TRANSPARENCY INTERNATIONAL U.S.
fighting corruption, promoting democracy

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July 22, 2024

Ms. Andrea Gacki
Director
Financial Crimes Enforcement Network
U.S. Department of the Treasury
P.O. Box 39
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Mr. Gary Gensler
Chairperson
U.S. Securities and Exchange Commission
100 F St. NE
Washington, DC 20549

Re: Customer Identification Programs for Registered Investment Advisers and Exempt Reporting Advisers, File No. S7-2024-02, RIN 3235-AN34

Dear Director Gacki and Chairperson Gensler,

Transparency International U.S. ("TI US")[1] appreciates the opportunity to provide comments on the Notice of Proposed Rulemaking ("NPRM" and "Draft Rule") on customer identification program ("CIP") obligations for registered investment advisers and exempt reporting advisers, published jointly by the Financial Crimes Enforcement Network ("FinCEN") of the U.S. Department of the Treasury ("Treasury") and the U.S. Securities and Exchange Commission ("SEC").[2] We offer these comments to commend key aspects of the Draft Rule and to recommend important considerations to ensure the adoption of a final rule that is comprehensive, effective, and practicable. As FinCEN and the SEC work to develop that final rule, please consider us partners in the effort.

Across the world, TI chapters are actively involved in efforts to establish comprehensive, robust, and accountable anti-money laundering ("AML") rules as a means of curbing corruption, increasing government accountability and financial transparency, and building public confidence

[1] TI US is part of the largest global coalition dedicated to fighting corruption. With over 100 national chapters around the world, Transparency International ("TI") partners with businesses, governments, and citizens to promote transparency and curb the abuse of power in the public and private sectors. For more information about TI US, please see our website at https://us.transparency.org/.
[2] *See* U.S. Department of the Treasury & Securities and Exchange Commission, "Customer Identification Programs for Registered Investment Advisers and Exempt Reporting Advisers," May 21, 2024, available at https://www.sec.gov/rules-regulations/2024/05/s7-2024-02.

in the integrity of financial and political systems.[3] Corruption and the laundering of funds acquired through corruption pose unique, multidimensional threats to societies and financial systems across the globe: They erode the rule of law, threaten our global financial integrity, and destabilize economies, among many other associated threats,[4] the power, scale, and severity of which, accordingly, are reflected in the U.S. National Security Council's June 2021 designation of the fight against corruption as a core U.S. national security interest.[5]

Yet just as these threats engender globally resonant problems, strong efforts to address them, including the adoption of comprehensive and effective CIPs for investment advisers ("IAs"), can produce correspondingly positive global impacts.

Background on U.S. Private Investment Vehicles and Corruption

As the world's largest economy and largest IA sector[6] by number of registered IAs, assets under management, and total value of related asset flows, the United States has a unique opportunity

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[3] *See* TI, "Dirty Money," available at https://www.transparency.org/en/our-priorities/dirty-money.

[4] *See generally* Treasury, "2024 Investment Adviser Risk Assessment,", February 2024, available at https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.pdf ("Treasury 2024 Investment Adviser Risk Assessment"); U.S. Department of State, "International Narcotics Control Strategy Report: Volume II Money Laundering", March 2022, available at https://www.state.gov/wp-content/uploads/2022/03/22-00768-INCSR-2022-Vol-2.pdf.

[5] *See* The White House, "Memorandum on Establishing the Fight Against Corruption as a Core United States National Security Interest," June 3, 2021, available at https://www.whitehouse.gov/briefing-room/presidential-actions/2021/06/03/memorandum-on-establishing-the-fight-against-corruption-as-a-core-united-states-national-security-interest.

