[316]	Fully Loaded Hourly Labor Cost
Policy (PD)	GS-12	1	$108,000	2.0	$217,000
	GS-13	1	$129,000	2.0	$258,000
Global Investigations (GID)	GS-13	2	$129,000	2.0	$258,000
	GS-14	1	$152,000	2.0	$304,000
Counsel (OCC)	GS-15	2	$184,000	2.0	$367,000
Strategic Operations (SOD)	GS-13	4	$129,000	2.0	$258,000
	GS-14	1	$152,000	2.0	$304,000
Enforcement and Compliance (ECD)	GS-12	10	$108,000	2.0	$217,000
	GS-13	4	$129,000	2.0	$258,000
	GS-14	2	$152,000	2.0	$304,000
	GS-15	1	$184,000	2.0	$367,000
Total		**29**	**$3,770,000**		**$7,540,000**

In addition, FinCEN estimates the average technology and IT costs associated with receiving SAR filings will be approximately $0.10 per SAR. Based on an average estimate of 60 SARs per entity per year, FinCEN anticipates it will receive approximately 1,245,420 SARs each year from RIAs and ERAs that do not currently have most AML/CFT measures in place. This estimate excludes SAR filings for dually registered entities because those entities are expected to be submitting SARs in the baseline. Therefore, the incremental technology and IT costs to FinCEN associated with the SAR filing requirement are estimated to be approximately $125,000 per year. Enforcement of this regulation will involve coordination with law enforcement agencies, which will incur costs (time and resources) while conducting investigations into non-compliance. FinCEN does not currently propose an estimate of these costs.

ii. Costs to SEC

The SEC is also estimated to incur costs, primarily relating to additional staff needed to examine for compliance with the requirements of the proposed rule, and to provide any needed regulatory guidance or analysis. Costs associated with implementing the proposed rule are expected to primarily affect the Division of Investment Management and the Division of Examinations, though certain potential costs may also be incurred by the Division of Enforcement. In addition, as the SEC receives a significant portion of its revenue from fees on registrants and other market participants, many of these costs would ultimately be paid for through those fees.[317]

The SEC's Division of Investment Management administers the Advisers Act and develops regulatory policy for investment advisers, among other responsibilities. The Division of Investment Management may require two additional staff to provide regulatory guidance or analysis related to the proposed rule. The average salary for a GS–15 equivalent is approximately $203,500 based on the SEC's SK series adjusted for the locality pay area of Washington, DC.[318] Applying an adjustment factor of 2.0 for fringe benefits and overhead yields an estimated fully loaded labor cost of approximately $407,000. Therefore, FinCEN estimates the total annual personnel cost to the SEC relating to administering this proposed rule to be approximately $814,000.

RIAs are subject to examination by SEC staff in the SEC's Division of Examinations. Within the Division of Examinations, the Investment Adviser/Investment Company (IA/IC) Examination Program completed more than 2,300 examinations of SEC-registered investment advisers in FY22.[319] The SEC maintains authority to examine ERAs as well. While the Division of Examinations may conduct examinations for compliance with the requirements of the proposed rule within its existing examination program, this may require additional examination staff. FinCEN does not currently have an estimate of the additional costs the SEC's Division of Examinations may incur for these activities.

(d) Summary of Costs

This section reports the total costs of the proposed rule on a per entity basis

[315] U.S. Office of Personnel Management, Salary Table 2023 Incorporating the 4.1 percent General Schedule Increase and a Locality Payment of 32.49 percent for the Washington-Baltimore-Arlington area. Rounded to three significant digits.

[316] The Department of Health and Human Services recommends using an adjustment factor of 2 to account for fringe benefits and overhead when agency-specific financial data are unavailable. (HHS, Guidelines for Regulatory Impact Analysis, 2016, p. 30).

[317] *See* SEC, *FY 2023 Agency Financial Report,* p. 32, *https://www.sec.gov/files/sec-2023-agency-financial-report.pdf#chairmessage.*

[318] This estimate is based on the midpoint salary for a GS–15 equivalent of $153,600 multiplied by the locality pay rate of 32.49 percent for Washington, DC.

[319] *See* SEC, *FY 2024 Congressional Budget Justification,* p. 22, *https://www.sec.gov/files/fy-2024-congressional-budget-justification_final-3-10.pdf.*

and in aggregate, by type and characteristics of each RIA or ERA. As described in ection 2, the regulated universe consists of RIAs and ERAs that vary in terms of business structure, number of employees, number of accounts, and the extent that existing AML/CFT measures are being applied (*e.g. significant, moderate, limited*). Table 4.15 summarizes the total number of entities by type and characteristics of each RIA and ERA.

Table 4.15. Number of Affected Investment Advisers by Type

Baseline AML/CFT Measures	Registered Investment Advisers			Exempt Reporting Advisers			Total
	Dual Registrant	Affiliated	Other	Dual Registrant	Affiliated	Other	
Significant	436	0	0	44	0	0	480
Moderate	0	1,727	4,307	0	216	1,877	8,127
Limited	0	576	8,345	0	72	3,637	12,630

i. Average Cost per Private Entity and Total Costs by Category of Investment Adviser

This section describes the estimated average cost per entity and total costs by type and characteristics of each RIA and ERA. The average costs per RIA and ERA are multiplied by the number of impacted entities to estimate the aggregate cost burden of the proposed rule, by category of RIA and ERA. Table 4.16 summarizes the estimated costs for RIAs and ERAs that are dually registered as a broker-dealer or a bank with a *significant* number of AML/CFT measures in place. The estimated costs for dually registered entities are minimal because most firms are expected to have an existing AML/CFT program in place. The relatively small incremental costs are associated with RIAs and ERAs maintaining and updating a written AML/CFT program and reviewing and updating AML/CFT training to ensure they cover the activities of all RIAs and ERAs and meet the requirements of the BSA.

Table 4.16. Total Costs for Dually Registered Entities with a *Significant* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)[320]

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	480	$1,000	$0.4
2025-2033	480	$0	$0.0

.

Table 4.17. summarizes the estimated costs for affiliated RIAs with a *moderate* number of AML/CFT measures in place.

Table 4.17. Total Costs for RIAs, Affiliated, with a *Moderate* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	1,727	$32,000	$55.7
2025-2033	1,727	$31,000	$53.8

Table 4.18. summarizes the estimated costs for affiliated RIAs with a *limited* number of AML/CFT measures in place.

[320] For Tables 4.16 to 4.37, costs are rounded to the nearest thousand dollars or two significant digits.

Table 4.18. Costs for RIAs, Affiliated, with a Limited Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	576	$76,000	$43.8
2025	576	$62,000	$35.9
2026	576	$63,000	$36.0
2027	576	$55,000	$31.5
2028	576	$55,000	$31.7
2029	576	$55,000	$31.9
2030	576	$56,000	$32.1
2031	576	$56,000	$32.3
2032	576	$57,000	$32.6
2033	576	$57,000	$32.9

Table 4.19. summarizes the estimated costs for other RIAs with a *moderate* number of AML/CFT measures in place.

Table 4.19. Costs for RIAs, Other, with a *Moderate* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	4,307	$32,000	$139.0
2025-2033	4,307	$31,000	$134.2

Table 4.20. summarizes the estimated costs for other RIAs with a *limited* number of AML/CFT measures in place.

Table 4.20. Costs for RIAs, Other, with a Limited Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	8,345	$61,000	$510.3
2025	8,345	$47,000	$394.3
2026	8,345	$47,000	$394.8
2027	8,345	$46,000	$383.7
2028	8,345	$46,000	$384.3
2029	8,345	$46,000	$385.0
2030	8,345	$46,000	$385.7
2031	8,345	$46,000	$386.6
2032	8,345	$46,000	$387.4
2033	8,345	$47,000	$388.4

Table 4.21. summarizes the estimated costs for ERAs, affiliated, with a *moderate* number of AML/CFT measures in place.

Table 4.21. Total Costs for ERAs, Affiliated, with a *Moderate* Number AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	216	$32,000	$7.0
2025-2033	216	$31,000	$6.7

Table 4.22. summarizes the estimated costs for ERAs that are affiliated with a bank or broker-dealer with a *moderate* number of AML/CFT measures in place.

Table 4.22. Costs for ERAs, Affiliated, with a *Limited* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	72	$59,000	$4.2
2025-2033	72	$46,000	$3.3

Table 4.23. summarizes the estimated costs for other ERAs with a *moderate* number of AML/CFT measures in place.

Table 4.23. Costs for ERAs, Other, with a *Moderate* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	1,877	$32,000	$60.6
2025-2033	1,877	$31,000	$58.5

Table 4.24. summarizes the estimated costs for other ERAs with a *limited* number of AML/CFT measures in place.

Table 4.24. Costs for ERAs, Other, with a *Limited* Number of AML/CFT Measures in Place, by Year (in 2022 dollars)

Year	Number of Entities	Average Cost per Entity	Total Costs ($M)
2024	3,637	$57,000	$206.7
2025-2033	3,637	$45,000	$163.0

ii. Estimated Burden of the Proposed Rule to Industry

Table 4.25 summarizes the total costs of the proposed rule on an undiscounted basis.

Table 4.25. Total Estimated Burden of the Proposed Regulation by Entity Type, by Year ($ Millions, 2022)

Year	SEC-registered Investment Advisers	Exempt Reporting Advisers	Customers	Federal Agencies	Total
2024	$720	$280	$25.0	$8.5	$1,000
2025	$620	$230	$2.4	$8.5	$860
2026	$620	$230	$2.6	$8.5	$860
2027	$600	$230	$2.8	$8.5	$840
2028	$600	$230	$3.1	$8.5	$840
2029	$600	$230	$3.4	$8.5	$840
2030	$600	$230	$3.7	$8.5	$850
2031	$600	$230	$4.1	$8.5	$850
2032	$600	$230	$4.5	$8.5	$850
2033	$600	$230	$4.9	$8.5	$850

Table 4.26 summarizes the total costs of the proposed rule by entity and business structure for dual registrants, affiliated advisers, and other advisers on an undiscounted basis.

Table 4.26. Total Estimated Burden of the Proposed Regulation by Entity and Business Structure, by Year ($ Millions, 2022)

Year	Dually Registered Entities	Affiliated Entities	Neither	Customers	Federal Agencies	Total
2024	$0.4	$110	$890	$25.0	$8.5	$1,000
2025	$0	$99	$750	$2.4	$8.5	$860
2026	$0	$100	$750	$2.6	$8.5	$860
2027	$0	$95	$740	$2.8	$8.5	$840
2028	$0	$95	$740	$3.1	$8.5	$840
2029	$0	$95	$740	$3.4	$8.5	$840
2030	$0	$96	$740	$3.7	$8.5	$850
2031	$0	$96	$740	$4.1	$8.5	$850
2032	$0	$96	$740	$4.5	$8.5	$850
2033	$0	$96	$740	$4.9	$8.5	$850

iii. Discounted Estimated Burden of the Proposed Rule

In regulatory impact analyses, discount rates are used to account for differences in the timing of the estimated benefits and costs. Benefits and costs that accrue further in the future are more heavily discounted than those impacts that occur today. Discounting reflects individuals' general preference to receive benefits sooner rather than later (and defer costs) and recognizes that costs incurred today are more expensive than future costs because businesses must forgo an expected rate of return on investment of that capital.[321] OMB recommends using a discount rate of 2 percent.[322] This represents the real (inflation-adjusted) rate of return on long-term U.S. government debt over the last 30 years, calculated between 1993 and 2022, and is a reasonable approximation of the social rate of time preference.

Table 4.27 summarizes the total costs of the proposed rule using a 2 percent discount rate. As shown in the table, RIAs account for approximately 72 percent of the annualized costs to industry, while ERAs account for the remaining 28 percent.

[321] U.S. Office of Management and Budget, Circular A–4, Nov. 9, 2023.

[322] Id.

