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Submitted by SEC Webform[1] and Federal E-Rulemaking Portal[2]

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549

Andrea M. Gacki
Director
Financial Crimes Enforcement Network
U.S. Department of the Treasury
Washington, DC 20220

RE: Customer Identification Programs for Registered Investment Advisers and Exempt Reporting Advisers (SEC File No. S7-2024-02; Treasury Docket No. FINCEN-2024-0011)

Dear Ms. Countryman and Ms. Gacki:

On behalf of the North American Securities Administrators Association, Inc. ("NASAA"),[3] I am writing in response to Release No. BSA-1, *Customer Identification Programs for Registered Investment Advisers and Exempt Reporting Advisers*, issued jointly by the U.S. Securities and Exchange Commission ("SEC" or the "Commission") and the Financial Crimes Enforcement Network ("FinCEN") (the "Joint Proposal").[4] The Joint Proposal builds on an earlier proposal by FinCEN to designate certain SEC-registered investment advisers and exempt reporting advisers as "financial institutions" under the Bank Secrecy Act and require them to develop and implement anti-money laundering/countering the financing of terrorism ("AML/CFT") programs (the

[1] https://www.sec.gov/comments/s7-2024-02/customer-identification-programs-registered-investment-advisers-and-exempt#no-back.

[2] https://www.regulations.gov/docket/FINCEN-2024-0011/document.

[3] Organized in 1919, NASAA is the oldest international organization devoted to investor protection. NASAA's membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, México, Puerto Rico, the U.S. Virgin Islands, and Guam. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

[4] The full text of the Joint Proposal is available at https://www.sec.gov/files/rules/proposed/2024/bsa-1.pdf. The citations to the Joint Proposal in this letter reflect the page numbers therein.

"FinCEN Proposal").[5] If the FinCEN proposal is adopted, the Joint Proposal would require such advisers to implement a "Customer Identification Program," or "CIP," that includes procedures for verifying the identity of each customer, maintaining records of that process, and ensuring that the customer is not on certain lists of known or suspected terrorists or terrorist organizations. NASAA supports the Joint Proposal for the reasons explained below.[6]

The Bank Secrecy Act and related AML/CFT regulations serve an important public policy objective of preventing the use of the U.S. financial services industry for illicit purposes. NASAA fully supports this objective. Alongside the FinCEN Proposal, the Joint Proposal would close a current gap in AML/CFT regulations by extending important AML/CFT regulatory requirements to SEC-registered investment advisers and exempt reporting advisers. As such, NASAA broadly supports the Joint Proposal's requirement that investment advisers implement CIPs, which "support the application of other AML/CFT measures by making it more difficult for persons to use false identities to establish customer relationships with investment advisers for [illicit] purposes . . . ."[7]

Nonetheless, we believe that certain aspects of the Joint Proposal can and should be strengthened to ensure that investment advisers are not used to facilitate illicit activity. First, the Joint Proposal should not exclude accounts "that the investment adviser acquires through any acquisition, merger, purchase of assets, or assumption of liabilities," as proposed.[8] The Joint Proposal reasons that "[c]ustomers do not 'open' such transferred accounts,"[9] but we believe that distinction elevates form over the substance and spirit of the applicable law.[10] In our view, the proposed exclusion creates an unnecessary regulatory gap that undermines the purpose of the Joint Proposal. Although such accounts by definition existed before their transfer or acquisition, they are nonetheless new accounts *at the investment adviser in question* even if the identity of the customer and the assets are the same. They should therefore be subject to the same identification requirements as "new" accounts opened first at that institution. If there are concerns about burden, we believe it would be appropriate to permit an investment adviser to rely on the transferring

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[5] *See* Proposed Rule, *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*, 89 FR 12108 (Feb. 15, 2024).

[6] NASAA also submitted a letter in support of the FinCEN Proposal in April 2024. *See* Letter from Claire McHenry, NASAA President and Deputy Director, Nebraska Bureau of Securities (Apr. 12, 2024) ("NASAA Letter to FinCEN"), https://www.nasaa.org/wp-content/uploads/2024/04/NASAA-Comment-Letter-re-FINCEN-2024-0006_4-12-24.pdf.

[7] Joint Proposal at 8.

[8] *See* Proposed 31 C.F.R. § 1032.100(a)(2)(i).

[9] Joint Proposal at 9.

