

USA Patriot Act: The Latest Updates for Private Equity Funds

Below you will find a memorandum from the National Venture Capital Association (“NVCA”) discussing the latest news about the USA Patriot Act and its applicability to venture capital funds.

Provided that the proposed Treasury regulations described in the NVCA memo do not change as a result of input submitted

during the sixty-day comment period ending November 17, 2002, private equity funds will be exempt from the anti-money laundering program requirements of the USA Patriot Act so long as they do not allow investors the right to redeem any portion of their ownership interests within two years after such interests were purchased.

We remain in communication with NVCA and will continue to monitor these and other regulations applicable to the venture capital community. We will keep you informed as further information becomes available. ■

NVCA MEMO

Major Victory: Federal Money Laundering Laws

TO: All Members

FROM: National Venture Capital Association

DATE: September 18, 2002

SUBJECT: Exemption for Many Venture Funds from AML Requirements

In a victory for the venture industry and NVCA, the Treasury Department has concluded that private equity funds, which do not provide a “right of redemption” within two years of investment, will not be required to comply with the new anti-money laundering provisions of the USA PATRIOT Act.

Until today, federal officials have indicated that all NVCA members would be required to have a four-part anti-money laundering program in place once Treasury regulations were issued. However, in keeping with the Treasury’s emphasis on risk-based analysis,

NVCA has continued to highlight the illiquidity of venture investments and low risk that venture funds would be used for money laundering activities.

Today, the Treasury Department issued the long awaited proposed rules requiring investment companies not registered with the Securities and Exchange Commission to establish anti-money laundering programs under Section 352 of the PATRIOT Act. (To view the proposed rules visit <http://www.treasury.gov/press/releases/docs/352investmentcompanies.pdf>) Importantly, the unregistered investment companies covered by the proposed rule include hedge funds, commodity pools, and investment companies investing in real estate. Specifically, the rule applies to any unregistered investment company that: (1) would otherwise be an investment company but for the Section 3(c)(1) and 3(c)(7) exemptions under the Investment Company Act of 1940, is a

commodity pool operator, or invests primarily in real estate; (2) permits investors (or owners of interests) to redeem his or her ownership interest within 2 years of the purchase of that interest; (3) has total assets of \$1 million or more as of the end of the most recently completed calendar year; and (4) is organized under the laws of a state or the United States, is organized, operated or sponsored by a U.S. person, or sells ownership interests to a U.S. person. Companies that fall within this category are required to implement the four-part money laundering program, a sample of which is set forth in the NVCA guideline published in March of this year, (see April 9th policy highlight on www.nvca.org) and to provide a notice (including name, contact information, total assets under management, etc.) to Treasury’s Financial Crimes Enforcement Network, or FinCEN. However, funds that do not provide the 2-year redemption feature—most NVCA members’ funds, we hope—are exempt from

both registration and AML program. The regulations are not yet final and a 60 day comments period will follow their official publication in the federal register.

NVCA has taken every opportunity to educate federal officials on the aspects of venture investing that mitigate the risks of their being used for illicit purposes. However, it

is still a significant turnaround that many VC funds can be exempted from the anti-money laundering program requirement entirely.

NVCA remains committed to the idea that the industry will do its part in the war on terrorism. We will continue our dialogue with federal officials and advise members

as the situation develops. Furthermore, we are grateful that our discussions to date have resulted in an exemption for our very low-risk members.

If you have any questions or comments or would like further information, please contact Jennifer Dowling or Ian Graves at 703/524-2549. **NVCA**

Contact Information

Broomfield 720/566-4000

Bernard Hatcher bhatcher@cooley.com

Kirkland 650/843-5100

John Dado jdado@cooley.com

Palo Alto 650/843-5000

John Dado jdado@cooley.com

Craig Dauchy cdauchy@cooley.com

Reston 703/456-8000

Thomas Salley tsalley@cooley.com

San Diego 650/843-5100

John Dado jdado@cooley.com

San Francisco 415/693-2000

Craig Dauchy cdauchy@cooley.com

Dan Frank dfrank@cooley.com

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