Table 4.27. Total Estimated Burden of the Proposed Regulation by Entity Type, by Year ($ Millions, 2022) using a 2 percent Discount Rate

Year	SEC-registered Investment Advisers	Exempt Reporting Advisers	Customers	Federal Agencies	Total
2024	$720	$280	$25.0	$8.5	$1,000
2025	$600	$230	$2.3	$8.3	$840
2026	$590	$220	$2.5	$8.1	$830
2027	$570	$220	$2.7	$8.0	$790
2028	$560	$210	$2.9	$7.8	$780
2029	$540	$210	$3.1	$7.7	$770
2030	$530	$210	$3.3	$7.5	$750
2031	$520	$200	$3.6	$7.4	$740
2032	$520	$200	$3.8	$7.2	$720
2033	$510	$190	$4.1	$7.1	$710
10-Year Undiscounted Cost	**$6,200**	**$2,400**	**$57.0**	**$85.0**	**$8,700**
10-Year Present Value	**$5,700**	**$2,200**	**$53.0**	**$78.0**	**$8,000**
Annualized Cost	**$620**	**$240**	**$5.8**	**$8.5**	**$870**

Table 4.28 summarizes the total costs of the proposed rule by entity and business structure for dual registrants, affiliated advisers, and other advisers using a 2 percent discount rate. As shown in the table, entities that are dual registrants account for less than 0.1 percent, affiliated advisers account for approximately 11 percent, and other advisers account for approximately 89 percent of the annualized costs to industry.

Table 4.28. Total Estimated Burden of the Proposed Rule by Entity and Business Structure, by Year ($ Millions, 2022) using a 2 percent Discount Rate

Year	Dually Registered Entities	Affiliated Entities	Neither	Customers	Federal Agencies	Total
2024	$0.4	$110	$890	$25.0	$8.5	$1,000
2025	$0	$97	$730	$2.3	$8.3	$840
2026	$0	$96	$720	$2.5	$8.1	$830
2027	$0	$90	$690	$2.7	$8.0	$790
2028	$0	$88	$680	$2.9	$7.8	$780
2029	$0	$86	$670	$3.1	$7.7	$770
2030	$0	$85	$660	$3.3	$7.5	$750
2031	$0	$83	$640	$3.6	$7.4	$740
2032	$0	$82	$630	$3.8	$7.2	$720
2033	$0	$80	$620	$4.1	$7.1	$710
10-Year Undiscounted Cost	**$0.4**	**$980**	**$7,600**	**$57.0**	**$85.0**	**$8,700**
10-Year Present Value	**$0.4**	**$900**	**$6,900**	**$53.0**	**$78.0**	**$8,000**
Annualized Cost	**$0.04**	**$98**	**$760**	**$5.8**	**$8.5**	**$870**

(e) Uncertainty Analysis

As described in section 2, the number of RIAs and ERAs is well-defined based on the number of Form ADV filings. However, there is uncertainty about the extent of existing AML/CFT measures within each group. While an uncertainty analysis could layer various assumptions about the percentage of RIAs and ERAs that have in place certain AML/CFT measures to address each individual requirement—and the degree to which those measures would have to be reviewed and modified to comply with the requirements of the proposed rule—such information is unavailable and the existing framework described in the section presents a simpler approach to account for this uncertainty by varying certain

assumptions around the categorization of RIAs and ERAs. Specifically, this Impact Analysis estimates the impact of varying assumptions regarding the distribution of RIAs and ERAs into categories of significant, moderate, and limited AML/CFT measures in place. This provides a lower and upper bound estimate of the potential costs of the proposed rule. The costs presented earlier in this section represent FinCEN's primary estimate of the burden of the proposed rule.

i. Lower Bound Estimate

The lower bound estimate assumes that a greater proportion of RIAs and ERAs have a *significant* or *moderate* number of AML/CFT measures in place and will have to implement relatively *fewer* additional measures under the proposed rule. Table 4.29 summarizes the total number of entities according to the business type and characteristics of each RIA and ERA. This represents an optimistic, but not implausible, scenario based on self-reported assessments indicating that approximately 40 percent of RIAs already have AML/CFT policies and procedures consistent with the BSA.[323] For the lower bound estimate, FinCEN assumes the same proportion of affiliated ERAs and other ERAs have a *significant* number of AML/CFT measures as the corresponding RIA groups. Thus, this estimate is optimistic in that the number of ERAs with policies and procedures similar to those of RIAs is highly uncertain—although it is still likely to be less than the overall percentage of RIAs.

Table 4.29. Number of Affected Investment Advisers by Type (Lower Bound)

Baseline AML/CFT Measures	Registered Investment Advisers			Exempt Reporting Advisers			Total
	Dual Registrant	Affiliated Advisers	Other	Dual Registrant	Affiliated Advisers	Other	
Significant	436	1,727	4,307	44	216	1,877	8,607
Moderate	0	576	4,795	0	72	2,090	7,533
Limited	0	0	3,550	0	0	1,547	5,097

Table 4.30 summarizes the total costs of the proposed rule in the lower bound scenario using a 2 percent discount rate. As shown in the table, although the overall costs of the proposed rule are lower, the distribution of costs between RIAs and ERAs is similar to the primary estimate.

Table 4.30. Total Estimated Burden of the Proposed Regulation by Entity Type, by Year ($ Millions, 2022) using a 2 percent Discount Rate (Lower Bound)

Year	SEC-registered Investment Advisers	Exempt Reporting Advisers	Customers	Federal Agencies	Total
2024	$390	$160	$9.5	$8.4	$570
2025	$330	$130	$0.9	$8.3	$480
2026	$330	$130	$1.0	$8.1	$470
2027	$310	$130	$1.0	$7.9	$450
2028	$310	$130	$1.1	$7.8	$440
2029	$300	$120	$1.2	$7.6	$430
2030	$290	$120	$1.3	$7.5	$430
2031	$290	$120	$1.3	$7.3	$420
2032	$280	$120	$1.4	$7.2	$410
2033	$280	$110	$1.6	$7.1	$400
10-Year Undiscounted Cost	**$3,400**	**$1,400**	**$21.0**	**$84.0**	**$4,900**
10-Year Present Value	**$3,100**	**$1,300**	**$20.0**	**$77.0**	**$4,500**
Annualized Cost	**$340**	**$140**	**$2.2**	**$8.4**	**$490**

Table 4.31 summarizes the total costs of the proposed rule by entity and business structure for dual registrants, affiliated advisers, and other advisers in the lower bound scenario using a 2 percent discount rate. As shown in the

[323] *See* 2106 IMCTS Survey, *supra* n. 150.

table, in the lower bound scenario a greater proportion of the costs (approximately 95 percent) are attributed to other advisers.

Table 4.31. Total Estimated Burden of the Proposed Regulation by Entity and Business Structure, by Year ($ Millions, 2022) using a 2 percent Discount Rate (Lower Bound)

Year	Dually Registered Entities	Affiliated Entities	Neither	Customers	Federal Agencies	Total
2024	$0.4	$27	$520	$9.5	$8.4	$570
2025	$0	$26	$440	$0.9	$8.3	$480
2026	$0	$25	$430	$1.0	$8.1	$470
2027	$0	$21	$420	$1.0	$7.9	$450
2028	$0	$20	$410	$1.1	$7.8	$440
2029	$0	$20	$400	$1.2	$7.6	$430
2030	$0	$20	$400	$1.3	$7.5	$430
2031	$0	$20	$390	$1.3	$7.3	$420
2032	$0	$19	$380	$1.4	$7.2	$410
2033	$0	$19	$370	$1.6	$7.1	$400
10-Year Undiscounted Cost	**$0.4**	**$240**	**$4,500**	**$21.0**	**$84.0**	**$4,900**
10-Year Present Value	**$0.4**	**$220**	**$4,200**	**$20.0**	**$77.0**	**$4,500**
Annualized Cost	**$0.04**	**$24**	**$460**	**$2.2**	**$8.4**	**$490**

ii. Upper Bound Estimate

The upper bound estimate assumes that a greater proportion of RIAs and ERAs have *limited* number of AML/CFT measures in place and will have to implement relatively *greater* additional measures under the proposed rule. Table 4.32 summarizes the total number of entities by type and characteristics of each RIA and ERA.

Table 4.32. Number of Affected Entities by Type (Upper Bound)

Baseline AML/CFT Measures	Registered Investment Advisers			Exempt Reporting Advisers			Total
	Dual Registrant	Affiliated Advisers	Other	Dual Registrant	Affiliated Advisers	Other	
Significant	436	0	0	44	0	0	480
Moderate	0	0	0	0	0	0	0
Limited	0	2,303	12,652	0	288	5,514	20,757

Table 4.33 summarizes the total costs of the proposed rule in the upper bound scenario using a 2 percent discount rate. As shown in the table, although the overall costs of the proposed rule are higher, the distribution of costs between RIAs and ERAs is similar to the primary estimate.

Table 4.33. Total Estimated Burden of the Proposed Regulation by Business Type, by Year ($ Millions, 2022) using a 2 percent Discount Rate (Upper Bound)

Year	SEC-registered Investment Advisers	Exempt Reporting Advisers	Customers	Federal Agencies	Total
2024	$890	$330	$45.0	$8.5	$1,300
2025	$700	$260	$4.2	$8.3	$970
2026	$690	$250	$4.5	$8.1	$950
2027	$660	$250	$4.8	$8.0	$910
2028	$640	$240	$5.2	$7.8	$900
2029	$630	$240	$5.5	$7.7	$880
2030	$620	$230	$6.0	$7.5	$870
2031	$610	$230	$6.4	$7.4	$850
2032	$600	$220	$6.9	$7.2	$830
2033	$590	$220	$7.4	$7.1	$820
10-Year Undiscounted Cost	**$7,200**	**$2,700**	**$100.0**	**$85.0**	**$10,000**
10-Year Present Value	**$6,600**	**$2,500**	**$96.0**	**$78.0**	**$9,300**
Annualized Cost	**$720**	**$270**	**$10.0**	**$8.5**	**$1,000**

Table 4.34 summarizes the total costs of the proposed rule by entity and business structure for dual registrants, affiliated advisers, and other advisers in the upper bound scenario using a 2 percent discount rate. As shown in the table, although the overall costs of the proposed rule are higher, the distribution of costs between the different types of RIAs and ERAs is similar to the primary estimate.

Table 4.34. Total Estimated Burden of the Proposed Regulation by Business Structure, by Year ($ Millions, 2022) using a 2 percent Discount Rate (Upper Bound)

Year	Dually Registered Entities	Affiliated Entities	Neither	Customers	Federal Agencies	Total
2024	$0.4	$160	$1,100	$45.0	$8.5	$1,300
2025	$0	$130	$830	$4.2	$8.3	$970
2026	$0	$130	$810	$4.5	$8.1	$950
2027	$0	$120	$780	$4.8	$8.0	$910
2028	$0	$120	$760	$5.2	$7.8	$900
2029	$0	$120	$750	$5.5	$7.7	$880
2030	$0	$120	$730	$6.0	$7.5	$870
2031	$0	$120	$720	$6.4	$7.4	$850
2032	$0	$110	$710	$6.9	$7.2	$830
2033	$0	$110	$690	$7.4	$7.1	$820
10-Year Undiscounted Cost	**$0.4**	**$1,400**	**$8,500**	**$100.0**	**$85.0**	**$10,000**
10-Year Present Value	**$0.4**	**$1,200**	**$7,800**	**$96.0**	**$78.0**	**$9,300**
Annualized Cost	**$0.04**	**$140**	**$850**	**$10.0**	**$8.5**	**$1,000**

iii. Comparison of Costs in the Lower and Upper Bound Estimates

As described in this section, FinCEN estimates the cost of the proposed rule to regulated entities will be approximately $870 million on an annualized basis. In comparison to alternative assumptions about the degree of existing AML/CFT measures among RIAs and ERAs subject to the proposed rule, FinCEN's primary estimate is relatively conservative in that it assumes a greater proportion of RIAs and ERAs have only a *moderate* or *limited* number of existing AML/CFT measures in place in comparison to input provided by industry suggesting that figure may be lower. Therefore, the primary estimate is closer to the upper bound than the lower bound. Under the

most pessimistic assumptions regarding the degree of existing AML/CFT measures, the proposed rule is estimated to cost approximately $1 billion on an annualized basis. This scenario is highly improbable because more than 520 RIAs (out of 690 surveyed) indicated that they already have a *significant* or *moderate* number of AML/CFT measures in place. Under more optimistic assumptions about the proportion of RIAs with a *significant* or *moderate* number of AML/CFT measures in place, FinCEN estimates the cost of the proposed rule will be approximately $490 million on an annualized basis. Table 4.35 provides a comparison of the estimated costs of the proposed rule under each of these scenarios.