[6] *See* Investment Adviser Association & National Regulatory Services, "Investment Adviser Industry Snapshot 2023," 2023, 37 (accounting for 37.9 percent of the global investment industry; assets under management ("AUM") self-reported industry statistics for the U.S. (15,114 fiduciary investment advisers managing $114.1 trillion in assets for 61.9 million clients)), available at https://investmentadviser.org/wp-content/uploads/2023/06/Snapshot2023_Final.pdf ("Industry Snapshot 2023"). Compare with industry statistics for the world's next largest economies and countries that have the highest number of RIAs not domiciled in the U.S. *See generally* U.S. Library of Congress, "China: Government Issues First Regulation on Private Investment Funds," Aug. 7, 2023, available at https://www.loc.gov/item/global-legal-monitor/2023-08-06/china-government-issues-first-regulation-on-private-investment-funds; (People's Republic of China ("PRC"): as of May 2023, assets under private fund management are 21 trillion yuan (approximately $2.938 trillion), as reported by Asset Management Association of China); Japan Investment Advisers Association, "Statistical Releases," available at https://www.jiaa.or.jp/toukei_e/index.html (Japan: as of Dec. 2023, total AUM are 592.5 trillion yen (approximately $3.9 trillion)); Bundesanstalt Fur Finanzdienstleistungsaufsicht, "Annual Report 2022", 2023, available at https://www.bafin.de/SharedDocs/Downloads/EN/Jahresbericht/dl_jb_2022_en.html (Germany: as of Dec. 2022, AUM are approximately US$2.7 trillion); The Investment Association, "Investment Management Survey 2022-23," 2023, available at https://www.theia.org/sites/default/files/2023-

through this and related rulemakings to prevent corrupt officials, terrorists, and other criminals from further poisoning and destabilizing the U.S. and global financial systems. As recognized by Treasury, and as made clear in consistent criticisms by the Financial Action Task Force ("FATF")[7]—the international AML standards-setting body that the U.S. co-founded, and that for years has criticized the United States over significant gaps in its AML regimes—the inadequacy of the current U.S. AML framework permits our country to serve as a safe-haven destination for dirty money, contributing to a global wealth drain that not only leaves nations across the world struggling to pay for critical government services, and rationing access to medicine, clean water, electricity, and more,[8] but that jeopardizes our own national security and public safety.[9]

These consequences and others are familiar to FinCEN, Treasury, and other U.S. agencies. In June 2021, for example, Treasury named combating corruption a government-wide priority for AML.[10] Since then, and in particular since the February 24, 2022, invasion of Ukraine by Russia, a canvassing of FinCEN advisories, relevant Treasury communications (including National Risk Assessments), information from federal law enforcement and other U.S. agencies,[11] as well as

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10/Investment%20Management%20in%20the%20UK%202022-2023%20-%20Chapter%201.pdf (United Kingdom: as of Dec. 2022, AUM are 8.8 trillion pounds sterling (approximately $11.1 trillion)); and Monetary Authority of Singapore, "Singapore Asset Management Survey 2022: Singapore—A Leading Asset Management Centre in Asia Pacific," 2023, available at https://www.mas.gov.sg/-/media/mas/news-and-publications/surveys/asset-management/asset-management-survey-report-2022_version-finalised.pdf (Singapore: as of Dec. 2022, AUM are 4.9 trillion Singapore dollars (approximately $3.65 trillion)).

[7] *See, e.g.*, FATF & Asia/Pacific Group on Money Laundering, "Anti-Money Laundering and Counter-Terrorist Financing Measures, United States, Mutual Evaluation Report," 2016, available at https://www.fatf-gafi.org/content/dam/fatf-gafi/mer/MER-United-States-2016.pdf.coredownload.inline.pdf (e.g., Executive Summary Table E).

[8] *See* International Monetary Fund, "2023 Review of the Fund's Anti-Money Laundering and Combating the Financing of Terrorism Strategy," 2023, available at https://www.imf.org/en/Publications/Policy-Papers/Issues/2023/12/05/2023-Review-of-The-Funds-Anti-Money-Laundering-and-Combating-The-Financing-of-Terrorism-542015 (describing the macroeconomic impact of money laundering and terrorism financing).

[9] *See* Treasury, "2024 Investment Adviser Risk Assessment," February 1, 2024, available at https://home.treasury.gov/system/files/136/US-Sectoral-Illicit-Finance-Risk-Assessment-Investment-Advisers.pdf.

[10] FinCEN, "Anti-Money Laundering and Countering the Financing of Terrorism National Priorities," 2021, available at https://www.fincen.gov/sites/default/files/shared/AML_CFT%20Priorities%20(June%2030%2C%202021).pdf.

[11] *See, e.g.,* FinCEN, "Statement of FinCEN Director Andrea Gacki before the House Committee on Financial Services," Feb. 14, 2024, available at https://www.fincen.gov/news/testimony/statement-fincen-director-andrea-gacki-house-committee-financial-services; *see also* Treasury, "NDAA: Russia Illicit Finance Report," 2023, available at https://home.treasury.gov/system/files/136/Treasury-NDAA-Ru-IFR-508.pdf; Treasury, "National Strategy for Combating Terrorist and Other Illicit Financing 2022," 2022, available at https://home.treasury.gov/system/files/136/2022-National-Strategy-for-Combating-Terrorist-and-Other-Illicit-Financing.pdf; FinCEN, "Financial Crimes

media and similar reports,[12] have highlighted the severity of current and prospective threats to the integrity and resilience of financial systems by, at, or through IAs.

