INVESTMENT COMPANY INSTITUTE

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By Electronic Transmission (via http://www.regulations.gov)

James H. Freis, Jr.
Director, Financial Crimes Enforcement Network
U.S. Department of the Treasury
P.O. Box 39
Vienna, VA 22183

Re: Defining Mutual Funds as Financial Institutions

Dear Mr. Freis:

The Investment Company Institute[1] ("ICI") appreciates the opportunity to provide Financial Crimes Enforcement Network ("FinCEN") with our comments on the proposed rulemaking (the "Proposal")[2] that would include mutual funds[3] within the general definition of "financial institution" in the rules that implement the Bank Secrecy Act (the "BSA"). Mutual funds thus would be subject to rules under the BSA on the filing of Currency Transaction Reports ("CTRs") and on the creation,

[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $11.02 trillion and serve over 93 million shareholders.

[2] *See* Notice of Proposed Rulemaking on Defining Mutual Funds as Financial Institutions (the "Proposal"), 74 Fed. Reg. 26,996 (June 5, 2009).

[3] The term mutual fund would be defined as "an 'investment company' (as the term is defined in section 3 of the Investment Company Act (15 U.S.C. 80a-3)) that is an 'open-end company' (as that term is defined in section 5 of the Investment Company Act (15 U.S.C. 80a-5)) registered or required to register with the Securities and Exchange Commission under section 8 of the Investment Company Act (15 U.S.C. 80a-8).

retention, and transmittal of records or information for transmittals of funds (commonly referred to as the "Travel Rule").[4]

The ICI and its members have long supported the government's efforts to combat money laundering activity in the financial services industry and, given the unique structure of mutual funds, the ICI has sought to provide Treasury with constructive feedback regarding the application of anti-money laundering regulations to mutual funds.[5] To help better inform FinCEN's further consideration of the Proposal, we explain below our views on, and concerns with, the Proposal.

Currency Transaction Reports

The ICI welcomes subjecting mutual funds to the CTR requirements for financial institutions under the BSA regulations, instead of the reporting requirements relating to currency payments received in a trade or business under the regulations implementing Internal Revenue Code Section 6050I and BSA Section 5331, which are reported on Form 8300.[6] We believe that this approach, which will result in currency transactions being reported under the CTR regime and suspicious cash equivalent transactions being reported under the suspicious activity report ("SAR") regime,[7] will achieve FinCEN's anti-money laundering objectives for the reasons discussed below.

Mutual Funds Present Low Risk at Placement Stage

[4] The regulatory definition of "financial institution" at 31 CFR 103.11(n) determines the scope of rules that require the filing of Currency Transaction Reports ("CTRs") and the creation, retention, and transmittal of records or information on transmittals of funds and other specified transaction (commonly referred to as the "Travel Rule"). *See* 31 CFR 103.22; 31 CFR 103.28; 31 CFR 103.29; 31 CFR 103.33; and 31 CFR 103.38.

[5] *See, e.g.,* Letter from Craig S. Tyle, General Counsel, Investment Company Institute, to Judith R. Starr, Chief Counsel, Financial Crimes Enforcement Network, dated May 29, 2002 ("2002 Letter").

[6] The ICI has previously recommended to FinCEN that mutual funds (and/or their transfer agents) be subject to the CTR reporting regime rather than the Form 8300 reporting regime. *See* Letter from Robert C. Grohowski, Senior Counsel – International Affairs, Investment Company Institute, to Glenn P. Kirkland, Internal Revenue Service, dated May 2, 2006 ("2006 Letter"); Letter from Robert C. Grohowski, Associate Counsel, Investment Company Institute, to Glenn P. Kirkland, Internal Revenue Service, and Judith R. Starr, Chief Counsel, Financial Crimes Enforcement Network, dated April 7, 2003; and 2002 Letter.

[7] *See* Final Rule Amendments to Bank Secrecy Act Regulations – Requirements that Mutual Funds Report Suspicious Transactions, 71 Fed. Reg. 26,213 (May 4, 2006).