Table 4.35. Comparison of Compliance Costs using Lower and Upper Bound Estimates Relative to the Primary Estimate ($ Millions, 2022) using a 2 percent Discount Rate

Year[1]	Lower Bound	Primary Estimate	Upper Bound
2024	$570	$1,000	$1,300
2025	$480	$840	$970
2026	$470	$830	$950
2027	$450	$790	$910
2028	$440	$780	$900
2029	$430	$770	$880
2030	$430	$750	$870
2031	$420	$740	$850
2032	$410	$720	$830
2033	$400	$710	$820
10-Year Undiscounted Cost	**$4,900**	**$8,700**	**$10,000**
10-Year Present Value	**$4,500**	**$8,000**	**$9,300**
Annualized Cost	**$490**	**$870**	**$1,000**

iv. Alternative Higher Third Party Vendor Cost Scenario

While the estimated costs of the proposed rule are not highly sensitive to several of the unit cost assumptions described in this section—in part because most of the labor costs are generally estimated in hours rather than days or weeks—two of the major cost drivers of the proposed rule are software licensing fees and independent testing. Therefore, FinCEN compared how the estimated costs changed if third-party vendor costs increased by 100 percent.[324] The estimated costs are relatively sensitive to assumptions regarding third-party fees for certain AML/CFT functions because these comprise a large share of the overall costs for RIAs and ERAs with a *moderate* or *limited* number of existing AML/CFT measures in place. Table 4.36 reports alternative cost assumptions for third-party vendor costs that are double the primary estimate.[325] FinCEN assessed that the average technology costs used in the primary estimate are more likely to be representative of the costs likely to be incurred by RIAs and ERAs, which are typically much smaller than the bank benchmark in the 2020 GAO BSA Report. Smaller banks generally reported lower technology costs. However, for direct comparison this regulatory impact analysis reports higher estimated technology costs as an alternative scenario.

Table 4.36 Alternative Compliance Costs for Independent Testing, Software, and Other Third Party Technology Vendors (in 2022 dollars)

Compliance Activity	Primary Estimate Cost Assumption	Alternative Cost Assumption
AML/CFT Software Costs	$12,400	$24,800
Independent Testing	$17,000	$34,000

[324] Independent testing under the proposed rule can be conducted by an adviser's employees and is not required to be conducted by a third-party vendor. The costs identified here could be less than estimated to the extent employees (and not third-party vendors) are used.

[325] The alternative third party vendor costs are more in line with the cost estimates in the 2020 GAO BSA Report for ''Large Community Bank A'' ($501 million to $600 million in assets) and ''Large Credit Union A'' ($101 million to $201 million in assets). In comparison, the primary cost estimates are based on ''Large Community Bank B'' ($401 million to $500 million in assets) in the same report.

Table 4.37 provides a comparison of the estimated costs of the proposed rule under the higher technology cost scenario. Overall, the estimated costs would be approximately 60 percent higher under this scenario relative to the primary estimate. FinCEN ascribes a low probability to the average technology/third-party vendor costs being this high given the typical size of RIAs and ERAs affected by the proposed rule.

Table 4.37. Comparison of Compliance Costs using Higher Technology Cost Relative to the Primary Estimate ($ Millions, 2022) using a 2 percent Discount Rate

Year[1]	Primary Estimate	High Technology Cost Estimate
2024	$1,000	$1,500
2025	$840	$1,300
2026	$830	$1,300
2027	$790	$1,300
2028	$780	$1,300
2029	$770	$1,200
2030	$750	$1,200
2031	$740	$1,200
2032	$720	$1,200
2033	$710	$1,100
10-Year Undiscounted Cost	**$8,700**	**$14,000**
10-Year Present Value	**$8,000**	**$13,000**
Annualized Cost	**$870**	**$1,400**

5. Regulatory Alternatives

This section evaluates the potential benefits and costs of regulatory alternatives in comparison to the proposed regulation. This regulatory impact analysis considers two alternatives as described below.

(a) Alternative 1: Inclusion of State-Registered Investment Advisers

In the first alternative, FinCEN considered including State-registered investment advisers in the proposed rule. This alternative would bring all investment advisers that file Form ADV and register with a Federal *or State* regulatory authority under the scope of the proposed rule. FinCEN estimates there are approximately 17,000 State-registered investment advisers, based on reports from the North American Security Administrators Association (NASAA).[326] Table 5.1 summarizes their characteristics.

Table 5.1: Characteristics of State-registered Investment Advisers[327]

Characteristic	
Number of Investment Advisers	17,063
Average No. Employees	2.9
Avg. No. Individual Clients	46
Avg. No. PIV Clients	0.1
Avg. No. Legal Entity Clients	1.1
Avg. AUM	$24.7 million

FinCEN assumed that the costs of the rule would apply to State-registered investment advisers in the same way as for RIAs that are ''other advisers''. If State-registered investment advisers are less likely than RIAs to have any AML/CFT measures in the baseline, then this assumption would understate the costs of the rule for State-registered investment advisers. Under the assumptions of the cost model in section 3, Table 5.2. summarizes the total costs of Alternative 1 for State-registered investment advisers in addition to the other entities subject to regulation.

[326] *NASAA Investment Adviser Section: 2023 Annual Report,* p.2, *https://www.nasaa.org/wp-content/uploads/2023/09/2023-IA-Section-Report-FINAL.pdf.*

[327] *See Id.* The average number of employees per investment adviser was calculated as a weighted average of the bins reported on page 5, using the following employees for each respective bin: 2 [0–2 employees], 6.5 [3–10 employees], 15 [11–20 employees], 25 [>20 employees].

Table 5.2. Total Estimated Burden of Alternative 1 by Entity Type, by Year ($ Millions, 2022)

Year	Registered Investment Advisers	Exempt Reporting Advisers	State-registered Investment Advisers	Customers	Federal Agencies	Total
2024	$720	$280	$820	$25.0	$8.5	$1,900
2025	$620	$230	$680	$2.4	$8.5	$1,500
2026	$620	$230	$680	$2.6	$8.5	$1,500
2027	$600	$230	$680	$2.8	$8.5	$1,500
2028	$600	$230	$680	$3.1	$8.5	$1,500
2029	$600	$230	$680	$3.4	$8.5	$1,500
2030	$600	$230	$680	$3.7	$8.5	$1,500
2031	$600	$230	$680	$4.1	$8.5	$1,500
2032	$600	$230	$680	$4.5	$8.5	$1,500
2033	$600	$230	$680	$4.9	$8.5	$1,500

FinCEN assesses the potential benefits of including State-registered investment advisers in the definition of ''financial institution'' are significantly smaller relative to the likely benefits of including RIAs and ERAs. Although the overall benefits may exceed those of the proposed regulation because the requirements extend to a larger number of entities, the limited incremental benefits of applying the requirements to State-registered investment advisers suggest this would be a less cost-effective approach to regulation.

Specifically, including State-registered investment advisers nearly doubles the cost of the proposed rule, because of the large number of State-registered investment advisers. But such inclusion is less likely to achieve the same degree of benefits as for other investment advisers, partly because State-registered advisers are smaller, in terms of number of clients and AUM, and their customers tend to be localized. Treasury's risk assessment found few examples of State-registered investment advisers being used to move illicit proceeds or facilitate other illicit activity.[328] Further, the vast majority of their clients are natural persons who are not high net-worth customers and are U.S. persons.[329] Therefore, FinCEN rejected this regulatory alternative in favor of the more cost-effective approach in the proposed regulation.

(b) Alternative 2: Requirements for Private Fund Advisers To Conduct Risk-Based Customer Due Diligence and Amendments to Form PF for Reporting Beneficial Ownership Information for the Private Funds Being Advised

In the second alternative, FinCEN considered whether to limit the rule requirements to only certain reporting requirements among private fund advisers. In particular, the alternative rule would require private fund advisers to conduct risk-based customer due diligence and to report beneficial ownership information.

Under Alternative 2, investment advisers would incur compliance costs associated with the following requirements: (1) identifying beneficial ownership for new legal entity and PIV accounts and (2) developing a customer risk profile for legal entities. Investment advisers would be exempt from other requirements of the BSA, including developing and maintaining an AML/CFT program, filing SARs, and other recordkeeping requirements. Investment advisers that do not advise private funds would also be exempt from any requirement. Alternative 2 would limit both the covered population and the number of requirements, relative to the proposed rule. FinCEN estimates there are approximately 11,000 RIAs advising private funds, as well as all ERAs. Some RIAs and ERAs already have measures in place that would meet the requirements of Alternative 2.

FinCEN estimated the cost of Alternative 2 based on the same cost methodology as in section 3, in this case only for investment advisers that report private funds in Form ADV. As described in sections 2 and 3, FinCEN's cost analysis assumed that RIAs and ERAs with a *significant* or *moderate* number of AML/CFT measures would already meet the requirements of Alternative 2; those RIAs and ERAs would have zero cost burden under this alternative. Therefore, the costs are borne only by RIAs and ERAs with a *limited* number of AML/CFT measures in the baseline. FinCEN used Form ADV data for those advisers that advise private funds, and Table 5.3. summarizes the total costs of Alternative 2. For Alternative 2, there are no estimated Federal agency costs attributed to the CDD requirement.

[328] *See* Treasury, *Investment Adviser Illicit Finance Risk Assessment, https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.*

[329] A survey of select State securities regulators found that for State-registered investment advisers they supervised, on average, less than 3 percent of their customers were non-U.S. persons.

Table 5.3. Total Estimated Burden of Alternative 2 by Entity Type, by Year ($ Millions, 2022)

Year[1]			Registered Investment Advisers	Exempt Reporting Advisers	Customers	Total	
2024	$33.0	$1.4	$25.0	$60.0			
2025			$9.1	$1.0		$2.4	$12.0
2026			$9.4	$1.0		$2.6	$13.0
2027			$5.9	$1.0		$2.8	$9.7
2028			$6.3	$1.0		$3.1	$10.0
2029			$6.7	$1.0		$3.4	$11.0
2030			$7.2	$1.0		$3.7	$12.0
2031			$7.7	$1.0		$4.1	$13.0
2032			$8.3	$1.0		$4.5	$14.0
2033			$8.9	$1.0		$4.9	$15.0

FinCEN rejected this regulatory alternative in favor of the proposed regulation because, although it is a less costly rule, it is less likely to provide a similar level of benefits and thus would not achieve FinCEN's objectives in addressing the illicit finance risk for investment advisers. The absence of mandatory SAR filing in this regulatory alternative would limit the potential benefits to law enforcement to investigate financial crimes and interagency cooperation on national security threats and their associated financial activity. Further, the lack of information sharing authorities would limit the ability of law enforcement and other agencies, as well as other financial institutions, to provide more specific information on illicit finance threats. This alternative would also not be sufficient for the U.S. to be in compliance with the international AML/CFT standards established by the FATF.

(c) Comparison

Table 5.4 reports the costs for each of the regulatory alternatives in comparison to the proposed regulation.