This threat is global, and only accelerating. For example, in January of this year, one of the most prominent Chinese private equity and venture capital firms operating in the U.S. was placed on the annual "Chinese Military Company" list.[13] This is the first time such a prominent investment

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Enforcement Network, Agencies Issue Statement on Bank Secrecy Act Due Diligence Requirements for Customers Who May Be Considered Politically Exposed Persons," Aug. 21, 2020, available at https://www.fincen.gov/news/news-releases/agencies-issue-statement-bank-secrecy-act-due-diligence-requirements-customers.

[12] *See, e.g.*, Forbes, "30 Under 30: Masha Drokova," available at https://www.forbes.com/profile/masha-drokova/?sh=3b390e4a11b8 (Day One Ventures, a Silicon Valley-based entity that invests in startups which, at the time of its founding, listed Russian oligarchs Alexander Mamut and Vladimir Yevtushenkov as investors); Marina Temkin, "Anti-Russia sanctions spur VCs to unravel ties to 'toxic' money," Pitchbook, Apr. 12, 2022, available at https://pitchbook.com/news/articles/russian-vc-firms-sanctions-almaz-alexander-galitsky (detailing Silicon Valley-based investor Alexander Galitsky's ties with Russia; Galitsky is founder of Almaz Capital which invests in software technologies and contributed to the launch of Russian Quantum Center; Galitsky is a former board member of Alfa-Bank, a U.S.-designated Russian bank); Joseph Menn, "Scrutiny mounts over tech investments from Kremlin-connected expatriates," The Washington Post, Dec. 19, 2022, available at https://www.washingtonpost.com/technology/2022/12/19/russia-expatriates-links-probed (highlighting Almaz Capital's investments in software technologies that raise national security concerns and Almaz Capitals' founders' connections with the launch of the Russian Quantum Center); Robert McMillan, Dustin Volz, and Aruna Viswanatha, "China is Stealing AI Secrets to Turbocharge Spying, U.S. Says," The Wall Street Journal, Dec. 25, 2023, available at https://www.wsj.com/tech/ai/china-is-stealing-ai-secrets-to-turbocharge-spying-u-s-says-00413594. Data rooms run by RIAs and ERAs are another entry point for access to sensitive technologies. For an example of how China presents itself to investors, *see* China Briefing, "China's Biopharma Industry: Market Prospects, Investment Paths," Nov. 10, 2022, available at https://www.china-briefing.com/news/china-booming-biopharmaceuticals-market-innovation-investment-opportunities/. *See also* TI US, Financial Accountability and Corporate Transparency ("FACT") Coalition, and Global Financial Integrity, "Private Investments, Public Harm: How the Opacity of the Massive U.S. Private Investment Industry Fuels Corruption and Threatens National Security," Nov. 2021, available at https://us.transparency.org/resource/private-investments-public-harm-report.

[13] U.S. Department of Defense, "DOD Releases List of People's Republic of China (PRC) Military Companies in Accordance with Section 1260H of the National Defense Authorization Act for Fiscal Year 2021," Jan. 31, 2024, available at https://www.defense.gov/News/Releases/Release/Article/3661985/dod-releases-list-of-peoples-republic-of-china-prc-military-companies-in-accord.

company has been placed on the list for funding Chinese military development,[14] and can trigger designation by Treasury.[15]

Background on the Statutory Framework and Related Rulemakings

The Bank Secrecy Act ("BSA"), in requiring financial institutions to establish and maintain systems to monitor transactions, maintain records, and report suspicious transactions, remains the U.S. Government's most important tool for fighting money laundering and other illicit financial activity in the United States.[16]

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[14] Echo Wong, "China private investment firms face growing U.S. scrutiny, analysts say," Nikkei Asia, Feb. 9, 2024, available at https://asia.nikkei.com/Politics/International-relations/US-China-tensions/China-private-investment-firms-face-growing-U.S.-scrutiny-analysts-say.