[10] *See* 31 U.S.C. § 5318(*l*).

entity's previous verification of the customer's identity, subject to the same conditions applicable to accounts opened by an existing, previously-verified customer of the investment adviser.[11]

Second, the Joint Proposal should be more definite about when investment advisers must look through customers that are not individuals, such as trusts and private funds, to identify their beneficial owners and individuals with authority and control over the accounts. The lack of such a requirement appears to continue an unnecessary and potentially harmful gap in the AML/CFT regulatory regime, particularly given the opacity of certain legal structures and arrangements.[12] It is difficult to understand how an investment adviser – or any financial institution – can ever "form a *reasonable* belief that it knows the *true* identity of [a non-individual] customer"[13] if it does not know the identity of the entity's beneficiaries and investors. At minimum, we would encourage the SEC and FinCEN to revise the Joint Proposal to affirmatively require a look-through in circumstances where "[t]he risk that an investment adviser will not have a reasonable belief that it knows a customer's true identity [is] heightened," as outlined in the Joint Proposal.[14] Such a requirement is unlikely to be unduly burdensome, as it would likely apply most readily to trusts and pooled investment vehicles with a manageable number of investors, rather than large mutual funds.[15]

The Joint Proposal further asks, "[s]hould closed-end registered funds, wrap fee programs, or other types of accounts advised by investment advisers be, on a risk-basis, exempted from an investment adviser's CIP program?"[16] In our view, the Joint Proposal should not exclude additional categories of customers unless, like mutual funds, they have developed and implemented a CIP pursuant to a rule implementing 31 U.S.C. § 5318(h) or that is otherwise consistent with the requirements of that section. Such a limitation would be consistent with the

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[11] *See* Joint Proposal at 14-15 (explaining that "if a customer whose identification has been verified previously opens a new account, the investment adviser would generally not need to verify the customer's identity again, provided the investment adviser (1) previously verified the customer's identity, to the extent required, in accordance with procedures consistent with the proposed rule, and (2) continues to have a reasonable belief that it knows the true identity of the customer based on the previous verification").

[12] *Cf.* FinCEN Proposal, 89 FR 12114 (noting that "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") ("Private funds can be a particularly attractive entry point for illicit proceeds because they present a possibility of high returns" and "can be used to obscure the names of individual investors or beneficial owners . . . .").

[13] *See* Proposed 31 C.F.R. § 1032.220(a)(2) (emphases added).

[14] Joint Proposal at 19.

[15] *See* Proposed 31 C.F.R. § 1032.220(a)(1) ("The investment adviser may deem these requirements satisfied for any mutual fund (as defined in 31 C.F.R. § 1010.100(gg)) it advises that has developed and implemented a CIP compliant with the CIP requirements applicable to mutual funds under another provision of this subpart.").

[16] Joint Proposal at 32, Question 10.

spirit of the exemption for mutual funds, which is premised on mutual funds' compliance with appropriate CIP requirements.[17] It is also consistent with the proposed provision allowing investment advisers to rely on another financial institution to perform some or all of its CIP obligations as long as, *inter alia*, "the other financial institution is subject to a rule implementing 31 USC 5318(h) and regulated by a Federal functional regulator."[18]

Finally, NASAA acknowledges and accepts FinCEN's assessment that it is unnecessary to extend the AML/CFT regime to state-registered investment advisers because FinCEN has not found evidence that state-registered investment advisers are being used as conduits for money laundering and considers this risk to be low.[19] However, we note the statement in the Joint Proposal that "[s]mall investment advisers have just as much exposure as large ones to the risks [at issue] since criminals may seek to place their funds at financial institutions with less sophisticated risk management capabilities."[20] Given that most "small advisers" are registered with the states rather than the SEC,[21] and therefore not subject to the Joint Proposal, we reiterate our expectation and hope that, consistent with 31 U.S.C. § 5318(h)(4)(B), FinCEN and the SEC will engage with NASAA and its members if either finds evidence that state-registered investment advisers are being used to launder money or for other illicit purposes addressed by the Bank Secrecy Act.

NASAA appreciates the opportunity to comment on the Joint Proposal to close a current gap in AML/CFT regulations. Nonetheless, we believe that the Joint Proposal can be further strengthened, as described above. Thank you for considering these views. Should you have any questions about this letter, please contact either the undersigned or NASAA's General Counsel, Vince Martinez, at (202) 737-0900.

Sincerely,

Claire McHenry
NASAA President and
Deputy Director
Nebraska Bureau of Securities

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17 *See* Proposed 31 C.F.R. § 1032.220(a)(1).

18 Proposed 31 C.F.R. § 1032.220(a)(6)(ii).

19 *See* NASAA Letter to FinCEN at 2 and n.6.

20 Joint Proposal at 38 n.61.

21 *See*, *e.g.*, *id.* at 73.