The Asset Management Industry
SERVING INDIVIDUAL INVESTORS
INVESTMENT COMPANY INSTITUTE
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Comment Letter on NASD's Proposed Anti-Money Laundering Program Standards, March 2002

March 18, 2002

Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: File No. SR-NASD-2002-24

Dear Mr. Katz:

The Investment Company Institute[1] appreciates the opportunity to comment on NASD Proposed Rule 3011 (Anti-Money Laundering Compliance Program). [2] The proposed rule would prescribe minimum standards for anti-money laundering compliance programs established by NASD members pursuant to Section 352 of the "USA PATRIOT Act" (Act).[3] Our comments address the rule's application to NASD members that underwrite securities issued by registered investment companies (funds).

The Institute strongly supports effective rules to combat potential money laundering activity in the investment company industry. With this in mind, we propose a narrowly crafted carve-out from Rule 3011 that would create no gaps in anti-money laundering compliance. Specifically, the Institute recommends that the rule provide a conditional exemption to any NASD member with respect to its activities as a principal underwriter of mutual fund securities. The exception would apply where the funds such NASD member underwrites have established an anti-money laundering program meeting the requirements of Section 352 of the Act (and any rule applicable to funds adopted thereunder).[4]

We propose this exemption for two reasons. First, it would avoid unnecessary regulatory duplication. In this regard, we note that the Act's requirement to establish an anti-money laundering compliance program by April 24, 2002[5] applies to funds as well as to broker-dealers, and it is our understanding that proposed regulations setting minimum standards for fund compliance programs are imminent. Where an underwriter is part of a fund complex, it would be logical for the funds' anti-money laundering program to cover any relevant activities of the underwriter. (Indeed, the underwriter and other entities in a fund complex frequently share common personnel.) In these circumstances, there is no need for the underwriter to comply with a separate, duplicative requirement imposed by the NASD on its members.[6] This is particularly true where, as is frequently the case, the underwriter does not open or hold shareholder accounts or process transactions in fund shares.[7]

Second, our proposed exemption would eliminate the illogical, bifurcated anti-money laundering compliance examination regime that Rule 3011 otherwise would create for fund complexes. Compliance with the anti-money laundering program requirement for funds likely will be examined by the Commission's Office of Compliance, Inspections and Examinations (OCIE). As we indicated in our recent Broker-Dealer SAR Comment Letter, due to the scope of the Commission's regulatory authority, we believe OCIE is in the best position to examine funds and their relevant service providers (e.g., underwriters and transfer agents) in a comprehensive and integrated fashion for compliance with applicable anti-money laundering requirements.[8] Subjecting fund underwriters to NASD examination authority for this purpose would create a piecemeal regulatory scheme that would be both duplicative and inefficient.

As noted in the Proposing Release, the legislative history of the Act makes clear that the compliance program provision "is not a 'one-size-fits-all' requirement."[9] Rather, the provision's requirements are general in nature because of Congressional intent "that each financial institution should have the flexibility to tailor the anti-money laundering programs to fit its business, taking into account factors such as . . . activities of the firm's business. . . ."[10] Our recommendation reflects the fact that the activities of broker-dealers in acting as underwriters of mutual fund shares are inextricably tied to the activities of the funds themselves. Allowing such broker-dealers to be covered under fund compliance programs with respect to these activities would be consistent with Congress's intent to

allow appropriate tailoring of these programs to fit different business models.

* * *

Thank you for considering our comments on proposed NASD Rule 3011. If you have any questions or need additional information, please contact me at (202) 326-5815, Frances Stadler at (202) 326-5822 or Bob Grohowski at (202) 371-5430.

Sincerely,

Craig S. Tyle
General Counsel

Attachment

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ENDNOTES

[1] The Investment Company Institute is the national association of the American investment company industry. Its membership includes 9,039 open-end investment companies ("mutual funds"), 486 closed-end investment companies and 6 sponsors of unit investment trusts. Its mutual fund members have assets of about $6.951trillion, accounting for approximately 95 percent of total industry assets, and over 88.6 million individual shareholders.

[2] See SEC Release No. 34-45457 (February 19, 2002), 67 Fed. Reg. 8565 (February 25, 2002) (Proposing Release).

[3] Uniting and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001, Pub. Law No. 107-56 (October 26, 2001). Section 352 requires financial institutions to establish such programs by April 24, 2002.

[4] Under our proposal, if a broker-dealer underwrites funds and also engages in other activities such as offering brokerage services to clients, it would be subject to Rule 3011 with respect to those other activities.

[5] We note that proposed Rule 3011 appears to require the establishment and implementation by April 24 of policies and procedures to comply with certain requirements that likely will not have been adopted in final form by that time (e.g., suspicious activity reporting requirements for broker-dealers). We suggest that the Commission’s adopting release clarify that programs established under Rule 3011 should provide for compliance with any applicable suspicious activity reporting or other Bank Secrecy Act requirements at the time specified by final regulations imposing those requirements.

[6] As noted above, proposed Rule 3011 would require NASD members to establish and implement policies and procedures that can reasonably be expected to detect and cause the reporting of suspicious transactions required under 31 U.S.C. 5318(g) and the implementing regulations thereunder. We recognize that fund underwriters may be required to comply with suspicious activity reporting requirements that have been proposed for broker-dealers, whereas funds themselves are not currently subject to such requirements. We believe this is a transitional issue rather than a potential gap in regulatory coverage, however. The Treasury Department reportedly is considering proposing a suspicious activity reporting rule for funds, and we have expressed our support for such an approach. See Letter from Craig S. Tyle, General Counsel, Investment Company Institute, to Judith R. Starr, Chief Counsel, Office of the Chief Counsel, Financial Crimes Enforcement Network, Department of the Treasury, dated March 1, 2002 (Broker-

Dealer SAR Comment Letter), at 3.

[7] These functions often are handled by the fund's transfer agent.

[8] Broker-Dealer SAR Comment Letter at 8.

[9] Proposing Release at 8566.

[10] Id.