[15] Note that, unlike American companies, Chinese-owned companies are required by their government to support the military through their Military-Civil Fusion ("MCF") policy. MCF is the elimination of barriers between the civilian research and commercial sectors and the military and defense industrial sectors, with the goal of developing the People's Liberation Army ("PLA") into a "world-class military" by 2049. *See* U.S. Department of State, "Military-Civil Fusion and the People's Republic of China," available at https://www.state.gov/wp-content/uploads/2020/05/What-is-MCF-One-Pager.pdf.

[16] *See* Pub. L. No. 91-508, 84 Stat. 1114 (1970). The BSA was a reaction, in large part, to stringent provisions in foreign jurisdictions that assured the secrecy of financial transactions. 116 Cong. Rec. 16, 950 (bounded.), May 25, 1970, Amended and passed House, Debated, H. Res. 941 agreed to ("In jurisdictions with secrecy laws our law enforcement agencies are placed in an impossible position. To have any hope of gaining the desired information, officials must subject themselves to long, drawn-out foreign legal processes. Oftentimes the 'evidence' has disappeared. To overcome this problem, and still not unduly interfere with the rights, laws, and sovereignty of foreign nations and their institutions, the bill is directed toward Americans and those doing business in the United States, and the Treasury Department is giving wide administrative flexibility to assure the uninterrupted flow of world commerce and trade. The aim is to place such persons in the same position with regard to his secret foreign transactions as he would be with respect to his domestic transactions."). Congress justified the BSA's provisions, in part, on the fact that such record keeping was already practiced, in private, by most financial institutions and that the BSA would therefore "impose almost no additional expense upon those affected." *Id.* at 16, 961. The BSA was also justified on the need for financial institutions to bear some of the burden of the costs of fighting crime which, at the time, was increasingly falling on taxpayers. *Id.* ("Even if there is some additional cost to the financial institutions of this country, even if there will be some burden, even if these institutions do have to do a little more in terms of recordkeeping than they have done, should not they as well as the rest of us bear some of the costs of fighting crime. In these days when all levels and types of crime are mushrooming beyond manageable proportions, the taxpayer is being called upon to pay more and more money for law enforcement. Surely the banks and other corporations who will be required to keep some additional records or maintain the records they already keep cannot complain too loudly about taking on a small portion of this burden. Perhaps the virtue of title I of this legislation is that it is designed to create the climate for more efficient law enforcement. It could serve as a very helpful crime preventive so that the benefits to be gained are far out of proportion to the burden taken.").

"[I]nvestment companies" have long been covered by the BSA,[17] but no subsequent rule(s) has spelled out exactly *how* to apply the law to these financial institutions, despite the many, and often opaque, layers through which illicit funds travel by, at, or through U.S.-linked IAs within the U.S. financial system. Fortunately, on February 15, 2024, FinCEN published a draft rule to combat money laundering, including the laundering of the proceeds of corruption, through the IA sector (the "February draft rule" or "February NPRM").[18] The February draft rule details the types of IAs covered by the proposal and many of the associated AML requirements for those IAs. As Director Gacki stated at the time:

> The current patchwork of AML/[countering the financing of terrorism, or "CFT"] requirements create regulatory gaps that criminals and foreign adversaries exploit to launder money, hide illicit wealth, and compromise American innovation...This Draft Rule would level the regulatory playing field, protect U.S. economic and national security, and safeguard American businesses.[19]

Under the February draft rule, Covered Investment Advisers ("CRAs") would be required to (1) establish AML/CFT programs; (2) file Currency Transaction Reports ("CTRs") and Suspicious Activity Reports ("SARs"); (3) maintain records of originator and beneficiary information for certain transactions; (4) share information with FinCEN and other law enforcement agencies (and authorize sharing with certain financial institutions); and (5) implement special due diligence requirements for private banking and correspondent bank accounts involving foreign persons and special measures under the USA PATRIOT Act[20] and the Combatting Russian Money Laundering Act.[21]

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[17] *See* 31 USC 5312(a)(2)(I).

[18] *See* FinCEN, "Anti-Money Laundering/Countering the Financing of Terrorism Program and Suspicious Activity Report Filing Requirements for Registered Investment Advisers and Exempt Reporting Advisers, Notice of Proposed Rulemaking," 89 FR 12108, Feb. 15, 2024, available at https://www.federalregister.gov/documents/2024/02/15/2024-02854/financial-crimes-enforcement-network-anti-money-launderingcountering-the-financing-of-terrorism.