Table 5.4. Comparison of Costs of Regulatory Alternatives to the Proposed Regulation ($ Millions, 2022) using a 2 percent Discount Rate

Year[1]	Alternative 1	Proposed Regulation	Alternative 2
2024	$1,900	$1,000	$60.0
2025	$1,500	$840	$12.0
2026	$1,500	$830	$13.0
2027	$1,400	$790	$9.1
2028	$1,400	$780	$9.6
2029	$1,400	$770	$10.0
2030	$1,400	$750	$11.0
2031	$1,300	$740	$11.0
2032	$1,300	$720	$12.0
2033	$1,300	$710	$12.0
10-Year Undiscounted Cost	**$16,000**	**$8,700**	**$170.0**
10-Year Present Value	**$14,000**	**$8,000**	**$160.0**
Annualized Cost	**$1,600**	**$870**	**$17.0**

Table 5.5 provides a detailed summary of the costs and benefits associated with each regulatory alternative (annualized using a 2 percent discount rate over 10 years).

Table 5.5. Summary of Benefits and Costs of Regulatory Alternatives ($ Millions, 2022)

	Alternative 1	Proposed Regulation	Alternative 2
Number of Covered Entities	38,300	21,237	17,614
Annualized Monetized Benefits (2%)	N/A	N/A	N/A
Unquantified Benefits	• Increase access for law enforcement to relevant information for complex financial crime investigations and asset forfeiture. • Enhance interagency understanding of priority national security threats and their associated financial activity. • Improve financial system transparency and integrity, and align with international financial standards to strengthen the U.S. financial system from abuse by illicit actors.	• Increase access for law enforcement to relevant information for complex financial crime investigations and asset forfeiture. • Enhance the ability of law enforcement to identify and prosecute money laundering and other financial crimes. • Enhance interagency understanding of priority national security threats and their associated financial activity. • Enhance the ability of national security personnel to protect against priority national security threats. • Improve financial system transparency and integrity, and align with international financial standards to strengthen the U.S. financial system from abuse by illicit actors.	• Improve financial system transparency and integrity for certain investment advisers.
Annualized Monetized Costs, millions (2%)	$1,570	$870	$17
Annualized monetized net benefits, millions (2%)	-$1,570	-$870	-$17
Change from the Proposed Regulation	-$700	N/A	+$850

B. Regulatory Flexibility Analysis

The RFA [330] requires an agency either to provide an initial regulatory flexibility analysis (IRFA) with a proposed rule or certify that the proposed rule would not have a significant economic impact on a substantial number of small entities. This section, VII.B, contains the IRFA prepared pursuant to the RFA. A final regulatory flexibility analysis or certification that the proposed rule would not have a significant economic impact on a substantial number of small entities will be conducted after consideration of comments received during the comment period.

1. Statement of the Need for, and Objectives of, the Proposed Rule

As described above in section IV.A.1 and section VII.A.1, FinCEN is proposing this rule to address identified illicit finance risks in the investment adviser industry. FinCEN is proposing regulations to apply AML/CFT program, recordkeeping and reporting requirements to RIAs and ERAs.

2. Small Entities Affected by the Proposed Rule

FinCEN is proposing to define the term small entity in accordance with the definition of ''small business'' or ''small organization'' under the Advisers Act rule adopted for purposes of the RFA, in lieu of using the Small Business Administration's definition.[331]

Relying on the SEC's definition, which it has adopted by regulation, has the benefit of ensuring consistency in the categorization of small entities for the SEC's purposes,[332] as well as providing the advisory industry with a uniform standard. Using the SEC standard also allows FinCEN to use the most current and precise data about investment advisers. Investment advisers must update Form ADV,

[330] 5 U.S.C. 601 *et seq.*

[331] *See* 13 CFR 121.201.

[332] As noted above, FinCEN is proposing to amend section 1010.810 to include investment advisers within the list of financial institutions that the SEC would examine for compliance with the BSA's implementing regulations.

including whether they qualify as a ''small entity,'' at least annually. Because Form ADV information is individualized to each investment adviser, FinCEN can identify the specific entities qualifying as ''small entities'' under the SEC standard.

In contrast, information on business revenue is derived from the Economic Census, and the most recent Economic Census data reflect business information for 2017. This data is not individualized to specific firms and as detailed below, likely includes other firms that are not covered by the proposed rule requiring FinCEN to make additional assumptions. This data represents the average revenues of all firms, not just RIAs and ERAs, with less than $50 million in annual receipts rather than firms with assets under management of less than $25 million. This is likely to be an underestimate because those firms that are required to register with the SEC tend to be larger and many of the firms reported in the SUSB, particularly State-registered investment advisers, would not be subject to the proposed rule. Given the data limitations, it is not feasible to directly estimate the average annual revenues of investment advisers that fall under the definition of ''small entity'' described above.

Further, using a standard tied to AUM is consistent with how Congress (in the 2010 Dodd-Frank Act) and SEC regulations distinguish between small, mid-sized, and large investment advisers and how other regulatory requirements are applied to investment advisers.[333] Using this standard would also be consistent with the standard applied by FinCEN in the Second Proposed Investment Adviser Rule and the SEC in recent rulemakings for investment advisers.[334] This is a well-known, common-sense understanding of investment adviser size based on assets under management (*e.g.,* small advisers are those managing less than $25 million in customer assets). Further, FinCEN notes that over 70 percent of advisers covered by the proposed rule manage at least $110 million in customer assets and accordingly would not be understood to be small entities.

In addition, FinCEN's proposed use of the SEC's definition of small entity will have no material impact upon the application of these proposed rules to the advisory industry. FinCEN requests comment on the appropriateness of using the SEC's definition for these purposes.

Under SEC rules under the Advisers Act, for the purposes of the RFA, an investment adviser generally is a small entity if it: (i) has, and reports on Form ADV, assets under management of less than $25 million; (ii) has less than $5 million on the last day of its most recent fiscal year; and (iii) does not control, is not controlled by, and is not under common control with another investment adviser that has assets under management of $25 million or more, or any person (other than a natural person) that had total assets of $5 million or more on the last day of its most recent fiscal year.[335]

Generally speaking, only large advisers, having $110 million or more in regulatory assets under management, are required to register with the SEC.[336] The proposed rule would not affect most investment advisers that are small entities (''small advisers'') because they are generally registered with one or more State securities authorities and not with the SEC. Under section 203A of the Advisers Act, most small advisers are prohibited from registering with the Commission and are regulated by State regulators.[337]

As of July 2023, there were 573 RIAs that would be considered ''small entities'' under the SEC's definition. We estimate that there are no ERAs that would meet the definition of ''small entity.'' [338] Therefore, approximately 2.7 percent of all investment advisers impacted by the proposed regulation are estimated to be small entities. Based on this, FinCEN estimates that the proposed rule will not impact a substantial number of small entities.

Regarding the economic impact on small entities, Form ADV does not collect revenue information. Therefore, additional information on investment advisers was obtained from the U.S. Economic Census. The Economic Census, conducted every five years by the U.S. Census Bureau, is the U.S. Government's official measure of American businesses, representing most industries and geographic areas of the United States and Island Areas.[339] It provides information on business locations, employees, payroll, and revenues. The most recent Economic Census data reflect business information for 2017. These data are reported in the U.S. Census Bureau's annual Statistics of U.S. Businesses (SUSB).

Based on data from the 2017 SUSB: Other Financial Investment Activities (for NAICS 5239), the average firm had approximately $7.4 million in annual revenue adjusted for inflation to 2022 dollars using the GDP price deflator.[340] Furthermore, according to that data, approximately 98 percent of firms had less than $50 million in annual receipts, with average revenues of approximately $1.6 million measured in 2022 dollars. Table B–1 reports the distribution of firms in other financial investment activities (NAICS 5239) by firm size.

[333] *See* 15 U.S.C. 80b–3a. As described above, SEC registration is generally determined by AUM. *See supra,* n. 24. In addition, investment advisers filing Form PF are required to provide additional information if they have more than $1.5 billion in hedge fund assets under management or more than $2 billion in private equity fund assets under management. *See* Form PF Instructions on p. 2 and 3 at *https://www.sec.gov/files/formpf.pdf.*

[334] *See* 80 FR at 52695; *see also* SEC, *Private Fund Advisers; Documentation of Registered Investment Adviser Compliance Reviews,* Final Rule, Investment Advisers Act Release No. 6383 (Aug. 23, 2023) 88 FR 63206, 63382–3, (Sep. 14, 2023).

[335] 17 CFR 275.0–7(a).

[336] *See* 17 CFR 275.203A–1.

[337] Based on Form ADV data as of July 31, 2023. To determine the number of RIAs that were ''small entities'', Treasury reviewed responses to Items 5.F. and 12 of Form ADV.

[338] In order for an adviser to be an ERA it would first need to have an SEC registration obligation, and an adviser with that little in assets under management (*i.e.,* assets under management that is low enough to allow the adviser to qualify as a small entity) would not have an SEC registration obligation. *See* 88 FR 63206, 63383 and footnote 1895 regarding small entity ERAs.

[339] U.S. Census Bureau, Economic Census, web page, last updated on Aug. 31, 2023.

[340] Data accessed at *https://www.census.gov/data/tables/2017/econ/susb/2017-susb-annual.html.*

Table B.1. Average Annual Receipts and Employment by Firm Size for NAICS 5239

Firm Size (based on 2017 receipts)	Percent of Firms	Average Annual Receipts ($2022)
<$100,000	20.3	$55,000
$100,000-$499,999	39.5	$300,000
$500,000-$999,999	15.0	$830,000
$1,000,000-$2,499,999	12.4	$1,800,000
$2,500,000-$4,999,999	4.8	$4,000,000
$5,000,000-$7,499,999	1.8	$6,800,000
$7,500,000-$9,999,999	1.0	$9,600,000
$10,000,000-$14,999,999	1.0	$13,000,000
$15,000,000-$19,999,999	0.6	$18,000,000
$20,000,000-$24,999,999	0.4	$23,000,000
$25,000,000-$29,999,999	0.3	$27,000,000
$30,000,000-$34,999,999	0.2	$30,000,000
$35,000,000-$39,999,999	0.2	$34,000,000
$40,000,000-$49,999,999	0.3	$40,000,000
$50,000,000-$74,999,999	0.4	$50,000,000
$75,000,000-$99,999,999	0.2	$67,000,000
$100,000,000+	1.5	$380,000,000
All Firms <$50,000,000	**97.9**	**$1,600,000**
All Firms $50,000,000+	**2.1**	**$280,000,000**
Total	**100**	**$7,400,000**

Importantly, as discussed above regarding the limitations with Economic Census data, the $1.6 million figure is an imperfect proxy for the annual revenues of investment advisers subject to the proposed rule that meet the SEC's definition of a small entity.

As further detailed in the section below, using information from the SUSB for firms with revenues below $50 million, FinCEN estimates that the annualized cost burden of the proposed rule would be approximately 2.6 percent of revenues for a small investment adviser. FinCEN is unable to conclusively determine whether such a cost burden would be ''significant'' for purposes of the RFA, and so as it is unable to certify that the proposed rule would not ''have a significant economic impact on a substantial number of small entities.'' Therefore, FinCEN is conducting this IRFA.

3. Compliance Costs

To examine the potential impact of the proposed rule on small entities, FinCEN estimates the average compliance costs for a small firm and compares those costs to small firms' average annual revenues. As described above, 573 RIAs would be considered small entities under the proposed definition. All small firms affected by this rule will bear upfront costs to revise their standard operating procedures to establish or update an existing AML/CFT program. Small firms that do not already have a *significant* or *moderate* number of AML/CFT measures in place would need to adopt additional measures, such as collecting additional information to develop a customer risk profile for new and existing clients and conducting ongoing CDD, filing SARs, acquiring AML/CFT software licenses, complying with other information collection requests, and general recordkeeping activities. To estimate these costs for small entities, FinCEN relies on the methodology described in the Impact Analysis applied to the subset of entities and relevant financial characteristics of small RIAs. Table B.2 reports the financial characteristics of small entities compared with all other RIAs impacted under the proposed rule based on information reported in their Form ADV filings.[341]

[341] This information is reported in Table 2.7 of the Impact Analysis.

