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July 22, 2024

Financial Crimes Enforcement Network
Policy Division
P.O. Box 39
Vienna, VA 22183

Re: Customer Identification Programs for Registered Investment Advisers
Docket Number FINCEN—2024—0011
RIN 3235-AN34
File Number S7-2024-02

Dear Sir or Madam:

On behalf of the SPARK Institute, Inc., we are writing regarding the impact on employer-sponsored retirement plans of the Financial Crimes Enforcement Network ("FinCEN") and Securities & Exchange Commission ("SEC") proposal that would newly require federally registered investment advisers ("RIAs") to establish and adhere to customer identification programs ("CIPs").[1]

The SPARK Institute represents retirement plan recordkeepers, mutual fund companies, brokerage firms, insurance companies, banks, consultants, trade clearing firms, and investment managers. Collectively, our member firms administer the retirement plans for over 110 million American workers.

Retirement Plans Should Be Carved Out from the Current Rulemaking

Consistent with the concerns that the SPARK Institute raised in our April 15, 2024 letter responding to a separate proposal that would more broadly apply anti-money laundering / countering the financing of terrorism ("AML/CFT") programs to RIAs, the SPARK Institute is concerned with the current proposal that would extend the CIP rules to RIAs when interacting with employer-sponsored retirement plans. As we explained in our April 15, 2024 letter, the SPARK Institute believes that these advisory relationships should be exempt from the CIP requirements and other AML/CFT requirements because RIA activities involving employer-sponsored retirement plans present a very low risk in terms of money laundering, terrorist financing, and other illicit financial activity. A more detailed discussion of why employer-

[1] For purposes of this letter, the term employer-sponsored retirement plan refers to 401(a) plans, 403(b) plans, and governmental and tax-exempt 457(b) plans. It also refers to nonqualified deferred compensation plans that permit participants to direct investments.

sponsored plans present low risks is provided in our April 15, 2024 comment letter, which we have attached to this letter as a reference.

Accordingly, the SPARK Institute was very disappointed with the preamble discussion in the current proposal indicating that the proposed definition of "account" would include accounts opened for the purpose of participating in an employee benefit plan established pursuant to the Employee Retirement Income Security Act of 1974 (''ERISA'').[2] Not only do we believe that this is the wrong approach, we also were surprised by this interpretation given the fact that ERISA accounts are excluded from the CIP requirements in other contexts.[3] Although the preamble to the current proposal acknowledges this departure from past rulemakings, this position is especially concerning as the preamble makes no effort to explain, and offers no support for, why a different approach is being taken for this rulemaking.

That said, we interpret the preamble's discussion indicating that RIAs will not be required to "look through" a trust or similar account to its beneficiaries to mean that the CIP requirements will generally apply to the retirement plan itself, and thus will not apply to every retirement plan participant simply because they are participating in an employer-sponsored retirement plan.[4] This is clearly the correct result, as the plan's trust is the "customer." Nonetheless, we are concerned that there may be situations in which RIAs would be required – unnecessarily – to apply the proposed CIP procedures to plan participants that access advisory services through an employer-sponsored retirement plan. Very similar to the concerns raised in our April 15, 2024 letter, this potential CIP requirement for retirement plan participants is especially concerning in the context of managed account programs offered through an employer-sponsored retirement plan to individual plan participants.

In considering the issues impacting employer-sponsored retirement plans, we strongly urge FinCEN and the SEC to consider how the CIP rules would interact with the Department of Labor ("DOL") regulations that expressly permit managed accounts to be used as a plan's default investment option.[5] As discussed in our prior letter, the issue in this context is that the population of participants who would be defaulted into a managed account are necessarily participants who have failed to make an election and otherwise do not engage with the plan. If FinCEN and the SEC do not provide a carveout for employer-sponsored retirement plans, they should consult with DOL to ensure that this proposal would not effectively eliminate a default investment option expressly recognized in longstanding regulations from DOL.