[19] FinCEN, "FinCEN Proposes Rule to Combat Illicit Finance and National Security Threats in Investment Adviser Sector," Feb. 13, 2024, available at https://www.fincen.gov/news/news-releases/fincen-proposes-rule-combat-illicit-finance-and-national-security-threats.

[20] *See* February draft rule at 12135; Pub. L. No. 107–56, § 312 (2001); *see also* Pub. L. No. 107–56, § 326 (2001) (Section 326 of the USA PATRIOT Act added subsection (l) to 31 U.S.C. 5318 (the BSA) that requires the Secretary of the Treasury to prescribe regulations setting forth minimum standards for financial institutions that relate to the identification and verification of any person who applies to open an account (i.e., implementation of a CIP)).

[21] *See* FinCEN, "FinCEN Identifies Virtual Currency Exchange Bitzlato as a 'Primary Money Laundering Concern' in Connection with Russian Illicit Finance," Jan. 18, 2023, available at https://www.fincen.gov/news/news-releases/fincen-identifies-virtual-currency-exchange-bitzlato-primary-money-laundering (discussed in attached Frequently Asked Questions document); *see also* Pub. L. No. 116–283, § 9714 (also known as the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021), the first and only use of § 9714 to date.

The February draft rule goes a long way toward responding to the recommendations that have been provided by our office and other civil society organizations.[22] It enhances transparency in the IA sector through its requirements to implement ongoing CDD, file SARs with FinCEN, collect and retain certain information in connection with fund transfers, and ensure that certain information which passes by, at, or through IAs and pertains to the transmittal of funds "travel" with the transmittal to the next financial institution in the chain.

The February draft rule did not, however, propose requiring covered IAs to collect or verify basic information about the beneficial owners of their legal entity clients. As FinCEN wrote at the time:

> In light of [the] 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.[23]

In our comment on the February draft rule, we strongly encouraged FinCEN to include such requirements, not only to be consistent with FinCEN's own recently proposed rule to combat money laundering through the U.S. residential real estate sector,[24] but to comprehensively and effectively address the risks posed to the U.S. and global financial systems by the lack of such requirements, as well as to bring the United States into compliance with relevant FATF standards.[25]

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[22] *See* "Letter from TI US et al., to Hon. Janet Yellen, Secretary, U.S. Dep't of Treasury and Hon. Gary Gensler, Chair, U.S. Sec. and Exch. Comm'n," Apr. 27, 2022, available at https://us.transparency.org/resource/civil-society-letter-urging-the-administration-to-pass-new-anti-corruption-rules-covering-investment-advisers (signed by 17 civil society organizations, the letter urges Treasury to adopt an AML/CFT requirement for investment advisers that includes ongoing customer due diligence ("CDD") and SARs; the letter states Treasury should immediately promulgate a rule "to require investments advisers and unregistered investment companies to implement robust AML programs with beneficial ownership identification, risk evaluations for investors, suspicious activity reporting to the Financial Crimes Enforcement Network, and ongoing monitoring of accounts…And the SEC should revise Form PF to require investment advisers to conduct risk-based customer due diligence, report beneficial ownership information (including information about any 'politically exposed person' or 'senior foreign political figure'), and disclose the country of origin of each investor, the source of their funds, and an approximate value of the funds invested").

[23] *See* February draft rule at 12129 (emphasis added).

[24] FinCEN, "Anti-Money Laundering Regulations for Residential Real Estate Transfers," 89 Fed. Reg. 12424, Feb. 16, 2024, available at https://www.federalregister.gov/documents/2024/02/16/2024-02565/anti-money-laundering-regulations-for-residential-real-estate-transfers.

[25] *See* February draft rule at 12150 ("If the [Draft Rule] is finalized, it will assist the U.S. in avoiding these consequences and strengthening compliance with the FATF standards.").

We echo those comments here, and again strongly urge the inclusion of these essential requirements in the final AML/CFT regime for IAs.