Table B.2: Characteristics of RIAs by Business Size

Characteristic	Small Entities	All Other RIAs
Average No. Employees	6	65
Percent that Advise Private Funds	23%	55%
Avg. No. Individual Clients	1,003	3,450
Avg. No. High-net Worth Clients	1	492
Avg. No. PIV Clients	0	7
Avg. No. Legal Entity Clients	15	187

Based on this information, the average cost of the proposed rule for a small investment adviser (*i.e.,* those managing up to $25 million in client assets) would be approximately $48,000 in the first year of the regulation and $40,000 in subsequent years. These costs vary slightly across the different categories of RIAs described in the Impact Analysis, with a small number of dual registrants likely to incur less than $1,000 in compliance costs. Table B.3. reports the average costs per small entity by compliance activity in the first year and subsequent years of the proposed regulation.

Table B.3: Average Costs Per Small Entity (in 2022 dollars)

Activity	Year 1	Years 2-10
AML/CFT Program	$25,000	$17,000
Customer Due Diligence	$1,500	$1,000
SAR Filings	$10,000	$10,000
Recordkeeping	$2,200	$2,200
314(a) Requests	$1,500	$1,500
Software Licensing	$7,700	$7,700
Section 311 Measures	$240	$240
Total	**$48,000**	**$40,000**

Therefore, the average annualized cost of the proposed rule for a small investment adviser over the first 10 years would be approximately $41,000. This suggests the annualized cost burden of the proposed rule would be approximately 2.6 percent of revenues for a small investment adviser when using information from the SUSB for firms with revenues below $50 million. However, this estimate assumes that less than 1 percent of small investment advisers have a *significant number of* AML/CFT measures in place and more than 60 percent have a *limited* number of AML/CFT measures in place and would have to develop a full AML/CFT program and initial and ongoing CDD measures. If the assumed distribution was overly pessimistic and more small investment advisers had a *significant* or *moderate* number of existing AML/CFT measures in place in the baseline, the average cost burden would be lower. Based on the lower bound estimate discussed in section 3, the average annualized cost of the proposed rule for a small investment adviser would be approximately $38,000, suggesting the average cost burden would be approximately 2.4 percent of revenues. Table B.4 reports the number of small entities, annualized cost, and compliance cost as a percentage of revenue for small firms, broken down by industry category.

Table B.4. Average Annualized Cost of the Proposed Rule for Small Entities

Investment Adviser Type	Number of Small Entities	Average Annualized Cost[1]	Compliance Cost as Percentage of Annual Revenue
Dual Registrants	5	<$1,000	<0.1%
Affiliated or Other Advisers with a *Moderate* Number of AML/CFT Measures	214	$31,000	1.9%
Affiliated Advisers with a *Limited* Number of AML/CFT Measures	12	$61,000	3.8%
Other Advisers with a *Limited* Number of AML/CFT Measures	342	$47,000	2.9%
All Small Entities	**573**	**$41,000**	**2.6%**

4. Duplicative, Overlapping, or Conflicting Federal Rules

As described above in section VII.A.1, there are no Federal rules that directly and fully duplicate, overlap, or conflict with the proposed rule. While some investment advisers implement AML/CFT requirements because they are dually registered as broker-dealers, as a bank, or affiliated with a bank or broker-dealer, the majority of the investment adviser industry is not subject to any comprehensive AML/CFT requirements. FinCEN is aware that requirements within the Advisers Act and other Federal securities laws impose requirements upon investment advisers that in some instances are similar to the requirements proposed within this rule and perform similar roles (*i.e.,* improving the integrity of the U.S. financial system and protecting customers). However, while these existing requirements may provide a supporting framework for implementing certain obligations in the proposed rule, they do not impose the specific AML/CFT measures in the proposed rule.

5. Significant Alternatives That Reduce Burden on Small Entities

FinCEN considered the burden this proposed approach would have on covered investment advisers. FinCEN is mindful of the effect of new regulations on small businesses, given their critical role in the U.S. economy and the special consideration that Congress and successive administrations have mandated that Federal agencies should give to small business concerns. FinCEN considered an alternative scenario in the Impact Analysis above (Alternative 2) that would apply a much more limited information collection requirement to only those RIAs that advise private funds and ERAs (who only advise private funds). In this scenario, advisers to private funds would be required to conduct risk-based customer due diligence and to report beneficial ownership information.

Table B.5: Average Cost of Information Collection for Ongoing CDD

Activity	New Account Clerk		Total Hours	Total Cost per Customer
	% Time	Hourly Cost		
Develop a Customer Risk Profile for a Legal Entity	100%	$34.74	0.25	$8.68
Collect Beneficial Ownership Information for a Legal Entity	100%	$34.74	0.5	$17.37
Collect Beneficial Ownership Information for a Pooled Investment Vehicle	100%	$34.74	3.0	$104.22

Based on the cost information in the table above and the number of legal entity and PIV customers of small entity RIAs identified in Table 2.7 of the Impact Analysis, FinCEN estimates that the cost of this alternative for each small entity would be less than $1,000 on average.

Despite the significantly smaller cost of this alternative, FinCEN determined that this alternative would not accomplish the objectives of the proposed rule. As noted above, the absence of a SAR filing requirement would limit the potential benefits to law enforcement to investigate financial crimes and interagency cooperation on national security threats and their associated financial activity. Further, without being defined as financial institutions and thereby being able to receive and share information under sections 314(a) and 314(b), investment advisers would be unable to access useful information to help mitigate illicit finance risks.

As another alternative to reduce the burden on small entities, FinCEN considered limiting the applicability of the proposed rule to investment advisers with AUM above a certain threshold, as reported on Form ADV. Investment advisers with AUM below the threshold would be exempt from the requirements of the proposed rule.

FinCEN decided not to pursue this alternative because doing so would not apply a risk-based approach to the industry. AUM by itself, without

considering the attributes of a particular customer (such as legal entity v. natural person, or U.S. v. non-U.S. person), is not a useful indicator of potential risk.[342] Such an exemption could also create a subset of ''smaller'' investment advisers who may actually be *more* vulnerable to illicit finance because they can offer the same services as other advisers, but without any AML/CFT requirements.

FinCEN also notes that the AML/CFT requirements in the proposed rule are designed to be risk-based and their cost is largely based on factors directly correlated with the size of an investment adviser, such as the number of customers and transactions, along with the risk level of its advisory activities and customers. For instance, according to the 2020 GAO BSA Report, the two most costly requirements for banks as a percentage of total AML/CFT compliance costs were the customer due diligence and SAR filing requirements, accounting for approximately 60 percent of total costs.[343] The cost of other requirements in the proposed rule, such as employee training, are also likely to vary with the size of the business. The requirements of the proposed rule therefore have some inherent flexibility whereby small entities serving a smaller number of customers are likely to have lower costs.

FinCEN welcomes comment on this IRFA and any significant alternatives that would minimize the impact of the proposed rule on small entities and still accomplish the objectives of the proposed rule.

C. Paperwork Reduction Act

The reporting requirements in the proposed rule are being submitted to OMB for review in accordance with the Paperwork Reduction Act of 1995 (PRA).[344] Under the PRA, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a valid control number assigned by OMB. Written comments and recommendations for the proposed information collection can be submitted by visiting *www.reginfo.gov/public/do/PRAMain.* This particular document may be found by selecting ''Currently Under Review—Open for Public Comments'' or by using the search function. Comments are welcome and must be received by April 15, 2024. In accordance with requirements of the PRA, 44 U.S.C. 3506(c)(2)(A), and its implementing regulations, 5 CFR part 1320, the following information concerns the collection of information as it relates to the proposed rule and is presented to assist those persons wishing to comment on the information collection.

The PRA analysis included herein is for the sections of the proposed rule requiring RIAs and ERAs to (a) establish AML/CFT programs, to include risk-based procedures for conducting ongoing customer due diligence; (b) report suspicious activity and file CTRs; (c) maintain records of originator and beneficiary information for certain transactions; (d) apply information sharing provisions with the government and between financial institutions; and (e) implement special due diligence requirements for correspondent and private banking accounts and special measures under section 311 of the USA PATRIOT Act.

Reporting and Recordkeeping Requirements: The proposed rule would require RIAs and ERAs to develop and implement AML/CFT programs, file SARs and CTRs, record originator and beneficiary information for transactions, respond to section 314(a) requests, and implement special due diligence measures for correspondent and private banking accounts. The AML/CFT programs must be written (first year only), and updated, stored, and made available for inspection by FinCEN and the SEC. The AML/CFT program must also be approved by the investment adviser's board of directors or trustees.

OMB Control Numbers: 1506–AB58.

Frequency: As required; varies depending on the requirement.

Description of Affected Public: investment advisers, as defined in the proposed rule.

Estimated Number of Respondents: 21,237 investment advisers. Of these, there are an estimated 15,391 SEC-registered investment advisers and 5,846 exempt reporting advisers. 1,356,780 clients of investment advisers in the first year and up to 266,407 new clients in each subsequent year, although this figure will vary from year to year.

Estimated Total Annual Reporting and Recordkeeping Burden: FinCEN estimates that during Year 1 the annual burden will be 7,142,302 hours for investment advisers and 508,792 hours for their clients. That burden will decrease after the first year because several information collection activities will only result in costs for these entities in Year 1. Specifically, investment advisers that do not already have a written AML/CFT program will have to develop one in the first year. In addition, entities that do not already conduct customer due diligence activities consistent with the requirements under the BSA will have to implement those information collection activities in the first year. FinCEN estimates that several of these costs will be incurred only in the first year of the regulation, but information collection activities related to understanding the nature and purpose of all existing customer accounts will likely be incurred over the first few years due to the large number of accounts—in this case, FinCEN assumes these costs will be spread over the first three years of the proposed regulation. Furthermore, FinCEN assesses that the information collection burden associated with customer due diligence will increase over time because the total number of clients is expected to grow each year. The number of clients and therefore the total costs associated with due diligence measures are expected to grow over time. Thus, there will be stepwise decrease in burden hours in Year 2 and Year 4, but a gradual increase in burden hours in Year 3 and Years 5 through 10 due to growth in the number of clients. In Year 10, FinCEN estimates the annual burden of the proposed regulation will be 5,395,622 hours for investment advisers and 99,903 hours for new clients, with no additional burden for existing clients.

Estimated Total Annual Reporting and Recordkeeping Cost: As described in section 3, FinCEN calculated a weighted fully loaded hourly labor cost based on the roles, hourly wage rates, and burden distribution of staff involved in each information collection activity. FinCEN estimates that during Year 1 the annual cost will be $429,383,548 for investment advisers and $25,016,407 for their clients. In Year 10, FinCEN estimates the total cost of the proposed regulation will be $311,901,932 for investment advisers and $4,812,035 for their clients.

Table C.1 reports the total number of investment advisers, burden hours, and costs by information collection activity. Burden hours and costs are calculated by multiplying the number of entities by the hours/costs per entity for each information collection activity. Burden hours and costs are summarized for Year 1 and Year 10.

Table C.2 reports the total number of clients, burden hours, and costs by information collection activity. Burden hours and costs are calculated by multiplying the number of clients by the hours per entity. Burden hours and costs are summarized for Year 1 and Year 10.

[342] *See* Treasury, *Investment Adviser Illicit Finance Risk Assessment, https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.*

[343] 2020 GAO BSA Report at p. 3.

[344] 44 U.S.C. 3506(c)(2)(A).

Table C.3 reports the total cost of information collection by year.

Tables C.4 through C.10 report additional detail for each subset of entities, including information on the distribution of the information collection burden across different groups. These tables summarize the number of entities, burden hours per entity, total burden hours, average cost per entity, and total cost.

Table C.11 reports the total cost of information collection for the customers of investment advisers. This table summarizes the number of customers, burden hours per customer, total burden hours, average cost per customer, and total cost.

