

**MEMO# 14085**

October 26, 2001

# **CONGRESS ENACTS ANTI-MONEY LAUNDERING LEGISLATION; GAO REPORT ON ANTI-MONEY LAUNDERING EFFORTS IN THE SECURITIES INDUSTRY**

[14085] October 26, 2001 TO: BOARD OF GOVERNORS No. 55-01 COMPLIANCE ADVISORY COMMITTEE No. 51-01 INTERNAL AUDIT ADVISORY COMMITTEE No. 6-01 INTERNATIONAL MEMBERS No. 20-01 INTERNATIONAL OPERATIONS ADVISORY COMMITTEE No. 12-01 PRIMARY CONTACTS - MEMBER COMPLEX No. 79-01 SEC RULES MEMBERS No. 70-01 TRANSFER AGENT ADVISORY COMMITTEE No. 86-01 SMALL FUNDS MEMBERS No. 30-01 UNIT INVESTMENT TRUST MEMBERS No. 35-01 RE: CONGRESS ENACTS ANTI-MONEY LAUNDERING LEGISLATION; GAO REPORT ON ANTI-MONEY LAUNDERING EFFORTS IN THE SECURITIES INDUSTRY I. Anti-Money Laundering Legislation On October 26th, President Bush signed into law comprehensive anti-terrorism legislation that includes provisions to combat money laundering. H.R. 3162, the "USA PATRIOT Act of 2001," was approved by the House of Representatives on October 24 by a 357- 66 vote, and by the Senate the next day by a 98-1 vote.<sup>1</sup> The anti-money laundering provisions are set forth in Title III of the Act. Several provisions of particular interest to investment companies are described briefly below.<sup>2</sup>

1. Treasury Authority to "Blacklist" Areas of Primary Money Laundering Concern. Section 311 of Title III provides the Secretary of the Treasury with new discretionary authority to designate a foreign jurisdiction, financial institution operating outside the United States, class of international transaction, or type of account to be of "primary money laundering concern." The Secretary may require all US financial institutions to take special measures with respect to any transaction involving one of those designated areas. The special measures may include requirements to obtain and retain records of beneficial ownership of accounts opened or maintained in the 1 A copy of the Act is available at [http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=107\\_cong\\_bills&docid=f:h3162enr.txt.pdf](http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=107_cong_bills&docid=f:h3162enr.txt.pdf). Title III of the Act begins on p. 25. 2 The term "financial institution" as used below includes, among other entities, investment companies and broker- dealers. It does not include investment advisers. 2 United States by foreign persons or their representatives. 2. Cooperative Efforts to Deter Money Laundering. Section 311 of Title III requires Treasury to prescribe regulations within 120 days of the legislation's enactment that are designed to encourage regulators and law enforcement authorities to share with financial institutions information about individuals or entities engaged in, or reasonably suspected based on credible evidence of engaging in, terrorist acts or money laundering activities. In addition, it provides protection from liability where, after notifying Treasury, two or more financial institutions and any association of financial institutions share information with each other regarding individuals, entities,

organizations or countries suspected of possible terrorist or money laundering activities. Section 311 specifies that information sharing in compliance with Title III shall not constitute a violation of the privacy provisions of the Gramm- Leach-Bliley Act. 3. Identification and Verification of New Account Holders. Section 326 of Title III requires Treasury, jointly with the SEC and other specified federal regulators, to adopt regulations setting forth minimum standards for financial institutions with regard to the identification and verification of customers in connection with the opening of an account. The regulations, at a minimum, will require financial institutions to implement "reasonable procedures" to verify the identity of any person seeking to open an account, maintain records of the information used to verify a person's identity and consult government lists of known or suspected terrorists or terrorist organizations. In adopting these regulations, Title III specifically requires Treasury to consider the various types of accounts maintained by different financial institutions, methods of opening accounts, and types of information available to make identifications. Final regulations are required to take effect within one year from the legislation's enactment. 4. Requirement to Establish Anti-Money Laundering Programs. Section 352 of Title III requires all financial institutions to establish anti-money laundering programs. These programs, at a minimum, must include the development of internal policies, procedures and controls, the designation of a compliance officer, an ongoing employee training program, and an independent audit function. Treasury may, in consultation with the Securities and Exchange Commission, prescribe minimum standards for these programs. The foregoing provisions are effective 180 days from enactment. In addition, Treasury must prescribe regulations within that 180-day period that consider the extent to which the requirements imposed under this section are commensurate with the size, location, and activities of the financial institutions to which such regulations apply. 5. Suspicious Activity Reporting by Broker-Dealers. Section 356(a) of Title III requires Treasury, after consultation with the SEC and the Board of Governors of the Federal Reserve System, to adopt regulations requiring brokers and dealers registered with the SEC to submit suspicious activity reports. These regulations must be proposed before January 1, 2002 and published in final form by July 1, 2002. 3 6. Report on Investment Companies. Section 356(c) of Title III requires Treasury, the Federal Reserve Board, and the SEC to jointly submit a report to Congress making recommendations for effective regulations to apply the requirements of the Bank Secrecy Act to investment companies. For these purposes, "investment companies" include both entities that are investment companies under the Investment Company Act of 1940 and entities that would be investment companies under the 1940 Act but for sections 3(c)(1) or 3(c)(7) of that Act (i.e., hedge funds). Section 356(c)(3) specifically provides that the recommendations may be different for the different types of investment companies covered. Section 303 of Title III provides that beginning on the first day of fiscal year 2005, Congress, by joint resolution, may terminate the provisions of and amendments made by Title III. It provides for expedited consideration of any such joint resolution. II. GAO Report on Anti-Money Laundering Efforts in the Securities Industry In response to a request by Senator Carl Levin (D-Mich.), Chairman of the U.S. Senate Permanent Subcommittee on Investigations, Committee on Governmental Affairs, the United States General Accounting Office (GAO) has issued a report entitled "Anti-Money Laundering Efforts in the Securities Industry." The report describes (1) government and industry views on the potential for money laundering in the securities industry, (2) current legal and regulatory requirements relating to anti-money laundering in the securities industry and the actions regulators have taken to oversee these requirements, (3) the efforts that broker-dealers and mutual funds have undertaken to detect and prevent money laundering (this information is based on a recent GAO survey of the anti-money laundering practices of broker-dealers and direct-marketed mutual fund firms), and (4) international anti-money laundering efforts relating to securities activities

and the effectiveness of these efforts. A copy of the report is available on the GAO's website at <http://www.gao.gov>. Robert C. Grohowski Associate Counsel

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