Overview of the Draft Rule

The money laundering, terrorism financing, and international corruption financing risks posed by the IA sector make crystal clear that a robust iteration of existing, best-practice AML/CFT rules, including comprehensive and effective CIPs, is both justified and necessary to ensure the integrity of the IA sector. As stated in the Draft Rule:

> Money laundering also provides the appearance of legitimacy to proceeds of international corruption. By requiring that investment advisers verify the identity of their customers, the proposed rule would make it more difficult for money launderers to use investment advisers as an entry point into the U.S. financial system, reducing money launderers' ability to launder the proceeds of these criminal enterprises and thereby decreasing incentives to engage in these crimes.[26]

In short, the Draft Rule would require both RIAs and ERAs to establish, document, and maintain written CIPs that are appropriate for their respective sizes and businesses.[27] This CIP would include procedures that are risk-based in verifying the identity of each customer to the extent reasonable and practicable within a reasonable time before or after the customer's account is opened.[28] And those procedures would have to enable the covered IAs to form, and continue to have a reasonable belief, that they know the true identity of each customer.[29]

In particular, covered IAs would be required to obtain certain identifying information with respect to each customer, such as the customer's name, date of birth or date of formation, address, and identification number.[30] The Draft Rule would also include procedures for, among other things, maintaining records of the information used to verify a customer's identity and notifying customers that the IA is requesting information to verify their identities.[31]

Specific Aspects of the Draft Rule

Identification and Verification

As stated in the NPRM:

> This proposed rule is generally consistent with existing rules requiring other financial institutions, such as brokers or dealers in securities, open-end investment companies (such as mutual funds), credit unions, banks, and other financial institutions, to adopt and implement CIPs.[32]

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[26] Draft Rule at 44581.
[27] *See id.* at 44574.
[28] *See id.* at 44575.
[29] *See id.* at 44576.
[30] *See id.* at 44575.
[31] *See id.* at 44578.
[32] *See id.* at 44573.

We agree with this assessment and commend FinCEN and the SEC for prosing industry-standard, best-practice elements of comprehensive and effective AML/CFT regimes via this rulemaking. Many other similarly situated countries have implemented similar CIP requirements for IAs[33] and we urge FinCEN and the SEC to maintain these elements in its final rule.

In distilling the risk-based procedures for determining and verifying the identity of each customer to the extent reasonable and practicable, the Draft Rule states that for legal entity customers, relevant identifying information would be the name, address, date of formation, and identification number (such as an employer identification number or "EIN") for the entity, and that "suitable documents would include documents showing the existence of the entity, such as certified article of incorporation, a government-issued business license, a partnership agreement, or a trust instrument."[34] The Draft Rule goes on to state that "The CIP must address situations where," based on an IA's risk assessment, the IA "will obtain information about individuals with authority or control over such account in order to verify the customer's identity" when the IA is not able to verify the true identity of a customer using typical verification methods.[35]

We would be remiss to not use this juncture to draw attention to the central need for the final AML/CFT regime for IAs, however accomplished, to also include the express requirement that covered IAs collect and verify beneficial ownership information ("BOI") for such legal entity clients. Only by doing so will the resulting regime be consistent with relevant requirements in similarly situated countries.[36]

As far back as 2020, Treasury highlighted that for IAs:

> [T]he systemic mismatch between AML obligations and the information available to those holding these obligations creates a real risk for the U.S. financial system. For instance, qualified custodians and prime brokers have AML obligations but do not know the source of wealth and identity for clients of an investment adviser they serve.[37]

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[33] Both BOI and source of funds are legally required to be collected for covered IAs in many countries, including, among others, Argentina, Barbados, Brazil, Canada, France, India, Ireland, Japan, Singapore, Switzerland, Thailand, and the United Kingdom, while New Zealand requires the collection of source of funds information.

[34] *See* Draft Rule at 44576.

[35] *See id.* at 44577.

[36] Among others, the AML legislation in Japan, Singapore, Ireland, India, Hong Kong, and Switzerland covers IAs within financial institutions or financial advisory services language. Note that proposed legislation enhances current AML/CFT frameworks for IAs in many of the top ten jurisdictions with the highest number of RIAs domiciled outside the U.S. These are the United Kingdom, Canada, Hong Kong, Switzerland, Singapore, Australia, Japan, the PRC, Ireland, and India. Of these top ten countries where RIAs are domiciled, only three (Hong Kong as a Special Administrative Region of the PRC, Switzerland, and the PRC) show a decrease in the number of RIAs from 2019 to 2022. The global trend is, therefore, increasing the dominance of the U.S. in the global IA sector.

[37] Treasury, "NDAA: Russia Illicit Finance Report," 2023, 6, available at https://home.treasury.gov/system/files/136/Treasury-NDAA-Ru-IFR-508.pdf.

