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# Implementing AML Program Requirements for Investment Advisers

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# Implementing AML Program Requirements for Investment Advisers

Covered investment advisers, including small to mid-sized advisers, are still parsing the implications of the groundbreaking Notice of Proposed Rulemaking (NPRM) issued by the Financial Crimes Enforcement Network (FinCEN) on 13 February 2024 to combat illicit finance and national security threats in the investment adviser sector. The proposed rule would subject certain investment advisers (IAs) to anti-money laundering and countering the financing of terrorism (AML/CFT) requirements pursuant to the Bank Secrecy Act (BSA), including requirements to maintain AML/CFT programs, report suspicious activity to FinCEN, and fulfill BSA recordkeeping requirements.

**Given both the breadth of the anticipated obligations and the challenges of securing compliance resources at impacted firms outside of standard budgetary cycles, it is important for investment advisers to begin planning immediately to ensure that effective systems and processes are in place to meet new AML/CFT requirements when the final rule goes live.**

As a reminder, the proposed rule would apply to both registered investment advisers (RIAs) and investment advisers that report to the Securities and Exchange Commission (SEC) as exempt reporting advisers (ERAs), such as private fund and venture capital advisers.

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## Our Services

K2 Integrity is uniquely positioned to help IAs of all sizes and business models proactively navigate and manage compliance with the proposed rule's new AML/CFT requirements. The services described below are organized by near-term and medium-term priorities for all covered investment advisers, as well as additional considerations for small- to mid-sized advisers.

### ***Near-Term Priorities***

Compliance with the requirements under the proposed rule will require IAs to budget for and begin executing on certain AML/CFT controls before the rule is finalized and goes into effect. Additionally, IAs should expect the fundamental elements of the NPRM—including the requirements to maintain an AML/CFT program, to file suspicious activity reports (SARs) and currency transaction reports (CTRs) instead of Forms 8300, and to fulfill BSA recordkeeping requirements—to remain unchanged as it proceeds to the final rulemaking stage. IAs can therefore begin planning for compliance with these core requirements even before the rule is finalized. K2 Integrity's experts can assist IAs in meeting the following near-term compliance priorities:

- **Undertaking an enterprise-wide financial crime risk assessment** that considers, among other factors, the types of accounts offered, the types of customers opening such accounts, the geographic location of such customers, and the sources of wealth for customer assets.
- **Adapting existing policies, procedures, and internal controls** to ensure they are aligned to the firm's risk profile and risk appetite and to incorporate core anticipated AML/CFT obligations, such as CTR and SAR filing requirements.
- **Identifying a BSA/AML compliance officer** to be responsible for implementing and monitoring the operations and internal controls of the AML/CFT program once it is operational.
- **Designing and documenting a system or process for conducting ongoing monitoring** to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

Regulators and auditors will expect a firm's policies, procedures, and controls—including its suspicious

activity monitoring systems and processes—to be tailored to the specific financial crimes risks presented by its customers and business activities. **We recommend that any firm that has not undertaken a financial crimes risk assessment or has not updated this assessment in the past 12 months do so as a matter of priority to enable the firm's AML/CFT program to satisfy its legal obligations and supervisory expectations when the proposed rule goes into effect.**

### ***Medium-Term Priorities***

IAs will have 12 months from the effective date of the final rule to develop, document, and operationalize an AML/CFT program tailored to its business and risk profile. Once the final rule is issued, K2 Integrity can assist firms with the following measures to ensure that their policies, procedures, and controls are implemented and operating effectively by the end of this 12-month period:

- **Developing operating procedures or manuals** to guide business and compliance staff in implementing the firm's internal AML/CFT policies and programs.
- **Providing independent testing of the AML/CFT compliance program.**
- **Developing and delivering ongoing training** to employees, senior management, and the board on AML/CFT risks and requirements relevant to the firm as a whole and on a role-specific basis.
- **Designing and implementing special due diligence requirements** for private banking and correspondent bank accounts involving foreign persons, including to 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.

In addition, FinCEN’s proposed rule also announced plans for at least two subsequent rulemakings that would require IAs to apply customer identification program (CIP) requirements and to collect and verify beneficial ownership information for legal entity customers, respectively, in line with other covered financial institutions. To this end, **IAs should consider—either categorically or on a risk basis—voluntarily collecting and verifying customer and beneficial ownership information** to support ongoing customer due diligence (CDD) monitoring, suspicious activity reporting, and Office of Foreign Assets Control (OFAC) compliance.

### **Considerations for Small to Mid-Sized Firms**

In keeping with the risk-based approach underpinning FinCEN’s proposed AML/CFT program requirements, smaller IAs may undertake simplified measures in certain circumstances where they have identified lower financial crime risks. For example, rather than deploying automated transaction monitoring or sanctions screening software to support their SAR filing and sanctions compliance obligations, smaller firms could instead implement less costly, largely manual processes

for detecting and reporting suspicious or prohibited activity. However, a firm’s size is only a rough proxy for its riskiness, and regulators and auditors will typically expect a firm to undertake and formally document an assessment of its financial crime risks to support any assertion that the firm is, in fact, lower risk.

**K2 Integrity specializes in conducting diagnostic financial crime risk assessments that are tailored to the size and business footprint of each client—**allowing smaller IAs to develop and document a full understanding and assessment of their financial crime risks in a streamlined, cost-efficient manner. Such diagnostic assessments can allow smaller, lower-risk IAs to demonstrate that they have in place a “reasonably designed risk-based program” as required under the proposed rule without implementing the full range of higher-cost measures that may be expected of larger, higher-risk firms.

K2 Integrity welcomes the opportunity to meet with smaller IAs to discuss how best to satisfy their obligations under the proposed rule within tighter staffing and budgetary constraints.

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