



**VIA E-MAIL**

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Attn: NPRM – Section 352  
Unregistered Investment Company Regulations

**Re: Comments on Proposed Rules Regarding  
Unregistered Investment Companies  
67 FR 60617**

Ladies and Gentlemen:

Wilson Sonsini Goodrich & Rosati appreciates the opportunity to offer comments regarding the proposed regulations issued on September 18, 2002<sup>1</sup> which would, if adopted, address the treatment of unregistered investment companies under the provisions of the International Money Laundering Abatement and Anti-Terrorist Financing Act of 2001 (the "Act" and the "Proposed Regulations"). These comments are based upon our experience as legal counsel to a substantial number of venture capital and other private equity funds, but are not submitted on behalf of any particular client or clients.

The Proposed Regulations provide, in relevant part, that "unregistered investment company means an issuer that is a company (A) that (1) would be an investment company under the Investment Company Act of 1940 (15 U.S.C. 80a) but for the exclusions provided for in sections 3(c)(1) and 3(c)(7) of that Act; [and] (B) *permits an owner to redeem his or her ownership interest* within two years of the purchase of that interest." (Proposed Regulations, Sections 103.132(6)(i)(A) and (B)).

We are concerned that the italicized language is ambiguous and may include within the meaning of "unregistered investment company" many venture capital and other private equity funds ("Funds") whose governing agreements contain industry-standard provisions that allow investors to withdraw under limited circumstances. If deemed to be unregistered investment companies, such Funds would then become subject to the Act's anti-money laundering program requirements.

We believe that limited withdrawal provisions of the types described below would not cause a Fund to become an attractive vehicle for money laundering. Accordingly, we respectfully request that the Proposed Regulations be revised to clarify that such provisions would not cause a Fund to be deemed an unregistered investment company.

***Redemptions to Comply with Applicable Law.***

Fund investors that are subject to government regulation often negotiate for special withdrawal rights. For example, pension funds subject to the Employee Retirement Income Security Act of 1974 ("ERISA") almost always obtain a special right to withdraw from a Fund if their continued participation in the Fund would cause them to be in violation of, or subject to material additional obligations under, ERISA.

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<sup>1</sup> U.S. Department of Treasury, Proposed Rule, 67 FR 60617.

Withdrawal rights with a similarly limited scope often are obtained by other regulated investors, such as banks and insurance companies.

It would not be consistent with public policy to require that an investor violate applicable law by continuing to hold a Fund interest. Moreover, it often would not be feasible for a regulated entity to invest in a Fund if, as a result of the investment, such entity were required to assume the risk of: (x) subsequent, unmitigated violation of applicable law; or (y) material additional regulatory obligations.

In our many years of experience, we have seen virtually no cases in which a regulated entity exercised this type of limited withdrawal right. Such rights are granted solely to assure regulated investors that a Fund investment will not ultimately force them into an untenable regulatory position. We see no reason why withdrawals under such rights should become more common in the future.

Accordingly, we believe that a Fund should not be considered an "unregistered investment company" within the meaning of the Proposed Regulations solely because investors are permitted to withdraw in order to avoid: (x) violation of applicable law; or (y) material additional regulatory obligations.

***Redemptions Allowed Solely at the Discretion of the General Partner.***

Many Fund agreements also permit an investor to withdraw upon obtaining consent from the Fund's "general partner" or "managing member" ("General Partner"). Such provisions typically permit a General Partner to refuse its consent, although some provisions explicitly require that such refusal be "reasonable" (i.e., based upon a reasonable determination by the General Partner that the proposed withdrawal would be inconsistent with the Fund's best interests).

Because withdrawals reduce a Fund's capital available for investment, General Partners typically have a fiduciary duty to withhold their consent. However, that duty may be offset by special circumstances. For example, a General Partner might permit an investor to withdraw in consequence of: (i) economic hardship; or (ii) fundamental business conflicts between the investor and the Fund.

It would not be consistent with public policy to require continued investment in the face of economic hardship or fundamental business conflicts. Moreover, Fund investors rarely seek to withdraw. This phenomenon is explained, in part, by the fact that venture capital and other private equity funds typically hold illiquid securities that cannot be easily sold even if distributed pursuant to a withdrawal.<sup>2</sup> Finally, because their compensation typically is linked to the volume of assets they manage, General Partners usually have an affirmative incentive (above and beyond their fiduciary duties) to prevent withdrawals.

During the last two years (following the bursting of the technology market "bubble"), we have seen an increased number of hardship-based withdrawals. However, such withdrawals remain fairly rare and are not used as a routine method of redeeming Fund interests. We see no reason why they should become more common in the future.

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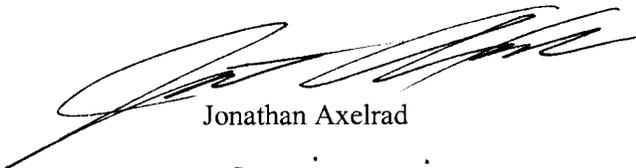
<sup>2</sup> Under most Fund agreements, an investor who withdraws will receive a pro rata share of the Fund's assets. Thus, early withdrawal typically will entitle an investor to receive a relatively small amount of cash and a much larger collection of illiquid securities. Often, such securities are not immediately transferred to the withdrawn investor but are, instead, held by the Fund on the investor's behalf for an extended period of time.

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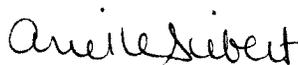
Accordingly, we believe that a Fund should not be considered an "unregistered investment company" within the meaning of the Proposed Regulations solely because investors are permitted to withdraw upon obtaining the General Partner's consent.

We appreciate your consideration of these issues. If you have any questions or need additional information to assist you in the evaluation of our comments, please do not hesitate to contact either of us at (650) 493-9300.

Very truly yours,



Jonathan Axelrad



Arielle Siebert