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FinCEN Issues Final Rule Requiring Investment Advisers to Establish Anti-Money Laundering Programs

September 20, 2024

On August 28, 2024, the US Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) **issued a final rule** that expressly includes certain investment advisers in the definition of a "financial institution" under the Bank Secrecy Act (BSA) and its implementing regulations, which collectively establish the US anti-money laundering (AML) and counter-terrorism financing (CFT) regime. The final rule incorporates a substantial portion of the requirements included in the **initial proposed rulemaking issued on February 13, 2024**, although certain key changes limit the scope of the final rule. The final rule does not encompass any rules related to the **customer identification program (CIP) proposed rulemaking** issued on May 13, 2024.

According to the fact sheet released alongside the final rule, FinCEN believes the requirements will "address the current uneven application of AML/CFT requirements across the investment adviser sector, which creates illicit finance risk and allows both legitimate and illicit investors to 'shop around' for an adviser who does not need to apply AML/CFT controls, such as inquiring into the investor's source of wealth."

Investment advisers covered by the final rule are required to comply by January 1, 2026.

Who is covered?

Consistent with the proposed rule, the final rule revises the definition of a "financial institution" under the BSA's implementing regulations to include:

- Investment advisers that are registered (RIAs) with the Securities and Exchange Commission (SEC).
- Exempt reporting advisers (ERAs) that rely on section 203(l) or section 203(m) of the Investment Advisers Act of 1940, as amended (Advisers Act).

The definition of an investment adviser under the final rule will **not** apply to the following:

- RIAs that register with the SEC solely because they are:
  - Mid-sized advisers.
  - Multistate advisers.
  - Pension consultants.
- RIAs that do not report any assets under management on their Form ADV.
- State-registered investment advisers.
- Foreign private advisers as defined in section 202(a)(30) of the Advisers Act.
- Family offices as defined in rule 202(a)(11)(G)-1 under the Advisers Act.

FinCEN also limits the scope of the final rule for investment advisers whose principal office and place of business are outside of the US. In those cases, the requirements of the final rule only apply to activities that take place within the US (including through the involvement of the investment adviser's US personnel) or provide services to a US person or a foreign-located private fund with an investor that is a US person.

Key highlights of the final rule

General AML/CFT requirements

Generally, the final rule requires covered investment advisers to implement an AML/CFT program to combat money laundering and the financing of terrorism through the institution. In the commentary to the final rule, FinCEN reiterates that it is not requiring AML/CFT programs to take a one-size-fits-all approach, but rather, such programs must be risk-based and reasonably designed to assure and monitor compliance with BSA/AML requirements. Further, the program must be approved in writing by the investment adviser's board of directors or trustees, or other persons that perform similar functions. In addition, under the final rule, investment advisers must:

- Establish AML/CFT programs that meet minimum BSA/AML requirements, including:
  - **Developing internal policies, procedures and controls**, which should be risk-based and commensurate with the risks of each adviser's services and customers.
  - **Designating a compliance officer** who is responsible for implementing and monitoring the operations and internal controls of the AML/CFT program. The compliance officer should be knowledgeable of BSA/AML requirements and have sufficient channels of communication with senior management.
  - **Establishing an ongoing employee training program**. The nature, scope and frequency of the training program should be determined by the responsibilities of the employees and the extent to which their functions would bring them in contact with BSA/AML requirements or possible money laundering activity.
  - **Implementing an independent audit function**. Independent testing must be done periodically and may be conducted by a qualified third party or employees of the investment adviser, as long as those employees are not involved in the operation and oversight of the AML/CFT program.
- Implement risk-based procedures for customer due diligence (CDD), which will be further informed by future CDD-related rulemakings. FinCEN is in the process of developing and finalizing rules imposing CIP requirements, including requirements to obtain beneficial ownership information.
- Timely submit suspicious activity reports (SARs) and currency transaction reports (CTRs) to FinCEN. FinCEN notes in the final rule that SARs should encompass certain transactions that are "conducted or attempted by, at, or through an investment adviser." FinCEN further states that it interprets this to encompass an investment adviser's advisory activities on behalf of its clients – e.g., when a customer provides an instruction for the investment adviser to relay to the custodian, or when an adviser instructs a custodian to execute transactions on behalf of its client.
- Comply with the Recordkeeping Rule, Travel Rule and any other general recordkeeping requirements under the BSA and its implementing regulations.
- Adhere 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. Under section 314(a), investment advisers will be required to search internal records for specified information on certain accounts, transactions, individuals and entities upon request from FinCEN. An investment adviser also is required to report any such identified information to FinCEN. Further, investment advisers may participate in voluntary section 314(b) information sharing arrangements, enabling them to gather information from other financial institutions that may, for example, help the investment adviser understand customer risk or file a SAR.

Differences from the proposed rule

While the final rule implements much of the proposed rule, it contains several substantive changes (as well as a few incremental ones). In addition to limiting the definition of an investment adviser, key substantive differences between the proposed and final rules include:

Applicability to mutual funds and other regulated entities – As in the proposed rule, investment advisers are not required to apply AML/CFT program requirements to the mutual funds they advise. However, in the final rule, investment advisers also are not required to verify that the mutual funds have implemented an AML/CFT program. Additionally, the final rule expands this exclusion to also apply to certain bank- and trust company-sponsored collective investment funds and any other investment adviser subject to the final rule that is advised by the investment adviser.

Implementation and oversight of AML/CFT programs by US persons – Unlike in the proposed rule, the final rule does not include language explicitly requiring that AML/CFT programs established by investment advisers be the sole responsibility of personnel in the US that are accessible to – and subject to – the oversight and supervision of FinCEN. This "duty provision" is a new statutory requirement under the BSA. FinCEN proposed to address it in its recent **proposed rulemaking on modernizing AML programs** for certain existing financial institution types, but did not address it in the final rule for investment advisers. Despite FinCEN not addressing the duty provision, the statutory obligation will still likely apply to investment advisers as financial institutions under the BSA, subject to any further interpretive guidance from FinCEN on this issue.

Examination authority delegated to the SEC

Under the final rule, FinCEN delegates its examination authority for the rule to the SEC, given the SEC's AML examination experience and expertise with investment advisers. FinCEN noted in the supplemental commentary to the final rule that it will coordinate with the SEC on whether to publish an investment adviser examination manual or other relevant resources specific to investment advisers in light of the new rule. FinCEN further noted that, for investment advisers with more than one functional federal regulator, supervisory coordination among regulators will remain important to maintain efficiencies and avoid duplication.

Next steps

With the extended effective date of the final rule, FinCEN emphasized that it expects covered investment advisers to implement and ensure that their AML/CFT programs are operating by January 1, 2026. Investment advisers should start determining whether the final rule applies and identify the actions needed to ensure they timely comply, which may range from creating an AML/CFT program to updating current policies and procedures to align with BSA/AML requirements. If you need assistance with determining your obligations under or complying with the final rule, please contact us.

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