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Table C.1. Total Burden and Cost for Investment Advisers (in 2022 dollars)

Number of Entities	Year 1		Year 10	
	21,237		21,237	
Information Collection	**Burden Hours**	**Cost**	**Burden Hours**	**Cost**
Develop AML/CFT Program	1,515,600	$103,897,022	0	$0
Maintain and Update Written AML/CFT Program	8,607	$590,025	12,630	$865,809
Store the Written AML/CFT Program	717	$49,169	1,053	$72,151
Produce Written AML/CFT Program Upon Request	717	$49,169	1,053	$72,151
Obtain Written Approval of AML/CFT Program	66,774	$11,513,265	25,260	$4,355,364
Customer Identification and Verification	472,719	$16,421,866	278,459	$9,673,426
SAR Case Review and Filing (1010.320)	3,425,943	$212,068,631	3,425,943	$212,068,631
CTR Recordkeeping and Reporting (1010.315)	0	$0	0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	1,037,850	$45,815,237	1,037,850	$45,815,237
Information Sharing Arrangements (1010.510)	505,087	$30,862,402	505,087	$30,862,402
Special Due Diligence and Special Measures (1010.610 and 1010.620)	25,260	$3,043,491	25,260	$3,043,491
Section 311 Special Measures	83,028	$5,073,271	83,028	$5,073,271
TOTAL	**7,142,302**	**$429,383,548**	**5,395,622**	**$311,901,932**

Table C.2. Total Burden and Cost for Clients (in 2022 dollars)

Number of Entities	Year 1		Year 10	
	1,356,780		266,407	
Information Collection	**Burden Hours**	**Cost**	**Burden Hours**	**Cost**
Provide Customer Information	508,792	$25,016,407	99,903	$4,912,035
TOTAL	**508,792**	**$25,016,407**	**99,903**	**$4,912,035**

Table C.3. Total Information Collection Cost by Year (in 2022 dollars)

Year	Information Collection Burden (Hours)	Information Collection Cost ($M)	
2024		7,651,095	$454.4
2025		5,772,942	$325.7
2026		5,790,333	$326.4
2027		5,336,657	$310.7
2028		5,357,509	$311.5
2029		5,380,341	$312.4
2030		5,405,343	$313.3
2031		5,432,721	$314.4
2032	5,462,698	$315.5	
2033		5,495,524	$316.8
TOTAL	**57,085,163**	**$3,301.1**	

Table C.4. Total Burden and Cost for Dual Registrants

Number of Entities	480							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	0	0	$0	$0	0	0	$0	$0
Maintain and Update Written AML/CFT Program	1	480	$68.55	$32,905	0	0	$0	$0
Store the Written AML/CFT Program	0.083	40	$5.71	$2,742	0	0	$0	$0
Produce Written AML/CFT Program Upon Request	0.083	40	$5.71	$2,742	0	0	$0	$0
Obtain Written Approval of AML/CFT Program	0	0	$0	$0	0	0	$0	$0
Customer Identification, Verification, and Recordkeeping	0	0	$0	$0	0	0	$0	$0
SAR Case Review and Filing (1010.320)	0	0	$0	$0	0	0	$0	$0
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	0	0	$0	$0	0	0	$0	$0
Information Sharing Arrangements (1010.510)	0	0	$0	$0	0	0	$0	$0
Special Due Diligence and Special Measures (1010.610 and 1010.620)	0	0	$0	$0	0	0	$0	$0
Section 311 Special Measures	0	0	$0	$0	0	0	$0	$0
TOTAL	**1.167**	**560**	**$79.98**	**$38,389**	**0**	**0**	**$0**	**$0**

Table C.5. Total Burden and Cost for Affiliated and Other RIAs

Number of Entities	6,034							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	0	0	$0	$0	0	0	$0	$0
Maintain and Update Written AML/CFT Program	1	6,034	$68.55	$413,641	0	0	$0	$0
Store the Written AML/CFT Program	0.083	503	$5.71	$34,470	0	0	$0	$0
Produce Written AML/CFT Program Upon Request	0.083	503	$5.71	$34,470	0	0	$0	$0
Obtain Written Approval of AML/CFT Program	2	12,068	$344.84	$2,080,781	0	0	$0	$0
Customer Identification, Verification, and Recordkeeping	0	0	$0	$0	0	0	$0	$0
SAR Case Review and Filing (1010.320)	165.05	995,912	$10,216.73	$61,647,739	165.05	995,912	$10,216.73	$61,647,739
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	301,700	$2,207.22	$13,318,357	50	301,700	$2,207.22	$13,318,357
Information Sharing Arrangements (1010.510)	24.33	146,827	$1,486.84	$8,971,611	24.33	146,827	$1,486.84	$8,971,611
Special Due Diligence and Special Measures (1010.610 and 1010.620)	0	0	$0	$0	0	0	$0	$0
Section 311 Special Measures	4	24,136	$244.41	$1,474,785	4	24,136	$244.41	$1,474,785
TOTAL	**246.55**	**1,487,683**	**$14,580.02**	**$87,975,855**	**243.38**	**1,468,575**	**$14,155.20**	**$85,412,493**

Table C.6. Total Burden and Cost for Affiliated RIAs with a *Limited* Number of AML/CFT Measures in Place

Number of Entities	576							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	120	69,120	$8,226.21	$4,738,297	0	0	$0	$0
Maintain and Update Written AML/CFT Program	0	0	$0.00	$0	1	576	$68.55	$39,486
Store the Written AML/CFT Program	0	0	$0.00	$0	0.083	48	$5.71	$3,290
Produce Written AML/CFT Program Upon Request	0	0	$0.00	$0	0.083	48	$5.71	$3,290
Obtain Written Approval of AML/CFT Program	4	2,304	$689.69	$397,259	2	1,152	$344.84	$198,629
Customer Identification, Verification, and Recordkeeping	233.76	134,645	$8,120.57	$4,677,450	137.70	79,314	$4,783.49	$2,755,288
SAR Case Review and Filing (1010.320)	165.05	95,069	$10,216.73	$5,884,836	165.05	95,069	$10,216.73	$5,884,836
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	28,800	$2,207.22	$1,271,358	50	28,800	$2,207.22	$1,271,358
Information Sharing Arrangements (1010.510)	24.33	14,016	$1,486.84	$856,422	24.33	14,016	$1,486.84	$856,422
Special Due Diligence and Special Measures (1010.610 and 1010.620)	2	1,152	$240.97	$138,801	2	1,152	$240.97	$138,801
Section 311 Special Measures	4	2,304	$244.41	$140,782	4	2,304	$244.41	$140,782
TOTAL	**603.14**	**347,410**	**$31,432.64**	**$18,105,202**	**386.25**	**222,478**	**$19,604.48**	**$11,292,181**

Table C.7. Total Burden and Cost for Other RIAs with a *Limited* Number of AML/CFT Measures in Place

Number of Entities	8,345							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	120	1,001,400	$8,226.21	$68,647,716	0	0	$0	$0
Maintain and Update Written AML/CFT Program	0	0	$0.00	$0	1	8,345	$68.55	$572,064
Store the Written AML/CFT Program	0	0	$0.00	$0	0.083	695	$5.71	$47,672
Produce Written AML/CFT Program Upon Request	0	0	$0.00	$0	0.083	695	$5.71	$47,672
Obtain Written Approval of AML/CFT Program	4	33,380	$689.69	$5,755,426	2	16,690	$344.84	$2,877,713
Customer Identification, Verification, and Recordkeeping	40.28	336,149	$1,399.35	$11,677,547	23.73	198,011	$824.30	$6,878,748
SAR Case Review and Filing (1010.320)	165.05	1,377,342	$10,216.73	$85,258,598	165.05	1,377,342	$10,216.73	$85,258,598
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	417,250	$2,207.22	$18,419,239	50	417,250	$2,207.22	$18,419,239
Information Sharing Arrangements (1010.510)	24.33	203,062	$1,486.84	$12,407,705	24.33	203,062	$1,486.84	$12,407,705
Special Due Diligence and Special Measures (1010.610 and 1010.620)	2	16,690	$240.97	$2,010,921	2	16,690	$240.97	$2,010,921
Section 311 Special Measures	4	33,380	$244.41	$2,039,623	4	33,380	$244.41	$2,039,623
TOTAL	**409.66**	**3,418,653**	**$24,711.42**	**$206,216,775**	**272.28**	**2,272,161**	**$15,645.29**	**$130,559,956**

Table C.8. Total Burden and Cost for Affiliated and Other ERAs

Number of Entities	2,093							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	0	0	$0.00	$0	0	0	$0	$0
Maintain and Update Written AML/CFT Program	1	2,093	$68.55	$143,479	0	0	$0	$0
Store the Written AML/CFT Program	0.083	174	$5.71	$11,957	0	0	$0	$0
Produce Written AML/CFT Program Upon Request	0.083	174	$5.71	$11,957	0	0	$0	$0
Obtain Written Approval of AML/CFT Program	2	4,186	$344.84	$721,756	0	0	$0	$0
Customer Identification, Verification, and Recordkeeping	0	0	$0	$0	0	0	$0	$0
SAR Case Review and Filing (1010.320)	165.05	345,450	$10,216.73	$21,383,613	165.05	345,450	$10,216.73	$21,383,613
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	104,650	$2,207.22	$4,619,709	50	104,650	$2,207.22	$4,619,709
Information Sharing Arrangements (1010.510)	24.33	50,930	$1,486.84	$3,111,963	24.33	50,930	$1,486.84	$3,111,963
Special Due Diligence and Special Measures (1010.610 and 1010.620)	0	0	$0	$0	0	0	$0	$0
Section 311 Special Measures	4	8,372	$244.41	$511,555	4	8,372	$244.41	$511,555
TOTAL	**246.55**	**516,029**	**$14,580.02**	**$30,515,987**	**243.38**	**509,401**	**$14,155.20**	**$29,626,839**

Table C.9. Total Burden and Cost for Affiliated ERAs with a *Limited* Number of AML/CFT Measures in Place

Number of Entities	72							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	120	8,640	$8,226.21	$592,287	0	0	$0	$0
Maintain and Update Written AML/CFT Program	0	0	$0.00	$0	1	72	$68.55	$4,936
Store the Written AML/CFT Program	0	0	$0.00	$0	0.083	6	$5.71	$411
Produce Written AML/CFT Program Upon Request	0	0	$0.00	$0	0.083	6	$5.71	$411
Obtain Written Approval of AML/CFT Program	4	288	$689.69	$49,657	2	144	$344.84	$24,829
Customer Identification, Verification, and Recordkeeping	5.27	379	$182.96	$13,173	3.10	223	$107.78	$7,760
SAR Case Review and Filing (1010.320)	165.05	11,884	$10,216.73	$735,604	165.05	11,884	$10,216.73	$735,604
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	3,600	$2,207.22	$158,920	50	3,600	$2,207.22	$158,920
Information Sharing Arrangements (1010.510)	24.33	1,752	$1,486.84	$107,053	24.33	1,752	$1,486.84	$107,053
Special Due Diligence and Special Measures (1010.610 and 1010.620)	2	144	$240.97	$17,350	2	144	$240.97	$17,350
Section 311 Special Measures	4	288	$244.41	$17,598	4	288	$244.41	$17,598
TOTAL	**374.65**	**26,975**	**$23,495.03**	**$1,691,642**	**251.65**	**18,119**	**$14,928.77**	**$1,074,872**

Table C.10. Total Burden and Cost for Other RIAs with a *Limited* Number of AML/CFT Measures in Place