Examples of the need for BOI collection and verification abound. For example, consider Treasury's specific delineation of obfuscating ties with Russia and the leadership of investment firms as one method by which investors continue to access investments in U.S. technology through venture capital funds.[38] Other examples include Russian oligarch Roman Abramovich's use of a sweeping network of anonymous companies in the U.S. private investment industry to move billions of dollars between major American hedge funds and private equity firms[39] to, in a global context, Singapore's current crisis dealing with illicit inflows tied to an exponential increase in family offices used as shell companies to hide assets.[40]

Accordingly, FinCEN and the SEC's final regulatory regime for covered IAs must include an explicit requirement that these IAs collect and verify BOI for their legal entity clients.

Pooled Investment Vehicles

Pooled investment vehicles ("PIVs") and other private funds are currently exempt from the standard reporting requirements of the Corporate Transparency Act ("CTA"),[41] as well as from the CDD rule. Those exemptions make it all the more critical for the U.S. Government, be it through the final version of the February draft rule, the final version of the Draft Rule, or a subsequent rulemaking, to ultimately include customized beneficial ownership rules for IAs that take into account the peculiar structures of PIVs. PIVs are often very different from corporations and limited liability companies ("LLCs") created on the state level: While most corporations and LLCs covered by the CTA, for instance, have fewer than four beneficial owners, many PIVs may be structured as limited partnerships in which *no* beneficial owner holds an ownership stake of more than a few percentage points. CTA and CDD beneficial ownership rules currently limit disclosure to beneficial owners holding at least a 25 percent ownership stake in, or that exercise substantial control over, an entity, and such an approach simply may not work for PIVs.

Exemption Mechanism

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[38] *See* Treasury, 2024 Investment Adviser Risk Assessment at 22. For an example of obfuscating ties with Russia, *see* Joseph Menn, Elizabeth Dwoskin, Douglas MacMillan, and Cat Zakrzewski, "From Russia with money: Silicon Valley distances itself from oligarchs," The Washington Post, Apr. 1, 2022, available at https://www.washingtonpost.com/technology/2022/03/26/silicon-valley-russia-oligarchs (founder and general partner subsequently denied any ties with Russia and issued a public statement condemning Putin's regime).

[39] Matthew Goldstein & David Enrich, "How One Oligarch Used Shell Companies and Wall Street Ties to Invest in the U.S.," The New York Times, Mar. 21, 2022, available at https://www.nytimes.com/2022/03/21/business/russia-roman-abramovich-concord.html.

[40] *See* Toh Ee Ming, "Singapore's clean image under scrutiny amid money laundering scandal," Al Jazeera, Sept. 18, 2023, available at https://www.aljazeera.com/economy/2023/9/18/singapores-clean-image-under-scrutiny-amid-money-laundering-scandal (noting that single-family offices increased from 700 in 2021 to 1,100 in 2022); *see also* Anshuman Daga, "Singapore steps up scrutiny of shell firms to combat money laundering," Reuters, Aug. 12, 2019, available at https://www.reuters.com/article/us-singapore-cenbank/singapore-steps-up-scrutiny-of-shell-firms-to-combat-money-laundering-idUSKCN1V2231.

[41] Corporate Transparency Act, Title LXIV of the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, Pub. L. No. 116-283 (2021).

Proposed §1032.220(b) of the Draft Rule provides that the SEC, with the concurrence of the Secretary of the Treasury, may exempt any covered IA, or any type of account, from the relevant CIP requirements as long as the Secretary and the SEC consider, in doing so, "whether the exemption is consistent with the purposes of the BSA and in the public interest."[42]

While such a broad exemption authority can be important to a functional final rule, we encourage FinCEN and the SEC to narrow this discretion by requiring the SEC and Secretary to consider whether the exemption is also consistent with the purposes of the BSA's accompanying regulations. If an argument cannot be made that a covered IA falls outside the ambit of the purposes of the BSA and its implementing regulations, FinCEN and the SEC should not exempt it from coverage through this exemption mechanism.

Bigger picture, though, we strongly encourage FinCEN and the SEC, in both designing and exercising any exemption mechanism, to consider potential unintended consequences of specific exemptions. In particular, we note an experience in the United Kingdom that can be instructive: When the United Kingdom adopted a beneficial ownership transparency requirement for companies, the law did not initially cover Scottish Limited Partnerships ("SLPs"). Following implementation of the law, the number of registered SLPs increased by over 23,000 (some 430 percent) between 2007 and 2016.[43] The United Kingdom government has since closed this loophole in order to address concerns that SLPs were being used to evade the law. To this end, FinCEN and the SEC must not design or permit an exemption mechanism that could similarly be exploited to evade the resulting regime.