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[2] 89 Fed. Reg. 44571, 44573 (May 21, 2024).

[3] 1 C.F.R. § 1024.100(a)(2)(ii). *See* Joint Final Rule on Customer Identification Programs for Mutual Funds, 68 Fed. Reg. 25131, 25134 (May 9, 2003) ("We believe that these accounts are less susceptible to use for the financing of terrorism and money laundering, because, among other reasons, they are funded through payroll deductions in connection with employment plans that must comply with federal regulations that impose various requirements regarding the funding and withdrawal of funds from such accounts, including low contribution limits and strict distribution requirements. Therefore, we have decided to exclude them from the definition of "account" in the final rule.").

[4] 89 Fed. Reg. at 44574.

[5] Labor Reg. § 2550.404c-5(e)(4)(iii).

Accordingly, for all of the reasons expressed in this letter and our April 15, 2024 letter, we are recommending that any final rules include a carveout for employer-sponsored retirement plans, or at the very least, make clear that investment advisers are not required to apply any of the final changes to participants in employer-sponsored retirement plans. In the context of the current CIP proposal, this could be achieved by, for example, clarifying that the definition of "account" does not include an account opened for the purpose of participating in an employer-sponsored retirement plan.

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The SPARK Institute appreciates the opportunity to provide these comments on the proposed expansion of the CIP rules to RIAs. If you have any questions or would like more information regarding this letter, please contact the SPARK Institute's outside counsel, Michael Hadley (mlhadley@davis-harman.com) or Adam McMahon (armcmahon@davis-harman.com), Davis & Harman LLP.

Sincerely,



Tim Rouse
Executive Director

Attachment

- SPARK's Comments on Proposed AML/CFT Programs for RIAs (April 15, 2024)



Filed electronically at regulations.gov

April 15, 2024

Financial Crimes Enforcement Network
Policy Division
P.O. Box 39
Vienna, VA 22183

Re: AML/CFT Programs for Registered Investment Advisers
Docket Number FINCEN—2024—0006
RIN 1506-AB58

Dear Sir or Madam:

On behalf of the SPARK Institute, Inc., we are writing regarding the impact on employer-sponsored retirement plans of the Financial Crimes Enforcement Network ("FinCEN") proposal that would newly apply certain anti-money laundering / countering the financing of terrorism ("AML/CFT") programs to federally registered investment advisers ("RIAs").[1]

For the reasons laid out below, we are recommending that the final rule include a carveout for employer-sponsored retirement plans, or at the very least, make clear that investment advisers are not required to apply any of the final changes to participants in employer-sponsored retirement plans. To address our concerns, improvements to the proposal could, for example, make clear that participants in employer-sponsored retirement plans are not the "customer" and, for purposes of the customer identification program ("CIP") and beneficial ownership requirements, make clear that the definition of "account" does not include an account opened for the purpose of participating in an employer-sponsored retirement plan.

The SPARK Institute represents retirement plan recordkeepers, mutual fund companies, brokerage firms, insurance companies, banks, consultants, trade clearing firms, and investment managers. Collectively, our member firms administer the retirement plans for over 110 million American workers.

Proposed Expansion of AML/CFT Programs to RIAs

The proposed amendments published by FinCEN on February 15, 2024 would require RIAs, for the first time, to: (a) implement AML/CFT programs; (b) file Suspicious Activity Reports

[1] For purposes of this letter, the term employer-sponsored retirement plan refers to 401(a) plans, 403(b) plans, and governmental and tax-exempt 457(b) plans. It also refers to nonqualified deferred compensation plans that permit participants to direct investments.

("SARs") and Currency Transaction Reports ("CTRs"); (c) maintain records of originator and beneficiary information for certain transactions; (d) apply information-sharing provisions between and among FinCEN, law enforcement, agencies, and certain financial institutions; and (e) implement special due diligence requirements for correspondent and private banking accounts and special measures under section 311 of the USA PATRIOT Act. Consistent with the overall purpose of the Bank Secrecy Act, these proposed changes are intended to prevent money laundering, terrorist financing, and other illicit financial activity.