Number of Entities	3,637							
Information Collection	Year 1				Year 10			
	Hours Per Entity	Burden Hours	Cost Per Entity	Cost	Hours Per Entity	Burden Hours	Cost Per Entity	Cost
Develop Written AML/CFT Program	120	436,440	$8,226.21	$29,918,723	0	0	$0	$0
Maintain and Update Written AML/CFT Program	0	0	$0.00	$0	1	3,637	$68.55	$249,323
Store the Written AML/CFT Program	0	0	$0.00	$0	0.083	303	$5.71	$20,777
Produce Written AML/CFT Program Upon Request	0	0	$0.00	$0	0.083	303	$5.71	$20,777
Obtain Written Approval of AML/CFT Program	4	14,548	$689.69	$2,508,386	2	7,274	$344.84	$1,254,193
Customer Identification, Verification, and Recordkeeping	0.42	1,546	$14.76	$53,696	0.25	911	$8.70	$31,630
SAR Case Review and Filing (1010.320)	165.05	600,287	$10,216.73	$37,158,241	165.05	600,287	$10,216.73	$37,158,241
CTR Recordkeeping and Reporting (1010.315)	0	0	$0	$0	0	0	$0	$0
Travel and Recordkeeping Requirements (1010.410(a) through (c) and 1010.410(f))	50	181,850	$2,207.22	$8,027,654	50	181,850	$2,207.22	$8,027,654
Information Sharing Arrangements (1010.510)	24.33	88,500	$1,486.84	$5,407,648	24.33	88,500	$1,486.84	$5,407,648
Special Due Diligence and Special Measures (1010.610 and 1010.620)	2	7,274	$240.97	$876,419	2	7,274	$240.97	$876,419
Section 311 Special Measures	4	14,548	$244.41	$888,928	4	14,548	$244.41	$888,928
TOTAL	**369.81**	**1,344,993**	**$23,326.83**	**$84,839,697**	**248.80**	**904,887**	**$14,829.69**	**$53,935,591**

Table C.11. Total Burden and Cost for Clients

Number of Entities	Year 1				Year 10			
	1,356,780				266,407			
Information Collection	**Hours Per Entity**	**Burden Hours**	**Cost Per Entity**	**Cost**	**Hours Per Entity**	**Burden Hours**	**Cost Per Entity**	**Cost**
Provide Customer Information	0.375	508,792	$18.44	$25,016,407	0.375	99,903	$18.44	$4,912,035
Total	**0.375**	**508,792**	**$18.44**	**$25,016,407**	**0.375**	**99,903**	**$18.44**	**$4,912,035**

BILLING CODE 4810–02–C

D. Unfunded Mandates Reform Act

UMRA (section 202(a)) requires Federal agencies to prepare a written statement, which includes an assessment of anticipated costs and benefits, before issuing ''any rule that includes any Federal mandate that may result in the expenditure by State, local, and Tribal governments, in the aggregate, or by the private sector, of $100 million or more (adjusted annually for inflation) in any one year.'' The current threshold after adjustment for inflation is $176 million, using the 2022 GDP price deflator.[345] The proposed rule would result in an expenditure in at least one year that meets or exceeds this amount.

The total annualized cost of the proposed rule is estimated to be approximately $1.0 billion to the private sector in the first year. The annualized cost of the proposed rule after the first year is estimated to be approximately $760 million to the private sector. The proposed rule does not foreseeably impose costs or other compliance burden that would impact any State, local, or Tribal government. FinCEN believes that the Impact Analysis provides the analysis required by UMRA.

E. Questions for Comment

FinCEN requests comment on all aspects of the regulatory analysis in section VI:

- Do you agree with how FinCEN has characterized the extent to which different types of investment advisers are already implementing a *significant, moderate,* or a *limited* number of the AML/CFT requirements of the proposed rule?
- For ERAs, do you agree with FinCEN's assumption that the percentage of ERAs currently applying AML/CFT requirements would be the same as RIAs across all scenarios described in the Impact Analysis?
- Do you agree with FinCEN's assumption that the number of employees of an ERA is similar to the number of employees of an RIA with the same number of private funds?
- Do you agree with FinCEN's decision to not quantify the estimated benefits from the proposed rule? If no, what other data or methods may inform estimates of potential benefits from the proposed rule?
- Do you agree that some RIAs would designate their existing compliance officer as the AML/CFT compliance officer? What other existing positions in an RIA or ERA may be designated as the AML/CFT compliance officer?
- Do you agree with FinCEN's use of the reported values for ''Large Community Bank B,'' from the 2020 GAO BSA Report, as the entity for which the costs were assessed to be the most similar to the costs likely to be incurred by investment advisers covered by the proposed regulation?
- Do you agree with FinCEN's assumption that dual registrants covered by an existing AML/CFT program and entities that have a *significant* or *moderate* number of AML/CFT measures in place would only need to update their existing program to comply with the requirements of the proposed rule?
- Do you agree with FinCEN's estimates that it would take approximately 4 hours for a trustee or director to review and approve a written AML/CFT program the first year and approximately 2 hours each subsequent year to review the program?
- Do you agree with FinCEN's estimate that it would initially take an RIA or ERA that does not have an AML/CFT program 50 hours to develop an AML/CFT training program, and that for entities that have an existing AML/CFT training program, it would take approximately 10 hours to review and update training materials?
- Do you agree with FinCEN's estimate that the average cost of independent testing of an adviser's AML/CFT program would be approximately $17,000?
- Do you agree with FinCEN's assumption that of all the AML/CFT measures in the proposed rule, RIAs and ERAs are most likely to have some CDD measures in place, and that RIAs and ERAs would have to modify these existing procedures rather than develop new procedures?
- Do you agree with FinCEN's assumption that RIAs and ERAs would update customer information on existing accounts over the first three years after the promulgation of the proposed rule?
- Do you agree with FinCEN's assumption that unless an investment adviser is dual registrant or affiliated adviser, they are not currently filing SARs?
- Do you agree with FinCEN's estimate that RIAs are likely to file approximately 60 SARs per year? Do you agree with FinCEN's assumption that ERAs would also file 60 SARs a year? If not, what other estimate for the number of SARs or an RIA or ERA would be reasonable?
- Do you agree with FinCEN's decision to attribute labor costs primarily to a compliance officer rather than a financial clerk or teller, due to the smaller size of investment advisers relative to banks and to avoid potentially underestimating the average hourly labor costs associated with these activities?
- Do you agree with FinCEN's estimate that since all investment advisers are required to report transactions in currency over $10,000 on Form 8300, the incremental cost for RIAs and ERAs to use the CTR would be *de minimis*?
- Do you agree with FinCEN's decision to define the term small entity in accordance with definitions obtained from SEC rules implementing the Advisers Act in lieu of using the Small Business Administration's definition?
- Do you agree with how FinCEN has characterized the potential costs and benefits of imposing the AML/CFT requirements of the proposed rule to State-registered investment advisers?
- Are there other significant alternatives that would minimize the impact of the proposed rule on small entities and still accomplish the objectives of the proposed rule?

List of Subjects

31 CFR Part 1010

Administrative practice and procedure, Anti-money laundering, Banks, Banking, Brokers, Brokerage, Investment advisers, Money laundering, Mutual funds, Reporting and recordkeeping requirements, Securities, Suspicious transactions, Terrorist financing.

31 CFR Part 1032

Administrative practice and procedure, Anti-money laundering, Banks, Banking, Brokers, Brokerage, Investment advisers, Money laundering, Mutual funds, Reporting and recordkeeping requirements, Securities, Small business, Suspicious transactions, Terrorist financing.

Issuance and Authority

For the reasons set forth in the preamble, chapter X of title 31 of the Code of Federal Regulations is proposed to be amended as follows:

PART 1010—GENERAL PROVISIONS

■ 1. The authority citation for part 1010 continues to read as follows:

Authority: 12 U.S.C. 1829b and 1951–1959; 31 U.S.C. 5311–5314 and 5316–5336; title III, sec. 314, Pub. L. 107–56, 115 Stat. 307 ; sec. 701, Pub. L. 114–74, 129 Stat. 599; sec. 6403, Pub. L. 116–283, 134 Stat. 3388.

[345] U.S. Bureau of Economic Analysis, National Income and Product Accounts Tables, Table 1.1.9. Implicit Price Deflators for Gross Domestic Product.

■ 2. Section 1010.100 is amended by:
■ a. Removing the word ''or'' at the end of paragraph (t)(9);
■ b. Removing the period at the end of paragraph (t)(10), and adding in its place ''; or''; and
■ c. Adding paragraphs (t)(11) and (nnn).

The additions read as follows:

§ 1010.100 General definitions.

* * * * *

(t) * * *

(11) An investment adviser.

* * * * *

(nnn) *Investment adviser.* Any person who is registered or required to register with the SEC under section 203 of the Investment Advisers Act of 1940 (15 U.S.C. 80b–3(a)), or any person that is exempt from SEC registration under section 203(*l*) or 203(m) of the Investment Advisers Act of 1940 (15 U.S.C. 80b–3(l), (m)).

■ 3. Section 1010.410 is amended by:
■ a. Removing the word ''or'' at the end of paragraph (e)(6)(i)(I);
■ b. Removing the word ''and'' at the end of paragraph (e)(6)(i)(J) and adding in its place ''or''; and
■ c. Adding paragraph (e)(6)(i)(K).

The addition reads as follows:

§ 1010.410 Records to be made and retained by financial institutions.

* * * * *

(e) * * *

(6) * * *

(i) * * *

(K) An investment adviser; and

* * * * *

■ 4. Section 1010.605 is amended by:
■ a. Removing the word ''and'' at the end of paragraph (c)(2)(iii);
■ b. Removing the period at the end of paragraph (c)(2)(iv) and adding in its place ''; and'';
■ c. Adding paragraph (c)(2)(v);
■ d. Removing the word ''and'' at the end of paragraph (e)(1)(iii);
■ e. Adding the word ''and'' at the end of paragraph (e)(1)(iv); and
■ f. Adding paragraph (e)(1)(v).

The additions read as follows:

§ 1010.605 Definitions.

* * * * *

(c) * * *

(2) * * *

(v) As applied to investment advisers (as set forth in paragraph (e)(1)(v) of this section) means any contractual or other business relationship established between a person and an investment adviser to provide advisory services.

* * * * *

(e) * * *

(1) * * *

(v) An investment adviser except that an investment adviser shall not be considered a covered financial institution for the purposes of § 1010.230.

* * * * *

■ 5. Section 1010.810 is amended by revising paragraph (b)(6) to read as follows:

§ 1010.810 Enforcement.

* * * * *

(b) * * *

(6) To the Securities and Exchange Commission with respect to brokers and dealers in securities, investment advisers, and investment companies as that term is defined in the Investment Company Act of 1940 (15 U.S.C. 80a–1 *et seq.*);

* * * * *

■ 6. Add part 1032 to read as follows:

PART 1032—RULES FOR INVESTMENT ADVISERS

Subpart A—Definitions

Sec.

Subpart B—Programs

Subpart C—Reports Required To Be Made by Investment Advisers

Subpart D—Records Required To Be Maintained by Investment Advisers

Subpart E—Special Information Sharing Procedures To Deter Money Laundering and Terrorist Activity

Subpart F—Special Standards of Diligence; Prohibitions, and Special Measures for Investment Advisers

Authority: 12 U.S.C. 1829b and 1951–1959; 31 U.S.C. 5311–5314 and 5316–5336; title III, sec. 314, Pub. L. 107–56, 115 Stat. 307.

Subpart A—Definitions

§ 1032.100 Definitions.

Refer to § 1010.100 of this chapter for general definitions not noted in this part.

Subpart B—Programs

§ 1032.200 General.

Investment advisers are subject to the program requirements set forth and cross-referenced in this subpart. Investment advisers should also refer to subpart B of part 1010 of this chapter for program requirements contained in that subpart that apply to investment advisers.

§ 1032.210 Anti-money laundering/countering the financing of terrorism programs for investment advisers.

(a) *Anti-money laundering/countering the financing of terrorism program requirements for investment advisers.* (1) Each investment adviser shall develop and implement a written anti-money laundering/countering the financing of terrorism (AML/CFT) program that is risk-based and reasonably designed to prevent the investment adviser from being used for money laundering, terrorist financing, or other illicit finance activities and to achieve and monitor compliance with the applicable provisions of the Bank Secrecy Act (31 U.S.C. 5311, *et seq.*) and the implementing regulations promulgated thereunder by the Department of the Treasury. The investment adviser may deem the requirements in this subpart satisfied for any mutual fund (as defined in 31 CFR 1010.100(gg)) it advises that has developed and implemented an AML/CFT program compliant with the AML/CFT program requirements applicable to mutual funds under another provision of this subpart.

