WILLKIE FARR & GALLAGHER

CLIENT
MEMORANDUM

Anti-Money Laundering Programs Proposed for—
(1) Registered Investment Advisers and Unregistered Advisers with $30 Million Under Management and
(2) Registered Commodity Trading Advisers that Direct Client Accounts

Proposed Rules

The Treasury Department issued proposed rules on April 29 that, if adopted, will require certain investment advisers and commodity trading advisers to establish anti-money laundering programs. The proposed rules will not impose additional anti-money laundering responsibilities on these advisers, although Treasury indicates that it is considering requiring suspicious activity reporting. This memorandum summarizes the scope and requirements of these proposed rules.

Scope

The anti-money laundering program requirements will apply to the following investment advisers and commodity trading advisers—

INVESTMENT ADVISERS

Group 1

- registered (or required to be registered) with the Securities and Exchange Commission
- located in the United States
- with assets under management.

Group 2

- exempt from registration with the Commission under § 203(b)(3) of Investment Advisers Act (for advisers with fewer than 15 clients that do not hold themselves out to the public as investment advisers)
- located in the United States
- with assets under management of $30 million or more.

COMMODITY TRADING ADVISERS

One Definition

- registered (or required to be registered) as commodity trading adviser with the Commodity Futures Trading Commission
- that directs client commodity futures or options accounts.

The proposed rules do not require investment advisers or commodity trading advisers to establish multiple anti-money laundering programs; the same program may work for a firm that qualifies as a "financial institution" in several ways, such as an investment adviser that also is a commodity trading adviser, so long as the program satisfies all applicable requirements.

Investment advisers and commodity trading advisers may exclude from the scope of their anti-money laundering programs advised hedge funds and other investment vehicles that are themselves subject to anti-money laundering programs requirements. (Due to the phasing-in of these requirements, this exclusion could be a little rough around the edges in the beginning.) The proposed rule for commodity trading advisers (but, oddly not the proposed rule for investment advisers) also permits exclusion from the scope of the anti-money laundering program of clients for whom the adviser does not direct accounts.

Notice

As it did with hedge funds, Treasury will require each unregistered investment adviser to file a notice with FinCEN (via FinCEN's website or by mail) within 90 days of becoming subject to the rule (that is, for advisers that will be subject to the rule when adopted, within 90 days of the effective date of the final rule). The notice is to contain the following information:

- name, address, e-mail address and telephone number of the company
- name, address, e-mail address and telephone number of the anti-money laundering compliance officer
- dollar amount of assets under management
- number of clients.

An adviser that has filed the required notice must file an amendment within 30 days of any change in the information in the notice, other than the amount of assets under management and the number of clients.

Program Requirements

Adoption of the Program. The proposed rules require approval of the anti-money laundering program by the investment adviser's or commodity trading adviser's board of directors or, if it does not have one, by its general partner or other person with a similar function. We recommend that, in approving the anti-money laundering program and appointing the AML compliance officer, the board or general partner authorize the AML compliance officer to amend the program in response to subsequent regulatory developments, so that each technical amendment will not require prior board or general partner consideration (but may be ratified later).

Policies, Procedures and Controls. An anti-money laundering program should be tailored to the business, size, location, activities and structure of an adviser, according to Treasury. An adviser should identify and weigh the anti-money laundering risks to which it is exposed and design an anti-money laundering program in the light of those risks. The anti-money laundering program must ensure compliance with applicable anti-money laundering regulations, as well as combat money laundering. Investment advisers and commodity trading advisers, like all U.S. persons, are subject to certain specific anti-money laundering rules, such as the requirement to report currency transactions exceeding $10,000 (including same-day transactions that total more than $10,000) and the requirement to report foreign bank and securities accounts.

AML Compliance Officer. An officer of the adviser must be designated as in charge of the anti-money laundering program (usually called the AML Compliance officer). This officer must be competent and adequately empowered for the job. All employees should know who the AML Compliance Officer is and how to contact him or her.

AML Training. Anti-money laundering training is one of the required elements of all anti-money laundering programs. It may be conducted in-house (by the AML Compliance Officer, for example) or by a third party. The frequency of this training depends on the anti-money laundering risks to which the adviser is subject, the responsibilities of the adviser's personnel and other factors. Initial training should follow adoption of the AML Program.

Periodic Audit. Again, periodic auditing or testing is one of the required elements of all anti-money laundering programs. It may be conducted in-house (but *not* by the AML Compliance Officer) or by a third party, such as an independent auditor. The audit probably should be annual, but the proposed rules are not specific on this point.

Observations

An investment adviser that sponsors an investment fund that will not itself be subject to an anti-money laundering program requirement—such as a private equity fund or other investment fund that does not give an investor a right to redeem any portion of the investor's interest within two years of the investment—must deal with the fund's investors the same way it does separate account clients. Intentionally or not, Treasury is here taking away some of what it gave last fall when it exempted private equity funds (and other similarly illiquid investment funds) from the requirement of establishing anti-money laundering programs.

An investment adviser or commodity trading adviser that advises an investment fund (sponsored by another party) that is not itself required to have an anti-money laundering program—such as an employee benefit plan or a private equity fund sponsored by another firm—must determine whether the nature of the fund is such that the money laundering risk it presents is low (based on location, applicable anti-money laundering laws, the adviser's past experience with the fund, the nature of the fund, etc.) or whether the fund's administrator is adequately managing that risk. Treasury says that, as the money laundering risk presented increases, the adviser's procedures should address that risk, such as by obtaining and reviewing information about the identities of the fund's investors.

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If you have questions regarding this memorandum, or if you need assistance in developing an anti-money laundering program, please contact John Cairns at (212) 728-8207 or the partner who regularly works with you. The partners of Willkie Farr & Gallagher's Investment Management Group are Rose DiMartino, Burt Leibert, Dan Schloendorn and Emily Zeigler. The Group advises investment managers, mutual funds, hedge funds, private equity funds and other institutional investors, both domestic and international. Willkie Farr & Gallagher is headquartered at 787 Seventh Avenue, New York, NY 10019-6099. Our telephone number is (212) 728-8000; our facsimile number is (212) 728-8111. Our website is at www.willkie.com.