

MEMO# 13400

April 10, 2001

SEC ISSUES GUIDANCE ON QUESTIONS RELATING TO REGULATION S-P

[13400] April 10, 2001 TO: BROKER/DEALER ADVISORY COMMITTEE No. 10-01 CLOSED-END INVESTMENT COMPANY MEMBERS No. 11-01 COMPLIANCE ADVISORY COMMITTEE No. 16-01 INVESTMENT ADVISER ASSOCIATE MEMBERS No. 2-01 INVESTMENT ADVISER MEMBERS No. 7-01 OPERATIONS COMMITTEE No. 13-01 PRIVACY COMPLIANCE PAPER WORKING GROUP SEC RULES MEMBERS No. 30-01 SMALL FUNDS MEMBERS No. 10-01 TRANSFER AGENT ADVISORY COMMITTEE No. 27-01 UNIT INVESTMENT TRUST MEMBERS No. 14-01 RE: SEC ISSUES GUIDANCE ON QUESTIONS RELATING TO REGULATION S-P The staff of the Division of the Investment Management of the Securities and Exchange Commission (SEC) has provided to the Institute written guidance on interpretive issues under Regulation S-P, the privacy regulation that was adopted by the SEC in June 2000. This guidance, which is presented in a question and answer format, contains fourteen questions that are divided into the following areas: scope of the regulation; consumer and customer relationship; privacy notices; exceptions to the opt-out requirements of the regulation; and monitoring third parties. The issues addressed in this guidance that may be of particular interest to the Institute's members are summarized below.

CONSUMER AND CUSTOMER RELATIONSHIP

- Investment Advisers -- According to Question 2, a wrap account client who has a written account with the wrap sponsor, but not with the wrap account's investment adviser, does have a customer relationship with the investment adviser for purposes of Reg. S-P.
- Fund Shares Sold through an Intermediary Broker-Dealer -- According to Question 4, an individual who purchases fund shares through a broker-dealer is a customer of the fund under Reg. S-P if the individual owns the fund shares in his or her own name, irrespective of whether the fund has any direct contact with the individual. Question 4 also notes that if the broker-dealer is the record holder of fund shares for the benefit of the individual, the individual would not be a fund customer under Reg. S-P.

PRIVACY NOTICES

- Joint Notices -- According to Question 6, a privacy notice provided jointly by multiple financial institutions in a fund complex need not separately name each institution to which the privacy notice applies as long as the notice clearly identifies the financial institutions covered by the privacy policy as members of the fund complex. So, for example, the privacy policy for ABC fund complex could state that it applies to all funds that include the ABC name without having to list each such fund separately. If, however, the policy includes funds that do not include the ABC name, the policy should specifically identify those additional funds.
- Householding -- Questions 7 and 8 address issues relating to householding. According to Question 7, a fund can satisfy the annual privacy notice requirement by delivering the notice in or with documents that are householded even if such documents (e.g., account statements) are not covered by the SEC's householding rules, provided that the fund obtained consent to household those types of documents. Question 8 notes that funds can household the initial privacy notice that must be sent by July 1, 2001 provided that such householding is in the

manner provided for householding annual privacy notices or is consistent with the staff's response to Question 7. The answer to Question 8 adds that opt out notices cannot be householded.

- **Customers with Multiple Accounts** -- The answer to Question 9 provides that funds may deliver a single initial or annual privacy notice to a customer with multiple accounts so long as such notice makes clear the accounts to which it applies and is accurate with respect to each such account.
- **Electronic Delivery of a Privacy Notice** -- Question 10 addresses whether posting an institution's privacy policy on its website will satisfy the notice requirements of the regulation. According to the staff's answer, an institution may reasonably expect that a consumer or customer who conducts business electronically will receive actual notice if the institution posts the notice on its website and requires the consumer to acknowledge receipt of the notice as a necessary step to obtaining a particular financial product or service.
- **Delivery of the Privacy Notice with a Prospectus** -- In Question 11, the staff reiterates its views that delivery of an initial privacy notice with a prospectus and confirmation is not timely delivery for purposes of Reg. S-P and states that such notice "would need to be provided to the investor no later than the trade date." The answer to Question 11 notes, however, that there are limited exceptions to this delivery rule provided in Reg. S-P -- i.e., when the relationship is not at the customer's election; when providing more timely notice would substantially delay the customer's transaction and the customer consents to later delivery; and when a nonaffiliated broker-dealer establishes the customer relationship between the fund and the customer without the fund's prior knowledge.

3• **Closed-End Funds** -- Question 12 addresses the duty of a closed-end fund to provide a notice to new investors who purchase fund shares on the secondary market. According to the staff, if the fund is sold by a broker-dealer affiliated with the fund, notice must be provided no later than the trade date. If the fund is sold by an unaffiliated broker-dealer, notice must be provided within "a reasonable time after . . . establish[ing] the customer relationship."

MONITORING THIRD PARTIES

- **Responsibility for Privacy Practices of Nonaffiliated Third Parties** -- Question 14 addresses a financial institution's responsibility under Reg. S-P for the privacy practices of a nonaffiliated third party with whom the institution shares information under an exception in Sections 248.14 or 248.15 of the regulation. While Reg. S-P limits the ability of these nonaffiliates to use and share the information they have received pursuant to the exception, the institution sharing the information is not responsible for monitoring the nonaffiliates' use of the information. According to the staff, if the nonaffiliate receiving the information is registered with the SEC, the SEC could enforce Reg. S-P with respect to the nonaffiliate. If the nonaffiliate is not within the SEC's jurisdiction, another regulator would have jurisdiction over the nonaffiliate.

* * * * As noted in the cover letter to this guidance, the comments expressed therein represent the informal views of the SEC's staff and do not necessarily reflect the views of the Commission. A copy of the cover letter and guidance provided by the SEC staff to the Institute are attached. It is our understanding that this guidance is not expected to be published on the SEC's website.

Tamara K. Reed Associate Counsel Attachments Note: Not all recipients receive the attachments. To obtain copies of the attachments to which this memo refers, please call the ICI Library at (202) 326-8304 and request the attachments for memo 13400. ICI Members may retrieve this memo and its attachments from ICINet (<http://members.ici.org>). Attachment no. 1 (in .pdf format)