The Asset Management Industry
SERVING INDIVIDUAL INVESTORS

INVESTMENT COMPANY INSTITUTE

MEMO# 11490

December 22, 1999

INSTITUTE MAKES RECOMMENDATIONS TO SEC FOR PRIVACY RULEMAKING

1 See Memorandum to SEC Rules Committee No. 99-99, dated November 22, 1999. [11490] December 22, 1999 TO: SEC RULES COMMITTEE No. 109-99 SEC PRIVACY RULES WORKING GROUP RE: INSTITUTE MAKES RECOMMENDATIONS TO SEC FOR PRIVACY RULEMAKING _____ As you know, Title V of the recently enacted Gramm-Leach-Bliley Act contains two provisions requiring the Securities and Exchange Commission to promulgate rules relating to the privacy and confidentiality of customers' nonpublic personal information held by the financial institutions subject to the Commission's jurisdiction.1 The rules must be adopted by May 12, 2000. Accordingly, we expect privacy rules to be proposed early next year. In anticipation of that proposal, the Institute has submitted a letter providing Commission staff with a few preliminary recommendations. Our comments address: (1) the appropriate entity or entities to provide the notices required by the Act; (2) the form, location and content of those notices; and (3) the standards for establishing administrative, technical and physical safeguards to protect the safety and security of customer records that are required to be adopted by the Commission. A copy of the letter, summarized below, is attached. Entity Responsible for Providing Notices In general, the Act imposes a disclosure regime with respect to privacy. All financial institutions are required to provide customers with notice of their policies with respect to protecting the confidentiality and security of nonpublic personal information and sharing that information with affiliates and others (a "privacy policy notice"). Financial institutions also must provide customers with additional disclosure before nonpublic personal information can be shared with a nonaffiliated third party (an "opt-out notice"). These notices must be provided in accordance with regulations prescribed by the Commission. One of the most important questions to be resolved for the mutual fund industry concerns which entity should be required to provide the notices prescribed by the Act. In this regard, the letter makes two recommendations: ! For shares sold through intermediaries, the letter recommends that the intermediary be required to provide the notices, rather than the fund. The shareholder in this situation has entered into a direct customer relationship with the intermediary (e.g., by opening a brokerage or other account), and it is the intermediary's privacy policy, rather than the fund's, that would be relevant to the shareholder. ! For shares sold directly to investors (i.e., not through an intermediary), the letter recommends that the Commission define the customer relationship to be between the shareholder and the fund complex. This would permit any entity in the complex to provide the notices required by the rules, eliminating the need for customers to receive notices from each financial institution in the fund complex. Initial and Annual Notices Required by the Act The Act requires a privacy policy notice to be provided at the time a customer relationship is established and at least annually thereafter. It also requires

an opt-out notice to be provided before the financial institution engages in certain activities, such as sharing nonpublic personal information with nonaffiliated third parties. The letter urges the Commission to propose rules that will permit financial institutions to determine the most appropriate vehicle for providing a required notice, so long as it is reasonably designed to reach investors. Standards for Administrative, Technical and Physical Safeguards The Act requires the Commission to establish appropriate standards for administrative, technical and physical safeguards to protect customers' nonpublic personal information. The letter urges the Commission to avoid prescriptive rules in this area. Rather, it recommends that the Commission propose rules requiring fund complexes to adopt written procedures reasonably designed to protect the security and confidentiality of customer records and information. The letter indicates that this approach would ensure that every fund complex has appropriate procedures in place to ensure the integrity, confidentiality and security of customer information, while allowing them the flexibility to tailor and amend those procedures as appropriate. Robert C. Grohowski Assistant Counsel Attachment

---