The SPARK Institute is concerned that, in the absence of a clear carveout, these proposed changes would unnecessarily impact RIA activities involving employer-sponsored retirement plans, including through their potential application to RIA-advised managed account programs and non-mutual fund investments that are made available to employer-sponsored retirement plans, such as collective investment trusts ("CITs"). While we appreciate FinCEN's efforts to combat money laundering, terrorist financing, and other illicit financial activity, we do not believe that any of the proposed changes should be extended to RIA interactions with employer-sponsored retirement plans because transactions involving these plans present a very low risk in terms of money laundering, terrorist financing, and other illicit financial activity.

Every day, thousands of Americans start a new job and become eligible for their employer's benefits, such as a pension plan or 401(k) plan. Many are *automatically* enrolled in the plan shortly after starting employment, and begin making contributions, receiving employer contributions, or begin accruing pension benefits.

These plans are heavily regulated by the Employee Retirement Income Security Act of 1974 ("ERISA") and the Internal Revenue Code ("Code"). For example, employers sponsoring ERISA-covered plans are held responsible as fiduciaries for plan oversight and, pursuant to ERISA section 404(b), except as otherwise authorized by the Secretary of Labor, "no fiduciary may maintain the indicia of ownership of any assets of a plan outside the jurisdiction of the district courts of the United States." As other examples, through requirements imposed by the Code, retirement plans are generally subject to contribution limits, limited withdrawal rights, and detailed tax reporting that connects distributees to a specific taxpayer identification number. These key elements – specifically limited withdrawal rights – are antithetical to high-risk anti-money laundering activity.

In a defined benefit retirement plan, which provides a fixed and pre-determined benefit to retirees, employee-participants do not exercise discretion over the investment of assets that are maintained on their behalf. Instead, such investments are selected and overseen by the employers who sponsor the plans and any investment professionals that such employers retain to assist them. In a defined contribution retirement plan, where an employee's benefit depends on their own account's investment performance, employees are typically given the ability to direct contributions among a diversified menu of investment alternatives comprised of, for example, mutual funds, CITs, or insurance company separate accounts. Employees who do not affirmatively choose an investment option are defaulted into an investment that is selected by their employer. This is known as the qualified default investment alternative or QDIA.

RIAs typically interact with employer-sponsored retirement plans in the following ways:

- ***Plan-Level Services.*** RIAs interact with employer-sponsored retirement plans by providing plan-level services, such as managing or recommending the investments that are held within the plan on behalf of employees and retirees. In this regard, an RIA may manage a mutual fund, insurance product, or CIT that may be selected by participants as part of a defined contribution plan's investment menu, or it may manage a fund that is part of a defined benefit plan's portfolio.

- ***Participant-Level Services.*** RIAs may also interact with employer-sponsored retirement plans by providing services directly to individual plan participants. For example, as part of a managed account program, an RIA will, based on the investments that have been selected by the plan's sponsoring employer, make investment recommendations or provide discretionary management over a participant's individual account under the plan. Like specific investment options offered through a plan's investment menu, before an RIA can provide managed account services to a plan participant, it must first be selected by the employer sponsoring the plan. Importantly, Department of Labor ("DOL") regulations make clear that a managed account can be the plan's QDIA.