(2) Each investment adviser's anti-money laundering/countering the financing of terrorism program must be approved in writing by its board of directors or trustees, or if it does not have one, by its sole proprietor, general partner, trustee, or other persons that have functions similar to a board of directors. An investment adviser shall make its anti-money laundering/countering the financing of terrorism program available for inspection by FinCEN or the Securities and Exchange Commission (SEC).

(b) *Minimum requirements.* The anti-money laundering/countering the

financing of terrorism program shall at a minimum:

(1) Establish and implement policies, procedures, and internal controls reasonably designed to prevent the investment adviser from being used for money laundering, terrorist financing, or other illicit finance activities and to achieve compliance with the applicable provisions of the Bank Secrecy Act and implementing regulations in this chapter;

(2) Provide for independent testing for compliance to be conducted by the investment adviser's personnel or by a qualified outside party;

(3) Designate a person or persons responsible for implementing and monitoring the operations and internal controls of the program;

(4) Provide ongoing training for appropriate persons; and

(5) Implement appropriate risk-based procedures for conducting ongoing customer due diligence, to include, but not be limited to:

(i) Understanding the nature and purpose of customer relationships for the purpose of developing a customer risk profile; and

(ii) Conducting ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

(c) *Effective date.* An investment adviser must develop and implement an anti-money laundering/countering the financing of terrorism program that complies with the requirements of this section on or before [DATE 12 MONTHS AFTER EFFECTIVE DATE OF FINAL RULE].

(d) *Duty.* The duty to establish, maintain, and enforce an anti-money laundering/countering the financing of terrorism program as required by this subpart must remain the responsibility of, and be performed by, persons in the United States who are accessible to, and subject to oversight and supervision by, FinCEN and the appropriate Federal functional regulator.

§ 1032.220 [Reserved]

Subpart C—Reports Required To Be Made by Investment Advisers

§ 1032.300 General.

Investment advisers are subject to the reporting requirements set forth and cross referenced in this subpart. Investment advisers should also refer to subpart C of part 1010 of this chapter for reporting requirements contained in that subpart that apply to investment advisers.

§ 1032.310 Reports of transactions in currency.

The reports of transactions in currency requirements for investment advisers are located in subpart C of part 1010 of this chapter and this subpart.

§ 1032.311 Filing obligations.

Refer to § 1010.311 of this chapter for reports of transactions in currency filing obligations for investment advisers.

§ 1032.312 Identification required.

Refer to § 1010.312 of this chapter for identification requirements for reports of transactions in currency filed by investment advisers.

§ 1032.313 Aggregation.

Refer to § 1010.313 of this chapter for reports of transactions in currency aggregation requirements for investment advisers.

§ 1032.314 Structured transactions.

Refer to § 1010.314 of this chapter for rules regarding structured transactions for investment advisers.

§ 1032.315 Exemptions.

Refer to § 1010.315 of this chapter for exemptions from the obligation to file reports of transactions in currency for investment advisers.

§ 1032.320 Reports by investment advisers of suspicious transactions.

(a) *General.* (1) Every investment adviser shall file with FinCEN, to the extent and in the manner required by this section, a report of any suspicious transaction relevant to a possible violation of law or regulation. An investment adviser may also file with FinCEN a report of any suspicious transaction that it believes is relevant to the possible violation of any law or regulation, but whose reporting is not required by this section. Filing a report of a suspicious transaction does not relieve an investment adviser from the responsibility of complying with any other reporting requirements imposed by the Securities and Exchange Commission.

(2) A transaction requires reporting under this section if it is conducted or attempted by, at, or through an investment adviser, it involves or aggregates funds or other assets of at least $5,000, and the investment adviser knows, suspects, or has reason to suspect that the transaction (or a pattern of transactions of which the transaction is a part):

(i) Involves funds derived from illegal activity or is intended or conducted in order to hide or disguise funds or assets derived from illegal activity (including, without limitation, the ownership, nature, source, location, or control of such funds or assets) as part of a plan to violate or evade any Federal law or regulation or to avoid any transaction reporting requirement under Federal law or regulation;

(ii) Is designed, whether through structuring or other means, to evade any requirements of this chapter or any other regulations promulgated under the Bank Secrecy Act;

(iii) Has no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage, and the investment adviser knows of no reasonable explanation for the transaction after examining the available facts, including the background and possible purpose of the transaction; or

(iv) Involves use of the investment adviser to facilitate criminal activity.

(3) More than one investment adviser may have an obligation to report the same transaction under this section, and other financial institutions may have separate obligations to report suspicious activity with respect to the same transaction pursuant to other provisions of this chapter. In those instances, no more than one report is required to be filed by the investment adviser(s) and other financial institution(s) involved in the transaction, provided that the report filed contains all relevant facts, including the name of each financial institution and the words ''joint filing'' in the narrative section, and each institution maintains a copy of the report filed, along with any supporting documentation.

(b) *Filing and notification procedures*—(1) *What to file.* A suspicious transaction shall be reported by completing a Suspicious Activity Report (''SAR'') and collecting and maintaining supporting documentation as required by paragraph (c) of this section.

(2) *Where to file.* The SAR shall be filed with FinCEN in accordance with the instructions to the SAR.

(3) *When to file.* A SAR shall be filed no later than 30 calendar days after the date of the initial detection by the reporting investment adviser of facts that may constitute a basis for filing a SAR under this section. If no suspect is identified on the date of such initial detection, an investment adviser may delay filing a SAR for an additional 30 calendar days to identify a suspect, but in no case shall reporting be delayed more than 60 calendar days after the date of such initial detection.

(4) *Mandatory notification to law enforcement.* In situations involving violations that require immediate attention, such as suspected terrorist

financing or ongoing money laundering schemes, an investment adviser shall immediately notify by telephone an appropriate law enforcement authority in addition to filing timely a SAR.

(5) *Voluntary notification to the Financial Crimes Enforcement Network or the Securities and Exchange Commission.* Investment advisers wishing to voluntarily report suspicious transactions that may relate to terrorist activity may call the Financial Crimes Enforcement Network's Financial Institutions Hotline at 1–866–556–3974 in addition to filing timely a SAR if required by this section. The investment adviser may also, but is not required to, contact the Securities and Exchange Commission to report in such situations.

(c) *Retention of records.* An investment adviser shall maintain a copy of any SAR filed by the investment adviser or on its behalf (including joint reports), and the original (or business record equivalent) of any supporting documentation concerning any SAR that it files (or that is filed on its behalf) for a period of five years from the date of filing the SAR. Supporting documentation shall be identified as such and maintained by the investment adviser, and shall be deemed to have been filed with the SAR. An investment adviser shall make all supporting documentation available to FinCEN or any Federal, State, or local law enforcement agency, or any Federal regulatory authority that examines the investment adviser for compliance with the Bank Secrecy Act, upon request.

(d) *Confidentiality of SARs.* A SAR, and any information that would reveal the existence of a SAR, are confidential and shall not be disclosed except as authorized in this paragraph (d). For purposes of this paragraph (d) only, a SAR shall include any suspicious activity report filed with FinCEN pursuant to any regulation in this chapter.

(1) *Prohibition on disclosures by investment advisers*—(i) *General rule.* No investment adviser, and no current or former director, officer, employee, or agent of any investment adviser, shall disclose a SAR or any information that would reveal the existence of a SAR. Any investment adviser, and any current or former director, officer, employee, or agent of any investment adviser that is subpoenaed or otherwise requested to disclose a SAR or any information that would reveal the existence of a SAR shall decline to produce the SAR or such information, citing this section and 31 U.S.C. 5318(g)(2)(A)(i), and shall notify FinCEN of any such request and the response thereto.

(ii) *Rules of construction.* Provided that no person involved in any reported suspicious transaction is notified that the transaction has been reported, this paragraph (d)(1) shall not be construed as prohibiting:

(A) The disclosure by an investment adviser, or any current or former director, officer, employee, or agent of an investment adviser of:

(*1*) A SAR, or any information that would reveal the existence of a SAR, to FinCEN or any Federal, State, or local law enforcement agency, or any Federal regulatory authority that examines the investment adviser for compliance with the Bank Secrecy Act; or

(*2*) The underlying facts, transactions, and documents upon which a SAR is based, including but not limited to, disclosures:

(*i*) To another financial institution, or any current or former director, officer, employee, or agent of a financial institution, for the preparation of a joint SAR; or

(*ii*) In connection with certain employment references or termination notices, to the full extent authorized in 31 U.S.C. 5318(g)(2)(B); or

(B) The sharing by an investment adviser, or any current or former director, officer, employee, or agent of the investment adviser, of a SAR, or any information that would reveal the existence of a SAR, within the investment adviser's corporate organizational structure for purposes consistent with Title II of the Bank Secrecy Act as determined by regulation or in guidance.

(2) *Prohibition on disclosures by government authorities.* A Federal, State, local, territorial, or Tribal government authority, or any current or former director, officer, employee, or agent of any of the foregoing, shall not disclose a SAR, or any information that would reveal the existence of a SAR, except as necessary to fulfill official duties consistent with Title II of the Bank Secrecy Act. For purposes of this section, ''official duties'' shall not include the disclosure of a SAR, or any information that would reveal the existence of a SAR, to a non-governmental entity in response to a request for disclosure of non-public information or a request for use in a private legal proceeding, including a request pursuant to 31 CFR 1.11.

(e) *Limitation on liability.* An investment adviser, and any current or former director, officer, employee, or agent of any investment adviser, that makes a voluntary disclosure of any possible violation of law or regulation to a government agency or makes a disclosure pursuant to this section or any other authority, including a disclosure made jointly with another institution, shall be protected from liability to any person for any such disclosure, or for failure to provide notice of such disclosure to any person identified in the disclosure, or both, to the full extent provided by 31 U.S.C. 5318(g)(3).

(f) *Compliance.* Investment advisers shall be examined by FinCEN or its delegates for compliance with this section. Failure to satisfy the requirements of this section may be a violation of the Bank Secrecy Act and of this part.

Subpart D—Records Required To Be Maintained by Investment Advisers

§ 1032.400 General.

Investment advisers are subject to the recordkeeping requirements set forth and cross referenced in this subpart. Investment advisers should also refer to subpart D of part 1010 of this chapter for recordkeeping requirements contained in that subpart which apply to investment advisers.

§ 1032.410 Recordkeeping.

For regulations regarding recordkeeping, refer to § 1010.410 of this chapter.

Subpart E—Special Information Sharing Procedures To Deter Money Laundering and Terrorist Activity

§ 1032.500 General.

Investment advisers are subject to the special information-sharing procedures to deter money laundering and terrorist activity requirements set forth and cross-referenced in this subpart. Investment advisers should also refer to subpart E of part 1010 of this chapter for special information sharing procedures to deter money laundering and terrorist activity contained in that subpart which apply to investment advisers.

§ 1032.520 Special information sharing procedures to deter money laundering and terrorist activity for investment advisers.

For regulations regarding special information sharing procedures to deter money laundering and terrorist activity for investment advisers, refer to § 1010.520 of this chapter.

§ 1032.530 [Reserved]

§ 1032.540 Voluntary information sharing among financial institutions.

For regulations regarding voluntary information sharing among financial institutions, refer to § 1010.540 of this chapter.

Subpart F—Special Standards of Diligence; and Special Measures for Investment Advisers

§ 1032.600 General.

Investment advisers are subject to the special standards of diligence; prohibitions; and special measures requirements set forth and cross referenced in this subpart. Investment advisers should also refer to subpart F of part 1010 of this chapter for special standards of diligence; prohibitions; and special measures contained in that subpart, which apply to investment advisers.

§ 1032.610 Due diligence programs for correspondent accounts for foreign financial institutions.

For regulations regarding due diligence programs for correspondent accounts for foreign financial institutions, refer to § 1010.610 of this chapter.

§ 1032.620 Due diligence programs for private banking accounts.

For regulations regarding due diligence programs for private banking accounts, refer to § 1010.620 of this chapter.

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