

November 8, 2002

**Treasury Issues Proposed Anti-Money Laundering Rule for
Unregistered Investment Companies**

On September 18, 2002, the Department of the Treasury's Financial Crimes Enforcement Network (FinCen) issued a proposed rule that would require certain hedge funds, commodity pools, real estate investment trusts, and other unregistered investment companies to establish anti-money laundering programs, and requiring each such entity to file a notice with FinCen identifying itself and providing basic information about the company.

**Application of the
Proposed Rule**

The proposed rule would apply to the following types of unregistered investment companies:

- Companies excluded from the registration requirements of the Investment Company Act of 1940 by virtue of sections 3(c)(1) and 3(c)(7) of the 1940 Act;
- Commodity pools;
- Companies that invest primarily in real estate or real estate investment trusts (REITs); and,
- Several types of unregistered investment companies, including hedge funds, private equity funds, venture capital funds, and commodity pools.

The proposed rule is limited to investment companies that have total assets of at least \$1 million and that give an investor the right to redeem any portion of his or her investment within two years after that interest was purchased. This limitation excludes companies offering investments that either are not redeemable or are redeemable only after a lengthy holding period, because such investments lack the liquidity that attracts money launderers in the first place.

Finally, because many unregistered investment companies operate offshore and offer investments in their companies to both U.S. and

foreign investors, the proposed rule would apply to companies that are organized under the laws of the United States; organized, operated, or sponsored by a U.S. person; or sell ownership interests to a U.S. person.

Required Anti-Money Laundering Program

The proposed rule would require that unregistered investment companies develop and implement anti-money laundering programs reasonably designed to prevent them from being used to launder money or finance terrorist activities. The programs will have to be implemented no later than 90 days following publication of a final rule. The proposed rule would also require that each company's program be approved in writing by the board of directors or trustees, the general partner or, if the foregoing do not exist, senior management. The proposed rule sets forth four mandatory elements to such a program.

Policies and Procedures

Investment companies must establish and implement policies and procedures designed to prevent the investment company from being used for money laundering. Written policies and procedures should set forth clearly the details of the program, including the responsibilities of the individuals and departments involved. Policies, procedures and internal controls should be reasonably designed to detect activities indicative of money laundering, such as the use of questionable checks and unusual wire activity. Policies, procedures and internal controls should also be designed to ensure compliance with the requirements of the Bank Secrecy Act (BSA). Although the only BSA requirement currently applicable to unregistered investment companies is the obligation to report on Form 8300 the receipt of cash or certain non-cash instruments totaling more than \$10,000 in one transaction or two or more related transactions, the Treasury has indicated that unregistered investment companies may become subject to additional BSA requirements, including customer and investor identification and verification and required filing of suspicious activity reports.

FinCen has noted that, like mutual funds, unregistered investment companies typically conduct their operations through separate entities such as fund administrators, investment advisers, commodity trading advisers, and broker-dealers and, therefore, some elements of the compliance program will best be performed by personnel of these separate entities. FinCen has said it is permissible for investment companies to contractually delegate the implementation and operation of those aspects of its anti-money laundering program to these entities. The investment company, however, will remain fully responsible for ensuring compliance.

Independent Testing

Unregistered investment companies would be required to conduct periodic testing of their programs to ensure that the programs are

functioning as designed. Testing should be done by persons knowledgeable about the company's money laundering risks and the BSA requirements. Testing may not be conducted by employees who are involved in the operation or oversight of the program. A written assessment or report should also be part of the review.

**Designation of a
Compliance Officer**

Unregistered investment companies would be required to appoint an individual (or committee) to be responsible for overseeing the anti-money laundering program. The person must be empowered with full responsibility and authority to develop and enforce appropriate policies and procedures. Although implementation and operation of the compliance program may in some cases be conducted by entities other than the unregistered investment company, the person responsible for supervising the overall program should be an officer, trustee, general partner, organizer, operator, or sponsor of the investment company.

Training

All anti-money laundering programs must provide employee training. Employees of both the investment company and any affiliated or third-party service providers must be trained regarding the relevant requirements of the BSA and applicable indicators of money laundering. The level, frequency and focus of the training should be determined by the responsibilities of the employees and the extent to which their job functions may bring them in contact with BSA requirements or possible money laundering activity. Employees should receive periodic refreshers regarding the anti-money laundering program.

Notice Requirement

Unlike other financial institutions, unregistered investment companies are not necessarily registered with or identifiable by Treasury or another Federal regulator. As such, there is currently no way for Treasury or other appropriate regulators to examine for and enforce compliance with the rule. Therefore, the proposed rule would require that each unregistered investment company file with FinCen a short notice ("Notice") identifying itself and providing basic information about the company, to include:

- The company's name, address, e-mail address and telephone number;
- The name, address, e-mail address and telephone number and registration number of any investment adviser, commodity trading adviser, CPO, organizer or sponsor of the company;
- The name, e-mail address and telephone number of the

designated anti-money laundering program compliance officer;

- The dollar amount of assets under management; and

- The number of participants, interest holders or security holders in the company.

The comment period on the proposed rules ends on November 25, 2002.

This document is intended as an informational reminder and does not constitute legal advice. If you have any questions or would like to discuss a particular situation, you should contact your usual W&D attorney or one of us.

David B. Fein	203-363-7603	dfein@wiggins.com
Gates Garrity-Rokous	203-498-4310	ggr@wiggins.com
Patricia L. Roer	203-363-7623	proer@wiggins.com

For more information about Wiggin & Dana's White-Collar Defense, Investigations and Corporate Compliance Practice Group, visit our web site at www.white-collardefense.com. For more information about the firm, please visit www.wiggins.com.