Employer-sponsored retirement plans contain a number of features that simply make them not susceptible to the concerns underlying your proposal:

- Perhaps most importantly, the information used to set up a participant's account under a plan generally comes from the employment data collected by the employer. And there are existing protections in place in the employment sphere, such as the need to collect the I-9 information to verify identity.
- Employer-sponsored retirement plans limit the ability of participants to make withdrawals.
- Employer-sponsored retirement plans are heavily regulated by ERISA and the Code.
- Through limits imposed by the Code, employer-sponsored retirement plans are generally subject to contribution limits. For example, in the case of a 401(k), 403(b), or governmental 457(b) plan, the regular elective deferral limit in 2024 is $23,000.
- In the case of the managed account programs and CITs that we are most concerned about, employer-sponsored retirement plans can only offer these services and products if they are first selected by the sponsoring employer or other plan fiduciary.

Accordingly, the SPARK Institute requests that the final rules expressly exclude RIA activities involving employer-sponsored retirement plans because they present a very low risk in terms of money laundering, terrorist financing, and other illicit financial activity. Furthermore, to the extent any final rules extend such requirements to employer-sponsored retirement plans, they should only apply at the plan level and <u>not at the participant level</u>.[2] To the extent that any final changes impact employer-sponsored retirement plans, FinCEN should also consider

[2] This means that any RIA activities dealing with an individual's account should be exempt. Additionally, if an RIA that has not been selected by the employer sponsoring the plan interacts with a plan participant, the RIA should not be required to perform any due diligence with regard to the plan itself or the plan sponsor.

appropriate grandfathering relief for relationships established prior to the final rule's effective date.

As noted above, this is especially concerning in the context of managed account programs offered through an employer-sponsored retirement plan to individual plan participants. If, for example, the proposed changes were to apply at the participant level, they would effectively prevent a retirement plan from using a managed account as the plan's QDIA, contrary to DOL regulations that expressly permit managed accounts to be used as a plan's default option.[3] The problem in this case is that the population of participants who would be defaulted into a managed account are necessarily participants who have failed to make an election and provide information to the plan.

The appropriateness of an express retirement plan carveout is further warranted by the fact that retirement plans necessarily require the involvement of other regulated entities that are independently subject to AML/CFT rules. Aside from the involvement of an RIA, retirement plans also utilize the services of broker-dealers, banks, and trust companies. Thus, to the extent that these related entities are already applying AML/CFT programs in connection with specific transactions involving retirement plans, such as certain plan-level transactions, the expanded application of these rules to any associated RIA would be redundant and should be avoided. [4] To be clear, however, a retirement plan exemption for RIAs should not depend on an RIA's affiliation with an entity that independently qualifies as a financial institution.

For example, in the case of a CIT that is advised by an RIA and only receives investments from retirement plans, the CIT must be maintained by a bank or trust company that is already subject to its own banking regulations and AML rules. Accordingly, given the CIT investor qualification rules and other regulatory requirements, these vehicles and other products offered through retirement plans present a very low risk in terms of money laundering, terrorist financing, and other illicit financial activity.

Verification of Beneficial Ownership

Although the proposal would not require RIAs to collect beneficial ownership information for legal entity customers through a CIP requirement, the proposal indicates that FinCEN anticipates addressing CIP requirements via a future joint rulemaking with the Securities & Exchanges Commission ("SEC"). For the same reasons expressed above, to the extent that such a rulemaking is pursued, we urge FinCEN and the SEC to carve out employer-sponsored retirement plans so that RIAs serving such plans would not be required to collect information or verify the beneficial ownership information relating to employer-sponsored retirement plans.

[3] Labor Reg. § 2550.404c-5(e)(4)(iii).

[4] At the very least, RIAs should be permitted to rely on determinations made by other financial institutions to the extent they are providing services to plans and are subject to the rules being extended to RIAs through FinCEN's proposal.

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The SPARK Institute appreciates the opportunity to provide these comments on the proposed expansion of the AML/CFT rules to RIAs. If you have any questions or would like more information regarding this letter, please contact the SPARK Institute's outside counsel, Michael Hadley (mlhadley@davis-harman.com) or Adam McMahon (armcmahon@davis-harman.com), Davis & Harman LLP.

Sincerely,



Tim Rouse
Executive Director