May 8, 2006

# BSA/AML Regulatory Alert

The Financial Crimes Enforcement Network (FinCEN) has issued a final rule requiring registered open-end investment companies ("mutual funds") to file suspicious activity reports (SARs) pursuant to the anti-money laundering provisions of the USA PATRIOT Act. The Securities and Exchange Commission will be primarily responsible for enforcing the new rule.

The final rule closely parallels the SAR rules already applicable to several other types of financial institutions, including banks and broker-dealers. It names four categories of transactions that require reporting:

- Transactions involving funds derived from illegal activity, or intended to hide funds derived from such illegal activity as part of a plan to violate federal law;
- Transactions designed to evade the requirements of the Bank Secrecy Act;
- Transactions that appear to serve no business or apparent lawful purposes, and for which the mutual fund knows of no reasonable explanation after examining the available facts; and
- Transactions that involve the use of the mutual fund to facilitate criminal activity.

Mutual funds must report transactions (i) that are conducted or attempted by, at, or through a mutual fund, (ii) that involve or aggregate at least $5,000 in funds or other assets, and (iii) that the mutual fund "knows, suspects, or has reason to suspect" fall into one of the foregoing four categories. Mutual funds are also encouraged to report voluntarily a suspected violation of law that involves less than the $5,000 threshold. By statute, a mutual fund cannot be held liable under federal or state law for information disclosed in a SAR, whether the SAR is required or voluntary.

In determining whether to file a SAR, a mutual fund must base the determination on all of the facts and circumstances relating to the transaction and customer in question. A mutual fund must file a SAR within 30 days after initial detection of a suspicious activity, although it may delay filing for another 30 days if it does not identify a suspect on the date of the initial detection. Violations that require immediate attention, such as suspected terrorist financing or ongoing money laundering schemes, should be reported promptly by telephone to an appropriate law enforcement authority in addition to filing a SAR. The mutual fund must maintain copies of the SARs and related documentation for five years from the date of filing. It may not notify any person involved in the transaction – except for other mutual funds with which it is making a joint filing – that the transaction has been reported.

The final rule is part of a series of steps FinCEN has taken to address the risk of money laundering through mutual funds. In April 2002, FinCEN issued an interim final rule requiring mutual funds to adopt anti-money laundering programs, and in May 2003, the agency required mutual funds to implement customer identification programs.

Please do not hesitate to call any member of our Financial Institutions Group, including Stuart Stock, Peter Flanagan, Keith Noreika, David Fagan, Fuad Rana, B.J. Sanford, or the undersigned, should you have any questions regarding the mutual funds SAR rule from FinCEN or any other BSA/AML regulatory issue.

D. Jean Veta
jveta@cov.com
(202) 662-5294

Mark E. Plotkin
mplotkin@cov.com
(202) 662-5656

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This information is not intended as legal advice, which may often turn on specific facts. Readers should seek specific legal advice before acting with regard to the subjects mentioned herein.

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