In the Proposal, FinCEN requests comment on whether mutual funds are less likely to be used during the initial placement stage of money laundering than depository institutions and therefore present a lower risk for money laundering. We understand that most mutual funds do not accept cash for the purchase of fund shares. For this reason, mutual funds generally are not as likely to be used during the initial placement stage of the money laundering process. FinCEN itself recognized this when it adopted the interim final rule for anti-money laundering programs for mutual funds in 2002.[8]

Current Reporting Requirements are Duplicative and Conflicting

Requiring mutual funds to file reports regarding transactions involving certain non-cash instruments on Form 8300 and also on Form SAR-SF subjects mutual funds to reporting requirements that are duplicative and conflicting.[9] First, the Form 8300 and SAR regimes have conflicting disclosure provisions. The subject of a Form 8300 is *required* to be notified that a report has been filed, while the SAR rule *prohibits* notifying any person involved in a reported transaction that a SAR has been filed.[10] A mutual fund's disclosure of a Form 8300 filing with respect to a transaction involving non-cash instruments effectively undermines the policy goals of the SAR non-disclosure provision – that the subject of an investigation into suspicious activity should not be tipped off as to the existence of that investigation.

Second, requiring mutual funds to report on Form 8300 and on SAR-SF is needlessly duplicative. In particular, cash equivalents (*i.e.*, money orders, traveler's checks, cashier's checks, and bank drafts) with a face amount of $10,000 or less are considered "cash" and are reportable on Form 8300 as suspicious if the recipient knows that the person conducting the transaction is attempting to avoid cash reporting requirements.[11] Similarly, transactions, including those involving cash equivalents,

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[8] *See* Anti-Money Laundering Programs for Mutual Funds, 67 Fed. Reg. 21117, 21118 (April 29, 2002).

[9] *See* 2006 Letter. In this letter, the ICI recommended that Treasury either (1) subject mutual funds to the CTR requirements or (2) exempt funds from reporting cash equivalents on Form 8300.

[10] *See* 26 CFR section 1.6050I-1(f) (requiring a written statement to be sent to every person whose name is set forth in a Form 8300 report) and 31 CFR section 103.15(d) (prohibiting a mutual fund from disclosing that a suspicious activity report was filed to any person involved in the transaction). We note that FinCEN has recently issued a proposed rulemaking clarifying the scope of the prohibition against disclosure, which would explicitly state that "a SAR, and any information that would reveal the existence of a SAR, are confidential and shall not be disclosed except as authorized..." *See* Notice of Proposed Rulemaking on Confidentiality of Suspicious Activity Reports, 74 Fed. Reg. 10,148 (Mar. 9, 2009).

[11] 26 CFR section 1.6050I-1(c)(1)(ii)(B)(2); 31 CFR section 103.30(c)(1)(ii)(B); and Form 8300.

are reportable as suspicious transactions under the SAR rule if they are designed to evade any transaction reporting requirements under federal law.[12] As a result, transactions in fund shares involving cash equivalents that otherwise would be reportable on Form 8300 are also reportable on Form SAR-SF as suspicious transactions, resulting in duplicative reporting.[13]

Time and Cost Savings

Replacing the requirement for mutual funds to file reports on Form 8300 with a requirement to file CTRs would reduce the expense and burden of currency transaction reporting for mutual funds and their transfer agents because the definition of "currency" for purposes of the CTR rule is different from, and less inclusive than, the definition of "currency" in the rule for Form 8300. In particular, mutual funds are required to file Form 8300s for certain transactions involving cash equivalents, whereas CTR filings are required only for transactions involving cash and not cash equivalents.[14] However, since essentially the same information regarding suspicious cash equivalents that is currently reported on Form 8300 would continue to be reported under the SAR regime, these cost and time savings would be realized without diminishing the quality or quantity of useful information reported to Treasury.

The Travel Rule and Related Recordkeeping Requirements

The ICI understands FinCEN's desire to extend the provisions of the Travel Rule and related recordkeeping requirements to mutual funds to better enable law enforcement agencies to trace the

[12] 31 CFR section 103.15(a)(2).

