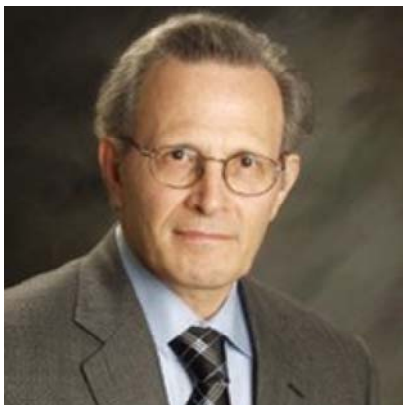


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AML Rule Proposal: Considerations for Investment Advisers

The U.S. Department of the Treasury rekindled its 2003 attempt to provide various investment advisers with an anti-money laundering (AML) regulation by issuing a notice of proposed rulemaking (NPRM) through its Financial Crimes Enforcement Network (FinCEN). In light of developments stemming from the Dodd-Frank Wall Street Reform and Consumer Protection Act related to investment adviser registration, FinCEN, which issued the NPRM in late August, chose to include only those investment advisers who are required to register with the Securities and Exchange Commission. Most of these advisers have over \$100 million in assets and already may have voluntary AML programs that now should be tuned to the proposed rules.

The proposed rule is similar in many ways to the [AML rules](#) for other financial institutions, but there are some issues that investment advisers and their counterparties should carefully consider with respect to making rule comments to FinCEN and planning future AML related operations.



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For example, although not part of the proposed rule text, FinCEN's comments in the NPRM specify that the required AML compliance officer (one or more people) should be AML knowledgeable and authorized to enforce AML policies and procedures that address the investment adviser's money-laundering risks. The recent emphasis on personal accountability of compliance officers seems paired with a push to give these officers corresponding power, and that may affect their relationship with the business. FinCEN has

used similar commentary in the past, such as for proposed AML rules regarding housing government sponsored entities.

In addition, while the proposed rule does not explicitly incorporate pending customer due diligence requirements applicable to other types of financial institutions, FinCEN requires a risk based approach. As a result, a covered investment adviser will need to tailor the customer information it collects according to the extent and nature of the risk of its business model. For investment advisers with complex business models, this could be a challenging process. The NPRM provides some illustrative examples of FinCEN's expectations for several kinds of investment advisers, however the examples are not formulaic. FinCEN also indicates that further due diligence clarification may be the subject of subsequent rules.

The proposed rule also requires "immediate" telephone notification to an "appropriate" law enforcement authority of "violations that require immediate attention." But, the definition of these terms is lacking in the rule. Further, the rule appears to be a mandatory version of existing advisory guidance and practice that encourages financial institutions not to wait until a suspicious activity report is filed to call law enforcement when a potential issue is important. This provision underscores the need to cultivate, on an anticipatory basis, law enforcement relationships. It is also novel for the investment adviser industry in that the obligation is framed in terms of "violations" rather than mere suspicious activity, the common standard for reporting obligations in the sector.

FinCEN's commentary section of the NPRM anticipates that investment advisers may delegate some of their AML program activities to outside parties, though they must still have their own compliance officer(s). This section suggests a new emphasis around the delegation relationships to ensure that reliance on others is reasonable, tested and documented. Since many advisers may rely on the same few vendors or financial institutions, such as transfer agents, the paperwork and scrutiny may pose operational issues that differ from the current informal arrangements regarding present voluntary AML programs.

Further, the proposed rule, as explained by the comments section, anticipates investment advisers sharing some AML activities, like reporting suspicious activity, with other institutions, particularly broker dealers. How integration of information across different entities is managed in light of confidentiality and other concerns remains to be worked out, although this should not be an insuperable task.

The industry has waited a long time for the proposal, and investment advisers are seen in the rule comments to have greater visibility into some risk aspects than other financial institutions that process their transactions. The proposed rule, as refined through the

upcoming comment process, should provide useful additional safeguards against financial crime.

—Produced by Robert M. Axelrod, an Advisory director, Deloitte Transactions and Business Analytics LLP, Deloitte Financial Advisory Services LLP.

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