Compliance

We agree that the six-month compliance period as of the final rule's effective date is reasonable and necessary for covered IAs to implement CIP requirements effectively. Covered IAs should also be permitted to delegate certain aspects of the implementation and operation of their CIPs to third parties. This reflects the reality that a covered IA's operations (including a range of compliance-related activities) may be conducted by agents or third-party service providers, such as broker-dealers in securities (including prime brokers), custodians, transfer agents, and fund administrators. This being said, we strongly urge FinCEN and the SEC to make covered IAs ultimately accountable for CIP compliance.

Furthermore, competing compliance measures, especially for RIAs and ERAs domiciled outside the U.S., are legitimate concerns, especially as the U.S. has expanded its application of the AML/CFT regulatory framework to foreign financial institutions. National security and due diligence regulatory frameworks in other countries could impede compliance by covered IAs with CIP requirements. In the interests of transparency and effective compliance, however, FinCEN and the SEC should state more clearly which metrics it will use in oversight, examination, and inspection under the final rule. Good instructions may help mitigate any potential de-risking that could accompany the imposition of CIP requirements on covered IAs, among other concerns, and we appreciate FinCEN and the

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[42] *See* Draft Rule at 44597.

[43] *See* STV News, "Scot firms with business model tied to $1bn fraud probed," Jan. 11, 2018, available at https://archive.news.stv.tv/politics/1406010-scots-firms-with-business-model-tied-to-1bn-fraud-probed.html.

SEC's sensitivity to this issue and the potential impact on communities made more vulnerable by the corrosive effects of corruption, money laundering, and terrorism financing.

Cost/Benefit Analysis

We find FinCEN and the SEC's accompanying costs and benefits analysis to be thorough, and its assumptions easy to follow. While we commend this approach, we nevertheless encourage FinCEN and the SEC to include more-quantifiable *benefits* that will accrue from the increased costs. The final rule's analysis should make greater effort to show clearly that initial and ongoing compliance burdens will have a lasting benefit for covered IAs and the durable resilience and health of the U.S. financial system. Otherwise, the absence of a method of quantifying these benefits makes the cost/benefit balance much more subjective. This element of subjectivity opens the Draft Rule to potential criticism.

To this end, we encourage FinCEN and the SEC to develop a solid example of quantifiable benefit(s) and to include a graph that visualizes breakeven analysis, framing this, perhaps, as follows:

> We estimate that $X and $Y is laundered through IRAs and ERAs, respectively, every year. If, as we believe, this rule, as a result of the adoption of CIPs by such IAs, prevents even Y% of those funds from being laundered, this would result in a benefit of $Z, which, when projected over the next 10 years, recoups the money invested by [year XXXX].

Such an analysis would help address criticisms regarding whether the CIP benefits realistically outweigh the costs. We encourage FinCEN and the SEC to consider this and other kinds of analyses that bolster the efficiency and long-term benefits arguments.

Conclusion

The Biden Administration has stated that the fight against corruption is "essential to the preservation of our democracy" and allows the United States to secure a "critical advantage" for itself and other democracies.[44] Through this Draft Rule, FinCEN and the SEC have taken a significant additional step toward comprehensive and effective rules that can meet the seriousness and urgency of these threats. Altogether, this Draft Rule, if combined with (1) a finalized version of the February draft rule that is responsive to our associated comment, (2) a revised CDD rule that expressly obligates covered IAs to collect and verify BOI, and (3) fully implemented U.S. Government efforts under the CTA to provide BOI to law enforcement, regulators, and financial institutions charged with AML/CFT responsibilities, will help protect the U.S. and global financial systems and ameliorate the consequences of corruption across the world.

We sincerely hope that FinCEN and the SEC seize the opportunity before them to finalize a rule that honors and reflects the Administration's designation of the fight against foreign corruption as a national security priority.

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[44] The White House, "Statement by President Joseph R. Biden, Jr. on the National Security Study Memorandum on the Fight Against Corruption," June 3, 2021, available at https://www.whitehouse.gov/briefing-room/statements-releases/2021/06/03/statement-by-president-joseph-r-biden-jr-on-the-national-security-study-memorandum-on-the-fight-against-corruption.

If you have any questions, or for additional information on TI US's work in this regard, please contact Scott Greytak, Director of Advocacy for TI US, at sgreytak@transparency.org.

Thank you for the opportunity to present these comments.

Respectfully submitted,

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