[13] We note that not all mutual funds or their transfer agents are required to file reports on Form 8300. It is our understanding that when a fund's transfer agent receives payments for fund shares, and the transfer agent either (1) is a bank, broker-dealer, or other financial institution subject to CTR requirements under the Bank Secrecy Act (the "BSA"), or (2) is acting as an agent of a bank, broker-dealer (*e.g.*, the fund's principal underwriter), or other financial institution subject to CTR requirements under the BSA, there is no requirement for the transfer agent (or the fund or its principal underwriter) to file reports on Form 8300. Rather, in these circumstances, the transfer agent would be required to comply with the reporting requirements applicable to banks, broker-dealers, or other financial institutions under the BSA regulations. This would include, as appropriate, requirements to report the receipt of cash on CTRs and the receipt of suspicious non-cash instruments on suspicious activity reports. The Proposal would, therefore, have the added benefit of subjecting all mutual funds to the same currency transaction reporting requirements.

[14] *See* 31 CFR section 103.30(c)(1) (for the definition of currency for purposes of Form 8300) and 31 CFR 103.22(b)(1) and 103.11(h) (for the definition of currency for purposes of CTRs).

proceeds of illegal activities and identify participants in money laundering schemes. We do not, however, concur with FinCEN's belief that these requirements would have a *de minimus* impact on mutual funds and their transfer agents simply because mutual funds are already subject to the record retention requirements of the Investment Company Act of 1940 and mutual fund transfer agents are subject to recordkeeping requirements under the Securities Exchange Act of 1934.[15] Although mutual funds or their transfer agents may already have some or all of the information required to be maintained, the information may not be retrievable in the manner required under the Travel Rule. Based on discussions with members, we understand that the impact of these requirements on mutual funds and their transfer agents will vary significantly depending on various factors, including the transaction processing and recordkeeping systems currently in place at a particular mutual fund or transfer agent, the size of the mutual fund complex and how the funds in that complex are distributed. Certain mutual funds will need to expend significant financial and personnel resources to alter their systems and processes in order to comply with these requirements.

To accommodate the mutual funds and transfer agents that will need to make substantial changes to their transaction processing and recordkeeping systems, we urge FinCEN to provide an implementation period of at least eighteen months after the adoption of the Proposal with respect to compliance with the Travel Rule. At a time when resources are stretched, mutual funds and their transfer agents are dealing with many competing priorities and other regulatory changes that are significantly impacting operations, such as the new cost basis reporting requirements that are necessitating substantial evaluation and will result in significant operational and technological changes in order for funds to capture and report the required tax information.[16] A more generous implementation period will enable mutual funds to fully and carefully consider the best way to implement the new requirements and appropriately manage their financial and personnel resources during this challenging time in the financial services industry. In addition, we believe this time may be needed because we are concerned that mutual funds and their transfer agents may encounter unique

[15] We appreciate FinCEN's recognition that many mutual funds contractually delegate their BSA compliance functions, including recordkeeping, to transfer agents (although the mutual fund remains responsible under the BSA for ensuring compliance). *See* Proposal at footnote 30.

[16] As a result of the Economic Stabilization Act of 2008, mutual funds and others will need to report a shareholder's basis in certain securities to the shareholder and the Internal Revenue Service upon a sale or redemption. The new reporting requirements take effect in 2012 for mutual fund shares. *See* Letter from Karen L. Gibian, Associate Counsel – Tax Law, Investment Company Institute, to Clarissa C. Potter, Acting Chief Counsel, Internal Revenue Service, dated April 9, 2009, available at http://www.ici.org/pdf/23387.pdf (commenting on the cost basis reporting requirements and explaining that compliance with the legislation by the financial services industry will require a herculean effort within a very short time period, including developing systems to accommodate various cost basis methods and transfers of such information to other brokers when shareholders transfer their accounts).

issues or challenges when implementing the requirements of the Travel Rule that have not been addressed in previously issued guidance. We may, therefore, seek additional guidance or clarification regarding compliance with the Travel Rule requirements during the implementation stage.

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If you have any questions, or need additional information, please contact Susan Olson (solson@ici.org or 202-326-5813) or Eva Mykolenko (emykolenko@ici.org or 202-326-5837).

Sincerely,

/s/ Susan M. Olson

Susan M. Olson
Senior Counsel – International Affairs